

# University of Miami Law Review

---

Volume 12 | Number 2

Article 3

---

1-1-1958

## Tax Administration in Underdeveloped Countries

Stanley S. Surrey

Follow this and additional works at: <https://repository.law.miami.edu/umlr>

---

### Recommended Citation

Stanley S. Surrey, *Tax Administration in Underdeveloped Countries*, 12 U. Miami L. Rev. 158 (1958)  
Available at: <https://repository.law.miami.edu/umlr/vol12/iss2/3>

This Leading Article is brought to you for free and open access by the Journals at University of Miami School of Law Institutional Repository. It has been accepted for inclusion in University of Miami Law Review by an authorized editor of University of Miami School of Law Institutional Repository. For more information, please contact [library@law.miami.edu](mailto:library@law.miami.edu).

# TAX ADMINISTRATION IN UNDERDEVELOPED COUNTRIES

STANLEY S. SURREY\*

## I. INTRODUCTION

In recent years considerable thought and attention have been devoted to the fiscal policies best suited to the economic development of the areas of the free world. As a part of this search for desirable fiscal policies, considerable stress is being placed on the role of tax policy. The various kinds of taxes—income, excise, property, import, export, succession—are being diligently surveyed. The combinations and alternatives within each class are all under scrutiny. Thus, in the income tax area, consideration is being given to individual and corporate taxes, to excess profits taxes, to taxes on increases in individual incomes, to taxes on dividends and other income payments, to the schedular and global forms of income taxes, and the like. In the excise area, there are sales taxes at the various levels of manufacture, wholesale or retail; taxes over the entire range of production and distribution, such as turnover and value added taxes; taxes on special pursuits such as mining or special products such as luxuries, and so on almost *ad infinitum*. Some countries are experimenting with an expenditure tax, which combines elements of income and excise taxation. The variety of taxes seems endless. Each must be considered in the light of particular fact situations and fiscal and economic goals. Each must be competitively analyzed against its rivals. And, when selected, the chosen tax must be imposed at the appropriate level of rates and scope of application.

The problems of tax policy are difficult. Our knowledge of the effect and impact of various tax tools is not too impressive. We cannot talk with satisfactory confidence regarding such matters as tax incentives to economic development, the use of tax techniques to spur production, or consumption, or investment, or saving. But we are diligently striving to increase our knowledge about these matters, to indicate our confidence in the predictions regarding the results of one or another policy or tax technique. The efforts being made on these fronts are necessary and encouraging. However, a warning note seems appropriate. The concentration on tax policy—on the choice of taxes—may lead to insufficient consideration of the aspect of tax

---

\*Professor of Law and Director of the International Program in Taxation, Harvard Law School.

This paper was originally prepared for the meeting of the International Institute of Public Finance at Rio de Janeiro, Brazil, September, 1954 and was published in the report of that meeting. Some revisions have been made for the present article.

administration. In short, there may well be too much preoccupation with "what to do" and too little attention to "how to do it."

A survey of the available literature developing from the growing number of technical assistance missions underscores this warning. The administration of the tax system of the country involved generally receives relatively slight attention. Often the remarks devoted to administration are in the form of generalities, all of which notably come down to the repeated recommendation of "improvement." Exceptions may of course be found, as in the 1949-1950 Shoup Tax Mission to Japan.<sup>1</sup> But usually tax administration is off the beaten mission paths.

It is increasingly apparent, however, that tax administration must receive far greater attention if the goals of tax policy are to be attained. Much of tax policy is being directed to obtaining increased revenues to enable governments to carry out their economic planning. The search is for additional taxes, for new sources of revenue. Yet it is true in many countries that the successful administration of some of the existing taxes would provide a considerable part of the needed additional revenue. The diligent execution of existing taxes may well make unnecessary, or at least reduce, the multiplication of taxes in the search for revenue. It should be noted that this multiplication of taxes can, through a dispersion of administrative resources, result in a weakening of the entire tax structure. Moreover, the adoption of new taxes to compensate for the failure to enforce existing taxes may distort the equity of the system, for soon the rationale of the structure is lost in a complex maze of one set of taxes imposed to adjust for the defects in another set. Also, in the search for revenues, the rates of existing taxes may be pushed to such heights that the taxes cannot be enforced effectively and may cause undesirable economic effect.

In addition to the direct improvement in the revenue yields of existing taxes that could be achieved by effective tax administration, there are other factors pointing to the need for strengthening tax administration. The trend toward the progressive income tax is steadily growing. The reasons lie in the equity of the tax, with its roots in the public's strong acceptance of the ability-to-pay concept, and in its revenue strength as the economy expands. The income tax, however, presents formidable obstacles to effective enforcement. The stress on family status and on the net change of the taxpayer's economic position over a period of time demands a precision in the application of the income tax which is far greater than that required of other taxes. The need for precision grows in importance both as the rates climb upwards and as the base broadens with decreasing exemptions.

---

1. See also the United States Economic Survey Mission (Bell Mission) to the Philippines, 1950.

The income tax may well be the favorite of the twentieth century, but it demands twentieth century administration. This requirement is even more urgent when one turns to the complex variations of that tax, such as a tax on excess profits or a tax on increases in individual incomes or a tax on expenditures. There are many who urge these variants without any comprehension of the complex legal and accounting problems which they create, without any recognition of the enormous difficulties being faced in the struggle to impose even the basic income tax, and without any realization that even countries with considerable experience in income tax administration have yet to master these specialized types of income taxation.

Another factor demanding emphasis on tax administration is the growing realization that the tax status of the agricultural sector of underdeveloped countries must be examined. There is strong support for the view that these sectors must furnish a substantial portion of the revenues if government is to carry out the social overhead projects necessary to economic development. But the tax devices to reach the agricultural sector are not fully developed and ready at hand to be utilized. One must explore the alternatives—the real property tax, the income tax, and excise taxes on agricultural products. Prominent in this examination must be a consideration of the aspect of administration with respect to these taxes.<sup>2</sup>

While many underdeveloped countries faced with dissatisfaction with their revenue systems are interested in making fundamental reforms, doing so may in some instances be putting the cart before the horse. Efforts to change the law may invoke sharp political and social struggles, whose effect might long delay any worthwhile changes. Also, desirable substantive reforms might be faced with the argument that they could not be administered and this could well be true given the present state of tax administration. Or, these changes if made might place such severe strains on an already weak administrative structure that the administration of the entire revenue system would be endangered. The sensible course in many countries may therefore be first to strengthen the existing administrative machinery and then when this has been accomplished to face the basic issues of tax reform.

We thus find, at least by comparison to substantive issues, insufficient consideration being paid to questions of tax administration at a time when the tax problems of underdeveloped countries accentuate the role of tax administration. Moreover, this lack of consideration is to be contrasted with the very acute difficulties which tax administrators face almost the world over. The tax administrator on the one hand sees new burdens falling on his shoulders — new taxes being imposed and existing levies becoming

---

2. See in general PROCEEDINGS OF CONFERENCE ON AGRICULTURAL TAXATION AND ECONOMIC DEVELOPMENT, Harvard Law School International Program in Taxation (1954).

more severe. He must collect more taxes, at higher rates, and from an ever expanding body of taxpayers. On the other hand he finds himself saddled with a staff which is insufficient, inexperienced and poorly paid. He faces a public in large part unfamiliar with the tax knowledge and record keeping requirements which a developing state must inevitably demand of its citizens. He cannot obtain the needed support from the legal and accounting professions — the necessary allies for the successful administration of any complex tax system — either because of their lack of experience or sometimes because they are almost non-existent. Finally, he often must demand the taxes from businesses and individuals with a deep-rooted suspicion ranging to contempt of the tax collector, from a public whose antagonism to tax payment, arising from a basic lack of confidence in the government, is almost the very antithesis of the attitude which must be the cornerstone of every successful democratic tax system — that taxes are the price necessarily paid for civilized society.

So much for the background of this paper. While it can readily be concluded that the field of tax administration is of major importance, it must also be recognized that any such study would involve many facets and open up many difficult problems. The balance of this paper will briefly present some of these facets and problems. It may be pertinent to observe, in connection with the consideration of these matters, that while the issues and goals of fiscal policy may well differ from country to country, the problems of tax administration are quite likely to be very similar the world over. A multi-national meeting of tax administrators would much more quickly find common grounds respecting their problems and solutions than would a meeting of finance ministers.

## II. CODIFICATION AND DRAFTING

Before a country considers how best to administer its tax system it must possess a clear picture of the scope of that tax system — what are the different taxes imposed, at what rates, and to whom do they apply. One would suppose that such knowledge is readily available, yet many countries really possess no such clear picture of their tax systems. Instead, there often exists a bewildering array of overlapping and contradictory taxes. Many of these taxes overlap so that a single commodity or transaction may be subject to a number of taxes, imposed at different or supplementary rates involving different tax bases with different times of payment, different returns, and separate administrative and judicial procedures. Some of these taxes are obsolete, yielding only a very small revenue or sometimes nothing at all, but remain on the books to complicate the tax structure. Others are so riddled with exemptions as to be scarcely applicable to anyone. Moreover, many tax measures are simply charges and fees for government conces-

sions or services. Often the administrative provisions and judicial procedures of an existing tax are applied without change to new taxes as they are enacted, without any examination of the differing requirements that the new taxes may warrant. In addition, the same words will be used in the various tax laws, but with different definitions or without definition, so that only confusion in application can result. Further, the controlling laws themselves may be extremely difficult to locate. Very often there is a tangled mass of laws, regulations, decrees and the like reaching far into the past, jumbled together with amendments and modifications. When the statutory picture is so confused, it is extremely difficult for the government to know what it must administer and for the taxpayers to know with what they must comply.

A first step in the improvement of tax administration, as many governments are now recognizing, is thus the codification of the various tax laws. This codification should be based on an orderly statutory rearrangement of the entire tax system in accordance with a definite outline. Thus, the various taxes should be classified among income taxes, succession taxes, property taxes, excise and sales taxes, and so on. Each field in turn should be subdivided, so that each tax is separately identified. Overlapping among the taxes should be eliminated, with the various taxes applicable to a single article or transaction consolidated into one tax. The substantive provisions describing the articles or persons taxed and fixing the rate and base of the tax should be separated from the administrative provisions. The latter should be divided functionally, as respects the returns to be filed, the time for payment, the other duties of the taxpayer, the powers of the administrator, the penalties imposed, etc. Thus, an excise tax codification recently enacted in one country has the following outline:<sup>3</sup>

## I. Definitions

Effect of Definitions  
List of All Definitions Used in Act  
General Definitions

## II. Rates of Tax

(In tabular form, giving only the name of the tax, the tax rate, and the section reference in Part III in which the tax is described.)

---

3. Excise Tax Act of Puerto Rico, enacted January 26, 1956, and initially prepared in 1954 by Stanley S. Surrey for the Secretary of the Treasury, Department of Finance, Puerto Rico.

## III. Description of Taxes

## A. Taxes on Articles and Merchandise

Jewelry  
Luggage  
Sugar, etc.

## B. Taxes on Certain Transactions

Public Documents  
Admissions, etc.

## C. License Taxes

## D. Exemptions

(General or special exemptions in addition to those basic to the description of the particular tax.)

## IV. Administrative Provisions

## A. Determination of Prices and Costs

## B. Determination of Taxpayer and Time of Payment

## C. Administration of Exemptions

## D. Duties of the Taxpayer and Other Persons

## E. Powers of the Secretary of the Treasury

## F. Miscellaneous Provisions

## V. Penalties

## VI. Effective Dates and Transition Provisions

Those familiar with the tax systems of underdeveloped countries will recognize that a serious obstacle to efficient codification lies in the pernicious habit of earmarking the revenues from a particular tax for a particular purpose. The revenues of a 10% tax on a commodity may go for relief purposes, the proceeds from an additional 5% tax on the same commodity may go for road building. This tax is earmarked for education, that tax for some health project, another tax for pensions, and so on. Earmarking may serve some short run political purposes, in that the function supported may make the tax less objectionable. Also, a bewildering array of taxes earmarked for many separate objectives may prevent the public from fully discerning the real impact of the tax burden. But it is generally agreed that the disadvantages of the system are serious. Proper budgeting and control of expenditures and receipts are made extremely difficult. The benefited institutions themselves are often greatly hampered in orderly planning since their revenues may depend not on their needs but on the particular taxes assigned to them. Moreover, the particular organization or institution benefited by the earmarking of revenue from a particular tax will often interfere

in the administration of that tax. Further, unless earmarking is dropped, the full benefits from a codification of the tax laws can scarcely be achieved since the overlapping and ramification of taxes would have to be preserved to support the earmarking. An elimination of the device of earmarking so that the revenues go into the general fund of the country as far as possible is thus a corollary of codification.

The task of codification would disclose another aspect of the tax structure which handicaps effective administration, that of poor legislative drafting. Once the tax policy is formulated, the task remains of expressing that policy in words of legal command, be they statute, decree, or administrative regulations. That task is not an easy one. The legal command should be precise, its boundaries defined, its exceptions clear, the possibilities of its abuse anticipated and blocked. The tax system is superimposed on the complex structures of business and family life with all their interwoven patterns. Its relationship to those complex structures in turn creates complex and interlocking patterns within the tax system. Yet very often the decisions on policy are regarded as the end of the tax job, with the drafting viewed as a simple and almost automatic process. Economists not experienced in drafting, or lawyers not versed in the technical ways of taxation, often act as the draftsmen of tax laws. A technique often adopted by these persons is simply to copy from other tax laws of the same or different countries. As a consequence the weaknesses of poorly drafted laws spread globally. The final result is often a hodge-podge of provisions poorly adapted to carrying out the policy decisions. Exceptions and provisions are piled on top of each other as each new problem is met by a new set of words put down without any analysis of the basic issues.

The solution here is to recognize that taxation requires skilled legal drafting by lawyers fully cognizant of the intricacies of the tax structure. Once such draftsmen are trained, continuity in drafting must be provided so that the developing tax policies can always be fitted into an orderly legal structure by draftsmen who at all times know the history and the exact contours of that structure.

Finally, codification by reducing the tax provisions to an orderly statutory and regulatory structure will permit the tax authorities to make available to those interested in taxation an authoritative, up-to-date, and manageable statement of tax rules. The legal, accounting and academic professions and the business groups will thus be enabled to participate more intelligently in the tax process. The statutory clarity that results from codification will also permit the tax administration to prepare for the lay public simplified explanations of the tax structure. These popular explanations will serve to increase the taxpayers' knowledge of their duties and thereby promote greater compliance.



### III. SOME BASIC ASPECTS OF ADMINISTRATIVE PROCEDURE

Once the various components of the tax system are properly arranged and integrated, the task of carefully surveying their administration may appropriately follow. While the problems will vary from tax to tax, there are a number of basic aspects that usually occur under nearly any tax. The following comments relate to some of these basic aspects, with principal reference to the income tax.

#### *A. Locating the Taxpayer*

The beginnings of tax administration lie in seeing that the taxpayers are on the tax rolls. Unless the tax authorities know who are the individuals or units subject to the tax, the whole machinery of administration must necessarily function with incomplete coverage of the taxable area. Consequently, the first task is the preparation of lists or registers of taxpayers for each tax. Various registers may be compiled — property owners, business concerns, employers, investment owners — and combined where appropriate. The registers must be kept current, and maintained in an order — alphabetical, geographical, etc. — which proves most convenient for effective use. Every possible source of names for these registers must be combed—local property rolls, registration of voters, visual inspection of properties, records of new construction, records of other government departments, membership list of trade or merchants' associations and clubs, automobile registrations, etc. If other agencies of government have had air photographs or other surveys made of certain farm or city areas, these should be utilized. Once it is decided to keep adequate registers, sources of information will readily occur to the administration. The important tasks are to select among the various sources only those which promise to be productive of names likely to be taxpayers under the tax in question (thus in some places telephone books may be very useful, while elsewhere these lists may contain more non-taxpayers than taxpayers); to gather only so much information as can be efficiently processed; and to devise an efficient system for converting the selected information into a continuously current form usable for enforcement purposes.

#### *B. Initial Taxpayer Compliance*

Once the taxpayer is ascertained, the next step is that of obtaining initial compliance. In an income tax, unless the tax is withheld at the source, this will usually be the filing of a tax return or declaration. This return must provide the basic data for the assessment of the tax, and in some countries will also carry with it the taxpayer's computation and pay-

ment of his tax. In this sense, every effective income tax is basically a self-assessed tax. Hence, tax administration must aim for as high a degree of compliance at this stage as is possible. To achieve this compliance it must concentrate on several factors. The taxpayer must be furnished with the return by the tax authorities or provided with ready access to it, as through post offices, local agencies, and other centers of mass distribution. The geographical distribution of returns should take account of the distribution of taxpayers in the country, so that all areas receive sufficient returns. The return should be distributed free, not sold by the government or a private party having the concession for the distribution of the form. It might be mailed to all taxpayers on the tax rolls, but with publicity given to the fact that the failure to receive a return is not an excuse for a failure to file a return. The form should be arranged in as simple a manner and the steps on the return and the instructions written in as simple a style as is possible. Very often the effort to simplify the tax return will dramatically illustrate complexities inherent in the tax itself and force the simplification of these substantive aspects as a necessary prelude to simplification of the return. The return should be of convenient size on appropriate paper, and adaptable to typewritten as well as handwritten use. The tax offices should be organized at return filing time to assist the taxpayer in every way possible. In fact, patient assistance will reveal those portions of the return which cause trouble to the taxpayers and thus enable their correction in subsequent forms. Newspapers and other media of public information should be utilized to explain the mechanics of the tax return and the requirements for filing. School children could be taught how to help their parents in filling out the returns. The filing dates for the various taxes should be coordinated, with concentration at one time wherever feasible of related taxes involving similar basic data.

If the tax is withheld, as is generally the case at least with wages and salaries, the initial steps relate to the withholding machinery. Here the employer must on the one hand secure the needed information from the employee as to his status and on the other hand obtain from the government exact instructions on the manner and extent of withholding. Here also the mechanics of withholding should be made as simple as possible, so that the employers can properly fulfill their role. Tables and other devices should be utilized which enable the employers themselves to compute the tax to be withheld, thereby making unnecessary the submission of the data in each case to the tax office for computation of the withheld tax. Care should be taken to see that employees are properly informed of the amount withheld from them and the employers promptly turn over to the government the sums collected.

*C. Check on Taxpayer Compliance: Audit and Examination*

After the taxpayer has performed the task of initial compliance, the tax authorities must take the next step. No tax will work effectively, especially an income tax, unless its administrators maintain an aggressive attitude with respect to the correctness of the taxpayers' actions. Some taxpayers will fail to file or will make mistakes through ignorance or neglect; others will deliberately cheat. A passive attitude by the authorities toward these errors and falsifications will soon undermine the entire structure, since the diligent and honest taxpayers will almost in self defense be forced to the level of the careless and dishonest. A tax administration which seeks compliance must protect those who comply or else compliance will not be forthcoming.

Consequently, the tax authorities must arrange systematically to check the compliance of the taxpayers. The taxpayer registers, if carefully prepared and matched against the returns, will reveal the failures to file. But after this step the path is difficult. Generally, limitations of personnel will make it impossible for each return to be given intensive scrutiny. A program of investigation and examination of returns must therefore be planned. Its objective should be an effective examination which both safeguards the government from major loss and instills in taxpayers a respect for the vigilance of the authorities. Moreover, the program must be capable of completion within the year, for the next year will inexorably bring a new set of returns to be examined.

There are no simple criteria to govern the selection of those returns to be investigated. Experience will suggest certain classifications and critical factors within those classifications. Thus, employee returns will usually not require much checking if the withholding procedure is effective, except as respects such factors as correctness of dependency claims or the expense accounts and disguised compensation of higher salaried employees and directors. Certain professions and businesses will warrant more scrutiny than others. It may be feasible to plan both for an annual examination of the most important returns and for reaching as much of the balance of the business returns on a schedule which insures that each business will be checked once in a period of years with all of the years in the period examined when that check is made. The period would vary with the length of the statute of limitations on additional assessments. Sources of information carefully collected in the tax offices—such as records of property sales, unusual bank transactions, large purchases of insurance, foreign currency transactions—will point to the selection of particular returns. The use of a system of estimated incomes, described later, will suggest other returns. Finally, a number of returns should simply be selected at random and examined, both to gauge the effectiveness of the planned programs and to make escape from detection of non-compliance more hazardous and less

predictable. Of course, if the taxpayer is not initially required to compute and pay his tax, then in a sense every return must be "audited." But in these cases the "audit" can of necessity only be primarily a computation of the tax from the data appearing on the return. Consequently, as far as possible the system should call for initial taxpayer computation and payment.

When a return is selected for examination, the investigation may take several forms. Matters on the face of the return which appear suspicious or incorrect could be handled by correspondence, especially for the smaller returns. Or such matters may be handled on an "office audit," with the taxpayer requested to bring to the tax office the data necessary to verify certain items. The most effective audit, and thus the method to be used for the returns requiring a careful check, is the "field audit" at the taxpayer's place of business. This is an intensive check of the taxpayer's records and business and should be conducted by a trained accountant. It may be possible effectively to combine audits of related taxes whose returns contain similar information. With respect to these audits, the tax agent should be given a check list of items which experience indicates require scrutiny, such as the wrongful deduction of reserves, the charging to expense of expenditures which should be capitalized, reported gross profits margins varying with those customary in the trade, or any variation between the closing inventory for one year and the opening inventory for the next year. This type of investigation presupposes effective record keeping by the taxpayer. Consequently, its utility will vary directly with the ability of the tax office to impress upon taxpayers the need for keeping adequate records and to enforce record-keeping requirements imposed by the tax law. Experience indicates that this success comes easiest with large and medium sized business, hardest with small concerns. Often, in the case of these small concerns successful administration by either the national government or local governmental units of excise taxes involving gross receipts and other sales data will be the prelude to effective application of an income tax.

Where adequate taxpayer records are lacking, the ingenuity and resourcefulness of the administration are challenged. It is not without weapons, however. It may attempt to reconstruct an average week, even a typical day, for the taxpayer's business and apply the resulting profit reasonably to the entire year. It can resort to the use of "estimates," informed guesses as to what profit the taxpayer's business should yield in the light of a comparison of its characteristics with those of businesses whose profits are known. This technique of estimates is familiar to most administrators and is used with varying degrees of success. The variation is largely in the care and precision with which the estimates or standards are built up, and the degree of control possessed by the tax office in their application. Thus, a method which is crude but helpful in the sense that it does produce some

check is that of the classification of businesses into various profit groups with the aid of trade associations or guilds. Too often, however, under this procedure the control rests with the trade association and not the tax office, with possibilities of favoritism among taxpayers or down-right bargaining between tax office and each trade operating as a unit to fix its share of the tax as compared with other trades. As rapidly as possible the tax office should pass beyond this stage to the compilation of its own standards, based on all of the workable data including investigations of taxpayers having proper records. With this refinement of standards accomplished, the next level of progress is to confine their use as far as possible to the selection of returns for individual audit rather than for the basis of the tax determination itself. Thus, the returns should initially be compared with the standards, and those returns showing considerable variation should be the subject of an office or field audit in which the taxpayer's actual situation would be decisive in the determination of his tax. It must never be forgotten that an income tax is an "individual" tax based on the particular taxpayer's net income and not on someone else's profit. The standards may help in approximating the determination of a taxpayer's net income, but the methods should not be confused with the goal. That goal is not the most accurate standards—it is the most accurate determination of the particular taxpayer's income.

A refined method of determining an individual's income in the absence of adequate records, but one requiring skill in its application, is the "net worth" technique. This may take several forms. If a taxpayer's net worth (assets less liabilities) is known with accuracy for a prior period, it can then be compared with his present net worth. The difference plus consumption items in the interval should represent his receipts. Or, expenditures over a period could be compared with sums stated to be available for spending and the excess of the former would then give a reasonable approximation of the income not disclosed. This "net worth" technique is obviously tailored to the individual's situation. Its effectiveness is balanced by the time and skill which it demands, and hence it can be used only in the most difficult and important cases. However, its utility could be greatly increased by a requirement that every individual with income over a certain level and every business be required annually to file a balance sheet along with the tax return. This would provide a starting point for net worth computations.<sup>4</sup>

The process of investigation can be materially assisted by statutory aids. Thus, tax offices should have the authority to obtain information from banks, insurance companies and other financial agencies, from stock brokers

---

4. Morag, *Some Economic Aspects of Two Administrative Methods of Estimating Taxable Income*, 10 NAT. TAX J. 176 (1957), contains an interesting discussion of the consequences for tax policy in the utilization by administrators of presumptive estimates and net worth techniques.

holding securities for clients, from corporations, and so on. "Information returns" should be required from those having significant financial relationships with the taxpayer, such as payors of dividends and interest where these items of income are not collected exclusively by withholding. The use of anonymous bank accounts, inadequate record keeping as to corporate shareholders, and other institutional devices facilitating tax evasion should be prohibited.

#### *D. Resolution of Controversies Between Taxpayers and Tax Offices*

The process of audit and investigation described above will result in the determination of the taxpayer's tax liability as the tax office views it. The taxpayer will then be called upon for payment of this amount, either as the entire tax or in those countries in which the taxpayer initially pays and computes his own tax as an additional tax liability. In turn, some of the taxpayers will agree that the amounts requested are properly due. But others will disagree and thus controversies will spring into existence between the tax office and the taxpayer. Accordingly, a procedure for handling and resolving these controversies becomes the next stage of tax administration. The procedure will necessarily depend on the concepts of administrative law and judicial review of the particular country. But essentially the procedure should furnish internal methods of settlement within the administrative system and external methods of judicial consideration when a settlement at the administrative level is not reached. Whatever may be the precise steps adopted, however, one factor is paramount—the taxpayer must have complete confidence in the fairness and impartiality of the procedure as a whole. He cannot be placed at the mercy of a single tax official; he cannot be faced with arbitrary administrative action unchecked by judicial review. A fair albeit a firm system of resolving these controversies will instill taxpayer confidence in the tax administration. With that confidence will come an increase in voluntary taxpayer compliance, and thus a basic step forward in successful administration.

The internal administrative machinery for the settlement of these controversies should in essence consist of a series of hierarchal reviews of the case. The taxpayer should be able to discuss his case with the agent who investigated it, then with a supervisor of that agent, then with a higher administrative echelon. There cannot, however, be an endless series of successive considerations of a case, and hence the number of layers of review must be limited. Under such a system properly conducted, most controversies should be settled at the first stage and a majority of the balance at the next stage, leaving only a relatively small number to be considered at the highest administrative level of review. Here all but a very small percentage should prove capable of settlement—the remaining few cases, relatively speaking, must go on to the courts. The skill and experience of

the administrative officials who consider these cases should, naturally, be the greatest at the top level, for only the most difficult cases should reach that stage. Where needed, checks against bribery or pressure for favoritism should be adopted. Thus, it might be required that the discussion with the investigating agent take place in the tax office with a higher official present so as to prevent a corrupt arrangement with the agent. Or, if the problem is pressure for favoritism at higher levels, the agent's original report would be sent to a special board for its information so that the higher officials are in a position to resist improper pressures to reverse the agent's report. The tax administration should be able at any stage of these reviews to assert any additional amount of tax that it believes owing on the basis of the information developed in the administrative review of the taxpayer's case. This will make the consideration a two-way street and thus discourage routine taxpayer appeals.

The discussion and consideration of a case should be on a conference basis rather than a formal hearing. There should be a full discussion of the issues and facts. The taxpayer should be given a clear statement of the issues, he should present his case, using the material, written or oral, that he believes pertinent, and after discussion the tax official should reach a decision. Very often the case will be "settled," that is each side will give way on doubtful points and a compromise of the issues in controversy thus reached. Many tax questions are clouded in uncertainty—the facts may be difficult to ascertain; the application of the law to the facts may be unclear; the issue may involve essentially an educated guess, as in the case of the determination of market values. The solution of these doubtful matters by a settlement is quite proper provided the settlement is reached by a careful weighing of the strength of the administrator's position and not by favoritism. Consequently, it is appropriate to have a special group check the quality of these settlements by a post-settlement sampling of the settled cases. Implicit in this procedure is a requirement that at each stage a report be written by the official handling the dispute. These reports should summarize the disputed issues, the basic evidence and arguments on each side, and the areas where agreement has been or is likely to be reached. These reports will aid in avoiding abuses by officials and will tend to assure greater uniformity in the application of the tax laws, provided an appropriate procedure is established for the review of the cases considered.

The proper resolution of a controversy will be more readily achieved if the taxpayer is represented by a person intelligently informed as to tax law and tax procedure. Hence, rules governing the qualifications of persons as taxpayers' representatives are needed. These rules should place stress on restricting taxpayer representation as far as possible to lawyers, accountants, and others who possess the requisite skill and tax knowledge, and on discouraging representation by those whose only stock in trade is influence.

In connection with this administrative procedure for the resolution of controversies it is often urged that fairness would be achieved by having the controversies heard by "citizen boards." It is said that these panels of prominent local citizens would prevent the taxpayers from being unfairly treated by an arbitrary administration. It is questionable whether this procedure is desirable. It might work where there is a long tradition of public duty and intelligent lay participation, and where the board's function is to aid in ascertaining the facts. But most likely the use of this system in countries attempting to improve tax administration would not be wise. At best, it divides responsibility between tax office and local citizenry, so that each can blame the other for any failures of administration. At worst, it could lend itself to placing the taxpayer at the mercy of local prejudices, to placing the tax administrator at the mercy of reciprocated favors among neighbors, and to strengthening tendencies in the cities or villages to domination by cliques. The responsibility for tax collection and administration is a government responsibility—it is dangerous to diffuse that responsibility among non-governmental officials, especially at the hearing level. The check against arbitrary, erroneous, or unfair administrative action lies with the judiciary and not with boards of local citizens.

As respects the judicial review of tax controversies, the procedure adopted will naturally be shaped by the judicial system of the country. Experience has definitely shown that tax cases require special procedures on the part of the judiciary. Tax cases are complex and difficult. Their resolution demands an informed knowledge of the intricacies of the statutory laws and regulations in the tax field. Hence, at the lower court level, it is preferable to have either specialized tax courts or at least tax judges who can concentrate on these cases. The avenues of appeal to the upper courts should be clear and efficient, so that differences among the lower courts may be readily resolved. The tax system applies to many taxpayers and it inexorably reaches those taxpayers year after year. Hence, unless controversies are speedily settled, tax cases will soon clog the judicial system. Any delay in decision, moreover, will rapidly create many new tax controversies as tax year succeeds tax year and as other taxpayers face similar problems. Also, as respects review by the upper courts, the taxpayer should, at least in important questions, be entitled to a review by an independent judicial tribunal.

Uniformity of judicial decisions and speed in reaching those decisions are essential to effective tax administration. The proper answer to the question of statutory interpretation in the tax field—which is the issue in most tax controversies that reach the courts—is generally debatable. What is needed, therefore, is a prompt and definite judicial answer rather than long delay in the search for the "true" answer. If the judicial answer is too



wide of the mark, the legislature will correct it so that an erroneous answer is not fatal. But the system cannot function if no answer is forthcoming.<sup>5</sup>

Another important aspect in the treatment of controversies is the reduction of controversy through administrative interpretation of the tax laws. The tax administration should as far as possible anticipate doubtful points of statutory interpretation and make its view on those points clear. A taxpayer aware of that view is at least on notice of the tax consequences of conduct on his part. Very often he can in the light of that interpretation shape his affairs and plan his activities covered by the tax so that controversy is thereby avoided. In fact, successful tax administrations have a prospective "ruling" system under which a taxpayer can present a planned transaction to the tax authorities and obtain their view of the tax consequences. If the tax cost is too high, the plan may be dropped or altered and controversy avoided. At the same time the tax authorities are thus constantly kept informed of the areas of the tax law regarded as uncertain by taxpayers and of the problems thus created. They can as a result keep abreast of potential tax controversies and attempt to minimize or eliminate them by administrative action or statutory change. These rulings, however, should be published and made generally applicable, so that they cannot be used to provide special treatment for favored taxpayers.

#### *E. Collection of Taxes*

The final stage—in fact the goal—of tax procedure is the collection of the tax. The sure sign of ineffective tax administration is the presence of a very large delinquency in tax payments, for it indicates the lack of taxpayer respect for the tax system. The taxpayer in effect is acting on his belief that the administrative machinery may bark, but that it has no bite. In large part the solution for tax delinquency lies in providing the bite. In this sense effective tax collection is a facet of the larger problem of providing adequate penalties, to which reference will later be made. But tax collection has its special procedural aspects, and here also attention to proper techniques and routines is essential.

To begin with, the delinquency in payment must be recognized. Hence, the taxpayer lists and registers referred to earlier must be so maintained that a taxpayer's non-payment may immediately be noted. As soon as the payment date has passed, a formal demand should be made. If this step is not effective, prompt and firm procedures to follow that demand must be devised. The taxpayer must be made to see that his delinquency is known, that it is serious, and that it will not be tolerated. If the administration is casual and unconcerned about collection, the taxpayer will more than match that

---

5. See papers on Judicial Guarantees of Taxpayers, INTERNATIONAL FISCAL ASSOCIATION CONFERENCE, Rome, October, 1956.

mood in his dilatory attitude toward payment. If the administration is alert and firm, taxpayers will react to that pressure and bring order into their payments.

Firmness requires the presence of sanctions and a resort to those sanctions when necessary. Hence the tax law must provide for the imposition of liens on real property where there is a registry system, for the distraint of property, for the garnishment of wages and salaries, and the like. It can also resort to collateral devices, such as the refusal of certain government services if taxes are unpaid. Above all, it must make non-payment expensive. The taxpayers should not through delay in payment in effect secure an interest-free loan from the government. Hence interest at a rate effectively higher than the commercial rate should be charged automatically for late payment. The tax administrator must, however, be intelligent in his firmness. Extensions of time, at interest, should be available to taxpayers who can show good cause for an extension. An honest but hard pressed taxpayer should be able to work out a schedule of installment payments arranged in the light of his financial condition. Where there are simply few or no assets available, the tax should be compromised, i.e., written-off, rather than carried for years in the future.

Another phase of the collection problem is proper integration between assessments and collection procedures. Those in charge of assessments should not permit unreliable assessments to be passed on to the collecting officials where the result can only be non-collection. It is simply a waste of effort all around to have most of the assessments returned for cancellation because they were unrealistic at the outset. On the other hand, the collection authorities should demonstrate initiative and enterprise in their search for the taxpayer. Sometimes a collector will return an assessment as uncollectible because of a "wrong address" without making any effort to locate the new address of the taxpayer. Also, bills which are for such a small amount that the cost of collection is out of all proportion to the tax involved should not be submitted for collection. In these and other ways proper working relations between these two branches of tax administration can promote the overall efficiency of the system. As indicated later, it is desirable to place these two activities under one agency.

The tax system itself should not be inherently conducive to tax delinquency. If the system attempts to collect last year's tax out of the current year's income, it is bound to run into collection difficulties when the income of the current year drops below that of the prior year. This may occur where the taxpayer becomes sick or unemployed, where his business or crops have suffered, or where there is an overall decline in the economic situation. Under such a system the taxpayer in a sense is always in debt to the government and any adversity in his fortunes will at once highlight that debt. As far as possible, therefore, the tax system should be placed on a current

basis, with the current year's tax being collected at current tax rates out of current income. In the case of an income tax, this can be achieved by withholding on certain forms of income, such as wages, interest, and dividends, and by a system of estimated tax payments based on estimates of current income, with a reconciliation on the final tax return. In this fashion the taxpayer is largely current in his taxes and a tax debt cannot arise. Where the tax administration finds that taxpayers habitually do not report their full incomes, it can be provided that the estimated current income must at least be as high as the corrected income of the prior year. In addition, the law could provide for percentage increases or decreases in the base of prior year's income to match a general rise or decline in the economy for the current year. The objective here is a reasonable estimate of current income, with the final tax return for the year showing the actual income once the year is closed. The taxpayer may then owe some additional tax or be entitled to a refund if he has over-estimated his income. The refund in turn could be applied to the payment of the next year's estimated tax.

#### *F. Penalties*

The tax administrator must be equipped with a variety of effective penalties which he can wield intelligently and firmly. However, it is usually at this point that most tax laws are found wanting. The penalty provisions were established years ago, and quite often consist of small lump sum amounts which do not serve as effective deterrents. The entire system of tax penalties will thus generally require legislative overhauling. The various violations must be catalogued, such as failure to file a return; failure to pay the tax on time; failure to withhold taxes or to pay over withheld taxes; deliberate action to avoid the tax through the intentional filing of a false return; fraudulent record keeping; and so on. An appropriate civil penalty which takes account of the severity of the offense and can be administratively imposed must then be provided. Often as respects these civil monetary penalties, a combination of lump-sum penalties and percentage penalties varying with the amount of tax will be the most desirable. The percentage penalty could operate over a range, with discretion in the administrator to choose the appropriate figure. Thus, a negligent failure to file a return could involve a five dollar flat penalty, plus a penalty of from ten to twenty-five per cent of the tax; an intentional failure to file a return, a starting percentage of twenty-five per cent; the filing of a fraudulently incorrect return, a starting percentage of one hundred per cent.

For most taxpayers a civil monetary penalty which reaches the pocket-book is usually an effective deterrent, but for some these monetary penalties while unpleasant are not sufficient. Consequently, in most countries with effective tax administrations, willful evasion and fraudulent conduct are criminal offenses punishable by fine and imprisonment. Moreover, and

certainly to the point, prosecutions are brought and jail sentences imposed. The failure to apply the criminal penalties on the statute books can have a demoralizing effect. In contrast, it is generally found that a few successful prosecutions and the attendant publicity can have a most exemplary effect. These two types of penalties, civil monetary penalties and criminal penalties, are not alternatives. Where criminal action is taken, the offending taxpayer should also be required to pay the tax and the accompanying civil penalty.

#### IV. THE IMPORTANCE OF DETAILS

The preceding section has considered some of the essential steps in the overall procedure of tax administration. In a sense it has dealt with broad problems and with major issues of administration. But in a good part successful tax administration is the cumulative effect of hundreds of minor details properly executed. Too often these details are neglected in the planning of broad reforms and top level projects. Frequently it is only the office of the tax administrator and his immediate assistants which is "reorganized" and the details of the day-to-day work of the tax officials at the routine level completely overlooked. A few examples may illustrate the point.

Most taxpayers generally come into contact only with the tax officials in the local tax offices. Consequently, the daily operation and organization of these offices are important matters. But in many countries insufficient attention is paid to the routine operation of these offices. Once their situation is examined, however, many questions will arise. Are the offices properly arranged from the standpoint of space utilization? Is there a place for taxpayers to present their problems in a confidential, orderly way? Are the various work processes and the personnel so arranged as to location within the office that the daily work flows efficiently in an orderly current? Are such matters as the handling, sorting, and filing of documents properly organized so that the documents can be quickly stored and quickly located when needed? Are there mechanical shortcuts and aids available to facilitate these operations — such as the use of different colors for the different returns or documents, or the use of standard sized papers chosen with an eye to handling and filing? How efficient is the office equipment that is being used and are more modern devices available? Are equipment and personnel used effectively with an eye to the variation in peak periods and slack periods? Are appropriate travel facilities available for those officials who must make field investigations of returns or check on delinquent taxpayers?

The above questions are but illustrations of the type of details that require effective handling for the orderly conduct of the tax offices. One method of dramatizing the proper attention required for these details and of improving tax offices generally is to select a few offices as "model offices." These model offices should be overhauled and placed in effective daily

operation. The officials of the other offices can then inspect and observe the model offices and carry back the improvements to their own offices. In effect the model offices serve both as guides to efficient operation and as targets to be attained by the remaining offices.

Finally, attention should be paid to the criticisms of taxpayers with respect to the operations of the tax procedures as they bear on the individual taxpayer affected. Too often these objections are regarded as mere resentment caused by the tax burden itself. But quite frequently the criticisms are occasioned by the irritations created through inefficient operation of the tax system rather than its monetary impact. Usually, persistent taxpayer complaint regarding "red tape" or inefficiency will be traceable to objectionable routines, though the complaints may have an exaggerated ring. Improvement in operation can be aided by an intelligent consideration of taxpayer reactions.

## V. THE ASPECT OF PERSONNEL

It is often argued that the problems of administration in underdeveloped countries are basically problems of personnel. The foregoing discussion is an effort to demonstrate that the procedure and details of tax administration are highly significant, and that most tax systems could stand marked improvement in these respects. But it is obvious that procedures which are orderly and effective on paper are subject to the human factor of the personnel who administer those procedures. Hence the problem of personnel does occupy a key role in tax administration. Here, the surveys of technical missions usually contain the same critical catalogue of the faults to be found, such as poor pay, lack of training, inefficiency, understaffing as respects able people and overstaffing as respects incompetent political appointees, and so on. In many countries the talent has steadily been drawn away from the tax agencies and into the central banks and development authorities. The surveys urge higher salaries and more skilled personnel. Yet, while sympathetic and often optimistic, the surveys recognize that these goals are difficult to obtain. Although the future, viewed realistically, is indeed a troubled one, is it possible, in conjunction with the basic improvements suggested above and the changes in public attitudes considered later, to adopt measures which will improve the personnel aspect of administration?

First, as to the matter of pay scales. The results of inadequate salaries are obvious: for example, they attract mainly the incompetent; they lead to part-time employment with its problems of divided loyalties and inadequate attention to the government's work; they breed dishonesty, bribery and corruption. But with hard-pressed budgets, how can a government avoid the vicious circle of low pay — incompetent personnel — undersirability of increasing the salaries of an incompetent staff? There would seem to be some avenues of escape. Salaries higher than the norm could be justified for

tax personnel on the ground that the resulting increase in efficiency will produce increased tax revenue. Where salary scales must be kept uniform among departments, the up-grading of the revenue positions is equally defensible. It is generally found in many countries that while the importance and difficulties of revenue tasks have increased, there has been little systematic re-grading of positions in the light of increased responsibilities. As a forerunner of the above, increases could be given to specially selected individuals to demonstrate the effectiveness of having skilled personnel working under appropriate salary scales. Proper travel allowances will often be a decisive factor and will eliminate the obvious distorted selection of cases that results when the cost of travel in investigating a case must be borne by the employee.

Attempts have been made to meet the salary problem by a bonus or commission system under which an individual receives a percentage of the additional taxes he assesses or collects. The disadvantages of this device are serious; the tendency toward arbitrary action, with resulting public hostility and overall inefficiency through the necessity of meeting the taxpayers' objections to the unfair assessments. Moreover, only those tax personnel engaged in assessment and collection can benefit from the plan.

If salary scales can be improved, then the recruitment of personnel must match those scales. Systematic procedures for attracting qualified and able individuals with an interest in the work must be adopted. Job standards must be devised, so that examinations and other objective testing of applicants can be substituted for political nomination. Close liaison should be maintained with universities and business schools so as to induce capable graduates to enter the tax service. Promotion policies should be coordinated with recruitment, so that recognition of talent and effort within the service is coupled with the flexibility obtained through the new ideas and talents of those chosen from outside the ranks.

The next step is the institution of appropriate training procedures. Tax work is technical and specialized. An effective recruitment policy will supply persons with the requisite intelligence and aptitudes, but it cannot be expected to yield fully-trained tax officials. Consequently, the personnel must through training be given an understanding of the operation of the system as a whole, of the relation of their specific jobs to that system, and of the requirements of their jobs. The training must be conducted in a systematic fashion by instructors qualified for the task and supervised by an official whose sole responsibility is that of the training program. The instruction should be regarded as a recognized part of the trainee's position, and not an added chore to be met at odd moments. It should offer incentives to advancement and new duties. The material should be suited to the personnel under instruction, with appropriate recognition of the differences in training required for non-specialist employees, supervisory personnel, tech-

nical personnel needing a knowledge of tax law and tax accounting, and so on. Various types of instructions must be utilized — full-time training schools for new employees or those selected for advancement, lectures and on-the-job training, instruction manuals, etc.

The aspect of delegation of authority is directly related to these personnel matters. The director of a tax office may consider himself as the sole person possessing capability and authority, a view sometimes rationalized on the basis of the responsibility he must bear. He then makes the decisions in each case and decides all the details of office management. This personalization of the tax office in the person of the director has important disadvantages. It adversely affects the morale and initiative of the other officials. It results in inefficiency and low output. It opens up avenues of abuse, since often the director is either chosen from the social and economic level of the wealthier taxpayers or is desirous of attaining that level, so that the concentration of authority makes for considerable pressure on the director as well as considerable opportunity for favoritism. Here also a vicious circle operates, in that the system is defended on the basis of inadequate personnel to warrant the delegation of duties from the director. One answer, building on the policies of recruitment and training described above, is that of manuals of procedure which recognize the necessary delegation of authority. These procedures should limit the authority of the director to inject himself into substantive decisions in particular cases, except under prescribed conditions. At the same time they should delineate the role of the director as a creative, energizing factor in the overall conduct of the office. The advantages that lie in freedom from routine, in the abandonment of procedures requiring him personally to sign every letter or document, should be emphasized.

Hovering over the entire field of tax administration is the spectre of dishonesty and corruption. As taxes rise, the opportunity to escape the tax by the payment of a lower amount in the form of a bribe is inevitably present. Moreover, as the taxes grow in complexity and as discretion and judgment on the part of the tax official play a greater role, the ability of an official to affect the result in a particular case without outward indicia of purchased favoritism is heightened. The personnel policies considered above are all antidotes to these temptations. Yet even countries with good personnel policies and traditions of fine administration have seen corruption in the form of bribery and influence emerge in unexpected places. Consequently, an effective system of discipline and personnel investigation becomes, unfortunately, a requisite to effective administration. But it must be recognized at the outset that unless it is crystal clear to all employees that complete honesty is demanded and that those in authority are unwaveringly firm in that demand, no system of disciplinary procedures and methods will be effective. The most effective method of achieving honesty is the

severe punishment of dishonesty. Moreover, the punishment must extend not only to the government employee but to the taxpayer or his representative who is a party to the dishonesty.

As to internal procedures, there should be a specifically trained corps of investigators acting as an inspection staff to check for possibilities of abuse and corruption, along with inspection for inefficiency. The work of the tax officials should be sampled from time to time. Rumors and informers' tips should be pursued. Care must be taken, however, that these controls deter dishonesty but not the appropriate exercise of discretion. Officials should not feel that they will be "second-guessed" on every decision they make, or that the investigator will turn hindsight or a different view of the problem into a suspicion of dishonesty. If the investigatory process exceeds its proper bounds, then officials will fear to make any decisions in favor of taxpayers and effective administration will be stultified.

As a supplement to individual checking, it is desirable to require each employee to submit a net worth statement at the time of his employment and periodically thereafter. These statements are then available as the basis for an investigation when suspicion arises, as when an employee's standard of living is beyond that which his salary and previous wealth would indicate. While the net worth statement may not be popular with all employees, it acts as a deterrent to temptation since its mechanical impact is clearly obvious. As a further measure, care should be taken to audit the income tax returns of as many tax officials as possible. Generalized sources of income, such as gambling, should be carefully scrutinized. Finally, a proper system of penalties should be available, ranging from criminal action, dismissal, loss of pay or suspension to reprimands and warnings.

## VI. THE ASPECT OF MANAGEMENT

Given a proper framework of administrative procedures and capable tax officials to operate those procedures, the next aspect of tax administration is that of overall management. The functioning of the system must be viewed as a whole, the parts must fit together, the entire organization must constantly be scanned for defects and improvements, the machinery must be intelligently guided toward the effective fulfillment of the ever-increasing burdens that will inevitably fall upon it.

Income tax administration starts as a highly centralized process involving relatively few taxpayers. Soon, however, especially in geographically large or heavily populated countries, the issue of centralization versus decentralization must be faced: How much of the detailed operations must go on at headquarters and how much may be properly conducted in the field? Which day to day decisions, especially those involving the application of law and regulations to particular cases, will be made at headquarters and which in the field? The answers to these questions, in the sense of the



degree of decentralization that is appropriate for a given country, will largely turn on inexorable factors: the number of taxpayers, their geographical location, and the technical state of communications and transportation. Continual observation of these factors must be made to solve the basic problem in the decentralization issue, that of the rate at which decentralization should progress. The accompanying problems are the very complex ones of effective administrative management of a large-scale organization. As decentralization progresses, the problem of effective central direction becomes more important. Headquarters must now conduct a unified field operation — there must be uniformity in the procedures followed in the field, in interpretations applied, in assessments and settlements made. In practice, effective controls must rest on the adoption of orderly procedures, formulated in writing and made available to all of the offices involved. Manuals of operation which inform and instruct the field organization are thus essential to centralized direction. In effect, there must be an adequate and constant flow of information from headquarters to the field.

Coordination between the field and headquarters will not be achieved if the headquarters operations are themselves uncoordinated. Yet, in many countries effective central direction is lacking because authority is divided among several agencies. Audit and assessment is in one agency and collection is in another agency; some taxes are under one authority and other taxes under different control. This parceling out of the functions of tax administration must be reversed and one central agency given responsibility for the task. The various departments within that agency must in turn be operated on an integrated basis.

The flow of information and instruction from headquarters to the field offices has been mentioned above. But supervision is a two-way street, and there must be a flow of information back from the field to the central staff. This information essentially involves reports of the activities of the field offices, so that their performance may be understood and weighed. The reports must contain sufficient details to be informative, yet not so voluminous as to enmesh both field and headquarters in a mass of wasted data. The reports should, for example, indicate how many returns have been filed, how much tax paid, how many returns audited, how many added assessments made, how much additional tax collected, and so on. They should be arranged so that they can readily be filled out by the field offices and as readily comprehended at headquarters.

These reports will enable the central body to gauge quantitatively the effectiveness of field operations as a whole and to spot incipient danger points in advance. But such progress reports and charts must be amplified by detailed inspections of each office. The top officials themselves should annually visit a number of offices, both to retain the “feel” of the tasks

and to improve morale. In addition, an inspection staff of competent officials should be maintained. Inspectors should visit each office to examine thoroughly the procedures followed, to check for compliance with instructions, to measure the overall quality of the work done and the general efficiency of personnel, and to catch weaknesses in instructions when tested by the problems of daily operation. The role of the inspectors is thus both critical and constructive, with an eye to desirable innovation and improvement as well as to substandard performance.

Finally, an extremely important phase of management, and the one that probably shapes the destiny of the entire system, is that of intelligent programing and planning for the administration as a whole. Effective administration is not achieved by accident. It must be reached by forethought and care. Hence, the headquarters should have a planning division, be it an individual or a unit, which is largely freed from the routine of daily tasks and which can thereby concentrate on future developments. Proper planning is not a matter to be fitted into the interstices of a director's busy day, but rather is a recognized task requiring adequate time and attention. As new taxes are considered, the planning unit can analyze their feasibility and requirements from the standpoint of administration — what kinds of returns will be needed, what instructions to taxpayers, how many additional tax personnel and with what training, what arrangement must be made for collection and payment, and so on. This advance planning permits a more informed decision as to the choice among possible new taxes, or as to the content of the tax selected. It also permits an orderly introduction of the tax into the activities of the taxpayers and the operations of the tax offices, instead of a confused and haphazard beginning. The planning unit should also constantly review existing operations in order to ascertain shortcomings and to introduce corrections. Thus, it can foresee the exchange of equipment and personnel among offices as the needs for them vary from place to place and time to time.

In another direction, the planning unit must seek ways to measure the effectiveness of the entire system. It must constantly ask itself such questions as: Just how effective are tax collections and taxpayer compliance? What is the correct number of taxpayers and what proportion of them are being reached by the administration? What is the degree of tax avoidance? These are difficult questions and even the most efficient of tax administrations do not as yet possess the statistical tools necessary to their answer. But progress is being made in the use of statistical analysis to reveal ways by which to measure present performance and realistic goals. Thus, analyses of national income and its components can provide some standards. The task of the planning unit, in cooperation with other agencies of government, is constantly to develop its statistical information, both as to coverage and accuracy, so that a realistic appraisal of tax administration is possible.

VII. THE ASPECT OF NATIONAL ATTITUDE  
TOWARDS THE TAX SYSTEM

The prior discussion has considered various aspects of tax administration and has indicated possible points of improvement with respect to existing procedures. But tax administration does not function in a vacuum. Its relationships at every turn are with the public, and since the combination of taxes reaches nearly every individual in one way or another, the administration finds itself dealing with the nation as a whole. Hence, inevitably its operations and effectiveness are affected by the attitudes of the nation towards the tax system. It is here that we enter on the broad currents of human affairs, on the play of history and tradition with respect to the interrelationships between citizenry and government. For present purposes we must acknowledge that national attitudes towards the tax system and tax administration differ, and that voluntary tax compliance will differ from country to country. We can appreciate that a full understanding of the nature, extent, and causes of these differences would be extremely helpful to the improvement of the existing situation. But that full understanding has yet to be achieved. Hence, as respects this larger problem, while not completely knowing the causes we must realistically face the effects. This means a recognition that in many countries the task of tax administration is adversely affected, and seriously so, by the prevailing tolerance of the public toward non-compliance and avoidance.

But while tax administration is thus affected by these national attitudes, it is equally true that the attitudes can in turn be affected by tax administration. All that has been said above is pertinent here. Rational and efficient procedures, higher personnel standards, better management, improvement in relations with the public and in the daily contacts between tax official and taxpayer, can operate to increase the public respect for the tax administration. Moreover, once the tax administration has been placed on a sound basis, it is in a position to assert that compliance must be forthcoming. Such an assertion would hardly be tolerated, or even taken seriously, as long as tax officials were themselves inefficient and corrupt. But if the administration has brought stability and honesty to its own operations, the self-respect thus achieved can form the foundation for its demand of respect and compliance from the taxpayer.

That demand will be considerably more effective if there are sanctions that can be applied when voluntary compliance is not forthcoming. It is here that the penalty provisions of the tax laws discussed above play a key role. But the presence of penalties on the books is not a self-operative sanction; there must be a will to enforce these penalties. And here the tax administrator must look to the heads of state for his answer. If there is a serious determination at the topmost political and governmental levels to bring about improvement in the tax system, then an affirmative answer to the use of

penalties will be forthcoming and tax compliance will commence to improve. If that determination does not exist, the best that can be expected is that the machinery of administration will be at hand ready to be effectively utilized on that future day when the tide of government changes.

A tax administrator faced with the task of changing taxpayer attitudes should seek allies in those professions interested in the tax field. Primarily, these are the legal and accounting professions, and the economists in the academic profession. All of these professional groups should interest themselves in the tax system and its administration. They should understand its operations and be able to criticize intelligently its activities, and they should aid in interpreting that system to the public. Such aid involves the writing of articles, the formation of professional organizations to conduct tax discussions, and the education of trade and business associations, as well as the advice given to individual clients. The universities should institute courses in the legal aspects of tax law as well as those in fiscal policy. The accounting profession should encourage the development of the role of independent certified or chartered public accountants. It should also assist in the standardization of accounting practices, and in the preparation of model record books and forms. These professional groups must realize that a significant share of the task of tax administration falls on them, and in these ways and many others they must aid the government in its striving for effective administration.

#### VIII. CONCLUSION

The foregoing is necessarily a brief summary of certain problems in the broad field of tax administration in underdeveloped countries. Even so, it may suffice to indicate both the importance of these problems and the need for intensive research respecting the many aspects of this part of the fiscal structure. In this connection the Harvard Law School International Program in Taxation,<sup>6</sup> in cooperation with the Fiscal and Financial Branch

---

6. This program, which is a part of the Harvard Law School's broad Program in International Legal Studies and which operates in close cooperation with the Fiscal and Financial Branch of the United Nations Secretariat, seeks to combine legal and economic studies of tax law and administration with the training of foreign tax officials in practical ways that will aid in the improvement of tax policies and administration throughout the world.

As a major aspect of this work, the Program provides intensive training in the problems of tax policy, law, accounting and administration for a select group of foreign officials. Most of the participants in this training, which has become an integral part of the recognized technical assistance programs, are nominated by their governments and receive scholarships and fellowships from the United Nations Technical Assistance Administration and the United States International Cooperation Administration. Other participants receive grants from their own governments and from private organizations. Graduate students, Rockefeller and Fulbright scholars, and others also take part in some of the training activities. The Program's own training activities are supplemented by regular courses in United States taxation, public finance, accounting, etc., at the Harvard Law School and other departments of the University. As an important part of his training activities each participant undertakes a detailed research project on an aspect of his country's fiscal and tax problems. Those officials whose primary responsi-

of the United Nations Secretariat, is engaged in the preparation of a *Manual of Income Tax Administration* which is especially designed for use in underdeveloped countries. The training activities of the Harvard Program conducted for foreign tax officials, largely from underdeveloped countries, have also emphasized the problems of tax administration. The work on this *Manual* and the interchange of ideas and experiences in the training program have indicated many fruitful topics for further study. It may be appropriate here as a conclusion simply to refer to some of these topics in summary fashion. The following list is not intended as a complete agenda for research. Rather it is illustrative of what are believed to be useful lines of inquiry. These topics relate primarily to those problems of tax administration which lie at top levels and which are at the core of the relationships between substantive tax policy issues and tax administration.<sup>7</sup> They do not concern the day-to-day administrative operations and managerial problems which are primarily the concern of the *Manual of Income Tax Administration* mentioned earlier. The topics follow:

#### A. ORGANIZATION FOR TAX POLICY FORMULATION AND MANAGEMENT

A consideration of some of the organizational factors essential to central formulation and direction of tax policy. The following are examples:

##### 1. *Research Facilities and Technical Services*

###### a. Effective use of statistics

(1) For forecasting revenue yields and for determining the distribution of the tax burden in relation to the distribution of national income, etc.

(2) For controlling tax audit operations through the selection of those geographical areas, income levels, taxpayer groups, tax problems, etc. most appropriate for administrative scrutiny.

---

bilities are administrative observe tax administration in operation in various offices of the United States Internal Revenue Service and the Canadian Ministry of National Revenue.

Since the inception of the training activities in 1953, about 60 tax officials from 30 different countries will have participated in the training program as of the end of 1958. See INTERNATIONAL CENTER FOR TAXES, December, 1957. HARVARD LAW BULLETIN.

Related activities of the Program include the preparation of volumes in the WORLD TAX SERIES, a series of descriptive reports of the tax systems of various countries, of which those on the United Kingdom, Brazil and Mexico were published in 1957; research in the taxation of international investment (studies in this area include BARLOW & WENDER, FOREIGN INVESTMENT AND TAXATION (1955); GIBBONS, TAX FACTORS IN BASING INTERNATIONAL BUSINESS ABROAD (1957); United States INCOME TAXATION OF PRIVATE UNITED STATES INVESTMENT IN LATIN AMERICA (United Nations, ST/ECA/18, 1953), and work under preparation on the operation of the foreign tax credit device); research in various aspects of domestic taxation with emphasis on underdeveloped countries (studies in this area include PROCEEDINGS OF CONFERENCE ON AGRICULTURAL TAXATION AND ECONOMIC DEVELOPMENT (1954); LEVIN, A THEORY

(3) As a tool of management control, to gauge the effectiveness of tax administration in general and in its various detailed operations.

b. Economic Research

The techniques of economic research necessary to illuminate the various aspects of substantive tax policy.

c. Legislative drafting

The techniques of legislative drafting, including such aspects as codification of laws and regulations, the preparation of rulings, consideration of the limits of detail to be included in legislation and of the relationship between the degree of discretion granted (so as to avoid detail) and the fairness of the tax in the light of the actual exercise of that discretion. For example, what are the administrative problems involved in the exercise of discretion which policy planners must take into account in the final formulation of the laws?

2. *Organization of Government for Fiscal Management*

a. Coordination of the various revenue departments, such as the departments dealing with the customs and those administering the internal taxes, or the departments dealing with the assessment of taxes and those dealing with the collection of taxes.

b. Coordination of revenue and non-revenue departments on matters affecting tax policy, such as land reform and property taxation.

c. Coordination of the planning of tax laws with the administration of those laws — how can policy planners and administrators properly communicate so that the final product is an intelligent policy that can be affectively administered?

d. Coordination of the administration of federal taxes with that of state or regional taxes.

e. Problems relating to the decentralization of operational assessment and enforcement activities and the centralization of supervisory authority as respects the administration of taxes.

---

OF EXPORT ECONOMIES—(manuscript stage, 1957), WALD, RECONSTRUCTION OF AGRICULTURAL LAND TAXES IN UNDERDEVELOPED COUNTRIES (manuscript stage, 1957), KUST, TAXATION FOR ECONOMIC DEVELOPMENT, WITH SPECIAL RELATION TO INDIA (manuscript stage, 1957), and work under preparation on tax incentives for domestic capital formation and foreign investment).

7. The formulation in the text of these topics draws in considerable part on an informal discussion of these matters in 1957 between members of the Harvard Program and staff members and consultants of the Fiscal and Financial Branch of the United Nations Secretariat.

## B. INSTITUTIONAL FACTORS AFFECTING THE TAX STRUCTURE

1. *The effect of institutional economic factors on the shape of the tax structure.*

How do the economic organization of a country and the patterns of its economic life affect both the basic tax structure and the content and administration of the particular taxes making up that structure? Thus, what are the consequences for taxation of a predominance of small business concerns, of the existence of anonymous bank accounts and bearer shares, of the patterns of production and marketing in various industries, and the like?

2. *The effect of social and political institutions on the tax structure.*

What is the effect of the patterns of family life and community organization on the tax structure? How do the patterns of family property disposition affect the tax laws? What are the institutional factors that have an effect on the degree of compliance or evasion to be expected from the public?

3. *The effect of legal institutions on the tax structure.*

What are the points of interaction between tax law and the civil and commercial law? How do the regular processes of civil and criminal litigation interact with the enforcement of the tax laws? What are sound procedures for the resolution of disputes between government and taxpayers, as respects questions of fact and questions of law, and how do these procedures fit with the legal process generally? What is a proper system of civil and criminal tax penalties and how does this system fit with the legal process generally?

C. THE IMPACT OF INFLATION AND OTHER INSTABILITIES  
ON THE TAX STRUCTURE

What problems are raised by the impact of inflation on the tax structure and its administration? Where are the stresses and strains of inflationary instability felt — in the consequences attendant upon a lack of currency in the timing of tax payments and collections; in the valuations of real property, inventories, and other assets; in the changing composition of income levels and tax brackets; in the changing importance of the types of taxes; in the need for revaluation of assets for depreciation and excess profits taxation, and so on?

What other instabilities are similarly important, such as sudden changes in export or import patterns?

What changes in substantive tax policies and tax administration are necessary to meet or ameliorate the effects of these instabilities?

D. THE MODERNIZATION OF THE TAX STRUCTURE TO DEAL  
WITH MODERN INDUSTRY AND FINANCE.

How do the organization and operation of modern industry and finance affect the administration of taxes? How can a tax administration so organize and operate that in its relationships with modern business it can both derive benefits from the efficiencies in operation and record keeping which the business world has achieved and avoid thrusting useless or annoying burdens on business? What are the significances for tax return and record requirements, for taxpayer audits and investigations, and the like, of the ways in which modern business manages its internal affairs and records its transactions?

E. THE ROLE OF VALUATION IN THE REVENUE SYSTEM

Recognizing that the role of valuation, broadly conceived, is pervasive in a revenue system, what important problems of valuation can be identified and what techniques can be used to solve or ameliorate those problems? May average prices be substituted for actual prices under certain excise taxes; how may fluctuations in the price structure be met; may valuation problems be altered by changing the time or economic stage at which valuation is required? To what extent are valuation problems a limiting factor in the substantive shaping of real property taxes, net worth taxes, income taxes, excise taxes?

These are some of the issues whose exploration would contribute to a better understanding of the problems of tax administration and their solution. We have much to learn the world over about this vital sector of the fiscal field. But if those interested in tax policy and in the problems of underdeveloped countries will recognize that the administration of tax laws is as much a matter of prime concern as is the substantive content of those laws, then there is real hope for steady progress and improvement in tax administration everywhere.