

TECHNICAL COOPERATION (TC) ABSTRACT

I. BASIC PROJECT DATA

Country/Region:	Belize
Technical Cooperation (TC) Name:	Support for trade and tax policy reform
TC Number:	BL-T1059
Team members:	Fernando Velayos (IFD/FMM), team leader; Mario Umaña (INT/TIU), alternate team leader; Alberto Barreix (IFD/FMM); Dougal Martin (CID/CNI); Agnes Rojas (IFD/FMM); Venetia Eck-Salazar (CID/CBL); and Marina Massini (IFD/FMM).
Type of operation:	Client support
Reference to Request:	IDBDOCS-#38573893
Date of TC Abstract:	January 24, 2014
Beneficiary:	Ministry of Finance of Belize
Executing Agency:	Inter-American Development Bank (IDB)
IDB Funding Requested:	US\$410,000
Local counterpart funding:	US\$0
Total:	US\$410,000
Disbursement period:	24 months
Required start date:	April, 2014
Type of consultants:	Individual
Prepared by Unit:	IFD/FMM
UDR:	IFD/FMM
Included in Country Strategy:	Yes
TC included in CPD:	Yes
GCI-9 Sector Priority:	Competitive Regional and Global Integration, Institutions for growth and social welfare

II. OBJECTIVE AND JUSTIFICATION

- 2.1 Belize has had one of the most revenue-effective systems in the Central America and Caribbean Region in the last decade. However, revenues have remained flat at around 22% of GDP, in a context where public debt amounted to 75% of GDP in 2012. Belize's tax system generates revenue in a manner that damages incentives, is inequitable and is complex. These adverse outcomes stem from five main problems: (i) too many different taxes; (ii) over-reliance on sub-optimal forms of taxation; (iii) relatively high nominal rates, counterbalanced by numerous exemptions; (iv) special tax regimes; and (v) fragmentation of tax administration¹.
- 2.2 Regarding indirect taxation, Belize's collection comes from three main taxes: trade-related taxes with 22% of total tax collection (import duties, Revenue Replacement Duty-RRD, and Environmental Tax-ET), General Sales Tax-GST (27%), and excises (3.5%). Besides the efficiency problem, the existence of various trade-related taxes makes their administration complex and, some may go against World Trade Organization (WTO) non-discrimination principles.

¹ These taxation issues are closely linked to trade policy, where there are significant tax and non-tax impediments to trade.

- 2.3 Revenue coming from GST is eroded by numerous exemptions and a zero-rate on many products, all of which generates differentiated effective rates across sectors. In addition, the tourism sector is exempted from the GST, but is subject to the Hotel and Tourism Accommodation Tax, adding more complexity to the system.
- 2.4 In terms of direct taxation, Belize charges a Business Tax (BT) in lieu of a “true” corporate income tax. This BT is considered a distortive element of the tax system because it does not tax net income, and the existence of numerous rates (0.75% to 25%), which are applied across sectors without major economic rationale.
- 2.5 Belize’s tax expenditures also manifest through fiscal and export incentives. The current incentives policy is based on three legal instruments: Fiscal Incentives Law, Export Processing Zone (EPZ) and Commercial Free Zone (CFZ). These systems are complex, fiscally costly and, with a high degree of likelihood, mostly non-compliant with WTO obligations after December 2015.
- 2.6 Regarding tax administration, it is organized by type of tax instead of functions. Four agencies are in charge of tax collection (not counting Social Security): GST, Income Tax, and Customs and Excise Departments, and the Belize Tourism Board, (responsible for the Hotel and Tourism Accommodation Tax-HTAC). Lack of coordination and duplication of functions characterize this system.
- 2.7 This project will provide support for the development of studies and proposals to address the problems in the four above mentioned areas. These studies, taking also into account Belize’s integration framework, in particular regarding the Caribbean Community and Common Market (CARICOM), will focus on the feasibility and economic consequences of such reforms, revenue and equity implications, and where it applies, implementation plans.
- 2.8 This TC is aligned with the Bank’s Trade and Tax Policy strategic priority of the Country Strategy with Belize 2013-2017, and with the sectorial priorities defined in the Report on the Ninth General Increase in the Resources of the Bank, GCI-9 (AB-2764), specifically with competitive regional and global integration, and institutional strengthening for fiscal efficiency and sustainability.

III. DESCRIPTION OF ACTIVITIES AND OUTPUTS

- 3.1 **Component I. Economic consequences of indirect taxation reform.** The objective is to analyze the consequences of a reduction (streamlining) of trade related taxes (import duties, RRD and ET) and excise taxes, a simultaneous maximization of the GST tax base, and the repeal of the HTAC. The analysis will include the revenue implication of such measures, and price and equity analysis.
- 3.2 **Component II. Economic consequences of income tax reform.** The objective is to analyze the potential of a gradual phase-in of a conventional corporate income tax, to replace the current BT. The analytical work would focus on the economic

consequences of such reform: (i) the revenue implications; and (ii) the final effective tax burden and differences before and after the change in the sectors of the economy to which it would apply.

- 3.3 **Component III. Tax incentives policy to boost investment.** Aimed at proposing a new incentives framework that adheres to international good practices, is WTO compliant and, if possible, aligned with the integrated policy that is being promoted in the rest of Central America. It will include the revenue and efficiency costs of EPZ and CFZ, as well as costs and benefits of the new framework.
- 3.4 **Component IV. Support for Tax Administration reform.** The objective is to propose a feasible plan to bring together some or all of the revenue collection agencies, building on previous works on the subject, such as the one carried out by the Caribbean Regional Technical Assistance Centre. The analysis will include the consequences of the elimination of the tax collection function of the Belize Tourism Board (due to the repeal of the HTAC).

IV. BUDGET

Activity	Description	IDB Funds	Counterpart	Total
Component I.	Consultancy/travel	180,000	0	180,000
Component II.	Consultancy/travel	50,000	0	50,000
Component III.	Consultancy/travel	70,000	0	70,000
Component IV.	Consultancy/travel	50,000	0	50,000
Supervision and monitoring		40,000	0	40,000
Dissemination of studies		20,000	0	20,000
Total		410,000	0	410,000

V. EXECUTING AGENCY AND EXECUTION STRUCTURE

- 5.1 The Bank will be the executing agency of this TC, and the beneficiary counterpart will be the Ministry of Finance of Belize.

VI. PROJECT RISKS AND ISSUES

- 6.1 Quality data are needed. While those are available in most of the cases, in the event they wouldn't, the work could not be carried out.

VII. ENVIRONMENTAL AND SOCIAL CLASSIFICATION

- 7.1 This TC is not expected to cause significant social or environmental impacts. Therefore, a C classification is proposed.