

TAX EXPENDITURES IN THE DOMINICAN REPUBLIC

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Abstract

This paper takes a broad approach in the sense that only the fundamental structure elements of each tax system are considered as part of the benchmark tax system. Moreover, this paper will go beyond the traditional tax expenditure reporting by taking into account an ideal tax system with minor distortions as part of the benchmark. Because of having an ideal tax system as a norm, the report makes some judgments about the appropriateness of the ideal tax structure in the Dominican Republic and the estimates of tax expenditures imply the extent to which the existing tax system is deviated from the ideal tax system. This paper provides empirical estimates of the foregone tax revenue of each tax provision for the year 2002 which deviates from the benchmark of the tax system. The tax systems we examine include the individual income tax, the corporate income tax, the tax on the transfer of industrialized goods and services (ITBIS), the selective tax on consumption, and import duties. In the other part of this paper we discuss the concept of the tax expenditures in order to facilitate the understanding and estimation of the tax expenditures. Finally this paper presents preliminary estimates of the foregone revenues of tax expenditures.

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Tax Expenditures in the Dominican Republic

I. Introduction

The concept of tax expenditure was first introduced by Stanley S. Surrey in November 1967.¹ He suggested that there should be a full accounting of tax revenue losses through various special exemptions, deductions, and credits that are deviated from the accepted concepts of net tax income in the government. Like government direct outlays, a tax expenditure reporting would increase the transparency of a tax system. Since then, tax expenditure budgeting has spread to a number of countries, especially the members of Organization for Economic Co-operation and Development. In some countries, the tax expenditure reporting has become regular and compulsory report.²

The Dominican Republic has not produced any tax expenditure report so far. The purpose of this report is to provide congressmen, government officials and the public with information regarding the tax system in the Dominican Republic. It is an important input into the process of evaluating the current tax system and also for formulating amendments to the tax system in order to make the system more efficient and to experience equitable economic growth. Like other tax expenditure reports, it should be recognized that the information on the tax expenditures itself has certain limitations and must be interpreted with caution.

The principal purpose of taxes is to raise the revenues necessary to finance government programs. There are other functions such as changing the behavior of taxpayers, improving income distribution, stabilizing the economy, and promoting economic growth. Tax expenditures, however, are another means to achieve some of the government objectives, similar to direct government expenditures. As a result, tax measures are often considered as tax instruments and employed to influence government policy objectives. These measures may take the form of tax exemptions, deductions, credits, deferrals of tax payments or subsidies provided to particular groups of individuals, businesses, or certain types of activities or locations. These special tax instruments or measures provide special tax incentives that are typically referred to as tax expenditures.

In order to identify tax expenditures, it is necessary to establish a norm or benchmark tax structure with minor distortions that does not contain any preferential tax provisions. As such, tax expenditures are defined as special tax provisions that deviate from the norm or benchmark tax system. It is important to recognize that the norm or benchmark tax system may not be defined in the same way across countries or among people within the same country and thus what constitutes the tax expenditures can also be quite different. Nevertheless, tax expenditure reporting is recognized by various developed and developing countries for its fiscal transparency.

¹ Stanley S. Surrey, "The U.S. Income Tax System – The Need for a Full Accounting", Speech before the Money Markets, (November 15, 1967).

² The countries such as Australia, the Netherlands, and the United States publish their tax expenditures yearly. See, e.g., Hana Polackova Bixi, Christian M.A. Valenduc, Zhicheng Li Swift, editors, Tax Expenditures – Shedding Light on Government Spending through the Tax System, (Washington, D.C.: the World Bank, 2004).

This report takes a broad approach in the sense that only the fundamental structure elements of each tax system are considered as part of the benchmark tax system. Moreover, this report will go beyond the traditional tax expenditure reporting by taking into account an ideal tax system with minor distortions as part of the benchmark. By doing this way, many tax provisions are considered as tax expenditures and thus a full range of tax measures can be identified and information can be provided for readers who can take a different position and construct a list of their own tax expenditures. Because of having an ideal tax system as a norm, the report makes some judgments about the appropriateness of the ideal tax structure in the Dominican Republic and the estimates of tax expenditures imply the extent to which the existing tax system is deviated from the ideal tax system.

This report provides empirical estimates of the foregone tax revenue of each tax provision for the year 2002 which deviates from the benchmark of the tax system. The tax systems we examine include the individual income tax, the corporate income tax, the tax on the transfer of industrialized goods and services (ITBIS), the selective tax on consumption, and import duties.

Section II of the report discusses the concept of the tax expenditures in order to facilitate the understanding and estimation of the tax expenditures. Section III presents preliminary estimates of the foregone revenues of tax expenditures. The data sources and methodology used to estimate the tax expenditures are also presented. Concluding remarks are made in the final section.

II. Definition of Tax Expenditures

To achieve its social and economic objectives, the government can provide tax exemptions, deductions, credits, deferral or subsidies. This tax relief represents an alternative form of government assistance similar to those of direct government expenditures and thus refers to tax expenditures.

Tax expenditures are generally used to achieve certain government objectives. These objectives can be an exemption of interest income from the individual income tax in order to stimulate household savings, a lower tax rates for small businesses in order to compensate their ability to have access to capital market or to have special tax credits for investment in slow growth regions. In the case of the ITBIS, an exemption of basic groceries may be a concern regarding the regressivity of the consumption tax. The estimates of the cost of such tax expenditures can be very helpful to policy makers in allowing them to compare the cost of using the tax system to achieve a policy objective, rather than employing a direct expenditure program, or to do nothing. Usually the cost of the tax expenditure option is unknown and the assumed value used to analyze policies is much less than their true revenue cost.

In short, tax expenditures represent an alternative way to direct expenditures by the government in order to achieve certain socio-economic objectives. They are defined as

deviations from a norm or benchmark tax system. The benchmarks can contain the basic tax structure and their tax rates in each of the tax systems. They are described below for each of the tax systems in the Dominican Republic.

2.1 Individual Income Tax System

The benchmark for the individual income tax system includes the existing tax rates and the associated tax brackets, tax unit, time frame of taxation, and the treatment of inflation designed to reduce the impact of inflation.

The individual income tax in the Dominican Republic is levied on income sourced from within the country and incomes arising from investments and financial gains from outside of the country. The scope of the tax and the definition of income are important in determining what the tax expenditure is. For most industrialized countries the base of the individual income tax system is the worldwide income of its residents. If this were defined as part of our benchmark, not taxing income earned abroad would have been considered tax expenditures. In this report, however, we treat the current system as the norm.

Income in the Dominican Republic is defined broadly to include all monetary and non-monetary income provided by employers to their employees, as such fringe benefits should be part of the benchmark. However, from the practical point of view imputed rent from owner-occupied housing is not considered as income nor is it taxable.

Taxes are imposed on an individual basis in the Dominican Republic as long as income is greater than the basic exemption. It is thus the individual rather than the family as being the tax unit.

In the Dominican Republic, taxable income can be classified as two categories, earned income and income from capital. The former is subject to the progressive taxation; at present there are three tax rates, 15 percent, 20 percent, and 25 percent in which the marginal tax rate increases with income in order to reflect the ability-to-pay concept. The basic tax exemption and the income tax brackets are annually adjusted for inflation, using the consumer price index. As the progressivity is widely accepted as one of the most elements of the individual income tax system, this report considers the legislated progressive rate scale as part of the benchmark. The latter, income from capital, is taxed at a flat rate of 25 percent on dividend income, the top marginal income tax rate.³ For the purpose of this report, the flat rate of 25 percent on all financial income is considered as the norm.

The individual income tax system is based on nominal income with the provisions that the basic exemption and the income tax brackets are annually adjusted for inflation. Any partial adjustment for inflation is considered as tax expenditures. In the case of financial

³ In certain countries such as Denmark, Finland, and Sweden, the financial income is taxed at a lower rate than the top marginal tax rate of the earned income.

income, it should be taxed in real income at 25 percent. Anything taxed at lower rates should be regarded as tax expenditures.

The individual income taxes are mainly withheld by employers on behalf of workers and no annual tax return filings are required. However, some people may file an annual income tax return in order to use any surplus tax credits from taxes paid on dividends against other sources of incomes.⁴ In the case of sole proprietors or independent professionals who provide services to non-corporate clients, there is no withholding mechanism but they are required to make advance payments. By the end of the year, they are required for filing an annual tax return. The benchmark taxation period for the individual income tax system is therefore set for the calendar year.

The benchmark for the individual income tax system in 2002 is summarized as follows:

- The existing tax structure of earned income in the progressive nature is taken as given. That is, the annual basic exemption was RD\$125,256. The tax rates and income brackets were 15 percent for income from RD\$125,256 to RD\$208,760, 20 percent for income from RD\$208,760 to RD\$313,140, and 25 percent for income above RD\$313,140;
- The above threshold and the income tax brackets are annually adjusted for inflation;
- In the case of financial income, a flat rate of 25 percent on real income is also given;
- The tax unit is the individual;
- Taxation is imposed on a calendar year basis; and
- Nominal income is used in defining income.

2.2 Corporate Income Tax System

Unlike the individual income tax, any income earned by a corporate is not considered final in terms of the beneficiary. This is because the after-tax-income will flow through and is ultimately attributed to shareholders. The corporate income tax system functions as a withholding tax. Therefore, the tax itself should not have the characteristic of progressivity built in the system. Nevertheless, the benchmark for the corporate income tax system should also encompass the fundamental tax structure, tax rates, unit of taxation, time frame of taxation, and the treatment of inflation for computing income tax liability.

Corporations generally pay tax on their profits after deducting various business expenses, including the depreciation expenses for capital assets and interest expenses. This is universal and worldwide in its application and can be viewed as the fundamental structure of the corporate income tax. Depreciation of assets is part of the benchmark tax system so long as the depreciation rate falls in line with economic depreciation on a replacement basis. At present, the applicable depreciation rates are 5 percent for buildings and their structural components, 25 percent for automobiles, office equipment and furniture, computers and data processing equipment, and 15 percent for all other

⁴ The tax on dividends is withheld by corporations. Details will be further explained in the section of the corporate income tax.

depreciable assets. Any depreciable assets with higher depreciation rates should be considered as tax expenditures.

The corporate profits are subject to a single tax rate at 25 percent. However, during the period from 2001 to 2003, a minimum tax of 1.5 percent rate was levied on the gross sales of all corporations in the Dominican Republic. If the amount is less than the corporate income tax by the end of fiscal year, the additional corporate income tax liability was paid to the authority. On the other hand, if the 1.5 percent turnover tax was greater than the corporate income tax, it became the final tax. This minimum tax seems to imply that businesses had business expenses averaging 94 percent of their gross receipts or the net income with 6 percent of the gross receipts.⁵ It had ignored the variations of profit margins for each individual firm.

The minimum tax of 1.5 percent was the most important and effective instrument in collecting corporate income taxes for three years from 2001 to 2003.⁶ Notwithstanding the turnover tax became an integral corporate income tax system during the said three-year period, it was a negative tax expenditure because of the additional tax burden being imposed on the unprofitable firms.

Beginning in January 2004 the 1.5 percent tax on turnover has become a mechanism of being withheld monthly by corporations and will be credited against their corporate income taxes at the end of their respective fiscal year, any excess credits will be refundable. It is no longer a minimum tax per se.

Provisions that reduce the tax rate for small firms are regarded as tax expenditures. These include the lower rates for those firms being levied at 0.75 percent for gross sales less than RD\$2 million, 1.00 percent for gross sales between RD\$2 to 4 million, and 1.25 percent for gross sales between RD\$4 to 6 million.

In the Dominican Republic where firms are located in free zones they are exempted from the corporate income tax. This has been viewed by WTO as inappropriate and the same corporate income taxes should be applied to companies operating in the free zones as those located outside the zones from 2007. However, for a small open economy producing traded manufactured goods, the tax policies that have been given to companies operating in the zones are the correct ones. There are no subsidies, nor are there indirect domestic or trade taxes. Furthermore, there has been no corporation income tax on income earned in the zones. For a country that is trying to raise the wages of its citizens by attracting foreign investment that will provide jobs this is also the appropriate tax policy.

In such a situation where the country has no control over the international cost of

⁵ In other words, the corporate income tax rate at 25 percent is equivalent to 1.5 percent of tax on turnover.

⁶ Of the largest 700 corporations in the Dominican Republic, more than 86.5 percent of their corporate income taxes paid through the 1.5 percent turnover tax in year 2002. See, e.g., Hector Guiliani Cury, Glenn P. Jenkins and Chun-Yan Kuo, "Fiscal Adjustment for Sustainable Growth in the Dominican Republic", paper prepared for the Government of the Dominican Republic, (March 24, 2004).

capital required to finance the investments in the zones and the prices of the services provided are fixed internationally, any additional corporation income taxes that levied on the income from capital investments in the zones will not change the net of tax return to companies but will force the wage rate being paid to labor they employ to be decreased. The reduction in the total wage bill paid to labor in the zones will be approximately equal to the additional corporation income taxes paid by these companies.⁷ That being said, due to general applicability of the WTO rule worldwide the Dominican Republic will likely be required to impose the corporate income tax in the near future. Thus, exemption of the corporate income tax in the free trade zones will be considered as a memorandum item of the tax expenditures because of the WTO rules.

In the case of border zones in which firms can sell their products in the domestic markets but the corporate income tax is exempt, it is clearly a tax expenditure item because of its preferential treatment as compared to other firms in the country.

There are concerns regarding the choice of the appropriate unit of the corporate income tax benchmark system. The possible tax units include the single legal corporate entity and the consolidated group of related corporations. The single legal corporate entity, rather than a branch or cost centre, is the relevant unit of taxation because that is supported by the fact that one part of a business can be offset by the other business losses within the same entity. However, for consolidated group of related corporations if considered as a tax unit, income losses or capital gains by one corporation can be used to offset the income or capital loss from other corporation; it would result in a reorganization of their corporate structure in order to reduce the corporate tax liability. Thus, the single legal corporation is a more appropriate unit as the benchmark tax unit.

The general fiscal year for the purpose of this tax is from January 1st to December 31st. Corporations, however, may elect their own fiscal period with the following closing dates, March 31st, June 30th, and September 30th. The benchmark taxation period for the corporate income tax is thus the fiscal year.

As the corporate income tax system is based on nominal income whereas the deductions or depreciation expenses for tax purpose must also be adjusted for inflation in the benchmark tax system. Any over or under adjustments for inflation should be considered as tax expenditures. Examples include the provision of loss carry-over. Capital investment with risk taking venture can be viewed as an activity over a number of years; as such the tax provision of loss carry-over may be regarded as part of the benchmark corporate income tax system. As a result, the loss carry-over should be indexed for inflation. Thus, the carry-over of losses over three years without inflation adjustment in

⁷ As there is a competitive labor market wages will tend to be lower than otherwise across the economy. While labor in its role as a consumer of services will benefit from somewhat lower prices of services due to the fall in wages, it will only be a partial offset to the reduction in wages. Hence, the burden of the increase in corporation income taxes on the income from capital used to manufacture traded goods will likely be borne more than 100 percent by labor.

the Dominican Republic would be considered as negative tax expenditures because of the absence of inflation adjustment.

Dividends are distributed after the corporate income tax. If taxed again, income earned from corporations would be taxed twice, once in the corporation and once at the individual level. The income tax integration argues for the integration of the individual and corporate income tax system so that the dividend tax credit or other schemes are considered as an essential feature of the overall income tax structure and serves to eliminate double taxation.

In the Dominican Republic, dividends are taxed and withheld at a rate of 25 percent when they are distributed to company's shareholders. The amount of tax withheld can then be used as a credit against the individual income tax liabilities of the shareholders. In other word, dividends are taxed only once and the dividend tax credits provided to individuals should not be considered in this report as the tax expenditure item.

By the same token, dividends distributed to other corporation are subject to 25 percent withholding tax that can be used as a credit against its corporate income tax. The net-of-tax dividends are excluded from the taxable income in the recipient companies. The scheme provides a vehicle to eliminate taxation between corporations.

The benchmark for the corporate income tax system in 2002 is summarized as follows:

- The existing general tax rate of 25 percent is taken as given;
- The tax unit is the legal corporation;
- Taxation is imposed on a fiscal year;
- Nominal prices are used in defining income and expenses and thus deductions for tax purposes must be adjusted for inflation; and
- An integrated income tax system is part of the benchmark tax system so that double taxation can be eliminated.

2.3 The Tax on the Transfer of Industrialized Goods and Services (ITBIS)

The benchmark system used to analyze the ITBIS is a broadly-based consumption tax. It is a multi-stage sales tax based on the destination principle. The tax is applied to the sales of goods and services at all stages of the production and distribution chain. By using a credit invoiced method, vendors at each stage are able to claim tax credits to recover the tax they paid on their business inputs including intermediate inputs and capital assets. As a result, the tax is in effect applying the tax only to the value added by each vendor. The only tax that does not get credited or refunded is the tax imposed on final consumption purchased by individuals and governments. In the case of government enterprises, they are considered to operate in a similar manner as the private sector; as such they charge the tax on their sales and receive credits on the tax they paid on their business inputs. The tax is equivalent to the retail sales tax on final consumption.

Since the tax is imposed at the destination principle, imports are taxed in the same way as domestically produced goods. Exports are zero-rated in which exports are not subject to tax while exporters are still able to claim their input tax credits. Therefore, the ITBIS is essentially applies to goods and services consumed domestically.

For technical difficulties, countries employing a value added tax generally exempt the domestic sales of financial intermediation, market intermediation, and insurance.⁸ Thus, exemption of the domestic sales of financial services is considered part of the benchmark tax system in this report.

The benchmark system has only one tax rate which is 12 percent. Any rates deviated from this rate are considered as tax expenditures.

The benchmark taxation period is the calendar year. Any delay in terms of payments to the treasury is considered as tax expenditures.

The essential features of the benchmark system for the ITBIS in 2002 are:

- The structure is a multi-stage sales tax system with a comprehensive tax base in which the only exception is the domestic sales of financial services;
- It is the destination principle;
- A general tax rate is 12 percent; and
- Taxation period is based on the calendar year.

2.4 The Selective Taxes on Consumption

The selective taxes on consumption in the Dominican Republic are the same as what are called excise taxes elsewhere in the world. There are levied on certain goods produced domestically as well as imported. These goods include alcoholic beverages, cigarettes and other tobacco products, petroleum, vehicles, jewelry, and many other products. This tax is levied on either specific tax rate or ad valorem rate. In the case of ad valorem rate, the tax rates vary from a 10 percent on ovens to 60 percent on revolvers and pistols. A special excise tax is levied on vehicles. It is a progressive rate imposed on the CIF price of the vehicle. The statutory tax rates increase from 0 percent to 80 percent as the prices of vehicles rise.

The selective taxes on consumption are a single stage sales tax. It is levied on goods irrespective of purchasers whether they are consumers or producers. Unlike the ITBIS, the tax is not creditable even if they are purchased by businesses.

At the present time, there are more than 135 commodities that are subject to the selective taxes on consumption in the Dominican Republic. This number of items is rather large for a modern tax system. The taxes are levied on either specific rate or ad valorem rate. In addition, vehicles are taxed in progressive rates. The system is extremely complicated

⁸ In addition to the Dominican Republic, New Zealand and Singapore are the only countries that tax the underwriting activity of general insurance.

and needs to be reformed. The ideal system is having the selective taxes on consumption limited to a few commodities and having the tax levied on both domestic and imported goods on equal basis. In the case of imported goods, they are taxed on duty-paid value.

For the purpose of this exercise, the excisable goods are restricted to a few commodities and services in the benchmark system. The choice of these commodities is based on the consideration of health, environment, luxury goods and tax administration. They would be taxed at a single ad valorem rate which would collect approximately the same amount of revenue under the current system.

The main features of the benchmark system for the selective taxes on consumption are:

- The tax is only levied on a few selected commodities, including alcoholic beverage, tobacco products, petroleum products, electricity, communication, insurance, airline tickets, vehicles and guns;
- The tax rate applies equally to the same domestically produced goods and imported goods at a single ad valorem rate that would generate the same amount of revenue as the current system;
- The tax applies equally to any purchasers; and
- The tax unit is the product.

Any provisions deviated from the above benchmark are considered tax expenditures.

2.5 Import duty

At present, there are mainly three classifications of imports in the Dominican Republic. First, there are those imports destined for the free trade zones. These enter duty free because the zones are considered for purposes of customs and taxation to be located outside of the country. All such imports are not taxed when they enter the zones and no goods are taxed when exported from the zones unless they are being sold within the domestic economy. The second category is imports originating from other Caribbean countries, Central America or covered by other bilateral trade agreements. In this category imports are largely exempt from the duty. These represent a very small amount of the Dominican Republic's international trade. The third category is imports from other than the first two categories. These items attract import duties.

The free trade zones are regarded as foreign jurisdiction for the tax purpose, as such no customs duties are collected from imports nor do they impose on the ITBIS or other indirect taxes. The free zones have played a very important role in the economy of the Dominican Republic. Unlike other countries, however, the free trade zones are spread across the country. In addition, the zones have expanded to incorporate a wide range of services that would be normally found outside of the zones in domestic economy.

To remove the tax burden that is embodied in the cost of inputs used to produce exports, a mechanism is needed to remove import duties from goods directly imported. For this to

happen in the free trade zones, the government exempt the import duties going to the zones because their products are all sold abroad. This is an international practice and is recognized by WTO and thus not considered as tax expenditures.

This report also recognizes that duty drawback and duty exemption are part of the benchmark system so long as the output is sold in the international markets.

The concession due to the bilateral agreements is a preferential treatment and should be considered as tax expenditures.

In the case of firms located in the border zones, the import duty is treated in the same way as those entering the free zones even though their products are sold to domestic markets. This would create a competitive advantage as compared to firms located outside of the border zones. The exemption of the customs duties on imports going to the border zone is, therefore, considered in this report as tax expenditures.

The import duty rates in the Dominican Republic have declined over time, especially since 2001. In 2002 the year we are interested in quantifying the tax expenditures, there were 8 duty rates imposed on imported goods for a variety of reasons including social, economic or industry-protected measures. These rates were 0, 3, 8, 14, 15, 20, 25, and 40 percent.

In addition to the import duties, a commission on foreign exchange transactions was introduced in 1999 on all foreign exchange purchases at the rate of 1.75 percent in the Dominican Republic. The rate was subsequently increased to 5 percent in October 1999 and then reduced to 4.75 percent two years later. In August 2002, a resolution eliminated the commission on foreign exchange transactions and designated the Customs as the agency in charge of collections. This implies that, thereafter, only imported goods are subject to the foreign exchange commission. The rate of this charge has been increased temporarily to 10.00 percent since October 23, 2003.

The commission on foreign exchange is equivalent to impose an additional tariff rate across all imported goods including the current zero-rate items. For all intent and purposes, the current tariff rate structure is equal to the current varying tariff rates plus the uniform commission charge on foreign exchange.

For the purpose of this analysis, the ideal tariff structure would be a uniform tariff rate so that no preferential rates would be created for specific imported goods. The rate used for the benchmark system would be set to collect the same amount of import duties including the charge on foreign exchange.

The benchmark taxation period is the calendar year.

The essential features of the benchmark system for the customs duty in 2002 are:

- A uniform tariff rate that would collect the same amount of tariff revenue inclusive of the commission on foreign exchange;
- Free trade zones for the purpose of customs duty are regarded as outside of the national territory;
- Duty drawback and duty exemption are integral part of the tax system; and
- Taxation period is based on the calendar year.

III. Measurement of Tax Expenditures

3.1 Alternative Approaches

There are several ways to measure the tax expenditures as a result of tax provisions for special exemptions, deductions or tax credits. Three approaches are generally undertaken by various countries. They are measured by the amount of revenue forgone, by the amount of the revenue gain if the special tax provision is repealed, or by the amount of the outlay equivalent to achieve the government objective.⁹

The revenue forgone approach measures how much tax revenues are forgone because of the existence of special tax provisions. This revenue cost estimate is calculated independently under the assumption that all other tax expenditures remain unchanged. It does not take into consideration taxpayers' behavioral responses. As a result, the estimates for tax expenditures should not be aggregated because neither interactions between tax provisions nor the behavioral responses are taken into account in the calculation.

The second approach measures the additional gain in tax revenues for the government if a special tax provision is repealed. The estimate takes into account the behavioral responses of taxpayers as well as the interactions between tax provisions in the economy. It would require a sophisticated simulation model with the anticipation of the likely changes in taxpayers' behavior and interaction between tax provisions. It is a kind of the dynamic analysis in the general equilibrium framework.

The third approach measures the tax expenditure by the equivalency of the government direct outlay so that the benefit or gain to the taxpayer generated by the specific tax expenditure provision would be the same as the impact of the direct government expenditure program. The approach takes into account the marginal tax rates of the recipients in which budgetary expenditure programs spent. Therefore, the outlay equivalent is generally grossed up from the revenue forgone.¹⁰ For example, an annual exemption of RD\$10,000 in the individual income tax would be worth RD\$2,500 for a taxpayer per annum if his marginal income tax rate is 25 percent. Suppose the

⁹ See, e.g., Emil Sunley, "Tax Expenditures in the United States: Experience and Practice", edited by Hana Polackova Brix, Christian M.A. Valenduc, Zhicheng Li Swift, editors, Tax Expenditures – Shedding Light on Government Spending through the Tax System, (Washington, D.C.: the World Bank, 2004), Chapter 7.

¹⁰ Neil Bruce, "Pathways to Tax Expenditures: A Survey of Conceptual Issues and Controversies", edited by Neil Bruce, Tax Expenditures and Government Policy, (Kingston, Ontario: John Deutsch Institute for the Study of Economic Policy, Queen's University, 1989).

government were instead to provide the individual with an equivalency of a taxable grant of RD\$2,500. The outlay equivalent would be approximately RD\$3,333 which is much greater than the figure presented in their forgone tax revenue approach. Since the estimates used in this approach is based on the cost-benefit outcome, a great deal of assumptions must be made and they could be quite tricky and different from the viewpoints of individuals.

3.2 Calculation of the Estimates

The approach adopted in this report is the amount of revenue forgone each year because of the presence of specific tax provisions. Each estimate represents the amount by which tax revenue in the Dominican Republic forgone because of the tax expenditure in question. As was previously mentioned, all measures are carried out independently with the assumptions that other tax expenditure provisions remain unchanged as well as no behavior response is taken into account. This is relatively an easier implementation because the alternative approaches would involve various assumptions regarding the behavioral responses of taxpayers or the equivalency of government outlay in terms of benefits. It should be noted that these methodological distinctions are also important as one interprets the implications of the estimates of the tax expenditures.

As the estimate of each tax expenditure item is conducted independently, the total amount of all or several tax expenditures cannot be aggregated to provide a meaningful estimate for the country as a whole. For example, the sum of two independent tax expenditures may generate a different amount of the tax expenditure from the case where the two tax expenditures are considered concurrently. Although most of individuals in the Dominican Republic do not file the individual income tax return, some sole proprietors or independent professionals such as accountants, lawyers, engineers and medical doctors who provide services to non-corporate clients do file their tax returns. Suppose a taxpayer whose taxable income was slightly more than RD\$10,000 below the threshold for the 25 percent tax bracket, he was placed in the 20 percent tax bracket. This was the result of using one tax exclusion and one tax deduction of RD\$10,000 each. The former refers to the exclusion of some fringe benefits paid to his employees while the latter refers to the exemption of interest income received from savings in banks. Eliminating either provision by itself would increase his taxable income by RD\$10,000 and his tax liability by RD\$2,000. Repealing both provisions simultaneously would raise his tax liability by RD\$4,500 instead of RD\$4,000 because the 25 percent tax rate would apply to the increase of the second RD\$10,000 in his income. Therefore, simply adding the two or more tax expenditures would provide a misleading figure of the revenue impact of eliminating two or more tax expenditures concurrently.

Since the estimates of the tax expenditures in this report are calculated based on the assumption that all other tax expenditure provisions remain unchanged, one can develop a revenue simulation model and simulate the tax revenues assuming a specific provision

in question is eliminated and then take the difference in tax revenues between the simulated case and the existing tax system.¹¹

While simulating the impact of removing the specific tax provision from the existing tax system on tax revenues, all other factors remain unchanged. This assumes no behavior responses by taxpayers and no policy changes by government. Thus, the following caveats should be noted.

First, the removal of a specific tax provision may cause taxpayers to rearrange their affairs in order to minimize the amount of their tax liabilities. For example, if the exemption of interest income of households were repealed in the individual income tax, taxpayers may either increase investment on equity markets or transfer most of their household savings offshore. By assuming no behavior responses by taxpayers, the estimate of the tax expenditure would tend to overstate the forgone tax revenues.

By the same token, if the tax exemption of gasoline under the ITBIS were eliminated, the tax-inclusive price of gasoline for consumers would likely increase and the demand for gasoline would fall and so would the demand for vehicles and other complementary goods. This, in turn, would cause further reduction in the demand for gasoline. Since our methodology has not taken into account the dynamics or feedback of the market, the actual reduction of tax revenue could be larger than the estimate of the tax expenditures indicated in the report.

Second, the estimates of tax expenditures do not take into account the potential impact of changes in government policy. For example, if the government were to eliminate the lower income tax rates for small businesses, it could require other measures for the political or economic reasons. The estimates do not account for the consequential changes in government policy.

Nor does the government take into consideration the potential impact of a particular tax provision on the overall economic activity. For example, if the government were to eliminate the exemption of electricity under the ITBIS, it would raise the price of electricity demanded by households and businesses. In the case of the latter, businesses can claim the tax credit for the taxes paid on electricity against the tax they have charged on the sale of their taxable goods and services. Households, however, would be stuck with additional taxes and the government may either provide subsidy to households on their consumption of electricity or pressure the power authority to lower the tariff rates. In any case, no allowances in this estimate are accounted for the economic impact and the consequential government responses of repealing the tax provision.

3.3 Estimates

¹¹ This is the case used in Canada to estimate the tax expenditures under the individual tax system and the corporate income tax system. See, e.g., Marc Seguin and Simon Gurr, "Federal Tax Expenditures in Canada", edited by Hana Polackova Brix, Christian M.A. Valenduc, Zhicheng Li Swift, editors, Tax Expenditures – Shedding Light on Government Spending through the Tax System, (Washington, D.C.: the World Bank, 2004).

This report provides estimates of the revenue cost of the tax expenditures in the individual income tax, corporate income tax, the ITBIS, the selective tax on consumption, and customs duty for 2002. As was previously discussed, we consider the most fundamental structural elements of each tax system, along with consideration of the ideal tax system under the selective tax on consumption and the import duty system, as the norm or benchmark. The benchmark includes to the tax structure, the tax base, the tax rates, the tax unit, and the tax accounting period of each tax system as established in the previous section. Any tax provision deviated from these established benchmarks is considered as tax expenditures.

Tax expenditures are generally tax concessions because of exemption, deduction or tax credits provided to a specific taxpayer, group of taxpayers, industry or location. However, when the government imposes a higher tax burden instead of benefit to the taxpayers, negative tax expenditures occur. Explanations of the special tax provisions and the methodologies used to estimate the tax expenditures are provided in this section.

All estimates of tax expenditures presented in this report are rounded in RD\$5 thousand.

3.3.1 Individual Income Tax

In the benchmark of the individual income tax system, income is imposed in a progressive manner on wages and salaries as well as net income earned by sole proprietors and other professionals without being incorporated. The tax is also levied on dividend incomes at a flat rate. The following tax expenditure items are organized in groups of tax base, tax rate, and tax in special locations.

3.3.1.1 Tax Base

Real interest income

All interest income earned by individuals from financial institutions as well as from savings and loans associations is currently tax exempt. This is a tax expenditure item as other financial incomes such as dividends are taxed at a flat rate of 25 percent that is considered as part of the benchmark system.

If interest income were taxed at the 25 percent, it should have been levied on real, rather than nominal, income because part of the nominal income is simply to compensate for the fall in value of the principal. This can be illustrated below. Suppose that the real annual interest rate is r , nominal annual interest rate is i , annual inflation rate is GP^e , the annual nominal interest income of principal RD\$1 will be:

$$i = r + r GP^e + GP^e.$$

If the tax rate, t , is applied to nominal interest income, then the amount of tax in real term will be rt plus an amount of inflation component, $tGP^e/(1 + GP^e)$, as shown below:

$$it/(1 + GP^e) = rt + tGP^e/(1 + GP^e)$$

In other words, one should remove from the nominal interest income the amount equal to the multiplication of principal and inflation rate. Thus,

$$Rt = it/(1 + GP^e) - tGP^e/(1 + GP^e)$$

In 2002, interest income and fees paid by banks and all other deposit taking institutions were approximately RD\$19,111 million, paid not only to individuals but also to companies. Since the norm were to tax real interest income received by individuals alone at 25 percent,¹² one can calculate the tax expenditures with the assumption that deposits by individuals account for 80 percent of the total deposit savings, inflation rate at 10.5 percent, and the average interest rate of deposits at 16.5 percent.

The estimates of the revenue cost are based on information obtained from the Central Bank, Dominican Republic, *Annual Report*, 2002.

Insured income received from life insurance

Any income received from life insurance is tax exempt by recipients.

No data are available.

Income received from being laid off

No tax is imposed on income received as a result of dismissal or layoff.

No data are available.

Income received by Chambers of Commerce

No tax is levied on income received by Chambers of Commerce.

No data are available.

Income received by religious institutions

No tax is levied on income received by religious institutions if those incomes are obtained from cult.

No data are available.

Income received by sport associations

¹² Interest incomes received by companies are taxable while interest payments can be deducted as a business expense.

No tax is levied on income received by sport associations.

No data are available.

Withholding tax on certain fringe benefits

Fringe benefits such as housing, vehicles, insurance premiums, domestic employees, insurance premiums, and special discounts on the sales of goods are regarded as part of compensation package to the supply of labor services and thus should be considered as part of income. They should all be subject to the individual income tax.¹³ In the Dominican Republic, fringe benefits are taxed at a special fringe benefits tax of 25 percent and withheld at the level of the employer on behalf of his employees. At the same time, the cost of providing fringe benefits is a tax-deduct expense for the employer and thus no tax expenditures are created at the corporate or the individual level.

There are, however, exceptions in which fringe benefits are neither withheld at the corporate level nor are they taxed at the individual level. The items include meals, uniform or dress provided by employers to their employees and they are thus regarded as tax expenditures.

No data are available.

3.3.1.2 Tax Rate

Low tax rate for small businesses

Small businesses are taxed at lower rates in the Dominican Republic. As will be discussed later in the corporate income tax section, the corporations are taxed at the greater of the corporate income tax and the 1.5 percent tax on turnover. In the case of small businesses, those with gross income less than annual sales of RD\$6 million are levied at lower tax rates. The rates on turnover range from 0.75 to 1.25 percent, lower than the standard 1.5 percent and thus considered as tax expenditures. In addition, the turnover rate on sales is a minimum tax which will be regarded as negative tax expenditures.

Due to the inseparable sales data obtained between corporate and unincorporated small businesses, the amount of the tax expenditure will be reported in the section of the corporate income tax.

Interest income received by non-residents

Interest incomes received by non-residents from financial institutions in the Dominican Republic were withheld at 15 percent in 2001, reduced to 5 percent in 2002 and then

¹³ While these benefits are not remunerated in money, they are often not taxed at the personal level in many developing countries.

increased to 15 percent in 2003. These flat tax rates are all lower than the rate imposed on return from equity capital at 25 percent, which is established as part of the benchmark.

The estimates are based on information obtained from the tax administration, Direccion General de Impuestos Internos, Dominican Republic. In 2002, the withholding tax on interest incomes received by non-residents were RD\$104,732 thousand. Again, only real interest income received by non-residents would have been taxed under the benchmark tax system.

Winnings from Casinos

Prior to 2000, a withholding individual income tax was based on 15 percent of the winning amount of gambling activities in excess of DR\$50,000. Due to the difficulty in administering this tax on various gambling activities, this withholding tax was withdrawn and replaced by other schemes.

Beginning in year 2000, casinos are supposed to withhold an individual income tax on the amount of winnings. The tax base is the total amount of tax collected based on the numbers of tables and machines owned by each casino and the withholding tax rate is 10 percent.¹⁴

In 2003, the total collections of the individual income taxes withheld by casinos were about RD\$16,828 thousand. In fact, it is not unclear what would be the true amount of winnings and thus impossible to correctly quantify the tax expenditures by using 25 percent as the norm rate. However, if the withholding taxes reported were the right figure, the tax expenditure would amount to RD\$25,240 thousand in 2003.

Winnings from sport betting

In the case of sport betting, beginning in 2001 three taxes inclusive of the corporate income tax, the ITBIS and the withholding individual income tax have been rolled into one tax. It is difficult to know what portion of the collections would belong to the individual income tax and what constitute the revenue cost of this tax.

No data are available.

Winnings from horse racing

In the case of horse racing, the withholding tax is based on 10 percent of the amount of winnings. The amount of withholding taxes collected were RD\$293 thousand, RD\$180 thousand, and RD\$189 thousand in year 2001, 2002, and 2003, respectively. If the rate of 25 percent is part of the benchmark, the revenue cost would be RD\$440 thousand in 2001, RD\$270 thousand in 2002, and RD\$284 thousand in 2003.

¹⁴ Casinos started to pay corporate income taxes in 1997 based on the number of tables and the number of machines they owned. Details of this scheme are described in the section of the corporate income tax.

Winnings from bingo

In the case of bingos, the withholding individual income tax on the winning amount was RD\$18 thousand in 2002 which is less than the benchmark and should be considered as tax expenditures.

If the withholding individual income tax on winnings from bingos were also 10 percent, the tax expenditures would have been RD\$27 thousand.

3.3.1.3 Tax in Special Locations

Non-taxation of dividends earned from companies located in free trade zones

Dividends from share ownerships received from firms operating in the free trade zones are exempt. This would provide a preferential treatment of investment in the free trade zones as compared to the rest of the country.

From Direccion General de Impuestos Internos, Dominican Republic, we obtained that the total dividends paid in free trade zones were RD\$1,008.4 thousand in 2001, RD\$84.8 thousand in 2002, and RD\$37.5 thousand in 2003. Since they are tax exempt, the revenue cost of this provision in 2002 would be RD\$20 thousand.

3.3.2 Corporate Income Tax

The benchmark of the corporate income tax was established in the previous section. The following tax expenditure items are organized in groups of turnover tax, tax base, tax rate, and tax on special locations.

3.3.2.1 Turnover Tax

As was described in Section 2.2, the 1.5 percent tax on gross sales is a minimum income tax regardless the companies are profitable or not. It is considered as negative tax expenditures in this report.

The estimates are based on 700 largest firms obtained from the tax administration, Direccion General de Impuestos Internos, Dominican Republic and then projected to all corporations in the country.

3.3.2.2 Tax Base

Non-taxation of non-profit organizations

Like unincorporated organizations, non-profit organizations, if incorporated, are exempt from the corporate income tax. This is a tax advantage to these organizations especially if they engage certain commercial activities.

No data are available.

Deductibility of donations

Donations made by corporations to institutions of public goods such as charity, religion, education and scientific research are tax deductible. The deduction is limited to 5 percent of net income. Since the deduction is not incurred to earn income, it would be considered as tax expenditures.

In 2002, the total amount of donations deducted by enterprises for their income tax purpose was approximately RD\$438,869 thousand. This implies that the revenue cost to the government would be RD\$50,315 thousand.

The estimates are based on annual returns of the 700 largest firms obtained from the tax administration, Direccion General de Impuestos Internos, Dominican Republic.

Non-taxation of income from lottery

There is one general administration of National Lottery, which is a state corporation and monopoly for lottery, as well as numerous private lotteries spread across the country. The private lotteries make payments based on their profits at 24 percent -- equivalent to license fees -- to the National Lottery.

No corporate income tax is levied on the income earned by the National Lottery.

No data on the financial statement of this corporation are available to estimate the revenue cost to the government.

Non-taxation of income from sport betting

As was previously mentioned, since 2001 three taxes including the corporate income tax, the ITBIS, and the withholding individual income tax from sport betting have been rolled in one law; the amount of tax is based on the building of the establishment. For those establishments located in the National Capital and two other big cities, the total annual amount of tax payment is DR\$250,349 per establishment. For the rest of the country, the annual payment is lower at DR\$150,554 per establishment.

This special treatment certainly deviates from the benchmark. However, it is impossible to quantify the tax expenditures for each component of the three tax systems as no breakdown of the aggregate payment was given in law or regulations. Moreover, the amount of tax payment differs among locations. If the payment per establishment were the same between locations, and if the payment in the National Capital were assumed to be the norm, the tax expenditure of this provision would have been RD\$9,737 thousand in 2002.

Non-taxation of income from horse racing

In the Dominican Republic, there is only one horse racing corporation and no tax is imposed on income earned by the firm which engages in the horse racing activities.

No data are available.

Non-taxation of income from bingos

There are eight bingo corporations. They paid a total of income taxes at RD\$259 thousand in 2002 and RD\$301 thousand in 2003. Since the amounts of taxes paid are less than the benchmark, it is considered as tax expenditures.

No detailed data are available.

Inflation Adjustment for Deduction in Depreciation Expenses

Under the corporate income tax the depreciated value of the assets is adjusted for inflation in order to obtain the correct basis for the purpose of calculation of the annual amount of depreciation expense. Although the income tax regulations now stipulate that the rate of inflation times the amount of net financial debt outstanding by the end of fiscal year should be included as part of taxable income, this part of adjustments for the effect of inflation on corporation taxable income has not been implemented to date.

Based on a 10.5 percent rate of inflation in year 2002, the revenue cost of this provision would be approximately RD\$665 million for the largest 632 firms. Since the total corporate income tax revenues of the 632 firms accounted for approximately 55.2 percent of the total tax revenues collected from all corporations in the country, the total revenue cost of this unimplemented provision would be RD\$1,204 million.

Deductibility of contributions to pension and retirement

Contributions to pension and retirement plans are tax deductible to corporations. The deduction was limited to 5 percent of net income before to 2001. Since then, the limitation has been lifted and companies are able to deduct whatever their contributions to social security and pension plans.

It may be questionable whether the deduction of pension and retirement should be considered as a tax expenditure item. However, since the pension income is not taxable under the individual income tax system, we would regard the deduction as a tax expenditure item. In 2002, the total amount of contribution to pension plans by enterprises was RD\$298,413 thousand. This implies that the maximum revenue cost to the government would be RD\$74,605 thousand.

3.3.2.3 Tax Rate

Low tax rate for small businesses

In the period of 2001 to 2003, the rate structure of the corporate income tax adopted was the greater amount of the 25 percent rate levied on corporate profits and the 1.5 percent turnover tax. However, a special turnover rate was applied to small businesses. That is, a turnover tax at the rate of 0.75 percent was withheld monthly from establishments with gross sales up to RD\$2 million, 1.00 percent from businesses with gross sales between RD\$2 to 4 million, and 1.25 percent on enterprises with gross sales between RD\$4 to 6 million. These small businesses paid lower turnover tax rates and are thus considered as tax expenditure item. Notwithstanding, this report only recognizes a single corporate income tax rate of 25 percent as the rate for the benchmark system. Thus, even with the lower, but minimum, turnover rates for small businesses, they would create negative tax expenditures.

From the data obtained from Direccion General de Impuestos Internos, we found that there were 1,834 enterprises registered for the small taxpayer regime. With the single tax rate of 25 percent as the sole benchmark rate, imposing the lower turnover tax rates on small businesses would have the tax expenditures of RD\$950 thousand. It should be noted that this figure was estimated for all small businesses regardless they were incorporated or not.

Special depreciation rates for leased assets

Leased depreciable assets have 50 percent higher depreciation rates than non-leased assets. That is, for leasing corporations 50 and 30 percent of depreciation rates on assets are provided for assets that are classified in Categories 2 and 3, respectively, as compared to the 25 and 15 percent for non-leased assets.

In year 2002, leasing companies deducted a total of RD\$11,155 thousand for Category 2 and RD\$93 thousand for Category 3 in their tax returns. However, no detailed data are available to simulate the tax expenditures of this provision.

Lower taxable income in casinos

Since 1997, casinos have paid their company taxes based on the number of tables and the number of machines they own. With this simple rule, income tax was exempt on profits earned from casinos.

The amount of tax paid on each table is based on the locations of operation as well as the number of tables owned by each casino. For those casinos located in Santo Domingo, Santiago, and La Ronana, the monthly tax schedules are shown below:

- DR\$12,000 per table for those who own 1 to 15 tables;
- DR\$14,000 per table for those who own 16 to 30 tables; and
- DR\$16,000 per table for those who own more than 30 tables.

For casinos which are located in the east, the monthly payment is DR\$8,000 per table regardless of the number of tables. For those located in the north, the monthly payment is lower at DR\$6,000 per table.

In the case of machines, the monthly taxes per machine are based on the types of machines. They are classified as follows:

- DR\$1,000 per machine for the 5 cents (US currency) machine;
- DR\$2,000 per machine for the 10 cents (US currency) machine;
- DR\$4,000 per machine for the 25 cents (US currency) machine;
- DR\$6,000 per machine for the 50 cents (US currency) machine; and
- DR\$10,000 per machine for the 1 dollar (US currency) machine.

This simple rule presumably imposes a lower tax liability on casino as compared to the benchmark tax rate system. However, it could be a negative tax expenditure item because the tax liability is given in spite of the case whether they are profitable or not. Without additional information about the operation of each casino, it would be impossible to quantify the tax expenditures.

Notwithstanding, the lower tax rates levied on tables located in the areas other than Santo Domingo, Santiago and La Ronana create further tax expenditures. Using the rate structure in Santo Domingo as the norm, this report estimates the tax expenditures in the amount of DR\$12,888 in 2002.

Non-taxation of income earned from the promotion of tourism activities

In October 2001, an incentive law was enacted to promote tourism industry. There are two kinds of tourism areas aimed at tourism promotion. The first is aimed at the rich areas which used to receive incentives and have already been developed as tourism area but need some incentives for complementary activities. These activities include investment in the areas of golf course, yacht, and hospital. The other kinds target at poor areas such as No. 4, 5 and 8. The incentives are much broad and extended to new investment in the areas of hotel, casino and restaurant.

The main incentives provided to firms with new investment include a ten-year income tax holiday and exemption of import duties and the ITBIS. However, the incentives may vary from area to area. For instance, firms in Area No. 3 are exempted from the indirect taxes levied on construction materials, equipment used in hotel but no tax holiday for the income tax is available. Council for Tourism Promotion was created to oversee approval of various incentives in various projects submitted.

Since its inception, the following 13 projects have been approved to receive tax incentives. The Ministry of Tourism has estimated that the amount of tax incentives would be about 25 percent of the approved capital investment. In the case of year 2002, the tax expenditures would have been US\$2,980,985 if the projects were carried out in 2002. This is problematic because no detailed data are available to quantify the potential

amount of incentives. In addition, no information is available as to the project in question has been carried out. Nevertheless, the following table provides the potential tax incentives and tax expenditures.

Projects	Date of Approval	Amount (US\$)
Parque Acuatico Y Marina (Deep Down Discovery)	June 2002	7,922,313.00
	February 2003	1,215,160.00
	December 2003	1,966,000.00
Campo de Golf Guavaberry	July 2002	3,198,659.00
Ampliacion Muelle Turistico (casa de Campo)	July 2002	802,969.53
Gran Hotel Del Cibao	February 2003	7,895,289.45
	December 2003	2,697,602.65
Embassy Suite Hotel Los Marlins Golf	March 2003	1,434,149.39
	May 2003	249,310.18
Campo de Golf Punta Espada (Cap Cana)	February 2003	6,271,450.04
Edificio de Condominio de Fundadores (Cap Cana)	April 2004	90,934.20
Hotel Puerto la Palma Beach Club Y Casino	March 2003	465,444.04
Hotel Bahia Estela Caribe	January 2004	331,941.20
Centro Medico Punta Cana	October 2003	352,896.75
Ampliación Marina Chavon (Casa de Campo)	October 2003	6,737,700.99
Infraestructura Electrica Y Sanitaria (Cap Cana)	December 2003	3,291,966.03
Las Villas del Caletón (Cap Cana)	April 2004	185,924.60

Sources: Secretaria de Estado de Turismo, Republica Dominicana.

Tax Treaty

Tax treaty provides preferential tax treatments for the countries which have tax treaty agreements with the Dominican Republic. In the Dominican Republic, there is only one tax treaty with Canada. The treaty provides the Canadian firms with a lower tax rate at 18 percent, instead of 25 percent, of the corporate income tax.

The estimates are based on the data obtained from the tax administration, Direccion General de Impuestos Internos, Dominican Republic.

3.3.2.4 Tax in Special Locations

Non-taxation of income earned from border zones

Levy 28-01 created special zones for the development along the border with Haiti in February 2001. These zones include the provinces of Pedernales, Independencia, Elias Pina, Dajabon, Montecristi, Santiago Rodriguez y Batoruco. This law intends to promote the enterprises in industrial, agricultural, metal, mining, energy and tourism sectors.

The incentives are provided for a period of 20 years including among others:

- Exemption of net income subject to income tax under Title II of No. 11-92;
- Exemption of the ITBIS under Title III of No. 11-92;
- Exemption of import duties on:
 - Fuel, lubricant for industrial use; and
 - Machinery, equipment, parts and accessories.
- 50% exemption of fees paid to port and airport;
- Exemption of 4.75% commission on foreign exchange;
- Exemption of 50% of the 2 percent temporary surcharge on imports; and
- Exemption of 50% of the 5 percent CST on exports.

The border zone incentives create distortions not only among domestic firms but also domestically produced goods versus imported goods. The latter would generate potential issues contradicted to the WTO rules.

Since the incentives were just enacted in 2001, no many firms have taken the advantages yet.

Lower income tax rates for operators of the parks in free trade zones

Operators of the parks in free trade zones and border zones have special tax privileges of the corporate income tax. Companies established in the border zones are exempt of the entire corporate income tax. Companies established in the National Districts or within 50 km of radius are exempt for 80 percent of their income taxes. For those located in the rest of the country, 90 percent of their income taxes are tax exempt.

The preferential tax treatment would cost the treasury RD\$6,010 thousand in 2002. The estimate is based on the data obtained from the tax administration, Direccion General de Impuestos Internos, Dominican Republic.

Non-taxation of income earned by firms located in free trade zones

The free trade zones have played a very important role in the economy of the Dominican Republic. They are not concentrated in one or two areas of the country. In total there are 53 parks that are spread over most of the areas of the country where there are concentrations of population. In 2002, there were 520 operating companies distributed across the country, providing employment for over 170,000 workers. The following table shows a significant amount of exports over imports expressed in millions of the U.S. dollars over the past three years. By 2002, exports from the free trade zones made up almost 84 percent of all exports from the country.

Year	Exports	Imports	Net Exports
2001	4,481.6	2,826.4	1,655.2
2002	4,317.3	2,600.3	1,717.0
2003	4,398.7	2,617.6	1,781.1

Sources: The Central Bank, Dominican Republic.

Companies operating in the zones have not paid corporate income taxes nor do they pay import duties or the ITBIS.¹⁵ As of 2007, the incentive provision regarding the corporate income tax will no longer be allowed under the new WTO rules. The same corporate income tax has to be applied equally to companies operating in the free zones as those located outside the zones.

One may argue that no corporate income tax should be imposed on companies operating in the zones because the country has no control over the international cost of capital required to finance the investment in the zones and the prices of the services provided are fixed internationally. Any additional corporate income taxes that levied on the income from capital investments in the zones will not change the net of tax return to companies but will force the wage rate being paid to labor they employ to be decreased. The reduction in the total wage bill paid to labor in the zones will be approximately equal to the additional corporate income taxes paid by these companies.

That being said, the current rule is discrimination in favor of companies operating in the zones and is therefore considered as tax expenditures. However, no detailed data are available to estimate the tax expenditure of this provision.¹⁶

3.3.2.5 Fiscal Period

Loss carry-overs

Loss carry-overs can be regarded as part of the benchmark tax system because the nature of business is risk-taking and income generated from the investment may last several years. This provision allows firms to average out their risk-taking in the future; in the

¹⁵ The only exception is the individual income taxes.

¹⁶ The revenue forgone from these firms would have been approximately US\$64.76 million in 2002 if the 1.5 percent turnover tax were imposed.

case of the Dominican Republic a tax provision allows for three years of loss carry-overs to reduce the taxpayers' liability.

The amounts of loss carry-overs by the end of the fiscal year 2001 and 2002 were about DR\$24,019,249 thousand and RD\$35,222,470 thousand, respectively. If one considers a fiscal year as the accounting base, the revenue cost in 2002 would have been RD366,195 thousand. Nevertheless, this tax expenditure may be theoretically arguable.

3.3.3 The Tax on the Transfer of Industrialized Goods and Services (ITBIS)

The Tax on the Transfer of Industrialized Goods and Services (ITBIS) is a multi-stage sales tax system wherein tax is applied to sales of goods and services at all stages of production and distribution chain. It is an invoiced method and a single tax rate with the destination principle. As such, any good sold domestically should not be zero-rated nor exempted.

With the consumption-type ITBIS on destination principle, vendors charge a tax on sales and receive credits or refunds for taxes that were paid on the purchases of business inputs used in the production of taxable sales. The number of the ITBIS taxpayers is about 36,250. What is not credited or refunded is the tax that is imposed on sales to final consumers including governments. Thus, under the ITBIS system sales on final consumption end up being taxed, which is equivalent to the single stage retail sales tax. Based on this equivalency, the ITBIS base can be estimated using the detailed final private consumption by commodity in the input-output tables, the detailed Central Government expenditures by commodity, and the National Accounts, prepared by the Central Bank of the Dominican Republic. By the same token, the data can be used to estimate the revenue costs of all the tax expenditures associated with the specific provisions of the ITBIS.

The latest detailed private consumption by commodity is available for the year 2001. The data are projected to the year 2002 using the growth rate of the aggregate private consumption in current prices provided in the National Accounts, which is 10.4 percent. The data are supplemented by the 1998 Household Expenditure Survey conducted in the Dominican Republic that was extremely detailed in terms of commodity breakdown in order to identify the revenue implications of certain specific goods and services which are tax exempt under the ITBIS.

This section describes various ITBIS tax expenditure items and how these tax expenditures were estimated for year 2002. As was defined in the previous section, the benchmark system is a broad based with a single rate and also taxed in destination principle. As such, spending on any good or service by final consumers should be considered as tax expenditure if it is either zero-rated or exempted or if it is not levied at the standard tax rate of 12 percent.

3.3.3.1 Tax Base

There are a wide range of goods and services that are specifically exempted from the ITBIS system. The revenue costs of tax expenditure by exempt commodity are estimated by using the detailed personal consumption expenditures of the input-output tables and the expenditures by the Central Governments. By not taking into account the expenditures made by local governments, the following estimates of tax expenditures in 2002 may be slightly understated.

Live animals and animal products

Live animals such as horse, goat, rooters, chickens, ducks, geese, turkeys, and fish are exempt of the ITBIS. The data are obtained from the input-output tables and the National Accounts.

Basic Groceries

Basic groceries including the main foodstuffs for preparation and consumption at home, dairy product, and vegetable are all tax exempt under the ITBIS. The foodstuffs include rice, bread, flour, cereals, potato, corn, noodles, and other processed food. Dairy products include milk, butter, and cheese. In addition, basic groceries also include eggs, vegetable, fruits, nuts that are all tax exempt. The data are obtained from the input-output tables and the National Accounts.

Agricultural products

Agricultural products include sugar cane, seeds, wood, and other traditional agricultural products which are currently subject to tax. The data are obtained from the input-output tables and the National Accounts.

Food for animals

Food for animals is exempt under the ITBIS. The data are obtained from the input-output tables and the National Accounts.

Coffee, tea, chocolate, sugar, salt and other spice items

This category includes coffee, tea, sugar, salt, honey and all other spices. They are currently exempted under the ITBIS. The data are obtained from the input-output tables and the National Accounts.

Books, magazines, and newspapers

This item refers to all reading materials. It includes books, magazines, and newspapers. It is all exempt under the ITBIS. Again, the data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Art works

Art works are exempt under the ITBIS. No data are available.

Fertilizer and insecticide

This item includes fertilizer and manure used for farming and home garden. It also includes fungicides, herbicides and insecticides. It should be noted that these goods, when purchased by farmers, are an input in the agricultural production and the tax paid can thus be claimed as credit against the tax charged on farm products by the end of the tax period. It becomes only a cash-flow problem under the ITBIS system and hence the revenue cost to the government would be small. Estimates of this revenue cost are mainly the taxes associated with the amount purchased by households for final consumption.

The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Soap, toothpaste and detergents

The ITBIS provides exemption on the sale of soap, toothpaste and detergents. The estimate is based on the data obtained from the input-output tables and the National Accounts.

Match

Match is also exempt under the ITBIS. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Medicine for human and animal use

Drugs or other medicine for human and animal use are exempt under the ITBIS. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Petroleum and its derivatives

The ITBIS provides an exemption for gasoline, diesel, aviation fuel, and cooking gas. When they are used as business inputs in the activities such as transportation, the ITBIS levied on them can be claimed as credit and should be considered as tax expenditure.

The revenue cost presented in this report is only related to the final consumption made by households and governments. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Electricity

Electricity is heavily subsidized in the Dominican Republic. It is specifically exempt under the ITBIS. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Water

Water is exempt under the ITBIS. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Residential rent

Residential rent is tax exempt under the ITBIS. However, data are not available to estimate the revenue cost.

Ground passenger transportation services

Ground transportation services including passenger and freight transportation services are exempt. In the case of passenger service, it includes municipal transit service as well as transportation services between cities. In the case of air or marine services, they are taxable under the ITBIS.

The revenue cost of this provision would be the services provided to the final consumers and governments only. In the case of services provided to businesses, they are neither charged nor do they get credits on this business input and therefore no tax expenditures would be contemplated.

The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Ground freight transportation services

Ground freight transportation services are tax exempt. The revenue cost is based on the expenditures spent by households and governments. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Health services

Health care services refer to institutional services (e.g., hospitals) as well as services provided by physicians such as general practitioners, dentists, chiropractors, psychologists, etc.

The estimates include the expenditures spent by households and governments in medical services. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Education services

Education and training services provided by the public and private sectors are all exempt under the ITBIS. It includes tuition fees paid for courses provided in elemental or secondary schools as well as university or college. Any meals supplied to students free of charge should also be included in the estimate of the tax expenditures in this provision.

Estimates of this cost refer to primary and secondary educational services only because of limited data. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Waste disposal services

Basic garbage collection services and other social are exempt under the ITBIS. Estimates of this revenue cost only refer to the personal spending on the services of waster disposal. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Barber shops, salons and other personal services

Barber shops, salons and other personal services are all tax exempt. The data used to estimate the revenue cost is obtained from the input-output tables and the National Accounts.

Domestic insurance services

Financial services are generally defined to include financial intermediation service, market intermediation service, and risk pooling. The last item refers to insurance and reinsurance. The price of most financial services is implicit and thus it becomes very difficult to determine and apply the tax to the sale of the service. As a result, virtually all the VAT jurisdictions in the world exempt the domestic financial services which are regarded as the benchmark in this report.

In the Dominican Republic, financial intermediation service and market intermediation service provided to residents are also exempt. However, insurance premiums are taxable under the ITBIS irrespective of life insurance or property and casualty insurance. As such, the insurances are taxed not only insurance services but also some investment income. It is a negative tax expenditure item.

The estimates are based on the data obtained from the tax administration, Direccion General de Impuestos Internos, Dominican Republic

Exemption for small businesses

Businesses or individuals who carry out commercial activities with gross sales less than RD\$2 million are tax exempt and thus outside of the ITBIS system. They are not required to register nor do they collect the ITBIS from their customers.

Although the amount of gross sales for small businesses can be obtained from the income tax file, no data are available about their business inputs. Thus no reliable estimates can be obtained for tax expenditure of this provision.

3.3.3.2 Exemption Associated with Exempted Customs Duty

Following the special exemption of customs duty provided to immigrants or returning residents, the public sector institutions, etc., the ITBIS also provides the same tax exemption. The estimates were based on the simulations that forgone tax revenues that would have been imposed on top of import-duty paid value plus specific excise taxes, if applied. Specifically, the estimates were simulated by the comparison between the status quo and the repeal of this special provision. It should also be noted that those imports which are used as business inputs in the production of exports are not regarded as tax expenditures as they are part of the fundamental multi-stage ITBIS structure.

Instead of reporting the tax expenditures by commodity, the tax expenditures in this provision refer to a variety of imported goods and are reported by resolution. The data source of these estimates is the Customs Department of the Ministry of Finance.

Imported goods by passengers

The ITBIS provides a tax exemption for personal use of imported goods that are exempted from import duties.

Imported goods by immigrants or returned migrants

Following the special exemption of customs duty provided to immigrants or returning residents, the ITBIS also provides the same tax exemption. These imported goods can include the vehicles, furniture, and other goods.

The estimate of this report only includes those returning Dominicans.

Imported goods by the public sector institutions

The ITBIS provides a special exemption for the institutions of public sector for imported goods if it is exempted by customs duty. These institutions include government departments and the office of Director of Communication.

It should be noted that the imports for the use by the government of a foreign country or by diplomats are also exempt under the ITBIS. However, they are a common international practice and thus it is not considered as tax expenditure in this report.

The estimate is derived from the simulations based on the data received from the Customs Department of the Ministry of Finance.

Imported goods by cooperatives for government employees

The ITBIS provides a special exemption for cooperatives for government employees for their imports if they are exempted by customs duty.

Imported goods by educational institutions

The ITBIS provides a special exemption for educational institutions for imported goods if it is exempted by customs duty.

Imported goods by medical laboratories

Imports by medical laboratories are exempt under the ITBIS.

Imported goods by NGOs

The ITBIS provides a special exemption for non-government organizations for their imports.

Imported goods for promotion in tourism

In order to promote tourism, the ITBIS provides a similar exemption as customs duty for the imports used to promote the tourism sector.

Imported goods for promotion in agriculture

In order to promote the development of the agricultural sector, the ITBIS provides a similar exemption as customs duty for the imports used in agriculture aimed at the promotion of agricultural sector.

Imported goods for promotion in textile manufacturing

In order to promote the development of textile manufacturing, the ITBIS provides a similar exemption as customs duty for the imports used in the manufacturing of textile products.

3.3.3.3 Tax Rate

Lower tax rates for advertisement

The advertisement services are subject to a 6 percent tax rate under the ITBIS. This lower tax rate is regarded as a tax expenditure item.

Data are not available.

3.3.3.4 Fiscal Period

Deferral of input tax credits

Like other value added tax systems around the world, the ITBIS is a multi-stage sales tax using the credit invoice method. However, in the Dominican Republic when input tax credits are greater than the tax charged on gross sales, the excess amount is not refunded, but transferred as a deduction to the following monthly periods. In the case of exporters, although the tax code has a provision to request for a refund for the ITBIS paid on business inputs within six months, the system does not function in practice. This practice creates a cash flow issue for taxpayers and thus imposes the negative tax expenditure.

No data are available.

3.3.4 The Selective Taxes on Consumption

There are more than 135 commodities that are subject to the selective taxes on consumption. The tax rates vary from commodity to commodity regardless who is the purchaser. Hence, the concession to any purchasers who receives a tax exempt status or a lower tax rate than the general statutory rate specified in law is generally considered as the tax expenditures.

In the case of vehicles, the tax is based on the CIF value of the imported vehicles and may be perceived as a progressive tax because the marginal statutory tax rates increase as the prices of vehicle go up. However, the effective tax rates if expressed as a percentage of import duty-paid collected by tax bracket were found surprisingly low for 2002 as shown below. This is resulted from the widespread granting of exemptions as well as the valuation of the price differentials between cars imported by automobile dealers and those imported directed by individuals. Clearly, the progressive rate of excise taxes provides a huge incentive for importers to make deals with Customs officials to lower the price in order to avoid the progressive excise tax burden.

Volume of Imports and Taxes Collections for Vehicles, 2002

Price of Vehicle (FOB @US\$)	Tax Rate (%)	Import at FOB Value (US\$ thousands)	Import at CIF Value (RD\$ millions)	Import Duty (RD\$ millions)	Excise Tax (RD\$ million)	Average Effective Excise Tax Rate (%)
0 to 15,000	0	329,490.6	6,412.0	1,282.3	0	0
15,000 to 30,000	15	166,733.8	3,273.6	654.4	106.4	2.71
30,001 to 40,000	30	37,916.9	741.2	148.2	46.6	5.24
40,001 to 50,000	45	16,580.6	316.7	63.2	33.8	8.90

50,001 to 60,000	60	4,431.3	84.1	16.7	9.5	9.42
60,001+	80	14,878.1	290.2	57.7	14.1	4.05
Total	-	570,031.2	11,117.8	2,222.5	210.4	1.58

In addition to vehicles, there are exemptions as result of various resolutions granted by the government.

At present, the excise taxes applied on imports by more than 135 items vary from a 10 percent rate on ovens other than microwave to 60 percent rate on revolvers and pistols. For the purpose of this excise, a single rate of 20 percent is assumed to be an ideal rate and is thus considered as the norm.

In addition, a total of more than 135 commodity items subject to excise tax is rather large for a modern tax system. Since the purpose of the tax for certain items is entirely for revenue purposes, and the present choice of commodity is difficult to justify on economic or tax policy grounds (e.g., air conditioners, microwave stoves). For the purpose of this excise, the list of excisable goods include all alcoholic beverages, tobacco products, petroleum products, electricity, communication services, insurance premium, airline tickets, vehicles, and guns. Therefore, the benchmark assumes that the above list of excisable goods and services are levied at 20 percent, which was set to generate approximately the same amount of the excise tax revenue as the current system.

Estimates of these tax expenditures are presented in Table 4.

3.3.4.1 Exemption Associated with Exempted Customs Duty

Following the special exemption of customs duty provided to immigrants or returning residents, the public sector institutions, etc., the Selective Tax on Consumption also provides the same tax exemption as import duties for those relate to passenger baggage, immigrants, returning residents, institutions of the public sector, etc. The estimates were based on the simulations that forgone tax revenues that would have been imposed on top of import-duty paid value, if applied. They were simulated by the comparison between the status quo and the repeal of this special provision.

The data source of these estimates is the Customs Department of the Ministry of Finance.

Imported goods by passengers

The Selective Tax on Consumption provides a tax exemption for personal use of imported goods that are exempted from import duties.

No data are available.

Imported goods by immigrants or returned migrants

Following the special exemption of customs duty provided to immigrants or returning residents, the Selective Tax on Consumption also provides the same tax exemption. These imported goods can include the vehicles, furniture, and other goods.

The estimate of this report only includes those returning Dominicans.

Imported goods by the public sector institutions

The Selective Tax on Consumption provides a special exemption for the institutions of public sector for imported goods if it is exempted by customs duty. These institutions include government departments and the office of Director of Communication.

It should be noted that the imports for the use by the government of a foreign country or by diplomats are also exempt under the Selective Tax on Consumption. However, they are a common international practice and thus it is not considered as tax expenditure in this report.

The estimate is derived from the simulations based on the data received from the Customs Department of the Ministry of Finance.

Imported goods by cooperatives for government employees

The Selective Tax on Consumption provides a special exemption for cooperatives for government employees for their imports if they are exempted by customs duty.

Imported goods by educational institutions

The Selective Tax on Consumption provides a special exemption for educational institutions for imported goods if it is exempted by customs duty.

Imported goods for promotion in tourism

In order to promote tourism, the Selective Tax on Consumption provides a similar exemption as customs duty for the imports used to promote the tourism sector.

3.3.5 The Import Duty

There are eight import duty rates imposed on different imported goods in the Dominican Republic. Any tax rate deviated from this tariff structure is generally considered as tax expenditures. For the purpose of this exercise, however, an ideal tax system is considered to be a uniform tariff rate that is assumed as the benchmark.

In addition to the customs tariff, the government imposes a commission on foreign exchange transactions as well as a temporary measure of the increase in tariff rates. The commission on foreign exchange is equivalent to impose an additional tariff rate across

all imported goods including the currently zero-rate items. In 2002, it was at a rate of 4.75 percent.¹⁷

For the purpose of this exercise, a uniform rate across is imposed on all imported goods to get the same revenue as the current system including the commission on foreign exchange, which is approximately at 14.2 percent. Using the 15 percent tariff rate as the norm, the tax expenditures will be presented below.

3.3.5.1 The Current Tariff Rate Structure

Since 15 percent is defined in this report as the norm of the tariff rate, any rate inclusive of the commission on foreign exchange deviated from this rate is considered as tax expenditures. The commission on foreign exchange in 2002 was 4.75 percent, any goods subject to lower than 10.25 percent of the tariff rate would be considered as positive tax expenditure. On contrary, goods that were subject to more than 10.25 percent would have negative tax expenditures. All tax expenditures for 2002 are presented in Table 5 according to the current tariff rate.

The estimates were simulated from the data obtained from the Department of Customs, Ministry of Finance.

3.3.5.2 Bilateral Trade Agreements

The Dominican Republic has bilateral agreements with Caribbean or other countries. The agreements will either not attract any import duty or impose lower import duty rates on certain commodities.

The estimate of this tax expenditure provision was obtained from the comparison of import duties collected under the status quo and that would have been collected if the agreements were removed. The latter was simulated by the data obtained from the Customs Department of the Ministry of Finance.

3.3.5.3 Border Zones

For firms located in the border zones, their imports are all exempt of import duty even if their products are sold to domestic markets. Since the incentives were just enacted in 2001, no many firms have taken the advantages yet.

3.3.5.4 Special Resolutions by the Government

¹⁷ It may be noted that on July 1, 2003, an additional 2 percentage points of import duty rate was imposed on all imported goods as a temporary measure. This temporary measure is treated differently from the regular tariff rates. In general, import duties are applied on top of the CIF value of imports and excise taxes are levied on top of CIF value plus the regular import duty. Excise taxes, however, are not imposed on top of the 2 percent of the import duty surcharge nor is the ITBIS levied on top of the 2 percent temporary surcharge.

At the discretion of the government, the special resolutions provide various exemptions of import duty to specific institutions or individuals. These resolutions constitute tax expenditures in this report, they are described below. The amount of the tax expenditures is the excess of import duties that would have been collected under the benchmark system – the uniform tariff rate of 15 percent -- over the import duties actually collected in 2002.

Imported goods by passengers

Goods are exempted from import duties for personal baggage.

Data are not available.

Imported goods by immigrants or returned migrants

A special exemption of customs duty is provided to immigrants or returning residents after living abroad for two years. The imported goods include the vehicles, furniture, and other goods.

Due to limited information, the estimate of this report only refers to those returning Dominicans.

Imported goods by the public sector institutions

A special exemption is provided for the institutions of public sector for their imports. These institutions include government departments and the office of Director of Communication.

It should be noted that the imports for the use by the government of a foreign country or by diplomats are not regarded as tax expenditures in this report because they are a common international practice.

The estimate is derived from the simulations based on the specific goods imported into the country. The basic data is obtained from the Customs Department of the Ministry of Finance.

Imported goods by cooperatives for government employees

A special exemption of import duty is provided to cooperatives for government employees for their imports.

Imported goods by educational institutions

A special exemption of customs duty is provided to educational institutions for their imports.

Imported goods by medical laboratories

A special exemption of import duty is provided for medical laboratories.

Imported goods by NGOs

A special exemption of import duty is provided to non-government organizations for their imports.

Imported goods for promotion in tourism

To promote tourism, a special exemption of customs duty is provided for the imports used at hotel aimed at the promotion of tourism sector.

Imported goods for promotion in agriculture

To promote the development of the agricultural sector, a special exemption of customs duty is provided for the imports used in agriculture.

Imported goods for promotion in textile manufacturing

To promote the development of textile manufacturing, a special exemption of customs duty is provided for the imports used in the manufacturing of textile products.

IV. Concluding Remarks

This report has developed the benchmark for each of the major tax systems and then estimated the tax expenditures associated with specific tax provisions in the Dominican Republic. The benchmark can be subjective. The approach adopted in this report is a broad view with only the most fundamental structural elements of each tax system as part of the benchmark system. It has also gone further by assuming a uniform tax rates for the Selective Tax on Consumption and the import duties as the ideal tax system and thus considered as part of the benchmark in this report. As such, it would provide some useful information for readers to make their own interpretation of the appropriateness of the tax expenditures.

The estimates of the tax expenditures should be interpreted with caution. The revenue cost of the tax expenditure does not take into account the dynamics of the market or feedback to the tax provision in question. Therefore, it may not reflect the true revenue cost of the provision or the revenue gain if the provision were repealed.

Notwithstanding, the information provided in this report may help the government assess whether the special tax provisions are the most efficient way to achieve its objectives. It would also identify some potential areas for a review in the process of tax reform.

Table 1
Individual Income Tax Expenditures in 2002
(Thousands of Pesos)

Tax Provisions	Amount
Tax Base:	
<i>Real interest Income</i>	1,257,820
<i>Insured income received from life insurance</i>	n/a
<i>Income received from being laid off</i>	n/a
<i>Income received by Chambers of Commerce</i>	n/a
<i>Income received by religious institutions</i>	n/a
<i>Income received by sport associations</i>	n/a
<i>Withholding tax on certain fringe benefits</i>	n/a
Tax Rates:	
<i>Low tax rate for small businesses</i>	See Table 2
<i>Interest income received by non-residents</i>	137,860
<i>Winnings from Casino</i>	25,240*
<i>Winnings from sport betting</i>	n/a
<i>Winnings from horse racing</i>	270
<i>Winnings from bingo</i>	25
Tax on Special Locations:	
<i>Non-taxation of dividends earned from companies located in free trade zones</i>	20

Note: *The figure refers to the year 2003.

Table 2
Corporate Income Tax Expenditures in 2002
(Thousands of Pesos)

Tax Provisions	Amount
1.5 percent Turnover Tax	(3,600,560)
Tax Base:	
<i>Non-taxation of non-profit organizations</i>	n/a
<i>Deductibility of donations</i>	50,315
<i>Non-taxation of income from lottery</i>	n/a
<i>Non-taxation of income from sport betting</i>	9,735
<i>Non-taxation of income from horse racing</i>	n/a
<i>Non-taxation of income from bingos</i>	n/a
<i>Inflation adjustment for deduction in depreciation expenses</i>	1,204,000
<i>Deductibility of contributions to pension and retirement</i>	74,605
Tax Rate:	
<i>Low tax rate for small businesses</i>	(950)
<i>Special depreciation rates for leased assets</i>	n/a
<i>Lower taxable income in casinos</i>	12,890
<i>Non-taxation of income earned from the promotion of tourism activities</i>	n/a
<i>Tax treaty</i>	182,930
Tax in Special Locations:	
<i>Non-taxation of income earned from border zones</i>	n/a
<i>Lower income tax rates for operators of the parks in free trade zones</i>	6,010
<i>Non-taxation of income earned by firms located in free trade zones</i>	n/a
Fiscal Period:	
<i>Loss carry-overs</i>	366,195

Table 3
ITBIS Tax Expenditures in 2002
(Thousands of Pesos)

Tax Provisions	Amount
Tax Base:	
<i>Live animals and animal products</i>	92,825
<i>Basic groceries</i>	10,886,155
<i>Agricultural products</i>	29,940
<i>Food for animals</i>	741,440
<i>Coffee, tea, chocolate, sugar, salt and other spice items</i>	634,965
<i>Books, magazines, and newspapers</i>	617,085
<i>Art works</i>	n/a
<i>Fertilizer and insecticide</i>	118,380
<i>Soap, toothpaste and detergents</i>	190,435
<i>Match</i>	20,795
<i>Medicine for human and animal use</i>	72,965
<i>Petroleum and its derivatives</i>	1,468,175
<i>Electricity</i>	767,770
<i>Water</i>	152,670
<i>Residential rent</i>	n/a
<i>Ground passenger transportation services</i>	1,733,940
<i>Ground freight transportation services</i>	120,380
<i>Health services</i>	1,550,695
<i>Education services</i>	886,555
<i>Waste disposal services</i>	2,330
<i>Barber shops, salons and other personal services</i>	1,051,100
<i>Domestic insurance services</i>	(554,730)
<i>Exemption for small businesses</i>	n/a
Exemption Associated with Exempted Customs Duty:	
<i>Imported goods by passengers</i>	n/a
<i>Imported goods by immigrants or returned migrants</i>	29,950
<i>Imported goods by the public sector institutions</i>	1,315,395
<i>Imported goods by cooperatives for government employees</i>	610
<i>Imported goods by educational institutions</i>	20,975
<i>Imported goods by medical laboratories</i>	22,360
<i>Imported goods by NGOs</i>	35,140
<i>Imported goods for promotion in tourism</i>	140
<i>Imported goods for promotion in agriculture</i>	6,355
<i>Imported goods for promotion in textile manufacturing</i>	70
Tax Rate:	
<i>Lower tax rates for goods and services</i>	n/a

Fiscal Period:	
<i>Deferral of excess input tax credits</i>	n/a

Table 4
Tax Expenditures for the Selective Tax on Consumption in 2002
(Thousands of Pesos)

Tax Provisions	Amount
The Current List of Excisable Goods	(71,055)
Special Resolutions by the government:	
<i>Imported goods by passengers</i>	n/a
<i>Imported goods by immigrants or returned migrants</i>	45,035
<i>Imported goods by the public sector institutions</i>	58,570
<i>Imported goods by cooperatives for government employees</i>	520
<i>Imported goods by educational institutions</i>	13,165
<i>Imported goods by medical laboratories</i>	0
<i>Imported goods by NGOs</i>	4,155
<i>Imported goods for promotion in tourism</i>	0

Table 5
Import Duty Tax Expenditures in 2002
(Thousands of Pesos)

Tax Provisions	Amount
The Current Tariff Rates:	
<i>Imported goods subject to 0 tariff rate</i>	1,623,700
<i>Imported goods subject to 3 percent tariff rate</i>	1,999,430
<i>Imported goods subject to 8 tariff rate</i>	180,180
<i>Imported goods subject to 14 tariff rate</i>	(211,575)
<i>Imported goods subject to 15 tariff rate</i>	(645)
<i>Imported goods subject to 20 tariff rate</i>	(2,878,920)
<i>Imported goods subject to 25 tariff rate</i>	(54,870)
<i>Imported goods subject to 40 tariff rate</i>	(28,160)
Bilateral trade agreements	57,780
Border zones	n/a
Special Resolutions by the government:	
<i>Imported goods by passengers</i>	n/a
<i>Imported goods by immigrants or returned migrants</i>	25,500
<i>Imported goods by the public sector institutions</i>	312,235
<i>Imported goods by cooperatives for government employees</i>	560
<i>Imported goods by educational institutions</i>	18,495
<i>Imported goods by medical laboratories</i>	22,930
<i>Imported goods by NGOs</i>	31,185
<i>Imported goods for promotion in tourism</i>	110
<i>Imported goods for promotion in agriculture</i>	5,015
<i>Imported goods for promotion in textile manufacturing</i>	55

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