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The Political Economy of Tax Reforms and the Implications for Social Development in Nicaragua

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prepared for the UNRISD project on
Politics of Domestic Resource Mobilization

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The project seeks to contribute to global debates on the political and institutional contexts that enable poor countries to mobilize domestic resources for social development. It examines the processes and mechanisms that connect the politics of resource mobilization and demands for social provision; changes in state-citizen and donor-recipient relations associated with resource mobilization and allocation; and governance reforms that can lead to improved and sustainable revenue yields and services. For further information on the project visit www.unrisd.org/pdrm.

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Acronyms

ANJF	Nicaraguan Alliance for Fiscal Justice (NAFJ): Alianza Nicaragüense por la Justicia Fiscal
ALN	Nicaraguan Liberal Alliance: Alianza Liberal Nicaragüense
ANN	Nicaraguan National Assembly (NNA): Asamblea Nacional de Nicaragua
BAGSA	The Agricultural and Livestock Exchange (ALE): Bolsa Agropecuaria de Nicaragua
BCN	Central Bank of Nicaragua: Banco Central de Nicaragua
CENIS	Negotiable Certificate of Investment
COSEP	Superior Council for the Private Enterprise (SCPE): Consejo Superior de la Empresa Privada
CPC	Citizen Power Councils
CSJ	Supreme Court of Justice (SCJ): Corte Suprema de Justicia
DGP	General Directorate of the Budget: Dirección General del Presupuesto
EMNV	Living Standards Measurement Survey (LSMS): Encuesta de Medición de Nivel de Vida
FNT	National Workers Front
FSLN	Sandinista National Liberation Front: Frente Sandinista de Liberación Nacional
GDP	Gross Domestic Product: Producto Interno Bruto (PIB)
IEEPP	Institute of Strategic Studies and Public Policy (ISSPP): Instituto de Estudios Estratégicos y Políticas Públicas
IFI	International Financial Institutions
IMF	International Monetary Fund: Fondo Monetario Internacional (FMI)
INIET	Nicaraguan Institute for Fiscal Studies and Research (NIFSR): Instituto Nicaragüense de Investigaciones y Estudios Tributarios
JGRN	National Government Reconstruction Board: Junta de Gobierno de Reconstrucción Nacional
LCT	Tax Concertation Law (TCL): Ley de Concertación Tributaria
NGO	Non-Governmental Organization: Organización No Gubernamental (ONG)
PLC	Constitutionalist Liberal Party: Partido Liberal Constitucionalista
PNDH	National Plan for Human Development (NPHD): Plan Nacional de Desarrollo Humano
PRGF	Poverty Reduction and Growth Facility
SCT	Selective Consumption Tax: Impuesto Selectivos de Consumo (ISC)
VAT	Value Added Tax: Impuesto al Valor Agregado (IVA)

Summary

This paper examines the mobilization of domestic resources for social development in Nicaragua, analysing the fiscal system, its main tool. The main argument of the paper is that many tax reforms that have taken place in Nicaragua since the 1970s have been motivated mainly by the objective to increase revenue collection. However, through all the periods studied in this paper, higher revenue levels have not necessarily translated into higher social spending, as the latter has fluctuated throughout the different time periods. This results from power relations that determine the economic and social effects of the different tax reforms, more specifically, tax burdens, winners and losers, perpetuating an unequal system of wealth and income distribution in Nicaragua.

The structure of the paper follows a historical timeline divided into four periods: the late Somoza Dictatorship (1972-1979), the Sandinista Revolution (1980–1989), the Neoliberal period (1990-2006), and the Ortega administration (2007-present). The different periods analysed in the paper show an upward trend of tax revenue collection since the 1970's, except for the years afflicted by the two armed conflicts, the Sandinista revolution (1978-1979) and the *Contras* War (1985-1989), the period of hyperinflation in the late 1980's, and the most recent global financial and economic crisis (2008-9). Tax reforms are identified as a key tool for the central government to generate revenue and it is posited that through further reforms increments in revenue could have been achieved. Nevertheless, shifting government priorities during those periods directly affected social spending, in some cases prioritizing expenditure on defense and economic stability over social development.

The main focus of this paper is on the Ortega administration (2007 – present) in terms of tax revenue collection vis-à-vis social spending, focusing on the most recent tax legislation: the Tax Concertation Law. This section elucidates the power dynamics that shape tax legislation through processes of contestation and bargaining, giving way to winners and losers from the new tax reform. Furthermore, trends on revenue collection and social spending are examined, emphasizing the shortcomings of the Tax Concertation Law, the low levels of tax revenue collection, and its implication for the politics of domestic resource mobilization for social spending. The paper concludes that the revenue collected is not sufficient to support higher levels of social spending. Therefore, changes to the tax legislation and administration could potentially improve the ability of the government to mobilize further domestic resources destined to the public sector, thus improving social development.

Roberto Molina is a Political Economist who graduated from the University of California, Berkeley.

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Introduction

This paper examines the political economy of resource mobilization for social development[1] in Nicaragua, focusing specifically on the fiscal system.[2] As the second poorest country in Latin America (World Bank 2014), Nicaragua needs to improve the policies that directly affect the wellbeing of its citizens. This study scrutinizes the Nicaraguan fiscal system as a tool for the mobilization and allocation of domestic resources and to what extent these are conducive to social development. More specifically, it will examine the main tax reforms that have taken place in Nicaragua, and how they are related to social expenditure trends since 1972. We are particularly interested in analysing whether the state is using the fiscal system for redistributive purposes and for reducing the significant and persistent inequalities that afflict its society. To achieve this, three different themes will guide the analysis: the processes of bargaining and contestation that have led to the different taxation legislation, changes in key relationships between actors, and institutional development of state fiscal entities.[3]

Taxation has proven to be a key tool for the collection of revenue by the government. Aaron Schneider argues that the fiscal system constitutes a social contract between society and the state (see also Martin, Mehrotra, and Prasad 2009, cited in Schneider 2014). Moreover, he argues that the fiscal system reflects the type of state and the vision of development that a country follows. This can be illustrated by the fact that mainly through taxes, governments acquire the necessary resources to finance public expenditures, including social expenditure. In the case of Nicaragua, USD 87.00 out of every USD 100.00 of total government expenditure, are financed with tax revenue,[4] making taxation the most important instrument to acquire the resources needed for social expenses.

Understanding fiscal systems in terms of a social contract indicates that the politics of domestic resource mobilization are closely intertwined with changes in the relationship between the state and its citizens. Although the majority of government expenditures are financed by tax revenues, civil society with its limited participation in these bargaining processes has not been able to demand improved public services in return, a quid-pro-quo process we would expect from theory and the literature on tax bargains.[5]

Therefore, this paper will examine the following question: Different tax reforms that have been implemented in Nicaragua since 1972 have been a direct result of an increasing need for higher revenue collection, and have been successful in this sense. But why have higher revenue levels not translated into higher levels of social spending necessary to sustain social development? The hypothesis is that within the process of tax reforms, power relations in the practice of bargaining and contestation and state-citizen relations directly determine the outcome of tax legislation, more specifically, winners and losers in terms of tax burdens, perpetuating an unequal system of wealth distribution and access to social services in Nicaragua.

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1 For the purpose of measuring social development in this paper, increases in social expenditures, specifically on education, health, and overall wellbeing of the society, will be used as a benchmark.

2 Social development is defined as a “processes of change that lead to improvements in human well-being, social relations and social institutions, and that are equitable, sustainable, and compatible with principles of democratic governance and social justice” (UNRISD 2011: 1).

3 The first two themes will guide the analysis throughout the paper, while the latter will be examined in less depth since there is less data on the subject. For the analytical framework, see UNRISD 2012.

4 Elaborated by author, based on DGP 2013.

5 For an overview on the literature on taxation and governance, see UNRISD 2012.

The main research questions that will guide the analysis are: how have tax revenues evolved over time? What were the drivers and outcomes (in terms of revenues and distributional effects) of tax reforms? What are the linkages between revenue performance and social expenditure? What are the effects of the fiscal system on social outcomes such as equality and social development?

To test the hypothesis and answer the research questions, this paper will provide a historical analysis of four different periods: The late Somoza Dictatorship (1972-1979), the Sandinista Revolution (1980-1989), the Neoliberal period (1990-2006), and the Ortega administration (2007-present). These sections will provide historical trends of tax collection and social spending, identify the government priorities and its justifications, and lay out the most relevant tax reforms. Each section will begin with a brief historical overview, focusing on the economic and political variables that influenced tax revenue collection and social spending. The objectives of the fiscal system and of the most prominent reforms will then be reviewed, as will the revenue collection trends, followed by an analysis of government social expenditures. These latter points will be analysed under the framework that will focus on bargaining and contestation and state-citizen relationship in the context of tax reforms.[6]

Methodology

This paper is based on the review and analysis of primary and secondary sources on the tax system and reforms in Nicaragua. The first steps were to review the literature and reports on the performance of the most relevant recent tax reforms: the Tax and Trade Justice Law, the Tax Equity Law, and the Tax Concertation Law.

Historical information on tax reforms and their outcomes were found in the Central Bank of Nicaragua and the Ministry of Finance. However, data for the year 1979 has been completely lost due to the period of war that prevented record keeping. There are few statistics and data about the tax system and disaggregated social spending from the 1970s to the 1980s. The data used for the purpose of this paper from the year 1972 to 1998 was extracted from the online publication of the Central Bank of Nicaragua, “Fifty Years of Macroeconomic Statistics: 1960-2009”. The data from 1999 to present was taken from the Ministry of Finance in the different Annual Budget Performance Reports of the Republic, which are available online.

Three in-depth interviews were conducted with leading fiscal policy experts in Nicaragua, as well as crucial stakeholders that have actively participated in the formulation, mediation, and evaluation of the most recent tax reform, the Tax Concertation Law. These interviews shed light on key issues such as civil society’s participation in the negotiating process and elaboration of tax laws, the guiding principles that the different tax reforms should be ruled by, the inequalities being generated by a regressive tax system, and the winners and losers from the different tax reforms, among others.

Statistical data from the Ministry of Finance was used to construct the different figures and tables that were elaborated in order to clearly portray the different trends on tax revenue collection, social expenditures, and highlight the weaknesses of the current tax system. For the collection of this data, government budget reports, annual expenditure reports, and macroeconomic indicators were used. Data on social expenditures was disaggregated by sectors starting from the year 2004 to the present, in order to focus the

[6] Institutional development will also be examined but to a lesser degree.

analysis on the most recent tax legislations. Data on social expenditures prior to 2004 will not be disaggregated.

It is worth mentioning that when collecting the data, the author encountered discrepancies between data reported by the Ministry of Finance and that of the Central Bank of Nicaragua. In these cases the data selected was the latest published data, making the assumption that the incongruities would have been resolved in the newer versions.

Conceptual Framework and Definition of Key Terms

This section lays out the conceptual framework through which the connections between resource mobilization through tax systems and social development are examined. It assumes that social development is primarily an outcome of policies implemented by public institutions, both in terms of legislation and regulation, and regarding delivery of public goods and social services. Furthermore, it will assess the ways in which power relations govern the outcome of tax systems, in terms of distributional and social development impacts.

The politics of domestic resource mobilization as conceptualized by UNRISD has three major themes, which will guide the analysis of the tax system in Nicaragua (UNRISD 2015, 2012). The themes are the processes of bargaining and contestation, relationships between key players and how they change in the process of resource mobilization, and institutional development. The first theme will feature more prominently in this paper, since it is pivotal for determining the tax system and the interconnectedness between key players in Nicaragua. The second theme, relationships between key players, will also feature prominently. This theme scrutinizes the state-citizen relationship as well as the donor-state relationship, which are central to policy making and demands for improved public services.

The tax system constitutes a direct linkage between the society and the state. It represents a direct monetary contribution from society, which is administered by the state, with the purpose of improving the overall wellbeing of its citizens. This makes it an extremely effective way of mobilizing domestic resources for social development. Revenue from taxation provides governments with the funds needed to invest in development, relieve poverty and deliver public services directed toward the physical and social infrastructure required to enhance long-term growth (OECD 2013).

Tax system design usually follows a set of principles: two important ones are the benefit principle and the payment capacity principle. The benefit principle considers taxes as the price individuals and enterprises must pay for the use of public goods. The second principle determines how much each individual pays for these services. It distinguishes between horizontal equity and vertical equity. Horizontal equity establishes that those individuals with an identical capacity of payment must pay a similar amount of taxes, in other words, bear a similar tax burden. Vertical equity on the other hand establishes that those individuals with higher capacity of payment must bear a relatively higher tax burden than those with lower income levels (Acevedo 2011b), which can also be understood as progressivity in tax systems. Schneider mentions that the tax system also has a dimension of universality that must not be overlooked (2014: 13). The tax universality is the degree to which the tax law is applied in a universal manner (for example across sectors and jurisdictions), regardless of the way in which wealth is created, stored, or transferred. In this sense, the universality of the tax system is a

coordination issue, since the different interest groups must commit to not seek special agreements and particular benefits in the fiscal system (Schneider 2014: 14). Tax universality is the ideal way to ensure that the principle of horizontality is met.

When analyzing tax revenue, it is important to make a clear distinction between direct and indirect taxes. These concepts are pivotal for determining the progressivity of the system. The basis for progressivity is not in higher revenue collection, but in establishing a fair system that will help redistribute income and wealth in a more equal manner, in such a way that higher income earners pay proportionately higher taxes than lower income earners. According to Báez and Báez (2001: 45), indirect taxes are those that are applied to the consumption of goods and are usually the fastest and easiest to collect, whereas direct taxes are levied on income and capital and are usually harder to collect. The indirect taxes include sales taxes (on imports and domestic goods and services), value added taxes (VAT)[7], duty tariffs on imports, excise taxes[8], among others. Direct taxes include business income tax, property tax and personal income tax. It is through the design of these taxes that progressivity can be established. Progressivity is based on the idea that marginal utility of income diminishes with higher levels of wealth. Taking an extra dollar from a wealthy person has a much smaller impact on his/her wellbeing than taking it from a less wealthy person (Schneider 2014: 14-15). Progressive taxation takes place when most of the tax revenue collected comes from direct taxes, abiding by the concept of vertical equity, in which the higher income earners pay more taxes as a share of their income. Progressivity measured in terms of tax collection outcomes increases when the share of direct taxes increases vis-à-vis the share of indirect taxes, which can be either the result of tax reforms or changes in the tax base.

There are two different ways to design tax systems: a global taxation system and a schedular system. A global system of taxation is an algebraic sum of all sources of income and taxed at a progressive rate, following the principles of horizontality and verticality. A system is schedular when it taxes different sources of income, such as economic activities or transactions without taking into account the person who is performing them. The main features of the schedular income tax system are:

- Each tax category or income category is treated differently and specifically
- There are no personal deductions considered
- Tax exempt minimum thresholds do not apply, it will always be a partial manifestation of the taxpayers ability to pay
- Assets or income not defined by law are not taxable
- It differentiates tax levies from different assets depending on their origin

In addition to the redistributive effects of the tax system itself, the relationship between taxation and social development is established mainly through social expenditures. However, the relationship between revenue policy and expenditure policy is not linear, because resource mobilization does not automatically translate into higher social expenditure. Furthermore, the delivery of public services is a result of both the State's fiscal capacity and decisions about resource allocation, making this connection dependent on government priorities as well as on the availability of alternative sources of funding such as external aid or private transfers. In other words, if a government prioritizes social expenditures, a higher percentage of its revenue will be directed towards social programmes, creating potentially (if resources are spent efficiently and

[7] Value Added Taxes (VAT): Taxes paid when purchases are made on specific goods (IRS 2014). It includes goods such as Non-alcoholic carbonated drinks, beer, rums and liquors.

[8] Excise Taxes are taxes paid when purchases are made on a specific good, such as gasoline.

social programmes are implemented effectively) higher levels of social development. However, if a government does not prioritize social development, even when revenue collection increases, social expenditures might remain stagnant.

Historical Trends of Tax Collection Vis À Vis Social Expenditures in Nicaragua

This section will examine historical trends of domestic resource mobilization for social development in Nicaragua. The analysis will focus on the themes of bargaining and contestation, as well as state-citizen relationships through the formulation of tax legislation throughout the different historical periods and applied to tax revenue collection and social expenditure allocations in Nicaragua. It will be divided into four time periods: the last period of the Somoza dictatorship (1972-1979), the Sandinista Revolution (1980-1989), the Neoliberal period (1990-2006)[9] and the Ortega administration (2007-present). All four sub-sections provide a background of the most significant events in the history of Nicaragua, focusing primarily on tax reforms and their effects on social development.

The Late Somoza Dictatorship (1972-1979)

The Somozas first came to office in 1937 with Anastasio Somoza Garcia. The executive power was later transferred to both his sons, Luis Somoza Debayle (1956-1967) and Anastasio Somoza Debayle (1967-1979), who ruled as military dictators, just as his predecessor before them. The rule of the Somoza dynasty came to an end with a liberation war that took place in the latter half of the decade (1974-1979), finally ousting Anastasio Somoza Debayle who fled to Paraguay in 1979. The Sandinista Revolution created the Government Board for National Reconstruction (JGRN for its acronym in Spanish) as a temporary new government led by revolutionary leaders and business and civil society representatives.

In general, the period from 1972 to 1979 was characterized by accelerated economic growth[10] compared to previous periods. However, the period was also characterized by marked economic inequalities and wealth concentration, with the elites gaining more and more power and enjoying the majority of economic benefits. Commodity production such as cotton, coffee, sugar cane, and livestock led the economic progress (Kinloch 2006: 284-287). However, by the end of the 1970s, only 1,946 producers owned 36 percent of cultivated land in the nation and five percent of the richest families in society received 28 percent of total national income. The immense wealth concentration that took place in this period is further illustrated by the Somoza family fortune, which rose above USD 300,000,000, while half of the farmer population had no land and very little to subsist (Kinloch 2006: 283). Even after the earthquake of 1972 that left the capital Managua in ruins, international aid was captured by the Somoza family and their allies, mostly members of the National Guard (Merrill 1993), and failed to cater for the needs of the country's poor.

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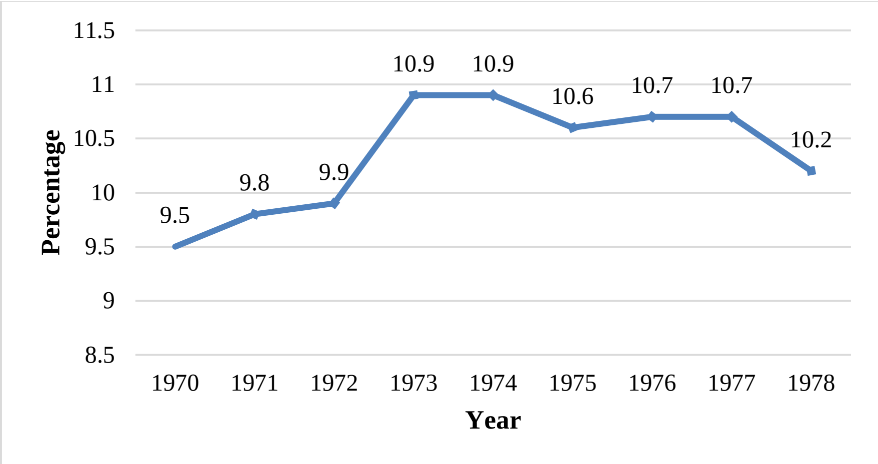
9 The subsection on neoliberal policies will be analysed in greater depth due to better data availability and the relevance of the period due to its influence in the overall tax framework legislation implemented in that period. Furthermore, the balance of power was not concentrated on a single actor as during the Somoza Dictatorship, but on a multiplicity of actors, giving way to new major tax reforms for each presidential period: Violeta Chamorro (1990-1996) – Reform to the VAT (Decree No. 52-92); Arnoldo Aleman (1997-2001) – Tax and Trade Justice Law (Law No. 257); and Enrique Bolaños (2002-2007) – Tax Equity Law (Law No. 453).

10 On average, economic growth from 1972-1977 was of 6.03 percent (BCN 2016b. The last 2 years of the period underwent economic contraction mainly due to the Sandinista insurrection (BCN 2012b).

In terms of the mobilization of domestic resources through taxation, there were but a few reforms instituted during the period that focused on revenue collection. The analysis of the tax reforms in this section will be based on three particular years: 1973, 1974, and 1978. These years are considered key in terms of tax legislation by the Central Bank (BCN 2011). The reforms that were implemented responded to a prolific foreign trade context, in which indirect taxes represented the most viable way of tax revenue collection. These taxes did not require a lot of capacity in terms of tax administration, given that the amount of tax to be paid is calculated from the sale of goods and paid directly to the Ministry of Finance.

Figure 1. Tax Revenue as a Percentage of GDP, Current Prices (1970-1978)



Source: Author, based on Acevedo 2011a.

The most prominent reforms of the period were those concerned with indirect taxes, specifically with Export Tax,[11] SCT,[12] and VAT.[13] As can be seen from Figure 1, tax revenue collection in terms of GDP remained fairly constant in the 1970s. There was an increase in revenue in 1973, which was the result of the reforms that affected the indirect taxes mentioned above. Throughout the period, most of the tax revenue that was collected came from indirect taxes, as can be seen from Figure 2. This demonstrates that any increase or decline in tax revenue came from the sales of goods and foreign trade, which are the economic activities for which export taxes, SCT and VAT are created. The rationale behind the implementation of tax reforms during this period was not design for progressivity or equality, but primordially for increased revenue collection. The last tax reform of the decade was introduced in 1978. It came in response to the deterioration of national income and a rising fiscal deficit reaching over USD 40 billion (Morley 1994), which had been increasing due to the political instability associated with the insurgence against the Somoza dictatorship and the eventual break out of the armed conflict. Until 1977, the government was able to finance the deficit with external sources, mainly from the United States. However, in 1978 the external financing sources decreased significantly when US President Carter came into office. The politically motivated change in this relationship between Nicaragua and one of its key donors resulted in domestic policy changes. It forced the Somoza government to finance the deficit with internal revenue sources, paving the way for new tax reforms. In response, three new reforms to the VAT and SCT were implemented throughout the year, as well

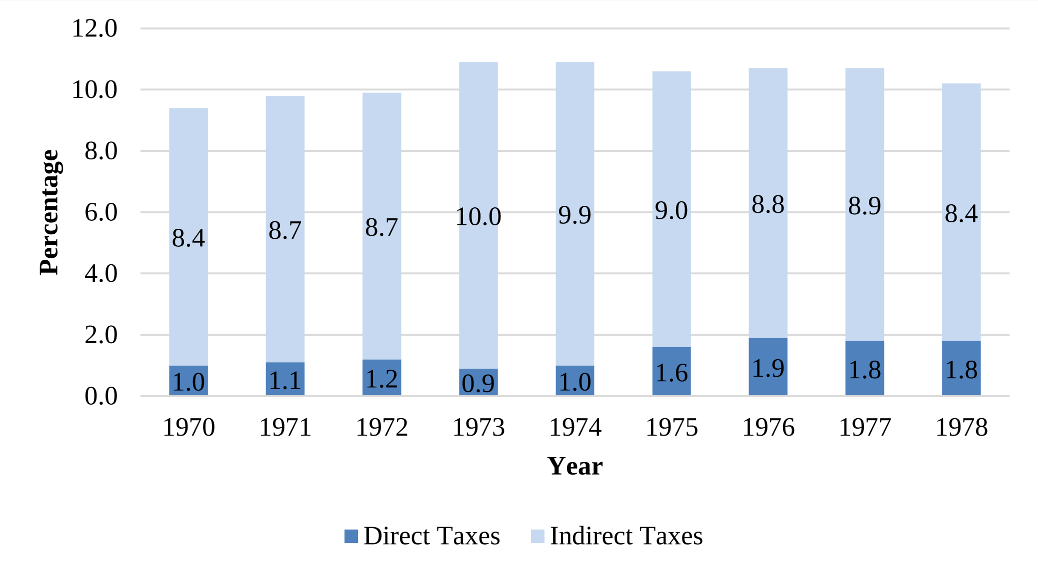
[11] Decree No. 85. Printed in La Gaceta Serial No. 1 on January 8th 1973.

[12] Decree No. 54. Printed in La Gaceta Serial No. 250 on November 8th 1973; Decree No. 663. Printed in La Gaceta Serial No. 262 on November 16th 1974; Decree No. 683. Printed in La Gaceta Serial No. 51 on March 3rd 1978; Decree No. 713. Printed in La Gaceta Serial No. 183 on August 16th 1978; Decree No. 31. Printed in La Gaceta Serial No. 183 on August 16th 1978.

[13] Decree No. 663. Printed in La Gaceta Serial No. 262 on November 16th 1974; Decree No. 683. Printed in La Gaceta Serial No. 51 on March 3rd 1978.

as a reform to the income tax.[14] Results of these reforms are difficult to quantify, given that there are no data for the year 1979 due to the political turmoil in that year, and the transitory nature of the reforms due to the subsequent regime change.

Figure 2. Direct and Indirect Taxes as a Percentage of GDP, Current Prices (1970-1978)



Source: Author, based on Acevedo 2011a.

Regarding social development indicators, this period of instability and political turmoil was characterized by major setbacks and further increases in inequality. Even though no official data can be found on actual social spending levels for each specific year of the decade, World Bank data show that between 1970-1975, education spending was equivalent to 2.8 percent of GDP (World Bank 2000: 33), whereas in the following decade, education expenses increased to 5.4 percent by 1985. This low level of expenditures in the 1970s reflects Somoza's disregard for educating Nicaraguan society. Indeed, illiteracy served as a means to ensure the passivity of the poor and to provide Nicaraguan elites with a large pool of unskilled low-paid labour that was crucial to the agro-export economy on which they depended (Zaremba 1992). Consequently, by the end of the decade, half of the Nicaraguan population was largely illiterate (Kinloch 2006: 298).

In the case of healthcare, during the first half of the decade expenditures amounted to 1.6 percent of GDP, again considerably lower than in 1985, when the levels of health expenditures rose to 4.9 percent. During the 1970s, according to Zaremba, institutionalized healthcare was virtually absent in most areas of the country (Zaremba 1992). By the end of the decade, 10 percent of the population consumed 90 percent of all the healthcare resources (Sanders et al. 2000). Furthermore, more than half of all the children in Nicaragua were malnourished (Sanders et al. 2000).

To add to the lack of investment in education and healthcare, the state-citizen relationship towards the end of the decade had deteriorated mainly due to lack of democracy, prevailing economic inequalities, and military repression (Merrill 1993). These were some of the main causes for the popular insurrection, led by the Sandinista

[14] Decree No. 683. Printed in La Gaceta Serial No. 51 on March 3rd 1978; Decree No. 713. Printed in La Gaceta Serial No. 183 on 16 August 1978; Decree No. 31. Printed in La Gaceta Serial No. 183 on 16 August 1978. Decree No. 740. Printed in La Gaceta Serial No. 254 on 10 November 1978.

National Liberation Front (FSLN) that eventually brought the Somoza dynasty to an end and prompted the beginning of the Sandinistas' first period in office.

The Sandinista Revolutionary Period (1980-1989)

Trends in Taxation

The Sandinistas took over a country that was devastated by the liberation war, natural disasters such as the earthquake in 1972, and by the exclusionary policies of the Somoza dictatorship. A Government Board for National Reconstruction (JGRN) was appointed to install an effective democratic regime, a justice system to promote political and social justice, and to guarantee the full enjoyment of human rights for all citizens (Kinloch 2006: 314). The JGRN proposed the creation of a mixed economy and a political system, which would guarantee the displacement of the privileged bourgeois elites from power and leave the working class in charge of the state (Kinloch 2006: 315). This change in the state-citizen relationship translated also into attempts to make the tax system more progressive by reforming direct taxes that would help income redistribution. However, several factors undermined the success of these reforms over the coming years, in particular a) a new armed conflict that broke out between Sandinistas and Contras since the beginning of the 1980s, b) rising economic instability mainly caused by an US embargo imposed in 1985, and c) an inflationary episode in the second half of the 1980s. As a result, tax revenue declined over the period, from a high 32.4 percent of GDP in 1984, to a low 19.4 percent by 1988, although in the second half of the decade the decline was mainly due to the Oliveira-Tanzi effect,[15] which eroded real value of tax revenue collected.

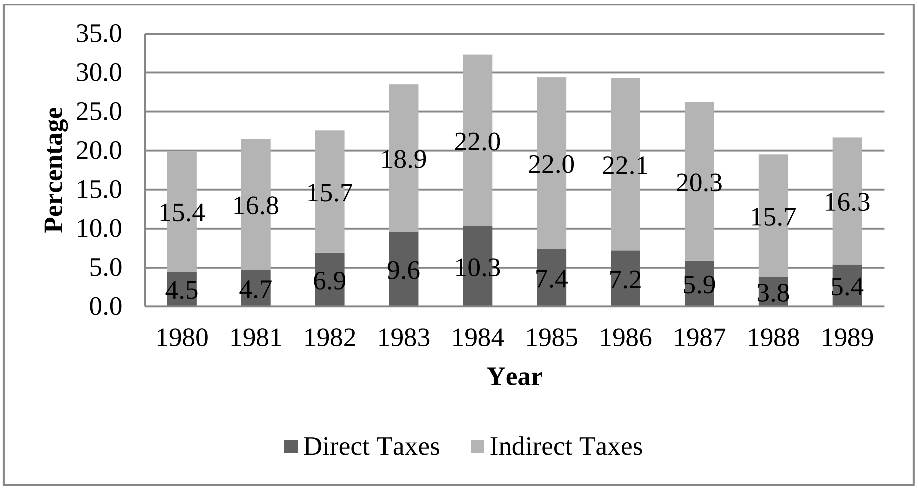
Throughout the decade, the most important tax reforms occurred in the years 1982, 1983, 1984 and 1987 (BCN 2012b). In those four years, 44 different tax policies came into effect.[16] While the most prominent reforms undertaken during this period aimed to add progressivity to the system, revenue collection came mostly through indirect taxes such as the SCT and VAT. The Sandinista government intended to increase the progressivity by increasing the weight that direct taxes would have in total revenue collection. For this purpose, two new taxes were created which tend to fall primarily on higher income groups: property tax and capital gains tax. The redistributive effect of both taxes were meant to be increased further through establishment of a minimum income that would be exempted from the taxes. As a result of these reforms revenue collection increased during the first half of the decade, while the tax burden fell more heavily on the wealthier classes. Other reforms to the income tax in 1983 and 1984 focused on taxing income from dividends and allowances that corporations provide to their highest paid employees, and created a system that taxed contributors based on the totality of their income, regardless of the source of income.[17] It was expected that this would not only comply with the principles of horizontal and vertical equity, but it would also lead to higher tax revenue.

[15] The Oliveira-Tanzi effect is the erosion of the real value of tax revenues that occurs during episodes of high inflation due to the lag between the time tax liabilities are accrued and actual payment is made.

[16] Refer to the Annex, Table 1. Source: Ayales 1991.

[17] Law No. 1249. Printed in La Gaceta Serial No. 106 on 11 May 1983.

Figure 3. Direct and Indirect Taxes as Percentage of GDP, Current Prices (1980-1989)



Source: Author, based on Acevedo 2011a.

As can be seen from Figure 3, the revenue from direct taxes as percentage of GDP increased and reached the highest point in 1984 with 10.3 percent of GDP, although the overall system remained regressive with indirect taxes reaching 22 percent of GDP. Total tax take stood at 32.4 percent of GDP, which reflected an impressive increase compared to the previous government and compares favourably with regional neighbours and other developing countries of similar income level. The increase in inflation rates caused by political and economic instability that led the government to finance the fiscal deficit by issuing money (Acevedo 2011a), eroded tax collection in the second half of the decade (Figure 4). Table 1 shows the evolution of the inflation rate, reaching levels of hyperinflation from 1986 onwards, illustrating the extreme macroeconomic instability during this period.

Table 1. Main Macroeconomic Indicators (1980-1990)

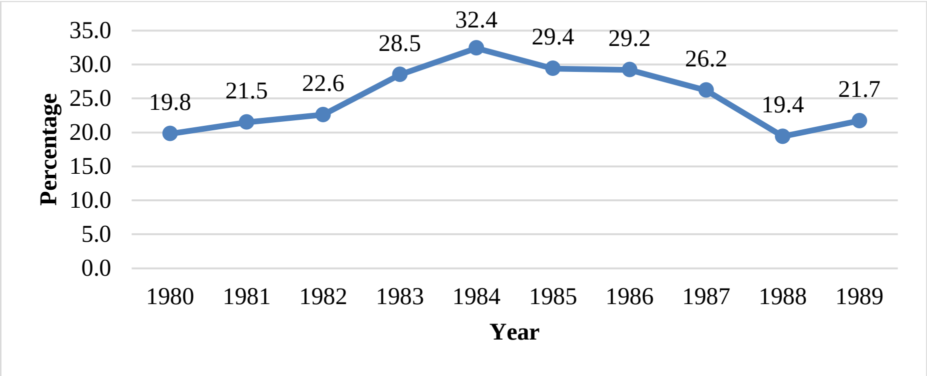
Concepts	1982	1983	1984	1985	1986	1987	1988	1989
Economic activity								
Real GDP growth *(%)*	(0.8)	4.6	(1.6)	(4.1)	(1.0)	(0.7)	(12.4)	(1.7)
GDP per cápita *(US$)*	793.8	712.0	767.7	676.5	580.8	575.3	366.0	252.3
GDP per cápita growth *(%)*	8.3	(10.3)	7.8	(11.9)	(14.1)	(1.0)	(36.4)	(31.1)
Prices and exchange rate								
National annual inflation *(CPI 2006=100)*	24.8	31.1	35.4	219.5	747.4	1,347.2	33,547.9	1,689.1
Average exchange rate *(C$ x US$)*	10.0	10.0	10.0	26.1	66.4	70.0	190.9	15,654.6
Monetary sector								
Monetary base *(percentage growth)*	34.6	79.3	87.6	185.9	234.7	609.6	(88.6)	1,781.5
Net international reserve balance *(millions of US$)*	(185.1)	(202.9)	(291.5)	(434.6)	(637.7)	(862.1)	(853.1)	(921.7)
Non-financial public sector *(as % GDP)*								
Balance of NFPS *(before grants)*	(12.2)	(21.6)	(22.1)	(23.0)	(15.8)	(17.6)	(27.7)	(8.1)
Balance of NFPS *(after grants)*	(11.2)	(19.7)	(21.4)	(22.4)	(14.3)	(17.0)	(27.1)	(4.6)
External financing NFPS	2.2	5.0	2.6	0.4	(0.0)	(0.1)	2.4	4.8

Internal financing NFPS	9.0	14.7	18.8	22.0	14.4	17.1	24.7	(0.2)
External sector								
Current account *(as % GDP)*	(17.1)	(19.2)	(21.5)	(29.0)	(27.0)	(29.9)	(43.7)	(36.2)
External public debt								
External public debt *(millions of US$)*	3,032.5	3,989.6	4,649.9	5,522.3	6,464.2	8,044.5	8,622.4	9,597.1
External debt service	45.0	36.9	34.1	41.1	39.7	38.7	40.9	19.9

Source: Author, based on BCN 2012b.

In terms of overall revenue collection, indirect taxes contributed the most to tax revenue, mainly because indirect taxes are accrued and paid at the same time any transaction is made, leaving less room for monetary erosion.

Figure 4. Tax Revenue as a Percentage of GDP, Current Prices (1980-1989)



Source: Author, based on Acevedo 2011a.

Trends in Social Spending

One of the key goals of the Sandinista government was to improve social spending after decades of neglect of the previous authoritarian governments. However, the revenue collected during the period through taxation was not sufficient, and it was therefore necessary to complement tax money with donations and aid in order to implement social programmes, such as the National Literacy Crusade. This reduced the illiteracy rate from 50 percent to 12 percent in only five months, due to the participation of 60’000 Nicaraguan youth volunteers (UNESCO 2007, RJC 2012). [18]

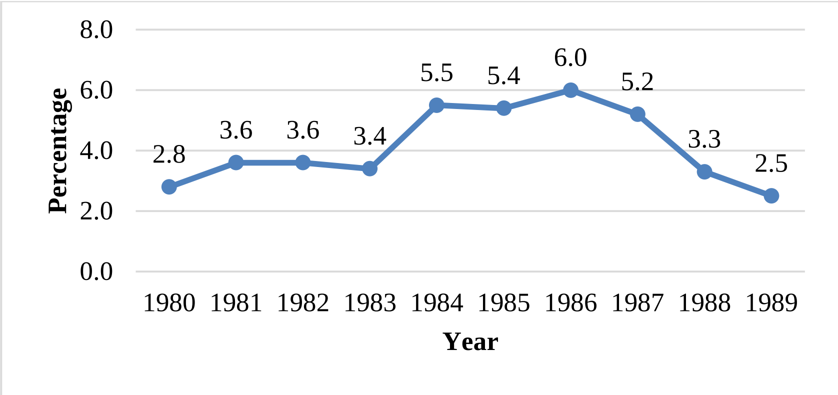
The average fiscal income for the decade was about USD 2,110.8 million, of which 87.5 percent came from tax revenue,[19] the remaining revenue coming from capital revenues, state enterprises, non-tax government revenue, and transfers. The income generated did not offset the negative balance of payments for the decade, which averaged 211.7 million (BCN 2016c). The high levels of expenditure that went into the defense budget in the context of the Sandinista-Contra war also put constraints on social spending. According to the Central Bank of Nicaragua, in 1987, the year with the highest revenue collected from the decade, 41 percent of total government expenses went into the defense budget (BCN 2012b). In contrast, social expenses from 1982 to 1989 reached levels between 18 and 24 percent of total expenses (Arana et al. 1999).

[18] It took place from March to August of 1980 under the direction of the Jesuit priest Fernando Cardenal. It mobilized around 60,000 youth, mostly high school students, to attend rural areas of the country. An additional 35,000 people participated in the campaign, alphabetizing in fabrics and slums in the cities.

[19] Calculation elaborated by author for the purpose of this paper. Source: BCN 2016c

Whereas education spending increased until 1986, it decreased afterwards, reflecting the increasing macroeconomic instability and military spending during the final episodes of the Contra-Sandinista armed conflict. However, the expenditure in education of the Sandinista period clearly exceeded that of the Somoza period, during which education was not a priority (Figure 5).

Figure 5. Education Expenses as a Percentage of GDP, Current Prices (1980-1989)



Source: Author, based on Acevedo 2011a.

Significant improvements in healthcare and other key social areas were not directly financed by tax revenue. The social programmes that were implemented during this period were mostly financed through foreign aid (Interview with Theódulo Báez Cortés, November 2014; Delmelle and Mendoza forthcoming). This was exemplified by the construction of five regional hospitals and 300 health centres, which allowed for a threefold increase in the number of medical consultations and a reduction in the child mortality rate from 113 to 64 per 1,000 live births (Kinloch 2006: 318).

The Neoliberal Period (1990-2006)

Between 1990 and 2006, Nicaragua was governed by three different neoliberal governments, whose presidents were: Violeta Barrios de Chamorro (1990–1996), Arnoldo Aleman (1997–2001), and Enrique Bolaños (2002–2007). When Chamorro assumed the presidency, Nicaragua was under the worst hyperinflation episode (1985-1992) that has ever afflicted the country, a result of a decade of civil war and economic setbacks. Chamorro was successful in stabilizing the currency and putting an end to a period of civil unrest, setting the stage for new tax reforms that were adopted by the following governments of Aleman and Bolaños. However, structural adjustment policies, in line with the Washington Consensus,[20] brought economic stability at a high social cost: extensive layoffs of public employees, and reduction of state expenditures, in particular of the social budget (Kinloch 2006: 347). In the period between 1990 and 1994, Nicaragua was the first aid recipient in the world, which reached USD 182.00 annually per inhabitant. However, by 1994, 96 percent of aid received had to be channeled directly to servicing external debt, which amounted to USD 11,695 million (BCN 2012b). Furthermore, a lack of strong governmental institutions gave way to corruption, which was exacerbated by lack of transparency in the use of public funds, discretionality in institutional or specific powers of officials, as well as weak regulation and control mechanisms in the management of government assets and funds.

[20] The Center for International Development at Harvard University (2003) defines the Washington Consensus, a term coined by John Williamson, to refer to the lowest common denominator of policy advice being addressed by the Washington-based institutions to Latin American countries as of 1989. It advocates for fiscal discipline, tax reforms, trade liberalization, and privatization, among others. See also Williamson 1990.

Trends in Taxation

Among the most significant policies and developments that took place during this period was the privatization of state enterprises and public services, an increase in foreign debt, corruption, and unemployment, among others (Kinloch 2006: 347-252). In addition to increased mobilization of foreign credit, two main tax reforms were implemented in the period that responded to different interests and power dynamics: the Tax and Trade Justice Law[21] (1997) and the Fiscal Equity Law[22] (2003).[23] Even though these were not the only tax legislations that were approved during the period, they were the most significant as they came to supersede any previous tax law at the time and each modified several additional laws.[24] Furthermore, specific revenue collection trends and their causes will be analysed to a deeper extent focusing only on the Fiscal Equity Law, in order to provide a basis for comparison with the current tax law that will be covered in the following section.

The Tax and Trade Justice reform adopted during Aleman's presidency was oriented towards the elimination of import monopolies and to reduce the protectionism of industrial oligopolies. Additionally, the reform reduced tax burdens for workers, but eliminated exonerations that favoured NGOs (Envío 1998). In this sense, the reform did attempt to create more equality and as can be seen from Figure 7: since the reform was implemented there was a small increase in progressivity from 1997 to 2003, which was when the Fiscal Equity Law came into effect. Furthermore, economist Nestor Avendaño mentions that this particular reform was a strategic move from Aleman to reduce the influence of the conservative elites that held economic power, and, in turn, to benefit a group of producers that would begin forming his support base to help him remain in office (Interview with Nestor Avendaño, November 2014).[25] The tax law directly affected the oligarchic capital and the newly formed Sandinista capital, benefiting instead the constituency of the liberal party (Envío 1997). In this particular case, the power dynamics responded to political interest by the party in power, but not directly to higher tax revenue collection to fund social expenditures.

In contrast, the Tax Equity Law that came into effect during the Bolaños administration in 2003 focused on eliminating negative distortions and biases in the fiscal system, shifting towards a more equitable tax system, increasing the tax base, and developing tax mechanisms that would stimulate exports (Doherty et al. 2003). This law came into effect not as a result of national power dynamics, but as part of the negotiations between Nicaragua and the International Monetary Fund (IMF), in the context of the Poverty Reduction and Growth Facility (PRGF) programme that intended to strengthen Nicaragua's fiscal situation and support a path for improving its primary balance (Gasparini et al. 2006). It is important to note that the negotiations between Nicaragua and the IMF have been ongoing since 1991, when Nicaragua's infrastructure, economy, and human capital were devastated by the war of the previous decade. In 2002, due to a series of shocks to the national economy, the state was under increasing pressure to reduce its fiscal deficit (Acevedo 2008), which set the stage for a bargaining process and eventual signing of an agreement with the IMF. The reform that was instituted after the PRGF programme introduced a more progressive legislation: no new indirect taxes were

[21] Law No. 257 published in La Gaceta No. 106–Official Journal of the Nicaraguan Republic.

[22] Law No. 453 published in La Gaceta No. 82–Official Journal of the Nicaraguan Republic.

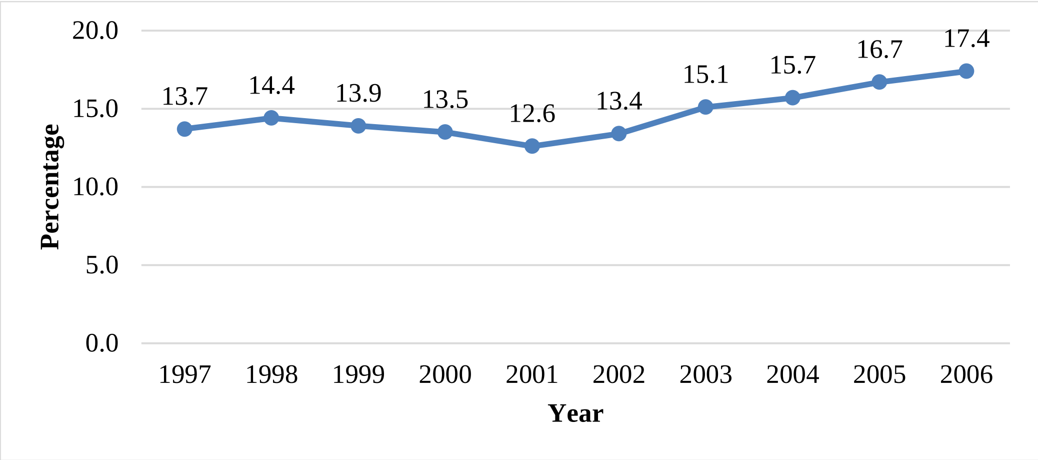
[23] The latter will be analysed until 2006, which marks the end of the neoliberal period; the analysis past 2006 will be examined in the following section The Ortega Administration period goes from 2007 to present.

[24] The Tax and Trade Justice law modified an additional 33 laws once it was implemented, while the Fiscal Equity Law was introduced along with 3 other complimentary and transcendental laws: Budget System Law, Law on Fiscal Responsibility, and the Tax Code (Envío 2003).

[25] This was demonstrated by the fact that the Tax and Trade Justice Law increased tax burdens to the industrial sector controlled by conservative economic elites, while lowering import taxes for the agricultural producers (Avendaño 2014).

created and three additional direct taxes were introduced. These included taxes on luxury goods, to more than 800 products, taxes on interests on bank deposits, and taxes on business assets. In addition, it eliminated exonerations, reduced the income tax of workers, did not include new taxes for low-income contributors, and exonerated from VAT 53 products from of the basic consumption basket (Envío 2003).

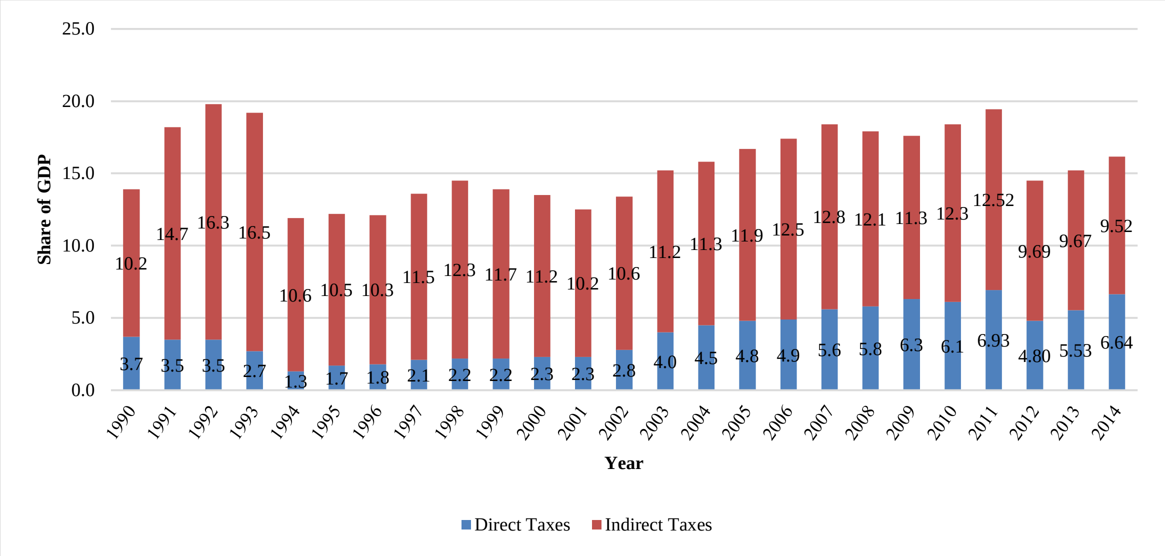
Figure 6. Tax Revenue as a Percentage of GDP, Current Prices (1997-2006)



Source: Author, based on Acevedo 2011a.

As can be seen from Figure 6, the Tax and Trade Justice Law did not generate as much revenue as the later Tax Equity Law, and it compared very weakly with the peaks of revenue collection achieved under the Sandinista government in the middle of the 1980s, which had exceeded 30 percent in 1984. Fall in revenue collection in real terms took place from 1999 to 2001, and was caused by a fall in coffee prices, reduction in different tax rates, a reduction in the sale of cigarettes which directly affected the SCT, and a reduction in the rate of the income tax from 30 percent to 25, a rate that is still valid today (GEE 2000). The international fall in coffee prices affected the performance of revenue collection in the next couple of years. This is mainly due to the fact that the majority of the taxes collected during this period were through indirect taxes, which are directly linked to the sales of goods and services. A fall in prices of certain commodities, such as coffee, would automatically translate into lower revenue generated by indirect taxes such as the SCT and VAT. Figure 7 shows the distribution of taxes in direct and indirect taxes for the period.

Figure 7. Direct and Indirect Taxes as a Percentage of GDP, Current Prices (1990-2010)



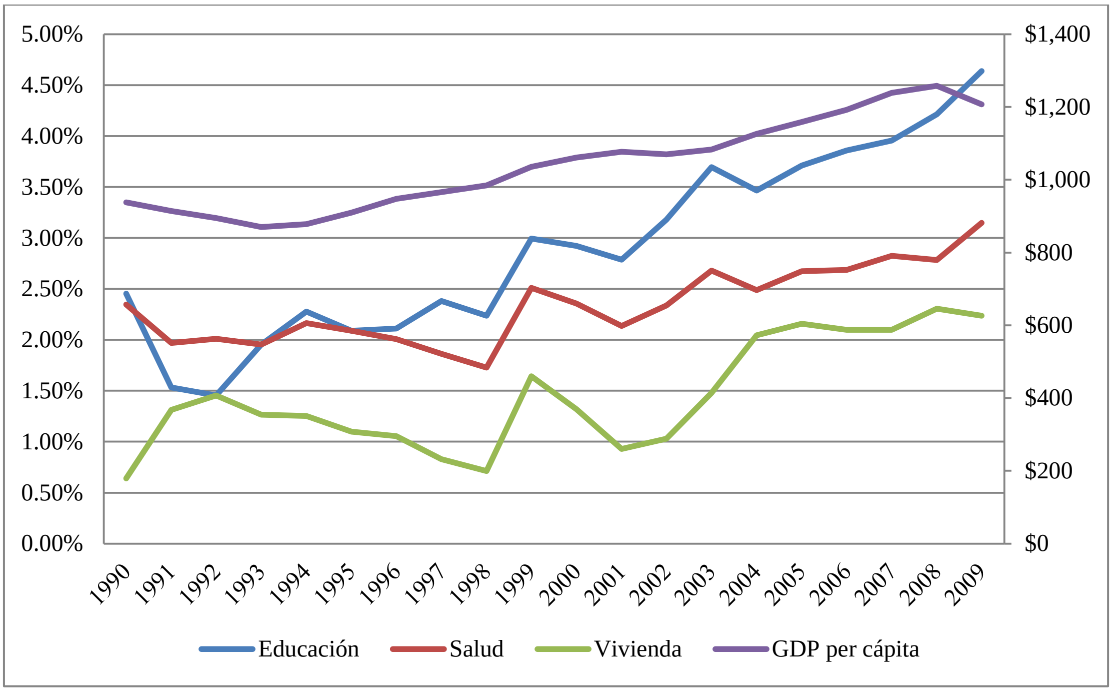
Source: Author, based on Acevedo 2011a and BCN 2012a and 2015.

Trends in Social Spending

In order to analyse the direct effects that these two tax legislations had on social expenditures, such as education and healthcare, the analysis will include data from 1997 to 2006. When comparing Figure 6 with Figure 8, we can see relatively similar trends in the two graphs before and after 2001. The increase in social expenditures that can be seen in 1999 is mainly due to the emergency response and reconstruction from Hurricane Mitch (Lopez-Calva 2004). In this year, even when tax collection was declining, social expenses clearly went up. In 2004 the opposite happened, when tax revenue collection went up, social expenses showed a decline. The decline was a reaction to an increase in the fiscal deficit caused by the issuing of illegal Negotiable Certificates of Investments (CENIS). These CENIS were issued to increase the foreign reserves of the Central Bank of Nicaragua, as well as to banks that were acquiring other bankrupt financial institutions. The certificates issued represented 95 percent of the total reserves, and meant that the internal debt servicing would increase significantly from 2003 to 2004. Therefore, there was a reduction in other expenses, which affected health and education (Figure 8), with a small decline in public expenditures for that year. The average ratio between social expenditure and total expenditure[26] for the period equalled 42.1[27] with a standard deviation[28] of 5.25 million.[29] This means that on average, for every USD 1.00 spent, 42.1 cents are spent on social expenditures, and this figure varies little from year to year.

[26] Total expenses do not include amortization of external and internal debt. When amortization is included, the proportion between social expenses and total expenses will be lower.
[27] Calculation elaborated by the author for the purpose of this paper. Source: BCN 2007; BCN 2007; BCN 2014.
[28] Standard deviation is a measure of dispersion from the data. It tells you how closely the values are clustered around the mean. Therefore, this means that on average, we can find variation as high or as low as 5.25 million dollars from the mean of 41.1 percent along the data set.
[29] Calculation elaborated by the author for the purpose of this paper. Source: BCN 2007; BCN 2007; BCN 2014.

Figure 8. Education Expenses, Healthcare Expenses and Housing Expenses as a Percentage of GDP and GDP per capita, Constant Prices (1990-2009)



Source: Demelle and Mendoza 2017, based on Acevedo 2011a.

In healthcare and education, the ratio between the yearly expense relative to total expenditures of the same years was 18.78 percent and 14.23 percent respectively.[30] The average ratio of education expenses over GDP for the nine-year period was 3.97 percent with a standard deviation of 0.57.[31] In healthcare, the average ratio equaled 3.0 percent for the same period, and with a standard deviation of 0.41[32], whereas the investment in education alone should be of at least 7 percent of GDP, a level achieved under the Sandinista government in 1985.[33] The stagnation in social expenditures during the neoliberal period was due to limited fiscal space due to high debt servicing, both external (in the decade of the 1990's) and internal (2002-2006).

During this period, political drivers for the most significant tax reforms were both internal and external, national political interests and requirements by the International Financial Institutions (IFI) in order to regain macroeconomic stability, reduce fiscal deficits and secure implementation of poverty reduction programmes. The implementation of these neoliberal policies created instability in the workforce, especially the reduction of state employment and public sector workers salaries. These ideas and policies were believed to work universally in order for a country to reach economic development; therefore, their approach and implementation were not open for dialogue. However, due to a strong Sandinista opposition, the political context was not favourable for the implementation of these policies. There were processes of contestation and dialogue between Sandinista organizations, the government in office, and the IFIs, in which the opposition was able to preserve spaces of political and economic influence as well as partial concessions to grant the political viability to this restructuring process (Acevedo 2008).

30 Calculation elaborated by the author for the purpose of this paper. Source: BCN 2007; BCN 2007; BCN 2014.
31 Calculation elaborated by the author for the purpose of this paper. Source: BCN 2007; BCN 2007; BCN 2014.
32 Calculation elaborated by the author for the purpose of this paper. Source: BCN 2007; BCN 2007; BCN 2014.
33 According to education specialist Josefina Vijil, in order to reduce the deficiencies in the educational system, an investment of at least 7 percent of GDP is required (Vijil 2008).

Tax Policy and Social Development during the Ortega Administration (2007-Present)

For the purpose of illustrating revenue collection trends and the performance of the main tax policies under the current presidency of Daniel Ortega and its implications for domestic resource mobilization, this section will be divided into two parts. The section covering the Fiscal Equity Law will review the period 2007 to 2012, and a different section that will focus on the most recent tax legislation, the Tax Concertation Law, will cover the remainder of the period until present time.

Fiscal Equity Law under the Ortega Administration, 2007 – 2012

In 2007, Daniel Ortega became president after having run for office in the previous four consecutive elections for the FSLN party. His incumbency put an end to 17 years of neoliberal governments in Nicaragua. The electoral outcome reflected the citizenry's response to the various neoliberal policies that took place in the 1990s, particularly the reduction of the workforce, unemployment that resulted from privatization of state enterprises, reduced wages, and corruption. Furthermore, the fragmentation of the previous party in office, the Constitutionalist Liberal Party (PLC), and the emergence of a new liberal party, the Nicaraguan Liberal Alliance (ALN), divided almost in half the liberal vote. In addition, a pact in the year 2000 between Aleman y Ortega allowed to reduce the percentage to win in the first round of the general elections to 35 percent of the votes, paving the way for a Sandinista victory. Ortega came into office securing 38 percent of the national vote, followed by the ALN and the PLC, in second and third place, with 28 and 29 percent of the vote respectively (Envío 2006).

In terms of foreign aid, Ortega's ideological alignment with the Chavez regime in Venezuela secured the government of Nicaragua substantial aid through concessional loans and crude oil amounting to US$ 250 million in 2008 and US$ 125 million in 2009 (Tinoco 2009). About 38 percent of these funds have been used to fund social programmes ran by the state. These programmes include financing for social housing, health services, credit for urban entrepreneurs (particularly women), road construction, and productive and food security bonus (Carrión 2017). Receipt of other sources of overseas development assistance (ODA), besides from Venezuela, have reduced or stopped since 2008, when official external cooperation was 1,249 million, decreasing 10 percent until 2015 amounting to 1,118 million (BCN 2016a). This change can be attributed to a variety of external and internal factors. At the national level, there was a Joint Agreement on Budget Support that began in 2005 and ended 2010, and in which many donor countries participated.[34] Most of ODA ended in 2008 when political opposition parties accused the Sandinista government of committing fraud in the Municipal elections in 2008 (Carrión 2017). Furthermore, given the global financial crisis, donor fatigue, and completion of the Joint Agreement, most of these donors began leaving the country after 2008, and in some cases like Sweden, even closed their diplomatic mission. However, officially, donors stated that global aid priorities were also changing and funds had to be re-channeled to Africa. Furthermore, Ortega's re-election in 2011 was highly controversial. According to the Constitution of Nicaragua, presidents are limited to two non-consecutive terms in office,[35] which raised questions about the legality of his candidacy. In 2014, the constitution was reformed, allowing the

[34] Germany, Finland, Norway, Holland, the United Kingdom, Sweden, Switzerland, the World Bank, the European Commission, the Inter-American Development Bank.

[35] Article 147, 4A, states that no president can serve more than 2 terms in office and that they must not be consecutive.

incumbent to run for office an indefinite number of times.[36] Amidst the controversy, Ortega remains president and he was re-elected in 2016 for five more years in office.

Trends in Taxation

During his first period in office, and in a context of a strong growth performance and macroeconomic consolidation, except for the crisis year 2009 (see Table 2), three reforms to the Fiscal Equity Law were implemented in 2009, 2011 and 2012.[37]

Table 2. Main Macroeconomic Indicators (2009-2013)

Concepts	2009	2010	2011	2012	2013
Economic activity					
Real GDP growth (%)	(2.8)	3.2	6.2	5.1	4.5
GDP per capita (US$)	1,432.5	1,475.8	1,626.9	1,723.1	1,768.9
GDP per capita growth (%)	(2.5)	3.0	10.2	5.9	2.7
Prices and exchange rate					
Inflation Rate (%)	0.9	9.2	8.0	6.6	5.7
Average exchange rate (C$ x US$)	20.3	21.4	22.4	23.5	24.7
Non-financial public sector - NFPS (as % GDP)					
Balance of Non-Financial Public Sector (before grants)	(3.9)	(2.2)	(1.6)	(1.7)	(2.2)
Balance of NFPS (after grants)	(1.3)	(0.6)	0.2	(0.3)	(1.1)
External financing NFPS	2.9	2.5	1.9	2.0	2.3
Internal financing NFPS	(1.6)	(1.9)	(2.0)	(1.8)	(1.2)
External public debt					
External public debt (millions of US$)	3,856.4	4,068.2	4,263.2	4,480.8	4,723.7
External public debt / GDP	46	46.5	43.7	42.8	43.5

Source: Author, based on GEE 2010-2014.

As can be seen from Figure 9, tax revenue collection for the first period of the Ortega administration shows an upward trend. In 2008-09, however, during Ortega's second year in office, the global financial crisis directly affected the performance of the fiscal system. The crisis began taking effect on tax revenue collection from 2008, a decline that was accentuated in 2009, as can be observed in Figure 9 and 10. A decrease in import taxes due to a reduction of its tax base plus a fall in the effective rate caused a decrease of 15.1 percent in the collection of this tax (GEE 2009). It was in this context that the Ortega administration first presented an initiative of a tax law, with the purpose of generating higher revenues to compensate for the shortfall of tax collection.

This new bill was first presented in August of 2009 to the National Assembly in the form of a power point presentation that was later circulated on the Internet. On the third of September of the same year, a National Forum on Tax Reform was held, in which people from civil society, academics, students, government officials, and businessmen actively debated the proposed bill. However, in October of the same year, the government went back on the process and recalled the previously circulated bill, and

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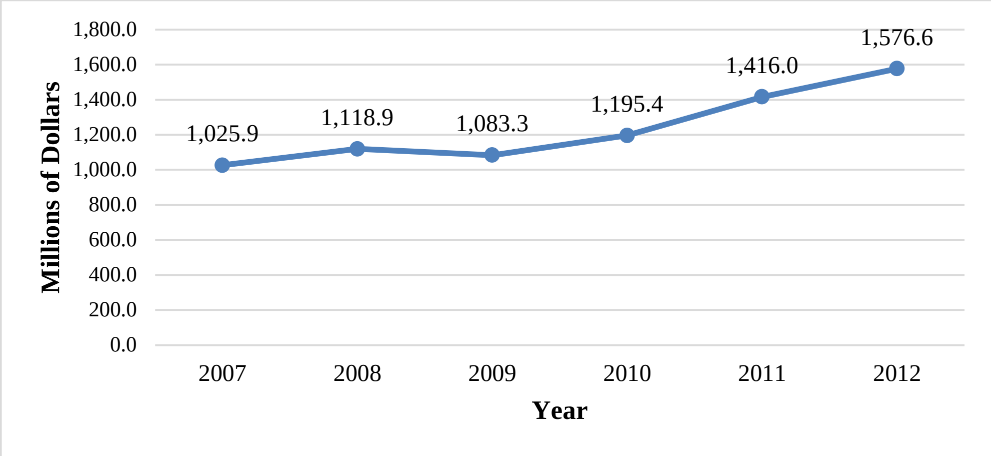
36 Law No. 854, approved on January 29th, 2014, reforms the constitution and removes the subsection of article 147, 4A, which states that presidents may only serve 2 non-consecutive terms in office.

37 Reforms to Law No. 453, Fiscal Equity Law, took place in 2009, 2011, and 2012. The Law was approved in 2003.

announced that a new one would replace it, called Tax Concertation Law. Due to pressure from the Superior Council for the Private Sector (COSEP for its acronym in Spanish) and the IMF, this law was not implemented. Instead, several reforms of the Fiscal Equity Law took place (Báez 2010).[38]

Figure 9. Total Tax Revenue Trend in millions of US dollars: Reforms to the Fiscal Equity Law (2007-2012)

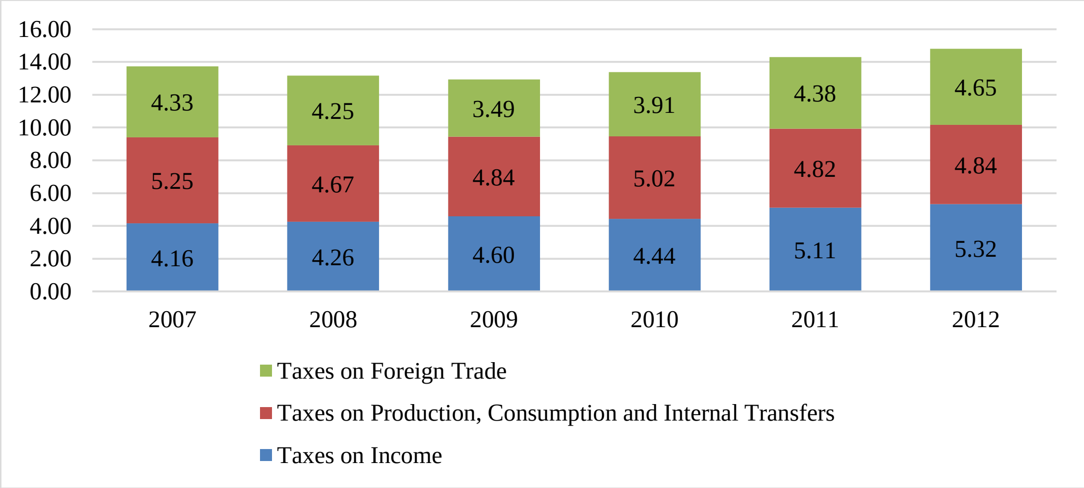


Source: Author, based on DGP 2007-2012.

The objective of the first reform was to generate additional tax revenue to the amount of 0.7 percent of GDP, which was equivalent to the estimated fiscal gap generated by the international financial crisis. To achieve this, the reform aimed to broaden the tax base as well as modify several tax rates that would boost revenue collection. Among the most significant changes included in the reform were the following: eliminating exemptions in some of the capital income, improvements in the collection system and elimination of exemptions and exceptions of a set of luxurious consumer goods. The results of this reform can be seen in Figure 10, in which we can see that taxes on foreign trade and taxes on income increased significantly after 2009. The end of the global financial crisis and the dynamism in the export of agricultural and manufactured products can explain the increase in export taxes (IMF 2011).

[38] In early November 2009, the government officials, including Daniel Ortega, held a meeting with the main economic representatives in the country to discuss the proposed law (Báez 2010). According to Baez, the meeting revolved around the government intention to tax financial revenues such as interests on loans granted by foreign and domestic financial institutions, and capital gains, dividends and foreign transactions. The original initiative on the Tax Concertation Law that the Executive first presented to the National Assembly was being rejected by the Superior Council for the Private Sector (COSEP for its acronym in Spanish), and the meeting concluded with a phone call to the IMF. Shortly after, Ortega publicly announced that the government advisors that drafted the first bill had 'gone too far' (Báez 2010).

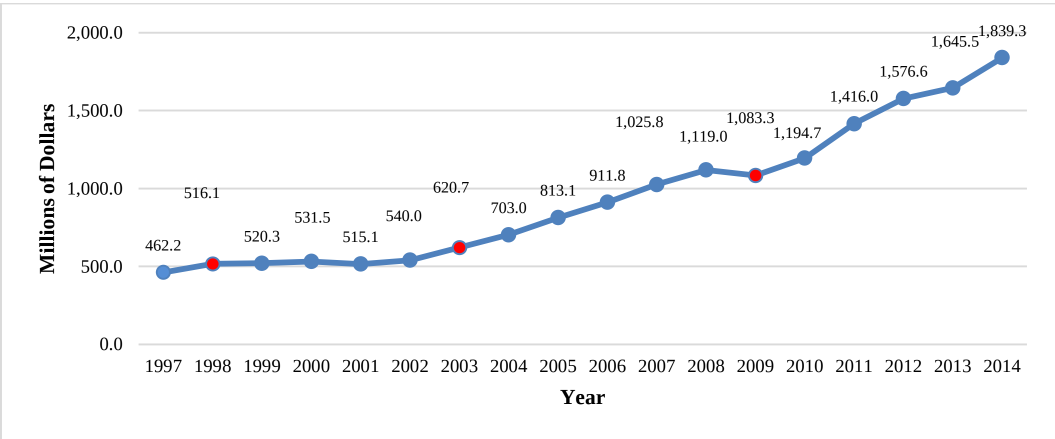
Figure 10. Tax Composition as Share of GDP (2007-2012)



Source: Author, based on the DGP 2007-2012.

Given the importance of tax revenue for the national budget in Nicaragua, whenever a shortfall occurs, tax reforms are seen as the main instrument to cover budget gaps, maybe because of difficulties to finance expenditure through internal and external credit. Official evidence of this can be seen in the Central Bank's annual report for 2012, which states that the reform of the Fiscal Equity Law in 2009 responded, exclusively, to a higher need for revenue collection from that year (GEE 2012). Furthermore, to illustrate this point, Figure 11 shows revenue collection from 1997 up to the third quarter of 2014, in which the years in which different reforms were implemented (for example 1998, 2003 and 2009) resulted in higher revenue collection.

Figure 11. Tax Revenue Collection (1997-2014)



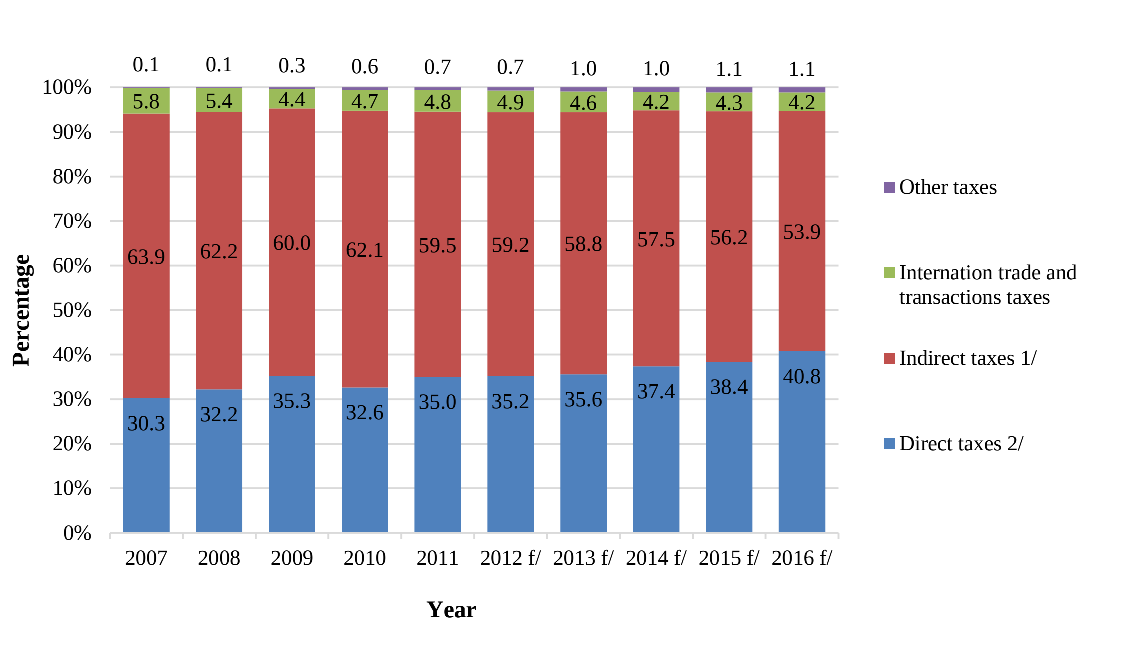
Source: Author, based on Acevedo 2011a and DGP 2010- 2015.

In 2011, revenues increased, in part due of the full implementation of the reform to the Fiscal Equity Law, which also aimed to improve the conditions for the increase of productivity and exports.[39] The year 2012 presented a major change to the tax system in Nicaragua, not only because the new law, the Tax Concertation Law, was approved in November of that year, but also because the government opted for an online system (Electronic Tax Window) to pay income taxes that would come to effect in 2013.

[39] Data on the array of contributors to the fiscal system is not published. However, several reports from the BCN and Ministry of Finance allude that the different reforms have broadened the tax base. Without any published data on this, no analysis can be made in terms of who is paying taxes and who is not.

To sum up, aided by the momentum that the Fiscal Equity Law had been building, Ortega's first period in office showed constant increases in tax revenue collection in absolute terms (Figure 11), with the exception of a decrease in 2009, which was caused by the international financial crisis. From year to year, the progressivity of the fiscal system, measured by the weight of direct taxes in overall tax revenue, increased from 30.3 percent in 2007 to a maximum of 35.3 percent in 2009, and the forecasted data in Figure 12 show an upward trend.

Figure 12. Central government tax collection structure (2007-2016)

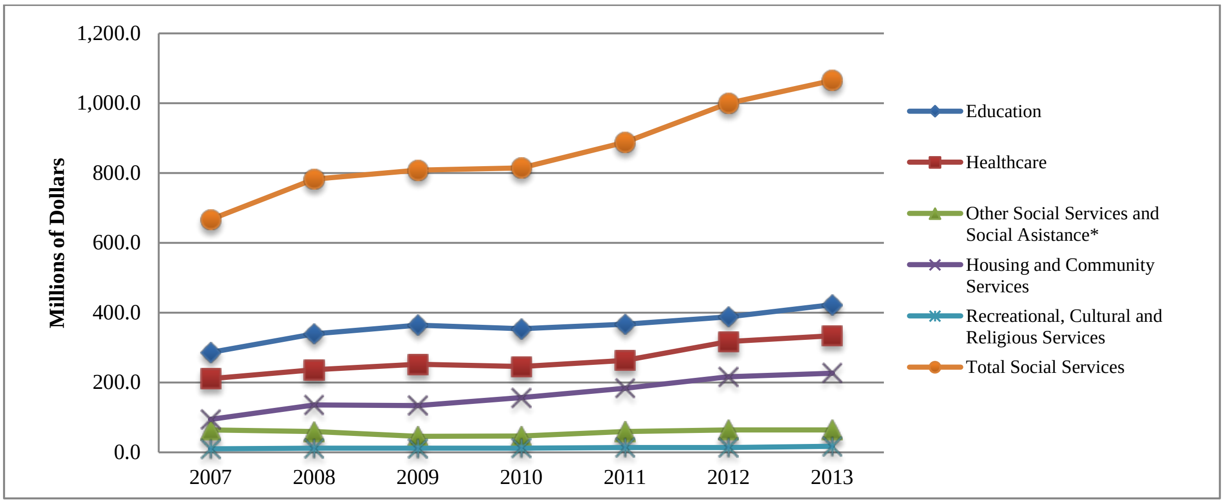


Source: Author, based on BCN Central Government Taxes 2002 – 2016.
f/: Forecasted data.
1/: Value added taxes (VAT) + selective consumption taxes (SCT).
2/: Income tax.

Trends in Social Spending

When Ortega assumed power in 2007, his government announced to prioritize social expenditures, poverty reduction, improvements of productive infrastructure, as well as social services such as education, health, housing, and water and sanitation (GEE 2007-2012). Figure 13 portrays the gross total social expenditure for the period. As can be observed, education, healthcare, and housing expenses indeed show an increase since 2007. This trend is also visible from 2007 to 2009 with regard to expenditures as a share of GDP (see Figure 14), and this in a context of falling tax revenue. However, if we look at social spending and tax revenue as a share of GDP, both declined by 2012 (Fig. 14). Furthermore, in the case of education, there is less investment in 2013 than there was in 2007 in terms of spending as a share of GDP, and only half of expenditure levels as a share of GDP achieved in the mid-1980s. In the case of healthcare and total social spending in terms of GDP, both of them have decreased when compared to 2007, by 0.3 and 1.4 points respectively.

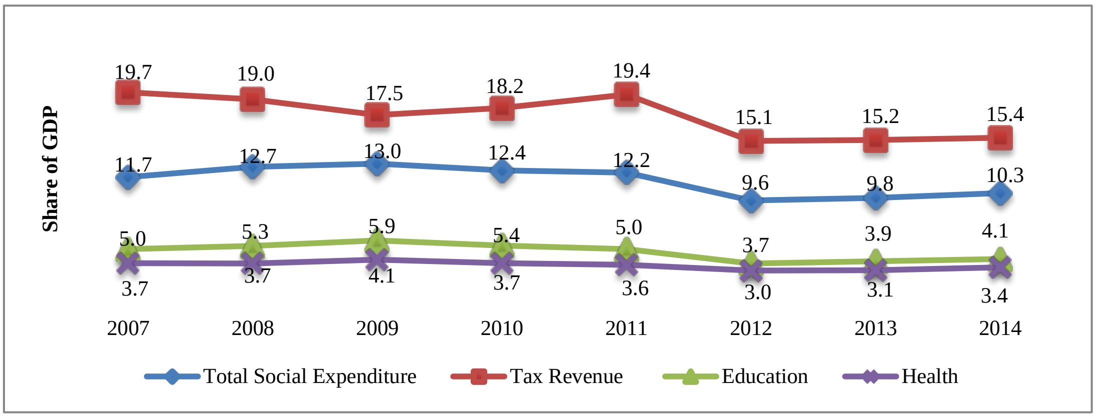
Figure 13. Gross Social Expenditure (2007-2013)



Source: Author, based on DGP 2008-2014.

*: The category Other Social Services varies from year to year, it includes funding for Ministries, such as Labor and Family, Ombudsman's Office, Nicaraguan Red Cross, Social Security Nicaraguan Institute, National Counsel for the Fight Against Drugs, etc (DGP 2001).

Figure 14. Tax Revenue–Social Expenses, Education Expenses and Healthcare Expenses as a Percentage of GDP (2007-2013)



Source: Author, based on BCN 2007-2014.

The Role the Private Sector and Civil Society have Played in the Reforms of the Fiscal Equity Law

Just as with previous governments, civil society has played a limited role in shaping the politics of resource mobilization in Nicaragua. There have been instances in which civil society has been consulted in matters of tax legislation, such as the National Forum on Tax Reform in 2009; however, the outcome of the forum had no impact on the reform that was finally approved. On the other hand, the Ortega administration has developed a strong relationship with the COSEP.

The relationship between COSEP and the Ortega administration was further strengthened since 2009, during the global financial crisis. That year, the national budget had to be reduced three times, as tax collection, remittances, imports and exports, production credit, and investments decreased significantly (Envío 2013). It was in that context that the first negotiations with the private sector took place, and one of the results was the first partial reform to the Fiscal Equity Law during that year (Envío 2010).

The reform to the Fiscal Equity Law was the result of the failed first draft of the Tax Concertation Law presented in 2009 and rejected by COSEP, as described above. According to Adelmo Saldino,[40] only a limited group of technocrats and economists, including him, participated in the negotiations on the reform of the Fiscal Equity Law. The purpose of the group was to give technical inputs to the state in the drafting of the law. However, most social actors and stakeholders that would be affected by the reform were not involved in the discussions and could thus not exert any influence in the outcome of the reform. Instead, the main participation and influence in the reform came from economic actors represented by COSEP.[41]

The special relationship between the state and the private sector was institutionalized in February of 2014 in the reform to the Constitution of the Republic.[42] Article 98 of the Constitution was modified to include the following: *Through the promotion of public and social policies, the State must play a role in the development of the private sector, which can improve the functionality and efficiency of public institutions, simplifying procedures, reducing entry barriers, increasing coverage of social security and benefits, and facilitating the performance of formal enterprises.*[43] The approval of this constitutional reform was mutually beneficial to the Ortega administration and COSEP since it granted legitimacy to the state, and it provided the private sector with a direct channel of communication to voice concerns and even draft policy as in the case of the reform of the Fiscal Equity Law.

Tax Concertation Law under the Ortega Administration, 2012 - Present

On 30 November 2012, the Nicaraguan National Assembly (NNA) approved the second important tax legislation under the Ortega administration known as the Tax Concertation Law. Its main objective was to modernize the fiscal system and to mobilize public resources towards social and investment projects that would reinforce the fight against poverty and generate economic growth (GEE 2012). However, since it was published in the official daily La Gaceta, it has been highly contested by tax experts and civil society organizations. As can be seen in Figure 15, there was a sharp decline in the rate of growth of revenue collection after the implementation of the reform, in 2012 and 2013. The reasons for the reduced rate of growth will be explained further down.

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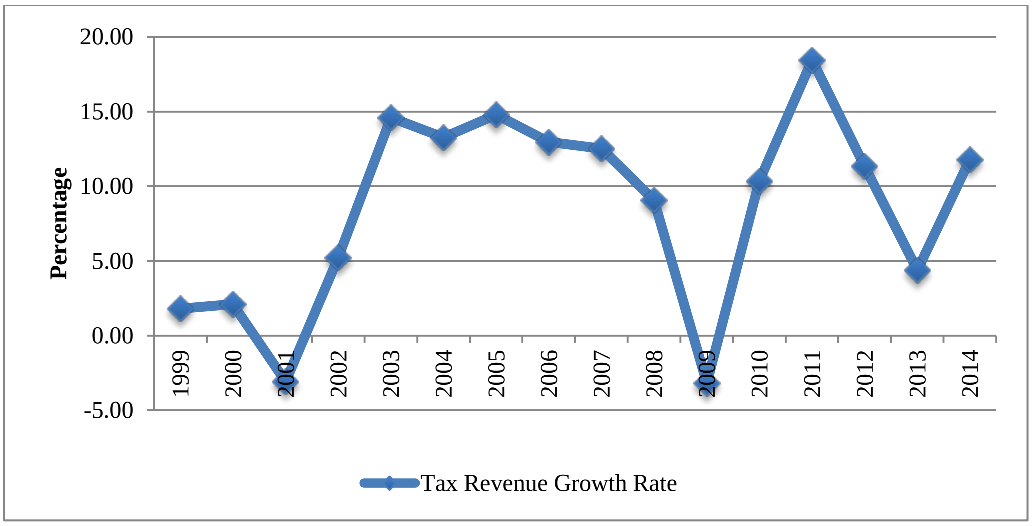
[40] Interview with Adelmo Sandino. Researcher of the Governance and Social Inclusion Program at Institute for Public Policy and Strategic Studies (IEEPP), 22 February 2017.
[41] Interview with Adelmo Sandino, IEEP, 22 February 2017.
[42] The article 98 before the reform to the Constitution of the Republic in 2014, did not mention to private sector: "*The main function of the State in the economy is to develop the country materially; suppress inherited backwardness and dependency: improve the living conditions of the people and realize an increasingly fair distribution of wealth*"
[43] Law No. 854, article 98, Printed in La Gaceta, number 26, February 10, 2014.

Figure 15. Rate of Growth of Revenue Collection (2003-2014)



Source: Author, based on DGP 2004-2015.

The new tax law came to correct the different distortions within the tax system, as well as to provide order to the existing system, and stimulate higher participation of tax revenue in the financing of public expenditures. Furthermore, the law is aiming to expand the tax base and reduce tax evasion, as previous laws attempted. For this purpose, the law introduced changes in the income tax, sales tax, selective consumption taxes, tax benefits, and in the tax administration (GEE 2012: 83). A further increase in tax revenue collection was also expected from the law, which was again to happen mostly through the elimination of different tax exonerations and exemptions, to be implemented gradually over a five-year period starting in 2015.

Even though the rate of growth of tax revenue was still positive for 2013, it fell below the 11.2 annual growth rate that was expected (Navas 2014). The reasons for the reduced growth rate in revenue collection reflected in 2013 will be discussed in more detail below:
Firstly, after the Law came into effect in January of 2013, many issues arose in terms of consistency from the Law with its Regulation. The law is as important as its Regulation, given that the Regulation functions as an operative manual for the implementation of the law. The most notorious issues that arose are related to the critical path of the law formulation. The Law was first published in December 2012; however, its Regulation was published on 22 January of 2013, and not only was it incomplete, but the Ministry of Finance lacked the capacity to implement a normative change of this magnitude (Interview with Nestor Avendaño, 20 November 2014). A good illustration of this is the fact that the income tax return form was not accessible to the public until a few days before the deadline of payment in March 2013 (Rodríguez 2014). Having to adjust to this, the income tax report came late and not only did it delay the tax collection report, but it could also be one of the reasons for the underperformance in revenue collection (Interview with Theódulo Báez Cortés, November 2014). Given the lack of institutional capacity of the tax administration, indignant taxpayers could all together refuse to pay their taxes, and most likely, without any legal repercussions.

Secondly, when the president first presented the draft law of the Tax Concertation Law in 2009 (see above), it included several positive items that would have meant a significant step towards a more progressive and egalitarian tax system, such as an integral revision of income tax, transfer prices, and fiscal incentives for small

agricultural producers in the Agricultural and Livestock Exchange. However, it also contained some items that undermined its progressivity, such as the timid reduction of exonerations, the introduction of an income tax for retirees, and a fixed fee regime for small businesses. Even though this new tax regulation looked promising, "the government, our tax authorities, economic agents, and of course the National Assembly, considered that it was not the time or the right economic conditions to discuss and approve an initiative of this nature" (Asamblea Nacional 2012). Experts, like Julio Francisco Báez, believe that it was due to the influence of powerful actors such as the financial sector in this process of bargaining and contestation that the reform eventually did not achieve the changes that it originally intended (Báez 2012). The result was the partial reform of the Tax Equity Law that was approved in order to generate higher income without having to create major changes to the fiscal system, thus postponing the approval and undermining the possible benefits of the Tax Concertation Law to the year 2012, when the National Assembly finally approved it.

Thirdly, in terms of revenue collection, the treatment of transactions that take place in the Agricultural and Livestock Exchange undermine better results. The Exchange is a private corporation that provides a public service and was created in 1993 to serve as facilitator between producers and industry. All the transactions that take place in the Exchange, are only subject to either a 1, 1.5, or 2 percent rate of income tax, and are exempt from sales tax and municipal taxes with a maximum annual roof of about 1.6 million dollars,[44] in order to foster food and agricultural production (Bagsa 2007). Báez mentions that about 50 to 55 percent of all national transactions take place in the Agricultural and Livestock Exchange, an estimated USD 849 million approximately (Báez 2012).[45] Regulating these transactions and increasing taxes could generate millions more in tax revenue. Reducing and regulating[46] the incentives given to the Agricultural and Livestock Exchange could produce the revenue that is needed in order to increase social spending.

As mentioned before, the Tax Concertation Law grants exonerations for a 5-year period, when they would be removed from the list of exonerations. According to Julio Báez, this regime answers to the strong relationship that the government has built with the private sector (Báez 2012). Although the amount lost in revenue collection from exonerations is difficult to quantify, Báez estimates that they amount to no less than 7.8 percent of GDP, which is equivalent to over 40 percent of taxes collected for 2010 (Báez 2012). The different exonerations, evasion, elusion, and smuggling are estimated to lead to the monumental loss in revenue equivalent to 14 to 15 percent of GDP (Báez 2012).

The Role of Civil Society and the Private Sector in the Tax Concertation Law

The preceding section has given an example illustrating the relationship between the private sector and the Ortega administration, especially the failed attempt to introduce a more progressive Tax Concertation Law in 2009. Furthermore, later in 2012, when the revised Tax Concertation Law was designed, the government and COSEP drafted the new tax bill, which had never happened before in Nicaragua, and is again representative of the close relationship between private sector and government.

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[44] The exchange rate used was the average exchange rate between 2013 and 2014. The equivalent in Córdoba Oro is of C$ 40,000,000.00.

[45] The exchange rate used for this transaction was the average rate for 2012: 1USD = C$ 23.55

[46] An example of regulating the transactions could be monitoring the sales of individuals who are exceeding the exemption roof and are spreading the overhead with relatives, and other people in order to elude paying higher taxes (Interview with Theódulo Báez Cortés, November 2014).

The name Tax Concertation Law implies a level of agreement between the different tax-paying sectors of the economy, therefore, making them stakeholders in the fiscal process. The name Concertation was chosen in order to make visible that in the process of elaboration, all the different stakeholders were consulted. However, this process was held behind closed doors and the most prominent actor was the government, which in this case presented the draft law and ultimately had the final say in any of the suggestions to the law. The second most important actor in the negotiations was COSEP, which brought in many consultants and tax specialists to the table in order to inform its positions and exert influence. In addition, the National Workers Front (FNT), Ministry of Finance were also present as well as the economic advisor to the president, Bayardo Arce (Interview with Freddy Blandon[47]).

However, these actors did not participate on equal terms. COSEP had special access to state representatives and key technical information, which strengthened and facilitated its position. In contrast, actors like FNT did not have the resources to hire tax specialists and consultants to develop technically sound proposals to influence the negotiating process. Issues of representation also arose as COSEP is not representative of all enterprises or the FNT representative of all workers. In fact, the majority of workers in the country that are affiliated to micro and small businesses are not affiliated to unions. Moreover, a law of such magnitude must be discussed with broader sectors (Potosme 2013).

Civil society organizations that were not included in the negotiating table united to form the Nicaraguan Alliance for Fiscal Justice. These organizations included cooperatives' federations, rural women's and youth organizations, NGOs like OXFAM and Christian Aid, research centers working on tax issues, academics, and civil society actors like the Coordinadora Civil comprised of both Nicaraguan NGOs and social movements.[48]

The objective of the Alliance was to create a common agenda and draft a technical proposal for the government. The Alliance had also envisioned presenting a law initiative to the National Assembly in the context of the Tax Concertation Law negotiations. Additionally, the Alliance aimed to make the negotiating process more inclusive by bringing other excluded sectors into the debate and influencing public opinion. They organized several workshops throughout the country in order to discuss fiscal equity issues with a broader audience. By 2011, around 8,000 people had assisted to these workshops.[49] A number of popular education and methodological material was prepared in order to make the discussions and issues at stake more accessible. Media campaigns and an ambitious lobby strategy were designed in order to influence the negotiating process.[50]
The Alliance's main proposals with regard to the Tax Concertation Law were (Acevedo, 2011):

- Income Tax of Natural Persons: tax all natural persons resident with a single progressive scale on all sources of income without distinction of origin (rent, interest, dividends, capital gains, profits).
- Corporate Income Tax: a) increase the tax base by reducing exonerations and exemptions; b) regulate transfer pricing between related companies of the same

[47] Legal representative of COSEP. He participated in the negotiation process of the Tax Concertation Law.
[48] Interview with Adelmo Sandino, IEEP, 22 February 2017.
[49] Interview with Adelmo Sandino, IEEP, 22 February 2017.
[50] Interview with Adelmo Sandino, IEEP, 22 February 2017.

transactional group; c) Preferential arrangements for small and medium-sized enterprises.
- Value Added Tax: maintain a rate of zero only for direct exporters.

However, the proposals made by the Alliance were not heard by the government. In fact, none of these proposals and concerns were captured in the final draft of the Law. Additionally, the government decided to speed up the negotiating process and an agreement with COSEP was reached only five months after the official launching of the negotiations.[51] This proved to be highly detrimental to the Alliance's lobby strategy.

Other excluded sectors from the negotiation process were unions from the political opposition, NGO's, retirees, teachers, and university professors.[52] The consequence of this exclusion has come in direct detriment to the majority of contributors, given that all tax legislation, including the most current one, as was shown above (see Figure 3, Figure 7, and Figure 10), have been regressive in nature and the burden falls disproportionately on the lower economic classes, including informal and formal workers.

It is important to highlight that the government established in article 309 of the Tax Concertation Law[53] that any new reform proposals to the Law would have to be the result of a negotiating process like the one that gave rise to the Tax Concertation Law in the first place. This article could thus imply the continuity of processes of tax reform negotiations behind closed doors and with little meaningful civil society's participation.

Reform to Tax Concertation Law (2014)

In December 2014, the Tax Concertation Law was reformed under law No. 891. The new law was again the result of a consensus between COSEP and the government (Vidaurre 2014). Even though it is too early to judge the performance of this reform, this section will explain the major changes that resulted from the law.

The reform was put into effect in order to improve the fiscal system. The majority of the reform contains technical changes that do not change the substance of the Fiscal Equity Law. The law was implemented to mitigate the negative effects of external shocks, therefore, the limits established to the exoneration regime were removed (Acevedo 2015). Among other changes that took place are the elimination of taxes to churches, other congregations, and NGO's (Estrada 2014). However, smaller industries such as the national shoe and clothing industry are directly affected, since VAT was not exonerated from the final sale of the products. Furthermore, it enhances the tax burden of the small businesses by increasing the fixed fee regime, and it affects used vehicle imports. This tax reform seems therefore to perpetuate a system of unequal distribution of wealth by maintaining a schedular system of taxation and by removing exonerations to small producers, increasing taxes to small businesses.

Analysing tax revenue collection and social spending trends is difficult, given that the Tax Concertation Law is still in its infant stages. Furthermore, exonerations have not been reduced as of yet, therefore the analysis of the law will not include the full potential of revenue collection that it could bring in the future.

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[51] Interview with Adelmo Sandino, IEEP, 22 February 2017.

[52] Discussions of sentences of decrees and laws. "Tax Concertation Law." November 2012. National Assembly. http://legislacion.asamblea.gob.ni/Diariodebate.nsf/76ed72912dd57e57062 5698c00773f5d /29db3f80f66e1f5706257b5900630b21?OpenDocument

[53] See, Law No.891, Law of reforms and additions to law No.822, article 309, Tax Concertation Law. http://legislacion.asamblea.gob.ni/normaweb.nsf/($All)/58A914309E95552006257DAF006A415D?OpenDocument

In terms of revenue collection, the Tax Concertation Law has followed the same trend of higher tax revenue collection as the previous reforms. Even though there was a reduction in the rate of growth of tax revenue from 2012 to 2013 as can be seen in Figure 15, it went back to 11.8 in 2014, which was a higher rate than the expected 11.2 percent increase.

Conclusions and Recommendations

Conclusions

Over the different time periods analysed in this paper, there is strong evidence that the different Nicaraguan governments have been able to mobilize substantial resources through the fiscal system, in particular through tax. The best performance was achieved in the middle of the 1980s during the Sandinista government, with over 30 percent of tax revenue as share of GDP. These revenues were complemented by external funds such as ODA, which at times financed up to 35 percent of the health budget, to give an example (Garcia 2014, cited in Delmelle and Mendoza forthcoming), as well as by private transfers such as remittances, which were crucial to fund private social expenditure at the household level. However, when analysing expenditure patterns for social development, the conclusion is that social expenditures have not kept up with increases in tax revenue collection throughout the different periods, including the present time. While overall revenue collection has followed an increasing pattern in nominal terms and in terms of share of GDP, social expenditures still need to reach higher levels, in particular as a share of GDP, as they have significantly fallen since the mid-1980s, in particular during the period of neoliberal adjustment policies.

During the Somoza dictatorship, the tax system was at an infant stage in which the institutional capacity of the tax administration was clearly in need of reinforcement. The political context was one of instability and repression, in which state expenses were focused on national defense rather than social development. There is little data to support that any negotiation was being held between the state and other key players in the formulation of tax reforms. Reforms were mainly targeted at higher revenue collection, and in later years, to fund the war effort against the Sandinista National Liberation Front in the late 1970s.

The Sandinista revolution of the 1980s saw changing levels of revenue collection that were directly affected by internal shocks, such as the Contra War and economic instability resulting in hyperinflation, which in turn eroded overall tax collection. Social expenditures were prioritized, and with additional help from foreign aid and donations, high impact social programmes were implemented, such as the National Literacy Campaign. Progressivity of the system increased, yet no clear direction towards a more egalitarian system was achieved due to adverse economic conditions and foreign relations. The state-society relationships favoured relations with the working classes, adopting reforms that were more progressive in nature, lowering the burden on the workers, and increasing it on the private sector.

Tax reforms between 1990 and 2006 were largely driven by donors’ policy priorities. With the need to combat hyperinflation and to reconstruct a country that was in ruins from the popular insurrection against the Somoza Dictatorship in the late 1970s and the Contra War in the 1980s, the state negotiated structural adjustment packages with the international financial institutions, which required the state to implement new tax reforms. The overall tax revenue collection trend was positive, although starting from a low level, and in some years tax collection did regress. It was in this period that the first tax reform negotiations were more visible, however, they were mainly between the business sector and government. Social expenses of the period showed little variation in terms of GDP, and it showed an upward trend, as a percentage of GDP, after 1993.

During the current government, laws and fiscal reforms have been conducted in tandem with economic actors represented by COSEP. The private sector has influenced laws

and reforms in ways that protect or minimize negative effect on their economic benefits and activities. However, the same cannot be said of small and medium enterprises. On the contrary, small and medium enterprises were one of the sectors adversely affected by these laws and reforms, for example, by eliminating the exemption of VAT for the footwear and clothing sector in 2014.

When comparing revenue collection trends to social expenditure trends, it can be inferred from the data that the politics of domestic resource mobilization in Nicaragua establish a clear demarcation between the politics of revenue collection and expenditure policy. A higher revenue collection will not necessarily translate into higher social spending, or vice versa. For this to happen, tax reforms must be drafted with clear and specific policy objectives for higher social expenditures.

As a result of the above analysis, the following policy recommendations are made:

Recommendations

- There must be an inclusive dialogue with civil society and the public, including independent experts, when drafting tax legislation in order to ensure a more equitable tax regime system that will not fall heavily on one particular sector of society, in particular on vulnerable and poor groups. The inclusion of experts from NGOs and other sectors could prove to be valuable to the negotiations, and ensure a fairer system. Transparency and access to relevant information for all is necessary.
- There is still a need to improve progressivity in the tax system. Even though there has been a small trend towards higher progressivity, in order to reach a higher level of equality, additional weight should be given to direct taxes over indirect ones.
- The schedular system of taxation must be changed back to a global tax system, in which all sources of income from an individual are arithmetically added together and charged a progressive tax rate. This will install more progressivity in the system and secure higher tax revenue that could potentially fund more social programmes.
- There is a strong need for improving the tax administration in order to avoid tax evasion, have greater control over and be able to follow up on the universe of contributors; initiatives such as the Electronic Tax Window could be an important contribution on this. Furthermore, the state has the responsibility of transparency to reach a level of legitimacy and accountability, and maintain the trust of its contributors, which will in turn help reduce tax evasion.
- In order to achieve higher social development, the government must rebalance its spending towards the social sector. In the case of health care, the government underspends when compared to all the countries in Central America. This must change in order to eliminate the deficiencies in this sector.
- The Agricultural and Livestock exchange is in dire need of greater regulation. A large amount of the national economy trades in the exchange; therefore, increasing the tax rate per transaction by a percentage point, while at the same time strengthening the regulation, could translate into additional millions of dollars in tax revenue and further increase the availability of domestic resources for social development.

Reforms must have clear policy objectives and a justification to link tax revenue collection with specific social objectives, in order to improve social development in

Nicaragua. If specific targets are developed and adhered to, tax reforms could become a reliable tool for social development. Reforms must be the end result of a general political agreement between the state, the private sector, and civil society.

As long as there is no general social and political agreement about the type of social contract that is needed in the country, the working class will remain on the losing end. When a society inherits entrenched structures of inequality, as is the case with the regressive tax system, it is challenging to reach social development objectives. In Nicaragua, multi-dimensional poverty decreased by 5 percentage points from 2005 to 2012 (Cepal 2014), which means that there are general improvements achieved through social policy. Political will is imperative to establish a more egalitarian system based on the needs and capacities of the different sectors. But also, a society willing to give up certain privileges for the common good is needed in order to break from the status quo. In this sense, the higher income sectors of the country must be willing to give up fiscal benefits for the greater good of the nation. It is unfair to increase revenue collection at the sole expense of the working class and small and medium enterprises. Furthermore, the state must become a true mediator between social groups and a facilitator of dialogue between them. Lastly, the state should strive to reduce power imbalances between stakeholders to make reform processes and outcomes more inclusive.

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Freddy Blandón, Legal Director of the Superior Council for the Private Enterprise (COSEP), 17 October 2014.

Theódulo Báez Cortés, Executive Director of Báez Cortés & Compañia Limitada, 18 November 2014

Adelmo Sandino. Researcher of the Governance and Social Inclusion Program at Institute for Public Policy and Strategic Studies (IEEPP), 22 February 2017.

Annex 1. Main Tax Reforms in the 1970's

Tax Decrees (1973, 1974, 1978)			
Decree Number	**Name**	**La Gaceta Serial Number**	**Date Published in La Gaceta**
1973			
84	Suspension of exemptions from various taxes	1	01/08/73
85	Create 10% tax on export items shipped outside the Central American area	1	01/08/73
1	Regulation of 10% tax over export items shipped outside the Central American area	22	02/01/73
6	Reform of the 5% Sales Tax	22	02/01/73
2	Tax to motorbike riders	48	03/03/73
95	It will be applied the 10% on Free On Board value	58	03/15/73
9	Suspension of Provisions of Vehicle Registration tax	72	03/31/73
39	Addition to article No. 3, regarding tax payment over tobacco sale	98	05/11/73
-	Reform Article 1, regarding reduction on employee salaries	177	08/11/73
54	Addition to Decree No. 56, Special Excise Tax validity	250	11/08/73
282	Tax of C$5 per litre of distilled hard liquor	270	12/01/73
283	Tax of C$1 per litre of beer	270	12/01/73
1974			
85	Regulation on the export of coffee	17	01/21/74
360	Tax Law modifications	143	06/27/74
657	Modification on the Stamp Tax Law	262	11/16/74
663	General Sales Tax and Excise Tax Law	262	11/16/74

660	Real State Tax Law	270	11/26/74
658	Movable Property Tax Law	270	11/26/74
662	Income Tax Law	270	11/26/74
659	Chapter 73 amend: Tariff Code on Imports of Motor Vehicles	271	11/27/74
4	Addition to Decree No. 2, regarding tariffs	278	12/05/74
662	Errata Corrects publication on Income Tax Law	285	12/13/74
1978			
1	Motor vehicles will pay taxes	20	01/26/78
683	Reform on General Sales Tax and Excise Tax Law	51	03/03/78
7	Regulation of Motor Vehicle Registration Tax Law	69	04/03/78
-	Central American Agreement Protocol of Tax Incentives to Industrial Development	87	04/24/78
713	General Sales Tax and Excise Tax Law reform	183	08/16/78
715	Decree of Stamp Tax Law reform	183	08/16/78
31	Payment Procedure of General Sales Tax and Excise Tax	183	08/16/78
717	Income Tax Law reform	184	08/17/78
32	Include Sales Tax to workshops, computers and photography studios	196	08/31/78
740	Income Tax Law reform	254	11/10/78

Annex 2. Main Tax Reforms in the 1980's

Tax Laws and Decrees (1982, 1983, 1984, 1987)			
Decree or Law Number	**Name**	**La Gaceta Serial Number**	**Date Published in La Gaceta**
1982			
949	Ad-Valorem Progressive Tax over sugar cane molasses export reform	35	02/12/82
950	Sesame Seed Export Tax Reform	35	02/12/82
951	Cotton Export Tax Reform	35	02/12/82
952	Beef Cattle Export Tax Reform	35	02/12/82
953	Ad-Valorem Progressive Tax over sugar export reform	36	02/13/82
954	Coffee Export Tax Reform	36	02/13/82
956	Tax Law for Public Debt Service	37	02/15/82
959	Faculty for the Reconstruction Board of Nueva Guinea to apply tax rate of the city of Chontales	38	02/16/82
979	Dispositions provided in the establishment law of the General Income Office	54	03/06/82
1003	Law of Extraordinary Burdens for National Emergencies	79	04/05/82
1054	Service rate of import items, addition to Article 1	138	06/14/82
1059	City Tax Plan And Service Rates Of The City Of Chinandega	148	06/25/82
1075	Alcohol taxes and prices reforms	168	07/20/82
1983			
1172	Reform of the Municipal Reconstruction Board tax plan	15	01/19/83
1223	Law of Extraordinary Burdens on Collections	75	04/04/83
1227	Tariff protection law for the types and sizes of wheels and tires produced by GINSA and the establishment of new list prices	79	04/08/83

1248	Alcohol sale taxes and prices reform	105	05/09/83
1249	Reforms and additions to the Income Tax Law	106	05/10/83
1251	Property Tax Law	107	05/11/83
1284	Additional regulation to the Income Tax Law	167	07/22/83
1293	Tax plan for the city of Managua reform	187	08/17/83
1302	Tariff Law for the Registration of Investment Patents	193	08/24/83
1323	Partial reform of the General Sales Tax and Excise Tax Law	227	10/05/83
1358	Reforms and Additions to the Property Tax Law	280	12/13/83
1363	Alcohol taxes and prices reforms	286	12/21/83
1369	Tax Receipt Law	286	12/21/83
1370	Common Tax Legislation Reform	286	12/21/83
1984			
1397	Fiscal incentives for the industrial development reforms	28	02/08/84
1427	Modification, Decree No. 633, General Sales Tax and Excise Tax Law	82	04/26/84
1431	Reform of the Migration and Immigration Law tariff	83	04/27/84
1434	Addition of one paragraph to the only article of Decree 1379 (Tax Law for Public Debt Service modification)	83	04/27/84
1438	Addition to paragraph 5 article 2 Decree No. 633 "General Sales Tax and Excise Tax Law"	85	05/02/84
1460	Extend Law of Extraordinary Burdens on Revenues	124	06/26/84
1469	Property Tax Law Reform	141	07/20/84
1470	Income Tax Law Reform	141	07/20/84
1532	Excise Tax Law (Reprinted La Gaceta No. 52, 14-03-85)	249	12/27/84
1533	Creation of Capital Gain Tax	249	12/27/84

1534	Presumptive Income Law	249	12/27/84
1539	Customs Stamps	250	12/28/84
1540	Reform to the Stamp Tax Law	250	12/28/84
1987			
262	Common Tax Legislation reform	101	06/09/87
268	"Creation of the Monetary Stabilization Rate Law"	126	06/08/87
276	Transit Tariff Law	200	09/07/87
277	Migration and Immigration Tariffs Law	200	09/07/87

http://movpuente.org/?publicaciones=de-equidad-fiscal-a-concertacion-tributaria

Annex 3. Summary of laws and reforms from 2003 to 2014

Laws or reforms	Fiscal Equity Law I	Tax Concertation Law Draft	Fiscal Equity Law II	Tax Concertation Law I	Tax Concertation Law II
Presidency	**Bolaños**	**Ortega**	**Ortega**	**Ortega**	**Ortega**
Implemented	**2003**	**Revoked 08/2009**	**2009-2011**	**2012-2013**	**2014**
Objective	Law intended to adapt the tax regime to principles of generality, neutrality and equity of taxes; reduce anti-export bias; facilitate investments and strengthen institutions responsible for collecting taxes.	Law sought broad restructuring of income tax through higher incidence on capital gains, dividends and foreign transactions between related parties, or transfer prices. Interest on loans granted by foreign and local financial institutions, which traditionally constitute non-taxable income, would be reached by income tax.	The purpose of this reform was to broaden the taxpayer base in order to mobilize additional resources to compensate for the fall in tax revenues as consequence of the international financial crisis.	The objective was to broaden the taxpayer base, reduce evasion rates and rationalize the system of exemptions, seeking to improve the conditions necessary for increased productivity, exports and employment. Beginning in 2013, the tax system moved towards a schedular system, separating these incomes in; income from work, income from economic activities, and capital income and capital gains.	The law was implemented to mitigate the negative effects of the world economy. The majority of the reform contains technical changes that do not change the substance of the law.
Main features	* Unification of the maximum marginal rate by 30 percent for the payment of income tax, for both natural and legal persons. * The zero rate was reserved for exports, since the products of the basic basket became exempt. *Widespread deduction of the Nicaraguan Institute of Social Security (INSS) to	* Businesses must pay 1 percent over total revenue as minimum payment, even if they have losses. * The minimum income tax of 0.6 percent on deposits that were comfortably paid by banks, would be modified and banks would become part of the general system applied to all companies. * Remove exemption for	* Incorporation as taxable base of the income tax the dividends and interest paid. * Elimination of the exception on the interests of securities issued by the State, as of 2010. * Introduction of an aliquot of definitive retention of the interests of securities issued by the state.	* For labour income, it seeks to increase the exempt base to 100 thousand Cordobas annually, to allow a deduction of up to 5,000 Cordobas in health, education and professional services expenses. * For incomes from economic activities, it allows companies with annual gross income equal to or less than 12 million	* Elimination of the VAT exemption to the footwear sector and national clothing. *Derogation of article 288 that established limits to the granting of exemptions to the private sector. *Elimination of taxes for churches, other congregations, and NGO's * Right to a tax credit of

	the basis of the IR calculation to all employees. * Reduction of the dispersion of the rates of the Selective Consumption Tax (SCT) on imports of luxury goods. *A repayment of 25 percent of the SCT of fuels was established to companies under the temporary admission regime.	the Agricultural Exchange. * Repeal taxes, including the levy of 0.5 percent of the value of milk production. * Payment of income tax by retirees or old-age pensioners, just as if they were salaried. * Eliminate the VAT subsidy in high-income residential areas for household electricity consumption, equivalent to 50 million cordobas yearly.	* Increase of the final retention rate from 1 to 1.5 percent on the transaction of primary goods traded on the Agricultural Exchange, maintaining the 2 percent rate for the rest of the goods. * Modification of the income tax retention rate on the value of real estate transactions, from 1 percent to 1, 2 and 3 percent, depending on what ranges of value apply. * Definitive retention of 10 percent on game prizes and winnings on bets. * Elimination of exemptions to liquor, tobacco, perfumes, jewelry, cosmetics, aircraft and yachts for private use. * Increase the SCT rate by 5 percent to private vehicles with a cylinder capacity greater than 3,000 cc.	cordobas, to pay their taxes according to a progressive table with income tax rates lower than the general regime on the cash flow. * For both income from work and from economic activities, it reduces the income tax rate by one percentage point from 2016, until reaching 25% by 2020. * Capital income and capital gains are separated from income from economic activities, strengthening the retention system, applying reduced rates to encourage investment and employment, as well as improving the effective rates of global income collection.	1.5 percent for all manufacturers of exportable goods, without the need of prior authorization. * Cooperatives must pay income tax when the annual gross income amount is greater than 40 million cordobas.