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FEATURED Q&A

Why Is Brazil's Tax Reform Plan So Controversial?



Brazilian Economy Minister Paulo Guedes unveiled a proposal that he said would simplify the country's tax system. // File Photo: Brazilian Government.

Q Brazilian Economy Minister Paulo Guedes last month unveiled to congressional leaders the first part of the government's tax reform proposals, a plan he said will be simpler, cheaper and more efficient for companies to comply with, in addition to more transparent for consumers. What are the benefits and drawbacks of the proposed tax changes? To what extent is it likely to pass Congress as drafted, and how long might that process take? What other measures should the government include in its broader reform of Brazil's tax system, which the ministry said would be announced in the period ahead?

A Gabrielle Trebat, managing director at McLarty Associates: "Abolishing the federal PIS and Cofins taxes in favor of a 12 percent federal value-added tax has the potential to reduce the costs of compliance and increase judicial security for corporations. It could also decrease tax evasion and boost public revenues without raising overall tax rates. However, the new tax would disproportionately affect the services sector, which on average pays taxes of between 3.5 percent and 4.5 percent, and it would be subject to the new 12 percent standard. This is the most controversial provision in the package, and industry associations are mounting a vigorous defense against it. An important complementary measure to offset the increased costs would be to reduce payroll taxes. Economy Minister Paulo Guedes has said this reduction could be made possible by the introduction of a new tax on digital transactions—the 'new CPMF.' This proposal is proving

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TODAY'S NEWS

POLITICAL

Opposition Parties Vow to Boycott Venezuela Election

Venezuela's main opposition parties vowed to boycott the country's planned Dec. 6 legislative election, saying President Nicolás Maduro's party has rigged the vote.

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BUSINESS

Facebook Follows Brazilian Judge's Order to Block Several Accounts

Facebook announced that it had complied with a Brazilian judge's order to block the accounts of 12 supporters of President Jair Bolsonaro who are under investigation for allegedly running a misinformation network.

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POLITICAL

Ali Inaugurated in Guyana Amid Long Legal Battle

Mohamed Irfaan Ali was sworn in as Guyana's president after he was named the winner of the country's March 2 election.

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Ali // Photo: People's Progressive Party/Civic.

POLITICAL NEWS

Venezuela Opposition Parties Vow to Boycott Election

Venezuela's main opposition parties said Sunday that they will boycott the country's legislative elections, planned for Dec. 6, saying that President Nicolás Maduro's government has rigged the vote and that participating in the elections would only result in them taking part in the "dictatorship's strategy," Reuters reported. "Venezuela, a nation undergoing a humanitarian crisis that is also subjected to a criminal, oppressive dictatorship, deserves free, democratic and transparent elections," the 27 parties said in a statement posted on the website of the opposition-controlled National Assembly. The parties include the Popular Will party of opposition leader and National Assembly President Juan Guaidó, who has recognition from dozens of countries as Venezuela's legitimate interim president. The parties that signed on to the statement also include Justice First, Democratic Action and A New Era, which, along with Popular Will, are collectively known as the G4. The announcement followed a move by the country's Supreme Court, which is loyal to Maduro, to name directors to Venezuela's

electoral council and also to appoint politicians widely believed to be Maduro allies to leadership roles at the main opposition parties. [Editor's note: See related [Q&A](#) in the July 20 issue of the Advisor.]

Ali Inaugurated in Guyana After Being Named Winner

Opposition presidential candidate Mohamed Irfaan Ali was sworn in as Guyana's president on Sunday after the country's electoral commission named him the winner of the March 2 election, The New York Times reported. The commission said Ali had defeated incumbent President David Granger by slightly more than 15,000 votes, or just more than 3 percent. Ali took office after a protracted legal battle, a 100-day recount of ballots and accusations of fraud against the country's two major political parties. Granger vowed to challenge the results in court and said Sunday that he "cannot endorse a flawed report," The New York Times reported. Granger has said a quarter of the votes cast showed signs of irregularities. However, at least four major organizations of international observers have endorsed the results. In taking office, Ali vowed to unify the country. "There is only one future, and that future requires a

NEWS BRIEFS

Argentina's Fernández Scraps Plans to Nationalize Vicentin

Argentine President Alberto Fernández said Friday in a tweet that he has scrapped plans to take over bankrupt soy producer Vicentin, Reuters reported. The statement came after a local judge partially blocked the move. In June, Fernández said his government would "rescue" Vicentin after the company went bankrupt last year, an announcement that sparked criticism by farmers and industry leaders who saw it as meddling in the private sector. "We have repealed the decree that ordered the intervention of Vicentin," Fernández said. [Editor's note: See related [Q&A](#) on the June 22 of the Advisor.]

Guatemalan Supreme Court to Hear Allegations Against Vice President

Guatemala's Supreme Court announced on Friday that it had accepted a request for a hearing in a case involving allegations that Vice President Guillermo Castillo abused his power in a recent personnel appointment, Reuters reported. Congress must now form a committee of lawmakers to discuss whether to remove Castillo's immunity from criminal proceedings, which would require a vote in the legislative assembly and could take at least a month. President Alejandro Giammattei defended Castillo in a statement on Friday.

Colombian Central Bank Cuts Key Interest Rate by Quarter Point to 2.25%

Colombia's central bank on Friday unanimously lowered its benchmark interest rate by 25 basis points to 2.25 percent, Reuters reported. With the latest cut, policymakers have lowered the key rate by 200 basis points since March. The central bank also said it expects a sharper contraction this year, of between 6 percent and 10 percent, amid the Covid-19 pandemic.

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highly controversial as it would hold online platforms responsible for the collection of taxes for any goods bought and sold on their sites by third parties. Former central bank president Ilan Goldfajn cautions that this 'new CPMF' could undermine the central bank's effort to promote digital payments. There are indications that Brazil's Congress wants to tackle a more comprehensive reform that encompasses municipal and state-level taxation. It is very likely that this proposed bill could be altered or merged with other bills. The timeline for approving any tax changes could also be delayed due to the local government elections scheduled

for November, given the diverging interests of municipalities, states and the federal government in tax revenue allocation."

A **Silvio Cascione, director for Brazil at Eurasia Group:** "Tax reform has been an issue for decades in Brazil, but this time is different. And not because of Guedes' proposal, but first and foremost because of unprecedented consensus in Congress and among state governors, who are pushing for a much more ambitious overhaul. While Guedes has proposed merging just two federal taxes, most party leaders and governors

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united Guyana," he said, Reuters reported. The election followed the start of oil production off Guyana's coast by a consortium led by ExxonMobil, a development that promises to transform the country's economy.

Mexico Has World's Third-Highest Covid-19 Death Toll

Mexico on Friday became the country with the world's third-highest death toll from Covid-19, behind only the United States and Brazil, the Associated Press reported. More than 47,700 people have died in Mexico from the disease, although local authorities have previously suggested the real number might be much higher than those reported. Mexico surpassed the United Kingdom, which has registered 46,286 deaths related to the novel coronavirus. Mexico's population is twice that of Britain. Also on Friday, 10 Mexican state governors from opposition parties criticized President Andrés Manuel López Obrador's government for its "confusing messages" on measures to curb the spread of Covid-19 and called for the resignation of Assistant Health Secretary Hugo López-Gatell, who has overseen Mexico's response to the pandemic, BBC News reported.

BUSINESS NEWS

Facebook Complies With Brazilian Judge's Order to Block Pages

Facebook announced on Saturday that it blocked the accounts of 12 supporters of Brazilian President Jair Bolsonaro who are under investigation for allegedly running a fake news network, in accordance with a Brazilian judge's order, the Associated Press reported. Supreme Court Justice Alexandre de Moraes on Friday night said that the social media company had failed to fully obey a previous ruling that ordered the shutdown of the accounts, saying they were still online and publishing by

THE DIALOGUE CONTINUES

Will Peruvians' Access to Health Care Improve?

Q **Peru's government has reached a deal with private clinics to set a fixed price for the treatment of Covid-19 patients who require intensive care, as the Andean nation struggles with one of the world's worst coronavirus outbreaks. To what extent and in what ways has the pandemic laid bare existing inequalities in Peruvian society, especially in terms of access to health care? How should Peru's social safety nets and health care systems be fortified, and why haven't previous governments been able to achieve that goal? Is the pandemic likely to provide impetus to address such weaknesses, or will tightened budgets amid the economic crisis prevent any significant improvements?**

A **Pedro Francke, Peruvian economist, research and consultant on poverty, health and social policies:** "High-income sectors in Peru have privileged access to private clinics through direct payment or private insurance, and the government has not effectively addressed public health. Moreover, the rural highlands, some of the country's poorest areas, have had very few Covid-19 cases, but Amazonian Indigenous people and Amazonian populations in general have had very high rates of infection and mortality amid the slow response of the health care system. The first necessary and most important thing to strengthen the health

system is a public budget. Additionally, it is necessary to unify a fragmented health system, improve the management of hospital investments and emphasize primary health care. The same can be said about social protection programs, which are a collection of fragmented, disjointed programs with little coverage. Again, the main problem is the lack of a budget. It is also necessary to articulate a true social protection system. Extremely urgent is a system of 'universal income,' or economic support to families in poverty, which in Peru has been called the 'universal bond,' especially in cities where there has never been a program of this type. In the immediate term, the government has expanded the budget for health, but it is unknown which policy will continue in 2021 and thereafter. The pandemic has brought economic crisis and with it a strong drop in tax collection, but fiscal savings and reserves allow Peru to sustain large fiscal deficits for several years. The current and the next government could and should expand public spending as part of a reactivation policy, and within this policy, investment in health and expansion of emergency social support measures, which could lay the foundations for a social protection network."

EDITOR'S NOTE: The comment above is a continuation of the Q&A published in the July 23 issue of the Advisor.

changing their registration to locations outside of Brazil. In a statement, Facebook said it complied due to a threat of criminal liability for an employee in the South American country, but it called the order "extreme" and said that it is a "threat to freedom of expression outside of Brazil's jurisdiction and conflicting with laws and jurisdictions worldwide." Facebook also said it would appeal to the full court. It added

that it had complied with the previous order by "restricting the ability for target pages and profiles to be seen from IP locations in Brazil." Last month, Facebook suspended a network of social media accounts that it found to have been spreading divisive political messages online by employees of Bolsonaro and two of his sons, Reuters reported. [Editor's note: See related [Q&A](#) in the July 2 issue of the Advisor.]

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are calling for the unification of five taxes, federal and local, into a single national value-added tax. That would be a revolution for Brazilian companies, as it would drastically reduce compliance and litigation costs and, above all, would encourage firms to invest where they can be more productive—and not where they can get more generous tax incentives. There are many reasons for such a consensus, but years of economic crises have certainly played a role. Few are taking advantage of the status quo, and most political actors and companies are interested in a structural reform. One important obstacle is that services companies would pay more taxes under the proposed VAT system, but lawmakers and Guedes are negotiating payroll tax cuts to offset that. And some other changes are likely to come in the package, such as taxation on dividends, for example. Given the stronger political support for an ambitious reform, Guedes' draft is very unlikely to be voted as it is; instead, Congress will probably blend it into a broader constitutional amendment that has been under discussion since last year. Approval is likely in 2021, but implementation of the new system will take much longer, so companies can adapt to the new system; under the current draft, the full transition into the new VAT would take 10 years."

A **Beatrice Rangel, member of the Advisor board and director of AMLA Consulting in Miami Beach:** "As it stands now, the Brazilian tax system is set up for evasion. Arcane and opaque regulations cheapen the cost of evasion, but if you want people to pay their taxes, the cost of evasion must be very high. According to the Financial Times,

it takes a typical U.S. company 100 work hours to file a tax return, while it takes a typical Brazilian company 2,000 work hours. In Brazil, the tax space is cluttered with laws, provisional measures, decrees, ordinances and other forms of regulation. This makes

“As it stands now, the Brazilian tax system is set up for evasion.”

— Beatrice Rangel

financial planning quite difficult for businesses. This tax labyrinth was created by the 1988 Constitution, which aimed to secure financial independence for municipalities and states. Instead, it has created powerful incentives for evasion as it is easier and cheaper to evade taxes than to comply with this regulatory kaleidoscope. More than three decades later, we have tax wars among states, excessive ancillary tax legislation and tax litigation, as well as sparse and subjective tax legislation. Minister Paulo Guedes' proposal is to simplify taxation through merging several sales taxes into a single indirect tax at the federal level. Five indirect taxes on consumption (ICMS, IPI, ISS, PIS and Cofins) would be consolidated into a new tax on goods and services, or IBS. This is the first, correct and fitting step toward introducing simplicity and clarity into Brazil's tax system. There is still much to do at the state and municipal levels, but every journey begins with the first step."

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