

5 Venezuela

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I. Introduction

Located on the northern part of South America, the Bolivarian Republic of Venezuela is a tropical country with 2,813 kilometers of coast in front of the Caribbean Sea. Covering an extension of 916,445 square kilometers of territory, Venezuela, as it is usually called, includes 72 federal dependencies, 23 states, 2 federal territories and one Capital District. The border countries are: from the west, Colombia, Brazil to the south and Guyana to the east. This geographic position makes this country privileged by its strategic location in respect to Europe, Africa and Central and North America. Rich in natural resources such as: oil, bauxite, hydropower, and others, this country enjoys different kinds of weather due to the variety of environments and altitudes, such as: rainforest, mountains, llanos (flat lands) and valleys.

Venezuela is considered a developing country with a population around 26 millions, mainly concentrated in major cities and their suburbs. That population is allocated by a typical pattern of movement from rural to urban zones, within a very slow decentralization process that is not constant. Though, the official language is Spanish, inherited by the Spanish colonization, there are still preserved some native languages in remote indigenous towns.

A. Political and Economic Background

At the beginning of 1990s, Venezuela was in the middle of the second administration of President Carlos Andres Pérez. During his first period Venezuela experienced a sudden increase of its oil revenue because of the extraordinary growth of the international prices that occurred since the decade of the 70s. It is also worthwhile to mention that during that period Venezuela's debt was held at most and showed a sustained increasing trend. This means, that Venezuelan people expected to get a good economic situation as well as experienced in the boom of oil revenue though during both periods of President Perez the government allowed a marked level of administrative corruption.

However, during the second term of President Perez a lot of economic reforms recommended by the International Monetary Fund (IMF) were undertaken and rapidly economic growth was recovered. Nevertheless, because of the attempt to bring down the government in 1992 (*coup d'état* leaded by the current President of the country), the economy turned over in a steady decrease of its Gross Domestic Product (GDP) mainly caused by the lost of business confidence originated by the uncertainty climate associated with the *coup d'etat*.

Since 1994, during the administration of President Rafael Caldera, Venezuela experienced strong economic recession which mainly happened, because the international oil prices went down tremendously. Actually, the oil price for the Venezuelan revenue dropped around 9 US\$/per barrel for a long period. Of course, that administration did not apply accurate policies in order to stop GDP decreasing trend, for example, reducing public expenditure. Indeed, this government was also invaded by many cases of corruption including one exchange controlled system (OTAC), which has been commonly good ground for Venezuelan politicians for mismanagement. As it could be expected, all of this led to a high fiscal deficit level as percentage of GDP.

Later, during the first year of President Caldera's administration, when it was created the Venezuelan Tax Administration, the country starts to develop a more complex tax system to get

revenue from another source different than hydrocarbons. Then, the Venezuelan Tax System was expanded rapidly to attend the recession held at that time.

Furthermore, that government reformed the legal basis of the hydrocarbons' exploitation, which has been called "the oil market opening", that allowed foreign direct investment toward this sector. Therefore, the new tax administration and the reform of the Venezuelan Income Tax Law during that administration made possible to increase the level of fiscal revenue.

The current administration was elected in 1998. It has had mainly political issues in his agenda, as the enactment of a new Constitution in 1999, and some other laws. Because of political differences, the current administration has been engaging in some conflicts with many sectors of society, especially entrepreneur private sector. It has been carrying out welfare programs to support Minister's duties and contribute to slow down unemployment.

Without getting good results, the administration has experienced large political-social problems during the last years. In the meantime, Venezuela has received the largest oil revenue ever had during the recent past, but according to specialists, they have not been invested in making the GDP to increase. On the contrary, there have been enforced some measures that are severely criticized by them.

B. Brief History of the Venezuelan Tax System

As Venezuela always received huge income derived from oil exploitation, the country did not promote a large fiscal policy. The first relevant fact in the contemporary time is in 1942, when it was enacted the first Income Tax Law to be enforced the first day of next year, which thereafter joined oil revenue as the largest sources of income.

Up to end of the 80s, Venezuela was structured by income tax, and some others minor taxes such as: excise taxes, stamp duties, property tax, business license tax, controlled by the Central Government in a centralized administration that did not have tax administration as separated organization; and tolls, Social Security's contribution and others, which were not administered as the rest of taxes by the Ministry of Inland, as used to be called the current Ministry of Finance.

Adding a lot of reforms issued on each version, The Venezuelan Tax System had enactments of new income tax laws, for example in 1948 had a version that used to be enforced by classifying economic activities; 1967, which included new topics such as sanctions, fiscal control rules, expirations, among others; and 1978, which finally established the principle of nature and juridical persons as taxpayers applied nowadays.

Nevertheless, ending that decade and most of the 90s, the oil prices dropped dramatically. Therefore, Venezuela starts developing a complex tax system rashly to attend the need of finance arisen at that time. For example, in 1989 it was proposed a Value Added Tax, which was finally enacted in 1993, but abolished and replaced after only one year.

Bring forward, the World Bank and the Venezuelan Government established a project to build on a tax administration. The successful project ended up to develop, after certain modifications in its name and expansion of functions that included the merger of the Customs Administration, the current National Integrated Service of Customs and Tax Administration "SENIAT" (the abbreviation in Spanish).

Nowadays, this tax administration has carried out many reforms and new taxes, as well as the strength in the enforcement of tax collection. Indeed, one of the core issues in the country nowadays is the tax system, which has been subject to be criticized at most while has been the pride of the Venezuelan tax collectors, in the middle of a difficult economic atmosphere.

Table 1 Brief Data about Venezuela

Capital	Caracas (District Capital)
Main Cities	Maracaibo, Valencia, Puerto La Cruz, Barquisimeto, San Cristobal, Maturin, Puerto Ordaz
Literacy	92.9% total (2002 est.)
Religions	Nominally Roman Catholic 96%, Protestant 2%, other 2%
Life Expectancy	76.6 male, 73.7 female (2002 est.)
% Per Sex	50.2 male, 49.8 female (2003 est.)
Currency	1 Bolivar (Bs) = 100 centimos (centimes)
GDP (per capita)	\$10,273 (2003 est.)
Industry	Petroleum, iron ore mining, construction materials, food processing, textiles, steel, aluminum, motor vehicle assembly
Agriculture	Corn, sorghum, sugarcane, rice, bananas, vegetables, coffee; beef, pork, milk, eggs; fish
Arable Land	4%
Natural Resources	Oil, natural gas, iron ore, gold, bauxite, other minerals, hydropower, diamonds

Source: National Institute of Statistics (INE) and http://go.hrw.com/atlas/norm_hm/venezuela.htm

Table 2 Population by Federal Entity, 2000-2004

Federal Entities	2000	2001	2002	2003	2004
Total	24,310,896	24,765,581	25,219,910	25,673,550	26,127,351
Capital Distric	2,046,193	2,051,427	2,056,875	2,062,544	2,068,268
States:					
Amazonas	116,013	119,564	123,228	127,009	130,805
Anzoátegui	1,293,687	1,323,655	1,351,648	1,377,527	1,403,141
Apure	404,634	414,107	423,471	432,700	442,345
Aragua	1,494,248	1,520,060	1,545,092	1,569,304	1,593,463
Barinas	643,229	660,007	676,395	692,348	708,359
Bolívar	1,319,453	1,351,520	1,383,204	1,414,453	1,445,310
Carabobo	1,971,544	2,009,117	2,046,330	2,083,141	2,119,677
Cojedes	257,721	263,696	269,766	275,939	282,092
Delta Amacuro	128,039	131,557	135,067	138,564	142,077
Falcón	790,375	805,743	821,393	837,332	853,334
Guárico	649,676	662,714	675,975	689,475	703,145
Lara	1,591,604	1,620,962	1,650,150	1,679,144	1,708,172
Mérida	734,894	748,786	763,700	779,684	795,708
Miranda	2,519,557	2,568,739	2,618,411	2,668,578	2,717,742
Monagas	725,319	744,615	763,643	782,357	800,921
Nueva Esparta	382,580	391,106	399,388	407,398	415,187
Portuguesa	760,875	776,090	791,628	807,509	823,628
Sucre	827,428	838,840	850,777	863,255	876,080
Táchira	1,033,743	1,053,026	1,072,867	1,093,293	1,113,962
Trujillo	626,318	637,343	648,818	660,775	673,011
Vargas	318,043	319,904	321,879	323,966	326,118
Yaracuy	516,010	527,183	538,583	550,220	561,959
Zulia	3,158,126	3,224,204	3,289,979	3,355,368	3,421,156
Federal Dependencies	1,587	1,616	1,643	1,667	1,691

Source: National Institute of Statistics (INE)

II. Overview of Macroeconomic Activity and Fiscal Position

Looking some years back, members of the Organization of the Petroleum Exporting Countries (OPEC), including Venezuela, decided to recover the oil prices' control by reducing the production quotas per country. This measure induced to reduce the Venezuelan oil revenue, but it was partially offset by the raise in the price of the commodity during 2002. Therefore, adding this fact to the President's fake resignation in that year, and an expansive policy of expenditure carried out by the Central Government, provoked some major consequences:

- Lack of fiscal revenue to confront the expenditure and increasing in public borrowing

- Lack of efficiency among the public sector due to the environment of uncertainty
- Steady political conflicts, legally and physically, that affected commerce and regular activities

Hence, GDP decreased 8.9% comparing to the prior year and the inflation rate doubled its level up to 31.2%.

One year later, the GDP decreased 9.4%. From December 2002 to February 2003, the country crossed difficult times by having many industries and workers enrolled on a national strike, including the national oil company, *Petróleos de Venezuela S.A. (PDVSA)*, which ended up in a truly disaster for the economic situation demonstrated in the falling of both oil and non-oil sectors' performance.

In the meantime, it was imposed an exchange control system derived from a capital drain happened during the confused atmosphere of the national strike. That decision has become in the most important influence in the economic performance of the whole 2003 and 2004, and it is forecasted to be forced for a long time. Since March 1998 (next month to the appointment of the current administration) to six years later in the same period, the exchange rate has devaluated in 72.9%.

Moreover, in 2002 the aggregate demand decreased, because the reduction on the exports. However, the domestic transactions included in this aggregate slowed down to rise, which contributed to stop the falling. In addition, the total domestic investments decreased in 38.9%, which intervened to reduce the demand of employment that also had a difficult year by keeping a decrease to 16.8% in average. The latter, affected most the labor market and the behavior of economically active people to flock to the informal sector of the economy.

It is worthwhile to mention that from 2002 to the end of 2004 and bring forward, there is a labor regulatory which avoid firing personnel. That measure has been used by Venezuelan governments during difficult times of employment or a new raise of minimum wage level in the past. However, to this extent the length of the current regulatory has harmed the entrepreneurial sector and the economy at all, and in the long term too.

At that time, the Balance of Payments accounted a surplus of US\$ 5.443 million, therefore the international reserves increased rapidly dropping behind the risk of the foreign capital drain happened. However, those reserves have been subject to be in discussion in terms of a requesting of the exceeding of oil revenue and exchange surplus, made by the administration to be applied in welfare purposes.

Regarding to Trade, both exports and imports decreased in 2003, in 3.4% and 21.4% respectively. Basically, they were negatively influenced by the exchange control levied. Nevertheless, the exchange control system affected imports much more due to the statutory imposed under this system. It is expected a better performance on these operations as a consequence of certain deregulation in the exchange control system applied in 2004.

A huge expansion in the public sector's monetary balance gathered, because the accumulation of funds derived from the constraint framed by the exchange control system. In addition, M1 and M2 increased in 74.7% and 57.5%. As the monetary policy in Venezuela is controlled by the Central Bank, this institution had to intervene in the market to constraint exceeding liquidity, using their open market securities. In that sense, the level of money absorptions increased, thus the level of money injections decreased.

Furthermore, the Central Bank of Venezuela (BCV) and the Central Government made an agreement after April 2002 to ensure the "economic stability", in which the BCV was assigned to support the monetary policy through emphasizing their public borrowing operations and monitor the money base at all.

On the other hand, there was a slight improvement in the government finance as public sector consolidated during 2003, which gathers the Central Government plus PDVSA, sampling of non-financial public entities, the Social Security Pension Fund (IVSS), the Deposit Guarantee Fund (FOGADE) and Investments Fund of Venezuela (FIV). Nevertheless, the Central Government

examined alone increased its expenditure significantly and has carried out this increase in a sustained position of expansion within the whole term of the administration.

As fiscal policy, the Administration established a fiscal policy aimed to solve the instability created by the events ending 2002, so it was implemented a strategy called “Measures for Eventuality 2003”. This strategy was basically composed by the following aspects:

- Focus on managing the public debt, especially domestic one, by modifying the yield of the Government Securities.
- The creation of a new law, the Macroeconomic Stabilization Fund (FEM), to abolish the others related to it, which regulates the transfer of resources to the FIV and other funds, including the amount of oil revenue above the stipulated in the National Budgetary Law that the administration may use for different purposes.
- The reform of one of these funds, the Macroeconomic Stabilization Investment Fund (FIEM) was done to give more availability of resources to the Government.

Furthermore, the administration through the SENIAT start an intensive policy of tax collection that has been strongly criticized by many sectors, however, it has achieved to increase the level of collection in 2.19% of GDP for 2003.

II.1 Macroeconomic Activity

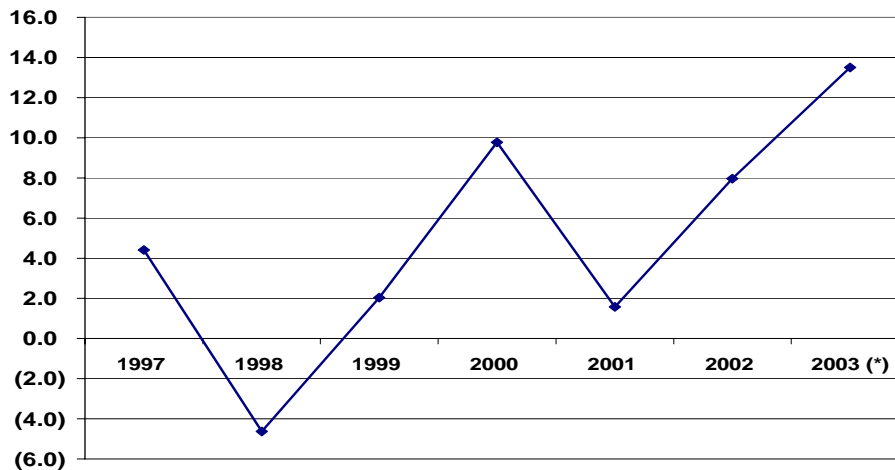
A. International Environment

The impact of the supply exceeding, the shrink experienced by the Venezuelan economy at the beginning of 2003, plus the exchange controlled system, ended up in a surplus in the total sum of the Balance of Payment of US\$ 5.443 million (5.4% of GDP) in that year. On the contrary, in 2004 this trend shows to go down, because the conditions of repression of operations that ended up in a stiffly growing of GDP for the last quarter of the prior year, are much more standardized, and the provisional amount in 2004 up to the second quarter is US\$ 1.902 million.

Current Account Balance

In 2003 the Current Account Balance made a surplus of US\$ 11.524 million that was used to reduce the level of deficit in the capital and financial account and the net errors and omissions account. The surplus mentioned means 13.5% of GDP, and derives from a favorable performance of exports comparing to imports, because of the shrink in the exchange system, which reduced the costs related to the exchange operations.

Figure 1 Current Account as percentage of GDP



Source: Central Bank of Venezuela (BCV)

Exports

Exports were affected mainly by the events occurred during 2003, first the exchange control system and the stagnation of the national oil industry, which were the outcome of the national strike, and the raise in the international oil prices. Despite of exports slightly increased in terms of percentage of income in 0.3%, both oil and non-oil exports decreased in the operations carried out that year, for a total of US\$ 26,861 million. Indeed, though the level of oil exports decreased, the total revenue accounted is US\$ 22,052 million for an increase of 2.4%, due to oil prices.

For non-oil exports it was different, the total amount was US\$ 4,809 million for a decrease of 8.4%, as the most affected. However, referring to sectors in general, the level of exports experienced many slight variations.

In 2004, non-oil exports increased up to 4,636 comparing to the prior year.

Table 3 Exports 2003-2004 by Sectors of the Economy

Sector	Million US\$ 2003	2003 (%)	Million US\$ 2004	2004 (%)	% Variation
TOTAL	3,202	100.00	4,636	100.00	44.80
AGRICULTURE (Vegetable)	73	2.30	98	2.10	33.70
FOOD INDUSTRY		-		-	-
BEVERAGES AND TOBACCO	109	3.40	98	2.10	-10.00
MINERAL PRODUCTS (1)	464	14.50	1,007	21.70	116.90
CHEMICALS	483	15.10	701	15.10	45.10
PLASTIC AND MANUFACTURING	88	2.70	151	3.30	71.50
METALS (2)	1,290	40.30	1,866	40.30	44.70
ELECTRIC GOODS	152	4.70	156	3.40	2.50
TRANSPORTATION GOODS	333	10.40	319	6.90	-4.20
OTHERS	210	6.60	241	5.20	14.80

(1) Exclude exports of oil and iron from the public sector., (2) Manufacturing of smelting of iron, steel, copper, nickel, aluminum, plumb, zinc, tin, and their manufacturing, including tools made of them

Source: National Institute of Statistics (INE)

Imports

Apart from the traditional impact caused by the imposition of a controlled regime of exchange, imports were mostly affected by the delay and inefficiency in granting foreign currency to many economic sectors during 2003. In a country that has a huge dependency on non-oil imports, there was certain lack of supply in many massive consumption goods that was seen along the complete

year. As a whole, imports dropped in 22.6%. Of course, private imports were mostly affected, around 30% (according to BCV), and non-oil imports decreased larger in 25.9% comparing to oil imports that experience certain increase.

According to data collected by the Central Bank of Venezuela, the Commission of Currency Administration (CADIVI) as the bureau that manages the exchange regulated system, achieved to grant 31.4% of the private-foreign-currency requirements of 2003 only, which ended up in a low level of imports. Actually, the effect of reduction in the services' account of the balance of payments for this year is attributed to the reduction of spending in shippers and insurance companies for imports. Later on, imports have not recovered in 2004, on the contrary they have decreased again in US\$ 189 million, but they have barely improved in terms of importers in getting foreign currency to carry out operations.

Both cases, exports and imports data do not match between National Institute of Statistics (INE) and BCV, because some adjustments are made to the balance of payments.

Table 4 Imports 2003-2004 by Sectors of the Economy

Sector	Million US\$ 2003	2003 (%)	Million US\$ 2004	2004 (%)	% Variation
Total	4,784	100.00	8,750	100.00	82.90
Agriculture (Vegetable)	398	8.30	588	6.70	47.70
Food Industry & Beverages and Tobacco	410	8.60	705	8.10	72.00
Others	462	9.70	891	10.20	92.90
Paper	226	4.70	354	4.00	56.60
Plastic and Manufacturing	303	6.30	496	5.70	63.70
Mining	134	2.80	202	2.30	50.70
Chemicals	895	18.70	1,508	17.20	68.50
Metals (2)	295	6.20	621	7.10	110.50
Electric Goods	1,155	24.10	2,224	25.40	92.60
Transportation Goods	506	10.60	1,161	13.30	129.40

Source: National Institute of Statistics (INE)

Exchange Controlled System

From January 2003, the current administration started a new exchange controlled system that was imposed, as a result of the excess in foreign currency transactions that were affecting enormously the international reserves, as consequence of the national strike. The Currency Administrative Regime (RAD) stopped dramatically the free exchange system managed before, imposing fixed exchange rates for selling and buying in a discretionally system to grant foreign currency, which worked for corporations and organizations at first stage only and included many requirements and documentation.

The exchange rates at closing 2004 are: 1,915.20 Bs/US\$ for selling and 1,920.0 Bs/US\$. When RAD begun, it enforced exchange rates of 1,596 Bs/US\$ and 1,600 Bs/US\$ respectively, so based on the trend and the rate included in the National Budgetary Law, it will be raised to the first quarter 2005. The new rate is estimated in 2,150 Bs/US\$.

Because of the search of investors implemented by the current administration, CADIVI has been releasing progressively the system to ease other sectors and natural citizens to get access to the exchange, through steady reforms carried out lately.

Capital and Financial Account

There is a substantial reduction in the capital and financial account of US\$ 4.108 million in 2003 which is mainly caused by the lack of private outgoing capital in that year. That reduction is equivalent to 3.5% of GDP, and a significant reduction of 4.3% of GDP (US\$ 5,135 million) comparing to the previous year. Despite of the trend of outgoing capital in the country that has

been around 5%, there is a relevant decrease since 2002, which is carried out by the intensive uncertainty for the changes held by the Government, and many political and social events that happened during that year. Nevertheless, because of the huge drops, 2004 shows a recovering for this account of US\$ 4.171 million for the first sixth months.

International Reserves

Regarding to International Reserves in Venezuela, it is important to point out the account of the FIEM, which is enforced by a law. Because there have had a constant underestimation of the oil price for the Venezuelan budget in respect of the increase in the recent past years, this fund obtained a bulk of unexpected revenue that should have been kept for earmarking purposes according to that law. However, the expanded expenditure policy carried out by the administration pushed the approval of a reform by the Parliament to get FIEM resources available for Government expenditure.

Right before the exchange controlled system was enacted, the quotation of the American dollar had raised to 1,853 Bs/US\$ and the exchange rate at closing 2002 was 1,403 Bs/US\$, thus it was experienced a depreciation of the local currency of 32.1%. Therefore, under a steady decrease in the international reserves by more than US\$ 600 million and no changes in the uncertainty produced by the conflicts it was unavoidable to establish an exchange regulation, otherwise it will not be possible to supply the foreign currency demand. In that sense, the stagnation in granting foreign currency and the operations of the national oil company make a surplus of 23.8% at the end of year in those reserves.

Part of the surplus in the International Reserves in 2004, received an unusual “withdrawal” required by the Central Government to develop welfare-agriculture programs, which explains the drop within the international reserves. Besides this measure has been bad seen by the specialists, the Administration still requires Central Bank of Venezuela to provide these funds, based on the boom of the oil prices, and the need to continue those programs.

Table 5 International Reserves (millions of US\$)

International Reserves	BCV	FIEM / FEM (1)	TOTAL (2)
2004 (*)	22,522	704	23,226
2003	20,666	700	21,366
2002	12,003	2,857	14,860
2001	12,296	6,227	18,523
2000	15,883	4,588	20,471

(1) FIEM: Macroeconomic Stabilization Investment Fund. Includes portfolio administered by BCV. On December 23, 2003, FIEM assets were transferred to the FEM (Macroeconomic Stabilization Fund) account., (2) Excludes the Investment Fund of Venezuela (FIV)., (*) First semester (provisional figures).

Source: Central Bank of Venezuela

Foreign Direct Investment

Total Foreign Direct Investment achieved in 2003 was US\$ 2,531 million which means at least three times the amount reached in 2002 of US\$ 779 million. This investment derived almost completely from foreign oil companies that invested after the period on stagnation of the national oil industry. Moreover, it should has been mentioned the concessions granted to U.S. oil companies directly that has allowed a large amount of FDI inward to Venezuela between 2003 and 2004.

In addition, the current administration is now “thirsty” of foreign-direct-oil investments as a policy, because non-oil investments are vaguely done due to the lack of confidence developed to the country. The Government’s policy enforced through several meetings held by the President in which has established new agreements with new countries such as China and Iran, as part of a

strategy. The estimation for 2004 reached US\$ 3.1 million establishes an increase which supports so.

Table 6 Foreign Direct Investment 2000-2003 (millions of US\$)

FDI - Flows	2000	2001	2002	2003
Inward	4,701	3,683	779	2,531
Outward	521	204	1,020	1,143
FDI - Stocks	2000	2001	2002	2003
Inward	6,975	26,944	31,710	34,241
Outward	3,918	5,766	6,807	7,950

Source: United Nations Conference on Trade and Development (UNCTAD)

External Debt

Since 1999, the administration of President Chavez has managed the treatment of the Venezuelan External Debt. It has been traditional to be refinancing the terms of external debt, due to the low income, for example in the early 90s, when oil prices had dropped dramatically. As a matter of fact, most of the period of this administration, and despite of period on strike mentioned above, oil prices has been upper the budget's assumption which has allowed to carry out slightly better the external debt of the country. Nevertheless, this is only applied to the Government's short term debt, but in the long term debt, it is clearly noticed the trend of increasing from 2002 that is US\$ 20,182 million in the third quarter 2004.

Some experts forecast that whether the country maintain the level of revenue and do the right thing with the liabilities during 2005, the total external debt could be reduced up to US\$ 29.2 million.

Table 7 External Debt IV Quarter 1998-III Quarter 2004 (million of US\$)

Total External Debt 2/	IVQ-1998	IVQ-1999	IVQ-2000	IVQ-2001	IVQ-2002	IVQ-2003	IIIQ-2004(*)
	35,087	37,016	36,437	35,398	35,114	38,043	37,752
Short Term	8,536	7,427	8,127	7,776	6,584	7,899	8,739
Monetary Authority	107	49	55	73	55	66	106
Government (as a whole)	724	695	809	794	737	634	590
Finance	250	242	416	567	280	201	244
Oil sector	1,494	1,224	1,060	646	967	842	846
Non-oil Sector	5,961	5,217	5,787	5,696	4,545	6,156	6,953
Long Term	26,551	29,589	28,310	27,622	28,530	30,144	29,013
Monetary Authority	1,360	855	305	88	76	57	50
Government (as a whole)	13,799	15,550	14,646	14,477	15,562	17,955	20,182
Finance	58	35	50	51	49	32	32
Oil sector	5,599	7,890	8,250	8,838	9,114	9,088	6,045
Non-oil Sector	5,735	5,259	5,059	4,168	3,729	3,012	2,704

1/ Drawn up according to the guidelines of the fifth edition of the Balance of Payments Manual of the IMF., 2/ Include Reserve Liabilities and debt with related and non-related entities., (*) It is not value at closing, belongs to third quarter
Source: Central Bank of Venezuela (BCV)

Aid

Venezuela, as the fifth oil exporter and a country among the five largest oil reserves worldwide and its potential of development, catches the attention of multilateral organizations. This country has a good position to receive financing by these organizations. Nevertheless, Venezuela receives huge aid to fight against poverty (in Venezuela more than 60%) and remarked social problems such as clean water, housing, health, education and so on. Despite of it is deemed as rich country of natural resources, its revenue has been vaguely invested in well infrastructure.

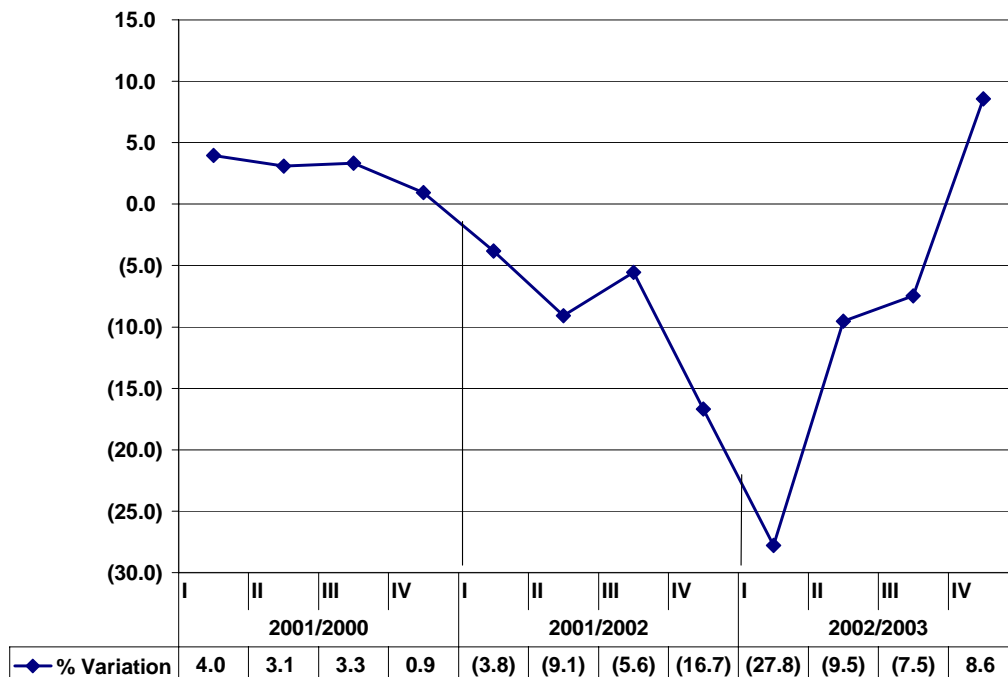
B. Domestic Environment

In principle, it must be pointed out that jointly to the effect produced by the imposition of an exchange controlled system, the economic environment is also experiencing a price controls in many items that has derived from the protectionist policies after the events occurred during the last 2 years. Those facts become the axis of many distortions experienced within the Venezuelan economy.

Economic Growth based on GDP

The Venezuelan economy performance, in terms of GDP from 2001 to 2003 clearly shows that it shrank twice, especially in 2002 because of the political conflicts regarding to the national strike, the announcement of the President Chavez's resignation by the highest army officer at the end of the first quarter of the year, in which GDP decreased 27.8%, among others; raised uncertainty rapidly. Though, the other quarters behaved in the opposite way, because of the delays on oil exports and the increasing in demand of this product, that surplus did not achieve to restate the GDP. As a result, the total variation was 9.4%.

Figure 2 GDP Quarterly Variation in Percentage 2001-2003 (Base on prices = 1984)



Source: Central Bank of Venezuela (BCV)

Table 8 Gross Domestic Product 1995-2003, at Current Prices (millions of Bs)

TYPE OF ECONOMIC ACTIVITY	1995	1996	1997	1998	1999	2000	2001	2002 (*)	2003 (*)
PETROLEUM ACTIVITY	2,367,190	7,778,329	8,755,039	6,422,505	9,916,209	18,688,206	15,355,915	24,102,354	33,729,919
Oil and Natural Gas	1,979,387	6,332,690	7,002,229	5,030,042	7,972,304	15,493,599	12,711,406	20,481,316	29,567,575
Refining activities	387,803	1,445,639	1,752,810	1,392,463	1,943,905	3,194,607	2,644,509	3,621,038	4,162,344
NONPETROLEUM ACTIVITY	10,533,983	19,925,034	31,457,171	42,233,708	48,623,765	59,200,440	70,596,069	80,783,209	96,080,700
Goods Production	3,670,543	7,081,640	10,375,746	13,225,347	13,821,990	16,088,177	19,068,338	21,824,528	25,450,276
Agriculture	712,857	1,244,088	1,786,247	2,461,132	2,880,633	3,258,018	3,872,766	4,549,229	5,813,001
Mining	113,970	284,548	357,839	382,101	349,014	424,146	500,689	795,613	1,037,772
Manufacturing	1,949,615	3,780,337	5,153,115	6,071,218	6,260,637	7,426,917	8,307,558	9,362,443	11,758,850
Electricity and Water	252,575	391,088	652,709	867,868	931,608	1,137,058	1,355,214	1,794,510	2,233,250
Construction	641,526	1,381,579	2,425,836	3,443,028	3,400,098	3,842,038	5,032,111	5,322,733	4,607,403
Service	7,478,956	13,582,563	22,157,789	30,923,517	36,598,262	44,963,906	53,618,937	61,502,257	74,144,887
Commerce	1,940,893	3,518,387	5,082,918	6,388,685	6,848,468	8,189,305	9,641,817	10,359,922	12,964,708
Restaurants and Hotels	538,200	990,676	1,613,635	2,386,929	2,946,515	3,499,211	3,835,530	4,373,467	5,246,904
Transport, Storage and Communications	1,056,769	2,158,001	3,716,565	4,893,346	5,716,383	6,920,770	8,063,945	9,617,765	11,503,003
Financial Institutions and Insurance	667,124	789,451	1,072,901	1,764,165	1,482,077	1,702,899	2,304,478	2,810,666	3,762,291
Real Estate	930,993	1,858,394	3,028,515	4,084,101	5,061,841	6,191,093	7,476,201	8,723,926	10,164,020
Services Provided to Companies	511,511	935,108	1,476,515	2,050,557	2,580,637	3,108,816	3,559,450	3,860,338	4,299,535
Non-Profit-Making Private and Community, Social and Personal Services	1,111,158	2,276,570	4,090,252	6,367,388	8,583,508	11,104,358	13,165,416	15,646,071	19,704,809
General Government Services	722,308	1,055,976	2,076,488	2,988,346	3,378,833	4,247,454	5,572,100	6,110,102	6,499,617
Less: Imputed Banking Services	615,516	739,169	1,076,364	1,915,156	1,796,487	1,851,643	2,091,206	2,543,576	3,514,463
SUB-TOTAL	12,901,173	27,703,363	40,212,210	48,656,213	58,539,974	77,888,646	85,951,984	104,885,563	129,810,619
Plus: Import Duties	784,513	1,734,319	3,131,459	3,826,253	4,037,065	4,562,028	5,372,789	5,896,793	7,557,537
TOTAL	13,685,686	29,437,682	43,343,669	52,482,466	62,577,039	82,450,674	91,324,773	110,782,356	137,368,156

Source: Central Bank of Venezuela (BCV)

Consumer Price Index

From 2001 to 2004 the inflation rates based on the consumer price index are 12.3%, 31.2%, 27.1% and 19.2% respectively. As it is noticed, there is a steady decreasing; however since February 2003 there is a price control that covers around 50% of the products that determine the level of this index. Hence, the percentage of items out of the price control, which raised more the 1% in the inflationary core index, was 54.9%.

The behavior of consumer price index in 2003 is basically attached to the following:

- Lack of supply of the massive products, because of the price control established.
- Adjustments made on prices because of the exchange rate of the parallel market.
- The enforcement of VAT rate of 8% on certain goods exempted before.
- Particular hyperinflation among agriculture products

During 2004, the price controls stayed and 38.46% of the items decreased, due to the lack of consumption.

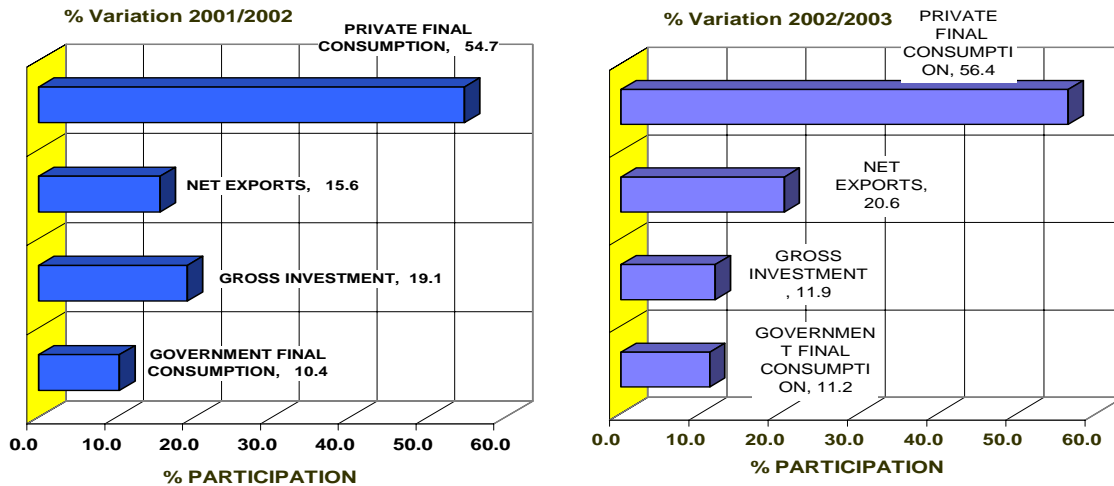
Consumption

Generally speaking the whole elements of the domestic aggregate demand dropped in 2003. However, among them consumption decreased slower than the prior year in both sectors, and also the delaying in getting goods and services in the last month of 2002 and the beginning of 2003 for the private sector. In fact, private consumption decreased 4.4% that is much higher than public, which was 1.3%, but the portion of private consumption is lighter than public.

Investment

The trend to drop held by domestic investment in Venezuela during 2002 (22%) and 2003 (38.9%) was tremendous. Nevertheless, this trend may slow down in 2004, in which the external element aggregate demand will be affected by the increasing in oil exports, around 160.9% up to the second quarter comparing to 2003 (the national strike finished on February 2004). Also, the cosmetic economic growth may influence because of the recovering in terms of GDP.

Figure 3 Consumption, Gross Investments and Net Exports 2001-2003 Variation %



Source: Central Bank of Venezuela (BCV)

Monetary Base

During 2003, the monetary base experienced a nominal increasing of 46.4%, which is larger than 18.9% accounted in 2002. This increasing is attributed to the monetary expand effect, within the exchange system controlled atmosphere, generated by the Central Government, PDVSA (national oil company), and a public financial institution BANDES (public financial institution created to finance projects to decentralize the country). However, this was not a steady trend during the year, due to the absorption operations carried out by the BCV, and in the contrary, the huge injection of income carried out by the institutions just mentioned.

The monetary aggregate M1 increased nominally in 74.7%. For M2, an increasing demand of financing by the Administration plus the increase of the monetary base ended up in a total expansion of the Liquidity in 57.5%.

Employment

The unemployment rate in Venezuela is one of the core points derived as a consequence of the general behavior of the economy during the last decade. This rate has increased constantly in total during that period, but it has emphasized since 2001. For 2003 the labor supply decreased more than the level of the demand side, which happened during the first semester due to the national strike. But later on, this became radically the opposite, and then plus the incidence of the shrink of the economy, the rate (16.8%) resulted higher than 2002. Many businesses did not recovered from this event, and the policy of control exchange and prices influenced them to close indefinitely. All this happened involved by a labor regulatory that avoid firing personnel.

Nevertheless, from 2003 the Government implemented some social welfare programs in education, health, and others that have attempted to reduce this trend, but that policy has not been enough to slow down unemployment more than 0.2%, because they have not achieved to boost the economy from the roots. Moreover, those programs as for “welfare”, does not contribute directly to the generation of goods and services to exchange.

Regarding employment there is also a core issue to point it out which is the informal employment rate within the Venezuelan labor market. This index overcomes 40% during the last decade. In fact, it has increased steadily since 2001 with 49.9% to 2003 with 52.7%, and taking the provisional data for 2004 shows that is still increasing. Whether this is not solved recovering the truth of entrepreneurial, it will be struggled to achieve a substantial change.

Table 9 Unemployment Rate Per Sector, I Semester 2001-I Semester 2004 (%)

Branch of Economic Activity	I Sem 2004 (*)	II Sem 2003 (*)	I Sem 2003 (*)	II Sem 2002 (*)	I Sem 2002 (*)	II Sem 2001 (*)	I Sem 2001 (*)
TOTAL	16.6	16.8	19.2	16.2	15.5	12.8	13.7
Agriculture, Hunting, Forestry and Fishing	7.7	7.9	8.7	9.0	8.4	6.8	7.0
Hydrocarbon, Mining and Quarry Exploitation Activities	24.4	21.2	27.0	12.5	15.2	9.9	8.8
Manufacturing Industry	15.0	15.3	18.4	15.1	14.9	12.0	13.7
Electricity, Gas and Water	8.3	13.1	16.3	10.8	11.5	11.8	15.9
Construction	29.3	28.6	37.3	27.6	27.6	21.6	25.1
Trade, Restaurants and Hotels	15.7	15.4	18.0	14.3	13.8	10.6	11.1
Transport, Storage and Communications	12.2	12.8	15.0	11.2	10.3	8.4	10.6
Financial Establishments, Real Estate and Services Provided to Companies	16.9	17.1	20.2	16.2	15.5	13.9	14.6
Community, Social and Personal Services	13.5	13.8	14.5	13.1	12.1	10.0	9.7

Notes: (*) The primary source of information is Statistics National Institute (INE) and its Household Survey performed by Sampling. From 1994 onwards, the sample's expansion is based on the projections derived from the definitive results of the 1990 Census.

Source: National Institute of Statistics (INE) and Central Bank of Venezuela (BCV)

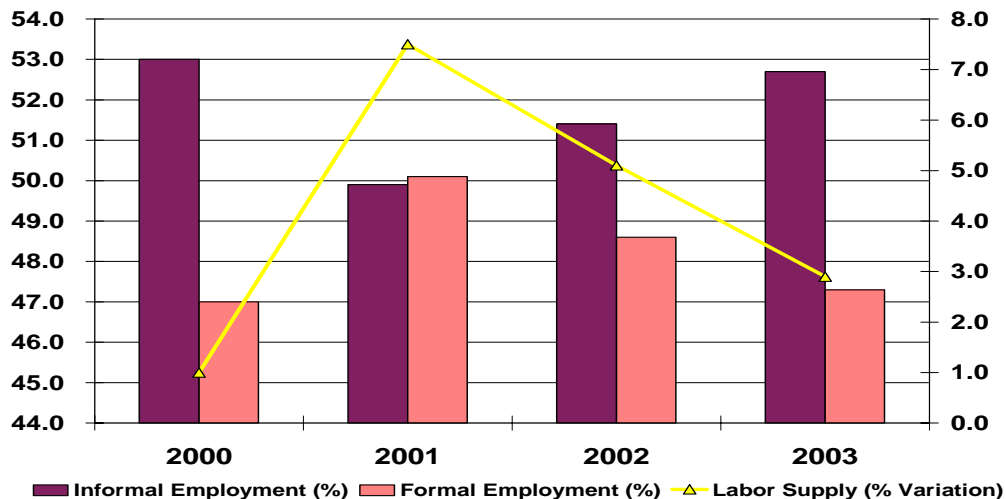
Table 10 Monetary Base 2001-2003 (millions of Bs)

	2003	2002	2001
SOURCES	11,274,439	7,701,120	6,478,295
Net International Reserves	32,919,902	16,717,674	9,344,729
Assets	32,983,363	16,776,604	9,369,171
Liabilities	(63,461)	(58,930)	(24,442)
Public sector net	(5,499,666)	2,149,244	1,457,460
Central Government	(2,532,435)	1,018,701	(3,918)
Investments in Government securities	889,622	1,532,905	895,019
National Treasury Agency net	(1,483,735)	(135,852)	(62,862)
Other accounts	(1,992,112)	(432,142)	(891,876)
Debt-equity swap securities	53,790	53,790	55,801
Other Government agencies	(662,209)	1,130,543	1,461,378
Petróleos de Venezuela, S.A. and its subsidiaries	(1,693,876)	(383,746)	(66,819)
Deposit Insurance Fund net	1,378,195	1,380,509	1,378,633
Investment Fund of Venezuela	(640,119)	(27,389)	(10,448)
Other placements and investments	293,591	161,169	160,012
Financial sector	1,345	37,001	43,432
Commercial banks	535	36,191	42,622
Investments in securities	9	9	9
Rediscouts, advances and repos	0	35,653	41,100
Debt-equity swap securities	0	0	0
Other accounts	526	529	1,513
Rest of banking system	810	810	810
Credit instruments issued by BCV	(7,692,239)	(553,022)	(106,374)
Other accounts net	(843,606)	(986,831)	(660,312)
Paid-in capital and reserves	(9,916,319)	(9,662,947)	(3,600,640)
APPLICATIONS	11,274,439	7,701,120	6,478,295

Notes: From December 1997 onwards, the liabilities recorded under reserves correspond to new

Source: Central Bank of Venezuela (BCV) classification criteria established in the Published Balance Sheet of Banco Central de Venezuela, which for analytical purposes were applied to the whole period under consideration. Universal Banks in Venezuela are those that carry out commercial banking, investment banking, and financial leasing operations.

Figure 4 Labor Market Structure 2000-2003 (%)



II.2 Fiscal Position

Government Expenditure

The Venezuelan governments have been characterized for mismanagement and expansion of the public expenditure. Indeed, the current administration has not been the exception, on the contrary, it is ranked as one of the largest representative of expanding public expenditure and the administration's machinery.

As an example, the Government carried out a policy of increasing its expenditure in 2002 and 2003. However, the Ministry of Finance reported for the consolidated government expenditure a deficit of 1.4% of GDP for 2002 and a surplus of 0.2% for 2003, as improving of the Government's finance consolidated. Certainly, this is a relative improving in terms of the rate, but it should be taken into account the following:

- There level of oil prices increase is larger than the increasing of the government expenditure, as a whole.
- Since 1998, the Venezuelan Central Government Expenditure has increased constantly during 6 years (the Administration of President Chavez started in 1999).

In that sense, the Central Government's balance ended 2003 with a total level of income of 22.8% of GDP, the largest income gotten by comparing to the average of the last decade, and a total expenditure of 27.1% of GDP, which represents the fourth year in that trend. As a result, 2003 ends with a fiscal deficit of 4.3% of GDP.

This increasing in the expenditure of the Central Government during 2003 is mainly attached to the raise of current transfers that was the highest increasing from the previous year, and remunerations and capital accounts too. Within the primary expenditure is also noticed that expenditure on interests, as the least increasing of that balance, because there was exceeding of liquidity on economy due to the stagnation, then the Internal Bonds offered low yield.

Public Borrowing

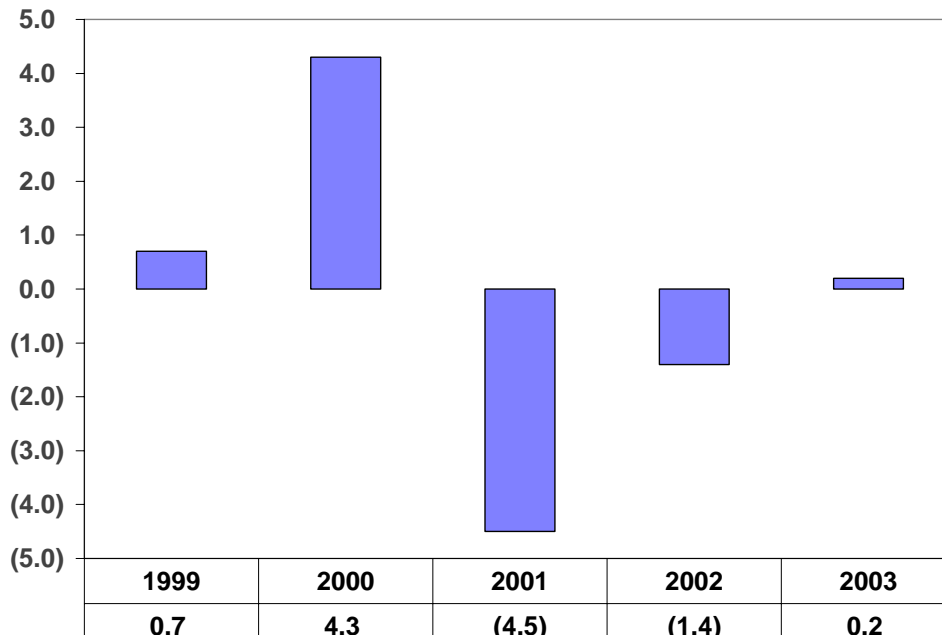
Public borrowing kept its usual tendency to increase during this Administration. Public borrowing has also been a highlighted point in the Venezuelan public finance because the weight of labor liabilities and the expansion of the Government's machinery, which requires to be compensated.

Public borrowing derived from the Venezuelan financial market steadily grew in a relevant way, based on GDP, of 2.7% in 2002 and 6.2% in 2003.

Talking about the National Public Bonds (DPN), they were basically in better performance in their nominal value than their precedents, besides that their effective yield reduced from 37.7% to 29%. That issuance characterized to have low yield due to liquidity, already mentioned. The treasury bonds experienced an increasing in net operations of 0.7% of GDP in respect of 0.3% from 2002.

Regarding to the external public borrowing, this has slowed down its growing up to 0.2% of GDP, because of payment of 2003 maturities and some amortizations for 2005, 2007 and 2008 by buying out brady bonds.

Figure 5 Consolidated Public Sector Balance 1999-2003 (as % of GDP)



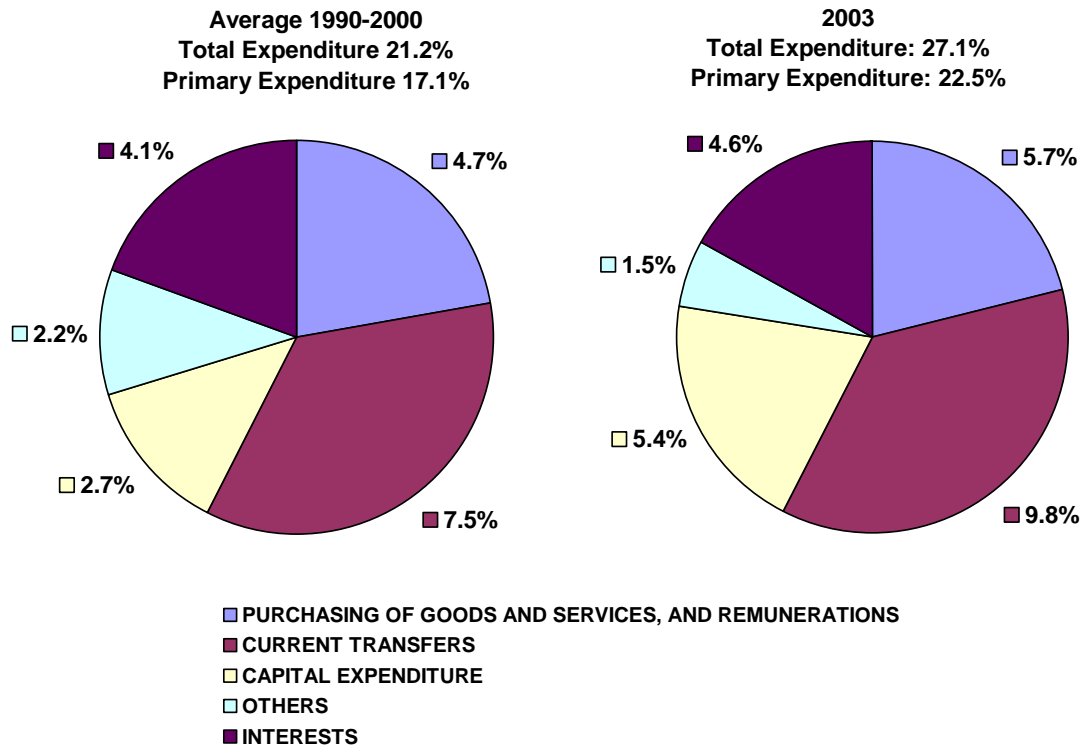
Source: Central Bank of Venezuela (BCV)

Table 11 Central Government Expenditure 2001-2003 (million of Bs)

Central Government Expenditure	2001	2002 (*)	2003 (*)	as % of GDP		
				2001	2002	2003
Total Expenditure	22,357,118	28,162,699	37,286,700	24.5	25.4	27.1
Current	17,147,463	20,567,828	27,887,957	18.8	18.6	20.3
Remunerations	3,924,575	4,507,110	5,709,134	4.3	4.1	4.2
Goods and Services Purchasing	1,108,170	1,720,760	2,064,390	1.2	1.6	1.5
Others	93,884	37,654	303,138	0.1	0.0	0.2
Public Borrowing Interests and Commissions	2,578,190	4,950,747	6,300,080	2.8	4.5	4.6
Internal	1,421,977	3,159,240	4,371,653	1.6	2.9	3.2
External	1,156,213	1,791,506	1,928,427	1.3	1.6	1.4
Transfers and Subsidies	9,442,644	9,351,557	13,511,215	10.3	8.4	9.8
Public Sector	8,918,970	9,045,320	12,927,689	9.8	8.2	9.4
Private Sector	522,553	305,572	581,353	0.6	0.3	0.4
External Sector	1,120	666	2,174	0.0	0.0	0.0
Capital	3,908,930	5,449,073	7,364,832	4.3	4.9	5.4
Gross Capital Formation	546,471	1,615,238	2,302,127	0.6	1.5	1.7
Transfers	3,362,458	3,833,836	5,062,705	3.7	3.5	3.7
Public Sector	3,351,572	3,829,923	5,056,603	3.7	3.5	3.7
Private Sector	10,886	3,913	6,102	0.0	0.0	0.0
Non-Budget Expenses	916,908	1,352,212	1,718,605	1.0	1.2	1.3
Borrowing Net Concession	383,818	793,586	315,306	0.4	0.7	0.2
Internal	336,090	748,650	231,894	0.4	0.7	0.2
External	47,728	44,936	83,413	0.1	0.0	0.1

Source: Ministry of Finance and Central Bank of Venezuela (BCV)

Figure 6 Expenditure Composition of Central Government 1990-2000 and 2003



Source: Central Bank of Venezuela (BCV)

Table 12 Finance of Central Government 2001-2003 (millions of Bs)

Central Government Finance	2001	2002 (*)	2003 (*)	as % of GDP		
				2001	2002	2003
Total Financing	3,869,790	4,273,465	5,901,766	4.2	3.9	4.3
Domestic	3,569,060	3,326,798	4,458,676	3.9	3.0	3.2
Central Bank	309,111	(76,116)	(2,088,079)	0.3	(0.1)	(1.5)
Rest of Financial Sector	2,792,442	2,947,181	9,038,381	3.1	2.7	6.6
Expenses	3,985,068	5,170,353	13,924,957	4.4	4.7	10.1
Net Treasury Bonds	416,433	303,563	1,012,619	0.5	0.3	0.7
Refinancing	-	-	(3,387,654)	-	-	(2.5)
Others	(72,007)	(9,358)	501,220	(0.1)	(0.0)	0.4
Amortization	(1,537,052)	(2,517,377)	(3,012,760)	(1.7)	(2.3)	(2.2)
Other Internal	467,507	455,733	(2,491,625)	0.5	0.4	(1.8)
External	300,730	946,667	1,443,090	0.3	0.9	1.1
Expenses	1,569,801	1,895,034	9,457,979	1.7	1.7	6.9
FIEM	133,224	1,917,724	746,211	0.1	1.7	0.5
Amortization	1,402,294	(2,584,390)	(5,836,499)	1.5	(2.3)	(4.2)
Refinancing	-	-	3,399,651	-	-	2.5
Others	0	(281,700)	475,050	0.0	(0.3)	0.3

Source: Central Bank of Venezuela (BCV) and Ministry of Finance

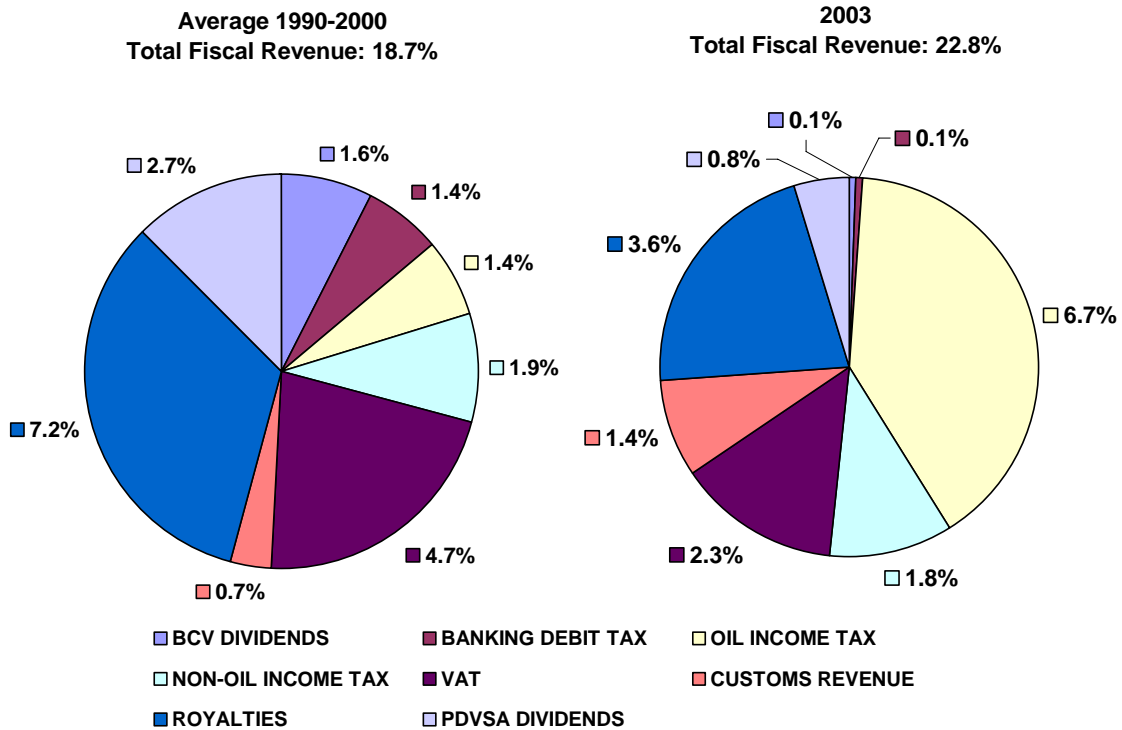
Fiscal Revenue

As oil revenue is the major source of income, the oil income tax and royalties cover the largest portion of the pie chart in a total 8.6%, which in comparison to the average 1999-2000 is 10.3% that reflects the influence of the tax system’s improvement.

In total, the fiscal revenue increased slightly from 11.3% to 11.5% in the variation 2003-2002. In terms of tax revenue, this variation happened mostly due to the increase of the VAT rate and also the implementation of the banking debit tax at the end of 2002, which stayed during the whole year 2003.

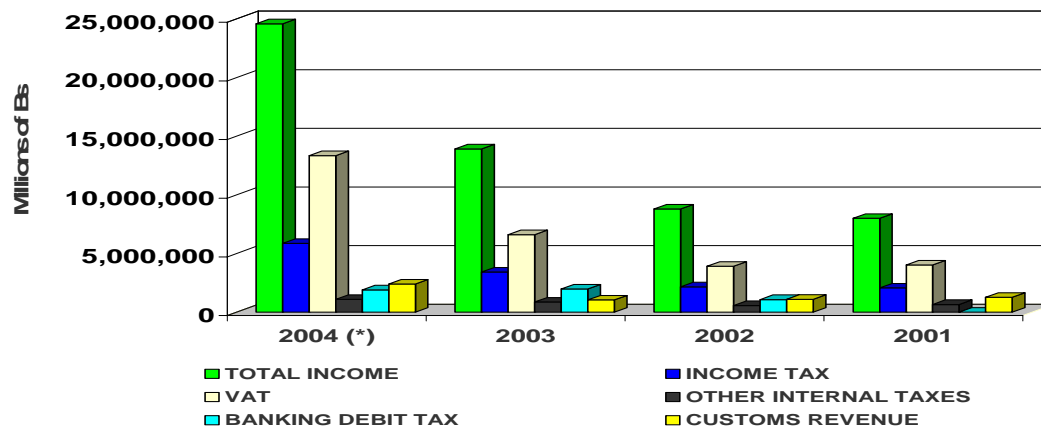
In respect of non-oil tax revenue, the enforcement of a strong policy for tax collection called “Cero Evasion Plan” implemented by the administration overcame the expectations of tax collection for 2003 and 2004 in respect of provisional data, which reached around Bs 13,924 and Bs 24,593 million. The decrease in the banking debit tax revenue is the result of a reduction of its tax rate from 0.75% to 0.5% in 2004.

Figure 7 Fiscal Revenue Composition of Central Government 1990-2000 and 2003



Source: Central Bank of Venezuela (BCV)

Figure 8 Tax Revenue Excluding Oil Revenue 2001-2004 (millions of Bs)



Source: SENIAT

III. Tax Structure: Institutions and the Reality

III.1 National Integrated Service of Customs and Taxes “SENIAT”

The level of corruption, illegal consignments and lack of organization manipulated within the customs required in May 1993 that, the Government created a new institution to manage customs separated from the Ministry of Inland, which was the Venezuelan Customs Autonomous Service (AVSA).

Later on, a jointly project called the System of Management and Control of the Public Finance (SIGECOF) among the Inter-American Development Bank (IADB), the Inter-American Center of Tax Administrations (CIAT) and The Venezuelan Government, established in 1994, and thereafter has been forced. The main outcome of this project, of course was the creation of SENIAT, which absorbed AVSA and the other departments and services related to tax. The SIGECOF also carried out the tax reform held in 1994.

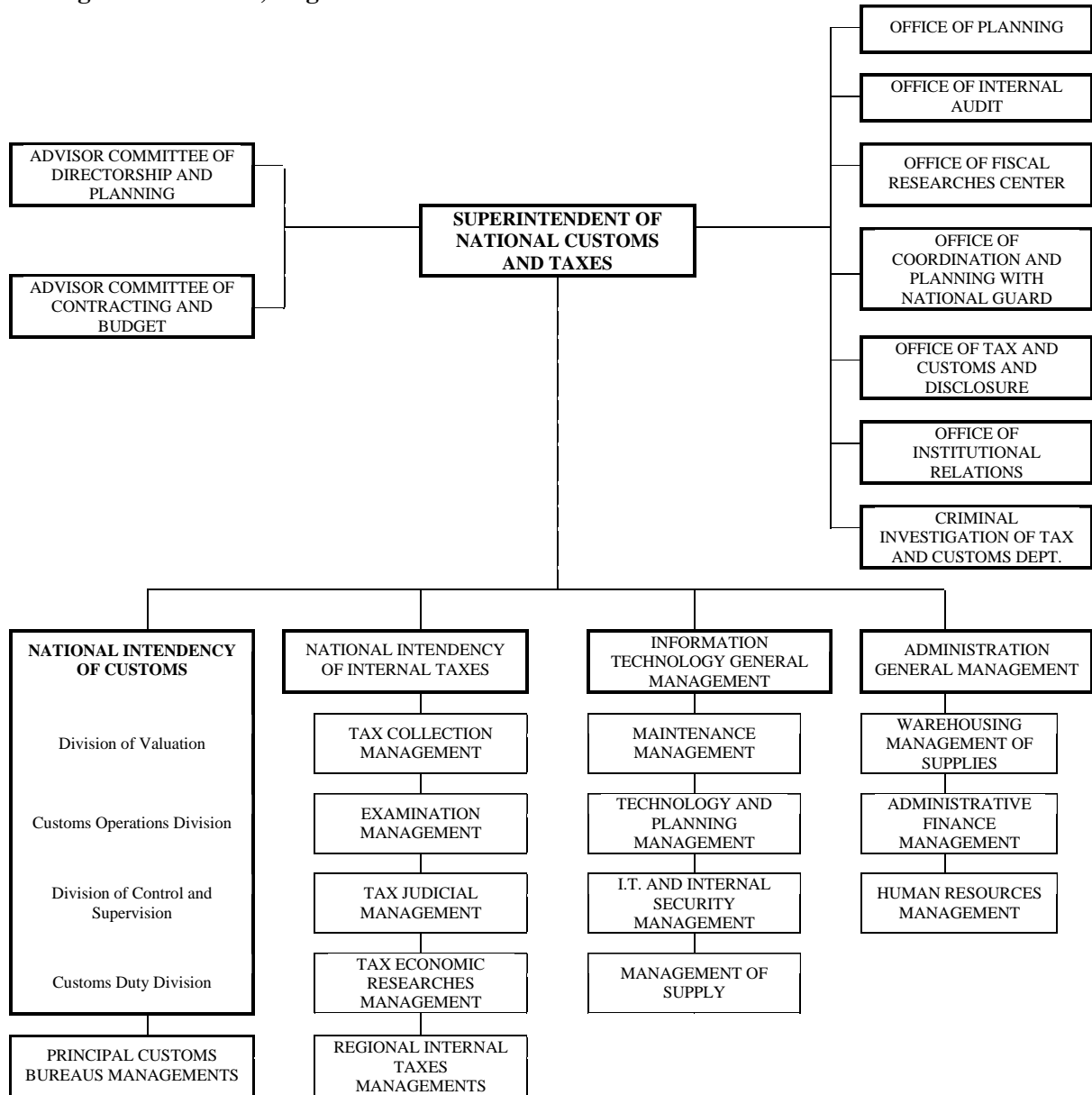
The SENIAT counts on several managements to lead the entire tax system which are mainly located in the capital Caracas at the head office’s dependencies, among them are: Office of the Superintendent, 2 Advisor Committees, which gather the Directors of the Offices; 7 Offices of Directors, 2 National Managements for Internal Taxes and Customs and 2 General Managements for Internal Operations.

It is also composed by 9 bureaus widespread within the country, which enclose the Regional Managements of Internal Taxes and the Managements of Principal Customs Bureaus. Every principal customs has several subordinate customs that usually attend remote places like frontier, small airports, and so on.

III.2 General Aspects of the Venezuelan Tax System

Generally speaking, the Venezuelan Tax System is structured by Internal and National Customs Taxes. However, the tributary administration is also divided by National and Local taxes, so the latter is applicable mostly to municipal taxes. There are also, some contributions that are deemed “earmarked taxes”, which are not administered by the SENIAT or the local governments, it means by the source of the liability.

Figure 9 SENIAT, Organization Chart



Source: SENIAT

Table 13 General Structure of Tax Liabilities and Liabile Contributions

COMPETENCE	TAXES		ADMINISTERED BY
NATIONAL	Income Tax	Individual	SENIAT
		Corporate	
	Value Added Tax	Domestic	
		Imports	
	Taxes on Hydrocarbons	Gambling, Sumptuary goods, etc.	Ministry of Finance
		Royalties	
		Surface Tax	
		Own Consumption Tax	
		General Consumption Tax	SENIAT
	Banking Debit Tax		
	Inheritance tax		
	Gift Tax		
	Excise Taxes	Alcohol	
		Tobacco	
		National Return of Matches	
	National Stamp Duties	Stamp	
Sealed Paper			
Others			
IVSS Contribution		Social Security Pension Fund Contribution (IVSS)	
INCE Contribution		National Institute of Educative Cooperation (INCE)	
Housing Fund Contribution		Ministry of Labor	
Unemployment Insurance Contribution			
LOCAL GOVERNMENT	Tolls		State Government
	Business License Tax		Municipal Government
	Property Tax		
	Advertising Tax		
	Car Tax		
	Other Municipal Taxes	Municipal Stamp Duties	
Others			

Source: SENIAT, Venezuelan Finance Law Association (Asovedefi), World Trade Executive Inc.

Tax Unit

This refers to a measure created to avoid the negative influence of the high rate of inflation on the tax base, so all of the tax instruments and some laws in the country use it to their enforcement, especially in the case of fines and progressive tax rates. It was created in 1996, as a result of the growing of inflation rate and lack of revenue held at that time. The variation of the Tax Unit is based on the price index, and is usually changed on a year basis, as it is shown:

Table 14 Value of Tax Unit from Startpoint up to January 2005

Year	Value of Tax Unit (Bs)	Enactments
2005	29,400	1/27/2005
2004	24,700	2/11/2004
2003	19,400	2/5/2003
2002	14,800	5/3/2002
2001	13,200	4/24/2001
2000	11,600	5/24/2000
1999	9,600	4/5/1999
1998	7,400	4/14/1998
1997	5,400	6/4/1997
1996	2,700	7/18/1996
1995	1,700	4/7/1995
1994	1,000	5/27/1994

Source: SENIAT

As a tax incentive for better compliance, despite of the Tax Unit could be changed before filing tax returns on March, the SENIAT enacts a providence to keep the prior value for income tax payment, as it will happen during the first trimester of 2005.

Taxpayer Identification (RIF)

The Venezuelan Tax system established since the foundation of the SENIAT the Taxpayer Identification (RIF) for income taxpayers. This identification is compulsory for corporate income taxpayers to do almost every transaction related to their organizations, not only for tax purposes. As usual, the requirements for this identification include ID, Constitutive Document and other documents of registration. However, it is required for foreign corporations a legal power of the representative in Venezuela, translated by an official translator and sealed by the Venezuelan embassy in the country of origin.

The taxpayer identification is required for inheritance tax, even in the case that the inheritor is not taxpayer so far, and it is also compulsory for corporate income taxpayers for any change in the board of directors, address, domicile, economic activity, etc.

Taxpayers have access to know the current status of their taxpayer identification through a link in the official web page of SENIAT.

Special Taxpayer

There is no disclosed an official criteria to grant the condition of “special taxpayer”. Actually, taxpayers receive an official notice from SENIAT, as soon as they acquired such condition. Nevertheless, some specialists have established certain pattern or common features that are common among those taxpayers:

- Persons performing economic activities other than exploitation of hydrocarbons or related operations that have declared a gross income of over 120.000 tax units in the preceding fiscal year or have more than 10.000 tax units summed from the last six months’ VAT returns.
- Persons performing hydrocarbons or related operations by virtue of Exploration and at Risk Exploitation Operating Conventions under a Shared Profit Plan, Strategic Associations or partnership.
- Individuals who, according to their latest final income tax return, have a gross income higher than 30.000 tax units, or who, during the last six months have carried out sales or provided services for 2500 tax units or more.
- Individuals with connected or subordinate operations, such as running a non-corporation organization, with 30.000 tax units of net income in the annual tax return.

Permanent Establishment

It is found the concept of permanent establishment in the 1999 new Venezuelan Income Tax Law that was later reformed in 2001. As it modified the principle of territoriality to add net profit from income overseas, the concept of permanent establishment acquires even more relevance. Within the Income Tax Law the permanent establishment condition is applied to taxpayers with more than sixth months within the country, with an office, branch or establishment of any business run by them and/or by a legal representative that has carried out it within the same period of time (forced by the Article No. 7 of the Law).

Tax Credit

Whether the taxpayer has paid income tax abroad, taxes derived from the transfer of fixed assets of goods, or any other taking into account the nature of the tax by the SENIAT, it is enforced the correspondent tax credit without exceeding the level of Venezuelan income tax’s

assessment, according to the international harmonization and provided by the Venezuelan Income Tax law.

Tax Litigation

Talking about tax litigation, this topic has been controversial due to the enactment of new tax courts to enforce the plan of tax collection. These are the stages of tax litigation in Venezuela:

- Taxpayers are entitled to file administrative tax appeals against tax deficiency assessment issued by SENIAT or a local government. Those appeals are decided by the same institution or government that issued them.
- Later, taxpayers are entitled to appeal again before the judiciary by presenting the respective tax appeals.
- The settlement made by the tax courts may be appealed before the Political-Administrative Chamber of the Supreme Court of Justice (Supreme Court), which will be the final stage and the settlement to be applied.

Certainly, because of the red tape and the inefficiency of the Venezuelan legal system, tax appeals may delay a very long time, maybe years to get the final decision. It is strongly recommended usually to deal with the tax administration itself.

There are nine tax courts in total to make up the whole country, they are:

Table 15 Supreme Tax Courts

Superior Tax Courts	Competence	City Located
Capital Region (3)	Capital District and States of Miranda, Vargas, Guarico y Apure (excluding the District of Páez)	Capital District
Zulian Region	State of Zulia	Maracaibo
Andean Region	States of Táchira, Mérida, Barinas, Trujillo, and the District of Páez from Apure State	San Cristóbal
Midwestern Region	Lara, Portuguesa, Falcón y Yaracuy	Barquisimeto
Eastern Region	States of Anzoátegui, Monagas, Sucre, Nueva Esparta, and the Federal Dependencies	Barcelona
Central Region	States of Aragua, Carabobo and Cojedes	Valencia
Guayana Region	States of Amazonas, Bolívar and Delta Amacuro	Ciudad Bolívar

Source: World Trade Executive

On-line Services

The Venezuelan Tax Administration SENIAT, in order to enhance compliance of taxpayers, developed e-tax filing and supplying of other services related to the tax system, at its web site www.seniat.gov.ve , such as:

- Individual and Corporate Income Tax filing return and payment (even if it is divided by quotas as option for individual income tax, which is provided by the law)
- Value Added Tax filing return, filing VAT's withholding system (Special Taxpayers) and VAT's payment. All of them in monthly basis.
- Customs Clearance for Customs Agent that avoid losing time in filing it in the customs bureaus, under the system SIDUNEA
- Taxpayer Identification (RIF) for all taxpayers
- Different Tax Forms
- Instructive in detail for each tax

Each taxpayer is encouraged to get an “user” and an “ID password” to be registered in the web page, otherwise is impossible to file any tax using this service. On the web page itself, taxpayer may get a manual for each category to guide him or her to use that service. The rest of information is available for public in general.

Indeed, for filing returns on March 2005, SENIAT enacted a providence to oblige tax officers and public employees in general, including taxpayers from Central Bank of Venezuela, National Universities, Public and Autonomous Institutes; and the Parliament, to use the e-tax filing only.

III.3 Internal or National Taxes

A. Income Tax

The Venezuelan Income Tax Law was enacted in 1999, after the enactment of the actual Constitution of the country. Later on, in 2001 this law was reformed and now is the current version that is applied in the tax system. Within the 2001 Venezuelan Income Tax Law is deemed that any annual net profit derived from economic activities, as in Venezuela as in other countries, independently who run those activities be national or not, will be subject to tax.

1. Individual Income Tax

Taxpayers

The principle of overseas net profit included in the income tax law start breaking the limitation that the principle of territoriality basis has, in order to expand the level of action that the Venezuelan tax system used to have. In that sense, this version classified taxpayers in three groups:

- First, natural and juridical persons that have domicile and residence in Venezuela, which their source of income is located in Venezuela or overseas;
- or those who do not have domicile and residence in Venezuela, which their source of income is within the country or abroad.
- Third, those with residence or domicile abroad that have permanent establishment within the country, which their source of income related to this permanent establishment or branch in Venezuela, is within the country or overseas.

Taxable Income and Tax Rates

Those, who are resident or domiciled in the country, are subject to be taxpayers when their worldwide annual net income is higher than a threshold of 1000 tax units, or the worldwide annual gross income is higher than 1500 tax units. Moreover, all assimilated or subordinated operations such as non-corporations organizations in which taxpayer has participation, must be accounted in his or her assessment. Also foreigners without residence and domicile are taxpayers with any income derived from Venezuelan source.

In the case of Venezuelan Individual Income Tax, they should figure out the net profit by using self-assessment system. The net profit is determined by summing gross profit minus the costs and deductions allowed by the law. Step by step this assessment is:

- Firstly, it is subtracted the loss in prior years and the deductions allowed. Among the most important deductions applied under certain conditions are: unique deduction (774 tax units), payment for education, hospitalization and other medical services, and their respective insurance primes for using them and interests and payments of mortgage loans of main housing.
- In addition, there are some reductions that are provided by the law that apply in case of taxpayers with ascendants and descendants who are sustained by him or her.
- After getting the taxable income, this is converted to tax units and multiply by the tax rate accordingly. Then it is applied a “subtract factor”, which is a quantity that is subtracted from the result obtained after having been applied the tax rate, in order to avoid taxing the level of previous returns with that level of tax rate.

- Tax rates are divided in two categories for the Venezuelan Individual Income Tax, which are resident and non-resident, that are in a range from 6 to 34%.

Estimated Tax Return

The Venezuelan individual income tax makes file estimated returns who their income derives from: commercial activities defined by the Commercial Code, credit businesses, sole proprietor or self-employed, rent or sublet of goods and/or real state businesses and dividends from juridical persons, organizations or communities that are not Venezuelan corporate income taxpayers.

Final Tax Return

On the other hand, it is compulsory for individual income taxpayers to file a final return according to the scope of being taxpayer, with the exception that taxpayers from agricultural sector that file returns after getting an income higher than 2625 tax units. Furthermore, people non-resident and/or without domicile in Venezuela who receive any income from Venezuelan source, or having a permanent establishment in the country, have also to present final return.

The fiscal year for Venezuelan individual income taxpayers has always compulsory framed inside the calendar year.

Withholding System on Salaries

Individual income taxpayers' salaries, based on the tax rate and the information provided by the employee, are subject to be withheld by the employer. This tax withheld must be paid by the employer within the first three working days of the following month, otherwise is subject to receive sanctions accordingly. In the case of non-resident will be withheld 34% of the gross income.

Table 16 Individual Income Tax Rate

Individual Income Tax	Tax Rate	Subtract Factor
For income up to 1000 tax units	6%	0
For income between 1000 and 1500 tax units	9%	30
For income between 1500 and 2000 tax units	12%	75
For income between 2000 and 2500 tax units	16%	155
For income between 2500 and 3000 tax units	20%	255
For income between 3000 and 4000 tax units	24%	375
For income between 4000 and 6000 tax units	29%	575
For income that exceeds more than 6000 tax units	34%	875
For non-resident people	34%	875

Source: SENIAT

2. Corporate Income Tax

Taxpayers

The classification of corporate income taxpayers establishes that those which are taxpayers are:

- Every juridical person or organization, which is classified within the Commercial Code, with profit purposes. Corporations and entities that work in mining sector, hydrocarbons industry and those in activities related to, receive a special treatment in terms of the tax rate and examination.
- Juridical and non-juridical associations, foundations, and so on (unless they demonstrate that they do not make any profit).
- Any permanent establishment or branch from any company worldwide which works in the Venezuelan territory as a business, office, etc. or even by offering professional services regarding to science, literature, art, education, and so on.

Taxable Income

For the Venezuelan Corporate Income Tax, it is assessed the Net Worldwide Taxable Profit by getting any revenue from Venezuelan source and derived in other countries, in which we obtain gross return, net profit, and so on. Only in the case of income from Venezuelan source is entitled to carry deduction of losses.

Table 17 Net Worldwide Taxable Profit Assessment

INCOME WITHIN VENEZUELA	INCOME FROM OVERSEAS
Gross Revenue - Costs	Gross Revenue - Costs
= Gross Profit - Deductions	= Gross Profit - Deductions
= Gain or Loss within the FY +/- Inflation by adjustment	= Net Profit from Overseas in foreign currency (multiply by official exchange rate or average if there is free exchange market)
= Profit within Venezuela - Losses in years before	
= Net Profit within Venezuela	= Net Profit from Overseas in Bs
Sum of every "Net profit" obtained = Net WORLDWIDE TAXABLE PROFIT	

Source: SENIAT

Tax Rates

After getting the Net Worldwide Taxable Profit, as in individual income tax assessment it is converted in tax units, then it is multiplied by the tax rate and finally, it is subtracted the factor mentioned before. Also it will be applied tax credits, reduction of tax incentives (enclosed in the Venezuelan Income Tax Law for investments), and any other reduction by credit from other taxes, estimated declaration, etc. In order to apply for corporate income taxpayers, there are tax rates of a range from 15 to 34% as well, and special tax rates of 50 and 60% for hydrocarbons and mining sectors respectively and their related companies.

Table 18 Corporate Income Tax Rates

Corporate Income Tax	Tax Rate	Subtract Factor
For income until 1000 tax units	6%	0
For income between 1000 and 1500 tax units	9%	30
For income between 1500 and 2000 tax units	12%	75
For income derived from hydrocarbon exploitation and activities closely related (as transportation)	50%	
For income derived from mining industry regarding to royalties and mining interests and activities closely related	60%	

Source: SENIAT

Estimated Tax Return

Those corporate taxpayers, which are not running businesses closely related to hydrocarbons or mining sectors, that make a net income higher than 1500 tax units during a prior fiscal year, have to file an estimated return and prepay for it at least 80% of that estimation. Moreover, other conditions are enforced to file that estimated return, such as:

- When taxpayers running businesses related to hydrocarbons and mining sectors, or those which their prior fiscal year is less than the official one, and make income higher than 1000 tax units.
- When taxpayers have an extra income with a relevant amount compared to the usual one.

The schedule for this prepayment of the estimated return varies from 45 days to the sixth month of the year according to the economic activity (whether belongs to oil and mining activities), and its condition of normal or special taxpayer, because the latter has a different schedule.

Final Tax Return

For the final return, all of the corporate taxpayers and their related companies are obligated to file final return no matter the amount of profit or loss they get from a fiscal year. The timing given by the law to file this return is 90 days after finishing the corporation or business' fiscal year, excepting in the case of the special taxpayer's schedule issued by the SENIAT.

Withholding System

In the Venezuelan Income Tax Law, corporate taxpayers are withholding agents of two major responsibilities: salaries (as individual income tax) and corporate invoice withholding tax system. In that sense, corporate taxpayers withhold certain amount of income tax from the exchange of goods and services invoiced that exceeds a threshold of Bs 2,450,000, so this system works in this basis:

Table 19 Corporate Income Tax Withholding System Rates

SECTOR	PERCENTAGE OF WITHHOLDING	SUBTRACT
SERVICES	3%	73,500
OTHERS	1%	24,500

Source: SENIAT

Whether the service is rendered by a foreign company, 90% of the gross amount will be taxable income for withholding system purposes.

B. Value Added Tax

After some reforms and versions, the Venezuelan Tax System finally adopted the figure of value added tax for commercial transactions, imports and exports, among others, though exports have always enjoyed 0% tax rate. Value added tax in this country is enforced through invoice system and monthly basis. The current Venezuelan Value Added Tax Law was recently reformed by the reduction of the rate from 16 to 15% that was enacted from September 1st, 2004.

Tax Base

In principle, this tax is imposed on any commercial transaction, but it is more specified in the following:

- Sales of taxable goods located in the country.
- Import of any good, unless those goods exempted by a legal provision or a tax incentive.
- Self-employed services carried out
- When assets, that are located within the country, are incorporated or retired from the financial statements or inventory of the corporation.
- Export of goods (0%)

Taxpayers

The Venezuelan Tax System classifies value added taxpayers by:

- Ordinary Taxpayers: those which are subject to be taxed by offering goods and services and importing ordinary goods. Taxpayers which do not import and carry out sales less than 3000 tax units, become part of the Formal Taxpayers.
- Formal Taxpayers: those that have the same features than before, but offering goods and services exempted within the Venezuelan Value Added Tax Law.
- Occasional Taxpayers: for those taxpayers that are not ordinary, but they occasionally carry out some imports.

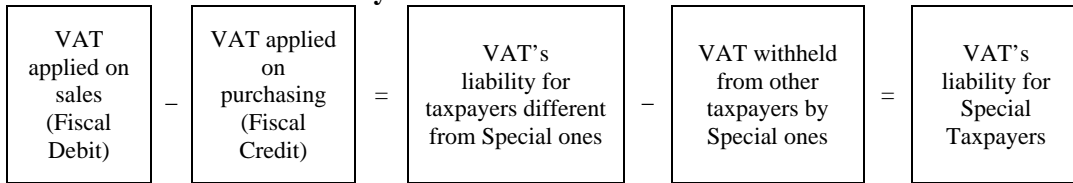
- **Special Taxpayers:** As it has been reflected before, the role of Special Taxpayers is relevant for the Venezuelan Tax System. Regarding to the Venezuelan Value Added Tax, these taxpayers are withholding agents.

In addition, companies subject to excise taxes such as matches and tobacco manufacturing are designated tax collectors for those sectors.

Taxable Income and Withholding System

As the country enforces VAT by invoice system, this tax is established on full price for customers, and for prior intermediaries by subtracting the previous tax imposed. Thus, through the withholding system in the Venezuelan Value Added Tax, when the special taxpayers acquire goods or services, and they are invoiced, the recipient of payment transfers the entire details about this invoice, in order to be issued a credit note for 75% of the VAT levied that is withheld and it must accompany the correspondent payment. Therefore, the following scheme shows how this system works:

Table 20 Value Added Tax System



Tax Rate

As it was mentioned above, the current Venezuelan Valued Added Tax Rate nationwide applied is 15%. However, there is a lower tax rate of 8% enforced for certain preferable items deemed important for the Venezuelan economy. Cattle to be bred; animals alive to be sent to the slaughterhouse; certain types of meat and fish for massive consumption, food oil, butter and lard; and their derivatives to be used for producing food; food for animals; services carried out for public institutions and plain tickets.

On other hand, the Venezuelan Value Added Tax Law enforces an additional tax rate of 10% for certain “luxury” or sumptuary goods. For example: vehicles valued above US\$30,000; motorcycles above 500 cc; gambling, lottery, and casino machines; airships and some jewels as the most important.

Exemptions and Exonerations

Some items are not liable to the Venezuelan VAT, as well as there are exemptions and exonerations. Among the most relevant are:

- **Not liable:** imports not concluded (i.e. In-bond), selling of stocks or financial certificates and intangible goods referred to this sector, any transaction carried out by financial institutions as banks and insurance companies, services carried out under the relationship between employer and employee and public services given by public institutions.
- **Exemptions:** food, except that which is not part of basic feeding basket; medication and medical services and some medical equipment; gasoline, gas and any other combustible and some of their raw materials; education; public transportation; utilities and services such as electricity, , water, gas, etc.; newspapers, books and magazines, and the paper to produce them; and imports carried out for the National and local governments and for duty free zones
- **Exonerations:** they are usually aimed to reduce the costs of Government’s projects and to give tax incentives for those projects and investments that the Government considers as extremely important for the country’s development.

C. Taxes on Hydrocarbons

As it was shown before the relevance of hydrocarbons' exploitation in Venezuela, this activity has been subject to pay dividends (in the case of the government owned) and royalties to the Government, and recently, taxes. Hence, all these liabilities owed to the country have been enforced through the "Law of Hydrocarbons". The previous version was the law of 1943, which was substituted by the new Law of Hydrocarbons under the Presidential Decree 1510 from November 11th, 2001. Although royalties are not a "tax" included within the tax administration, it was deemed important to be mentioned for the purpose of this report.

Royalty

The Government is entitled to receive a royalty of 30% of all volumes of hydrocarbons extracted from any reservoir. This could be requested in money or in kind in the proportion they need it. However, it is understood that it must be paid fully and in cash, unless they ask for and this payment in kind could be for transportation and storage purposes.

Surface Tax

Surface Tax is applied to surface area granted by the Nation which is not exploited at all. The tax base refers to the square kilometers (Km²) that are not exploited, and it is imposed 100 tax units per Km² or fraction. The amount of tax is increased after the grant as follows:

Table 21 Hydrocarbons Surface Tax

Tax Amount	First 5 years	From 6th year and in advance
Qty of Km ² not exploited x 100 tax units	An increase of 2% per year	An increase of 5% per year

Source: SENIAT

Own Consumption Tax

The basis of the tax are products derived from hydrocarbons, produced and consumed (i.e. fuel in own operations), in which is applied a rate of 10% of the value of each cubic meter (m³), calculated based on the sales price to the end consumer. If the product is not sold out in the domestic market, the Ministry of Energy and Mines sets the price.

General Consumption Tax

In this case, the Ministry of Energy and Mines fixes a tax rate from 30% to 50%, levied on the price paid by the end consumer of product derived from hydrocarbons sold in the domestic market. The tax rate is disclosed by enacting a decree or providence.

D. Banking Debit Tax

The Banking Debit Tax is a tax imposed nationwide on any debit or transactions of withdrawal made in current bank accounts, deposits in custody or any other type of debit on saving accounts or stocks issued by financial institutions within the country, above a threshold. The financial institutions that regard this tax are those which are regulated by the General Law of Banks and Other Financial Institutions, the Central Bank of Venezuela Law and the Stock Market Law.

The banking debit tax is enforced on the debit transactions mentioned before that do not cross the threshold of 40 tax units per transaction or by the average of bank accounts' monthly debit transactions, with the rate of 0.5%. It is deemed that these rules are counted by person, each bank account and each financial institution. Thus, the taxpayers for this tax are the financial institutions which offer the stocks or bank accounts.

This tax was imposed by another government in the past and always it has been usually levied as earmarking tax for specific purposes. Indeed, the current period started after the enactment of the Banking Debit Tax Law in August 2002 with the same purpose. However, banking debit tax was reformed to be re-enacted in March 2003 and March 2004. By the end of 2004, the current administration decided to change this tax into a regular tax, so this decision ended up in the enactment of the “Partial Reform of the Law that Establishes the Banking Debit Tax” that has expiration date for the rate currently applied in December 2005, when it is forecasted that the current administration will vary it by depending on the level of oil revenue and the Government’s expenditure.

There are some exemptions derived from this tax, among them are: the debits carried out to pay the tax itself, debit transactions related to the public budget, transactions by the stock market, debit transactions for acquiring stocks from the Central Bank of Venezuela, the mortgage loans issued by the Law that Rules the Subsystem of Housing and Inhabitant Policy, which rules the national housing fund, and the debit transactions related to Diplomatic Missions and some international organizations in Venezuela according to the Venezuelan Income Tax Law.

E. Inheritance Tax

The Inheritance Tax in Venezuela is enforced right after the inheritors present the declaration of balance of the deceased relative and start the legal procedure, and it will be based on the goods and values the deceased used to own. After distribution of inheritance, tax base is assessed based on the cash portion correspondent to each inheritor, according to the assessment of the net wealth which means to subtract the amount for creditors whether exist and liabilities from the assets and goods, and after being subtracted any exemption needed which had been provided by the law.

Taxable Income

For calculating assets, apart from obvious assets or goods owned by the deceased, there are certain conditions that the Venezuelan Inheritance Law requires for this assessment, for example:

- Those transferred during the two previous years of the decease that have not been registered by the law accordingly, or five previous years that have been transferred to the inheritors.
- Those acquired during the three previous years of the decease that have been transferred to the inheritors.
- The value for all is calculated based on the value at the time the decease occurred.
- Those accepted as benefit of inventory. The value is assessed in the legal inspection.

Those liabilities mentioned above that are subtract from the assets are also ruled within the law, these rules are, generally speaking:

- Liabilities with creditors at the time the legal registration of inheritors happened
- Expenses on funeral, and related to it.
- Expenses on reading the will, and any expenses carried out to this reading or valuation of the inheritance. Fees owned by lawyers, economists, public accountants etc., which are regulated by the law as follows:

Table 22 Net Wealth Assessment for Inheritance and Gift Tax

Cash Portion of Net Wealth	Rate
From 20.01 to 50 tax units	6%
From 50.01 to 200 tax units	4%
From 200.01 to 500 tax units	3%
When exceeds 500.01 tax units	2%

Source: SENIAT

- Those what have expiration date before the decease are not allowed.
- Those which are included in the will are not allowed.
- Those which are carried out abroad, unless those related to investments in Venezuela that are not guaranteed by mortgage on assets abroad, are not allowed.
- Those which derive from mortgage loans in the prior year to the decease, and mortgage loans based on the main housing used to be used by the deceased, are not allowed.

Exemptions

Among the exemptions of the Venezuelan Inheritance Tax are:

- When the amount inherited by parents, spouses, sons and daughters even adoptive ones; does not exceed 75 tax units.
- Amounts inherited by non-territorial public entities that are held for welfare and health care.

Exonerations

Among the exonerations of the Venezuelan Inheritance Tax are:

- The public and non-profit private institutions, entities and so on, that are carried out for educational and similar purposes. This also applies for foundations that are constituted by a will mandatory with the same purposes.
- Savings and stocks that are part of the heritage inheritance that exist in financial institutions authorized to receive them to be invested in themselves which do not exceed 500 tax units.

Tax Rates

Table 23 Inheritance and Gift Tax Rates

Blood Relationship	1st degree = Ascendants, Decendants, Spouse, Adopted Children	Substract Factor	2nd degree = Brothers and Sisters, nephew and niece	Substract Factor	3rd and 4th = other relatives	Substract Factor	Other Relatives & Acquaintances	Substract Factor
Up to 15 tax units	1%		2.5%		6%		10%	
From 15.01 to 50 tax units	2.5%	0.23	5%	0.38	12.5%	0.98	15%	0.75
From 50.01 to 100 tax units	5%	1.48	10%	2.88	20%	4.73	25%	5.75
From 100.01 to 250 tax units	7.5%	3.98	15%	7.88	25%	9.73	30%	10.75
From 250.01 to 500 tax units	10%	10.23	20%	20.38	30%	22.23	35%	23.25
From 500.01 to 1000 tax units	15%	35.23	25%	45.38	35%	47.23	40%	48.25
From 1000.01 to 4000 tax units	20%	85.23	30%	95.38	40%	97.23	45%	98.25
From 4000 tax units and ahead	25%	285.23	40%	495.38	50%	497.23	55%	498.25

F. Gift Tax

The Gift Tax is imposed on the base of the entire value of the asset or good under the following conditions:

- When transferring of assets or goods between relatives that have fourth degree of blood relationship and second degree of affinity are transferred with a value less than 20% of the market value.
- The total or partial remission of liabilities, unless they are carried out for bankruptcy or government entities
- The resign of inheritances only if they are not subject to any reimbursement for this fact, which means that, it is resigning for a better reallocation of the inheritance.

Exemptions

Among the exemptions of the Venezuelan Gift Tax are:

- Amounts received by all territorial public entities and non-territorial public entities which are held for welfare and health care.
- Those which do not exceed 25 tax units.
- Savings in any financial institution that belong to under aged sons and daughters, which do not exceed 250 tax units each.
- Insurance premiums paid for under aged sons and daughters, which do not exceed 375 tax units each, and their reimbursements.

The Gift Tax shares the first item of exonerations and the tax rates with the Inheritance Tax.

G. Excise Taxes

Excise taxes are imposed on production, importation, expedition and selling of ethylic alcohol and alcoholic species, tobacco and matches. Those taxes are levied before leaving the warehouse of manufacturer or retailer and when they are imported. Indeed, such warehouse might be controlled by the SENIAT as a Fiscal Warehouse when the amount of collection requires so, which implies that they are always attended by tax officers as a compulsory authority to supervise any inventory out of the place.

Alcohol and Tobacco

Alcohol and tobacco excise taxes are required to be paid after 90 days of the sale (for imports, before coming out Customs' territory), excepting for the last quarter of the year when is required to be paid the last weekday of that period. License for ethylic alcohol and alcoholic species are granted by the SENIAT.

National Return of Matches

In the case of production of matches, this is a concession granted by the Executive Power through the Ministry of Finance, which obliges manufacturer to pass through a large number of requirements because of the nature of the product. Apart from the requirements imposed, bookkeeping is also strictly required according to the law.

Matches Excise Tax is not included within the self-assessment system. Taxpayers present their status of expedition within the first three days of the first two weeks of each month, an after that the SENIAT provides the tax form to carry out the payment at most, three days later taxpayer receive the form.

H. Business Assets Tax

The business assets tax used to levy 1% of tax rate. It was abolished in August 2004 and was not subject to be deducted from the income tax return with certain exceptions. Though this tax was abolished there are some relevant considerations for this report, such as:

- Fiscal years that were being still worked finished with the decree of abolishment, which was around 30 days after the publication.
- The Decree abolished all of the rules of assessment, liquidation, filing and payment of this tax only in regarding to the last fiscal year before the enactment of it.
- Taxpayers that had acquired permission to transfer payment of business assets tax as credit of Income Tax for next three periods are enjoying this benefit up to dates established.

I. International Taxation

1. Tax Treaties

Venezuela has effective Double Taxation Agreements with several countries and seems that are few for the fifth oil exporter worldwide, however, the list includes most of important European countries, which is the region with a steady economic growth in its community, and United States, which is the largest trader with Venezuela. Nevertheless, comparing to other developing countries it is ranked in good position. The fact sheet of tax treaties carried out by Venezuela is:

Table 24 Fact Sheet of Venezuelan Tax Treaties

VENEZUELAN FACT SHEET	For Income Tax and others starting from	Type of agreement on Transportation	Agreement on Transportation starting from	DTAs for Approval by the Parliament	DTAs to subscribe in the Parliament	DTAs to Under Negotiation
ARGENTINA		Air	1988 (*1)			Income Tax and Others
BRAZIL		Air	1989		Income Tax, Capital Tax (Brazil) and Others	
BARBADOS	2001					
BELGIUM	1999					
CANADA	2005	Air / Sea	1993			
CHILE		Air / Sea	1993			Income Tax and Others
CHINA				Income Tax and Others		
CUBA				Income Tax and Others		
CZECH REPUBLIC	1988					
DENMARK	2002					
FRANCE	1994	Air / Sea	1988			
GERMANY	1997	Air / Sea	1998			
INDONESIA	2001					
ITALY	1994	Air / Sea	Air / 1980 Sea / 1988			
MALAYSIA					Income Tax and Others	
NETHERLANDS	1998	Air / Sea	1993			
NORWAY	1999					
PORTUGAL	1999	Air	1980			
RUSSIA				Income Tax and Others		
SPAIN	2005 (*2)	Air / Sea	1986			
SWEDEN	1999					
SWITZERLAND	1998	Air	1986			
TRINIDAD & TOBAGO	1998	Air	1986			
UNITED KINGDOM	1997	Air / Sea	1988 (*2)			
UNITED STATES	2000	Air / Sea	1988			
ANDEAN COMMUNITY: (Bolivia, Colombia, Ecuador and Peru)	2004					

(*1) Treaty under Decree 1268 – 1986, (*2) Treaty renegotiated

Source: SENIAT and the Venezuelan Finance Law Association (ASOVEDEFI)

Table 25 Withholding Rates as Established in the Double Tax Treaties Entered by Venezuela

COUNTRY	Germany	Belgium	United States	France	Netherlands	Italy	Norway	Portugal	United Kingdom	Sweden	Switzerland	Trinidad & Tobago	Czech Republic	Republic of Indonesia	Barbados	Denmark
Business Profits (*1)	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Dividends (*2)	- (A) - 15% all other cases	- (B) - 15% all other cases	- (C) - 15% all other cases	- (C) - 15% all other cases	- (E) - 10% all other cases	10%	- (C) - 10% in all other cases	10%	- (D) - 10% in all other cases	- (B) - 10% in all other cases	- (B) - 10% in all other cases	- (C) - 10% in all other cases	- (A) - 10% in all other cases	- (E) - 15% in all other cases	- (F) - 10% in all other cases	- (B) - 15% in all other cases
Interests paid to banks	4.95%	4.95%	4.95%	4.95%	4.95%	4.95% %	4.95%	4.95%	4.95%	4.95%	4.95%	4.95%	4.95%	4.95%	4.95%	4.95%
Other interests	5%	10%	10%	5%	5%	10%	15%	10%	5%	10%	5%	15%	10%	10%	15%	5%
	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Royalties	5%	5%	5% or 10%	5%	5%, 7% or 10%	7% or 10%	12% or 9%	12% or 10%	7% or 5%	10% or 7%	5%	10%	12%	20% or 10%	10%	10% or 5%
Technical Assistance	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	10.20%	10%	10%	5%
Technological services	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	12%	17%	10%	0%
Real estate rental	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%

(*1) Including commissions and professional service fees.

(*2) (A) 5% if beneficiary owns at least 15% of the capital; (B) 5% if beneficiary owns at least 25% of the capital; (C) 5% if beneficiary owns at least 10% of the capital; (D) 0% if beneficiary owns at least 10% of the capital; (E) 10% if beneficiary owns at least 10% of the capital; (F) 5% if beneficiary owns at least 5% of the capital.

Source: Baker & Mackenzie (Venezuela)

2. Transfer Pricing

Transfer Pricing rules were added in the 1999 Venezuelan Income Tax Law as a mixture of the Brazilian regime, in which fixed gross profit margins, the treatment for import and export transactions are separated, and based on the arm's length principle.

In terms of transfer pricing rules, the Venezuelan Income Tax Law of 2001 abolishes the method of fixed gross profit margins and unifies the methodology for import and export transactions. In addition, the version of 2001 adopts the same methods included in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD guidelines) specifying the original names of these methods in English between parentheses as complementary support of the articles, which means that included all the transactional profit methods.

The most relevant information for taxpayers regards to the documentation that they should collect for future examinations, so summarizing the core points, they are:

- List of risks derived from the operation, such as: commerce and finance, assumed for: production line, transformation, commercialization, sale of goods and/or services carried out by passive party; being or not subject to value and/or accounting quantification.
- Organizational chart of the group of companies and/or enterprise, information of functions of departments and/or divisions, strategic associations and channels of logistic of distribution.
- Information of related parties, directly or indirectly, any documentation that arises the type of relationship, type of business, main customers and amount of shares owned in other enterprises. For multinational enterprises requires shareholding of the related companies in detail, contracts of share transferring, increase or decrease of capital, mergers, etc.
- Information about operations established with related parties, directly or indirectly, date of transactions, amount of transactions and currency used. Any contract, agreement or transaction carry out with any related party abroad, and information in detail about the intangible assets such as: description, market price, transferring, property rights, copyrights, etc.
- List of fixed assets involved in getting returns gathered by type, including depreciation methods, historical costs, financial cost of liquidating assets and accounting method, and all of the documentation that support those transactions.
- Apart from financial statements prepared according to International Accounting Standards, it should be added capital maintenance adjustments account statement and cash flow; production costs statement and costs of stock and/or services sold out.
- Information about commercial strategies, volume of operations, credit policy, payment terms, quality systems, national and international certifications of goods and services, sole right contracts, guarantees, among others.
- Specific information whether any related party is or was subject to a transfer pricing examination, or if any of them are getting any tax dispute against other tax administration, and the information of the status of such dispute. If there is any settlement issued by any other tax tribunal in the past, taxpayer should keep a copy of it.
- Information related to merchandise stocks, "in" and "outs" in monthly basis plus inventories, plus the information of method used for controlling and value them.
- Functional Analysis of transfer pricing, method and methodology of assessment and criteria for choosing that method.

It is important to point it out that the Transfer Pricing Unit of the SENIAT was created in 2002. This unit has not carried out examinations yet; instead, they are collecting information about potential taxpayers and future examinations through the enforcement of the Informative Final

Return for Related Parties called PT-99, which has one main declaration and five attachments to fill out.

III.4 Customs and Local Taxes

A. Customs

As it was established before, Venezuela has 9 Principal Customs Bureaus which are the strategic bases for the whole customs operations nationwide. Therefore, the Customs Bureaus are classified in:

- Principal: Those created to be in charge of determined customs' territory and carry out the management of the other customs.
- Subordinate: Those created to report their activities to the Principal Customs, and they are created to attend a specific zone out of the principal customs territory.
- Provisional: Those authorized by the Ministry of Finance to function with specific purposes.

Customs Bureaus in Venezuela work according to the World Customs Organization (WCO) which provide the international standards to harmonize customs for international trade, in terms of procedures, type of operations, structure, etc.

SIDUNEA

Automation of Customs System (SIDUNEA) is the IT system developed to control customs operations. This new system includes innovations such as: inputting customs clearance through SENIAT's web page by the customs agent, scan of goods to determine illegal consignment, and assess the customs duties and fees automatically using the minimum officer's intervention (i.e. to avoid manually recognition of goods in all cases).

In addition, SENIAT jointly to the United Nations Conference for Trade and Commerce (UNCTAD), which has sponsored the entire process of SIDUNEA, are developing the SIDUNEA Regional Center for America with the goal to attend all of the countries that have already installed this system, providing technical support, upgrades, information on line, among others.

B. Local Taxes

Business License Tax

As the most relevant local tax, this tax imposed on the compulsory fact that any commercial, industrial, or organization included within the Commercial Code is subject to get a license to run this business, granted by the municipality. Based on that, the tax is assessed on the taxpayer's gross receipts from the previous year, and is it is requested under certain conditions such as economic activity. This tax may vary, because of the municipality's autonomy as the other local taxes, from one municipality to another. However, taxes among municipalities are very similar and they are also mostly applied on yearly basis.

The rest of local Taxes vary from one municipality to another.

IV. Country Specific Fiscal Issues

A. Cero Evasion Plan (original name “*Plan Evasion Cero*”)

The Special Taxpayers Management of the SENIAT announced in August 2003 the enforcement of a new strategy for tax collection called “Cero Evasion Plan”. Based on the articles 289 to 301 of the Organic Tax Code that refers to the “Executive Judgment”, or in few words through administrative procedures originated by tax payment, sanctions or interests; and their judicial collection, the SENIAT has applied an aggressive plan of examination and tax collection, which includes extreme measures such as the closing of the establishment between 1 to 5 days, seizure of physical or electronic files, among other elements to use for the examination process; caution measures to ensure the taxpayer’s liabilities; plus the correspondent pecuniary sanction. The SENIAT has conducted such examinations to ordinary and special corporate income taxpayers, in many sectors of the economy.

Indeed, the level of compliance traditionally has been low among Venezuelan taxpayers. For the Venezuelan Tax Administration is a fair plan to implement conscious in all taxpayers and raise the level of compliance. On the contrary, for the taxpayers this plan is a strategy to “frighten” them, because most of taxpayers that have been subject to the Cero Evasion Plan’s audit have been closed, though they claim that findings were minor infractions.

Legal invoice

Within the collateral actions derived from this plan of examination, the SENIAT enacted an administrative providence to pursuant taxpayers must request legal invoice as a result of a consumption of goods and/or services. From that standpoint, whether taxpayers do not request invoices to providers of the goods and/or services, they may incurred in responsibility to the evasion of the tax imposed.

Of course, legal invoice applies at first to corporate taxpayers as part of their operations. Nevertheless, the SENIAT is preparing an examination procedure on individual in shopping centers, establishments, outdoors, and so forth, in which tax officers would request invoice to consumers in those places, then if they do not have such invoice, they would be subject to receive a pecuniary sanction from 1 to 5 tax units.

Besides the opposite positions regarding these actions carried out by the SENIAT between the taxpayers and the SENIAT itself, the fact is that tax collection went up tremendously, apart from the influence of the CADIVI system’s requirements of tax returns, basically due to the enforcement of this plan.

B. Tax Incentives

Investments Tax Credit

The most relevant tax incentive available within the Venezuelan Tax System arises from specific investments. Those investments engaged on sectors: industrial, agro-industrial, agricultural, construction, electricity, telecommunications, science and technology, which are made in assets that improve or develop productivity, are entitled to get a tax credit for 10% of the qualified investment. This incentive may be applicable to investments made before February 27, 2007.

Hydrocarbons Activities Tax Credit

It was mentioned before that, the current administration is highly promoting investments in the oil sector, because of the level of development of it. Hence, in the Law of Hydrocarbons, establishes that taxpayers engaged in those activities are entitled to an investment tax credit of 8%

of the amount of the new investment. There is an additional tax credit of 4% of the total costs of new investments made in exploration, drilling and related production, transportation and storage facilities; secondary recovery of hydrocarbons; utilization, conservation and storage of gas, including liquefied gas; and upgrading of hydrocarbons and research expenses.

Promotion of Investments Law

Under a Decree with force of Law, the Presidency of the Republic enacted the Promotion of Investments Law. The promotion of investments that this law tries to grasp refers to the goal of the Government in improving the level of investments, foreign and domestic, through the creation of an adequate legal infrastructure, environment, and equality of opportunities for them, and then establishing an attractive market for such kind of investments.

In respect of fiscal issues, the Government is granted to stabilize, create, or suit the entire fiscal issues to a sector of the economy of national interest. However, those actions cannot ever give preference to a chosen group of investors; they must benefit generally the whole sector without damaging other one.

Regarding to those incentives or measures, in terms of internal taxes, they need the validation of the SENIAT, and the compulsory approval of the Parliament.

C. Tax Auditing Division for Mining, Hydrocarbons and Related Activities

The SENIAT, to pursuant its power of developing the structure required to enhance the level of tax collection, created the Tax Auditing Division for Mining, Hydrocarbons and Related Activities, to attend mostly special taxpayers involved on those activities that belongs to the largest source of income of the Venezuelan Treasury. Consolidating the core responsibilities granted to this division, they are:

- Apply, supervise and control tax investigation at all to this sector.
- Apply and control the auditing relating to penalties and calculation of interest, whether it applies.
- Develop methods to analyze and detect tax evasion and measures needed to prevent it.
- Be part of the tax investigation
- Prepare technical guidelines for the design and application of computer systems related to those activities.

V. Where We Stand and Where We Go?

A. Cero Evasion Plan 2005

The Venezuelan Tax System is now entirely framed by the Cero Evasion Plan. After the success in collection experienced in 2004 (around Bs. 24 billion), the National Intendent of Internal Taxes announced that they will emphasize and expand the length of the effect of this plan by creating new models of examination applied on sectors that have not been examined as a whole yet. Literally expressed by the Officer to the media that “the Evasion Plan Cero has as core objective to collect and increase the subjective risk among the taxpayers”, which means the risk to be examined. The goal of collection for 2005 is around Bs 27 billion in which would be 54% for VAT, according to information of the Superintendent of National Customs and Taxes.

Examination on Individual Taxpayers

As part of the expansion of the Cero Evasion Plan, the SENIAT will start conducting examinations to individual income taxpayers. Because of this plan begun with the corporate taxpayers, and one of the core goals advocated by the Tax Administration is to induced more level of compliance, they will prepare a strategy for examination, which would be enforced by analyzing and processing individual taxpayer’s information, making comparison between that information, the rest of taxes linked and the taxpayer return mainly. As it happened in the case of corporate taxpayers, the SENIAT may impose several sanctions in reference to the articles mentioned before for this plan.

Examination on Suppliers of Public Sector

Among the strategies to enforce for 2005, the SENIAT is preparing intensive examination aimed to public sector’s suppliers. Apart from being taxpayers, the rationale that moves this focusing establishes that whether a business or commercial activity is a supplier of the public sector, it is an unavoidable condition to be on time and regularized, in terms of the tax system and tax liabilities.

B. Tax Land Registration

After visiting many farms and lands in specific zones within the country, in which the Government, jointly to the SENIAT and the State Governments, have started to check the property of landlords in order to prove accurately their property and the level of agricultural productivity they are used for. In the meaning of raises the growth of the small-sized agricultural sector, the Government through its tax administration is already requesting part of the unutilized lands to be redistributed among the non-own-land country people who work with crops.

After many claims, the SENIAT is requesting all landowners to be registered from January 2005. In that registration must be proved the property of lands. The next stage, will end up in a new tax for unused lands or “idle lands”, in terms of agriculture, to the extent of making a research among the SENIAT, the National Institute of Lands (INT) and the Geographic Institute “Simón Bolívar”, to develop the tax mentioned.

C. Reduction of Value Added Tax Rate and Exchange Surplus of the Central Bank

The Ministry of Finance has announced the strong possibility of the reduction in the VAT rate for 2005. This rate was already reduced during 2004 from 16% to 15%, as a measure to boost the economy of the country. However, the reduction was slightly appreciated by the President of the Associations and Chambers Federation of Venezuela (FEDECAMARAS), organization which

gathers most of the private sector, by expressing a low level of growth within the Venezuelan economy.

In the same announcement, the Ministry of Finance still confirmed the requesting made by the Central Government to the Central Bank of Venezuela to share out the exchange surplus obtained from the exchange control system, for the administration to spend them in welfare programs.

D. State Public Inland Law

The State Public Inland Law that is created to decentralize the Venezuelan Tax System from taxes with national competence to local administration partly, in order to give more autonomy, and harmonize the municipal and State taxes nationwide.

Summarizing, the enforcement of such State law allows local governments to move from 6% of current administration of the total income to 13.4%, in principle. Later, granting a percentage of the national VAT rate (as in Japanese Tax System), they may raise to administer up to 24% of national income, which represents 1.5% of GDP, whether it is applied the highest tax rate permitted. Certainly, this applies by decreasing national VAT rate.

It is worthwhile to point it out that this law is already an axis of controversies from many sectors. For example, some specialists sustain that the legal instrument in discussion allows local governments to get indebtedness, though that law deems measures to avoid so, they are not enough. On the other hand, the State Public Inland Law should be a matter of pride by the Government, because it makes fiscal policy to move forward, but instead, the General Attorney of the Republic announced relevant objections to that law, which is expecting for the Supreme Court to enact a settlement.

E. Unique Tax Law

There are small-sized businesses and self-employed persons that are exempted or VAT's Formal Taxpayers, so the SENIAT and the administration are designing a "monotax" or unique tax for such taxpayers.

F. SIGECOF

The SENIAT and the IADB are currently making new agreements to enhance the tax system in the country. At this time, this agreement is focused in two main objectives: i) Jointly the SENIAT and the Ministry of Education, Culture and Sports, to develop educational materials to give tax education to scholars, and ii) the modernization and automation of the tax administration as a whole.

G. Harmonization of the Andean Community

Within the VIII Advisor Council of Ministries of Inland or Finance, Central bank Governors and those who are responsible for Macroeconomic Planning of the Andean Community Countries, agreed to harmonize the Value Added Tax and any other consumption tax within the community. This must be officially enacted during 2005.

Although there are have gone through many circumstances experienced during the last decade, Venezuela has enhanced its tax administration, applying several tax instruments and tax reforms that are still in process to achieve the development of a well-structured tax system.

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