

CAUSES OF TAX REFORM IN LATIN AMERICA, 1977–95¹

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Abstract: Among the policy changes associated with neoliberalism in Latin America, tax reform has played a leading role as it has been crucial not only to price stabilization but also to managing economic liberalization. But it also has a larger significance, since it involved a reconstitution of core state powers, and these could prove useful to any future government that seeks to expand the state's economic role. This paper seeks to determine its causes more precisely by analyzing data from fifteen Latin American countries from 1977 to 1995. Findings show that the definition of "tax reform" has been remarkably similar across the region with less progressivity, fewer exemptions, a new leading role for the value-added tax (VAT), and the strengthening of tax administration. The data analysis then finds reform is predicted by (in roughly descending importance) past inflation, explicit IMF performance conditions, new administrations, more authoritarian-elected governments, the dominance of the president's party in the legislature, established electoral systems, closed-list proportional representation, less polarized party systems, and more numerous parties. Little or no support exists for the causal importance of past changes in gross domestic product (GDP), the constitutional powers of the president, party institutionalization, or partisan balance. The analysis concludes by placing these results in historical context, referring to theories of state formation and the building of institutions in exchange for resources.

In the drama of Latin American policy changes during the late twentieth century, tax reform played a pivotal role. It was crucial to price stabilization, which depended on finding a substitute for the inflation tax; it supported trade liberalization, in that the most common tax reform, the introduction or expansion of the VAT, made up for cuts in

1. The first stages of work on this project were funded by the National Science Foundation under SPS-9320878. I would like to thank the staff of the Archives of the International Monetary Fund for their helpfulness, and Leonora Dodge and Martha Rodríguez for dedicated research assistance. Thanks to Ken Shadlen, Carlos Elizondo, Jonathan Conning, Kurt Weyland, Marcelo Bergman, and three anonymous reviewers for comments on previous versions or fragments of this study. Thanks also to Samuel Morley for sharing his tax reform index database with me. Details of the data analysis and spreadsheets of key variables are available at <http://www.williams.edu/PoliSci/mahon.htm>. My entire database is available to any interested researchers upon e-mail request to me at jmahon@williams.edu.

Latin American Research Review, Vol. 39, No. 1, February 2004

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tariffs; and it often played a big part in efforts to change economic incentives on the “supply side.” Yet it has a more fundamental claim to importance as well: major reforms of tax law and administration, complete with new penalties for evasion, amount to a real reconstitution of a core area of the state, with implications for its relationship with civil society (Bird and Casanegra de Jantscher 1992; Durand 1994; UN-ECLAC 1998). In more practical terms, for many Latin American governments the new taxing power will prove especially useful as they seek to extract resources—either because they face higher debt service costs or because they wish to increase public spending—without compromising economic growth. Tax reform matters a lot even if, or especially if, Latin American governments decide to break with neoliberal orthodoxy.

Despite this importance, we do not have a precise idea of what, in general, brings about tax reform. In the literature on Latin America, no study has tested hypotheses about its determinants over a large data set. There are good general treatments of the policy choices involved (Brodersohn 1988; Bird 1988; Gillis 1989; Goode 1990; Gillis, Shoup, and Sicat 1990; Thirsk 1997, chap. 1) and fine discussions of politics and policy in particular cases (e.g., Gil Díaz 1987; Mann 1989; McLure 1989; Elizondo 1994; Boylan 1996; Weyland 1996, chap. 5; Thirsk 1997, chaps. 2–9). The most important region-wide studies confine themselves to descriptions of the trend (Shome 1992, 1995), to understanding the macroeconomic peculiarities of Latin American taxation (Cowan, Betancour, and Larraín 1999), to theoretical underpinnings without broad empirical testing (Ascher 1989; Bates 1989), or to a useful and rich but unsystematic exploration of causes (Bird 1992; Rodríguez 1993; Carciofi and Cetrángolo 1994; Elizondo 1995; UN-ECLAC 1998). This paper attempts to fill this gap with empirical results from a broad study of the determinants of tax reform in fifteen Latin American countries from 1977 to 1995. Drawing on these results, it then explores their implications for our ideas about policy reform and institutional reform more generally.

Briefly, it finds first of all that the major elements of recent tax reforms have been remarkably similar across Latin America, as indeed they have been across the globe. The great majority involved the reduction of rate progressivity in personal and corporate income taxes, a decline in special exemptions, the institution or expansion of the VAT (along with a decline in tariffs, as just noted), and the creation of stronger tax administration and penalties for evasion. Turning to the determinants of reform, the data analysis finds reform related to past inflation but not to past GDP growth. It shows that reform often takes place when the International Monetary Fund (IMF) makes it a performance condition for its loans, but is even more likely when IMF conditions are placed on a government in its first year. Well-established political systems are more likely to see reform, but governments are less likely to undertake it the

longer they have held office. Authoritarianism does not predict reform except, relatively speaking, in the narrower range of variation among elected governments. Characteristics of a country's party system also show somewhat unexpected relationships to tax reform: having stronger, more institutionalized political parties appears to have little effect; closed-list proportional representation (PR) and the number of parties in a political system have a weak positive association with reform; and party polarization has a weak negative association. Finally, partisan dominance, rather than partisan balance, seems to favor tax reform.

The next section describes the nature and the notable similarity of tax reforms undertaken in Latin America over the past three decades. The succeeding section introduces the relevant literature regarding the causes and significance of tax reform, focusing on studies of taxation, neoliberal reform, and the politics of state reform and resource extraction. Operational definitions of key variables, the form of the data analysis, and the results, qualitatively and statistically, follow. The last section of the paper speculates briefly about what these results mean in historical context, referring to theories of state formation that involve "fiscal contracts," or the building of institutions in exchange for resources.

TAX REFORM IN LATIN AMERICA: ITS NATURE AND EVOLUTION

It is not obvious that there should be a single definition of "reform" when it comes to taxes. Rates and progressivity might rise or fall, and so might the relative share of direct and indirect levies, personal and corporate taxes, and so on. Yet just as the general sense of the word "reform" gained (in Latin America as elsewhere) a particular connotation as it was used to describe the dominant neoliberal trend in policy change in the 1980s and 1990s, so did Latin American tax reforms move in remarkable near-unison during the period.² Hence, for the present purposes we can define the term unambiguously. Its core elements include, first, a decline in the progressivity of personal and corporate income tax rates, coupled with a reduction in special exemptions (which had become especially common on the corporate side). That is, there has been a new priority on "horizontal equity" (across sectors of the economy and households of similar income) over "vertical equity" (progressivity), despite the acknowledged failure to tax the richest ten percent of households effectively (Carciofi and Cetrángolo 1994, 13, 27). Second, it has generally meant the institution or expansion of the VAT, along with a decline in

2. I realize that this ignores, for the moment, that reforms with different primary goals (revenue enhancement, efficiency enhancement, or redistribution) might have different causes. Some of this might be captured by examining differences in results between the two indices used here—as I suggest with reference to regime age, below.

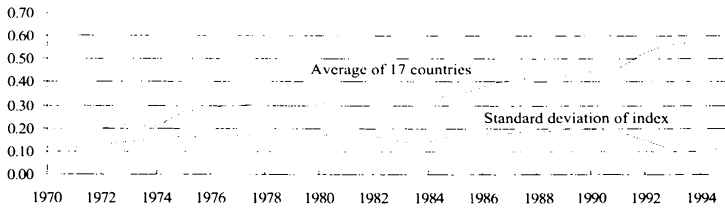
tariff revenues (and an even greater fall in tariff rates). Third, there has been a push to simplify tax regimes, eliminating, for example, old stamp duties and special excises. Finally, tax reform has meant more controlled and rationalized tax administration, sometimes involving the creation of new administrative units, along with changes in the tax code to permit more severe penalties (including prison sentences) for evasion.

This trend can be seen clearly in two different ways. First, in a 1999 ECLAC study, Morley, Machado, and Pettinato constructed a tax reform index for seventeen countries in Latin America and the Caribbean. The index contains four equally weighted components: maximum marginal tax rates on corporate and personal incomes (in which a reduction counts as a positive contribution to the index); the VAT rate; and the efficiency of the VAT (defined as the ratio of the VAT rate to VAT receipts, the latter expressed as a proportion of GDP). The index rises as income rate progressivity declines, as VAT rates rise, as the VAT covers more of the economy, and where it is imposed, is evaded less. Thus the study defines "reform" somewhat more narrowly than the description given above, but still captures its most important points: a combination of falling progressivity of direct taxes (in rates, though perhaps not in incidence), greater reliance on indirect taxes, and rising efficiency in the collection of the latter.

Figure 1 shows an average of these reform indices for seventeen countries in Latin America and the Caribbean, along with the standard deviation across the set in each year. (If Latin American governments were a company of soldiers and the index's sign their direction of march, the top curve would give the company's position and the bottom curve, the degree of dispersion of its ranks.) As can be seen from the figure, the index shows a fairly steady rise in regional tax reform over the period, in 1975, the years 1985–87, and especially 1992–93, being important moments for tax reform regionally. It is also notable that the standard deviation of the index falls in the last period, and stays low, reflecting the establishment of a new regional norm for "reformed" tax policy.

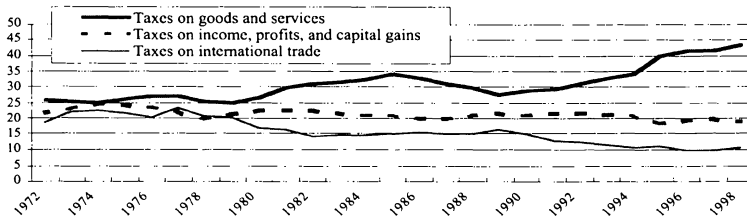
We can see another portrait of Latin American tax reform by looking at changes in the sources of tax revenues. Figure 2 shows the evolution of three kinds of revenue, averaged over fifteen countries (compared to the ECLAC set, it excludes El Salvador, Honduras, and Jamaica, while including Panama), from 1972 to 1998. This is the set of countries covered (though only for the period from 1977 to 1995) in the data analysis in the next section. As the figure clearly shows, while revenue from income, profits, and capital taxes declined only slightly over the period, there is a clear and nearly symmetrical pattern of falling inflows from trade taxes and rising revenues from taxes on goods and services (here, chiefly the VAT). In the mid-1970s, trade duties accounted for about a fifth of total tax revenues, while goods and service taxes supplied about

Figure 1. Tax reform index, seventeen countries, 1970–1995



Source of data and authors of index : Morley, Machado, and Pettinato, 1999

Figure 2. Tax revenue by type, fifteen countries, 1972–1998 (percent of total revenue)



Source: World Bank, *World Development Indicators*

a quarter; by 1998, the relative weight of the former was cut in half, to 10 percent, while the latter accounted for over 43 percent of tax revenue. In these changes Latin America broadly followed global trends (cf. Thirk 1997, 18–27).

EXPLAINING REFORM

Now that we have an idea of the character of recent tax reforms in Latin America, it remains to investigate what has brought them about. We can gain insight into this subject from works in several areas—those specifically on taxation (e.g., Ascher 1989; Bates 1989; Bird 1992; Elizondo 1995; Morley, Machado, and Pettinato 1999), those that consider tax changes as part of liberal economic reform (Haggard and Kaufman 1992; Williamson and Haggard 1994; Weyland 1998), those that describe it as part of a democratic transition (Boylan 1996), and those on administrative

reform (Geddes 1994; Heredia and Schneider 2002). In broad terms, we find here three areas of focus—economic crises, international influence, and domestic politics—of which the last is by far the most varied, contested, and potentially informative.

Economic Crisis

Since Aristotle, political scientists have commonly and repeatedly posited that emergencies enhance state power and are good moments to introduce major policy or institutional changes. What Levi (1988, 105–08) posits about the role of war in facilitating taxation in early modern Europe might apply to contemporary situations of dire economic stress. Regarding recent Latin American reforms, Weyland makes this point by drawing on prospect theory psychology. He argues that because a crisis (especially one involving hyperinflation) creates expectations of future decline under the status quo, it makes it more likely that leaders will take—and voters approve—a risky path of bold reform, even if this means paying short-term costs (1998). Thus leaders overcome the institutional context of “normal politics,” and political-institutional considerations contribute less to explaining their actions (646). Other observers differ on this point. For Haggard and Kaufman (1992), since “different governments have widely different thresholds of tolerance for economic distress,” even though crisis is important we should also look to “other organizational and ideological factors” to explain policy outcomes (21). A study by Williamson and Haggard also found that “crisis is neither a necessary nor a sufficient condition to initiate reform” (1994, 565). Observers of tax reforms express a similar range of conclusions. From a wide variety of Latin American experience, Bird (1992) concludes that “major changes in tax structure and administration are usually possible only when times are bad, during a crisis of some sort. Only then is it possible to overcome the coalition of political opposition and administrative inertia that normally blocks significant change” (32).

However, Ascher notes the importance of a sense of crisis to tax reforms in Colombia, concluding that, in general, financial crises are good moments to introduce reforms “if the government maintains both credibility and good macropolicy” (1989, 464). Moreover, many governments first responded to the economic turbulence of the 1980s by adopting a technically easier and fiscally less risky strategy of raising rates on existing taxes, not by overhauling the whole system (e.g., see Dain and Menandro 1993, 21–22). We might also need to distinguish between reforms carried out in a context of crisis—aiming mainly at stabilization—and those pursuing “non-revenue objectives” (Carciofi and Cetrángolo 1994, 28–29).

International Influences

To many the most remarkable thing about neoliberalism in Latin America has been its uniformity across the region, leading to the conclusion that external forces caused it. Looking at the overall trend of reform in the 1980s, Barbara Stallings argued that the rush to privatization and liberalization in the 1980s, especially in the latter half of the decade, is *prima facie* evidence that external forces were operating. She finds it hard to construct an argument suggesting that domestic forces just happened to coincide in so many dissimilar countries to bring about such similar policy decisions (1992, 82).

Indeed, the IMF, World Bank, and the Inter-American Development Bank (IDB) have energetically funded and advised governments undertaking tax reform, while the IMF has often made it a performance condition (Barbone et al. 1999; IDB 1995). By this reasoning, Latin American countries, once encumbered with debt, had to accept the dictates of the institutions that offered relief or renewed access to capital. For example, a Costa Rican observer noted, somewhat bitterly, that because governments required agreements with international financial institutions (IFIs) in order to obtain recognition from financial markets, and such recognition was needed for loans and trade, “Costa Rica’s tax system will change” (Alvarez 1994, 7). Drawing on many years observing Latin American taxation, Bird concurs, though for different reasons, that major explicit tax changes are almost invariably political dynamite, which is one reason why they usually occur only when no other option is open. In Latin American terms, this point has too often meant only when the IMF really puts on the pressure (1992, 23, n. 26).

It might also be true, however, that the importance of foreign pressure is often overstated, possibly for domestic political consumption, as politicians blame hard decisions on the IMF or the World Bank. Leaders might enjoy substantial autonomy—demonstrated, perhaps, when they enact austerity programs even tougher than those demanded by the IMF. For example, the Bolivian senate passed the reform of 1986 in a marathon session to make (barely) a deadline established by the IMF, even though the IMF did not specify the nature of the reform and was not its principal author (*FBIS Latin America* 5/21/86, C01; Mann 1989, 384–87). All in all, foreign influence does not have to be conflictual or even direct to be effective. For Williamson and Haggard, the effect of IMF conditionality is most plausibly described as strengthening the hand of reformers internally by making external resources available for reform (1994, 567).

Obviously, this ties in with the notion of crisis, since it is unusual scarcity that makes the offer of resources powerful and after all, it is under such conditions that countries approach the IMF in the first place.

This would imply a pattern of reform across the region similar to, though perhaps later than that predicted by the degree of economic crisis.

Political Conditions

As noted above, neither an economic crisis nor an IMF agreement necessarily implies that a tax reform will follow. Governments might have a high tolerance for inflation and declining income, or they might craft a solution that avoids tax reform. They could also manage to avoid the IMF or at least, in negotiating a letter of intent, keep tax reform and fiscal conditions out of it. Failing this, they might just flout such conditions, as many have. Hence domestic politics ought to be a major part of any explanation of tax reform.

There is also a more fundamental question of domestic politics here, one that historically connects taxation and the state. Rational-choice analysts have painted a picture of state formation in early modern Europe in which the evolution of taxation plays a central role (e.g., Tilly 1975, 1985; Levi 1988; Kiser and Hechter 1991). According to one hypothesis, parliaments arose as states found it necessary to tax increasingly mobile assets (Bates and Lien 1985). If this is right, "no taxation without representation," or rather the converse, should be regarded as a widely occurring historical tendency. Of course, on this score Latin America diverged considerably from early modern Europe. First, the taxation of assets never constituted a major source of state revenue (in general, see Centeno 1997, 2002). In addition, the entry of the popular sector into politics pushed states even further from the prototypical relationship between taxation and formal representation, as the wealthy gave up terrain in legislatures but kept their influence behind the scenes. Nevertheless, participants and observers tell us that recent tax reforms in Latin America *did* seem like bargains in which new tax revenue was granted in return for assurances of more responsible and transparent government (Durand 1994, 1; Cámara de Comercio de Caracas 1994, 2), or that they failed because these issues were not dealt with satisfactorily (Elizondo 2001). If so, we ought to expect that reforms would be easier to accomplish where institutional variables (such as the election cycle or the party system) facilitate such "fiscal contracts."³

Even if we agree that tax reform is a fundamentally political issue, what political characteristics might be relevant to achieving it? Here the literature is somewhat divided. For the purposes of this analysis, I have grouped political conditions into four areas: the degree of authoritarianism or (within democratic systems) executive dominance; the age of the government in

3. Cf. UN-ECLAC 1998. The first use of this term, to my knowledge, is Carciofi 1990.

power and of (democratic) systems; party system institutionalization, fragmentation, and polarization; and finally, partisan balance and the rules, under proportional representation (PR), for the voting of party lists.

1. Democracy, authoritarianism, and presidential power. Based on the experience of the 1980s, Kaufman and Stallings saw authoritarian regimes (along with established democratic ones) as more likely to undertake economic policy reforms (1989, 205–12). Haggard and Kaufman also observed that “the most comprehensive adjustment initiatives have generally come under the auspices of authoritarian regimes,” yet they go on to qualify this statement by stating that authoritarianism does not guarantee, nor democracy prevent, the kind of political autonomy necessary to undertake major reforms (1992, 32–33). Weyland’s prospect theory, by contrast, entails that insofar as democratic procedures regularly bring to power presidents unencumbered by status-quo bias, democracy makes bold reforms more likely (1998, 669).

Looking more narrowly at taxes, the picture is equally mixed. VATs have been famously initiated under authoritarian regimes—Brazil in 1968, Chile in 1975, Guatemala in 1983, and Ecuador in 1970. But democracies have imposed them, too—for example, as in Costa Rica and Uruguay (1968). In Paraguay a VAT did not arrive until after Stroessner was toppled. Looking more closely at elected regimes, it may be possible that even under crisis conditions, legislative interests might push for the retention of tax exemptions. To overcome these obstacles, elected leaders could move in an authoritarian direction, perhaps resorting to the decree powers granted under states of exception. In Bolivia the passage of tax reform coincided with political protest by unions and threats by the Interior Ministry to enforce a state of siege (although none was actually called in the crucial months of mid-1986). In Peru, Fujimori deepened his tax reform after the *autogolpe* of April 1992, but he did so using powers granted to him by a law passed in 1991 (Durand 1994, 19).

The last theme relates to the constitutional power of the executive. It may be the case that, within a Latin American context dominated by presidential systems, major reforms are more likely where the president has significant powers to decree or to introduce legislation (Shugart and Mainwaring 1997, 40–52).

2. Age of the system and of the government in power. Tax reforms might be easier to undertake in well-established systems, if political actors feel more confident that the rules will be respected and hence, feel less pressure to behave opportunistically. As noted above, Kaufman and Stallings conclude from the experience of the 1980s that while authoritarian regimes often enacted significant neoliberal reform, governments under established democratic systems—as opposed to new democracies—

reformed even more often. Settled democratic procedures could allow for more successful reorientations of economic strategy (1989, 201–33).

As for the age of the government in power, it accords with experience that major reform projects succeed best in the first months of a new administration, when the executive still enjoys the election's popular mandate without having the time to elicit much popular disappointment by actually governing (cf. Thirsk 1997, 27). Thinking in terms of fiscal contracts, if a reform raises the tax burden through a broadly incident VAT, it might be especially important for it to quickly follow the broadly enacted consent entailed in a presidential election. As already noted, Weyland also posits that new leaders are more likely to be free of status quo bias, and thus to undertake risky reform projects, especially if they face a crisis upon taking power (1998, 650). Hence there are various reasons to expect reforms to be more likely to happen early in an administration.

3. Party-system institutionalization, fragmentation, and polarization. In recent years, there has been a renewed appreciation for the role of strong parties in the preservation and deepening of democracy. Mainwaring and Scully argue that having a multitude of parties, especially in the presidential systems that dominate Latin America, tends to encourage polarization and create other problems of governability (1995, 28–33). Most relevant here, they argue that better institutionalized party systems make major policy reforms easier to accomplish, because they entail disciplined support in the legislature (and in the ruling party's organizations) for the executive's policy initiatives (26). In a similar way, Haggard and Kaufman have argued that party system fragmentation is likely to cause delays in the initiation of stabilization and adjustment measures and, if class-based polarization and policy immobilism continue, could encourage coup-makers to break the deadlock (1992, 35). These considerations ought to matter for tax reforms, since these generally require legislative approval and often involve the elimination of sectoral tax exemptions championed by legislators on behalf of particular interests.

4. Partisan balance and closed-list PR. Related and more specific hypotheses about parties and policy change can be gleaned from work on the reform of public administration. As we have noted, tax reform often involves the creation of new merit-based administrative bodies and empowers these bodies to punish tax evasion. Tax reform projects have also called for the elimination of special rates and exemptions for favored sectors. Hence their passage might depend on overcoming the resistance of legislators who use the tax code (or impunity for well-connected tax evaders) as vehicles for clientelism (Carciofi and Cetrángolo 1994, 36; for a broader version of this argument see Stein, Talvi, and Grisanti 1999). In this way,

tax reforms might resemble civil service reforms and thus represent important watersheds in the development of the state. Geddes (1994) argues that reforms eliminating bureaucratic spoils in favor of a merit-based civil service depend to a large degree on the nature of the party system. Above all, reforms are more likely when the major parties are in approximate balance in the legislature, so that even when enjoying power, none of them regard their future access to spoils as assured (chap. 4). In addition, reform is more likely to win legislative approval when party leaders can enforce interparty pacts on their members in the legislature; this capability, in turn, improves under a closed-list PR system, in which party leaders determine the order of party lists on the ballot (102–03). However, against the balance hypothesis, tax reforms might best be promoted under conditions of dominance by the president's party—that is, circumstances that facilitate approval of legislative initiatives coming from the executive (Thirsk 1997, 27).

Before proceeding, it remains to emphasize that while to some degree these theories are complementary, they are also at odds on many points. While a focus on economic crisis does not necessarily entail a view of politics and political institutions as passive or “superstructural,” Weyland's focus on how crisis prompts executive-led reform largely removes these from the picture: hyperinflation and the arrival of a new president produce a determined embrace of risk both at the top and by a willing public. By the same token, if external forces set the reform agenda, determining the shape and, in broad terms, the timing of reform, it would be wrong to emphasize the importance of political institutions and the election cycle.

DEFINITIONS AND DATA SOURCES

The basic model posited here contains two operational definitions of tax reform and several clusters of variables corresponding to the categories noted above.

Tax Reform

Tax reform is here defined in two ways, one drawing upon the existing literature and the other, developed here, focusing on the legislative passage of reform initiatives. The first is simply the year-to-year change in the tax reform index of Morley, Machado, and Pettinato, discussed here and featured in Figure 1. However, while this index is a useful sum of several reform indicators and a continuous function between 0 and 1, it is also likely to blur a focus on politics because it tracks some key legislative moments only with a (variable) lag. This happens for two main reasons: first, some legislation calls for the delayed implementation of changes in

rates or tax types (as in Mexico, where a reform passed in late 1978 went into effect in 1980), understandable where new taxes require new collection methods and institutions; and second, VAT efficiency might rise only gradually after the enactment of a law creating a new administrative and enforcement body. Values for the index (here called the MMP index) appear on page 1 of the summary tables in the on-line appendix (available at <http://larr.lanic.utexas.edu/appendix/Mahon.htm>). Statistical tests using the year-to-year changes in the index appear in table 1.

The second tax reform index focuses on legislative moments but at some cost in reproducibility and mathematical neatness. Somewhat more broadly than the rate- and efficiency-based indicator of Morley, Machado, and Pettinato, it defines tax reform as the institution of a VAT, the expansion of the VAT, the elimination of stamp and other minor duties, the simplification and broadening of personal or corporate income or assets taxes, or the revision of the tax code to enact comprehensive administration of taxation and institute criminal penalties for evasion. Like the other index it uses a 0–1 scale; a thoroughgoing tax reform, marked by all or nearly all of these policy changes, would come closer to a score of 1 on the tax reform index. Only one or two of these policy changes would put the index in the range of 0.2. Rises in tax rates, if accompanied by only minor changes in coverage, count as 0.1; unusually large tax cuts or the addition of numerous exemptions are counted negatively (–0.1). In some cases, legislatures changed tax code provisions that had been the subject of earlier reforms; these “re-reforms” would show up more strongly in this index than in the MMP index. Moreover, many reform packages, either as initially proposed or as finally passed, could be regarded as mixed, with some measures representing steps forward in reform and other measures tending backward (e.g., Guatemala in 1987). Coding these packages obviously calls for an exercise of judgment. The moment of reform is marked at the time of the final approval of the measures, usually in the legislature. This variable (TAXREF) appears on page 2 of the summary table in the appendix. Statistical tests using it appear in table 2. Its simple correlation with year-to-year changes in the MMP index is 0.307.

Economic Crisis

With regard to the first set of explanatory variables, the analysis should begin by separating the unproblematic and expected influence of economic crisis—deriving from a major shortfall in public revenues—from those aspects whose influence on policymakers is of greater interest. For this reason, we begin by making the previous year’s fiscal deficit (FISCBAL) a control variable. Expressed as a proportion of GDP, here it is lagged one year to separate cause and effect.

We can also think of crisis in a way that captures *public* perceptions of economic conditions, in order to chart the effect on policymakers by this route. Perhaps the most alarming indicator of crisis—and the one whose possible effects on policymakers' choices were discussed above—would be inflation. For reasons noted above, it is also lagged one year. The inflation variable (INFLN) is the logarithm of the consumer price index inflation rate from the previous year. Another indicator of economic malaise would be the growth rate in GDP, again lagged one year (the variable GDP).

International Pressure

For the purposes of data analysis, international pressure is the trickiest variable to operationalize and measure. A general sense of international pressure might be visible in the country's bond rating or the "country risk" premium it pays on bonds issued internationally. However, such measures exist only from about 1992 onward, and they do not capture the pressure to reform the tax system specifically. Another general measure of international pressure, available for the entire period under study, would simply be whether or not the country's government has concluded an agreement with the IMF (a Standby Agreement, Extended Funds Facility, Structural Adjustment Facility, Enhanced Structural Adjustment Facility or, in rare cases, a Rights Accumulation Program). However, this says nothing about what was actually stipulated in the agreement, whether or not tax reform was on the list of performance criteria. A more refined operationalization of the variable, then, ought to take this information into account.

This refinement required extensive consultation of IMF documents for the period in question (the IMF releases the relevant documents only after a period of five years). Following this procedure, IMFCOND has a value of 1 where the IMF explicitly made the passage of tax reform a condition of disbursement of higher-tranche monies. Where the IMF stipulates overall fiscal deficit targets, this would also tend to encourage tax reform. How should this condition be scored for our purposes? To comply with it, governments might cut spending (as most did, especially in public investment, in the years immediately after the 1982 debt crisis) or raise taxes, perhaps with a major tax reform. If these were the only two alternatives, IMFCOND would merit a value of 0.5 when the IMF sets fiscal targets. But the general character of the fiscal target creates a third possibility—to do nothing, waiting to see if exogenous trends (e.g., an economic recovery or a rise in export prices) put the country in compliance. For these reasons it is appropriate to put the value of IMFCOND at 0.3 when the IMF states deficit targets as performance conditions. Because performance conditions are generally enforced contemporaneously,

IMFCOND represents the same year as the tax reform outcomes in the regressions. To check for delayed effects of such conditions, however, a lagged value of this variable (IMFLAG) was also put into the model.

Political Variables

As noted above, political variables fall into four categories: degree of authoritarianism or (within democratic systems) executive power; government and (electoral) system age; party system institutionalization, fragmentation, and polarization; and finally, the degree of partisan balance and the presence or absence of PR party list rules. The last two sets of variables refer entirely to the abbreviated data set, comprising only those countries and years above a democratic threshold (the next section). The first two sets refer both to the large data set and its more democratic half.

Authoritarianism and Presidential Power

In studying the effect of regime type on economic outcomes, we need to avoid considering all elected regimes as equally democratic, since many abridge labor and other rights, lack independent judiciaries, or, perhaps more important for the present topic, operate under states of emergency in which the executive has decree powers over matters relevant to tax policy. Thus, despite all the difficulties this entails, it makes sense to make regime type an interval variable. This analysis uses values given by the Polity IV dataset (Marshall and Jaggers 2000) for its DEMOC variable. Here it is referred to as POLDEM and ranges from 0 for violently authoritarian to 10 for very democratic. For the purpose of defining “democracy” to restrict the ranges of other variables (see PRESPOW and TENDEMSYS), I have chosen a threshold POLDEM value of 4.

Turning to the degree of executive dominance in a democratic context, for present purposes presidential power (PRESPOW) is coded on a scale of 1 to 4 according to the classification of Shugart and Mainwaring, noted above (1997, table 1.6, 49), excluding the most authoritarian cases (thus PRESPOW has a value only where POLDEM scores 4 or above).

Years in Office and Age of (Democratic) Systems

Values for both of these variables are derived from Philip Keefer’s “Database of Political Institutions” (version 3.0, May 2001, available at the World Bank’s Internet address). The first value (called YRSOFFC both in the DPI and here) is included in all equations in table 1 and in the larger data set in table 2 (Equations 1–3). The second value represents the DPI’s variable relating to the tenure or age of the political system, for all systems (TENSYS), but limited to cases here defined as

democratic (those in which $POLDEM > 3$) for reasons noted above. The variable is labeled *TENDEMSYS* in tables 1 and 2.

Along with the government age variable (*YRSOFFC*) just described, a dichotomous variable for the presence of a new administration was created (called *NUADM*, it appears on page 6 of the appendix) and tested on the legislative index of tax reform. It was coded 1 in the same year as the inauguration if this happened before 1 July; if not, it was 1 in the next year. It appears in table 2, equations 4–6, accompanied by its interaction product with *IMFCOND* and *INFLN* in the last two equations.

Party-System Institutionalization, Number of Parties, and Polarization

These party system variables are derived from Mainwaring and Scully 1995 (tables 1.6, 1.7; figure 1.1, pp. 17, 30, 31).

Closed-List PR and Partisan Balance

PR rules come from the “Database of Political Institutions,” in which the variable *CL* takes a value of 1 if closed lists are used and 0 if they are not. This variable here is called *CLOSED*. Partisan dominance or balance can also be measured with DPI variables. The DPI variable *MAJ* gives the fraction of legislative seats held by the government. The index of partisan balance is equal to 1 minus twice the difference between 0.5 (perfect legislative balance) and *MAJ*. Thus a governing party that occupied half the seats in the legislature would have a *MAJ* value of 0.5 and a *BALANCE* value of 1, while a government holding all the seats (or none) would have a *BALANCE* value of 0.

Six specifications of the model are offered for each definition of tax reform, for a total of twelve equations (tables 1 and 2). The first three specifications refer to the larger data set while the rest refer only to the more democratic part ($POLDEM > 3$) of the data set. Data analysis took the form of linear regressions of cross-sectional time series, with panel-corrected standard errors (cf. Beck and Katz 1995), allowing for across-panel heteroskedasticity on the estimates and correcting for contemporaneous correlation between countries.⁴ They also included panel-specific correction for first-order autocorrelation. The overall data set was composed of fifteen countries over nineteen years, yielding a maximum of 285 observations of each variable.⁵

4. Heteroskedasticity was substantial. Cook-Weisberg tests were conducted on the variables in equation 4. Using fitted values of tax reform on the MMP index and the legislative index, the null (constant-variance) hypothesis was rejected with chi-squared values of 25.23 and 26.18, respectively.

5. It is a valid question whether it is appropriate to treat the second, judgmental

RESULTS AND DISCUSSION

The regressions show some expected and some surprising results. We find significant coefficients with expected signs on only one of the economic variables, inflation, and strong evidence that tax reform occurs when a government is under explicit IMF fiscal conditions, especially if it is new in office. We see no significant effect from authoritarianism when considering the entire gamut of regimes, but among elected regimes it does appear that the relatively more authoritarian ones reformed more readily. The analysis also gives some evidence that governments (democratic or not, IMF conditions or not) reform less the longer they are in power (the rare exceptions might be new democratic regimes undertaking redistributive-oriented reforms), and that governments in established democratic systems are more likely to reform. (Though both inflation and newly seated governments were found to favor reform, their interaction was weak.) We can also see a negative effect from party polarization, a small positive one from party institutionalization, and an unexpectedly positive effect from the number of parties. The analysis shows effects of the wrong sign from partisan balance, even where it is interacted with inflation to check on cases where tax reform was not part of a stabilization effort. Partisan dominance is a better predictor of tax reform over this data set. Finally, there is a weak indication that closed-list PR favors reform. Let us consider these conclusions in more detail by referring to the variables and equations shown in tables 1 and 2.

Economic Crisis

As noted, the variables designed to capture the role of economic crises showed mixed results. The effect of the state of fiscal accounts (FISCBAL), treated as a control variable, is not significant in any equation and bore the expected negative sign a bit more than half the time. Inflation is expectedly positive on all and significant on all but a few of the equations (in these, usually because of the inclusion of an interaction term). Previous-year income growth (GDP) is significant in only one specification. Two anomalies were produced in equations including interaction terms with inflation and GDP growth (see section on authoritarianism and democracy).

measure of tax reform (focused on the degree and timing of legislative changes, table 2) as an interval measure—rather than as a binary phenomenon that would be better tested with logit or probit regressions. However, to do this would be to forfeit the real information derived from painstaking data collection on tax reform packages across fifteen countries and almost two decades. TAXREF is treated as an interval variable because it is felt that the arithmetic differences across coded values, say, of 0.1, 0.4, and 0.8, constitute a reasonable approximation of real variation, and are thus suitable for inclusion in a multivariate linear regression analysis.

International Pressure

International pressure, here denoting explicit tax-reform or fiscal-balance performance conditions in an IMF agreement, seems to have been a major explanation of tax reform in Latin America during this period, particularly when a new administration was also in power. It seemed to have less effect, or less immediately, among the more democratic regimes, as can be seen in the tests of IMFCOND using the MMP index (table 1). The lagged variable (IMFLAG), referring to performance conditions imposed the previous year, was also a strong and generally robust predictor of tax reform on both measures of the latter. It also seems to be even stronger across the more democratic regimes.

Political Variables

As noted above, results for the political variables were mixed. Several were significant predictors of reform but a few of these had unexpected signs.

Authoritarianism and Presidential Power

The data analysis confirms the impression that authoritarianism and tax reform are generally uncorrelated. These results complement those of Cheibub (1998), which found no relation between regime type and taxing power. However, on the attenuated ($POLDEM > 3$) data set, signs were evident of an association between reform and the less democratic of the elected regimes. However, presidential power showed no effect, nor did the interactions of inflation and regime type ($INFLN * DEM$) or income growth and regime type ($GDP * DEM$).

Years in Office and Age of (Democratic) Systems

Here we find important domestic political explanations for tax reform. Regarding the first, over the large data set (not restricted to the more democratic regimes) the coefficient integer variable YRSOFFC is negative and significant on both indices (equation 1). As for the binary time-in-office variable, NUADM, as the fourth equation on table 2 shows, it is highly significant. The interaction terms show that both new administrations and IMF fiscal conditions are significant predictors of tax reform, and that they have a strong positive interaction. It appears that more of the effect of IMF conditionality depends on being in the first year of an administration than vice versa. Compared to the interactions just described, this analysis found a decidedly weaker interaction between time in office and inflation rates.

Table 1 Pooled Time-Series Results: Change in MMP (UN-ECLAC, 1999) Tax Reform Index

Explanatory variables	Model specifications (**=significant at 95%, ***=at 99% level; *=nearly significant, at 90%)					
	1 N=243	2 N=243	3 N=243	4 N=122	5 N=122	6 N=122
FISCBAL	-.0006 (.0007)	-.0002 (.0007)	-.0005 (.0007)	.0003 (.0008)	.0013 (.0008)	.0002 (.0008)
INFLN	.0140 (.0196)	.0170** (.0073)	.0150* (.0077)	.0193* (.0108)	.0280*** (.0109)	.0206 (.0145)
GDP	.0022** (.0010)	.0010 (.0007)	.0011 (.0006)	.0006 (.0011)	.0001 (.0010)	.0007 (.0011)
IMFCOND	.0482*** (.0171)	.0855*** (.0295)	.0476*** (.0168)	.0360 (.0232)	.0686* (.0387)	.0384 (.0236)
IMFLAG	.0384** (.0152)	.0364** (.0148)	.0371** (.0154)	.0520** (.0226)	.0412* (.0222)	.0498** (.0225)
POLDEM	.0005 (.0038)	-.0003 (.0011)	-.0004 (.0010)	-.0141* (.0084)	-.0208** (.0086)	-.0198** (.0089)
INFLN*DEM	-.0001 (.0021)					
GDP*DEM	-.0002 (.0002)					
PRESPOW				.0055 (.0141)	.0050 (.0130)	.0075 (.0144)
YRSOFFC	-.0020** (.0009)	-.0017* (.0009)	-.0029 (.0028)	.0011 (.0030)	.0028 (.0031)	-.0001 (.0072)
YRSOF*IMF		-.0163* (.0094)			-.0178** (.0083)	
YRSOF*INFL			.0008 (.0019)			.0004 (.0039)
TENDEMSYS				.0000 (.0009)	-.0003 (.0008)	.0001 (.0009)
PARINST				.0108* (.0062)	.0163*** (.0062)	.0092 (.0061)
PARNUM				.0207 (.0206)	.0371* (.0200)	.0284 (.0215)
PARPOL				-.0237 (.0163)	-.0423*** (.0164)	-.0401** (.0201)
BALANCE				-.0340** (.0139)	-.0300** (.0131)	
BAL*INFLN					-.0613** (.0307)	
MAJ						.0620*** (.0233)
CLOSED				-.0042 (.0236)	-.0249 (.0230)	-.0022 (.0246)
Constant	dropped	.0227 (.0189)	-.0198 (.0202)	dropped	dropped	dropped
Overall R ²	.134	.133	.127	.305	.371	.315
Base R ²	.079	.082	.061	.249	.344	.253
Wald χ^2 (DF)	(23) 245.8	(21) 65.4	(21) 49.6	(16) 4515.0	(19) 338.4	(20) 144.2

Source: Analysis of data from Morley, Machado, and Pettinato, 1999.

Table 2 Pooled Time-Series Results: Tax Reform Coded on 0–1 Scale, When Legislated

Explanatory variables	Model specifications (**=significant at 95%, ***=at 99% level; *=nearly significant, at 90%)					
	1 N=264	2 N=264	3 N=264	4 N=125	5 N=125	6 N=125
FISCBAL	-.0009 (.0013)	.0006 (.0013)	.0007 (.0013)	-.0030* (.0018)	-.0010 (.0019)	-.0029 (.0019)
INFLN	.0714*** (.0240)	.0606*** (.0124)	.0674*** (.0140)	.0460** (.0214)	.0559** (.0221)	.0508** (.0231)
GDP	.0007 (.0011)	.0007 (.0012)	.0007 (.0012)	.0010 (.0025)	.0006 (.0025)	.0007 (.0025)
IMFCOND	.2534*** (.0408)	.2931*** (.0613)	.2469*** (.0406)	.2269*** (.0648)	.1191 (.0858)	.2317*** (.0645)
IMFLAG	.0990*** (.0364)	.1056*** (.0374)	.0979*** (.0367)	.1327** (.0624)	.1134* (.0640)	.1295** (.0634)
POLDEM	.0027 (.0043)	.0001 (.0020)	.0002 (.0020)	-.0154 (.0184)	-.0285 (.0195)	-.0250 (.0201)
INFLN*DEM	-.0017 (.0027)					
PRESPOW				-.0461 (.0301)	-.0419 (.0310)	-.0468 (.0310)
YRSOFFC	-.0049*** (.0014)	-.0049*** (.0015)	-.0017 (.0039)			
YRSOF*IMF (2)		-.0217 (.0218)	-.0025 (.0027)			
YRSOF*INFL (3)						
NUADM				.0542*** (.0210)	.0419* (.0231)	.0572 (.0371)
NUAD*IMF (5)					.1564 (.1124)	.0005 (.0089)
NUAD*INFL(6)						
TENDEMSYS				.0037** (.0016)	.0040** (.0016)	.0039** (.0016)
PARINST				-.0157 (.0152)	-.0060 (.0160)	-.0187 (.0154)
PARNUM				.0600 (.0399)	.0871** (.0407)	.0767* (.0433)
PARPOL				-.0423 (.0337)	-.0726** (.0358)	-.0725* (.0380)
BALANCE				-.0656** (.0317)	-.0587* (.0305)	
BAL*INFLN					-.0841 (.0709)	
MAJ						.0869* (.0513)
CLOSED				.1432** (.0571)	.1096* (.0602)	.1454** (.0588)
Constant	-.0854 (.0466)	.0085 (.0299)	.0169 (.0309)	dropped	dropped	dropped
Overall R ²	.381	.374	.377	.493	.525	.486
Base R ²	.283	.274	.281	.474	.505	.465
Wald χ^2 (DF)	(22) 245.9	(22) 236.4	(22) 248.8	(18) 350.1	(21) 6748.0	(19) 346.4

Source: Analysis of data in Appendix.

As for system age, the analysis shows mixed results, depending on the measure of tax reform chosen. One possible explanation is that the MMP index registers relatively little variation in tax reform in several countries with long-established electoral systems (Colombia, Costa Rica, and especially Uruguay), while the legislative index counts “re-reforms” (i.e., instances in which taxation rules are changed several times in a decade, but the changes are not fully cumulative, as in Uruguay 1982–90) as legislative actions of a similar magnitude. It is also possible that the relatively few reforms with redistributive goals, which would be scored as negative on the MMP index and positive on the legislative one, tended to occur in newly re-established democratic systems (e.g., Chile in 1990). All in all, this result should be counted as a weak confirmation of Kaufman and Stallings’ observation that established democratic regimes are unusually likely to undertake policy reform.

Party-System Institutionalization, Number of Parties, and Polarization

The analyses gave mixed results for Mainwaring and Scully’s party system variables. All in all, institutionalization did not matter much, polarization tended to discourage reform, and, surprisingly, when it came to passing tax reform, a fractured legislature was, on one measure, a slight net advantage.

Closed-List PR and Partisan Balance

Taking PR first, the analysis gives weak support to the idea that closed-list PR systems predict tax reform, with positive results only on the legislative index. As for partisanship, we find support for the hypothesis that dominance, rather than balance, favors tax reform. On both measures of tax reform the partisan balance variable is significant (or nearly so, as in table 2, eq. 5) and negative. Since BALANCE measures the absolute value of the difference between 0.5 and the actual governing (presidential) party’s fraction of the legislature, it is still ambiguous because it also gives higher values the further a governing party’s share of seats drops below 0.5. We find confirmation of the idea that partisan dominance favors tax reform in the tests on the variable MAJ.

The apparent contradiction between the positive results for both partisan dominance and number of parties is not a direct one: in the only equation in which the number of parties gave a significant result (table 2, eq. 5), neither BALANCE nor MAJ did. More speculatively, these results might be reconciled by supposing that partisan dominance could coincide with a fractionalized legislature if the latter’s divisions were found mainly among the opposition.

Summary

The data analysis yields these factors as determinants of tax reform in Latin America over the period 1977–95, in approximately the following order of importance: specific IMF fiscal conditions (including tax reform itself), especially where these are imposed on a government newly in office; high inflation; a new government not under IMF fiscal conditions; an elected but somewhat authoritarian government where the president's party holds a majority of seats in the legislature; an established democratic system featuring closed-list proportional representation; and a party system that is not polarized, contains more than the average number of parties, and (this seems least important) is well institutionalized. The analysis provides no support for several hypothesized and plausible determinants of reform: declining GDP; dictatorship; elected regimes with strong presidential powers; a smaller-than-average number of parties, and partisan balance in the legislature. It gives weak support to the idea that the coincidence of high inflation and a new administration makes tax reform more likely than we might predict by simply adding the effects of each factor.

THE IMF AND THE “FISCAL CONTRACT”

A picture of the typical politics of tax reform emerges from these results. Facing an economic crisis marked by high inflation, officials from a new administration sign an agreement with the IMF that stipulates detailed fiscal performance conditions, perhaps a tax reform. These officials then try to get a package of measures that meet IMF guidelines through the legislature. They are more likely to succeed if their president's party has a majority, if party leaders are strengthened by the presence of closed-list PR electoral rules, if the country enjoys an established but less than a fully open democracy, and if the legislature is not overly polarized. IMF conditions appear to have a more delayed effect on democratic regimes. All in all, while much of the story deals with domestic politics, inflation often sets the stage and the IMF moves the plot along.

Some observers might not be surprised to find that tax reform often happens with a strong push from Washington. Given the centrality of taxation to the formation of the modern state, I think we are justified, by way of conclusion, in trying to understand the role of the external actors, and specifically the multilateral banks, in historical context.

First, a note to skeptics. It is possible that the values of IMFCOND used in the data analysis actually underestimate the true importance of the IMF and the World Bank in shaping the content and timing of tax policy changes. IMFCOND misses a few instances where reform was

approved as a prerequisite to an IMF agreement, while other tax reforms were passed with IMF advice and the expectation of an agreement to follow, with the reform falling in the previous calendar year (e.g., Panama 1991–92) and thus not showing up in the regressions. Beyond this, governments of member countries often received extensive technical assistance from the IMF's Fiscal Affairs Department even without an agreement or conditions—such as Paraguay in the early 1990s—just as they received similar help from the World Bank or IDB.

In some cases, the IMF continued to have influence over reform planning even though the formal agreement had long since lapsed. In Venezuela, for example, the basic design of a VAT emerged during the first (1989) standby and it finally passed in 1993, during negotiations on a second one. The next president then abolished the VAT, making good on one of his most popular campaign promises. When he faced severe fiscal problems soon after, an IMF official helpfully suggested a name for a new tax that obscured its basic similarity to the hated VAT. The tax and the name were adopted.⁶

However, IMF documents also show that government officials used IMF agreements as leverage against legislatures. For example, in 1983, according to the Staff Report on the Dominican Republic's request for an Extended Agreement, the staff noted that "enactment of a 6 percent general sales tax before April 1, 1983, has been made a performance criterion at the specific request of the authorities" (EBS/82/239, 19). In the notes to the Costa Rican Stand-by Agreement of October 1987, IMF staff observed that the government made expenditure restraint an explicit condition so as to help push the legislature into approving a pending tax reform proposal (EBS/87/33, 17–18). Given that government officials do not always discuss their domestic political gamesmanship with IMF staff, and based on my own conversations with such officials, these examples probably represent a pattern that is more common than the documents suggest.

It can be argued that it is misleading to spotlight the IMF simply because of its ability to demand (if not obtain) specific policy outcomes. Globalization has brought new challenges for tax policy across the world, while also bringing tax officials into closer cooperation. Apart from tax treaties and other formal agreements, tax officials in the western hemisphere (and especially those from Latin America) constitute an increasingly distinct social network and epistemic community, perhaps best exemplified by the activities of CIAT (Centro Interamericano de

6. *Impuesto al consumo suntuario y ventas al por mayor* (Tax on luxury consumption and sales up to the wholesale level), a name that placed first the progressive but fiscally inconsequential part. A senior analyst, then of the Fiscal Affairs Department, claimed credit for this in an August 1996 conversation with me.

Administraciones Tributarias), founded in 1967 and based in Panama. They also respond to intellectual fashions (Carciofi and Cetrángolo 1994, 35). All of this helps account for the similar shape of reforms across the region, but as we have seen, the IMF did more to determine their timing. All in all, the IMF deserves top billing because it united the roles of advisor, benefactor, and “heavy” in the drama of reform.

Perhaps we can interpret the plot more clearly by returning to the idea of the “fiscal contract,” discussed earlier. While the tax reforms considered here often formed part of neoliberal packages, their central purpose was not to shrink the state. They included the increase (or at least the recovery) of average revenue levels, legal simplification, and administrative fortification—in short, not the circumscription of the state, but its strengthening. It is also evident that reform politics included negotiations with major taxpayers, business groups, and key business-friendly legislators over the loss of valuable exemptions, new penalties for evasion, and possible remedies for the state’s own inefficiency. On these two points, Latin American reforms resembled the taxes-for-institutions bargain that some historians and theorists find at the core of state formation in medieval and early modern Europe. Furthermore, as in the historical cases, these measures often responded to an emergency—though here it was destructive inflation, rather than war. And from the fact that newly elected administrations reformed taxes much more often than did old ones, we might surmise that proximity to the act of consent—the representation that is supposed to go along with taxation—indeed helped governments act. But as we have found, this was not the whole story. The prominence of the IMF has no clear counterpart in the historical model. How should we think of it?

One of the lessons from the history of fiscal politics is that those who enjoy effective representation in fiscal matters are not always the ones who provide the most resources to the state, but rather those who provide resources at critical times and are already well organized. It may be true, as many have observed, that where the state finances itself from oil or other natural-resource rents, rulers have less need to respect or create institutions of representation and law (Luciani 1994). But history is full of dictators and absolutist monarchs who had no such rents to fund them. In early modern Europe, for example, some rising absolutists relied on indirect taxes such as the excise—or on borrowing—mainly because these expeditors allowed them (at least for a time) to circumvent the established power of the Estates (Poggi 1978, 53, citing Schiera 1965; Beloff 1954, 125–26; Bonney 1984, 274). In a world of universal suffrage, the mere existence of a legislature is no guarantee that taxpayers are effectively represented there, as an entire school of public-choice theorists have strenuously argued (e.g., Buchanan 1967). Contemporary Latin American legislatures, often dominated by parties organized for the

distribution of patronage, would seem to be very far from the liberal economic ideal in which citizens face their government primarily as contributors rather than clients. With this in mind, one might take the IMF to be acting as a kind of upper house or appropriations committee, "representing" Latin American taxpayers with its combination of sufficient expertise to design tax legislation and sufficient power to deny critical resources to the executive.

Still, perhaps the last point misses an important issue. Governments do not turn to the IMF when they can no longer tax, but when they can no longer make their foreign payments—which is to say (in recent Latin American experience, at least), when they can no longer borrow. Creditors—local and foreign banks, and especially the buyers in international bond markets—obviously favor a strong tax system because, especially in countries without big state-owned mineral companies, taxation is how they get paid. This does not necessarily mean they favor a tax policy opposed to the public interest. In fact, they have a strong interest in seeing that taxes are efficiently collected and do not hamper economic growth. Here the IMF effectively acts in their interest. It is also clear, however, that when the IMF calls for tax increases, as in Bolivia in February 2003, it sets bondholders against taxpayers. On the expenditure side of the ledger, where debt service competes with education, health, and infrastructure spending, the Latin American beneficiaries of these programs might find their interests opposed to those of their countries' mostly international creditors.

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