How Rio de Janeiro Used an Electronic Invoicing Program and the Participation of Stakeholders to Streamline and Increase Service-Tax Collection

Overview

This case study examines tax administration reform in the municipality of Rio de Janeiro, Brazil. It traces the implementation of Nota Carioca, an electronic invoicing program that enlisted consumers to monitor service-tax declarations. Nota Carioca’s successful initiation would address a crucial issue facing Rio: How to increase revenue from service taxes without raising tax rates or placing significant new burdens on either the public administration or businesses. This case study focuses on how Nota Carioca was implemented, with particular attention to several delivery challenges. Political leadership combined a democratic mandate for reform with faith in skilled technocrats and an ability to work with influential stakeholders (including the city’s business association and the accountants union) to generate trust in the program. The system was successfully rolled out and appears to have generated increased revenues and increased tax collection in some sectors. It also offers an opportunity to use the databases of sales tax receipts to provide benchmarks for governments budgeting funds for specific procurements.

Key contextual conditions: The government of Rio de Janeiro faced many economic and fiscal challenges in 2009, such as moderate growth coupled with high levels of poverty, scant infrastructure, poor security, a high government debt burden, and high interest payments. With taxes already high, and limited popular patience for tax increases, the city’s options for raising revenue were restricted. Municipalities in Brazil rely on sales taxes on services and a property tax; other major revenue streams are generated by the federal government through the income tax and by the state governments through the value added tax on goods.

Key stakeholders: Government of Rio de Janeiro and in particular, its Finance Secretariat, mayor, finance secretary, and subsecretary for taxation; the Accountants Union; Brazil’s Association of Secretaries of Finance of Capitals; the Commercial Association of Rio de Janeiro; business owners; consumers; TIPLAN; and IPLANRIO.

Lessons Learned

- Incentives for vendor and consumer participation are as important as policy and systemic changes.
- The use of important behavioral insights, such as harnessing availability bias in designing the lottery system, generated a range of incentives to persuade consumers to use the electronic invoicing system.
- The government reaped huge benefits from the support of business allies seeking reduced paperwork and a less cumbersome system.
Working across stakeholder groups to implement the technical aspects of the rollout and putting all members of the software working group in the same room to ensure strong communication helped to ensure Nota Carioca’s successful implementation.

The software was developed using an approach that was purposefully collaborative and iterative, open to adjustment based on feedback from customers and changes to the overall system, and phased in, starting with the biggest companies. As a result, the government was able to adjust and fine-tune the system as issues arose.

The leadership commitment of the mayor and finance secretary was essential throughout the Nota Carioca design and implementation.

Focusing on system design enabled the Finance Secretariat to roll out a system that was robust and met the specific policy and process requirements of Rio de Janeiro, as well as one that used standards designed to allow integration with other systems in the future.

The Finance Secretariat was able to leverage its success in implementing Nota Carioca by using the system as a foundation for further improvements to revenue administration, with the long-term aim of creating a paperless tax system.

**Development Challenges**

- The need to increase revenue from service taxes
- The lack of public faith in both the revenue and expenditure capabilities of the government and its implications for the broader social contract
- The need to reduce the burden on businesses and the public administration of a cumbersome revenue collection system

**Delivery Challenges**

- Efficiently monitoring service-tax payments would be crucial to increasing collections of service-tax revenues. This required the development of a mechanism to generate service-tax declarations by vendors, and a mechanism to monitor these declarations without significantly increasing numbers of staff and administrative burdens. The huge backlog of unresolved and outdated tax cases suggested that there was no credible threat of inspection and audit in Rio de Janeiro.
- Incentivizing consumers to participate would be crucial and would depend on monetary rewards for requesting and checking electronic invoices. Most customers in Rio de Janeiro did not ask for receipts when they paid for a service, so there was little pressure on vendors to record transactions accurately.
- Gaining buy-in by service providers would be critical to the program’s success, but small, cash-based business might be reluctant to participate.
- System implementation would have to be designed to avoid the common failures of new large-scale government IT systems.