

I. COUNTRY REFORM PROGRESS

On the revenue administration side, this three-year Global Public Finance Partnership (GPFP) project commenced in January 2025. It aims to consolidate the gains achieved through prior tax administration reforms to enhance tax compliance and further mobilize revenue. At the request of the authorities, the project also supports the strengthening of customs administration as part of efforts to facilitate international trade, aiming to reduce tax evasion and customs fraud in a manner that contributes to long-term and inclusive growth.

To strengthen Compliance Risk Management, a practical three-day workshop focused on developing a compliance improvement plan (CIP) was conducted. The Honduran tax administration (*Servicio de Administración de Rentas* - SAR) demonstrates robust analytical capacities for the identification and valuation of compliance risks. It is recommended to enhance the governance of compliance risks involving operational areas in the process and to reinforce the role of the Tax Compliance Risk Committee.

A staff visit was undertaken to update the assessment of SAR's performance, which, since 2023, has centered around the implementation of the new IT system (SIISAR), with its main modules operational since June 2024. Next steps for capacity development (CD) activities under the GPFP project and CAPTAC-DR were agreed upon with the SAR General Director, focusing on the continued support for tax incentives management and control, as well as improving the VAT refund process.

The authorities are promoting a significant tax reform bill—*Ley de Justicia Tributaria* (LJT)—which aims to reduce widespread exemptions. Due to the political environment, the approval of the LJT remains uncertain. CD activities aim to develop a CIP for managing risks associated with tax incentives and formulating recommendations and an action plan for the audit program concerning beneficiaries of tax incentives.

The project also provides guidance on improving the tax refund process for value-added tax by employing a risk-based model in accordance with international best practices. The administrative procedure was reviewed, identifying areas for improvement. Next steps were agreed upon during the short-term expert (STX) assignment to continue designing and implementing a risk-based model that summarizes the risk factors associated with the tax refund process, thereby streamlining the decision-making process of tax officials.

To address initial budgetary constraints, customs-related activities were initiated with IMF-01 funding and coordinated with CAPTAC-DR. This led to a workshop focused on developing a risk-based CIP, starting the construction of a tool to segment the total trader population, and establishing guidelines for a Risk Committee to ensure effective governance. Additionally, support was provided to identify key requirements for a new risk analysis system and to design a new cargo traceability and clearance model. A mission was conducted to review the draft of a new Customs Law, proposing concrete measures to align it with international best practices, ultimately ensuring it addresses current trade challenges and help improve compliance.

On the spending side, in the public financial management (PFM) module, this project aims to strengthen budget formulation and execution for improving the delivery of public spending and help mainstream climate change considerations into them. This will be done notably through advising on (1) how to strengthen budget preparation to formulate comprehensive and credible budgets, (2) how to lift bottlenecks to improve budget execution, and (3) how to identify and track strategic budget allocations that will benefit the fight against climate change.

A four-day virtual workshop, delivered in April 2025, provided a solid platform for further collaboration with the authorities to strengthen budget preparation in Honduras. Positioned as a launch-pad for a HQ mission planned later this calendar year, the virtual workshop showcased good practices and techniques on a range of budget formulation issues. These presentations facilitated active participation and engagement with officials in Honduras to establish a common perspective on the current situation, challenges and bottlenecks.

The mission was able to reach consensus with the authorities on the issues and challenges associated with budget preparation in the country. Primary among these is the frequent and constant budget adjustments that undermine the credibility of the budget ceilings and occupy a significant share of the Ministry of Finance staff time. These continuous adjustments seem to be driven by unresolved issues in the budget negotiation process between the ministry of finance and line ministries, the latter viewing the budget formulation process as a compliance exercise, rather than a strategic one, and a lack of consequences for not adhering to budget ceilings.

II. PROJECT DELIVERY HIGHLIGHTS

RM II: Revenue Module II – Revenue Administration

Key Progress in FY25: Related tax compliance, it was recommended to strengthen the governance of tax compliance risks by reinforcing the role of the Tax Compliance Risk Committee and involving operational areas in compliance risk management. Additionally, the Honduran tax administration plans to implement an auditing framework for tax incentives, following previous recommendations and capacity development (CD) activities. The administrative procedure for VAT refunds was reviewed, identifying areas for improvement and beginning to develop a risk-based model in accordance with international best practices.

Regarding the strengthening of customs administration, recommendations were provided to enhance the regulatory framework. Furthermore, officials were trained to implement a risk-based compliance improvement plan. Collectively, these measures will serve as a foundation for better targeting of control and facilitation actions.

Next Steps: In tax administration, upcoming activities will focus on implementing a risk-based model for the VAT refund process. An HQ-led mission will be conducted to update tax authorities' priorities after the upcoming presidential elections in November 2025.

Upcoming customs activities will concentrate on establishing the groundwork for adopting an integrated risk management approach. This will support the objectives of the IDB-financed customs modernization project.

SM II: Spending Module II – Managing Public Finance

Key Progress in FY25: A four-day virtual workshop, delivered in April 2025, provided a solid platform to discuss issues and challenges associated with budget preparation that undermine the credibility of the budget ceilings and occupy a significant share of the Ministry of Finance staff time:

- The President and Executive, including the Finance Minister, are not sufficiently involved in priority setting process and priority initiatives for the budget are not clearly communicated to line ministries to aid effective reallocation of resources.
- Budget rigidities are significant and restrict resource allocations.

- The link between planning and the budget is weak and even though there are several planning documents (national and sectoral plans), plans are not costed nor policies prioritized through the budget process.
- While there is a medium-term orientation to the budget, the estimates for the forward years are not connected to the economic parameters or program demand variables and the program baselines are opaque and do not reflect the true cost of a program, despite previous efforts at a zero-based budgeting exercise

Next Steps: a full HQ mission will be delivered later this calendar year to set a reform plan to address these vulnerabilities and support strengthening the budget formulation process in the country. Follow-up STX visits will provide hands-on continue support to implement the milestones comprised in the reform plan.

III. LOGICAL FRAMEWORK

Country – Honduras		
RM II: Objective - Strengthened revenue administration management and governance arrangements (SDG 17.1) - RAM		Rating – 2
Outcome	Rating	Narrative
Capacity for reform increased due to clear reform strategy and a strategic management framework adopted and institutionalized	1 – Not Achieved	The tax reform bill promoted by the authorities which aims to rationalize tax incentives, eliminates banking secrecy and introduce a registry of beneficial ownership is still under General Assembly discussion with limited chance to be approved before the upcoming presidential elections in November 2026.
Corporate priorities are better managed through effective risk management	2 - Partially Achieved	The project was approved in January 2025, so the first activities related to customs will begin in FY26. However, using resources from IMF01, a workshop was held on how to develop a risk-based compliance improvement plan, and practical guidance was provided to develop an analytical tool to segment the total population of traders. In tax administration, authorities have decided to resume the activities of the compliance risk committee. No further actions have been taken
Support functions enable more effective delivery of strategy and reforms	2 – Partially Achieved	Based on previous CD activities, tax authorities have continue working on human risks management making progress in the training program and improvements in remuneration. However, other activities to identify workloads have been delayed. The political environment, particularly the upcoming presidential elections, could slow down activities related to human resources management.

Tax and/or customs laws are updated, simplified, and better aligned with modern standards and international protocols	2 – Partially Achieved	The project was approved in January 2025, and the first activity was conducted in April 2025. The initial activity focused on reviewing the draft of a new customs law, providing several recommendations to ensure its alignment with international best practices and readiness to tackle current international trade challenges
Digital technologies are better aligned with strategic objectives	2 – Partially Achieved	The project was approved in January 2025, so the first activities will begin to be carried out in FY26. However, some activities were carried out through IMF01 resources and CAPTAC-DR. While progress is being made, it is still too early to achieve more concrete results.
RM II: Objective - Strengthened core tax administration functions (SDG 17.1) - TAD		Rating – 0
Outcome	Rating	Narrative
A larger proportion of taxpayers meet their payment obligations as required by law	2 – Partially Achieved	The general characteristics of a risk-based model for improving the VAT refunds process have been defined. The administrative process was reviewed. The implementation of the new IT system SIISAR offers an opportunity to improve the refunds process. Further actions will be taken during FY26 to implement the model.
RM II: Objective - Improved customs administration functions (SDG 17.1) - CAD		Rating - 2
Outcome	Rating	Narrative
Foreign trade operators better comply with their reporting and payment obligations	2 – Partially Achieved	The project was approved in January 2025, so the first activities will begin to be carried out in fiscal year 2026. Using resources from IMF01 and CAPTAC, progress has been made in defining a new traceability and customs clearance model, as well as establishing a new national intelligence center.
SM II: Objective - Strengthened Budget Management - PBM		Rating - 2
Outcome	Rating	Narrative
Strengthened budget execution and control processes	2 Partially Achieved	CD supported the development of a methodological and practical manual for budget execution programming that will be expected to contribute to the institutionalization of budget execution programming and improve budget execution processes.
Strengthened annual budget process, and effective allocation	2 Partially Achieved	The April 2025 virtual workshop showcased good practices and techniques on a range of budget formulation issues. The focus of the planned HQ

		mission will be targeted to a selected number of issues and identifying practical solutions to address the challenges. A comprehensive assessment to be made after the HQ mission takes place later in 2025.
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IV. RISK ASSESSMENT

Description	Rating	Mitigation Measures
External Climate/Conditions		
RM II: Risks that external events create a more challenging environment to implement reforms.	Low	Ensure sufficient flexibility in program execution and allow for ability to adjust activities in the case of adverse events.
SM II: Natural disasters and other external shocks could hinder CD delivery in the field.	Low	Remote CD when necessary.
Political Support		
RM II: Political instability due presidential elections in November 2025 can slow the implementation of reforms	Medium	HND has prioritized strengthening tax and customs administration based on its needs assessment. Focus on strategic advice and hands on capacity building to have a more permanent impact.
Management and Technical Staff Support and Commitment		
RM II, SM II: Continuous rotation and lack of preparation of managers undermine the absorptive capacity.	Medium	The missions will work with stable staff and officials encouraging authorities to implement administrative reforms that contribute to a more stable staff. Continual/regular high-level engagement and monitoring.
Resource Adequacy		
RM II: Deterioration of fiscal situation may impact availability of resources to finance reforms.	Low	Careful alignment of reforms with the main priorities of the government. Reforms at SAR, Customs and ministry of finance are underpinned by comprehensive strategic plans, and the projected results from the respective government's strategic decision to strengthen tax and customs administrations and to reduce noncompliance.
SM II: Availability of funding and staff for CD.	High	Plan CD well in advance to secure resources.
Other Risks		
RM II: Lack of coordination among capacity building partners duplicate efforts and deliver contradictory advice.	Low	Take an active role in engaging with other donors to ensure support is well coordinated specially with IADB

V. PROJECT MANAGERS CONTACT INFORMATION

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