Building Fiscal Capacity in Africa

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Caveat: These are personal, not official, views.
Stagnant growth in African has put pressure on public finances.
Expenditure has pulled ahead of revenue
Deficits have increased (on average by 2.5pp 2002-12 vs 2012-22)
Government borrowing to finance short term expenditure rather than investment
... leading to increase in public debt
While tax revenues have remained low
Tax revenues have remained low by any standard
But low revenue mobilization has not been due to low tax rates
Low tax revenues in Africa seem to be primarily a function of weak enforcement and compliance

- Tax enforcement depends on observability, but returns to investment in information trails in SSA are constrained by deeper economic structures – self-employment, low financial intermediation.

- But even when tax authorities have the information they need for collection, they cannot exploit it due to weak enforcement and compliance

- In Uganda, buyers and sellers report different VAT quantities to the Revenue Authority 79% of the time... without repercussions (Almunia et al. 2021)
Raising tax revenues and building fiscal capacity is central to development

• Power to tax lies at the heart of state-building

• “How does a government go from raising around 10% of GDP in taxes to raising around 40%?” (Besley and Persson 2014)

• Viewing development as acquisition of state capacities, the key to improving taxation lies in effective:
  • enforcement, and
  • “quasi-voluntary compliance” (Margaret Levi, 1988)
Avenues for tax reforms

• There are three broad sets of challenges:
  1. Tax Morale / Social Compact
  2. Tax Administration Reform
  3. Tax Enforcement
Compliance and Tax Capacity

State legitimacy and citizen noncompliance

Low tax revenue collection: weak administration, and enforcement

Poor public service delivery and infrastructure
Taxation and building an effective state: Evidence from DRC
(Wiegel 2021, others)

• Property taxation in DRC shows evidence on how taxation can impact state-building through a variety of channels

• Public Goods, Participation Dividend, Accountability, Social Compact

• Citizens also had a more positive perceptions of the provincial government, perceiving more revenue, less leakage, and a greater responsibility to provide public goods.

• The tax morale that may exist among a subset of taxpayers can also be leveraged and may have social multiplier effects.
Strengthening social compact through tax-benefit linkage (Khan, Khwaja, Olken, Shaukat work in progress)

- Social compact between citizens and state: citizens pay taxes, govt delivers public goods and services
- Tax-benefit link may generate tax morale and may be one reason why people pay taxes -- even when audit probabilities and penalties are low.
- This link is often broken leading to a vicious cycle of low taxes and low service provision
- Working with the tax/municipal authorities to strengthen this link by tying services citizens get with the taxes they pay
Linking Tax Revenues with Service Delivery at the neighborhood level
Tax Administration Reform - Creating large/medium taxpayer units

- Tax ministries understaffed and poorly funded
- Increasing staff-to-taxpayer ratio can boost revenue
- Example: medium taxpayer offices in Indonesia (Basri et al. 2021)
Optimising assignment of tax inspectors

• Field-based tax inspectors typical in SSA

• Two ways to improve assignment:
  
  1. **Inspector teams**: assign high-ability inspectors together
  
  2. **Postings**: assign high-ability teams to neighborhoods most likely to pay

• In DRC, the government could increase property tax compliance by 37% simply by reallocating inspectors (Bergeron et al 2022)

• No additional financial or human resources necessary
Sharpening tax inspectors’ incentives

• Tax inspectors often have weak performance incentives (salaried, tenured)

• Sharpening incentives can raise performance (Khan et al 2014; 2018)
  
  • Financial bonuses: increase property tax revenue growth by 46% in Pakistan
  
  • Performance-based postings: increased property tax revenue growth by 31-40% in Pakistan

• Caveat: need monitoring to ensure against adverse events
Regularising assessment and collection

- Taxation often arbitrary and unsystematic in SSA
- **Regularising assessment and collection** can:
  - Improve transparency and perceived fairness
  - Boost compliance
- **Examples:**
  - Systematic door-to-door assessment and collection improved views of government integrity and willingness to pay the property tax in the DRC (Weigel 2020)
  - Using satellite maps and house characteristics to mass assess properties suggests revenue gains in Freetown (ICTD 2021)
Leveraging technology

• Technology can strengthen tax administration by:

  1. Improving monitoring of field-based inspectors
  2. Creating a paper trail to aid enforcement
  3. Reducing the hassle cost of compliance
  4. Improving citizens’ views of government integrity

• Examples: electronic billing machines

  • Rwanda: raised VAT payments in Rwanda by 5.4% (Eissa et al. 2015)
  • Ethiopia: raised VAT payments by 43% and CIT by 12% (Mascagni et al. 2021)
Summing up

• Building fiscal capacity in Africa through domestic revenue mobilization is critical. This is ultimately a political challenge.
  • It is a process, not a product

• There is a growing body of evidence and resources to support this process
  • African institutions – ASE, AERC, others
  • FCDO Centre on Public Finance, IGC, JPAL, TAXDEV, ICTD, others

• Creating organic analysis-capacity reinforcement cycle is important
  • Independent, local capacity
  • Long-term collaborations with researchers
Value for Money in Public Procurement?
Variation in price paid for A4 paper (Bandiera et al. 2021)