TAX EVASION AND FISCAL CORRUPTION
Essays on compliance and tax administrative practices in East and South Africa

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Introduction

No underdeveloped country has the manpower resources or the money to create a high-grade civil service overnight. But it is not sufficiently recognized that the revenue service is the 'point of entry'; if they concentrated on this, they would secure the means for the rest.

(Nicolas Kaldor, 1963: 417).

Compliance and tax administrative practices

Tax evasion and fiscal corruption have been universal and persistent problems throughout history with manifold economic consequences. Two thousand five hundred years ago, Plato was writing about tax evasion, and the Ducal Palace of Venice has a stone with a hole in it, through which people once informed the Republic about tax evaders (Tanzi, 2000a).[1] The classic document of Hindu statecraft, the *Arthasastra*, advises kings of Mauryan India in the third century B.C. to maintain personal control of government finances in order to protect themselves from treachery.[2] The basic assumption was that without control man, self-serving by nature, would appropriate more than his share of the king's revenue:[3]

> *Just as it is impossible not to taste the honey or the poison that finds itself at the tip of the tongue, so it is impossible for a government servant not to eat up at least a bit of the king's revenue.*

Today, corruption and tax evasion seem to take place in practically every country in the world, and should be considered a potential problem everywhere. Still, evasion and fraud in tax administration are phenomena which hit developing countries hardest.[4] Firm evidence on the extent of such illegal practices is naturally hard to come by. But anecdotal evidence from different developing countries indicate that half or more of the taxes that should be collected

[1] A modern version of this technology is found in Uganda: On a special telephone hot-line people can report corrupt tax officials or tax dodgers. They get a reward, usually around 10%, of the tax recovered (*The Economist*, July 17th 1996: 38).
[2] Mauryan India was contemporary with the empire of Alexander the Great. After the Hellenistic armies invaded India there were periodic contact between India and the older monarchies to the north and west. Some scholars believe that the *Arthasastra* reflects the influence of Egyptian, Persian and Hellenistic ideas of the monarch's central authority and role in government (Webber and Wildavsky, 1986:62).
[3] Ibid, p. 82.
[4] Klitgaard (1994:1) asserts that corruption is 'clearly one of the two or three major problems holding back economic and political advancement in most developing countries'.

cannot be traced by the government treasuries due to corruption and tax evasion.[5] This erosion of the tax base has several detrimental fiscal effects. The consequences of lost revenue to the funding of public services are of special concern (Tanzi, 2000a). In addition, corruption and tax evasion may have harmful effects on economic efficiency in general (Chand and Moene, 1999; Tanzi, 2000b), and income distribution in particular because the effective tax rates faced by individuals and firms may differ due to different opportunities for evasion (Hindriks *et al*, 1999). Thus, tax evasion and corruption can make the real effects of the tax system very different from those that the formal system would have if honestly implemented.

In-depth knowledge about who actually are caught and escapes the tax net – and why – and how relations between taxpayers and tax authorities are affected by revenue mobilisation efforts – is scarce in sub-Saharan Africa. There is also limited knowledge about the impacts of recent tax administrative reforms on revenue collection and corruption. This thesis is an attempt to narrow this knowledge gap by analysing tax compliance and revenue administration in three African countries: South Africa, Tanzania and Uganda. Such knowledge is required in a situation where the public sector in most poor sub-Saharan African countries is not sustainable at present levels of domestic resource mobilisation, as reflected in often substantial budget deficits and high levels of aid dependency (OECD-DAC, 2006). Aid alone now accounts for almost half the income of many governments of low-income countries. The Poverty Reduction Strategy processes adopted in a number of poor countries (Dijkstra, 2002) are likely to exacerbate the public finance and aid dependency crises due to the future financial obligations thereby created.

According to the *International Monetary Fund*, African countries 'have significant potential for raising tax receipts by broadening the tax base, improving tax administration, and rationalising the tax system' (Hadjimichael *et al.* 1995: 44). This view underpins the rationale for many ongoing tax reforms.[6] Attempts at improving revenue collection have also brought

[5] For instance, in 2003 the Guatemalan revenue administration (SAT) estimated the total tax evasion to more than two-thirds of actual collections (Mann, 2004). For India, Mookherjee and PnG (1995) report a confidential survey finding that 76% of all government tax auditors took bribes, and that 68% of taxpayers had paid bribes. According to a study from Tanzania, official import statistics underreported the value of imports by as much as 70% (ESRF, 1996). Evasion of other types of taxes was also reported to be widespread. In a business survey conducted in Uganda in 1998, which covered 243 firms, as many as 43% said they were paying bribes to tax officers occasionally or always (Gauthier and Reinikka, 2001:22).

[6] Some of the early literature in development economics addressed similar issues. In 1966, for instance, Arthur Lewis argued that 'most developing countries need to raise at least 17 per cent of gross domestic product in

local government taxes in focus (Bird and Vaillancourt, 1998). They typically affect millions of people directly, while central government taxes influence relatively fewer citizens. This puts new demands on tax authorities as many more people – including the poorer segments of the population - become liable to contribute financially to the public sector (Fjeldstad and Moore, 2006). However, in the current debate on revenue mobilisation, few concrete suggestions are presented on how to increase the tax effort, except for improving the effectiveness of the tax administration. Obviously, as shown is this thesis, tax administrations in many African countries are weak, inefficient and corrupt. But merely offering wage incentives to tax collectors as a way of increasing revenue generation can actually lead to more corruption (see Essays 4, 5 and 6). Furthermore, the emphasis on revenue targets does not seem to acknowledge other major impacts of the tax system. Many revenue bases in Africa perform poorly with respect to the basic principles of taxation: They are often distortive, costly to administer, and exacerbate inequity. Attempts to squeeze additional revenues from poorly designed taxes may, therefore, have negative effects on the economy and society in general.

A main finding of the thesis is that tax administration decisions and practices – as much as declared tax policies and legislation – shape how taxation affects different groups of taxpayers. Tax administration practices refer to the interactions between taxpayers and tax authorities concerning identification of tax liabilities, actual tax payment and collection, and prosecution and penalty of tax evaders (Das-Gupta & Mookherjee, 1998: 28). Some of these practices share two key features. They are transaction intensive, often involving face to face contacts between taxpayers and tax officers. Furthermore, revenue authorities at both central and local government level have considerable discretionary powers *vis-à-vis* taxpayers. Some powers are defined in the tax legislation and operational rules, but these are often contradictory and/or unclear and they may be violated. Moreover, their organisational capacity is usually limited and they have insufficient information about taxpayers. They are at the same time both weak and powerful.

Whether tax administration practices are compliance enhancing in poor countries depends on how the tax law is enforced, the honesty of tax collectors and government trustworthiness

taxes and other government revenues, taking central and local authorities together' (Lewis, 1966: 129). Today, 40 years later, many African countries south of the Sahara are not even close to this. In fiscal year 2005/06, Tanzania's tax take was around 14% of GDP (URT, 2006: 11), and in Uganda it was less than 13% in 2004/05 (RoU, 2005: 44).

with respect to service delivery. In circumstances where citizens perceive taxes to be unfair and receive few tangible benefits in return for taxes paid, only coercive methods of enforcement can generate revenues (see Essays 1 and 2). Roadblocks manned by soldiers, police and militia and physical punishment of suspected tax defaulters have become common. At times taxpayers reciprocate violently with 'counter-attacks' on collectors or by burning tax offices (see Essay 3). People have various resources to draw upon in dealing with tax authorities and revenue officers: political connections, social networks ('know-who'), and actions through collective organisations (e.g., business associations, religious organisations, NGOs etc). Tax evasion and fiscal corruption must therefore, at least to some extent, be understood in the context of a political economy in which social relations may rule out the formal bureaucratic structures and positions. As a consequence, reforms that otherwise seem consistent with principles of good public administration are undermined. Moreover, if taxpayers' rights are unclear for both taxpayers and for tax authorities, tax compliance and accountability will be affected. As long as excessive use of force is accepted as an integral part of tax collection it is unlikely that state-society relations can become more accountable. Thus, the challenge for African states is to increase their ability to collect more revenue with greater efficiency and less public resistance.

One ought to be cautious to offer general policy recommendations based on individual case studies. However, the essays included in this thesis point in some directions which might be worth to consider when designing reforms to addressing tax evasion and fiscal corruption in poor countries. The essays emphasise that as long as tax administrative practices in East Africa, and to some extent also in South Africa, are perceived by taxpayers to be influenced by extortion, corruption, and nepotism, it is unlikely to contribute to the fostering of a more conducive taxpaying culture. Tax legislation is unclear and causes random and partly *ad hoc* collection procedures. Assessors often have wide discretionary powers to interpret tax laws, for instance, to allow or disallow expenses or charges, or to exempt items from import duties. These factors, combined with a perception of limited tangible benefits in return for taxes paid, seem to legitimate tax evasion. In such circumstances it is not surprising that taxation often takes place in an atmosphere of distrust and fear between taxpayers and revenue officers. Thus, the government's credible commitment about the use of tax revenues and its procedures to design and implement tax policy non-arbitrarily are crucial to regain legitimacy. The credibility or trustworthiness of the revenue administration's sanctions against tax defaulters is also important in this context. Reforms of tax legislation and collection procedures, including measures to improve transparency in the taxpayer-tax officer relations, should therefore take place concurrently to reduce opportunities for corruption and the demand for corrupt services. When the government decides what measures to take as part of its tax reform programme, it should bear in mind the state of the economy and the resources at hand. Tanzania and Uganda, like most poor countries, but also a middle income country like South Africa, have neither the political capital nor the administrative capacity to sustain more than a limited range of concurrent initiatives. Nevertheless, an incremental process of change can add up to a radical transformation if it is sustained for long enough.

The thesis

The thesis is organised in three parts, each containing two essays: Part I examines factors determining citizens' compliance in local government authorities in Tanzania (Essay 1) and South Africa (Essay 2), respectively. The research finds that the way taxes and charges are collected may impact significantly on taxpayers' compliance. Excessive use of sanctions and force are likely to fuel tax resistance. This finding leads to Part II of the thesis, which focuses on different tax enforcement regimes and what factors determine the extent of coercion practised in revenue collection. Essay 3 analyses tax collection in local government authorities in Tanzania, the stakeholders involved and the impacts of their relative bargaining powers on revenue collection. In Essay 4, strategies that aim to reduce tax evasion and improve revenue collection by strengthening the bargaining powers of corrupt tax officers are critically assessed. The studies conclude that although corrupt and extortive tax collection may raise revenues in the short run, sustained development cannot occur in an institutional framework that fosters corruption and extra-legal tax enforcement. Thus, a starting point for policy debates in this area is to design and implement measures to fight fiscal corruption. Such measures are analysed in Part III, which explores recent experiences to fight corruption in the Tanzania Revenue Authority (Essay 5) and the Uganda Revenue Authority (Essay 6).

PART I: TO PAY OR NOT TO PAY?

What factors determine citizens’ decisions on whether to pay taxes (or services charges) or not? Based on survey data from Tanzania and South Africa, essays 1 and 2 apply the analytical frameworks suggested by Levi (1988, 1997) and Slemrod (2003), to examine the impacts of three variables on taxpayers’ compliance behaviour: (1) coercion; (2) fiscal exchange; and (3) social influences.

Essay 1 Why people pay taxes. The case of the development levy in Tanzania

Published in *World Development,* Vol. 29, No. 12 (Dec 2001), pp. 2059-2074.
Co-authored with Joseph Semboja.

This paper examines factors determining tax compliance behaviour in local authorities in Tanzania. The poll tax - locally named ‘development levy’ - is used as case. The study finds support for the hypotheses that tax compliance is positively related to factors such as ability to pay, the (perceived) probability of being prosecuted and the number of tax evaders known personally by the respondent. Oppressive tax enforcement, harassment of taxpayers and discontent with public service delivery seem to increase tax resistance and may explain the widespread tax evasion observed.

Essay 2 What’s trust got to do with it? Non-payment of service charges in local authorities in South Africa

Published in *The Journal of Modern African Studies*, Vol. 42, No. 4 (2004), pp. 539-562.

A major financial problem in many municipalities in South Africa is the inadequate collection of service charges due to widespread non-payment. The prevailing view is that non-compliance is caused by poverty and the existence of an ‘entitlement culture’. However, huge variations in compliance exist both within poor communities and between communities with similar socio-economic characteristics. How can these differences be explained? Moreover, what factors determine citizens’ compliance? The paper argues that non-payment is not only related to inability to pay and ‘a culture of entitlement’, but also to whether citizens perceive the local government to act in their interest. In particular, three dimensions of trust may affect citizens' compliance: (1) trust in the local government to use revenues to provide expected services; (2) trust in the authorities to establish fair procedures for revenue collection and distribution of services; and (3) trust in other citizens to pay their share.

PART II: TAX ENFORCEMENT AND THE BARGAINING POWER OF COLLECTORS

Why do the tax enforcement regimes differ between local government authorities in Tanzania? Who are the stakeholders involved in the domestic tax enforcement process, and what is their relative bargaining power? Recent literature on incentives in tax administration, argue that increased fiscal corruption in some contexts may contribute to reduced tax evasion and thereby increased tax revenues. Does this justify a policy to improve revenue collection by strengthening the bargaining power of corrupt tax officers *vis-à-vis* taxpayers? These are some of the questions examined in essays 3 and 4, using arguments put forward by Moore (1998) and Mookherjee (1997) as points of departure for the analysis.

Essay 3 Taxation, coercion and donors. Local government tax enforcement in Tanzania

Published in *The Journal of Modern African Studies,* Vol. 39, No. 2 (2001), pp. 289-306.

This paper presents three propositions about tax collection by local authorities in Tanzania. First, revenue performance depends on the degree of coercion involved in tax enforcement. Reciprocity does not seem to be an inherent component of the state-society relationship in connection with local government taxation. Second, the extent of coercion depends on the bargaining powers of the stakeholders involved in the tax enforcement process. In particular, coercive tax enforcement is facilitated when the ‘bargaining powers’ with respect to tax collection favour the council administration, and the elected councillors have no direct influence on collection. Third, the presence of donors in a local authority may be crucial by changing the ‘balance of power’ in favour of the council administration, with implications for accountability, responsiveness and democratic development. These results may explain why widespread differences in revenue performance between local authorities are observed.

Essay 4 Fiscal corruption: A vice or a virtue?

Published in *World Development,* Vol. 31, No. 8 (August 2003), pp. 1459-1467.
Co-authored with Bertil Tungodden.

Recent literature on tax administration in poor countries suggests there are virtues of allowing fiscal corruption. By strengthening the bargaining power of corrupt tax officers, it is argued that tax evasion may be reduced and tax revenues increased. But does such an intriguing paradox justify policies that stimulate corruption? Our answer is no, and this paper puts forward three arguments to support our view. First, while an increase in corruption may raise revenues in the short run, in general the opposite will be the case in the longer run. Second, the instrumental value of reducing corruption goes far beyond its effects on tax evasion and tax revenues. Accepting corruption as a policy strategy to increase tax revenues may undermine values of democracy and good governance. Third, eliminating corruption should be considered an end in itself. Thus, contrary to recent suggestions on incentive reforms in tax administration, the reasonable starting point for policy debates in this area should still be that an increase in fiscal corruption is not an appropriate instrument for raising tax revenues. Sustained development cannot grow from an institutional framework that fosters corruption and extra-legal tax enforcement.

PART III: CONTROLLING FISCAL CORRUPTION

What factors explain the patters of corruption observed in revenue administrations in East Africa? What are the impacts of incentive schemes introduced to curb corruption? Essays 5 and 6 explore the above questions, drawing on recent economic literature on corruption (Rose-Ackerman, 1998, 1999), incentives in revenue administrations (Chand and Moene, 1999; Das-Gupta and Mookherjee, 1998), and anthropological literature on patronage (Smith, 2003).

Essay 5 Fighting fiscal corruption: Lessons from the Tanzania Revenue Authority

Published in *Public Administration and Development,* Vol. 23, No. 2 (May 2003), pp. 165-175.

Over the past two decades many developing countries have implemented comprehensive reforms of their tax administrations in order to increase revenue and curb corruption. This paper examines recent experiences in the fight against corruption in the Tanzania Revenue Authority. Two lessons of broader relevance are highlighted. Firstly, even with relatively high wages and good working conditions, corruption may continue to thrive. In a situation where there is high demand for corrupt services, it is unrealistic to provide tax officers with pay rates that can compensate for the amount gained through bribery. Without extensive and effective monitoring, wage increases may produce a highly paid but also highly corrupt tax administration. Secondly, hiring and firing procedures may lead to more corruption. Corrupt tax officers often operate in networks, which also include external actors. These corruption networks seem to have been strengthened because many of those fired were recruited to the private sector as 'tax experts'. This partly explains why the positive process experienced in the initial phase of the new revenue authority was later reversed.

Essay 6 Corruption in tax administration. Lessons from institutional reforms in Uganda

Forthcoming as Chapter 17 in Susan Rose-Ackerman ed. (2006) *International Handbook on the Economics of Corruption*. Cheltenham, UK/Northampton MA, USA: Edward Elgar.

The Uganda Revenue Authority (URA), established in 1991, is the oldest integrated revenue authority in sub-Saharan Africa. The revenue authority model aimed to limit direct political interference in day-to-day operations by the Ministry of Finance and to free the tax administration from the constraints of the civil service system, especially by paying salaries above civil service pay scales and to more easily recruit, promote and dismiss staff. Such steps were expected to provide incentives for greater job motivation and less corruption. After marked success in the first years after its creation, revenue has dropped as a share of GDP, and corruption is believed to be pervasive. The paper shows that the establishment of the URA with comparatively generous remuneration packages and substantial budgets has not protected it from political interference. To the contrary, it has made the revenue administration a more attractive target because the authority offers both relatively well paid jobs and considerable rent-seeking opportunities. Further, the paper argues that the motives of individual actors are often inextricably tied to the interest of the social groups to which they belong. Tax officers are often seen by their families and networks as important potential patrons who have access to money, resources, and opportunities that they are morally obliged to share. People in positions of power are expected to use that influence to help their kin and community of origin. Hence, increased salaries may lead to increased social obligations, which again may push tax officers into taking bribes to accommodate the growing expectations around them. This implies that such social relations may rule out the formal bureaucratic structures and positions. Fiscal corruption must therefore, at least to some extent, be understood in the context of a political economy in which access to social resources depends on patron clientilism. If these problems, which are rooted in social norms and patterns of behaviour rather than administrative features, are overlooked, the result may be to distort incentives. As a consequence, reforms that otherwise seem consistent with principles of good public administration may be undermined.

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Why People Pay Taxes: The Case of the Development Levy in Tanzania

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Summary. — This paper examines factors determining tax compliance behavior in local authorities in Tanzania. The case study is the poll tax—locally named "development levy." The study finds support for the hypothesis that tax compliance is positively related to factors such as ability to pay, the (perceived) probability of being prosecuted, and the number of tax evaders known personally by the respondent. Oppressive tax enforcement, harassment of taxpayers, and discontent with public service delivery seem to increase tax resistance and may explain widespread tax evasion. © 2001 Elsevier Science Ltd. All rights reserved.

Key words — taxation, tax evasion, tax collection, compliance, local government, Tanzania

1. INTRODUCTION

Studies from different developing countries indicate that it is not uncommon for half or more of the potential tax revenues to remain uncollected (Bird, 1992, 1989; Krugman, Alm, Collins, & Remolina, 1992; Richupan, 1984). This tax base erosion has had a variety of fiscal effects and there are at least four reasons for concern. First, revenue losses from noncompliance are particularly critical in the context of substantial budget deficit (Tanzi, 1991). Second, both horizontal and vertical equity suffer since the effective tax rates faced by individuals differ because of different opportunities for tax evasion (Alm, Bahl, & Murray, 1991; Cowell, 1992; Slemrod & Bakija, 1998). Third, the expanding underground economic activities, which are often the other face of tax evasion, may affect implementation and outcomes of economic policies (Cowell, 1990; Tanzi, 2000). Finally, evasion and citizens' disrespect for the tax laws may go together with disrespect for other laws, and, thus contribute to undermine the legitimacy of government (Graetz, Reinganum, & Wilde, 1986).

Dealing with the policy problem of tax evasion requires some understanding of the factors underlying the individual's decision whether to pay or evade taxes. Little is known, however, about tax compliance behavior in developing countries (Andreoni, Erard, & Feinstein, 1998). This study attempts to shed light on some of the factors underlying tax compliance in local authorities in Tanzania using the experience with the poll tax as the case. The poll tax, commonly referred to as "development levy," has been in place at the local government level since 1983–84, and is the single largest source of tax revenue for district councils in Tanzania. In 1997, revenues from the development levy contributed on average

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about 30% of total own revenues in rural councils and 19% in urban councils (Price Waterhouse, 1998). [1] The poll tax is, in principle, levied on every person above the age of 18 years and ordinarily resident in the area (URT, 1991, p. 284). Women are exempted in many councils. [2] In most areas, the tax is levied on a flat basis, but in some urban areas graduated rates based on incomes are applied. There is widespread unwillingness among the public to pay the levy, and noncompliance is a serious problem. This has led some councils to abandon the tax in recent years.

Different arguments are used to explain the extensive noncompliance. Bukurura (1991, p. 91) argues that the evasion of the development levy is primarily due to taxpayers' inability to pay and to a lack of clarity with respect to obligations and reasons for paying. This argument is supported by the Tax Commission (URT, 1991, p. 287) claiming that "[a]s with other taxes, understanding of the need for local revenues will improve compliance." Implicitly these studies assume that an understanding of the relationship between taxes and the provision of public goods and services is a critical factor for tax compliance, hence the need for education and political mobilization. Other studies show that unwillingness to pay is the result of a combination of political protest to the degradation of local public services, perceptions of unfairness of the charges which do not take ability to pay into consideration as well as corruption and other administrative failings by the councils (Tripp, 1997; URT, 1996). Consequently, the prescription is to improve the administrative capacity and efficiency of local authorities.

While the above studies focus on identifying possible causes for people *not* paying taxes, it is equally relevant to ask who pays and why. This paper aims first to answer the question of who pays the head-tax in local authorities in Tanzania, and second, to explore why people pay, i.e., to identify which parameters are determining their compliance behavior. Accordingly, this approach may facilitate an explanation of the observed differences between and within local authorities with respect to tax compliance. The paper is organized as follows: Section 2 presents the theoretical framework for analyzing tax compliance. The methodological approach and organization of the empirical study are addressed in Section 3. Section 4 presents the results, and Section 5 summarizes and concludes the paper.

2. THEORETICAL FRAMEWORK

The relationship between a taxpayer and the local government includes at least three elements (Levi, 1988; Spicer & Lundstedt, 1976). First is an element of coercion, as represented by the enforcement activities of tax collectors and the penalties imposed on noncompliance. Second is an element of fiscal exchange, whereby taxation and the provision of public goods and services are interpreted as a contractual relationship between taxpayers and the (local) government. Third is the impact of social influences on the taxpayer's compliance behavior. For example, an individual's perception of the probability of his tax evasion being detected, in combination with his opportunities, may determine the decision regarding tax payment.

(a) *Coercion*

The coercive element of the taxpayer–government relationship is the focus of the classical tax evasion model (Allingham & Sandmo, 1972), which assumes that the taxpayer's behavior is influenced by factors such as the tax rate determining the benefits of evasion, and the probability of detection and penalties for fraud which determine the costs. The problem is thus one of rational decision making under uncertainty whereby tax evasion either pays off in lower taxes or subjects one to sanctions. This implies that if detection is likely and penalties are severe few people will evade taxes. [3]

The conceptual framework needed to study the development levy is to some extent different from the standard model of tax evasion which typically focuses on the declaration of taxable income with possibilities of detection. Nonpayment of development levy has more to do with disobedience than cheating (see Besley, Preston, & Ridge, 1993). In principle, the local tax authorities can observe the fraction of evaders. Thus, taxpayers cannot hide their liability except by hiding their existence or migrating to councils where the tax is not imposed or is at a lower rate. In so far as sanctions are probabilistic, this reflects the effectiveness of the local authority in enforcing the tax. It is therefore reasonable to suppose that taxpayers' perceptions concerning the likelihood of being prosecuted and the severity of penalties affect their choice to pay or not.

(b) *Fiscal exchange*

The presence of government expenditures may motivate compliance (Alm, Jackson, & McKee, 1992; Andreoni *et al*., 1998; Cowell & Gordon, 1988). Individuals may pay taxes because they value the goods provided by the government, recognizing that their payments are necessary both to help finance the goods and services and to get others to contribute. A taxpayer may therefore be seen as exchanging purchasing power in the market in return for government services (Levi, 1988). Positive benefits may increase the probability that taxpayers will comply voluntarily, without direct coercion. [4] Without a material benefit, compliance becomes less assured. Although most taxpayers cannot assess the exact value of what they receive from the government in return for taxes paid, it can be argued that they have general impressions and attitudes concerning their own and others' terms of trade with the government (Richupan, 1987). [5] It is then reasonable to assume that a taxpayer's behavior is affected by his satisfaction or lack of satisfaction with his terms of trade with the government. Thus, if the system of taxes is perceived to be unjust, tax evasion may, at least partly, be considered as an attempt by the taxpayer to adjust his terms of trade with the government.

(c) *Social influences*

The importance of social interactions in forming tastes and actions has been stressed by sociologists and social psychologists (Hessing, Elfers, & Weigel, 1988). It is reasonable to assume that human behavior in the area of taxation is influenced by social interactions much in the same way as other forms of behavior (Snavely, 1990). Compliance behavior and attitudes toward the tax system may therefore be affected by the behavior of an individual's reference group such as relatives, neighbors and friends. Thus, if a taxpayer knows many people in groups important to him who evade taxes, his commitment to comply will be weaker. On the other hand, social relationships may also help deter individuals from engaging in evasion for fear of the social sanctions imposed once discovered and revealed publicly (Grasmick & Green, 1980; Grasmick & Scott, 1982). Theoretical research on herd behavior in economic situations (Banerjee, 1992; Sah, 1991) also indicates that social influences may affect compliance, in particular by affecting the perceived probability of detection. Thus, evidence suggests that perceptions about the honesty of others may affect compliance behavior. [6]

(d) *Hypotheses*

The theoretical approaches suggest a number of predictions. First is the expectation to observe the highest compliance rates among persons whose opportunity to evade is low and whose probability of being prosecuted is highest. [7] Second is the expectation that willingness to pay is correlated with what taxpayers perceive they get in return from the (local) government. Third is that the perceived honesty of peer groups (i.e., family, neighbors and friends) with respect to taxation might affect the decision whether to pay or not. Fourth is the expectation that ability to pay also matters.

From this initial framework, five hypotheses have been derived and explored using survey data from Tanzania:

H1. Compliance is more likely the higher income a taxpayer has.

H2. Compliance is more likely when the probability of prosecution is perceived to be high.

H3. Compliance is more likely when sanctions against tax evasion are perceived to be severe.

H4. A taxpayer is more likely to comply when he perceives his terms of trade with the government as fair.

H5. The fewer evaders a taxpayer knows, the more likely he himself will comply.

3. METHODOLOGY AND ORGANIZATION OF THE STUDY

The study was carried out in Kibaha District Council, Coastal Region, and in Kilosa District Council, Morogoro Region, in the late 1996 and 1997.

(a) *Selection of sample and administration of the survey*

The predominant religion in the study areas is Islam, and the majority of people are agriculturists. According to World Bank (1993, p. 29) the poverty profiles in Coastal Region (Kibaha, DC) and Morogoro Region (Kilosa DC) are fairly similar. This observation is based on a comparison of farming environments in different regions, since agriculture is the main economic activity in rural areas. Due to its proximity to Dar es Salaam and the abundance of productive land, many people have migrated to Kibaha from other regions. In Kilosa, the abundance of land and job opportunities in the plantations, mainly in the sugar industry, have attracted many migrants. Both councils apply flat development levy rates. In Kibaha DC, the rate for 1995 was TSh 500 and TSh 1,000 for 1996. In Kilosa DC, the rate for both years was TSh 1,000. A penalty of 50% is added if the levy is paid later than October 1.

(i) *The survey in Kibaha*

In Kibaha, the sample included three rural villages; *Pangani*, *Misugusugu* and *Disunyara*; and one combined rural–urban village, i.e., *Mwendapole* (see Table 1). The villages were selected from four different wards on the basis of a balanced representation of rural and township respondents, and accessibility.

The respondents were randomly selected from the Tax Register Books of the Village Executive Officers (VEOs) in two of the villages (Pangani and Misugusugu), and from the Tax Register Books of the Ward Executive Officers (Mwendapole and Disunyara). The designated respondent was the head of the household, who was the person registered in the Tax Register Book and the one who most likely managed or played a major role in managing tax matters on behalf of the household. The interviews were carried out in Swahili.

In total, 146 taxpayers were selected for the survey in Kibaha (Table 1). Not all the selected respondents were available when we looked for them: some had gone to their "shamba" to farm, others came back late because they worked as employees or did other businesses. In those instances where the executive officers knew that the persons selected were not available, they were replaced in the sample by the person next to the selected one in the Tax Register Book, or, if this person was not available, by the person listed before the selected one. This technique was also used when the selected person lived in a remote or difficult accessible area, and was excluded from the sample on that basis. The final sample included 128 respondents, corresponding to a response rate of 0.88. [8]

(ii) *The survey in Kilosa*

Three villages in three different wards were selected on the basis of the same criteria as in Kibaha. The sample included the rural villages of *Chanzuru* in Chanzuru ward and *Mamoyo* in Mabwerebwere ward, and the rural–urban village of *Dumila* in Dumila ward. In contrast to Kibaha, tax collection at the village level in Kilosa was carried out by the ward office and organized by the Ward Executive Officer (WEO). The village executive officers were to a large extent excluded from the collection process.

Tax Register Books were unavailable in both Chanzuru and Dumila wards. According to the Ward Executive Officers, they had either been stolen or had just disappeared. Lists of names of development levy payers were provided on hand-written sheets of paper by the WEOs. For Mamoyo village the sample was selected on the

Table 1. *The survey sites in Kibaha and Kilosa, and compliance rates in the surveyed villages*

Wards	Villages	Number of registered taxpayers in the villages (1996)[a]	Number of taxpayers selected for the survey	Number of respondents (response rates in brackets)	1995 Compliance rate (%)	1996 Compliance rate (%)
Tumbi	Pangani	138	35	33 (0.94)	76	55
Visiga	Misugusugu	348	36	31 (0.86)	68	39
Kibaha	Mwendapole	566	35	27 (0.77)	74	48
Mlandizi	Disunyara	257	40	37 (0.92)	51	35
Total, Kibaha			146	128 (0.88)	66	44
Chanzuru	Chanzuru	n.a.	25	19 (0.76)	95	89
Dumila	Dumila	n.a.	25	8 (0.32)	88	88
Mabwerebwere	Mamoyo	n.a.	25	17 (0.68)	59	76
Total, Kilosa		n.a.	75	44 (0.58)	80	84

[a] Compiled from the Tax Register Books of the Village Executive Officers and Ward Executive Officers.

basis of the Tax Register Book that had just been compiled by the newly appointed Ward Executive Officer. In each village, 25 respondents were randomly selected on the basis of these lists. The final sample in Kilosa included 44 people, equivalent to a response rate of 0.58 (Table 1). In Chanzuru, 19 taxpayers were interviewed, and 17 in Mamoyo. In Dumila village, however, the final sample only included eight respondents. The low response rate in Dumila was partly due to people refusing to participate, linking the exercise with tax collection, and partly because it was the harvesting season.

There is some question as to how representative the Kilosa sample is both in terms of size and how it was selected. Only two of the respondents were traders (both from Chanzuru village), and one was a wage employee in the private sector (from Mamoyo). The remaining individuals were peasants. But this probably reflects fairly well the occupational distribution in the research area. The average household size of the sample is seven persons, which is identical with Kibaha, and also corresponds with the average rural household size in Tanzania of 6.37 persons (Tinios, Sarris, Amani, Maro, & Zografakis, 1993).

(b) *The questionnaire*

The objective of the study was to explore the decision-making behavior of individual taxpayers in the study area. To reduce errors of recall, compliance behavior for the two previous years only, i.e., 1995 and 1996, was considered. Questions that focused directly on the respondents' income were eliminated and only questions that provided indirect indicators of wealth were included. The questions were organized around five main headings.

(i) *Background information on the respondent*

Key data collected were on the main occupation of adult members of the household and the principal source of income as these variables are assumed to affect both the opportunity to evade and the ability to pay taxes. Based on previous survey studies in Tanzania (Semboja & Therkildsen, 1989; Tinios *et al.*, 1993), a specific set of assets were chosen as indicators of wealth: Bicycle, house (own or rent), type of house (mud wall, bloc wall, iron sheeted roof, cement floor), radio and wristwatch. Questions on religion (Christian, Muslim, other) and place of origin (born in the area or migrant from other regions of the country) were also included, since these variables may have an impact on the respondent's social network (i.e., peer groups) in the local communities. Marital status and age were controlled because research from Western countries indicate that these variables may be related to compliance behavior, for instance, via perceptions on the severity of sanctions (Kinsey, 1992, p. 266; Hessing, Elfers, Robben, & Webley, 1992, p. 292).

(ii) *Admitted (non)compliance*

The respondents were asked if they had paid development levy in each of the two recent years. Respondents giving an affirmative answer were then asked about the tax rate paid. The answers were compared with the correct rates to establish the credibility of the answers given.

(iii) *Tax enforcement*

A series of questions were asked on tax collection procedures, including which part of the council was involved and how payment was made. Moreover, the respondents were asked if they knew someone in the neighborhood not paying and the types of legal sanctions applied to noncompliers. These questions aimed to examine how contact with tax enforcers and procedures of collection might affect taxpayer behavior. Questions were also asked about their view of tax collectors and local politicians with respect to integrity, and whom they considered were most to blame for the problems of collecting the development levy.

(iv) *Perceptions of others' behavior*

Respondents were asked about their perceptions of other taxpayers' behavior regarding compliance. One question focused on their perception of why some people paid, while another asked about their perception of whether taxpayers would comply if the probability of being detected was low.

(v) *Perceptions of the terms of trade with the government*

To measure perceptions of the terms of trade with the government, a series of questions were asked about the quality of public services and the value received in return for tax payment. Emphasis was put on the perceived relationship between tax compliance and the provision of public services.

(c) *Data analysis and problems*

The limitations of survey methods are acknowledged, yet more rigorous methods were found unsuitable in this particular research effort. Although the case studies do not cover the whole range of possible choices by taxpayers, they probably represent many of the most important choices and decisions. Thus, if the findings are consistent with the theoretical models, the case studies may provide means to consider the plausibility of the hypotheses generated by the models outlined above. [9]

In surveys of tax evasion in Western countries (e.g., Kinsey, 1992) it is argued that because tax evasion is considered socially undesirable, responses to a questionnaire will be adversely biased. This might also be the case in Tanzania, although anecdotes suggest that tax evasion is *not* associated with the type of social stigma referred to in the West. In contrast, some observers describe nonpayment of the development levy as a form of popular opposition toward state policies (Tripp, 1997, p. 154). If this description is correct, we would expect an "inverse adverse bias" compared to surveys from developed countries, i.e., a larger share of the respondents claims not to have paid relative to the actual compliance rate. Data in the study did not, however, show any indications of such an inverse relationship.

The share of compliers in the sample (Table 1) is far higher than the figures of aggregate compliance rates compiled from the Tax Register Books in Kibaha and the accounts of the revenue department in Kilosa. At least three factors may explain this seemingly "overrepresentation" of compliers.

First, due to time and budget constraints, taxpayers living in more remote areas of the selected villages were excluded from the sample. It can be assumed that remote areas have fewer compliant people compared to more accessible places, because of less strict tax enforcement. Thus, a certain overrepresentation of compliers in the sample seems reasonable. The reduced participation level in Kilosa may have also led to an overrepresentation of compliers. Second is strategic answering. The answers on how much respondents paid in development levy in each of the two years were checked against the actual development levy rate. The assumption was that noncompliers claiming to have paid the levy would be unable to provide correct answers on the rates. The responses indicate a higher degree of strategic bias in Kilosa compared to Kibaha. Controlling background variables such as age and migration showed that the age group below 30 years in Kilosa is overrepresented among those claiming to have paid but providing wrong response on the rates. The third factor has to do with embezzlement. Evidence of prevalent embezzlement of tax revenues by collectors is found in many local authorities in Tanzania (CIET International, 1996; Fjeldstad & Semboja, 2000). Thus, tax revenues reported in the accounts of local authorities may be significantly lower than what is actually collected. Aggregate compliance, therefore, is likely to be higher than indicated by the district council's revenue files.

The statistical analysis consisted of a step-by-step process, starting with frequencies, crosstabulations combining bi- and multivariables, and, finally, an exploratory analysis of the two cases. Clearly, no findings of statistical significance can be generated by these case studies except generating suggested explanations to the tax compliance behavior observed. Thus, although the analysis developed in the following sections is limited by the cases upon which it is based, it has a more general interest and application.

4. RESULTS

This section first provides a descriptive presentation of the characteristics of those who pay development levy (i.e., compliers), and then proceed to analyzing why (some) people pay.

(a) *Who pays*

The aggregate compliance rate of the sample in Kibaha is 66% in 1995 and 44% in 1996 (Table 1). [10] The corresponding figures for Kilosa are 80% and 84%. The sharp decline in aggregate compliance in Kibaha during 1995–96 may be related to the doubling of the development levy rate from TSh 500 to TSh 1,000. Important background variables characterizing compliers are place of residence (i.e., village), migration, religion, occupation, wealth and age.

(i) *Place of residence and compliance*

Compliance rates vary between the selected villages (Table 1). In Kibaha, compliance is highest in Pangani in both years (76% and 55%, respectively). The compliance rate is also relatively high in Mwendapole. Tax resistance is highest in Disunyara (51% complied in 1995 and 35% in 1996). The *relative* compliance rates between the surveyed villages in Kibaha are consistent with figures from the accounts of the ward executive officers. The figures from Kilosa also indicate differences in compliance rates between the villages, although we should be cautious to draw general conclusions from the small sample, in particular for Dumila village.

(ii) *Migration and compliance*

Migrants from other regions constitute 53% of the sample in Kibaha and 30% in Kilosa. The difference between the two councils reflects fairly well the real situation. Due to its proximity to the city of Dar es Salaam a larger share of the population in Kibaha is expected to be migrants. Migrants appear to be more compliant than people born in the study areas. This is the case for both Kibaha and Kilosa, although the difference in compliance rates between migrants and nonmigrants in Kilosa in 1996 is insignificant (Table 2). Since the share of migrants among the taxpayers in the villages varies, this may contribute to explain the differences in compliance rates between villages.

(iii) *Religion and compliance*

The majority of the respondents are Muslims, i.e., 75% of the sample in Kibaha and 73% in Kilosa. In Kibaha, the majority of Christian and 39% of the Muslim respondents have migrated to the area from other regions of Tanzania. In the Kilosa sample, 75% of the Christians are migrants, while only 13% of the Muslims are not born in the area. Christian respondents in Kibaha appear to be more compliant than Muslims. In Kilosa, we find only minor differences between Muslims and Christians in this respect.

The observed differences between Muslims and Christians in Kibaha may indicate that cultural differences, including religion, matter in tax compliance. Compliance rates of Muslim and Christian migrants differ less, however, than the compliance rates of Muslims and Christians as aggregated groups. The data indicate that migrants, in general, independently of religion, are more compliant than nonmigrants. We do not find noteworthy differences between Muslims and Christians with respect to other variables.

(iv) *Occupation and compliance*

We find only small differences between the three rural villages in Kibaha with respect to principal income. In the rural–urban village of Mwendapole, however, self-employment is more important as source of income than in the other villages where agriculture is predominant. In Kilosa, the majority of the respondents in all villages are agriculturists.

The highest compliance rate is found in households with wage employees in the public sector in both districts. The compliance rate for self-employed in trade and commerce is also relatively high. Furthermore, households with more than one income earner are more compliant than households with only one income earner. Thus, income (ability to pay) seems to be an important background variable in explaining compliance.

(v) *Wealth and compliance*

Three of the selected wealth indicators seem to have explanatory power in Kibaha: Radio and wristwatch ownership and house with iron sheeted roof. [11] The compliance rate of respondents who live in houses with corrugated iron- sheeted roofs is found to be higher than average. Out of the total sample, 63% of those living in houses with iron-sheeted roofs are migrants. Furthermore, a larger share of the migrants (64%) own wristwatches compared to nonmigrants (22%).

In Kilosa, respondents owning bicycles are more compliant than those not owning this asset. Moreover, a larger share of migrants (85%) compared to nonmigrants (67%) owns bicycles, [12] possesses wristwatches and lives in

Table 2. *Compliance rates among migrants and people born in the area (in percentage)*

	Kibaha ($N_{\mathrm{Migr}} = 68$ and $N_{\mathrm{Nonmigr}} = 60$)		Kilosa ($N_{\mathrm{Migr}} = 13$ and $N_{\mathrm{Nonmigr}} = 31$)	
	Compliance rate in 1995	Compliance rate in 1996	Compliance rate in 1995	Compliance rate in 1996
Migrants	72	54	92	85
Nonmigrants	60	32	74	84

houses with iron-sheeted roofs. In general, the survey data indicate that migrants are wealthier than nonmigrants.

(vi) *Age and compliance*

The data on the relationship between age and compliance show that compliance is lowest for the youngest age group (i.e., 18–29 years of age). The age groups between 30 and 59 years appear to be the most compliant ones. In Kilosa, however, respondents above the age of 60 were the most compliant in 1995. [13] The small number of respondents in the age groups below 30 and above 50 in Kilosa makes generalizations on the basis of age questionable.

(b) *Why people pay*

Three of the five hypotheses are supported by this explorative analysis. Tax compliance seems to be positively related to ability to pay, the (perceived) probability of being prosecuted (including opportunities for evasion), and the number of tax evaders known personally by the respondent. Positive relationships were not found between tax compliance and the perceived severity of sanctions against defaulters. In contrast, severe sanctions and discontent with the terms of trade with the government seem to increase tax resistance, and, thus, contribute to explain the widespread tax evasion observed.

(i) *Ability to pay*

A general observation from the surveys is that the relatively better-off respondents seem to be most compliant, as seen from households with more than one income earner compared to households with only one income earner. In addition, better-off migrants seem to be more compliant than nonmigrants. Furthermore, the relationship between age and compliance may be related to ability to pay with the youngest age group being less wealthy in durable assets.

The poor compliance of the oldest age group in the Kibaha sample negates the view that elderly people are generally more compliant than younger ones for fear of being embarrassed in court. It diverges also from surveys carried out in Western countries which find that increasing age appears to be related to lower tax resistance (e.g., Spicer & Lundstedt, 1976). Our result either suggest poor measurement or a failure to include other important variables. It does, however, support the result that income and wealth are important background variables when explaining compliance. Elderly people often have low ability to pay, representing small and less affluent households. Thus, the marginal utility of evading one shilling is higher for these people compared to better-off people, and their opportunity costs of hiding from tax collectors are less. Given the traditional respect for elders in African societies, we may also expect that tax enforcement is less strict on elderly people.

The increased number of admitted noncompliance in Kibaha (1995–96) and in Kilosa (1996–97) indicates that higher taxes may have led to larger compliance problems. [14] The respondents' views on the tax rate also provide an indication of the importance of ability to pay. Eighty-nine percent of the respondents in Kilosa consider the development levy rate to be too high, while only 11% consider it to be reasonable. The corresponding figures for Kibaha are 51% and 44%. The development levy rate in Kilosa was twice as high as in Kibaha when the study was carried out. These responses indicate that ability to pay is an important background variable in explaining compliance. But, establishing a link between ability to pay and compliance does not show which way causation flows. For example, it does not show whether tax resistance is lower among the better-off migrants, or whether tax enforcers directly target these people.

(ii) *Probability of being prosecuted*

The differences in compliance between occupations are partly based on different opportunities to evade and partly on the probabilities of being prosecuted. The highest compliance rate (100%) is found among wage earners in the public sector because development levy is withheld from their salaries.The relatively low compliance rates of agriculturists and self-employed (i.e., carpenters, charcoal makers, etc.) in Kibaha are consistent with findings from Western countries, which reveal that admitted tax evasion is relatively high among the self-employed (e.g., Mason & Lowrey, 1981). [15] Thus, the relatively high compliance rate of self-employed in trade and commerce may seem surprising. Several factors, however, may contribute to explain this observation.

Tax campaigns are organized by the Ward Executive Officers accompanied by the local militia (Fjeldstad, 2001). During these campaigns many taxpayers literally run away and "hide in the bush." In principle, tax campaigns are instigated when the deadline for payment has expired, usually after October 1. Before this date, and according to tax by-laws, payment is considered to be "voluntary," although, tax campaigns seem to be an ongoing affair throughout the year. It is reasonable to assume that the opportunity costs of hiding from tax enforcers are relatively higher for the more wealthy people compared to poorer households. The relatively better-off persons thus put less effort into hiding and are more easily targeted by tax enforcers. Furthermore, the marginal utility of a shilling saved by evading taxes is higher for the poorer households than for the better-off, which induces poorer households to hide during the campaigns.

Given limited administrative resources, tax collectors maximize yields by concentrating on the most accessible and better-off taxpayers. Thus, ability to pay and accessibility become key variables when enforcement priorities are made. Such mechanisms, in addition to factors related to opportunity for evasion, explain the relatively high compliance rate of self-employed in trade and commerce. Shopowners, for example, need a development levy card (a receipt) to get a business license. Their opportunities to evade are thereby reduced. In addition, even if they had the opportunity, their opportunity costs of hiding from tax enforcers are relatively high compared to people in other occupations, say agriculture.

The same factors may also explain differences in the compliance rates of villages (Table 1). According to the wealth indicators, respondents in Mwendapole village are relatively better-off than people in the other villages. This is due to its location by the main road and being a rural–urban village. More trading and easier access to markets may arguably contribute to greater wealth. For instance, a larger share of the respondents in Mwendapole (93%) own radios compared to other villages. A similar pattern is found with respect to the other wealth indicators (wristwatches and iron-sheeted roofs). Wealth, reflecting ability to pay, may therefore be an important background variable in explaining compliance in this village. Mwendapole is also more easily accessible than the other villages for tax collection and enforcement. Thus, the probability of being prosecuted is likely to be higher in Mwendapole than in other villages.

In Pangani, the most compliant village in Kibaha DC, two different factors from those observed in Mwendapole support the assumption that coercion influences compliance behavior. First, there is more efficient enforcement compared to the situation in the other villages. Since recruitment of a new Village Executive Officer (VEO) in Pangani in August 1995, revenue collection increased significantly. Moreover, the relatively small size of this village makes it easier to target noncompliers. Second, more respondents in Pangani are migrants who, in general, are better-off and more compliant than nonmigrants. The migrants are also less integrated and have looser relations to local authorities, including tax collectors, than people born in the area, making them easier targets of tax enforcers. This indicates that the *actual probability* of being prosecuted is higher for migrants compared to nonmigrants. In Kibaha, this proposition is supported by the finding that a larger share of the migrants (25%) compared to nonmigrants (8%) considers lack of opportunities for evasion to be the main reason why people pay the levy.

Direct targeting by collectors requires that the collectors know the taxpayers and their ability to pay. This is the case in Kibaha where tax collection is carried out by the Village Executive Officer (VEO), who lives in the village and is nominated by the Village Government. But, in Kilosa where tax collection is carried out by the ward-level personnel there is less knowledge of the villagers and their ability to pay. The ward officials are nominated by the district level officers and are not villagers *per se*. Thus, there is probably less direct targeting in Kilosa. Some forms of targeting may, however, still be of importance. For instance, respondents owning bicycles in Kilosa are found to be more compliant than others. This is most likely due to the use of roadblocks as tools of tax enforcement. At these roadblocks people are required to show their tax receipts or to pay the levy. Since bicycles are frequently used to transport goods to and from markets it is inconvenient for the users to find alternative routes through the bush to avoid payment of taxes, including the development levy and bicycle tax. [16] Therefore, according to more than 30% of the respondents in Kilosa, people pay taxes "to avoid disturbances."

Another factor which induces migrants to comply is their relations with (and obligations toward) the family at their home-place. In a study from Kenya, Smoke (1994, p. 39) reports that "[f]amilies of migrants remain in their 'home' area of origin, and the migrants visit 'home' frequently, fully intending to return there to settle down after accumulating some desired level of resources.'' This probably describes fairly well the situation in Tanzania, too. It could thus be assumed that migrants travel more compared to nonmigrants. Anecdotal evidence shows that the police often control travelers, in particular bus passengers, at road checkpoints, and request people to present their development levy receipts (Bukurura, 1991; Tripp, 1997). Therefore, to avoid police harassment and inconvenience migrants may decide to ''voluntarily'' pay the levy. This argument is also consistent with the observation that the self-employed in trade and commerce are more compliant than other occupations in the private sector.

(iii) *Perceptions on the severity of sanctions*

Anticipated positive relationships between compliance and the perceived severity of sanctions against defaulters are not supported by the data. Personal experience with and observation of other peoples' experiences with tax enforcement at the village and ward levels are indicators of the severity of sanctions.

A noteworthy observation in Kibaha is the different experiences of migrants and nonmigrants. Thirty-four percent of the migrants answered that they (or someone they knew personally) had *never* been contacted by the tax collector to pay tax with penalty, while only 13% of the respondents born in the area gave this answer. In Kilosa, only minor differences between migrants and nonmigrants were found on this issue. On the question whether the respondents knew someone who had been convicted for not paying, 68% of the migrants in Kibaha answered negatively, compared to 47% of the nonmigrants. The corresponding figures for Kilosa were 77% and 68%. On the reaction of the council or ward to tax evaders, 57% of the migrants said they ''have to pay tax plus penalty,'' while 75% of the nonmigrants gave this answer.

From the standard theory it would be expected that the more severe the sanctions perceived by taxpayers, the higher the compliance. The survey results seem to point in the opposite direction: The more severe the sanctions observed, the more widespread the tax resistance. The reason for this ''perverse'' relationship may be due to reciprocity considerations. [17] The reciprocity argument leads to the proposition that tax authorities' unresponsive, disrespectful and unfair treatment of taxpayers fosters disrespect for and resistance against tax authorities and tax laws—also a kind of reciprocation in kind (Smith, 1992, p. 227).

The strength of the possible reciprocity effects on compliance behavior probably depends on the taxpayers' experiences with the tax authorities. Those who have been brought to court by the militia may have resentment and develop a generalized normative response. Those who have had no experience with tax authorities rely on experiences of others and from their more general perceptions of the tax system and of how government officials treat citizens. Since these perceptions are typically less specific than are personal experiences, their effects on compliance are likely to be primarily indirect through generalized normative commitments.

If the proposition on reciprocity is correct, it may contribute to explain the widespread noncompliance observed in the survey area. Oppressive enforcement of the development levy and harassment by collectors may induce tax evasion which may in turn be interpreted as a strategy of public resistance and opposition against the authorities. Strict tax enforcement is considered to be a problem in many councils, not least by politicians (Fjeldstad, 2001). During election campaigns both local and central government politicians usually deliver the message that tax collectors should relax on tax enforcement and not harass taxpayers.

Tax resistance may sometimes also take more violent forms. In Kilosa tax collectors are reported to have been attacked by the public. One collector, for example, had been seriously wounded after being hit on the head with a panga (a large chopping knife used by peasants) when he approached an assumed tax defaulter. In 1996 the ward office in Chanzuru was destroyed during night and the Tax Register Books burnt. Some villages in Kilosa are either avoided by collectors or only visited by collectors in company of local militia. Similar cases are also reported from other councils. For example, the *Daily News* (November 28, 1997, p. 5) reported an attack on over 20 Moshi Municipal Council workers who were on a special operation to net development levy defaulters. Some of the officials were seriously injured by the mob.

(iv) *Terms of trade with the government (fiscal exchange)*

A major problem perceived by taxpayers is that they see few tangible benefits in return for the taxes paid. [18] The respondents' perceptions of the quality of public services are fairly similar in Kilosa and Kibaha (Table 3). But, dissatisfaction seems to be highest in Kilosa where 75% of the respondents consider the quality to be bad compared to 66% in Kibaha. None of the respondents in Kilosa perceive the public services to be good. [19] The majority of the respondents in both councils say the current quality of services is worse than three years ago. [20]

More than 80% of the respondents in both councils ascertain that the development levy is "only partly" or "not at all" used to provide public services. On the issue of major problems with tax collection (Table 4), there are minor differences between compliers and noncompliers. In Kibaha, the major problem mentioned is that taxes are not spent on public services (55% of the respondents), while in Kilosa high tax rates (doubled in 1997 from the previous year) are considered to be the major problem (46% of the sample), followed by nonprovision of public services.

Two observations seem evident. First, there is a widespread discontent among people regarding their terms of trade with the government. More than 60% of the respondents in Kilosa indicated that all taxpayers would cheat if they could get away with it mainly because of poor public services. The corresponding figure for Kibaha is 55%. Other studies support this assertion. Bukurura (1991, p. 91), for example, cites investigations from 1987 by the *Tanzania News Agency* in Kigoma Town Council, which reported that "many people were defaulting apparently because the council was not doing its best to serve the residents." Tripp (1997, p. 233) refers to an article in *Daily News* (June 9, 1985) where a Dar es Salaam resident confirmed that: "When it comes to Development Levy we have... seen nothing as a result of the levy we pay... the city is very dirty and the situation is deteriorating day in and out... What we want to see is how such taxes are being spent." Second, migrants seem to be more dissatisfied than nonmigrants possibly because of greater expectations for improved living conditions, and particularly so because migrants are generally more compliant. When the expected improvements are not fulfilled their disappointment and frustration may possibly be reflected in their perceptions of the authorities, including their views of the quality of public services.

Table 3. *Perceptions on the quality of public services (in percentage of total number of respondents)*

Perception	Kibaha ($N = 128$)	Kilosa ($N = 44$)
Good	6	0
Average	26	25
Bad	66	75
Do not know	2	0

On the question "do you agree with people saying that they will not pay taxes until they get better services in return from the Council," many respondents disagreed (68% in Kibaha and 43% in Kilosa). Although this response may seem contradictory to the findings discussed above, it indicates that many people do in fact understand the relationship between taxes and public services. One respondent used the metaphor that "one cannot build a house without first buying concrete." Furthermore, a majority of the respondents (more than 90%) indicated willingness to pay more taxes if services were improved although some expressed reservation that it depended on their ability to pay. [21] These results therefore deviate from other studies, including URT (1991) and Bukurura (1991) which claim that people in Tanzania lack a basic understanding of their duty to pay taxes.

(v) *Social influences*

The survey data support the hypothesis concerning the influence of social pressure on taxpayer's compliance. Knowledge of tax evasion may have an impact on the behavior of

Table 4. *The most important problems with respect to tax collection, Kibaha and Kilosa (in percentage—Kilosa in brackets)*

Problem	Aggregate $N = 128$ ($N = 39$)	Nonmigrants $N = 60$ ($N = 29$)	Migrants $N = 68$ ($N = 10$)
Too high rates	12 (46)	18 (48)	6 (40)
Taxpayers are unwilling to pay	17 (13)	17 (10)	18 (20)
Taxes are not spent on public services	55 (23)	47 (21)	62 (30)
Other	16 (18)	18 (20)	14 (10)

a taxpayer by influencing his perceived probability of being detected. Most compliers in Kilosa say they do not know anyone not paying. In Kibaha, there are only minor differences between compliers and noncompliers on this issue. Most migrants in both councils also claim that they do not know anyone not paying which may signify that they are less integrated in the village society, and thus have less knowledge of the behavior of others. The larger the fraction of the local population that is observed not paying, the lesser the perceived risk of being prosecuted. Since migrants seem to know fewer tax evaders than nonmigrants, this may imply that—on average—a migrant's perceived probability of being prosecuted is higher than that perceived by a nonmigrant which partially explains why migrants are more compliant than nonmigrants.

5. SUMMARY AND CONCLUSIONS

While acknowledging some obvious weaknesses of an essentially exploratory study, the survey data suggest that the following factors contribute to explain compliance behavior.

Opportunities: Differences in opportunities for evasion matter, for example, employees paying their head-tax through a tax withholding system have fewer opportunities to evade than the self-employed.

Ability to pay: Some of the relatively better-off respondents, in particular migrants and traders, are more compliant due to: (a) higher opportunity costs connected with evasion, and (b) because they are easily targeted by tax collectors. The opportunity costs of hiding from tax collectors are higher for the better-off, since hiding "puts one out of business." Thus, relatively better-off persons put less effort into hiding, and, therefore, are more accessible to tax enforcers. This result further implies that the development levy is a less regressive tax than what is usually claimed (URT, 1991).

Probability of prosecution: Given the limited administrative resources, it is rational for collectors to concentrate on the more accessible and better-off taxpayers. In this case the ability to pay and accessibility are key variables. Since migrants are less integrated and have looser relations to local authorities than nonmigrants, it is easier and probably more convenient for the tax enforcer at the village level to target migrants rather than people from the area who might be their relatives, friends or who have closer links to local politicians and authorities. This indicates a lack of integrity in the tax enforcers' relationship with taxpayers, and implies that the probability of being prosecuted is most likely higher for migrants. Moreover, taxpayers who travel regularly are more compliant than others because of control mechanisms such as roadblocks where travelers are requested to present their tax receipts.

Social influences: Knowledge of the compliance behavior of others seems to influence the taxpayer's perceived probability of being prosecuted. The larger the fraction of the local population that is observed not paying the lower the perceived risk of being prosecuted.

Severity of sanctions: The way the law is enforced and the severity of sanctions appear to have fuelled tax resistance. This contradicts the standard theory which tells us that the more severe the sanctions perceived by taxpayers, the higher the compliance expected. The survey results point in the opposite direction: The more severe the sanctions, the more widespread the tax resistance. The reason for this "perverse" relationship is not entirely clear, however, it may be due to reciprocity considerations. The coercive behavior of tax authorities fosters resistance and disrespect for tax laws. Accordingly, oppressive enforcement and harassment by collectors also induce tax evasion. Tax evasion may, therefore, to some extent be interpreted as a strategy of public resistance and opposition against the authorities.

Fiscal exchange: Generally, the development levy is perceived to be unfair. Perceptions of exploitation due to unfair terms of trade with the government promote noncompliance. Thus, peoples' tax resistance seems to be correlated to the decline or absence of public service provision.

We have not explored the relative strength of the various factors in explaining the observed patterns of tax compliance. The results suggest, however, that the standard economic influences of tax size and detection probability are at work, although other determinants also are essential in understanding taxpayers' behavior. In particular, the relationship between taxation and service provision and how the tax law is enforced seem to be important. If our analysis of the factors determining compliance behavior is correct, it also contributes to explaining observed differences in tax compliance between local authorities and between areas within individual councils. Thus, the experience with the development levy may enrich our understanding of tax compliance behavior in Tanzania. Furthermore, citizens' experience with the development levy has contributed to undermine tax morale and the legitimacy of the state, which may have long-term consequences for the performance of local governments in the country.

The study provides us with some directions for future research. For an improved understanding of tax compliance behavior in poor countries, there is a need for a more thorough examination of the concept of fairness in fiscal exchange, i.e., the contractual relationship between taxpayers and the government. In this context it is also relevant to analyze if—and when—user charges are to be preferred instead of general taxes to finance public services. Critical factors in this respect are citizens' perceptions about the role of the state, how the tax law is administrated, perceptions about enforcement, and government trustworthiness. Furthermore, there is a need for research focusing on taxpayers' rights in situations where the government—and donors—are pressing for increased domestic tax effort. Can, and under what conditions, compliance be established in poor countries without an extensive and costly enforcement apparatus? This question is important because it is likely that governments, seeking power on the basis of popular consent, face restrictions in their use of coercion in tax collection. Thus, the challenge for taxation in poor countries is to raise domestic revenues from consenting citizens.

NOTES

1. Revenues from the development levy have fallen in recent years. In 1984–85, the levy contributed with over 60% of total own revenues in rural councils and about 50% in urban councils (URT, 1991). These aggregate figures do, however, hide major differences between individual councils. In 1995, for instance, the development levy as a percentage of total own revenues in district councils varied from 3.3% in Kilwa District Council (DC) to 63.5% in Singida DC (Fjeldstad & Semboja, 2000).

2. The issue of women paying the levy has been controversial (Tripp, 1997, p. 157). Supporters of the levy on women argue that women are equal to men according to the law, and thus have the same rights and obligations as men. Opponents argue that women in rural areas are economically dependent on men and therefore should be exempted. In particular, the development levy has revealed a conflict between upper- and lower-income women.

3. Nearly all economic approaches to tax evasion are based on this economics-of-crime framework. Cowell (1990) provides a review of this literature.

4. The potential for free-riding is obvious when the government offers collective goods in return for taxes (Axelrod, 1984). According to the Folk theorem, however, voluntary provision may not always play as a "prisoner's dilemma" game, in which each individual has an incentive to free-ride on the provision of others. Instead, individuals may in many cases voluntarily contribute to a public good, implying that they will pay taxes. In theory, this occurs when service provision is both repeated and interdependent. See Gibbons (1992) for an introduction to the literature.

5. Survey research from Western countries also suggests that taxpayers make judgements about the fairness of particular taxes (e.g., Smith, 1992).

6. One of the most consistent findings in survey research in Western countries about taxpayer attitudes and behavior is that those who report compliance believe that their peers and friends (and taxpayers in general) comply, whereas those who report cheating believe that others cheat (Yankelovich, Skelly, & White, 1984).

7. We distinguish between (a) *perceived probability* which is the taxpayer's own perception of the probability of being detected, and (b) *actual probability* which is determined by the resources put into tax enforcement by the tax collecting agency.

8. As illustrated in Table 1, the response rate varied between the villages. The lowest one (0.77) was experienced in Mwendapole village, while Disunyara and Pangani had response rates above 0.90.

9. Levi (1997) discusses the strengths and weaknesses of this methodological approach.

10. Compliance rate is here defined as the share of respondents who claims to have paid the levy.

11. According to World Bank (1993, p. 41) radios and watches are the two durables whose ownership is most closely connected with poverty in households in Tanzania.

12. The greater importance of bicycles as an indicator of wealth in Kilosa compared to Kibaha is consistent with our observations during the field studies. But, the national 1991 survey on households' consumption and poverty found no positive correlation between the ownership of bicycles and income (World Bank, 1993, p. 41).

13. Regarding the background variable "age," there is a bias in our sample. In Mwendapole village only one respondent is below the age of 30. Since this age group seems to be the less compliant, this may contribute to explain the higher compliance rate found in this village.

14. In Kilosa, the compliance rate for 1997 was found to be only 18%. This low rate may partly be due to the doubling of the development levy rate from TSh 1,000 in 1996 to TSh 2,000 in 1997. But, since the deadline for voluntary payment had not expired when the survey was carried out a relatively low compliance rate is expected. Therefore, the results for 1997 are not included in this study.

15. The number of self-employed and wage employees in the samples is very small. These results should therefore only be considered as indicative.

16. The bicycle tax is paid annually. In Kilosa it was TSh 1,000 in 1997. The estimated number of bicycles in the council was 13,718. When the bicycle tax is paid a receipt in the form of a sticker to be attached to the bike is provided. This system is similar to the "car sticker" used as a receipt for various car-related taxes in many Western countries.

17. Sugden (1984) refers to the response of reciprocating behavior as a "cross-societal norm of reciprocity: a norm both in the sense of a universal regularity and a moral responsibility." The reciprocity norm evokes an obligation for individuals to make a concession to someone who has made a concession to them. The reciprocity argument may also be linked to the argument on "tax morale." Thus, Frey (1997, p. 49) argues that the more extensive citizens' direct political participation possibilities are, the higher is intrinsic motivation in the form of tax morale and *ceteris paribus* tax compliance.

18. Local authorities are responsible for running a range of public services of which the key sectors are primary education, health care, rural roads and water supply. In principle, priorities may differ by councils. In practice, however, the four key sectors have received most attention. A recent survey on "grassroots' views," covering the whole country, showed that in particular education and health were perceived as priority concerns in many rural areas (URT, 2000).

19. The response from people in Kilosa is interesting considering the long-term involvement of international development aid agencies in the area, in contrast to Kibaha which has experienced limited donor support. For instance, the main roads in Kilosa have a fairly good standard due to donor funding. Furthermore, donors are involved in the education and health sectors. But, people do seem to be well aware about who is responsible for the different services. Thus, the main roads are referred to as "Irish roads" and the almost nonpassable feeder roads are named "council roads."

20. These results are consistent with the findings of a study of local government health services in Tanzania (Cooksey & Mmuya, 1997). Sixty-five percent of the respondents in this study considered the poor quality of these services to be a major problem. Furthermore, 69% of the respondents said they disagreed with the statement that the quality of public health services had improved in recent times.

21. This response is consistent with studies from other countries which show that even poor people are willing to pay something for services they value, for example, education (Bird, 1990, p. 407). Bird adds that people also value more those things for which they have to pay.

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What's trust got to do with it? Non-payment of service charges in local authorities in South Africa

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ABSTRACT

A major financial problem in many municipalities in South Africa is the inadequate collection of service charges due to widespread non-payment. The prevailing view is that non-compliance is caused by poverty and the existence of an 'entitlement culture'. However, huge variations in compliance exist both within poor communities and between communities with similar socio-economic characteristics. How can these differences be explained? Moreover, what factors determine citizens' compliance? This paper argues that non-payment is related not only to inability to pay and 'a culture of entitlement', but also to whether citizens perceive the local government to act in their interest. In particular, three dimensions of trust may affect citizens' compliance: (1) trust in the local government to use revenues to provide expected services; (2) trust in the authorities to establish fair procedures for revenue collection and distribution of services; and (3) trust in other citizens to pay their share.

INTRODUCTION

This paper examines factors determining compliance behaviour with respect to service charges in local authorities in South Africa. Local authorities rely to a large extent on user charges – especially utility fees on electricity and water – to obtain the revenues that are needed to finance their operations (RSA 2001). However, a major problem is inadequate collection of revenues, mainly due to widespread non-payment. The results are year-end deficits, a reduction of local government services to balance the budget, and higher fees and taxes for those who do pay. In

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recent years non-compliance with respect to service charges, fees and rates has worsened (*ibid.*: 151). Consequently, the issue of non-payment has entered the core of current policy debates in South Africa on poverty alleviation, service delivery and local governance. According to the minister for provincial and local government, the government regards 'addressing the issue of non-payment for services as fundamental to the challenge of creating effective, accountable, developmental local government' (Mufamadi 2002: 11).

The non-payment of rates and service charges, particularly in African and coloured areas, is not, however, a new phenomenon in South Africa (Bond 2000; McDonald 2002a).[1] During the apartheid period, boycotts of rents and user charges became the chief weapons against what was considered an illegitimate regime. In the late 1980s, many townships and rural areas in the homelands were already effectively ungovernable (SoG 1998). With the passing of the apartheid system, such boycotts were expected to cease, but they did not. Non-compliance with respect to service charges seems to have become an established 'norm' in many areas, creating major constraints to attempts to develop a viable new local government system in South Africa (Timm *et al.* 1998). Moreover, the phenomenon of non-payment, which until recently has been an African one, is likely to spread into other ethnic groups in accordance with growing dissatisfaction with government performance (Mattes *et al.* 2000).

Different arguments are used to explain the extensive and increasing non-compliance. A recent study by the Centre for Development Support (CDS 2001) at the University of the Free State concludes that non-payment is primarily an issue of inability to pay. It is argued that the poverty of many households makes them unable rather than unwilling to pay, hence the need for free basic services to the poorer segments of the population and/or a lowering of the rates. This argument is supported by, for instance, Fiil-Flynn (2001) and McDonald (2002b). Other studies, however, claim that widespread unwillingness to pay exists due to an 'entitlement culture', and the 'culture of non-payment' inherited from the apartheid era (Ajam 2001; Johnson 1999). It is assumed that an understanding of the relationship between payment and the provision of services is a critical factor for compliance. Consequently, the prescription is education and political mobilisation of ratepayers, combined with the restoration of law and order.

I do not contest the ability-to-pay argument, or the claim that there might exist a 'culture of non-payment'. However, in this paper I argue that the causes for non-payment are more multifaceted and complex. Huge variations in compliance exist both within poor communities and between communities that have quite similar socio-economic characteristics. How do we explain such differences? Furthermore, what factors determine citizens' compliance behaviour with respect to service charges? In particular, I argue that three dimensions of trust may affect compliance: (1) trust in the local government to use revenues to provide expected services; (2) trust in the authorities to establish fair procedures for revenue enforcement and distribution of services; and (3) trust in other citizens to pay their share of service charges. Hence, non-compliance is a question not only of state–society relationships, but also of relationships between citizens and/or between groups of citizens within local communities. Considerations of these issues may shed light on the observed differences between and within local authorities with respect to service charge compliance, and factors determining citizens' compliance behaviour.

The remaining part of the article is divided into four sections: The first section provides a brief description of the extent and characteristics of non-payment across and within municipalities in South Africa. Can trust affect economic behaviour? This question is the point of departure for the second section, which briefly reviews the theoretical arguments on how trust between citizens and the (local) government and trust among private parties may affect citizens' willingness to pay. The third section focuses on the social, economic, administrative and political factors that are expected to influence citizens' compliance behaviour with respect to service charges. In particular, the section discusses whether trust can explain differences in compliance between local authorities and population groups. Finally, the fourth section concludes by discussing possible approaches to improving compliance.

LOCAL GOVERNMENT FINANCES AND NON-PAYMENT OF SERVICE CHARGES

Local authorities in South Africa generate, in aggregate, about 92% of their own revenues (RSA 2001: 146). The remaining revenues are transfers from the national and provincial governments.[2] However, huge differences exist between municipalities. For instance, metropolitan councils mobilise, on average, 97% of the revenues themselves. In contrast, some smaller municipalities only raise 65% of their revenues from their own sources. Revenue sources also differ between local authorities depending on local circumstances. These are largely similar to the former apartheid tax regime for local government (FFC 1997: 16). The most important sources are (1) user charges on services (electricity, water and sanitation); (2) property rates in urban areas; and (3) the Regional Service Council

(RSC) levy charged by district and metropolitan councils on staff or labour. Utility fees from trading services comprised 32% of the revenue base of municipalities in 1999/2000, with electricity charges making up the largest share followed by water. Property rates contributed 21% of the aggregate municipal revenues, intergovernmental transfers 8%, RSC levies 7%, and other revenues 32%.[3]

A major financial problem for local authorities is poor compliance and inefficient collection of revenues, in particular with respect to electricity and water charges. The most recent figures from the Department for Provincial and Local Government (RSA 2003: 43–4) show that since 1994 municipalities have accumulated a total of ZAR 24·3 billion of consumer debt due to non-payment. This compares with budgeted municipal operating expenditure for 2002–03 of ZAR 61·4 billion (*ibid.*: 32–3). Moreover, the level of outstanding debtors as a percentage of annual billing in many municipalities has steadily increased in recent years (RSA 2001: 150). For instance, in George (Western Cape) the outstanding debtors as a percentage of annual billing were approximately 44% in Fiscal Year (FY) 1997/98, and increased to 61% in FY 1999/00. The corresponding figures for Johannesburg are 24% and 36%, respectively. Furthermore, revenue collection levels, measured as the amount collected as a percentage of the amount billed, have worsened in many municipalities in recent years. For instance, in Johannesburg metropolitan area, revenue collection levels decreased from around 74% in FY 1997/98 to 65% in FY 1999/00.

The ministry responsible for local government has been unwilling to issue an overview of those communities that are regarded as chronic non-payers of service charges. But, based on available statistics, Yorke (2003) estimates that approximately 63% of consumer debt is owed to the six metropolitan councils. As three of these are in Gauteng, the level of consumer debt is highest in that province. According to Johnson (1999: 2), roughly one third of all African townships are 'chronic' non-payers, another one third are 'partial' payers, and the remaining are 'reasonable' payers. Available data also indicates that huge differences in compliance levels exist between communities that have fairly similar socio-economic characteristics (Solomon 1998). Moreover, in some very poor areas some people continue to pay for the services they receive, even when they could get away without doing so.

The Masakhane campaign

To heighten citizens' awareness of issues associated with local government finances and service provision, the Masakhane campaign was launched by the government in February 1995 (Timm *et al.* 1998: 123). The overall aim of the Masakhane campaign, meaning 'let us build together', was to normalise governance and the provision of basic services at the local level.[4] The campaign has a broad set of objectives, including (i) accelerating the delivery of basic services and housing; (ii) stimulating economic development in both urban and rural areas; (iii) promoting the resumption of rent, service charge and bond payments; and (iv) creating conditions for large-scale investments in housing and service infrastructures and local economic development. However, the Masakhane campaign has been seen as a general and narrowly focused programme to 'get people to pay for services', while the importance of delivery has not received adequate attention (*ibid.*: 124).

Although the campaign has had a substantial budget and administrative structure, the general view of a cross-section of people at national and provincial levels is that it has not been successful (Cashdan 2002: 159). On the positive side, it may have contributed to increasing the awareness of issues associated with local government and service provision. But with respect to improving payment of service charges the results are dubious. A general picture is that the Masakhane campaign contributed to increased payments for either a short period only or not at all (Johnson 1999: 65). In some communities non-payment even worsened after the launching of the campaign. For instance, between July 1995 and April 1996 payment levels in Soweto declined from 34% to 23% and in Alexandria from 23% to 13% (*Business Day* 14.07.1996).

Surveys on the determinants of non-compliance

In recent years, several studies have explored the possible reasons behind the limited success of the Masakhane campaign (see Cashdan 2002; Timm *et al.* 1998). Also, some citizen surveys have been carried out to identify the determinants behind the sustained high levels of non-payment of service charges. Two comprehensive national surveys, which explicitly focus on payment of municipal services, have been conducted by the Centre for Development Support, University of the Free State (CDS 2001) and by the Helen Suzman Foundation (Johnson 1999), respectively.[5]

The CDS survey was carried out in 2000, and covered 1,600 households in 32 localities across South Africa. Both rural and urban sites were included. The Johnson survey was conducted in late 1998, and covered 1,754 respondents in various urban councils known to have high levels of non-compliance (795 respondents in Gauteng, 326 in other cities and 633 in smaller towns). In both surveys, the respondents were grouped according to socio-economic characteristics such as type of housing (ownership), language, size of the household and income. The surveys included questions on service delivery, e.g. changes over time for better or for worse, perceptions on the capacity and effectiveness of municipalities in providing services (implicitly the trustworthiness of the local authorities), the role of community leaders, perceptions on the rate level (i.e. ability to pay), perceptions on why (some) people did not pay, perceptions on others' compliance behaviour (i.e. implicitly trust in others), and how to deal with defaulters (i.e. credibility of sanctions).

Combined, the two surveys provide an extensive database on citizens' perceptions and attitudes with respect to service delivery, community development and the non-payment of service charges in local authorities in South Africa. Many of these perceptions are consistently shared by the respondents in both surveys. Interestingly, however, the main conclusions of the surveys on the determinants of the widespread non-compliance observed among ratepayers differ. CDS (2001) concludes that non-payment is primarily an issue of inability to pay. It is argued that the poverty of many households makes them unable rather than unwilling to pay, hence the need for free basic services to the poorer segments of the population and/or a lowering of the rates. Johnson (1999: 101), however, concludes that 'the most central problem clearly lies in the complex of issues surrounding "the entitlement culture" and even the "culture of non-payment"'. But he does not reject the ability-to-pay argument, and emphasises (*ibid.*: 50) that 'no one should doubt that there is severe social and economic distress behind such behaviour' (i.e. non-compliance).

The divergences between the two studies with respect to the key explanatory factors behind the problem of non-payment may, of course, be due to differences in the way the samplings were done (e.g. with respect to localities, language groups or affluent versus poor areas), differences in the ways the surveys were organised, hypotheses and so on. The discrepancy may also be due to different theoretical foundations of the studies, as well as the way the survey data is interpreted.

But one observation, which cuts across the surveys, is that huge variations in compliance exist both within communities and between communities that have quite similar socio-economic characteristics, including levels of income. How to explain such differences? The ability-to-pay argument can only be part of the answer, and it may not be the one with the strongest explanatory power. Moreover, why does the 'culture of non-payment' differ between communities which are very similar in many other respects? The rich dataset in CDS (2001) and Johnson (1999) indicates that the problem of non-payment of service charges is more multifaceted than inability to pay and the existence of an entitlement culture. In particular, I argue, trust relations between state and society and within local communities may be important determinants for citizens' compliance behaviour. However, before I start elaborating my arguments, let me first qualify some of the key findings of the surveys with respect to the 'ability to pay' and the 'entitlement culture' determinants.

Ability to pay

CDS (2001) finds that the relatively better off ratepayers are the most compliant. According to the survey, 'the poverty of many households in low-paying areas makes them unable rather than unwilling to pay'. In particular, inability to pay seems to be more acute in rural than in urban settings. This is not surprising, and is consistent with findings from other African countries (e.g. Fjeldstad & Semboja 2001). Poverty is a major problem in municipalities in South Africa. The issue of free basic services (including water and electricity) has, therefore, also been a major theme in recent election campaigns.

This observation is supported by Johnson (1999: 72): on the question 'why do you believe people are sometimes not paying for their services', the main reasons given were inability to pay due to unemployment (59 % of respondents) and/or low salaries (69 % of respondents). Moreover, almost 70 % of respondents believed that rates were too high (*ibid.*: 56). The claim that charges are too high may, of course, for some be part of a rationale for non-payment. Thus, Johnson (1999: 57) reports that while 60 % of the households in the sample reporting 'no income' said that the rates were too high, as many as 90 % of the most affluent households in the sample also claimed that rates were too high. In general, the better-off respondents were most likely to say that rates were too high. CDS (2001) also finds that in many urban municipalities, many households and individuals who could pay for the services opt for a free ride.

It is, however, reasonable to assume that there exists a correlation between ability to pay and willingness to pay. Moreover, given limited administrative resources, it is likely that rate collectors maximise yields by concentrating on the most accessible and better-off ratepayers. Thus, ability to pay and accessibility become key variables when enforcement priorities are made. Such mechanisms, in addition to factors related to reliable service provision and small opportunities for non-payment, may explain the relatively high compliance rates in communities dominated by whites. Although the white business community has economic power in most local authorities in South Africa, political power rests, in general, with the black majority. Hence, it may be rational for the service providing agencies to focus enforcement efforts on the wealthier but less politically connected white minority.

Entitlement culture

Johnson (1999) refers to the problem of non-payment as the 'culture of entitlement' and dependency. This argument is supported by other studies which claim that political morale at the grassroots in South Africa has been undermined by high expectations of big changes following the ANC election victory not being met (Ruiters 1996: 121). The liberation promises by the ANC, and the fact that township residents themselves directly fought for their own political liberation, weigh heavily in favour of a culture of rights and entitlement (*ibid.*: 125). Thus, it is argued, many people believe that public services (i.e. housing, water, electricity, health etc.) are a basic right (Johnson & Schlemmer 1996). Hence, some observers claim, for instance, that the underlying cause of the electricity crisis in Soweto, is the 'culture of non-payment, not electricity prices that are too high for Soweto consumers …' (*Focus* 2002: 17).

While entitlement culture certainly plays a role in understanding the non-payment crisis, the explanatory power of this factor is more dubious. Actually, many people seem to understand the relationship between service charges and service delivery. In the CDS (2001) survey, 8 out of 10 respondents realised that if the current trend of non-payment for services continued in the future, a collapse in service delivery would become inevitable (*ibid.*: Table 49). This is consistent with Johnson (1999: 72): on the question 'Why do you believe people are sometimes not paying for their services?' only 5% of respondents agreed with the statement that people should not pay for services because they were a basic right. In contrast, the main reason for not paying was said to be inability to pay, reflected by statements that members of the household were unemployed or had low salaries. Secondly, were claims of inefficient or incorrect billing by the service providers, and thirdly, complaints of poor quality of the services.

Both surveys reveal differences between areas and municipalities on this issue. In general, the respondents in Gauteng seem to be more inclined to blame non-payment on poverty (i.e. inability to pay) and on the service providers (i.e. poor quality of services and/or incorrect billing). Moreover, on the statement that 'Government should provide all services free even though that would mean paying higher taxes', 32% of respondents in Gauteng agreed, compared with only 16% of the respondents in other cities (Johnson 1999: 70). This may be explained by the fact that non-payment of service charges in recent years has been more organised in Gauteng compared with other provinces. For instance, the Soweto Electricity Crisis Committee (SECC) has actively battled the primary electricity provider ESKOM, by illegally reconnecting households which have been cut off by the provider due to extensive arrears (Fiil-Flynn 2001).[6]

CAN TRUST AFFECT ECONOMIC BEHAVIOUR?

In the standard economic model of taxpayer behaviour, the perceived quality of government does not influence the level of taxes remitted. The basic behavioural assumption is that people are free riders: no one will voluntarily contribute to the government unless the threat of punishment makes it sensible (Allingham & Sandmo 1972). But an increasing amount of evidence from experimental studies and survey data reveals that the rate of contribution to a public good is affected by factors such as citizens' trust in others and perceptions of the trustworthiness of the government (Slemrod 2003).

As Scholz (1998: 137) points out, without trust there is little basis for social cooperation and voluntary compliance with laws and regulations that could potentially benefit everyone. Thus, without trust, coercion provides a reasonable guide for governance. The temptation not to comply even if others comply defines the free-riding problem that is endemic in collective action situations in private as well as public institutions (Hardin 1982). Why should the ratepayer not take advantage of the opportunity for a free ride? In this perspective, Levi (1998) argues that citizens are likely to trust the government only to the extent that they believe that it will act in their interests, that its procedures are fair and reasonable, and that their trust of the state and others is reciprocated. She stresses that government trustworthiness, plus the perception that others are doing their share, can induce people to become 'contingent consenters' who cooperate even when their short-term interest would make free riding the individual's best option.[7] Accordingly, citizens' willingness to pay service charges voluntarily rests on the existence of the local government's capacity to provide services and its demonstrated readiness to secure the compliance of the otherwise non-compliant. This is the perspective I will apply in this paper.

It should, however, be acknowledged that the conceptual framework needed to study service charges is to some extent different from the standard model of tax evasion referred to above, which typically focuses on the declaration of taxable income when detection is problematic. In contrast, local authorities and service providers can, in principle, observe the fraction of non-payers of service charges. Service users cannot hide their liability except by hiding their existence or migrating to a municipality which provides services free of charge or which imposes the charges at a lower rate. In so far as sanctions are probabilistic it is because the revenue administration's capacity to bill and to effectuate sanctions is questionable. It seems, however, reasonable to suppose that a service user's perception concerning the likelihood of being prosecuted and the severity of penalties will affect his or her choice between paying the charge or not.

WHAT'S TRUST GOT TO DO WITH IT?

In this section I examine factors that may influence citizens' decisions on whether to pay service charges or not in municipalities in South Africa. Following the analytical approach suggested by Levi (1988, 1997), the relationship between a ratepayer and the local government includes at least three elements. First, there is an element of *fiscal exchange*, as payment of service charges and the provision of services may be interpreted as a contractual relationship between ratepayers and the local government. A citizen's decision to pay derives from the perception that the local government is trustworthy. Second, there is an element of *coercion*, as represented by the enforcement activities of rate collectors and the penalties imposed on those detected for non-payment. The credibility or trustworthiness of the revenue administration's sanctions against defaulters is important in this context. A third element is the impact of *social influences* and norms on the ratepayer's compliance behaviour. For example, attitudes toward the government may affect the ratepayer's normative commitment to comply with the laws. Individuals' perceptions, in combination with their opportunities, may thus determine their current choice of whether or not to be a non-payer.

Fiscal exchange

Compliance can be motivated by the presence of government expenditures. Individuals may pay service charges because they value the goods provided by the government, recognising that their payments are necessary both to help finance the goods and services and to make others contribute (Andreoni *et al.* 1998; Cowell & Gordon 1988). Hence, a ratepayer may be seen as exchanging purchasing power in the market in return for government services. Fiscal exchange, however, requires trade-off gains that may be seen as prerequisites of voluntary compliance (Levi 1988: 56). The existence of positive benefits, measured according to quantitative and qualitative criteria, may therefore increase the probability that ratepayers will comply voluntarily, without direct coercion. Most ratepayers are, of course, unable to assess the exact value of what they receive from the government in return for charges paid. However, it can be argued that ratepayers have general impressions and attitudes concerning their own and others' terms of trade with the government. If this is the case, then it is reasonable to assume that ratepayers' behaviour is affected by their satisfaction or lack of satisfaction with their terms of trade with the government. In psychological terms, an unfair rate system could lead people to 'rationalise' cheating. Thus, if the system of user fees is perceived to be unfair, non-payment may, at least partly, be considered as an attempt by citizens to adjust their terms of trade with the government.

The survey data reported in Johnson (1999) and CDS (2001) do not support this proposition. Actually, the majority of the respondents in both surveys said they were satisfied with the delivery of services. In Gauteng, about 80% of the respondents said they were satisfied with water delivery, compared with 70% in smaller towns (Johnson 1999: 27). The corresponding figures for electricity were 79% and 71% (*ibid.*). Since the problem of non-payment is worst in Gauteng, it may seem striking that the same area showed the highest levels of satisfaction with service delivery both for water and electricity. CDS (2001: Table 60) provides corresponding results; more than 80% of the respondents said they were satisfied with the core services delivered to their households, such as electricity, water supply and refuse removal. Respondents in low-paying areas were, however, slightly less satisfied than respondents in high-paying areas.

Nor does the quality of services seem to be a major cause for non-payment. For instance, fewer than 25% of respondents in Johnson (1999: 46, Table 26) reported leaking taps and pipes and broken toilets as problems in the area. Interestingly, given Gauteng's relatively higher incidence of non-payment, significantly fewer respondents there reported such problems compared with respondents in other cities and towns. Moreover, when asked whether they agreed or disagreed with the statement that 'people should not pay for services until they have been improved', only about 30% of respondents agreed (Johnson 1999: 70, Table 49).

However, there seems to be an increasing perception that the quality of services is declining (Johnson 1999). In Gauteng, for instance, as many as 40% of the respondents said that services had deteriorated since the election in 1994/95 (*ibid.*: 25, Table 5). In smaller towns, more than 60% of respondents gave this answer (*ibid.*). If this perception continues and is strengthened, this may have an impact on citizens' future compliance behaviour. An indication of this development is the increasing non-compliance observed among the white, more affluent segments of the population. In interviews, whites complain about deteriorating public services, and also that they consider it unfair to pay when a large majority of others do not pay. For instance, the ratepayers association in Worchester, Western Cape, has organised actions involving non-compliance. Their main arguments are that it is not 'fair' that the white community should bear the whole tax burden, and that services are deteriorating. These actions are considered to be legitimate within the white community.[8]

But, at present, the survey data does not provide clear correlations between fiscal exchange and compliance with respect to service charges. This observation is supported by other studies. For instance, Hlope & Friedman (2002: 68) argue that South Africa today provides little support for theories linking compliance with public obligations to a 'social contract', in which the government earns its legitimacy by demonstrating a capacity to meet citizens' instrumental needs. They argue that, as in most other African countries, a liberation movement turned into a ruling party like the ANC largely earns its legitimacy and trustworthiness because it is a liberator responsible for the sense of freedom among the previously dominated. Thus, what the ruling party did in the liberation period counts more than its performance in government.

Coercion

Trust and coercion are closely linked in the new perspective on compliance and governance (Scholz 1998: 163). The government is sometimes crucial in establishing levels of trust among citizens that make possible a whole range of social, political and economic transactions that would otherwise not be possible (Levi 2002: 20). Critical to this task is its use of coercion to ensure that non-compliers are punished. As argued by Scholz, no law can reshape behaviour without the backing of an effective enforcement agency. On the other hand, an effective enforcement agency does not deter each citizen from breaking the law, but instead tries to provide a basis for trust by ensuring that non-compliers will be made to obey the law.

At the same time, agencies concerned with trust would minimise the use of ruthless enforcement techniques on trustworthy citizens, and ensure that enforcement procedures are perceived by the broader public as reasonable, fair and in accordance with accepted standards of the society. Therefore, in the long run, trust-enhancing enforcement cannot be separated from legal processes and contents of the law, since trust-based compliance is dependent on long-term social gains that make up for compliance costs (Scholz 1998: 163). With reference to service charges, this implies that factors expected to affect payment are the knowledge that basically all other people have to pay, that fair and reasonable enforcement mechanisms ensure that there is no way of avoiding payment, and that failure to pay will be punished with fines or eventually the cut-off of services.

The survey data support to some extent the proposition that the credibility of the enforcement mechanisms and the penalties imposed on defaulters affect citizens' compliance behaviour. Johnson (1999: 60, Table 30) found that in Gauteng only 27 % of the respondents believed that people who did not pay were worried about getting into trouble for not paying. The corresponding figure for other urban areas in the sample was about 50 %. In addition to differences between geographical areas, the study also found differences between income and language groups. When comparing the responses of different income groups, a smaller share of the highest income group (47 %) compared to the lowest income group (57 %) said that people would get worried (*ibid.*). Why? One possible explanation might be that the relatively more affluent households are more cynical about compliance. Moreover, a larger share of Xhosa-speakers (66 %) said they believed non-payers were worried, compared to less than 40 % of respondents from other language groups (*ibid.*: 61, Table 37). The difference between Xhosa and others might be because Xhosa-speakers generally are more loyal to the government's policies on service delivery.[9]

Most respondents did not consider the sanctions against those in arrears of payment to be credible. This might be due to the widespread practices of illegal connections to water and electricity supplies in many black and coloured areas.[10] In particular, the water account seems to be the easiest to cheat on, partly because water authorities are unlikely to turn off the water completely (Johnson 1999: 82). Informal reconnections are practised in many townships when water and/or electricity are cut off by the municipality due to massive non-payment. For instance, when the electricty in the township of Katlehong in the East Rand was cut off in April 1997, the council discovered that about 80 % of all households still had electricity (*ibid.*: 15). According to some reports, syndicates in the East Rand carried out illegal reconnections for a flat payment of 50 Rand. This was clearly a bargain for any household. Even if the reconnection was discovered, one was likely to get the benefit of far more than ZAR 50 worth of electricity in that time. With respect to water supply, a recent study in Cape Town found an illegal reconnection rate of 60% after cutoffs were implemented by the Tygerberg Municipality (McDonald & Smith 2002).

Furthermore, the survey data indicate that ratepayers not only take into consideration the incentive structure of rate payment, including the credibility of sanctions against defaulters, but also the way enforcement is carried out in practice. Accordingly, the trustworthiness of the local government seems to be a function of whether government agents trust or distrust those whom they are demanding cooperation and compliance from. The hostility of lower-level bureaucrats in the revenue administration seems to be particularly counterproductive.[11] Oppressive enforcement of service charges and harassment of ratepayers by collectors may thus induce non-payment which in turn may be interpreted as a strategy of public resistance and opposition against the authorities.

While rarely used prior to 1994, service cut-offs have become a major enforcement mechanism and have been implemented by municipalities throughout South Africa (McDonald 2002b: 169–70). For instance, in 1997 and 1998 many of the municipalities of Greater Johannesburg took tough action against non-payers (Johnson 1999). These measures included not only disconnection, but actually tearing electricity cables out of the ground to prevent illegal reconnections. Moreover, legal actions were instituted and property and buildings were seized from non-payers in an attempt to recover some of the payment arrears. This approach had some effect: by May 1998, ZAR 117 million had been recovered (*ibid.*: 14). But although this draconian campaign achieved the objective of raising revenues in the short run, it also encountered large-scale resistance.[12]

From the standard economic theory on compliance, it would be expected that the more severe the sanctions perceived by ratepayers, the higher the compliance (Allingham & Sandmo 1972). Experiences from local authorities in South Africa point in the opposite direction: the more severe the sanctions observed, the more widespread the resistance to pay. The reason for this 'perverse' relationship may be due to reciprocity considerations.[13] The reciprocity argument leads to the proposition that the authorities' unresponsive, disrespectful and unfair treatment of ratepayers fosters disrespect for and resistance against local authorities and the service providing agencies – a kind of reciprocation in kind.

The strength of the possible reciprocity effects on compliance behaviour probably depends on the ratepayers' experiences with the local authorities and service providers (e.g. ESKOM). Those who have been disconnected may have resentment against the authorities and develop a generalised normative response.[14] Those who have not had such experience with the authorities may rely on the experiences of others, and on their more general perceptions of the service charging system, and of how government officials treat citizens. Since these perceptions typically are less specific than personal experiences, their effects on compliance are likely to be primarily indirect through generalised normative commitments.

Resistance to pay also sometimes takes more violent forms. In Soweto, there have been clashes between ESKOM officials and members of the Soweto Electricity Crisis Committee (SECC). On at least one occasion shots were fired, and ESKOM officials were reported wounded (*Focus* 2002: 14). In 1997, four people were killed in rates riots in Eldorado Park, Johannesburg's largest coloured township (Cashdan 2002: 161). In Kwa Thema, east of Johannesburg, three councillors' homes were burned down, and in Tembisa, residents destroyed thousands of pre-payment electricity meters (*ibid.*). Moreover, in 1998 in Tsakane on the East Rand, 30,000 non-payers stoned the police to prevent the seizure of their goods.

If the proposition on reciprocity is correct, it may contribute to explain the widespread non-compliance observed in some townships. Oppressive enforcement of service charges, including cut-offs and harassment by revenue collectors, may induce non-compliance which in turn may be interpreted as a strategy of public resistance and opposition against the authorities. Fierce enforcement is considered to be a problem in many townships, not least by politicians. During election campaigns local government politicians usually deliver the message that rate collectors should relax on enforcement and not harass citizens. Hence, as the 1999 election approached, it was noticeable that such hard-line attempts to achieve payment ceased. According to Johnson (1999: 14) this was because ANC mayors and councillors were under instruction 'not to ruffle the electorate too much'.

Social influences

The importance of social interactions in forming tastes and actions has long been stressed by sociologists and social psychologists (Hessing *et al.* 1988). It is reasonable to assume that human behaviour in the area of whether to pay service charges or not is influenced by social interactions, in much the same way as other forms of behaviour. Compliance behaviour and attitudes towards the service charge system may thus be affected by the behaviour of an individual's reference group, such as relatives, neighbours, friends and political associates. Consequently, we may reasonably argue that if ratepayers know many people in groups important to them who do not pay service charges, their commitment to comply will be weaker.[15] On the other hand, social relationships may also help deter non-payment. Individuals can be dissuaded from engaging in evasion out of fear of the social sanctions incurred should their action be discovered and revealed publicly (Grasmick & Green 1980; Grasmick & Scott 1982). Theoretical research on herd behaviour in economic situations (Banerjee 1992; Sah 1991) also indicates that social influences may affect compliance, in particular by affecting the perceived probability of detection and punishment. Hence, evidence suggests that perceptions about the honesty of others may play an important role in compliance behaviour.

Furthermore, evidence from behavioural science suggests that greater individual participation in the decision process will foster an increased level of compliance (Lewis *et al.* 1995; Hessing *et al.* 1988). This is partly because participation implies some commitment to the institution, and such commitment in turn requires behaviour that is consistent in words and actions. Thus, we may expect that compliance is higher when ratepayers feel that they have a voice in the way their service charges will be spent, for instance, whether a share of the charges paid is retained in the local community. Another potential criterion is the level of popular support for the government: a government's lack of legitimacy almost by definition diminishes the moral justification for obeying its laws. In contrast, widespread support tends to legitimise the public sector, and may thus impose some social norm to pay rates.

The survey data supports the proposition that social influences affect compliance. Three mechanisms seem to be important in this respect: first, little stigma appears to be attached to non-payment in black and coloured communities. To the contrary, non-payment seems to be the 'norm' in some areas. Hence, the majority of the respondents in Gauteng believed that people who could not pay their rates and other service charges would *not* feel uncomfortable about admitting this to their neighbours (Johnson 1999: 54). Moreover, only one third of the respondents in any of the major metropolitan areas believed that most of their neighbours were payers, a figure that rose to 44% in smaller towns (*ibid.*: 85).

Secondly, less than half of the respondents in Gauteng believed that their political leaders really cared about whether people paid their rent and service charges, and an equal number believed they did not care (*ibid.*: 50). Actually, some respondents believed that their leaders sympathised with those who did not pay (*ibid.*: 51). Over 90% of respondents in Gauteng believed that at least some of their councillors were unlikely to pay rates, and two-thirds of them believed that this was true of a substantial number. In contrast, 57% of respondents in other cities believed that none of their councillors were likely to be non-payers. The corresponding figure for towns was 36% (Johnson 1999: 52).

Thirdly, 76% of respondents in Gauteng said they could not trust the people around them, compared to 58% in smaller towns and 44% in the other big cities. With respect to income, Johnson (1999: 44) found only minor differences between income groups, except for the very richest group which had a markedly more rosy view of community support than others. A high incidence of non-payment may thus encourage non-payment even by those who can afford to pay.

The interaction between social networks and overlapping collective activities may indeed in some instances, as in Soweto with respect to electricity charges, provide a framework in which it is difficult to comply (i.e. to pay the charges) without provoking punishment from neighbours and other members of the community networks. In other cases, the situation may be reversed where the interaction between peer networks and collective activities provides a framework in which it is difficult to free ride due to community norms. Lieberman (2001), for instance, argues that the 'culture of payment' implanted in whites during apartheid still survives, though most likely in a diluted form. He argues that in spite of the fact that many white South Africans are assumed to harbour deep reservations about majority rule, which might lead to reluctance to pay taxes (and service charges), they are expected to act in one way if they are guided by present sentiment, and quite another if they follow customs and past practice of their community. The same argument applies to their black counterparts, but with the opposite impact on compliance.

HOW TO PRODUCE TRUST IN SOCIETY AND IMPROVE COMPLIANCE?

While acknowledging the weaknesses of an essentially exploratory study, I have argued in this paper that two dimensions of trust seem to affect citizens' compliance behaviour with respect to payment of service charges in local authorities in South Africa. First, the survey data analysed support the proposition that the trustworthiness of the revenue enforcement mechanisms and the penalties imposed on defaulters affect citizens' compliance behaviour. However, in a number of cases the way the law is enforced and the severity of sanctions appear to have contributed to undermine trust in local authorities and fuelled resistance. This contradicts the standard economic theory, which tells us that the more severe the sanctions perceived by ratepayers, the higher the compliance expected.

Observations from South Africa point in the opposite direction: the more severe the sanctions, the more widespread and organised resistance to paying rates and charges. The reason for this 'perverse' relationship may be due to reciprocity considerations. The oppressive and uncompromising behaviour of service providers (e.g. ESKOM) may actually have fostered resistance to pay and disrespect for the laws. Non-payment may, therefore, to some extent be interpreted as a strategy of public resistance and opposition against the authorities.

Secondly, trust in other citizens to pay their share seems to be important. The data support the proposition that social influences affect compliance. In particular, knowledge of the compliance behaviour of others seems to influence the perceived probability of being detected for non-payment. The larger the fraction of the local population that is observed not paying, the lower the perceived risk of being prosecuted. This has impacts on the individual ratepayer's perception of the credibility and trustworthiness of the revenue administration. Moreover, the attitude of local political leaders with respect to payment seems to be important, for instance by legitimising non-payment through their own behaviour. Furthermore, the interaction between social networks and overlapping collective activities may in some instances, such as in Soweto with respect to electricity charges, provide a framework in which it is difficult for individuals to pay their charges without provoking reactions from their non-paying neighbours and other members of the community.

The data analysed do not provide clear linkages between payment and service delivery, i.e. the fiscal exchange proposition. However, there seems to be a perception among respondents that the quality of services has deteriorated in recent years. If this perception persists and is fortified, this may have an impact on future willingness to pay, and lead to a further erosion of people's trust in the government's capacity to provide expected services.

The relevance of the fiscal exchange argument to explain compliance behaviour is, however, questioned by Hlope & Friedman (2002). They argue that for the majority of the population the South African government today earns its legitimacy because it is perceived as a liberator, and not by demonstrating a capacity to meet citizens' instrumental needs. This argument may first and foremost apply to the national government, and less to lower levels of government. For instance, a survey carried out by the Institute for Democracy in South Africa (IDASA), found that local government was considered the sphere of government least receptive to citizens' needs (Taylor & Mattes 1998). Moreover, across a range of performance indicators – responsiveness, performance, corruption and trust – local governments in South Africa fared consistently worse than higher levels of government. Harrison (2002: 223) reports that in a series of surveys conducted in Gauteng, a minority of the respondents (less than 40%) believed that local government was interested in them. Furthermore, little trust was found within the communities. More than 70% of the respondents felt that most people were basically dishonest.

The low level of trust in many local communities may, as argued by Offe (1999: 54–5), lead to a vicious circle:

> Those lacking resources (power, wealth, information) cannot afford to trust, as misplaced trust is feared to have disastrous consequences from which actors are incapable of protecting themselves through other means. So they have to spend the severely limited resources they actually have in highly trust-saving and inefficient ways – with the consequence of perpetuating their poverty. The apparent paradox is that those who are most in need of trust-based relations (because they have little else to rely upon) cannot afford the risk involved, while those who need it least enjoy it most.

How can local governments move from a low trust situation characterised by extensive non-payment and oppressive revenue enforcement, to a high trust situation where these problems, while existing, are much less severe? As argued by Williams *et al.* (1995: 18), institutions can be changed almost at will, but political memories are long and hence belief systems relatively entrenched. The majority of South Africans have very good reasons to be distrustful of their local government institutions. This is, by and large, an effect of the local authorities' historical record of being untrustworthy. It may therefore not be the present formal local government institutions as such but the perceived history of how these institutions have acted that matters. Hence, as North (1998: 506) points out, while formal institutions can help to create trust, 'it is the informal constraints embodied in norms of behaviour, conventions and internally imposed codes of conduct that are critical'. Apparently, without strong ethical norms against self-interested behaviour, the 'rule of law' cannot work as a trust-enhancing institution (Rothstein 2000: 483).

From this perspective, a major challenge is to address the existence of a destructive mistrust within municipalities in South Africa. Conflicts between various groups in the local communities suggest that intimate knowledge of others does not always produce either trust or cooperation, but can actually generate just the opposite. This observation suggests that government policies which reduce personal interdependencies on friends, family and neighbours, and facilitate exchange among strangers, may actually increase trust in local communities under certain conditions (see Levi 2002: 15). Thus, by increasing social rights and protection of the poorest segments of the population, the state can play an important role in eliminating risky personal reliance on others. Moreover, local governments, by constraining their enforcement mechanisms, demonstrating fiscal rectitude, and improving the equity of the service delivery system, may gain legitimacy and also enhance social trust among the population. The national government's policy of making service delivery its priority seems to reflect this approach. The two pillars of this policy (RSA 2001: 131) are to enable local governments to make basic municipal services accessible to all citizens, and provide free basic services for poor citizens who cannot pay.

The policy documents stress that the challenge is foremost to ensure that poor households are the primary beneficiaries of the free services policy and associated resources. Since July 2001, every municipality in South Africa is supposed to provide minimum free 'lifeline' supply to households of 6,000 litres of water and 50 kWh of electricity per month (Pape 2002: 184).[16] However, in addition to the financial constraints, the risky dimension of this policy is due to the fact that affirmative action programmes and special dispensations may inflame those who do not receive the benefits (e.g. free services), and who consequently believe that the government is acting unfairly towards them. In particular, this approach may upset segments of the white population who consider the black and coloured to be free riding on their compliance.

To improve service delivery it is of crucial importance to address the broader problem of free riding (CDS 2001). Many people seem to be in a position to pay, but opt for non-compliance. This observation is also supported by survey data. According to Johnson (1999: 73, Table 51), the majority of the respondents (85–94 %) believed that 'if everyone else started paying' this was the measure that would have most effect on altering non-payment. However, as discussed above, the mechanisms for enforcing compliance are not indifferent for the outcome. For instance, the fierce and uncompromising way ESKOM has approached non-payers in some townships may actually have contributed to increasing resistance by ratepayers. Hence, measures to improve the efficiency and effectiveness of the revenue administration are crucial (van Ryneveld *et al.* 2003). Relevant measures include improvements to the billing and accounting systems, establishing more accessible and efficient payment facilities, and strengthening the capacity to follow up cases of non-payment through fair and reasonable enforcement.

To summarise, a trust enhancing approach to improving payment of service charges might be based on the proposition that citizens are likely to perceive the local government as reciprocating their trust when they feel they are being treated with respect. Furthermore, as Rothstein (2000: 496) points out, it is necessary for the stakeholders to have accurate information about 'the others', i.e. whether they will betray trust or whether they will be trustworthy. The problems of non-payment should therefore be attacked on several fronts, including service delivery, better administration and payment schemes, and community involvement. To achieve this, in-depth knowledge and data are required on payment levels for each ward, the proportion of municipal accounts delivered, the number and type of complaints received, living conditions for the poorest segments of the population, including the elderly and unemployed, etc. Moreover, customer care must show that complaining will bring results. Citizens should therefore be encouraged to report faults such as leaking taps or streetlights not functioning. The prompt redress of such complaints may help convince people that the municipality means business. Furthermore, citizens' involvement in identifying problems and setting priorities may motivate a greater sense of community involvement. Initially, it might be advisable to link payment directly to visible improvements in services. Finally, cooperation between local government officials, councillors and community leaders in setting common goals might be a crucial trust-enhancing device.

NOTES

1. 'African' and 'coloured' areas refer here to the historically defined residential areas set aside by the previous apartheid regime. These distinctions no longer exist as legal entities, nor are they uncontested and readily defined geographical areas for specific groups of the population. However, much of the literature and the political debate still applies these distinctions.

2. In December 2000, the existing 843 councils were rationalised into 284 municipalities (RSA 2003: 27). Reliable and comparable financial data is difficult to come by. For instance, it is difficult to compare financial information for the pre-demarcation councils with that for the 284 new ones. Furthermore, in many councils the budgeting and accounting systems are outdated and inconsistent. Financial management, including billing, is also weak in many municipalities (RSA 2001: 143).

3. *RSC levies* are collected from business and comprise two components: one is based on company turnover and makes up two-thirds of the total levy. The second is based on the annual value of the company's payroll. According to government regulations, the RSC levies should be used to fund capital infrastructure. The levy is based on self-assessment by businesses, and paid monthly to district municipalities and metros. *Other revenues* include interest on investments, no-trading services, fees and charges (e.g. recreation and burial fees), and fines.

4. The campaign has, however, been run at all three levels of government: national, provincial and local.

5. To my knowledge, the only other national survey of this nature was conducted in 2001 by the Municipal Services Project (www.quensu.ca/msp) in collaboration with South Africa's Human Sciences Research Council (www.hsrc.ac.za). The findings and conclusions of this survey, reported in McDonald (2002b), are congruent with the CDS (2001) survey.

6. More recently, residents of Soweto have developed an informal network of people called *Operation Khanyisa* ('to light') that will reconnect consumers to the electricity grid illegally. This open challenge by Sowetan residents has led ESKOM to threaten to press charges (see *The Star* 4.6.2001). ESKOM is an abbreviation for the parastatal company the Electricity Supply Commission.

7. The analytical distinction between trust and trustworthiness is clarified in Levi (1998: 80): 'Only persons can trust or be trusting, but trustworthiness can attach to either individuals or institutions.' She writes that institutional trustworthiness implies procedures for selecting and constraining the agents of institutions so that they are competent, credible, and likely to act in the interests of those being asked to trust the institution.

8. Personal interviews with representatives from the business community in Worchester, Western Cape (November 2000).

9. In an analysis of data from a national survey of adult South Africans, Lieberman (2002) found that citizens' evaluations of their obligations to the state, including tax compliance, were largely conditioned by feelings of closeness or affinity towards other groups included in the state's definition of the national political community.

10. See Fiil-Flynn (2001) and McDonald & Smith (2002) for more detailed accounts of re-connections after service cutoffs.

11. For example, Hardin (1996) argues that the professionalism and morality of public office holders can be an important source of political trustworthiness. Hence, to the extent that citizens and groups recognise that bureaucrats gain reputational benefits from competence and honesty, we may expect that those regulated will expect bureaucrats to be trustworthy and will act accordingly (Levi 1998). Therefore, it might be expected that a competent and relatively honest bureaucracy not only reduces the incentives for corruption and inefficient rent-seeking, but also increases the probability of cooperation and compliance.

12. According to McDonald & Smith (2002), close to 100,000 households in Cape Town had their water cut off for non-payment between 1996 and 2001. Fiil-Flynn (2001) reports that in Soweto up to 20,000 homes a month had their electricity cut off by ESKOM in early 2001.

13. Sugden (1984) refers to the response of reciprocating behaviour as a 'cross-societal norm of reciprocity: a norm both in the sense of a universal regularity and a moral responsibility'. The reciprocity norm evokes an obligation for individuals to make a concession to someone who has made a concession to them. Hessing *et al.* (1992) provide insights on the effects of deterrence on tax compliance based on experimental studies.

14. According to a South African Broadcasting Corporation (SABC) Special Assignment documentary in 2001, accumulated total disconnections in Soweto were 58,000. Moreover, a citizens' survey carried out in Soweto in August 2001 by the Municipal Services Project at the University of the Witswatersrand, found that more than 60 % of the households interviewed had experienced cut offs by ESKOM during the past 12 months (Fiil-Flynn 2001). Of the households experiencing cut offs, 45 % were without electricity for more than a month and 10 % had their electricity cables removed permanently by ESKOM (*ibid.*).

15. One of the most consistent findings in survey research in Western countries about taxpayer attitudes and behaviour is that those who report compliance believe that their peers and friends (and taxpayers in general) comply, whereas those who report cheating believe that others cheat (see Yankelovich *et al.* 1984). Furthermore, it has been found that interpersonal networks act to reduce an individual's fear of governmental sanctions (Mason 1987).

16. Some observers have raised concerns with the manner in which this 'lifeline' policy has been designed and implemented. First, it is argued that the quantity of the free services provided is too small (Pape 2002: 184). Secondly, since households are not means-tested to see if they qualify for the free services, some middle and upper-income households benefit more from the provision than poor households (McDonald 2002a: 28). Finally, there is the problem of delivering free services across the country, particularly in rural areas (McDonald 2002a: 28–9). Van Ryneveld *et al.* (2003) provide an informative discussion on the shortcomings of the current approach, and provide concrete recommendations on how to improve the system to ensure that the basic needs of the poor are met and their rights upheld.

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Taxation, coercion and donors: local government tax enforcement in Tanzania

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ABSTRACT

This paper presents three propositions about tax collection by local authorities in Tanzania. First, revenue performance depends on the degree of coercion involved in tax enforcement. Reciprocity does not seem to be an inherent component of the state–society relationship in connection with local government taxation. Second, the extent of coercion depends on the bargaining powers of the stakeholders involved in the tax enforcement process. In particular, coercive tax enforcement is facilitated when the 'bargaining powers' with respect to tax collection favour the council administration, and the elected councillors have no direct influence on collection. Third, the presence of donors in a local authority may be crucial by changing the 'balance of power' in favour of the council administration, with implications for accountability, responsiveness and democratic development. These results may explain why widespread differences in revenue performance between local authorities are observed.

INTRODUCTION

In recent years there has been an increasing focus on the possible linkages between high levels of development aid and taxation in Africa. Without aid, governments would have to cut spending, raise taxes or borrow from other sources. Thus, it is argued, high levels of aid may diminish a government's incentive to make full use of its domestic resources for revenue generation (Brautigam & Botchwey 1999; Moore 1998).[1]

Some development agencies have responded to the critique levelled against them by introducing various incentive schemes to reduce the

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assumed free riding problems by recipient governments, and thereby increasing domestic tax effort. Thus, in many aid dependent African countries, revenue targets have become a major component of aid conditionality.[2] For instance, the International Monetary Fund argues that African countries 'have significant potential for raising tax receipts by broadening the tax base, improving tax administration, and rationalising the tax system' (Hadjimichael *et al.* 1995: 44). Furthermore, some donors involved in district development programmes have adopted matching schemes, under which aid is supplied only on the basis of matching funds from the local government (Catterson & Lindahl 1998).

The rationale behind this policy is based on the perception that the current tax effort in most African countries is low.[3] Some observers, however, question the premise behind this policy. Collier (1997: 56), for instance, claims that tax levels in Africa are already high. He argues that high taxation retards the growth process and induces tax evasion. Thus, the build-up of the taxable base of the economy is delayed, and so is the time at which fiscal sustainability can be achieved. Accordingly, increasing tax effort would be 'both ludicrous and self-defeating' (*ibid.*: 54).

Recently, Moore (1998) has introduced a new element into the debate on taxation and aid. Moore focuses on the anti-democratic effects of aid dependency. He argues that the means used by donors to promote development in the poorest countries undermine the values of democracy and good governance that they are otherwise trying to promote through 'general' political conditionality and specific aid interventions.[4] Moore's point of departure is the acknowledgement that bargaining over the budget and over tax policy is one of the primary ways in which different state and societal goals are reconciled in a democracy. For instance, in Europe over the past two centuries, taxation and disputes over the use of revenues stimulated the development of greater citizen rights and privileges, with democratic institutions enforcing accountability and greater transparency in expenditures (Tilly 1992).

Moore's key proposition is that the more a state 'earns' its income through the operation of a bureaucratic apparatus for tax collection, the more it needs to enter into reciprocal arrangements with citizens about provision of services and representation in exchange for tax contributions.[5] Thus, the greater the share 'earned' incomes represent of total revenues, the more likely it is that state–society relations will be characterised by accountability, responsiveness and democracy. In many cases, however, aid dependency may thwart these processes in Africa. African states have significant 'unearned' incomes in the form of foreign aid (Goldsmith 2000: 18). Aid alone now accounts for almost half the income of many governments of low-income countries. Therefore, many African governments seem currently to face more organised and effective pressures for accountability and transparency from the international donor agencies than from their own citizens and parliaments (Brautigam & Botchwey 1999).

The purpose of this paper is to explore the possible linkages between taxation and accountability in a poor aid dependent country. In particular, does the social contract argument that Moore uses appropriately specify the political and administrative problems of a poor country? Furthermore, who are the likely stakeholders involved in the domestic tax enforcement process, and how does the presence of donors influence their relative bargaining power? What impact does their presence have on domestic revenue generation? Local authorities interact more closely with the citizens than other organs of the state apparatus, and hence provide a good case for exploring these questions at a disaggregated level.

The paper draws on findings from research carried out in local authorities in Tanzania during the late 1990s.[6] The field studies were conducted in Kibaha District Council, Coastal Region, and Kilosa DC, Morogoro Region. The studies covered all three council levels: the district headquarters, the wards and the village levels. Information was collected from a variety of sources, including staff members of the council administrations, local politicians and taxpayers. These studies aimed at providing primary data and analyses of the capacities and constraints of the local government administrations, especially in relation to revenue collection, incentive problems and service delivery. In addition, data on tax revenues for about fifty councils were collected from the Ministry of Regional Administration and Local Government.

The remaining part of the article is divided into five sections. In the first section the empirical background for the analysis is briefly presented. The second section explores why different levels of revenue raising effort may be observed in local authorities which have very similar socioeconomic characteristics. The institutional set-up for tax collection is examined in the third section, emphasising the roles of tax collectors and elected councillors in the tax enforcement process. Thereafter, a fourth section discusses possible impacts of donors. Finally, section five concludes.

THE CASES

Four main revenue sources are available to almost all district councils in Tanzania. These are 'development levy' (a head tax), crop and livestock cess (agricultural cess), business licences and market fees. In 1997 these sources averaged two-thirds (66 per cent) of the reported tax revenues in a sample of 42 district councils studied. Development levy dominated (30 per cent of total own revenues), followed by agricultural cess (22 per cent), business licences (about 9 per cent) and market fees (5 per cent).[7]

Total tax revenues per capita reveal substantial differences between councils. In 1995, in a sample of twenty councils, reported revenues per person above the age of 18 ranged from TSh 344 in Lindi DC, to TSh 1,541 in Mbinga DC. Some of these differences may be explained by different economic structures, revenue bases, population densities, incomes per capita, and the level and quality of public services. However, we also observe variations in revenue performance between councils that apparently have fairly similar socioeconomic characteristics, such as Kibaha DC and Kilosa DC.[8] How do we explain these observations?

The experiences with the head tax will be used as a frame of reference. Development levy is, as noted above, the single most important local government tax base in Tanzania. The levy is, in principle, levied on every person above the age of 18 years and ordinarily a resident in the area. Women are exempted in many councils. In district councils the tax is in general levied on a flat basis. In contrast to most other local tax bases that are based on agricultural outputs and, thus, may fluctuate according to annual rainfall (e.g., market fees and crop cesses), development levy is in principle a fairly stable revenue base. Therefore, it is an attractive tax base for local authorities.

The ratio between development levy revenues reported to the district treasury and projected revenues (based on population statistics) differs significantly between the two councils. For instance, in 1996 the collection ratio, referring to the percentage of the estimated tax potential collected, was 26·7 per cent in Kibaha DC, compared to 45·6 per cent in Kilosa. Thus, although the statutory tax rate per head was the same in the two councils in 1996 (TSh 1,000), the effective rate, measured as revenues per eligible taxpayer, was more than 60 per cent higher in Kilosa than in Kibaha (Table 1).

TABLE 1

Effective development levy rate (in TSh per eligible taxpayer)

Council	1994	1995	1996
Kibaha DC	120	137	267
Kilosa DC	321	288	456

Source: Computed from data collected from the District Revenue Offices in Kibaha DC and Kilosa DC.

COERCION

How do we explain the different tax collection ratios between the councils? I suggest the following proposition:

Proposition 1: Differences in revenue performance between local authorities are due to variations in the degree of coercion involved in tax enforcement.

Coercive methods yield higher taxes per capita, but the need for coercion reflects higher levels of distrust in the governmental system and dissatisfaction with service delivery. The evidence supporting this proposition emphasises the importance of different tax enforcement regimes, and, thus, the relationship between the state apparatus and the citizens. Analytically, the relationship between a taxpayer and the (local) government contains at least two elements (Cowell 1990; Levi 1988):

- *The coercive element*: This refers to the bureaucratic apparatus that the local authority deploys to collect revenues. It is represented by the enforcement activities of collectors and the penalties imposed on those detected for non-compliance, i.e. the organisational effort.
- *The element of fiscal exchange*: This has to do with reciprocity, i.e. how far citizens are obtaining some reciprocal services in return for their tax contributions. Thus, taxation and the provision of public goods and services may be interpreted as a contractual relationship between taxpayers and the (local) government.

It should be noted that there is always a coercive element in taxation (Andreoni *et al.* 1998). However, to minimise the costs of enforcement and to maximise the output that can be taxed, the government has to create some kind of voluntary compliance.[9] First, the government must create confidence in its ability and its capacity to deliver promised returns for taxes. Second, to reduce the problems of free-riding, it must

TABLE 2

Perceptions on the quality of public services (in percentage of total number (N) of respondents)

Perception	Kibaha (N = 128)	Kilosa (N = 44)
Good	6	0
Average	26	25
Bad	66	75
Don't know	2	0

Source: Fjeldstad & Semboja (1998).

coordinate the actions of taxpayers so that each perceives that others are paying their share (Levi 1988: 53).

Most taxpayers are of course unable to assess the exact value of what they receive in return from the government for taxes paid. However, it can be argued that the taxpayer has general impressions and attitudes concerning his own and others' terms of trade with the government (Levi 1988). If this is the case, then it is reasonable to assume that a taxpayer's behaviour is affected by his satisfaction or lack of satisfaction with his terms of trade with the government. Thus, if the system of taxes is perceived to be unjust, tax resistance may, at least partly, be considered as an attempt by the taxpayer to adjust his terms of trade with the government.[10]

Taxpayers in local authorities in Tanzania see few tangible benefits in return for the taxes they pay. Virtually no development activities are undertaken through councils' financial sponsorship, and even the existing capacities do not produce the expected services, due to lack of operation and maintenance funds (Semboja & Therkildsen 1992, 1995). The deterioration and in some cases non-existence of public services raises taxpayers' perceptions of exploitation from an unequal contract with government, and promotes tax resistance.[11]

Taxpayers' perceptions of the quality of public services in Kilosa and Kibaha are presented in Table 2. Dissatisfaction seems to be most widespread in Kilosa, where 75 per cent of the respondents considered the quality to be bad (compared with 66 per cent in Kibaha). None of the respondents in Kilosa considered the public services to be good (6 per cent in Kibaha); 77 per cent of the respondents in Kilosa said that the quality of the services today was worse than three years ago (the corresponding figure for Kibaha was 66 per cent).[12] Furthermore, 83 per cent of the respondents in Kibaha DC answered that in their view taxes were 'only partly' or 'not at all' used to provide public services. The corresponding figure for Kilosa was 88 per cent (of whom 70 per cent answered 'not at all'). Taxpayers' perceptions were supported by the tax collectors interviewed.

Widespread tax resistance is observed in the study areas. People may take to the extreme to evade taxes, for instance, by literally hiding in the bush when tax collectors are approaching. In particular, the revenue administration in Kilosa DC relies heavily on simple physical coercion to obtain the resources they need from their subjects and to ensure compliance. Roadblocks, manned by the local militia or police, are frequently used as tools of tax enforcement. Taxpayers reciprocate sometimes in the form of violent 'counter-attacks' on collectors, burning tax offices, etc. In 1996, for instance, the ward office in Chanzuru was destroyed during the night, and the Tax Register Books were burnt. Tax collectors avoid certain villages in Kilosa due to the high personal risk involved in tax collection. Other villages are only visited by collectors accompanied by the local militia.[13] In contrast, tax collection in Kibaha is characterised by greater laxity.

The argument that tax resistance is correlated with deteriorating public services is supported by other studies. Bukurura (1991: 91) refers to an investigation from 1987 by the *Tanzania News Agency* in Kigoma Town Council, which reported that 'many people were defaulting apparently because they thought the council was not doing its best to serve the residents'. Tripp (1997: 154) describes non-payment of development levy as a form of popular opposition towards state policies. She argues (p. 8) that tax evasion may be understood as one of many 'quiet strategies of resistance in the form of economic non-compliance'.

Thus, in circumstances where taxes are perceived to be unfair and people receive few tangible benefits in return for taxes paid, we may expect that only coercive methods of tax enforcement will generate tax revenues. The reciprocity or contractual relationship between taxpayers and the local government seems to be absent. Moreover, harsh tax enforcement combined with poor service delivery contribute to undermine the legitimacy of the local government and increase tax resistance.

THE INSTITUTIONAL SET-UP FOR TAX COLLECTION

Why do the tax enforcement regimes differ between the two councils, leading to substantial differences in the use of coercion? I put forward the following proposition:

Proposition 2: Coercive tax enforcement is facilitated when the 'bargaining powers' with respect to tax collection are in favour of the council administration, and the elected councillors have no direct influence on collection.

The arguments and observations supporting this proposition focus on the stakeholders involved in tax collection, and their relative bargaining power. Local government tax collection is basically a council staff affair, and completely separate from the central government revenue authority (i.e. the Tanzania Revenue Authority). In district councils it is organised at three levels, namely the council headquarters, the ward and the village.[14]

At the district headquarters the responsibility rests with the council treasury, headed by the district treasurer (DT). At the ward level the responsibility for tax collection rests with the office of the ward executive officer (WEO), who also handles developmental and law and order functions at that level. For this purpose the local militia is at their disposal. In larger wards which may possess greater revenue potential, there will also be a ward revenue collector (WRC) to spearhead revenue collection in the ward. At the village level, the responsibility rests with the office of the village executive officer (VEO), who is also responsible for village developmental issues. Village executive officers are nominated to their position by the village councils, but appointed and employed by the district council. The system of nomination ensures that the VEO has to come from the village. At the sub-village level the *kitongoji* leader is expected to assist in mobilising taxpayers.

This institutional set-up encompasses at least three principals: (i) the administrative leadership (management team) of the local authority; (ii) local politicians; and (iii) the central government administration (i.e. the ministry responsible for local government). These stakeholders, sometimes independent of each other and sometimes through collusion, try to influence the revenue target and, thus, the actions of the tax collectors. Based on evidence from fieldwork, the various stakeholders' objectives can be summarised as follows:

(i) The objective of *the management of the local authority* (the administrative leadership) is to generate enough tax revenues to pay the wage bill and allowances of the staff. This target seems to be a minimum performance requirement from the central government.[15] This argument is supported by observations from Kibaha and Kilosa. The performance of tax collectors at the ward and village levels is related to their capability to collect enough revenues to cover their wage bills. In recent years, several VEOs and some WRCs have been fired due to poor performance.

However, since both revenue estimates and reports on revenue collection are based on information from the administrative staff, there is room for manufacturing numbers. These observations are consistent with Migdal's (1988: 253) argument that political systems under pressure from the centre to produce certain development results are likely to exercise their own form of accommodation. The most common form is simply to pass false or inflated accounts of development results to superiors who are out of touch with local conditions. Thus, where supervision is lax, district leaders, including local bureaucrats, may use their budgetary discretion and the force at their disposal for personal gain.

(ii) One important objective of *local politicians* is to get re-elected (and thereby also to achieve sitting allowances when participating in council meetings). Politicians may say they want an efficient tax administration – but only to the point at which voters begin complaining that they are being harassed. Councillors are, in general, reluctant to raise local taxes and charges, not only due to concerns about their popularity, but also because they may be major local landowners or businesspeople who consider higher taxes to have a direct negative impact on them. As a result councillors try to intervene in revenue collection.

Indications of the impact of political intervention on tax collection can be found in the councils' financial statements. For instance, many councils experience revenue shortfalls in election years, particularly with respect to development levy. In a sample of forty-eight councils, thirty-one experienced a drop in revenues in the election year 1995.[16] This may be due to the influence of politicians (local as well as in central government). In both Kibaha and Kilosa, we were informed that CCM (ruling party) politicians tried to moderate the tax collectors' efforts to enforce taxes during election years, by issuing statements such as 'don't harass taxpayers' or 'relax on tax collection'. Politicians from the opposition parties, in contrast, approached taxpayers directly and advised them 'not to pay taxes', since taxes, according to their view, were used to 'finance the CCM government'. Such statements are said to be common in election years.

(iii) The objective of the *central government administration* (i.e. the ministry responsible for local government) is vague with respect to taxation. However, a tax system is also a mechanism of political control. According to Moore (1998: 105), it comprises two main elements: (1) the sets of information on citizens that a government otherwise might not collect and maintain; and (2) a network of public collection agents who use this information, and become 'repositories of knowledge' about what is going on in remote areas where the state elites have little direct influence and knowledge. Thus, the revenue itself may not be the most valuable product of tax enforcement. But active revenue raising may be an important means of keeping a state machinery alive and active at the local level. An indicator used by the central level to assure that this machinery is alive, is that the local authority generates sufficient revenues to cover its wage bill.

By and large, however, the central government is not directly involved in matters of local government taxation. For instance, the tax by-law system gives local authorities in Tanzania quite a wide discretion to introduce new local taxes and to set tax rates, subject to ministerial approval. Due to lack of capacity and poor coordination between the central and local government, only limited restrictions are in practice imposed by the central level on local governments' tax design. Therefore, the local revenue systems have developed without much interference from the central level.[17]

Social networks further complicate the picture outlined above. Such networks may play important roles in how tax enforcement is carried out in practice. In societies where family and ethnic relations are strong and important, civil servants are expected to take them into account. Tax collectors at the village level, as mentioned above, are recruited from the villages. Traditional networks may thus impose heavy constraints on the collector's actions, including who is to be targeted for tax enforcement and who is to be exempted.

For instance, in a survey of taxpayers in Kibaha and Kilosa, respondents who had migrated to the study areas from other regions in Tanzania were found to be more compliant than people who were born in the area (Fjeldstad & Semboja 1998). Migrants seemed (not surprisingly) to be less integrated and had looser relations to local authorities, including tax collectors, than people born in the area. Furthermore, migrants, in general, were found to be relatively more wealthy than people from the area. Thus, we may expect that it is easier and probably more convenient for the tax collector at the village level (i.e. the village executive officer), who lives in the village and is nominated to his position by the Village Council, to target migrants rather than people from the area who may be his relatives or friends, or have close links to local politicians and authorities.

In contrast to the ambiguous motivations of the village level collectors, tax collectors at the ward and district levels seem to be driven by motivations to maximise revenues. Thus, tax collectors can report sufficient revenues to cover the wage bill and pocket whatever is left, with or without collusion with their superiors.[18] The larger the amount collected, the larger the amount that can supplement their own meagre salaries.

To summarise, the various stakeholders involved in tax enforcement have divergent objectives with respect to tax collection. In particular, political pressure seems to be a major impediment to revenue collection. Political intervention sometimes results in conflicts between the revenue administration and local politicians. For instance, a general view expressed by the tax administrations in the study areas was that elected councillors obstructed tax collection and were talking 'cheap politics'. Such conflicts seem to be rooted partly in divergent objectives with respect to tax enforcement, and partly in lack of trust between administrators and politicians at the local level. Based on data from fourteen district councils Jacobsen (1999) finds that there is a 'trust deficit' in the political-administrative relations at the local level in Tanzania. Furthermore, lack of trust seems to reduce the flow of information between politicians and bureaucrats.[19]

The conflict between the tax administration, including collectors, and local politicians is particularly evident in Kilosa DC. Local politicians have little influence on the tax enforcement process. Collection is facilitated through extortive and violent approaches that are mainly advocated and implemented by council administrators, with minimum support from local politicians. Thus, in the absence of democratic forms of accountability, tax collection in Kilosa has turned into a licence for collectors on-the-ground to more or less freely augment the local treasury and supplement their own salaries through extortion from local residents.[20]

In accordance with Mamdani's (1996: 59) notion of 'decentralised despotism', financial autonomy has provided the framework in which lower-level officials resort to extra-legal enforcement and violence to extort money from the population. This argument can be illustrated by a few examples. For instance, the statutory voluntary period for paying development levy in Tanzania is from 1 January up to 30 September. All tax payments made after the deadline are subject to a penalty equivalent to 50 per cent of the tax rate. From 1 October to 31 December development levy payment 'campaigns' are conducted, organised by the ward office and using state organs, such as the local militia and judiciary, to ensure compliance. Defaulters may be visited in their homes, or people may be required to show their tax receipts at roadblocks. Non-compliers who are caught are brought to court at the primary court or ward level. Due to widespread resistance, tax campaigns for development levy in Kilosa DC (involving the militia) start as early as in July, i.e. three months before the voluntary (and statutory) payment period expires. The district treasury staff argued that by waiting until the end of September, taxpayers would have spent their money and nothing would be left for taxation.

Furthermore, in Kilosa the village level has been excluded from collection, and tax enforcement has been taken over by the ward level. According to the district treasury staff, this was due to incentive problems connected with tax collection at the village level. One problem arises from the presence of two principals for the VEOs, that is, the village council as the nominating authority and the district council as the appointing and employing authority, leading to divided loyalty. Another problem arises from VEOs operating within their areas of domicile. Thus, personal relationships between collectors and taxpayers may be expected to play an important role in village tax collection. In many villages the sub-village (*kitongoji*) leaders also resist mobilising people to pay taxes due to the unpopularity of taxation.[21]

In Kibaha DC, too, tensions between the administration and councillors are observed, although much less pronounced than in Kilosa. In general, tax collection in Kibaha is characterised by greater laxity than in Kilosa, due to the intervention of politicians. In some wards in Kibaha local politicians partly act as executives. A general view expressed by the tax collecting staff, reflecting their frustration at this intervention, was that councillors obstructed tax collection. The expected consequence of this intervention is reduced tax effort. Thus, this simple analysis suggests that tax effort depends on the relative 'bargaining power' between the elected councillors and the management of the council.

DONORS

Why does the relative influence of the council administration and local politicians on tax enforcement vary between councils? I suggest the following proposition to explain these observed differences:

Proposition 3: Donor presence empowers the managerial level in local authorities at the expense of elected councillors.

Through district development programmes, donors often exert strong influence on the behaviour, decisions and actions of local authority administrators and politicians. Generally, donors cooperate with council administrators and staff to implement their activities, usually through the creation of parallel structures. This intervention increases the influence and power of the bureaucracy, at the expense of the political system.[22] In Kilosa District Council, which has a long history of donor support, indications were found that this was indeed the case.[23]

Since donors, as noted above, increasingly use revenue generation as an indicator of the performance of the councils they are involved in, this may further empower the management level.[24] One strategy donors have used to reduce the problems of free riding by local councils has been to adopt a matching scheme, which supplies aid only on the basis of matching funds from the local government. According to Catterson & Lindahl (1998: 20), this has 'created strong incentives for revenue collection' in Tanzania. Furthermore, donor support may cushion council administrators against possible taxpayers' opposition. Service provision through donor supported activities provides a free riding opportunity to council administrators who often claim to be the providers of such services.[25]

Kibaha, in contrast, has experienced limited donor support. As noted above, local politicians there play an important role in tax enforcement, and tax collection is characterised by greater laxity. The level of corruption (both absolute and relative) also seems to be lower in Kibaha than in Kilosa. This might be because local politicians in Kibaha to some extent carry out informal monitoring of the collectors. In general, the formal monitoring and auditing devices do not function at the local level in Tanzania.

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This paper has explored the reasons why revenue-raising performance may differ between local authorities in Tanzania. The analysis shows that coercion is likely to be an integral part of the tax collection methods. Furthermore, the study demonstrates that the involvement of donors at the local level may have at least two impacts on tax enforcement: (i) donors' presence may induce increased tax effort, however, (ii) at the expense of accountability and democratic consolidation.

Thus, Moore's (1998) proposition that the more a state (in this case a local government) 'earns' its income through bureaucratic tax collection, the more likely are state–society relations to be characterised by accountability and democracy, is not supported. In contrast, increased tax effort is achieved through coercive methods, often characterised by violent and extortive forms of enforcement. The reciprocal element between the state and citizens seems to be absent in connection with local government taxation in Tanzania.

However, the analysis does support Moore's argument that donors, by the means they use to promote development, may undermine democracy and good governance. For instance, arrangements which supply development aid on the basis of matching funds from the local government may lead to increased extortion, and empower the administration at the expense of the elected councillors. Harsh tax enforcement in situations with poor service delivery may thus contribute to further undermining the legitimacy of the government and increase tax resistance.

The results presented in this paper emphasise the importance of knowing how local government institutions work as a prerequisite for good policy decisions. In certain contexts external interventions may have impacts that are contrary to those intended. Such interventions may contribute to undermine the legitimacy of the local government and hamper democratic development by disempowering the political organs of local authorities.

Furthermore, the emphasis on revenue targets does not seem to acknowledge other major impacts of the tax system. Many local revenue bases in Tanzania perform poorly with respect to the basic principles of taxation: they are often distortive and costly to administer, and exacerbate both horizontal and vertical inequity (Fjeldstad & Semboja 2000). Attempts to squeeze additional revenues from poorly designed taxes may, therefore, have negative effects on the economy and society in general. However, these issues do not appear to be recognised by either local authorities or donors, whose main concern simply seems to be to increase tax revenues at any cost.

The paper provides us with some directions for further research. In particular, there is a need for a better understanding of (i) the impacts of development aid on revenue collection, and (ii) the relationship between taxation, accountability and processes of democratisation.

First, the role of donors in relation to local government tax systems in poor aid dependent countries is a fairly unexplored area of research. This is surprising, given that questions of revenue generation affect ordinary people in basic and sometimes very serious ways. A comparative study of tax collection in councils with varying degrees of donor involvement may shed light on this and other issues, including the possible impacts on revenue generation of the ongoing democratisation process. Second, many issues of accountability are unexplored. For instance, are citizens in poor countries likely to be able to hold bureaucrats (and politicians) accountable? Furthermore, can, and under what conditions, compliance be established in poor countries without an extensive and costly enforcement apparatus? These questions are important because it is likely that governments which seek power on the basis of popular consent will face restrictions in their use of coercion in tax collection.

NOTES

1. The empirical evidence is, however, inconclusive on the actual impacts of aid on domestic revenue raising effort (White 1994; Devarajan *et al.* 1998).

2. In 1997, aid represented 10 per cent or more of GDP in twenty-one African countries (World Bank 1999).

3. For instance, Heller (1997: 39) calls the tax effort in most African countries 'disappointingly low'.

4. Democracy in this context is understood as a sub-species of a broader concept: the accountability of state to society (Therkildsen 2000). This political accountability is about those with authority being answerable for their actions to the citizens, whether directly or indirectly. Day & Klein (1987: 26–7) make an important distinction between political and managerial accountability, the latter being about making those with delegated authority answerable for carrying out agreed tasks according to agreed criteria of performance.

5. Moore (1998: 94) argues that the use of the concept 'earned' is a logical extension from the term 'rentier', since rentier is 'unearned' in the language of classical political economy.

6. Results of these studies are reported in Fjeldstad & Semboja (1998, 1999).

7. The four main sources of revenue have dominated district councils' revenue generation since local government was reintroduced in 1983 (URT, 1991). In 1987/88, from a sample of ten rural councils, development levy, crop cess and business licences contributed 77 per cent of the revenues. Thus, although there is a tendency for their contribution to decline, they still account for the major shares of the councils' own revenues.

8. According to the World Bank (1993: 29) the poverty profiles in Coastal Region (including Kibaha DC) and Morogoro Region (including Kilosa DC) are quite similar. This observation is based on a comparison of farming environments in different regions, since agriculture is the main economic activity in rural areas.

9. Levi (1988) uses the concept 'quasi-voluntary compliance'. It is 'voluntary' because taxpayers choose to pay. It is 'quasi-voluntary' because the non-compliant are subject to coercion – if they are caught.

10. Scott (1985) argues that one of the most important 'weapons of the weak' is the ability to withdraw compliance. This can take a passive form, such as shirking, or an active form, such as rebellion. Historically, unwillingness of the population to comply with a tax that is deemed unjust has been a catalyst for political action. The Boston tea party and the Thatcher poll tax are illustrative examples. Bates (1983) provides some examples from Africa.

11. Enemuo (2000: 181), reviewing the problems and prospects of local governance in Africa, supports this argument.

12. These results are consistent with the findings of a study of local government health services in Tanzania (Cooksey & Mmuya 1997); 65 per cent of the respondents in this study considered the poor quality of these services to be a major problem. Furthermore, 69 per cent of the respondents said they disagreed with the statement that the quality of public health services had improved in recent times.

13. Cases of tax revolts are also reported from councils in other regions, including Kilimanjaro Region and Coastal Region. *Daily News* (Dar es Salaam, 28.11.1997: 5) reports that 'over twenty Moshi Municipal Council workers who were on a special operation to net development levy defaulters were attacked by a mob at Mbuyuni Market on Wednesday afternoon and eight of them were injured, some seriously …'. These revolts are in general spontaneous and disorganised. According to Bratton & van de Walle (1994: 462), such uprisings characterise the way political protest erupts in neo-patrimonial regimes. Because civil society is underdeveloped in such regimes, the foundation for anti-systemic change is weak.

14. District and urban councils are sub-divided into wards (kata). Currently there are about 2,400 wards in Tanzania, and more than 9,000 registered villages. Each village is supposed to have at least 250 households (*kayas*). Villages are sub-divided into *vitongoji*.

15. In *Africans: the history of a continent*, John Iliffe (1995: 196) discusses the priorities of the colonial administration. He quotes a veteran native commissioner in Southern Rhodesia who remembered his duties as follows: 'Get to know your district, and your people. Keep an eye on them, collect tax if possible, but for God's sake don't worry headquarters.' To some extent Iliffe's description from the colonial period reflects the present district official's approach in Tanzania: Don't worry headquarters, i.e. the central government. To achieve this it is necessary to collect enough revenues to pay the salaries of the local employees, otherwise complaints will be forwarded through the trade unions.

16. Based on data from the Ministry of Regional Administration and Local Government (see Fjeldstad & Semboja 1999).

17. Lack of coordination between the central and local levels has led to duplication of taxes and inconsistencies between taxes imposed by local authorities and the national government's development policies (e.g. with respect to export promotion). An illustrative example is the cess rate on cashew nuts, a major export crop, which in 1997 represented 20 per cent of the price paid to producers in Kibaha DC, creating huge disincentives for export production. In border areas, smuggling has become extensive due to relatively high local cess rates on some crops, for instance on coffee. Thus, peasants dodge and manoeuvre to avoid the deprivation inflicted upon them by public policy.

18. Corruption is often embedded in the hierarchical structure of the bureaucracy (Rose-Ackerman 1999: 49). Low-level officials collect bribes and pass a share to those at higher levels. Conversely, higher-ups may organise and rationalise the corrupt system to avoid wasteful competition between lower levels. This system has some similarities with sharecropping systems in agriculture. Sharecropping is a land-tenure system where the landlord gets a (percentage) share of agricultural output, and the tenant keeps the remaining output (Sah & Stiglitz 1992).

19. Conflicts between council employees and local politicians are not, however, a new phenomenon in Tanzania. Dryden (1968: 144–9), referring to the mid-1960s, describes some areas of conflict between these stakeholders.

20. Wunsch (1990: 54), based on Hyden (1983), argues that in circumstances where national leaders were dogmatic on implementing comprehensive programmes, as Tanzanian leaders were during the late 1970s regarding Ujamaa villagisation, bureaucrats have been reduced to authoritarian instruments for enforcing compliance.

21. According to the tax by-law, 20 per cent of the development levy collected at village level must go back to the village for developmental and operational purposes. A part of this money is to be given to the *kitongoji* leaders as an incentive for mobilising taxpayers to pay the levy. However, nothing was returned from the council treasury to the villages visited in Kilosa. The administration's argument for this was that since the villages did not contribute in tax collection they should receive nothing in return. This position, however, affects peoples' attitude toward the government and probably also promotes tax resistance.

22. This argument is supported by other studies. In a comprehensive study on the role of government in adjusting economies, Batley (1999) reports that public sector reform programmes pushed by donors and emphasising technocratic solutions, lead to increased managerial power without a strengthening of the accountability of the managers to politicians and the public.

23. The Irish funded 'Kilosa District Rural Development Programme' (KDRDP) was initiated in 1979. In 1994 it was one of the largest district development programmes in Tanzania (Mullen *et al.* 1995).

24. Changes in the performance of decentralised institutions have tended to be studied principally in terms of financial performance or revenue mobilisation (Crook & Manor 1998: 8). For instance, in a study exploring the determinants of success in African local governments, Smoke & Olowu (1992) define success mainly in terms of fiscal performance.

25. However, people in Kilosa seem to be well aware about who is providing the various services, and distinguish between 'council services' and 'donor provided services'. For instance, the main roads in Kilosa which have a fairly good standard due to donor funding, are locally referred to as 'Irish roads', while the almost non-passable feeder roads are named 'council roads'.

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Fiscal Corruption: A Vice or a Virtue?

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Summary. — Recent literature on tax administration in poor countries suggests there are virtues in allowing fiscal corruption. By strengthening the bargaining power of corrupt tax officers, it is argued that tax evasion may be reduced and tax revenues increased. But does such an intriguing paradox justify policies that stimulate corruption? Our answer is no, and this note puts forward three arguments to support our view. First, while an increase in corruption may raise revenues in the short run, in general, the opposite will be the case in the longer run. Second, the instrumental value of reducing corruption goes far beyond its effects on tax evasion and tax revenues. Accepting corruption as a policy strategy to increase tax revenues may undermine values of democracy and good governance. Third, eliminating corruption should be considered an end in itself. Thus, contrary to recent suggestions on incentive reforms in tax administration, the reasonable starting point for policy debates in this area should still be that an increase in fiscal corruption is not an appropriate instrument for raising tax revenues. Sustained development cannot occur in an institutional framework that fosters corruption and extra-legal tax enforcement.

Key words — corruption, tax evasion, tax administration, incentives

1. INTRODUCTION

One of the areas of government where the impacts of corruption loom largest is in the assessment and collection of taxes (Galtung, 1995). Studies in various developing countries indicate that it is not uncommon that half or more of the taxes that should be collected cannot be traced by government treasuries due to corruption and tax evasion (Alm, Bahl, & Murray, 1991; Bird, 1990, 1992; Krugman, Alm, Collins, & Remolina, 1992; Richupan, 1984). This tax-base erosion is particularly damaging since insufficient domestic revenue mobilization is considered the root of the adjustment and growth problems faced by many poor countries (Chand & Moene, 1999). To alleviate this problem, tax reforms in recent years have focused on redesigning the tax structures and improving tax administration. Addressing fiscal corruption and tax evasion has become an integrated part of this strategy (Klitgaard, 1988; Toye & Moore, 1998).

A growing literature emphasizes the importance of incentive schemes in motivating tax officers to work harder and in accordance with the overruling objective of improving revenue performance (Chand & Moene, 1999; Das-Gupta & Mookherjee, 1998; Mookherjee, 1997). Such incentive schemes *may*, however, increase corruption. Actually, as we elaborate

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in Section 2, a standard way of justifying incentive schemes is by showing that such schemes strengthen the position of corrupt tax officers and thereby make tax evasion less attractive. Nevertheless, it is argued, in cases where the effect on taxpayers' compliance and government revenues is positive, incentive schemes are still justified: "Eliminating corruption is... not an end in itself; effects on tax evasion and revenues are more fundamental" (Mookherjee, 1997, p. 16).

In this note we put forward three arguments that question this way of defending incentive schemes. First, while an increase in fiscal corruption may contribute to an increase in tax revenues in the short run, it is highly implausible that such an increase is sustainable (Section 3). The dynamics of corruption suggest that policies of this kind will decrease tax revenues in the longer run. Second, a much broader view of this problem is needed in the development debate, including the effects of fiscal corruption on accountability and government legitimacy (Section 4). Third, eliminating corruption *is* an end in itself. In our view, any reasonable conception of a good society should count corruption—that is, the abuse of public offices and rules for personal gain—as intrinsically bad (Section 5).

2. THE VIRTUE OF FISCAL CORRUPTION

How may corruption contribute to reducing tax evasion and thereby increasing tax revenues? The essential link, studied by Mookherjee (1997) among others, is based on the idea that the possibility of negotiating bribes from evasive taxpayers motivates corrupt tax officers to work harder in order to detect evasion. [1] This is anticipated by the taxpayers, and hence tax evasion is less attractive because it is more likely to be detected.

Since corruption works to make tax evasion less appealing and thereby increases tax revenues, it might be a good idea to design a bonus system for tax collectors that mimics or competes with the bribery system already in place in many tax administrations. Actually, this has been attempted in Ghana (Chand & Moene, 1999) and has been suggested in several other countries. The intention behind a bonus system is to initiate more work effort among tax collectors by promising them a share of the tax revenues. This is the way it works for noncorrupt tax collectors, who within a bonus system, aim at detecting evasion because this increases tax revenues and *thereby* their income. But what about corrupt tax collectors?

Consider a bribe as the outcome of a negotiation between an evasive taxpayer and a corrupt tax collector. The introduction of a government bonus certainly makes the bribe less attractive for the corrupt tax collector, because he has to give up the bonus when accepting the bribe. But, this does not necessarily insure that the tax collector becomes less corrupt. Actually, it makes him stronger in his negotiations with the taxpayer, and as a result he receives a larger part of the pie not reported to the tax authorities. Thus, the bonus system provides incentives for the corrupt tax collector as well (by increasing the negotiated bribe), and may thereby contribute to increase tax revenues. This happens because the bonus system strengthens the position of the corrupt tax collector and therefore may increase overall corruption. [2]

Generally, the implications of a bonus system depend on whether the tax administration consists of corrupt or noncorrupt tax collectors. In both cases, we might experience an increase in overall tax revenues, but in the case of corrupt tax collectors, the bonus system may also lead to increased corruption. Hence, in a situation where there is a mixture of corrupt and noncorrupt tax collectors, it seems straightforward to say that we have to make a tradeoff between the gain of more revenues and the problem of more corruption when evaluating a bonus system. But, this is not how bonus systems are justified in the theoretical literature on corruption and incentives.

Mookherjee (1997), for example, considers bonus systems in the context of corrupt tax collectors *only*, and then argues for the need "to go beyond the question of what levels of corruption arise and examine induced effects on tax compliance and audit incentives" (p. 13). Hence, when evaluating bonus systems, Mookherjee solely considers the possible gain in tax revenues following from the fact that the position of corrupt tax officers is strengthened. In our view, this way of justifying bonus systems should be rejected because it does not capture the long-term effects of an increase in corruption on tax revenues and government legitimacy. We find it highly implausible that sustained development can occur in an institutional framework that fosters corruption and extra-legal tax enforcement.

Mookherjee is, of course, aware of the vices of corruption, and stresses the important point that when considering incentive reforms we also need to take into account the possibility of wider administrative reforms, including changes in supervision systems, information and monitoring procedures. More precisely, he suggests that "if incentive reform causes various undesired side effects, the range of policy instruments must be expanded to moderate their effects" (p. 8). This is however, a problematic position within the present mode of reasoning. If one considers an increase in corruption an undesirable side effect to be moderated, then an incentive reform cannot be justified by showing that it increases tax revenues by (possibly) inducing *more* corruption. Such a justification would be undermined by the policies aiming at reducing corruption.

Let us examine another example of how the strengthening of the position of corrupt tax collectors has been considered part of a "virtuous circle" in reforming tax administrations. Chand and Moene (1999) are concerned with the need for noncorrupt higher-level bureaucrats in tax administration when introducing bonus systems, and illustrate this by the following story. Consider the case of a corrupt tax collector who tries to negotiate a bribe from an evasive taxpayer in return for underreporting his tax liabilities. If they do not reach an agreement—that is, if the taxpayer refuses to pay the bribe and the collector reports the evasion—a higher-level bureaucrat is informed about the true tax liability of the taxpayer and settles the case. If the higher-level bureaucrat is corrupt, the evasive taxpayer pays him a bribe and provides taxes only on the underreported tax liability. In contrast, a noncorrupt higher-level bureaucrat collects the taxes on the true tax liabilities. Therefore, the presence of a noncorrupt higher-level bureaucrat strengthens the position of the corrupt tax collector in the negotiations with the taxpayer. Why? Because it becomes less important for the corrupt collector to reach an agreement with the taxpayer. The collector knows that as long as the higher-level bureaucrat is not corrupt, he will receive the bonus on the whole tax liability if he does not reach an agreement with the taxpayer. This would not be the case if the higher-level bureaucrat was corrupt. The tax collector would then not receive any bonus. Hence, in order to have an effective bonus system, noncorrupt higher-level bureaucrats are required. They make it possible for the *corrupt* tax collector to get a higher bribe by strengthening the collector's bargaining position in relation to taxpayers and thereby also stimulate his work effort. Consequently, this will contribute to an increase in tax revenues in the short run. But is this really the virtue of having noncorrupt higher-level bureaucrats in tax administration when introducing a bonus system?

Let us close this section by briefly pointing at some of the mechanisms we expect to reflect the real virtues of an incentive reform. First, as already stressed, an effective bonus system induces more effort among noncorrupt tax collectors. Second, and maybe more important, a bonus system, within an administration containing noncorrupt higher-level bureaucrats, may cause less corruption among tax collectors. [3] Let us provide a simple illustration of this point. Assume that a company reports the profit R, whereas the true profit is Π. The tax rate is t and the bonus rate is γ. All tax collectors assign a certain disvalue $1/m$ to accepting a bribe, $m \geqslant 1$, where $m = 1$ would imply that the tax collector is indifferent between receiving a certain amount of money as a bribe or as a regular bonus. [4] If the tax collector does not accept the bribe and reports the evasion to a noncorrupt higher-level bureaucrat, then he receives a bonus on the true profit. In this case, a collector would only accept a bribe b if: [5]

$$\gamma t R + b/m > \gamma t \Pi \tag{1}$$

Obviously, the bribe will not exceed the taxes saved on the underreported amount $t(\Pi - R)$. [6] Hence, on the basis of (1), we find a cut-off value m^* such that no tax collector having a value *above* m^* would choose to be corrupt. [7]

$$m^* = 1/\gamma \tag{2}$$

From (2), we can see that an increase in the bonus (γ) decreases m^* which indicates that the number of corrupt tax collectors should decrease in an effective bonus system. [8]

To summarize, there are important positive effects from incentive reforms in the tax administration. The reforms make noncorrupt tax collectors work harder, and may reduce the number of corrupt tax collectors in the administration. Hence, possible tradeoffs must be made between reducing corruption and increasing tax revenues when considering incentive reforms. We doubt however, that it is a reasonable strategy to improve revenue collection by strengthening the bargaining power of corrupt tax officers *vis-à-vis* taxpayers. Thus, we question the claim that one of the positive effects of such reforms is that increased tax revenues can be achieved by stimulating corruption among corrupt tax collectors.

3. LONG-TERM IMPACTS OF FISCAL CORRUPTION

Poor taxpayer compliance is particularly damaging in situations with substantial budget deficits, as is the case in many poor countries (Tanzi, 1991). But, accepting fiscal corruption as an instrument for raising revenues in the short run may undermine tax collection in the longer run, for several reasons. Let us here point at some of the most important ones.

First, implicit in the discussion of the positive link between fiscal corruption and tax revenues is the assumption that the willingness to pay taxes is independent of the way taxes are collected. This assumption is in contrast to the literature on reciprocity considerations in tax collection. For instance, Smith (1992, p. 227) argues that tax authorities' unresponsive, corrupt and unfair treatment of taxpayers fosters disrespect for and resistance against tax authorities and tax laws. [9] In a study of Tanzania, Fjeldstad and Semboja (2001) find that the unresponsive way taxes are enforced appears to have fuelled tax resistance. Accordingly, they argue, tax evasion may to some extent be interpreted as a strategy of public resistance and opposition against the authorities. Hence, an increase in corruption may establish a negative public perception that causes citizens to be unwilling for a long period to enter into reciprocal relationships with the government. Thus, accepting fiscal corruption as an instrument to raise revenues may contribute to undermining the legitimacy of the tax administration, and thereby *increase* tax evasion and decrease tax revenues over time (Tanzi, 1995, 2000). We believe this to be an important issue, because public opinion is not easily restored over time.

Second, the relationship among tax collectors also needs to be considered. Tax collectors do not operate on their own, but are influenced by the behavior of their reference group, such as colleagues and friends. [10] As stressed by Fehr and Gächter (2000, p. 167), "[s]ocial sanctions by peer members are probably a very important determinant of effort behavior in work relations." Therefore, if a tax officer knows that colleagues are becoming more corrupt, his commitment to honest behavior may be weakened. There are at least three arguments supporting this view (Sah, 1991; Banerjee, 1992):

—internalized feelings of guilt from fraudulent behavior become weaker as the number of corrupt tax officers increases;
—when many others are involved in corruption, the loss of reputation (stigma) for each collector when discovered decreases; and
—when many others are corrupt, this lowers the probability of corruption being revealed due to the fact that the capacity of internal and external investigation units are constrained.

In other words, "corruption may corrupt" (Andvig & Moene, 1990). Thus, an increase in fiscal corruption may initiate a vicious circle in the long run in the tax department.

Third, this vicious circle may have impacts on the recruitment process of the tax administration. It is reasonable to assume that more fiscal corruption among tax collectors will attract potentially more corrupt employees (Besley & McLaren, 1993). Furthermore, an atmosphere of corruption can result in a recruitment process based on the wrong premises (Huther & Shah, 2000). Significant above-market rate wages in specific public institutions in order to reduce shirking and corruption may imply that one gets two prices for the same type of service. This may in general create fertile ground for corruption and rent-seeking where attractive jobs are likely to be sold, and the sale price has built in the capital value of the salary surplus. Andvig (1999), for instance, reports from Azerbaijan that a regular customs official at a "fat site" has to pay US$100,000 to get his position. A position is normally financed by the incumbent borrowing from family and friends. The customs official is assumed to have earned enough to repay the investment after six months. Thereafter he is supposed to send a percentage (85% is indicated by Andvig) of what he gains on corruption upward to his superiors.

Fourth, accepting corruption may have negative impacts on the future possibility of reforming the tax system. For instance, important stakeholders, including bureaucrats and politicians, as well as powerful taxpayers, may resist changes in an attempt to protect their influence and control of the tax system. According to Winters (1996, p. 166), the strongest resistance to tax reforms in Indonesia came from the tax officials themselves, since they had the most to lose from the depersonalization and simplification of the tax system. Flatters and Macleod (1995, p. 409), also referring to Indonesia, assert that tax collectors actively opposed simplifications in property tax administration, income tax laws and tariff structures. Moreover, some observers argue that the extensive public sector regulations and complicated tax systems observed in many poor countries are the result of a deliberate strategy by civil servants, including senior tax officials, to facilitate corruption (Tanzi, 2000; Myrdal, 1968).

Developments in the tax administration in Ghana, which is the crosscutting case to which Chand and Moene (1999) refer, may support our general point. Following the reforms, tax revenues in Ghana increased from 4.6% of GDP in 1983 to 17% in 1994 (Chand & Moene 1999, p. 1135, Table 2), despite reductions in tax rates. But if the increase in tax revenues in Ghana was due to a strengthening of the positions of corrupt tax officers, then we would expect a difficult future for the tax administration in the longer run. In fact, this seems to be what Ghana has experienced; the initial success has not been sustained (Devas, Delay, & Hubbard, 2001, p. 213). According to Hadler (2000, p. 40), the tax administration in Ghana, the first country in Africa to establish an autonomous revenue agency, is "reputedly now in disarray." [11]

In summary, increasing fiscal corruption by strengthening the position of corrupt tax officers may initiate two vicious circles in the longer run. On the one hand, it may reduce peoples' willingness to pay taxes; on the other hand, it may weaken a commitment to honest behavior in the tax administration. Both these effects are closely related to the importance of values in tax collection and tax compliance. Our general point is that inducing fiscal corruption in the long run undermines the values essential to an efficient tax administration. As observed by Amartya Sen:

> Indeed, in societies in which corrupt behaviour of the standard type is quite unusual, the reliance is, to a great extent, on compliance with codes of behaviour rather than on financial incentives to be corrupt. This forces attention on the norms and modes of behaviour that respectively prevail in different societies (Sen, 1999, p. 276).

Of course, this does not imply that incentives are of no importance. But we question the idea of fostering fiscal corruption in order to gain short-term increases in tax revenues. [12]

4. GOVERNMENT TRUSTWORTHINESS

Fiscal corruption is likely to undermine government trustworthiness and, thus, the legitimacy of the government, where legitimacy refers to citizens' approval of the government, which in turn justifies citizens' obedience. [13] When the institutions are legitimate, citizens have a predisposition to consider obedience to them as reasonable and appropriate (Fauvelle-Aymar, 1999). A government's lack of legitimacy, on the other hand, diminishes almost by definition the perceived moral justification for obeying its laws (we return to this point in Section 5). Furthermore, of particular importance in this context is that citizens' disrespect for the tax laws may initiate disrespect for other laws, and, thus contribute to further undermining the legitimacy of government (Graetz, Reinganum, & Wilde, 1986). This suggests a vicious circle where distrust breeds distrust. In contrast, government trustworthiness and widespread public support tends to legitimize the public sector, and may therefore impose some social norm to pay taxes. Hence, it is important to take a broader view of the societal effects of corruption in tax administration. [14]

The need for a broader view on taxation derives from the fact that taxation is essential for shaping state-citizen relations (Levi, 1988; Moore, 1998). For instance, in Europe over the past two centuries, taxation and disputes over the use of revenues have stimulated the development of greater citizen rights and privileges, with democratic institutions enforcing accountability and greater transparency in expenditures (Tilly, 1992). Moreover, it almost goes without saying that fiscal corruption, as an integral part of tax collection, does not contribute to establish productive state-society relations. Survey research from a number of countries concludes that citizens in general view corruption negatively even where it is widespread. Miller, Grødeland, and Koshechkina (1998), for instance, in a study of bribery in the Czech Republic, Slovakia, Bulgaria and Ukraine, find that public opinion in all four countries is against corruption. The morality of public officeholders is therefore most likely an important source of government trustworthiness (Brennan, 1998; Hardin, 1996).

Recent research also indicates that citizens' trust in their fellow citizens is strongly influenced by whether they have confidence in the government that they share (Brehm & Rahn, 1997). This observation strengthens the need for a broader view of the societal effects of fiscal corruption. We know that a functioning social order requires social behavior (Coleman, 2000; Putnam, 1993; Serageldin & Grootaert, 2000) and a productive set of common norms (Bardhan, 1995; Offe, 1999), which will only evolve in a society of trustworthiness (Dasgupta, 1988; Sztompka, 1999).

To summarize, there are two main reasons for taking a broader view on fiscal corruption. First, when government is perceived to be trustworthy, citizens are more likely to comply with its demands in general (Levi & Stoker, 2000). From this perspective, government trustworthiness is closely linked to citizens' perceptions of the capacity of the government to make credible commitments about the use of their taxes, as well as the government's procedures for designing and implementing policy nonarbitrarily (Levi, 1997, 1988). Second, government trustworthiness contributes to social behavior in general and a productive set of common norms in society. These norms are important for establishing the more informal social networks and associations of civic engagement that effects the productivity of the community (Putnam, 1993). Moreover, they are also crucial for strengthening the formalized institutional relationships such as the political regime, the rule of law, the court system, as well as the tax system, that may have important effects on the rate and pattern of economic development (North, 1990; Olson, 1982).

5. ELIMINATION OF CORRUPTION AS AN END IN ITSELF

Mookherjee (1997, p. 6), claims that the elimination of corruption should *not* be considered an end in itself, and he substantiates this point by arguing that complete elimination of corruption may be impossible. We reject this line of reasoning. A noncorrupt society may be a utopian ideal, but this does not undermine the possibility of assigning intrinsic disvalue to corruption. To consider reduced corruption an end in itself is simply to say that it is important in its own right, and does not have to be justified (as a value) on the basis of its effects on the economy and society in general. We believe this to be a reasonable position to take. Of course, there are other ends to consider, and hence we have to make tradeoffs. But this only shows that there is a plurality of constitutive elements in the process of development.

Corruption is the violation of established rules for personal gain, and the disvalue of corruption depends on the legitimacy of these rules. But within a fair system of cooperation, the elimination of corruption should be considered an end in itself. This has been argued forcefully by Rawls among others, who views a fair system of cooperation as involving:

> terms that each participant may reasonably accept, provided that everyone else likewise accepts them. Fair terms of cooperation specify an idea of reciprocity: all who are engaged in cooperation and who do their part as the rules and procedures require, are to benefit in an appropriate way as assessed by a suitable benchmark of comparison. Since the primary subject of justice is the basic structure of society, these fair terms are expressed by principles that specify basic rights and duties within its main institutions... (Rawls, 1993, p. 16).

Moreover, Rawls (1993, p. 19) argues that anyone with a sense of justice should apply and act from the public conception of justice which characterizes the fair terms of social cooperation, and hence ought not to be involved in any kind of corruption.

Considerations of this kind may be perceived as having little relevance to policy debates in poor countries that are far from any ethical equilibrium of fair cooperation. We doubt, however, the validity of such a point of view. In particular, we believe that Rawls' line of reasoning may contribute to establish an understanding of the main institutions in society in general—and tax administration in particular—as ways of specifying fair terms of cooperation, where violation of these terms is considered wrong in itself. By recognizing this, we also see the plausibility of considering the elimination of corruption as an end in itself.

6. CONCLUDING REMARKS

The point of departure for this note is the literature showing that increased fiscal corruption in some contexts may contribute to increased tax revenues. We do not argue against the relevance of this argument. On the contrary, it is important to clarify this relationship. There are obviously cases where tradeoffs must be made between reducing corruption and increasing tax revenues by using incentive reforms. We doubt however, that it is a reasonable strategy to improve revenue collection by strengthening the bargaining power of corrupt tax officers *vis-à-vis* taxpayers. Hence, we question the claim that one of the positive effects of such reforms is that increased tax revenues can be achieved by stimulating corruption among corrupt tax collectors. Based on existing literature on corruption, incentives, compliance and normative reasoning, we conclude that the reasonable starting point for policy debates in this area should be the straightforward one that an increase in fiscal corruption is not an appropriate instrument for raising tax revenues. Sustained development cannot occur in an institutional framework that fosters corruption and extra-legal tax enforcement.

NOTES

1. More generally, Mookherjee (1997) focuses on the problems likely to be encountered in designing and implementing incentive reforms, and on evaluating the effects of pay-for-performance schemes for tax collectors on corruption and tax revenues.

2. The total amount of bribes received by corrupt tax collectors does not necessarily increase in equilibrium. This depends on the reaction of the taxpayer to the fact that the work effort of the tax collector increases. There are, of course, other ways of measuring corruption than by the bribe rate. For instance, corruption can be measured as the proportion of corrupt tax officers in the tax administration. Although the precise conclusion on the effect of incentive reforms on corruption may depend on how corruption is measured, this is not essential for our argument.

3. See also Besley and McLaren (1993) for a related discussion.

4. This way of modeling moral costs is quite standard within a static framework, and pursued by among others Laffont and Tirole (1991). Within a dynamic setting however, more elaborate modeling is needed.

5. We do not consider the issue of monitoring, and hence the tax collector knows for certain that the acceptance of a bribe will not be punished. The example can, however, easily be extended to include monitoring, but this would not add anything to our story.

6. The possibility of extortion is not considered in this simple example (see Hindriks, Keen, & Muthoo, 1999 and Klitgaard, 1988).

7. Eqn. (2) is not well defined for the exact case where there is no bonus, but the implication of the equation is that if the bonus approaches zero then all tax officers will be corrupt (except for tax officers having a deontological approach to corruption; represented by m equal to infinity).

8. Here, we ignore the equilibrium response of the companies, and assume that they do not increase underreporting when the bonus increases. Notice that m^* is not the critical value of m defining the partitioning of the set of tax collectors into corrupt and noncorrupt, and that we implicitly assume a continuous distribution of the value of m among tax collectors. Thus, we cannot draw any definite conclusions from (2), but for our purpose this should give a reasonable indication of the mechanism in question.

9. This proposition can also be stated in positive terms: Tax authorities responsive, honest, respectful and fair treatment of taxpayers tends to foster respect for and cooperation with the tax system.

10. For a more general analysis of these mechanisms, see Hessing, Elfers, and Weigel (1988) and Snavely (1990).

11. To explain this development in revenue performance, we also have to look at factors other than corruption, including general economic trends and changes in tax policy.

12. See also Elster (1989, p. 158).

13. Following Lipset (1959, p. 86), legitimacy can be defined as "the capacity of a political system to engender and maintain the belief that existing political institutions are the most appropriate or proper ones for the society."

14. Daunton (1998) provides an excellent historical account of the role of trust and trust formation in the British fiscal administration from the Napoleonic wars to WW II.

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FIGHTING FISCAL CORRUPTION: LESSONS FROM THE TANZANIA REVENUE AUTHORITY

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SUMMARY

Over the last decade, several African countries have undertaken comprehensive reforms of their tax administrations to increase revenue and curb corruption. This article examines recent experiences in the fight against corruption in the Tanzania Revenue Authority (TRA). Two lessons of broader relevance are highlighted. Firstly, even with relatively high wages and good working conditions, corruption may continue to thrive. In a situation where there is high demand for corrupt services, it is unrealistic to provide tax officers with pay rates that can compensate for the amount gained through bribery. Without extensive and effective monitoring, wage increases may produce not only a highly paid, but also a highly corrupt tax administration. Secondly, hiring and firing procedures may lead to more corruption. Corrupt tax officers often operate in networks, which also include external actors. These corruption networks seem to have been strengthened because many of those fired were recruited to the private sector as 'tax experts'. This partly explains why the positive process experienced in the initial phase of the new revenue authority was later reversed. Copyright © 2003 John Wiley & Sons, Ltd.

INTRODUCTION

Tax systems in most poor countries are characterised by widespread corruption and tax evasion. Substantial amounts never reach the treasury (Kiser and Baker, 1994; Ul Hague and Sahay, 1996; Ghura, 1998). This erosion of the tax base has several detrimental fiscal effects. The consequences of lost revenue to the funding of public services are of special concern (Tanzi, 2000a). In addition, corruption and tax evasion may have harmful effects on economic efficiency in general (Chand and Moene, 1999; Tanzi, 2000b) and income distribution in particular (Slemrod and Bakija, 1998; Hindriks *et al*., 1999).

In order to increase revenue and curb corruption, a number of African countries have implemented comprehensive reforms in their tax administrations over the past 10–15 years (Devas *et al*., 2001). Tanzania introduced a major reform in 1996 with the formation of a semi-autonomous revenue authority—the Tanzania Revenue Authority (TRA). The choice of a revenue authority model aimed partly to limit direct political interference by the Ministry of Finance and partly to free the tax administration from the constraints of the civil service system. This was considered to be essential for several reasons of which the most important were to attract and retain quality staff by paying rates above the civil service regulations, and to make dismissals easier. Moreover, the tax administration's senior management and many tax officers were replaced. It was assumed that these steps would provide incentives for greater job motivation and less corruption.

How successful was this reform? It is obviously too early to pronounce a final verdict, only 7 years after the Authority was put in place. Reforms need time and results always depend on the criteria underlying the evaluation. The reform appeared, however, to be a success in TRA's first year of existence. Reported revenue increased sharply—from 11% of GDP in 1995–1996 to more than 12% in 1996–1997. Corruption seemed to be declining too.

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Table 1a. Tanzania tax revenue components (in TSh billions, nominal prices)

	1994	1995	1996	1997	1998	1999	2000
Total tax revenues	220.4	299.9	385.8	514.6	566.1	616.5	685.1
Tax on imports	50.2	91.3	121.2	174.2	180.7	218.9	220.4
Tax on exports					4.7		
Sales and excise tax on domestic goods	70.4	72.6	104.7	141.7	140.5	161.3	180
Income taxes	58.5	86.7	112.3	134.2	149.8	162.9	209.7
Other taxes	41.2	49.4	45.6	64.5	90.4	73.4	75.1

Table 1b. Annual changes in tax revenues (%)

	1994–1995	1995–1996	1996–1997	1997–1998	1998–1999	1999–2000
Total tax revenues	36.1	28.6	33.4	10.0	8.9	11.1
Tax on imports	81.9	32.8	43.7	3.7	21.1	0.7
Tax on exports					−100.0	
Sales and excise tax on domestic goods	3.1	44.2	35.3	−0.9	14.8	11.6
Income taxes	48.2	29.5	19.5	11.6	8.7	28.7
Other taxes	19.9	−7.7	41.5	40.2	−18.8	2.3

Table 1c. Tax revenues (% of GDP)

	1994	1995	1996	1997	1998	1999	2000
Total tax revenues	11	11.3	11.4	12.1	10.9	10.1	10
Tax on imports	2.5	3.4	3.6	4.1	3.5	3.6	3.2
Tax on exports	0	0	0	0	0.1	0	0
Sales and excise tax on domestic goods	3.5	2.7	3.1	3.3	2.7	2.6	2.6
Income taxes	2.9	3.3	3.3	3.2	2.9	2.7	3.1
Other taxes	2	1.9	1.3	1.5	1.7	1.2	1.1

Source: Mokoro and Oxford Policy Management (2001).

But since then, tax revenue has declined to 10% of GDP in 2000 (see Table 1c). There are also clear indications that corruption is on the rise again. The key facts of the development in Tanzania's tax administration are as follows:

- *Prior to the establishment of TRA*: Widespread and systemic corruption. Low tax revenues in percentage of GDP (Table 1c).
- *Establishment of TRA*: Focus on wage incentives, control, recruitment and steps to reduce political interference.
- *Post-reform phase 1*: Low(er) corruption levels. Sharp annual growth in tax revenue (Tables 1b and 1c).
- *Post-reform phase 2*: Rising corruption levels. Declining revenue in percentage of GDP (Table 1c).

The purpose of this article is to explore in greater detail, factors that may explain this pattern of corruption within TRA and, to a lesser extent, to shed light on revenue trends.[1] Rising levels of corruption may help explain why the growth in revenue has tailed off in recent years (see Table 1c).[2] But there are clearly other explanatory factors also at work. First, tax revenue depends on external factors over which the tax administration has no control, for instance, impact of general economic trends on tax bases such as income tax, VAT and import duties. Import restrictions and politically allocated tax exemptions for different sectors and businesses also contribute

[1]This pattern, initial increases in revenue collection followed by stagnation or decline, is not atypical for tax administrative reforms in Africa as the experiences from Ghana and Uganda show (see Chand and Moene, 1999; Hadler, 2000; Therkildsen, 2002). According to Taliercio (2001), similar developments are observed in several Latin-American countries.

[2]One should be careful in drawing too confident a conclusion about successes and failures on the basis of the tax-to-GDP ratio since it tends anyway to be a relatively imprecise measure of performance (see Stotsky and Wolde Mariam, 1997). However, increase in revenues has been the major performance criterion publicly announced by the Government, clearly reflected in the budget speeches of the Minister of Finance.

to reducing the tax base.[3] Furthermore, staff productivity may have changed possibly due to falling motivation caused by, for instance, declining real wages. However, there are many indications that an increase in fiscal corruption has contributed to reducing the growth in reported revenues. Thus, a closer look at the pattern of corruption may shed light on the development of tax revenues.

Reliable information on corruption and tax evasion levels is obviously hard to come by. Given the sensitive issues at stake, one cannot work towards an understanding of the phenomena discussed in this article by the standard methods of random sample, structured questionnaires and formal interviews.[4] A combination of informal and formal methods is often required. This analysis is therefore based on a variety of sources of information collected during a series of fieldwork between 1996 and 2002: official reports and data on tax revenues and the TRA; available grey literature produced by the Government, the TRA itself, donors and business communities; personal interviews and discussions with present and past TRA staff and board members, staff at the Ministry of Finance, business people and customs clearing agents in Dar es Salaam, aid workers, tax consultants and researchers; and newspaper articles on Tanzania tax issues.

The remaining part of the article is divided into five sections. The first Section describes the state of affairs in the tax administration in Tanzania prior to the establishment of TRA. Factors identified as crucial in explaining the extent and types of corruption in the tax administration are reviewed in section two. The administrative reforms are discussed in section three, while their results are presented in section four. Finally, section five concludes and examines lessons learned from this case study which could benefit future reforms of tax administrations in poor countries.

CONDITIONS PRIOR TO THE ESTABLISHMENT OF TRA

Corruption is not a new phenomenon in Tanzania. According to Mukandala (1983, p. 261), the public sector in the early 1980s was 'increasingly riddled by corruption and embezzlement of public funds'. The Auditor General's reports from the 1980s show that this trend continued (Semboja and Therkildsen, 1992, p. 1103). By the mid-1990s, corruption in Tanzania was rampant in all sectors of the economy and politics (URT, 1996a). In tax administration, these issues were particularly worrying given the need to raise more tax revenues, but also to mitigate corruption in other parts of public services.

Extensive corruption and embezzlement of public funds are documented in a number of reports from both commercial and official sources. For instance, the Confederation of Tanzanian Industries (CTI) estimated that the value of lost revenues from customs and sales tax due to inefficient tax administration and misclassification and undervaluation of imported goods amounted to more than TSh 250 billion for the period March 1993–March 1994 (Osoro *et al*., 1999, p. 5). According to ESRF (1996, p. 6), official import statistics underreported the value of imports by as much as 70%. One indication of the extent of this problem is that some types of textiles (including those used in the most popular type of clothing, the 'khanga') were sold in the early 1990s for 30% less than the value of the customs duty per metre of the textile. Official statistics on reported revenue from customs duties also indicate large leakages. While the most commonly applicable import duty rate was 30% during 1988–1994, the customs tariff generated a revenue equivalent to less than 6% of the official import value during that period (Gandhi *et al*., 1995, p. 15).

Evasion of other types of taxes was also widespread. For sales tax and excises on domestic goods, underreporting of production volumes was a common form of evasion (Osoro *et al*., 1999, p. 6). With regard to corporate taxes, underreporting of profits and falsified tax deduction claims were common (Mwinyimvua, 1996). In both cases, such underreporting could be achieved with or without the help of staff within the tax administration. For personal income taxes, including pay-as-you-earn (PAYE), one method used by employers to evade taxes was not to report

[3] There has been a considerable increase in the use of tax exemptions in Tanzania in recent years, which obviously erodes the tax base, at least in the short run. For instance, generous investment incentives in the form of tax exemptions have been granted to foreign investors, especially in the mining and tourism sectors (Mokoro and Oxford Policy Management, 2001).

[4] Wade (1982) provides an excellent account of methodological challenges and approaches for analysing systems of corruption in public sector institutions.

taxes collected from employees to the tax authorities. Another was to pay wages and other cash emoluments to workers 'under the table'. But the discrepancies between potential and reported tax revenue could also be due to plain and simple theft. For instance, TCCIA (1995, pp. 22–23) reported that embezzlement of collected taxes by tax collectors and administrators—which did not implicate taxpayers—was widespread. It was caused by poor control routines in the tax administration. In some cases, the tax inspectors and auditors were also involved in corruption.

Evidence of the amount of taxes and duties lost to the treasury was extensive. Surprisingly, the donor community did not react until Autumn 1994. A report from two of the Pre-Shipment Inspection (PSI) companies in charge of the pre-imports inspection and valuation of cargos to Tanzania then revealed that lost tax revenues in the form of unpaid customs duties amounted to TSh 70 billion (then equivalent to US$ 134.5 million) in the fiscal year 1993–1994 (*The Indian Ocean Newsletter*, No. 647, 19 November 1994, p. 1). In comparison, recorded customs revenues in that same year were TSh 28.4 billion (Gandhi *et al.*, 1995, p. 10). In other words, lost customs revenues represented an amount 2.5 times higher than reported customs duties. This revelation led to an aid freeze to Tanzania in November 1994. Several major donors, including Norway and Sweden, decided to withhold aid while they awaited the results of investigations of what was assumed to be corruption involving senior officials. The Government promised a full-scale investigation into the matter.

On 23 February 1995, the Office of the Controller and Auditor General submitted its report to the President. The report exposed negligence and dishonest practices by high-level civil servants (*The Indian Ocean Newsletter*, No. 661, 4 March 1995, p. 1). Of the total amount of TSh 70 billion that could not be accounted for, TSh 20 billion could be put down to tax evasion by importers, while TSh 50 billion was due to tax exemptions. Of the latter, legal exemptions granted to public institutions and religious and humanitarian organisations made up a substantial share, but a large number of cases were found to be illegitimate exemptions granted to various businesses by the Ministry of Finance.

According to Osoro *et al.* (1999, p. 28), 'the third schedule of the Customs Tariff Act and a number of Government notices which allow for exemptions [was] probably the most abused section of tax legislation'. Within the Ministry of Finance, the *Revenue Department* went under the nickname the 'Tax Exemption Department'. In response to pressure from Western donors, the Minister of Finance Kighoma Malima was removed from his post in the spring of 1995 and installed in a new ministerial position. In June that year, he was forced to resign from the Government altogether. The investigations also led to the dismissal of several senior civil servants in the Ministry of Finance, including the head of the revenue department.

FACTORS LEADING TO PERVASIVE CORRUPTION

The corruption scandals in the tax administration were instrumental in President Benjamin Mkapa's decision to establish a *Commission on the Causes of Corruption in Tanzania*. The commission was appointed in January 1996 with a mandate to map the extent of corruption in the country and identify steps to deal with it (URT, 1996a, pp. i–iii).

Investigations identified four factors as keys to explaining the extent and types of corruption pervasive in the Tanzanian tax administration:

- *Political intervention*. This generally took place in the form of discretionary tax exemptions granted to business people who were willing to pay and/or had the 'right connections' (URT, 1996a, pp. 307–311).
- *High tax rates and complicated regulations*. The potential gain from involvement in corruption could be considerable, both for officials and taxpayers. Relatively high rates and a complex and partly incoherent set of rules, especially for customs and corporate taxes, resulted in large potential rewards for taxpayers willing to bribe to cut their own tax burden and/or speed up customs clearance of their goods (URT, 1996a, pp. 291–295, 316–329). For customs officials, the bribes taken for clearing specific containers in Dar es Salaam harbour could be as much as a whole year's salary. In general, the system gave tax officials considerable discretionary powers.
- *Poor pay and working conditions*. The low wage levels at the tax administration compared to the private sector invited corruption. The average public employee's salary including allowances in the early 1990s was sufficient

to cover only about 40% of normal household expenditures (Mans, 1994, p. 378). Moreover, working conditions were characterised generally by a lack of technical equipment and poor office facilities, as well as unclear criteria for recruitment, promotion and rewards (URT, 1996a, pp. 100–117, 281).

- *Low probability of detection and punishment for corruption*. Internal auditing and monitoring functions had become for the most part non-operative and ineffective (Cunningham, 1996; URT, 1996a, p. 50). For instance, the internal operational auditing unit in the Customs Department at the head office in Dar es Salaam had only four staff members in early 1996 and five persons for the whole Dar es Salaam region, where about 80% of the total customs revenues in Tanzania are collected. Responsibility for internal auditing was therefore outsourced to external auditors from the Office of the Controller and Auditor General, which stationed on a permanent basis six–seven people at the customs administration. But this compromised, of course, their independence and opened up for collusion between auditors and tax officers. According to Cunningham (1996, p. 66), these auditors were 'part of the system and the peer network to be inspected'. Audits were further crippled by low skills. The auditing staff lacked the training in auditing and inspection methods, and the required equipment and basic facilities to perform controls. In practice, the probability of being detected and punished for corruption was virtually non-existent.

THE FOUNDING OF TRA

The crisis riddling the tax administration was the immediate cause behind the formation of the Tanzania Revenue Authority (TRA). TRA became operational from 1 July 1996. Its objective was to reach a given revenue target, expressed as a given ratio of tax revenue to GDP. This target would be revised annually in the Finance Minister's budget speech.[5] *The Indian Ocean Newsletter* (No. 726, 6 July 1996, p. 1) wrote on this occasion that 'a beginning has been made in tackling the country's two major ills: corruption and tax evasion'.

A key element of the administrative reform was to move the existing revenue departments out of the Ministry of Finance into a semi-autonomous revenue authority.[6] The philosophy behind this move was twofold: first to eliminate the direct political influence of the Ministry of Finance on the day-to-day operations of the tax administration. And second, to raise the salary of tax officials without parallel increases for the rest of the public sector. A revenue authority, established outside the civil service system, is not, in principle, bound by wage rates and employment regulations that apply to other sectors of government (see Devas *et al*., 2001, p. 214). This means that the institution can pay rates which enables it to attract and retain highly qualified staff. In TRA, this involved dramatic increases in pay rates—for some categories of staff up to ten times higher than corresponding positions in the civil service. Further emphasis was laid on strengthening accounting and internal monitoring systems and curtailing the opportunity of tax officers to deal with cases on the basis of their own discretion. The general scarcity of qualified accountants, lawyers and IT-experts in Tanzania meant, however, that these groups at TRA would be equally sparse. Finally, steps were taken to improve working conditions for employees by improving offices, expanding computer services, purchasing service vehicles etc.

To ensure a sense of 'local ownership' to the reforms, efforts were made to fill board and executive management positions with Tanzanians. Persons recognised for their integrity and past good performance were appointed as Chairman of the Board and as Commissioner General. The rest of the executive management was generally recruited from outside the system, most from jobs in government-owned enterprises. Exceptions were the Commissioner for Tax Investigation and the Commissioner for Customs, who were both already employed in the tax administration.

[5]Revenue targets are set on the basis of negotiations between the TRA and the Ministry of Finance (URT, 1998, p. 5). Moreover, the Research and Policy Department of the TRA plays the policy role of setting collection targets for TRA revenue departments, once the total tax revenue budget has been agreed with the Ministry (Mokoro and Oxford Policy Management, 2001, p. 18). This arrangement indicates a strengthening of the tax bureaucracy at the expense of politicians. Caulfield (2002) provides an interesting analysis on how recent public sector reforms in Tanzania may have strengthened the hand of bureaucrats such that, without enhanced mechanisms of accountability and political control, the potential for rent-seeking is high.

[6]The main functions of the TRA, its organisational structure, composition of the board, etc. are detailed in URT (1995, 1998); and TRA (1999). See also www.tra.go.tz

Table 2. TRA staff dismissed for misdemeanours

	1995–1996	1996–1997	1997–1998	1998–1999	2000–2001
Staff at start of fiscal year	3365	2201	1962	1927	1897
Dismissed	1164	239	35	30	24
Percentage dismissed	35	11	1.8	1.6	1.3

Source: World Bank (2001, p. 28).

Drastic measures were put in place to break the 'culture of corruption' in the administration. All former staff members were dismissed and had to re-apply for a position at the new TRA. More than a third (35%) were rejected on evidence or suspicion of misconduct (see Table 2). Almost 1200 earlier staff members, of whom 500 were former customs officers, were not re-employed. All new employees were given a 1-year probation period before being accepted on a permanent basis. Staff had to report their private financial circumstances, including wealth, on starting. Furthermore, a new unit was set up for internal investigation and monitoring. The first board of TRA, chaired by Professor Benno Ndulo (1996–1998), played an essential role here by virtue of its autonomy, integrity and expertise. The accountability relationships between the board and the Ministry of Finance also seemed to work effectively during this period (Clarke and Wood, 2001, p. 84).

HOW DID THE ADMINISTRATIVE REFORMS WORK?

Developments after the founding of TRA can be divided into two periods. The first was characterised by decreasing corruption and a sharp increase in tax revenue. As already indicated, the trend reversed, corruption seemed to increase and growth in revenue declined. In what follows, these changes in corruption levels over the two periods are explained.

Phase 1 (1996–1997)

In the first year of TRA's operations, tax revenues grew by more than 30% compared to the previous fiscal year (Table 1b). Since there were only minor changes in the tax structure (rates and bases) and external conditions in this period, the growth in revenue must have been mainly due to the efforts of the tax collectors and other officials at TRA.[7]

It may also suggest that the internal control mechanisms worked. During the probation period (1996–1997), 239 staff members were dismissed (Table 2). A survey of taxpayers in Dar es Salaam also concludes that corruption shrank during the first year (PriceWaterhouseCoopers, 1998). But, according to the respondents, at the same time as the *number* of corrupt acts fell, the *price* per bribe rose (ibid., p. 3). Since there is no evidence that the demand for corrupt services grew during the period, the most plausible explanation is that tax officers who were willing to take bribes considered it more risky than before, and, thus, incorporated a 'risk premium' in the bribes. According to the PriceWaterhouseCoopers' study, the most corrupt staff members during this period were junior officers. Interviews with business people in Dar es Salaam confirmed this observation. This may imply that younger staff members were more inclined to accept a higher risk, or that they acted as agents for players higher up in the tax administration and then shared the 'proceeds' with them.[8]

Phase 2 (1997–2002)

After the initial success, tax revenues have dropped in percentage of GDP (Table 1c). Moreover, a new increase in corruption and tax evasion set in (Osoro *et al*., 1999, p. 36). In particular, corruption seems to be growing at the middle and lower levels of TRA (Waller, 2000). According to taxpayers interviewed, there is also an increase in the

[7]In the Budget Speech for financial year 1996–1997, the Minister of Finance focused on implementing measures to improve efficiency in revenue collection, in particular legal and administrative measures against tax evasion and corruption (URT, 1996b, pp. 59–63).
[8]URT (1996a, p. 284) reports that such mechanisms were in place in the previous tax administration too.

number of tax collectors, *openly* demanding bribes after presenting taxpayers with unreasonably high assessments (ibid., Appendix 2, Section 9.2). How can this relapse be explained? Five factors may contribute to shed light on this development:

- probation period;
- declining real wages;
- group dynamics and social obligations;
- corruption networks; and
- social distance between staff and management.

Firstly, one explanation could be that the first year's success was due to the fact that most employees were working on a probation basis and, additionally, had yet to learn how the new system worked (TRA, 1997). So although their attitudes to corruption may not have changed, it was perceived to be more risky to get involved at that stage in corrupt dealings. Tax officers did not know how the internal control mechanisms worked, or how the top management would execute the rules and whether they stood in danger of losing prospects of a permanent job. These points were also confirmed in interviews with present and former TRA staff. It was stressed that many employees in the operational departments used their probation period to 'study' how the system worked: 'sitting on the fence waiting for better times'. Later, it was shown that some staff at TRA's Internal Investigation and Monitoring Unit (IIMU) were willing to take bribes to turn a blind eye to corruption. Rumours of corruption in the IIMU were circulating as early as 1997, but it was not until December 2000 that the TRA management and board took action, resulting in 24 IIMU officers, including the head of the unit, being 'retired in the public interest'.

Secondly, despite a dramatic increase in pay rates compared with normal rates in the public sector, it was not enough to compensate for the potential gains from corruption (URT 1996a, p. 285): 'For a 'Long-Room' employee who is used to get bribes of TSh 20–30,000 daily, a tenfold increase of his salary from the present level will not make him desist from demanding and accepting bribes'. The situation worsened even more due to the erosion by inflation of the initial pay rates for TRA staff, since nominal wages between 1996 and 2000 remained unchanged.[9] It is therefore no surprise that the wage reforms seem to have had limited impact on restraining the extent of corruption in the tax administration. But, irrespective of wage rates, the tax administration remains a very attractive workplace. According to the Commissioner for Human Resources and Administration, TRA receives hundreds of applications for every advertised vacancy. The tax collection departments are particularly attractive. There is also considerable internal competition within TRA for vacancies in the operational departments. The 18% increase in salaries of TRA-staff in 2001, may, thus, prove to have only minor impacts on motivation (ESRF and FACEIT, 2002, p. 63).

Thirdly, the assumption that higher salaries will boost productivity over time is most likely exaggerated. It is a well-known fact in sociological management theory that workplaces are social environments and that people in these are motivated by much more than pure economic self-interest (Gillespie, 1993). Recent economic research on human behaviour also indicates that reformers and economists have an inclination to exaggerate the impact of monetary incentives because of a too narrow understanding of intrinsic motivation and group dynamics (see Frey, 1997). An additional aspect of wage incentives that has received little attention in connection with institutional reforms in Africa is associated with the role of family networks and obligations. Increased pay rates may imply more extensive social obligations, resulting actually in a net loss to the individual. This state of affairs can develop into a vicious circle with higher wages leading to more corruption because the tax officer has to make up for the loss caused by such obligations.[10]

Another explanatory factor is linked to the impact of corruption networks. Research shows that corruption in public institutions has often been conducted by reasonably well-organised networks, where trust and reciprocity is found between network members (Rose-Ackerman, 1999; Gehlbach, 2001). Such relationships are likely to reduce

[9] Personal interview, M. E. Sila, then Commissioner for Human Resources and Administration, March 2001.
[10] This point was raised by several past and present TRA-officials interviewed. See Rose-Ackerman (1998, pp. 317–323) for a discussion of the role of traditional networks in reform processes.

transaction costs, as well as any moral costs that may arise from allowing oneself to be involved in corruption. Furthermore, the peer networks often function as 'repositories of knowledge' for members, for example, on the attitudes of the top management to corruption, how the internal monitoring unit works, and who is potentially bribable among staff members and management.

The reforms probably managed to break a few existing networks, but not to hinder new networks, within and outside TRA, from emerging. The following anecdote may illuminate this process within TRA.[11] The TRA board is responsible for appointing people to high-ranking positions, while vacancies at lower levels are taken care of by middle-level managers. Already in TRA's first year, board members were made aware of a practice in some units in TRA where applicants had to pay 'speed money' just to have their applications processed. The board suspected this to be a method of sifting applicants which ensured that only those who signalled their readiness to pay bribes—and therefore probably also a readiness to get involved with the internal corruption networks—were recruited. This indicates the emergence of an informal market for jobs in TRA.[12]

Just as intriguing is to see how new networks gradually formed connections between TRA and former employees in the tax administration. As already mentioned, about one-third of former employees in the tax administration were not given new jobs in TRA. They were considered by the new management and board to have been compromised through involvement in corrupt dealings and misbehaviour. The private sector however was attracted to many of these dismissed people due to their inside knowledge of actual working of the system. For example, former customs officers were recruited by clearing agencies or they set up their own agencies.[13] These persons had intimate knowledge of the tax administration and of loopholes etc. Since many of their former colleagues remained in the tax administration, good connections to the inside were assured.[14] It is therefore not surprising that this type of corruption network eventually managed to reverse the positive process that characterised TRA's first period.

Finally, the reforms also increased the distance between the executive management and the staff. Few in the top management of TRA had any previous experience with tax administration, in contrast to other staff members who were largely recruited from the former tax administration. The commissioners lack, in the view of a broad section of the staff, knowledge of how the organisation actually works on the ground. This may of course change in the future, and it is obviously positive that the present TRA leadership is considered to be 'clean'.[15] But it is not obvious that the *esprit de corps* among the top managers that has characterised TRA will sustain and permeate the rest of the organisation.[16] The reforms may also, to some extent, have hindered this by allowing huge differences in pay levels between the top and bottom grades.[17]

CONCLUSIONS

One lesson to be learned from TRA's first 7 years of operation is that even with relatively respectable salaries and working conditions, corruption may still thrive. The study shows that pay level is only one of several factors affecting the behaviour of tax officers. In an environment where the demand for corrupt services is extensive and monitoring ineffective, wage increases may end up functioning as an extra bonus on top of the bribes taken by corrupt

[11]Personal interview with former board member of TRA (December, 1998).

[12]According to the Warioba Report, such mechanisms also existed in the previous tax administration (URT, 1996a, p. 284). From other countries, it is known that a market for lucrative positions can emerge in public institutions that pay wages considerably over the market rate, where those with the capacity to pay the most get the jobs (see Andvig, 1999).

[13]Since 1995–1996, a total of 1492 employees of the tax administration have been dismissed (Table 2). Of these, 656 came from the Customs Department (*Business Times*, 21–26 September 2001).

[14]An employee in the Research and Policy Department of TRA referred to these former tax collectors as 'ticking bombs', loaded with potentially dangerous information and knowledge about TRA (personal interview, March 2001).

[15]These opinions emerged from personal interviews with business people in Dar es Salaam.

[16]In July 2002, the TRA Board declined to renew the contracts of six members of the top management team, including the Secretary of the Board and Chief Counsel, the Commissioner for Human Resources and Administration and the Acting Commissioner for Tax Investigation (*Daily News*, 26 July 2002). Moreover, several heads of department received an extension of their contracts with only 6 months against the 'normal' tenure of office of 3 years.

[17]A similar situation prevails in the Uganda Revenue Authority (URA), where the internal wage compression rate is 34, that is, equivalent to a wage gap of 3300% between the top and bottom grades (personal interview, Commissioner for Personnel at URA, June 2000).

officers. The situation requires strong internal control mechanisms and effective sanctions that make it easier to dismiss staff.

Moreover, the study shows that hiring and firing procedures may lead to more corruption. Corrupt tax officers often operate in networks, which include both internal and external actors. The way the administrative reforms were implemented, where many of those dismissed were recruited to the private sector due to their knowledge of the workings of the tax system and their inside contacts, may have strengthened the corruption networks. Thus, a major challenge facing reformers of tax administrations is to crack corruption networks and the inherent trust that appears to prevail between members of such networks. One suggestion is to introduce rotation systems for staff in tax administrations, where tax collectors remain only for shorter periods in the same post (Das-Gupta and Mookherjee, 1998). But a danger of the rotation system is that the uncertainty which is thereby created for employees may result in increased corruption, as collectors may use the opportunity to try enriching themselves while they are stationed in the most ‘lucrative’ posts. The rotation of officials may also give corrupt superiors undue power (URT, 1996a, pp. 284–285). For instance, they might ‘sell’ assignments to attractive positions or reassign officials to remote stations as a punishment for honesty (Rose-Ackerman, 1999, p. 84). The scarcity of qualified personnel like auditors and accountants further reduces the potential of rotation schemes in the poorest countries.

Furthermore, partial reforms may soon run into difficulties (Tanzi and Pellechio, 1997). Despite quite comprehensive changes in the tax structure (rates and bases) after 1998, the tax system in Tanzania is still complicated and non-transparent (World Bank, 2002, pp. 133–137). Tax legislation is unclear and causes random and partly ad hoc collection procedures (Luoga, 2002). Assessors are considered to have wide discretionary powers to interpreting tax laws, for instance, to allow or disallow expenses or charges, or to exempt import duty on items imported (ESRF and FACEIT, 2002, p. 62). Reforms of tax legislation and procedures, including measures to improve transparency in the taxpayer–tax officer relations, should therefore take place concurrently to reduce opportunities for corruption and the demand for corrupt services. If not, one faces the risk that the administrative reforms will leave behind them not only a highly paid, but also highly corrupt civil servants.

But the successful implementation of such reforms requires political will to back them up (Tanzi and Pellechio, 1997; Rose-Ackerman, 1999). An indication of the limited political will power to fight fiscal corruption and tax evasion is the rise in tax exemptions granted in recent years. While exemptions accounted for 15.2% of total tax revenues (actually collected tax plus exemptions) in 1996–1997, this percentage grew to 37% in 1998–1999 (Mokoro and Oxford Policy Management, 2001). Experience has shown that tax exemptions create room for bribery and corruption, reduce the tax base and increase loopholes for tax evasion (URT, 2002, p. 19). In the 2002–2003 budget, however, the Government discontinued customs duty exemptions for public sector imports of goods and services. This is a step in the right direction. But, many openings remain to abuse the system. The removal of tax exemptions, including those granted to aid organisations and their employees, would help boost the credibility of both the authorities and the donors in relation to anti-corruption measures and, at the same time, contribute to widening the tax base and simplifying the tax system.

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Corruption in tax administration.
Lessons from institutional reforms in Uganda

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SUMMARY
The Uganda Revenue Authority, established in 1991, is the oldest integrated revenue authority in sub-Saharan Africa. The revenue authority model aimed to limit direct political interference in day-to-day operations by the Ministry of Finance and to free the tax administration from the constraints of the civil service system, especially by paying salaries above civil service pay scales and to more easily recruit, promote and dismiss staff. Such steps were expected to provide incentives for greater job motivation and less corruption. After marked success in the first years after its creation, revenue has dropped as a share of GDP, and corruption is believed to be pervasive. The paper shows that the establishment of the URA with comparatively generous remuneration packages and substantial budgets has not protected it from political interference. To the contrary, it has made the revenue administration a more attractive target because the authority offers both relatively well paid jobs and considerable rent-seeking opportunities. Further, the paper argues that the motives of individual actors are often inextricably tied to the interest of the social groups to which they belong. Tax officers are often seen by their families and networks as important potential patrons who have access to money, resources, and opportunities that they are morally obliged to share. People in positions of power are expected to use that influence to help their kin and community of origin. Hence, increased salaries may lead to increased social obligations, which again may push tax officers into taking bribes to accommodate the growing expectations around them. This implies that such social relations may rule out the formal bureaucratic structures and positions. Fiscal corruption must therefore, at least to some extent, be understood in the context of a political economy in which access to social resources depends on patron clientilism. If these problems, which are rooted in social norms and patterns of behavior rather than administrative features, are overlooked, the result may be to distort incentives. As a consequence, reforms that otherwise seem consistent with principles of good public administration may be undermined.

JEL classification: D73, H26, H30, J33, K42, Z13

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Introduction

Over the past two decades many developing countries have implemented comprehensive reforms of their tax administrations in order to increase revenue and curb corruption. This chapter examines recent experiences in the fight against corruption in the Uganda Revenue Authority (URA). It argues that the technocratic remedies supported by donors have underplayed the degree to which progress in tax administration depends upon a thorough "cultural change" in the public service. The motives of individual actors are often inextricably tied to the interests of the social groups to which they belong. In the URA, patronage runs through networks grounded on ties of kinship and community origin. As such, people recognize the benefits of large extended families and strong kinship ties, even as their social and economic aspirations may be indisputably modern. This implies that such social relations may undermine formal bureaucratic structures and positions. If these problems, which are rooted in social norms and patterns of behavior rather than in administrative features, are overlooked, the result may be to distort incentives. As a consequence, the government's commitment to reforming the tax administration may also be undermined.

In most developing countries national tax collection is carried out by line departments within the Ministry of Finance (MoF). However, over the past two decades more than 20 developing countries, especially in Latin America and Africa, have established revenue authorities whereby the tax administration function is moved out of the Ministry of Finance and granted to a semi-autonomous entity (Devas, Delay, and Hubbard 2001; Taliercio 2004).[1] Although each country that has established a revenue authority has done so under differing circumstances, there are some general patterns with respect to underlying political and economic circumstances. First, governments have been greatly dissatisfied with the performance of revenue collection, especially in the face of fiscal deficits and expanding public expenditure needs, and with the chronic inefficiencies of the existing tax administration arrangements placed in the Ministry of Finance (Mann 2004). Second, perceptions of widespread corruption and tax evasion, combined with high taxpayer compliance costs, led to calls for wholesale reform of the tax administration (Barbone, Das-Gupta, Wulf, and Hansson 1999; Ghura 1998). Third, in some aid-dependent African countries the shift to a semi-autonomous revenue authority model was also attractive to foreign donors because it created opportunities for more widespread reforms of the tax administration (Therkildsen 2004).

The revenue authority model is designed partly to limit direct political interference in day-to-day operations by the Ministry of Finance and partly to free the tax administration from the constraints of the civil service system (Devas et al. 2001; Taliercio 2002). A revenue authority is not meant to be as autonomous as a central bank or as dependent as departments in line ministries. It is "semi-autonomous."[2] But a revenue authority is meant to be quite independent of the financing and personnel rules that govern the public sector in general. A semi-autonomous revenue authority (SARA) can in principle recruit, retain, and promote quality staff by paying salaries above civil service pay scales, and can also more easily dismiss staff. Such steps are expected to provide incentives for better job performance and less corruption. Moreover, a single purpose agency is meant to integrate tax operations and focus its efforts on collecting revenues more effectively than is usually possible under civil service rules.

Studies from a number of countries in Latin America (Taliercio 2002, 2004; Mann 2004) and Africa (Chand and Moene 1999; Fjeldstad 2003; Hadler 2000; Terpker 1999; Therkildsen 2004) show that the reforms appeared to be successful in the initial years. But the initial successes were in many cases not sustained. The first years after the establishment of a SARA often witnessed sharp increases in revenues. Reported corruption also seemed to decline. Thereafter, revenue enhancement stagnated and in some countries revenues as a percentage of GDP dropped. There are also clear indications that corruption is on the rise again in many revenue administrations, especially in Africa (Waller 2000). This pattern, initial increases in revenue collection followed by stagnation or decline, often took place despite continued economic growth, reforms of important tax legislation in line with "best practices" as prescribed by the IMF, and accumulated operational experience in the new revenue administrations.

This chapter examines the experiences of the Uganda Revenue Authority (URA) in controlling fiscal corruption. The URA, established in 1991, is the oldest integrated revenue authority in sub-Saharan Africa.[3] Hence, it is possible to assess the reform initiative on the basis of developments over a relatively long period of time. The reform appeared to be a success in URA's first years of existence. Reported revenue increased sharply – from 7 percent of GDP in 1991 to around 12 percent in 1997 (Katusiime 2003). Corruption also seemed to decline. During this period many observers referred to the URA as a model for other sub-Saharan African countries (Barbone et al. 1999; Silvani and Baer 1997; World Bank 1997). Unfortunately, since then, URA has failed to meet its targets and revenue has dropped as a percentage of GDP amid accusations of increasing corruption.[4] An evaluation commissioned by the British Department for International Development (DFID) points to the continued public perception of a high level of corruption, reflected in the widespread availability of "duty free" goods on local markets and arrests of senior URA officers (EME 2000, p. 20). The Ugandan government seems to support this view. For instance, in March 2000 President Yoweri Museveni is reported to have called the URA "a den of thieves" (Therkildsen 2004, p. 82). Likewise, in March 2003 the former Commissioner General of the URA, Annebritt Aslund, listed corruption as "problem number one" in the organization.[5] Frequent media reports support the perception that corruption is endemic in the URA.

Rising levels of corruption may help explain why the growth in revenue has tailed off in recent years.[6] But there are clearly other explanatory factors at work as well. First, tax revenue depends on external factors over which the tax administration has no control. For instance, general economic trends affect tax bases such as income tax, value-added-tax (VAT), and import duties. Import restrictions and politically allocated tax exemptions for different sectors and businesses also contribute to reducing the tax base. Furthermore, staff productivity may have changed, possibly due to falling motivation – whether this is unrelated to, causes, or is caused by an increase in corruption is not known. However, there are many indications that an increase in fiscal corruption has contributed to the drop in reported revenues as percentage of GDP. Thus, a closer look at the pattern of corruption may shed light on the development of tax revenues.

Reliable information on levels of corruption and tax evasion is obviously hard to come by. Given the sensitive issues at stake one cannot work towards an understanding of the phenomena discussed here by the standard methods of random sample, structured questionnaires, and formal interviews. A combination of informal and formal methods is often required.[7] This analysis, therefore, is based on a variety of sources of information collected during fieldwork in Uganda: official reports and data on tax revenues; available grey literature produced by the government, the URA, donors, and business communities; personal interviews and discussions with present and past tax officers and board members of the revenue authority, staff at the Ministry of Finance, business people and customs clearing agents in Kampala, aid workers, tax consultants, and researchers; and newspaper articles on tax issues and the URA.

The next section describes the state of affairs in the tax administration in Uganda prior to the establishment of the URA. The following section examines key elements of the tax administrative reform. I then focus on patterns of corruption in the URA and seek to determine which factors are crucial in explaining the extent, types, and causes of corruption in the tax administration. Finally, the chapter concludes with a discussion of ways to improve URA's performance in a situation where the broader social, political, and economic environment, as well as the public sector in general, is seriously detrimental to good performance.

Factors leading to the establishment of the URA

Preliminary work on reforming the Ugandan tax administration began soon after the downfall of the Idi Amin regime in 1980. Over the next ten years at least two government commissions and three consultancy studies dealt with the problem of tax administration in the face of increasing fiscal problems (Republic of Uganda 1983; Ministry of Finance 1989; Republic of Uganda 1990; CLD 1991). Together these reports describe "the decline of a previously highly regarded Ugandan civil service into a sorry state of inefficiency, irresponsibility, indiscipline and corruption" (Therkildsen 2004, p. 68).

The reports identified four main causes of poor tax administration:

- <u>Lack of taxpaying culture among taxpayers.</u> This was partly caused by a tax system perceived as unfair. Relatively high rates and a complex and partly incoherent set of rules, especially for customs and corporate taxes, resulted in large potential rewards for taxpayers willing to bribe to cut their own tax burden and/or speed up customs clearance of their goods.

- Low wage levels. The poor salaries at the tax administration compared to the private sector invited corruption. The average public employee's salary in 1989 was about 20 percent of the corresponding salary in the private sector, and was only 5 percent for unskilled staff.
- Poor working conditions and little encouragement for staff to exercise initiative. Working conditions were generally characterized by a lack of technical equipment and poor office facilities. Moreover, the criteria for recruitment, promotion, and rewards of staff and management were unclear and subject to substantial discretion.
- Low probability of detection and punishment for corruption. Internal auditing and monitoring functions had become for the most part non-operative and ineffective due to weak management and poor information. In practice, the probability of being detected and punished for corruption was virtually non-existent.

The suggested remedies were first and foremost increased salaries and better management. According to Ole Therkildsen (2004, p. 68), the idea for the establishment of a revenue authority was inspired by the IMF and by experiences from Ghana. The arguments for an autonomous revenue authority were (Harvey and Robinson 1995, pp. 48-9):

> [B]y moving away from civil service terms and conditions of service and management practices …many…problems can be overcome. In particular, with higher salaries staff will not need to seek alternative sources of income; coupled with stricter discipline this should reduce corruption, increase morale and productivity and thus the revenue intake.

It was expected that the revenue authority model would provide "stronger and more effective management of staff and resources, supported by better facilities and information and with adequate checks and auditing of both staff and taxpayers" (CLD 1991, executive summary).

Key elements of the tax administration reform

The Uganda Revenue Authority (URA) was set up on 5 September 1991 by the Uganda Revenue Authority Statute No. 6 of 1991 as a central body to assess and collect specified tax revenue, to administer and enforce the laws relating to such revenue, and to account for all the revenue to which those laws apply. In practical terms, the main objective of the URA was to reach given revenue targets, expressed as a ratio of tax revenue to GDP. These targets were to be revised annually on the basis of negotiations between the URA and the Ministry of Finance and reflected in the Finance Minister's budget speech. The URA was also required to advise the Government on matters of revenue policy.

A key element of the administrative reform was to move the existing revenue departments out of the Ministry of Finance into a semi-autonomous revenue authority overseen by a fairly independent Board of Directors.[8] The objective behind this move was mainly to provide incentives for the staff to improve its performance and thereby increase revenues. A revenue authority, established outside the civil service system, is not bound by wage rates and employment regulations that apply to other sectors of government (Devas et al. 2001, p. 214). This meant that the URA, in principle, could pay rates which would enable it to attract and retain highly qualified staff. Hence, the consultants involved in setting up the URA recommended that management and professional staff remuneration should be competitive with the private sector (Therkildsen 2004, p. 71). Other staff should be paid a "living wage". Accordingly, they recommended a pay increase of up to 1,800 percent for low-level staff and 600 percent for mid-level staff. However, because commissioners in the Ministry of Finance were already very well paid compared to the private sector and also received generous tax-free benefits, a pay decrease of 30 percent was suggested for this category. These suggestions implied a dramatic decrease in the compression rate (that is the pay difference between the top and bottom positions in the organization). The pay for the top positions would decrease from the excessive 729 times the pay at the bottom in the MoF to 34 times in the new URA (ibid). Although these recommendations were only partly implemented, the staff that moved to the URA received dramatic increases in pay rates – some categories of staff received salaries that were 8-9 times higher than salaries for corresponding positions in the civil service.

The reform also strengthened accounting and internal monitoring systems and curtailed the opportunity of tax officers to use their own discretion in dealing with cases. The general scarcity of qualified accountants, lawyers, and IT-experts in Uganda meant, however, that the URA would also have only small numbers of these professionals. Finally, working conditions for employees were improved by upgrading offices, expanding computer services, purchasing service vehicles, and so on. Thus, the initial focus was mainly on internal matters; less attention was paid to the URA's external relations.

Drastic measures were put in place to break the "culture of corruption" in the administration. All former MoF revenue staff, including the revenue commissioners, were transferred to the URA and employed on a probation basis (Therkildsen 2004. p. 70). During the probation period everybody was screened. Out of the approximately 1,700 people who had worked in the former revenue departments of the MoF, some 200 tax officers and 40 secretaries were dismissed during this exercise, a screening process in which the Board was heavily involved. The Customs and Excise Department registered the largest number of staff dismissals. This created "shock waves" among those who were left. Moreover, after one year of operations only two out of eight top-level positions were occupied by Ugandans (ibid).

The hiring of expatriates was initially pushed by foreign donors who were heavily involved in financing the administrative reform through technical assistance. Hence, the first Commissioner General (1991-97) was a Ghanaian, and later (2001-2004) the URA was led by a Swede. The idea behind the use of expatriates was that it would contribute to improved professionalism and integrity. When the Swedish born Commissioner General, Ms. Annebritt Aslund was appointed in 2001, President Museveni is reported to have remarked that she came from a "very distant tribe" (Taliercio 2002). Given tribal interests and the prevalence of patronage in the public sector, the President thus indicated that it was necessary to hire an outsider in order to undertake serious reform of the tax administration.

The autonomy of the original Board of Directors led to conflicts between the Board, the Ministry of Finance, and the Commissioner General (CG). The statute set up conflicting responsibilities for the Board, which was responsible for both the formulation and implementation of the policy of the URA. Moreover, the Ministry of

Finance came to see the Board as problematic, partly because powerful members of the Board who were not appointed by the Ministry disagreed with the Ministry in some cases, and partly because the Ministry perceived that the Board did not possess the required technical expertise on taxation matters. Thus, when the statutes were amended in 1998, the Ministry of Finance's primacy as tax policy organ became more clearly established and the Board became less independent (Therkildsen 2004, p. 69).[9]

Under the legislative changes in 1998 the MoF increased its presence on the Board by controlling four out of seven seats, as opposed to four out of nine under the original statute. To provide for taxpayer representation, Parliament also gave the Uganda Manufacturers Association (UMA) a seat on the board. As a consequence, the role of the Board changed from the being responsible for the formulation and implementation of the policy of the revenue authority to being responsible for monitoring the revenue performance of the authority and for determining the policies related to staffing and procurement. The Board also received more powers vis-à-vis the Commissioner General (CG) to intervene in staffing matters. Furthermore, it was responsible for complying with any directives given by the Minister of Finance. Consequently, these legislative changes, which implied that the Minister of Finance appointed the majority of the members of the Board and also gave directives to the Board, laid the foundation for conflicts between the Board (i.e. the MoF) and the CG. In practice, the new legislation gave day-to-day management authority, especially in staffing matters, to both the Board and the CG.

Corruption in the URA

Although the level of corruption was perceived to drop during the initial phase, corruption has been considered a problem in the URA since its outset. For instance, a survey conducted in Kampala in 1993, two years after the authority was established, revealed that there was "a general impression that URA is a corrupt institution, high-handed and inconsiderate" (Zake 1998, p. 77). In a household survey covering the period 1995-97, the URA was rated as relatively corrupt – less corrupt than the courts and the police, but worse than the health services and local government (Cockcroft and Legoretta 1998). Moreover, in a business survey conducted in 1998 covering 243 firms, 43 percent said they were paying bribes to tax officers occasionally or always (Gauthier and Reinikka 2001, p. 22).[10]

Exemptions increased in prevalence and importance from 1995-1997 (ibid) – despite official policies to the contrary. In particular, large firms have benefited from exemptions. Although the Income Tax Act of 1997 provided more effective means to reduce exemptions, the introduction of accelerated depreciation allowances have diminished this reduction (EME 2000, p. 17).

Revenue fraud in the form of smuggling, undervaluation and underdeclaration of income and taxable goods, misclassification of goods, and so on, has been a rising problem. The government itself has increasingly focused on this problem in recent budget speeches and background papers on the budget. According to the Uganda Manufacturers Association (UMA), smuggling accounted for a revenue loss of 10 percent per year in the late 1990s (ibid).[11] The Customs Department in particular has consistently had difficulties in meeting its targets (Obwona and Muwonge 2002, p. 27). Hence, various forms of revenue fraud, which imply the involvement of customs officers, are likely to be part of the explanation for the tax share stagnation in recent years.

Senior managers seem to be heavily involved in corruption in the URA. This is, for instance, reflected in the court case in 2003 against five senior officers attached to the Large Taxpayers Department (LTPD) who were accused of defrauding the URA of USh 338 million. The accused included the commissioner of the LTPD, three assistant commissioners for audits and business analysis, and the public relations officer (The New Vision 11 March 2003, p. 4). However, according to officials in the URA, this court case is only the "tip of the iceberg."[12]

As a measure to combat corruption, all URA staff members were requested in January 2002 to fill out an asset declaration for themselves and their relatives. This is something Members of Parliament are supposed to do as well,[13] although several MPs refuse to comply (Musamali 2002; Mwenda 2002; Osike 2002). Asset declaration has proved to be a very difficult process in the URA as well. Many staff members own property that is not registered in their own name and sometimes not even in the name of their spouses or other relatives. As part of the anti-corruption program, "Integrity Councillors" are supposed to "carry the message" to the rest of the staff. A letter was distributed in 2002 within the URA that asked all staff members to tell what they knew about misappropriation of tax revenues. According to the then Commissioner General (CG), this initiative resulted in a good deal of information. The CG also established a separate e-mail address to which only she had access, and where the general public could report. Several newspapers have published information on this address (Mpagi 2002).

In March 2002 a Commission of Inquiry of Corruption in the URA was appointed by the Government. On this occasion, the BBC News Online wrote (BBC 2002): "A three-month judicial probe into Uganda's tax authority has started to root out 'massive' corruption and boost tax revenues." The Commission was chaired by High Court Magistrate Julia Ssebutinde, who had previously headed inquiries of corruption in the police force and the army. Judge Ssebutinde was assisted by two co-commissioners, Fawn Cousenes and James Kahoza. The Commission started its work in May 2002 and was expected to deliver its report and recommendations after 3-4 months. However, the enquiry took a much longer time than expected and was followed by rumors and accusations, including an alleged assassination attempt on Judge Ssebutinde.[14]

The much delayed and feared report was presented to the government in February 2004. However, Ssebutinde's two co-commissioners distanced themselves from the report's conclusions, and the public did not get access to it. Moreover, its legality was questioned by Members of Parliament and some of those that Ssebutinde accused of wrongdoing. Later in August 2004, the High Court nullified the report. Thus, the initial enthusiasm and expectations which met the Commission vanished. There are also indications that the long drawn out investigations carried out by the Commission and the rumors surrounding it, contributed to further eroding staff morale within the URA. In a farewell e-mail sent to the URA staff in September 2004, the departing Commissioner General, Annebrit Aaslund, expressed her frustration at the way Justice Ssebutinde's Commission lost credibility following bickering between the commissioners. According to Aaslund, corruption "remains a stain on the URA's reputation," but "[u]nfortunately an exercise, which I had hoped would help promote reform, has become a weight around the URA's neck" (The Monitor, September 2004).

Leaks from the Commission's report suggest that around 100 corrupt individuals are named, which, according to some people interviewed, were fewer than what one "hoped for", considering the total number of the staff (about 2,200) and the size of the problem. Moreover, some of the known offenders did not appear to be mentioned in the investigation. Some observers therefore suspected that the Commission's inquiry had become so politically sensitive that its conclusions under any circumstances were unlikely to have positive impact on the fight against corruption in the URA. According to Darryn Jenkins (2003), other methods are required to break the cycle of corruption. He argues that a major re-staffing is needed to "eliminate" corrupt staff (ibid, p. 15): "This measure will also send a signal that the URA management is serious," and he adds, "[t]hat signal is awaited by the core of good staff." However, according to senior officials interviewed in the URA, there is only a limited pool of qualified people who can fill the positions of the corrupt officers if they are to be retrenched. In other words, it is hard to replace corrupt staff. The URA cannot recruit expertise, but must take on the costs of training new hires. Another issue emphasized by senior officials interviewed is that there are corrupt officers who are efficient, and non-corrupt officers who simply "do not do anything."

Understanding corruption in the URA

After the initial success, tax revenues have stagnated and in recent years dropped as a percentage of GDP. Moreover, corruption and tax evasion seem to be increasing at all levels of the URA. According to taxpayers interviewed, there is also an increase in the number of tax collectors *openly* demanding bribes after presenting taxpayers with unreasonably high assessments. How can this relapse be explained? The following factors may shed light on this development:

- Declining real wages.
- Bonus systems and revenue targets.
- Hiring and firing of staff.
- Human resource management and job security.
- Political interference.

- Patronage.
- Taxpayers’ compliance.

Declining real wages

Despite a dramatic increase in pay rates compared with normal rates in the public sector, it was not enough to compensate for the potential gains from corruption. The situation worsened even more by the erosion of the initial pay rates by inflation. Between 1991 and 1998 nominal wages remained unchanged. Hence, although the URA staff on average received salaries 8-9 times higher than salaries for corresponding positions in the civil service in 1991, this had shrunk to a factor of 4-5 in 2000 (EME 2000, p. 20). Furthermore, compared to the salaries in other autonomous authorities in Uganda, for example the Wildlife Authority and the Human Rights Commission, the URA pays less (Mitala 2001). This erosion of salary differentials is likely to have contributed to the erosion of staff motivation. It is therefore no surprise that the initial wage reform seems to have had only a limited impact on restraining the extent of corruption in the tax administration. But, irrespective of wage rates, the tax administration remains a very attractive workplace. The tax collection departments are particularly attractive. There is also considerable internal competition within the URA for vacancies in the operational departments. Thus, the erosion of wage rates in not sufficient to explain the prevalence and growth of corruption.

Bonus systems and revenue targets

Generally in a principal-agent setting, bonuses improve the performance of the agent by making the right sort of effort more rewarding in monetary terms. There are different ways in which to fashion a bonus system. One important distinction in this context is between individual and group bonuses. With individual bonuses each tax officer is rewarded for his or her individual effort. The upside to this bonus system is the direct link between what a tax officer does and what he or she receives. Possible downsides are opportunism and a lack of coordination between collectors, as each pursues the tasks that are most personally rewarding. With group bonuses, tax collectors are rewarded for the performance of a group as a whole. The upside is greater coordination of tasks, the downside a possibility of free-riding behavior, as each officer sees only a marginal effect of his or her own effort on the bonus. Which of the two systems is chosen depends on several factors of which an important one is the ease of monitoring individual versus group output. The question of what bonuses are tied to is also important. If they are tied to a revenue collection target, performance depends on both effort and factors outside the revenue authority's control, such as fluctuations in the overall economic activity in the country.

In the case of the URA, group bonuses have been used. Performance is gauged in terms of a revenue target measured in term of tax revenues as a percentage of GDP. A 10 percent salary bonus to staff was paid in 1998 when the revenue target was met. However, in the period 1991-1999, URA reached its revenue targets in five out of eight years, while only one bonus payment was made (URA 2002, p. 18). To the staff this was regarded as a broken promise.

Since 1998, there also seems to be a growing perception among staff and management that revenue targets are set unrealistically high, based on desired government expenditure levels rather than on the ability to tax (Therkildsen 2004). URA staff interviewed pointed to the shaky empirical basis for the revenue targets set by the MoF, and they complained about their lack of influence in setting targets. This has been a major source of conflict between the URA and the MoF (ibid, p. 78). Hence, a sustained upward revision of revenue targets could prove detrimental to staff motivation. Moreover, revenue targets set in terms of revenues to GDP may be too broad a measure of performance. For individual staff members, the perceived ability to influence the percentage of revenues to GDP is likely limited, and bonuses based on this performance measure may not have much of an effect on staff effort and corruption. If group bonuses are to be used, bonuses awarded according to departmental revenues may provide a closer link between effort and reward.

To summarize, pay reforms are likely to have had little impact on staff performance and corruption in the URA, since the conditions under which pay would affect performance do not seem to hold. The bonus system was too general to provide effective incentives for individual staff members.

Hiring and firing of staff

More than 85 percent of the staff who had worked in the former revenue departments within the Ministry of Finance was re-engaged when URA was established, despite the fact that corruption was entrenched in the former tax administration. So when corruption was perceived to drop during the initial phase of the URA, it may have been due to the fact that most employees were working on a probation basis and, additionally, had yet to learn how the new system worked. Thus, although their attitudes toward corruption may not have changed, it was perceived to be more risky to get involved in corrupt dealings at that stage. Tax officers did not know how the internal control mechanisms worked or how the top management would execute the rules and whether they stood in danger of losing the prospect of a permanent job. These points were also confirmed in interviews with present and former URA staff. It was stressed that many employees in the operational departments used their probation period to study how the system worked while "waiting for better times."

Looking at trends in employment at the URA, the initial shake-outs where staff was dismissed have not been sustained in the years following the establishment of the revenue authority, except for top-level managers (Therkildsen 2004). This seems to indicate that dismissals are not as extensively used to discipline unproductive staff behavior as in the initial phase. Thus, there is reason to believe that the staff perceives that the risk of being fired for misconduct is dwindling.

Although the level of unemployment in Uganda is quite high, this might not be directly relevant to former staff of the URA seeking employment. Former tax officers are attractive to the private sector, due to their knowledge of how the tax administration works and their connections in the tax administration. The time a sacked tax official spends in unemployment might therefore be relatively short. Taken together, the dwindling probability of being fired and the ease with which former tax officials, especially customs officers, can get new employment, suggest that pay increases in the tax administration would have to be very large to elicit more effort from staff.

Timothy Besley and John McLaren (1993) propose a model of corruption in tax collection which offers additional insights into the evolution of corruption in the URA. In this model, a proportion of tax collectors is corruptible and chooses between taking bribes and not taking bribes. A tax collector who takes bribes is caught and fired with a certain probability. Tax collectors, thus, compare bribes received to the expected loss from being fired, when deciding whether or not to take bribes. An increase in wages in the revenue authority means that losing your job is more costly, and therefore makes taking bribes less attractive. If wages are sufficiently high, all corruptible tax collectors will choose not to accept bribes. The level of wages sufficient to deter bribe taking then depends on the level of bribes and on the probability of being caught and fired when a bribe is accepted.[15] The higher the bribes received by corrupt officials, the higher must the wages be to deter corruption. And more, the lower the probability of being sacked for corruption, the higher are the wages needed to make tax collectors desist from taking bribes. Therefore, a given pay increase has less of an impact on corruption if bribes are high and the risk of being caught low.

The bribe levels in certain parts of the tax administration, especially in customs, are very high compared to wages (McLinden 2005). As for the probability of being sacked for corruption, recall that the initial wave of dismissals has not been sustained. In addition, the appointment of executives known for their integrity in the initial stages of the reform has been undermined by recent examples of politically motivated appointments and interference into revenue authority affairs. A perception of a more lenient attitude towards corruption may, thus, have formed among the URA staff. The initial pay increases in the URA might consequently not have had much of an impact on corruption, and the subsequent decline in real wages has most likely eroded any initial impact.

An explanatory factor related to hiring and firing mechanisms is the impact of corruption networks. Corruption in public institutions is often conducted by reasonably well-organized networks, where trust and reciprocity is found between network members (Rose-Ackerman 1999; Gehlbach 2001). Such relationships are likely to reduce transaction costs, as well as any moral costs that may arise from allowing oneself to be involved in corruption. Furthermore, the peer networks often function as "repositories of knowledge" for members, for example on the attitudes of the top management to corruption, how the internal monitoring unit works, who is potentially bribable among staff members and management, and so on.

The reforms probably managed to break up a few existing networks, but did not hinder new networks from emerging – both within and outside URA. Furthermore, new networks gradually formed between URA staff and former employees in the tax administration. Many of the dismissed people were attractive to the private sector due to their inside knowledge of the workings of the system. For example, former customs officers were recruited by clearing agencies or set up their own agencies. These persons had intimate knowledge of the tax administration, loopholes, etc. Because many of their former colleagues remained in the tax administration, good connections to the inside were assured.

Human resource management and job security

The URA is perceived by staff members to be a top-down organization characterized by submissiveness. Promotion is in general based on seniority. Younger staff members are given few opportunities to develop their skills. Incentives are in general weak in the sense that good performance is not rewarded and bad performance is not punished. According to interviews conducted during the period 2000-2003, the core of committed staff who would be willing to participate in change either are induced by peer pressure to conform to corrupt practices, or they are turned off by an apparent lack of interest by a management – and a board – that seems mainly concerned about maintaining the status quo.

As noted above, the establishment of the URA reduced the extremely high pay differences between top- and bottom-level staff compared to the former tax administration. However, a wage gap of 3,300 percent between the top and bottom grades is still high and contributes to maintaining the distance between the executive management and the staff. Moreover, the bonus payment in 1998, equivalent to 10 percent of each individual staff member's gross salary, amplified the already high wage differentials. In interviews, this was mentioned as a source of much resentment by URA staff. Moreover, in the view of a broad section of the staff, the commissioners lack detailed knowledge of how the organization actually works on the ground.

Although the turnover of ordinary staff members has been reduced after the initial shake outs, job insecurity seems to have increased for top managers. This may help explain corruption at the managerial level in the URA, in spite of the fact that the top managers are among the best paid officials in Uganda, even excluding their tax-free benefits such as housing and transport. In 2000/2001, for instance, a top manager in the URA was paid 3.6 times more per month than the corresponding position in the central government (Mitala 2001). Changes at the top level have been pervasive throughout the URA's history. There are reasons to believe that the uncertainty which is thereby created has contributed to the observed high level corruption as managers try to enrich themselves while they are in the position to do so.[16]

The presence of corrupt managers may also have a contagious effect on the general corruption level within the revenue authority. Firstly, corrupt leaders may not worry very much about corruption at lower levels in the organization. Hence, the probability of being detected for corruption is likely to be lower for the rank and file tax officers. Second, corrupt leaders contribute to a reduction in the moral and stigma costs connected with corruption. In such a situation we would expect the general level of corruption to increase.

Political interference

Few public agencies are as powerful and as interwoven with society as the tax administration, which monitors and appraises the economic activities of many of the citizens and businesses in the country. For instance, the tax administration often has important financial information about the economic operations of these actors. Hence, having political control over the tax administration can pay high political dividends (Taliercio 2002, p. 17). Politicians can, for example, intervene in the tax administration to grant favors such as tax exemptions to supporters or to harass political opponents through audits. Political interference in the recruitment process has been a source of dissatisfaction and unease among staff, who see this as causing job insecurity and also further exposing the URA to accusations of corruption.

A reform of the tax administration is costly to sustain in terms of increased pay and the purchase and maintenance of equipment. However, the costs of foregone opportunities for patronage and discretion in matters of taxation are probably at least as important to the delegating institutions. And arguably, the more successful a revenue authority is in increasing tax revenues, the higher are the costs of foregone patronage, because higher revenues provide more opportunities for embezzlement. Hence, the

URA has become an attractive target for political interference, especially in personnel matters, because the authority offers both relatively well-paid jobs and considerable rent-seeking opportunities.

The URA has been riddled with political interventions, especially in managerial appointments and dismissals. In 1997, for instance, the President personally intervened in the appointment of the new General Commissioner, although the person appointed by the president was not among the candidates listed for interview by the Board and was not the preferred candidate of the minister of finance (Therkildsen 2004, pp. 80-1). He also had close family ties to the president. Thus, President Museveni did what other members of the elite continuously try to do: influence staffing in the URA. Moreover, as noted above, the President on several occasions publicly criticized the URA staff for being corrupt. This certainly had a major negative impact on taxpayers' perceptions of the revenue agency. The URA lost its legitimacy in the eyes of taxpayers. It also lost its formal and informal authority vis-à-vis the MoF and the state elites.

Patronage

Certain tribal networks are strong in the URA and influence promotions and transfers within the organization. Many tax officers and managers remain under the strong influence of traditional patterns of social relations and recognize the benefits of large extended families and strong kinship ties. This implies that such social relations operate at cross purposes to formal bureaucratic structures and positions. For instance, according to some informants, one of the Commissioners of the URA is fully controlled by a lower ranking official in the department, because this person ranks above the Commissioner in the kinship system.[17] The traditional system rules over the formal "modern" one. Fiscal corruption may therefore, to some extent, be understood in the context of a political economy in which access to social resources depends on patron-client links which exist independently of the URA yet influence its performance.[18]

Generally, kinship and other social relationships of reciprocity are used to mobilize affective ties for instrumental political and economic purposes (Smith 2003). Such relationships combine moral obligation and emotional attachment. They also serve to perpetuate an ethic of appropriate redistribution that fuels corruption (Olivier de Sardan 1999). The importance of such ties may be growing rather than withering away as the country tries to modernize and democratize in a context of economic instability and uncertainty.[19] Thus, many people rely on the social connections of their extended families to secure admission to schools and to get help in paying school fees, to gain employment, obtain business contracts, or benefit from government services.

But although kinship and social networks are pervasive at all levels of the URA, their most obvious impact is at the top. Serious cases of corruption, involving high-level, politically well-connected officers are rarely investigated. Thus, with a few exceptions such as the recent court case against five senior officials of the URA's Large Taxpayers Department, investigations into fiscal corruption only touch the surface. For instance, the Inquiry of Corruption in the URA (the Ssebutinde Commission) did not investigate systemic corruption and the role of family relations and nepotism in sustaining corruption networks. Consequently, neither key stakeholders in the central government nor donor representatives interviewed expected that the Ssebutinde Commission would have much impact.[20]

To some degree the URA has contributed to strengthening existing social networks. For instance, when someone gets a job in the tax administration he or she is expected to help his or her kin and family. Because Ugandans perceive that URA officers receive high salaries, extended family members expect to get their share of the high wages. It is one's social obligation to help and share. URA staff are therefore seen by their family members and social networks as important potential patrons who have access to money, resources, and opportunities that they are morally obliged to share. A person in a position of power is expected to use that influence to help his or her kin and community of origin. Hence, increased salaries may lead to increased social obligations, which again may "force" tax officers to take bribes to compensate for the higher expenses. What looks like corruption from the outside is undertaken by some tax officers in a context where the reciprocal obligations of kinship and community loyalty require such behavior in order to be regarded as a "good person." Hence, as argued by Daniel J. Smith (2003), the standard definition of corruption as "the abuse of public office for private gain" assumes a rigid dichotomy between public and private that glosses over a complexity that characterizes the relationship between the individual and society in many African bureaucracies.

In the Ugandan context, to accumulate, even in corrupt ways, is not necessarily bad in itself. It is accumulation without distribution which is considered unethical (Barber 1997). Only someone who accumulates can redistribute and be identified as “a man of honor” or “a big man.” In an interview, Annebritt Aslund, the former General Commissioner of the URA, gave the example of two URA employees from the same family. One of them is honest, the other is corrupt. The one who has not accumulated more than he could from his official wage, is, according to her, “regarded as a fool by the society” and earns no respect whatsoever (Fjeldstad, Kolstad, and Lange 2003, p. 36). He can not offer needy relatives or friends much assistance. In their eyes his un-corrupt attitude is not only foolish but is, in essence, selfish.

Furthermore, it is in the tax officer’s own interest to help others because he or she might be the one who needs help in the next time around. Thus, a manager in the tax administration may “forgive” a tax collector who is caught taking bribes or embezzling money, because next time he or she may be the one who needs forgiveness (Tripp 2001). This may explain why the quite extensive use of dismissals in the initial phase of the URA has not been sustained (Obwona and Muwonge 2002). Instead of being fired, several tax officers detected for corruption have been transferred to other positions within the tax administration. Favors of this kind may also be understood as a way of consolidating and building social capital. In other words, tax officers are building up networks made up of family, friends, and acquaintances that are based on trust and reciprocity as a way of banking assistance for the future. The larger the network, the greater the accumulation of social capital that can be drawn on in a future time of need. Thus, one possible explanation for the persistent corruption in the URA may be the fact that people at the middle and low end of the political-economic spectrum are just as involved in vertical networks of patronage as the elite patrons who benefit the most.

Why do people continue to depend so greatly on their kin? What motivates people to follow social norms and patterns of patronage? The simple answer is that it is rational. The state is perceived to be unreliable when it comes to delivering basic services and assistance through formal channels. The use of kinship and other social relationships enables ordinary people to get access to resources that they might otherwise be denied (Smith 2003, p. 707). It is, in part, the very demands of the clientelistic networks to deliver public resources, including employment, based on moral obligations and affective attachments, that make it difficult for officeholders to run offices in accordance with Weberian principles. Hence tax officers and managers in the URA find themselves in a schizophrenic situation. Their administrative and professional legitimacy is derived from their training and work in a modern bureaucratic organization and therefore in its values concerning “public service” (Olivier de Sardin 1999, p. 48). This widespread adherence to abstract official norms of Western origin thus coexists with an equally prevalent pattern of behavior in conformity with social norms and family obligations. Many tax officers may be sincerely in favor of respecting the public domain and may want the tax bureaucracy to be at the service of citizens, but still they participate in everyday actions that reproduce the system that they denounce. Thus, a spiral is created in which networks of kin and tribe undermine efforts to modernize the tax administration and thereby create an ongoing need for these very networks to continue to operate.

Taxpayers’ compliance

In Uganda, as in many other African countries, the frequent use of the tax administration for political purposes has helped erode taxpayers’ confidence in the fairness and impartiality of the tax administration, which has itself contributed to undermine tax compliance. An important element of the revenue authority reform in Uganda was therefore to give the new management of the tax administration autonomy from undue political influence. The establishment of a semi-autonomous revenue authority might be interpreted as an attempt by politicians to create a credible commitment to taxpayers that the tax administration will be more competent, effective, and fair by delegating power to tax bureaucrats (Taliercio 2004). The promise of autonomy enables politicians to make the commitment credible because tax administration traditionally has been characterized by high levels of political intervention. The failure to sustain the autonomy of the URA may reflect the particularly difficult problem of credible commitment in these matters.

The formal autonomy awarded the URA upon its inception and the degree to which this autonomy was exerted in the initial phases of its existence, could very well have had a favorable impact on taxpayers’ perceptions of the tax administration’s operations, and hence possibly on compliance rates. In particular the initial increases in wages and the extensive use of dismissals arguably would be easily observable indicators of a high degree of personnel autonomy. Similarly, the appointment of board and management from outside the tax administration and from abroad, and the recruitment of individuals publicly recognized for their integrity, would be a signal of a high degree of managerial autonomy. The initial reform could therefore be expected to have had an impact on taxpayers' perceptions of fairness and competence in collecting taxes.

However, failure to sustain the initial reform efforts has provided a powerful signal to the contrary. The fact that nominal wages in the URA have been stagnant until recently and that the use of dismissals has decreased substantially both point to a decreasing degree of personnel autonomy. Increasing board and government interference in staffing matters has had a similar effect and also signals a lesser degree of managerial autonomy. In addition, managerial autonomy has been substantially undermined by the increasing use of tax exemptions granted by the politically motivated appointment of new board members. Several instances of political interference in the operations of the URA have been heavily featured in the local press. There is thus reason to believe that any initial improvement in taxpayer perceptions due to the administrative reforms was reversed in later years. To the extent that taxpayers were able to foresee this backlash, the reforms might not have had much of an impact on tax compliance in the first place, which indicates that any initial rise in tax revenues should be attributed to other factors.

Concluding remarks

Several factors have contributed to the disappointing results of the URA, and it is difficult to distinguish among them and determine their appropriate weights. However, one lesson to be learned from the URA's first 15 years of operation is that even with relatively respectable salaries and working conditions, corruption may still thrive. The study shows that pay level is only one of several factors affecting the behavior of tax officers. In an environment where the demand for corrupt services is extensive and monitoring ineffective, wage increases may end up functioning as an extra bonus on top of the bribes taken by corrupt officers.

Recent economic research on human behavior indicates that reformers and economists have an inclination to exaggerate the impact of monetary incentives because of an overly narrow understanding of intrinsic motivation and group dynamics (Frey 1997). In Uganda, however, the failure of reforms that stress monetary rewards and incentives may have a more straightforward explanation. Because of the importance of family networks, increased pay rates may imply more extensive social obligations, and in some cases actually result in a net loss to the individual. This state of affairs can develop into a vicious circle with higher wages leading to more corruption because the tax officer has to make up for the loss caused by such obligations. An outsider might conclude that officials lack intrinsic motivation to perform well and do not respond to incentives. However, a more careful study of the situation would instead conclude that the tax officials are responding very well to monetary incentives in a situation where higher nominal pay actually makes the official poorer. This might be a reason for the popularity of in-kind benefits among civil servants, which may be harder to share with one's kin (Platteau 2000, pp. 208-11).

We have seen that norms, as reflected in patronage and social obligations in the URA, are liable to discourage the development of a professional tax administration. At the same time, the experiences of the URA emphasize the particular importance of breaking the influence of kin-based networks on the operations of the revenue administration. One suggestion is to introduce rotation systems for the staff, where revenue collectors remain only for short periods in the same post (Das-Gupta and Mookherjee 1998). But a danger of the rotation system is that the uncertainty which is thereby created for employees may result in increased corruption as collectors try to enrich themselves while they are stationed in the most "lucrative" posts. The rotation of officials may also give corrupt superiors undue power. For instance, they might "sell" assignments to attractive positions or reassign officials to remote stations as a punishment for honesty (Rose-Ackerman 1999, p. 84). The scarcity of qualified personnel like auditors and accountants further reduces the potential of rotation schemes in the poorest countries. Under such conditions it is little wonder that the revenue authority performs poorly because its behavior is shaped by conditions over which it has little control. It is difficult to insulate the revenue administration from contexts in which graft and corruption are normal in public sector operations.

Must we conclude then that it is generally impossible to overcome traditional social restraints on the development of a professional, modern tax bureaucracy in a country like Uganda? If it is true that similar conditions were widespread in Western societies before modern public finance management took roots, the answer to that question must be negative. Also, observations of contemporary African societies suggest that the impact of traditional values and social obligations on the behavior of public officials have fluctuated and can be changed (Platteau 2000). There are revenue authorities in poor African countries that perform relatively well despite dauntingly unfavorable contexts and an overall poor public sector performance.

The experience of the Zambia Revenue Authority, for instance, shows that expatriate senior advisors and top managers who are in place for a pre-defined and limited period of time can contribute to effective change by building integrity and professionalism in the organization through systemic changes (Wulf 2005). Placing expatriates in key management positions might also help to reduce the impacts of patronage and predatory authority. Strong expatriate leadership may more easily confront political and bureaucratic pressures, and thus provide a "buffer zone" within which systemic changes and new forms of staff behavior are implanted. URA's experiences with expatriate top management, however, are mixed.

As the Ugandan case shows, it should be recognized that tax administrative reforms often are highly political processes that will inevitably pose a threat to important domestic stakeholders. The successful implementation of such reforms therefore requires political will to back them up (Tanzi and Pellechio 1997). The reforms are unlikely to succeed if the main source of energy and leadership comes from outside. In general, strong leadership of the revenue authority is essential for overcoming the political and bureaucratic obstacles that confront the URA. This also requires a better demarcation of management authority between the Board and the Commissioner General. A board acting as the chief executive is certainly not a recipe for the strong and effective daily leadership which the revenue authority needs. The present problems of micro-management by the Ministry of Finance and the Board's involvement in day-to-day operations must therefore be addressed. This may imply a re-composition of the Board that better matches the expectations of the Government about the status and performance of the tax administration. Such measures, however, do not imply the end of mutual cooperation between the URA and the Ministry of Finance. The revenue authority possesses unique datasets on taxpayers and revenue bases, and this information is essential for improving tax policy and legislation. But, the role of the Ministry in formulating and designing tax policy, and the responsibility of the revenue administration to implement this policy, must be unambiguous and mutually respected.

The argument in favor of stronger managerial autonomy of the URA is consistent with recent studies on why some public organizations work well and others do not in developing countries. For instance, in a study of 29 organizations in six countries Merilee S. Grindle (1997) found that organizations with higher salaries paid to their staff did not perform better than public organizations which conformed to the low general public sector remuneration scales.[21] Instead, good-performers had well-defined missions, where the employees internalized the organizations goals and saw themselves as vital contributors to their accomplishment (ibid, p. 486). Effective managerial practice and high expectations about employee performance were factors that led organizations to perform well, while some autonomy in personnel matters allowed a mission to be identified and enabled skilled managers to have some room to maneuver in setting standards for their organizations. This underscores the importance of leadership styles and internal performance management practices that focus on results.

Encouraging the development of a positive organizational culture may thus be an important way of improving the URA's performance in a situation where the broader environment, including the public sector in general, discourages good performance. If the enabling environment is weak, managers tend to drive performance. Therefore, internal leadership and culture are likely to be keys to establishing meritocratic and performance-oriented organizational behavior in situations where the formal political and administrative institutions are weak. Accordingly, a reasonable hypothesis would be that if the URA was given more real autonomy in personnel matters, this would contribute to greater capacity to set performance standards for its employees and hold them accountable to the organization for meeting those standards. Autonomy in personnel matters can here be understood as a facilitating condition that provides the URA and its managers with the ability to build cultures that allow the organization to rise above the norm for the public sector in Uganda (Grindle 1997, p. 488). Required measures would include a rigorously planned and executed re-staffing process, also at the senior management levels, and introduction of human resources policies relating to transparent recruitment, adequate remuneration, pension/retirement schemes, etc. Such measures ought to take place before proceeding with traditional forms of technical assistance such as the design and implementation of integrated computer systems, organization of formal training courses and on-the-job training, and process re-engineering in a wide range of areas, including better forms and filing, auditing and management of revenues, taxpayer education programs, and so on. The experiences with the latter forms of technical assistance for revenue enhancement and capacity building in tax administrations are mixed in Africa.

Tax administrative reforms take time to achieve and are often contested, high profile measures. They therefore require political will and support from the highest level of government. The URA was set up in 1991 by external consultants who arrived with a pre-fabricated “blue-print” for tax administration reforms. Although the reforms were supported by the political leadership and senior officials in the Ministry of Finance for a number of years, this support soon began to erode, beginning with the change in the role and composition of the board in 1997. Thus, it is reasonable to ask whether the political support behind the establishment of a semi-autonomous revenue authority was genuine from the outset, or whether it reflected the bargaining power of donors. The assumption that donors can build state capacity despite the lack of effective internal demand for a more effective tax administration is questionable.[22]

Many observers conclude that a lack of a taxpaying “culture” is the largest obstacle to building a firm long-term revenue base in Uganda. The opposite may, however, also be the case: as long as the tax administration culture is perceived to be influenced by sectarianism, nepotism, and corruption, it is unlikely to contribute to the fostering of a more conducive taxpaying culture. Despite quite comprehensive changes in the tax structure (rates and bases) in recent years, the tax system in Uganda is still complicated and non-transparent (Obwona and Muwonge 2002). Tax legislation is unclear and causes random and partly ad hoc collection procedures (Kasimbazi 2003). Assessors have wide discretionary powers to interpret tax laws, for instance, to allow or disallow expenses or charges, or to exempt items from import duties. These factors, combined with a perception of limited tangible benefits in return for taxes paid, legitimate tax evasion.

In such circumstances it is not surprising that taxation takes place in an atmosphere of distrust and fear between taxpayers and revenue officers. Extensive use of force is often required to collect revenues, as reflected in the use of special military units to enforce taxes and fight smuggling. Thus, the government's credible commitment about the use of tax revenues and its procedures to design and implement tax policy non-arbitrarily are crucial to regain legitimacy. The credibility or trustworthiness of the revenue administration's sanctions against tax defaulters is also important in this context (Slemrod 2003). Reforms of tax legislation and collection procedures, including measures to improve transparency in the taxpayer-tax officer relations, should therefore take place concurrently to reduce opportunities for corruption and the demand for corrupt services. When the government decides what measures to take as part of its tax reform program, it should bear in mind the state of the economy and the resources at hand. Uganda, like most poor countries, has neither the political capital nor the administrative capacity to sustain more than a limited range of concurrent initiatives. But an incremental process of change can add up to a radical transformation if it is sustained for long enough.

A strong bond of accountability between citizens (taxpayers) and the public sector may contribute to generate demand for tax administrative reforms. For instance, business communities, taxpayers' associations, trade unions, and other influential domestic institutions have a potential to put pressure on the revenue administration to do a better job. For taxation to have a positive effect on accountability between government and taxpayers, taxation must be "felt" by a majority of citizens in order to trigger a response in the form of demands for greater accountability and improved public service delivery (Moore 1998). But the tax reforms during the last decade in Uganda have not done much to widen the tax base. It has proven especially difficult to incorporate both the many informal business operators and the professionals, such as lawyers, doctors, and private consultants, into the revenue base. Only formal business corporations appear to be visibly affected by the central government tax reforms. Still, there are indications that an organized voice and response to the revenue policies is developing within the Ugandan business and trading communities. The fact that some tax issues are being treated through formal, public organizations, rather than through bribery and public deals may indicate the beginning of a link between economic elites and government in issues of revenue generation.

Notes

[1] In Latin America, revenue authorities have been established in Jamaica (1981), Argentina (1988), Bolivia (1987, re-established in 2001), Peru (1988/1991), Colombia (1991), Venezuela (1993), Mexico (1997), Ecuador (1999), Guatemala (1999), and Guyana (2001). In Africa, the revenue authority model has been instituted in Ghana (1985), Uganda (1991), Zambia (1994), Kenya (1995), Malawi (1995), Tanzania (1996), South Africa (1997), Rwanda (1998), Zimbabwe (2001), Ethiopia (2002), Sierra Leone (2002), and Lesotho (2003). Burundi and Mauritius are planning revenue authorities and several West African countries may follow.

[2] The revenue authority model is motivated by the executive agency model, which is one institutional model of the new public management (NPM), which is inspired by the radical public sector reform programs of the 1980s that began in the UK, USA, Australia, and New Zealand. Autonomous agencies are seen as a remedy for a number of institutional problems that plague the public sector, such as multiple layers of principals and agents, byzantine rules and regulations, and poor incentives. It is a way of separating certain governmental functions into arms-length units, giving management the autonomy to operate the activity like a business, emphasizing economic norms and values. Willy McCourt and Martin Minogue (2001) examine the conceptual and practical problems connected with such policy transfers to developing countries.

[3] In 1985, Ghana established the first revenue authority in Africa, but each major tax (for instance, income tax and customs duties) was collected by its own agency (Terpker 1999).

[4] Still, in URA’s corporate plan for 2002/03-2006/07, the target is to achieve a tax-to-GDP ratio of 17 percent in 2006/07, which implies an annual increase in revenues by 1 percent of GDP (URA 2002, p. 27). One should however be careful about drawing a too confident conclusion about successes and failures on the basis of the tax-to-GDP ratio, since it tends to be a relatively imprecise measure of performance (Stotsky and WoldeMariam 1997). Nevertheless, increase in revenues measured as a percentage of GDP is the major performance criterion publicly announced by the Ugandan government, clearly reflected in the Budget Speeches of the Ministers of Finance and also in the URA’s strategic plan. Moreover, the International Finance Institutions (IFIs) and various bilateral donors usually refer to the tax share as the key performance indicator.

[5] Personal interview, Kampala, 20 March 2003.

[6] In theory an increase in fiscal corruption may contribute to an increase in tax revenues. The essential link, studied by Dilip Mookherjee (1997) among others, is based on the idea that the possibility to negotiate bribes from evasive taxpayers motivates corrupt tax officers to work harder in order to detect evasion. This will be anticipated by the taxpayers, and hence tax evasion will be less attractive because it is more likely to be detected. Thus, it is claimed, corruption works to make tax evasion less appealing and thereby may increase tax revenues. Other scholars, however, argue that accepting fiscal corruption as an instrument for raising revenues in the short run may undermine tax collection in the longer run (Fjeldstad and Tungodden 2003).

[7] Wade (1982) provides an excellent account of methodological challenges and approaches for analyzing systems of corruption in public sector institutions.

[8] Initially the Board was composed of nine persons: the Chairperson appointed by the Minister of Finance; the Commissioner General of the URA; the Secretary to the Treasury; the Principal Secretary of the Ministry of Commerce; the Commissioner for Industry; the Governor of the Bank of Uganda; and three members appointed by the Minister of Finance (RU 1991, p. 5). The main functions of the URA, its organizational structure, composition of the board, etc. are detailed in Fjeldstad et al. 2003, pp. 21-25). See also www.ugrevenue.com/

[9] After the amendment of the Finance Bill, the Board is composed of seven persons (Republic of Uganda 1998): the Chairperson, appointed by the Minister of Finance; the Commissioner General of the URA; one representative of the Ministry of Finance; one representative of the Ministry of Trade and Industry; one representative of the Uganda Manufacturers Association; two other persons appointed by the Minister of Finance who are not public officers but who are made members of the board because of their special knowledge and experience in taxation matters.

[10] The survey was conducted by the World Bank and the Uganda Private Sector Foundation. Businesses from four major economic sectors were interviewed: the manufacturing sector (66 percent of the sample); commercial agriculture (13 percent); tourism (12 percent); and construction (9 percent). The firms were interviewed on their activities in the period 1995-1997, including issues like infrastructure services, physical investments, taxation, regulation, and corruption.

[11] During the 1990s, successions of more or less militarized units have been established to deal with smuggling and tax evasion (Therkildsen 2004, p. 80). These units include the Anti-Smuggling Unit (ASU), until 1996; the Revenue Protection Service (RPS), until 1998; and the Special Revenue Protection Service (SRPS), thereafter. Although the RPS was under URA control, the SRPS is outside the URA and employs mainly people from the army, the Internal Security Organization, and the External Security Organization. These militarized units are extremely unpopular among ordinary citizens, due to their often extensive use of force. They are also unpopular within the URA because the units have a dual mandate (i) to track tax evaders, and (ii) to "check those big shots in URA who collaborate with smugglers" (The Monitor, 28 June 1998).

[12] Personal interviews, Kampala, March 2003.

[13] Leadership Code Act of July 2002.

[14] On Friday night 10 October 2003, Justice Ssebutinde's home was reported to have been attacked by six gunmen. No one was hurt. In an interview, Ssebutinde linked the attack to the inquiry of corruption in the URA: "I don't think it was an attempted robbery. Otherwise they would have begun with my neighbours who are richer, do not have armed guards and have expensive cars parked in their compounds. But the report (on URA) is ready and will be out anytime. We shall stand by our positions and leave the rest to God" (The Monitor, 13 October 2003).

[15] Besley and McLaren (1993) assume that fired workers are reemployed at market wages, so unemployment does not play a part here, though one could easily fit this idea into the model.

[16] This is supported by historical evidence from Germany and the Nordic countries (Rothstein 1998) and more recently in an econometric study by James E. Rauch and Peter B. Evans (2000) on bureaucratic structure and performance in a sample of developing countries. Here it is shown that increased job insecurity for public officials goes together with increased corruption.

[17] Personal interviews, Kampala, March 2003.

[18] In an influential study Patrick Chabal and Jean-Pascal Daloz (1999) argue that politics in Africa must be understood as driven by vertical ties of patronage. The power of these ties is maintained by redistributing resources accumulated through 'corruption' to clientilistic networks according to rules of reciprocity that have their origin in a kinship-based social organization and morality. According to Chabal and Daloz (p. 27), peoples' reference unit in Africa remains family- and kin-based, which is the

fundamental 'circle of trust' within which individuals operate. Moreover, political elites seek to establish principles of mutual aid, of patron-client reciprocity, based on kin and family relations.

[19] See Susan Rose-Ackerman (1998, pp. 317–323) for a discussion of the role of traditional networks in reform processes.

[20] Personal interviews, Kampala, March 2003. According to a Member of Parliament interviewed in May 2003, the lack of support for the Commission from senior politicians is because the top management of the URA is perceived to support the government. This contrasts with the government's support for the investigation into corruption in the police, since the police force, and in particular the top brass, was perceived to house widespread opposition.

[21] The six case countries were Bolivia, Central African Republic, Ghana, Morocco, Sri Lanka, and Tanzania.

[22] In a recent review of the experiences with IMF-supported programs of fiscal adjustment, Ales Bulir and Soojin Moon (2003, p. 24) conclude that "…revenue enhancing measures, and perhaps also technical assistance provided to program countries, failed to provide a sustainable increase in the revenue-to-GDP ratio."

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