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Donor support for tax administration reform in Africa

Experiences in Ghana, Tanzania, Uganda and Zambia

Christian von Soest

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Dr. Christian von Soest, Political Scientist, is Research Fellow at the GIGA German Institute of Global and Area Studies in Hamburg. His main areas of research are the state in non-OECD-regions and development policy.
E-mail: soest@giga-hamburg.de

Tulpenfeld 6, 53113 Bonn
☏ +49 (0)228 94927-0
🖷 +49 (0)228 94927-130
E-Mail: die@die-gdi.de
http://www.die-gdi.de

Abstract

Tax administration reforms are of prime importance for strengthening fiscal state and governance relations in developing countries. African countries have been particularly deficient in this respect. Donor support for tax administration reform in Africa therefore might have a strong impact in enhancing the developing prospects of the continent. This study analyses the experiences gathered to date with donor support for tax administration reform in four African countries: Ghana, Tanzania, Uganda and Zambia. With strong assistance, all have established semi-autonomous revenue agencies. The study assesses their capacity to collect and process taxpayer information, their merit orientation in the area of human resource management, their relationships with other state organisations and donors, their tax structures and exemptions, and, finally, their revenue performance. One special focus area is the political and socio-economic environment in which the reform projects are embedded. The aim is to draw lessons from the case studies' different trajectories for future donor assistance.

The two main recommendations presented here are: **First**: a broadening of donor support beyond administrative issues. This entails systematic cooperation with civil society stakeholders and a strengthening of the Ministry of Finance's capacities. **Second**: ensuring the sustainability of tax administration reforms. Flexible donor conditionality, not purely focussed on the tax-to-GDP ratio and on fulfilling revenue targets, as well as coherent and needs-based technical support are prime means for enhancing the prospects of partner countries' consistent commitment to tax administration reform.

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Abbreviations

ACCA	Association of Chartered Certified Accountants
ASYCUDA	Automated System for Customs Data
CCM	Chama Cha Mapinduzi (Revolutionary Party of Tanzania)
CEPS	Customs, Excise and Preventive Service (Ghana)
DFID	Department for International Development (United Kingdom)
ERP	Economic Recovery Programme (Ghana)
EU	European Union
FAST	Flexible Anti-Smuggling Team
GDP	Gross Domestic Product
GPRTU	Ghana Private Road Transport Union
GPT	Graduated Personal Tax (Uganda)
GTZ	Deutsche Gesellschaft für Technische Zusammenarbeit GmbH (German Technical Cooperation)
HIPC	Heavily Indebted Poor Countries Initiative
IMF	International Monetary Fund
IRS	Internal Revenue Service (Ghana)
ITAS	Integrated Tax Administration System (Zambia)
ITAX	Integrated Tax Administration System (Tanzania)
LTU	Large Taxpayer Unit
MDBS	Multi-Donor Budget Support Programmes
MMD	Movement for Multiparty Democracy (Zambia)
MOF	Ministry of Finance
NRM	National Resistance Movement (Uganda)
NRS	National Revenue Secretariat (Ghana)
ODA	Overseas Development Administration (United Kingdom)
PRSP	Poverty Reduction Strategy Paper
RAGB	Revenue Agencies Governing Board (Ghana)
RIZES	Revenue Institutions in Zambia Enhanced Support (DFID)
RMS	Revenue Mobilisation Support (GTZ, Ghana)
TAP	Tax Administration Project (Tanzania)
TATA	Tanzania Taxpayers Association
TIN	Tax identification number
TRA	Tanzania Revenue Authority
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNIP	United National Independent Party (Zambia)
URA	Uganda Revenue Authority
URAP	Uganda Revenue Authority Project (DFID)
USAID	United States Agency for International Development
VAT	Value-Added Tax
VATS	Value-Added Tax Service (Ghana)
VIT	Vehicle Income Tax (Ghana)
ZRA	Zambia Revenue Authority

1 Introduction: Donors and Tax Administration Reform in Sub-Saharan Africa

State income through tax revenues is of central importance for development. It serves as the financial basis for all state functions (e.g. internal and external security, public welfare). African states have been particularly deficient in this respect and have shown a persistent inability to collect taxes (van de Walle 2001, 182–183; Bräutigam 2002, 14; Olowu 2003, 105).[1] An IMF study (Silvani / Baer 1997, 6–7) found that more than 60 % of the tax potential in some African countries remains untapped. As a consequence, hardly any of the African states is financially self-sufficient. The continent today is the most donor-dependent region in the world (World Bank 2005).

There has been a growing recognition of the relevance of internal revenue collection in sub-Saharan Africa (and other developing regions) among multilateral and bilateral donors. In the course of concentration on questions of good governance and new aid modalities, the donor community is now devoting increasing attention to fiscal reforms (World Bank 2002a, 110–115; Olsen 2001, 148, 150, 154). Besides donor harmonisation, as prominently argued in the Paris Declaration on Aid Effectiveness, a key goal for making development aid more effective in future is the strengthening of partner countries' institutional capabilities and the finding of context-sensitive solutions (High Level Forum 2005). This implies that assistance which narrowly focuses on technical issues is inadequate and that a holistic approach is needed to improve the self-sufficiency of partner countries.

Effective tax administration is of key importance in this respect. Hadler (2000, 10) estimates that better administration of existing tax legislation may increase revenue by 30 % or more in many countries in sub-Saharan Africa. Accordingly, strengthening the tax administration has been an important area of technical donor support towards public administration in sub-Saharan Africa. The proliferation of semi-autonomous revenue authorities constitutes its most visible expression (on the concept see Devas et al. 2001).

In addition, taxation inherently touches on questions of governance and accountability. A state can efficiently tax its citizens only with their general consent. The concept of a "fiscal contract" refers to a bargaining process between two parties in order to establish their respective obligations. Scholars perceive the fiscal contract between citizens (paying taxes) and the state (providing public services in exchange) to be particularly defective in sub-Saharan Africa (e.g. Fjeldstad/Therkildsen 2004, 1; Guyer 1992, 57, 70). Donor support for tax administration therefore might bring a significant *governance dividend* (DFID 2005, 5).

At the same time, tax administration reform projects on the African continent have posed a particular challenge to development assistance: Development levels are low, public administration is often ineffective, and political conditions are comparatively unstable. The environment in sub-Saharan Africa is unfavourable to sustainable tax administration reform. In spite of significant efforts, tax administration reform therefore often remains unsuccessful (Stewart / Jogarajan 2004, 158).

1 In this study, the terms "taxes" or "revenue" encompass direct taxes, indirect taxes and customs duties.

This is the point of departure for this study, which will analyse the impact of donor support on tax administration reform in four African countries, with special attention to multilateral and bilateral donor agencies.

The main questions to be answered are: What experience has been gained with donor support for tax administration reform in Africa, and what can be learned for future assistance?

The four case studies of Ghana, Tanzania, Uganda and Zambia provide a comprehensive spectrum of experiences gained in relation to donor support for tax administration reform in sub-Saharan Africa. These four countries have all established semi-autonomous revenue authorities, albeit with different results. With the oldest reform projects on the continent, Ghana and Uganda are particularly well-suited to provide information about long-term changes in relation to tax administration reform projects, whereas Zambia and Tanzania more recently started their reforms. All four countries have been strongly dependent on donor funds and on technical assistance for improving their tax administration.

An assessment of lessons learned must be sensitive to the political and socio-economic contexts in which the reform projects are embedded. This relates to the increasing attention the donor community pays to contextual factors of external assistance (e.g. High Level Forum 2005, 2).[2] In particular, the study refers to socio-economic development and political commitment (or potential opposition) in the case studies, i.e. to factors which might impede or support tax administration reforms. The analysis is based on desk research of primary and secondary literature. It will focus particularly on the effects of donor assistance to the semi-autonomous revenue authorities in Ghana, Tanzania, Uganda and Zambia.

The four case studies follow the same analytical pattern. Each starts by outlining the major political and socio-economic context factors as well as the main features of donor support in the countries. The analysis then focuses on the collection and processing of taxpayer information and the merit orientation of human resource management. Both are core capability indicators for tax administration: First, any tax administration is particularly dependent on data. For Bird, each "is first and foremost an organization dealing with information" (2003, 20). Without an active auditing process and the utilisation of data through information technology, a tax administration cannot carry out its duty of collecting revenue. Second, improvement of the qualification levels of normal staff and tax administration management is of fundamental relevance for the success of donor-supported reform processes. In other words, "it is the superior, well-motivated, performance of the fiscal officer that makes the difference" (Chand / Moene 1999, 1137). The question is how donors have assisted in strengthening these capability indicators.

The study then assesses the relationship of semi-autonomous revenue authorities to other state organisations, such as the Ministry of Finance, and to donors. Autonomy of the political sphere in operational decisions, for instance, is seen as a crucial factor for the capability of the tax administration (e.g. Taliercio 2004). The donor's relationship to the tax administration will also be analysed.

2 See for instance the extensive literature of German development cooperation on this topic (BMZ 2002; Schmidt 2002; Dümcke 2003); for a specific analysis of "taxes and culture" see GTZ (2006a).

A second external factor affecting administrations and influencing the outcome of reform approaches will also be analysed, namely the fact that complicated tax laws, high tax rates and widespread exemptions inhibit the tax collection process. Revenue performance, i.e. output, serves as the final indicator for the impact of donor-supported tax administration reforms. The quantitative data used here are the tax-to-GDP ratio, the collection of different tax types, and the taxation of the economies' informal, i.e. unregistered sector. Revenue performance is covered for the most recent ten years.

Following the four case studies, the final chapter integrates differences and common denominators in the countries. On this basis it will provide specific recommendations for future donor support in the field of tax administration reform. The study's two main arguments are:

- Donor support in the past has often lacked context-sensitivity and awareness of the specific political aspects of tax administration reform. A broadening of focus, characterised by a systematic incorporation of civil society stakeholders and a strengthening of each Ministry of Finance's capacity, is suggested.

- The political rationale of partner countries for *starting* tax administration reform projects is different from *maintaining* political support for such new entities; this has proven to be elusive. Flexible donor conditionality, not purely focussed on the tax-to-GDP ratio and on fulfilling revenue targets, as well as coherent and needs-based technical support is of key importance in supporting the sustainability of reform commitment.

2 Tax Administration Reform in Ghana

Since independence in March 1957, Ghana's development has been characterised by political turmoil and a steep economic decline (Azarya / Chazan 1998 [1987], 117). The history of "chronic regime instability" (Callaghy 1990, 266) ended only with a military coup on 31 December 1981, led by Jerry Rawlings. His government embarked on a comprehensive political and economic reform programme. In April 1983, it initiated the Economic Recovery Programme (ERP), which has achieved considerable success. Its key features were a reform of the exchange rate regime and the tax system, and a reduction of government bureaucracy, the government deficit, and state-owned enterprise subsidies (Leith / Lofchie 1993, 259).

Ghana's government has shown strong commitment to structural adjustment (Sandbrook / Oelbaum 1997, 609). The efforts of the country, which saw a change of government through peaceful elections in 2000, have been supported and rewarded by the donor community. Since 1981, Ghana has received fluctuating but generally increasing levels of aid (Osei 2000, 257). Since 2003, the country has been a pilot country for the Multi-Donor Budget Support Programmes (MDBS) project, which in Ghana is financed by ten different donors. Currently, common budget support constitutes 10 % of Ghana's budget and amounted to 309 million US$ in 2004. The largest contributors are the World Bank (approx. 45 %) and the British Department for International Development (DFID)[3] (approx. 25 %) (GTZ information).[4]

In 1986, the Ghanaian government launched the National Revenue Secretariat (NRS) in order to sustainably strengthen tax administration (Devas et al. 2001, 213). The Secretariat took over functions of the Ministry of Finance's Revenue Department; it was empowered with ministerial responsibilities and shared policy formulation with the Ministry of Finance.[5] Two separate revenue authorities, the Internal Revenue Service (IRS) and the Customs, Excise and Preventive Service (CEPS), were placed under this holding structure. This gave them operational autonomy from the civil service (Terkper 1999, 171; Osei 2000, 259). The semi-autonomous revenue authorities in Ghana constitute the oldest donor-supported reform project of its kind on the African continent.

However, in 1991 the two revenue authorities were again brought under the direct control of the Minister of Finance and the Chief Director (Technical) in the Ministry (Jenkins 1994, 80). It was only in December 1998 that Ghana's parliament passed a law to create a Revenue Agencies Governing Board (RAGB) to replace the NRS and to increase the autonomy of revenue agencies, which now number three: the IRS, the CEPS, and the VAT Service (VATS), created in 1998. The RAGB oversees the three agencies, which operate independently of each other. One important reason for this division can be seen in the chronology of creating the semi-autonomous entities: The IRS and the CEPS had already been launched before the NRS holding structure was established. The different authorities have resisted a merger and have remained comparatively strong. Furthermore, the Ghanaian government has argued that constitutional requirements stand in the way of creating one integrated, stand-alone revenue authority (Terkper 1999, 171, 177; Atuguba 2006, 16).

Tax administration reform in Ghana has been strongly supported at various stages by technical cooperation from donors. Prominent in this regard has been the introduction of the ASYCUDA programme for CEPS, which is supported by the United Nations Development Programme (UNDP) (Tettey 1997). Also important has been DFID's assistance for the creation of VATS (Gray et al. 2001c) and efforts made by GTZ to strengthen the RAGB and, in particular, to computerise the IRS. The conceptual impetus for the introduction of VAT came in 1989 with a feasibility study conducted jointly by the Harvard Institute for International Development and Crown Agents of the United Kingdom (Osei 2000, 260). Since 1992, DFID has supported the VATS in Ghana in two projects reflecting the two attempts to introduce VAT. The first, which provided 1.5 million £, was terminated after the repeal of VAT in June 1995 (see the analysis below). The second project was implemented from 1997 to 2000 (Gray et al. 2001c, 189). In March 2004, GTZ established a new project, the Good Financial Governance Programme,[6] to improve the efficiency and effectiveness of tax legislation and tax administration. Its tax component focuses mainly on direct taxes and cooperates with the RAGB as well as the IRS (GTZ information).

3 Until 1997, DFID was known as the Overseas Development Administration (ODA). DFID also encompasses ODA in this study.

4 Based on information provided by GTZ and internal GTZ documents.

5 The official name is "Ministry of Finance and Economic Planning".

6 This GTZ programme operated under the name "Revenue Mobilisation Support" (RMS) project until the end of 2006.

2.1 Information Collection and Processing

The collection of accurate taxpayer data is the basis for any effort to raise state revenue. In order to curb widespread tax evasion, the reform of the Ghanaian tax administration included setting up a special tax police to check whether or not individuals had paid their taxes. Leith and Lofchie in 1993 found that "it did provide rough equity in the administration of taxes, and consequently has relatively widespread acceptance" (1993, 272). Furthermore, the IRS and the VATS have made the auditing of taxpayers and the collection of information on tax liabilities more effective and accurate.

Nevertheless, a GTZ-commissioned survey of around 1000 Ghanaian taxpayers found that taxpayers dislike the aggressive approach of tax officials (Atuguba 2006, 26). The study concluded that donor support has been instrumental in improving data collection efforts, but that there was a need to increase the number and competence of the personnel employed to collect taxes (Atuguba 2006, 67). With respect to VAT, moreover, more frequent inspections would yield increased revenue. In one region, Cape Coast, a DFID study found that although a target of 16 inspectors had been established for the region, only 5 were actually employed (Gray et al. 2001c, 203).

Improved utilisation of taxpayer data is a further crucial precondition for increasing revenue collections. Since corruption has been a major problem at Customs in the past, attempts have been made since the end of the 1980s / the beginning of 1990s to computerise the CEPS. The initiative for introducing the ASYCUDA system to Ghana came from the United Nations. The UNDP funded the initial acquisition of hardware and the training of CEPS staff abroad to operate the system (Tettey 1997, 352). However, Tettey finds that support for the introduction of information technology at the CEPS yielded only mixed results: First, computers had not taken over all processes within the service. Customs officers retained considerable personal discretion. Second, ineffective procedures at the authority remained in place and were only "computerised". No coherent reform of the whole organisation was carried out (Tettey 1997, 347, 353–354). At least initially, the reform had only a narrow technical focus. The automation of customs clearing procedures was finally completed only in 2003 (De Wulf 2004b, 26).

In contrast to the VATS (Gray et al. 2001c, 190), the IRS has not yet been computerised. It has no proper databases of taxable persons, property or other possessions. This makes it very difficult to mobilize taxes from outside the registered, formal sector of the economy (Atuguba 2006, 45). It remains unclear why no donor support was rendered to computerise this agency before. Probably other entities, such as the CEPS, were deemed more important. Only recently, the RAGB and the Tanzania Revenue Authority (TRA) signed an agreement to hand over the TRA's software (i.e. the Integrated Tax Administration System (ITAX)) to Ghana's tax administration (Ghanaian Chronicle 8.12.2006). The adaptation of ITAX to Ghana's needs will be supported by GTZ.

Finally, due to Ghana's institutional setting of three independent revenue authorities, the integration and exchange of data remains seriously deficient. The establishment of the Large Taxpayer Unit (LTU), in May 2004 can be seen as a step towards integration. The LTU collects all tax types and duties from the 350 largest taxpayers of the country. It is expected that it will raise around 70 % of all tax revenues (GTZ information). The IMF strongly advocates Large Taxpayer Units as a "good practice" for increasing revenue performance (e.g. Baer 2002) and has made its introduction one of the conditionalities for its financial support to Ghana. The LTU already seems to fare better than the rest of the Ghana's tax administration (Atuguba 2006, 59).

2.2 Human Resource Management

Before creation of the NRS in 1986, civil servants, including tax officers, had experienced a deterioration of employment conditions. By 1983, civil servants earned only one-sixth of what they had originally received after independence (Chand / Moene 1999, 1135). This caused widespread demoralization of tax and customs employees. In contrast, in 1986, the employment conditions of tax officers were superior to those of the rest of Ghana's civil service. This followed the revenue authorities' removal from the core public administration structure. All three revenue agencies use the same remuneration scheme (Terkper 1999, 175). Similarly, the hierarchy of employees and the remuneration and benefits structures are common.

At the beginning, an attempt was made to wean out those officers who were perceived to be corrupt and/or not performing. With donor assistance, aptitude tests and job interviews were put in place to recruit qualified and motivated staff. Furthermore, the NRS implemented an incentive scheme in order to strengthen merit orientation among its staff (Osei / Quartey 2005, 9). Across-the-board annual bonuses were paid to tax and customs officers for exceeding revenue targets set for the revenue authorities. Amounting to 10–15 % of base salaries, these bonuses constituted a considerable performance incentive (Chand / Moene 1999, 1137). Yet, these generous bonus schemes were not maintained.

Regarding the VATS, a DFID-funded report found that although core employees have all undergone training, a shortage of supervisory staff persists (Gray et al. 2001c, 190). Furthermore, due to staff vacancies, the outfield offices are operating with inadequate management. The VATS has found it difficult to recruit and retain highly qualified staff. The main explanation for these difficulties is that the VATS has not been given autonomy in setting and raising staff salaries (Gray et al. 2001c, 203). This has limited the effectiveness of DFID's technical support to the VATS.

Despite donor-supported staff training, computerisation and the tough stance which they have taken, the merit orientation of Ghana's revenue authorities appears to be seriously hampered by a high prevalence of corruption. After an initial period, bribery and corruption have again become pronounced. This assertion seems to be particularly valid for the CEPS (Tettey 1997, 351), but also applies to the IRS.[7] This finding in the literature is mirrored by sentiments among Ghana's population. A GTZ-funded survey of around 1000 taxpayers established that many of them think that corruption of tax officials is common (Atuguba 2006, 35). Chand and Moene (1999, 1138) attribute the resurgence of corruption *inter alia* to the loss of NRS independence vis-à-vis the Ministry of Finance and to stronger influence from the political level after 1991. It is noteworthy that Ghana's authorities have not resorted to the employment of foreign management teams in order to

7 Since 2000, Ghana and donors have strengthened efforts to modernise the CEPS in order to facilitate trade (see analysis in De Wulf 2004).

curb corruption, to limit interventions from the political sphere and to strengthen merit orientation of human resource management generally.

2.3 Relationship with other State Organisations and Donors

As already outlined, the historical development of Ghana's revenue authorities and their relationship to the Ministry of Finance can be separated into different phases. From 1986 to 1991, they operated largely autonomously under the NRS' auspices. In 1991, this autonomy was effectively revoked, and the Ministry gained more direct control. This change of status is of particular interest for analysing the effects of tax administration reform and their relationship to the political sphere in Ghana.

The revocation can be mainly attributed to the lack of delimitation between the roles of the Ministry of Finance and the NRS. The NRS appeared to "perform functions that overlap or duplicate those of other departments of MOF" (Terkper 1999, 172; see also Chand / Moene 1999, 1138). There also was considerable initial resistance to institutional change by those at the top of the civil service hierarchy, who perceived the newly created authorities and the supervising NRS as a threat to their positions (Jenkins 1994, 80). This seems to have been underrated by the donors involved as well as by government. Outsourcing of the tax administration appears to have been inadequately communicated and explained to them. Finally, and in contrast to the CEPS and the IRS, the NRS was established by administrative directive and not by a law of parliament. Therefore it did not operate on a solid legal basis, and no adequate formal definition of its role existed when it was formed (Terkper 1999, 172). The relationship between the revenue authorities and the Ministry of Finance therefore has been characterised by frictions. The formal foundations for regulating the cooperation have remained inadequate.

As with other revenue authorities, the annual target-setting mechanism for the three Ghanaian revenue authorities is strongly influenced by the donor community, namely the IMF.[8] The semi-autonomous authorities have recurrently failed to meet revenue targets, with the CEPS being the weakest entity (Chand / Moene 1999, 1138). The Ministry of Finance lacks basic analytical skills for revenue forecasting and the assessment of legislative changes. Until today, there is no Tax Policy Unit within the Ministry of Finance. Its Budget Division concentrates primarily on expenditure issues (Terkper 1999, 175). Accordingly, it is one of the key elements of GTZ's Good Financial Governance Programme to support the establishment of a Tax Policy Unit in the Ministry of Finance. This, however, comes more than 20 years after the establishment of the IRS and CEPS.

Donors have had strong financial leverage in order to influence fiscal policies in general and tax administration reform more specifically.[9] With respect to VAT for instance, they have played the dual role of exerting pressure and rendering support. Nevertheless the

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8 Since revenue authorities collect revenue on behalf of the state, there is an annual negotiation process over revenue targets to be met. The stakeholders involved are, in the African context, the Ministry of Finance, the revenue authority, and the IMF as the most important multilateral donor of financial assistance.

9 For an early analysis of the political economy of structural adjustment in Ghana see Leith and Lofchie (1993).

donor community has not been successful in convincing Ghana's government to merge the three independent revenue authorities into one entity. As outlined above, the legal basis of the holding structure NRS was weak from the start; the revenue authorities have resisted a merger, and the government perceives the constitution to block a single semi-autonomous revenue agency. Nevertheless, it remains puzzling why the government desists from institutional integration. Donors argue that this would be a crucial step in organising the tax administration along functional lines instead of tax types and, in turn, in improving performance (e.g. Gray et al. 2001c, 204). At the beginning, Ghana was able to give advice to Uganda, Kenya and Malawi, countries which were also planning to establish semi-autonomous revenue authorities (Chand / Moene 1999, 1138; De Wulf 2004a, 113). Due to lack of integration and higher costs, however, Ghana today is not perceived to be a model for other African countries.

2.4 Tax Structure and Tax Exemptions

Since the introduction of the Economic Recovery Programme (ERP) in 1983, the government has significantly reformed the tax structure. Principally, the changes involved a) the liberalisation of the customs regime, b) a change of the tax mix favouring indirect taxes on domestic production and consumption, and c) a subsequent lowering of direct tax rates, coupled with the reduction of tax exemptions (Chand / Moene 1999, 1136; Osei / Quartey 2005, 7).

In 2000, an Income Revenue Act was passed which became operational in 2001. The minimum taxable personal income was raised and the top marginal rate of 35 % for incomes was now applied to incomes exceeding 48.0 million Cedis[10] (from 17.4 million Cedis). The reform therefore had favourable outcomes for low-income groups of the population. Subsequently, the top marginal rate was reduced from 35 % to 25 % for the higher-income group and from 25 % to 17.5 % for the middle-income group (GTZ information). These measures also had the potential to lower revenues from direct taxes.

Tax policy support from the IMF has been intense. Furthermore, the GTZ has been involved in tax policy reform since 2004. According to an internal GTZ report, its support has induced a dialogue between important stakeholders (researchers, tax administrators, politicians and representative from civil society) which in turn contributed in 2006 to the first presentation of a coherent tax policy strategy in that year's budget speech. Its main component was a reduction of the company tax rate to 25 %.

Special legal and administrative instruments for taxing the informal economic sector are important in a country where the informal sector comprises about 80 % of economic activity (GTZ 2006b, 7). In this respect, Ghana has been quite innovative: Since 1987, the tax administration had delegated responsibility for collecting income tax from informal passenger transportation operators to their unions, primarily the Ghana Private Road Transport Union (GPRTU). By offering the unions a share (2.5 %) of the total revenue collected, incentives were set to maximise revenue collection (Joshi / Ayee 2002, 95).

10 Roughly 14.000 US$ in 2000 prices.

However, the transfer of revenue collected soon became an increasing problem and other, less visible sectors such as manufacturing were largely bypassed by taxation. In response, the government introduced two new instruments, the Vehicle Income Tax (VIT, in 2003) for commercial drivers and the Tax Stamp for small-scale enterprises in 2005 (GTZ 2006b, 2). While the VIT, which operates with stickers on the windscreen of busses and taxis controlled by the police, has shown noteworthy results, the Tax Stamp has yet to have a notable effect on revenue (GTZ 2006b, 3).

The introduction of a broad-based VAT was a contentious issue in Ghana. In 1995, the country's first VAT was repealed after just three and a half months.[11] The main reasons for this initial failure were poor information of the public and the high VAT rate (Osei 2000, 263). The indirect tax was introduced at a rate of 17.5 %, which was higher than the standard 15 % rate of the previous sales tax (Gray et al. 2001c, 199). Furthermore, the VAT applied to a wider range of products and services. This provoked civil unrest, with demonstrations and riots resulting in several deaths. In June 1995, the Parliament stopped VAT and reintroduced the sales tax (World Bank 2001, 1; Osei 2000, 255). Apparently, the government as well as donors had underestimated the need to prepare and inform the public for successful implementation of VAT.

At the end of 1998, a new VAT was introduced with a low rate of 10 % and a higher threshold (World Bank 2001, 2). This improved public acceptance of the tax, less than two years after the tax was introduced, its rate was raised to 12.5 %. Increasing the tax rate was explicitly required by the IMF in 1999.[12] Currently, the statutory VAT rate stands at 15 %.[13] However, the VAT schedule is characterised by extensive exemptions (Gray et al. 2001c, 197).

With respect to customs duties and tariff structures, a uniform tariff rate for most imports was established; this simplified the collection process (Leith / Lofchie 1993, 271). A particularity of the customs regime is the export tax on one of the economy's mainstays, cocoa (Stewart / Jogarajan 2004, 155, 157). However, rates have been significantly lowered and the variety of different tariffs has been reduced. In accordance with the general policy goal of changing the tax mix in favour of indirect consumption taxes, international trade taxes have decreased over the years (Osei / Quartey 2005, 9–10).

2.5 Revenue Performance

Tax administration reform resulted in a dramatic initial increase of the tax-to-GDP ratio. Tax revenues rose from 5.6 % of GDP in 1983 to 17.0 % in 1994 (Chand / Moene 1999, 1135). It is difficult to directly attribute the rise of the tax-to-GDP ratio to any one single factor. In this case, however, improvements in tax administration seem to have made a significant contribution. Although there were increases in revenue due to tax policy changes, losses were sustained from phasing out export duties. Furthermore, economic

11 See analyses in Osei (2000) and World Bank (2001).

12 For an analysis of the IMF's tax conditionality in general and in Ghana specifically see Stewart / Jogarajan (2004).

13 The rate comprises the 12.5 % "real" VAT and 2.5 % National Health Insurance levies.

growth was not particularly high (Chand / Moene 1999, 1137). However, tax revenues levelled off after this period. According to the literature, this pattern is typical for tax administration reforms in Africa, as the experience of other countries shows (Fjeldstad et al. 2003; Hadler 2000, see other case studies). The tax-to-GDP ratio has risen significantly again only since 2003, with the rate amounting to more than 20 % on the average (see table 1 below). This can be attributed to increased collection efforts and comparatively strong economic growth (Atuguba 2006, 16–17).

Table 1: Revenue Performance Indicators Ghana, 1996–2006*

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Tax revenue	15.1	14.7	15.8	14.8	16.3	17.2	17.3	20.2	21.7	20.7	21.4
Income taxes	3.8	4.3	4.4	4.5	5.2	5.6	5.7	6.1	6.6	6.7	6.4
Indirect taxes	6.5	5.9	6.4	6.6	7.4	7.5	7.7	9.3	10.1	10.3	10.8
Trade taxes	4.8	4.5	5.0	3.8	3.6	4.1	4.0	4.8	4.8	4.2	4.3

* In percent of GDP. Ghana's fiscal year begins on 1 January and ends on 31 December. Indirect taxes include sales tax/VAT, petroleum tax, and other indirect taxes. The rise in indirect taxes in recent years is predominantly due to increased revenue from the petroleum tax (3.9 % of GDP in 2004). Data for 2005 are preliminary, data for 2006 are projected.

Sources: 1996–2000: IMF (2003, 101–102); 2001: IMF (2005a, 35); 2002–2006: IMF (2006a, 28).

The data reflect the policy change from taxation of trade towards taxation of domestic consumption and income. Direct taxes are the hardest tax type to collect. Despite the deficiencies already alluded to, Ghana's tax administration seems to have made some progress in this regard, particularly in recent years. Income and property taxes have been the major source of tax revenue since 1998, accounting for 24.5 % of total revenue in 1999 and increasing consistently to 27.1 % by 2002 (Osei / Quartey 2005, 1). According to donor reports, revenues from direct taxes rose by 57 % from 2003 to 2005 (inflation-adjusted: 22 %), and corporate taxes increased by 86 % (inflation-adjusted: 44 %) in the same period, despite a subsequent lowering of the statutory tax corporate rate to 25 %. One decisive reason for this increase is seen in the 2004 establishment of the Large Taxpayer Unit (GTZ information).

VAT has become the second major tax component in Ghana after its (re-)introduction in 1998, contributing 21.9 % of total revenue in 1998 and increasing thereafter to 22.3 % by 2002. International trade taxes, which were once the largest component of tax revenue, ranked third in 2002, with 19.3 % of total revenue (Osei / Quartey 2005, 1). Despite this positive development, particularly in the recent years, and despite the passing of special tax laws for the informal sector, the broadening of the tax base remains insufficient. Apart from the taxation of the informal transport sector, tax evasion is widespread. According to a survey of 1 000 citizens, Ghanaians commonly doubt the benefits of paying taxes (Atuguba 2006, 29). As a result, Ghana's tax base remains narrow. The current positive development should also not distract from the fact that Ghana has failed to meet the IMF's quantitative revenue criteria on a number of occasions (Stewart / Jogarajan 2004, 160).

The revenue potential is not fully tapped. This is despite the comparatively favourable tax-to-GDP ratio in the African context.

2.6 Summary: Tax Administration Reform in Ghana

The Ghanaian experience offers important lessons on the effects of tax administration reform and donor support in this area. First, an initial attempt to provide the revenue authorities with more autonomy from the Ministry of Finance was reversed in 1991. Apparently the respective roles of the Ministry and the holding structure NRS had not been clearly specified. There was also considerable resistance to the new structure within the administration and the Ministry. It appears that neither the government nor the donor community were aware of these potential problems on the political and administrative level in the beginning, and that preparation was insufficient.

Second, Ghana has chosen a unique path for organising its revenue authorities. In contrast to other countries on the African continent, the three agencies IRS, CEPS and VATS remain autonomous entities under the supervision of the Revenue Agencies Governing Board. This is despite clear donor advice and IMF conditionality to the contrary. In principle, it is to be regarded as positive when countries pursue context-adequate solutions to increase the capability of their tax administration. However, in this case it appears that it is less a form of ownership than the inertia of a structure introduced 20 years ago. The initial drive to reform tax administration in the face of an economic and fiscal crisis has waned. This suggests that tax administration reform is a long-term exercise which requires a long-term view on the part of donors. Tax administration reform is essentially a political phenomenon – purely technical approaches do not constitute adequate responses (GTZ 2006a).

Finally, donor support in Ghana concentrated for a long time exclusively on the tax administration. Important capacities, like those of a Tax Policy Unit, are missing in the Ministry of Finance. The capacity for strategic planning and for executing the role of a counterpart to revenue authorities therefore is inadequate. However, it is noteworthy from a governance perspective that general awareness for taxation issues has grown in the country since the unsuccessful first attempt to introduce VAT in 1994. Nevertheless, the large tax gap suggests that more support could be rendered to improving “quasi-voluntary” compliance from Ghanaian taxpayers.

Main lessons to be learned from tax administration reform in Ghana

- The roles of the revenue authority, the Board and the Ministry must be clearly and formally delimited.
- The integration of different tax departments is crucial for the success of donor-supported tax administration reform projects.
- Explaining the prospective reforms of tax administration (and tax policy) and their implications to stakeholders inside and outside the tax administration is of outmost importance.

3 Tax Administration Reform in Tanzania

Shortly after independence in 1961, mainland Tanganyika merged with Zanzibar (in 1964) to establish the United Republic of Tanzania. The new country adopted a socialist development strategy, but by the late 1980s, after more than a decade of economic decline and deterioration in public services, it was clear that the strategy had failed (McCluskey et al. 2003, 6). Tanzania moved to a multiparty system through a gradual and government-controlled constitutional reform process culminating with multi-party elections in 1995, but with continued dominance by the Chama Cha Mapinduzi ("Revolutionary Party of Tanzania", CCM). In consequence, reform progress has been particularly dependent on political support at the highest level.

As a least-developed country, Tanzania is one of the poorest countries in the world and also one of the first which introduced a Poverty Reduction Strategy Paper (PRSP). In December 2000, the IMF and the World Bank accepted the final PRSP document (United Republic of Tanzania 2000). It is estimated that at least 60–70 % of the country's economic activity takes place in the unregistered informal sector (Fischer 2004, 339). However, low domestic revenue up to the beginning of the 1990s was also caused by serious deficiencies of the tax administration itself. There is a consensus among researchers that inefficiency and systematic corruption were responsible for low tax shares (Fjeldstad 2003a, 166–167).[14]

In response, the government established the semi-autonomous Tanzania Revenue Authority (TRA), which became operational on 1 July 1996. Its prime objective has been to strengthen central government revenue collections by reducing corruption, improving the merit orientation of human resource management, and building a more coherent organisational structure (Fjeldstad 2003a, 169).[15] Donor involvement has been strong. The strengthening of Tanzania's tax administration has been an explicit conditionality by the donor community (see also analysis in chapter 3.3). Since 1990, more than 12 studies – often funded by donors – have informed the reform processes (Luoga 2002, 54).

The TRA has been supported by a comprehensive reform project called the Tax Administration Project (TAP) and predominantly run by the World Bank. Originally, it was planned to start the TAP in 1996, but it became operational only in 1999. 73 million US$ were pledged altogether, with contributions coming from the World Bank, a variety of bilateral donors and from the Tanzanian government (BMZ 2003, 29). On the whole, it seems that the tax administration reform efforts have brought only mixed success.

3.1 Information Collection and Processing

As with all other revenue authorities on the African continent, active collection and assessment of taxpayer data in order to determine tax liabilities has been a prime rationale of the TRA. Before 1996, evasion of all types of taxes was widespread in Tanzania. With

14 Tanzania is ranked 93rd among 163 countries listed on the Transparency International 2006 Corruption Perception Index CPI 2006 (Transparency International 2006).

15 There has also been a considerable amount of research on local taxation in Tanzania (e.g. Eriksen 1999; Fjeldstad 2001; 2002a). This account, however, focuses on the reform of the central tax administration.

respect to sales tax and excises on domestic goods, production volumes were systematically underreported. With regard to corporate taxes, underreporting of profits and falsified tax deduction claims were widespread (Fjeldstad 2003a, 167). Evidence for the amount of taxes and duties lost to the treasury was extensive: For instance, two studies carried out in 1993 and 1994 found that lost customs revenues represented an amount 2.5 times higher than reported customs duties (reported in Fjeldstad 2003a, 168).

The TRA has strengthened the auditing functions of the tax administration. A Tax Investigations Department supports the different revenue departments in enforcing tax laws through regular investigation of tax cases where substantial amounts of revenue are at risk (Fjeldstad et al. 2003, 14). Furthermore, in October 2001, a Large Taxpayer Department was established, which specifically deals with Tanzania's 100 largest taxpayers (BMZ 2003, 27). Since this group of taxpayers accounts for the majority of tax revenue, this reorganisation has been of crucial importance. With respect to customs, an international preshipment company was put under contract to assess the value of imports to Tanzania (cf. Fjeldstad / Rakner 2003, 20). Integrity problems in this area were so severe that outsourcing this crucial function was deemed necessary by the government as well as by donors.

Nevertheless, donors have repeatedly criticised that the strengthening of information collection has not gone far enough. In 2004, for instance, an IMF report noted the need to strengthen the post-clearance verification and audit unit of the Customs Department through the recruitment of additional auditors by January 2005 (IMF 2004a, 11). The doubling of staff in this section of customs was a structural benchmark set by the IMF for the end of March in 2006 (IMF 2006b, 10). Further action required is the establishment of a single department with responsibility for all domestic taxes, i.e. the merger of the Income Tax and VAT Departments. This would facilitate the exchange of information between the different tax departments (IMF 2006b, 39).

The donor community has also been heavily committed to providing information technology to the TRA.[16] In contrast to other revenue authorities (compare the Zambia case study), however, the Automated System for Customs Data (ASYCUDA++) software has not yet been rolled out to all major customs stations (IMF 2006b, 11). The biggest problem is the plethora of information systems introduced by different donor projects. According to one donor report, there exist 14 different software systems which can hardly be linked to each other. This diversity has produced three different systems of taxpayer identification numbers which are unrelated to each other (BMZ 2003, 29; see also IMF 2006b, 37). Hence, donors exacerbate problems of internal cohesion and exchange of information. This has been inherently detrimental to a coherent auditing process.

3.2 Human Resource Management

The Commissioner General is the chief executive of the TRA and is directly appointed by the Tanzanian President (Fjeldstad et al. 2003, 14). This way of appointing the Commissioner General is meant to give him or her the personal clout needed to run the operational

16 GTZ has, for instance, provided support for the computerisation of the Income Tax Department. It has been instrumental in implementing the system ITAX 2002 (see analysis in Olivier 2003; BMZ 2003).

affairs of the revenue authority independently of the political sphere (Fjeldstad 2003a, 165). Prior to the creation of the TRA, political interventions took the form of discretionary tax exemptions granted to business people who had connections with the Ministry (United Republic of Tanzania 1996, 307–310).

This autonomy in operational affairs is partly due to the business-mimicking organisation of the TRA's human resource policy. Job security is weaker than in the traditional public sector. When the TRA was introduced in 1996, all former staff members were dismissed and had to re-apply for the new TRA. More than a third were rejected because of prior misconduct (Fjeldstad 2003a, 165), and almost 1,200 earlier staff members, of whom 500 were former customs officers, were not re-employed. Members of the staff had to declare their private assets and business interests. Furthermore, an internal Investigation and Monitoring Unit was established (Fjeldstad et al. 2003, 15).[17] In contrast to practices in other revenue authorities, local, non-expatriate managers (paid by donors) were employed to turn Tanzania's tax administration around. Board and executive management positions were filled with Tanzanians. Apart from the Commissioner General and two other Commissioners, the management was recruited from outside the old state-integrated tax administration (Fjeldstad 2003a, 169).

In the beginning, the TRA's remuneration levels were considerably above-average and attracted well-qualified professionals. Fjeldstad (2002b, 8) reports that salaries in some staff categories were up to ten times higher than those for corresponding positions in the public sector. However, these initial pay differentials could not be maintained. Since nominal wages have remained constant between 1996 and 2000, the salaries for TRA staff have been significantly eroded by inflation, thus lowering motivation (Fjeldstad 2003a, 171).

The biggest impediment to merit orientation of the TRA's human resource management has been the resurgence of corruption within the organisation. Whereas corruption initially appeared to decline after establishment of the revenue authority (Fjeldstad 2003a, 165), it has now increased particularly among middle- and lower-level staff (Waller 2000). Analysts found one of the prime reasons for this in "corruption networks" between TRA staff and former tax officers who are now employed by the private sector as "tax experts" (BMZ 2003, 28; Fjeldstad 2003a, 173). It was also found that even some staff members at the TRA's Internal Investigation and Monitoring Unit were apparently willing to accept bribes (Fjeldstad 2003a, 171). Thus, despite the general impression that TRA managers are persons of integrity, recent studies indicate that initial successes in fighting corruption in Tanzania's tax administration have been reversed. In spite of considerable donor support, it has not been possible to fence off the tax administration from its corrupt environment.

3.3 Relationship with other State Organisations and Donors

Relations between the TRA and its principal, the Ministry of Finance, are generally viewed in more favourable terms than those prevailing in other African reform projects. In

17 This section is largely based on Fjeldstad (2003) and Fjeldstad et al. (2003).

particular, accountability relationships between the authority's Board and the Ministry of Finance functioned effectively immediately upon establishment of the TRA in 1996 (Clarke / Wood 2001, 84).

The TRA Board (including the chairperson, who is appointed by the President) consists of ten members, five are appointed by virtue of their positions (Fjeldstad et al. 2003, 14). The TRA management's efforts to consistently and transparently report on revenue performance against collection targets has been an important factor in ensuring that the principal-agent relationship with the Ministry remains solid (Clarke / Wood 2001, 84). Revenue targets are negotiated annually between the TRA and the Ministry of Finance, with input from the IMF. The Research and Policy Department of the TRA also plays a strong role, since it provides the empirical data on which revenue forecasts are made. It also sets collection targets for the TRA revenue departments after the total tax revenue budget has been agreed on with the Ministry (Fjeldstad et al. 2003, 12). However, the Ministry's capability to assess the revenue implications of legislative changes and to formulate realistic budgets is deficient (Fjeldstad et al. 2003, 75). Since donor support has focused less on the Ministry of Finance, the TRA's principal, the revenue authority and the IMF have a dominating position in the process by which its revenue targets are set.

While various donors have taken centre stage in reforming the tax administration in Tanzania, the Tax Administration Project (TAP) can also be seen as a prime example for inadequate donor coordination. Multilateral and bilateral donor agencies such as the World Bank, USAID, GTZ, DFID and the EU have been engaged in different parts of the reform project, with the result that representatives from the donor community and advisors to the TRA complain of a lack of clear focus and coordination in the TAP. The project was even managed for a long time from the World Bank's headquarters in Washington, DC rather than from a local office. This has slowed down implementation of the reform programme (Fjeldstad et al. 2003, 72; BMZ 2003, 7, 10, 33). In addition, the TRA itself failed to employ a responsible project manager for the TAP (BMZ 2003, 30).

In donor-dependent Tanzania, external actors also play a dominating role in determining tax policy and setting revenue targets. Among the IMF's structural performance criteria have been the formulation of a new Income Tax Act, a revision of the VAT threshold to reduce the number of VAT taxpayers, and a revision of the threshold for the presumptive tax (IMF 2004a, 52). The IMF has also exerted pressure to curtail tax exemptions. Finally, it has been a decisive actor in the annual revenue-target setting process between the TRA and the Tanzanian Ministry of Finance.

3.4 Tax Structure and Tax Exemptions

Tanzania inherited its tax system from the colonial period and began to introduce major changes only at the beginning of the 1990s (Luoga 2002, 52; Fjeldstad / Rakner 2003, 4). Widespread exemptions and prohibitive rates had made the tax structure difficult to administer. Consequently, the reforms were aimed at rationalising the tax system, broadening the tax base, and lowering rates (Fjeldstad et al. 2003, 13). The number of income tax bands was significantly reduced, and the highest marginal rate was lowered to 30 % of income. The rate for corporate income tax also stands at 30 %. In April 2004, the Parliament approved a new Income Tax bill. The law introduced self-assessment of the income tax (IMF 2004a, 37).

Although the plethora of exemptions was repealed, generous tax incentives have been granted to foreign investors, especially in the mining and tourism sectors (Fjeldstad 2003a, 167; Fjeldstad / Rakner 2003, 19). This has eroded the tax base. Fjeldstad (2003a, 173) perceives the rise in tax exemptions in recent years as an indication of limited political will to fight fiscal corruption and tax evasion in the country. As IMF documents confirm, the government plans to limit the Minister's power to grant exemptions to emergency situations only. The government has also established a working group to review taxes for mining companies (IMF 2004a, 12). On balance, however, tax policy reform in Tanzania during the last decade has succeeded in widening the tax base only to a limited degree.

A further part of the tax reform process was the introduction of a 20 % VAT in 1998. In order to facilitate the collection process, the VAT threshold was doubled, with a corresponding adjustment in the presumptive tax, on 1 July 2004 (IMF 2004a, 7). Since food commodities are commonly zero-rated and most agricultural inputs are exempted, VAT has not brought many new groups into the tax net (Fjeldstad et al. 2003, 73). In order to facilitate trade-led growth, export taxes were abolished in the financial year 1999/00 (Fjeldstad et al. 2003, 6). This was due to strong recommendations from the IMF. Import duties, commonly 30 % in the past, were also lowered to a maximum of 25 % (Fjeldstad / Rakner 2003, 20).

The Tanzanian reforms (rate reduction, simplification of the tax structure, wide-ranging abolition of trade taxes, introduction of VAT) generally mirror tax reforms in other countries in sub-Saharan Africa. However, despite comprehensive changes after 1998, the tax system in Tanzania remains complicated and opaque (World Bank 2002b, 133–136; Luoga 2002, 54). In this respect, the advice of the IMF has not been adhered to. In regional comparison, the Tanzanian tax system is characterised by higher tax rates but fails to realize its potential due to exemptions (BMZ 2003, 23). Tax policy reforms during the last decade in Tanzania have succeeded in widening the tax base only to a limited degree. Overall, however, they have provided better support for tax collection than the policies of the previous regime.

3.5 Revenue Performance

The TRA increased tax revenue by more than 30 % in its first year of operation (1996/97). The tax-to-GDP ratio rose from 11.4 % to 12.1 % between 1996/1997 and 1998. "Since there were only minor changes in the tax structure in this period, the growth in revenue must have been mainly due to the efforts of the tax collectors and other officials at the TRA", writes Fjeldstad (2003a, 170). However, this initial growth of revenue was not maintained. Revenue has declined to around 10 % of GDP in 2000 (see table 2). This pattern of initial increases in tax revenues followed by stagnation or even decline has also characterised tax administration reforms in Ghana, Uganda and Zambia.

The increase in the tax-to-GDP ratio has been the major performance indicator used by the government and the donor community, which expected tax revenues to grow by 1 % overall until 2002 and by more than 2 % up to 2004 (Fjeldstad et al. 2003, 12). However, this did not materialise. As already mentioned, this can be traced to the continued provision of tax exemptions and the high rate of corruption within the TRA. Only in the last two years have revenue collections exceeded projections in the budgets (IMF 2004a, 13). Key contributory factors have been strong economic growth and a substantial increase in imports. The IMF also found that these developments have recently been “underpinned by on-going tax administration reforms” (IMF 2006b, 7).

Table 2: Revenue Performance Indicators Tanzania, 1996/97–2005/06*

	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06
Tax revenue	11.4	12.1	10.9	10.1	10.0	10.9	11.0	11.7	12.4	13.0
Income taxes	3.3	3.2	2.9	2.7	3.1	2.6	2.7	3.2	3.5	3.6
VAT	3.1	3.3	2.7	2.6	2.6	4.1	4.2	4.4	5.2	5.5
Trade taxes	3.6	4.1	3.5	3.6	3.2	3.1	3.0	3.1	2.7	2.8

* In percent of GDP. Tanzania’s tax year begins on 1 July and ends on 30 June. Trade taxes include excise taxes. Data for 2005/06 are projected.

Sources: 1996/97–1999/00: Fjeldstad (2003a, 166); 2001/02–2002/03: IMF (2004b, 21; 2004a, 25); 2003/04–2005/06: IMF (2006b, 25).

Indirect taxes on goods and services are the major revenue base and contributed about 52 % of total tax revenue in 2000. Direct taxes on income and wealth are also important, and generated almost 40 % of total tax revenues in 2000 (Fjeldstad et al. 2003, 5). However, improvement and stabilisation of revenue was predominantly due to collection from the formally registered sector and not to expansion of the tax net, i.e. to the inclusion of formerly unregistered businesses. Overall, the tax rate may even be viewed as regressive inasmuch as the poor part of the population pays few direct taxes but is taxed through indirect taxes on goods (BMZ 2003, 23).

Compared to its neighbour countries, the revenue performance of Tanzania’s tax system remains poor. The tax-to-GDP ratio of 13.0 % projected for the most recent fiscal year is below the regional average of 15.6 % for 2003 (World Bank 2003, 14, sub-Saharan Africa excl. South Africa). There has not been consistent improvement since establishment of the TRA, although tax revenue overall has increased (BMZ 2003, 21). Although donor support has played an important role in the reform of Tanzania’s tax administration, improvements have been offset on the other hand by a narrow tax base, the granting of exemptions, and corruption levels within the TRA. This has significantly reduced revenue performance.

3.6 Summary: Tax Administration Reform in Tanzania

Tax administration reform in Tanzania has not been successful in significantly raising revenue performance. The country is rarely getting closer to fiscal self-sufficiency. In contrast to other revenue authorities, the TRA has been free of outright interference with its operations (for a comparison, see the case study of the Uganda Revenue Authority below). Nevertheless, political support for the new, semi-autonomous TRA has proven to be inadequate. Moreover, the political will to reduce the many exemptions provided by tax policies has been lacking.

The TRA management has not succeeded in curbing corruption within its organisation. The revenue authority is still closely integrated into corruption networks. “Strong” expatriate managers, backed by the donor community, might have been in a better position to fight corruption and to remove staff members involved in these activities. Due to direct donor involvement, they might have also been in a stronger position to organise effective government support for the TRA. However, technical assistance in itself was largely contraproductive, at least at the beginning. The multiplicity of active donors in the Tax Administration Project undermined a coherent reform effort. For instance, the introduction of information technology and taxpayer identification numbers was not coordinated. For a long time the donor community sent mixed signals and inhibited strengthening the TRA as a single, integrated authority. Since the TAP was managed from the World Bank’s headquarters in Washington, DC rather than from a local office, it was also largely detached from local conditions.

It is difficult to determine the respective importance of these factors for the rather disappointing results of tax administration reform in Tanzania. To date, it is difficult to predict whether the capability of the TRA will again weaken or whether the current phase of improvement will be maintained. There is almost no institutionalised political support for tax administration reform. However, there are at least some signs for a more consistent donor approach towards technical assistance in the future.

Main lessons to be learned from tax administration reform in Tanzania

- Tax administration reform can increase revenue performance only if tax exemptions are reduced to a minimum.
- Donor support must be coherently organized among the different donors involved and must be context-sensitive.
- Political support for tax administration reform needs to be strengthened and institutionalised.

4 Tax Administration Reform in Uganda

Since gaining independence in 1962, Uganda’s political development has mostly been characterised by political upheavals during which human rights were abused on a large scale. Uganda’s economy had been in decline for 15 years before the 1985–86 civil war, and much of its economic activity took place on the black market. The internal warfare (apart from Uganda's northern part) came to a stop only when Yoweri Museveni, the current President, came into power in 1986. Poverty in the post-conflict country was massive, and the economy was in a sorry state (Mackinnon / Reinikka 2002, 268).

Upon assuming power, President Museveni and his National Resistance Movement (NRM) took an anti-IMF stand and reimposed price and foreign exchange controls in order to curb inflation. When these measures did not succeed, he became convinced at the end of the 1980s that structural adjustment, market-based development and cooperation with donors such as the IMF were needed to reduce inflation and strengthen economic growth (Kjaer 2004, 396). These reforms paid off: there was a considerable improvement in macro-economic management during the 1990s. Inflation has dropped to a stable annual rate of about 5 % since 1994, and the economic growth rate has remained between 5 and 10 % since the beginning of the 1990s (World Bank 2005). Uganda has also gained from an influx of financial donor assistance since the end of the 1980s.

The rebuilding of the government's revenue administration from an almost complete collapse has been a key feature of Uganda's public administration recovery (Di John / Putzel 2005, 15). Preliminary work on reforming the Ugandan tax administration began soon after the downfall of Idi Amin's regime in 1980. Over the next ten years, at least two government commissions and three consultancy studies dealt with the problem of tax administration (Fjeldstad 2005b, 3). In September 1991, the Uganda Revenue Authority (URA) was formed as a semi-autonomous revenue authority (Coopers and Lybrand / Deloitte 1991). It was inspired by the IMF and by the example of Ghana (Chen / Reinikka 1999, 1; Therkildsen 2004, 68; De Wulf 2004a, 113). The aim was to reduce political interference with the tax administration and to improve revenue performance. The URA was the first tax reform project on the African continent which combines the Departments of Taxes and Customs under one roof (Therkildsen 2004, 59).

Since 1991, the British DFID's Uganda Revenue Authority Project (URAP) has supported the revenue authority in five principal areas: 1) setting up the authority, 2) introducing VAT (in June 1996), 3) strengthening the internal management systems of the administration, 4) providing technical and management training, and 5) improving the customs infrastructure. DFID also financed initial studies assessing the feasibility of a revenue authority for Uganda (Coopers and Lybrand / Deloitte 1991) and the hiring of expatriate managers for the URA (Gray et al. 2001b, 79, 87). The total value of financial assistance given to the project up to 2000 was 8.6 million £ (Gray et al. 2001b, 79).

Amidst political commitment and economic growth, the URA was initially a success. However, revenue performance has since stagnated at a comparatively low level. In its most recent Article IV consultation report, the IMF stated that "restructuring of the URA is key to the program [of fiscal consolidation]" (IMF 2005c, 21, see also 13).

4.1 Information Collection and Processing

Particularly in the first years of the URA's operation, the donor-supported reform project increased the auditing capacity of Uganda's tax administration. A prominent feature of the URA is its frequent tax audits, which take place either at the desk, in the field or both. According to a World Bank study conducted between 1995 and 1997, 68 % of all firms interviewed were audited during the period under review (Gauthier / Reinikka 2001, 7). This figure is extremely high and indicates "a serious lack of voluntary compliance and a low level of mutual trust between the tax authority and the taxpayer" (Chen et al. 2001, 293). 51 % of Ugandan firms disagreed with URA on their assessments and at least every third company had to pay additional taxes (Chen / Reinikka 1999, 21–22). In addition, the URA instituted a special unit, the Anti-Smuggling Protection Unit, to augment efforts to reduce smuggling and tax evasion (Ayoki et al. 2005, 10).

The collection of information by the URA has met with two main criticisms. On the one hand, analysts point to frequent complaints about taxpayer harassment. This is a recurrent topic in the newspapers. According to Therkildsen (2004, 73), the revenue authority "has brought a good deal of fear into the relationship". On the other hand, donor reports have argued, particularly in recent years, that audits of large taxpayers and anti-smuggling measures must be intensified in order to reduce tax evasion (Gray et al. 2001b, 90; IMF 2005c, 4).

The processing of taxpayer data has shown mixed success. In general, technical donor support has strengthened accounting and internal processing systems. This has limited the opportunity of tax officers to be arbitrary in dealing with taxpayers. Donor-supported measures included first steps to computerise the Income Tax Department in 1994 and automation of URA Customs by introduction of the ASYCUDA system and the special VENUS system in the VAT Department (1996) in order to record revenues and track receipts (Ayoki et al. 2005, 10). However, further development in the area of information processing seems to have stagnated. In 2001, a DFID report noted that future development "will depend on the more comprehensive adoption of modern information technology throughout the URA" (Gray et al. 2001b, 82). An uneven development of computerised systems was found, with direct taxation lagging behind Customs and VAT (Gray et al. 2001b, 95). The ASYCUDA++ version was rolled out in November 2003 (De Wulf 2004a, 124). Furthermore, the URA is only beginning to use cross-checking to identify tax evaders and to enforce registration and tax compliance (IMF 2005c, 14).

Donor support has been instrumental in providing information technology (computers, software) and staff training for building up the capacity to collect and process taxpayer information. However, these efforts have not been sustained after the initial investments were made. The comparatively low level of computerisation in the URA encourages tax evasion (Kangave 2005, 158).

4.2 Human Resource Management

When the URA came into operation in September 1991, all staff members of the former state-integrated tax administration were transferred to the new entity and employed on a probation basis (Therkildsen 2004, 70). Of the roughly 1700 people transferred, some 200 tax officers and 40 secretaries were dismissed during a screening process. In other words, more than 85 % of the staff was employed by the URA despite the fact that corruption was deeply entrenched in Uganda's state-integrated tax administration (Fjeldstad 2005b, 5, 9).

In contrast to the TRA's donors in Tanzania, donors in Uganda pushed for the employment of expatriates in high level positions of the URA. The reasons: foreign managers were thought to be less integrated into local social networks and less prone to political interference. They were also thought to be able to improve professionalism and integrity. In 1991, only two out of eight high-level positions were occupied by Ugandans (Hadler 2000, 14). The first Commissioner General (1991–1997) was a Ghanaian, and the URA was later led by a Swede (2001–2004).

However, this donor-supported recruitment of managers has not averted political interference with the recruitment of local managers (Therkildsen 2004, 73). The Ugandan who became Commissioner General in 1998, for instance, had family ties to the President. Despite donor protests, he was "handpicked" by the President (Therkildsen 2004, 70). In 2004, the IMF exerted pressure for the appointment of a new management of the URA (IMF 2005c, 16).

For a long time, salary levels allowed the URA to attract highly-qualified personnel. At the beginning of the 1990s, URA tax officers received wages 8-9 times higher than those of other civil servants (Di John / Putzel 2005, 15; Fjeldstad et al. 2003, 25). They were set at levels comparable to the high salaries paid at the Bank of Uganda. Nevertheless, remuneration was not adequately adjusted and has therefore been eroded significantly by inflation. In 2004, salaries at the Bank of Uganda were 40 % higher than those at the URA (De Wulf 2004a, 115). Since, as with other revenue authorities, the pay scale for tax officers is measured against the private sector, tax officers in Uganda feel underpaid. In consequence, the URA is increasingly losing qualified staff to international accounting firms (Gray et al. 2001b, 98). Furthermore, career promotion of tax officers is based on seniority or sometimes even on ethnic affiliations rather than on merit. Good performance often goes unrewarded, and bad performance often remains unpunished (Fjeldstad 2005b, 10).

Corruption has been the most serious deficiency limiting the merit orientation of URA human resource management. Ugandans consistently perceive the URA as one of the most corrupt government entities (Therkildsen 2006, 14). Support for this perception was provided by a survey of 243 firms in 1998. As many as 43 % of them reported paying bribes to tax officials occasionally or always (Gauthier / Reinikka 2001, 22). Even the Ugandan government seems to hold this view. President Museveni is reported to have called the URA "a den of thieves" in March 2000 (Therkildsen 2004, 82). In contrast to other revenue authorities, corruption also seems to be prevalent among senior tax officers. A report by the British DFID describes corruption as a "continuing problem area" and notes that corruption "is still very prevalent at all levels of the URA" (Gray et al. 2001b, 95). Due to the absence of prominent backing from the political sphere, donor support and pressure has on balance remained unsuccessful in comprehensively strengthening the merit orientation of human resource management in the URA.

4.3 Relationship with other State Organisations and Donors

The original URA Statute of 1991 created a relatively autonomous Board of Directors as supervisory body for the revenue authority (Fjeldstad et al. 2003, 23). However, the Board not only supervised the URA but also became directly involved in the authority's day-today operations. This caused conflicts between the Board, the Ministry of Finance[18] and the Commissioner General. In 1998, the Parliament restructured the relationship and put the Board under the control of representatives selected by the Ministry of Finance (Fjeldstad 2005b, 5). This significantly reduced the autonomy of the URA, which is supposed to be an operationally independent agent of its principal, the Ministry of Finance.

Since 1996, the URA has repeatedly failed to meet revenue targets set by the Ministry of Finance. In consequence, relations between the two organisations soured. While the Ministry has criticised the incapacity to meet the targets, the URA has claimed that these were unrealistic (Di John / Putzel 2005, 16).[19] Of particular significance has been the authority's increasingly tense relationship with the President, in contrast to the very strong personal support initially given by the Head of State to the URA.

There are at least two sources for this tension: First, the authority's reputation has progressively deteriorated. In a 1994 survey of Ugandan firms, the revenue authority was rated the most difficult agency which the business community has to deal with (Chen / Reinikka 1999, 20). Its semi-military forces for the prevention of smuggling and tax evasion have become hugely unpopular not only among big taxpayers but also with the general public. In consequence, political actors soon began to distance themselves from the URA. Second, the introduction of VAT in 1996 caused widespread resentment. Therkildsen (2004, 81, 83) argues that the President felt himself to be let down by the URA when his government tried in the face of strong resistance to implement the indirect tax. Tax revolts occasioned by the introduction of VAT hurt the government's basis of support and induced President Museveni to make the URA a scapegoat (Di John / Putzel 2005, 16). After this incident, he repeatedly and publicly blamed the URA for incompetence (Therkildsen 2004, 71).

As already noted, donor involvement in Uganda's tax administration reform has been strong. Since 1991, the British DFID's Uganda Revenue Authority Project (URAP) has been instrumental in setting up the URA. Technical support was also given to the Tax Policy Unit of the Ministry of Finance. However, the Ministry still lacks the expertise to calculate the revenue effects of legislative changes and to set appropriate revenue targets (Fjeldstad et al. 2003, 29). According to Mackinnon and Reinikka (2002, 288), pressure from donor agencies has "often been very constructive." The donor community has supported the autonomy of Uganda's tax authority. However, this has been a two-edged sword: On the one hand, donors have helped the URA to uphold its autonomy by making it less dependent on government financing. On the other hand, donors such as the IMF have been involved in setting high and sometimes unrealistic revenue targets (Therkildsen 2004, 76). The resulting lack of success in fulfilling these targets has contributed to the increasingly soured relationship between Uganda's government and the revenue authority after 1996.

18 The official name of the Ministry is "Ministry of Finance, Planning and Economic Development".

19 This result contradicts a 2001 report which stated that "there was a sound relationship between the authority and the Ministry of Finance, with close co-operation in respect of the technical issues of target setting and revenue forecasting" (Gray et al. 2001a, 113f.).

4.4 Tax Structure and Tax Exemptions

Reform of the tax administration went hand-in-hand with adjustments in tax policies. Before the creation of the URA, tax revenue was heavily dependent on the export tax on coffee and on high import duties. Since 1991, in accordance with the government's liberalisation strategy, the massive implicit and explicit export trade taxes were abolished (Gray et al. 2001b, 99; Chen et al. 2001, 271; Gloppen / Rakner 2002, 34). They have been replaced by increased indirect taxation and by improved collection of corporate and personal income taxes.

Income tax rates have also been subsequently lowered. In the 1970s, the maximum marginal rate was 87.5 %; today it stands at 30 % of income. Large companies currently also pay 30 % on taxable profits (Therkildsen 2006, 8). With the 1991 Investment Code, however, the government also instituted a range of tax incentives to compensate firms for major investments (Chen / Reinikka 1999, 5). These tax exemptions have fundamentally undermined the tax base.

In 1997, the Income Tax Act replaced the 1974 Income Tax Decree. The aim was to simplify the tax law and to eliminate the above-mentioned tax exemptions (Kangave 2005, 148). Furthermore, under IMF conditionality, a presumptive tax was introduced in 1998. It provides for a tax rate of 1 % on turnover of small businesses whose turnover falls below 50 million Ugandan Shillings per annum. According to a DFID report, this presumptive tax in principle provides a simple way of bringing business persons in the informal sector into the tax system. However, the report also noted a number of administrative problems with the application of the tax (Gray et al. 2001b, 114). Its relevance in terms of revenue has remained low.

In 1996, the government phased out the Sales Tax and Commercial Transaction Levy and introduced the broader-based VAT instead. The new tax was meant to significantly increase revenues from indirect taxes. The rate now stands at 18 % for most goods. However, most basic goods and services are exempted or zero-rated (Ayoki et al. 2005, 11; Fjeldstad et al. 2003, 10). With respect to customs duties, the policy reforms included the simplification and reduction of import duties as well as the phasing out of many exemptions and deductions (Fjeldstad et al. 2003, 10). Export taxes have been reduced from 11 % to zero. Uganda's trade taxes today are among the lowest in sub-Saharan Africa (De Wulf 2004a, 113, 126). Significant from a governance perspective has also been the abolishment of the local Graduated Personal Tax (GPT) in 2005. Originating from the colonial period, it was the most controversial tax in Uganda and inspired recurrent popular protests (Mackinnon / Reinikka 2002, 272). In 2001, the GPT was substantially modified and then abolished during the run-up to the presidential elections in 2006 (see analysis in Therkildsen 2006).

On balance, tax reforms in Uganda have significantly simplified the tax structure and lowered tax rates. The Income Tax Act of 1997 has also reduced the practice of approving discretionary tax exemptions. Nevertheless, the overall picture remains inconclusive. According to Fjeldstad (2005b, 17), the tax system in Uganda is "still complicated and non-transparent". The country's tax structure remains too complicated for effective implementation by the URA and leaves room for arbitrary application by tax officials. Apart from trade taxes, neither technical support (mostly rendered by the IMF) nor conditionality has been able to create a tax structure coherent enough for implementation by the URA.

4.5 Revenue Performance

From 12.6 % of GDP in 1970/71, the tax-to-GDP ratio dropped by nearly 50 % to a dismal 6.5 % in 1989/90 (Ayoki et al. 2005, 4). In its early years, the URA turned this development around. It contributed to an impressive growth of revenue, which amounted to 10.5 % of GDP by 1996/97 (IMF 2005c, 14). Most of this improvement was attributable to the establishment of the revenue authority, although economic growth and changes in tax policy also have been contributory factors. Nevertheless, since 1996 revenue has increased at a much slower pace and has stagnated at about 11–12 % of GDP in recent years (IMF 2005c, 14). This level is low by international and regional standards, even after taking into account the prevalence of poverty and the dominance of the informal sector in Uganda's economy.

The stagnation of revenue can be attributed to a combination of factors both outside and inside the URA. External factors include a temporary economic downturn, a low buoyancy in the tax system, a heavy dependence on agriculture, and the exhaustion of "easy" sources of revenue stemming from improved compliance of the formal economic sector (Gray et al. 2001b, 79). The continued application of tax exemptions may also have been a contributing factor. However, there is a consensus in the literature that it is internal factors which are dominant in explaining the URA's stagnating revenue performance. According to a DFID-funded report from 2001, "Further major progress in overall revenue performance will require both the cultivation of a tax-paying culture and progress in combating corruption in the service" (Gray et al. 2001b, 80, see also 92; Fjeldstad et al. 2003, 2; Clarke / Wood 2001, 84). This has not yet materialised.

The share of income taxes in total tax revenue has gradually improved from 10 % in 1990/91 to about 18 % in 1999/00 (Fjeldstad et al. 2003, 8). Nevertheless, direct tax returns have been depressed by a failure to broaden the tax base. Uganda's informal sector largely remains untouched by direct taxes. The URA has focussed on companies in the formal sector. This has led to accusations from the business community that the URA applies tax instruments inequitably between larger and smaller taxpayers (Gray et al. 2001b, 92). Additionally, the VAT yield has not shown consistent growth but has hovered around 4 % of GDP. In accordance with the liberalisation of the trade regime, revenues from the taxation of trade have been very low (see table 3).

Both in the government and among the donor community, as in other countries, the broadening of the tax base and the incidence of direct taxation – the most difficult tax type to levy – has rarely featured as a performance indicator. The tax-to-GDP ratio has virtually remained the only measure of success.[20] The empirical basis for target-setting appears to be weak. For example, the revenue target in 2001 was based on an exaggerated estimate of a 7 % growth rate for Uganda (Gray et al. 2001b, 91).

20 Therkildsen (2004: 77, emphasis in original) also maintains: "Increased revenue collection has been *the* key criteria against which the MOF, donors and some politicians have judged the URA's performance since 1991." See also Gray et al. (2001b, 85).

Table 3: Revenue Performance Indicators Uganda, 1996/97–2005/06*

	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06
Tax revenue	12.2	11.8	13.0	11.2	11.1	12.2	11.3	11.7	11.9	12.2
Income taxes	1.5	1.6	2.0	1.8	2.0	2.7	3.0	3.3	3.7	3.8
VAT	3.6	3.8	4.4	3.8	3.7	4.2	3.9	4.0	3.7	3.6
Trade taxes	1.2	1.1	1.3	1.2	1.4	1.1	1.1	1.0	1.0	1.0

* In percent of GDP. Uganda's tax year begins on 1 July and ends on 30 June. Data for 2005/06 are projected.

Sources: 1996/97–2001/02: Ayoki et al. (2005, 48) based on Ministry of Finance data, 2002/03–2005/06: IMF (2005c, 31).

4.6 Summary: Tax Administration Reform in Uganda

The URA reform project can be separated into two basic phases: The first, from 1991 to 1996, was characterised by strong political support and a remarkable improvement of capability. The authority pursued a policy of active data collection (which some stakeholders found too aggressive), and the tax-to-GDP ratio increased to around 11 %. This positive development, however, has not been sustained. In the second phase, political support, particularly from the President, waned and even turned into public hostility. The URA is increasingly being used as a political scapegoat (Di John / Putzel 2005, 16). Furthermore, the government has intervened with the revenue authority's operations and recruitment of staff. A high incidence of corruption, along with the heavy-handed collection approach, has clouded the relationship with the taxpaying public.

Today the URA is characterised by weak administrative capabilities. In conjunction with the complex tax structure, this has been largely responsible for poor tax revenues (IMF 2005c, 13; Kangave 2005, 149). The creation of a – heavily donor-supported – semi-autonomous revenue authority can be understood as an attempt of the government to demonstrate credible commitment to a) eliminate political intervention in the tax administration's activities and b) strengthen revenue performance (Fjeldstad 2005b, 14; in principle Taliercio 2004). In Uganda, this promise of credible commitment by the government has not been fulfilled; initial reform efforts have not been sustained.

The Ugandan example suggests that technical cooperation and conditionality can make it possible for donors to have an important influence in strengthening tax administration. This has in fact proven possible even in the adverse socioeconomic environment of post-conflict Uganda. However, the positive effects of donor assistance have also been dependent on government support. After the URA's autonomy became compromised, revenue performance stagnated despite donor efforts to the contrary (Fjeldstad 2003b, 4). The donor community and the Ugandan government today are faced with the need *to reform the* *reform project* started in 1991. The question of how to revitalise (and subsequently uphold) the government's commitment to the URA remains open.

Main lessons to be learned from tax administration reform in Uganda

- The activities of revenue authorities can be in conflict with the political interests of partner countries' governments. Moreover, because of their prominent position, they can easily be used as scapegoats for policy failures.

- Since the image of the revenue authority in the population and among politicians is of key importance for its success, donors should make strong efforts to improve the revenue authority's relationship to its environment.

- Even with strong donor support, semi-autonomous revenue authorities cannot be fenced off against political intervention and corruption without government support.

5 Tax Administration Reform in Zambia

Zambia experienced a steep economic decline following the first boom years after independence in 1964. By 2000, real GDP per capita had sunk to about 55 % of the 1975 level (World Bank 2003, 112). Up to the debt relief in 2005 under the Heavily Indebted Poor Countries (HIPC) initiative, Zambia was one of the most heavily indebted countries in sub-Saharan Africa (IMF 2005b). For the first two and a half decades after independence, the political development of Zambia was dominated by the United National Independent Party (UNIP), which pursued a state-led development strategy that included nationalisation of the economy's mainstay, copper production. This policy swiftly changed after the democratic transition. The new Movement for Multiparty Democracy (MMD) government in 1991 announced an ambitious, donor-backed programme of liberalisation, stabilisation and privatisation.

A prominent part of the reform package was the strengthening of the tax administration. On 1 April 1994, the government launched the Zambia Revenue Authority (ZRA), a semi-autonomous agency, and transferred revenue collection from the traditional public administration under direct control of the Ministry of Finance to this new entity. This strengthening of Zambia's tax administration was also a donor requirement: at the beginning of the 1990s, the IMF made the strengthening of internal revenue collection one of its conditionalities for the provision of new loans (Hill 2004, 141; Gloppen / Rakner 2002, 32).

The ZRA has also been strongly supported by technical assistance. Up to 2004, the British DFID as the main bilateral donor had provided technical assistance worth 15.8 million £ through its Zambia Revenue Authority project.[21] The rationale for this was to finance technical equipment such as computers, to provide expertise through short-term advisors, and to support staff training (Hoover / McPherson 2004, 392; Kasanga 1996, 20). Most

21 The scope of DFID intervention has expanded considerably beyond mere support of the ZRA. Since 2000, the DFID has also supported the Tax Policy Unit within Zambia's Ministry of Finance and National Planning and has assisted local NGOs to build knowledge on taxation issues. Therefore the sum was not awarded to the ZRA alone.

important was the provision of a foreign management team for the ZRA (see the chapter 5.2 below).

Analyses show that Zambia's political elite under President Chiluba (1991–2002) misused state resources in order to maintain their rule.[22] Thus Zambia has received low scores on Transparency International's Corruption Perceptions Index from 1998 to 2006. Zambia is currently ranked 111th out of 163 countries assessed (Transparency International 2006). Despite this unfavourable environment, the ZRA is widely seen as a successful tax administration reform project in sub-Saharan Africa.

5.1 Information Collection and Processing

The ZRA has pursued an active, even aggressive approach to the collection of information on taxpayer income. Compared to its state-integrated predecessor, this tax authority has massively increased the number of auditors and has closely supervised large companies, which are the most important source of revenue. Insufficient coordination has further increased the frequency of audits carried out by the different divisions in charge of direct taxes, VAT and – to a lesser extent – customs and excise. These *ad hoc* and uncoordinated surveillance efforts feature among the most common business complaints with respect to the revenue authority (von Soest 2007, 358). Two Flexible Anti-Smuggling Teams (FAST) have, as in the case of other revenue authorities, been "effective in forming a highly visible threat to smugglers allowing for improved deterrence" (Delay et al. 1999, v). In November 2000, the ZRA set up the Central Investigations Unit, which deals with serious cases of tax evasion and supports the investigative units of the ZRA's three tax divisions. However, the ZRA has generally not acted as an integrated organisation in exchanging information between different departments. Information concerning one tax type is almost never cross-checked with that of another (Hill 2004, 126, en. 27).

Information technology in particular is regarded as a necessary tool for making effective use of taxpayer data and reducing customs officials' discretion (De Wulf / McLinden 2005, 309). Accordingly, computerisation of the Customs Division has been one of the first priorities of donors and the ZRA management. The computer programme ASYCUDA, which standardises the customs clearance process, became operational in early 2000, with full completion of the implementation project in April 2001 (Republic of Zambia 2001, 21; Hill 2004, 141). With substantial technical donor support, the software system was later upgraded to its current version ASYCUDA++.

Computerised systems are also in place for processing VAT. They allow the responsible officers to disaggregate revenue performance by income group, occupation and gender and to predict future risks for revenue (Gray et al. 2001a, 32, 42). After some delays, the ZRA in 2004 finally introduced the "Integrated Tax Administration System" (ITAS) computer programme, which merged the old VAT software with the database of the Taxes Division. This integration is useful, since defaults in payment of direct taxes tend to be strongly correlated with evasion of indirect taxes and vice versa (Gray et al. 2001a, 43). Again, the

22 See Burnell (2001), Transparency International Zambia (TIZ 2003) and von Soest (2006) on the abuse of public funds. Further instances are presented in Rakner / Svåsand (2005, 93–96).

acquisition of software was financed to a large degree by DFID. Nevertheless, IT-experts from the ZRA itself were also engaged in customising this information technology to match the authority's needs.

It appears that the tax administration reform project has brought significant progress in establishing taxpayer liabilities. The computerisation of Zambia's tax administration has been one of the focal areas for donor support. In conjunction with training programmes for tax officers, the drive to improve the collection and processing of taxpayer data has largely been successful. Through consistent training, the project has built up technical expertise within the ZRA to use the information technology which has been installed.

5.2 Human Resource Management

From the outset, the ZRA has pursued its own recruitment policy independently of the rest of Zambia's civil service. Before the authority was launched, every civil servant had to reapply in order to be employed by the new institution. Recruits for the well-paid and, in turn, highly sought-after positions at the authority are hired on the basis of interviews and aptitude tests.[23] Later, the ZRA introduced a minimum qualification policy, meaning that every employee, starting from the middle level, must hold a diploma or a higher degree from university. Many of the ZRA's high-ranking officers today hold a degree from the Britain-based Association of Chartered Certified Accountants (ACCA).

The authority's basic orientation was established by managers from outside the country; this was financed by the DFID. None of the four most senior managers in 1995 was Zambian. It was thought that expatriate leadership would be less responsive to local corruption networks and to interventions from the political arena (Kasanga 1996, 21; Delay et al. 1999, 23; Gray / Chapman 2001, 40). It was only in February 2002, nine years after the creation of the ZRA, that a Zambian took over the post of the Commissioner General. It appears that this foreign management has indeed provided a "buffer zone" (Fjeldstad 2005a, 2) against influence from the political level. The strong Commissioner General took firm action against corrupt staff and established a programme for recruiting and training qualified staff (Delay et al. 1999, 16). The reform project has also been successful in preparing local managers for leadership positions.

The ZRA's human resources policy represents a substantial departure from the classic public administration approach of life-long employment and promotion in line with seniority. Zambian tax officers are employed only on the basis of five-year contracts (in the beginning, the period was three years). Management may without explanation decline to offer a new contract. This has been a much-debated issue within the organisation, whose management views the contract system as a necessary incentive for creating a business-driven work ethic. Today, after more than ten years of operation, most of the authority's employees have worked for the private sector before and see themselves as well-qualified professionals. This perception is generally mirrored by business representatives who ac-

23 The ZRA salary for certain positions is approximately eight times higher than for similar positions in the public sector (von Soest 2006, 109).

knowledge that Zambian tax officers today are better qualified than civil servants in the core public administration (section based on von Soest 2006, 105–110).

One of the ZRA's biggest achievements has been the separation of recruitment of low and middle level staff from Zambia's political environment. A major factor in this was the donor-funded employment of a strong expatriate management team, which found acceptance both within the revenue authority and in the Zambian government. In contrast, the recruitment and promotion process of local managers has been more opaque and seems to be influenced by government.[24] This attests to the fact that it is impossible – even for a revenue authority with a comparably high degree of merit orientation among staff – to insulate itself completely from the political level.

5.3 Relationship with other State Organisations and Donors

As with other revenue authorities, the ZRA's main organisational principle is its managerial autonomy. The executive Commissioner General, appointed by the Zambian President, is alone responsible for the collection of revenue. He or she reports to a nine-member Governing Board (Republic of Zambia 1996b, sec. 10 (1), (3)). The revenue authority must meet revenue targets set out in annual negotiations with its principal, the Ministry of Finance.[25] Meeting these revenue targets is the key task and measure of success of the organisation (Hill 2004, 143).

However, it appears that the Ministry is almost incapable of evaluating revenue performance and determining revenue targets on its own. With its Executive Support Unit, the ZRA is not only able to analyse tax policy and to forecast the revenue impacts of policy changes but has also has played a major role in formulating Zambia's tax policy and making revenue predictions. There is a significant imbalance in the abilities of the Ministry and the revenue authority, in favour of the latter (von Soest 2006, 109). Furthermore, the high salaries and technical equipment of the ZRA have created some resentment within the Ministry of Finance. For their part, tax officers have expressed disregard for the abilities of the Ministry. The relationship between the two organisations has therefore been somewhat tense. DFID's efforts to strengthen the Tax Policy Unit at the Ministry have shown mixed results, not least because the ZRA occasionally recruits officers from this unit.

The IMF's Fiscal Affairs Department began providing technical assistance to Zambia's government as early as 1991, "mostly in tax administration, and expenditure management control" (Muzondo et al. 2001, 11). The British government started its support for Zambia's tax administration in 1992 with the funding of initial studies which in turn recommended establishment of the semi-autonomous revenue authority (Coopers and Lybrand 1992). Up to September 2004, the manager of DFID's Revenue Institutions in Zambia

24 The close connection between the ZRA's management and the Zambian government became obvious when a Commissioner directly appealed to the President after being dismissed and was reinstated following pressure from the Presidency (Times of Zambia 20.5.2004; 25.5.2004). At the beginning of 2007, moreover, President Mwanawasa, rather than the ZRA's Governing Board, terminated the contract of the Commissioner General (Times of Zambia 3.1.2007).

25 The official name of the Ministry today is "Ministry of Finance and National Planning".

Enhanced Support (RIZES) project had his office *within* the revenue authority's headquarters.

This close collaboration has served to avert instances of political intervention in the revenue authority's operations. A former expatriate Commissioner General has reported that he at times appealed in fact to the British Ambassador or the local IMF Representative in order to protect the interests of the ZRA vis-à-vis the Zambian government (von Soest 2006, 100). This external control has been much weaker regarding the Zambian Commissioner General, whose salary is not financed by DFID. Since the ZRA has lost much of its "exterritorial" status, the political environment is now able to exert more pressure on the ZRA. This points to the crucial importance of donor influence in pressing for the revenue authority's freedom to operate along rational-legal lines and for the preservation of its special status.

5.4 Tax Structure and Tax Exemptions

In accordance with its liberalisation policy and private sector-based development strategy, the new MMD government announced a tax reform immediately in its first 1992 budget speech (TPTF 1992, 1; Kasanga 1996, 3, 5; Hill 2004, 108, 112). The number of income tax bands was reduced from seven to three, the highest marginal company tax rate was lowered from 50 to 35 %, and penalties for tax defaulters were increased (Republic of Zambia 1992, 19). These measures brought significant improvements for the tax administration. The direct taxation system is now fairly simple and straightforward, the highest income tax rate stands at 37.5 %; company taxes are 15 % for farming, 35 % for manufacturing, and 40 % for banks. The exemption threshold for income tax in 2005 was raised to 280,000 K per month (Republic of Zambia 2005, 19).[26]

However, fundamental problems remain with respect to Zambia's tax policy. First, the granting of tax exemptions to particular companies has affected the coherence of the tax structure. Although tax incentives for businesses have been reduced since 1993 (Deloitte 1997, 132), it is still possible for investors to strike bilateral deals with the Ministry of Finance. The procedure has been opaque and has hardly been rule-based. At its peak in 1998, the Zambian government had granted tax exemptions to 500 large corporations (Gray et al. 2001a, 22). This significantly reduced the potential tax income. The widespread exemption of the copper industry from taxation, for instance, means that Zambia has rarely benefited from the high world copper prices of 2004 and 2005 (IMF 2006c, 11).

Second, since the advent of multi-party democracy in 1991, the government has largely desisted from formulating a specific tax policy for the large informal sector of the economy. Both the agricultural and the non-agricultural informal sector, which account for almost all employment, have remained outside the direct tax net (Gloppen / Rakner 2002, 34, 39). Only with the 2003 budget did the government announce that small-scale traders, marketers, unregistered mini-taxis and rental income would increasingly be targeted for taxation (Republic of Zambia 2003, 14). In 2004 it introduced a presumptive tax of 3 %

26 This amount roughly equalled 60 US$ in January 2005 prices.

for businesses with an annual turnover of 200 million K and below (Republic of Zambia 2004, 19).

Indirect taxation of consumption constitutes the second pillar of a modern tax system. The government on 1 July 1995 successfully replaced the sales tax with a 20 % VAT; this was reduced to 17.5 % in 1997. However, the government also reduced its tax take by granting more than 100 exemptions (Gloppen / Rakner 2002, 34; Hill 2004, 120; Muzondo et al. 2001, 15). Although the 2004 budget eliminated voluntary VAT registration of small farmers, following strong IMF advice (Republic of Zambia 2004, 21), the scope of exemptions of Zambia's VAT has remained wide.

The tariff structure seems to be more favourable. In 1993, the government lowered tariff rates for different types of import products from 100 % to 20 %, 30 %, and a maximum rate of 40 % (Republic of Zambia 1993, 16). The 1996 budget again significantly reduced import duty rates to 5 %, 15 % and 25 % while eliminating most exemptions as "a means of sustaining revenues and reducing distortions" (Republic of Zambia 1996a, 12). The customs structure today is relatively simple to administer and supports trade.

5.5 Revenue Performance

As a consequence of severe economic crises in Zambia *and* internal deficiencies of the tax administration, the tax-to-GDP ratio dropped by nearly 50 % from around 30 % at the time of independence to 15.3 % in 1993, before the start of the ZRA (Coopers and Lybrand 1992, par. 1; World Bank 2003, 15). Indicators show that the ZRA initially improved important aspects of revenue performance (the tax-to-GDP ratio went up from 15.3 to 18.7 % in the ZRA's first year of operation (World Bank 2003, 15)), but that in the following years the tax-to-GDP ratio remained largely stagnant (17.5 % in 2004, see table 4).

As a DFID-funded study stated, it has been a success just "to maintain the revenue/GDP ratio, despite the poor macroeconomic situation" (Gray et al. 2001a, 2, see also 11). This is echoed by IMF consultants, who argued that "Zambia's tax effort is good compared with that of selected countries in its region" (Muzondo et al. 2001, 11).[27] Since 2000, however, Zambia's economy has grown by 4.4 % on the average with no significant increase in revenue collected (IMF 2005d, 55). At the beginning, major factors depressing the tax share certainly lay beyond the ZRA's influence and must be attributed to its environment, e.g. tax policy and economic development (Rakner / Gloppen 2003, 97, en. 6). Yet, in recent years the ZRA has been less able to participate in the growing tax base, measured relative to GDP.[28]

27 In 2003, the average for sub-Saharan Africa excluding South Africa was 15.6 % (World Bank 2003, 14).

28 The tax-to-GDP ratio, as the name indicates, is a measure of tax collected *relative* to the GDP; however, the *ratio* tends to rise in an expanding economy as taxable income, spending and corporate profits increase. As a consequence, the tax-to-GDP ratio also tends to improve without the necessity of administrative improvements and vice versa in a declining economy (Economist 2006). In Zambia, the tax-to-GDP ratio has not increased in line with economic growth. This must be at least partly attributed to the ZRA.

The ZRA has also left the administratively (and politically) demanding task of expanding direct taxation unresolved. According to a DFID-commissioned study, the revenue authority's impact on direct tax incidence has remained "modest" (Gray et al. 2001a, 12; see also Gloppen / Rakner 2002, 31). Income tax collection has never amounted to more than 8 % of GDP – not even in the most recent years with comparatively strong economic growth (see table 4). Revenue collection has largely been confined to formalised economic activity. As a result, Zambia's tax gap, i.e. the difference between tax potential and taxes actually collected, remains large.

Table 4: Revenue Performance Indicators Zambia, 1996–2006*

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Tax revenue	19.0	18.8	18.1	17.2	19.2	18.6	17.5	17.3	17.5	17.0	16.2
Income taxes	5.6	5.8	6.3	6.5	6.3	7.5	7.6	7.9	7.8	7.6	7.6
VAT	3.5	3.6	3.3	3.3	2.3	2.1	2.1	1.9	1.7	1.9	2.0
Trade taxes	6.1	5.6	4.7	2.4	3.4	4.1	5.1	5.1	5.6	5.1	4.2

* In percent of GDP. Zambia's tax year begins on 1 January and ends on 31 December. Trade taxes include sales tax/VAT on imported goods. Data for 2005 are preliminary, for 2006 are projected.

Sources: 1996–2002: IMF (2004c, 35), 2003–2006: IMF (2006d, 22).

On balance, the ZRA's revenue performance has been similar to that of other African revenue authorities: a first phase of increased tax collection was followed by stagnation or even decline. Additionally, the collection of income taxes has remained at a comparatively low level. Nevertheless, the ZRA's performance is primarily measured through the tax-to-GDP ratio and the fulfilment of revenue targets set in annual negotiations. Among other things, these indicators, set also by donors, do not capture the widening of the tax net. This would be desirable from a governance perspective.

Furthermore, tax administration reform in Zambia (as in other developing countries) comes at a high cost: Since 1998, the ZRA's cost of collection has been well above 3 % of tax revenue (data provided by the ZRA). The expenditure has also included necessary capital investments in technical equipment, e.g. information technology. However, the collection costs have remained in the range of 3–4 % of tax revenue. The initial target in the ZRA project documents agreed upon by the Zambian government and the DFID stood at only 1.9 % (Devas et al. 2001, 216).

5.6 Summary: Tax Administration Reform in Zambia

The ZRA has been closely donor-monitored and dependent on support from the political sphere. On the whole, the Zambian government has sustained the ZRA's independent position. However, it is still possible to satisfy political demands through tax exemptions and – most importantly – through state expenditures. Since most Zambians work in the informal sector, they have rarely been forced to pay direct taxes. The introduction of VAT went smoothly and was cushioned by a considerable number of exemptions. However, there are signs that taxation is gaining political relevance. High taxes for civil servants and exemptions for foreign investors, particularly in the copper industry, were a major campaign issue in the run-up to Zambia's 2006 national elections (Times of Zambia 21.9.2006; 7.11.2006).

Some features stand out with respect to the role of donors in supporting Zambia's comparatively successful tax administration reform: first, technical support was predominantly rendered by *one* bilateral donor, the DFID. Accordingly, there was not a plethora of competing external interests, as for example in Tanzania. Second, a long-term approach was pursued. DFID support to the ZRA formally ended in March 2005, with some project activities running until the end of the year 2005. That means that technical assistance was provided for over eleven years. Third, the DFID assisted other important stakeholders, such as the Ministry of Finance (albeit less successfully) and civil society organisations in order to strengthen their ability to engage in tax (administration) issues. Fourth, the project was successful in training local staff and local managers. Of particular importance in this regard was the expatriate management team, which was accepted within both the government and the revenue authority.

However, the ZRA has increasingly lost its special, donor-supported status. As a consequence of the DFID's exit in 2005 and the complete takeover of a Zambian management team, external actors have had declining leverage in the effort to create a tax administration which operates along rational-legal lines. Political support for the revenue authority in Zambia currently depends on the government and the respective President and is not strongly institutionalised.

Main lessons to be learned from tax administration reform in Zambia

- A low number of donors involved in technical assistance and a high degree of coherence are crucial for successful tax administration reform.

- Technical assistance must pursue a long-term and comprehensive approach and must also incorporate the Ministry of Finance and civil society.

- Even when foreign managers are employed, strong political support is the most crucial variable in determining the success of donor-supported tax administration reform.

6 Tax Administration Reform in Africa and Recommendations for further Donor Support

Tax administration reform has been of crucial relevance in Ghana, Tanzania, Uganda and Zambia. It has the potential to reap major fiscal benefits for these heavily-aid dependent countries and might also induce a substantial governance dividend through increased domestic tax collection. However, reforms described above in four case studies have brought only mixed results. Overall, donor support has not yet been successful in supporting the improvement of tax administration capability on a sustainable basis.

Accordingly, revenue performance in Ghana, Tanzania, Uganda and Zambia has been mixed: In each case, a phase of strong initial increases was followed by stagnation or decrease. This is not only to be correlated with negative socio-economic development and tax policy changes but must also be attributed to problems in the revenue authorities, such as increasing corruption, loss of qualified staff, inadequate integration of the different departments, and, at least in the Ugandan case, political intervention.

This analysis provides crucial lessons for different elements of donor-supported tax administration reform in Africa. On this basis, recommendations for making future donor assistance more effective in this area are made in the following.

6.1 Collection and Processing of Taxpayer Data

Technical assistance generally promotes a more active auditing approach and frequently includes the provision of hardware and software needed to process tax information. Nevertheless, the collection of information has been almost exclusively confined to the formal, registered sectors of the economies under study. Furthermore, the four countries analysed, with their high level of indebtedness and their low socio-economic development levels, have been almost completely reliant on donor financing for capital investments in tax administration.

Too aggressive an auditing approach is detrimental to taxpayer rights

Active collection and assessment of taxpayer data in order to determine tax liabilities has been a prime rationale of reform on the African continent. In all countries, tax evasion of all types was widespread before the creation of semi-autonomous revenue agencies. Donor support has contributed to a massive increase in the number of auditors, who in turn have focused on monitoring large companies, the most important source of revenue. Donors have also supported the formation of special investigation units which deal with serious cases of tax evasion. Therefore, technical assistance has been instrumental in turning Africa's formerly passive tax administrations into revenue authorities which actively audit taxpayers and collect taxpayer information.

Nevertheless, taxpayers in the formal sector of the economy often feel harassed by this aggressive auditing approach, which concentrates on close supervision of the most important corporate taxpayers. This approach has at times been detrimental to the rights of such visible businesses; instruments for safeguarding their rights have often remained underdeveloped. On the other hand, the large informal sector in African countries often remains outside the tax net, since the “return on investment” for revenue authorities which operate in line with business principles is generally low.

Recommendation: Active collection of taxpayer information is necessary in order to reduce tax evasion in hard-to-tax environments. Nevertheless, it appears that the pendulum has swung too far in the countries studied here. Donors should therefore increasingly support taxpayer associations and similar organs of civil society in order to provide a better check of revenue authorities’ auditing efforts. Better training is also needed to improve the service orientation of tax officials in reformed tax administration.

Integration is of key importance for the exchange of information

Technical donor support for tax administration reform has also centred on accounting and data processing systems. One prominent feature has been the provision of information technology (“computerisation”) in order to improve the utilisation of taxpayer data and to eliminate personal discretion from tax officers and customs officials in particular.

Donor-supported measures have included steps to computerise the Income Tax Departments, automated customs procedures, commonly by introducing ASYCUDA (“Automated System for Customs Data”),[29] and special systems for VAT Departments in order to record revenues and to track receipts.

However, the processing of data has often stagnated. Information systems have not been developed further, capital investments have heavily relied on donor funds. Furthermore, revenue authorities are only beginning to use the potential for cross-checking one tax type with another in order to identify tax evaders and enforce registration and tax compliance. In contrast to the donor objective of supporting coherent revenue authority structures, these authorities have generally not acted as integrated organisations in terms of exchanging information between different departments.

Since there are often no properly maintained databases of taxable persons, property or other possessions, it is very difficult to mobilize taxes from outside the registered, formal sector of the economy. While donor support has therefore led to a better utilisation of taxpayer data within revenue authorities, the use of outside sources such as registration of company data has often been wanting. Greater success has been had with the establishment of Large Taxpayer Units (LTU), which often raise more than 70 % of all tax revenues. The IMF strongly advocates these LTUs as a “good practice” for increasing revenue performance and often makes their introduction a conditionality for further financial aid.

Recommendation: Supporting the integration of tax departments is of key importance for greater efficiency in the collection and utilisation of taxpayer information. More sophisticated means of data processing, such as cross-checking tax data with outside data sources, is dependent on computerisation in other areas of public administration. Donors should therefore consider supporting the most important databases such as the registries of companies as well.

29 UNCTAD’s ASYCUDA system standardises the customs clearance process and has been installed in over 80 developing countries worldwide.

Technical donor support requires coherence

Various donors have provided technical assistance to newly-established revenue authorities on the African continent. Often these efforts were rather uncoordinated. In some cases, different information technologies and taxpayer identification numbers were used. In these instances, donors have thus exacerbated the lack of coherence between different tax departments. The existence of different information systems has also precluded systematic auditing processes across different tax types.

Recommendation: In successful reform projects, technical support was predominantly rendered by *one* bilateral donor. This serves to prevent a plethora of often competing external interests. From the outset, therefore, donors should pursue a proactive approach of coordinated technical support to tax administration reform.

6.2 Human Resource Management

Merit orientation of human resource management has emerged as a particularly important variable which determines the success of reforms. Remuneration schemes, corruption levels and expatriate management are crucially important factors in this regard.

High remuneration schemes have often been impossible to maintain

In many African countries, the conditions of employment of tax officers had severely deteriorated before the establishment of revenue authorities. Following donor advice, remuneration levels and other employment conditions of newly-established revenue authorities were highly favourable in the beginning and served to attract well-qualified professionals. Nevertheless, initial pay levels could not be maintained. Nominal wages in many cases have been eroded by significant inflation.

Since the yardstick for officials who work for revenue authorities (which operate along business lines) is the private sector, these employees commonly feel underpaid. In consequence, reformed tax administrations have often found it difficult to recruit and retain highly qualified staff. They are increasingly losing qualified tax officers to international accounting firms and other private sector companies. This has reduced the effectiveness of technical support rendered to revenue authorities.

Recommendation: Revenue authorities have not *per se* been a remedy against deteriorating employment conditions. The opportunities for donors to provide support in this regard appear to be limited. A prime means, however, would be to stress to partner governments the importance of attracting and retaining qualified tax officers as a means of improving state revenue. Maintaining favourable employment conditions is fundamental in this regard.

Corruption poses a major threat to human resource management

One of the biggest impediments to merit orientation of human resource management in the four African revenue authorities analysed here has been the resurgence of considerable corruption. Some revenue entities, such as the Uganda Revenue Authority, laid the basis for this disappointing result from the start: they did not consistently remove corrupt and underperforming staff, but rather took over most officers from the former state-integrated tax administration.

Due to donor advice and pressure, however, most countries have pursued a more radical (and effective) approach: all former tax officers were dismissed and had to re-apply for the new authority. Aptitude tests and job interviews were put in place to recruit qualified and motivated staff. In some cases, more than a third of the former staff was rejected because of prior misconduct.

Despite donor-supported staff training, computerisation, and this tough stance, however, bribery and corruption have again become pronounced after an initial period. Analysts have found the establishment of “corruption networks” between revenue authority staffs and former tax officers now employed by the private sector as “tax experts” to be one important reason for this. This assertion seems to be particularly valid for customs departments, which are characterised by direct interaction between employees and taxpayers. Generally, revenue authorities have been unable to insulate themselves from their unfavourable environments. Furthermore, it appears that political and administrative efforts have often been insufficient to fight corruption.

Recommendation: Donors should provide expertise on how to detect corruption within tax administrations. Internal investigative units should be explicitly supported. Hiring expatriate personnel for these units, potentially from other African countries, might also be a viable option. The fact remains, however, that a revenue authority principally struggles to keep internal corruption at low levels when such a project is not flanked by government-wide activities to eradicate corruption, i.e. attempts to create a more favourable environment.

Foreign management personnel, although potentially instrumental in making improvements, is still dependent on political support

One of the most notable aspects of donor support of revenue authorities has been the recruitment of management teams from outside the country in order to limit interference from the political sphere and to strengthen merit orientation in hiring and promoting staff.

It appears that in comparatively successful reform projects, such as the Zambia Revenue Authority, expatriate managers have indeed functioned as a “buffer zone” (Fjeldstad 2005a: 2) against influences from the political level. In that case, the foreign Commissioner General took firm action against corrupt staff and established a programme of recruiting and training qualified staff. The reform project has also been successful in preparing local managers for leadership positions.

In other countries, donors have also pushed for the employment of expatriates in high-level positions of the revenue authority. However, donor-funded recruitment of foreign managers has not always averted political interference with the revenue authority’s operations (as the Ugandan example demonstrates).

Recommendation: Although expatriate managers often serve to strengthen professionalism, they are of themselves not a determinant to success or failure of tax administration reform. Foreign managers are dependent both on domestic political commitment in partner countries and on consistent support from donors. Commitment on the part of partner countries has been volatile and inconsistent, as evidenced by the widespread provision of tax exemptions. Donors should therefore aim at actively strengthening the support base for tax administration reform through collaboration, for example, with key actors in civil society.

6.3 Relationship with other State Organisations

The creation of semi-autonomous revenue agencies not only changes the institutional setting of tax collection but also the relationship between the administrative and the political levels of government. Indeed, limiting opportunities for political intervention has been one of the prime rationales for the establishment of revenue authorities. In this respect, the relationship of such a semi-autonomous revenue agency with the Ministry of Finance is of fundamental importance.

The roles of a revenue authority, its board, and the respective Ministry of Finance must be clearly delimited

A revenue authority's most important organisational principle is that of managerial autonomy in collecting state revenue. As with private sector companies, the management of a revenue authority is usually supervised by a board, often named the Board of Directors or Governing Board. The third relevant party is the Ministry of Finance, which expects a certain amount of revenue to be delivered. Thus, the executive Commissioner General, often appointed by the state president, is responsible for the collection of revenue. The revenue authority must meet revenue targets which are set in annual negotiations with the Ministry of Finance. Meeting these revenue targets is the key task and the measure of success of the organisation.

Donors regularly funded initial studies, which assessed the feasibility of semi-autonomous tax administration and its particular design. It appears that – despite the explicit goal to outsource a key state function – the broader implications of this institutional shift have found less attention. Often, the roles of the management, the supervisory board and the Ministry of Finance have not been clearly delimited from the outset. The formal foundations for regulating cooperation have remained inadequate. Donors seem to have underrated these delimitation problems. Furthermore, the high remuneration and the equipment of the revenue authority staff have created some envy and resentment within the ministries of finance.

A second problem has been the role of boards *vis-à-vis* the management. Often, members of the supervisory boards have been engaged in managing the day-to-day operation of the revenue authority, thereby weakening the position of the Commissioner General and his or her managers. This has caused inherent conflicts between the board, the Ministry of Finance, and the Commissioner General.

Recommendation: Donors shall increasingly provide expertise for the clear formal, i.e. legal delimitation of the roles of different parties involved in tax administration reform. When planning major support for tax administration, it is necessary to incorporate not only the perspective of tax administration, but also of its supervisory institutions and the government.

Communicating the effects of prospective reforms

Outsourcing the collection of taxes from the core state structure constitutes a major change. Experience has demonstrated that there is often considerable initial resistance to this institutional shift among civil servants and powerful economic actors who profit from a weak tax administration. Tax officers regularly perceive the newly created authority as a threat to their positions. This seems to have been underrated by the donors as well as by partner governments. The outsourcing of tax administrations has often been inadequately communicated and explained to tax officers and the general public.

Often, the dire financial situation in partner countries has been the trigger for radical, donor-supported tax administration reform. Such situations make it easier to overcome resistance. Nevertheless, interest in such reforms has often waned after this initial impulse. The example of Ghana is important in this respect: despite strong donor advice to the contrary, the country maintained three largely independent revenue authorities for income taxes, customs duties, and excise and VAT. Since 1998 these authorities have operated under a strengthened holding structure but have remained independent from each other. After an initial window of opportunity for wider changes, inertia of tax administration structures seems to be strong.

Recommendation: Communicating the effects of prospective reforms to the relevant constituencies such as tax officers, taxpayers and governments is of prime importance for ensuring the success of donor-supported tax administration reform. It is recommended that before starting assistance donors should a) identify important stakeholders and vested interests which might oppose reform and b) develop a strategy of how to communicate the prospective changes and advantages of reform in cooperation with partner countries.

Revenue authorities can be detrimental to the political interests of partner governments

Administrative reforms can only work if they are accompanied by tax policy changes which entail the lowering of rates, reducing the number of taxes, and, in particular, scrapping tax exemptions. Nevertheless, despite substantial tax administration and tax policy reform on the African continent, tax exemptions have not been reduced as expected. This indicates that in spite of strengthened tax administration, political interests continue to be served by the tax structure. There is still room for appropriation and bypassing of donor-supported tax administration projects. The scope of reform must therefore go beyond mere support for the core administration.

The prominent, stand-alone position of revenue authorities also makes them vulnerable for being singled out for policy failures. In some countries, such as Zambia, business persons acknowledge the professionalism of staff members. In other countries, the revenue authority is rated the most difficult agency businesses have to deal with. As the hugely unpopular revenue authority continued to harm their interests, political actors in Uganda began to distance themselves increasingly from the tax administration.

Recommendation: In extreme cases of waning government commitment, donors should consider ceasing to provide support for tax administration reform altogether. It is important that donors find a common answer to challenges on the political level and send a coherent message. On the other hand, partner governments' concern to protect their political interests can be valid. Donors should therefore support mechanisms of restraint such as revenue tribunals in order to limit over-aggressive enforcement tactics applied by the revenue authorities.

6.4 Relationship with Multilateral and Bilateral Donors

Donors have played a strong role in providing technical assistance to newly-created revenue authorities in Africa and have also exerted pressure to uphold the integrity and capability of the new entities. Nevertheless, they may also have induced unintended consequences by pressing for increased revenue performance, often measured through the tax-to-GDP ratio.

Donor involvement is important for strengthening capability and upholding autonomy

In highly-indebted African countries, donors have the financial leverage to influence fiscal policies in general and tax administration reform more specifically. Donor conditionality was the trigger for creating semi-autonomous revenue authorities in the four cases studied here. Thus the immediate impulse for reform came from the outside. At the beginning of the 1990s, this often met with the aim of incoming African governments to put the state budgets on a sounder basis than in the past.

Technical donor support has been instrumental in improving capabilities. On the political level, donors have tried to strengthen domestic support for tax administration reform and to counter instances of political interference with the revenue authorities' operations. In doing so, an attempt has been made to fill the gap of either nonexistent or weak internal interest groups pressuring for an efficient and accountable tax administration. Nevertheless, this donor protection clearly has its limits: the political will of partner governments is the most crucial factor for ensuring the success of tax administration reform in unfavourable environments. This cannot be imposed from the outside.

Recommendation: Donors must not be the driving force in tax administration reform. Before starting to provide support, they should analyse whether the partner government has expressed a need for it. The initiation of tax administration reform may also merely reflect donor conditionality. Indicators of this are the lack of reform efforts in other areas of public administration, the maintenance of complicated tax laws, the continuance of various exemptions, and a start-stop approach to beginning reform. Only if the political will exists can donors play an important role in strengthening capabilities and supporting autonomy.

Donor domination of annual revenue target negotiations may be counter-productive

Donors (in particular the IMF) play a dominating role in setting revenue targets for revenue authorities. In the business-mimicking setting of the Ministry of Finance which "commissions" the revenue authority to collect taxes on its behalf, the annual target negotiations are of prime importance. In the process, the IMF often makes use of its financial leverage as the most important provider of loans and determines targets for domestic revenue generation. This influence was particularly strong in the run-up to the Heavily Indebted Poor Countries (HIPC) Initiative completion point. The poorest countries in Africa and other developing regions had to fulfil certain structural criteria in order to qualify for debt cancellation. All of the four case studies analysed in this study are HIPC countries.

From a governance perspective, targets sometimes create wrong incentives. A strong focus on the tax-to-GDP ratio may sideline other measures such as widening the tax base. An exclusive focus on tax share induces revenue authorities to concentrate on large taxpayers. The IMF strongly advocates Large Taxpayer Units to increase revenue performance and often makes their introduction one of its conditionalities for partner countries. In this respect it is noteworthy that donors have not promoted "Small Taxpayer Units". This could bring favourable results from a governance perspective. Finally, the external setting of revenue targets can run counter to partner countries' ownership of tax (administration) reform.

Recommendation: Donors should be aware that they are setting incentives for tax administration in highly aid-dependent countries. Domination of annual target-setting negotiations by external actors is counter-productive. Donors should at least broaden the scope of indicators for success (beyond the tax-to-GDP ratio). Furthermore, bilateral donors providing technical assistance to revenue authorities should find a common position with the IMF on how to appropriately measure success in the partner countries.

Donors need to pursue a long-term approach in providing technical assistance

Tax administration reform is a long-term exercise. In many African countries, revenue authorities had to be built up from scratch. Staff had to be trained, information technology had to be provided, and completely new organisational structures had to be created. In response, donors have often pursued a long-term approach to technical support. Assistance was sometimes provided for more than ten years. In Zambia, for instance, the British government started its support in 1992 with the funding of initial studies which in turn recommended establishment of the semi-autonomous Zambia Revenue Authority (ZRA). DFID support to the ZRA formally ended in March 2005, with some project activities running until the end of the year 2005. Only in February 2002, nine years after creation of the revenue authority, did the expatriate Commissioner General, the last manager from abroad, leave. This long-term horizon for tax administration reform stands in contrast to other areas of technical assistance and must be viewed positively. Principally it makes it possible to work closely together with partner countries and to apply context-specific solutions.

The sustainability of technical donor assistance remains a fundamental issue. Whereas management is viewed as a "buffer zone" against interference from the political level, local managers who are not being funded by donors are potentially subject to much stronger influence. Furthermore, experience demonstrates that political support for tax administration reform, even if strong at the outset, tends to wane.

Recommendation: Pursuing a long-term approach towards tax administration reform in unfavourable environments is an adequate donor strategy. However, donors need from the outset to prepare for their own exit. This entails a) building up a merit orientation of staff and managers as well as b) institutionalising political support for reformed tax administration, e.g. by collaborating with civil society and ministries.

6.5 Principal Recommendations for Future Donor Support

Two main conclusions emerge from the experience gained in these four case studies for future donor support to tax administration reform in developing countries.

First, donors have to be aware that tax administration reforms are highly political. Awareness for this fact and context-sensitivity has often been absent, and reform approaches, at least in the beginning, have commonly been characterised by a narrow technical focus. Therefore a broadening of support is necessary in order to strengthen the environment for tax administration. First attempts in this direction are already discernable: For example, the DFID extended the scope of its RIZES Project in Zambia and built up the capacity of civil society to comment on taxation and tax administration issues. It also supported the Tax Policy Unit in the Zambian Ministry of Finance. This capacity-building has, however, yielded less sustainable results. In Ghana, the GTZ's Good Financial Governance Project not only assists the Internal Revenue Service but is also engaged in improving the whole budgeting process and tax policy formulation in the Ministry of Finance. These more holistic approaches are promising routes for improving the effectiveness of donor support to tax administration reform. They also readily fit into the Paris Declaration on Aid Effectiveness, with its focus on providing context-sensitive assistance and strengthening the institutional capacities of partner countries (High Level Forum 2005). Thus there are indications that donor support to tax administration reform in sub-Saharan Africa increasingly takes into account principles of comprehensive and modern development aid strategies.

Apart from core tax administration issues, the embeddedness of the tax-paying mechanism has to be taken into account. The quasi-voluntary compliance of taxpayers, particularly in the African context, can only be increased if taxation is perceived to be fair and if tangible benefits can be seen in response. As surveys in Ghana and Uganda indicate, this is not the case. Particularly in the large informal sector, there is widespread hostility with respect to the tax administration. According to Fjeldstad (2003b, 1),

> *Coercion, conflict, informalisation of the economy and tax administration technology – rather than politically negotiated contracts about services in exchange for taxes between citizens and rulers ("democracy") – seems to be central for the size of revenue mobilisation in poor countries.*

For taxation to have a positive effect on governance, taxation must be "felt" by a majority of citizens in order to induce demands for greater accountability (Gloppen / Rakner 2002). Due to strong monitoring necessary and the widespread exemption of the dominating informal sector, the governance dividend of donor support to tax administration reform hitherto has been smaller than originally envisaged.

On a positive note, donor-supported tax and tax administration reforms in the four case studies have increased public awareness for the politics of taxation. Of relevance in this respect has been the introduction of VAT, which, particularly in Ghana and Uganda, was initially a very contentious issue. The recurrent public discourse on the adequate rates of this indirect tax suggests that VAT's political effect has been in fact very direct. In Zambia, campaigning for the 2006 national election centred on tax exemptions for foreign investors and on the high tax burdens of civil servants. The Tanzania Taxpayers Association (TATA) was founded to specifically comment on taxation and tax administration (Gloppen / Rakner 2002, 38). In other countries in sub-Saharan Africa, this role has increasingly been filled by business associations. More and more often, taxation issues are taking centre stage in political contests. These promising developments also imply that tax administration is under closer public scrutiny. They suggest that donor-assisted reforms will reap more pronounced governance dividends in the future. Donors should therefore support all stakeholders involved.

Second, supporting the sustainability of tax administration reform is crucial. From a political economy perspective, the reasons for *establishing* a revenue authority are quite different from the mechanisms for *maintaining commitment* to tax administration in an unfavourable environment (Kidd / Crandall 2006, 20; Di John / Putzel 2005, 15). As already outlined, initial improvements in Ghana, Tanzania, Uganda and Zambia have been remarkable. However, after the end of core technical donor support (and oversight) they have often, particularly in Uganda, fallen back into the routines of the old, state-integrated tax administration. Political commitment has waned and the authorities have again been influenced to differing degrees by their environments. This corresponds with mounting evidence that the institutional mode of "semi-autonomous" revenue authority in itself does not ensure improvements any more than traditional tax administration (Kidd / Crandall 2006, 51; DFID 2005, par. 32; Mann 2004, ii). In the words of Devas et al. (2001, 221): "They do not guarantee insulation from political interference, nor guarantee against incompetence and malpractice."

Fiscal crises in partner countries have often been the immediate trigger for installing a revenue authority. This has also allowed political leaders to create symbols of reform commitment and gain leverage over the reform process (Di John / Putzel 2005, 16). Initially, technical donor support also kept the costs for governments low. However, extreme cases such as publicly blaming the revenue authority in Uganda and the widespread application of tax exemptions in all case studies calls this commitment into question. Apparently, the maintenance of support for a revenue authority causes political costs. As a consequence, Ghana and Uganda today are faced with the need to reform a reform project which went off track.

In order to enhance the effectiveness of support, donors should therefore pursue a needs-based rather than a donor-driven process for supporting tax administration reform. This again would put the basic principles of the Paris Declaration into practice. Tax administrative reform is unlikely to succeed if the main leadership comes from outside (Fjeldstad et al. 2003, 73). Recurrent stakeholder analysis helps to identify the potential supporters or opponents of reform. If commitment is not discernible, donors should desist from supporting tax administration reform. Funds would then be more effectively spent on other areas. At the same time, the flexible utilisation of IMF conditionalities for providing financial aid can support the maintenance of commitment to tax administration reform. Such conditionalities should not only be oriented toward the tax-to-GDP ratio but should also incorporate measures such as the widening of the tax base.

In a nutshell, further donor support for tax administration reform should be guided by context-sensitivity, awareness of the political aspects of reform, flexible donor conditionality, and a coherent, needs-based approach to technical aid.

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