The political economy of taxation and public expenditure in the developing world

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Research on taxation and public finance management at CMI
How to accomplish an efficient, responsive and accountable public sector? This is the main concern informing the research on taxation and public finance management at CMI. Focus is on how governments in poor countries can raise and manage domestic financial resources in ways that enhance their effectiveness and political legitimacy.

Most poor states are unable to raise the revenue they need for providing basic services to the majority of its citizens. The dependence on foreign aid or revenues from natural resources, especially oil and minerals, may create disincentives for developing the domestic tax system. Building onto the Taxation, Aid and Democracy programme, but with a stronger focus on tax administrative practices and the political economy tax policies, a key research issue is how governments in poor countries can raise financial resources in ways that enhance their effectiveness and political legitimacy. Historically, bargaining and negotiation over taxation have been central to the idea of a social fiscal contract between state and society: a pattern of accountability based on the principle of reciprocity and mutual obligations, rather than patronage and coercion. However, high levels of aid or ‘rents’ from extractive industries raise concerns about disconnections between governments and their citizens. The research aims to examine whether and how the idea of a social fiscal contract can be realised by developing countries and progressed with help from donors. One specific area of research in this context is tax evasion. This includes the question of possible links between the level and arbitrariness of taxes and regulations, the resulting evasion and corruption, and the evolution of the shadow economy. Of special concern are the impacts of central and local government tax systems on the formalisation of small- and micro enterprises.

The challenges that tax havens and capital flows represent for developing countries, in particular in relation to tax avoidance, tax evasion and money laundering, are also an important part of this research agenda. The research aims to examine the impact tax havens have on developing countries’ ability to generate tax revenue. Linked to this and of particular significance for the research cluster is the role of national and international institutions in mitigating the problems that tax havens represent.

The research agenda also deals with the expenditure side of the fiscal system, and aims to examine how to establish better links between taxation and public service provision. In many developing countries, the absence of effective citizen influence and accountability has contributed to expenditure patterns that are not directed to the needs of the poor and often
riddled by inefficiency. The way foreign aid is provided may also be a disincentive to increasing the efficiency of public spending. The government’s plans for development and their fiscal priorities are reflected in the budgetary allocations, and our research will use that information to understand how, and if, governments respond to their citizens. Of special interest is whether and under what conditions local government reforms will improve the efficiency and responsiveness of the public sector.

The research area, including theoretical perspectives and methodologies, is based primarily in the disciplines of economics and political science, but also involves law and history. Within the analytical frameworks of political economy, incentive and regulation theories, and new institutionalism, this research cluster aims to contribute with empirical and theoretical insights to inform the reform agenda and policy debates on public sector reforms in developing countries. The purpose of the research is to undertake research on these issues and to act as a clearing-house and stimulus for research undertaken elsewhere.

Distinct programmes and projects constitute central focal points of the broader research agenda. In particular, the research will be conducted in close partnership with the International Centre for Tax and Development (ICTD), which is a research network focused on high quality, practically-oriented political economy research and communication activities, with the aim of improving taxation in poorer countries. In addition, the current portfolio includes projects on capital flight and the banking sector; synergies in combating money laundering and corruption; good tax governance in Africa; donor support to strengthening the tax systems in poor countries; citizens’ views of taxation; fiscal decentralization; participation, representation and taxation in local governance; and the political economy of public procurement.

Chr. Michelsen Institute is committed to quality and relevance, and puts strong emphasis on reaching its core target groups through tailor-made outputs. There is a strong emphasis on publications in international refereed journals to ensure and maintain a high academic standard. CMI publishes CMI Reports and CMI Working Papers, CMI Briefs, CMI News and CMI Annual Report, as well as U4-publications in the form of Briefs and Issue Papers.

CMI enjoys an extensive network of international contacts, and has formal co-operation agreements with various research institutions in Africa, Asia, Latin-America, and the Middle East. Institutional co-operation facilitates joint research and projects, institutional development and competence building. In Norway, CMI has close formal institutional collaborations with the University of Bergen and the Norwegian School of Economics and Business Administration, including teaching, joint research projects and support to graduate students and PhD candidates. CMI is not an educational institution, but 10 Master students, mainly from the University of Bergen, are affiliated to the institute and write their thesis at CMI. The Institute also hosts several PhD students.
Selected projects

1. The tax systems in Mozambique, Tanzania and Zambia: capacity and constraints

Client/funder: Norad  
Project period: 2010 – 2012 (current)  
Project members: Odd-Helge Fjeldstad (project leader), Kari Heggstad  

Summary:  
The purpose of this study is to systematise and analyse existing knowledge on taxation and tax administration in selected African countries, and to advice Norwegian authorities on how this knowledge can be translated into practical, effective and concrete development policies. This report focuses on Mozambique, Tanzania and Zambia. It examines current work to strengthening the tax systems in these countries, identifies gaps and provides recommendations for Norwegian support to build effective and accountable tax systems.

2. Peoples’ views of taxation in Africa

Client/funder: ICTD (funded by DFID & Norad)  
Project period: 2011 (current)  
Project members: Odd-Helge Fjeldstad (project leader), Collette Schultz-Herzenberg (ISS-Cape Town), Kari Heggstad, Charlotte Ringdal, in partnership with Afrobarometer  

Summary:  
The main objective of the project is to provide new insights into citizen’s perceptions, attitudes and behaviour with respect to taxation. Attempts to broadening the tax base require better understanding of how the large majority of citizens perceive the tax system, and whether and how their tax behaviour is correlated with how they perceive the state (e.g. with respect to service delivery, legitimacy etc). Important questions to assess are whether people perceive they are paying taxes or not, what they eventually pay, their views on tax administration and enforcement, and what factors underlie the individual’s decision whether to pay or evade taxes. Further, the political settlement between élites and citizens over how to raise public revenues is critical for state-building. Thus, there is a need to acquire more knowledge of the élites willingness to pay taxes in Africa. Do economic and politically weaker groups tend to perceive taxation differently than more prosperous and influential groups? Findings have potentially important implications both for research and policy design.

3. Local government taxation and tax administration: a comparative study of Francophone and Anglophone African countries

Client/funder: ICTD (funded by DFID & Norad)  
Project period: 2011 (current)  
Project members: Jean-François Brun (coordinator, CERDI - Claremont Ferrand), Gérard Chambas (CERDI), Odd-Helge Fjeldstad, Kari Heggstad  

Summary:  
The main objective of the project is to provide better evidence on how to promote effective, efficient and legitimate local government tax systems and tax administrations in low income countries, based on comparative studies of local taxation in selected sub-Saharan African countries. Local government revenues generally contribute to a very modest share of total
national public revenues in poor countries. Whereas central government taxes are dominated by indirect taxes and by narrowly based income taxes, local government revenues are heavily reliant on broad based direct taxes (mainly property taxes and taxes on businesses), various levies, licenses, fees and user charges. Thus, while central government taxes affect directly only few people, local government taxes affect many directly, including the poor. Local taxation may, thus, be particularly important to fostering positive linkages between taxation, responsiveness and accountability because local taxes are more visible and broad based, owing to the simple fact of proximity.

4. The political-economy of property tax collection in Tanzania

**Client/funder:** ICTD (funded by DFID & Norad)
**Project period:** 2011 (current)
**Project members:** Odd-Helge Fjeldstad (project leader), Joanita Magombo (REPOA - Dar es Salaam), Lucas Katera (REPOA), Juda Lyamai (REPOA), Muhammad Mujtaba Piracha (IDS-Sussex)

**Summary:**
In 2008, on a piloting basis, a new system for property tax collection was introduced in some municipalities in Dar es Salaam. While the municipalities previously administered and collected the property taxes, which is the case in most other East African countries, the central government tax administration, the Tanzania Revenue Authority (TRA) was assigned the task of collecting property taxes on behalf of the municipalities. The objective of this study is to assess the experiences with this collection system, in order to inform subsequent reform efforts by policymakers and to contribute to the knowledge base on the political economy of property tax reform.

5. U4 Anti-Corruption Resource Centre: illicit financial flows

**Client/funder:** DFID, Norad, CIDA, Sida, BTC, GIZ, AusAID and MinBuza
**Programme period:** since 2002 (current)
**Programme members:** U4 staff

**Summary:**
The U4 Anti-Corruption Resource Centre (www.u4.no) assists 8 donors and their counterparts to more effectively addressing corruption challenges through their development support. One of U4’s work streams addresses issues related to international drivers of corruption, illicit financial flows, money laundering and asset recovery efforts (http://www.u4.no/themes/international-drivers-corruption/main.cfm). The objective of this work is to clarify the points of contact between debates on illicit financial flows and the fight against corruption, and how experiences in the latter can enhance bilateral donors’ activities on the other. U4 aims also to indicate possible practical ways for bilateral donors to integrate anti-money laundering work into their current work on anti-corruption.
6. Allowances and per diems in sub-Saharan Africa

**Client/funder:** Norad  
**Project period:** 2011 (current)  
**Project members:** Tina Søreide (project leader), Arne Tostensen, Ingvild Aagedal Skage, Odd-Helge Fjeldstad, Michael Davies, Mekonnen Gebeyehu, Tom Kavinya, Samuel Wangwe (REPOA)

**Summary:**  
The study aims to acquire better understanding of the origins and consequences of the payment of per diems (non-salary daily allowances) and related allowances in connection with seminars and workshops organized by governments, civil society organizations and donors in sub-Saharan Africa. The study explores these issues with a particular focus on their effects on development programmes, national budgets and civil service incentives. There are four main categories of consequences, and to some degree they can overlap: (i) the intended compensatory aspect; (ii) informal system for reward for good performance; (iii) unintended distortion of incentives for those involved (less time in office, too much allocation to seminars); and (iv) fraud and corruption. Case studies of Ethiopia, Malawi, and Tanzania will provide empirical evidence and insights about the extent to which these consequences can be expected to impede the results of aid-funded programmes as well as service delivery in general.

7. Corruption in public works in Angola

**Client/funder:** The Norwegian Embassy, Luanda  
**Project period:** 2010 – 2011 (current)  
**Project members:** Tina Søreide, Alves da Rocha (CEIC-UCAN), Regina Santos (CEIC), Nelson Pestana (CEIC)

**Summary:**  
The project examines the risks of corruption in the procurement and construction of public works in Angola. The study aims to identify and analyse the key factors (political, social, legal, procedures, and technical) that directly and indirectly contribute to the high costs of infrastructure, particularly in road construction and housing. The study also examines the adjudication procedures of contracts and the concepts and systems of transparency and governance for public finance management in infrastructure development.

8. Participation, representation and taxation in local governance in Angola

**Client/funder:** Norwegian Embassy, Angola  
**Project period:** 2008-14 (current)  
**Project members:** Aslak Orre (project leader), Odd-Helge Fjeldstad and Nelson Pestana (CEIC, UCAN - Luanda)

**Summary:**  
The project’s contribution is to generate knowledge of one of the most crucial issues in Angolan local government and decentralisation debate: Are the evolving institutions at the interface of state and citizenry conducive to pro-poor local governance? The knowledge and
consequent debate is necessary for policy-makers, civil society critics and activists, as well as to international “players”, like donors and academics. Specific objectives are:

1. Contribute to the public debate in Angola, by publicising research findings, as well as to suggest reform options.
2. Build pressure on an overly centralised state structure to promote citizen participation and representation at local level.
3. Highlight theoretical knowledge and cross-country comparisons, and make them available for an Angolan audience, so as to think radically new in the country’s efforts in decentralisation and local state building.

9. Good tax governance in Africa

Client/funder: The Collaborative Africa Budget Reform Initiative (CABRI) and the African Tax Administration Forum (ATAF)
Project period: 2010 (completed)
Project members: Joseph Ayee (UKZN - Durban), Odd-Helge Fjeldstad, Aidan Keanly (SARS - Pretoria), Lincoln Marais (ATAF - Pretoria)

Summary:
Good Tax Governance (GTG) is an essential ingredient of Good Financial Governance (GFG). At the heart of both is not only the mobilization and judicious use of resources to promote development and thereby achieving the Millennium Development Goals, but also measures and strategies aimed at promoting accountability, transparency and trust. Against this backdrop, this study examines some of the key dimensions of tax governance in Africa, including the drivers of tax reform, tax administrative practices, tax compliance, the capacity of the state to improve revenue mobilization, and how challenges of transparency, accountability and oversight are addressed by African governments. It identifies key issues and perspectives, priorities, challenges and opportunities for further tax reform efforts. The study is designed to provide inputs to the project Towards an African Declaration on the Good Financial Governance.

10. Local government reform and fiscal decentralisation in Tanzania

Client/funder: Norwegian Embassy Tanzania
Programme period: 2005 – 2010 (completed)
Programme members: Odd-Helge Fjeldstad, Lucas Katera (REPOA), Erasto Ngalewa (REPOA, coordinator)

Summary:
The overall objective of this research programme is to document the processes of change and impacts of the ongoing Local Government Reform in Tanzania, and to provide managers and key stakeholders with operationally relevant data and analyses of lessons learned during implementation. The research aims to promote informed dialogue among stakeholders to ensure that policy making is a consultative process. The vision of the local government reform is to see improvement in service delivery to poor people in Tanzania. Finances and financial management are crucial for the successful implementation of the reform. CMI’s work focuses on the following issues and changes over time: (i) financial planning and budgeting in local
government authorities; (ii) revenue administration and mechanisms of tax enforcement; (iii) central government transfers; (iv) local government own revenue generation; (v) financial accountability; and (vi) taxpayers’ compliance.

There is a strong overlap of issues between governance and local finances and financial management. Therefore, relevant governance issues are considered as part of the research. Moreover, an important element of CMI’s engagement in the research programme has been to contribute to building capacity for local government research in Tanzania.


11. Linking procurement and political economy

**Client/funder:** World Bank Institute (WBI) and DFID  
**Project period:** 2010 – 2011 (completed)  
**Project members:** Odd-Helge Fjeldstad (project leader), Mona Frøystad, Kari Heggstad

**Summary:**  
National procurement systems handle a substantial share of total government expenditures in most countries. If the public procurement systems in poorer countries were improved, there would be substantial positive effects on public services, private enterprise, economic growth, and the legitimacy and effectiveness of public authority. These messages are now widely appreciated. The task is to translate them into practical, effective and concrete policies. The achievements of procurement reforms are mixed with few obvious success stories, reflecting the need for better understanding of the main constraints and how the challenges can be addressed. There is, however, increasing awareness among development practitioners that procurement and the political context are tightly connected. At present, there are no guides available that link political-economy tools that may guide procurement processes, and (2) to fill some of the gaps in the existing political economy tool box to establish a more specific focus on procurement.

12. Capital flight and the banking sector

**Client/funder:** NORAD  
**Project period:** 2009 – 2010 (completed)  
**Project members:** Odd-Helge Fjeldstad (project leader), Kari Heggstad

**Summary:**  
Capital flight erodes the financial basis of developing countries, and the illicit financial flows are a major constraint for the implementation of efficient development policy by facilitating corruption, tax evasion and organized crime. The role of banks and financial institutions in facilitating capital flight is acknowledged, but there is a need for more systematic studies of the banking sector’s involvement to be able to formulate policies to address the problem. On this background Norad commissioned CMI to conduct a review of existing literature on the role of banks and financial institutions in capital flight from Africa. The mapping study is an initial step in the process to identifying possible areas for Norwegian development aid interventions related to capital flight. The paper focuses on Africa because of the large challenges connected to the relatively unregulated banking sector in many African countries. The project is a desk study that that addresses the following issues:
- What are the main concerns and areas of focus in the existing literature?
- What does the literature say are the most common methods when using banks to channel illegal money flows?
- Which actors and institutions are currently occupied with the issue?
- Which knowledge gaps can be identified?

The full report can be accessed here: [http://www.cmi.no/file/?972](http://www.cmi.no/file/?972)

### 13. Evaluation of the World Bank’s support for public sector reform

**Client/funder:** World Bank  
**Project period:** 2007 – 2008 (completed)  
**Project members:** IEG-staff and international consultancy team, including Odd-Helge Fjeldstad and Jan Isaksen

**Summary:**
The World Bank’s *Independent Evaluation Group* (IEG) has undertaken evaluation of the Bank’s support for public sector reform (PSR). The main objective of the evaluation was to help the World Bank learn how to contribute more effectively to PSR in its member countries. The intended audience also included government officials and other stakeholders who wanted to see what lessons were available for improving project and program design and for better using the Bank’s support for PSR. The themes of the evaluation included (1) public expenditure and financial management, (2) civil service and administrative reform, (3) tax administration, and (4) anti-corruption and transparency. It focused on what has been learned from the 1999-2006 experiences, but also looked back to the 1990s to cover the full trajectory of World Bank support for these reforms. The three main areas of work for the evaluation team were country case studies, thematic analyses of the four areas mentioned above, and statistical analysis of the pattern of public-sector issues, interventions and outcome in a large country sample.

**Evaluation report:**

### 14. Effects of the tax systems in Africa on investments and growth

**Client/funder:** FIAS/IFC and DFID  
**Project period:** 2006 – 2007 (completed)  
**Project members:** FIAS consultants and Odd-Helge Fjeldstad

**Summary:**
The objective of this study was to assess the impacts of the tax system on the growth of firms within five key sectors (agriculture, tourism, mining, financial sector, and manufacturing) and small businesses, in eight African countries (Lesotho, Madagascar, Mozambique, Rwanda, South Africa, Tanzania, Zambia, and Uganda). CMI's inputs to the project aimed to shed light on the link between tax policy and its administration, and the broader political economy.
context for business development and poverty reduction. The study was co-managed by Foreign Investment Advisory Service (FIAS), a unit within the International Finance Corporation (IFC), and the UK’s Department for International Development (DFID). The country reports are available on the FIAS website: www.fias.net. The final synthesis report, extracting lessons from the seven country studies, was presented at an international tax conference in Livingstone, Zambia, in February 2007.

15. Taxation, aid and democracy. Research programme 2000-2004

Client/funder: Research Council of Norway and Danida

Programme period: 1999 – 2004 (completed)

Programme members: Odd-Helge Fjeldstad (programme coordinator), Ole Therkilsen (DIIS-Copenhagen, coordinator), Lise Rakner, Joseph Semboja (REPOA), Erasto Ngalewa (REPOA), Deo Moshi (ERB/REPOA), Dirk Hansohm (NEPRU - Windhoek), Hoster Bebi (NEPRU), Rosa Endjala (NEPRU), Klaus Schade (NEPRU), Emmanuel Kazimbazi Makerere University, Law – Kampala), Adam Mugume (Makerere University, Economics), Caiphas Chekwoti (Makerere University, Economics), Marios Obwona (EPRC – Kampala), Bertil Tungodden (NHH - Bergen)

Summary:
Taxation, aid and democracy (TAD) are closely related in poor aid-dependent African countries. The way they tackle the issue of domestic revenue mobilisation significantly influences their potential for economic growth and democratic consolidation. This proposition is based on the reading of historical, political and economic literature, and it forms the general basis for this research programme that started in late 1999. Namibia, Tanzania and Uganda were the case countries. To our knowledge this is the first comparative study of revenue systems in African countries that explores the evolution and performance of the local and central government tax systems. The research aimed to understand and explain the performance of the tax systems in the three case countries. The concept of tax system performance was made explicit: Performance is not just about increasing revenues, but also about implementation efficiency, accountability and taxpayer perceptions. Constraints and options available for policy making and implementation on revenue mobilisation were explored in light of current political, economic and administrative reforms.

Among the key findings are: Coercion, conflicts and methods of tax collection - rather than politically negotiated contracts about services in exchange for taxes between citizens and rulers (‘democracy’) – are central for the size of revenue mobilisation in poor countries. Administrative problems and political interference in the actual implementation of tax policies are often bigger obstacles to increased revenue than lack of political will to change tax policy. While central government taxes in the poorest countries affect only relatively few people directly, local government taxation affect many more. To the extent that state-citizens relations are influenced by taxation (which is the experience in Western countries), local government taxation is therefore central to a better understanding of state-citizen relations.

Further information on the outline of the research programme and the major areas of research, including findings and publications, can be found on the programme’s web-site: http://www.cmi.no/research/tax/
Publications

Books


Articles in international journals


**Book chapters**


Articles in Scandinavian journals


Shorter articles and briefs


**Reports in external series**


CMI publications


**Conferences, workshops and seminars**


11. Fjeldstad, O.-H. ‘Perspectives on taxation and state building in Africa.’ Presented at conference at Centro de Estudos e Investigação Científica (CEIC), Universidade Católica de Angola (UCAN), Luanda, 4 November 2010.


45. Fjeldstad, O.-H. Non-payment of service charges in South Africa. Research seminar at the


