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Chr. Michelsen Institute *Development Studies and Human Rights*

CMI Working Papers

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Price: NOK 50 + postage

ISSN 0804-3639

ISBN 82-90584-94-6

Indexing terms

Local government

Decentralisation

Taxation

Tax administration

Tanzania

JEL classification: H71, O18, O23, R51

Fiscal Decentralisation in Tanzania: For better or for worse?

Odd-Helge Fjeldstad*

ABSTRACT

Tanzania is currently implementing a local government reform aimed at improving public service delivery. An important component of the reform is to increase the fiscal autonomy of local authorities. This policy is encouraged and partly initiated by the donor community. The purpose of this article is to explore to what extent we can expect that increased fiscal autonomy will improve the efficiency and responsiveness of the public sector. The paper concludes that it is unrealistic to expect that the present administration in many local authorities in Tanzania has adequate capacity and the required integrity to manage increased fiscal autonomy. In fact, there is a real danger that, in the absence of substantial restructuring of the current tax system combined with capacity building and improved integrity, increased autonomy will increase mismanagement and corruption.

Introduction

Fiscal decentralisation – the devolution of taxing and spending powers to lower levels of government - has become an important theme of governance in many developing countries in recent years. As a consequence of much dissatisfaction with the results of centralised economic planning, reformers have turned to decentralisation to break the grip of central government and induce broader participation in democratic governance (Olowu 2000; World Bank 1999; Manor 1999; Smoke 1994). Being closer to the people, it is claimed, local authorities can more easily identify people's needs, and thus supply the appropriate form and level of public services (Crook & Manor 1998; Oates 1972). In turn, it is argued, communities are likely to be willing to pay local taxes where the amounts they contribute can be related more directly to services received (Livingstone & Charlton 1998; Westergaard & Alam 1995). As a result, it is expected that the level of tax revenue can be increased without excessive public dissatisfaction.

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Yet, both the approach and the results of decentralisation have varied widely between countries. According to Smoke & Lewis (1996:1281), the limited success is attributed to two factors: (1) The decentralisation process has been resisted or undermined by central government institutions fearful of losing power and rationale. (2) Many initiatives have been donor driven, over-ambitious, and not taking into consideration the complex institutional realities that govern the extent to which, and the pace at which, decentralisation can occur in a particular country. Oates (1998) argues that the case for decentralisation has often been made in a very general and uncritical way with little systematic empirical support. Predictably, the argument for decentralisation has provoked response from some observers who assert that the case for fiscal decentralisation is much-overstated (Prud'homme, 1995).

Despite the mounting concern, Tanzania is currently implementing a local government reform within the framework of the reform of the civil service. The new Local Government Act was approved by the Parliament in February 1999. The reforms aim at improving public service delivery (URT, 1996). An important component of the reforms is to increase the fiscal autonomy of local authorities. This policy is encouraged and partly initiated by the donor community.

How realistic are the various expectations about fiscal decentralisation in Tanzania? The purpose of this article is to explore the extent to which we can expect that increased fiscal autonomy will improve the efficiency and responsiveness of the public sector. In particular, what are the linkages between taxation and accountability in local authorities in Tanzania? Are local officials through sheer proximity more accountable for their performance? Furthermore, what is the scope for improving local revenue collection?

The remaining part of the article is divided into five sections. In the first section the general characteristics of the local government revenue system are reviewed. The importance of various revenue sources is discussed and the institutional set-up for revenue collection briefly examined. The second section explores how the present revenue system emerged. It examines the role of the by-law system and discusses the criteria used for tax design. Thereafter, a third section attempts to explain the gap between revenue potential and what actually is reported to the local government treasury. Both administrative and political factors are examined. In section four the outline for a revised local government revenue system is presented. Finally, section five concludes.

The local government revenue system

Local authorities have three major sources of funding: own revenues, central government transfers, and development aid. In addition, user charges and various forms of self-help activities contribute to the running and maintenance of public services such as primary schools and health facilities. Although data on the extent of user charges and self-help activities is not available, recent studies indicate that these contributions are significant and increasing (Cooksey & Mmuya 1997; Semboja & Therkildsen 1995).

Local governments' own revenues represent less than 6 % of total national tax revenues in Tanzania. This share has been almost unchanged since 1996. These revenues are mainly used to finance operational costs, and in particular salaries for local government employees. The lion's share of the operational costs, however, are funded by central government transfers. In 1994 these transfers funded 85 % of the total operational costs in district councils, and 75 % in urban councils. Recent studies from the ministry responsible for local governments indicate

that the councils' own revenues are funding a declining share of the operational costs. With respect to investments, many councils are almost completely dependent on donors. For instance, in a sample of local authorities in the Arusha, Kagera and Shinyanga regions more than 93 % of the councils' investment budgets in 1996 were funded by various donors (ERB 1997).

Local governments' own revenues

Local authorities levy a large number of taxes, licences, fees and charges. However, there are large variations between councils.¹ In 1997, there were at least 25 types of revenue sources being levied in Kibaha District Council, compared to more than 60 for Kilosa DC and about 50 in Dar es Salaam. These figures, however, do not take into account the various sub-groups of particular revenue bases. For instance, in Kilosa DC *trade licence* and *weight and measure fee* had 9 components each. In Kibaha, *business licence* had 8 components and *building inspection fees* had 5 main components and 12 sub-groups (including inspection fees for the different components of a building such as foundation, roofing, walls, finishing and occupation). The by-law on *hawking and street trading* in Kibaha DC from 1991 specifies in detail 38 different components (including licences for bicycle repairs, tyre puncture repairs, shoe shiner, car wash, carpenter, firewood, potato chips seller, etc.). Different rates are often imposed on the various sub-categories.

In spite of the large number of revenue sources, four main sources are crosscutting almost all councils. These are *development levy* (a head tax), *crop* and *livestock cess* (agricultural cess), *business licences* and *market fees*. In 1997 these sources averaged two-thirds (66 %) of the reported tax revenues in a sample of 42 district councils.² 'Development levy' dominated by contributing 30 per cent of total own revenues. In a sample of 10 urban councils, the major own revenue bases in 1997 were licences (33 %), property tax (21 %) and development levy (19 %).

Tax revenues per capita also differ substantially between councils. In 1995, it ranged from TSh 344 per person above the age of 18 in Lindi District Council, to TSh 1541 in Mbinga DC. Furthermore, there are often large variations on the tax rates imposed by councils on similar revenue bases. For instance, the head tax in Kilosa was TSh 2000 in 1997, compared to TSh 1000 in Kibaha.³ Local taxes on agricultural products also vary between the councils. This has led to extensive 'smuggling' of agricultural goods across council boundaries.

The revenue administration

Local government tax collection is the responsibility of the council staff, and is completely separated from the central government. In district councils it is organised around three levels, namely the council headquarters, the wards and the village levels.⁴ At the council

¹ In October 1998, there were 111 local authorities in Tanzania: 92 District Councils; 9 Town Councils; 9 Municipal Councils; and 1 City Council (Dar es Salaam).

² The four main sources of revenue have dominated district councils' revenue generation since local government was re-introduced in 1983 (URT, 1991). In 1987/88, from a sample of ten rural councils, development levy, cess and business licences contributed 77 per cent of the revenues (Semboja and Therkildsen, 1991:19). Thus, although there is a tendency that their contribution is declining, they still account for the major share of the councils' own revenues.

³ In 1997, the exchange rate was USD 1 = TSh 580 (annual average).

⁴ Councils are sub-divided into wards (*kata*). Currently there are about 2,400 wards in Tanzania and more than 9,000 registered villages. Villages have at least 250 households (*kayas*) and are sub-divided into vitongoji.

headquarters the responsibility for tax collection rests with the council treasury, headed by the District Treasurer (DT). At the ward levels, the responsibility rests with the office of the Ward Executive Officer (WEO). The WEO also handles developmental issues and law-and-order functions at that level. For this purpose the local militia is at their disposal. In wards with greater revenue potential there will also be a ward revenue collector (WRC) to support the WEO. At the village level, the responsibility rests with the office of the village executive officer (VEO). The VEO is also responsible for village developmental issues. These officers are nominated to their position by the village governments, but appointed and employed by the council. The system of nomination ensures that the VEOs come from the villages of their domicile. At the sub-village level the politically appointed *kitongoji* leader is expected to assist in mobilising taxpayers.

In practice, organisation of tax collection may vary between councils. For instance, in Kilosa DC the village level has been excluded from collection, which has been taken over by the ward level. According to the district treasury staff, this was due to incentive problems connected with tax collection at the village level. One problem arises from the presence of two principals for the VEOs, i.e., the village government as the nominating authority and the council as the appointing and employing authority, leading to divided loyalty. Another problem arises from VEOs operating within their areas of domicile. Thus, personal relationships between collectors and taxpayers are expected to play an important role in village revenue collection. Lack of arm's-length relationship between tax collectors and taxpayers introduces economics of affection into village tax collection. In many villages the sub-village (*kitongoji*) leaders also resist mobilising people to pay taxes due to the unpopularity of taxation.

Roadblocks are frequently used to control taxpayers. For instance, manned barriers are used to control buyers of certain crops like cashew nuts in the Coastal Region. The buyer has to produce receipts before they are allowed to transport the purchase outside the district. Similar checkpoints are used to control people for 'development levy' and bicycle tax. Roadblocks are sometimes also used to collect market fees, implying that the fees have to be paid before the goods enter the market place.

One consequence of the present local revenue system is the high costs of administration. In Kilosa DC, for instance, the wage bill represented about 80 per cent of total own revenues reported in 1995.⁵ The corresponding figure for 1996 was about 64 per cent. However, when disaggregated by wards, large variations are observed.⁶ In some wards in Kilosa DC, the administrative costs are higher than the revenues remitted to the council. For instance, in Lumbiji ward the wage bill was 2.75 times higher than the revenues reported in 1996. The corresponding figures for Mwatani and Ulaya wards were 1.92 and 1.44, respectively. These administrative costs are largely unrecognised by local authorities. There is little appreciation of the opportunity costs of the staff already employed by the council. One might even argue that for certain small taxes and charges the collection costs are the reason for the levy. In other words, the purpose is to create employment or at least an income-earning opportunity for someone who might otherwise be unemployed.

⁵ The wage bill includes wages and allowances for the staff of the revenue department and the ward offices, including village executive officers.

⁶ The figures include the salaries of Ward Executive Officers and Village Executive Officers. These officials are also responsible for law and order and other administrative tasks in the ward and/or village. However, according to the WEOs and VEOs interviewed, they spend a considerable part of their time organising and/or participating in tax collection.

How did the current revenue system emerge?

No clear pattern can be discerned from the current local government revenue structure as each council has its own tax structure, implying that there are more than 110 local government revenue structures in the country. How did this revenue system emerge? There are three main reasons for this (Fjeldstad & Semboja 2000): Firstly, the by-law system allows local authorities to introduce new taxes and rate changes, subject to ministerial approval. In principle, every activity located within the jurisdiction of an authority is taxable.⁷ Indeed, the Local Government Act provides that activities can pay tax to both central and local government. The Act requires the Minister to approve the proposals for new taxes and rate changes before implementation. In practise, however, proposals from the councils on tax changes seem to be rarely turned down by the Ministry. The most substantial impact of the Ministry's involvement is to delay the process of approving new by-laws. Thus, approvals may not be granted until well into the financial year in which they were expected to come into effect.

Secondly, there are no clear criteria for tax design. For instance, there is no clause in the Finance Act that encourages local authorities to take economic efficiency into consideration. Neither is there any reference to the administrative costs of the tax system. Thus, the various decision-makers involved in tax design can pursue different criteria more rigorously than the others. There are therefore inherent reasons in the local government institutional arrangement to design a tax system that points in many directions. In some councils reviewed, the administrative staff, including tax collectors, put more emphasis on revenue generation than elected councillors who emphasise people's ability to pay. Local politicians are interested in securing their political base at all levels. Thus, politicians are most likely influenced by their constituents when proposing changes in revenue bases and rates. In some councils this influence is reflected in the fine-tuning of the tax structure, based on equity considerations. The large number of sub-bases and rates observed in some councils reflects the influence of local politicians in tax design. This implies that we may observe huge variations in tax design between local authorities depending on the relative bargaining power of councillors and bureaucrats.

Thirdly, there has until recently been little or no co-ordination between the ministry responsible for local government and the Ministry of Finance with respect to taxation.⁸ This has partly to do with lack of capacity at all levels. At the local level the serious shortage of qualified staff at the treasury and planning departments has been noted across almost all councils. Even the ministerial level has no expertise on tax issues. However, even if it contained any, they would easily be over-flooded by the influx of proposals from more than 100 councils. Due to lack of capacity and poor co-ordination between the central and local governments only limited questions are raised at the central level on local governments' tax proposals. Therefore, the local revenue systems have developed without much interference from the centre. Furthermore, lack of co-ordination has led to duplication of taxes and inconsistencies between taxes imposed by local authorities (e.g., high taxes on export crops) and the national government's policy to encourage export production.

⁷ Specific exemptions do, however, apply to publicly owned lands and buildings, cemeteries and burial grounds, charitable and educational institutions.

⁸ In January 1999, a 'Task Force on Rationalisation of Central and Local Government Taxation' was established. The Task Force presented its preliminary recommendations to the Tanzanian Government in March 1999. However, until now, this Task Force has had little impacts on actual tax policies.

The gap between reported and projected revenues

One major administrative problem for many councils is their inability to realise fully the revenue due to them. Thus, the ratio between reported and projected revenues differs significantly both between councils and between areas within the councils. The following factors provide some explanations for this wedge: (1) poor administrative capacity to enforce the taxes; (2) explicit and intentional tax evasion and resistance from taxpayers; (3) corruption, including embezzlement of revenues; and (4) political pressure on the local tax administration to relax on revenue collection.

Poor administrative capacity

In many rural councils there are fewer collectors than the number of major market centres. In such cases, tax collectors must travel among market sites, making collection more occasional and difficult to enforce. Lack of reliable transport further exacerbates the situation. Given the complicated revenue system, it is justified to suggest that local governments do not have adequate collection personnel, and that a substantial strengthening of staff is needed to administer the present revenue system. However, there are about 110 local authorities in Tanzania, each with a different tax system. To establish adequate capacity for designing and administering the existing revenue system in all these councils will require more resources than can be available in the short to medium term in Tanzania.

Resistance from taxpayers

Taxes are widely perceived to be unfair. Taxpayers see few tangible benefits in return for the taxes they pay. Virtually no development activities are undertaken through councils' financial sponsorship, and even the existing capacities are not producing the expected services due to lack of operation and maintenance funds. The deterioration and in some cases non-existence of public services heighten taxpayers' perceptions of exploitation from an unequal contract with government. This promotes tax resistance. Thus, tax resistance may be considered as an attempt by the taxpayers to adjust their terms of trade with the government.⁹

People may take to the extreme to evade taxes, such as literally hiding in the bush when tax collectors are approaching. Tax resistance sometimes also takes more violent forms (Fjeldstad, 2001). In Kilosa DC, tax collectors avoid certain villages due to the high personal risks involved in tax collection. Other villages are only visited by collectors accompanied by the local militia. Cases of tax revolts are also reported from councils in other regions, including Kilimanjaro Region and the Coastal Region. For instance, *Daily News* (28 November, 1997:5) reports that '[o]ver twenty Moshi Municipal Council workers who were on a special operation to net development levy defaulters were attacked by a mob at Mbuyuni Market on Wednesday afternoon and eight of them were injured, some seriously, ...' These revolts are in general spontaneous and disorganised.¹⁰

⁹Non-compliance is sometimes an important political weapon. Scott (1985), for instance, argues that one of the most important 'weapons of the weak' is the ability to withdraw compliance. This can take a passive form, such as shirking, or an active form, such as rebellion. Historically, unwillingness of the population to comply with a tax that is deemed unjust has been a catalyst for political action. The Boston tea party and the Thatcher poll tax are illustrative examples. Bates (1983) provides some examples from Africa.

¹⁰ According to Bratton & van de Walle (1994: 462), such uprisings characterise the way political protest erupts in neo-patrimonial regimes. Because civil society is underdeveloped in such regimes, the foundation for anti-systemic change is weak.

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

Corruption

Fiscal corruption is extensive in local authorities. It takes many forms and varies by types of taxes, methods of tax collection and location. It cuts across all levels of the local government, from the villages to the councils' headquarters. The magnitudes in terms of the amounts of money involved seem to rise in step with the administrative level of the council. Although many cases of collusion between taxpayers and collectors are reported, the most common type of corruption is embezzlement of revenues by tax collectors and administrators. Three factors have led to widespread theft of tax revenues within the local authorities: the low level of wages paid to staff; the complex nature of the tax structure; and inadequate controls.¹¹

The official wages of government employees in Tanzania are very low.¹² According to Mans (1994:378), the average civil servant's pay package covers only about 40 per cent of the expenses of a typical household. Therefore, to say that civil servants cannot live on their wages is a statement of fact. As administrators and tax collectors do manage to make a living, it means that they have other sources of income in addition to their salaries. These other sources may include income from farms or jobs in the private sector, as well as from embezzled funds.

The characteristics of the local government tax system in Tanzania may promote corruption. As described above, the revenue structure is extremely complicated and non-transparent. A large number of tax bases, sub-bases and rates exist for any given local government. Furthermore, the revenue target for tax collection does not necessarily refer to fulfilling the budget, but rather to amassing sufficient revenues to cover the wage bill of the council. When this is achieved, the central government will usually not interfere into the affairs of the local authority. The performance of tax collectors at the ward and village levels is also related to their capability to collect enough revenues to cover their wage bills. Thus, many village executive officers are fired in recent years due to poor performance. In general, ward executive officers are transferred to less attractive or remote wards if they do not perform successfully according to the wage bill criterion.

However, since both revenue estimates and reports on revenue collection are based on information from the same staff, there is room for manufacturing numbers and results. Thus, tax collectors can report enough revenues that cover the wage bill and pocket whatever is left. These observations are consistent with Migdal's (1988:253) proposition that political systems under pressure from the centre to produce certain development results are likely to exercise their own form of accommodation. The most common form of accommodation is simply to pass false accounts of development results to superiors who are out of touch with local conditions. Thus,

¹¹ Prud'homme (1992) discusses the impacts of these factors on embezzlement in local authorities in Zaire.

¹² The structure of wages for civil servants is fixed unilaterally by the Government. Salaries of some public enterprises, such as the Bank of Tanzania and Tanzania Revenue Authority, are determined outside the civil service system.

where supervision is lax, local bureaucrats may use their budgetary discretion and the force at their disposal for personal gain.

In principle, financial control in local authorities in Tanzania is exercised through internal and external audits. However, both functions are weak. In some councils no internal audit units are in place. Furthermore, the Auditor General's office responsible for external audits is in general understaffed and has limited capacity to undertake comprehensive audits in all councils because of severe shortage of qualified and trained staff, especially at the senior professional levels. In spite of these constraints, the number of councils whose accounts have been audited has risen recently. The audits show that financial performance of many councils is poor. An increasing number of cases has been reported in recent years where the Auditor General has not approved the councils' accounts. In 1998, for instance, the Auditor General revealed a substantial gap between reported tax revenues and the amount transferred to the bank accounts of the councils. In a sample of 31 councils this amount corresponded to 3.5 % of total reported tax revenues from all local authorities to the ministry of local government (*Daily News* 23 March 1998). Later the same year the *East African* (30 September 1998) reported that the Auditor General suspected extensive embezzlement of tax revenues from agricultural products in various councils. The amount in question, corresponded to about 10 % of the total reported local government tax revenues in 1997.

Prolonged embezzlement of large amounts of tax revenues requires the involvement of relevant senior officials from the councils' headquarters. Furthermore, the prolonged existence of such corruption is made easier when: (a) the collectors and tax inspectors are stationed relatively permanently in their positions, i.e., they are rarely transferred; (b) the network is limited to a relatively small number of people in the tax administration; and (c) taxpayers are not directly involved. The exclusion of taxpayers from the embezzlement corruption network is possible because the tax collectors may indeed provide genuine receipts to taxpayers on taxes paid. In some cases two sets of similar receipt books are used.

Political pressure

Political pressure is considered a major impediment to revenue collection in some councils. This problem stems from the fact that taxes are generally disliked and councillors who want to be re-elected disassociate themselves from increased taxation. In some cases councillors are also reluctant to raise local taxes and charges because they are major local landowners or business people who seek to minimise their personal tax burden. Tax collectors interviewed stated that councillors obstructed tax collection and talked 'cheap politics'. This apparent conflict between collectors and politicians is rooted partly in divergent objectives with respect to tax design, and partly in the lack of trust between administrators and politicians at the local level. Based on data from 14 district councils, Jacobsen (1999) finds that there is a 'trust deficit' in the political-administrative relations at the local level in Tanzania.¹³

Evidence concerning the impacts of political intervention in tax collection can be found in the councils' financial statements. Some councils experience revenue shortfalls during election years, particularly with respect to development levy. In a sample of 48 councils, 31 experienced

¹³ Conflicts between council employees and local politicians are not of any new date in Tanzania. For instance, Dryden (1968:144-9), referring to the mid-1960s, describes in detail some areas of conflict between these stakeholders.

a drop in revenues in the 1995 election year (Fjeldstad and Semboja, 1999). This may be due to the influence of politicians (both local and central government politicians). Statements such as ‘don’t harass taxpayers’ were quoted from CCM-politicians (the ruling party) who tried to moderate the tax collectors’ efforts to enforce taxes during election years. On the other hand, politicians from the opposition parties approached taxpayers directly and advised them ‘not to pay taxes’, since taxes, according to their view, were used to ‘finance the CCM-government’.

Why has the current revenue system been maintained?

Why has the present tax system persisted for such a long period of time in spite of all its weaknesses? One proposition is that important stakeholders, including bureaucrats and politicians, as well as powerful taxpayers, resist changes in an attempt to protect their influence and control of the local tax system. Some observers also argue that extensive public sector regulations and complicated tax systems, are the result of a deliberate strategy by civil servants, including senior tax officials, to facilitate corruption (Tanzi, 2000a; and Myrdal, 1968). We have no evidence that this is the case amongst local authorities in Tanzania. However, the combination of a complicated tax system and poor administrative capacity breeds corruption and facilitates evasion. Thus, when the non-transparent tax system is in place, it is rational for the stakeholders to maintain the system in spite of the inefficiencies it generates because it also performs other functions. Firstly, it offers informal incomes for civil servants and their social network members. Secondly, the tax system provides a visible arena for local councillors to play out their political aspirations *vis-à-vis* their constituents. Thirdly, some powerful taxpayers, in particular, business people, landowners, parastatals and the co-operative unions, may be interested in retaining the status quo, since it facilitates evasion. Finally, lack of trust between the stakeholders involved may increase their risk aversion and thereby maintain and even reinforce the existing tax structure. Most likely the combined effects of these factors contribute to explaining the existing situation.

The limited central government intervention on local government tax design and enforcement, may be due to the fact that the local government tax system also functions as a mechanism for political control. According to Moore (1998:105), such a system comprises two main elements: Firstly, information on citizens (names, addresses, occupations, incomes, wealth, etc.) that the government might otherwise have difficulties to collect and maintain. Secondly, a network of public tax enforcers who use this information and thereby become ‘repositories of knowledge’ about what is going on in areas of the country where state elites have limited direct influence. Thus, revenue generation for public service provision may not be the most important function of the tax system. However, revenue raising may be an important means of keeping the state apparatus alive and active at the local level.

Options for fiscal reforms

It is clear from the above analysis that the local government tax system in Tanzania is overripe for reform. The current system is partly a result of poor administrative capacity for tax collection and tax design, as well as political pressure and lack of co-ordination between the local and central government. Thus, redesigning the tax structure and building local administrative capacity for collection may reduce revenue losses caused by inefficiency and corruption. However, tax resistance is likely to continue (and increase) if service provision does not improve, necessitating costly and coercive methods of tax enforcement. Improvement in service delivery - a key objective of public sector reforms in Tanzania - is

therefore a necessary condition to improve tax compliance. In this setting, the fundamental issues to be addressed in the context of local government fiscal reforms are: (1) to redesign the current revenue structure; and (2) to enhance tax compliance through improved service delivery.

Redesigning the current revenue structure

There is undoubtedly room for improved fiscal and financial management in local authorities as well as improved co-ordination between the different levels of government. However, attempts to squeeze additional revenues from poorly designed taxes may exacerbate the negative effects of the tax system on the economy and the society in general. Clearly, improved tax administration cannot compensate for bad tax design. Thus, reforming the tax structure should precede the reform of tax administration since there is not much merit in making a bad tax system work somewhat better. In redesigning the tax structure, the following options should be considered:

- abolition of unsatisfactory local taxes;
- improvements to remaining revenue bases; and
- cost recovery through user charges.

Abolition of unsatisfactory local taxes

Given the poor performance of many local taxes, any reform programme should include the abolition of a large number of these taxes. In particular, the head tax ‘development levy’ should be abolished. This is a tax that is costly to enforce, and which is extremely unpopular among taxpayers leading to widespread tax resistance. A reform should also include the abolition of nuisance taxes like the bicycle tax, livestock levy, the entertainment levy, etc.. This should also be the fate of many fees such as pushcart fees, cattle trekking fee, bicycle registration fee, etc., that simply have a high nuisance value and that cost more to enforce than what they yield in terms of revenues.

Improvements to remaining taxes

In particular, there is a need to simplify the licence and fee structures by reducing the number of rates and coverage. Fees and licences that have regulatory functions, such as sand fees, hunting and business licences, should be harmonised with central government taxes, to avoid double taxation and conflicts with national development policies such as export promotion and environmental protection. Furthermore, the establishment of uniform rates on agricultural taxes (crop cess) is necessary to minimise distortions. In this context it may be logical to appoint revenue collection agencies, including the possibility to centralise the collection of certain taxes. For instance, cess on export crops could be collected at their points of export by the Tanzania Revenue Authority.

Export taxes should, in general, be discouraged. But until recently many local cess rates have been very high, discouraging export production and/or encouraging smuggling in border areas. The 20 per cent cess on cashew nuts in Kibaha DC provides an illustrative example. High local cess rates can also be found on other export crops, including coffee and tea. Thus, by abolishing all local cesses and imposing a lower (flat) national cess rate on export crops across all councils, the effective tax rate on these products can be reduced. For instance, based on data from 1997, a 5 per cent tax on export crops would levy TSh 10.5 billion, equivalent to 34

per cent of total reported local government tax revenues in 1997.¹⁴ The central government's move in July 1999 to fix the maximum cess on export crops to 5 per cent of the off-farm price is a step in the right direction.

Land and property taxes have some attractions as local bases since they are imposed on immobile resources, and therefore are difficult to avoid - at least in principle. However, they also have some obvious weaknesses which need to be taken into consideration before heavy reliance is placed on them. Political and partly administrative weaknesses are manifested in problems of valuation and tax enforcement. Experience from other developing countries shows that courts are often swamped by appeals from angry property- and landowners (Skinner, 1993:364). Furthermore, harsh enforcement mechanisms may result in intervention from politicians facing complaints from their constituents (Enemuo, 2000:193). Thus, experience advocates cautiousness when extending property tax to district councils, and when imposing a commercial land tax in local authorities.

In general, a fundamental requirement when redesigning the local tax system is greater emphasis on the cost-effectiveness of revenue collection, taking into account not only the direct costs of tax administration, but also the overall excess burden to the economy, including the compliance costs to the taxpayers (Devas, 1988). In addition, reduced losses through corruption and tax evasion are needed. Such improvements may take a long time to achieve, although a simplification of the local revenue system should provide a positive contribution towards these aims.

Cost recovery through user charges

Taxes are not the best mechanism for matching demand and supply of public services. Better links can be achieved through cost-recovery charging systems, which tie the amount paid directly to the amount consumed. In addition, user charges may address many of the present intergovernmental problems (Bennett, 1990: 21). User charges can also reflect differences in ability to pay by incorporating sliding scales for the type of user or the amount of usage (Rondinelli *et al.*, 1989:71), although this will require adequate administrative capacity.

There are obviously a number of constraints on user charges and other means of cost recovery in Tanzania. These arise, for instance, from equity considerations, fluctuations in demand, and the relations between services financed by charges and private sector provision compared to those financed by public general revenues (Crook and Manor, 1998:301). However, the government as well as the public have too readily seen general revenue, particularly tax revenue, as the easy way out of difficult decisions and the 'normal' financial source, as illustrated by the large and increasing number of taxes imposed by local authorities. But the general sources for taxation have tended to impose significant economic, political and social costs, amidst ample evidence that the poor are already contributing substantial resources towards maintaining 'public' services, for instance through various forms of user charges and self-help activities. This suggests that there are reasons and scope for innovation.

¹⁴ Total export value in 1997 for the major export crops coffee, cotton, sisal, tea, tobacco and cashew nuts was TSh 213.45 billion, equivalent to USD 355.75 million (URT, 1998:55).

Intergovernmental fiscal transfers

Whatever is done to improve the local government revenue system, the reality is that local authorities in Tanzania will for a long time continue to be heavily dependent on fiscal transfers from the central government. Transfers should therefore be considered an important component of the decentralisation programme. To achieve adequate service standards, expenditures (on both salary and non-salary) need to be raised to a certain threshold level. Increments below this funding level will most likely only produce limited impacts.

In the process of fiscal decentralisation, however, it is particularly important to be aware of the potential problems for macroeconomic management and fiscal discipline. Substantial devolution of revenues and spending responsibilities to local authorities may affect the central government's ability to carry out stabilisation and macroeconomic adjustment through the budget (World Bank, 1999). The destabilising potential of local governments is greatest when they face no hard budget constraint (Bardhan, 1996; Ter-Minassian, 1999). Expectations of bail-out in case of financial trouble may weaken the incentives within local authorities to economise on costs, and generate resource waste and rigidity. These inefficiencies may, in turn, lead to macro-economic imbalances (Tanzi, 2000b). Thus, short-run macro-economic management considerations call for effective limits on local governments' deficits, consistent with national objectives for growth, as well as internal and external balances. The creation of institutional fora, to ensure regular and frequent dialogues between the central government and local authorities on budget trends may help in this regard.

Concluding remarks

Local taxes represent less than 6 per cent of total national tax revenues in Tanzania. However, the large number of these taxes, together with their unsatisfactory nature, means that their economic, political and social impacts are considerably more significant than their revenue figure indicates. Moreover, the deterioration of public services, combined with extensive corruption, reinforces taxpayers' perceptions of exploitation and promotes tax resistance, necessitating costly and coercive methods of tax collection.

Tanzania is now implementing a local government reform. An important component of the reform is to increase the fiscal autonomy of local authorities. This policy is encouraged and partly initiated by the donor community. It is beyond doubt that large changes are necessary to improve performance and to re-establish legitimacy of local authorities. However, the claim that increased fiscal autonomy will improve the efficiency and responsiveness of the public sector has to be taken with caution. Sustained development in local governments cannot grow from an institutional framework, which encourage coercion and extra-legal tax enforcement. Furthermore, attempts to raise additional revenues from poorly designed taxes may aggravate the negative effects of the tax system on the economy and the society in general. It is unrealistic to expect that the present staff in many councils has adequate capacity and the required integrity to manage increased fiscal autonomy. In fact, there is a real danger that, in the absence of substantial simplification and restructuring of the current revenue system combined with capacity building and improved integrity, increased autonomy may cause greater mismanagement and corruption in local authorities.

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Summary

Tanzania is currently implementing a local government reform aimed at improving public service delivery. An important component of the reform is to increase the fiscal autonomy of local authorities. This policy is encouraged and partly initiated by the donor community. The purpose of this article is to explore to what extent we can expect that increased fiscal autonomy will improve the efficiency and responsiveness of the public sector. The paper concludes that it is unrealistic to expect that the present administration in many local authorities in Tanzania has adequate capacity and the required integrity to manage increased fiscal autonomy. In fact, there is a real danger that, in the absence of substantial restructuring of the current tax system combined with capacity building and improved integrity, increased autonomy will increase mismanagement and corruption.