

Dilemmas of Fiscal Decentralisation.
A Study of Local Government Taxation in Tanzania*

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Abstract:

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. This paper reviews the main characteristics of the existing local tax system. It discusses how the present tax system emerged, and why it has been maintained for such a long period in spite of all its weaknesses. Finally, it considers options for reform.

Indexing terms:

Local government
Decentralisation
Taxation
Tax administration
Tanzania

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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 (Fukasaku and de Mello, 1999; Manor, 1999; World Bank, 1999; Shah, 1998; Crook and Manor, 1998; Devas, 1997). 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; Smoke, 1994; Wunsch and Olowu, 1990). 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 (Enemuo, 2000; Rondinelli *et al.*, 1989; 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 and Charlton, 1998; Westergaard and Alam, 1995). As a result, it is expected that the level of tax revenue may be increased without excessive public dissatisfaction.

Yet, both the approach and the results of decentralisation have varied widely between countries. According to Smoke and Lewis (1996:1281), the limited success is attributed to two factors. First, the decentralisation process has been resisted or undermined by central government institutions fearful of losing power and rationale. Second, 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 reform.¹ Both aim at improving services 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. A key element in this process is the provision of conditional block grants from the centre to local authorities. Additional reforms include measures to strengthen local governments' revenue raising and measures of revenue sharing between local and central government.

How realistic are the various expectations about fiscal decentralisation in Tanzania? 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. 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?

¹ The new Local Government Act was approved by the Parliament in February 1999.

This article draws on research carried out through 1996, 1997 and 1998. The field studies were conducted in Kibaha District Council, Coastal Region, and Kilosa DC, Morogoro Region. These studies aimed at providing primary data and analyses of the capacities and constraints of the local tax administrations, especially in relation to tax design, revenue collection, incentive problems and service delivery. They covered all three council levels; the district headquarters, the wards and the village levels. Information was collected from a variety of sources and through different methods, and covered staff members of the tax administration, local politicians and taxpayers. In addition, data on tax revenues for about 50 councils were collected from the Ministry of Local Government in Dodoma.² Data on central government taxes were acquired from the Ministry of Finance and Tanzania Revenue Authority, where we also interviewed officials on the relationship between local and central government taxation.

The article is organised as follows: Section 2 reviews the general characteristics of the local government tax system. The importance of various revenue sources is discussed and the institutional set-up for revenue collection briefly examined. Section 3 explores how the present revenue system emerged. It examines the role of the by-law system, and discusses the criteria used for tax design. Section 4 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 5 the outline for a revised local government revenue system is presented. Finally, section 6 offers conclusions.

The current local government revenue system

The revenue structure

Local authorities levy a large number of taxes, licences, fees and charges, some of which are listed in Table 1. The table lists 10 major categories of taxes; 18 major categories of licences; 40 groups of charges and fees; and 16 items listed as 'other' revenue sources. The distinction between taxes, licences, charges and fees is, however, often unclear. A number of levies are referred to as charges although they are in reality taxes, since no service is rendered directly and exclusively to the payer. In addition, a wide variety of fees for forms and permits exist. The primary purpose of such permits is regulation, although in many councils they have become mainly a source of local revenue rather than a control mechanism. Thus, in this paper the concept 'tax' includes taxes, licences, charges and fees, unless otherwise stated.

TABLE 1 SOMEWHERE IN HERE

² Until 1998, the Ministry of Local Government was incorporated in the Prime Minister's Office. In September 1998 a new, independent 'Ministry of Regional Administration and Local Government' was established.

The number of different taxes, licences, charges and fees is high and varies between the councils.³ In 1997, for instance, there were at least 25 types of revenue sources being levied in Kibaha DC, compared to more than 60 for Kilosa DC and about 50 in the Dar es Salaam City Commission. 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, *hunting licence* had 10 components (varying with the type of animal), *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.).

In spite of the large number of revenue sources, four main sources are crosscutting almost all councils. These are *development levy* (head tax), *crop* and *livestock cess* (agricultural cess), *business licences* and *market fees*. In 1997 these sources averaged two-thirds (66 per cent) of the reported tax revenues in 42 district councils studied (see Table 2). The head tax ‘development levy’ dominated by contributing 30 per cent of total own revenues, followed by agricultural cess (22 per cent), business licences (about 9 per cent) and market fees (5 per cent).⁴ In a sample of 10 urban councils, the major own revenue bases in 1997 were licences (33 per cent), property tax (21 per cent) and development levy (19 per cent).

TABLE 2 IN SOMEWHERE HERE

Some taxes are levied on a daily basis, others biannually or yearly. In addition, some fees and licences are imposed on individual ‘transactions’. For instance, sand fee is levied in tons per load of sand, and hunting licences are levied per animal (varying with the type of game in question). Market fees are in general levied daily on people selling their goods at market places. However, some councils offer the option of paying an annual fee. Agricultural cess is levied on the

³ 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). However, the number of councils is increasing. Due to attempts to equalise rates on some revenue bases among councils within the same region, some rates have tended to differ by regions.

⁴ 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.

sale of major crops such as maize, rice, coffee, tea, cotton, cashew nuts, sweet-potatoes, etc., and on livestock. Generally, the cess is levied on physical units (weight or volume) rather than value. Large variations in cess rates exist between various crops. Furthermore, there are often large variations in rates between councils. This is also the case for other taxes, including the head tax 'development levy' and the bicycle tax, which are levied on an annual basis.

In 1998, local government own revenues corresponded to 5.8 per cent of total central government tax revenues for 1997/98. This share has been almost unchanged since 1996.⁵ However, tax revenues per capita differ substantially between councils (Fjeldstad and Semboja, 1999). In 1995, it ranged from TSh 344 per person above the age of 18 in Lindi District Council, to TSh 1,541 in Mbinga DC. Furthermore, there are large variations between wards and villages within councils.

The tax 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. At the sub-village level, the kitongoji leader is responsible for mobilising taxpayers.⁶

At the council 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. As such they have access to the local militia. 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 kitongoji leader is responsible for mobilising taxpayers.

In practice, however, 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. Lack of arm's-length relationship between tax collectors and taxpayers introduces economics of affection into

⁵ The fiscal year of local authorities follows the calendar year, while the fiscal year for the central government is from 1 July to 30 June. In 1997/98, total central government tax revenues were TSh 624.1 billion, compared to TSh 36.2 billion in reported local government tax revenues for 1998. In 1997, the exchange rate was USD 1 = TSh 580 (annual average).

⁶ 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. On average there are about 3 vitongoji per village.

village tax collection. In many villages the local politicians resist to mobilise people to pay taxes due to the unpopularity of taxation. In yet other councils, villagers are employed as agents of the council to collect development levy and other minor revenue sources. In Lindi DC, for instance, the council pays a commission of 20 per cent of the total revenue collected to the village collectors.⁷

Most taxes are paid in cash. One exception is for civil servants whose head tax ('development levy') is withheld from their salaries. For others, development levy can be paid during office hours at any of the revenue collecting centres mentioned above. The statutory voluntary period is from January 1 up to September 30. All tax payments made after the deadline are subject to a penalty equivalent to 50 percent of the tax rate. As from October 1 to December 31 development levy payment 'campaigns' are conducted, organised by the ward office and using state organs, i.e., the local militia and judiciary, to ensure compliance. Defaulters may be visited in their homes, and people may be required to show tax receipts at roadblocks. Non-compliers who are caught are brought to the primary court or ward offices. Due to widespread resistance, tax campaigns for development levy in some councils (involving the militia) may start several months before the voluntary (and statutory) payment period expires. The treasury staff argues that by waiting too long after the harvest period taxpayers' would have spent their money and nothing would be left for taxation.

Market fees and crop cesses are, in general, collected at the selling points and markets. However, 'big buyers' of cessable goods (often co-operatives) are expected to pay directly to the council treasury. The buyer then pays the council in advance based on the strength of the figures estimated by the co-operative officer from Ministry of Agriculture. If the figures are not accepted by the 'big buyer', negotiations are opened. Most licences and some fees have to be paid at the respective offices at the district headquarters. Licences are often issued on an annual or biannual basis. The council may carry out spot-checks of entrepreneurs and businesses to control that licences are paid.

Roadblocks are frequently used to control taxpayers. For instance, 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 may also be used to collect market fees, implying that the fees have to be paid before the goods enter the market place.

⁷ This incentive scheme has some parallels to 'tax farming': Businessmen (either individual or syndicates) who wish to become state fiscal agents submit competitive bids to the government (council) specifying how much they are willing to pay for the privilege of collecting taxes. In principle, the highest bidder is to win the council's choice. Proponents of the system today argue that it minimises administrative costs and results in more efficient collection (Azabou and Nugent, 1989). Opponents argue that the supposed gains are largely illusory because the system leads to extortion through overzealous collection. Thus, the government would have to spend considerable resources on monitoring tax collectors (Stella, 1993). Historical evidence indicates that tax farming has often led to extortion, initiating tax riots (Webber and Wildavsky, 1986).

Administrative costs

One consequence of the present local revenue system is the high costs of tax administration.⁸ In Kilosa DC, for instance, the wage bill represented about 80 per cent of total own revenues reported in 1995.⁹ The corresponding figure for 1996 was about 64 per cent. However, when disaggregated by wards, large variations are observed.¹⁰ In some wards in Kilosa DC, the administrative costs are higher than the revenues remitted to the council (Figure 1). 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. In Kidodi ward the wage bill corresponded to 18 per cent of the reported revenues from the ward. In Kibaha DC we also found large differences between the wards (Fjeldstad and Semboja, 1999).

FIGURE 1 IN SOMEWHERE HERE

The costs of tax enforcement also vary between different revenue sources. Some revenues are relatively less costly to administer because there are clear methods to deal with defaulters. For instance, water services may be disconnected if the user fails to pay the water fees. Similarly a licence may be withdrawn if business people fail to pay a licence fee. Furthermore, civil servants and employees in formal sector businesses pay the development levy through a withholding system where the employer collects the tax on behalf of the local authority. Many taxes are, however, relatively difficult to collect. Tax collectors at the ward and village levels in Kibaha DC and Kilosa DC considered development levy to be the most problematic tax to collect, followed by crop cess and livestock cess. Tax officials at the district headquarters also ranked development levy as the most problematic one, followed by property and land taxes.¹¹ The many sub-bases with different rate structures add to the costs.

⁸ In comparison, the administrative costs of the central government 'Tanzania Revenue Authority' constitute approximately 3 per cent of gross revenues reported (TRA, 1998).

⁹ The wage bill includes wages and allowances for the staff of the revenue department and the ward offices, including village executive officers. Revenues refer to the calendar year, while the wage bill refers to the fiscal year of the central government that runs from 1 July to 30 June.

¹⁰ The figures include the salaries of Ward Executive Officers and Village Executive Officers. These officials are, as noted above, 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.

¹¹ The experiences of local government tax officials with respect to property taxes diverge significantly from the recommendations made by consultants involved in the ongoing reform process in Tanzania. Price Waterhouse (1998), for instance, recommends the local authorities to use 'more easily collectible taxes, such as property taxes'.

However, 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. Furthermore, the way in which budgets are compiled, whereby tax revenues appear under one heading and the costs of the local revenue office under another, does not encourage cost-effectiveness. In addition, many costs are simply not made explicit, for instance the use of government owned buildings, or the use of co-operative officers to collect certain taxes.

How the current revenue system emerged

The local government revenue structure in Tanzania is extremely complicated and non-transparent. Moreover, large variations exist among councils with respect to the number of revenue sources and rates. Revenues per capita vary significantly between councils indicating both differences in tax potential and differences in the effectiveness of the local tax administrations. No clear pattern can be discerned from this structure as each council has its own tax structure, implying that there are more than 110 local government revenue structures in the country (excluding village councils). How did this revenue system emerge? There are three main reasons for this:

- (1) the by-law system allows local authorities to introduce new taxes and rate changes, subject to ministerial approval;
- (2) lack of clear criteria for tax design; and
- (3) poor co-ordination between the various levels of government has allowed local government revenue systems to develop without much interference from the centre.

By-laws

At present local authorities in Tanzania have a high degree of autonomy in proposing tax by-laws. The Local Government Finances Act of 1982, and regulations made by the minister responsible for local government specify sources of finance and procedures for imposing and collecting taxes. In principle, every activity located within the jurisdiction of an authority is taxable.¹² Indeed, the Act provides that activities can pay tax to both central and local government.

Proposals about new taxes and rate changes are, in principle, initiated by the Finance and Planning Committee (FPC) of the council, consisting of politically elected councillors. In practice, however, these proposals may originate from the council's Management Team (MT).¹³ The FPC forwards its recommendations to the full Council for discussion and approval. The council's legal section, if available, drafts the by-law to match with legal requirements and jargon.

¹² Specific exemptions do, however, apply to publicly owned lands and buildings, cemeteries and burial grounds, charitable and educational institutions.

¹³ The MT consists of the District Executive Director (chairman) and the heads of the departments (the District Treasurer, the District Water Engineer, the District Engineer, the District Educational Officer, the District Medical Officer, the District Land Officer and the District Administrative Officer).

Thereafter, the recommendations to introduce new taxes and rate changes are forwarded to the Minister for Local Government. The Act requires the Minister to approve the proposals for new taxes and rate changes before implementation. In practise, proposals from the councils on tax changes seem to be rarely turned down by the Ministry.¹⁴ 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 it was expected to come into effect.

Criteria for tax design

The Local Government Finance Act is not explicit about the criteria to be followed when proposing and approving new taxes and rate changes. However, the criterion of revenue generation can be taken for granted to be central to local government taxation. Only implicit suggestions can be read in between the lines with respect to other criteria, including considerations of ability to pay. Provision for graduated rates allows for considerations as regards ability to pay, and implicitly emphasises the issue of vertical equity. Furthermore, the Finance Act encourages horizontal equity across local authorities by providing that residents who choose to pay taxes in another authority should pay the difference, if the rate is lower in the authority in which payment is made. No clause in the Finance Act encourages local authorities to take economic efficiency into consideration. Neither is there any reference to the administrative costs of the tax system. However, provision of a uniform rate per capita may implicitly be aimed at lowering the administrative costs.

We would expect that the various decision-makers involved in tax design pursue different criteria more rigorously than the others. Therefore, there are inherent reasons in the local government institutional arrangement to design a tax system that points in many directions. Differences between the various stakeholders with respect to tax design seem to be exacerbated by internal and external pressures that contribute to strengthening or altering their priorities and choices. First, central government pressure on bureaucrats to raise enough revenue to finance salaries of council staff will alter the relative importance of the revenue criterion at the expense of other criteria. For instance, the survey data from Kibaha and Kilosa District Councils show that the administrative staff, including tax collectors, put more emphasis on revenue generation than elected councillors who emphasise the ability-to-pay criterion. Second, taxpayers' pressure on councillors to lower taxes will alter the relative weight between the ability-to-pay criterion and other criteria. Local politicians are interested in securing their political base at all levels. Thus, politicians most likely are 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 (e.g., in Kibaha DC) reflect the influence of local politicians in tax design. This implies that we may observe large variations in tax design between local authorities depending on the relative bargaining power of councillors and bureaucrats.

¹⁴ In Kibaha DC, we were informed of one case dating a few years back where the Ministry of Local Government did not approve a proposal to increase the development levy rate. The Ministry returned the proposal and requested the council to come up with a new proposal based on a lower rate.

Co-ordination between central and local government

The Finance Act requires the Minister for Local Government to consult with the Minister of Finance in making rules that prescribe limitations and impose conditions on local authorities' financial legislation. However, the Minister for LG has final authority over the proposals. The reasons for incorporating top ministerial level decisions in the designing of local government taxes are not explicitly stated in the act. The point may, however, be to ensure that inconsistencies between local government taxation and central government policies are avoided. In practise, 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.¹⁵ This has partly to do with lack of capacity at all levels.

Presently all the relevant decision-making levels lack the required tax expertise and resources for designing an appropriate tax system.¹⁶ 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 available staff lacks expertise on tax issues. At the ministerial level, experience shows that the main concerns with respect to local tax design are raised by the Legal Department; the ministry has no tax experts.¹⁷ However, even if it contained any, they would easily be overflooded by the influx of proposals from more than 100 councils. Due to lack of capacity and poor co-ordination between the central and local government 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 between the central and local levels 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.

The gap between the statutory and the effective revenue system

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;

¹⁵ 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 Government in March 1999. Some of these suggestions were incorporated into the Minister of Finance's budget speech for fiscal year 1999/2000.

¹⁶ The necessary skills are knowledge to read, understand and interpret the tax statutes and central government guidelines, regulations and policy directions; availability of the relevant information for estimating accurately the budgetary requirements (both revenues and expenditures), tax bases and rates. They require substantial human resources such as statisticians, tax experts, including accountants, auditors, lawyers, etc..

¹⁷ One recommendation made by the 'Task Force on Rationalisation of Central and Local Government Taxation' is to establish a tax unit within the Ministry of Regional Administration and Local Government since the Ministry at present does not possess such expertise.

- (2) explicit and intentional tax evasion and resistance from taxpayers;
- (3) corruption, including embezzlement of revenues;
- (4) political pressure on the local tax administration to relax on revenue collection;
and
- (5) negligence on the part of many government agencies and parastatals to pay taxes.

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 may further exacerbate the situation. Given the complicated revenue system, already discussed above, 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.

There is undoubtedly room for improved tax administration. However, before considering the issue of capacity a more fundamental issue has to be addressed. This has to do with the rationale to squeeze additional revenues from poorly designed taxes. In other words, improved administrative capacity may increase the negative effects on the economy and society in general, and lead to more inferior outcomes than the present system. Thus, the major problem may not be lack of capacity, but the tax structure itself. This reasoning has implications for the sequencing of the reform activities to be discussed below.

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 (Semboja and Therkildsen, 1992). The deterioration and in some cases non-existence of public services heighten taxpayers' perceptions of exploitation from an unequal contract with government, and this promotes tax resistance (Fjeldstad and Semboja, 1998). Although most taxpayers are unable to assess the exact value of what they receive from the government in return for taxes paid, it can be argued that they have general impressions concerning their terms of trade with the government.¹⁸ In this context, it can be assumed that taxpayers' behaviour is influenced by their satisfaction or lack of satisfaction with the terms of trade with government (Levi, 1988). Thus, if the system of taxes is perceived to be unjust, tax resistance may be considered as an attempt by the taxpayers to adjust their terms of trade with the government.¹⁹

¹⁸Survey research from Western countries also suggests that taxpayers make judgements about the fairness of particular taxes. See, for instance, Spicer and Lundstedt (1976) and Smith (1992).

¹⁹Non-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

The argument that tax resistance correlates with deteriorating public services is supported by other studies. Bukurura (1991:91), for instance, refers to an investigation from 1987 by the Tanzania News Agency in Kigoma Town Council, which reported that ‘many people were defaulting apparently because they thought the council was not doing its best to serve the residents’. Tripp (1997:233) refers to an article in *Daily News* (from 9 June 1985) in which she quotes a typical comment by a Dar es Salaam resident: ‘When it comes to Development Levy we have ... seen nothing as a result of the levy we pay... the city is very dirty and the situation is deteriorating day in and out... What we want to see is how such taxes are being spent.’

Tax resistance sometimes also takes more violent forms. In Kilosa DC, for instance, tax collectors avoided certain villages due to the high personal risks involved in tax collection. Other villages were only visited by collectors accompanied by the local militia. In 1996 the ward office in Chanzuru was destroyed during night and the Tax Register Books were burnt. Cases of tax revolts are also reported from councils in other regions. *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, ...’

Corruption

Fiscal corruption is extensive in local authorities.²⁰ 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, our findings show that the most common type of corruption is embezzlement of revenues by tax collectors and administrators. Three factors may have led to widespread theft of tax revenues within the local authorities (Prud’homme, 1992):

- the low level of wages paid to staff;
- the complex nature of the tax structure; and
- inadequate controls.

The official wage level

The official wages of government employees in Tanzania are very low.²¹ 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

political action. The Boston tea party and the Thatcher poll tax are illustrative examples. Bates (1983) provides some examples from Africa.

²⁰ Fiscal corruption is here defined as any action in which tax collectors use their position to extort money from taxpayers or collude with taxpayers to defraud the treasury or find some other means to embezzle money from the tax authorities.

²¹ 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.

that civil servants cannot live on their wages is not a metaphor, but a statement of fact.

In a survey on corruption in Tanzania, 78 per cent of the respondents mentioned low salaries of public service workers as a major incentive for seeking and accepting bribes (CIET International, 1996:24). One respondent stated: 'You may find someone having not received salary for at least three or four months. What do you think he will eat? He will eat us!'

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 from a second or third job in the private sector, as well as embezzled funds.²²

The tax structure and revenue target

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.²³ 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. In Kibaha DC, several village executive officers (VEOs) and some ward revenue collectors (WRC) had been fired in recent years, due to poor performance. In general, ward executive officers were transferred to less attractive or remote wards if they did not perform with success according to the wage bill criterion. However, in Kilosa DC, the Ward Executive Officer in Lumbiji ward was fired in 1997 due to poor performance.

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.²⁴ 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

²² In our survey in Kibaha and Kilosa, the majority of the tax administrative staff interviewed said that they experienced long delays in payment of their salaries. When asked how they managed to survive, the majority answered that they survived on products and incomes from their "shamba" (plot of land). Some also said they borrowed money from relatives.

²³ An examination of budgeted versus actual figures for several years in Kibaha and Kilosa DC, indicates that these two sets of figures bear little resemblance to each other. Budget estimates often overstate revenues and sometimes understate expenditures.

²⁴ According to Rose-Ackerman (1999:49), corruption is often embedded in the hierarchical structure of the bureaucracy. Low-levels officials collect bribes and pass a share to those at higher levels. Conversely, higher-ups may organise and rationalise the corrupt system to avoid wasteful competition between lower levels. This system has some similarities with sharecropping systems in agriculture. Sharecropping is a land-tenure system where the landlord gets a (percentage) share of agricultural output and the tenant keeps the remaining output (Sah and Stiglitz, 1992).

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

Controls

The lack of effective controls also facilitates embezzlement. In principle, financial control in local authorities in Tanzania is exercised through internal and external audits. However, both functions are weak. In some councils, including Kilosa and Kibaha, no internal audit units are in place.

Regarding external audits, the Auditor General's office 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. According to Sedigh and Muganda (1999:167), the Auditor General's Office has been hindered by financial constraints and its inability to attract, train or keep suitable staff since the private sector tends to offer more rewarding employment to professionals. 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, and an increasing number of cases has been reported in recent years where the Auditor General has not approved the councils' accounts. Between 1993 and 1996, out of 64 councils audited, the accounts of 33 councils (52 per cent) were classified as poor, 12 as average and 19 as good (Semboja, 1999).

Some cases

The combination of low wages, a non-transparent tax system, and lack of controls promotes corruption. To illustrate the mechanisms and scope of corruption we present below a few cases:

As noted above, most taxes are collected in the form of cash. The collector is supposed to deliver a receipt to the taxpayer, a copy (counterfoil) of which is retained for auditing. In principle, the tax collector is required to surrender to the office the used receipt books showing used counterfoils and unutilised receipts before receiving new ones. In practice this procedure is often not followed. In Kilosa DC we found evidence that large numbers of tax receipt counterfoils were not surrendered to the council headquarters as required by the financial regulations.²⁵ It is reasonable to assume that the counterfoils not returned are used to embezzle tax revenues. A note from the district chief executive (dated 12 March 1997) supports this proposition. Referring to the missing receipt books it states cautiously: '... In these circumstances, it is possible that the revenue collected was not submitted in the proper office.'²⁶

The estimated development levy not submitted in this way in 1995 corresponded to more than 35 per cent of the council's actual revenues from this source. The corresponding figure for 1996 was about 15 per cent. It is not possible to estimate the amount embezzled in this way for other categories of taxes such as crop cess, livestock cess and market fees, since the receipts issued vary from one transaction to the other, depending on the specific tax item, rates and units. However, for 1995

²⁵ In total, 771 receipt books were not surrendered in the period 6 January 1995 to 26 February 1997. The number of receipts in each book varied from 50 to 150, depending on the type of tax.

²⁶ Translated from Swahili.

more than 30 per cent of the receipt books issued for such taxes were not surrendered.

Even those receipt books that are surrendered can easily be modified. One well-known method of stealing money paid in by taxpayers is through the use of *the carbon shipping system* (see, for instance, URT, 1996a:318; and TCCIA, 1995): The taxpayer is given a receipt showing the amount paid. Since no carbon paper is put under the original receipt in the process of writing, the collector later enters a lesser figure on the copy and pockets the difference. Another method is to write receipts noting a lower amount than the amount paid by the taxpayer. This method is more common when dealing with illiterate taxpayers. In other cases, the carbon paper is placed in such a way that the counterfeit only registers a part of the figure written on the taxpayer's receipt, for instance, omitting some zeros.

Embezzlement also takes place through collusion between staff of the council's treasury department and bank officials, leading to the non-banking of tax revenues. Bank officials issue a receipt on the correct amount to the treasury official. The receipt is brought back to the council's revenue office for control, and is consistent with the money remitted. However, only a part of the tax revenues is actually deposited into the council's account. The rest is shared between the bank officials and the collectors involved. This method can be sustained over time since what actually is deposited in the council's bank account is rarely controlled. Recently, one such case was brought to court, involving several staff members of the council's revenue department. The amount embezzled in this specific case during the first 6 months of 1997 corresponded to 10 per cent of the total own revenues of that council in 1996.²⁷ In early 1998, the Controller and Auditor General uncovered cases from 31 councils where cashbook-receipts were not reflected in the bank statements. The total unaccounted amount in these cases was TSh 1.1 billion, corresponding to 3.5 per cent of the total recorded local government tax revenues in 1997 (*Daily News*, March 23 1998).

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

- the collectors and tax inspectors are stationed relatively permanently in their positions, i.e., they are rarely transferred;
- the network is limited to a relatively small number of people in the tax administration; and
- 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 a major impediment to revenue collection in some councils (Semboja and Therkildsen, 1992:1107). This problem stems from the fact that

²⁷ In the case referred to above, the embezzlement-network was revealed when a new treasurer took over and initiated internal controls.

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.²⁸

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 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'.

The influence of international donors may partly explain differences between councils with respect to the influence of politicians on revenue collection. Through district development programmes donors have often exerted strong influence on the behaviour, decisions and actions of local authorities' administrators and politicians. In general, donors co-operate with council administrators and staff to implement their activities, usually through the creation of parallel structures. This has increased the influence and power of the bureaucracy, at the expense of the political system. The Kilosa DC, which has a long history of donor support, provided two lessons supporting this proposition:

- firstly, tax collection in Kilosa DC is facilitated through harsh and violent approaches that are mainly advocated and implemented by council administrators, with minimum support from local politicians;
- secondly, donor support may cushion council administrators against possible taxpayers' opposition since service provision through donor-supported activities provides a free-riding opportunity to council administrators who often claim to be the providers of such services. This has provided opportunity for corruption.

In Kibaha DC, which has experienced limited donor support, local politicians, in contrast, seem to play a more important role in the design and enforcement of council revenues. Thus, tax collection is characterised as being more lax compared to Kilosa. The level of corruption also seems to be lower in Kibaha. This may have to do with the fact that local politicians to some extent monitor the collectors.

²⁸ Conflicts between council employees and local politicians are not of any new date in Tanzania. For instance, Dryden (1968:144-149), referring to the mid-1960s, describes in detail some areas of conflict between these stakeholders.

Negligence by government institutions, parastatals and co-operative unions

A final major administrative problem faced by many councils is the negligence of government institutions and parastatals in submitting the taxes and charges they owe to local authorities. Local government officials cannot easily turn off the water supplies to schools and hospitals, and they cannot force central government ministries, district commissioners or other local authorities to pay for such services.

Furthermore, many councils have experienced huge problems in collecting crop cess from the co-operative unions. Our interviews with district and union officials in Kibaha and Kilosa revealed that co-operative unions often were reluctant to pay cess owed to the council. In 1995, for instance, the Mlandizi Disunyara Co-operative Union in Kibaha DC was brought to court for not paying the cashew nut cess, and thereby forced to pay the taxes it owed. In June 1997 Kilosa DC was preparing a court case against the sugar company due to large arrears in cess remission.²⁹ Similar cases have been reported from other councils. For instance, ERB (1997) reports that in 1995 the co-operative union SHIRECU owed Maswa DC TSh 50 million in crop cess (an amount equivalent to more than 50 per cent of the council's total tax revenues the same year). SHIRECU also owed Meatu DC TSh 33 million (equivalent to 34 per cent of the council's tax revenues). In that year, various companies owed Meatu DC TSh 60 million in unremitted crop cess (equivalent to more than 60 per cent of its reported tax revenues).

Why the current revenue system has 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, 1998; and Myrdal, 1968;).³⁰ We have no indications that this is the case amongst local authorities in Tanzania. A deliberate strategy requires capacity and detailed knowledge on how the tax system works, and that capacity is in general poor at the local level. 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

²⁹ Information provided by council officials.

³⁰ According to Winters (1996:166), the strongest resistance to tax reforms in Indonesia came from the tax officials themselves, since they had the most to lose from the depersonalisation and simplification of the tax system. Flatters and Macleod (1995:409), also referring to Indonesia, assert that tax collectors actively opposed simplifications in property tax administration, income tax laws and tariff structures.

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 explain the existing situation. But here again there may be variations between councils.

Options for fiscal reforms

It is clear from the above analysis that the local government tax system in Tanzania is overdue for reform. The current local tax 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 further undermining the legitimacy of the government. 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. A recent report to the Government suggests measures to improve capacity building for revenue mobilisation and collection (Price Waterhouse, 1998). 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:

- (1) abolition of unsatisfactory local taxes;
- (2) improvements to remaining revenue bases; and
- (3) 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 we have found costly to enforce. The levy is extremely unpopular among taxpayers and tax resistance is widespread.

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 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.³¹

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 1997.³² 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.

For larger establishments the hotel levy has been subsumed into the VAT rate of 20 per cent collected by the central government. Thus, local governments should not impose hotel levy on VAT-registered establishments. However, since smaller hotels and guesthouses with an annual turnover of less than TSh 20 million are not registered for VAT, the hotel levy could in principle be retained for smaller establishments. But the current levy of 20 per cent of turnover in some councils is very high. Since the possibilities to monitor are small and the incentives to evade are large, the suitability of hotel levy as a local revenue source should be reconsidered.

Property tax may continue to be an important source of revenue in urban councils. It may also become important in semi-urbanised centres in district councils. In recent years, some rural councils have passed by-laws levying taxes for commercial land use (for instance, Hai District Councils and Simanjiro DC).

³¹ It is sometimes argued that the central government needs to exercise tight control over money that comes from the centre, but local governments should be free to do what they like with their 'own' revenues, such as local taxes. However, the fact is that all money comes from the taxpayer, and it is largely a matter of convenience which level of government collects particular taxes. Thus, Devas (1997:358) argues that tight control over certain sources of money and wide discretion over others is somewhat illogical if the objective is to ensure proper use of public resources and to protect citizens.

³² 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).

Commercial land use includes agriculture, mining operations, sand extraction etc.. Some consultants even claim that commercial land tax 'will be one of the principal revenue sources for most of the rural councils' (Price Waterhouse, 1998).

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.³³ However, they also have some obvious weaknesses that 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. In theory, assessment of property value and revenue collection are straightforward: conduct a cadastral survey that assesses the market or site value of each plot of land or property, and send a tax bill to each owner. In practice, cadastral surveys are expensive and time-consuming. Tax offices are, in general, short on assessors, if they have any at all. Thus, it is often difficult to maintain assessments, which are also often eroded by inflation. In principle, non-compliance of property tax can be enforced by confiscation and sale of the owner's personal effects in the building initially, and ultimately upon the collateral of the real estate itself. However, it may prove difficult to carry out such tax enforcement: Firstly, experience shows that courts are often swamped by appeals from angry property- and landowners (Skinner, 1993:364). Secondly, harsh enforcement mechanisms may result in intervention from politicians facing complaints from their constituents (Enemuo, 2000:193).

Thus, experience from other countries and historical evidence from Tanzania advocate cautiousness when (1) extending the present property tax to district councils, and (2) when imposing a commercial land tax in local authorities. At this stage of the reform process it is important to identify the fundamental causes of the problems experienced, in depth and with open minds, to avoid counterproductive biases. In particular, it is important to seriously consider the administrative capacity to maintain assessments of property value. Furthermore, the enforcement mechanisms must be carefully designed to avoid a mushrooming number of court cases and widespread resistance from taxpayers.

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

³³ In some Western countries, including Denmark and Norway, local property taxation is a good source of local taxation.

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. Furthermore, user charges have the potential of enhancing resource allocation by reducing wasteful usage since users pay from their own resources. User charges may also stimulate a supply response by service producers closer to customer demands that in turn may raise quality and remove unnecessary production.

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, as we already have seen, 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. This suggests that there are reasons and scope for innovation.

Improving institutional capacity

As discussed above, the capacity of local governments is very weak in tax design. The resource requirements for building this capacity are high, and can only be done in the medium to long run. Therefore, in the short run, external support should be given by providing very clear guidelines and limits in the design of local government tax systems. Furthermore, the current system of approving tax by-laws should be strengthened. In particular, there is an urgent need to improve co-ordination with the national tax system and policies. As a first step, an expert committee (a 'Finance and Fiscal Commission'), to advise both the Minister of Finance and the Minister of Local Government on the local government tax system may be established. This committee should advise the two ministers before a by-law is approved. The expert committee should not be a substitute for the work of staff at the council and Ministry of Regional Administration and Local Government. However, since it may require more resources than are available in the short term to build relevant capacity at the councils and the Ministry, the importance of a 'Finance and Fiscal Commission' cannot be overemphasised.

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.³⁴ Transfers should therefore be considered an important component of the decentralisation programme.

The basic rationale for a system of transfers is the existence of a fiscal gap between own revenue and expenditures (Ahmad, 1997). This is exacerbated by central government requirements that require different regions and localities to maintain established 'minimum' standards of public services. It is beyond the

³⁴This has been the situation since independence (see Dryden, 1968:128).

scope of this article to quantify the financial resources needed in the form of transfers from the central government. These magnitudes are also difficult to estimate due to lack of reliable information on potential revenues and adequate expenditures required to meet established standards. However, as argued by Semboja and Therkildsen (1992:1104), 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 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, 1996). 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, such as a 'Financial and Fiscal Committee', to ensure a regular and frequent dialogue 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.

Substantial decentralisation is also likely to make it more complicated for the central government to carry out macroeconomic stabilisation through budgetary policies. For the time being it is particularly important to impose hard budget constraints on local authorities by ensuring that there is adequate balance between expenditure responsibilities and their own revenues, in addition to clearly defined transfers from the centre. Therefore, due to Tanzania's acute fiscal imbalances and its aid dependency, fiscal decentralisation should proceed more cautiously.

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Table 1 Current local government revenue sources

TAXES	NON TAX SOURCES		
	Licences	Fees and Charges	Other Revenue
<ol style="list-style-type: none"> 1. Development levy 2. Crop cess 3. Livestock cess 4. Industrial cess 5. Property taxes 6. City service levy 7. Hotel levy 8. Guest house levy 9. Entertainment levy 10. Bicycle tax 	<ol style="list-style-type: none"> 1. Business licence 2. Street vending and hawking licence 3. Intoxicating liquor licence 4. Foreign liquor licence 5. Local liquor licence 6. Livestock licence 7. Dog keeping licence 8. Fisheries licence 9. Hunting licence 10. Gun holding licence 11. Blood drying activity licence 12. Forestry product 13. Road licence 14. Taxi, pick-up and lorry licence 15. Bus stand licence 16. Scaffolding licence 17. Plying licence 18. Human resource licence 	<ol style="list-style-type: none"> 1. Market fees 2. Tax registration fees 3. Street vending fee 4. Sand fee 5. Entertainment fees 6. Advertising board fee (billboards) 7. Cattle market charge 8. Abattoir (slaughter) fee 9. Bicycle registration fee 10. Business licence application fee 11. Licence transfer fee (for business people changing area or type of business) 12. Tender application fee 13. Refuse collection charge 14. By-law permit charge 15. Burial charge 16. Business premises inspection charge 17. Playing ground charge 18. Cesspit emptying fee 19. Planning scrutiny fee 20. School fee 21. UPE contributions fee 22. Weights and measures fee 23. Motor vehicle parking fee 24. Water pipe installation fee 25. Storm water drainage fee 26. Inoculation/vaccination fee/clinic fee 27. Medical examination fee 28. Fire service fee 29. Market stall renting fee 30. Hire of plant fee 31. Valuation fee 32. Cultural games/recreation fee 33. Ambulance hire fee 34. Public convenience fee 35. Recovering charge of lost dev. levy receipt 36. Contract approval fee 37. Skin treating fee 38. Push cart fee 39. Cattle trekking fee 40. Pupil transfer fee (paid by parents) 	<ol style="list-style-type: none"> 1. Road toll 2. Land rent and service charge 3. Rent from council's houses/buildings 4. By-law fines 5. Stray animals fine 6. Permit to move animals in urban areas 7. Tourist hunting fee 8. Sale of fish commission 9. Bank interest 10. Sale of assets 11. Hire of plants and vehicles 12. Sale of plants and seeds 13. Sale of identity cards 14. Investment dividends 15. Other transfers 16. Other income

Source: By-laws and revenue schedules from various councils.

Table 2 Local government own revenue sources, 1995-1998 (Mill. TSh)

A: District Councils (N=42)	1995		1996		1997		1998	
<i>Revenue sources</i>	<i>Actual</i>	<i>%</i>	<i>Actual</i>	<i>%</i>	<i>Actual</i>	<i>%</i>	<i>Budget</i>	<i>%</i>
Development levy	913,40	24,4	1482,60	27,2	1882,50	30,7	4017,70	30,8
Agricultural cess (crop & livestock)	944,20	25,2	1377,60	25,2	1352,70	22,1	3369,00	25,9
Business licences	362,00	9,7	557,50	10,2	522,80	8,5	690,40	5,3
Market fees	204,30	5,5	328,30	6,0	305,50	5,0	480,20	3,7
Other taxes	108,60	2,9	163,50	3,0	285,80	4,7	826,60	6,3
Liquor licences	82,50	2,2	94,00	1,7	118,10	1,9	171,90	1,3
Other fees & fines	457,40	12,2	648,60	11,9	758,20	12,4	1657,00	12,7
Miscellaneous	668,60	17,9	804,40	14,7	899,20	14,7	1817,90	14,0
<i>Total</i>	<i>3741,00</i>	<i>100,0</i>	<i>5456,50</i>	<i>100,0</i>	<i>6124,80</i>	<i>100,0</i>	<i>13030,70</i>	<i>100,0</i>

B: Urban Councils (N=10)	1995		1996		1997		1998	
<i>Revenue sources</i>	<i>Actual</i>	<i>%</i>	<i>Actual</i>	<i>%</i>	<i>Actual</i>	<i>%</i>	<i>Budget</i>	<i>%</i>
Development levy	292,9	10,9	890,8	17,4	1659,6	18,9	2368,8	17,3
Property tax	423,2	15,7	965,4	18,9	1869,6	21,3	3184,2	23,3
Licences	712,0	26,4	1359,0	26,6	2918,3	33,3	3825,9	28,0
Industrial cess	124,0	4,6	223,3	4,4	262,3	3,0	387,1	2,8
Other cess	120,9	4,5	145,7	2,8	191,6	2,2	327,0	2,4
Fees	275,6	10,2	417,4	8,2	493,6	5,6	952,6	7,0
Levies	272,6	10,1	335,3	6,6	345,7	3,9	724,4	5,3
Miscellaneous	474,7	17,6	776,0	15,2	1027,8	11,7	1910,9	14,0
<i>Total</i>	<i>2695,9</i>	<i>100,0</i>	<i>5112,9</i>	<i>100,0</i>	<i>8768,5</i>	<i>100,0</i>	<i>13680,9</i>	<i>100,0</i>

Source: Computed from Price Waterhouse (1998).

**Figure 1 Size of wage bill (1996/97) in relation to tax revenues (1996),
by wards in Kilosa DC**

