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"AID AS A CATALYST TO INCREASE DOMESTIC REVENUE MOBILISATION IN SUB SAHARAN AFRICA"

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"AID AS A CATALYST TO INCREASE DOMESTIC REVENUE MOBILISATION IN SUB SAHARAN AFRICA"

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ACRONYMS

AAA	Accra Agenda for Action
ACCA	Association of Chartered Certified Accountants
AEO	African Economic Outlook
AFRITAC	African Regional Technical Assistance Centers
ARAs	Autonomous Revenue Authorities
ASYCUDA	Automated System for Customs Data
ATAF	African Tax Administration Forum
Bn	Billion
CEPS	Customs, Excise and Preventive Service
CFA	Committee of Fiscal Affairs
CTPA	Centre for Tax Policy and administration
DAC	Development Assistance Committee
DFID	Department for International Development
DIE	German Development Institute
DPs	Development Partners
DRM	Domestic Revenue Mobilization
EAC	East African Community
ECOWAS	Economic Community for West African States
EITI	Extractive Industries Transparency Initiative
ERP	Economic Recovery Programme
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GEAR	Growth Employment and Redistribution
GTZ	Germany's International Co-operation Enterprise
HIPC	Heavily Indebted Poor Countries
ICF	Investment Climate Facility for Africa
IFC	International Finance Cooperation
IMF	International Monetary Fund
IRS	Internal Revenue Services
ITAS	Integrated Tax Administration System (Zambia)
ITAX	Integrated Tax Administration System (Ghana)
ITC	International Tax Compact
ITD	International Tax Dialogue
LDCs	Least Developing Countries
LTU	Large Taxpayer Unit
MCP	Managing Compliance Programme
MDBS	Multi-Donor Budget Support Programmes
MDGs	Millennium Development Goals
MMD	Movement for Multiparty Democracy
MoFPED	Ministry of Finance Planning and Economic Development
Norad	Norwegian Agency for Development Co-operation
NRS	National Revenue Secretariat
ODA	Official Development Assistance
OECD	Organization for Economic Co-operation and Development

PEAP	Poverty Action Eradication Plan
PRSP	Poverty Reduction Strategy Paper
RAGB	Revenue Agencies Governing Board
RIZES	Revenue Institutions in Zambia Enhanced Support
RPD	Reconstruction and Development Programme
SACU	Southern African Customs Union
SADC	Southern African Development community
SARS	South African Revenue Service
SECO	Swiss State Secretariat for Economic Affairs
SSA	Sub-Saharan Africa
TAP	Tax Administration Project
TIN	Taxpayer Identification Number
TRA	Tanzania Revenue Authority
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
URA	Uganda Revenue Authority
USD	United States Dollars
VATS	VAT Service
WAEMU	West African Economic and Monetary Union
ZAR	South African Rand
ZRA	Zambia Revenue Authority

EXECUTIVE SUMMARY

Donors and programme countries[1] increasingly acknowledge the potential of aid as a means of leveraging other flows towards to reduce aid dependency. There is also emerging consensus that aid can have beneficial effects when it acts as a catalyst to promote domestic tax mobilization. Domestic revenue is the main source of development finance and the foundation for long term poverty reduction and sustainable development in many programme countries. Based on this premises this background paper draws on experience of five Sub Saharan African countries (Ghana, South Africa, Tanzania, Uganda and Zambia) to review impact of aid on tax reforms, good practices and assess prospects. The Ghana, Tanzania and Zambia case studies were drawn form on donor support for tax administration Africa commissioned by the German Development Institute in 2008 and updated to 2011. South Africa was sourced from the SARs website while the Uganda case was from various URA reports and experiences.

The need for an increase in Domestic Revenue Mobilization (DRM) is substantial in Sub Saharan African (SSA) countries; however improving DRM has importance beyond that. Requirements for reducing poverty and improving infrastructure are substantial and achieving Millennium Development Goals (MDGs) may require SSA countries to increase tax to Gross Domestic Product (GDP) ratio by around 4 per cent (UN, 2005). However quality of measures matters i.e. increase of revenue from already compliant taxpayers can worsen distortions and perceived inequalities thus the need to increase the tax base. More fundamentally the centrality of taxation in exercise of State powers means that more efficient fairer and less corrupt tax system can spear head improvement in wider governance relations.

Trends of aid show that net Official Development Assistance (ODA) flows to Africa from Development Assistance Committee (DAC) has risen from USD 21.3 Bn in 2002 to USD 47.8 Bn in 2010, an average of 37% of net ODA aid disbursements to all developing countries. Despite the call for aid to more productive sectors by aid recipients, more of it continues to go to social sectors whose share of aid to Africa has increased from 22.6% of net ODA flows in 2005 to 38.8% in 2010. Given that tax administration is a subset of aid allocated to public sector financial management which has received an average of 0.1% of the aid allocation over the period between 2002 to 2010, then allocation to tax administration is less than 0.1%. Therefore if development is to take off this ratio will have to be dramatically increased.

Experiences from the countries understudied show that aid has impacted positively on the tax reforms. For all countries except South Africa, donor assistance was fundamental in the creation of the autonomous revenue authorities which have achieved revenue growths in a short period. South Africa used her own funding from the South African treasury to create the South African Revenue Services. Donor assistance has also been instrumental in the computerization of the revenue collection processes in the programme countries. Support was offered in the introduction of computer systems for customs; ASYCUDA, management of Value Added Tax computerized systems, domestic taxes systems and for some cases an

[1] Programme countries include the 27 European Union countries, Iceland, Liechtenstein, Norway and Switzerland.

integrated domestic taxes system. For some of the countries the donors were fully involved in the management of the funds (Tanzania) while for others the Revenue management was given the autonomy to manage the funds (URA's second modernization phase). For the case of Zambia donor assistance was extended to other important stakeholders and civil society organizations in order to strengthen their ability to engage in tax issues. For the case of South Africa the tax reforms were supported by the National treasury.

There have also been a number of challenges that have faced the tax reforms; There are cases where there was a multiplicity of donors undermining coherent reform effort (Tanzania, introduction of information technology and Taxpayer Identification Number (TIN) were not coordinated at introduction). In Ghana donor support led to the computerization of the processes however the human resource was not adequately trained and the recruitment of staff was not to the recommended numbers leading to ineffective implementation of the reforms. There were also incidents where the reforms processes were managed offshore in the donor country (Tanzania) leaving the recipient country inexperienced.

Overall donor support has had mixed results in supporting the improvement of tax administration capability on a sustainable basis. For some cases revenue performance had a strong initial phase followed by stagnation or decline. On this basis recommendations have been made on making future donor assistance more effective; Increase support of taxpayer associations and similar organs of civil society in order to provide better data as a check for revenue auditors; better training needed to improve the service orientation of tax officials in reform administration; It is not enough for revenue administrations to be under one umbrella but have a full integration of the agencies (Ghana) and processes(i.e. ASYCUDA & ITAX) for cases where the revenue functions are fully integrated; technical donor support needs coherence. Success of this preferred the basket funding (Uganda) and for other cases the recipient countries should have a strong program management office; ensure that skills development is taken as a national priority so as to improve quality of labor that will lead to growth in industrial and services sector thus formalization of the economy; Provide expertise on how to detect corruption within tax administrations; actively strengthen the support base for tax administration reform through collaboration; Change management of the reforms demands that communication of the effects of prospective reforms has to be made to the relevant constituencies such as tax officers, taxpayers and governments. It is recommended that Revenue Authorities identify important stakeholders and develop communication strategies; support mechanism for restraint such as revenue tribunals in order to limit over aggressive enforcement tactics; donors must not be the driving force in tax administration reforms and donor domination of annual revenue target setting negotiations may be counterproductive; donors should at least broaden the scope of indicators for success (beyond the tax to GDP ratio); support value addition to raw materials especially in minerals and agricultural sectors i.e. refinery of oil and gas creates jobs, increases tax base, allows origin country to use by products and leads to early eradication of poverty; support activities in the main economic growth sectors such as energy, infrastructure, human capital and access to credit; and support formulation of regional blocks for wider market.

Emerging trends in the global context that are likely to have negative impact on national tax system are; globalization of the economy; integration of the World Economies and declining share of world trade from low developed countries; internationalization of the global financial sector; increased dependence on mineral sources; supply constraints and fluctuations in commodity prices; and declining Foreign Direct Investment (FDI).

Saharan African countries are still having a number of concerns despite the flow of ODA and increase in DRM; narrow tax base, on average 40% of the GDP in Africa is informal (Schneider Buehn& Montenegro, 2010); weak administrative systems, low tax moral and poor governance; capital flight; tax incentives and exemptions; low savings; and challenges associated with globalization of the private sector such as ecommerce and transfer pricing.

In conclusion a number of factors influence revenue mobilization in developing countries. On the positive side, the global economy continues to recover from the financial crisis, especially the emerging economies that play an increasingly important role in Africa. In combination with rising commodity prices, this economic recovery makes for a favorable scenario for resource-exporting countries that can expect increasing FDI flows. As investors, especially from emerging partners become more comfortable with the overall African business environment, the global upswing will also likely increase investment in developing economies. The most effective way of increasing public revenue for developing countries is through policies that increase the tax-base through sustained economic growth. Efficient tax collection also strengthens public resource mobilization without over-taxing the economy. Developing countries need to devise strategies of managing the trends in the economy while developed countries need to uphold commitments made at various fora on helping developing countries end the dependence on aid and actively participate in world economy.

1. INTRODUCTION

The overwhelming desire to fill Africa's development resource gap and the continuous efforts to attain this has been intensified since the turn of the century (United Nations (UN), 2009). This according to the UN report is further evidenced by the United Nations Financing for Development Conference held in Monterrey in 2002 and other high profile summits on African development since then. However despite all good intentions, the heavily indebted poor country (HIPC) debt relief programme has fallen short of its own cardinal principle of additionality. This has further been exacerbated by the revolving fears that aid to Africa will decline[2] as donors struggle to contain the social and economic consequences of the crisis on their own citizens. This therefore means that the current economic crisis highlights the problems associated with overreliance on external financial resources and makes Domestic Resource Mobilization (DRM) even more relevant.

As further observed by the Department for International Development (DFID) report of 2009, the need for public revenue depends on the whole context of public finances: levels of aid, capacity to borrow, and the size of public expenditure since there is no agreed upon optimal size for the public sector, but it is clear that the Millennium Development Goals (MDGs) create an increased demand for public services. In this regard, governments use taxation as the central source of state revenue in order to provide public services and to enhance human and economic development in their countries, it can however be observed that some developing countries are not able to finance all desirable public expenditures and investments through the tax revenue they collect, which is why bilateral and multilateral donors provide development assistance and thereby alleviate budget constraints. These official resource inflows continue to be crucial sources of external financing for developing countries, typically being used to finance economically and socially essential public spending (Atsushi and Yasuhisa, 2005).

Developing countries also need to ensure that their own policies are coherent and do not undermine their development priorities. It is clear, therefore, that African countries cannot count solely on external financial resources to meet their development needs. DRM and efficient investment in areas that promote the structural transformation and sustainable development of African countries are of utmost importance. Effective tax systems are thus a vital pillar to strengthen the fiscal space of governments, allowing them to determine and fund national priorities. As such, tax policy needs to be viewed as an intrinsically political issue that requires international attention and support to combat illicit financial flows, tax avoidance and evasion; and reduce the impact of tax havens[3].

This paper therefore seeks to illustrate the role of Official Development Assistance (ODA) as a catalyst to improve domestic tax structures in Sub Saharan Africa (SSA) such that dependency on aid by African Countries may eventually come to an end. In doing so, the paper highlights the current trends of aid and revenue Mobilization in Africa. The paper further presents a review on the suitability, effectiveness and impact of Aid in increasing tax

[2] The OECD report of 2010 indicates that the deceleration is likely to be more marked for low income countries and for Africa in particular, where foreign aid is projected to increase at about 1% per year in real terms, compared to a 13% annual growth rate in the past three years. Thus, additional aid to these countries is likely to be outpaced by population increases.

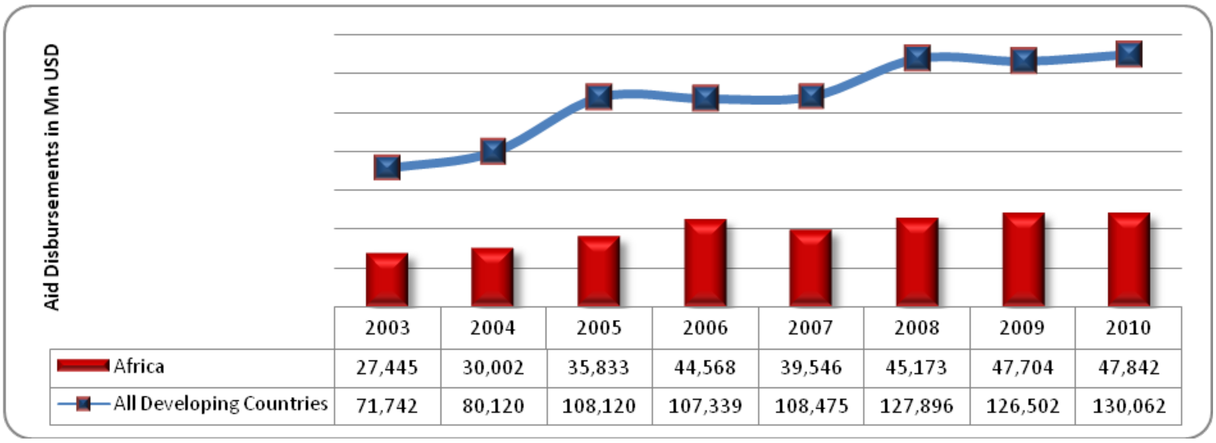
[3] International Tax Compact (2010): Mapping Survey Taxation and Development, Eschborn: GTZ

revenues in the Sub Saharan African countries by drawing on five SSA counties' experiences. It goes further to assess the impact of the evolving "development effectiveness" agenda on the use of aid to help developing countries increase tax revenues. Finally, the paper delves into an analysis of stakeholder concerns in programme countries on tax reform by critically looking at the challenges faced by African governments in failing to fully finance their expenditure and subsequently other challenges associated with tax reform.

2. TRENDS OF ODA IN AFRICA

It is estimated that in 2010 net ODA from members of the Development Assistance Committee (DAC) of the Organisation for Economic Co-operation and development (OECD) to developing countries reached USD 130.1Bn representing an increase of 2.8% over the USD 126.5 Bn of 2009.The development partners increase aid is in response to calls for MDGs support and debt relief to HIPC Countries.

Figure 1: ODA Total Net Disbursements (2003 – 2010)



	2003	2004	2005	2006	2007	2008	2009	2010
Africa	27,445	30,002	35,833	44,568	39,546	45,173	47,704	47,842
All Developing Countries	71,742	80,120	108,120	107,339	108,475	127,896	126,502	130,062

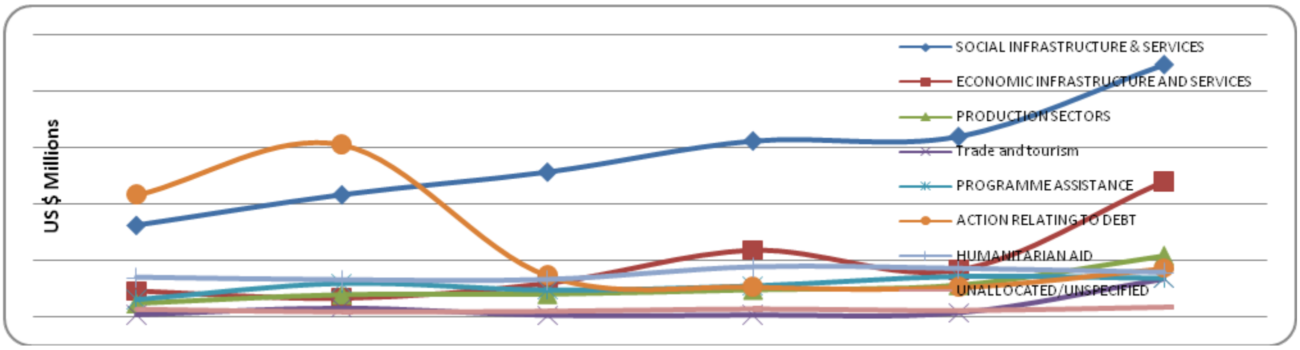
Source: data extracted on 11 May 2012 09: 57 UTC (GMT) from OECD.Stat

Aid to Africa has risen recently, from USD 27.4 Bn in 2003 to USD 47.8 Bn in 2010. This is an average of 37 per cent of net ODA aid disbursements to all developing countries. According to data available from OECD, the high amount of aid received in 2006 i.e. USD 44.6 Bn, 41 per cent of aid to all developing countries, was mainly due to debt relief grants by DAC countries. 2007 saw a 10 per cent decline in revenue before growing at an average of 10 per cent over the period 2008 and 2009.

2.1. Trends of ODA in Africa by sector

Given the often low administrative capacity of recipient countries to effectively employ these inflows, the OECD's DAC members agreed in their "Paris Declaration on Aid Effectiveness"(PDAE) of 2005 to concentrate on strengthening partner countries' capacities and national development strategies (OECD 2006: 8). With this in mind, the focus has been to channel aid for social development, with increased focus on directing aid to sectors that would enable Africa achieve the MDGs by 2015. As a result, more aid has gone to the social sectors compared to other sectors as illustrated in Figure 2.

Figure 2: Trend of Aid Allocation to Africa by Sector (2005 – 2010)



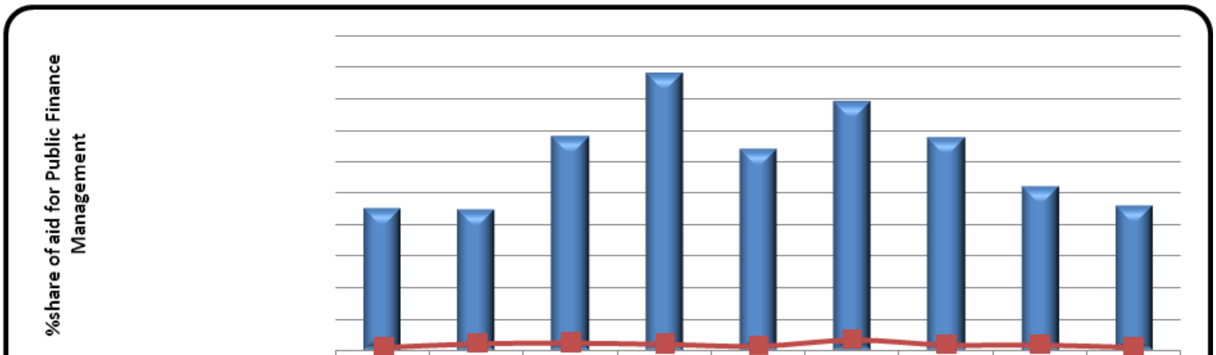
Source: www.oecd.org/dac/stats, data extracted on 11 May 2012 09:57 UTC (GMT) from OECD. Stat

Despite calls for aid to be allocated to more productive sectors by aid recipients, more of it continues to go to social sectors, whose share of aid to Africa has increased from 22.6% (USD 8.1 Bn) in 2005 to 38.8% (USD 22.43Bn) in 2010, as opposed to share of aid to production sectors that has gone up marginally from 3.2% to 9.3% over the same period of time. This does not augur well for increased productivity and self-sustainability in Africa which would form the basis for increased DRM. This confirms Paul Collier findings that aid has and continues to finance consumption rather than investment and foreign aid has continued to fund unproductive public consumption as opposed to promoting investment (Paul Collier, 2007).

2.2. How Aid has been used to boost Revenue Mobilization

Aid often includes components designed to increase revenue collection, such as direct funding for tax reform; conditionality that requires increased or at least constant, domestic revenue generation; requirements for local matching funds for aid projects; and/or demands for increased social spending which, indirectly, generate pressure for greater revenue mobilization. It has been observed that the proportion of aid allocated to Public Finance Management (PFM), public sector policy and administration to developing countries increased from 2.26% in 2002 to 4.40% in 2005; however since then it has taken a declining trend to 2.3% in 2010 as is illustrated in fig 3.

Figure 3: Share of Aid allocated to Public Finance management, public sector policy and administration management (2002 – 2010)



	2002	2003	2004	2005	2006	2007	2008	2009	2010
All Developing Countries	2.26%	2.23%	3.41%	4.40%	3.19%	3.95%	3.39%	2.61%	2.30%
Africa	0.05%	0.11%	0.12%	0.10%	0.07%	0.17%	0.09%	0.09%	0.05%

Source: OECD Aid Activity database at http://stats.oecd.org/qwids and authors calculations

Aid allocation to public financial management to Africa is much lower as illustrated in figure 3 , averaging 0.1 per cent between 2002 and 2010. Given that tax administration is a subset of aid allocated for public sector financial management, donors’ support to DRM is much lower than the 0.1 per cent recorded. Therefore, if development is to take off, this ratio will have to be dramatically increased.

3. IMPACT OF AID IN INCREASING DRM IN 5 SUB SAHARAN AFRICAN COUNTRIES

Tax administration reforms are of prime importance for strengthening fiscal state and governance relations in developing countries. African countries have been particularly deficient in this respect. Donor support for tax administration reform in Africa therefore might have a strong impact in enhancing the developing prospects of the continent. This section of the paper analyses the experiences gathered on donor support for tax administration reform in five African countries: Ghana, Tanzania, South Africa, Uganda and Zambia. Evidence gathered is backed by a study on donor support for tax administration reform in Africa commissioned by the German Development Institute (DIE) in 2008 focusing on areas that have received donor support and the resultant revenue growth. The case studies of Ghana, Tanzania and Zambia within the DIE study have been updated with more recent information. For the case of South Africa we study a country that has been able to carry out reforms without funding from donors. The aim is to draw lessons from the case studies' at different trajectories for future donor assistance that will impact positively on tax revenue and ultimately address poverty reduction in the respective economies.

3.1. Ghana

3.1.1. Foreign Aid and Tax reforms in Ghana

In 1986, the Ghanaian government launched the National Revenue Secretariat (NRS) in order to sustainably strengthen tax administration (Devas et al. 2001). The NRS was empowered with ministerial responsibilities and shared policy formulation with the Ministry of Finance (MOF). Two separate revenue authorities, the Internal Revenue Service (IRS) and the Customs, Excise and Preventive Service (CEPS), were placed under this holding structure. This gave them operational autonomy from the civil service (Osei 2000). The semi-autonomous revenue authorities in Ghana constitute the oldest donor-supported reform project of its kind on the African continent. However, in 1991 the two revenue authorities were again brought under the direct control of the MOF and the Chief Director (Technical) in the Ministry (Jenkins1994). In December 1998 that Ghana's parliament passed a law to create a Revenue Agencies Governing Board (RAGB) to replace the NRS and to increase the autonomy of revenue agencies, which numbered three: the IRS, the CEPS, and the VAT Service (VATS), created in 1998. The RAGB was to oversee the three agencies, which operated independently of each other. However in December 2009 the three tax agencies, CEPs, IRS, VATS and RAGB secretariat were merged in accordance with Ghana Revenue Authority ACT 2009 (GRA). GRA replaced revenue authorities in the administration of taxes and customs duties in the country and its formation was supported by the Public Finance Management which includes GTZ, financed by BMZ(Germany) and SECO (Switzerland).Ten million euro was committed by GTZ to the day to day implementation of GRA tax reforms

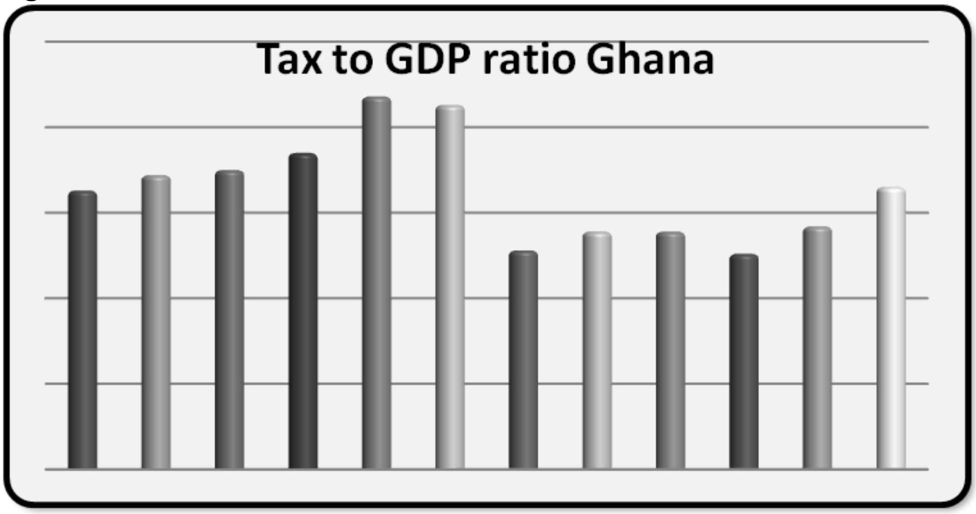
Tax administration reform in Ghana has been strongly supported at various stages by technical cooperation from donors. Prominent in this regard has been the introduction of the ASYCUDA programme for CEPS, which was supported by the United Nations Development Programme (UNDP) (Tettey 1997). The conceptual impetus for the introduction of VAT came in 1989 with a feasibility study conducted jointly by the Harvard Institute for International Development and Crown Agents of the United Kingdom (Osei

2000). Since 1992, DFID has supported the VATS in Ghana in two projects reflecting the two attempts to introduce VAT. The first, which provided 1.5 million £, was terminated after the repeal of VAT in June 1995. The second project was implemented from 1997 to 2000 (Gray et al. 2001c). In March 2004, GTZ established a new project, the Good Financial Governance Programme, to improve the efficiency and effectiveness of tax legislation and tax administration. Its tax component focused mainly on direct taxes and cooperates with the RAGB as well as the IRS (GTZ information).Since 2003; the country has been a pilot country for the Multi-Donor Budget Support Programmes (MDBS) project, which in Ghana is financed by ten different donors. The largest contributors are the World Bank (approx. 45 %) and DFID (approx. 25 %) (GTZ information). In 2006, the RAGB and the Tanzania Revenue Authority (TRA) signed an agreement to hand over the TRA's software (i.e. the Integrated Tax Administration System (ITAX)) to Ghana's tax administration (Ghanaian Chronicle 8.12.2006). The adaptation of ITAX to Ghana's needs was supported by GTZ. Donors have also had strong financial leverage in order to influence fiscal policies in general and tax administration reform more specifically with respect to VAT and involved in the annual revenue target setting process. In 2010 the GTZ under the Good Financial Governance program funded the renovation and refurbishment of the GRA headquarters to facilitate easy coordination of progamme activities. Registration and re registration of Ghana's taxpayers to facilitate the one stop service under the GRA using the Total Revenue Integrated Processing System (TRIPS) commenced in December 2011 under the Geogov project. Ongoing in 2011/12 is the transformation of the LTU to LTO and creation of MTOs and STOs. This is enhanced by the business process review being conducted with the help of Crown Agents UK in collaboration with GCNet.

3.1.2. Observed benefits due to tax reforms

Tax administration reforms resulted in initial increase of the tax-to-GDP ratio. Tax revenues rose from 5.6 % of GDP in 1983 to 17.0 % in 1994 (Chand / Moene 1999). It is difficult to directly attribute the rise of the tax-to-GDP ratio to any one single factor. In this case, however, improvements in tax administration seem to have made a significant contribution. Figure 4 further emphasizes the tax to GDP growth from 16.3% in 2000 to 21.3% in 2005. The rebasing of the GDP in 2010 collapsed the tax to GDP ratio; however there has been a remarkable growth of over 3% from 12.7% in 2010 to 15.9% in 2011 as is illustrated in figure 4. (www.gra.gov.gh)

Figure 4: Revenue Performance Indicators Ghana, 2000-2011



Source: World Bank data

One of the decisive reasons for increase in revenue performance was seen in the 2004 establishment of the Large Taxpayer Unit (LTU) which can be seen as a step towards integration. The LTU collects all tax types and duties from the 350 largest taxpayers of the country. Furthermore the IRS and VATS made the auditing of taxpayers and collection of information on tax liabilities more effective and accurate (Christian 2008). The performance in 2011 which was 46.6% over that of 2010 was attributed reforms such as integration and modernisation through information sharing between customs and domestic taxes; streamlined clearance on permits; introduction of Ghana integrated cargo clearance system to track location of goods at the ports and streamlined tax exemptions. Further to the tax revenue administration improvements was the commencement of oil production in Ghana.

The formation of GRA had a number of achievements such as; functionally integrated pilot DT offices; VAT flat rate scheme; LTO re-evaluation and implementation; establishment of a tax policy unit; capacity building and improvement in tax administration and tax policy among others.

3.1.3. Challenges experienced during the reform process

A GTZ-commissioned survey finding showed that though donor support had been instrumental in improving data collection efforts, there was a need to increase the number and competence of the personnel employed to collect taxes. In one region, Cape Coast, a DFID study found that although a target of 16 inspectors had been established for the region, only 5 were actually employed (Gray et al. 2001c). Tettey also found that support for the introduction of information technology at the CEPS yielded only mixed results as computers had not taken over all processes within the service, customs officers retained considerable personal discretion and ineffective procedures at the authority remained in place and were only “computerised”. No coherent reform of the whole organisation was carried out (Tettey 1997). The IRS had not yet been computerised by 2008 and had no proper databases of taxable persons, property or other possessions; making it very difficult to mobilize taxes from outside the registered, formal sector of the economy .

Regarding the VATS, a DFID-funded report found that although core employees had all undergone training, a shortage of supervisory staff persisted (Gray et al. 2001c).

Furthermore, due to staff vacancies, the outfield offices were operating with inadequate management. The VATS has found it difficult to recruit and retain highly qualified staff, mainly because it has not been given autonomy in setting and raising staff salaries (Gray et al. 2001c). This has limited the effectiveness of DFID's technical support to the VATS.

A report by the GRA Commissioner General (Sept 2011)highlighted challenges faced by its implementation such as; conditionality associated with DPs support causing delays in release of funds; stringent procurement rules causing delay in project implementation by partner nations; disagreements among DPs on which project to support resulting in inefficient harmonisation of projects and delays.

3.1.4. Summary: Tax Administration Reform in Ghana

The tax reforms in Ghana have been used in three broad areas (i) restoration of the tax base (ii) provision of better production incentives for investors and (iii) improvement of tax administration.

However, an initial attempt to provide the revenue authorities with more autonomy from the Ministry of Finance was reversed in 1991. In contrast to other countries on the African continent, in Ghana the three agencies IRS, CEPS and VATS remained autonomous entities under the supervision of the RAGB only until 2009 when GRA was formed to merge them. Further, donor support in Ghana concentrated for a long time exclusively on the tax administration and only addressed important capacities, like those of a Tax Policy Unit after the formation of GRA in 2009. With the GRA in place, despite the introduction of oil production in Ghana and the challenges faced, the tax revenue admin reforms seem to have a significant impact on revenue mobilization. GRA is now progressing with the redesign and improvement of business processes and procedures.

3.1.5. Main lessons to be learned from tax administration reform in Ghana

The Ghanaian experience offers important lessons on the effects of tax administration reform and donor support in this area.

- The revenue model where all revenue collection functions are under one body may be more effective than the separation of internal revenue service from Customs administration.
- The roles of the revenue authority, the Board and the Ministry must be clearly and formally outlined.
- Tax administration reform is a long-term exercise which requires a long term view on the part of donors.
- Explaining the prospective reforms of tax administration (and tax policy) and their implications to stakeholders inside and outside the tax administration is very important.
- Effective tax administration move hand in hand with adequate staffing.

3.2. South Africa

3.2.1. Foreign Aid and Tax reforms in South Africa

The South African Revenue Service Act of 1997 amalgamated the former Inland Revenue, and the Customs and Excise departments, resulting in the formation of South African Revenue Service (SARS). SARS's mandate is to collect and administer national taxes, duties and levies, as well as to protect and support the South African economy by facilitating trade and managing stakeholder relationships. SARS, being in the best position to judge the exchequer potential of the economy, also advises the Ministry of Finance in South Africa on tax reforms, widening tax base, tax simplifications and concessions.

In the period 1997 to 2000, SARS initiated a diagnostic study of its operations in order to identify issues, problems and recommend measures for resolving them. This exercise culminated in the development of a programme (2000-2001) "**Siyakha**" ('we are Building').

The Siyakha 1 key initiatives included; the development of a taxpayer and business strategy; process redesign in revenue and customs; overhauling taxpayer services; the implementation of policies to promote integrity and professionalism among staff (e.g. by re-advertising all new positions and through training, standardizing work methods, the creation of work teams, creating a professional management cadre etc.); and refurbishment and re-tooling initiatives to improve the working environment.

Successful implementation of Siyakha 1 resulted in : (1) Flatter organizational structure; (2) redesigned and standardized processes; (3) a dedicated taxpayer function was established; (4) the enforcement function was strengthened; and (5) staff were better trained and more motivated.

The Strong collaboration between SARS and the National Treasury has been instrumental to successes in revenue mobilization. These interventions coupled with a the urgency to deal with issues of poverty and inequality led to the launch of Reconstruction and Development Programme (RDP), whose goal was to mobilize revenue resources for development to meet these challenges.

The RDP was effectively replaced by the Growth Employment and Redistribution (GEAR) Strategy. GEAR set a vision and framework for growth from 1996 to 2001. Key medium-term interventions under GEAR included: accelerating fiscal reforms; firming up trade and industrial policy reforms; investing in infrastructure; further relaxing exchange controls; moderating wages and prices to enhance public service delivery e.t.c. Promoting the growth of small, medium and micro-enterprises was a key area of focus. Reforms in education, health and welfare, and housing were also high on the agenda.

3.2.2. Observed benefits due to tax reforms

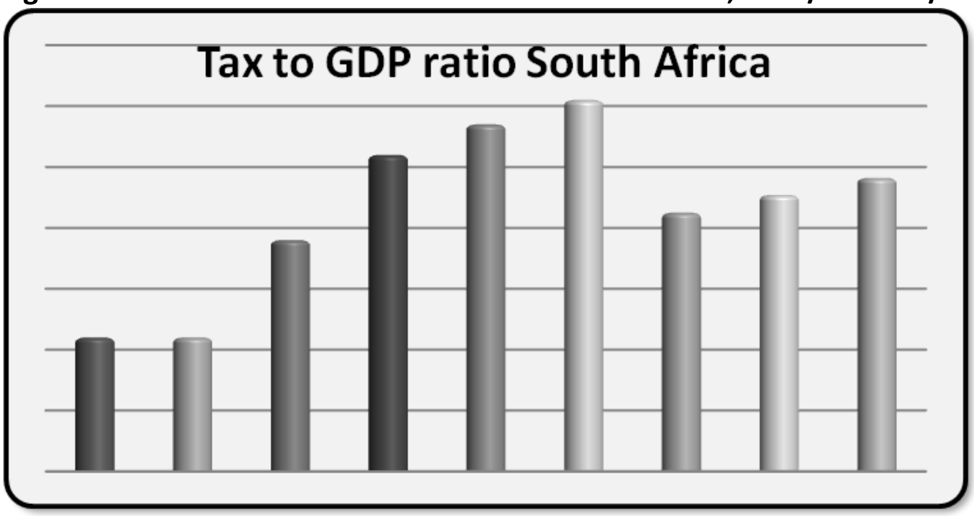
Implementation of these reforms by SARS has resulted in a rise of the national revenue as a percentage of GDP from 24.8% (2002/03) to 27.8% (2007/08) as illustrated in the figure 5. However for the years 2008/09 to 2009/10 the global recession affected tax revenues causing a decline in tax to GDP.

In 2007/08, SARS launched Siyakha 2. The thrust under this second wave of reform centered on the modernization of SARS over a five to seven year period, in particular, —transforming both the tax and customs administration through automation and other operational efficiency gains (SARS, 2008).

Siyakha 2 comprises ten programmes of modernization which are clustered around implementing a new operating model, implementing national priorities (i.e. protecting borders and implementing social security and a wage subsidy) and strengthening SARS's operational foundation.

At the end of Siyakha 2, SARS anticipates that it will be able to better: secure revenue; enhance compliance; secure and manage its borders; and maximize productivity as a result of operational effectiveness.

Figure 5: **Revenue Performance Indicators South Africa, 2002/03-2010/11**



Source: South Africa Revenue Services website

The above mentioned reform phases recorded tremendous success, from 2007 as is recorded the SARS's annual reports which have published actual achievements against targets. Initially other than working towards meeting revenue targets SARS focused on a number of key result areas (e.g. improving technology, tighter customs control, business process changes etc.). However, from 2001/02 it embarked on the development of a performance management system informed by the balanced scorecard approach (SARS, 2001).

In sum, the results suggest that the administrative reforms contributed to increased tax revenue due to one or more of the following factors: the simplification of systems and processes encouraging voluntary compliance; improved enforcement arrangements (e.g. with respect to risk based audits and debt collection); and quicker processing times (e.g. for tax returns).
With respect to these recent administrative reforms, it is also noteworthy that e-Filing contributed to a dramatic reduction in the time taken to process income tax returns in 2006/07 and 2007/08 the percentage of tax returns processed within 48 hours was 1.6% and 34% respectively. In 2006/07 and 2007/08 the number of registered taxpayers

(particularly CIT payers) grew by 17% and 12% respectively. So did SARS‘s success in risk based audits – 68% (2006/07) and 73% (2007/08) of cases yielded additional revenue.

3.2.3. Challenges experienced during the reform process

SARS is respected by many revenue administrations in Africa and beyond. It is particularly strong because of its ability as an organization to be introspective, reflective, plan next steps and take action. As SARS charts its way to becoming a world class services provider, it grapples with a few key medium to long-term challenges and issues.

DRM efforts must be stepped up to finance national development strategies particularly with respect to job creation, the provision of services in education and health, rural development, and combating corruption and crime (National Treasury, 2009).

It has also been noted that a different approach for dealing with taxpayer segments is needed through restructuring to build on existing infrastructure. It is important to bear in mind the different risks associated with each segment (e.g. keeping practitioners honest and ensuring that any exceptions arising with respect to small businesses are dealt with at contact).

SARS must continue to widen its tax base for the foreseeable future. In addition to the above, SARS is challenged to bring into the tax net both new taxpayers evolving as a result of economic growth, and actors operating in the informal economy.

SARS's staff capacity must keep abreast with its transformation; SARS is aware that whilst it has made great strides in enhancing staff capacity, more needs to be done to strengthen skills. The leadership management training initiative needs to be rolled out across the organization.

The increased cases of crime and corruption need to be kept in check; SARS reports an increase in syndicated crime, particularly in the areas of fraud and corruption. It is also alleged that corrupt officers employed by the Companies and Intellectual Property Registration Office may have been part of a syndicate which registered non-existent companies with the intention of defrauding SARS of VAT revenue.

There are challenges around regional trade integration; There is on-going dialogue around expanding this customs union arrangement to the 14 SADC (South) countries which are all signatories to a free trade agreement. However, there are issues around rules of origin, leading to a lot of paperwork. South Africa is challenged to lead in addressing these issues.

3.2.4. Summary: Tax Administration Reform in South African

On the basic parameter of tax revenue to GDP ratio, the tax system in South Africa has consistently improved performance since the onset of the reforms that followed the end of the apartheid era (see Figure 5). The wide breadth and depth of policy, institutional and administrative changes were informed by the analytical, policy and strategic development work of the Katz Commission, which existed parallel to both the mainstream government policy organs and tax administration systems for a period of five years, 1994-1999.

Impressive and sustained improvements in the efficiency and effectiveness of SARS since its establishment, has of course been crucial to achieving the overall high rate of growth in tax revenue (an annual average rate of about 13.3% in the 1995-2008 period). SARS has been particularly successful in building and applying systems and capacity for enforcements as well as encouraging compliance. In more recent years, aggressive and smart utilization of ICT applications has been the bedrock of the reforms.

Despite the fact that South Africa is not a recipient of any significant assistance by any bilateral government and that it has consistently resisted the influence of International development organizations in its macro-economic and fiscal affairs, the recent global financial crisis adversely affected government‘s ability to mobilize domestic resources from taxes. Government has indicated that it will borrow resources as a short-term measure while the economy recovers, and as tax revenue collections rise.

3.2.5. Main lessons to be learned from tax administration reform in South Africa

- The strong collaboration between SARS and the National Treasury has been instrumental to revenue mobilization.
- Solid policy formulation and evaluation capacity is also key to strong revenue performance.
- Compacts with professional and industry groups can reinforce compliance and facilitate administrative efficiency and effectiveness.
- Minimizing the level of exemptions ensures tax policies remain neutral.
- Modernizing through the use of ICT can result in significant operational efficiencies but must be applied judiciously
- Good client service is critical for promoting voluntary compliance
- A policy of zero tolerance to corruption is an important deterrent

3.3. Tanzania

3.3.1. Foreign Aid and Tax reforms in Tanzania

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

The TRA has been supported by a comprehensive reform project called the Tax Administration Project (TAP) and predominantly run by the World Bank. This became operational in 1999 and USD 73 million was pledged altogether, with contributions coming from the World Bank, a variety of bilateral donors and from the Tanzanian government (BMZ 2003). The donor community has been heavily committed to providing information technology to the TRA, in contrast to other revenue authorities. In 2004, an IMF report noted the need to strengthen the post-clearance verification and audit unit of the Customs Department through the recruitment of additional auditors by January 2005 (IMF 2004). The doubling of staff in this section of customs was a structural benchmark set by the IMF for the end of March in 2006 (IMF 2006b, 10).Among the IMF's structural performance criteria have been; the formulation of a new Income Tax Act, a revision of the VAT threshold to reduce the number of VAT taxpayers, and a revision of the threshold for the presumptive tax (IMF 2004). The IMF has also exerted pressure to curtail tax exemptions.

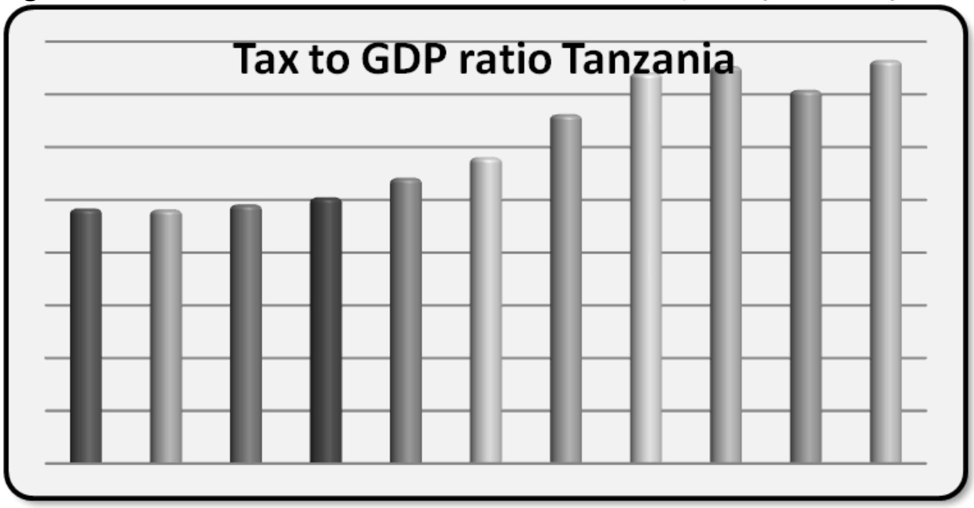
The donor funding in TRA has facilitated a number of reforms mainly aimed at increase in revenue administration efficiency through automation such as; Oil production monitoring and exemption system introduced in 2008 to track and monitor the use of exemptions; Data warehouse and TRA ISO Certification in 2009; upgrade of ASYCUDA++ to include ASYSCAN to manage customs transactions and improve services in 2009; Replacement of the Electronic cash registers with electronic fiscal device system that was more efficient in monitoring the VAT taxpayers; Introduction of the biometrics function in the TIN registration system in 2011 to eliminate duplicate registrations; and Interface of the ITAX system with ASYCUDA , CMVRS and mobile money agents in 2011 . The IFC/World Bank is currently helping the TRA to reengineer the Vat, Income tax and PAYE processes under the project "Tanzania Tax Administration Simplification project"

3.3.2. Observed benefits due to tax reforms

Tax policy reforms during the last decade in Tanzania have succeeded in widening the tax base. Overall, however, they have provided better support for tax collection than the policies of the previous regime.

The increase in the tax-to-GDP ratio has been the major performance indicator used by the government and the donor community, which expected tax revenues to grow by 1 % overall until 2002 and by more than 2 % up to 2004 (Fjeldstad et al. 2003). Key contributory factors have been strong economic growth and a substantial increase in imports. The IMF also found that these developments have recently been "underpinned by ongoing tax administration reforms" (IMF 2006).

Figure 6: Revenue Performance Indicators Tanzania, 2000/01–2010/11



Source : Tanzania Revenue Authority Databases

3.3.3. Challenges experienced during the reform process

Although donor support has played an important role in the reform of Tanzania's tax administration, improvements have been offset on the other hand by a narrow tax base partly attributed to limited capacity to tax and administer the informal sector, the granting of exemptions, and corruption levels within the TRA. This has significantly reduced revenue performance.

According to one donor report, there exist 14 different software systems which can hardly be linked to each other. This diversity has produced three different systems of TINs which are unrelated to each other (IMF 2006). Hence, donors exacerbate problems of internal cohesion and exchange of information. This has been inherently detrimental to a coherent auditing process.

In spite of considerable donor support, it has not been possible to fence off the tax administration from its corrupt environment.

The DIE study noted that while various donors had taken centre stage in reforming the tax administration in Tanzania, the Tax Administration Project (TAP) could also be seen as a prime example for inadequate donor coordination. Multilateral and bilateral donor agencies such as the World Bank, USAID, GTZ, DFID and the EU have been engaged in different parts of the reform project, with the result that representatives from the donor community and advisors to the TRA complain of a lack of clear focus and coordination in the TAP.

The project was managed for a long time from the World Bank's headquarters in Washington, DC rather than from a local office. This slowed down implementation of the reform programme (Fjeldstad et al. 2003). In addition, the TRA itself failed to employ a responsible project manager for the TAP (BMZ 2003). The donors have been a decisive factor in the annual revenue-target setting process between the TRA and the Tanzanian MOF.

The other reform related challenges as mentioned by the TRA in the 2011 annual report were ; the inability of the tax system to keep pace with the technology speed of sector like the telecom, tourism and services; the infrastructure problems such as power failures impacting on productivity; unclear segmentation of taxpayers according to complexity of their businesses; and unsatisfactory utilization of the available ICT i.e. e-filing, EFD, TRAMED etc for decision making.

3.3.4. Summary: Tax Administration Reform in Tanzania

The DIE study noted that political support for the new, semi-autonomous TRA has proven to be inadequate, as, the political will to reduce the many exemptions provided by tax policies has been lacking. Technical assistance in TRA was largely contra productive. The multiplicity of active donors in the TAP undermined a coherent reform effort. For instance, the introduction of information technology and TIN was not coordinated. For a long time the donor community sent mixed signals and inhibited strengthening the TRA as a single, integrated authority. Since the TAP was managed from the World Bank's headquarters in Washington, DC rather than from a local office, it was also largely detached from local conditions. It is difficult to determine the respective importance of these factors for the rather disappointing results of tax administration reform in Tanzania. However, there are at least some signs for a more consistent donor approach towards technical assistance in the future. There is also evidence that the technical assistance is addressing issues that arose from the inconsistent coordination such as the TIN registration using biometrics and the efforts to integrate the ITAX with other electronic systems in TRA in 2011.

3.3.5. Main lessons to be learned from tax administration reform in Tanzania

• Tax administration reform can increase revenue performance only if tax exemptions are reduced to a minimum.

• Donor support must be coherently organized among the different donors involved and must be context-sensitive.

• Political support for tax administration reform needs to be strengthened and institutionalized

3.4. Uganda

3.4.1. Foreign Aid and tax reform in Uganda

The Uganda Revenue Authority (URA) was established in 1991 under the Ministry of Finance, Planning and Economic Development (MoFPED) as an agency for the assessment and collection of specified tax revenue, to administer and enforce the laws relating to such revenue and to account for all the revenue to which those laws apply. Between 1991 and 1996, the agency was substantially organized along functional lines where over 200 ineffective and corrupt staff were removed and a Ghanaian was selected to lead the agency in an effort to disrupt patronage networks. Salaries were increased by an average of 250%, which aided in the recruitment of highly skilled staff. Revenue collection increased spectacularly, from 7% of GDP in 1991 to 12.3% in 1996. These dramatic gains suddenly ceased after 1996 with widespread accusations of proliferated corruption and thus led to the ultimate reforms of 2004.
In 2006, the URA developed a Modernization Plan (2006-2010) to improve revenue collections by the URA to enable the government of Uganda to achieve and sustain the targets set out in its Poverty Action Eradication Plan (PEAP). The Modernization Plan was aimed at adopting modern, efficient and effective processes and systems to collect tax and customs revenues and achieve a high level of voluntary compliance from taxpayers.

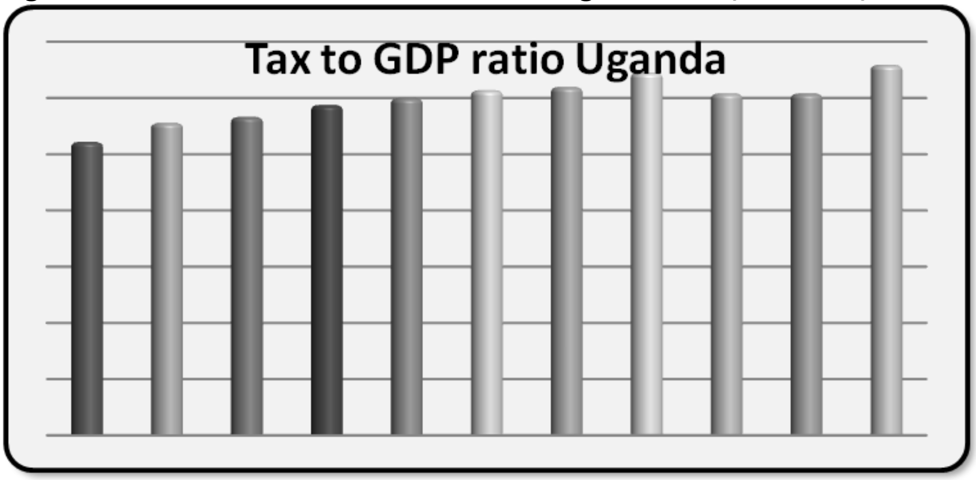
The successful implementation of the Modernization Plan was supported by the Netherlands, the UK, DFID, World Bank, IMF, Japan, and China, CIDA, Denmark and the government of Uganda under an integrated technical co-operation and basket funding framework for an approximated amount of USD 15 million. The program was governed by the URA management and staff with the help of both foreign and local consultants, to allow URA to better focus management effort and resources on targeted priorities, implementation of reforms and results achieved. The proposed arrangements, which are in line with the Paris Declaration on Aid Effectiveness (2005), were also aimed at supporting the government of Uganda in progressing towards budget support, which is its preferred development assistance modality. During this period a number of reforms were executed such as; Unified Communication Infrastructure (URA Net) for both Voice and Data from 29 points in 2004 to a WAN linking 62 operational points by 2010; Electronic Tax Administration Platform for Domestic Taxes (E-Tax) aimed at efficiency gains; Revenue Authorities Digital Data Exchange (RADDEx) a regional system aimed at streamlining the cumbersome customs procedures and facilitate information sharing across the region; Introduction of a new strategy management methodology , the balanced score card to enhance a client focused workforce; Integrity enhancement ; Capacity building; and reengineering of processes.

Subsequently a new reform programme known as Managing Compliance Programme (MCP) has been developed in line with the URA Corporate Strategic Plan 2011/12 – 2014/15. In this regard the URA intends to consolidate the gains and maintain the pace of change in its drive towards corporate excellence over the period from 2011/2012 to 2014/2015. This program is also supported by DPs and it is expected that with the MCP URA will provide the required revenue to finance the National Development Plan.

3.4.2. Observed benefits due to tax reforms

These interventions coupled with a relatively stable macroeconomic environment have resulted in growth in revenue with Net URA collections growing at a five year average of 17% as compared to 15% in the period prior to the reforms. Conversely, Tax revenue for government expenditure has been steadily increasing from 52.06% at the time of the most recent reform save for the financial years 2008/09 and 2010/10 due to the effects of the global financial crisis to 67.7% in 2010/11. The tax to GDP ratio that averaged at 12.2% in 2007/08 and 2009/10 increased to 13.2% in 2010/11.

Figure7: Revenue Performance Indicators Uganda 2000/01- 2010/11



Source: Uganda Revenue Authority Databases

The prevailing tax reform agenda in Uganda has also recorded success in the areas of Information technology upgrading where it has been a part of virtually all reform programmes. The aim is to improve data management and analysis; lower compliance costs reduce the scope for corruption and collusion and improve monitoring. The integrated tax system "*eTax*" currently in use at URA has shown great potential in increasing the compliance levels of taxpayers coupled with a sustained improvement in audits. This has been attributed to the notable successes recorded during the integration with old processes and the well planned implementation phase. Taxpayer services have also shown great prominence geared towards improving taxpayer education and awareness, reducing compliance costs and adopting a "customer" orientation. Through this, a tax payer charter has been drafted to address and create awareness for taxpayers in regards to their tax obligations and rights. Since 2003/04, URA has been able to bring down the cost of collecting tax from 3.38% to 2.26% in the financial year 2010/11. This reduction demonstrates another benefit of the restructuring, reengineering and automation initiatives.

Aside from general improvements in capacity, re organization, autonomy, and information technology and taxpayer services other elements have characterized the reform agenda in Uganda tax system especially in areas of Agriculture, Health and Education. Many tax legislations within these sectors have been enacted inform of exemptions especially in the agricultural sector because Uganda is predominantly an agrarian state. Through the Income Tax Act and VAT, a number of provisions relating to these sectors have been exempted from payment of taxes. Other challenges notwithstanding, Uganda has posted impressive figures as regards the progress of the MDGs.

3.4.3. Challenges experienced during the reform process

Despite the considerable efforts that have gone into modernizing the tax system in URA, with a view to realizing its vision, major challenges are still evidenced and will thus need to be addressed for this vision to be realized and sustained.

The proliferation of tax incentives and exemptions in the Ugandan tax system is posing a big challenge due to the conflict between the politics and economics of the day. According to the African Development Bank report of 2010, tax revenue as a percentage of GDP could easily go up to 16%, if, some of the revenue negating measures, particularly incentives and exemptions were removed. The elimination of non-value adding incentives and exemptions will however, demand the resolve and commitment of Uganda's political leadership.

Uganda also experiences the stringent procurement rules that delay project implementation and the MCP is facing conditionality associated with the DPs support causing delay in release of funds.

Building a sustainable management capacity in URA is also another impediment in that specialized skills of personnel and institutional knowledge are lost each time such staff depart from the organization. This is related to the issue of remuneration, which has not been adjusted for senior staff and personnel in professional and technical positions since 2004/05. As a result, it is argued that URA has been unable to retain specialized skills in areas such as ICT and audit among others. Therefore most of the reform initiatives supported by development partners face a huge bottleneck of sustainability.

Weak and poorly coordinated controls over the rules of origin continue to pose major problems for the URA in the East African Community (EAC) member states.

3.4.4. Summary

It can therefore be conclusively summarized that there is no single 'package' that fits the requirements of any individual country. The government of Uganda through the URA must take the lead and define the needs for tax reform. The URA will have a prominent role by providing analysis and data to the domestic policymakers, and to implementing tax policy. Strong engagement on tax issues by domestic civil society organizations, including business and taxpayer associations, is essential to enhance the legitimacy and accountability of the tax system. Addressing the gaps identified will also require long-term commitment by the international community. This is so because, it takes time to build institutions and change peoples' behavior, whether they are policymakers, tax officers or ordinary citizenry.

3.4.5. Lessons learned from the tax reform process

Uganda has come a long way in reforming her tax systems. A number of good things have been reported, in particular with respect to simplification of the tax system, procedures, and improved tax administration at the central government level. Some of the lessons learnt are ;

- Basket funding arrangement play a major role in successful donor coordination of donor supported reform.
- Even with strong donor support, semi autonomous revenue authorities cannot be fenced off against political intervention without government support.
- Most of the reform initiatives supported by development partners face sustainability challenges if the human resource skills development is not addressed.

3.5. Zambia

3.5.1. Foreign Aid and tax reform in Zambia

On 1 April 1994, the government of Zambia launched the Zambia Revenue Authority (ZRA), a semi- autonomous agency, and transferred revenue collection from the traditional public administration under direct control of the MOF to this new entity. This strengthening of Zambia's tax administration was also a donor requirement: at the beginning of the 1990s, the IMF made the strengthening of internal revenue collection one of its conditions for the provision of new loans (Hill 2004). Up to 2004, the British DFID as the main bilateral donor had provided technical assistance worth 15.8 million £ through its ZRA project. The rationale for this was to finance technical equipment such as computers, to provide expertise through short-term advisors, and to support staff training (Hoover / McPherson 2004). Since 2000, the DFID has also supported the Tax Policy Unit within Zambia's Ministry of Finance and National Planning and has assisted local NGOs to build knowledge on taxation issues.

With substantial technical donor support, the ASYCUDA was established in early 2000 and later upgraded to its current version ASYCUDA++. Computerized systems are also in place for processing VAT. In 2004 ZRA introduced the "Integrated Tax Administration System" (ITAS) computer programme, which merged the old VAT software with the database of the Taxes Division. The acquisition of software was financed to a large degree by DFID. Nevertheless, IT-experts from the ZRA itself were also engaged in customizing this information technology to match the authority's needs.

None of the four most senior managers in 1995 was Zambian. It was thought that expatriate leadership would be less responsive to local corruption networks and to interventions from the political arena (Gray / Chapman 2001)

The IMF's Fiscal Affairs Department began providing technical assistance to Zambia's government as early as 1991, "mostly in tax administration, and expenditure management control" (Muzondo et al. 2001, 11). The British government started its support for Zambia's tax administration in 1992 with the funding of initial studies which in turn recommended establishment of the semi-autonomous revenue authority (Coopers and Lybrand 1992). Up to September 2004, the manager of DFID's Revenue Institutions in Zambia Enhanced Support (RIZES) project had his office within the revenue authority's headquarters. ZRA together with COMESA introduced the simplified tax regime to facilitate clearance of low valued goods and reduce taxpayer costs. In 2010 refocused on taxpayer orientation rather than tax type and with the help of the Royal Norwegian Government, built capacity in the auditing of mining, tourism and finance sectors.

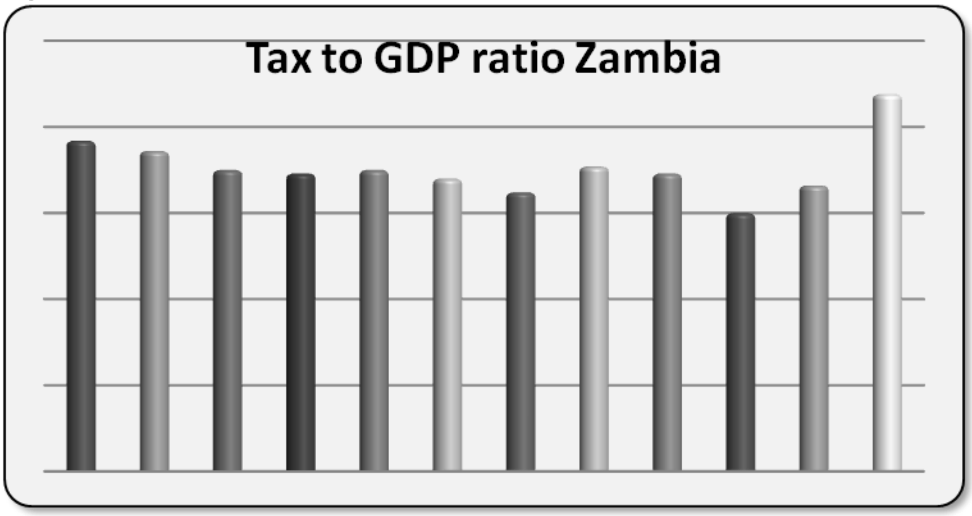
The ZRA has partnered with the ICF to undertake acquisition and implementation of new tax administration system in the ICF – ZRA project. Phase 1 of project commenced in 2011 with the installation of call centers, training customs services and launch of the wide area communication campaign.

3.5.2. Observed benefits due to tax reforms

It appears that the tax administration reform project has brought significant progress in establishing taxpayer liabilities. The computerization of Zambia's tax administration has been one of the focal areas for donor support. In conjunction with training programmes for tax officers, the drive to improve the collection and processing of taxpayer data has largely

been successful. Through consistent training, the project has built up technical expertise within the ZRA to use the information technology which has been installed.
Many of the ZRA's high-ranking officers today hold a degree from the Britain-based Association of Chartered Certified Accountants (ACCA). The authority's basic orientation was established by managers from outside the country; this was financed by the DFID.
This close collaboration of ZRA and the donors has served to avert instances of political intervention in the revenue authority's operations pointing to the crucial importance of donor influence in pressing for the revenue authority's freedom to operate along rational-legal lines and for the preservation of its special status.
Indicators show that the ZRA initially improved important aspects of revenue performance (the tax-to-GDP ratio went up from 15.3 to 18.7 % in the ZRA's first year of operation (World Bank 2003), but that in the following years the tax-to-GDP ratio remained largely stagnant. As a DFID-funded study stated, it has been a success just "to maintain the revenue/GDP ratio, despite the poor macroeconomic situation" (Gray et al. 2001a). However in 2011 the tax to GDP ratio recorded its highest at 21.9%

Figure 8: Revenue Performance Indicators Zambia, 2000–2011



Source: Zambia Revenue Authority Website and World Bank Indicators

3.5.3. Challenges experienced during reform process

According to a DFID-commissioned study, the revenue authority's impact on direct tax incidence has remained "modest" (Gloppen / Rakner 2002). Revenue collection has largely been confined to formalized economic activity. As a result, Zambia's tax gap, i.e. the difference between tax potential and taxes actually collected, remains large.
Despite the reforms in tax administration ZRA is still facing a few challenges such as dilapidated physical infrastructure, malfunctioning of the ICT systems , reduced inspection and enforcement effort, tax evasion and revenue leakages (ZRA annual report 2010).

3.5.4. Summary: Tax Administration Reform in Zambia

The ZRA has been closely donor-monitored and dependent on support from the political sphere. The Zambian government has sustained the ZRA's independent position. However, it is still possible to satisfy political demands through tax exemptions and – most

importantly – through state expenditures. Since most Zambians work in the informal sector, they have rarely been forced to pay direct taxes.
Some features stand out with respect to the role of donors in supporting Zambia's comparatively successful tax administration reform: first, technical support was predominantly rendered by one bilateral donor, the DFID. Accordingly, there was no evidence of competing external interests, as for example in Tanzania. Secondly, technical assistance was provided to ZRA was for over eleven years with DFID support formally ending March 2005.Third, the DFID assisted other important stakeholders, such as the Ministry of Finance (albeit less successfully) and civil society organizations in order to strengthen their ability to engage in tax (administration) issues. Fourth, the project was successful in training local staff and local managers. Of particular importance in this regard was the expatriate management team, which was accepted within both the government and the revenue authority.
According to the DIE study, the ZRA has increasingly lost its special, donor-supported status. As a consequence of the DFID's exit in 2005 and the complete takeover of a Zambian management team, external actors have had declining leverage in the effort to create a tax administration which operates along rational-legal lines. Political support for the revenue authority in Zambia currently depends on the government and the respective President and is not strongly institutionalized.

3.5.5. Main lessons to be learned from tax administration reform in Zambia

• A low number of donors involved in technical assistance and a high degree of coherence are crucial for successful tax administration reform.
• Technical assistance must pursue a long-term and comprehensive approach and must also incorporate the Ministry of Finance and civil society.
• Even when foreign managers are employed, strong political support is the most crucial variable in determining the success of donor-supported tax administration reform.

3.6. Recommendations on effectiveness of aid in increasing tax revenues in Sub Saharan Africa

Tax administration reform has been of crucial relevance in the SSA countries. It has the potential to reap major fiscal benefits for these heavily-aid dependent countries and might also induce a substantial governance dividend through increased domestic tax collection. . Overall, donor support has not yet been successful in supporting the improvement of tax administration capability on a sustainable basis. Accordingly, revenue performance in Ghana, Tanzania, Uganda and Zambia has been mixed: In each case, a phase of strong initial increases was followed by stagnation or decrease. This is not only to be correlated with negative socio-economic development and tax policy changes but must also be attributed to problems in the revenue authorities, such as increasing corruption, loss of qualified staff, inadequate integration of the different departments, and, political intervention in some cases. On the other hand South Africa's experience shows that where political and revenue raising authorities have a common interest in enhanced collection, their collaboration is an important source of effectiveness. This analysis with the support of recommendations from the DIE study provides crucial lessons for different elements of donor-supported tax administration reform in Africa. On this basis, recommendations for making future donor assistance more effective in this area are made.

(1) Collection and Processing of Taxpayer Data

Technical assistance generally promotes a more active auditing approach and frequently includes the provision of hardware and software needed to process tax information. Nevertheless, the collection of information has been almost exclusively confined to the formal, registered sectors of the economies under study. Technical assistance has been instrumental in turning Africa's formerly passive tax administrations into revenue authorities which actively audit taxpayers and collect taxpayer information. On the other hand, the large informal sector in African countries often remains outside the tax net, since the "return on investment" for revenue authorities which operate in line with business principles is generally low. In this context active collection of taxpayer information is necessary in order to reduce tax evasion in hard-to-tax environments. Donors should therefore increasingly support taxpayer associations and similar organs of civil society in order to provide a better check of revenue authorities' auditing efforts. Better training is also needed to improve the service orientation of tax officials in reformed tax administration.

(2) Integration of departments is of key importance for the exchange of information

Donor-supported measures have included steps to computerize the Income Tax Departments, automate customs procedures, commonly by introducing ASYCUDA ("Automated System for Customs Data") and integrate domestic tax systems in order to record revenues and to track receipts. However, the processing of data has often stagnated. In contrast to the donor objective of supporting coherent revenue authority structures, these authorities have generally not acted as integrated organizations in terms of exchanging information between different departments (for example in Ghana). Since there are often no properly maintained databases of taxable persons, property or other possessions, it is very difficult to mobilize taxes from outside the registered, formal sector of the economy. While donor support has led to a better utilization of taxpayer data within revenue authorities, the use of outside sources such as registration of company data has often been wanting. The IMF strongly advocates for the establishment of LTUs as a "good practice" for increasing revenue performance and it has been observed that these LTUs often raise more than 70 % of all tax revenues these countries. Therefore, supporting the integration of tax departments is of key importance for greater efficiency in the collection and utilization of taxpayer information. Donors should therefore consider supporting the most important databases such as designing linkages with the registries of companies. It is not enough to be in one umbrella but integrate. Even for the integrated departments there is urgent need to integrate the processes and systems there in (case of eTax in Uganda)

(3) Technical donor support requires coherence

Various donors have provided technical assistance to newly-established revenue authorities on the African continent. Often these efforts were rather uncoordinated. In some cases, different information technologies and TINs were used. In these instances, donors have thus exacerbated the lack of coherence between different tax departments. The existence of different information systems has also precluded systematic auditing processes across different tax types. In successful reform projects, technical support was predominantly rendered by one bilateral donor[4]. This serves to prevent a plethora of often competing external interests. From the outset, therefore, donors should pursue a proactive approach of coordinated technical support to tax administration reform. It however observed that the basket funding approach has been successful in Uganda's modernization of tax processes. It is however advised that in the absence of a basket funding approach, a strong program management office (PMO) be established as a coordinating approach with the donors. The PMO should include sections that address; change management& communication; risk, finance, quality and procurement management aspects.

(4) Human Resource Management

Merit orientation of human resource management has emerged as a particularly important variable which determines the success of reforms. Remuneration schemes, corruption levels and expatriate management are crucial factors in this regard in the sense that high remuneration schemes have often been impossible to maintain. In many African countries, the conditions of employment of tax officers had severely deteriorated before the establishment of revenue authorities. In the initial stages following donor advice, remuneration levels and other employment conditions of newly-established revenue authorities were highly favorable and served to attract well-qualified professionals. However these nominal wages in many cases have been eroded by significant inflation. In consequence, reformed tax administrations have often found it difficult to recruit and retain highly qualified staff as they continually keep losing them to international accounting firms and other private sector companies. This has reduced the effectiveness of technical support rendered to revenue authorities. Revenue authorities have not per se been a remedy against deteriorating employment conditions coupled with the limited opportunities for donors to provide support in this regard. The recipient countries need to stress to partner

[4] For Uganda under the first modernization program, all the donor funds were channeled through DFID which culminated into a successful implementation of the project.

governments the importance of attracting and retaining qualified tax officers as a means of improving state revenue. Maintaining favorable employment conditions is fundamental in this regard. There is also need to support capacity building in support of public resource mobilization. Ensuring that skills development is undertaken as a national priority so as to improve quality of labour needed for the growth of the industrial and services sectors and thus formalisation of the economy.

(5) Corruption

Corruption poses a major threat to human resource management. One of the biggest impediments to merit orientation of human resource management in the African revenue authorities analyzed here has been the resurgence of considerable corruption. Some revenue entities, such as the URA through donor advice pursued a more radical (and effective) approach where all former tax officers were dismissed and had to re-apply for the new authority. SARS reports a syndicate between corrupt officers employed by companies and intellectual property registration office intention to defraud SARS of VAT revenue. In some cases, more than a third of the former staff was rejected because of prior misconduct. Despite donor-supported staff training, computerization, and this tough stance, however, bribery and corruption have again become pronounced after an initial period. Donors should provide expertise on how to detect corruption within tax administrations. Internal investigative units should be explicitly supported. Hiring expatriate personnel for these units, potentially from other African countries, might also be a viable option. The fact remains, however, that a revenue authority principally struggles to keep internal corruption at low levels when such a project is not flanked by government wide activities to eradicate corruption, i.e. attempts to create a more favorable environment.

(6) Support of the Research function in SSA revenue authorities

Development assistance based on the generic policy of "one size fits all" without recourse to the peculiar circumstances in the recipient country. Sometimes development assistance is out of sync with the cultural settings of the beneficiary country. There is need to recognize and accept the fact that commitments need to be interpreted in the light of the specific situation.

Application of "best practices" principles that overlook individual country structures and systems is problematic. Best practice may not be appropriate in some cases therefore the risks of making investments that are not demand driven.

Further, besides best practices it is critical to make strategic investment in research in order to develop effective risk solutions to donor support. In SSA understanding risk management is less developed yet the consequences can't be ignored. Effective research in aid effectiveness must also be intensified and effectively coordinated across donor partner landscape. This would require a strong and sustainable collaboration among research institutes.

(7) Change management

Outsourcing the collection of taxes from the core state structure constitutes a major change. Experience has demonstrated that there is often considerable initial resistance to this institutional shift among civil servants and powerful economic actors who profit from a weak tax administration because tax officers regularly perceive the newly created authority as a threat to their positions. The outsourcing of tax administrations has often been inadequately communicated and explained to tax officers and the general public. Often, the dire financial situation in partner countries has been the trigger for radical, donor-supported tax administration reform. Such situations make it easier to overcome resistance. Nevertheless, interest in such reforms has often waned after this initial impulse. Communicating the effects of prospective reforms to the relevant constituencies such as tax officers, taxpayers and governments is of prime importance for ensuring the success of donor-supported tax administration reform. It is recommended that before starting assistance, donors should; a) identify important stakeholders and vested interests which might oppose reform and; b) develop a strategy of how to communicate the prospective changes and advantages of reform in cooperation with partner countries. There must be a clear and well defined path regarding tax administration reform.

(8) Ensure tax administration reforms are accompanied by enabling legislation

Administrative reforms can only work if they are accompanied by enabling legislation. For example a tax reform demanding that taxpayers file returns using internet shall need legislation allowing electronic returns in the tax laws. Sometimes there may be a need for policy changes which entail the lowering of rates, reducing the number of taxes, and, in particular, scrapping tax exemptions. South Africa has qualified that revenue source is collected very efficiently with minimal exemptions. Nevertheless, despite substantial tax administration and tax policy reform on the African continent, tax exemptions have not been reduced as expected. This indicates that in spite of strengthened tax administration, political interests continue to be served by the tax structure. The scope of reform must therefore go beyond mere support for the core administration. The prominent, stand-alone position of revenue authorities also makes them vulnerable for being singled out for policy failures. In some countries, such as Zambia, business persons acknowledge the professionalism of staff members. In other countries, the revenue authority is rated the most difficult agency businesses have to deal with. It is important that donors find a common answer to challenges on the political level and send a coherent message. On the other hand, partner governments' concern to protect their political interests can be valid. Donors should therefore support mechanisms of restraint such as revenue tribunals in order to limit over-aggressive enforcement tactics applied by the revenue authorities.

(9) Relationship with Multilateral and Bilateral Donors

Donors have played a strong role in providing technical assistance to newly-created revenue authorities in Africa and have also exerted pressure to uphold the integrity and capability of the new entities. Nevertheless, they may also have induced unintended consequences by pressing for increased revenue performance, often measured through the tax to-GDP ratio. Donor involvement is important for strengthening capability and upholding autonomy. On the political level, donors have tried to strengthen domestic support for tax administration reform and to counter instances of political interference with the revenue authorities' operations. In doing so, an attempt has been made to fill the gap of either nonexistent or weak internal interest groups pressuring for an efficient and accountable tax administration. Donors must not be the driving force in tax administration reform. Before starting to provide support, they should analyse whether the partner government has expressed a need for it. The initiation of tax administration reform may also merely reflect donor conditionality. Indicators of this are the lack of reform efforts in other areas of public administration, the maintenance of complicated tax laws, the continuance of various exemptions, and a start-stop approach to beginning reform. Only if the political will exists can donors play an important role in strengthening capabilities and supporting autonomy.

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

Donors (in particular the IMF) play a domineering role in setting revenue targets for revenue authorities. In the process, the IMF often makes use of its financial leverage as the most important provider of loans and determines targets for domestic revenue generation. This influence was particularly strong in the run-up to the HIPC Initiative completion point. From a governance perspective, targets sometimes create wrong incentives. A strong focus on the tax-to-GDP ratio may sideline other measures such as widening the tax base. An exclusive focus on tax share induces revenue authorities to concentrate on large taxpayers as advocated for by the IMF. In this respect it is noteworthy that donors have not promoted “Small Taxpayer Units”. Finally, the external setting of revenue targets can run counter to partner countries’ ownership of tax administration reform. Donors should be aware that they are setting incentives for tax administration in highly aid-dependent countries. Domination of annual target-setting negotiations by external actors is counter-productive. Donors should at least broaden the scope of indicators for success (beyond the tax-to-GDP ratio). Furthermore, bilateral donors providing technical assistance to revenue authorities should find a common position with the IMF on how to appropriately measure success in the partner countries.

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

Tax administration reform is a long-term exercise. In many African countries, revenue authorities had to be built up from scratch. Staff had to be trained, information technology had to be provided, and completely new organizational structures had to be created. In response, donors have often pursued a long-term approach to technical support. Assistance was sometimes provided for more than ten years. In Zambia, for instance, the British government started its support in 1992 with the funding of initial studies which in turn recommended establishment of the semi-autonomous Zambia Revenue Authority (ZRA). This long-term horizon for tax administration reform stands in contrast to other areas of technical assistance and must be viewed positively. The sustainability of technical donor assistance remains a fundamental issue. Whereas management is viewed as a “buffer zone” against interference from the political level, local managers who are not being funded by donors are potentially subject to much stronger influence and also experience demonstrates that political support for tax administration reform, even if strong at the outset, tends to wane. Therefore, pursuing a long-term approach towards tax administration reform in unfavorable environments is an adequate donor strategy. However, donors need from the outset to prepare for their own exit. This entails; a) building up a merit orientation of staff and managers as this will ensure sustainability of the reforms within tax administration as well as; b) institutionalizing political support for reformed tax administration, e.g. by collaborating with civil society and ministries

Other recommendations for donors to address sectors directly impacting on revenue generation

- Encourage public private partnerships and private sector involvement in development of policy regulation frameworks through development and enforcement of efficiency quality standards; contracting private sector to deliver services; Improving the capacity of the local financial institutions to support services.
- Support value addition to raw materials especially in the minerals and agriculture sectors. Refinery of oil and gas will create jobs, increase tax base and lead to early eradication of poverty. Processing food crops ensures food security, while commercialising the agricultural sector and increasing the tax base.
- Support activities in the main economic growth drivers; energy, infrastructure, human capital and access to credit.
- Support creation of African financial and goods markets this will boost local savings as well as attract more investment to the continent.
- Formation of regional trading blocs for wider markets. This addresses trade capacity constraints, promotes trade, reduces cost of trading, promotes export diversification and improves Africa’s trade competitiveness. (Stephen N & Vincent L 2009). Trade oriented commodity driven economies such as Zambia, Kenya and Uganda should look at boosting trade with China.
- Reduction of economic inefficiencies such as maximization of services from available quantity of system inputs; cost minimizing production techniques; appropriate allocation of resources; capital investment decisions and choice of interventions should be based on cost effectiveness and cost benefit analysis criteria.

4. EMERGING TRENDS IN THE GLOBAL CONTEXT THAT ARE LIKELY TO HAVE AN IMPACT ON NATIONAL TAX SYSTEMS

4.1. Globalization of the economy

As a result of globalization, the impact of borders is declining due to the establishment of Multi-National Enterprises (MNEs). Creation of MNEs and investment in Africa has come with challenges of transfer pricing and thin capitalization for several African countries. Improper transfer pricing has been identified as an international problem that affects developed and developing nations alike. The main beneficiaries instead, are assumed to be tax havens and the multinationals. One way in which multinational enterprises may try to benefit from their international presence is misuse of transfer pricing, *e.g.* by artificially shifting taxable profits from high tax jurisdictions to low tax jurisdictions. Kar and Cartwright-Smith (2008), estimate that total trade mis-pricing in 2006 was more than USD 500 Bn while Hollingshead (2010) reckons that the amount of tax revenue lost by developing countries to transfer pricing averaged between USD 98 Bn and USD 106 Bn annually from 2002 to 2006. In Africa, it is estimated that a yearly average of USD 3.8 Bn would have been lost between 2002 and 2006. Therefore this trend is negatively affecting revenue collection and efforts are in place to improve the capacity of African tax administrators to address this issue.

4.2. Integration of the world Economies and declining share of world trade from LDCs

The resulting integration of the world economy has raised living standards around the world. Most developing countries have shared in this prosperity; in some, incomes have risen dramatically. Moreover, trade between developing countries has grown rapidly, with 40 percent of their exports now going to other developing countries. However, the progress of integration has been uneven in recent decades. Progress has been very impressive for a number of developing countries in Asia and, to a lesser extent, in Latin America because they chose to participate in global trade, helping them to attract the bulk of FDI in developing countries. But progress has been less rapid for many other countries, particularly in Africa and the Middle East. The poorest countries have seen their share of world trade decline substantially, and without lowering their own barriers to trade, they risk further marginalization. This has been attributed to dependence on production and exports of traditional commodities, structural problems, weak policy frameworks and institutions, and protection at home and abroad.

4.3. Internationalization of the global financial sector

Emerging markets have experienced an extensive internationalization of their financial sector in recent years: gross capital flows have surged and cross-border entry has become more common, with foreign banks holding market shares of more than 50% in many emerging markets. The large foreign presence in banking and capital markets – both foreigners operating in the local market cross-border financial services provision, and local institutions using off-shore markets poses a greater challenge to emerging markets and developing countries as avenues for capital flight. Already most developing countries have challenges managing and taxing the financial sector, which has been exacerbated by the emergence of multinational banks operating in their economies. Therefore this will have a negative impact on the tax base if policies are not developed to address this challenge. MNEs may take advantage of the different tax regimes, including tax havens to maximize after-tax profits and shift them abroad though these banks.

4.4. Increased dependence on mineral sources

The African Economic Outlook (AEO) 2010 reports that vast extractable natural resources – oil, gas and minerals – are already an essential revenue source for many African nations. African export revenues, which had fallen to some 51 percent of their pre-crisis August 2008 levels by January 2009, had almost recovered by November 2010(UNCTAD, 2011). Much of the increase was due to the surge in commodity prices. In volume terms, the World Bank reports that exports increased by a moderate 7.5 percent in 2010. However, even though the prices of the principal merchandise exports of many oil importing Sub- Saharan countries improved in 2010, they still suffered deterioration in their terms of trade. The African Development Bank's 2007 *African Development Report* highlighted the widely held belief that African countries get less money from resources than many other countries in the world. *Keen and Mansour* 2007 report that there is evidence that African countries are not maximizing the tax revenue they obtain for the resources which may easily result in the "resource curse", This is due to the fact that several African countries have not developed the capacity to manage their mineral resources locally and thus continue to have low value exports.

4.5. Supply constraints and fluctuations in commodity prices

Driven by the expansion of global demand, commodity prices continued to increase in 2010, and in first months of 2011 some prices reached a new historical peak. The price of gold has continued its steep rise during 2010 and into 2011, driven mainly by global demand while other metal prices have similarly recovered from their trough in early 2009. Export prices for agricultural products have further increased especially cotton, coffee and cocoa. On the other hand, import prices of basic foodstuffs have increased sharply in the course of 2010. Since the African continent is a net food importer, the sharp increase in food prices will increase the import bill which will negatively affect the trade balance. Further to this, production of agricultural commodities is mainly dependent on the weather patterns, which make commercialization very difficult. Attempts to mechanize and commercialize agriculture in LDCs have been very slow and going forward, supply shortages will continue to exist. Therefore the journey to a commercial agricultural sector may be longer than expected, further shrinking the tax base for African countries.

4.6. Explosive growth of the IT tools

These tools include the internet and ecommerce. Ecommerce has had significant effect on the way we do business internationally. Business transactions may be faster and more global and as a result the nature of global service chain and global trade as managed by multinationals has fundamentally changed. However on the other hand the more depth issue is examined some things won't change and could even become more local as a result of the globalization that the internet and economy bestow on us.

4.7. Declining Foreign Direct Investment

In 2008, due to the financial crisis and the global economic downturn, outward foreign direct investment (OFDI) flows from developed countries fell by almost 17% from US$1.8 trillion in 2007 to US$1.5 trillion. Although intra-African investment is growing in importance, it does not yet make up the majority of foreign investment flows originating in Africa. Between 2000 and 2009, 63% of all African FDI outflows were invested in OECD countries (AEO, 2011). In 2009 this ratio was 56% of a total of USD 5 Bn outward FDI (Combining data from UNCTAD, 2010a and OECD) On the one hand, this investment can play a critical role in bringing expertise to the continent through acquisitions in more advanced economies and investment of incomes in developing economies leading to increased economic activity. This large share of African investment going to OECD countries instead of other African countries presents an untapped revenue potential, which if re-invested locally would create more avenues for DRM.

4.8. Other trends

Asian and Latin America financial crisis; emergence of the BRICs (Brazil, Russia, India and China); Global Financial Crisis caused by the US subprime mortgage loan crisis since late 2008 ravaging integrity of global economy with unpredictability severity.

5. CHALLENGES IN SUB SAHARAN AFRICAN COUNTRIES DESPITE THE AID AND INCREASED DRM

African countries are facing a series of challenges when it comes to optimizing DRM through taxation while aiming to reach development targets. Perhaps the most inherently difficult challenge is how to find the optimal balance between a tax regime that is business and investment friendly, while at the same time leveraging enough revenue for public service delivery (which, in turn, makes economies more attractive to investors). It's on this note that African Policy makers are challenged by the need to balance the following imperatives[5]:

5.1. Narrow tax base

A tax system concerned to facilitate growth should both reduce the cost of operating in the formal sector[6]and increase the cost of operating in the informal sector. African countries do face a challenge of mobilizing domestic resources and broadening the tax base to secure steady revenue streams for development financing and to diversify revenue sources especially in the context of tariff liberalization that impacts strongly on tax revenue. The ratio of tax to GDP in developing countries is only about half of what it is in the developed world. Developing countries typically have a narrow tax base, with a relatively small part of the population subject to personal income tax[7]. In Ghana and Uganda for example, 20% of tax payers contribute 80% of direct tax revenue and the remaining 80% contribute only 20%.This is because SSA countries are faced with the reality of a large share in agriculture and employment in total output mainly in the informal sector. Tax reform needs to be promoted to widen the tax base and bring a larger part of the population into the formal economy.

5.2. Weak Administrative systems and organizational capacities

There are weak administrative systems, scarce and poor quality data as a result of widespread informal activities. Limited reporting and low levels of education in the general population and seemingly a general culture of non compliance which accounts for the low DRM. There is a challenge of organizational capacity and resourcing where staff of most tax administrations in Africa lack the requisite capacity to perform efficiently. Communication capacity is limited and the resource to purchase machinery and equipment necessary to facilitate work is also often not available which makes it difficult to create an efficient tax administration. This is often worsened in some developing countries that have tax administrations that suffer from corruption, poorly-trained and underpaid officials and a weak administrative structure. There is need for effective taxation systems to reduce excessive reliance on aid (for example the trend taken by Uganda in modernising the tax administration system) and mineral rents in countries like Nigeria, Botswana, Congo etc to offer a path away from unsustainable revenue streams.

[5]Taxation for investment and development ; an overview of policy challenges in Africa

[6]World Bank publication *Paying Taxes 2008* in which India rests near the bottom (165 out of 178 countries considered) compared to, say, Singapore which ranks second in the world with respect to the costs to formal business of complying with the tax system.

[7]**TAXATION FOR INVESTMENT AND DEVELOPMENT: An overview of policy challenges in Africa**

5.3. Capital flight

Capital flight remains one of the profound impactful stumbling blocks to DRM. Tax flights from developing countries are estimated to be several times higher than aggregate inflows from development assistance. Capital flight severely weakens DRM in Africa. It undermines social contracts and damages good governance. In the context of Africa the (UNCTAD) estimated in 2007 that capital flight caused considerable damage because African investments world- wide were worth 400billion USD which was double the entire African debt worth 215billionUSD. These outflows are estimated at 7.6% of the annual GDP of the region and, in effect, make African countries net creditors of donor countries[8]. They also undermine African countries' tax bases. These are funds that could otherwise have been used to fund development priorities in the African economies.

5.4. Tax Incentives and Exemptions

Experience shows that a high occurrence of tax exemptions reduces the tax base, creates room for bribery and corruption, and increases the appearance of loopholes for tax evasion. Hence, the extent of tax exemptions can be seen as an indication of a government's political will to fight fiscal corruption and tax evasion (Fjeldstad and Heggstad, 2011). It has also been observed that tax incentives distort resource allocation leading to some sub-optimal investment decisions and therefore harmful to long term growth. For example often than not, many multinationals enjoy foreign tax credit at home and giving them tax incentives may have minimal impact on their profit which in effect allows the developed home country to be the final beneficiary of the tax break. Most often, start- up companies make losses for several years and do not benefit from tax exemptions. It is however the firms that make profit from the start that benefit from tax exemptions and these would have invested anyway. Typical example is the housing industry in Ghana. In Kenya there are 11 export promotion and investment related incentives targeted at enhancing investment and export growth and employment creation, although these have led to revenue losses.

5.5. Low Savings

Another important feature affecting revenue mobilization in Africa is that the region's savings ratio is low relative to investment requirements. In African countries savings rates are low and do not compare with those of Asia. The gross domestic saving in SSA amounted to17.6% of GDP in 2006 compared to 26% in South Asia and about 43% in East Asia and Pacific countries (World Bank, 2007). This represents a serious constraint to growth thus low revenue mobilization. Studies have shown that countries with high growth performance tend to have high saving ratios (Rodrik, 2000). This is further compounded by very low levels of financial intermediation and credit on the continent and the fact that over 40% of African savings are invested outside Africa. Consequently, one of the key challenges of African governments is how to increase domestic savings and channel them into socially productive investments.

5.6. 5.7 Challenges associated with globalization of private sector

These include transfer pricing and thin capitalization which contributes greatly in reducing the revenue base of most African countries. Improper transfer pricing is an international

[8] Pretoria Communique, http://www.oecd.org/dataoecd/1/33/41227692.pdf

problem that affects developed and developing countries alike. MNEs operating in African countries might take advantage through different tax regimes, including tax havens, under-invoice or over-invoice for goods and services, and financial transactions to maximize after-tax profit at the expense of the host country. With the administrative capacity constraints and the considerable amounts of tax revenue at stake, a pragmatic approach is needed that is adapted to the administrative and institutional means available to governments.

6. CONCLUSION

A number of factors influence revenue mobilization in developing countries. On the positive side, the global economy continues to recover from the financial crisis, especially the emerging economies that play an increasingly important role in Africa. In combination with rising commodity prices, this economic recovery makes for a favorable scenario for resource-exporting countries that can expect increasing FDI flows. As investors, especially from emerging partners, become more comfortable with the overall African business environment, the global upswing will also likely increase investment in developing economies.

The most effective way of increasing public revenue for developing countries is through policies that increase the tax-base through sustained economic growth. Efficient tax collection also strengthens public resource mobilization without over-taxing the economy. Developing countries need to devise strategies of managing the trends in the economy while developed countries need to uphold commitments made at various fora on helping developing countries end the dependence on aid and actively participate in world economy.

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