

FIGHTING FISCAL CORRUPTION: LESSONS FROM THE TANZANIA REVENUE AUTHORITY

ODD-HELGE FJELDSTAD*

Chr. Michelsen Institute, Bergen, Norway

SUMMARY

Over the last decade, several African countries have undertaken comprehensive reforms of their tax administrations to increase revenue and curb corruption. This article examines recent experiences in the fight against corruption in the Tanzania Revenue Authority (TRA). Two lessons of broader relevance are highlighted. Firstly, even with relatively high wages and good working conditions, corruption may continue to thrive. In a situation where there is high demand for corrupt services, it is unrealistic to provide tax officers with pay rates that can compensate for the amount gained through bribery. Without extensive and effective monitoring, wage increases may produce not only a highly paid, but also a highly corrupt tax administration. Secondly, hiring and firing procedures may lead to more corruption. Corrupt tax officers often operate in networks, which also include external actors. These corruption networks seem to have been strengthened because many of those fired were recruited to the private sector as 'tax experts'. This partly explains why the positive process experienced in the initial phase of the new revenue authority was later reversed. Copyright © 2003 John Wiley & Sons, Ltd.

INTRODUCTION

Tax systems in most poor countries are characterised by widespread corruption and tax evasion. Substantial amounts never reach the treasury (Kiser and Baker, 1994; Ul Hague and Sahay, 1996; Ghura, 1998). This erosion of the tax base has several detrimental fiscal effects. The consequences of lost revenue to the funding of public services are of special concern (Tanzi, 2000a). In addition, corruption and tax evasion may have harmful effects on economic efficiency in general (Chand and Moene, 1999; Tanzi, 2000b) and income distribution in particular (Slemrod and Bakija, 1998; Hindriks *et al.*, 1999).

In order to increase revenue and curb corruption, a number of African countries have implemented comprehensive reforms in their tax administrations over the past 10–15 years (Devas *et al.*, 2001). Tanzania introduced a major reform in 1996 with the formation of a semi-autonomous revenue authority—the Tanzania Revenue Authority (TRA). The choice of a revenue authority model aimed partly to limit direct political interference by the Ministry of Finance and partly to free the tax administration from the constraints of the civil service system. This was considered to be essential for several reasons of which the most important were to attract and retain quality staff by paying rates above the civil service regulations, and to make dismissals easier. Moreover, the tax administration's senior management and many tax officers were replaced. It was assumed that these steps would provide incentives for greater job motivation and less corruption.

How successful was this reform? It is obviously too early to pronounce a final verdict, only 7 years after the Authority was put in place. Reforms need time and results always depend on the criteria underlying the evaluation. The reform appeared, however, to be a success in TRA's first year of existence. Reported revenue increased sharply—from 11% of GDP in 1995–1996 to more than 12% in 1996–1997. Corruption seemed to be declining too.

*Correspondence to: O.-H. Fjeldstad, Chr. Michelsen Institute, PO Box 6033, PT, N-5892 Bergen, Norway. E-mail: odd.fjeldstad@cmi.no
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Table 1a. Tanzania tax revenue components (in TSh billions, nominal prices)

	1994	1995	1996	1997	1998	1999	2000
Total tax revenues	220.4	299.9	385.8	514.6	566.1	616.5	685.1
Tax on imports	50.2	91.3	121.2	174.2	180.7	218.9	220.4
Tax on exports					4.7		
Sales and excise tax on domestic goods	70.4	72.6	104.7	141.7	140.5	161.3	180
Income taxes	58.5	86.7	112.3	134.2	149.8	162.9	209.7
Other taxes	41.2	49.4	45.6	64.5	90.4	73.4	75.1

Table 1b. Annual changes in tax revenues (%)

	1994–1995	1995–1996	1996–1997	1997–1998	1998–1999	1999–2000
Total tax revenues	36.1	28.6	33.4	10.0	8.9	11.1
Tax on imports	81.9	32.8	43.7	3.7	21.1	0.7
Tax on exports					–100.0	
Sales and excise tax on domestic goods	3.1	44.2	35.3	–0.9	14.8	11.6
Income taxes	48.2	29.5	19.5	11.6	8.7	28.7
Other taxes	19.9	–7.7	41.5	40.2	–18.8	2.3

Table 1c. Tax revenues (% of GDP)

	1994	1995	1996	1997	1998	1999	2000
Total tax revenues	11	11.3	11.4	12.1	10.9	10.1	10
Tax on imports	2.5	3.4	3.6	4.1	3.5	3.6	3.2
Tax on exports	0	0	0	0	0.1	0	0
Sales and excise tax on domestic goods	3.5	2.7	3.1	3.3	2.7	2.6	2.6
Income taxes	2.9	3.3	3.3	3.2	2.9	2.7	3.1
Other taxes	2	1.9	1.3	1.5	1.7	1.2	1.1

Source: Mokoro and Oxford Policy Management (2001).

But since then, tax revenue has declined to 10% of GDP in 2000 (see Table 1c). There are also clear indications that corruption is on the rise again. The key facts of the development in Tanzania's tax administration are as follows:

- *Prior to the establishment of TRA*: Widespread and systemic corruption. Low tax revenues in percentage of GDP (Table 1c).
- *Establishment of TRA*: Focus on wage incentives, control, recruitment and steps to reduce political interference.
- *Post-reform phase 1*: Low(er) corruption levels. Sharp annual growth in tax revenue (Tables 1b and 1c).
- *Post-reform phase 2*: Rising corruption levels. Declining revenue in percentage of GDP (Table 1c).

The purpose of this article is to explore in greater detail, factors that may explain this pattern of corruption within TRA and, to a lesser extent, to shed light on revenue trends.¹ Rising levels of corruption may help explain why the growth in revenue has tailed off in recent years (see Table 1c).² But there are clearly other explanatory factors also at work. First, tax revenue depends on external factors over which the tax administration has no control, for instance, impact of general economic trends on tax bases such as income tax, VAT and import duties. Import restrictions and politically allocated tax exemptions for different sectors and businesses also contribute

¹This pattern, initial increases in revenue collection followed by stagnation or decline, is not atypical for tax administrative reforms in Africa as the experiences from Ghana and Uganda show (see Chand and Moene, 1999; Hadler, 2000; Therkildsen, 2002). According to Taliario (2001), similar developments are observed in several Latin-American countries.

²One should be careful in drawing too confident a conclusion about successes and failures on the basis of the tax-to-GDP ratio since it tends anyway to be a relatively imprecise measure of performance (see Stotsky and Wolde Mariam, 1997). However, increase in revenues has been the major performance criterion publicly announced by the Government, clearly reflected in the budget speeches of the Minister of Finance.

to reducing the tax base.³ Furthermore, staff productivity may have changed possibly due to falling motivation caused by, for instance, declining real wages. However, there are many indications that an increase in fiscal corruption has contributed to reducing the growth in reported revenues. Thus, a closer look at the pattern of corruption may shed light on the development of tax revenues.

Reliable information on corruption and tax evasion levels is obviously hard to come by. Given the sensitive issues at stake, one cannot work towards an understanding of the phenomena discussed in this article by the standard methods of random sample, structured questionnaires and formal interviews.⁴ A combination of informal and formal methods is often required. This analysis is therefore based on a variety of sources of information collected during a series of fieldwork between 1996 and 2002: official reports and data on tax revenues and the TRA; available grey literature produced by the Government, the TRA itself, donors and business communities; personal interviews and discussions with present and past TRA staff and board members, staff at the Ministry of Finance, business people and customs clearing agents in Dar es Salaam, aid workers, tax consultants and researchers; and newspaper articles on Tanzania tax issues.

The remaining part of the article is divided into five sections. The first Section describes the state of affairs in the tax administration in Tanzania prior to the establishment of TRA. Factors identified as crucial in explaining the extent and types of corruption in the tax administration are reviewed in section two. The administrative reforms are discussed in section three, while their results are presented in section four. Finally, section five concludes and examines lessons learned from this case study which could benefit future reforms of tax administrations in poor countries.

CONDITIONS PRIOR TO THE ESTABLISHMENT OF TRA

Corruption is not a new phenomenon in Tanzania. According to Mukandala (1983, p. 261), the public sector in the early 1980s was 'increasingly riddled by corruption and embezzlement of public funds'. The Auditor General's reports from the 1980s show that this trend continued (Semboja and Therkildsen, 1992, p. 1103). By the mid-1990s, corruption in Tanzania was rampant in all sectors of the economy and politics (URT, 1996a). In tax administration, these issues were particularly worrying given the need to raise more tax revenues, but also to mitigate corruption in other parts of public services.

Extensive corruption and embezzlement of public funds are documented in a number of reports from both commercial and official sources. For instance, the Confederation of Tanzanian Industries (CTI) estimated that the value of lost revenues from customs and sales tax due to inefficient tax administration and misclassification and undervaluation of imported goods amounted to more than TSh 250 billion for the period March 1993–March 1994 (Osoro *et al.*, 1999, p. 5). According to ESRF (1996, p. 6), official import statistics underreported the value of imports by as much as 70%. One indication of the extent of this problem is that some types of textiles (including those used in the most popular type of clothing, the 'khanga') were sold in the early 1990s for 30% less than the value of the customs duty per metre of the textile. Official statistics on reported revenue from customs duties also indicate large leakages. While the most commonly applicable import duty rate was 30% during 1988–1994, the customs tariff generated a revenue equivalent to less than 6% of the official import value during that period (Gandhi *et al.*, 1995, p. 15).

Evasion of other types of taxes was also widespread. For sales tax and excises on domestic goods, underreporting of production volumes was a common form of evasion (Osoro *et al.*, 1999, p. 6). With regard to corporate taxes, underreporting of profits and falsified tax deduction claims were common (Mwinyimvua, 1996). In both cases, such underreporting could be achieved with or without the help of staff within the tax administration. For personal income taxes, including pay-as-you-earn (PAYE), one method used by employers to evade taxes was not to report

³There has been a considerable increase in the use of tax exemptions in Tanzania in recent years, which obviously erodes the tax base, at least in the short run. For instance, generous investment incentives in the form of tax exemptions have been granted to foreign investors, especially in the mining and tourism sectors (Mokoro and Oxford Policy Management, 2001).

⁴Wade (1982) provides an excellent account of methodological challenges and approaches for analysing systems of corruption in public sector institutions.

taxes collected from employees to the tax authorities. Another was to pay wages and other cash emoluments to workers 'under the table'. But the discrepancies between potential and reported tax revenue could also be due to plain and simple theft. For instance, TCCIA (1995, pp. 22–23) reported that embezzlement of collected taxes by tax collectors and administrators—which did not implicate taxpayers—was widespread. It was caused by poor control routines in the tax administration. In some cases, the tax inspectors and auditors were also involved in corruption.

Evidence of the amount of taxes and duties lost to the treasury was extensive. Surprisingly, the donor community did not react until Autumn 1994. A report from two of the Pre-Shipment Inspection (PSI) companies in charge of the pre-imports inspection and valuation of cargos to Tanzania then revealed that lost tax revenues in the form of unpaid customs duties amounted to TSh 70 billion (then equivalent to US\$ 134.5 million) in the fiscal year 1993–1994 (*The Indian Ocean Newsletter*, No. 647, 19 November 1994, p. 1). In comparison, recorded customs revenues in that same year were TSh 28.4 billion (Gandhi *et al.*, 1995, p. 10). In other words, lost customs revenues represented an amount 2.5 times higher than reported customs duties. This revelation led to an aid freeze to Tanzania in November 1994. Several major donors, including Norway and Sweden, decided to withhold aid while they awaited the results of investigations of what was assumed to be corruption involving senior officials. The Government promised a full-scale investigation into the matter.

On 23 February 1995, the Office of the Controller and Auditor General submitted its report to the President. The report exposed negligence and dishonest practices by high-level civil servants (*The Indian Ocean Newsletter*, No. 661, 4 March 1995, p. 1). Of the total amount of TSh 70 billion that could not be accounted for, TSh 20 billion could be put down to tax evasion by importers, while TSh 50 billion was due to tax exemptions. Of the latter, legal exemptions granted to public institutions and religious and humanitarian organisations made up a substantial share, but a large number of cases were found to be illegitimate exemptions granted to various businesses by the Ministry of Finance.

According to Osoro *et al.* (1999, p. 28), 'the third schedule of the Customs Tariff Act and a number of Government notices which allow for exemptions [was] probably the most abused section of tax legislation'. Within the Ministry of Finance, the *Revenue Department* went under the nickname the 'Tax Exemption Department'. In response to pressure from Western donors, the Minister of Finance Kighoma Malima was removed from his post in the spring of 1995 and installed in a new ministerial position. In June that year, he was forced to resign from the Government altogether. The investigations also led to the dismissal of several senior civil servants in the Ministry of Finance, including the head of the revenue department.

FACTORS LEADING TO PERVASIVE CORRUPTION

The corruption scandals in the tax administration were instrumental in President Benjamin Mkapa's decision to establish a *Commission on the Causes of Corruption in Tanzania*. The commission was appointed in January 1996 with a mandate to map the extent of corruption in the country and identify steps to deal with it (URT, 1996a, pp. i–iii).

Investigations identified four factors as keys to explaining the extent and types of corruption pervasive in the Tanzanian tax administration:

- *Political intervention*. This generally took place in the form of discretionary tax exemptions granted to business people who were willing to pay and/or had the 'right connections' (URT, 1996a, pp. 307–311).
- *High tax rates and complicated regulations*. The potential gain from involvement in corruption could be considerable, both for officials and taxpayers. Relatively high rates and a complex and partly incoherent set of rules, especially for customs and corporate taxes, resulted in large potential rewards for taxpayers willing to bribe to cut their own tax burden and/or speed up customs clearance of their goods (URT, 1996a, pp. 291–295, 316–329). For customs officials, the bribes taken for clearing specific containers in Dar es Salaam harbour could be as much as a whole year's salary. In general, the system gave tax officials considerable discretionary powers.
- *Poor pay and working conditions*. The low wage levels at the tax administration compared to the private sector invited corruption. The average public employee's salary including allowances in the early 1990s was sufficient

to cover only about 40% of normal household expenditures (Mans, 1994, p. 378). Moreover, working conditions were characterised generally by a lack of technical equipment and poor office facilities, as well as unclear criteria for recruitment, promotion and rewards (URT, 1996a, pp. 100–117, 281).

- *Low probability of detection and punishment for corruption.* Internal auditing and monitoring functions had become for the most part non-operative and ineffective (Cunningham, 1996; URT, 1996a, p. 50). For instance, the internal operational auditing unit in the Customs Department at the head office in Dar es Salaam had only four staff members in early 1996 and five persons for the whole Dar es Salaam region, where about 80% of the total customs revenues in Tanzania are collected. Responsibility for internal auditing was therefore outsourced to external auditors from the Office of the Controller and Auditor General, which stationed on a permanent basis six–seven people at the customs administration. But this compromised, of course, their independence and opened up for collusion between auditors and tax officers. According to Cunningham (1996, p. 66), these auditors were ‘part of the system and the peer network to be inspected’. Audits were further crippled by low skills. The auditing staff lacked the training in auditing and inspection methods, and the required equipment and basic facilities to perform controls. In practice, the probability of being detected and punished for corruption was virtually non-existent.

THE FOUNDING OF TRA

The crisis riddling the tax administration was the immediate cause behind the formation of the Tanzania Revenue Authority (TRA). TRA became operational from 1 July 1996. Its objective was to reach a given revenue target, expressed as a given ratio of tax revenue to GDP. This target would be revised annually in the Finance Minister’s budget speech.⁵ *The Indian Ocean Newsletter* (No. 726, 6 July 1996, p. 1) wrote on this occasion that ‘a beginning has been made in tackling the country’s two major ills: corruption and tax evasion’.

A key element of the administrative reform was to move the existing revenue departments out of the Ministry of Finance into a semi-autonomous revenue authority.⁶ The philosophy behind this move was twofold: first to eliminate the direct political influence of the Ministry of Finance on the day-to-day operations of the tax administration. And second, to raise the salary of tax officials without parallel increases for the rest of the public sector. A revenue authority, established outside the civil service system, is not, in principle, bound by wage rates and employment regulations that apply to other sectors of government (see Devas *et al.*, 2001, p. 214). This means that the institution can pay rates which enables it to attract and retain highly qualified staff. In TRA, this involved dramatic increases in pay rates—for some categories of staff up to ten times higher than corresponding positions in the civil service. Further emphasis was laid on strengthening accounting and internal monitoring systems and curtailing the opportunity of tax officers to deal with cases on the basis of their own discretion. The general scarcity of qualified accountants, lawyers and IT-experts in Tanzania meant, however, that these groups at TRA would be equally sparse. Finally, steps were taken to improve working conditions for employees by improving offices, expanding computer services, purchasing service vehicles etc.

To ensure a sense of ‘local ownership’ to the reforms, efforts were made to fill board and executive management positions with Tanzanians. Persons recognised for their integrity and past good performance were appointed as Chairman of the Board and as Commissioner General. The rest of the executive management was generally recruited from outside the system, most from jobs in government-owned enterprises. Exceptions were the Commissioner for Tax Investigation and the Commissioner for Customs, who were both already employed in the tax administration.

⁵Revenue targets are set on the basis of negotiations between the TRA and the Ministry of Finance (URT, 1998, p. 5). Moreover, the Research and Policy Department of the TRA plays the policy role of setting collection targets for TRA revenue departments, once the total tax revenue budget has been agreed with the Ministry (Mokoro and Oxford Policy Management, 2001, p. 18). This arrangement indicates a strengthening of the tax bureaucracy at the expense of politicians. Caulfield (2002) provides an interesting analysis on how recent public sector reforms in Tanzania may have strengthened the hand of bureaucrats such that, without enhanced mechanisms of accountability and political control, the potential for rent-seeking is high.

⁶The main functions of the TRA, its organisational structure, composition of the board, etc. are detailed in URT (1995, 1998); and TRA (1999). See also www.tra.go.tz

Table 2. TRA staff dismissed for misdemeanours

	1995–1996	1996–1997	1997–1998	1998–1999	2000–2001
Staff at start of fiscal year	3365	2201	1962	1927	1897
Dismissed	1164	239	35	30	24
Percentage dismissed	35	11	1.8	1.6	1.3

Source: World Bank (2001, p. 28).

Drastic measures were put in place to break the ‘culture of corruption’ in the administration. All former staff members were dismissed and had to re-apply for a position at the new TRA. More than a third (35%) were rejected on evidence or suspicion of misconduct (see Table 2). Almost 1200 earlier staff members, of whom 500 were former customs officers, were not re-employed. All new employees were given a 1-year probation period before being accepted on a permanent basis. Staff had to report their private financial circumstances, including wealth, on starting. Furthermore, a new unit was set up for internal investigation and monitoring. The first board of TRA, chaired by Professor Benno Ndulo (1996–1998), played an essential role here by virtue of its autonomy, integrity and expertise. The accountability relationships between the board and the Ministry of Finance also seemed to work effectively during this period (Clarke and Wood, 2001, p. 84).

HOW DID THE ADMINISTRATIVE REFORMS WORK?

Developments after the founding of TRA can be divided into two periods. The first was characterised by decreasing corruption and a sharp increase in tax revenue. As already indicated, the trend reversed, corruption seemed to increase and growth in revenue declined. In what follows, these changes in corruption levels over the two periods are explained.

Phase 1 (1996–1997)

In the first year of TRA’s operations, tax revenues grew by more than 30% compared to the previous fiscal year (Table 1b). Since there were only minor changes in the tax structure (rates and bases) and external conditions in this period, the growth in revenue must have been mainly due to the efforts of the tax collectors and other officials at TRA.⁷

It may also suggest that the internal control mechanisms worked. During the probation period (1996–1997), 239 staff members were dismissed (Table 2). A survey of taxpayers in Dar es Salaam also concludes that corruption shrank during the first year (PriceWaterhouseCoopers, 1998). But, according to the respondents, at the same time as the *number* of corrupt acts fell, the *price* per bribe rose (ibid., p. 3). Since there is no evidence that the demand for corrupt services grew during the period, the most plausible explanation is that tax officers who were willing to take bribes considered it more risky than before, and, thus, incorporated a ‘risk premium’ in the bribes. According to the PriceWaterhouseCoopers’ study, the most corrupt staff members during this period were junior officers. Interviews with business people in Dar es Salaam confirmed this observation. This may imply that younger staff members were more inclined to accept a higher risk, or that they acted as agents for players higher up in the tax administration and then shared the ‘proceeds’ with them.⁸

Phase 2 (1997–2002)

After the initial success, tax revenues have dropped in percentage of GDP (Table 1c). Moreover, a new increase in corruption and tax evasion set in (Osoro *et al.*, 1999, p. 36). In particular, corruption seems to be growing at the middle and lower levels of TRA (Waller, 2000). According to taxpayers interviewed, there is also an increase in the

⁷In the Budget Speech for financial year 1996–1997, the Minister of Finance focused on implementing measures to improve efficiency in revenue collection, in particular legal and administrative measures against tax evasion and corruption (URT, 1996b, pp. 59–63).

⁸URT (1996a, p. 284) reports that such mechanisms were in place in the previous tax administration too.

number of tax collectors, *openly* demanding bribes after presenting taxpayers with unreasonably high assessments (ibid., Appendix 2, Section 9.2). How can this relapse be explained? Five factors may contribute to shed light on this development:

- probation period;
- declining real wages;
- group dynamics and social obligations;
- corruption networks; and
- social distance between staff and management.

Firstly, one explanation could be that the first year's success was due to the fact that most employees were working on a probation basis and, additionally, had yet to learn how the new system worked (TRA, 1997). So although their attitudes to corruption may not have changed, it was perceived to be more risky to get involved at that stage in corrupt dealings. Tax officers did not know how the internal control mechanisms worked, or how the top management would execute the rules and whether they stood in danger of losing prospects of a permanent job. These points were also confirmed in interviews with present and former TRA staff. It was stressed that many employees in the operational departments used their probation period to 'study' how the system worked: 'sitting on the fence waiting for better times'. Later, it was shown that some staff at TRA's Internal Investigation and Monitoring Unit (IIMU) were willing to take bribes to turn a blind eye to corruption. Rumours of corruption in the IIMU were circulating as early as 1997, but it was not until December 2000 that the TRA management and board took action, resulting in 24 IIMU officers, including the head of the unit, being 'retired in the public interest'.

Secondly, despite a dramatic increase in pay rates compared with normal rates in the public sector, it was not enough to compensate for the potential gains from corruption (URT 1996a, p. 285): 'For a 'Long-Room' employee who is used to get bribes of TSh 20–30,000 daily, a tenfold increase of his salary from the present level will not make him desist from demanding and accepting bribes'. The situation worsened even more due to the erosion by inflation of the initial pay rates for TRA staff, since nominal wages between 1996 and 2000 remained unchanged.⁹ It is therefore no surprise that the wage reforms seem to have had limited impact on restraining the extent of corruption in the tax administration. But, irrespective of wage rates, the tax administration remains a very attractive workplace. According to the Commissioner for Human Resources and Administration, TRA receives hundreds of applications for every advertised vacancy. The tax collection departments are particularly attractive. There is also considerable internal competition within TRA for vacancies in the operational departments. The 18% increase in salaries of TRA-staff in 2001, may, thus, prove to have only minor impacts on motivation (ESRF and FACEIT, 2002, p. 63).

Thirdly, the assumption that higher salaries will boost productivity over time is most likely exaggerated. It is a well-known fact in sociological management theory that workplaces are social environments and that people in these are motivated by much more than pure economic self-interest (Gillespie, 1993). Recent economic research on human behaviour also indicates that reformers and economists have an inclination to exaggerate the impact of monetary incentives because of a too narrow understanding of intrinsic motivation and group dynamics (see Frey, 1997). An additional aspect of wage incentives that has received little attention in connection with institutional reforms in Africa is associated with the role of family networks and obligations. Increased pay rates may imply more extensive social obligations, resulting actually in a net loss to the individual. This state of affairs can develop into a vicious circle with higher wages leading to more corruption because the tax officer has to make up for the loss caused by such obligations.¹⁰

Another explanatory factor is linked to the impact of corruption networks. Research shows that corruption in public institutions has often been conducted by reasonably well-organised networks, where trust and reciprocity is found between network members (Rose-Ackerman, 1999; Gehlbach, 2001). Such relationships are likely to reduce

⁹Personal interview, M. E. Sila, then Commissioner for Human Resources and Administration, March 2001.

¹⁰This point was raised by several past and present TRA-officials interviewed. See Rose-Ackerman (1998, pp. 317–323) for a discussion of the role of traditional networks in reform processes.

transaction costs, as well as any moral costs that may arise from allowing oneself to be involved in corruption. Furthermore, the peer networks often function as 'repositories of knowledge' for members, for example, on the attitudes of the top management to corruption, how the internal monitoring unit works, and who is potentially bribable among staff members and management.

The reforms probably managed to break a few existing networks, but not to hinder new networks, within and outside TRA, from emerging. The following anecdote may illuminate this process within TRA.¹¹ The TRA board is responsible for appointing people to high-ranking positions, while vacancies at lower levels are taken care of by middle-level managers. Already in TRA's first year, board members were made aware of a practice in some units in TRA where applicants had to pay 'speed money' just to have their applications processed. The board suspected this to be a method of sifting applicants which ensured that only those who signalled their readiness to pay bribes—and therefore probably also a readiness to get involved with the internal corruption networks—were recruited. This indicates the emergence of an informal market for jobs in TRA.¹²

Just as intriguing is to see how new networks gradually formed connections between TRA and former employees in the tax administration. As already mentioned, about one-third of former employees in the tax administration were not given new jobs in TRA. They were considered by the new management and board to have been compromised through involvement in corrupt dealings and misbehaviour. The private sector however was attracted to many of these dismissed people due to their inside knowledge of actual working of the system. For example, former customs officers were recruited by clearing agencies or they set up their own agencies.¹³ These persons had intimate knowledge of the tax administration and of loopholes etc. Since many of their former colleagues remained in the tax administration, good connections to the inside were assured.¹⁴ It is therefore not surprising that this type of corruption network eventually managed to reverse the positive process that characterised TRA's first period.

Finally, the reforms also increased the distance between the executive management and the staff. Few in the top management of TRA had any previous experience with tax administration, in contrast to other staff members who were largely recruited from the former tax administration. The commissioners lack, in the view of a broad section of the staff, knowledge of how the organisation actually works on the ground. This may of course change in the future, and it is obviously positive that the present TRA leadership is considered to be 'clean'.¹⁵ But it is not obvious that the *esprit de corps* among the top managers that has characterised TRA will sustain and permeate the rest of the organisation.¹⁶ The reforms may also, to some extent, have hindered this by allowing huge differences in pay levels between the top and bottom grades.¹⁷

CONCLUSIONS

One lesson to be learned from TRA's first 7 years of operation is that even with relatively respectable salaries and working conditions, corruption may still thrive. The study shows that pay level is only one of several factors affecting the behaviour of tax officers. In an environment where the demand for corrupt services is extensive and monitoring ineffective, wage increases may end up functioning as an extra bonus on top of the bribes taken by corrupt

¹¹Personal interview with former board member of TRA (December, 1998).

¹²According to the Warioba Report, such mechanisms also existed in the previous tax administration (URT, 1996a, p. 284). From other countries, it is known that a market for lucrative positions can emerge in public institutions that pay wages considerably over the market rate, where those with the capacity to pay the most get the jobs (see Andvig, 1999).

¹³Since 1995–1996, a total of 1492 employees of the tax administration have been dismissed (Table 2). Of these, 656 came from the Customs Department (*Business Times*, 21–26 September 2001).

¹⁴An employee in the Research and Policy Department of TRA referred to these former tax collectors as 'ticking bombs', loaded with potentially dangerous information and knowledge about TRA (personal interview, March 2001).

¹⁵These opinions emerged from personal interviews with business people in Dar es Salaam.

¹⁶In July 2002, the TRA Board declined to renew the contracts of six members of the top management team, including the Secretary of the Board and Chief Counsel, the Commissioner for Human Resources and Administration and the Acting Commissioner for Tax Investigation (*Daily News*, 26 July 2002). Moreover, several heads of department received an extension of their contracts with only 6 months against the 'normal' tenure of office of 3 years.

¹⁷A similar situation prevails in the Uganda Revenue Authority (URA), where the internal wage compression rate is 34, that is, equivalent to a wage gap of 3300% between the top and bottom grades (personal interview, Commissioner for Personnel at URA, June 2000).

officers. The situation requires strong internal control mechanisms and effective sanctions that make it easier to dismiss staff.

Moreover, the study shows that hiring and firing procedures may lead to more corruption. Corrupt tax officers often operate in networks, which include both internal and external actors. The way the administrative reforms were implemented, where many of those dismissed were recruited to the private sector due to their knowledge of the workings of the tax system and their inside contacts, may have strengthened the corruption networks. Thus, a major challenge facing reformers of tax administrations is to crack corruption networks and the inherent trust that appears to prevail between members of such networks. One suggestion is to introduce rotation systems for staff in tax administrations, where tax collectors remain only for shorter periods in the same post (Das-Gupta and Mookherjee, 1998). But a danger of the rotation system is that the uncertainty which is thereby created for employees may result in increased corruption, as collectors may use the opportunity to try enriching themselves while they are stationed in the most 'lucrative' posts. The rotation of officials may also give corrupt superiors undue power (URT, 1996a, pp. 284–285). For instance, they might 'sell' assignments to attractive positions or reassign officials to remote stations as a punishment for honesty (Rose-Ackerman, 1999, p. 84). The scarcity of qualified personnel like auditors and accountants further reduces the potential of rotation schemes in the poorest countries.

Furthermore, partial reforms may soon run into difficulties (Tanzi and Pellechio, 1997). Despite quite comprehensive changes in the tax structure (rates and bases) after 1998, the tax system in Tanzania is still complicated and non-transparent (World Bank, 2002, pp. 133–137). Tax legislation is unclear and causes random and partly ad hoc collection procedures (Luoga, 2002). Assessors are considered to have wide discretionary powers to interpreting tax laws, for instance, to allow or disallow expenses or charges, or to exempt import duty on items imported (ESRF and FACEIT, 2002, p. 62). Reforms of tax legislation and procedures, including measures to improve transparency in the taxpayer–tax officer relations, should therefore take place concurrently to reduce opportunities for corruption and the demand for corrupt services. If not, one faces the risk that the administrative reforms will leave behind them not only a highly paid, but also highly corrupt civil servants.

But the successful implementation of such reforms requires political will to back them up (Tanzi and Pellechio, 1997; Rose-Ackerman, 1999). An indication of the limited political will power to fight fiscal corruption and tax evasion is the rise in tax exemptions granted in recent years. While exemptions accounted for 15.2% of total tax revenues (actually collected tax plus exemptions) in 1996–1997, this percentage grew to 37% in 1998–1999 (Mokoro and Oxford Policy Management, 2001). Experience has shown that tax exemptions create room for bribery and corruption, reduce the tax base and increase loopholes for tax evasion (URT, 2002, p. 19). In the 2002–2003 budget, however, the Government discontinued customs duty exemptions for public sector imports of goods and services. This is a step in the right direction. But, many openings remain to abuse the system. The removal of tax exemptions, including those granted to aid organisations and their employees, would help boost the credibility of both the authorities and the donors in relation to anti-corruption measures and, at the same time, contribute to widening the tax base and simplifying the tax system.

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