

# Participation, representation and taxation: Why collect taxes in natural resource rich Mozambique

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## Talking points:

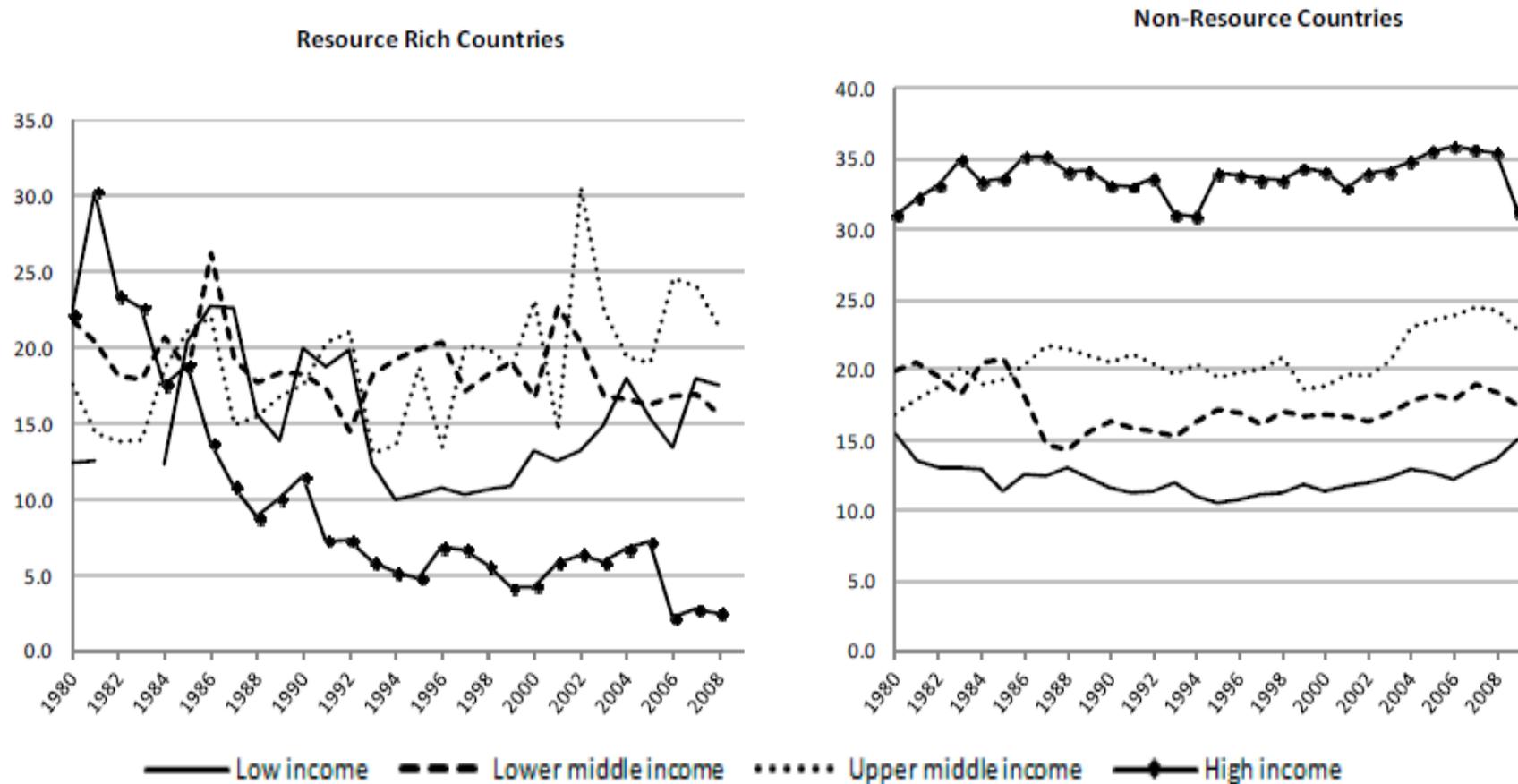
- I. Taxation and state-building
- II. Taxation in Africa and Mozambique
- III. Strengths and weaknesses of the current tax system
- IV. Towards governance focused reforms:  
Building the social fiscal contract

# I. Taxation and state-building

- Tax is not an end in itself, but a means towards a well-functioning state:
  1. Governments dependent on taxes will be inclined to pursue policies to expand the economy and thus the tax base
  2. Dependence on taxes requires states to develop tax raising capacities
  3. Bargaining over taxes is central to building relations of accountability between state and citizens based on mutual rights and obligations
  4. Rising tax revenues combined with economic growth is the **exit strategy** out of aid dependency

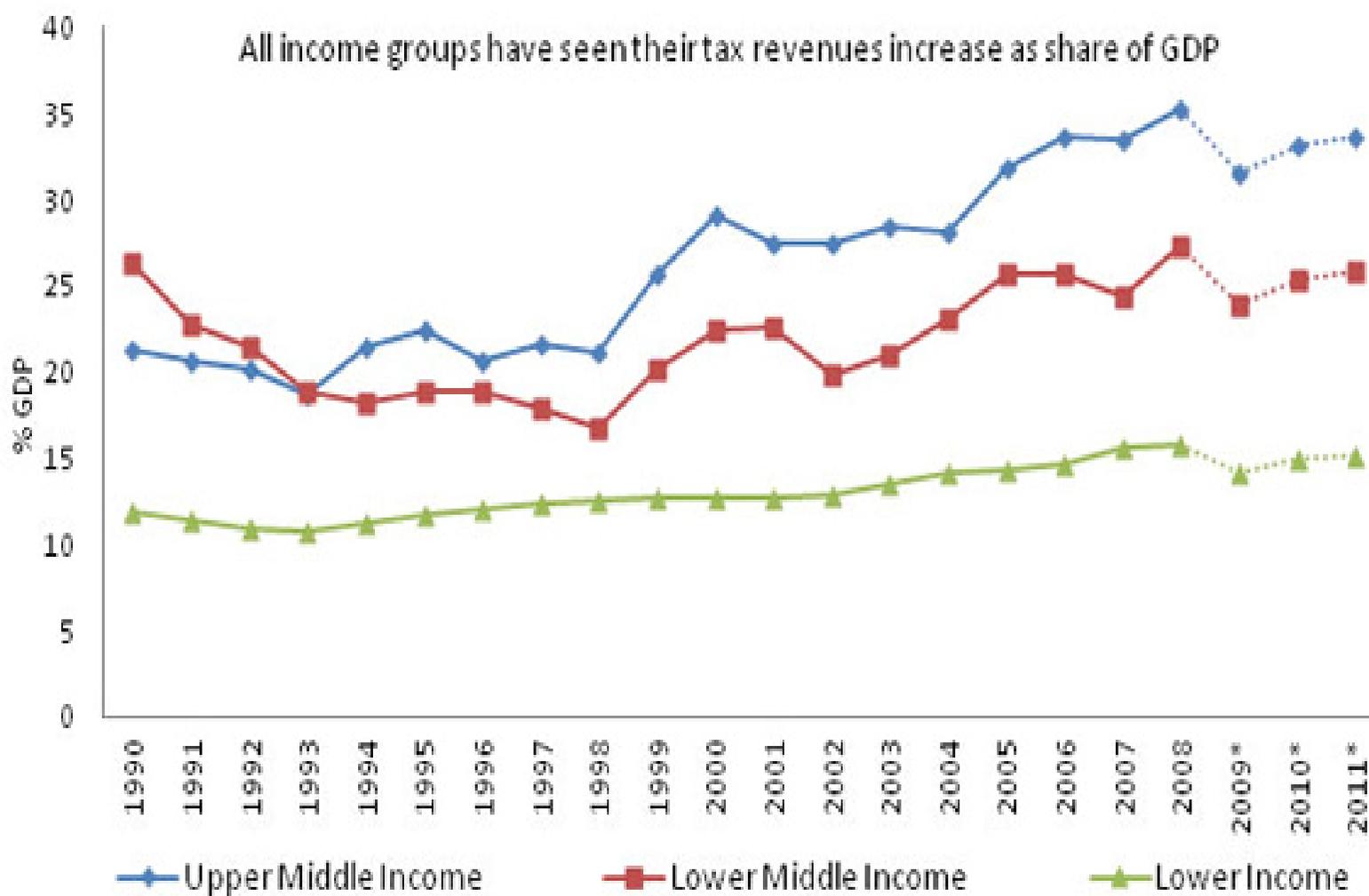
- Bad governance is often correlated with limited state reliance on revenues from taxation of its citizens and businesses:
  - Non-tax revenues tend to leave regimes more free to make whatever expenditures they wish without their having to be concerned about the likely reactions of citizens
  - Rentier states have limited incentives to build up institutions to collect and administer tax, or to extend the reach of the government to poorer, more remote regions
  - In particular, large oil and mineral revenues are associated with low levels of democracy and states unbound by law
  - Natural resource revenues much more volatile than tax revenues

# Revenue developments in Resource-Rich and Other Countries, 1980–2009 (in % of GDP)



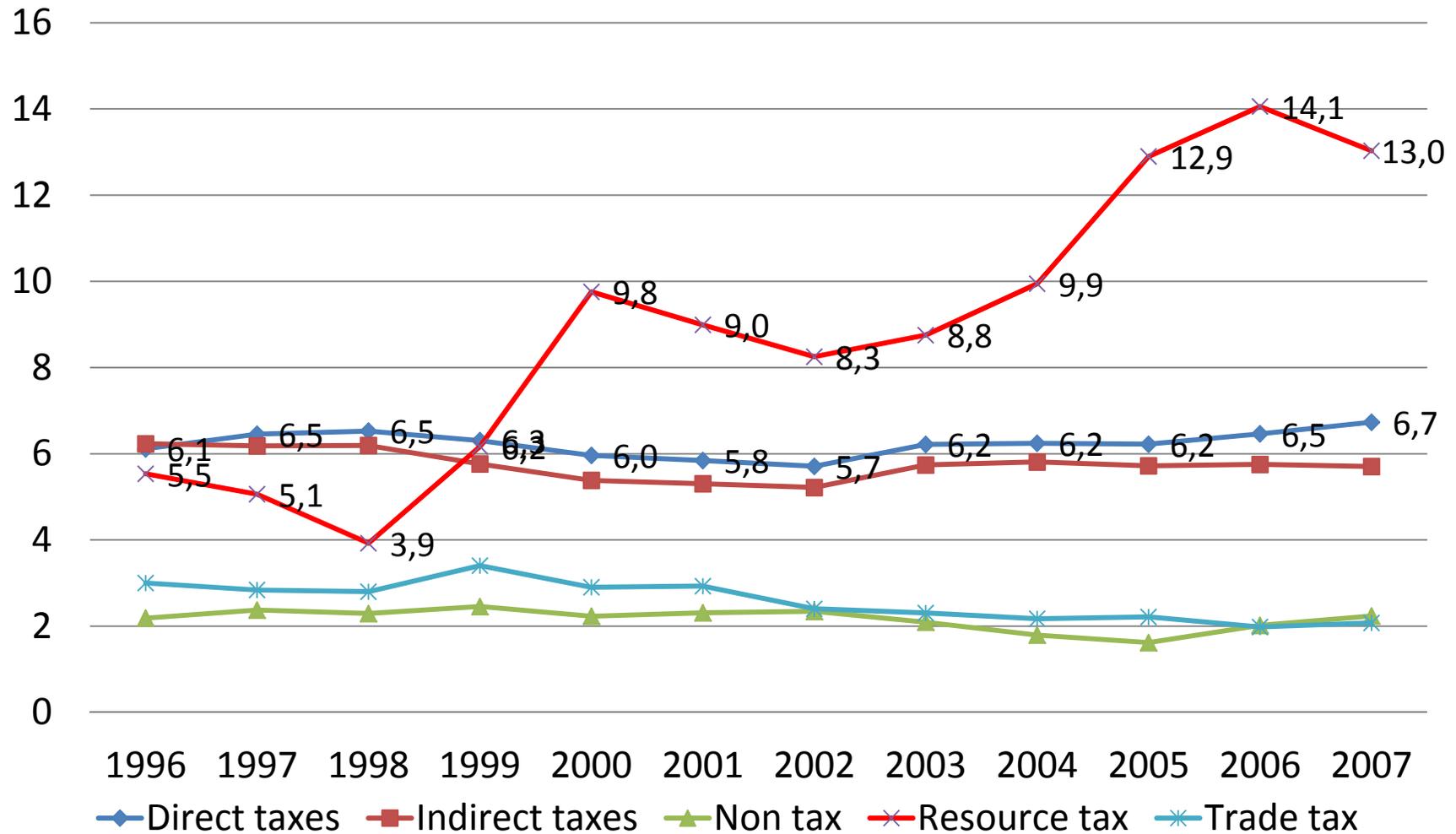
Source: IMF staff estimates

## II. Taxation in Africa and Mozambique

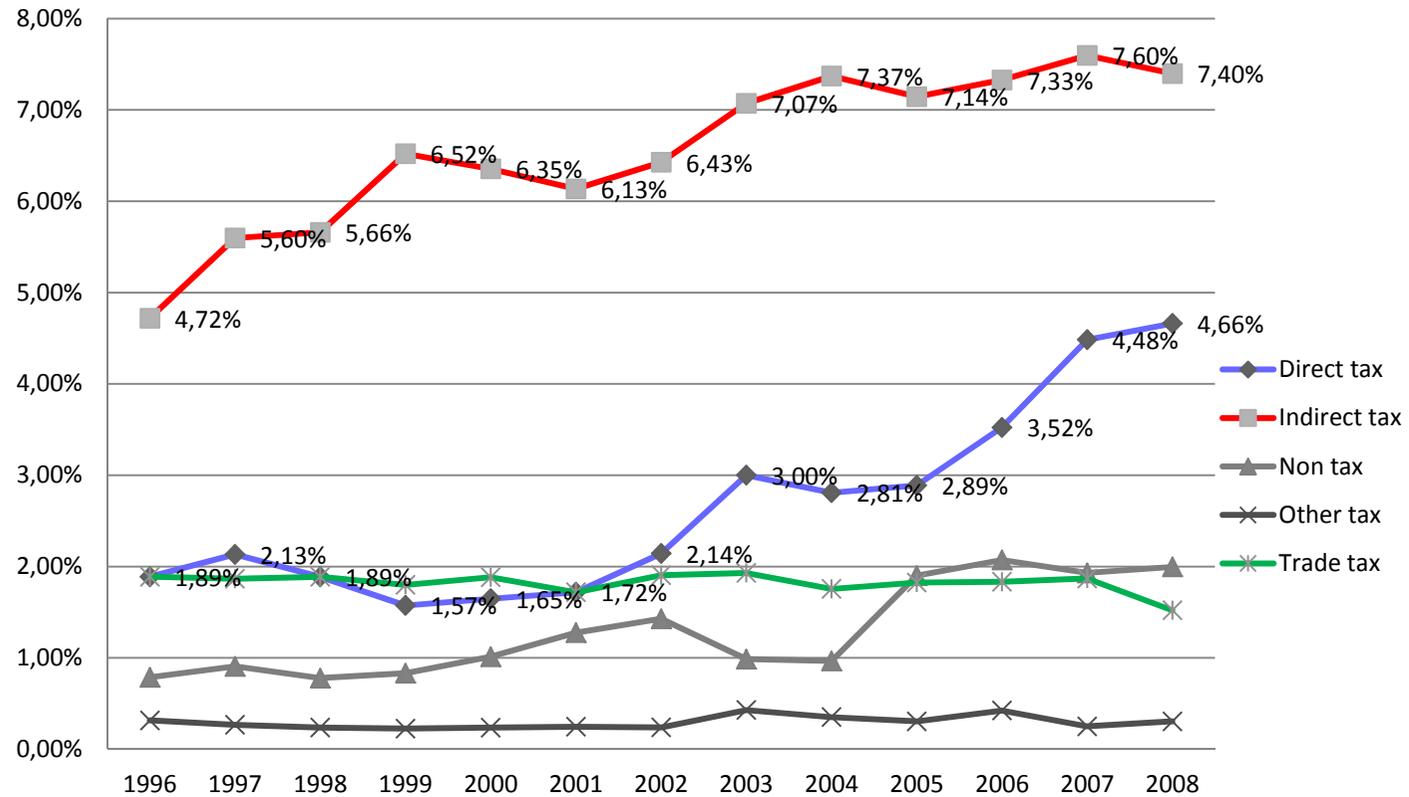


# Taxation in Africa

Africa: Domestic revenue mix as share of GDP

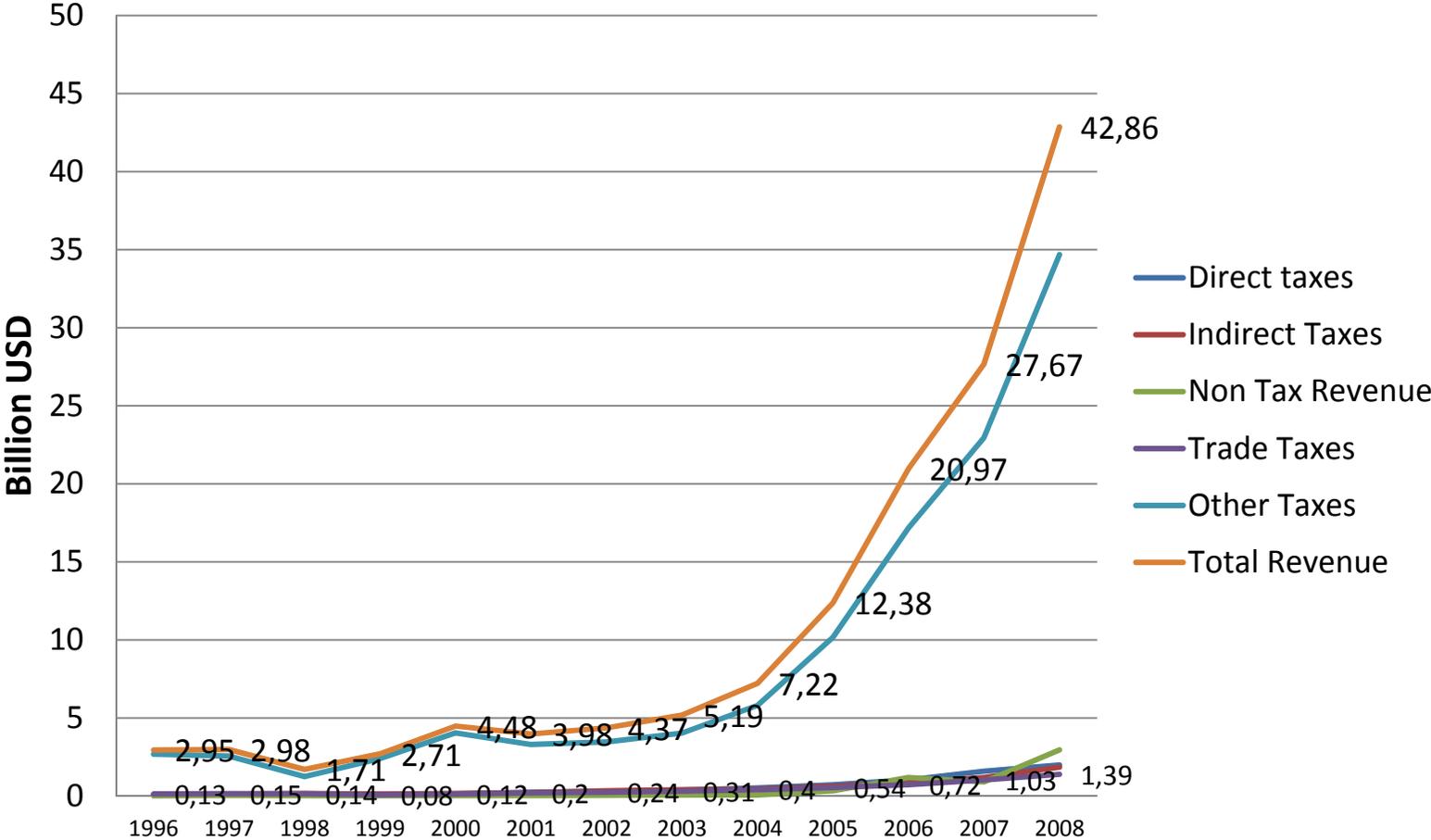


## Mozambique: Tax mix in % of GDP (1996-2008)



Sources: World Bank (2011a) and AEO (2010a)

# Angola: The tax mix (1995-2008)



Source: AEO 2010

### III. Strengths and weaknesses of the current tax system in Mozambique

#### ➤ A number of good things to report:

1. Simplification of tax laws, regulations and rate
  - Much remains to be done with legislation and licensing of natural resources
  
2. Improved tax administration at central gov. level
  - Simplification of customs clearance and tax payment
  - Reduced tax compliance and administrative costs
  
3. Improved tax administration – taxpayer dialogue
  - Consultations between AT and representatives of major business associations (CTA and ACIS)
  - Taxpayer education and outreach

## ... good things to report ... (cont.)

### 4. Substantial increase in tax collection

2011: Tax-to-GDP ratio  $\approx$ 19%

2007: Tax-to-GDP ratio 14.2%

### 5. Number of registered taxpayers increased

2009: 960,000

2006: 382,000

2011: Increase by 327,000 personal and 6,300 companies

## ... and some major challenges ...

### 1. Intra-governmental communication

- Inadequate
- Facilitates exemptions & proliferation of tax incentives

### 2. Narrow tax base

- Large taxpayers contribute 56% of all revenue (1200 companies)
- Large untaxed informal sectors

## ... major challenges ... (cont.)

### 3. Extensive and increasing tax incentives & exemptions

- Lost revenues
- Creates room for bribery and corruption
- Increases loopholes for tax evasion
- Distorts competition
  
- Financial sector paid more in revenue in 2011 than the megaprojects: 3 billion MZM versus 2.8 billion MZM

#### ➤ **Perceptions of an unfair tax system**

- Unlikely to achieve broad based 'voluntary' taxpayer compliance without substantial reforms of the exemption and tax incentive regime

## ... major challenges ... (cont.)

### 4. Capital flight: Estimated capital flight from Mozambique, Angola, Nigeria, Tanzania and Zambia

<i>Units: mill USD</i>	<i>2002</i>	<i>2000-2008</i>	<i>1970-2008</i>	<i>1990-2008 (average annual IFF in % of GDP)</i>
<b>Mozambique</b>	<b>178</b>	<b>1 121</b>	<b>5 450</b>	<b>8.9%</b>
<b>Angola</b>	2 156	24 062	29 500	10.9%
<b>Nigeria</b>	5 135	169 871	217 738	
<b>Tanzania</b>	597	2 545	7 356	2.9%
<b>Zambia</b>	72	5 120	9 348	7.6%
<b>Sub-Saharan Africa</b>	21 808	323 577	532 926	

# What is a tax haven?

Tax havens ~ Offshore Financial Centre ~ Secrecy jurisdiction

1. Very low or no tax on capital income
  2. A special tax regime for shell companies ('ringfencing')
  3. A lack of transparency concerning ownership and/or lack of effective supervision
  4. No effective exchange of information on tax issues with other countries and jurisdictions
- Combination of secrecy rules and virtually zero tax terms
- Granting tax residency based on no substantial activity means that tax havens steal other countries' tax bases

- **British Virgin Islands (BVI)**

- 19 000 inhabitants (low level of education)
- 830 000 registered companies on BVI
- Authorities **claim** that these **companies run and/or manage** their business from BVI and thus are tax residents there

→ There are 43 (=830 000/19 000) companies pr. capita

→ Some BVI residents are board members (and directors even) of hundreds (and in some cases even thousands) of companies

**Illustrative of the lack of activity of substance in tax havens**

## 'Tax havens': not only small, islands in the sun

	<b>Absolute share</b>	<b>Secrecy</b>	<b>FSI 2011</b>
1	United States	Nauru	Switzerland
2	United Kingdom	Maldives	Cayman Islands
3	Luxembourg	Turks & Caicos	Luxembourg
4	Switzerland	Marshall Islands	Hong Kong
5	Germany	Belize	USA
6	Cayman Islands	St Lucia	Singapore
7	Hong Kong	Vanuatu	Jersey
8	Singapore	Seychelles	Japan
9	Ireland	Montserrat	Germany
10	Japan	Bermuda	Bahrain

Financial Secrecy Index (2011); (Components: secrecy + size)

## Tax evasion facilitated by tax havens (secrecy jurisdictions) undermine the national tax system

- Tax havens (secrecy jurisdictions) make it **harder** to tax enterprises
  - ❖ Transfer pricing practiced by multinational companies
- Consequently, tax revenue **falls** - or to compensate - taxes are levied at a **too high rate** on the fewer remaining tax bases: **this hampers growth**
- In some countries, capital flight may also have reduced the political elite's interest in local economic growth and development

## IV. Towards a state-building approach to strengthen the tax system in Mozambique

### ❖ 'Build the social fiscal contract'

➤ A fiscal challenge for Mozambique is to develop a domestic revenue-system that simultaneously facilitate:

- ✓ **Revenue growth** to enhance revenues from both the 'regular' tax system and from natural resources
- ✓ **Build tax administrative capacity** at the national, provincial and local government levels
- ✓ **Build accountability** by encouraging constructive state-society engagements around taxes

# General recommendations

## Build a tax regime characterised by :

1. Clear, unambiguous rules with not too many exceptions
2. Long term stability and predictability for investors
3. Equal treatment of all companies with no exemptions
4. Simplicity for both tax administration and taxpayers
5. Better links/consistency between the national and sub-national tax regimes
6. Clear(er) links between taxes paid and benefits/services received by taxpayers

## Some specific recommendations:

### **Make tax 'rock' on the domestic political arena**

#### **1. Tax policy**

- Technical Assistance to the Ministry of Finance
- Advisory, training and research support to Members of Parliament

#### **2. Tax administration**

- Continue to build expertise on specialised tax audit functions
- Strengthen research & analytical capacity

#### **3. Create broader citizen engagement around taxation**

- More emphasis on the 'demand side' to strengthen citizen and private sector engagement
- Encourage media and civil society attention to tax

#### **4. Build domestic research capacity on taxation and capital flight**

- Tax incentives and exemptions
- Capital flight from Mozambique
- Informal sector taxation
- **Inspire students to focus on tax topics**

Muito obrigado!

THANK YOU FOR YOUR ATTENTION!