

The Domestic Dimension: Fiscal Legitimacy, Tax Administration and Poverty Reduction

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Taxation and tax reform is central to state-building:

- to ensure sustainable funding for social programs, and for public investments to promote economic growth and development.
- taxation is the main nexus that binds state officials with interest groups and citizens.
- taxation, particularly in the form of land and property taxes, customs and border collection can help increase the territorial reach of the state.
- fiscal capacities are needed to build a legitimate state. Democratic elections do not themselves ensure state legitimacy

Politics of Administrative Reforms: The Case of Autonomous Revenue Authorities

- Role of macroeconomic and particularly fiscal and inflationary crises has provided opportunities for leaders to gain leverage over the reform process.
- Centralised public authority and executive support is essential for tax reform to be undertaken and sustained (e.g. Rwanda, Ghana, South Africa, Ethiopia)
- the creation of a (semi-) autonomous revenue authority paradoxically can increase the political attention it receives (e.g Uganda)
- the pressure on governments to meet revenue targets can create tensions between the state and interest groups which can undermine the tax authority's legitimacy.

Lessons from South Africa

- high degree of administrative cooperation within the state, particularly between SARS, the Finance Ministry and the Central Bank.
- the state has historically maintained a cooperative relationship with upper-income groups, including large firms, which helped reduce the transaction costs of collecting income taxes.
- reforms were introduced with substantial consultation with representatives from the state, political parties, business chambers, labour unions, and national and international tax and legal experts.
- sustained campaign by SARS which emphasizes in its campaigns that its task effective tax collection is central for ‘the protection of the national economy’.
- SARS was formed in the context of a strong national political party, the African National Congress (ANC).

Urban property taxes

- The role of land and property taxes is especially important as local governments seek to raise revenues in the context of decentralization reforms. The same is true for local governments in urban areas. Why focus on this tax?
- **one of the most underutilized forms of taxation in LDCs** and can potentially provide the financing of urban infrastructure investment which is central to improving the production and export capacity of light manufacturing plants, many of which are located in urban centres.
- **provides one of the few potential sources of taxation for municipal governments.**
- **can provide the impetus for the creation of urban property databases** which could help improve the synergy between municipal taxation and urban planning.
- **provides one of the few mechanisms through which progressive taxation can be developed in LDCs.**
- **contributes to making property rights more secure.**

Tax Policies to Improve the Fiscal legitimacy of the State

- there is a need to improve the capacity and legitimacy of Large Tax Payer Offices (LTOs)
- Harsh tax enforcement in situations with poor service delivery may contribute to undermining the legitimacy of local government and increase tax resistance. Trying to meet very ambitious tax targets can be counterproductive
- Tax exemptions of donor employees creates a bad demonstration effect for low-income states trying to build domestic tax bases.
- Avoid the problem of the ‘dual public sector’ in aid delivery
- Taxing the informal sector may require linking tax policy to production strategies.

Recommended Readings

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