

Domestic Resource Mobilization in Partner Countries of Belgian Development Cooperation

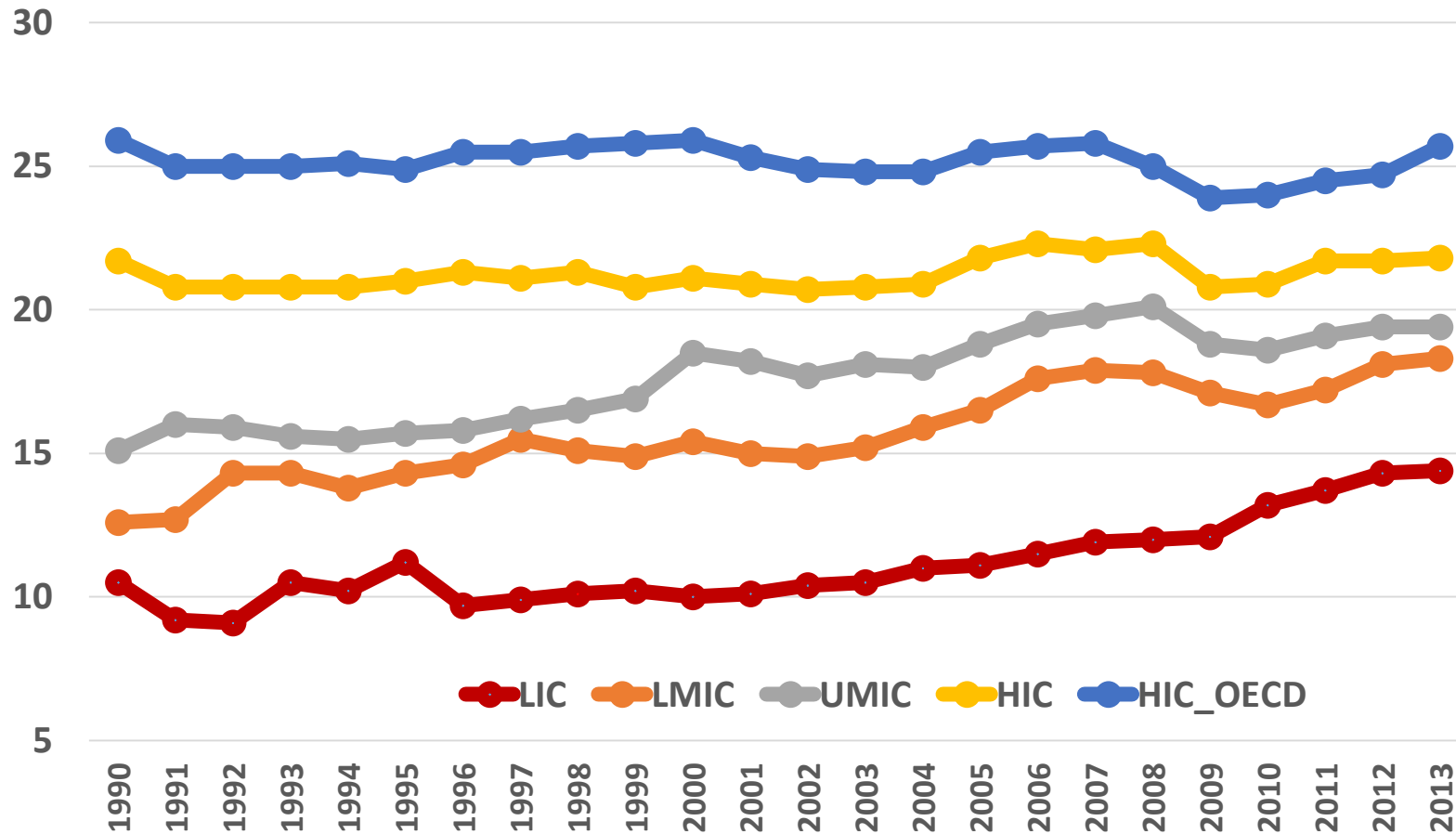
Romain Houssa, & Roukiatou Nikiema

21 May 2017, Ouagadougou

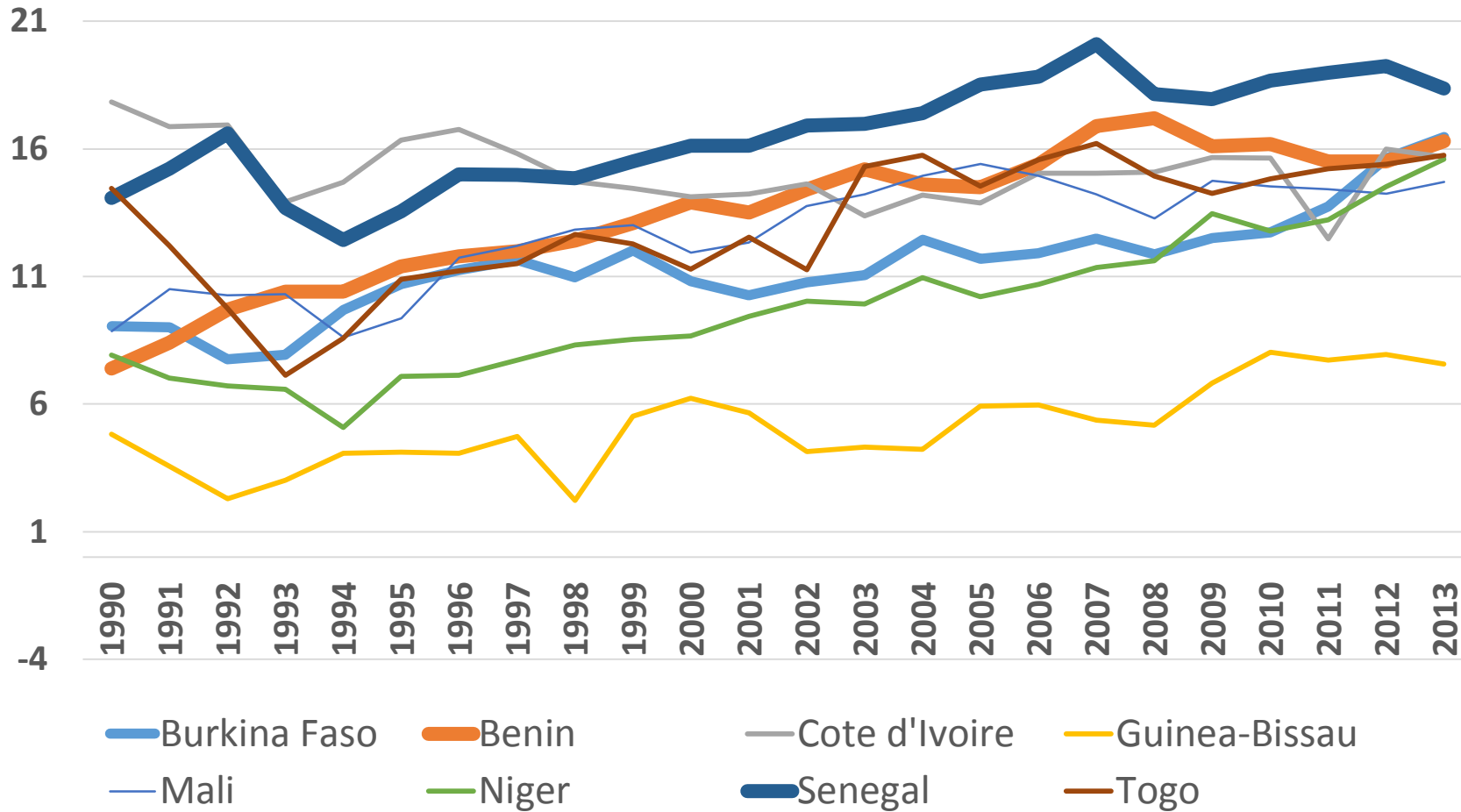
Introduction

- Huge-resource gap required in LICs (DMDF, 2015)
- Focus on **domestic taxation**
 - enhance state building and strengthen the state-citizen relationships (Tilly 1975)
 - relatively more stable

Tax Revenue Across Income Groups



Tax Revenue Across WAEMU Members



Policy (Research) Objectives at BeFinD

- **We analyze...**
 - The principles of tax design & State of Domestic Resource Mobilization (DRM)
 - Taxation of multilateral companies
 - The role of Value Added Tax (VAT) for DRM
 - Assessing rooms for improvement in VAT systems
 - The role of institutions for DRM

Research on Taxation at BeFinD

- various (interlinked) studies on DRM capacities of DGD partner countries (+) other developing countries...recent examples
 - [Institutional quality, economic development and the performance of VAT](#), *BeFinD Working Paper N°15* (Romain Houssa and Kelbesa Megersa)
 - [The Performance of VAT in DGD-partner Countries](#), *BeFinD Working Paper N°16* (Mattéo Godin, Romain Houssa and Kelbesa Megersa)
 - [Taxpayer behaviour and institutions in Sub-Saharan Africa](#), *BeFinD Working Paper N°169* (Roukiatou Nikiema and Pam Zahonogo)
 - [A Review of critical issues on tax design and tax administration in a global economy and developing countries](#), *BeFinD Working Paper N°7* (Mattéo Godin & Jean Hindriks)
 - [Follow you, follow me: public investment under tax competition](#), *BeFinD Policy Brief N° 1* (Jean Hindriks and Yukihiro Nishimura)

...for more, visit <http://www.befind.be/publications/taxes>

Outline

- **I. Impact of VAT on DRM**
- **II. Role of institutional quality on DRM**
- **III. Sources of VAT Inefficiencies: Case study in Burkina Faso**
- **IV. Concluding Remarks**

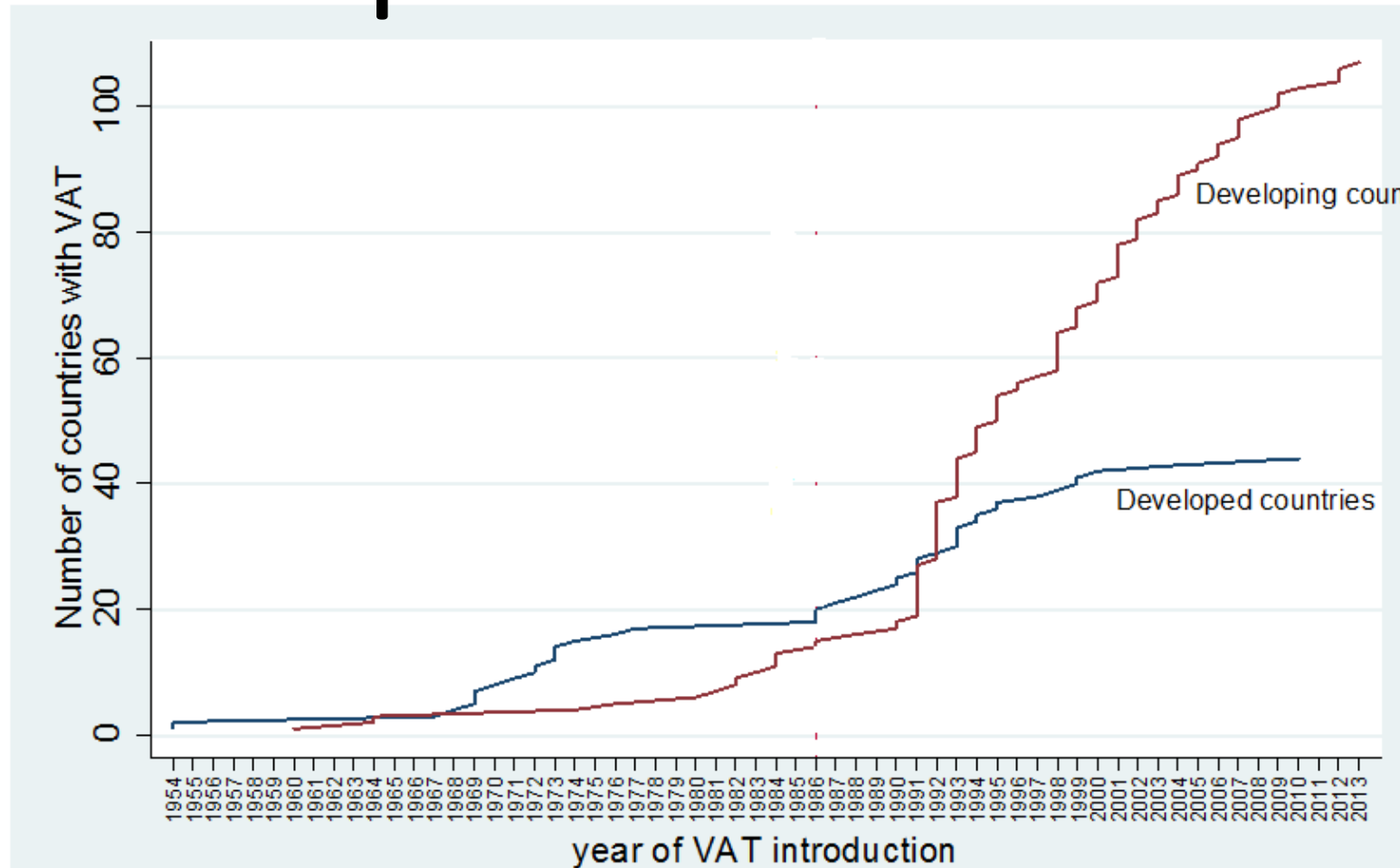
I.

Impact of VAT on DRM

Why is VAT important?

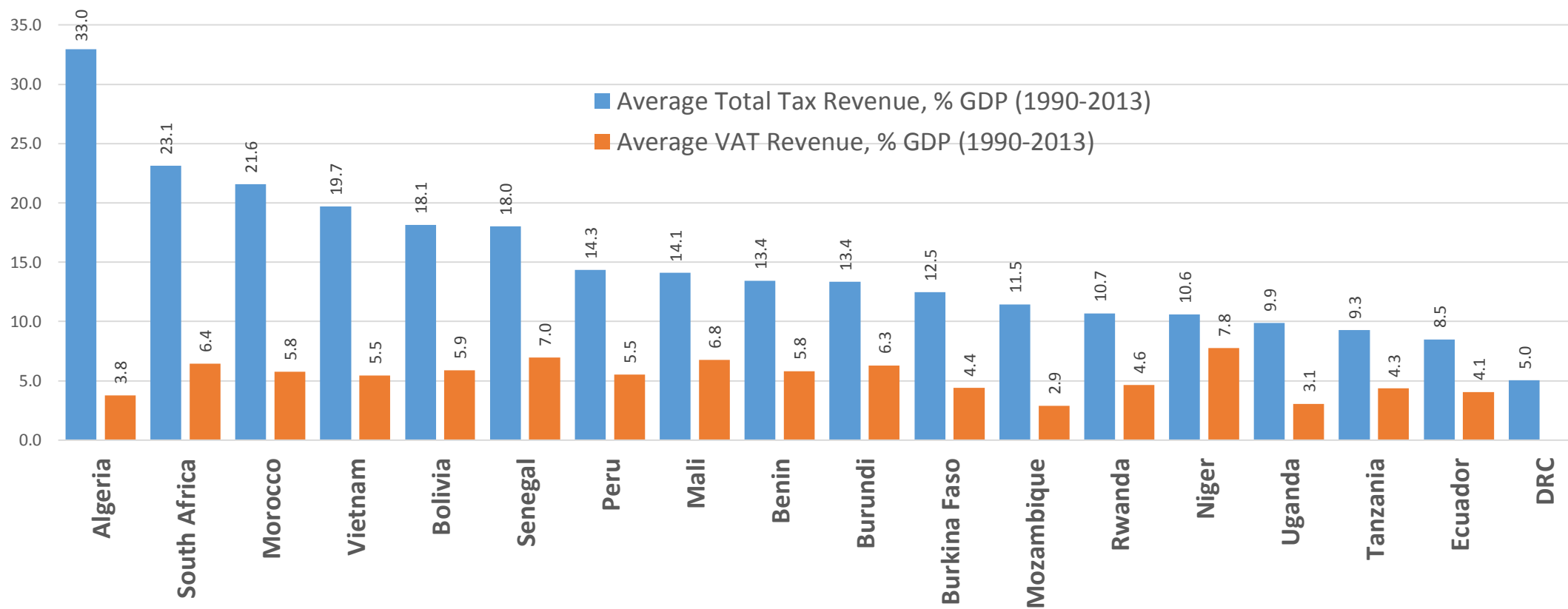
- VAT is relatively easy to administer → Less prone to tax evasion
- Suitable for developing countries
 - less sensitive to the informal market
 - If well designed, it can even reduce the size of the informal sector
- Less distortionary among taxes
 - In comparison with income taxes, VAT does not change consumption decisions relative to savings and investment decisions
- No cascading effects
 - Unlike other consumption taxes
 - Tax on a commodity is charged at separate stages of the production process without deductions
 - Sellers or firms paying VAT, can receive credit for the VAT paid on intermediate inputs

VAT adoption across the world

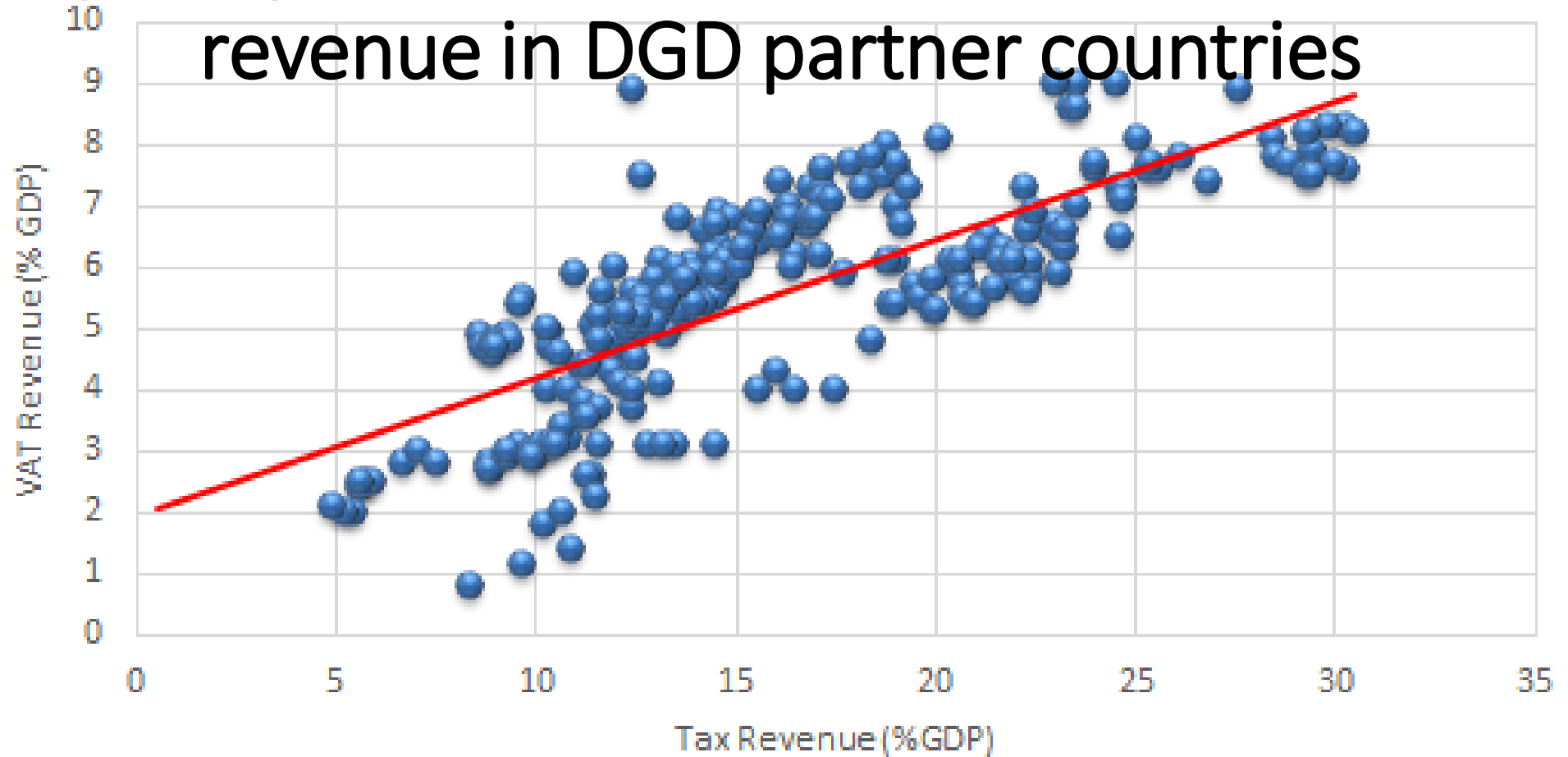


Current state of DRM:

Tax and VAT revenue in partner countries



High degree of correlation between Tax & VAT revenue in DGD partner countries



VAT, DRM and developing countries:

The overall picture...across the developing world & elsewhere

- We estimate the following tax-effort equation

$$Tax_{i,t} = \alpha + \beta VAT_{i,t} + \gamma X_{i,t} + \delta \sum_{j=1}^n w_{ij} Tax_{j,t} + \varepsilon_{i,t}, i = 1, \dots, n$$

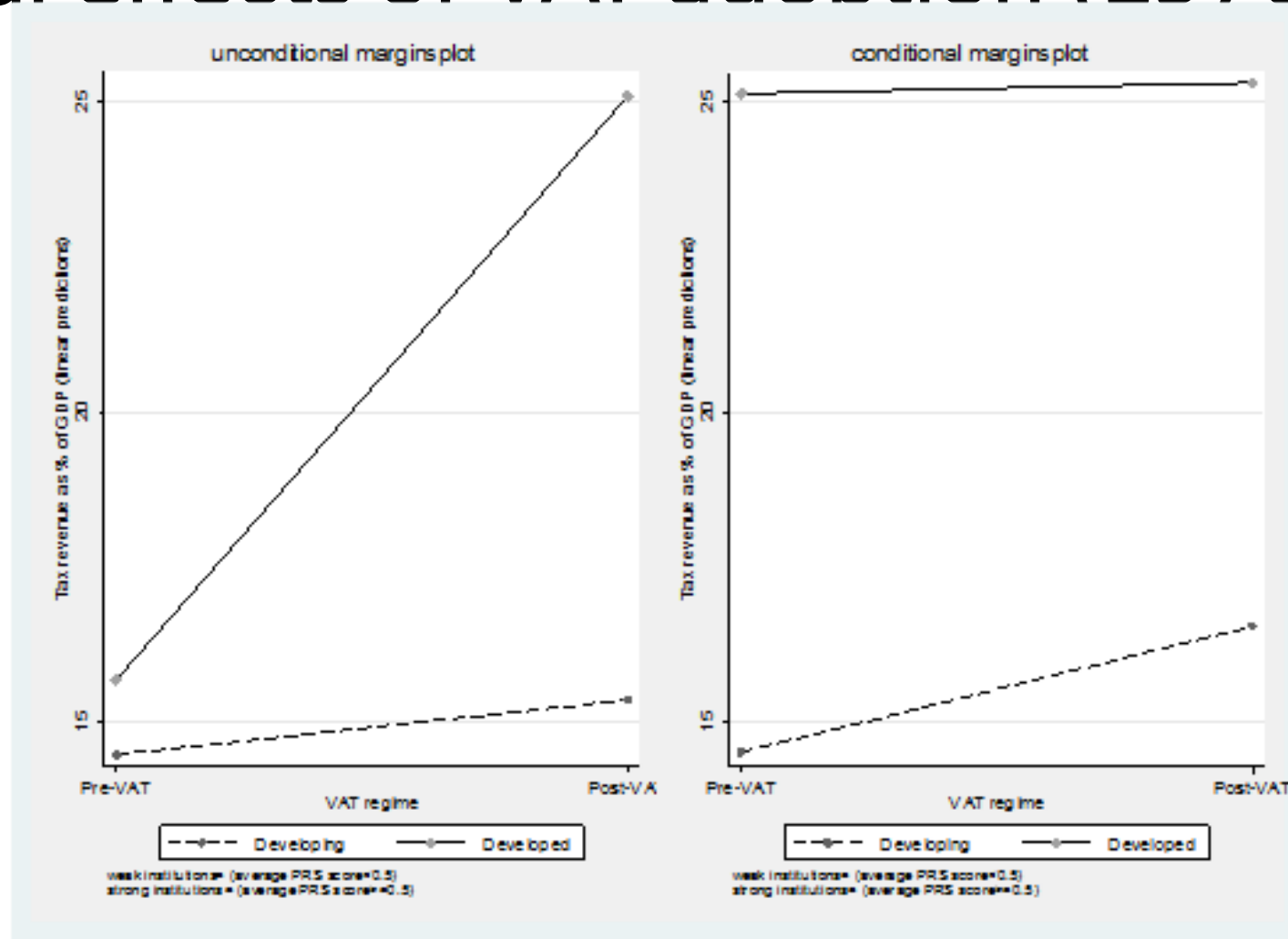
- $X_{i,t}$ include: the level of development, size of the informal sector, country size, size of dependent population, institutional quality ...

VAT, DRM and developing countries:

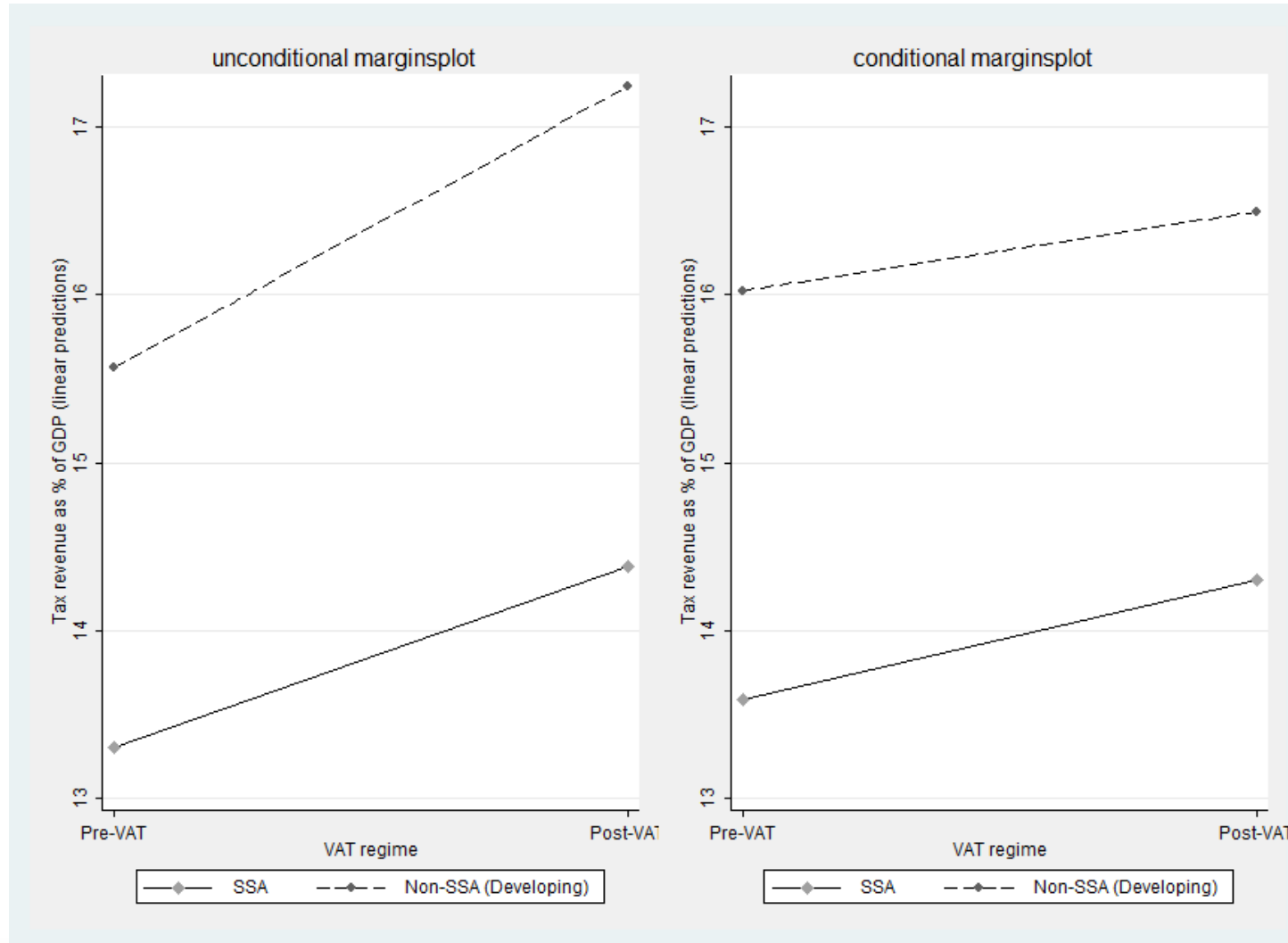
The overall picture...across the developing world & elsewhere

- Data from 149 countries over the 1970 - 2013
- Developing countries
 - Sub-Saharan Africa (SSA) and
 - Non-SSA Developing countries
- Developed countries

Marginal effects of VAT adoption (1970-2013)



Marginal effects of VAT adoption (1970-2013)



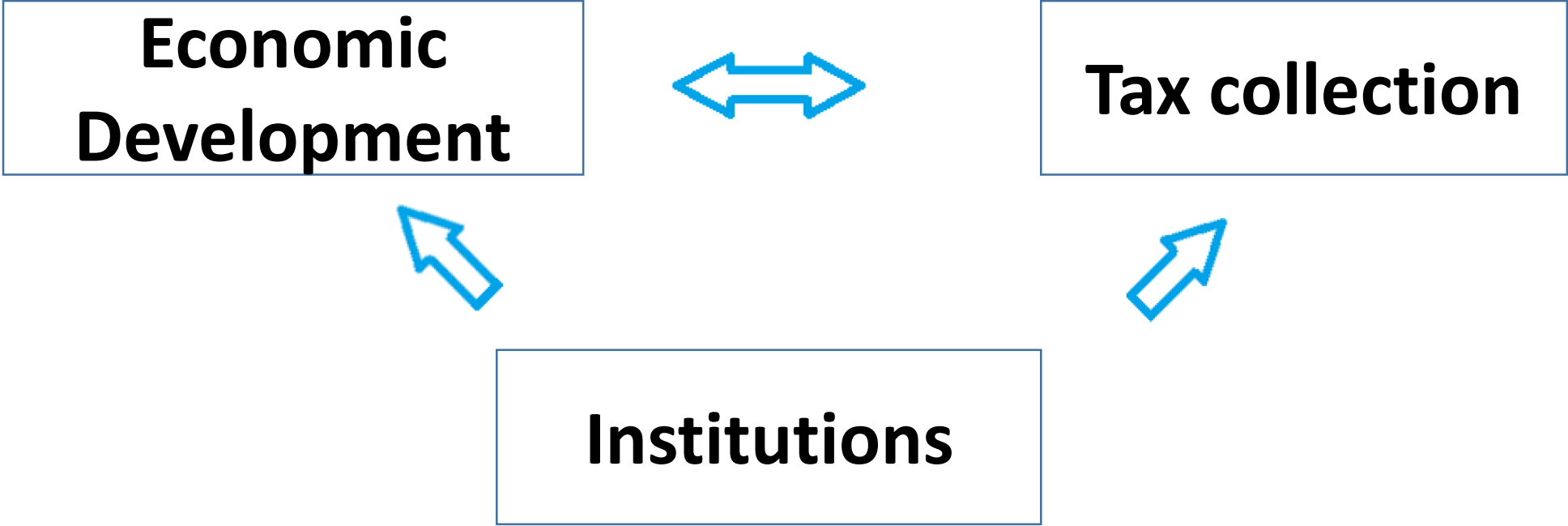
Performance of VAT in SSA

- Marginal effect of VAT adoption (i.e. relative contribution of VAT to tax revenue) is estimated to be strong for SSA and other developing countries
- The positive effect of VAT on tax collection in SSA is reassuring because some earlier studies were not able to identify an overall positive effect for the region
- We show that analysis of data over the recent period (where VAT has become more contributive) is important to highlight its positive role in SSA's DRM efforts

II.

Role of institutional quality on DRM

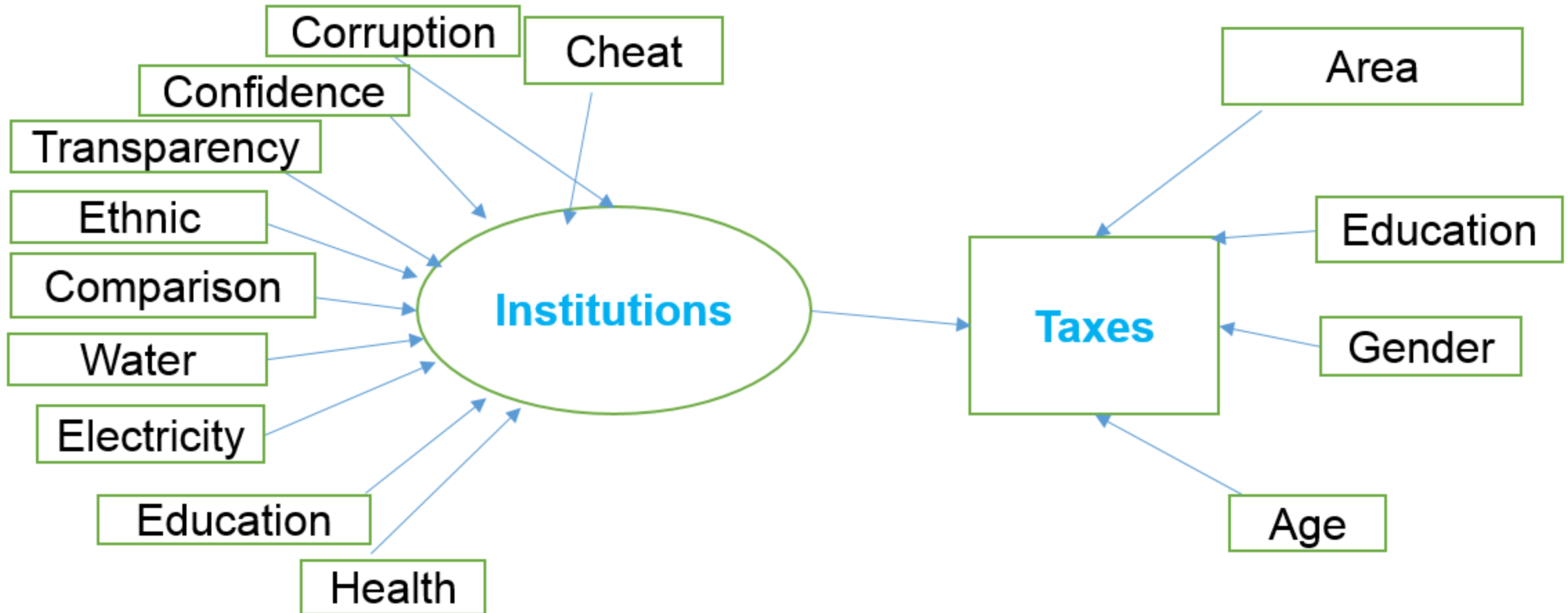
Taxation, Institutions & Economic Development



Institutional quality & DRM

- A good-institutional environment should improve both the demand as well as the supply factors inherent to the performance of VAT.
- Including: the capacity of the tax administration, government effectiveness in providing public goods, trust in the government, ...
- We provide micro and macro evidences

Institution & Taxes (Micro Evidence)



Institution & Taxes (Micro Evidence)

survey in 29 SSA countries

please tell me whether you think the action is not wrong at all, wrong but understandable, or wrong and punishable : Not paying the taxes they owe on their income

	Observation	Percentage
Not wrong at all	4,566	11.36
Wrong but understandable	14,362	35.73
Wrong and punishable	19,193	47.67
Do not know	2,108	5.24
Total	40,199	100,00

Institution & Taxes (Micro Evidence)

Variables	Odds ratio
Quality of institutions	1.718***
Cheat	0.324***
Health	0.286***
Education	0.242***
Electricity	0.188***
Water	-0.012
Partial confidence	0.185***
Total confidence	0.919 ***
Transparency	0.326***
Ethnic	0.115***
Comparison of attitudes	0.388***
Corruption	-0.147***

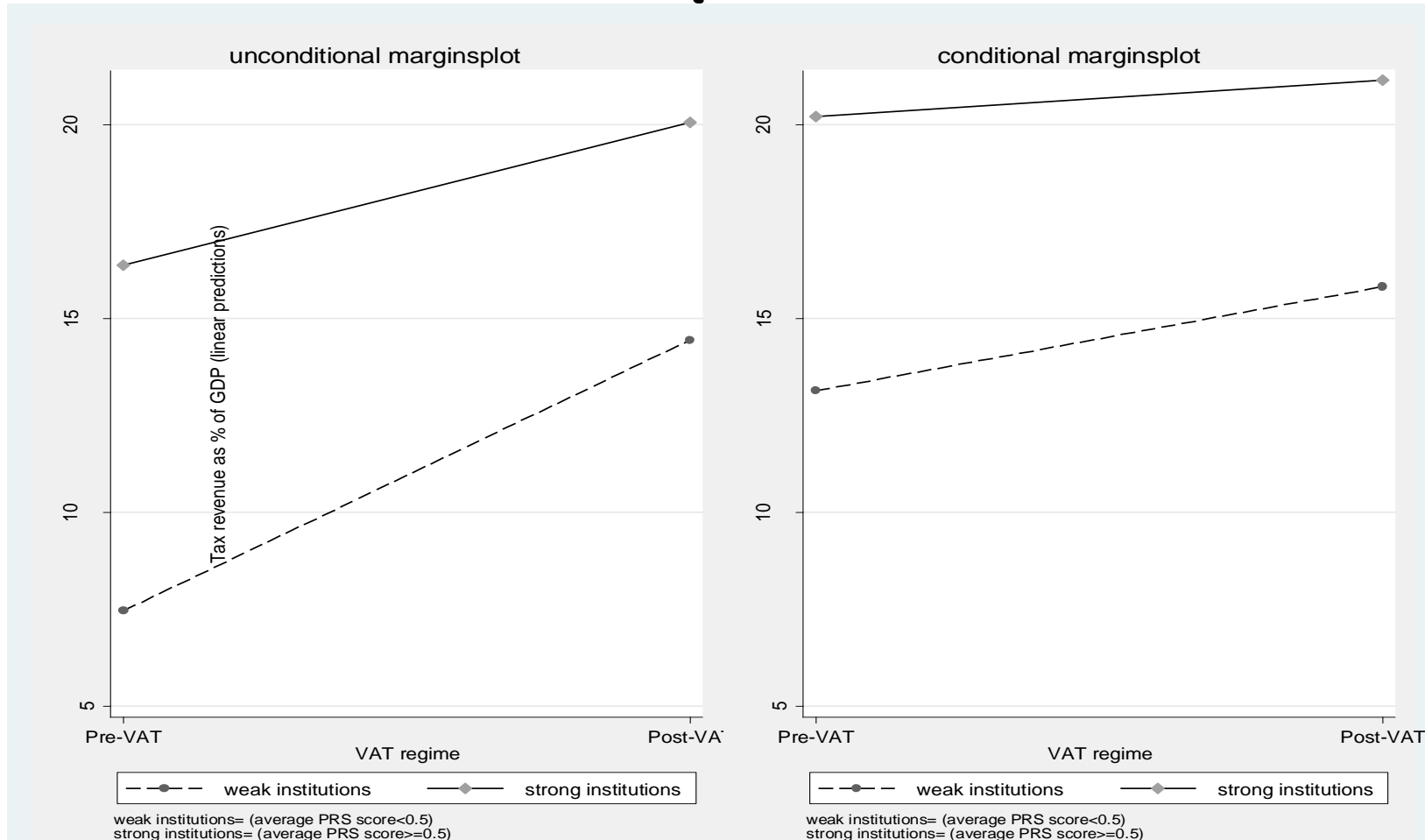
Institution & Taxes (Micro Evidence)

- Taxpayer behaviour is affected by quality of institutions
- Individuals' attitudes towards paying tax are significantly dependent on the quality of institutions
- When the quality of institutions is perceived as good, individuals are more likely to pay taxes
- Indirect effects of quality of institutions:
 - Individual's perception of difficulty to evade taxes → more likely to pay tax
- Quality of public services offered by the state:
 - Confidence in the tax authorities (partial or total) & transparency → more likely to pay tax
 - perception of corruption, cheating, quality of health, quality of education, quality of electricity, confidence, ethnic discrimination... have a significant effect on tax payment!

Institution & Taxes (Micro Evidence)

- Individuals are more likely to pay taxes if they have:
 - Perception of difficulties to evade taxes;
 - Better confidence in the tax authorities & transparency, (less corruption, ethnic discrimination...);
 - Perception that the quality of public services is good: health, education, electricity ...

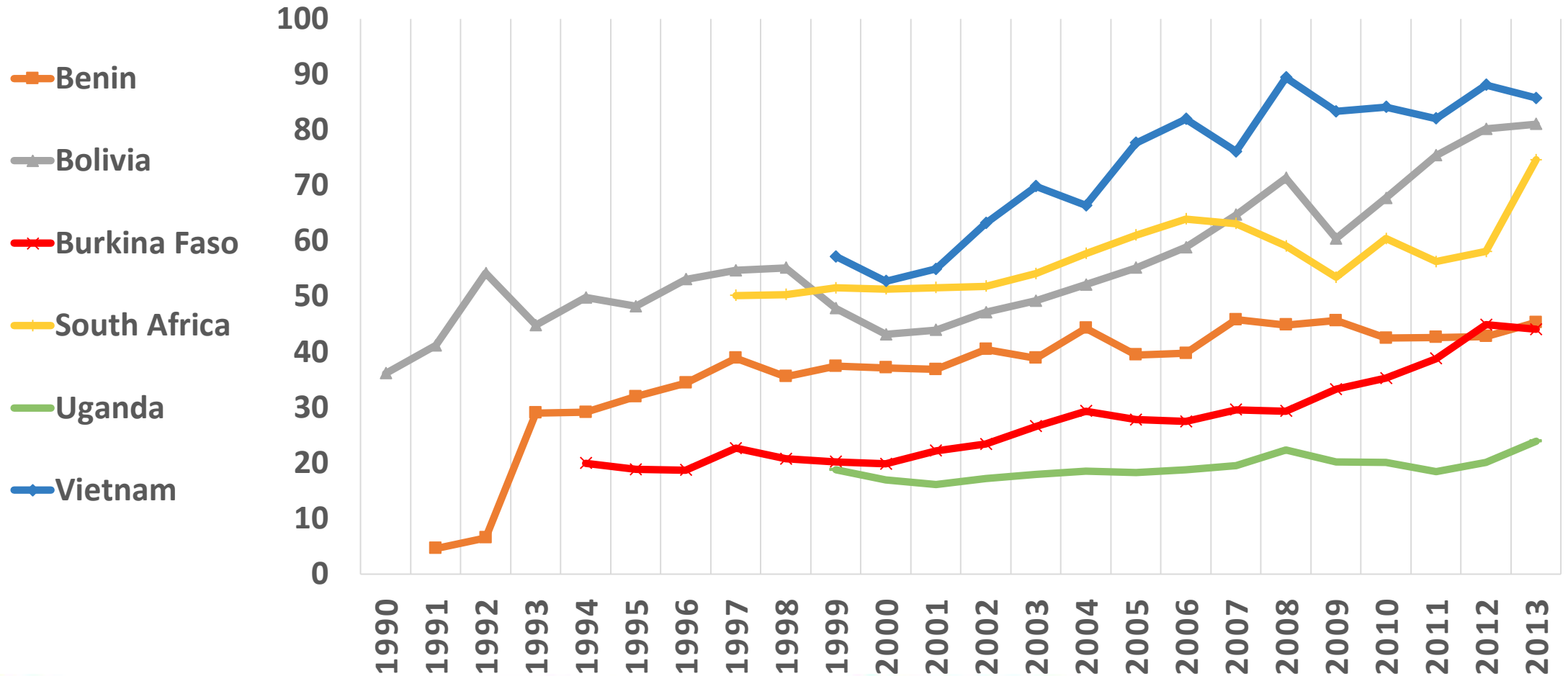
Institution & Taxes (Macro Evidence)



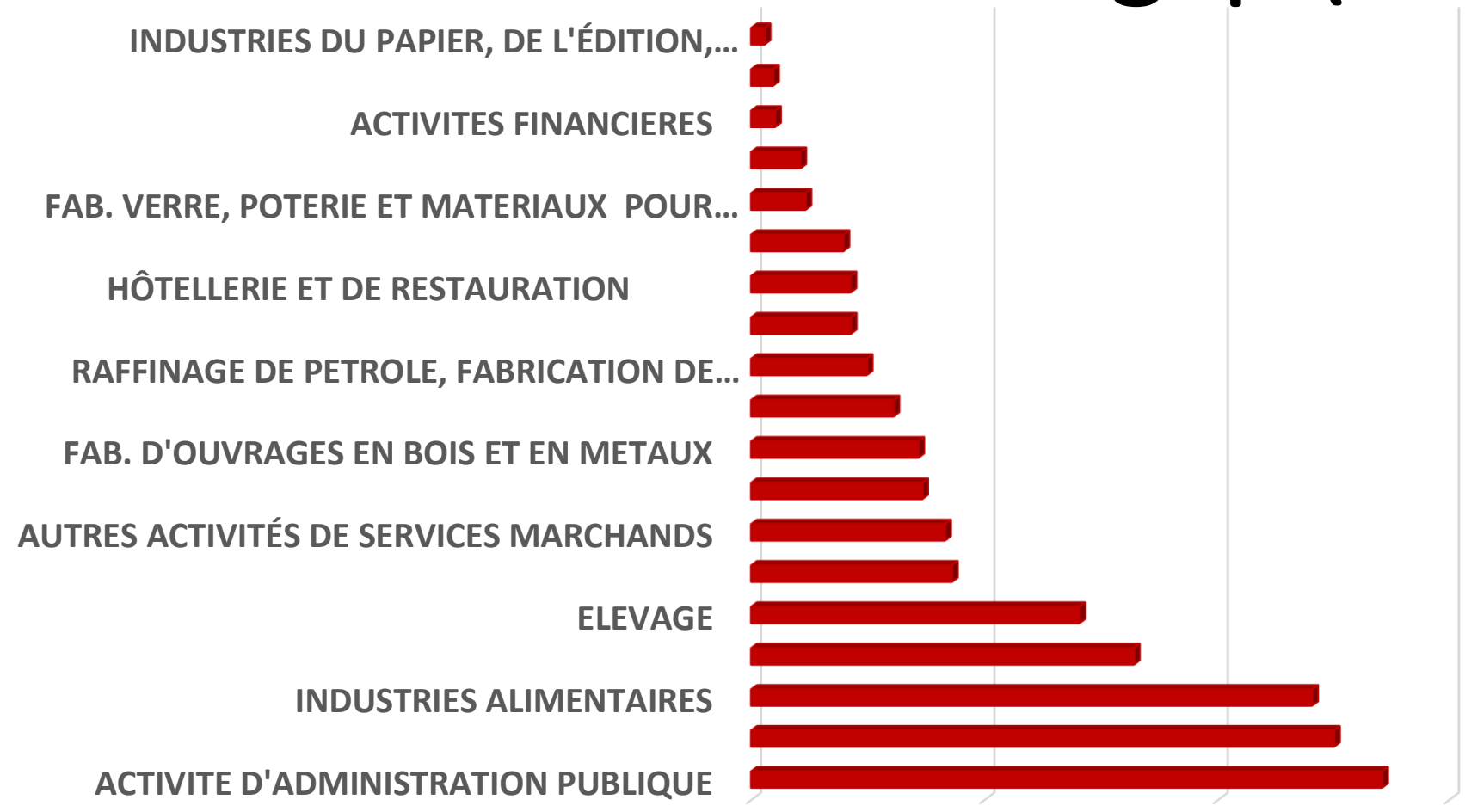
III.

Sources of VAT Inefficiencies: Case study in Burkina Faso

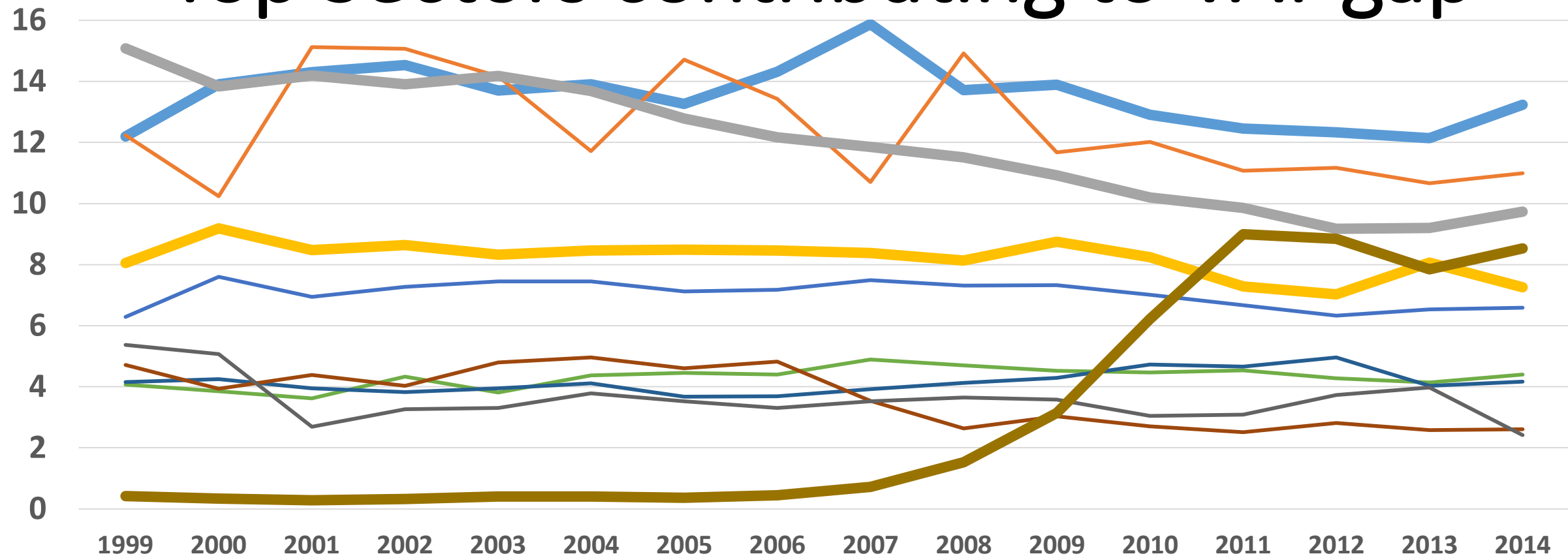
VAT efficiency (Selected partner countries)



Sectoral Sources of VAT gap (1999-2014)

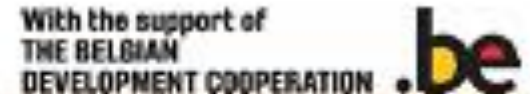
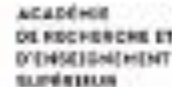


Top Sectors contributing to VAT gap

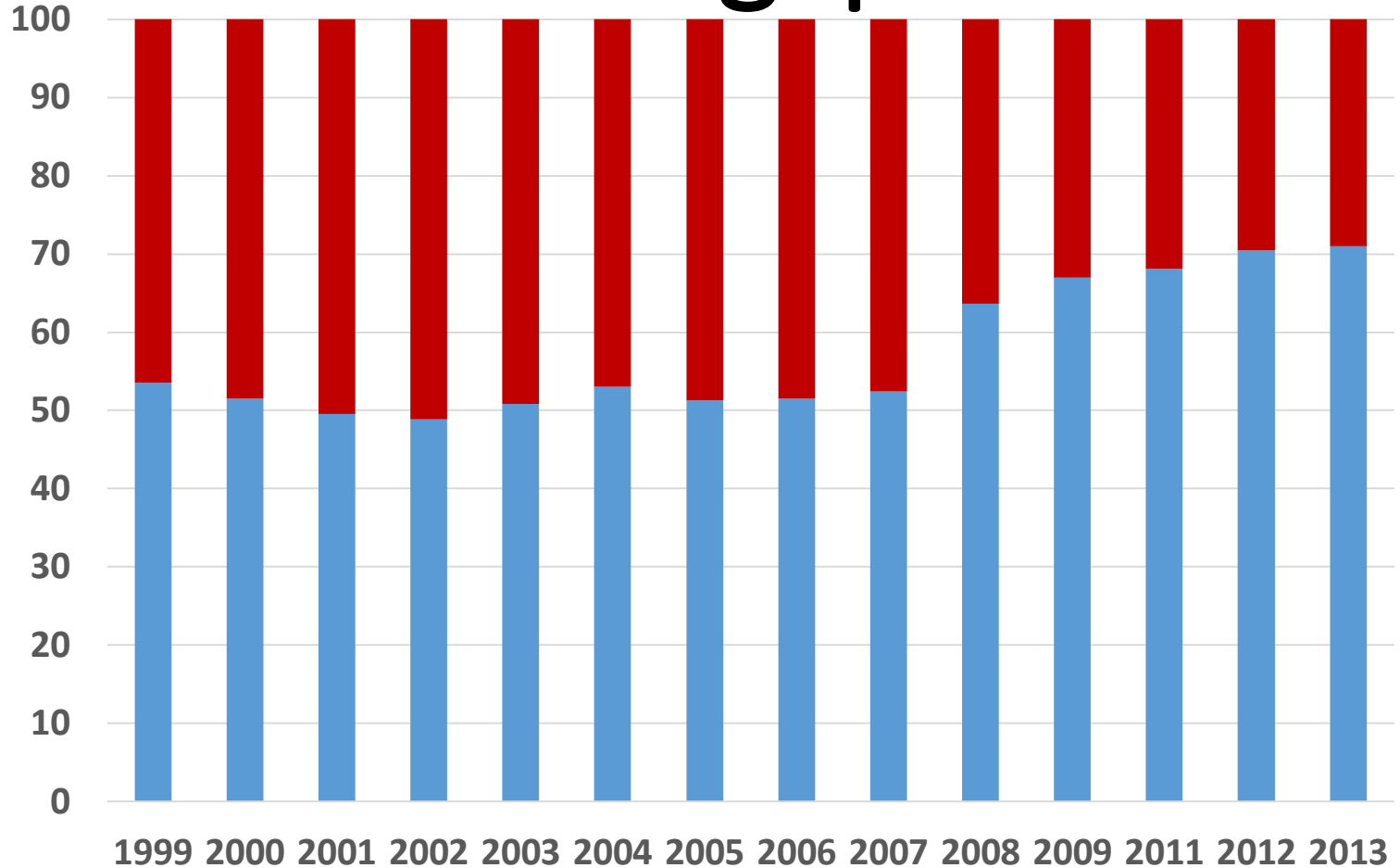


- ACTIVITE D'ADMINISTRATION PUBLIQUE
- INDUSTRIES ALIMENTAIRES
- ELEVAGE
- AUTRES ACTIVITÉS DE SERVICES MARCHANDS
- FAB. D'OUVRAGES EN BOIS ET EN METAUX

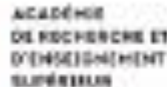
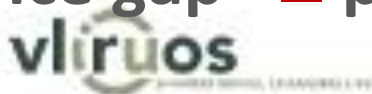
- AGRICULTURE
- COMMERCE
- TRANSPORTS, POSTES ET TELECOMMUNICATIONS
- EGRENAGE DE COTON, FABRICATION DE TEXTILES ET ARTICL. D'HABILL..
- EXTRACTION



Sources of VAT gap



■ compliance gap ■ policy gap



IV. Concluding remarks

What role can donors (Belgium) play?

- Conduct more (in depth) studies to identify sources of tax gaps and policy experiments
- Contribute to the capacity building of the tax authorities and statistical offices
- Encourage/Support institutional reforms that facilitate good governance and the provision of public goods

Thank you!