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Conference Item [eg. keynote lecture, etc.]

Original citation:
This version available at: http://eprints.lse.ac.uk39870/

Available in LSE Research Online: [January 2012]

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Local taxation and institutional accountability in Rwanda’s growing cities: the case of Kigali

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IPAR Annual Research Conference
Kigali, 7th-9th December 2011
Structure of presentation

1) Taxation, state-building & accountability in theory
2) Fiscal decentralisation in Rwanda
3) Kigali local revenues in comparative perspective
4) Detailed breakdown of local revenues
5) Performance of the three decentralised taxes
6) Strengths, weaknesses, opportunities and challenges
Taxation, state-building and accountability: a virtuous circle?

• Taxation is considered central to building state capacity in both theory and historical experience

• Two-way relationship between taxation and accountability

• Importance of ‘fiscal social contract’ (Moore)

• ‘Quasi-voluntary compliance’ (Levi): effective taxation depends on government legitimacy & credibility as well as state capacity
Taxation can fulfil multiple functions

- Building bureaucratic capacity
- Building accountability
- Increasing citizen engagement with public affairs
- Stabilising the economy
- Incentivising /discouraging particular types of investment
- Regulating economic activity
- Redistributing wealth
- Discouraging dangerous/undesirable activity
- Decreasing dependence on aid/increasing autonomy

Even if the intention of a tax relates to just one of these, it may affect some of the others as well.
Which taxes are suitable for decentralisation?

• Effective decentralisation of service delivery requires *fiscal* decentralisation, not just dependence on transfers

• Taxes relating to stabilisation functions (e.g. tariffs & VAT) are not suitable for local authorities; they are too cyclical

• Most taxes relating to distribution are not considered suitable: can exacerbate regional inequalities if wealth moves to areas with lower taxes

• But distributive taxes relating to *immobile assets* (land & property) are considered highly suitable for decentralisation

• So are business licenses and user fees for services
Fiscal decentralisation in Rwanda

- 3 taxes were decentralised by Law No. 17/2002 (along with various fees). What are the characteristics of these 3 taxes?

  - **Property Tax:** in theory is non-distortional, efficient & progressive; but also difficult to administer
  
  - **Rental Income Tax:** linked to immobile assets (property) & potentially very lucrative, but difficult to capture; not often decentralised
  
  - **Business Licences:** relatively straightforward to collect; tends to also have a regulatory function, which can sometimes conflict with its revenue-raising objectives

- **District authorities in urban areas offer particular potential for raising these taxes, and need to maximise them due to especially large service delivery mandates**
Rwanda: local taxation in national perspective

• RRA has been very successful: highly motivated and competent; enjoys strong government support

• RRA success reflects its high levels of bureaucratic capacity, but also government legitimacy, motivation & credibility

• How does local taxation relate to this national picture?

• RRA is model revenue authority for Africa, and Kigali has been called a ‘model city’. Could Kigali also provide a model in terms of effective local revenue collection?
Kigali: local revenues in comparative perspective

- Kigali collects more local taxes per capita ($14) than Kampala ($11), & local revenues have grown more steadily

- Local revenues remain under 50% but grew in all 3 districts
Kigali: local revenues in comparative perspective

Local revenues and transfers, Kigali’s three districts combined

- **a) Absolute figures (RWF)**

- **b) As a percentage of total**

Local taxes grew as % of total city revenues, while in Kampala transfers have grown much faster than local taxes
Breakdown of Kigali districts’ local revenues

**Kicukiro (Jan-Sep 2009)**

- Property tax: 2%
- Rental income tax: 7%
- Trading licence: 9%
- Rent on plots: 21%
- Fees and other income: 44%

**Nyarugenge (2008)**

- Building permits: 0%
- Notary charges: 9%
- Billboard tax: 1%
- Rent on shopping centres: 1%
- Mkt fees: 3%
- Admin fees: 6%
- Rental Income Tax: 12%
- Trading licence: 18%
- Rent on plots (arrears): 1%
- Other revenues: 42%
- Fines and Penalties: 1%

**Gasabo (2008)**

- Property Tax: 4%
- Rental income tax: 12%
- Trading Licence: 11%
- Admin and other fees: 31%
- Rent on Plots: 33%
- Market Fees: 5%
- Notary Charges: 3%
- Billboard tax: 1%
Breakdown of Kigali districts’ local revenues

- Much revenue in Kigali’s districts comes from various fees, rent on plots, and sale of district assets.
Breakdown of Kigali districts’ local revenues

- Nyarugenge District local revenue composition, 2007-2009
Performance of the 3 decentralised taxes

1) Trading licenses
   • These have performed best & most consistently: 85-95% of businesses are registered and pay this tax
   • Already almost ‘saturated’, so potential increase is limited
   • Issue of size differentiation within categories of business

2) Rental income tax
   • Has been increasing fast in all districts (both in terms of registered taxpayers and absolute sums collected)
   • Report was inconclusive regarding whether districts or RRA were more effective in collecting this tax
   • Potential to increase even more due to large rental market
   • May be difficult to distinguish rental from other income
Performance of the 3 decentralised taxes

3) Property tax

- Remains the most limited: amounts to around 12% of the three decentralised taxes, and 3% of all local revenue
- Very small increases each year and sometimes decreases
- Only around 1000 people registered in whole city
- Holds great potential: PT amounts to 20-30% of revenue in many African countries, and more in many other regions

- Lack of capacity for market-based valuation
- Valuation is expensive; has to be balanced against benefits
- Given the scale and pace of Kigali property boom, the more time that passes, the harder it will be
High dependence on non-fiscal revenues: does it matter?

• Around 70-80% of local revenues in Kigali are from sources other than taxes (i.e. non-fiscal)

• Potential reasons why this may be problematic
  • Sustainability of certain sources over time
  • Fluctuations in certain sources may make them unreliable
  • Possible implications for accountability and state-building

• The only way to raise ratio of taxes to other revenues may be through RIT and PT

• User fees?

• To what extent should local taxes be tied to development vs recurrent expenditure?
Strengths & weaknesses of existing system

• Local revenues already high compared with some countries
• Impressive on business licensing, formalising the economy
• National government is supportive of local authorities
• District revenue systems are becoming streamlined at KCC
• Dependence on transfers still quite high (which may impede local state-building and accountability)
• Some revenue sources may lack sustainability over time
• The most progressive local taxes have a relatively small share
Opportunities and challenges

• PT and RIT are closely linked & can be improved in concert

• New titling system should increase property tax revenues

• The fact that local revenues are increasing overall may facilitate greater accountability/civic engagement

• Trading licenses may have limits as a local revenue source

• Low/non-market based PT may encourage speculation on property at the expense of other forms of investment

• Districts’ capture of rental income tax remains uncertain

• Potential confusion over relationship between property tax & land tax (rent on plots) under new titling system