BUILDING TRUST IN THE TAX SYSTEM
A NEW APPROACH

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Innovations in Tax Compliance

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Overview – The EFT Conceptual Framework

- Tax Compliance
  - Political Support for Reform
  - Enforcement
  - Facilitation
  - Tax Morale
  - Norms
  - Values
  - Trust
Overview – The Diagnostic Toolkit

Compliance problem

- Technical assessment
- Taxpayer trust survey
- Political economy analysis

Binding constraints (technical/political)

Recommendations for (joint) investments in Enforcement, Facilitation and Trust
Innovations in Tax Compliance

Conceptual Framework

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Traditional Theory of Change

- Political Support for Reform
- Enforcement and Facilitation
- Expanded Tax Compliance
- Fiscal Contract
An Alternative Theory of Change: Adding Trust

- Political Support for Reform
- Enforcement
- Facilitation
- Trust
- Expanded Tax Compliance
- Fiscal Contract
- Fairness
- Equity
- Reciprocity
- Accountability
An Alternative Theory of Change: Adding Politics

Tax Governance Outcomes: Reciprocity and Accountability

Political Support for Reform
- Enforcement
- Facilitation
- Trust

Fiscal Contract
- “Enforced” Compliance
- “Quasi-voluntary” Compliance

Tax System Outcomes: Fairness and Equity
Diagnostic Toolkit: 3 Modules

1. **Technical binding constraints assessment**
   - Develop a decision tree laying out all potential causes of suboptimal performance;
   - Systematically identify which causes are most important;
   - Identify binding constraints based on likely gains and importance for other actions.

2. **Taxpayer trust survey**
   - Citizen’s perspective on tax compliance
   - Covering taxpayer attitudes, taxpayer experience, tax morale
   - Often includes survey experiments

3. **Problem-focused political economy analysis**
   - Assess political constraints on reform
   - Identify politically feasible reforms
   - Inform design of reform strategy
Case Studies: 3 Active Pilots

1. Kaduna State, Nigeria
   - Property Tax
   - Supports DLIs in PforR to Kaduna State @ USD400mln

2. Karachi, Pakistan
   - Cross-border trade
   - Supports DLIs in IPF for the Federal Board of Revenue @ USD400mln

3. Georgia
   - VAT for medium size taxpayers
   - Supports work on informality, possibly DPO
Case Study
Kaduna, Nigeria: Context

Focus:
- Property tax compliance assessment in Kaduna State
- Should be major source of internally generated revenue (IGR)
- In 2017 good for <1% of IGR

Ongoing reforms:
- PT moved from local level (LGA) to state level (KADIRS)
- Heavy investment in IT systems
- Harmonization of tax law

EFT analysis:
- reprioritized the direction of short term reform towards;
  - investments in robust front-line administrative systems;
  - improved facilitation by lowering information-related transaction costs;
  - strengthening trust, specifically through investments in fairness.
Kaduna, Nigeria: Mapping the Constraints

**Land use charge**

- **Policy**
  - **Land Titling**
  - **Tax Laws**
    - Simplification and Rationalization of Taxes
    - Successful Simplification and Consolidation of Laws
  - **Tax Assignment**
    - Imperfect Harmonization between LGA and KADIRS for collection, despite legal assignment to KADIRS

- **Harmonization between agencies**
  - Lack of Harmonization between KADIRS and other relevant agencies

- **Property valuation**
  - No valuation policy
  - Unclear capacity for valuation

- **Technical capacity for tracking payment (Billing/collection)**

- **Compliance**
  - Property identification divorced from valuation/Land Use Charge
  - Weak enforcement
  - Weak voluntary compliance
  - Incomplete spatial cadastre

**Administration**

**Technical capacity for property identification**
Kaduna, Nigeria: the Binding Constraints
Conclusion

What is new?

1. Analyzing local drivers of trust
   - Links to compliance and political support for reform
   - Operationally relevant dimensions

2. Practical political economy
   - What are the most important political barriers to reform
   - How can reformers navigate these barriers

3. Move from gaps to bindings constraints

What is next?

1. Further empirical validation through more pilots
2. Expand operationalization of trust-related interventions
Georgia: Work in progress

Focus:
- VAT compliance among SMEs firms
- Compliance gap sizable, but declining
- Suggestive evidence that it is mostly located SME sectors
- Significant unclaimed VAT credits

Ongoing reforms
- From heavy-handed enforcement to (extreme) facilitation
- Introduction of data analytics and risk-based auditing
- Automatic VAT refunding

Preliminary EFT analysis:
- Significant gains, but …
- Extreme facilitation might be undermining equity
- Taxpayers are maintaining a wait-and-see position towards recent reforms
- Dual approach to reducing stock of VAT credits is affecting perceived fairness
Kaduna, Nigeria: Citizens’ Perspectives

1. **Compliance**
   - 66% reported paying property taxes

2. **Enforcement**
   - Majority reports that evading taxes is (very) difficult

3. **Facilitation**
   - Only 7% managed to name both taxes they are supposed to pay

4. **Morale**
   - A majority believed that citizens have an unconditional obligation to pay tax, but understand evasion
   - Trust in KADIRS is higher than in LGA, but the level is low
   - LGA assessment negotiable almost twice as frequently compared to KADIRS
   - KADIRS is thought to treat taxpayers more fairly than LGA

Survey results suggest importance of:
1. improving facilitation by lowering information-related transaction costs
2. strengthening trust, specifically through investments in fairness
Kaduna, Nigeria: Recommendations

EFT analysis *reprioritized the direction of short term reform* towards investments in robust front-line administrative systems, coupled with targeted facilitation measures and trust building strategies, to ensure efficient use of transformative investments in IT:

1. **Investments in enforcement**
   - Increase the number and capacity of KADIRS staff in key local tax offices
   - Build capacity to improve distribution and tracking of demand notices

2. **Investments in facilitation**
   - Improve communication to taxpayers about tax obligations

3. **Investments in trust**
   1. Effective implementation of property tax collection by KADIRS (only);
   2. Improve fairness of collection;
   3. Operationalize the Tax Tribunal;
   4. Improve reciprocity by prioritizing capital investment;
   5. Improve accountability for example via popular participation in budgeting.