Agricultural Taxation in Tanzania:
With special reference to produce cess

Inception Report on Key Issues and Study Design
Michigan State University
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Acknowledgement

- **USAID** for financial support
- Ministry of Agriculture for providing MSU a chance to contribute in promoting evidence based policy making
- PMO – RALG for making data available
- ACT and the World Bank for pioneering studies on produce cess
- All key stakeholders for raising key issues that help shaping the study design
Background

- Crop cess established under the 1982 Local Government Finance Act
  - With amendments in subsequent years
  - Part of the decentralization programme

- Has long sparked concern regarding impact on
  - Agriculture competitiveness
  - Market distortions

- In 2012, GoT committed to eliminate cess by July 2013
  - Under G8 New Alliance on Food Security and Nutrition
But strong opposition from LGAs and PMO-RALG
- Why the focus just on cess?
- How will the foregone revenue be made-up?
- What about decentralization?

MSU requested by the Ministry of Agriculture to provide technical support
- Fill information and analytical gaps from previous studies

Much political economy in the issue, hence need for:
- Evidence-based policy dialogue
- Consensus building
Previous Analytical Studies

- World Bank, 2009 – Tanzania – A study of the burden of local taxes on the agricultural sector
- Agricultural Council of Tanzania, 2012 – A study on produce cess taxation system in Tanzania
- Analytical pieces by TAHA (2013) and USAID (MicroCLIR, 2011)
Issues of Concern in Produce Cess

- **Taxation rate**
  - Affects competitiveness of value chains and levels of tax evasion

- **Effectiveness and efficiency of cess administration**
  - Raises transactions costs of market participants, can increase uncertainty

- **Differences in practice across LGAs**
  - E.g. differences in cess rate on same product in neighboring LGAs
  - Distortions in market behavior?
Issues of Concern in Produce Cess (2)

- **Accountability** in tax administration and expenditure
  - How is the money used?
  - “Value for money”

- **Misinterpretation and lack of clarity** of the Produce Cess Act
  - Divergence between the Act and actual practice, e.g.
    - Should seed be taxed?
    - Double taxation (e.g. paddy vs. rice)
    - Implementation at “farm level” but “buyers” must pay

- **Statutory versus economic incidence**
  - Who really pays the tax after prices adjust?
Key Stakeholders and Divergent Opinions

- **LGAs** – Support produce cess as a key source of revenue; some is re-invested to support agriculture

- **Civil society** – Produce cess important for empowering LGAs to take leadership and define development agenda; have some reservations in tax administration

- **Tanzania Revenue Authority** – farmers need to contribute something for the development of their country; salaried workers pay up to 30% of income
Key Stakeholders and Divergent Opinions (2)

- **Agribusiness** – cess adds to already high tax burden, increases cost of doing business

- **Farmers** – regardless of who pays the tax, eventually the tax is passed to farmers in form of low producer price

- **GoT** – Claims by LGAs of importance of the tax are not supported by share of revenue as shown in the audit reports; **leakages** seen as major problem
The Essential Challenge

- Decentralization has little meaning without ability to raise and spend funds locally
- Society has right to expect that
  - Revenue collection be efficient, honest, and equitable
  - Expenditure be productive and equitable
  - The entire process be transparent
- Very difficult challenges in the physical, technological, and social setting of rural Tanzania/SSA
The Essential Challenge (2)

- So:
  - What kind of performance is reasonable to expect?
  - How can it be continuously improved?
Insights from recent interviews

- Abolition is problematical
  - Wide range of dependence on cess revenue
    - Need to understand patterns
  - Agriculture a huge portion of the economy
    - Can the country afford not to tax it?
  - Sense at local level that central government does not fully replace revenue from abolished taxes
    - E.g. development levy
  - What are the possibilities for incremental improvement?
    - Capacity building for responsible local governance
    - Technology to improve efficiency of collection, reduce leakages
Insights from recent interviews (2)

- Yet rates can be big expense for some
  - Export horticulture: cess calculated on export price, not farm price
  - Seed companies
    - Lack of clarity in Act
  - Other large companies, large-scale farmers
  - When prices decline, effective cess rate rises
    - See next slide
  - Higher effective rate on gross margins
    - Effectively a tax on input use
Insights from recent interviews (3)

- And varying practice leads to distortions
  - Traders favoring areas with lower cess
  - *Lumbesa*

- Wide range in difficulty of administration
  - Cash crops relatively easy
  - Maize, rice much more difficult because largely informal
Insights from recent interviews (4)

- Wide range in difficulty of administration (cont’d)
  - Typical practice: convert % cess into fixed rate
    - And apply same fixed rate to all crops
    - Results in highly variable % charges (rice example)
    - *Driven by limited capacity and limited information*
  - How to reduce avoidance??
Insights from recent interviews (5)

- Wide range in difficulty in administration (cont’d)
  - Outsourcing very common
    - Common to specify fixed pmt per month
    - Many incentive problems
    - Would mobile money payments address these?
Insights from recent interviews (6)

- Credibility / legitimacy of local governments
  - Perceived large leakages / corruption
  - What is the money spent on? (80/20)
  - CAG Audit Reports focus only on books
    - “Value for money” audits done only upon complaint
    - What about doing random value-for-money audits?
    - Can central government reward good behavior and performance with matching grants, awards, public recognition?
      - “The Annual 10 Best LGA Administrations in Tanzania”
Insights from recent interviews (7)

- Burden of paying the tax before sale is made
- Availability of data
  - Data from Council Financial Reports for every LGA available on the web
  - *Great transparency!*
  - Epicor does not always well reflect actual activities of LGAs – needs more tuning to capture reality at LGA level
Objectives

- Examine patterns in levels of, and reliance on, cess across LGAs using national LGA-level data
  - Capture and understand heterogeneity

- Document commonalities and differences in cess administration across a sample of LGAs
  - Compare practices to Produce Cess Act
  - Assess effectiveness and efficiency
Objectives (2)

- (If data allow) Estimate price distortions generated by differing practice across LGAs
- Estimate likely range of economic incidence of cess
  - Who pays how much after prices adjust?
- Clearly reflect opinions of a range of stakeholders
  - SHF
  - commercial SHF
  - large-scale commercial farmers
  - agribusiness firms (including seed firms)
  - LGAs, central government, civil society
Objectives (3)

- Assess pros and cons of several concrete options
- Actively engage stakeholders in discussion of results and options
Tax Reform Options for Appraisal

- Abolish in one step
- Gradual phasing out
- Reduce rate, broaden base, improve collection
  - Mobile money
  - “Item cards”
  - Improved incentives in contracts with private collectors
- Institute tax differential between food- (rice and maize) and non-food crops
- Complete removal in food crops
Timeline

- February 1 – 15: Synthesis of previous studies, secondary data analysis and field survey logistics
  - Initial Policy Brief
- February 16 – March 16: Field survey
- March 17 – March 31: Draft report
- April – Peer review and targeted stakeholder consultation
- May – Stakeholders’ workshop and final report
- June – Support legislative process
- July 2014 – July 2015 – Follow on studies
Study Team

- David Nyange, MSU Policy Advisor to MAFS – Lead researcher
- David Tschirley, MSU – Counterpart Lead Researcher
- Francis Gasper, Hussein Nassoro – Consultants
- Iddy Alfan, MAFS – Tax reforms task force
- Stella Steward, PMO-RALG – Data resource person
- MSU back up team (Mark Skidmore, David Mather, Eric Scorsone)
- MAFS/PRC back up team (Daktari Hango, Esther Mutatemwa)
Thank You!
Questions/Issues for Discussion

- Have we raised the right issues? Left out?
- Value chain and LGA selection (David Nyange)
- Any other data sources?
- Any left out stakeholder?
- Study timeline versus the legislative process
  - Key intervention points?
- Feasibility of electronic payment methods
  - Require or reward?
  - Practical issues of implementation
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<tr>
<th>ZONE</th>
<th>REGION (LGAs)</th>
<th>CROPS/Farming system</th>
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<td>Northern zone</td>
<td>Arusha (Arumeru)</td>
<td>Coffee, Horticulture</td>
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<td>Kilimanjaro (Moshi rural)</td>
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<td>Tanga (Muheza)</td>
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<td>Central zone</td>
<td>Dodoma (Kongwa)</td>
<td>Sorghum, oil seed, maize</td>
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<td>Singida (Singida)</td>
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<td>Southern highlands</td>
<td>Morogoro (Kilombero)</td>
<td>Rice, sugar cane, tea, livestock</td>
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<td>Njombe (Njombe)</td>
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<td>Mbeya (Mbaralî)</td>
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<td>Lake zone</td>
<td>Shinyanga (Kahama)</td>
<td>Cotton, livestock, rice</td>
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<td>Mwanza (Kwimba)</td>
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<td>South cost</td>
<td>Lindi (Lindi rural)</td>
<td>Cashew, cassava</td>
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<td>Mtwara (Masasi)</td>
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<td>Western zone</td>
<td>Tabora (Urambo)</td>
<td>Tobacco, maize, livestock</td>
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<td>Rukwa (Sumbawanga)</td>
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