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Working Paper

Municipal tax base in Mozambique: high potential – low degree of utilisation

Discussion Paper, No. 1/2012

Provided in Cooperation with:

German Institute of Development and Sustainability (IDOS), Bonn

Suggested Citation: Weimer, Bernhard (2012) : Municipal tax base in Mozambique: high potential – low degree of utilisation, Discussion Paper, No. 1/2012, ISBN 978-3-88985-544-2, Deutsches Institut für Entwicklungspolitik (DIE), Bonn

This Version is available at:

<https://hdl.handle.net/10419/199370>

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Discussion Paper

1/2012

Municipal Tax Base in Mozambique: High Potential – Low Degree of Utilisation

Bernhard Weimer

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Bernhard Weimer

Discussion Paper / Deutsches Institut für Entwicklungspolitik
ISSN 1860-0441



Die deutsche Nationalbibliothek verzeichnet diese Publikation in der Deutschen Nationalbibliografie; detaillierte bibliografische Daten sind im Internet über <http://dnb.d-nb.de> abrufbar.

The Deutsche Nationalbibliothek lists this publication in the Deutsche Nationalbibliografie; detailed bibliographic data is available in the Internet at <http://dnb.d-nb.de>.

ISBN 978-3-88985-544-2

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Acknowledgements

This study draws on work produced by a team of researchers involved in a joint research project on municipal taxation. The fieldwork was carried out from June to December 2010 within the framework of the Joint Municipal Support Programme to 13 municipalities in Central and Northern Mozambique (P-13)¹ in collaboration with the World Bank. The author would like to acknowledge Jamie Boex (Urban Institute, Washington, D.C.), Uri Raich (World Bank), Ozias Chimunuane (P-13), Minoz Hassam and Sven Hindkjaer (consultants), as well as Hans Erskog (DANIDA, Maputo) for their contributions, which arose from joint research, discussions and writings.

The author would also like to express his gratitude to all those municipal and central government officials in Mozambique as well as his former colleagues in P-13 and in the Swiss Agency for Development and Cooperation (SDC) for their continuous support to this study, as well as for permission to use the data gathered in the course of the research project.

His gratitude is extended to the directors and staff of the Deutsches Institut fuer Entwicklungspolitik (DIE), Bonn, for hosting him as a guest researcher for three months, and for the conducive work environment and fruitful discussions on matters of taxation and decentralisation, among others. He would like to extend a special thank you to the colleagues Joerg Faust, Christian von Haldenwang, Armin Schiller and Julia Leininger from DIE's Division III (Governance, State and Security) for their guidance and help during the research stay at DIE and the production and review of this paper. To Julia a special *muito obrigado!* Finally, I like to thank Robert Furlong and Gisela Kuhlmann for their excellent support during the editing process.

Bonn, January 2012

1 The Programa Conjunto de Apoio à 13 Municípios na Zona Centro e Norte (P-13) was hosted from October 2008 to June 2011 at the Centro de Desenvolvimento Sustentável – Zonas Urbanas of the Ministry of Coordination of Environmental Action (Ministério de Coordenação da Acção Ambiental) in Nampula City in northern Mozambique, and has been funded by the Austrian Development Cooperation (ADC), the Danish International Development Agency (DANIDA) and the Swiss Development Cooperation (SDC).

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Abbreviations

ADC	Austrian Development Cooperation
AR	Assessment / Applied Ratio
ATM	Autoridade Tributária de Moçambique (National Tax Authority)
CLR	Collection / Compliance Ratio
CTA	Código Tributário Autárquico (Municipal Tax Code)
CVR	Coverage Ratio
DANIDA	Danish International Development Agency
DIE	Deutsches Institut fuer Entwicklungspolitik
DUAT	Direito de Uso e Aproveitamento da Terra (Land Use Right)
IAV	Imposto Autárquico sobre Veículos (Vehicles Tax)
INE	Instituto Nacional de Estatística (National Statistics Office)
IPA	Imposto Pessoal Autárquico (Head/Poll Tax)
IPRA	Imposto Predial Autárquico (Property Tax)
IRN	Imposto de Reconstrução Nacional (National Reconstruction Tax)
ISISA	Imposto Autárquico de Sisa (Municipal Property Transfer Tax)
MC	Municipal Council
MT	Metical (Mozambique currency)
P-13	Joint Municipal Support Programme to 13 Municipalities in Central and Northern Mozambique
PROGOV	Projecto de Governação Autárquica Democrática
SDC	Swiss Agency for Development and Cooperation
SUC	Serviços de Urbanizacao e Cadastro (Cadastre and Urbanisation Services)
TA	Tribunal Adminstrativo (Administrative Tribunal)
TAE	Taxa por Actividade Económica (Economic Activity Tax / Fee)
TB	Tax Base
TE	Tax Effort
TR	Tax Rate
UP	Unrealised Revenue Potential

Executive summary

Fiscal decentralisation and financial and fiscal autonomy are key features of the municipalisation process in Mozambique's 34 municipalities. Endowed with a wide range of typical local government functions (provision of basic services, management of land, solid waste management, etc.), their resource base follows the logic of integrated fiscal decentralisation: together with their entitlement to annual transfers from central government (general non-purpose and conditioned grants), the municipalities can count on a considerable revenue base of their own. Although the reform of local governance finances in 2008 reduced central government transfers in the form of the Intergovernmental Compensation Fund from 3 to 1.5 per cent of annual domestic revenue, it conceded the municipalities a wide range of own local revenue sources, ranging from concession of land use rights, a property and property transaction tax via a vehicle tax to non-fiscal sources of revenue related to economic and market activities, as well as user fees for municipal services. Own source revenue (fiscal and non-fiscal revenues and user fees) make up 37 per cent of all municipal revenue, with 48 per cent stemming from central government transfers and 15 per cent from donations (average of all municipalities). The percentage of fiscal revenue in relation to total own source revenue is below 15 per cent. With a cap on central government grants – which are low by any standards – and their ineligibility for access to the capital market and the planned increase of the number of municipalities, their hope for increased central government transfers seems to be a rather unlikely prospect for solving the existing gap between available resources on the one hand, and the need to fulfil their core business – i.e. improved coverage and quality of public services – on the other. Part of the solution lies in tapping into the considerable, underutilised own source revenue potential.

In taking up strands of relevant literature on fiscal decentralisation and local revenue generation, the present study explores three questions. Firstly, what are the fiscal characteristics (base, taxation rates, collection modalities, etc.) of the municipal revenue base? Secondly, what are the main reasons for its underutilisation. Thirdly, what would be necessary steps to successfully tap into the existing revenue reserves?

In seeking to answer these questions, the author reviews and discusses the findings of six case studies conducted in 2010/2011 and produced through extensive fieldwork on municipal revenue administration and patterns. They were part of a governmental municipal support programme in Mozambique financed by Austrian, Danish and Swiss development agencies and were executed in collaboration with the World Bank. The key features of seven types of own source revenues (four fiscal and three non-fiscal sources) are discussed, and the effort of collecting them is examined, case by case, across the sample of the six case studies. Three criteria for the assessment of the effort are used: a) the quality and coverage of tax registers / cadastres ("coverage ratio"), b) the assessment of the fiscal obligations of tax payers ("assessment ratio") and c) the degree by which taxpayers comply with their obligations ("compliance ratio"). This method allows for estimating the total revenue potential by type of revenue on the basis of the revenue yields in 2009; in other words, the unutilised reserves of own source revenue potentially available to the municipalities is being estimated.

As to be expected, the results show that the (untapped) revenue potential varies across the sample according to the size, localisation and age of the municipalities, the existing type of urbanisation, the institutional capacity of the municipal tax administration and other factors. In a way, each of the municipalities examined tells its own circumstantial story about revenue collection policies, priorities and results. Despite these variations, there are common features: revenues from market

fees generally contribute proportionally more as compared to the effort and thus have less (non-utilised) potential, whereas revenue from property (and property transactions) is rarely collected, with the exception of a major provincial capital city, Beira, which has recognised the potential buoyancy of property taxes and has invested in its institutional capacity to collect them. The poll tax – a politically unpopular tax that has connotations to the colonial coercive taxation practices – is rarely collected in all sample municipalities. In the case of recently decentralised taxes on vehicle and property transactions, the effort and potential illustrate somewhat erratic practices. This is attributed to the fact that the central government has not yet fully transferred the instruments and databases for the collection of these taxes to the municipalities. A comparison between a good and less-well-performing municipality shows that the better performing local government has made strategic investments in the institutional capacity of land management (cadastre) and its revenue administration, together with the leadership qualities of the mayor.

The own source revenue with the highest unutilised potential is clearly the property tax, followed by the property transaction tax and the poll tax. In comparison, the non-fiscal revenue base (markets and business activities) are utilised much more. On aggregate terms, the (sample average) unused own source revenue potential is 1.5 times the total own source revenue yield (in 2009) or equivalent to half of total revenue (including transfers) in that year. These figures show that, theoretically, Mozambican municipalities have considerable revenue reserves they could tap into for the financing of basic services. To do so requires, from a technical perspective, investments in improving the institutional capacity for land- and property-related taxation, notably in the case of rapidly urbanising municipalities. However, there is a political economy dimension involved: property-related taxes (where the reserves are highest) touch on the established power structure and thus may not be popular with the local elite dominating municipal politics and policies. Continued emphasis by politicians on the increased use of the revenue reserve identified for the poll tax (with strong regressive effects) and the emphasis on conventional non-fiscal revenue (market and business fees) pose a different political challenge in a country where a considerable number of urban dwellers live in poverty and expect improved coverage and quality of basic public services, as well as opportunities for economic activities and employment. Thus, the municipalities face a dual dilemma, with a political price concerning the legitimacy of municipal governments attached to each: on the one hand, ignoring own revenue potential does not result in improved services; on the other hand, the increased use of own source revenue cannot be employed without equal considerations and corresponding services that are commensurate with the increased tax burden. Overcoming these dilemmas requires, in the author's view, a kind of municipal tax compact, not only between government and citizens, but also across the strata of society, in the sense that revenue increases stemming from the hitherto underutilised sources are translated into improved services and quality of municipal life for urban dwellers. Participatory approaches to planning and budgeting may contribute to such a solution.

1 Introduction and context

Fiscal decentralisation and financial and fiscal autonomy are key features of the municipalisation process in Mozambique. Endowed with a wide range of typical local government functions (provision of basic services, management of land, solid waste management, etc.), the resource base of the municipalities follows the logic of integrated fiscal decentralisation (Faust / von Haldenwang / Neidhardt 2009). Together with their entitlement to annual transfers from the central government, the municipalities can count on a considerable revenue base of their own, consecrated by law and sanctioned by the reform of local governance finances in 2008.² The latter resulted, on the one hand, in a reduction of central government transfers – via the Intergovernmental Compensation Fund – from 3 to 1.5 per cent of annual government domestic revenue.³ On the other hand, it conceded to the municipalities a wider range of local revenue sources, ranging from concession of land use rights, property and property transaction taxes via a vehicle tax to non-fiscal sources of revenue related to economic and market activities, as well as user fees for municipal services.⁴

However, as a broad and in-depth study on the first decade of municipalisation in Mozambique – its achievements and challenges – reveals, the generation of sufficient own revenue by local councils is one of the shortcomings diagnosed (ANAMM / World Bank 2009, 113 ff.). In 2006, revenues from the municipalities' own revenue base represented around one-third of their total revenue, which, with annual per capita of less than US\$ 10, is considerably low by all standards (ANAMM / World Bank 2009, 99). This low degree of utilisation of their own tax base might not be surprising: first, Mozambique as a whole has been relying on foreign aid to the tune of around 50 per cent of its annual budget during the past decade, making it one of Africa's most aid-dependent countries (de Renzio / Hanlon 2008); second, taxation by local African governments is generally not very dynamic, thereby posing many socio-economic, technical and political challenges (Fjeldstad 2001a; Fjeldstad / Therkildsen 2008; Hyden 2007). Mozambique's municipalities are no exception. Yet, if the *raison d'être* of a local government is to provide public services and goods in a more efficient, better-informed and need-oriented way than the central government (Bailey 1999; Bird 1990) and thus contribute to national poverty-reduction plans at the local level (de Jong et al. 1999; Thomsen / Saïde 2011), the low degree of utilisation of their own revenue base poses serious challenges to the municipalities' capacity to fulfil their core business, and thus challenges their legitimacy as well. In Mozambique, these challenges are emphasised through the ever-widening cleavage between municipal resources and expenditures (ANAMM / World Bank 2009).

The present study seeks to answer two questions:

-
- 2 Law 1/ 2008 on Municipal Finances together with Decree 63/2008 (Municipal Tax Code).
 - 3 Thus, donor support to the central government within the framework of the Paris Declaration on Aid Effectiveness, to the tune of roughly 50 per cent of the annual budget, has no direct bearing on the calculation of transfers and on municipal budgets.
 - 4 The net effect between the gains and losses may be detrimental to the municipalities, especially if one takes into account that the incremental increase in the number of municipalities implied in the gradualist approach to decentralisation reduces the share available for each of them (Ilal 2008).

1. What are the sources of revenue available to Mozambican municipalities within the established framework of integrated fiscal decentralisation, and what are their fiscal characteristics (base, taxation rates, collection modalities, etc.)?
2. What are the main reasons for the under-utilisation of the municipalities' own tax base and what would be necessary to tap into the existing revenue reserves?

In addressing these questions, the author endeavours to contribute to a better understanding of the sustainability of municipal development in Mozambique – flagged as a pertinent issue in 1999, when the question was raised of whether the municipalities would be able to “learn to walk without a borrowed walking stick” (Soiri 1999).⁵ At the time, autonomous municipal governments had been in existence only since 1997. They were established in the wake of the profound transformations of the political and economic system following the Rome Peace Process, which ended a 16-year war that had civil and regional dimensions and led to major economic, technical and political challenges (Weimer / Fandrych 1998; Fandrych 2001).

In line with a gradualist devolution approach to decentralisation (Buur 2009), by 2008 a total of 43 municipal governments had been created, with local elections for mayors and assemblies held in 1998, 2003 and 2008. These reproduced – with very few exceptions, also at the local government level – the hegemonic structure of politics in Mozambique, establishing the FRELIMO party, which had ruled the country since independence in 1975, as the dominant political force. These local self-governments, referred to as *poder local* (local power) are restricted to urban areas and include the national and provincial capitals as well as the 33 urbanised centres of the 131 districts. Despite the aforementioned major study on the first 10 years of municipalisation, and the availability of (unpublished) studies on fiscal relations between the central government and the municipalities in Mozambique (Boex et al. 2008), a thorough examination of the local revenue base and its use has been missing. Thus, this and other studies associated with it (Boex 2011) seek to fill an information gap that is relevant not only to the municipalities themselves but also to the dialogue between the central and local governments as well as the dialogues with the donors on fiscal matters.

By examining in some detail the array of local revenue sources available to municipalities and estimating their overall potential, as well as their underutilisation, the author also intends to contribute – in the sense of a case study – to the wider debate on taxation and fiscal decentralisation in Africa, which has merited increasing attention of policy makers, development experts and scholars alike. Authors have examined the question of taxation and intergovernmental fiscal relations from various angles: from that of state-building in developing countries (Fjeldstad / Moore 2008; Prichard / Leonhard 2010), via the relationship between taxation and culture (Edling / Nguyen-Thanh 2006), public sector administrative and fiscal reform (Boex et al. 2008; Bird 2004), public policy (Volkerink 2009), and local governance (Smoke 2007) to donor policies and the Paris Declaration on Aid Effectiveness (von Soest 2008; Faust / von Haldenwang / Neidhardt 2009; Faust / von Haldenwang 2010). In this scholarly literature, matters of local government taxation have been at the margin of attention and research, with few exceptions (Boex / Martinez-Vazquez 2004; Bird 1990). This may be explained by the numerous challenges facing

5 Translation from the Portuguese: *aprender a caminhar com uma bengala emprestada?*

such research, such as access to information on local finances, reliability of data, the understanding of political economy of local governments, and the sheer number of cases one would need to examine to come up with plausible trends and conclusions. Thus, the present study, which dwells on information gathered on the basis of privileged access to about a third of municipal governments in Mozambique, attempts to fill a gap in the research landscape on intergovernmental finances and local taxation.

The following analysis is based on data and information gathered in the context of a multi-lateral, pool-funded programme in support of Mozambican municipalities in the centre and north of the country, commonly known as P-13. In this framework, a considerable database on municipal revenue and expenditure for the years 2004–2009 was produced (see Section 2.2. below). In particular, the study draws on six case studies on municipal revenue potential as well as on a policy-oriented summary report produced through a collaboration between P-13 and the World Bank (Boex 2011).⁶ The author was part of a team of Mozambican and international consultants and researchers who generated the necessary data and contributed to the production of the aforementioned reports.

2 Theoretical considerations

Recent influential literature on the relationship between taxation and state-building assumes that the exploration of a country's own tax base and budgetary process can be considered a key element in the construction or consolidation of a state (Moore 1998; Moore 2008; Braeutigam 2008). One of the arguments is that state-building historically requires taxation, which in turn needs state-society relations that are conducive to revenue generation for the reproduction of the state. Thus, governments need to give voice and representation to “tax citizen” (*Steuerbuerger*) and need to reflect the interests and priorities of their taxpayers in their spending patterns in order to generate sufficient revenue and avoid tax evasion by their citizens. With other words, there must be a “Wicksellian Link” between spending and taxing, in the sense that the benefits of expenditure in terms of public goods and services outweigh the burden of taxation.

Although historically the logic of a reciprocal relationship between the taxing state and the “taxpayer with voice” is not a feature of state-building in colonial and most of post-colonial Africa (Mkandawire 2010; Fjeldstad / Therkildsen 2008; Therkildsen 2001), the pattern and structure of the tax base and the way the taxes and fees are collected and administered has profound implications for the capacity and legitimacy of a local government (Vaillantcourt 2003, 330). While coercive methods of tax collection, like in the case of the poll tax in Tanzania, may trigger revolt and eventually the abandoning of that type of tax (Fjeldstad / Therkildsen 2008) the so-called associational taxation, i.e. the tax collection delegated to associations of business and society on the basis of a bargain, may produce more stable flows of revenue, as in the case of Ghana (Joshi / Ayee 2008; von Soest 2008). The mix of taxes and fees is also an important criterion from the point of view of local citizens: if they receive value for money regarding basic municipal services (refuse collection, water and sanitation, basic infrastructure, security, etc.), and can expect the effective and transparent management of municipal budgets, they will be inclined to

6 For the six case studies, see Chimunuane et al. (2010) and Chimunuane / Hassam / Weimer (2010a, b).

pay taxes and fees (Wampler / Barboza 1999). A survey of five Mozambican municipalities confirms this observation: citizens are even inclined to pay more if the services improve in terms of quantity and quality (de Brito et al. 2007).

The proposition that the increasing use of its own tax potential contributes to the construction and consolidation of the state (Braeutigam 2008) seems to be particularly relevant for the local state and its services, i.e. municipal and other forms of local government, which have been notoriously distant and under-structured in colonial and post-colonial Africa (Herbst 2000). According to this proposition, state construction – in the sense of building effective local government institutions capable of delivering basic services – can happen in at least three ways. Firstly, a better trained and more efficient local tax administration, together with, secondly, the introduction of appropriate technology and databases (computers, registers / cadastres and corresponding software, etc.), might not only trigger or accelerate the emergence of a Weberian local bureaucracy, together with increased municipal planning, budgeting and management capacity⁷; thirdly, it would also provide a local arena for bargaining between local citizens (taxpayers) and the municipal authorities on matters such as investment priorities, tax burden, social justice, etc. Thus, it would give substance to the citizens' voice and empowerment in local government – deemed a necessary criterion for successful decentralisation of local governance and service delivery (Brinkerhoff / Azfar 2010).

While the advantages of fiscal decentralisation and a major role for local governments in service delivery and taxation are generally accepted, major challenges for local government finances are identified.

The first is that municipalities, as part of the public sector, are notoriously under fiscal stress, i.e. they have insufficient resources (both locally generated resources as well as those transferred from the central government) in relation to their tasks. Even in industrialised countries such as Germany, the situation of local government finances is dramatic: mayors even speak of “*the end of local autonomous government*”, despite efficient and transparent management of their budgets and tax base (Slawig 2011).⁸ In many countries of the world and in Africa, the situation is little different, although in African countries municipalities usually do not have access to credit. Most often, the principle that “finance follows function” (Bird / Smart 2002) is not adhered to, so that local governments suffer acutely from a vertical fiscal gap, i.e. they lack the minimal transfer of central government resources necessary for the execution of their statutory tasks.

7 Erdmann and Engel (2006) demonstrated the importance of a Weberian bureaucracy even in neo-patrimonial and clientelist settings. However, it is doubtful, at least on a national level, whether this is a linear or even automatic process (Pritchard / Leonhard 2010) and whether fiscal authorities and local government departments are able to retain professional and well-performing tax administrators (von Soest 2008).

8 The reasons being structural economic and demographic change in many towns (i.e. narrowing of the tax base) coupled with fewer transfers from central government, as well as rising recurrent wage and non-wage expenditures, including maintenance of infrastructure and crippling debt service (Slawig 2011).

Although in the case of Mozambique, the “finance follows function” principle is enshrined in municipal legislation (Law 2/1997; Law 1/2008), the municipalities regularly complain about lack of sufficient transfers from the central government.⁹

Secondly, the lack of sufficient coverage of expenditures through revenues – either locally generated or from transfers – may be caused by local governments’ failure to maintain discipline in spending. Theoretically, central government transfers, which often make up the major part of available resources, especially block grants, are considered as representing a “soft budget constraint” that enables local governments to expand their expenditures without assuming the economic and political costs and risks of the growing fiscal imbalance (de Mello 2000; Rodden / Eskeland / Litvack 2003). As a result, these local governments become increasingly dependent on central government transfers, loans, special appropriations or bail-outs (in the case of highly indebted cities). Such financial behaviour provides a theoretical and practical justification for imposing stricter, hard budget constraints and for substitution of block grants with conditioned grants (Bird / Vaillantcourt 1998).

Thirdly, the local government practice of optimising revenue from their own tax bases through effective and transparent collection efforts as part of tax reform in support of sub-national governments touches upon structures, interests and the political and economic practices of those who benefit from the status quo tax system. The general pattern in developing countries of the wealthiest and the poor being the least likely to pay taxes (Braeutigam 2008) is likely to pertain also to local government taxation. In other words, attempts to change existing fiscal patterns and practices may be conflictual and face resistance. In Africa, the existing taxation patterns are connoted with the coercive and exclusionary colonial tax system. And the predominant local taxes and user fees (poll tax, market fees, etc.) have regressive effects that favour the property-owning /wealthier classes at the expense of the poorer ones. On the other hand, proportional or progressive property taxes are often not collected. Consequently, any attempt to change this pattern by emphasising the taxation of property (with progressive rates), has to face and overcome resistance from those who benefit from the status quo. In other words, to understand the tax system, it is necessary to take into consideration the dynamics of the local political economy and relations between the local state and society – this is a decisive factor for the success or failure of effective and transparent taxation based on own local revenue sources.

Finally, one of the main challenges is local government financial and fiscal administration – its efficiency, effectiveness and transparency. The fiscal efforts and yields are not only functions of allocating human and material resources to the municipal tax administrations; the approach and method (e.g. coercive collection), the instruments used (e.g. database on taxpayers, computerised technology and programmes, etc.), as well as the degree to which the tax officials are also part of a meritocratic local administration. Corruption and tax evasion are associated with a weak local tax administration (Fjeldstad / Semboja 2000; Fjeldstad / Therkildsen 2008). In the case of Mozambique, it is estimated that approximately 50 per cent of the yield of market fees in small and medium-sized towns is not accounted for as a result of being siphoned off by municipal officials, tax collectors and

9 They do this on the occasions of the more or less regular National Meetings of Municipalities organised by the central government, i.e. the Ministry of State Administration.

supervisors (Ilal 2007). The observation of Bird et al. (2008) that improving institutional performance of the (tax) administration, curbing corruption and increasing accountability are part of the solutions to rectifying poor tax efforts, is also valid for local governments. The choice of tax collection methods – and the local governments’ tax policy and its priorities – has a considerable influence on the efficiency of the tax administration, the results of its work, on the tax effort as well as on the yield (Bird 2004).

Based on those considerations, in the case of Mozambican municipalities, I argue that the comprehensive and integrated fiscal decentralisation system in place since 1998, and reformed in 2008, has not yet produced the desired effects, i.e. it has not endowed the Mozambican municipalities with sufficient resources to meet the demand for better public services and goods and allowed them to contribute tangibly to the achievement of the global and national poverty reduction agendas, i.e. the Millennium Development Goals and the National Poverty Reduction Strategy Paper – called Programa Acelerado de Redução de Pobreza Absoluta since 2011.

The resulting fiscal stress and lack of investment in social and technical infrastructure of Mozambican municipalities can, theoretically, be resolved in four ways:

- a) by collective bargaining between the municipalities – namely their national association and the central government – for a percentage increase of the latter’s share of transfers, e.g. through a change of the revenue-sharing formula in the established legal framework for intergovernmental transfers;
- b) an extension of donor support to local government levels within the framework of the Paris Declaration on Aid Effectiveness, e.g. negotiating a fair share of the donor support to the national budget to be transferred to municipalities;
- c) a more efficient utilisation of the municipalities’ own revenue potential, including the necessary investment in human resources, equipment and tax registers; and finally
- d) a combination of all previous ways of generating more resources for municipal governments.

Given the absence of a well-established, nationwide institutional framework for options a) and b) and the fact that central government transfers to municipalities flow more or less regularly within the established framework – redefined through the local government tax reform of 2008 – the political will of government for a new reform, and thus the likelihood for these options to occur, is rather low. Given the perceived high rates of urban poverty, central government transfers have, in fact, been increased through additional funding for urban poverty reduction in provincial capitals – not via negotiations, but by central decision and without alteration of the existing legal framework for intergovernmental transfers.¹⁰

Thus, assuming, as it were, that the municipalities’ tax potentials are clearly underutilised, option c) is the only viable option at present.

10 Through the Fund for Urban Poverty Reduction (Fundo para Redução da Pobreza Urbana), first established in the 2011 budget as a “conjunctural” policy measure, to which the municipalities, however, do not have a permanent legal entitlement.

This means that Mozambican municipalities would need to not only better understand their local revenue base – the diversity of sources, their buoyancy and their potential – but also to design adequate revenue mobilisation policies and collection strategies that reflect aspects of equity and efficiency. They would also need to improve their institutions (in terms of human resources and technology) and their domestic accountability, including finding ways of minimising the risk of moral hazard, e.g. combating corruption.¹¹

For the purposes of the present analysis, the total municipal revenue potential is considered to vary with:

- a) the type of revenue sources legally attributed to municipalities, their relevance by type of municipality and their buoyancy;
- b) the capacity, efficiency and transparency of the municipal tax administration, including the methods (coercive or not) of tax collection and administration.

There are, of course, other factors that – as compared to the present study – a more comprehensive analytical framework focussing explicitly on the political economy of municipalisation could possibly consider. They include the following: the tax policy of the local municipal government, which itself is related to the type of local political economy, politics and the type of political settlements among local and national elites; the cost-benefit of the tax burden to local citizens – namely the balance between the taxes and the public services provided by the authorities (Wicksellian Link)¹² – is a potential explanatory factor, since it determines, to a large extent, tax compliance or evasion by the local citizenry; finally, the economic dynamics of the municipality and the area, district or region where it is located – the degree of urban poverty would need to be taken into consideration in a wider analytical framework.

Other constraints arising from the design of the original research project is the somewhat limited scope concerning the municipal revenue categories to be examined in this study, since not all sources of revenue provided to the municipalities by the local government tax legislation could be scrutinised due to time and budget constraints. Leaving aside the category of user fees for water, refuse collection¹³ and other non-fiscal sources of revenue (e.g. advertisements in public spaces, etc.), the six case studies provide data for and examine a total of seven primary sources of revenue – four of a fiscal and three of a non-fiscal nature.

11 The risks at the municipal level are considerable, notably in procurement and management of markets. See Nuvunga et al. (2007).

12 I owe this reference to the Swedish economist Wicksell (1851–1926) to conversations with Jamie Boex. See also Boex (2011, 36).

13 Especially water fees are difficult to compare on an aggregate level, since they accrue not necessarily to the municipal government, depending on the type of water management model in place (public central, local, private or a mix of all three). Concerning revenue from refuse collection, little systematic information and few research results are available. Case studies in one small and one medium-sized town show that the fee collection – usually collected in “piggy back” arrangements by the public electricity provider Electricidade de Moçambique – is low and covers only 10 or 30 per cent of the collection cost in the small and the medium-sized town, respectively. Electricidade de Moçambique usually retains 25 per cent of the yield for “administrative” costs (Allen 2006).

Fiscal revenue

- a) Municipal Poll Tax (Imposto Pessoal Autárquico – IPA)
- b) Municipal Property Tax (Imposto Predial Autárquico – IPRA)
- c) Municipal Property Transaction Tax (Imposto Autárquico de Sisa – ISISA)
- d) Municipal Vehicle Tax (Imposto Autárquico sobre Veículos – IAV)

Non-tax revenue

- e) Land Use and Development Licence (Direito de Uso e Aproveitamento da Terra – DUAT)
- f) Economic Activity Tax / Fee (Taxa por Actividade Económica – TAE)
- g) Fees from the occupation and use of public space reserved for markets and fairs

For the assessment of each of the seven sources' revenue potential, three determinants have been chosen: i) the quality and coverage of revenue registers, ii) the assessment of tax obligations of citizens and iii) the degree of compliance (also as a function of the efficiency and transparency of the local tax administration). These are defined in the following section.

3 Methodology and data

3.1. Selection of case studies

The methodology used in this study and the supporting studies referred to above is the methodology of a case study. Given the unavailability of aggregate data for all 43 municipalities, and the limited human resources and time available, this choice was considered to be the most adequate and economical one. Six municipalities were selected as cases for the sample, from which general conclusions are drawn, based on the values of each of the variables used for the calculation of the municipal revenue-generating efforts obtained through the fieldwork, as well as the sample average for these variables.

The sample is not representative in a stochastic sense; it rather assembles cases with *diverse* (in terms of geography and economic activity) and *typical* features, in the sense that both urbanised areas (towns, city) and rural district centres (*vila*) were included. These criteria correspond to selection criteria established by the theoretical literature on qualitative research methods and case studies (Gerring 2007, 86 ff.).

The extremes among the wide range of the 43 municipalities – e.g. Maputo, the capital city, with more than one million inhabitants, and very small village municipalities such as Metangula (approximately 8,000 inhabitants) – were not taken into consideration.

Thus, the selection process for the sample first took into consideration a mix of basic features of municipalities (see Table 1 below). Secondly, given the budget and time constraints of the research project, economic and logistical criteria were observed, such as

No	Name	Region	Population	Type	Economic activity / mainstay
1	Beira	Central	436,240	City, provincial capital	Port and railways, industry, trade, administration, services
2	Cuamba	North	79,848	Town	Agriculture, rural market, rail and road, commerce
3	Marromeu	Central	39,409	Vila	Sugar plantation
4	Nacala	North	105,820	Town	Port and railways, industry, trade and commerce, Economic Free Zone
5	Ribáuè	North	21,121	Vila, new municipality	Agriculture
6	Vilankulo	South	38,432	Vila	Tourism

Source: census 2007, own observations.

easy and economical access by air to the sample municipalities, and/or access by road from Nampula city – the location of the P-13 office and its logistics department.

Beyond that, the municipalities may be clustered into three categories, each of which can be said to “tell its own story” in terms of institutional capacity.

Group 1: Major and medium-sized (port) towns (Beira and Nacala)

This group represents municipalities that have above-average institutional capacity, including the quality of human resources, given their size, status as town (Nacala) or provincial capital (Beira), educational resources and/or a long history of technical assistance for urban management and planning (Nacala). Given the considerable number of modern buildings and businesses, theoretically they have a base for property tax.

Group 2: Small to medium-sized (rural) towns and vilas (Cuamba, Marromeu, Vilankulo)

This group represents the official category of small town (Cuamba), as well as that of *vilas*,¹⁴ i.e. centres of district administrations turned into autonomous municipalities. This group usually has the characteristics of rural, urbanised administrative and commercial centres, and the main revenues come from market transactions, at least at the time of the creation of the Mozambican municipalities. Over time their institutional capacities have increased, as has the diversity of sources of revenue. Given the fact that there are only a few major cities and towns in Mozambique with a population above 100,000 inhabitants (a total of 13, or 30 per cent of all municipalities), this category represents what might be called archetypical rural municipalities. It is from this category that the two examples used for inter-municipal comparisons are drawn (Section 5.3).

14 The Mozambican municipalities are classified by four types of cities / towns, notably a) the capital city (Maputo), b) 10 provincial capital cities, c) 12 towns and d) 20 *vilas* at present.

Group 3: Newly created, small vila-type municipality (Ribáuè)

This category represents the second-generation municipalities. Only Ribáuè, one of the 10 created in 2008, was included in the sample. Together with its nine sister municipalities, Ribáuè is characterised by very weak institutional and revenue capacities, which are still under construction, so to speak. Thus, the database for this type of municipality is still very weak and partially incomplete.

3.2. Data collection

Gathering the **financial data** (i.e. data on expenditure and revenue by the established classifiers) relevant to our analysis was a major challenge, since at the central level, neither the Ministry of Finance, the National Tax Authority (Autoridade Tributária de Moçambique – ATM), the National Statistics Office (Instituto Nacional de Estatística – INE) or the National Auditing Agency, i.e. the Administrative Tribunal (Tribunal Administrativo – TA),¹⁵ have a systematic and regularly updated collection of financial and other data (demographic, economic, etc.) on municipalities available. The National Budget Directorate (Direcção Nacional de Orçamento) in the Ministry of Finance publishes only budget projections of the municipalities before the approval of the municipal budgets by the respective municipal assemblies. These differ considerably from the executed budgets.

For reason due to the unavailability of reliable data aggregated at the central government level, the application of a methodology known as the Tax Performance Assessment (von Haldenwang / Ivanya 2010) had to be discarded.

Instead, the study draws on a database generated by the author with the support of colleagues and consultants – partially within the framework of P-13, partially from the Universidade Eduardo Mondlane – during approximately 16 months between 2009 and 2011. This base provides data on **executed** budgets (expenditure and revenue) for a total of 12 municipalities, including the six sample municipalities, for the years 2005 to 2009. Most of the expenditure and revenue data is classified according to the established legal norms for Mozambican public finance (Law 9/2002 and Decree 34/2004). They are contained in the municipal accounts (Conta de Gerência), which the municipal government needs to submit to the Assembly for approval within two months after the end of the fiscal year (January to December) and which need also to be submitted to the TA for auditing.

The quality of the data is mixed. It varies according to the size of the municipality, the technical capacity of its staff and the quality of information provided by central state agencies on revenue, which belongs to the municipal tax base but is collected and transferred by the central government. Triangulation and, when necessary, rectification were required, in most cases via several visits by members of the research team, often as part of capacity-building and project work within the framework of P-13.

For the gathering of **specific data on the selected revenue categories and their determinants** referred to above, a specific method was chosen. Each of the six cases was examined with regard to key features relevant for taxation (demography, size base, cadastre,

15 The Third Section of the TA has the function of the General Auditor.

number and type of houses, vehicles, etc.). This methodological choice was prompted by the absence of primary data for the six municipalities in the 2007 General Population and Housing Census compiled by INE. This could have been an important source of information for calculating or estimating municipal tax potential, such as

- age structure of the population in the municipality;
- total housing by type and area (neighbourhoods) in the municipal territory;
- number of vehicles per household within the municipality's jurisdiction.

However, despite initial requests on this matter, it was clear that the INE does not use the category “local authority / municipality” as a territorial classifier for its database.

Consequently, the research team used the “within-case analysis” as an alternative method¹⁶ to estimate the tax potential of each type of revenue under scrutiny, namely, information and estimates shared and validated by interviewees in municipal councils and other stakeholders,¹⁷ in particular for the following items:

- size of the economically active population;
- distribution of buildings by territorial area (urban, peri-urban, rural) and type of use (residential, commercial and industrial);
- market prices for buildings, by type of use;
- number of property transactions;
- number of vehicles registered and/or based in the municipality.

In order to estimate the quality and coverage of the tax registers, notably land and building cadastres, a random sample was taken from the municipal register of land and buildings, whenever a register existed and was accessible to the researchers. A satellite photograph was used (Google Earth) to obtain a sample number of buildings with statistical significance in a limited area, and this was followed by fieldwork interviews with residents to gather more detailed information on the randomly identified buildings (owner, number, etc.). The data obtained through this method were compared with information contained in the respective registers in the municipal administration, thus providing an estimate of the quality and coverage of the register. This methodology required triangulation of data and, in all cases, a second visit to validate the data before it was calculated and used.

16 This alternative methodology was prepared and approved in a methodological workshop organised in Nacala Porto by P-13 and the World Bank. In addition to the researchers, participants included the project's international consultant, Mr Jamie Boex; the World Bank public finance specialist Mr Uri Raich; the P-13 financial manager, Mr Hans Erskog; as well as technical staff from Nacala MC. The Mozambique Tax Authority participated in a video conference with the researchers and senior World Bank staff on 27 January 2010, demonstrating their interest in the topic.

17 The interviewees typically included the mayor, the council member in charge of municipal finances (*vereador*), the technical and administrative staff of the relevant departments (accounting, urbanisation and cadastre, economic affairs), administrators of sub municipal units (wards or urban districts) as well as the local representatives of the notary's office ATM.

The data generated were entered and systematised in a spreadsheet for all municipalities of the sample, and for each of the seven revenue sources analysed. This matrix can be considered a **key element** in the study's within-case methodology for estimating the tax potential.

3.3. Estimating the tax potential

How can the tax potential of a local authority be estimated?¹⁸

In this section we present a mathematical approach to estimating tax collection. We look at its *de facto* yield and the share that is not collected; when both are taken together, we see the overall tax potential in a given municipality and for each of the seven revenue categories presented above. Proceeding in this way does not necessarily take into consideration the institutional and practical challenges of a municipal tax administration, the quality of the human and technical resources available for tax collection in a given municipality and the basics of getting the relevant databases and registers right and updated. These challenges are dealt with in the subsequent sections.

A simple approach is to define the product of a municipality's tax effort for each of the seven revenue categories selected for this case study, as the relationship between the revenue collected and the total own revenue that is theoretically available. In other words, the tax effort (TE) can be expressed by the ratio of revenue collected (R) and the total tax base (TB) multiplied by the tax rate (TR) of this revenue. Mathematically, the tax effort can be expressed by the following equation:

Equation 1: Tax effort

$$TE = R / TB \times TR,$$

with

TE	Tax effort reflects the effort with which a municipality collects revenue compared to its revenue potential. It is expressed as a ratio between zero and one (or zero and 100 per cent).
TB	The tax base reflects the statutory tax base, as defined according to the government policy in terms of what is and is not taxed. For instance, in the case of the Municipal Poll Tax (IPA), the tax base is the number of individuals subject to IPA. In the case of the Municipal Property Tax (IPRA), the tax base is the aggregate value of all taxable properties.
TR	The tax rate is defined as the statutory (legal) tax rate. As discussed in Section 2.3 above, in the case of municipal fiscal revenues in Mozambique, the tax rate is defined by the Law on Municipal Finance.

¹⁸ This part draws extensively from Boex (2011).

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Under this formula, the level or percentage of unrealised revenue potential (UP), i.e. the reserve of a revenue source, can be defined as follows:

Equation 2: Unrealised revenue potential

$$UP = \frac{(TB * TR) - R}{(TB * TR)} = 1 - TE$$

What are the factors that influence variations in this ratio, i.e. determine a rise in the TE? Put another way: What are the factors that determine R? What are the administrative instruments that the Municipal Council (MC) can employ to increase R? These questions assume that the TB changes, largely for reasons outside the control of the MC (for example, population and economic growth).

As proposed by Kelly (2000), this study used three analytical categories or determinants for all the revenue sources studied: a) the coverage ratio (CVR), b) the assessment / applied ratio (AR), and c) the compliance ratio (CLR). These are related to the quality of the tax administration and complement factors emanating from tax policy decisions (including the tax base and tax rate). Together they are used to define the collections for a specific revenue source:

Equation 3: Collected revenue from a particular source

$$R = (TB * TR) * (CVR * AR * CLR)$$

The characteristics of each of these ratios are defined as follows:

CVR	The coverage ratio is defined as the share of the statutory tax base that is covered by the municipal tax administration. For instance, in the case of IPRA, the coverage ratio is calculated as the number of taxable properties that are captured in the municipal cadastre, divided by the total number of taxable properties in a jurisdiction. The coverage ratio measures the accuracy and completeness of the role of taxpayers or taxable properties.
AR	The assessment / applied ratio is defined as the share of the statutory tax rate that is assessed by the municipality. A municipality could either under-assess a tax by simply lowering the tax rate that it applies (below the statutory rate), or alternatively, by undervaluing the value of the tax base. For example, in the case of IPA, municipalities generally collect a tax amount that is less than the tax rate prescribed by law. In the case of IPRA, the AR could be defined as the value of a property on the valuation rolls divided by the real market value of the property on the valuation roll. The AR measures the accuracy with which the value of the tax base is assessed and the accuracy with which the tax rate is imposed.
CLR	The collection / compliance ratio is defined as the tax revenue collected over the total tax liability billed for that year, measuring the collection efficiency. The CLR reflects the vigour with which the municipality administers and enforces municipal revenue collections, as well as the degree to which municipal taxpayers comply with municipal revenue collection efforts.

Coverage ratio

The ratio or level of coverage answers the following question: Does the Municipal Council try to collect the tax from all taxpayers who are legally obliged to pay it and does it have the necessary instruments for this purpose?

The ratio is defined as the total number of taxpayers (for the tax being studied) in the municipal database (e.g. in the case of buildings, those covered by fiscal registration), divided by the universe of taxpayers (or the total number of buildings). This ratio measures the extent to which the database (the registers and tax records) are complete and accurate.

Assessment / applied ratio

Determining this ratio answers the following initial question: Is the local authority charging the taxpayer the right (or the legally allowed) amount? The ratio is defined as the percentage of the tax rate actually applied compared to the statutory maximum tax rate. In the case of real estate transactions, the ratio expresses any possible differences in the application of the legally established rate between the amount recorded in the documentation and the property's market value. In other words, the ratio measures exactly the extent to which the MC is or is not applying the maximum statutory rates in its assessment of the property's value.

Collection / compliance ratio

Determining this ratio answers the initial question: How successful is the municipality in collecting revenue from taxpayers?

The collection ratio is defined as the revenue actually collected in any given year as a percentage of the estimated total revenue liability of taxpayers according to tax bills and notices issued that year, respective of the estimated mathematical product of the total number of taxpayers with the individual rate or value of the tax or fee. This ratio thus measures the effectiveness of the institution in collecting revenue. It is influenced by the quality and effectiveness of the municipal administration, as translated by its capacity to issue tax bills and notices, by which the taxpayer can pay his or her tax dues, by the extent of corruption in tax collection and delivery, and the extent to which the taxpayer fulfils his duty to pay his taxes, namely, the tax evasion phenomenon and the effectiveness of control and inspection, including coercive collection in severe cases.

Returning to the initial formula, and combining equation 1 with equation 3, the tax effort can be expressed through equation 4:

Equation 4: Tax effort (enhanced formula)

$$TE = CVR * AR * CLR$$

This equation suggests that for the assessment of the tax effort (and, by implication, of the unrealised revenue potential), quantifiable data is needed for each revenue source in each of the six municipalities concerning both the statutory size of the tax base for the sources of revenue under scrutiny (e.g. the estimated number of registered citizens or vehicles) and

the actual number as measured by the municipal government itself. Further quantification is needed of the statutory tax rate for each source of revenue, together with the valuation of the tax base and the tax rates applied by each municipality for each revenue source under consideration. These operations permit the computing of the CVR, the AR and the CLR for each of the revenue sources under consideration in each of the six municipalities. In turn, this more detailed picture of revenue potential and revenue effort will allow us to pinpoint the gaps between actual revenue collections and revenue potential at each stage of the revenue collection cycle.

This formula, reflected in the construction of the matrix on the estimated tax potential (Table 4, Chapter 5.1), was applied to all sources of income examined in the six case studies.

4 Municipal own-source revenue

4.1. Some key features

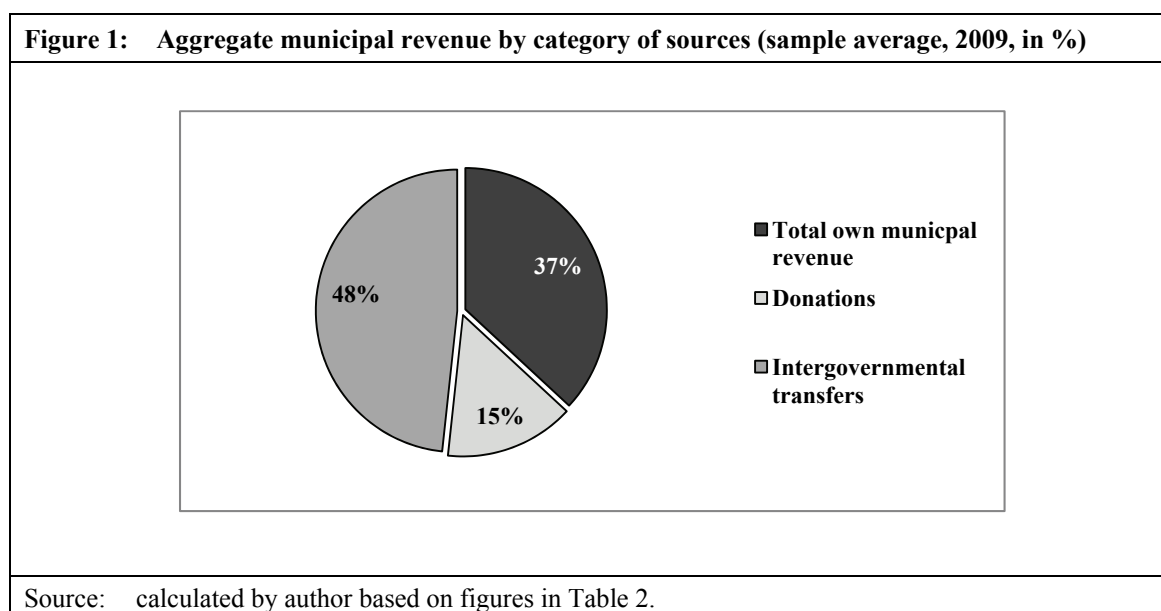
The following table and figure give a general snapshot of available total municipal revenue by source of revenue for the sample municipalities, including fees (average value, for 2009). Table 2 is based on the extensive research done by the study team, reflecting executed budgets. A couple of striking features can be mentioned:

- There is a low percentage of tax revenue in comparison to non-tax revenue.
- Own revenue is only just above one-third of total revenue.
- The central government is the major source of municipal revenue.
- Donations seem to have less weight in municipal budgets in comparison to own and government sources, although care must be taken with this affirmation, since the major recipient of aid among all municipalities, Maputo, is outside the sample, and also because there is a tendency of underreporting donations in the municipal budgets.

Main revenue sources	Own-source revenue		Total revenue	
	Meticais	%	Meticais	%
Imposto Pessoal Autárquico (IPA)	678,144	0.6	678,144	0.2
Imposto Predial Autárquico (IPRA) *	8,271,830	18.4	8,271,830	6.8
Imposto Autárquico de Sisa (ISISA) **	3,681,926	2.8	3,681,926	1
Imposto sobre Veículos (IAV)	7,243,165	4.8	7,243,165	1.8
Uso do Solo Autárquico (DUAT)	18,926,507	14.2	18,926,507	5.2
Taxa por Actividade Económica (TAE)	7,308,808	5.4	7,308,808	2
Uso de espaço público (Mercados e Feiras)	16,646,416	11.3	16,646,416	4.2
Recolha, depósito e tratamento de lixo ***	18,726,432	14	18,726,432	5.2
Subtotal (main municipal rev. sources)	81,483,228	71.3	81,483,228	26.3
Other own-source municipal revenue	38,379,042	28.7	38,379,042	10.6

Total own-source municipal revenue	119,862,270	100		119,862,270	36.9
Intergovernmental fiscal transfers				174,751,830	48.3
Donations				53,617,305	14.8
Total municipal revenue sources				362,120,097	100
<p>(*) The relatively large collection of IPRA in our sample is driven by a single outlier, Beira.</p> <p>(**) ISISA was devolved to municipal level in 2008 and had not yet been incorporated in the municipal budget classifications by 2009. Therefore, ISISA collections reflect the team's estimate.</p> <p>(***) Solid waste fees are collected by the power utility Electricidade de Moçambique, which transfers the fee to the municipalities without supporting evidence on the revenue base or the overall number of energy consumers. Electricidade de Moçambique usually retains 25 per cent of the yield for "administrative" costs. The areas in grey reflect fiscal (tax) sources of revenue.</p> <p>Source: own calculations, based on Boex (2011), Chimunuane et al. (2010), Chimunuane / Hassam / Weimer (2010a, b).</p>					

The last four lines (11–14) of the last column, which show the aggregate municipal revenue by source of revenue, can be summarised in the following figure¹⁹:



The following table presents the available data for each of the six municipalities.

19 The percentage giving the share of total own-source revenue (fully rounded values) includes revenue from the municipalities' main sources (including waste collection fees) and other sources of fiscal and non-fiscal revenues (revenue from publicity, administrative and other licensing fees, fines, etc.) not covered by the present studies. These two categories represent 71 and 29 per cent respectively of the total revenue of the sample municipalities (see column 4, lines 9 and 10).

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	Beira	Cuamba	Marromeu	Nacala	Ribáuè	Vilankulo	Sample Total
Imposto Pessoal Autárquico (IPA)	0.4	1.6	6.2	0.3	0.0	0.3	0.5
Imposto Predial Autárquico (IPRA)	22.7	0.0	2.6	0.4	0.0	0.0	18.4
Imposto Autárquico de Sisa (ISISA)	3.0	0.0	0.0	0.6	0.0	6.3	2.8
Imposto sobre Veículos (IAV)	4.9	0.0	9.3	1.2	49.7	9.0	4.8
Uso do Solo Autárquico (DUAT)	10.4	15.3	1.0	46.8	0.0	11.0	14.2
Taxa por Actividade Económica (TAE)	5.7	5.3	7.9	1.8	0.0	9.5	5.4
Uso do espaço público (Mercados e Feiras)	10.2	38.5	49.9	0.0	50.3	21.2	11.3
Recolha, depósito e tratamento de lixo	15.2	7.3	3.0	14.0	0.0	1.9	14.0
Sub-total	72.5	68.0	79.9	65.1	100.0	59.2	71.4
Other own revenue	27.6	32.0	19.9	34.8	0.0	40.8	28.7
Total own revenue	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Note: The sample total is a weighted average, so municipal averages do not add up to the sample average.
Source: Boex (2011).

It shows that municipalities use their taxation possibilities according to their political priorities and with regard to sources, which are deemed buoyant and the management of which they are familiar with. The emerging pattern is diverse, with the selected municipalities each facing their own particularities in terms of history, leadership, administrative competence, etc. Concerning property tax, Beira is an exception in the sense that it is quite advanced in utilising its base, given the availability of cadastres and a defined policy to this effect. Marromeu, surrounded by sugar estates, stands out as a municipality that has, relative to the others, a high yield of IPA revenue from markets and a very low one from land use licences (DUAT). All these features are related to the presence of the sugar factory, where IPA is collected by the company at source, and where land for private use is scarce, whereas market turnover for the labour force and family is high. Nacala's revenue from land use concessions is extremely high due to the booming demand attributable to the Economic Free Zone around the port. On the other hand, the market as a source of revenue appears to be neglected for reasons of inadequate management arrangements and unpopularity.²⁰ The variation of data concerning vehicle tax (IAV), collected at the time by the National Tax Authority (ATM) and transferred to the municipalities, is attributable to incorrect processing. It certainly does not reflect the number of vehicles in the six municipalities.

²⁰ Reasons given by municipal official responsible for the management of markets. See Weimer et al. (2010b, 28 f.).

These features of each case and their causes and practical consequences for fiscal matters are further explored in the six individual municipal case studies (see bibliography).

Despite these particularities, what are the striking features and what are common denominators of the six municipalities studied?

Firstly, there is a weak contribution of fiscal revenue to total own revenue, with an average of between 20 and 25 per cent, or about 10 per cent in relation to overall revenue. This in turn means a considerable reliance on sources of non-fiscal revenue.

Secondly, personal income tax (Poll Tax – IPA) and Municipal Property Tax (IPRA) and Municipal Property Transaction Tax (ISISA) play, in general, a minor role. As pointed out, Beira represents an outlier, which has favourable institutional conditions for collecting IPRA and it has created a technical policy base for doing so.

Thirdly, the land use fee (collected only once, on the occasion of the granting and licensing of the use right) is considered highly buoyant and varies with the demand for, and the availability of, land (see below). In the case of Nacala, it is particularly high, due to the establishment of a Special Economic Zone in the area. Marromeu, on the contrary, has little demand attributable to lack of availability of land, given that the adjacent areas are occupied by the sugar estates.

Fourthly, market fees make up the bulk of revenue, with the exception of Nacala, for the reasons given above, and Beira, which has a taxation policy prioritising the collection of IPRA and balancing between fiscal and non-fiscal sources of revenue. Market fees are of particular importance in smaller municipalities, which have a limited base for fiscal revenue (vehicles, buildings). In contrast, revenue from TAE, a type of local business tax (in the form of a fee), is relatively low. The exception is Nacala.

And finally, the relative weight of the Vehicle Tax (IAV) in the overall tax structure is modest, as it most likely has a greater potential. This is related to the fact that the tax was fully transferred to the municipalities at the end of 2008, with the municipalities only gradually building up capacity to collect it.

What explains the weak performance of municipalities in tapping into their own diverse fiscal base?

Before I analyse the results of the research on the potential and use of the municipal tax base, I present, in some detail, the main revenue sources they have that were analysed in the present study.

4.2. Characteristics of the revenue sources studied

This section contains a brief presentation of the main sources of own revenue, whether fiscal (taxes) or non-fiscal (fees) under legislation in force since 2008 (CTA 2008). They

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account for more than 70 per cent of revenue generated from the local government tax base.²¹

4.2.1 Municipal Poll Tax (Imposto Pessoal Autárquico – IPA)

As in other countries in southern Africa and under a variety of different names, the Municipal Personal Tax (IPA) – “poll tax” or “head tax” – dates back to colonial times. The literature describes how this tax has several disadvantages as a revenue source, such as: regressive effects, high collection costs and its association with the coercive practices of the colonial period. As such it is inappropriate today (Fjeldstad 2001a; Fjeldstad / Therkildsen 2008).

IPA charged in municipal areas corresponds to the National Reconstruction Tax (Imposto de Reconstrução Nacional – IRN) of the state territorial tax base under Decree 2/78 of February 16. In the past, IRN was justified by the need to rebuild the country after years of liberation war and the damage caused by natural disasters at that time. Following the creation of local governments in Mozambique in 1997, in order to differentiate them it was established that the municipalities would collect IPA and the state tax authorities would continue to collect IRN. To some extent, this tax is not suited to the current context. Given the above-mentioned disadvantages and the new forms of taxation being promoted by the Mozambique Tax Authority (Autoridade Tributária de Moçambique – ATM), it is possible that IRN might be abolished.

In the case of Mozambique’s municipalities, however, IPA is part of the municipal tax base (Law 1/2008 Art. 53 ff.; Municipal Tax Code, Chapter II, Art. 3 ff. [Decree 63/2008]). The tax is levied on the economically active population (people aged 18 to 60 years of age), with some exceptions. The law allows the tax to be **collected** in several different ways: at source (in the case of company employees, the civil service and municipality staff), by mobile teams operating through the lowest municipality structures (administrative posts, heads of neighbourhoods, community authorities) and at the head office of the Municipal Council, where a receipt showing payment of the tax is required when a municipality citizen goes to deal with an administrative matter, etc. The law requires the municipality to keep an updated register of taxpayers. The tax can be collected throughout the year, between January 2 and December 31. Despite this requirement, few municipalities have a register of taxpayers and it is collected in an ad hoc manner, contrary to the systematic approach required by law. Collection of IPA is often associated with coercive and corrupt practices.

4.2.2 Municipal Property Tax (Imposto Predial Autárquico – IPRA)

Under Law 1/2008 Art. 55 ff. and the Municipal Tax Code, Chapter III, Art. 35 ff. (Decree 63/2008), IPRA is part of the municipality tax base. The tax is levied on the objective **real**

21 This includes revenue from waste collection fees. Other sources, such as the “improvement contribution” and fees linked to the provision of other services (water, etc.) and licences (e.g. for construction) are not included in the analysis, for reasons given above (see footnote 13).

estate value of an urban building that is regarded as infrastructure and built on the municipality's urban land. The real estate value is the value recorded in the property register and, where this does not exist, the market value declared by the owner. Inaccurately recorded values – many of them never updated since colonial times, due to the database being held by the Provincial Directorate of Finance and the absence of efficient means of coercion – are the greatest challenges to the collection of this tax by the municipality. The methodology for estimating the market value of a building usually takes into consideration the following criteria:

- basic construction value/cost per m²;
- gross construction area (building and land);
- application coefficient (type of use, e.g. housing, commerce, services, warehouse, industry);
- location coefficient (rural, peri-urban, urban, etc.);
- age coefficient

The evaluation or updating of a building's value should be based on specific regulations. These are being prepared by the Ministry of Finance, which has regulatory authority over tax revenue. The draft regulations envisage, *inter alia*, requiring the taxpayer to register the building in the municipal tax register, and also suggest an annual assessment of all building values by a municipal building valuation committee.²²

The law stipulates an annual tax rate of 0.4 per cent of the value of residential buildings and 0.7 per cent for buildings used for commerce, industry, storage and other professional purposes. IPRA is to be paid annually in two instalments, falling due on June 30 and December 31. Buildings owned by the state, philanthropic organisations and other states (i.e. embassies) are exempt from IPRA. New residential buildings are also exempt for a period of five years from the date the housing permit is issued in the name of the owner.

The main challenges faced by the municipal government when collecting IPRA are: first, the production and updating of complete building registers, and second, determining the value of each building for the property register. While the former is entirely up to the municipality, in practice the second requires open collaboration between the National Tax Authority and local governments, as foreseen for the above-mentioned municipal building valuation committee. At the moment, the values recorded in the property register reflect the situation at the end of the colonial period and are thus way below current market values.

Although the strategic importance of a cadastral register of plots and buildings for both fiscal purposes and spatial planning is widely recognised, few municipalities have made the necessary investment in building the capacity of their Cadastre and Urbanisation Services (Serviços de Urbanizacao e Cadastro – SUC). This means that an important prerequisite not only for IPRA but also for all revenue related to land use (DUAT), construction and occupancy (IPRA) and sale of buildings (ISISA) is missing.

²² Ministry of Finance, draft regulations on the valuation of urban buildings, Maputo, July 2010.

4.2.3 Municipal Property Transfer Tax (Imposto Autárquico de Sisa – ISISA)

ISISA was introduced into local government legislation by Law 1/2008 (Article 59) and the Municipal Tax Code (Decree 63/2008, Art. 94 ff.). Prior to this it was solely a central government tax, payable in the local ATM office (formerly the Finance Department). The tax is levied on the transfer of ownership of urban property in a municipal territorial area, involving either purchase and sale, transfer in return for payment, permanent benefit and enjoyment or other types of transactions, excluding exemptions (e.g. property belonging to the state, the municipality, etc.) established by law. The **basis** of the tax is the respective declared or market value (the highest of the two being used) in a real estate transaction, payable by the buyer when the transaction is recorded and before the property is registered. The **rate** is 2 per cent of the value of the transaction.

In general, the challenge is that local authorities do not yet have a database for this tax, which was only assigned to them in 2008. The case studies revealed weak collaboration between the Municipal Council, the Ministry of Justice's Registry and Notary Public Office (where transactions are or should be registered) and the ATM, where ISISA is usually paid. The territorial area covered by the Registry Office often does not match the jurisdiction of the municipality, i.e. records are not classified by municipal area. This makes it difficult for registrars to identify the exact number of transactions per municipality. Some municipalities do not even have a Registry Office section where transactions can be recorded (purchase and sale, transfer, etc.). But even when these transactions are recorded and reported to the municipal administration, the declared value used for the ISISA payment is often much less than the building's market value. This adversely affects the income from ISISA.

Another challenge is collaboration and sharing of information between the ATM, the Registry Office and the municipality. The tax was only recently transferred to municipalities, but without any norms and procedures on decentralisation about the information and documentation needed by the municipality to collect payments. In some cases this produces conflicts between the local ATM offices and the municipal government, and there are some cases where both ATM and the Municipal Council collect ISISA. These charges are clearly not transparent and are contrary to the public interest as well as the effective collection of this tax.

4.2.4 Municipal Vehicle Tax (Imposto Autárquico de Veículos – IAV)

Legislation passed in 2008 (Law 1/2008, Art. 65 ff.; Decree 63/2008, Art. 64 ff. – Municipal Tax Code) required the transfer of this tax revenue to the municipalities. The tax base is the universe of all registered vehicles in a municipality (including passenger vehicles, lorries, public transport, pleasure boats and aircraft), except those belonging to the state, local authorities and diplomatic missions. The rate varies depending on the type, engine capacity and age of the vehicle: 50.00–4,400.00 MT (cars), 60.00–2,160.00 MT (lorries), 37.50–500.00 (motorbikes) and 60.00–2,160.00 (passenger vehicles).

As in the case of ISISA, this tax is not residence-based. For example, the vehicle of a citizen residing in Cuamba can be registered anywhere in the country. Moreover, statistical data on vehicles (as well as other socio-economic and demographic data) are not broken

down by local authority, much less by district, and are only available at the provincial level.

Although the law states that the MC and its tax department is the competent authority to receive and collect IAV, the tax is currently being levied and administered entirely by the ATM. Each year it transfers the share that is supposedly due to the municipalities and explains the methods used and provides documentation showing how the portion of the total income transferred to the municipality was calculated. The municipalities, which have no vehicle records of their own, do not know the details of the IAV calculation. The case studies indicate that even the regional ATM offices do not have enough information on how IAV is calculated for each individual municipality. It is thus difficult to explain the difference in, for example, IAV transfers to the small, relatively new Ribáuè municipality (created in 2008) compared to other municipalities. Although there are few cars circulating in Ribáuè, its IAV revenue is 10 times higher than its estimated potential, and larger than Cuamba, a town with many more registered vehicles (Weimer et al. 2010b, 19).

As in the case of ISISA, one of the biggest challenges is to improve inter-institutional cooperation between the ATM, the National Traffic Institute and the MC for the regular exchange of information on vehicle registration so that IAV transfers to the municipality are accompanied by documentation. The law envisages, perhaps unrealistically, that conditions for transferring collection of IAV (and ISISA) to municipalities will be created within three years of the December 2008 publication of Law 1/2008 as well as the Municipal Tax Code (Código Tributário Autárquico – CTA), i.e. by December 2011.

4.2.5 Municipal Land Use Licence (Licença de Uso e Aproveitamento do Solo Autárquico – DUAT)

Land in Mozambique is state property and cannot be sold or otherwise disposed of, mortgaged or charged against / pawned. As a universal means of wealth creation and social welfare, it is the right of all Mozambicans to use and benefit from land. The conditions for using and benefiting from land are determined by the state. The right to use and benefit from land is given to all individual and corporate persons, taking into account their social purpose. When issuing a title to use and benefit from the land (DUAT), the state recognises and protects rights acquired through inheritance or occupation, except in the case of a legal reserve or if the land has been legally assigned to another person or entity. The right to use and benefit from land cannot be granted totally, or in part, in protected areas, as these are areas in the public domain (areas that are in the public interest). Only a certain number of activities requiring special licences are permitted in these areas. Approval of an application for DUAT does not mean exemption from licences or other permits required by legislation applicable to commercial activities. Applications for DUAT are submitted to the provincial / municipal cadastral service where the land in question is located. For municipality areas with urbanisation plans, i.e. areas demarcated for this purpose, the relevant legislation on land²³ (which is not part of the “local authority package”) contains provisions on the authority of Presidents of Municipal Councils and villages, and District Administrators in places where there are no municipal bodies, as long as there is a public

23 Law 19/97 of October 1 – the Land Law.

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cadastral service. In areas not covered by urban development plans, Provincial Governors, the Minister of Agriculture and the Council of Ministers have powers to approve the issue of DUAT licences.

Demand for land that produces applications for DUAT is a sufficiently strong tax handle for the municipality to charge for the licence / title once (with a lower annual fee for a maximum of five years), until construction of the building is complete. Then the land with the building must be added to the municipal property register and the building is subject to IPRA.

So municipal revenue from a DUAT licence depends on two factors: first, demand to occupy land (in areas demarcated for urbanisation), and second, the availability of land for this purpose in the municipality's jurisdiction. In other words, in this instance the revenue is finite and has an associated "price": the transfer of land for occupation, construction and use for residential and commercial purposes. Local authorities in Mozambique are not yet accustomed to earmarking DUAT revenue for investment in the areas that "produce" this revenue – namely, improving social amenities such as roads, property registration, electricity, water and sewers. There is also no experience of the municipality auctioning land that is in great demand and/or has basic infrastructure, as DUAT is allocated on a "first come, first served" basis and the fee is the same for all land in that area. Auctioning land, at least in areas with the strongest demand, could increase this municipal income.

4.2.6 Economic Activity Tax / Fee (Taxa por Actividade Económica – TAE)

TAE is applied to the exercise of any trade or business, including the provision of services, within the jurisdiction of the respective local authority, provided it takes place in an establishment "with an open door". This was the idea when the fee was established under the CTA (Decree 52/2000 of December 21) but it has since been repealed. TAE was a fee under the former Municipal Tax System (Sistema Tributário Autárquico) and at the same time, a source of fiscal revenue. Under the new CTA (Decree 63/2008) TAE is considered non-fiscal revenue. As part of the Mozambican Municipal Tax System, and as non-fiscal revenue, it is governed by regulations / a resolution adopted by the Municipal Assembly. The municipal citizen should make use of all information on the regulation of TAE – as foreseen in the decree now repealed – as produced through resolutions of the Municipal Assembly.

However, collection of TAE neither impairs nor replaces the collection of other licence fees by other institutions in order to carry out a given activity. This means that non-tax revenue based on economic activities also includes revenue from licences including DUAT, the use of municipal space for markets and fairs and fees paid in exchange for the provision of public services. However, for the purposes of this study, revenue from DUAT and market licences is different from TAE.

How is the TAE rate applied calculated? The calculation of TAE usually takes into account the following factors:

- nature of the business
- location of the establishment
- occupied area (in m²)

There is no standard TAE rate applicable to all municipalities, as each one regulates this revenue through its own by-law. In practice, in all municipalities it is based on a fee or “quasi tax” on the area of the property where the economic activity takes place; the amount charged does not take into account the company’s economic viability. So this fee is a kind of quasi tax related to IPRA. TAE clearly increases the tax burden for companies, as they not only have to pay municipal IPRA but also Company Income Tax (Imposto sobre Rendimento de Pessoas Colectivas), a central government revenue. In some cases, local authorities in tourist areas (for instance Vilankulo) also charged hotel companies a tourism tax calculated on the basis of occupancy per night, a kind of “special TAE” for the tourism industry. This can be justified if the income from this revenue is used to finance municipal services that benefit tourism directly.

Collecting TAE is relatively simple because few companies and businesses are covered by the tax, and the Municipal Council usually has a register for this purpose, although it is not always updated. As a company is not usually obliged to display the document certifying payment of TAE, it is difficult for the general public to know whether or not a company has fulfilled its tax duties. The six case studies found that it is quite common for companies not to pay TAE, or for the fee to be the subject of “negotiations” by the company manager and the collector. Coercive collection of the tax by the municipality, i.e. closure of the business in case of non-payment of a cumulative TAE debt, is rare.

4.2.7 Occupancy and use of public space reserved for markets and fairs (ocupação e uso do espaço público reservado para mercados e feiras)

The occupation and use of places reserved for markets and fairs provides non-fiscal revenue, usually considered one of the main sources of revenue for municipalities. In order to be a market-fee payer, the citizen / seller must submit a request to the Municipality Directorate of Finance for an annual licence to operate somewhere within the market. After the request has been approved and an annual licence granted and paid for, from then on the citizen / seller has the right to operate a stall, paying daily or monthly stand or stall fees, depending on the agreement reached by the seller, the market vendors’ association and the municipality. This licence may be temporary (for hawkers) or annual (for permanent vendors).

As mentioned in the previous chapter, revenue from markets and fairs constitute a large part of the non-fiscal revenue of Mozambican local authorities. Nevertheless, this revenue source has its limitations:

- Collection costs are high. Case studies in the main markets in Vilankulo and Chimoio concluded that collection costs (collectors, inspectors, production and administration of voucher books, etc.) can reach 20 per cent of revenue. The calculation includes depreciation / amortization of market construction costs, maintenance, management,

cleaning and security. This can rise to 75 per cent of revenue from this source (Ilal 2006, 2007).

- The collection and administration of this revenue is vulnerable to corruption (Ilal 2006, 2007) – an observation confirmed by the six case studies. The author estimates that income from this source could be doubled if there was a more effective and transparent method for the financial management of markets.
- The effect of the market fee is regressive. This means that the tax burden not only makes basic essentials more expensive, it is also higher for social groups with a low income.
- Finally, collection of the market fee is not always matched by a corresponding municipal service for the taxpayer, i.e. in return for the fee, the seller does not always receive a stall in a market that is safe and clean with water and electricity, etc. This is not the case, particularly for hawkers outside markets, i.e. the informal sector, where the rate is often collected coercively, with the risk of the goods being confiscated.

In short, the net effect of taxation on stands, stalls and transactions in markets is far less than the relative weight of this revenue in the municipal budget. In addition, the excessive taxation of markets has undesirable social effects, particularly for the poorest.

5 Municipal revenue potential – results

5.1. Aggregate results and key features

To offer an overall picture and the dimensions of the used and unused revenue potential for each of the examined sources, we start with the presentation and discussion of the aggregate data. This is followed by looking at the variations in results across the sample and a comparison of two of the sample cases: Vilankulo and Cuamba. This sheds light on the main reasons for differing performance in making use, or not, of the revenue base.

The following table gives an overview of the estimations of the aggregate revenue potential for the six sample municipalities by type of revenue source. It results from the application of the methodology for estimating the information presented in Section 3 (particularly 3.3). The data includes the estimated values for the three variables, i.e. the coverage ratio (CVR), the assessment / applied ratio (AR) and the collection / compliance ratio (CLR). This permits for examining the bottlenecks in the exercise of revenue administration. The results are given as a percentage both for the tax effort (TE) and the unrealised revenue potential (UP). This is complemented by the overall monetary value (in meticaais) of the overall potential based on the actual revenue collections for 2009.

I	II	III	IV	V	VI	VII	VIII
Revenue source	Collec- tion ratio (CLR)	Assess- ment ratio (AR)	Cover- age ratio (CVR)	Tax effort (TE)	Unreal- ised potential (UP)	Unrealised revenue potential (2009)	Revenue collected in 2009
	(%)	(%)	(%)	(%)	(%)	(MT)	(MT)
1. IPA	17	54	92	8	92	7,798,656	678,144
2. IPRA	11	31	24	1	99	818,911,121	8,271,830
3. ISISA	33	29	53	5	95	69,956,594	3,681,926
4. IAV	69	92	74	47	53	8,167,824	7,243,165
5. DUAT	55	73	55	22	78	67,103,070	18,926,507
6. TAE	64	70	80	36	64	12,993,436	7,308,808
7. Market fees	72	94	72	49	51	17,325,862	16,646,416
Unweighted average	46	63	64	24	76	198,729,852	62,756,796
Average sample (MT)						33,121,642	10,459,466

Source: Boex (2011), Chimunuane et al. (2010), Chimunuane / Hassam / Weimer (2010a, b).

How should this table be read?

Let us look, for instance, at the case of revenue from the collection of market fees (source 7). The coverage ratio in column IV suggests that, on average, close to three-quarters of all market stalls and vendors within the municipalities are actually covered by the register of market stalls / vendors, i.e. the coverage ratio is 72 per cent. Each market vendor is subject to paying a daily or monthly fee, set by the Municipal Council, approved by the Local Assembly and published through documents referred to as municipal statutes.²⁴ The assessment ratio in column III tells us that on average, they pay 94 per cent of the maximum fee value fixed by the statutes. In turn, 72 per cent of the market fees that are imposed are actually collected and find their way into the municipal treasury (collection ratio in column II). Combining these partial results of the municipal revenue collections process and its three stages, the municipalities, on average, collect 49 per cent ($72 * 94 * 72$ per cent) of the maximum potential collections for market fees (column V). This implies an unrealised share of market fee collections of 51 per cent of the revenue potential for market fees. Columns VII and VIII show the corresponding monetary values in meticaís, based on the market fees actually collected in 2009.

Analysing the matrix shows that, on average, the six municipalities in the sample use less than one quarter (24 per cent) of the tax base of these seven sources. In other words, the UP, or revenue reserve, corresponds to 76 per cent of the own tax base. The revenue reserve is, on average, highest with IPRA (with lowest values for the CLR, AR and CVR),

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and lowest with the market fees. With other words, market fees are at the high end of the spectrum when it comes to the aggregate average municipal tax effort (49 per cent). At the other end of the spectrum is IPRA, with an overall average tax effort estimate of 1 per cent and an unrealised potential of 99 per cent. There are two reasons for this low value: the CLR is very low (11 per cent), which means that only very few taxpayers pay IPRA, which, in turn, is related to a low value (24 per cent) for CVR, meaning the tax registers are of poor quality. In the case of IPA, the CLR is also very low (17 per cent), despite the existence of a pretty good register of those citizens who are obliged to pay this tax (CVR: 92 per cent). The main reason for the high value of UP is both a deliberate municipal policy to not insist in collecting IPA and possibly problems of moral hazard.

In monetary terms, calculated on the revenue actually realised in 2009, the average UP per municipality in the sample corresponds to approximately 31.9 million MT.

The following table shows, for 2009, the average UP per municipality in relation to various revenue categories.

I	II	IV	V
Revenue category	Sample average figure (2009) (MT)	Estimated average UP (MT)	Multiplier (IV/II)
Revenue (1–7)	10,459,466	33,121,642	3.2
Total own revenue	22,291,827	33,121,642	1.5
Total revenue	60,353,350	33,121,642	0.5

Source: own calculations based on Boex (2011), Chimunuane et al. (2010), Chimunuane / Hassam / Weimer (2010a, b).

The table above means that each of the six municipalities studied could, on average, more than triple the average own revenue of the six sources analysed in relation to their collection 2009. The multiplication factor is 3.2. In relation to total own revenue, UP for 2009 is 1.5 times higher than the average value of revenue actually collected. And with regard to total revenue, UP is almost half of the former's average value.

In other words, the average unexploited tax reserve is quite high, almost half of the overall revenue for 2009 per sample municipality – the same as the sample's average budget.

Looking at the results by source of revenue, it is clear that the least exploited tax potential is taxation related to property and its transactions: IPRA and ISISA and also the IPA base. It also confirms that market fees and IAV are the most exploited tax sources, with the qualifications mentioned in the previous section concerning IAV.

5.2. Variations

5.2.1 Comparison between municipalities

The following Figure 2 presents the revenue collection performance by source of revenue for each of the six sample municipalities and thus permits a comparative analysis. The four

Figure 2: Municipal revenue effort and revenue potential by revenue source and municipality

1. IPA	Ratios			ET	UP 100- ET %
	RCu	RA	RCa		
Beira	17 %	37 %	100 %	6 %	94 %
Cuamba	13 %	74 %	80 %	8 %	92 %
Marro- meu	54 %	56 %	100 %	30 %	70 %
Nacala	2 %	27 %	90 %	1 %	99 %
Ribaue	3 %	74 %	90 %	2 %	98 %
Vilankulo	11 %	56 %	90 %	6 %	94 %
<i>media</i>	<i>17 %</i>	<i>54 %</i>	<i>92 %</i>	<i>8 %</i>	<i>92 %</i>

2. IPRA	Ratios			ET	UP 100- ET %
	RCu	RA	RCa		
Beira	45 %	20 %	35 %	3 %	97 %
Cuamba	12 %	68 %	11 %	1 %	99 %
Marro- meu	2 %	30 %	30 %	0 %	100 %
Nacala	5 %	37 %	40 %	1 %	99 %
Ribaue	0 %	0 %	0 %	0 %	100 %
Vilankulo	0.1 %	30 %	30 %	0 %	100 %
<i>media</i>	<i>11 %</i>	<i>31 %</i>	<i>24 %</i>	<i>1 %</i>	<i>99 %</i>

3. IASISA	Ratios			ET	UP 100- ET %
	RCu	RA	RCa		
Beira	50 %	40 %	85 %	17 %	83 %
Cuamba	0 %	0 %	0 %	0 %	100 %
Marro- meu	50 %	40 %	85 %	17 %	83 %
Nacala	50 %	53 %	60 %	16 %	84 %
Ribaue	0 %	0 %	0 %	0 %	100 %
Vilankulo	50.0 %	40 %	85 %	17 %	83 %
<i>media</i>	<i>33 %</i>	<i>29 %</i>	<i>53 %</i>	<i>5 %</i>	<i>95 %</i>

4. IASV	Ratios			ET	UP 100- ET %
	RCu	RA	RCa		
Beira	85 %	100 %	60 %	51 %	49 %
Cuamba	55 %	90 %	90 %	45 %	55 %
Marro- meu	85 %	90 %	80 %	61 %	39 %
Nacala	11 %	90 %	60 %	6 %	94 %
Ribaue	90 %	90 %	90 %	73 %	27 %
Vilankulo	85 %	90 %	65 %	50 %	50 %
<i>media</i>	<i>69 %</i>	<i>92 %</i>	<i>74 %</i>	<i>47 %</i>	<i>53 %</i>

5. DUAT	Ratios			ET	UP 100- ET %
	RCu	RA	RCa		
Beira	90 %	90 %	80 %	65 %	35 %
Cuamba	88 %	90 %	10 %	8 %	92 %
Marro- meu	50 %	100 %	50 %	25 %	75 %
Nacala	35.6 %	60 %	39 %	8 %	92 %
Ribaue	0 %	0 %	0 %	0 %	100 %
Vilankulo	65 %	100 %	75 %	49 %	51 %
<i>media</i>	<i>55 %</i>	<i>73 %</i>	<i>42 %</i>	<i>17 %</i>	<i>83 %</i>

6. TAE	Ratios			ET	UP 100- ET %
	RCu	RA	RCa		
Beira	81 %	56 %	100 %	45 %	55 %
Cuamba	72 %	90 %	95 %	62 %	38 %
Marro- meu	100 %	92 %	100 %	92 %	8 %
Nacala	39 %	83 %	86 %	28 %	72 %
Ribaue	0 %	0 %	0 %	0 %	100 %
Vilankulo	90 %	100 %	100 %	90 %	10 %
<i>media</i>	<i>64 %</i>	<i>70 %</i>	<i>80 %</i>	<i>36 %</i>	<i>64 %</i>

7. Mar- kets	Ratios			ET	UP 100- ET %
	RCu	RA	RCa		
Beira	85 %	75 %	67 %	43 %	57 %
Cuamba	60 %	100 %	68 %	41 %	59 %
Marro- meu	90 %	100 %	93 %	84 %	16 %
Nacala	60 %	100 %	50 %	30 %	70 %
Ribaue	75 %	100 %	79 %	59 %	41 %
Vilankulo	62 %	90 %	76 %	42 %	58 %
<i>media</i>	<i>72 %</i>	<i>94 %</i>	<i>72 %</i>	<i>49 %</i>	<i>51 %</i>

Source: Boex (2011), Chimunuane et al. (2010), Chimunuane / Hassam / Weimer (2010a, b); Weimer et al. (2010), Weimer / Hassam / Chimunuane (2010a, b).

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tables on the left present the results for fiscal revenue, and those on the right for non-fiscal revenue.

The figures for *fiscal revenue* show a range of different municipal revenue patterns across the different revenue sources and phases of revenue collection represented by the three ratios.

Concerning IPA, the CVR is quite high in all municipalities, as the taxpayers are known and advised to pay, usually via media. But, as observed above, there is generally little effort to collect the poll tax (particularly low in Vilankulo, Ribáuè and Nacala), and none of the municipalities collect the legally possible rate in full, with the assessment / applied ratio varying between 27 per cent (Nacala) and 74 per cent (Cuamba and Ribáuè). This suggests that this tax is both unpopular and expensive to collect, as we will discuss below.

IPRA is rarely collected, with the exception of Beira, which shows a CVR and a CLR that are way above average, but it has an extremely low AR. With regard to the CLR, whereas the provincial capital of Sofala collects 45 per cent of the IPRA bills, the next best municipality (Cuamba) only collects 12 per cent. The latter's tax effort (and that of Nacala) with regard to IPRA is only 1 per cent, i.e. one-third of that of Beira. For Ribáuè, one of the new municipalities, it makes little sense to start investing in IPRA collection (and ISISA, for that matter), since it has very few taxable buildings.

ISISA collection is only done in Beira, Marromeu, Nacala and Vilankulo, with the CVR and CLR pretty much at the same levels across these municipalities, with a relatively high CVR (84 per cent) for all except Nacala. However, low AR and CLR work together to make this revenue source an underutilised one.

IAV in 2009 – collected by the central government and transferred to the municipalities – is a buoyant source of revenue in all municipalities, with a uniformly high AR of close to 100 per cent. If the CVR and CLR, already between 60 and 80 per cent for both in all cases except for Nacala, could be increased by the municipality's own effort, the performance could even be better, probably with the exception of Ribáuè, which has few taxable vehicles in comparison to all other sample municipalities.

Concerning *non-fiscal revenue*, the figures confirm that **market fees** are consistently well-collected across municipalities, with notable and consistently high collection ratios and coverage ratios for every municipality – Nacala being the exception. This, in turn, suggests that municipalities are generally doing well and have sufficient capacity to administer market fees, which are correctly assessed (AR of 100 per cent in all cases except for Beira and Vilankulo).

For TAE collection, the champion is Marromeu, followed by Vilankulo. Effort is at a medium level in Cuamba and Beira, with Ribáuè not yet having started collection. Again, Nacala is at the lowest rank, basically due to a low CLR.

Finally, the collection of licence fees for DUAT is done quite successfully in Beira and Vilankulo, with little effort noticeable – and thus high untapped reserves – in Cuamba and Nacala, despite the high demand for land in the latter municipality. In the case of Cuamba, this is explained by a very low CVR due to lack of investment in a cadastre (see next section), while the CVR and CLR of under 40 per cent account for the poor performance of

Nacala. Ribáuè, having started to organise a land register, has yet to initiate assessment and collection of DUAT licence fees.

Concluding, we see that the different patterns and results of using the revenue potential not only correspond to the general features of each municipality described by the selection categories for the case studies (see Section 3.1), but also to the individual competencies and preferences gained from the municipalities' experiences since the municipalisation process in 1997. The emerging picture is diverse, and there are considerable differences in the collection of revenues from different sources. With other words, the fact that one municipality is performing well with regard to the collection of one type of revenue does not necessarily mean that it can do so with regard to another. We will see in the next section that a more coherent approach to taxation depends to a large extent on qualities such as leadership, strategic vision and making necessary investments in the tax administration.

5.2.2 Cuamba and Vilankulo: differentiated, comparative within-case analysis

In the next step of comparative analysis, we select two municipalities of the second group of clusters (see 3.1), namely Cuamba and Vilankulo, and examine in more detail their respective structural features and fiscal performance using the *within-case* analysis approach. This comparison allows us to see differences in their fiscal management performance and identify the causes and effects.

The data confirms that Vilankulo has much better fiscal performance than Cuamba, despite having only half of Cuamba's population (Indicator 1) and a third of its area (Indicator 2). Not only does Vilankulo have a much higher absolute (Indicator 4) and per capita budget (Indicator 5) than Cuamba (more than three times), it also raises more tax revenue (Indicator 7), allocates more public investment funds (Indicator 9) and is more sustainable, if we look at the coverage of current expenditure by income generation (Indicator 8).

Cuamba only performs better in the "Own revenue / total revenue" category (Indicator 6). Its own revenue has more weight in total revenue than Vilankulo's. In other words, in recent years, Vilankulo has been more dependent than Cuamba on transfers and grants. One

	Indicators	Cuamba	Vilankulo
1	Population (2009) *	88,032	42,371
2	Area (km ²)	132	43
3	Number of neighbourhoods	11	9
4	Budget – expenditure (2009, MT)	20,553,197	32,025,572
5	Budget per capita (2009, MT)	233.47	755.83
6	Own revenue / total revenue 2005–2009, in %)	28.4%	24%
7	Fiscal revenue / own revenue (average 2005–2009, in %)	10.5%	21%
8	Current expenditure / own revenue (average 2005–2009, in %)	44.7%	49%
9	Capital expenditure / total expenditure (average 2005–2009, in %)	27.4%	56.7%
*baseline: census 2007 = annual population growth rate of 5 per cent			
Source: Weimer (2011), based on Chiminuane / Hassam / Weimer (2010a, b).			

explanation may be that non-tax revenue is higher in Cuamba. Another cause could be that Vilankulo attracted more central government grants and earmarked funds (e.g. the Road Fund) following cyclone *Favio* in 2007. An important factor in this may have been that the Vilankulo mayor has stronger bargaining and lobbying power with central government institutions and external aid organisations than his Cuamba counterpart. He is a well-known businessman and member of the FRELIMO Party Central Committee who is currently serving his third consecutive term, whereas his Cuamba counterpart is serving his first term.²⁵

However, the quality of Vilankulo’s leadership and its economic dynamism as a tourist centre of national and international repute do not explain the considerable difference in fiscal performance in comparison to Cuamba. The key is that Vilankulo is better managed – from a strategic and an operational as well as from a governance point of view.²⁶

The following table delves into the data already presented in the previous section, exclusively for the cases of Cuamba and Vilankulo.

Table 7: Cuamba and Vilankulo – revenue effort and unrealised revenue potential by type of revenue source

I	II		III		IV		V		VI	
Source	Ratios						Tax effort		Unrealised revenue potential	
	CLR		AR		CVR		TE		UP	
Title	Cuama	Vilank	Cuam	Vilank	Cuam	Vilank	Cuam	Vilank	Cuam	Vilank
	%	%	%	%	%	%	%	%	%	%
1. IPA	13 %	11 %	74 %	56 %	80 %	90 %	8 %	6 %	92 %	94 %
2. IPRA	12 %	0.1 %	68 %	30 %	11 %	30 %	1 %	0 %	99 %	100 %
3. ISISA	0 %	50 %	0 %	40 %	0 %	85 %	0 %	17 %	100 %	83 %
4. IAV	55 %	85 %	90 %	90 %	90 %	65 %	45 %	50 %	55 %	50 %
5. DUAT	88 %	65 %	90 %	100 %	10 %	75 %	8 %	49 %	92 %	51 %
6. TAE	72 %	90 %	90 %	100 %	95 %	100 %	62 %	90 %	38 %	10 %
7. MARKETS	60 %	62 %	100 %	90 %	68 %	76 %	41 %	42 %	59 %	58 %

Source: Weimer (2011).

The data confirms, in general terms, the findings of the macro picture presented in the previous chapter: the revenue mainstay is guaranteed by the sources markets and vehicles, as well as DUAT in the case of Vilankulo. The sources not used or rarely used are IPRA and IPA in both municipalities, and ISISA (in Cuamba only).

The results presented in columns V (TE) and VI (UP) show common revenue patterns: both IPA and IPRA are not used or rarely used as revenue sources, and revenues from IAV

25 For a discussion of vertical bargaining power, i.e. in intergovernmental relations as a divisive factor on decentralisation and local governance, see Manor (1999, 81ff.)

26 At the time of writing, the Cuamba mayor bowed to pressures from his electorate and assembly, most likely reinforced by internal mechanisms of the party he belongs to (FRELIMO) and terminated his mandate prematurely, with the consequence that there will be by-elections for his successor. The allegation was “ruinous management of municipal finances”. See: *Edis sucumbem às ordens do partido* [Mayor succumb to orders of party], *O País* [Maputo], Saturday 13 August 2011, <http://www.opais.co.mz/index.php/politica/63-politica/15875-edis-sucumbem-as-ordens-do-partido.html>.

and markets are, roughly speaking, equal in both municipalities. Consequently, there are high reserves concerning IPA and IPRA, but considerable lower ones concerning the taxation of vehicles and markets.

The management of the ISISA tax base, DUAT licences and TAE (highlighted in grey in the table) is very different in the two municipalities. While Cuamba follows the general pattern and does not explore its ISISA base, Vilankulo was able to use 17 per cent of the potential of this source in 2009. Vilankulo municipality also makes better use both of its DUAT base and TAE revenue base.

What is the explanation for this difference?

Looking at the CVR column – an indicator of the coverage and quality of the register – we can see one of the main causes for Vilankulo’s better fiscal performance, concerning DUAT in particular. In Vilankulo, the taxpayer register is better organised, as shown by the CVR ratios for these sources. Even in the case of IPRA – although not collected at present in both municipalities – the Vilankulo Municipal Council has made solid investments in its land and property register with a view to producing a legal instrument to start taxing them (in the case of real estate).²⁷ During fieldwork it was quite clear that over the past few years Vilankulo had made considerable and consistent investments in its Cadastre and Urbanisation Services (SUC) in terms of skilled manpower, technical and office equipment (computers), transport and office working conditions, including archives. And this “strategic investment”²⁸ has had positive effects: the SUC team has a computerised land register of reasonable quality, at present being extended to eventually include buildings / houses, with the former updated occasionally. In comparison, investment in training and equipping the Cuamba SUC in 2000, supported by the (Swiss) Support Programme for Decentralisation and Municipalisation, has had little effect. There is no land and building register other than that produced by the colonial administration and that produced at the time with Swiss assistance, with extremely limited coverage and quality.

As regards ISISA, the Vilankulo MC took the strategic decision to start watching the property market and property transactions and collecting this tax, even though the collaboration and exchange of information with other relevant entities (ATM, Registry Office) was weak initially. The SUC register and the good organisation of this unit certainly facilitated recording transactions and collecting the tax. Cuamba’s Registry and Notary Public Office has no section for recording transactions – a typical case of absent / distant government services in the Mozambican peripheral areas. As the closest department is in Lichinga, about a five-hour drive away, people in Cuamba give up registering their property transactions, preferring an informal transaction approach instead.²⁹ Turning this deficiency into an opportunity, the Cuamba MC could theoretically have invested in improving its registration and cadastral service. But this was an opportunity not considered and thus lost.

27 It was only in July 2010 that the Ministry of Finance produced draft regulations intended to identify the methodology for assessing and updating property values (see footnote 6).

28 Interview with Suleimane Esep Amuji, Mayor of Vilankulo, 12 June 2010.

29 Interview with Mr Estêvão, Registrar in the Cuamba Registry and Notary Public Office 9 July 2010.

The case of TAE revenue confirms yet again the great need for a complete and updated register of taxpayers in the municipality, as demonstrated by the case of Vilankulo. The town council has made considerable investment in establishing an electronic database on business entities and companies, although it is not updated regularly. As Vilankulo is a tourist town, many companies that pay TAE are linked to tourism, and also have to pay IPRA as well as a “tourism tax”. The harmonisation of these taxes and standardisation of the respective registers would benefit both the municipality and the taxpayer.

Investment in urban services and tax registers is the result of the municipal leadership’s strategic vision, its allocation of resources and its negotiating partnerships for this purpose. It is likely that the case of a relatively small town like Vilankulo is a good example of a German proverb *Not macht erfinderisch* (Want stimulates creativity). It seems that the Cuamba leadership’s recent recognition of the vital importance of investing in taxpayer registers came late regarding the mayor’s aborted mandate. It is hoped that the introduction of an IT-supported system of taxpayers’ registers (started in 2010 at the municipal unit of Economic Activity Services), together with updating the (colonial) cadastre for plots and houses and training of technicians – in partnership with the Millennium Challenge Corporation³⁰ – will be sustainable and produce the expected impact on revenue generation.

5.3. Discussion and conclusions on tapping the revenue potential

In this section, we discuss some of the pertinent issues associated with the analysis in this chapter and draw some conclusions, firstly about the three phases of revenue collection, and secondly about the revenue reserves by type of revenue and ways of tapping into it.

First of all, the reader should keep in mind that the method used to estimate the tax effort and, by implication, the estimated unrealised revenue potential results from a mathematical operation. This means that the estimated potential is of a mathematical nature, rather than resulting from a technical or practical effort of actually collecting the revenue. This means that in reality, the tax effort will be less than a maximum of 100 per cent, given technical and material constraints of various dimensions on the ground. The same must be assumed for the percentages for each of the three ratios (CVR, AR, CLR), maybe with the exception of CVR for certain sources of revenue, e.g. those related to land and buildings (DUAT, IPRA and ISISA). As such, the figures given are indicators of the dimension of the revenue reserves rather than an exact calculation of the reserves. Or, in other words, a ratio of 100 per cent is an ideal rather than a realistic proposal. Nevertheless, the percentages presented in the various tables give the municipal leaders and the local taxpayer a fair indication of where the revenue reserves are, what (monetary) dimension they have and – looking at the ratios – where, in the three phases constituting the collection process, improvements are necessary to tap into the reserves.³¹ It should also be borne in mind that more effort in collection also implies additional costs, which would need to be compared

30 Interview with Ms Laurinda, Head of the Economic Activity Service, and Mr Eusébio Costias, Councillor, Urbanisation, Infrastructure and Environment, Cuamba, 9 July 2010.

31 In the practical on-the-job capacity-building work in the municipalities, the tables can be transformed into spreadsheets to be used as “taxation simulators”. They show the change of the yield in one source of revenue as a consequence of altering one or all the ratios of the three phases of revenue collection.

to the additional gain, in terms of tax yield, arising from the additional effort. In certain cases, such as IPA, the latter may not be offset by the former, which may make tapping into the reserve an expensive exercise.

How should we read the results concerning the partial ratios (CVR, AR and CLR), and what are the technical lessons to be drawn from the foregoing analysis? The following three points can be made.

On coverage ratio

The coverage ratio is consistently above 50 per cent across all sources of revenue, except for IPRA and, partially, DUAT. This means that the municipalities, on average, know pretty well where and how to identify their taxpayers, despite anecdotal evidence to the contrary, and that their tax registers are fairly functional, even if not always well-organised and updated.

On assessment / applied ratio

The assessment ratio shows considerably more variability across municipal revenue sources than the coverage ratio. It ranges from 29 to 94 per cent, depending on municipality and type of revenue. Boex has observed that, “*in some sense, this ratio could generally be seen as a popularity index: the less popular a municipal tax, the lower local politicians wish the assessment ratio to be. By lowering the assessment ratio, the effective tax burden (and hence the political price of local taxation) is proportionately lowered*”³² (Boex 2011, 34). The assessment ratio with regard to taxes related to property (IPRA, ISISA) is generally low. Anecdotal evidence (see Section 4.2.2) suggests that there is a major discrepancy between the value of a property declared by its owner to the authorities, and its actual market value, which in general is significantly higher, and which – under this condition – ought to be applied for taxation purposes. A new regulation on IPRA recognises this “assessment risk” and tries to mitigate it by establishing an Annual Municipal Property Evaluation Commission to verify the veracity of the value declared by the property owner.³³

On collection / compliance ratio

This ratio shows the greatest variability for different municipal revenue sources. It may be seen to be influenced by three factors: i) the popularity of a certain tax or fee, ii) the technical degree of collecting it, iii) the effectiveness and transparency (or lack thereof) by which the municipal tax administration is collecting and accounting for it, and, iv) the inclination of the local taxpayer to pay her or his dues, taking into account what was referred to above as the Wicksellian Link. With regard to the first factor, IPA – highly unpopular and with a connotation of coercive colonial taxation – is a good example. For this reason, a number of municipalities do not put a major effort into collecting this tax – although, for smaller ones, such as Ribáuè, it represents an important source of revenue and is often

32 In the case of IPRA, if the assessed value of the taxable property is self-reported (or can be influenced by the taxpayer), then a low assessment ratio could also be an indication of tax evasion.

33 IPRA regulation, Decree 61/2010 of December 27.

collected coercively.³⁴ As we have seen, the collection of IPRA is, technically speaking, a complicated matter for which even almost all Mozambican municipalities are ill-equipped and thus abstain from collecting it. The aforementioned introduction in 2010 of a regulation on the establishment of (market) values of urban property is aimed at assisting the municipalities in making use of the revenue source with the largest potential. The question of the local political economy also play a role: for IPRA, the average value of the CVR is considerably higher than that of the CLR, which is the lowest of all revenue categories. This suggests the existence of two phenomena: firstly, a (technical) effort is made to produce a register, but without accompanying political drive to actually collect this tax. And secondly, the collection of other taxes and fees are given priority over property taxes. Both factors may be linked by suggesting that the strata of property-owning citizens exert political influence to minimise the incidence of taxation on their property.

As for the effectiveness and transparency of the municipal tax administration machinery, it is generally assumed that practices of corruption and embezzlement of public money are not foreign to municipalities. The aforementioned studies (Ilal 2006, 2007) show that up to 50 per cent of revenue collected from municipal markets is not registered in their treasury accounts, but remains in the private pockets of dishonest tax collectors and their supervisors. Disciplinary and legal methods of curbing such practices do exist; however, it often requires political courage and clout of municipal leaders to use them. The general public is quite aware of such illicit practices (de Brito et al. 2007) and point to them, on occasion, to justify their lack of willingness to pay their taxes or fees. The same study suggests that the same is true for withholding, as best as possible, payment for services that are of inadequate, irregular or poor quality. With other words, the compliance / collection ratio could be higher if local accountability was better and if there were a greater correspondence between public services offered and taxes and fees raised.

But gradually reducing the volume of the unrealised revenue potential is foremost a question of **technical capacity**. Particularly the comparative analysis of the two case studies, Cuamba and Vilankulo, stresses the importance of strategic and operational planning and institutional capacity-building as being instrumental for increasingly tapping into the unrealised revenue potential and thus improving the ratio between own-source revenue / total revenue. Already in the 2009 study on the lessons of a decade of municipalisation (ANAMM / World Bank 2009), the authors had made pertinent observations to this effect, suggesting that:

- the generation of own revenue can be improved, particularly with regard to property taxes (IPRA) in urban areas;
- non-tax revenue could also be increased considerably through better management;
- collaboration between the central government and local authorities in collecting and administering ISISA and IAV should be improved;
- heavy investment is required to develop and improve financial management systems in the municipalities;

34 For example, citizens wishing to obtain a certain official document or other service from their local authority have to produce the IPA tax receipt as a precondition to receive the requested service.

- focussing on own tax base and technical aspects, the obvious must be repeated: realising the full fiscal potential requires investment in the institutional capacity to collect and manage its own resources, i.e. human resources, technical and computer resources as well as tax registers. Training in fiscal and financial management and the retention of municipal technical staff have a vital role to play. What is particularly needed is an integrated register / cadastre on land and property that makes it possible to track the history of a plot of land from demarcation to granting of the DUAT licence, the construction of a building and its registration as well as every eventual building transaction. This would allow the payment of a one-time fee (DUAT) for a plot of land to be replaced by an annual tax (IPRA) on the building erected and complemented by ISISA when the property is sold or transferred. The necessary investment in increased capacity would be well-invested public money, since it produces a permanent (annual) flow of return that would surpass by far the initial investment cost and enable the MC to invest in serviced land development and infrastructure, to the immediate benefit of taxpayers.

The choice of the main revenue sources – and investment in the institutional capacity to collect them – should observe the criteria established for the collection of an optimum of own revenue. Bird and Vaillantcourt (1998, 13) emphasise, among other aspects, a preference for property-based revenue with variable rates reflecting the behaviour of expenditure (“buoyancy”) and with a technical approach to collection that is both fair and effectively administered. Others compare municipal tax administration to a “production process” directed by the Municipal Council that needs a solid base of qualified staff with well-defined responsibilities, an information base and clear rules that are easy to administer and comprehend and include penalties for violation. The taxpayer should be viewed as a customer, meriting a simple and didactical approach to taxation (Bird 2004).

These criteria suggest that of the municipalities’ unused resources, IPRA associated with DUAT is one of the preferred options, at least in medium and large municipalities and even in rural areas (Bird / Slack 2006). As regards the effectiveness of collection, the overall pattern of property taxation leads to the conclusion that the bulk of the IPRA’s potential can be achieved through taxation that focusses solely on buildings for residential, commercial and tourist purposes in areas with good accessibility, urban services and a cadastral register. This means that these areas have a medium to high property value compared to most buildings in the municipality’s rural and peri-urban areas. In other words, on the whole the tax effort that targets top-quality buildings earns much more than the one taxing lower-value buildings, as well as being more economical in terms of tax administration costs. This argument also takes into consideration the fact that consumption of municipal services is usually greater in high-cost areas. Further, collection of IPRA could be combined with that of TAE. The latter, as a municipal tax on business turnover, is the most appropriate form of taxation in other countries.

Following the same logic of maximising effects and minimising costs, one could consider abolishing IPA, as it is, as discussed above, an economically and politically costly tax to collect, as well as having regressive effects with a negative impact on national and local poverty-reduction policies.

Other measures that could increase the institutional capacity of local authorities include:

- the creation of a specific tax unit in the municipal administration and finance departments, and a review of collection, accounting, audit and revenue administration procedures and instruments, including innovative methods for managing markets;
- the admission and training of qualified technicians in this unit, for example, on taxation legislation and techniques, etc.;
- consolidation and systematic use of computers, electronic spreadsheets and eventually the introduction of the Municipal Management System (Sistema de Gestão Municipal). In addition to having an accounting engine for managing expenditures, revenues and assets that is aligned with norms established by the State Financial Management System (Sistema da Administração Financeira do Estado), it has several municipal management modules (such as markets, registers, payrolls, budgeting, bank reconciliation, etc.).³⁵
- the eventual transformation of TAE into a local tax on business based on turnover. As we can see in the case of Brazil (next section), this kind of tax can be one of the main sources for local governments, especially in cases where there is a growing and dynamic local economy. In China the local business tax was part of a tax reform that, together with other elements, produced enterprising local governments and impressive local economic dynamics (Hi 1992).

Obviously, the use of an improved tax base associated with a review of the tax structure (e.g. the abolition of IPA) has costs: the expenditure required for the above-mentioned investment in capacity-building will mean increased current budget expenditure. But given the size of the expected additional revenue that this investment brings, the net cost-benefit effect may well be positive. The Vilankulo case study clearly supports this conclusion.

6 Conclusions

6.1. Considerable revenue reserves

Let us take another look again at Table 5 of the previous section. It shows the existence of an untapped fiscal reserve that, in monetary terms, is equivalent to roughly three times the own revenue collected in 2009, and roughly five times the amount collected from the seven income sources examined in this study. Comparing the unrealised revenue potential with expenditure, we can conclude that the sample average in 2009 was almost equivalent to total expenditure and nearly four times the capital expenditure analysed in the study.

The analysis of the previous section has demonstrated why – from a technical and institutional point of view – that huge potential resource is insufficiently exploited.

This implies that the partial use of the tax base, at an average 24 per cent of the maximum possible, has high opportunity costs in terms of lost investment in public services. The

35 The development of the “second generation” Municipal Management System has been supported by the P-13 in collaboration with the municipalities of Nacala and Mocuba (Zambézia Province), in collaboration with the Centro de Desenvolvimento de Sistemas de Informação Financeira of the Ministry of Finance, as entity for certification of the various modules of the Municipal Management System.

municipalities fail, in part, to produce and deliver basic public services, as on average their expenditures only cover 32 per cent of their budgets for capital expenditures and investment. So they partially fail to perform their essential function, the *raison d'être* of their creation through legislation in 1997. However, this conclusion does not disregard the difference that local authorities have made and continue to make as compared to the *status quo ante*, i.e. the provision of services by the then Executive Councils, before the commencement of the municipalisation process. After 10 years of decentralisation, this observation is undeniable (ANAMM / World Bank 2009, 6 ff.). Nevertheless, the municipalities could have done much better had they increasingly used their own tax base. *Ceteris paribus*, they could have increased the value of their budgets for infrastructure investment, services and capital expenditures up to four times. Answering the question referred to in Section 1, namely whether municipalities would learn to “walk without a borrowed walking stick”, the answer clearly is yes, if they wanted to and could get used to using their own muscles instead of waiting for help from either the central government or donors.

This analysis leads us to conclude that making the most of the current real tax base potential of Mozambique's municipalities would transform local authorities into viable and financially sustainable local governments, with substantial resources for investment. This does not question the logic and volume of central government transfers, which is to be considered another part of their resource base that municipalities are entitled to. It would have allowed all transfers to be used for institutional capacity-building, staff training, attracting more qualified staff, the preparation of structure and environmental protection plans, housing projects or for supplementing investments funded by their own resources.

The tax collection hitherto ignored can trigger a dynamic all of its own, as has happened in many cities in the world. In Brazil, for example, in the first 10 years after the promulgation of the 1988 constitution,³⁶ local authorities' own resources grew 197 per cent. “*The average annual growth of local government own revenues was so dynamic, it was 2 to 3 times higher than the federal and state tax growth rate*” (Afonso / Araújo 2000, 21). Even small towns and poor areas were not left behind: “*the increased revenue is usually explained by simple rules and starting to collect taxes and fees, as most of these units were not charged anything a decade ago*” (ibid.).

In the late 1990s in Brazil, the most significant revenue sources were: a tax on the sale of services – a kind of TAE that takes into account a company's turnover (contribution to own revenue: 37.5 per cent); the Urban Building and Land Tax (28 per cent); fees for the provision of municipal services (15 per cent); and the Property Transfer Tax, the Brazilian equivalent to ISISA, with 6.8 per cent. Among the most dynamic sources are those related to land use, construction and the sale of property – sources that are badly neglected by Mozambique's local authorities.

6.2. Revenue potential and sustainability

The data presented and discussed in Sections 3 and 4 clearly showed that one of the structural deficiencies of municipal revenue is the low incidence of fiscal revenue collection

36 The 1988 Brazilian Constitution determined that Brazilian local authorities were part of the federation.

(taxes), implying a comparatively high reliance on non-fiscal revenue (mainly fees and licences). On average, the sample municipalities only generate around 15 to 16 per cent of their own-source revenue from taxes. This is corroborated by a study that examines a sample of 13 of the 43 municipalities, including those selected for the present study (Nguenha / Raich / Weimer 2011). This factor contributes to a high degree of dependence on transfers and donations, as measured by the ratio of non-own-source revenue / total revenue. In the case of the sample municipalities, this ratio is around 63 per cent of total revenue (see Figure 1), whereas in the larger sample, which includes major towns and cities (including Maputo) supported by major donor financed programmes, the value is around 70 per cent.

These figures, however, do not necessarily explain sustainability, since they do not relate recurrent revenues to recurrent expenditures, which would serve as a measure for the capacity of a local government to generate enough of its own resources to cover its operating expenses (recurrent expenditures). This measure, however, was not examined in the data set analysed in the previous sections. Therefore, I suggest gleaning the study referred to above for a proxy answer. This study suggests – on the basis of a larger sample – that Mozambican municipalities consistently cover more or less half of their regular operating costs / recurrent expenditures with their own-source revenue, with a variation between 80 per cent for municipalities with a large tax base, such as Maputo, and 30 per cent in the case of those with a more limited base (Nguenha / Raich / Weimer 2011). Undoubtedly, a better use of their own revenue reserves, especially their tax base related to property, would make the municipalities more sustainable – an objective that should be within reach, given the large untapped reserves.

6.3. On the political economy of the use of the revenue potential

Aspects associated with the political economy of taxation are more complex and politically charged. Achieving full taxation potential involves more than just the choice of appropriate technical instruments and the MC's institutional tax administration capacity. Public finance – as expressed in the composition of budgets in general (expenditure or revenue), and taxation in particular – has a political dimension. For governments, this involves making political choices that produce desirable political and socio-economic consequences for society and the citizen as a taxpayer, consumer, voter and entrepreneur, with a special emphasis on the private sector.

Taxation patterns reflect social power relations, so any change in the composition of the budget and taxation have direct and indirect effects on these relations. For example, starting to collect IPRA means changing the tax burden to the detriment of the property-owning (buildings, land) social classes and strata, while abolition of IPA will lighten the tax burden of the poorest. The analysis in the previous chapter suggests that the predominance of certain sources of revenue (market fees, IAV, TAE) implies a considerable tax burden for the poorer strata of the municipal populations, whereas the burden is lower for the property-owning (land, buildings) socio-economic classes, i.e. the local elite.

As regards underutilisation of the local tax base, politicians and local leaders face a dilemma: on one hand, there is a tendency to avoid increasing their own tax efforts, on the grounds that taxes are unpopular and can jeopardise re-election (or they appeal to the cen-

tral government to increase its transfers). On the other hand, they are aware that the lack of revenue prevents the provision of public goods and services. So they have to choose between increasing revenue to provide better services or doing without any additional tax efforts, resulting in poor – quantitatively and qualitatively – public services. The topic of “institutional congruence” (Wicksell) between taxation and the municipal services provided, is not just a classic subject in public finance (Levi 1988).

Consequently, a municipality that uses its tax potential to generate revenue predominately for the consumption of a small local elite without producing anything equivalent in terms of better roads, services, water supply and sanitation systems, etc., will fail to address the reason for its existence. This failure will have a variety of consequences, including: the municipal government’s loss of legitimacy, tax evasion by the municipal citizen, a fiscal budget gap between revenues and expenditures, poorly and inefficiently managed public goods and abstentions in local elections, or even the “sacking” of its mayor. The recent dismissals of six mayors and the necessary by-elections that followed in the respective municipalities suggest that in a setting such as Mozambique, the mayor has a mandate arising from democratic elections, and is not only accountable to the electorate, but also to the party he belongs to.

One possible way out could involve municipal citizens participating in the urban planning and budgeting process, or the notion of the “fiscal contract” (Moore 2008), based on reciprocity and fiscal bargaining over municipal services (Hoffman / Gibson 2005). As regards strengthening the state and local society, there is talk of “embedding” taxation in the socio-economic fabric through a binding social contract between local government and economic agents (Braeutigam 2008, 30), professional and economic associations, among others (Joshi / Ayee 2008). This is as important as the transparent, efficient and effective management of municipal finance and, above all, the production and maintenance of public goods and services to be enjoyed by all taxpayers – in correspondence to the collected revenue and the use of the municipality’s own tax base. Municipal citizens’ participation in the formulation of urban planning instruments will provide municipal authorities, organised civil society, the private sector and local residents in general an opportunity to clarify their interests, to understand the interests of others, to make proposals and set their priorities. Municipal leaders who want to better engage their citizens can draw on a number of experiences of participatory planning and budgeting (Roque / Tengler 2000; Weimer / Nguenha 2004; PROGOV 2008; Nguenha 2009).

As regards the questions raised at the beginning of this study, the answers can be summarised as follows.

- The municipalities have an institutional framework that, in theory, gives them considerable fiscal autonomy – one of the key criteria for successful, integrated fiscal decentralisation (Faust / von Haldenwang 2010).
- They have a wide range of revenue sources and, thus, a theoretically sufficient resource base for their devolved functions, including potentially buoyant taxes linked to the use and occupancy of land and the taxation of buildings. However, they do not make sufficient use of it, both for technical reasons linked to the crucial phases of collection and for reasons of the political economy and the local power relations.

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- The analysis of the revenue collection pattern lets us conclude that the main sources of revenue collected (market fees, IAV, TAE) burden the poorer strata of local society and have less of a tax burden for property-owning (land, buildings) socio-economic classes, i.e. the local elite, since property tax is rarely collected.
- The underutilisation of their own resources makes the municipalities (unnecessarily) dependent on non-own-source revenue (transfers and donations) and jeopardises their already weak sustainability.
- Above all, the underutilisation of their own-source revenue deprives the municipalities of resources for public investment and services, crucial for their legitimacy and that of the elected mayors.
- There is some evidence of positive experiences and growing institutional and instrumental capacity for the collection and management of revenue, as well as practical experience of some participatory approaches in planning and budgeting.

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