Policy Research Working Paper 9032

# Innovations in Tax Compliance

## Conceptual Framework

*Wilson Prichard*
*Anna Custers*
*Roel Dom*
*Stephen Davenport*
*Michael Roscitt*

WORLD BANK GROUP
Macroeconomics, Trade and Investment Global Practice
&
Governance Global Practice
October 2019

Policy Research Working Paper 9032


## Abstract

This paper presents a conceptual framework for developing more effective approaches to tax reform and compliance. The framework proposes that by combining complementary investments in enforcement, facilitation, and trust, reformers can not only strengthen enforced compliance but can also (a) encourage quasi-voluntary compliance, (b) generate sustainable political support for reform, and (c) create conditions that are more conducive to the construction of stronger fiscal contracts. A key challenge for governments lies in finding the right combination of these three measures—enforcement, facilitation, and trust—to achieve revenue and broader development goals. The framework proposes greater reliance on locally grounded binding constraints analysis, coupled with careful attention to understanding politics and the drivers of trust in particular contexts, to guide analysis of how best different investments may be combined, prioritized, or sequenced. This framework can help policy makers to think about the right combination of strategies in specific contexts, and thus to allocate resources most effectively.


This paper is a joint product of the Macroeconomics, Trade and Investment Global Practice and the Governance Global Practice. It is part of a larger effort by the World Bank to provide open access to its research and make a contribution to development policy discussions around the world. Policy Research Working Papers are also posted on the Web at http://www.worldbank.org/prwp. The authors may be contacted at acusters@worldbank.org and sdavenport@worldbank.org.

# Innovations in Tax Compliance

# Conceptual Framework

**Wilson Prichard, Anna Custers, Roel Dom, Stephen Davenport and Michael Roscitt**

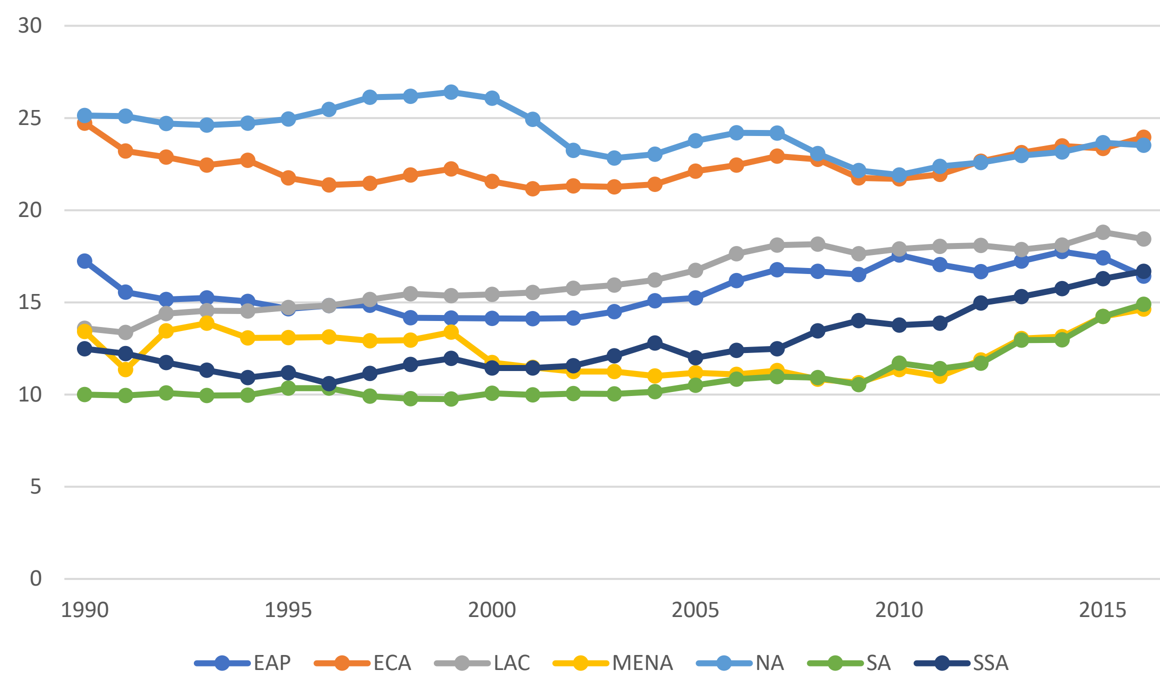
JEL: H26, P16, D73
Keywords: Tax compliance, political economy, trust, policy reform.

## TABLE OF CONTENTS

## INTRODUCTION

Questions of how to effectively reform and strengthen tax systems have moved to the center of development debates. On one hand, there is an opportunity to build on the successes of tax reform efforts in recent decades. Across much of the developing world, countries have achieved significant administrative and policy modernization, and meaningful improvements in revenue mobilization. On the other hand, successes have been uneven, and major challenges remain. Tax revenue in many countries remains well below the levels needed to finance the achievement of the sustainable development goals, with 15 percent of GDP often cited as a rough annual target (Figure 1).[1] Meanwhile, revenue collection is frequently characterized by significant unfairness and inequity, with particularly weak compliance and enforcement among the rich, and often significant – though overlooked – formal and informal burdens on lower income groups.[2]

**Figure 1: Total Non-Resource Tax Collection by Region, 1990-2016 (% of GDP)**




*Source:* International Centre for Tax and Development/UNU-WIDER Government Revenue Dataset

Observers have questioned whether recent improvements in revenue collection have contributed to the construction of broader "fiscal contracts". Revenue collection is not an end in itself. It only becomes socially desirable if it is translated into efficient and effective spending by governments. There is now extensive research documenting the ways in which the expansion of taxation may spur greater accountability and contribute to state building. Yet the research makes clear that while

---

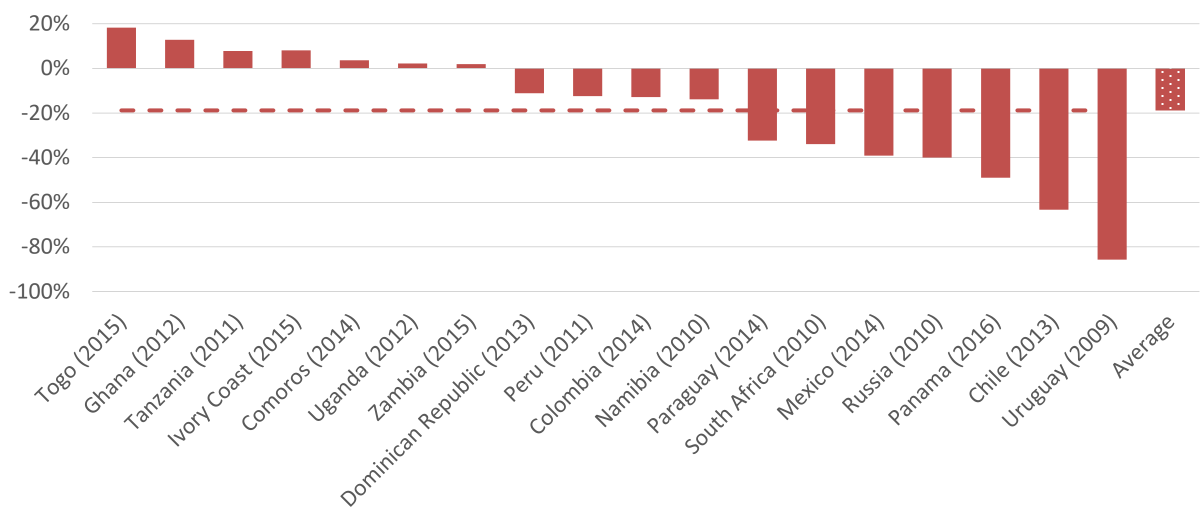
[1] Gaspar, V., Jaramillo, L and Wingender, P. (2016) Tax capacity and growth: is there a tipping point? *IMF Working paper* WP/16/234. Washington DC: International Monetary Fund.

[2] Moore, M., & Prichard, W. (2017). How can governments of low income countries collect more tax revenue? *ICTD Working Paper 70.* Brighton: International Centre for Tax and Development.

there have been real success stories, a strong connection between taxation, responsiveness, accountability and state building is far from guaranteed.[3] Questions remain about whether current reform efforts have focused sufficiently on fostering broader development gains.[4]

The limited focus on building fiscal contracts is evident in scant fiscal redistribution in many low-income countries and correspondingly limited trust in tax systems. OECD data point toward far lower levels of fiscal redistribution among new members from the Global South.[5] Looking more deeply, while simulation estimates are inevitably imperfect, the Commitment to Equity Institute has sought to estimate total fiscal redistribution through taxes and direct transfers at the country level. The pattern is striking: while middle-income countries sometimes achieve significant reductions in extreme poverty, this is not the case for lower-income countries, where direct fiscal redistribution is limited by heavy reliance on indirect taxes and weak transfer systems (Figure 2). While the impact of taxes on poverty reduction likely looks more encouraging when the in-kind value of all public services funded by government revenues is considered, there remains ample evidence that service delivery targeting the poor is frequently ineffective.[6] Unsurprisingly, evidence of inequitable tax burdens and poor translation of revenue into services is reflected in limited trust in tax systems in much of the low-income world (Figure 3).

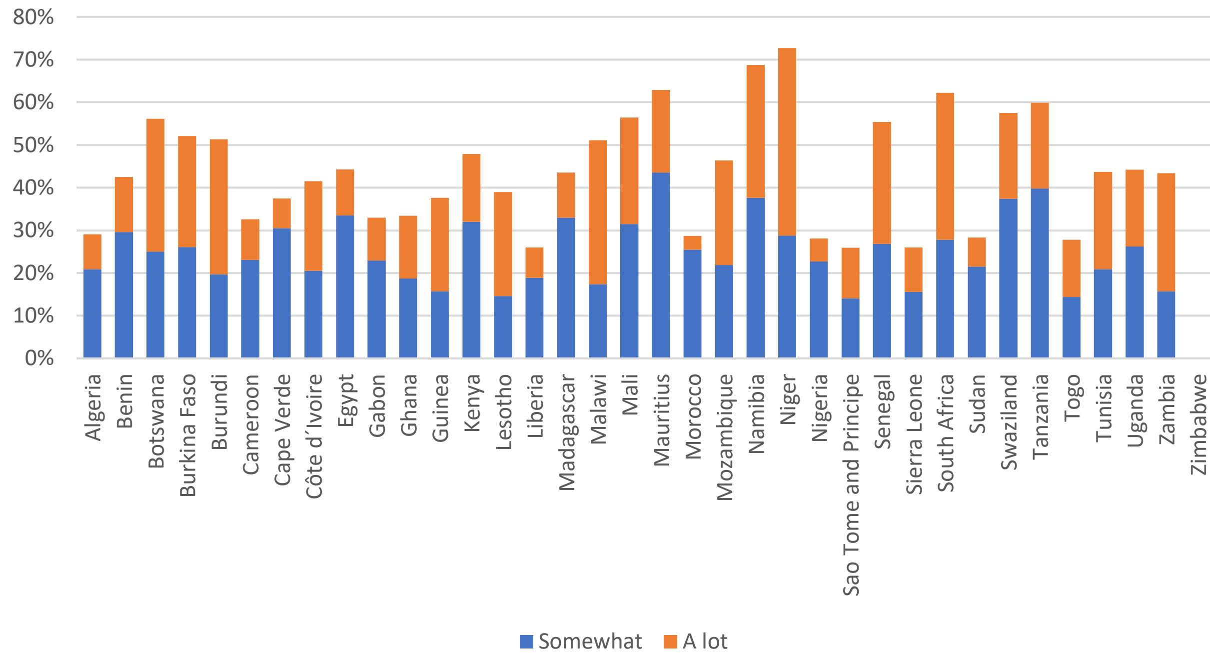
**Figure 2: Estimated Reductions in Extreme Poverty from Taxes and Transfers**




*Notes*: The poverty line is defined as $1.9 PPP/day. Positive values imply an *increase* in extreme poverty after taxes and transfers.
*Source*: Jellema, Lustig, and Papelbon (forthcoming).[7]

[3] Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining*. Cambridge: Cambridge University Press.
[4] Ibid; Prichard, W. (2016). What have we learned about taxation, state building, and accountability? *ICTD Summary Brief 4*. Brighton: International Centre for Tax and Development.; Prichard, W. (2010). Taxation and state building: Toward a governance focused tax reform agenda. *IDS Working Paper 341*. Brighton: Institute of Development Studies.
[5] OECD (2019). Income inequality (indicator). doi: 10.1787/459aa7f1-en (Accessed on 14 June 2019).
[6] Hirvonen, K., Mascagni, G., & Keetie Roelen. (2018). Linking taxation and social protection: Evidence on redistribution and poverty reduction in Ethiopia. *International Social Security Review*, *71*(1), 3-24.
[7] Lustig, N., Jellema, J., & Martinez Pabon, V. (Forthcoming). Leaving No One Behind: Can Tax-funded Transfer Programs Provide Income Floors in Sub-Saharan Africa? in Kharas, H and McArthur, J. (Eds.). *Leave No One Behind*. Washington: Brookings Institution Press.

**Figure 3: Trust in the Tax Department (% of respondents)**




*Notes*: Respondents were asked: "How much do you trust each of the following, or haven't you heard enough about them to say: The tax department?" (% who say "Somewhat" and "A lot"). Afrobarometer R6 2014/2015 (Algeria, Benin, Botswana, Burkina Faso, Burundi, Cameroon, Cape Verde, Côte d´Ivoire, Egypt, Gabon, Ghana, Guinea, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritius, Morocco, Mozambique, Namibia, Niger, Nigeria, Sao Tome and Principe, Senegal, Sierra Leone, South Africa, Sudan, Swaziland, Tanzania, Togo, Tunisia, Uganda, Zambia, Zimbabwe). *Source:* Isbell (2017) based on Afrobarometer.

The central challenge facing reformers lies in identifying innovative strategies to strengthen revenue mobilization, trust, and fiscal contracts. Recent research points toward potential elements of a strategy to strengthen the links between revenues and public benefits, including a greater emphasis on building trust and tax morale among taxpayers, expanded attention to the political challenges of reform, efforts to better tailor reform to local contexts and needs, and clearer focus on empowering taxpayers. However, these strands of research have been somewhat fragmented, and have yet to be consistently applied in practice or translated into an overarching vision for reform.

The Innovations in Tax Compliance project develops an integrated framework to expand our understanding of more effective approaches to tax reform. This is best understood not as an effort to fundamentally rethink what we know about tax reform, but, rather, to provide a coherent framework for tax reform by bringing together – and consistently operationalizing – recent research on the drivers of tax compliance, trust and fiscal contracts, with lessons from the field.

Traditionally, approaches to reform have stressed the importance of technical measures to strengthen enforcement and, more recently, facilitate tax compliance. This focus has reflected early models of tax compliance, which presented the decision to comply as the product of a rational economic calculus: a taxpayer's decision to comply is a function of the perceived probability of an audit, the extent of penalties, and a taxpayer's risk aversion. Stronger detection and higher penalties were thus the keys to inducing compliance.[8] Over time these models came to be complemented by an expanded focus on facilitating tax compliance, recognizing that taxpayers were more likely to comply when doing so was straightforward and low cost, thus shifting the rational economic calculus in favor of compliance.[9]

This focus on enforcement and facilitation has underpinned a range of desirable reforms across the developing world, along with modest, but consistent, revenue gains. Efforts to strengthen enforcement have included investments in building expanded assessment and audit capacities, new IT systems designed to reduce the scope for avoidance, improved collection methods, efforts to expand access to third-party information, and policy changes designed to reduce the scope for evasion.[10] Meanwhile, efforts to facilitate compliance – and emphasize "customer service" – have correspondingly sought, among other aims: (a) to simplify tax systems, and related reporting requirements; (b) to provide easy access to information about tax liabilities; (c) to provide access to support and advice; (d) to provide simple methods for making tax payments, including online, at banks and via SMS; and (e) to reduce face-to-face interactions with tax collectors, which have historically caused delays and increased the risk of abuses.[11] The priority given to these issues is reflected, for example, in the World Bank's Doing Business surveys, which track the difficulty of tax compliance for businesses.[12] Finally, reform efforts have not only targeted tax *payers*, but also sought to improve the effort and performance of tax *officials*, in order to reduce collusion, corruption and simple shirking. These have included pay increases, performance contracts, increased monitoring, efforts to reduce opportunities for corruption and collusion, and a broad emphasis on strengthening the "customer orientation" of tax administrations.[13]

However, despite important successes, efforts to strengthen enforcement and facilitation have not been sufficient to deliver more effective, equitable and accountable tax systems. The taxation of the wealthy remains highly ineffective in much of the developing world, with collection of personal income taxes at only about a quarter of the levels found in OECD countries – this represents the largest gap in comparative revenue mobilization (Figure 4). Subnational tax systems generally fail to generate significant revenues, especially from property taxes, while in areas of weak governance there is mounting evidence of heavy burdens on lower income groups created by user fees and demands for informal payments.[14] While value-added taxes have been hailed as

[8] Cummings, Ronald, G., Martinez-Vazquez, J., McKee, M., & Torgler, B. (2009). Tax morale affects tax compliance: Evidence from surveys and artefactual field experiment. *Field Experiments in Economics*, 70 (3):447-457.

[9] Alm, J., Cherry, T., Jones, M., & McKee, M. (2010). Taxpayer information assistance services and tax compliance behavior. *Journal of Economic Psychology,* 31 (4):577-586; Alm, J. & Torgler, B. (2011). Do ethics matter? Tax compliance and morality. *Journal of Business Ethics*, 101:635-651.

[10] Slemrod, J. (2018). Tax compliance and enforcement. *NBER Working Paper No. 24799*. National Bureau of Economic Research.

[11] Fjeldstad, O.-H. & Moore, M. (2008). Tax reform and state building in a globalized world, in D. Brautigam, O.-H. Fjeldstad & M. Moore, (Eds), *Capacity and Consent: taxation and state building in developing countries*. Cambridge: Cambridge University Press, 235–60.

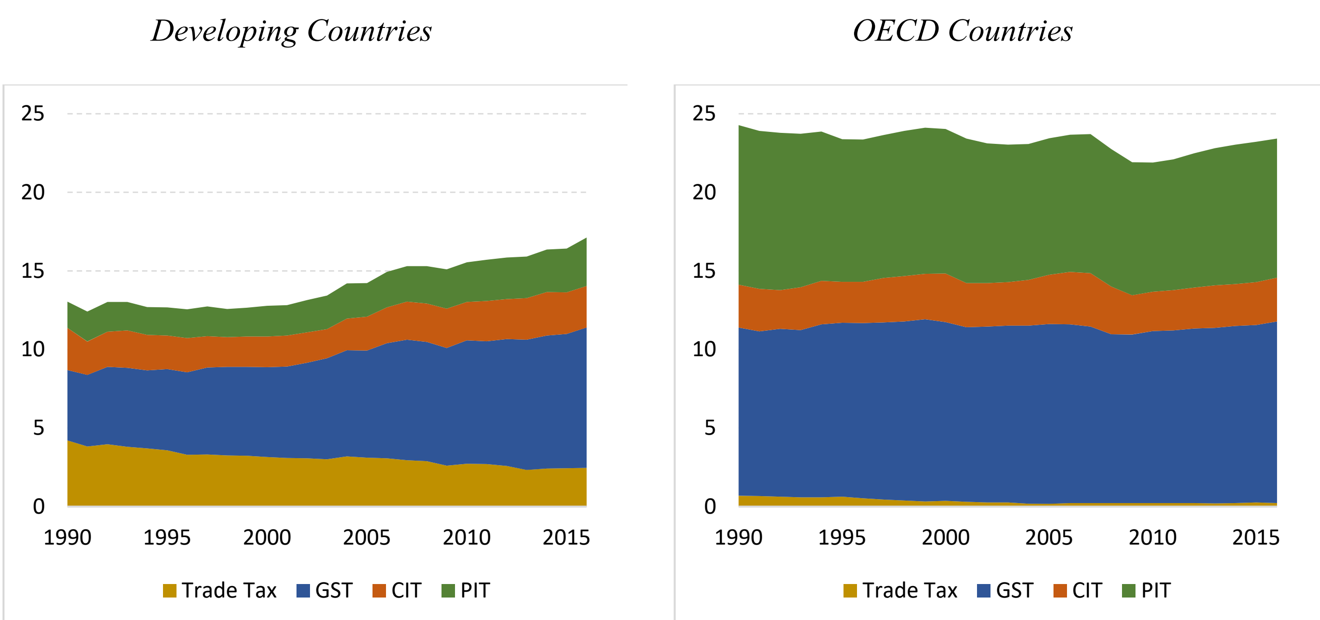
[12] World Bank & PwC. (2018). Paying taxes 2019: Fourteen years of data and analysis of tax systems in 190 economies: How is technology affecting tax administration and policy? Washington: The World Bank.

[13] Mookherjee, D. (1998). Incentive reforms in developing country bureaucracies: lessons from tax administration. *Annual World Bank Conference on Development Economics 1997*, Washington: World Bank, 103-138; Fjeldstad, O. H. (2003). Fighting fiscal corruption: lessons from the Tanzania Revenue Authority. *Public Administration and Development: The International Journal of Management Research and Practice*, 23(2), 165-175; Raballand, G., Chalendard, C., Fernandes, A., Mattoo, A., Rijkers, B., (2017). Customs Reform and Performance Contracts: Early Results from Madagascar. *Governance Notes, No. 2*.

[14] Bird, R. (2011). Subnational taxation in developing countries: A Review of the Literature. *Journal of International Commerce, Economics and Policy*, 2 (1):139-161; Franzsen, R., & McCluskey, W. (2017). *Property tax in Africa: Status, challenges and*

a relative success, in lower-income countries their performance has still lagged behind expectations, with c-efficiency ratios (which measure collection relative to potential) in Africa far below other regions (Figure 5).[15] Corporate tax collection continues to be plagued by extensive and poorly managed exemptions, despite decades of international pressure for enhanced transparency, and recent estimates suggest that revenue losses as a result of international tax evasion and avoidance are larger as a share of GDP in developing countries than in OECD member states.[16] Meanwhile, institutional reforms aimed at strengthening IT systems,[17] limiting political interference, reducing corruption,[18] and improving transparency and expanding engagement[19] have frequently underperformed. Finally, surveys reveal that trust in tax systems remains sharply limited, undermining compliance and the potential for constructing broader political support for reform (Figure 3, above).[20]

**Figure 4: Composition of tax revenue in developing and OECD countries, 1990-2016**




*Source:* ICTD /UNU-WIDER Government Revenue Dataset

---

*prospects*. Cambridge, MA: Lincoln Institute for Land Policy; van den Boogaard, V., Prichard, W., & Jibao, S. (2018). Informal taxation in Sierra Leone: Magnitudes, perceptions and implications. *African Affairs* 118(471): 259–284.

[15] Keen, M. (2013). The anatomy of the VAT. *IMF Working Paper 13/111*. Washington: International Monetary Fund.

[16] Cobham, A., & Jansky, P. (2017). Global distribution of revenue loss from tax avoidance: Re-estimation and country results. *WIDER Working Paper, no. 2017/55.* Helsinki: United Nations University World Institute for Development Economics Research.

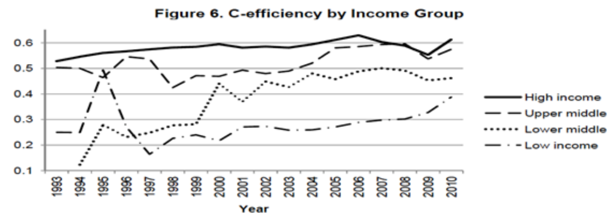
[17] Bird, R., & Zolt, E. (2008). Technology and taxation in developing countries: From hand to mouse. *National Tax Journal*, 4 (2):791-821.

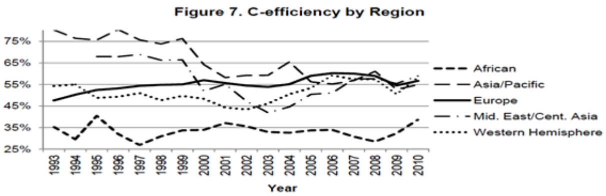
[18] Ahlerup, P., Baskaran, T., & Bigsten, R. (2015). Tax innovations and public revenues in Sub-Saharan Africa. *Journal of Development Studies*, 51(6): 689-706; Dom, R. (2019). Semi-autonomous revenue authorities in Sub-Saharan Africa: Silver bullet or white elephant. *The Journal of Development Studies*, *55*(7), 1418-1435

[19] Moore, M. (2014). Revenue reform and state building in Anglophone Africa. *World Development,* 60: 99-112.

[20] Aiko, R., & Logan, C. (2014). Africa's willing taxpayers thwarted by opaque tax systems, corruption. *Afrobarometer Policy Paper 7*.

**Figure 5: VAT C-Efficiency Ratios by Income Group and Region**




*Source*: Keen (2013)

To advance a more effective reform agenda, research has challenged traditional approaches, focusing instead on non-pecuniary drivers of tax compliance, the politics of reform, and building fiscal contracts. First, there is now extensive evidence that non-pecuniary drivers of compliance ("tax morale") – rooted in ethics, social norms and views about the fairness, equity, reciprocity, and accountability of tax systems – are a critical determinant of the extent of tax compliance.[21] Second, it is now widely accepted that the key barrier to many types of tax reform – and, perhaps most notably, to better taxing elite groups – lies in staunch political opposition, and the difficulty of mobilizing pro-reform coalitions.[22] Third, it is increasingly recognized that expanded taxation can be a catalyst for strengthening citizen demands for responsiveness and accountability, but that such positive outcomes depend on making the strengthening of accountability an explicit focus of reform programs and reform design.

Expanding efforts to build trust in tax systems is likely to be pivotal. Expanded trust can yield benefits that cut across diverse challenges: improving taxpayers' willingness to pay, strengthening political support for reform, and contributing to the construction of a broader fiscal contract. While existing research has conceptualized trust in diverse ways, it is useful to think of four broad components of trust, capturing the extent of taxpayer beliefs that: (a) tax systems are fairly and competently designed and administered ("fairness");[23] (b) burdens are equitably distributed, and everyone pays their share ("equity");[24] (c) tax revenues will be translated into reciprocal publicly

[21] Given the limited enforcement resources available to most governments, observed compliance rates are higher and inconsistent with what rational compliance calculations would predict. Cummings, R. G., Martinez-Vazquez, J., McKee, M., & Benno, T. (2009). Tax morale affects tax compliance: Evidence from surveys and artefactual field experiment. *Field Experiments in Economics*, 70 (3):447-457. A range of other factors are found to be relevant, for a recent overview, see Alm, J. (2018), What Motivates tax compliance? *Journal of Economic Surveys,* no. 33(2).
[22] As is also highlighted in the WDR 2017: World Bank Group. 2017. *World Development Report 2017: Governance and the Law.* Washington, DC: World Bank. See further: Fairfield, T. (2015). The political economy of progressive tax reform in Chile. In Mahon, J., Bergman, M., & Arnson, C. (Eds.,). *Progressive Tax Reform and Equality in Latin America*, Washington: Woodrow Wilson International Center for Scholars, 30-56; Fairfield, T. (2013). Going where the money is: Strategies for taxing economic elites in unequal democracies. *World Development*, 47:42-57; Hassan, M. & Prichard, W. (2016). The political economy of tax reform in Bangladesh: Political settlements, informal institutions and the negotiation of reform. *Journal of Development Studies* 52 (12):1704-1721.
[23] Kirchler, E., Hoelz, E., & Wahl, I. (2008). Enforced versus voluntary tax compliance: The "Slippery Slope" framework. *Journal of Economic Psychology* 29:210-225.
[24] Castro, M. (2014). Tax compliance under horizontal and vertical equity conditions: An experimental approach. *International Tax and Public Finance*, 21 (4):560-577; Bazart, C., & Bonein, A. (2014). Reciprocal relationships in tax compliance decisions. *Journal of Economic Psychology*, 40: 83-102.

provided goods and services ("reciprocity");[25] and (d) the governments administering those tax systems are accountable to taxpayers ("accountability").[26]

Most research to date has focused on the potential for expanded trust to increase broader tax morale, which would drive expanded "quasi-voluntary" tax compliance. Tax morale reflects individual ethics and values, social norms, and the extent of trust in tax systems, with the latter offering the most immediate target for prospective reformers. Research in this area initially came overwhelmingly from OECD countries, but has rapidly expanded in developing countries, and is reaching similar conclusions.[27]

Trust and tax morale have great potential to expand political support for reforms, given the common deep distrust between taxpayers and tax authorities.[28] In OECD countries, the need to facilitate compliance is often the primary barrier to improved tax collection. By contrast, in most developing countries it is increasingly accepted that the most important barriers to collection are frequently political – that is, reform is not only about identifying strategies to encourage taxpayer compliance, but about identifying strategies that are politically feasible and mobilizing necessary political support for their implementation. This growing attention to political constraints is rooted in evidence that across the developing world there are immediate reform opportunities available, which have been consistently frustrated despite being both low cost and technically straightforward. For example, many governments fail to engage in even basic data sharing within tax administrations to identify the most obvious and egregious examples of tax evasion by elite groups – despite clear evidence that such data sharing can yield immediate gains.[29] A lack of political will emerges as the most compelling explanation.

The increasingly-recognized centrality of politics in bringing about tax reforms is consistent with its role in other aspects of public sector performance. The World Development Report (WDR) 2017, *Governance and the Law,* argues that asymmetries of power—which lead to exclusion, capture, and clientelism—lie at the root of a wide range of development challenges. Tax reform inevitably creates winners, losers, and confronts strong vested interests. It cannot succeed without political support—but broad-based political support is frequently absent owing to perceptions that the system is unfair, and to the absence of clear reciprocity and benefits from expanded tax

[25] Cummings, R. G., Martinez-Vazquez, J., McKee, M., & Benno, T. (2009). Tax morale affects tax compliance: Evidence from surveys and artefactual field experiment. *Field Experiments in Economics*, 70 (3):447-457.
[26] Alm, J., Jackson, B., & McKee, M. (1993). Fiscal exchange, collective decision institutions, and tax compliance. *Journal of Economic Behavior and Organization* 22: 285–303.
[27] Lago-Peñas, I., & Lago-Peñas, S. (2010). The determinants of tax morale in comparative perspective: Evidence from European countries. *European Journal of Political economy*, 26(4), 441-453; Torgler, B. (2005). Tax morale in Latin America. *Public Choice*, 122(1-2): 133-157; Chan, H. F., Supriyadi, M. W., & Torgler, B. (2017). Trust and tax morale. In *The Oxford Handbook of Social and Political Trust*. Oxford University Press; NESG. (2019). A survey of Nigerian households and small businesses: What do Nigerians think about taxes? Lagos: The Nigerian Economic Summit Group.
[28] Torgler, B. (2003). Tax morale, rule-governed behaviour and trust. *Constitutional Political Economy*, 14(2):119-140.
[29] Kangave, J., Nakato, S., Waiswa, R, & Lumala Zzimbe, P. (2016). Boosting revenue collection through taxing high net worth individuals: The case of Uganda. *ICTD Working Paper 45*. Brighton: International Centre for Tax and Development; Kangave, J., Nakato, S, Waiswa, R, Nalukwago, M, & Lumala Zzimbe, P. (2018). What can we learn from the Uganda Revenue Authority's approach to taxing high net worth individuals? *ICTD Working Paper 72*. Brighton: International Centre for Tax and Development; Moore, M, & Prichard, W. (2018). Tax reform for low-income countries: Five ideas for simplifying tax systems to fit local realities. *ICTD Summary Brief 17*. Brighton: International Centre for Tax and Development.

collection.[30] The WDR 2017 proposes that it is possible to make progress by (a) shifting the incentives and preferences of those with power; (b) paying more attention to the interests of previously-excluded participants; and (c) enhancing the contestability of the decision-making process. As with the framework developed here, the WDR ascribes a central role to building trust and to expanding fairness: "delivering on commitments feeds…back into building trust in institutions and strengthening outcome legitimacy". This is most likely where government actions "resonat[e] with peoples' needs and perceptions of fairness".[31] Operationally, more effectively navigating the political barriers to reform—by explicitly considering power as a relevant factor—is likely to involve a combination of opportunism in identifying political opportunities for reform, strategies designed to build a sustainable political foundation for reform, and more effective approaches to assessing the extent of political commitment to reform.

Finally, where governments invest in building trust in tax systems this can directly and indirectly contribute to strengthening the broader fiscal contract. Strategies that focus exclusively on strengthening enforcement risk ignoring the broader social objectives of tax systems, as they offer no mechanism for increasing the likelihood that revenues will be used to provide public benefits. By making expanded trust central to reform, these broader goals are given greater prominence. Expanded trust in tax systems will often be achieved precisely by improving public benefits from taxation through greater equity, reciprocity and accountability. Meanwhile, recent research has argued that where fairness, equity, reciprocity and accountability feature more prominently in tax reform, this can serve to empower taxpayers to make more successful demands of governments for improved outcomes. Finally, pursuing these same goals can strengthen the potential state-building role of taxation – and thus the competence of governments to deliver benefits to taxpayers.[32]

Critically, investments in enforcement and in building trust are complementary, rather than distinct strategies. Taxpayers are more likely to comply when: (a) the likelihood of detection, and penalties for non-compliance, are higher ("Enforcement"); (b) when it is relatively easy and low cost to comply ("Facilitation"); and (c) when they have a higher intrinsic willingness to pay – either because they believe that paying taxes is "the right thing to do", that taxes are fair, or because they believe that taxes will be translated into public benefits ("Trust"). Importantly, these elements reinforce one another. A key component of trust in the tax system is a belief that everyone pays their fair share and is punished fairly if they do not. This depends on the existence of adequate enforcement.[33] Meanwhile, where there is little trust it may be impossible to mobilize the necessary *political commitment* to strengthen enforcement capacity. Investing in strengthening trust is thus very centrally about also creating a supportive political environment for expanded enforcement.

---

[30] Moore, M. (2017). The political economy of long-term revenue decline in Sri Lanka. *ICTD Working Paper 65*. Brighton: International Centre for Tax and Development.; Hassan, M, & Prichard, W. (2016). The political economy of tax reform in Bangladesh: Political settlements, informal institutions and the negotiation of reform. *Journal of Development Studies*, 52 (12):1704-1721.

[31] World Bank Group. (2017). *World development report 2017: Governance and the law*. Washington, DC: World Bank.

[32] Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining*. Cambridge: Cambridge University Press; Prichard, W. (2016). What have we learned about taxation, state building and accountability? *ICTD Summary Brief 4*. Brighton: International Centre for Tax and Development.; Jibao, S, & Prichard, W. (2015). The political economy of property tax in Africa: Explaining reform outcomes in Sierra Leone. *African Affairs*, 114 (456): 404-431

[33] Touchton, M., Wampler, B., & Peixoto, T. 2019. "Of governance and revenue: Participatory institutions and tax compliance in Brazil." *World Bank Policy Research Working Paper 8797.* Washington: World Bank.

Ultimately, innovative approaches are needed to overcome persistent technical *and* political barriers to improving tax compliance. These approaches would also contribute to expanding the broader public benefits of taxation through complementary investments in enforcement, facilitation and trust. The Innovations in Tax Compliance project correspondingly seeks to develop a conceptual framework that links these competing needs into a holistic vision for approaching tax reform. No individual component of this framework is, in and of itself, particularly novel or transformative. Indeed, the very best reform programs likely already do much of what is proposed here, though often in more *ad hoc* ways. The key value added of the framework lies in unifying relatively siloed and fragmented strands of research, embedding discrete research findings in a holistic framework for reform, developing tools to consistently transform these research insights into operational outcomes, and providing a platform for conducting systematic research into the effectiveness of these approaches to reform.

This more holistic approach to reform is likely to imply the development of more targeted and locally-specific reform strategies. The approach would identify the "binding constraints" on reform and develop targeted strategies for overcoming them. Identifying binding constraints implies understanding, in any particular context, what explains poor outcomes – that is, how much do different factors matter, in what ways, and in what combinations? Many successful interventions have been shown to be effective under certain circumstances.[34] A key goal of this framework is to help policy makers to think about the right combination of strategies in specific contexts, and thus to allocate resources most effectively. In some cases, there may, for example, be significant technical capacity in place, but little political support for reform – necessitating a focus on shifting the politics of reform rather than on technical capacity building. In other cases, there may be significant political support for reform, but limited technical capacity – with potentially large payoffs to investing in technical support. It is also possible to have significant technical capacity and political will, but major concerns about equity or accountability, thus necessitating strategies seeking to build trust and support the construction of more inclusive fiscal contracts among specific segments of taxpayers. Meanwhile, across all these scenarios, a focus on "binding constraints" seems likely to encourage simplicity and a focus on the basic building blocks of effective reform, which have in many areas proven stubbornly difficult to put in place.[35]

The remainder of this paper develops a formal framework that combines enforcement, facilitation and trust to develop more effective approaches to tax reform. This underpins a broader project that will explore the framework's application to specific tax segments and types, develop operational tools for its deployment in the field, and seek to systematically study the framework's impacts in specific countries. The paper is organized as follows. The next section provides an overview of the full framework. The third section provides a more detailed discussion of the roles of enforcement, facilitation, and trust in shaping tax compliance. The final section discusses concrete

[34] For example: Mascagni, G., Nell, C., & Monkam, N. (2017). One size does not fit all: A field experiment on the drivers of tax compliance and delivery methods in Rwanda. *ICTD Working Paper 58*. Brighton: International Centre for Tax and Development; Khan, A., Khwaja, A, & Olken, B. (2016). Tax farming redux: Experimental evidence on performance pay for tax collectors. *Quarterly Journal of Economics*, 131 (1):219-271; Touchton, M., Wampler, B., & Peixoto, T. 2019. "Of governance and revenue: Participatory institutions and tax compliance in Brazil." *World Bank Policy Research Working Paper 8797.* Washington: World Bank.

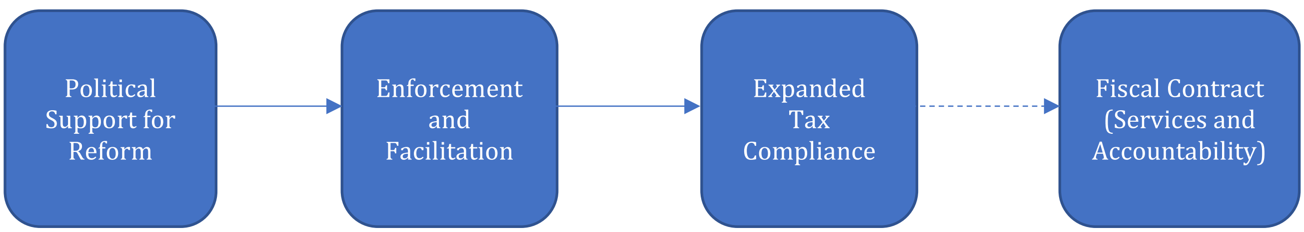
[35] Moore, M, & Prichard, W. (2017). How can governments of low income countries collect more tax revenue? *ICTD Working Paper 70*. Brighton: International Centre for Tax and Development; Moore, M., & Prichard, W. (2017). Tax reform that fits in low-income countries: Five ideas for simplifying tax systems to fit local realities. *ICTD Summary Brief 17*. Brighton: International Centre for Tax and Development.

strategies for designing locally-appropriate reform strategies that combine investments in enforcement, facilitation, and trust to construct stronger fiscal contracts.

## CONCEPTUAL FRAMEWORK

Traditional approaches to tax reform have generally aimed to strengthen compliance through investments in enforcement and facilitation of tax payment. These approaches reflect standard models of tax compliance, which treat taxpayers as rational economic actors responding to the likelihood of audit, the strength of penalties, and the ease and cost of compliance. The logic has been relatively straightforward: identify contexts in which there appears to be political support for reform, implement relatively standard investments in strengthening enforcement and facilitation based heavily on international experience,[36] and trust that expanded revenue collection will, ultimately, be translated into broader public benefits. This stylized, and admittedly highly simplified, model of reform is illustrated in Figure 6.

**Figure 6: Traditional Theory of Change for Reform**




This approach has significant merit, and has achieved meaningful gains, but it neglects three key factors. It pays limited attention to political realities, the need to foster quasi-voluntary compliance, and the importance of strengthening fiscal contracts. Research suggests that each of these elements can and should play a critical role in tax reform programs. The conceptual framework developed here is thus centered on addressing these three broad challenges.

First, ample evidence now suggests that political support is critical to reform,[37] yet traditional models largely consider it exogenous. Recent developments in public administration research stress the need to think and work politically when pursuing reform and emphasize the role of trust in generating political support.[38] However, it is not always clear whether these findings are being translated into changes in development programming. While some reform programs have internalized this insight,[39] many have not, or they focus on identifying environments in which sufficient political support appears to exist but there is a lack of clear metrics and strategies to

[36] Fjeldstad, O-H., & Moore, M. (2008). Tax reform and state-building in a globalized world. In Brautigam, D., Fjeldstad, O-H., & Moore, M. (Eds.) *Taxation and State-Building in Developing Countries: Capacity and Consent*. Cambridge: Cambridge University Press; Sanchez, O. (2006). Tax systems reform in Latin America: Domestic and international causes. *Review of International Political Economy*, 13 (5):772-801.
[37] World Bank Group. (2017). *World development report 2017: Governance and the Law*. Washington: World Bank.
[38] Andrews, M. (2013). *The limits of institutional reform in development: Changing rules for realistic solutions*. Cambridge: Cambridge University Press; McCulloch, N., & Piron, L-H. (2019). Thinking and working politically: Learning from practice. Overview to Special Issue. *Development Policy Review*, 37(S1):1-15.
[39] Booth, D. (2014). Aiding institutional reform in developing countries: Lessons from the Philippines on what works and what doesn't and why. *Working Politically in Practice Series Case Study 1*. The Asia Foundation and the Overseas Development Institute.

measure and foster political support over time. A more forward-looking strategy aims to move beyond such an *ad hoc* approach to the politics of reform by applying existing insights in a more systematic way.

Second, investments in strengthening trust have been relatively *ad hoc* and low priority, despite research showing their importance to strengthening compliance. Meanwhile, evidence about concrete interventions that have enjoyed success is still quite limited. Recent research has drawn a distinction between "enforced compliance", which results from the enforcement power of the state, and "voluntary" (or "quasi-voluntary") compliance, which is driven by values, social norms *and* levels of trust in the fairness, equity, reciprocity, and accountability of tax systems. Overall compliance will be highest when both enforcement power and trust are high, while strengthening voluntary compliance may be subjectively preferable. At the same time, the "slippery slope" framework developed by Kirchler, Hoelzl and Wahl[40] predicts that compliance may decline rapidly when either trust or enforcement declines to very low levels. This reflects the fact that the two are deeply interdependent. Political scientists, for example, have long preferred the language of "quasi-voluntary compliance" because it captures the idea that trust and voluntary compliance are unlikely in the absence of complementary investments in enforcement. Stronger enforcement is likewise less likely in the absence of trust.

Third, it cannot be assumed that tax revenues will be used for public purposes – therefore strategies to strengthen accountability should ideally be part of reform. There is now a broad literature that highlights the potential for expanded taxation to spur greater accountability by prompting taxpayers to demand results and generating incentives for governments to make concessions in order to encourage quasi-voluntary compliance.[41] However, we likewise know that such positive outcomes are not guaranteed. Although tax authorities will never have direct control over the extent of government reciprocity and accountability, there may be specific aspects of tax reform design that can enhance accountability by empowering popular engagement and demand making. Recent research has referred to these as a "governance-focused tax reform agenda", placing greater weight on increasing the political salience of taxation (including through direct taxation), increasing horizontal equity in tax enforcement, expanding meaningful transparency around taxation and budget (including, possibly, earmarking), and directly supporting popular engagement through new institutional spaces and investments in civil society capacity.

Reflecting these insights, the Innovations in Tax Compliance framework makes politics, "quasi-voluntary compliance" and the construction of stronger fiscal contracts central to reform design (see Figure 7). As noted earlier, none of the individual elements of the framework is particularly novel or controversial. The importance of combining investments in enforcement, facilitation, and trust is increasingly accepted,[42] as is the need for careful attention to politics in designing reform.[43]

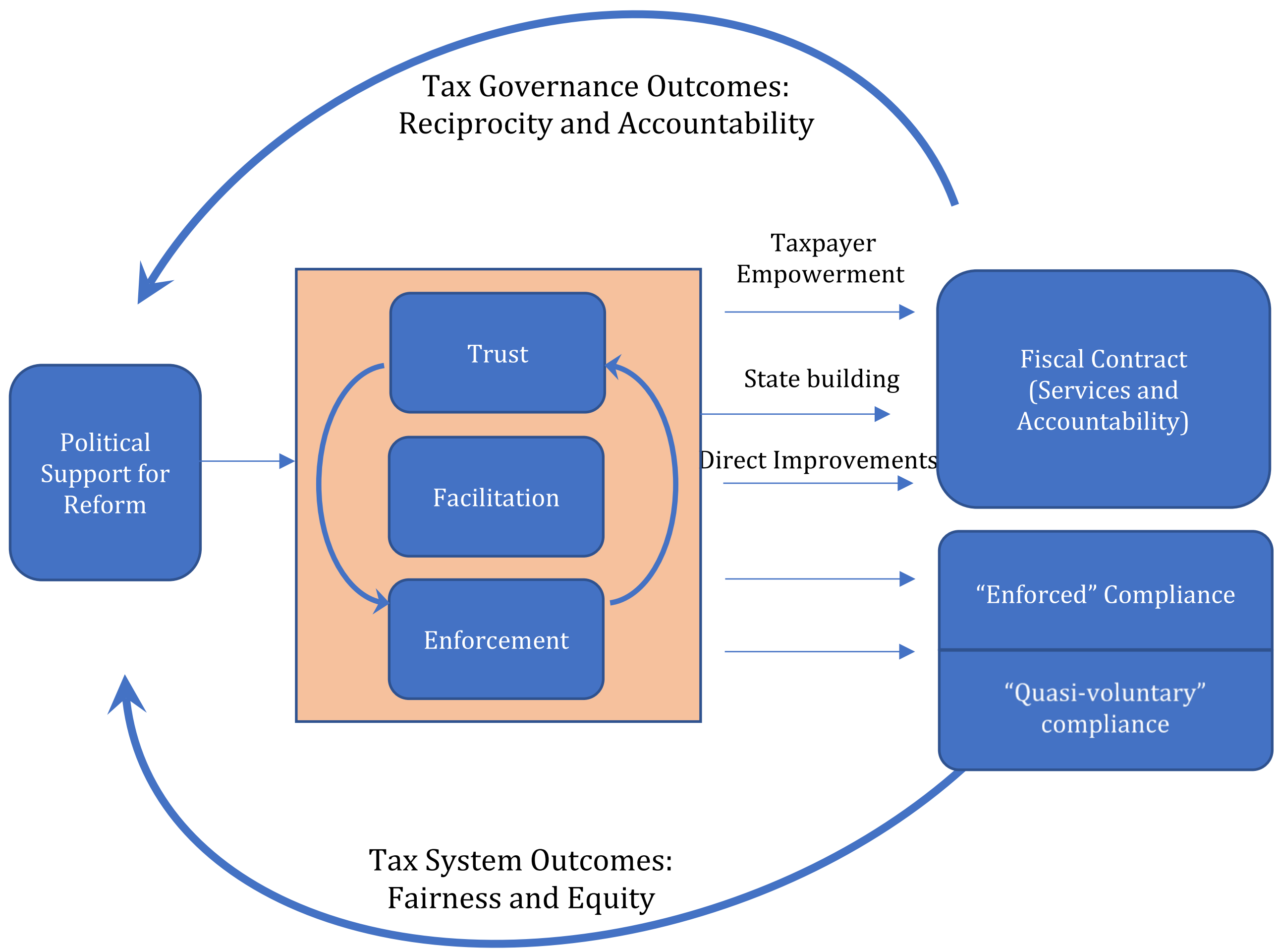
---

[40] Kirchler, E, Hoelzl, E., and Wahl, I. (2008). Enforced versus voluntary tax compliance: The "Slippery Slope" framework. *Journal of Economic Psychology*, 29:210-225.
[41] Prichard, W. (2015). *Taxation, responsiveness and accountability in Sub-Saharan Africa: the dynamics of tax bargaining*. Cambridge: Cambridge University Press; Dom, R. (2018). Taxation and accountability in sub-Saharan Africa: New evidence for a governance dividend. *ODI Working Paper 544*. London: Overseas Development Institute.
[42] For a recent overview, see Alm, J. (2018). What motivates tax compliance? *Journal of Economic Surveys, 33(2)*.
[43] Fairfield, T. (2015). The political economy of progressive tax reform in Chile. In James Mahon, J., Bergman, B. & Arnson, C. (Eds.,). P*rogressive Tax Reform and Equality in Latin America*. Washington: Woodrow Wilson International Center for Scholars, 30-56; Fairfield, T. (2013). Going where the money is: Strategies for taxing economic elites in unequal democracies. *World*

The main value of the framework lies in pulling these disparate elements together in a coherent vision for reform, and in translating research insights into operational guidance.

The framework proposes that by combining complementary investments in enforcement, facilitation, and trust, reformers can not only strengthen "enforced compliance" but can also (a) encourage "quasi-voluntary compliance"; (b) create conditions conducive to strengthening fiscal contracts; and (c) generate sustained political support for reform. Ideally, this sets the stage for virtuous circles of reform: successful investments in building trust provide the political capital needed to pursue further reform, while the translation of resultant revenues into public benefits further builds trust and compliance among taxpayers. The following discusses each component of the framework in greater detail.

**Figure 7: Theory of Change for Innovations in Tax Compliance**




The central "box" in the model in Figure 7 captures the interconnected nature of investments in enforcement, facilitation and trust. Greater trust strengthens the effectiveness of enforcement

*Development*, 47:42-57; Hassan, M, & Prichard, W. (2016). The political economy of tax reform in Bangladesh: Political settlements, informal institutions and the negotiation of reform. *Journal of Development Studies*, 52 (12):1704-1721.

efforts by providing a stronger political and social foundation. In turn, more equitable enforcement, and greater ease of paying taxes, builds trust in the fairness of the tax system.

Investing in trust-enhancing reforms can help reinforce improvements in both "enforced" and "quasi-voluntary" compliance. Recent reform efforts and research have often tended to focus on strengthening enforcement or facilitation. One particular tool that has become increasingly popular in tax reform is the so-called "nudge" intervention. Nudges are meant to strengthen quasi-voluntary compliance by making choices – and their consequences – more visible to taxpayers.[44] These interventions often take the form of targeted communication about tax-expenditure links or the likelihood of enforcement action through letters or text messages to taxpayers.[45] While nudges have proven their value in some contexts, their effectiveness may be short-lived, have a limited ceiling, or have diminishing returns.[46] The framework presented here stresses the interconnected nature of the two types of compliance, and the need to make trust building – and the strengthening of quasi-voluntary compliance – a central consideration in every aspect of reform, going beyond nudges to ensure sustained and durable change.

The focus on trust likewise brings the construction of stronger fiscal contracts explicitly inside the model. Existing research has made clear that trust-building measures are also likely to lead to broader improvements in the quality of governance. Trust building can contribute to governance in three ways. First, increasing trust in the tax system often goes together with improvements in equity, reciprocity and accountability – that is, focusing on building trust makes strengthening public benefits an explicit part of reform design. Second, investments in building trust – and, particularly, greater and more meaningful transparency and consultation, greater political salience, increased focus on direct taxes, more equitable enforcement, and direct investments in taxpayer engagement – can serve to empower taxpayers and expand their ability to make successful demands on governments for public benefits from tax revenues. Finally, strategic investments in enforcement and trust – including elements like improved data sharing, greater transparency and simplification – can help to support state-wide improvements in administrative performance, and thus improve state capacity to deliver broader benefits to taxpayers.

Finally, investments in building trust – and the accompanying strengthening of quasi-voluntary compliance and fiscal contracts – can generate political support for sustaining and advancing reform. This can occur through two broad channels, reflecting the different dimensions of trust: the fairness and equity of tax systems ("tax system outcomes"), and the reciprocity and accountability in the system ("tax governance outcomes"). Where taxpayers see visible gains in both dimensions, they will be more willing to support future reform, thus potentially underpinning a virtuous circle of reform.

---

[44] Sunstein, C. and R. Thaler (2008), *Nudge*, New York, NY: Penguin Books.

[45] e.g. Mascagni, G., Nell, C., & Monkam, N. (2017). One size does not fit all: A field experiment on the drivers of tax compliance and delivery methods in Rwanda. *ICTD Working Paper 58*. Brighton: International Centre for Tax and Development. For a further discussion on targeted communication campaigns see section on Reciprocity.

[46] For a further discussion on targeted communication campaigns see section on Reciprocity. Mascagni, G. (2018). From the lab to the field: A review of tax experiments. *Journal of Economic Surveys*, 32(2), 273-301; Sustein, C. (2017). Nudges that fail. *Behavioural Public Policy*, 1(1):4-25; Manoli, D. S., & Turner, N. (2014). Nudges and learning: Evidence from informational interventions for low-income taxpayers. *NBER Working Paper 20178*. Cambridge, MA: National Bureau of Economic Research; Bronchetti, E. T., Dee, T. S., Huffman, D. B., & Magenheim, E. (2011). When a nudge isn't enough: Defaults and saving among low-income tax filers. *NBER Working Paper 16887.* Cambridge, MA: National Bureau of Economic Research.

Of course, there remains the danger of designing reform programs that attempt to do everything, and ultimately prove too complex and ambitious. Older debates about the relative merits of "comprehensive" versus more piecemeal approaches to reform reflect this concern.[47] Seeking to focus attention on trust has the potential to generate expanded quasi-voluntary compliance, mobilize additional political support for reform, and strengthen the fiscal contract. However, it also introduces new points of potential resistance to reform. A push for greater fairness in tax implementation may be resisted by tax officials who fear a reduction in opportunities for collusion and corruption. An expanded emphasis on equity is likely to be met by resistance from wealthy taxpayers, who often escape their full tax liabilities. Finally, governments themselves may be supportive of increasing revenue collection – but resistant to constraints on their spending or to demands for accountability. More narrow approaches to reform have often been adopted because they have been expedient in the short term. However, stagnating reforms in many countries show the limits of pursuing short-term expediency.

Successful implementation of the framework laid out here is therefore likely to depend on tailoring reform to local contexts. This requires carefully defining local reform priorities, analyzing the local politics of reform, identifying binding constraints and focusing on developing evidence-based approaches to trust building. In most cases, it is unlikely that it will be practical for a reform program to simultaneously target all existing weaknesses, as doing so would be politically unfeasible and technically too ambitious. Tailoring reform to local needs is likely to mean answering four questions. First, what are the central objectives of reform? Is reform narrowly focused on increasing revenue, or does it also aim to increase equity, strengthen pro-poor economic growth or strengthen the fiscal contract? If the latter, what strategies can contribute to these broader goals? Second, what are the key political barriers to reform? Problem-focused political economy analysis aims to understand what kinds of reform are consistent with local political constraints, as well as what kinds of strategies could be adopted to enhance political support for reform. Third, what are the binding constraints on reform? Which potential reform targets are most essential to success, in that (a) they can immediately unlock improvements in performance; and (b) a failure to address them risks undermining other potential reform strategies? Fourth, how can investments in enforcement, facilitation and trust best be combined? In particular, how can trust-building strategies be developed that complement investments in enforcement and facilitation, reflect local sources of distrust, and are rooted in local evidence about how to build trust moving forward?

Overall the framework presented here seeks to refocus the goals of reform beyond a comparatively narrow focus on enforcement and facilitation – and beyond excessive reliance on international models of reform. It also raises a broader question: if governments are unwilling to enhance the fairness, equity, reciprocity and accountability of their tax systems, are international investments in tax reform justifiable? Making trust central to tax reform efforts not only presents a variety of opportunities and challenges, but also brings the broader social goals of tax reform more clearly into focus.

[47] Gillis, M. (1989). Towards a taxonomy for tax reform. In Gillis, M. (Eds.) *Tax Reform in Developing Countries*. Durham: Duke University Press.

**ELEMENTS OF THE FRAMEWORK: ENFORCEMENT, FACILITATION, TRUST**

This section develops the elements of the conceptual framework – and the role of trust in particular – in greater detail. First, it reviews recent research and evidence on the roles of enforcement and facilitation in strengthening tax systems. It then expands on the role of trust. The goal is to highlight potential reform directions – and to provide a framework for prioritizing different reform strategies in different contexts.

The discussion aims to move beyond a singular focus on technical efficiency. Instead, any approach to reform should be technically effective, politically feasible and socially desirable. *Technically effective* implies that each intervention – whether related to enforcement, facilitation or building trust – should be shown to be an effective strategy for improving compliance. *Politically feasible* implies that the reform strategy must either enjoy political support or include a clear strategy for mobilizing it in a sustainable way. *Socially desirable* implies that any tax reform should be designed not only to increase revenue, but to do so in a way that is equitable, engages and empowers taxpayers, and creates conditions favorable to the construction of stronger fiscal contracts.

*Enforcement*

Dominant models of tax compliance have long taken enforcement as the starting point, with research progressively expanding the understanding of enforcement tools available to governments. The benchmark model of individual tax compliance developed by Allingham and Sandmo treats taxpayers as welfare-maximizing economic actors, with compliance decisions reflecting the likelihood that non-compliance will be detected, and the extent of penalties.[48] Their original model assumed individual taxpayers declaring their own income, subject to audit – and predicted levels of compliance far lower than those that are actually observed in OECD countries. Subsequent research has begun to explain this, focusing in particular on the ways in which third-party information and tax withholding can dramatically improve enforcement outcomes. Given this potential, effective and equitable enforcement is likely to remain the bedrock of any successful reform strategy.

Two elements are common among efforts at strengthening enforcement: measures to increase monitoring of taxpayers, and measures to improve tax collectors' performance. Most models of tax compliance – particularly in OECD contexts – have focused on strategies to improve the monitoring of taxpayers. This reflects an assumption that tax collectors are committed to enforcing tax compliance, but that they lack the necessary tools. However, particularly in developing country settings it may be that tax collectors are not fully committed to enforcement, reflecting some combination of shirking behavior, collusion, corruption and/or political interference. Networks based on collusion and corruption are often deeply embedded within tax administrations, with rents flowing upward to higher levels – or, in some cases, helping to finance broader state patronage.[49]

[48] Allingham, M.G., & Sandmo, A. (1972). Income tax evasion: A theoretical analysis. *Journal of Public Economics* 1: 323–38.
[49] Piracha, M., & Moore, M. (2015). Understanding low-level state capacity: Property tax collection in Pakistan. *ICTD Working Paper 33*. Brighton: International Centre for Tax and Development; Khan, A., Khwaja, A., & Olken, B.. (2016). Tax farming redux: Experimental evidence on performance pay for tax collectors. *Quarterly Journal of Economics*, 131 (1):219-271; Hassan, M., & Prichard, W. (2016). The political economy of tax reform in Bangladesh: Political settlements, informal institutions and the negotiation of reform. *Journal of Development Studies*, 52 (12):1704-1721.

In these contexts, improvements in enforced compliance may depend not only on deploying new tools to monitor taxpayers, but on expanding rules-based enforcement efforts by tax collectors.

Improving access to information has been at the heart of efforts to improve monitoring of taxpayers. These strategies have reflected the centrality of information to tax enforcement: it is through access to information on income, wealth and economic transactions that governments are able to identify evasion and avoidance, pursue enforcement, and impose penalties. Some reform efforts have focused on improving the collection, management and sharing of data that is already possessed by governments – including improved data sharing across divisions *within* tax administrations in order to cross-reference the tax declarations of firms and individuals across tax types. Meanwhile, many countries have also sought to improve access to third-party data. This third-party data can come from a variety of sources: cross-referencing of tax declarations from firms that do business together, data from other government agencies e.g. on land, property or business registrations, or external sources like public contracts, bank accounts, stock exchanges or credit cards. Finally, tax withholding often enables a particularly effective form of data gathering for tax enforcement. In most developing countries the bulk of income taxes are already collected via withholding taxes on salaries. Some countries have correspondingly considered the potential merits of expanding withholding taxes, for the VAT and elsewhere, in order to widen the tax net.

Reforms have also sought to expand audit capacity – while reducing opportunities for taxpayers to engage in tax evasion and avoidance. Along with expanded access to information, governments and donors have invested in the expansion of audit capacity, with a particular focus on the introduction of risk-based audits. The goal has been to improve the technical capacity of audit departments – increasingly focused on challenges related to international taxation – while putting in place strategies to ensure the most efficient targeting of audit resources. Meanwhile, efforts have focused in parallel on simplifying tax rules – and eliminating loopholes – in order to reduce opportunities for evasion and avoidance. For example, governments may reduce the range of VAT rates in order to simplify enforcement,[50] may introduce simplified methods for property tax assessment,[51] or may explore simplified approaches to confronting cross-border transfer pricing.[52] Finally, in many cases governments have made access to certain kinds of services conditional on producing evidence of tax compliance – though enforcement of such rules often appears to have been uneven, or short-lived.[53]

Similarly, extensive reform efforts have been focused on improving the performance of tax administrations themselves. Semi-autonomous revenue authorities have been created across much of Latin America and Anglophone Africa in particular, in order to provide improved work

[50] Bird, R., Gendron, P. P., & Rotman, J. L. (2005). VAT revisited: A new look at the value added tax in developing and transitional countries. United States Agency for International Development.
[51] Jibao, S., & Prichard, W. The political economy of property tax in Africa: Explaining reform outcomes in Sierra Leone. *African Affairs* 114(456): 404-431; Fish, P. (2018). Practical guidance note: Training manual for implementing property tax reform with a points-based valuation. *African Tax Administration Paper 2.* Brighton: International Centre for Tax and Development.
[52] Durst, M.C. (2019). *Taxing multinational business in lower-income countries: Economics, politics and social responsibility.* Brighton: International Centre for Tax and Development.
[53] For example, a fiscal sustainability project in the West Bank in 2011 made local municipalities services, such as car registration, conditional on proof of property tax payment. Within participating municipalities collection increased to between 85 and 100 percent. World Bank. (2012). *West Bank & Gaza - WBG Support for Fiscal Sustainability And Public Financial Management*. Washington: World Bank.

conditions for tax collectors and greater freedom from political interference. Salary increases have been key to many reform programs, as an effort to improve staff recruitment and performance incentives. In other contexts, the focus has been on improving monitoring of staff and reducing opportunities for collusion and corruption. The simplest measures have focused on reducing face-to-face interactions between taxpayers and tax collectors through the introduction of self-assessments, automatized selection for audits, making tax payments online or at banks, and so forth. More ambitious efforts have relied on increasing internal audit capacity,[54] improving performance incentives,[55] or employing IT systems to introduce better data controls and to assess staff performance. Meanwhile, in extreme cases some local administrations have experimented with tax farming methods for smaller taxes – auctioning tax collection rights to independent contractors, who then retain any surplus revenue. This, however, raises fresh concerns about overhead costs, corruption at the contracting stage, lost revenues and arbitrary enforcement efforts.[56]

There are signs that these reform efforts have yielded meaningful revenue gains across a number of countries. As was illustrated in Figure 1, tax collection has increased meaningfully over the past two decades across the developing world, and particularly in Latin America and Sub-Saharan Africa. These revenue gains have occurred across both direct and indirect taxes, though the most important gains have been from the VAT, which has been a focus of donor support and new investments. There is now, for example, emerging evidence of the impact of electronic tax registers in strengthening VAT compliance in low-income countries,[57] and the ability of higher capacity administrations to use the paper trails created by the VAT to strengthen compliance.[58] Even in places where progress has been slower overall, research has captured important successes if political commitment has been present: for example, some localities have successfully introduced and expanded digitized property tax systems,[59] while other administrations have expanded the use of third-party data for income tax enforcement.[60] Qualitatively, many senior tax administrators themselves have become defenders, and promoters, of the modernized approaches to enforcement introduced in recent decades – though others have continued to attempt to preserve more informal ways of working.

Nevertheless, reform results have been disappointing in many areas. While VAT performance has been relatively strong, total revenue gains have struggled to compensate for decreases in trade tax

[54] Schreiber, L. (2018). Broadening the base: Improving tax administration in Indonesia, 2006-2016. *Innovations for Successful Societies*. New Jersey: Princeton University.
[55] Khan, A., Khwaja, A., & Olken, B. (2016). Tax farming redux: Experimental evidence on performance pay for tax collectors. *Quarterly Journal of Economics*, (1):219-271.
[56] Iversen, V., Fjeldstad, O-H., Bahiigwa, G., Ellis, F., & James, R. (2006). Private tax collection - Remnant of the past or a way forward? Evidence from rural Uganda. *Public Administration and Development*, 26 (2):317-328.
[57] Ali, M., Shifa, A., Shimeles, A., & Woldeyes, F. (2015). Information technology and fiscal capacity in a developing country: Evidence from Ethiopia. *ICTD Working Paper 31*. Brighton: International Centre for Tax and Development.
[58] Pomeranz, D. (2015). No taxation without information: Deterrence and self-enforcement in the value added tax. *American Economic Review*, 105 (8):2539-2569.
[59] Jibao, S., & Prichard, W. (2015). The political economy of property tax in Africa: Explaining reform outcomes in Sierra Leone. *African Affairs*, 114 (456):404-431; Cheeseman, N., & de Gramont, D. (2017). Managing a mega-city: Learning the lessons from Lagos. *Oxford Review of Economic Policy*, 33 (3):457-477.
[60] Carillo, P., Pomeranz, D., & Singhal, M. (2017). Dodging the taxman: Firm misreporting and limits to tax enforcement. *American Economic Journal: Applied Economics*, 9(2)*: 144-64.*

revenue[61] — and the majority of VAT revenue continues to be collected at the border in many countries.[62] Weak enforcement has reflected the limited implementation of IT systems, an inability in lower income countries to fully exploit the paper trails created by VAT invoices, and weak audit capacity. More broadly, new investments in IT systems have frequently failed to deliver promised benefits, and the introduction of risk-based audits has been slow in many countries, while audit capacity overall has often remained weak. Meanwhile the creation of autonomous revenue authorities has not always produced significant revenue gains, with corruption and politicization returning over time.[63] As a result, tax agencies remain among the least trusted government organizations in many countries (Figure 3, above).

Third-party information, relevant in particular for strengthening income tax receipts and VAT administration, has not been a panacea. Research by Carrillo et al. reveals that greater reliance on third-party information in Ecuador led businesses to declare significantly greater revenues, but to simultaneously declare larger deductions, thus limiting actual increases in tax payments.[64] As they explain, third-party information about only one margin of tax declarations may be insufficient, as taxpayers may then manipulate other margins of their declaration to reduce liabilities. Ultimately, information is needed from multiple sources, and most importantly there is a need for effective follow-up audit capacity and capacity to pursue arrears where evasion and avoidance are detected.[65] There is also the challenge of translating information into enforcement effort. In Uganda, for example, the domestic tax department expanded internal and external data sharing in order to identify High Net Worth Taxpayers but has only been able to scale up enforcement slowly due to political sensitivities.[66]

In response to persistent challenges, including capacity constraints in lower income countries, some researchers and practitioners have advocated experimenting with simplified approaches to enforcement. In the global dialogue, there have been calls to increase transparency around the financial operations of MNCs through country-level reports and calls for simplifying access for developing countries to information on wealth held abroad by their nationals. At the national level, there have been calls for simplifying approaches to taxing income, in order to reduce the scope for abuse. Based on research in Pakistan, Best et al. present evidence that shifting corporate income taxation away from profits – which are more easily manipulated – in favor of turnover taxes may reduce evasion by 70 percent or more, while creating relatively little economic distortion.[67] Durst has argued for shifting tax regimes in the extractive industries toward greater reliance on revenue-

---

[61] Baunsgaard, T., & Keen, M. (2009). Tax revenue (or?) trade liberalizations. *IMF Working Paper 05/112*. Washington: International Monetary Fund.

[62] World Customs Organization (2017). *Annual Report 2016–2017*. Brussels, Belgium: WCO.

[63] Dom, R. (2019). Semi-autonomous revenue authorities in Sub-Saharan Africa: Silver bullet or white elephant. *The Journal of Development Studies*, *55*(7), 1418-1435; Fjeldstad, O-H. (2005). Corruption in tax administration: Lessons from institutional reforms in Uganda. *CMI Working Paper 2005:*10. Bergen: Chr. Michelsen Institute.

[64] Carillo, P., Pomeranz, D., & Singhal, M. (2017). Dodging the taxman: Firm misreporting and limits to tax enforcement. *American Economic Journal: Applied Economics*, 9(2): 144-64.

[65] Ibid; Slemrod, J., Collins, B., Hoopes, J. L., Reck, D., & Sebastiani, M. (2017). Does credit-card information reporting improve small-business tax compliance? *Journal of Public Economics*, 149, 1-19.

[66] Kangave, J., Nakato, S., Waiswa, R., Nalukwago, M., & Lumala Zzimbe, P. (2018). What can we learn from the Uganda Revenue Authority's approach to taxing high net worth individuals? *ICTD Working Paper 72*. Brighton: International Centre for Tax and Development.

[67] Best, M., Brockmeyer, A., Jacobsen Kleven, H., Spinnewijn, J., & Waseem, Mazhar. (2015). Production versus revenue efficiency with limited tax capacity: Theory and evidence from Pakistan. *Journal of Political Economy*, 123 (6):1311-1355.

based royalty taxes, while encouraging tax administrations to take greater control over the pricing of transactions in commodities.[68] For tax administrations in low-income countries, simplification – when well calibrated to administrative capacity – holds considerable potential to further strengthen enforcement. Moreover, simplification could also benefit taxpayers to the extent that it makes it easier for them to comply with their tax obligations – facilitating "quasi-voluntary" tax compliance.

*Facilitation*

While enforcement has remained the bedrock of most reform strategies, efforts to facilitate tax compliance have become a standard feature of reform programs over the past decade. Reforms aimed at facilitation recognize the role of the tax administration as a provider of services and information that should make compliance "as easy as possible." Non-compliance is not solely a function of purposeful evasion (intent), but may also result from taxpayer ignorance, inability to pay or transaction costs that tip the scales away from compliance. Facilitation is often alternatively presented as making tax administrations "customer friendly", with taxpayers treated as clients rather than potential criminals. The intuition is clear: at the margin, a taxpayer is more likely to comply if the government does not erect hurdles to doing so.

Initially, facilitation efforts were viewed in primarily technical terms: while enforcement efforts sought to raise the cost of non-compliance, facilitation measures aimed to reduce the cost of complying. These kinds of reforms had several key elements. First, they sought to ensure that taxpayers understood what they were required to pay and had easy access to the information required to do so. This has involved simplifying and stabilizing relevant laws and making relevant information readily available. Second, reforms have sought to reduce the cost of compliance by simplifying policies, simplifying forms and filing requirements, and reducing redundancies and points of contact. And, third, reforms have aimed to reduce the scope for harassment and abuse by tax officials, particularly at the point of payment. This has involved reducing face-to-face contact with tax officials, reducing officials' discretion, increasing reliance on self-assessment where possible, introducing online portals, and expanding the scope for tax payments to banks (or, more recently, via SMS).

The most ambitious of these efforts in most developing countries have focused on simplification of laws and regulations. Income tax reforms have sought to reduce the number of rates and increase reliance on self-assessment. VAT reforms have similarly sought to reduce the number of rates. Presumptive tax regimes have frequently moved away from distinct regulations for every sector and toward relatively standardized tax rates on (estimated) turnover. Mining tax regimes have aimed to replace complex webs of regulations and fees with simplified combinations of royalties and corporate income taxes. Recently successful property tax reforms have sought to replace complex market-based valuation systems with simplified systems based on the size and observable features of properties and land.[69]

---

[68] Durst, M. (2016). Improving the Performance of Natural Resource Taxation in Developing Countries. *ICTD Working Paper 60*. Brighton: International Centre for Tax and Development.

[69] Such strategies have been adopted, among others, in Sierra Leone, Malawi and Pakistan. In Pakistan, with the support of the World Bank, the government revised its valuation formula from an area-based to a factor-based assessment, rather than moving directly to a value/market-based system. It initially employed "plot size", "covered area", "age of the property", and "location" as factors for property assessment.

Reforms aimed at simplification have also reduced unnecessary regulations and reduced the (sometimes large) number of taxes businesses must pay (especially small businesses). In most cases, national governments now collect a relatively small number of taxes – income taxes, the VAT and customs duties, most notably – that offer comparatively limited discretion to tax collectors, and for which payments can be made in a variety of ways. While there is still much to be done, costs of compliance have decreased, while the scope for day-to-day corruption and collusion has similarly declined. The global average for time required for companies to comply with their tax obligations has fallen from 324 hours in 2006 to 205 hours in 2019, while the average number of required payments dropped from 34 to 24. However, significant regional differences remain.[70]

While these facilitation reforms have enjoyed significant success, their impact on actual compliance rates is less clear. At some level, there is no doubt that facilitation reforms have led to concrete gains in tax receipts: tomes of psychological research make clear that reducing costs virtually guarantees increased compliance. In addition, there is some evidence that, for example, the introduction of "one-stop-shops" for (small) business registration has aided formalization and compliance.[71] Yet there have been few systematic efforts to study the magnitude of these effects, especially in developing countries. Additional evidence could have substantial value in helping tax agencies to allocate resources, and in confronting institutional inertia – or vested interests – slowing the implementation of useful reforms.

Another concern is that while facilitation reforms – and simplification efforts in particular – have advanced significantly at the national level, benefits have not always extended to the sub-national level. Many sub-national governments, typically lacking access to the most productive tax bases, have continued to employ tax systems that include large numbers of distorting, unnecessary and overlapping taxes, and offer substantial discretion to tax collectors engaging in face-to-face interactions with taxpayers. While this has been a means for local governments lacking adequate revenue sources to maximize receipts, it has sometimes been accompanied by enormous complexity, horizontal inequities and opportunities for abuse and informal arrangements. The Democratic Republic of Congo presents a particularly extreme case: while the national tax system resembles those of Western countries, local governments officially have more than 400 types of taxes, levies and fees. Unsurprisingly, recent evidence suggests that this has contributed to high levels of extraction from taxpayers, with very little of that revenue reaching the government budget, and low levels of trust in government.[72]

While facilitation reforms initially adopted a technical focus on reducing the costs of compliance, they have evolved to include an interest in building taxpayer trust. Efforts to expand transparency, promote taxpayer education and create new points of engagement between taxpayers and officials are in part designed to increase understanding of tax obligations, and thus ease compliance. But they also reflect a belief that if taxpayers have a clearer understanding of what they need to pay,

[70] World Bank. (2019). *Doing business 2019: Training for reform.* Washington, DC: The World Bank.
[71] Devas, N., & Kelly, R. (2001). Regulations or revenues? An analysis of local business licenses, with a case study of the single business permit reform in Kenya." *Public Administration and Development*, 21:381-391.
[72] Paler, L., Prichard, W., Sanchez de la Sierra, R., & Samii, C. (2017). Survey on total tax burden in the DRC, Final Report. Kinshasa: Department for International Development.

and why, they may find the system fairer and more trustworthy – and be more willing to comply. For example, efforts to reduce face-to-face encounters between taxpayers and tax collectors are designed to simplify payment – but also to reduce the types of harassment and corruption that can undermine trust in the fairness of the tax system. Both were, for example, explicit goals motivating the introduction of the iTax system by the Kenya Revenue Authority in 2015.[73] Simplification reforms have similarly served a dual purpose: they have made it easier to comply, but have also sought to make tax systems more transparent, fairer and more equitable – thus expanding trust and quasi-voluntary compliance.

Tax reform programs aimed at compliance have thus gradually shifted toward a greater focus on building trust. That said, the extent of actual reforms, and their impact on trust and tax morale, remains unclear. Almost all tax authorities have formally undertaken initiatives to expand transparency and taxpayer education. However, their impact appears highly variable. Formal transparency initiatives often appear to be inaccessible to most taxpayers, while taxpayer education is sometimes synonymous simply with telling people why they should pay taxes. There appears to be a continuing need to stress more meaningful and accessible forms of transparency, and to construct forums for reciprocal engagement between taxpayers and governments around paying taxes *and* how those revenues are used.[74] Meanwhile, efforts to reduce face-to-face interaction and thereby reduce opportunities for corruption have advanced rapidly for higher-income taxpayers, but have been slow to emerge for the much larger majority of smaller taxpayers.[75]

In short, recent reform experiences – both in enforcement and facilitation – present a puzzle: they seem highly promising, but in practice progress has been much slower than expected. Most of the reform options described here have experienced significant success in at least some places. Yet attempts to replicate success stories in a different context have often failed. Even seemingly simple measures to improve performance have frequently proven stubbornly difficult to enact. For example, enabling access to basic information across government agencies on things like home and vehicle ownership appears straightforward, but is rarely done. Meanwhile, governments have seemed reluctant to adopt the types of policy experiments, and simplifying reforms, that are consistent with the existing research and appear to hold substantial promise.

The lack of progress on parts of the reform agenda that are both low cost and technically straightforward appears to speak to the dominant role of politics in shaping reform trajectories.[76] This is unsurprising, as tax reform presents a significant political challenge across several dimensions. It confronts powerful and relatively organized vested interests, since tax reforms depend on securing resources from relatively small groups of wealthy and frequently well-connected taxpayers and firms. Tax administrators, in turn, have historically proven to be complex allies in reform. They often favor improved performance in the abstract, and in some cases the

---

[73] Franzsen, R., & McCluskey, W. (2017). *Property tax in Africa status, challenges, and prospects*. Cambridge, MA: Lincoln Institute of Land Policy.

[74] Prichard, W., Beach, R., Mohiuddin, F., & van den Boogaard, V. (forthcoming). The micro-links between taxation and accountability initiatives. *ICTD Working Paper*. Brighton: International Centre for Tax and Development.

[75] Moore, M., Prichard, W., & Fjeldstad., O-H. (2018). Small taxes and large burdens: Informal and subnational revenues. *Taxing Africa Coercion, Reform and Development*. London: Zed Books. 147-178.

[76] Prichard, W. 2019. "Tax, Politics and the Social Contract in Africa." In *Oxford Research Encyclopedia of Politics*. Oxford: Oxford University Press.

leadership of tax administrations have been able to successfully push forward controversial reform.[77] However, members of tax administrations have at other times resisted reforms that increase transparency, reduce discretion and thus curtail opportunities for collusion and corruption.[78] Meanwhile, building broad popular support for tax reform is notoriously difficult, as the bulk of taxpayers are relatively poorly organized, and frequently have little trust in the government.[79] This lack of trust is, in turn, a key factor, because tax reforms frequently ask taxpayers to bear a heavier burden of taxation immediately, based on the promise of future improvements in public spending. Few taxpayers are willing to actively support such efforts where trust in government is limited.

*Trust*

Recent research has increasingly stressed the importance of building trust in order to strengthen "tax morale"' and encourage tax compliance. Tax morale is generally defined as capturing "non-pecuniary motivations for tax compliance"[80] – that is, all the factors *other than* enforcement and facilitation that may drive levels of tax compliance. Some of these factors can be thought of as capturing individual values, ethics and attitudes, which vary across individuals and are relatively unrelated to, and "unconditional" on, government performance. Other factors are more "conditional" on the extent to which taxpayers trust governments – the extent to which taxpayers believe that they are treated fairly, that tax systems are equitable, that they receive services in return and that governments are broadly accountable. Improvements in trust thus stand to improve these more conditional aspects of tax morale, and thus contribute to enhanced tax compliance.[81]

Less frequently emphasized is the likely importance of building trust in order to strengthen political support for reform. The conventional view from research is that governments should enhance trust to encourage individual taxpayers to quasi-voluntarily comply with taxes. This narrow focus makes sense in Western countries, where core features of well-functioning tax systems are already in place. By contrast, in most developing countries a lack of political support for tax reform presents the most immediate barrier to progress—while there is even some evidence that tax administrators themselves may be less committed to enforcement where there is little trust in government.[82] In most countries, for example, political leaders have been unwilling to bear the political costs of expanding revenue collection among elites via income or property taxes. By increasing trust in the tax system, it may be possible to encourage *compliance* by those elites, and equally to mobilize necessary *political support* for expanded enforcement. Put more simply,

---

[77] Schreiber, L. (2019). Righting the ship: Uganda overhauls its tax agency, 2004-2014. *Innovations for Successful Societies*. New Jersey: Princeton University; Shreiber, L. (2019). Bolstering revenue, building fairness: Uganda extends its tax reach, 2014-2018. *Innovations for Successful Societies*. New Jersey: Princeton University; Schreiber, L. (2018). The foundation for reconstruction: Building the Rwanda revenue authority, 2001-2017. *Innovations for Successful Societies*. New Jersey: Princeton University; Schreiber, L. (2018). Keeping up with growth: Building a modern tax administration in Vietnam, 2004-2015. *Innovations for Successful Societies*. New Jersey: Princeton University.
[78] Hassan, M., & Prichard, W. (2016). The political economy of tax reform in Bangladesh: Political settlements, informal institutions and the negotiation of reform. *Journal of Development Studies,* 52 (12):1704-1721.
[79] Ascher, W. (1989). Risk, politics and tax reform: Lessons from some Latin American experiences. in Gillis, M. (ed.) *Tax Reform in Developing Countries*. Durham: Duke University Press.
[80] Luttmer, E., & Singhal, M. (2014). Tax Morale. *The Journal of Economic Perspectives*, 28 (4):150.
[81] Prichard, W. (forthcoming). Rethinking Tax Morale. Toronto: University of Toronto.
[82] Prichard, W. (2016). Electoral competitiveness, tax bargaining and political budget cycles and taxation in developing countries. *British Journal of Political Science* 48(2): 427-457.

building trust is not a substitute for enforcement, but a complement. Consistent with this view, research has highlighted the *political* payoffs to crackdowns on illegal tax evasion,[83] and to linking public services more clearly to new revenue collection.[84] In Colombia, for example, the government struggled to generate buy-in from elites for an income tax increase, but ultimately secured political support and expanded compliance by earmarking the income tax levy for security spending – a priority for income tax payers.[85]

Building trust as part of tax reform strategies seems likely to be particularly important in developing countries, where trust in tax authorities is limited, compliance is poor and political support for taxation is low. Illustratively, across 36 countries in 2014/2015, Africans expressed more trust in informal institutions such as religious and traditional leaders (72 percent and 61 percent respectively) than in the tax department (on average 44 percent). More than one-third of Africans report believing that all or some people working for domestic tax agencies are corrupt.[86] Moreover, there is extensive evidence of unfairness and inequity in tax burdens: weak enforcement among elites exists alongside often heavy burdens of smaller, formal and informal, taxes, fees and levies on lower-income taxpayers. A relatively small number of existing studies correspondingly suggests that even small measures to enhance trust can lead to substantial improvements in compliance, and, likely, reduce political resistance to reform.[87]

A focus on building trust can therefore plausibly be conceptualized as helping countries to escape a low-level equilibrium in tax collection. Taxpayers would theoretically be willing to pay more taxes in exchange for more effective service provision by governments. However, a lack of trust leads to non-compliance and a lack of support for expanded enforcement. Meanwhile, governments would like to collect more revenue, but are unwilling to bear the short-term political costs of increasing enforcement, and do not trust that taxpayers will reward them politically even if new revenues are translated into improved services. Neither side wants to move first. A strategic focus on building trust can help to break this impasse by making tax reform more popular, and thus generating both short- and long-term political payoffs to reform.[88]

---

[83] Casaburi, L., & Troiano, U. (2016). Ghost-House busters: The electoral response to a large anti-tax evasion program. *The Quarterly Journal of Economics*, 131 (1):273-314.

[84] Jibao, S., & Prichard, W. (2015). The political economy of property tax in Africa: Explaining reform outcomes in Sierra Leone. *African Affairs*, 114 (456):404-431; Prichard, W. (2015). *Taxation, Responsiveness and Accountability in Developing Countries: The Dynamics of Tax Bargaining*. Cambridge: Cambridge University Press.

[85] World Bank. (2015). *Colombia - Enhancing fiscal capacity to promote shared prosperity development policy loan project*. Washington: World Bank.

[86] Bratton, M. and Gyimah-Boadi, E. (2016). Do trustworthy institutions matter for development? Corruption, trust, and government performance in Africa. *Afrobarometer. Dispatch No. 112*. Afrobarometer; Isbell, Thomas (2017). Tax Compliance. Africans affirm civic duty but lack trust in tax department. *Afrobarometer Policy Paper No. 43*. Afrobarometer.

[87] See, for example, Prichard (2015) on the use of earmarking to secure political support for tax reform, Jibao and Prichard (2015) on trust building to underpin property tax reform in Sierra Leone, and Mascagni et al. (2016) on the use of SMS messages stressing reciprocity in encouraging income tax compliance. Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining*. Cambridge: Cambridge University Press; Jibao, S., & Prichard, W. (2015). The political economy of property tax in Africa: Explaining reform outcomes in Sierra Leone. *African Affairs*, 114 (456):404-431; Mascagni, G., Nell, C.,& Monkam, N. (2017). One size does not fit all: A field experiment on the drivers of tax compliance and delivery methods in Rwanda. *ICTD Working Paper 58*. Brighton: International Centre for Tax and Development.

[88] Lagos, Nigeria, offers an interesting example of this kind of positive dynamic. Cheeseman, N., & de Gramont, D. (2017). Managing a mega-city: Learning the lessons from Lagos. *Oxford Review of Economic Policy*, 33 (3):457-477.

Translating the growing interest in building trust into practice requires clearer definitions, concepts and strategies. Many accounts of tax morale focus on underlying "ethics" or "values", and on conceptions of government "legitimacy". This has been reflected in public-facing campaigns stressing the importance of paying taxes and seeking to establish a "culture of tax compliance". Yet there are reasons to question the value of these vaguely-defined campaigns. Values and ethics certainly help to explain variation in compliance across individuals but are likely to be difficult to change over the short or medium term.[89] More importantly, recent research suggests that cross-country variation in tax compliance is driven primarily by differences in governance rather than in individual ethics and values.[90]

There is a need for an operationally-focused understanding of what it means to strengthen trust in tax systems, and how this might be achieved. As a starting point, definitions of trust vary across disciplines, but generally share a common orientation around whether governments are behaving "in accordance with normative expectations", and about whether they will continue to do so.[91] As importantly, the degree of trust felt by an individual is consistently understood as a learned behavior, shaped by changing experiences, rather than a stable personality trait. There is broad agreement that levels of trust in government, for example, fluctuate in response to who is in power, to the policies that are adopted, and to the way that they are implemented. More simply, concrete government action can drive increased trust, expanded compliance, and broader support for tax reform.

Social norms are likely to play an important intervening role in translating increased trust into tax compliance. Such social norms are not about individual ethics and values, but, rather, "are usually defined as prevalence or acceptance of tax evasion among a reference group".[92] Where social norms of compliance are weak, improvements in trust may translate into improved compliance more slowly. But over time, improvements in trust in the tax system are likely to shift broader social norms as well. Likewise, where norms of compliance are strong, this may sustain quasi-voluntary compliance for a while even where trust is declining. But over time, declining trust in the tax system is likely to undermine the social norms of compliance. Social norms thus act as the "sticky" component shaping the translation of changes in trust into changes in compliance and political support for reform.

The conceptual framework presented in this paper focuses on four key drivers of trust: fairness, equity, reciprocity and accountability. This captures the extents to which (a) tax systems are fairly and competently designed and administered ("fairness"); (b) burdens are equitably distributed, and everyone pays their share ("equity"); (c) tax revenues are translated into reciprocal publicly provided goods and services ("reciprocity"); and (d) governments administering tax systems are accountable to taxpayers ("accountability"). This does not capture every possible dimension of trust but focuses attention on elements that map naturally onto specific areas of potential tax reform.

---

[89] Alm, J., & Torgler , B. (2011). Do ethics matter? Tax compliance and morality. *Journal of Business Ethics*, 101:635-651.

[90] Andrighetto, G., Zhang, N., Ottone, S., Ponzano, F., D'Attoma, J., & Steinmo, S. (2016). Are some countries more honest than others: Evidence from a tax compliance experiment in Sweden and Italy. *Frontiers in Psychology*, 7 (472).

[91] Miller, A., & O. Listhaug. (1990). Political parties and confidence in government: A Comparison of Norway, Sweden and the United States. *British Journal of Political Science*, 20 (357-86):358.

[92] Kirchler, E., Hoelzl, E., & Wahl, I. (2008). Enforced versus voluntary tax compliance: The "Slippery Slope" framework. *Journal of Economic Psychology*, 29:210-225.

These components of trust can be usefully divided into two broad types: elements that are specifically related to the tax system ("fairness" and "equity"), and elements related to the broad use of tax revenues by the government ("reciprocity" and "accountability"). The first set, which we refer to as "tax system outcomes", falls within the traditional remit of tax reform efforts. Those with responsibility for tax policy and administration can, with the political license to do so, directly improve levels of fairness and equity in both policy and administration. By contrast, the latter set – which we refer to as "tax governance outcomes" – is not directly under the control of tax authorities. Instead, they depend on the broader actions of government beyond tax agencies in delivering reciprocal services or expanding the extent of political accountability. Even a politically-empowered tax agency cannot guarantee improved reciprocity in service delivery, as it depends upon the engagement of a broader set of government actors.

Underpinning these elements of trust is a basic requirement for competence. Classic accounts of trust in political officials distinguish between what have been labeled "judgements of integrity" and "judgements of competence". That is, governments need to have both the intent ("integrity") and the ability ("competence") to increase fairness, equity, reciprocity and accountability.[93] However, in the context of this framework, "competence" is best understood not as a distinct component of trust, but as a partial pre-condition for it. A government can be highly competent without being at all trustworthy if that competence is not combined with positive intent. Meanwhile, a government with positive intent may fail to be entirely trustworthy if it lacks the basic competence to deliver reliably on its promises. Different "sources" of mistrust will, of course, require distinct types of strategies.

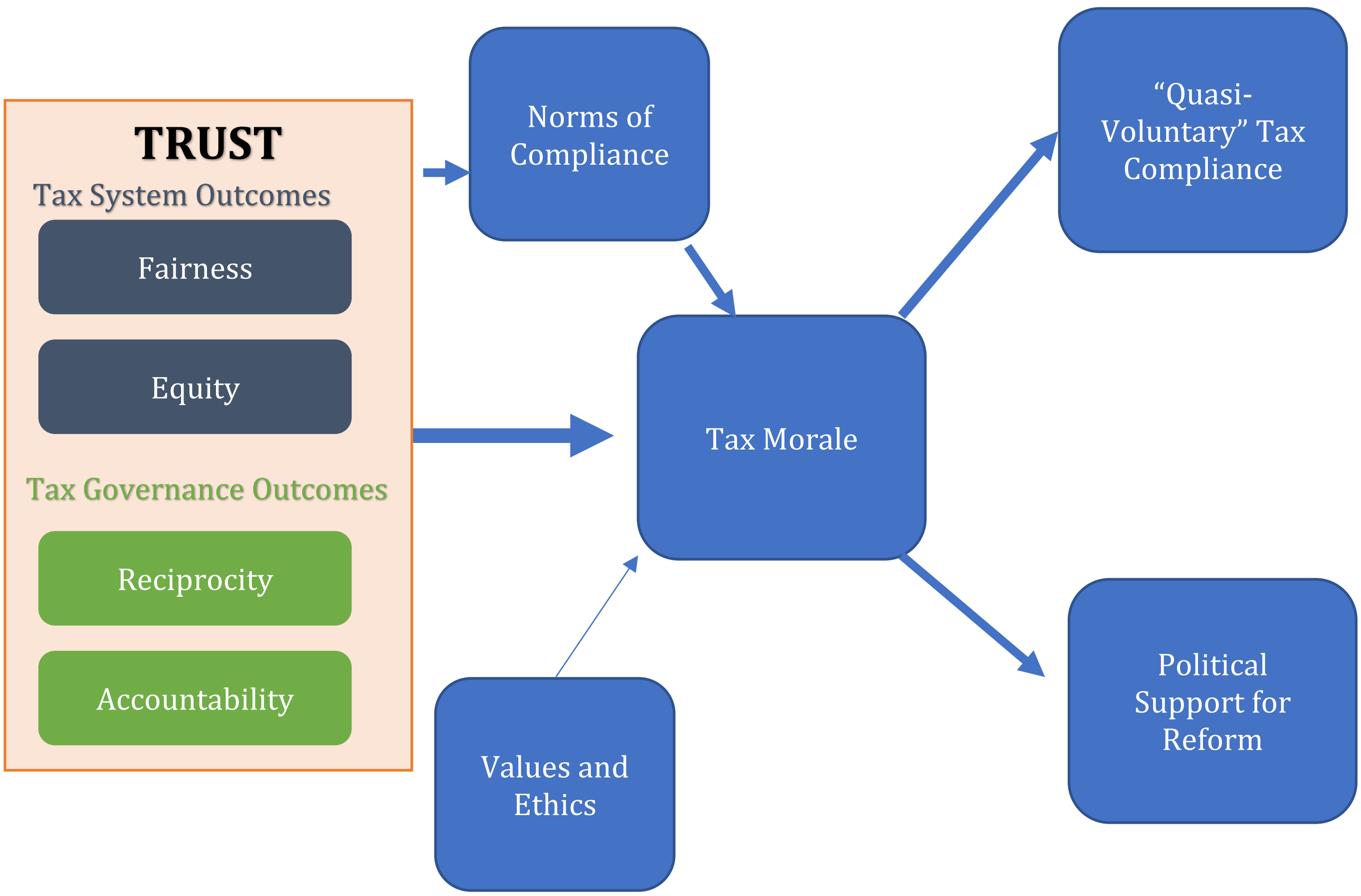
Ultimately, it is important to understand the construction of trust around tax compliance in active, reciprocal terms. Trust is not, in and of itself, socially beneficial. Blind trust in government can undermine long-term reform by reducing citizens' demands for improved outcomes.[94] The central goal of reform is not taxpayer education to convince them to pay taxes. Trust is, instead, something to be constructed through reciprocal action by taxpayers and governments. In the language of political science and sociology, the goal is not simply to foster trust among citizens, but to foster the trustworthiness of governments.[95] Taxpayers will increasingly trust the government if the government can successfully deliver fairness, equity, reciprocity and accountability. Governments will increasingly trust taxpayers if taxpayers increase tax compliance in response to improvements in government performance and openness. Given very limited public trust in public authorities, improvements are likely to be incremental. The payoff for governments is clear: not only improved tax compliance, but also the construction of political support for continued reform and expanded enforcement.

Figure 8 presents an operational model of trust as it relates to tax compliance and tax reform. This deepens the "trust" component of the overarching conceptual framework presented in Figure 7. Here, expanded trust is driven by each of four components – fairness, equity, reciprocity and accountability – which can, in turn, be divided into two categories: "tax system outcomes", which

[93] Barber, B. (1983). *The Logic and Limits of Trust*. New Brunswick: Rutgers University Press.
[94] Hardin, R. (1999). Do we want trust in government? In Hardin, R. (Ed.) *Democracy and trust*. Cambridge: Cambridge University Press, 22-41.
[95] Levi, M., & Stoker, L. (2000). Political trust and trustworthiness. *Annual Review of Political Science,* 3:475-507.

are broadly under the control of those responsible for tax policy and administration, and "tax governance outcomes", which relate to the management of tax revenues, and overall accountability, within the broader government. Where trust is expanded – driven by both positive intent and competence within government – this leads to expanded tax morale, while also shaping norms of compliance. Tax morale, in turn, drives two broad outcomes: enhanced "quasi-voluntary" tax compliance, and enhanced political support for current and future reform. In the bottom left of the model lie "ethics" and "values", which may equally shape levels of tax morale. However, they are kept outside the core model, as changes in trust are likely to be more operationally relevant for shaping compliance and reform.

**Figure 8: Trust, Tax Morale, Compliance and Politics**




A final note is required about the unique meaning of tax morale, and trust building, in the case of business taxpayers. The vast majority of academic research into tax compliance generally – and tax morale specifically – has focused on individual taxpayers, with ideas about tax morale then extrapolated to businesses as well. Yet compliance decisions by businesses may operate very differently: for example, for businesses potential reputational effects may be a key consideration in analyzing the costs and benefits of tax compliance. In turn, there may be sharp differences among different types of businesses. For small owner-operated businesses the distinction between individual and business taxation is modest, and the drivers of compliance may be comparatively similar. However, as businesses get larger – and particularly when they are internationally owned

– the contrast in drivers of compliance may be starker.[96] Among other factors, businesses may be (a) less directly reliant on, and concerned with, many kinds of public services valued by individuals; (b) less concerned with broad-based accountability, and more concerned with narrow responsiveness to business needs; (c) more narrowly focused on profit maximization owing to competitive pressures; and (d) subject to more fragmented, technocratic and bureaucratic decision-making, with more limited scope for tax morale to shape compliance decisions.

In light of the distinct characteristics of business tax morale, we apply the same broad trust framework – focused on fairness, equity, reciprocity and accountability – but tailored to the realities of different kinds of businesses. At a broad level, this means shifting what exactly we mean when we think about tax morale. To a greater extent than for individuals we expect business concerns about fairness, equity, reciprocity and accountability to be self-interested, and closely linked to long-term firm competitiveness and profit. Firms are likely to be concerned about fairness and equity not primarily owing to ethical concerns, but owing to concerns about their profitability, the predictability of the business environment and their competitive position. Firms are likely to be concerned about reciprocity and accountability not primarily out of a broad concern for social welfare, but out of a desire to secure specific government investments and policies relevant to their long-term well-being. In turn, we expect this broad orientation to result in issues related to fairness and equity – which have particularly direct implications for profit and competitiveness – to be comparatively important. Where individual tax morale is often defined as "non-pecuniary motivations for paying taxes," this line is less clear-cut for businesses. While business tax morale remains focused on motivations for compliance beyond the likelihood of detection and extent of penalties, to some extent all business decisions are expected to have at least an indirect pecuniary dimension. This does not preclude the possibility that different firms may have quite different "values" around compliance, rooted in different strategies and identities, nor the possibility of the existence of social norms shaping tax compliance across firms.

The rest of this section turns to exploring each component of trust in greater detail, both for individuals and businesses.

### Fairness

Fairness captures the extent to which taxpayers feel that the process for paying taxes is fairly designed and administered. This includes their understanding of the system, their treatment by tax collectors, the fairness of penalties and the availability of recourse in cases of abuse. It broadly combines the categories of "procedural justice" and "retributive justice" from economic psychology and is fundamentally about how individual taxpayers experience tax administrators and the tax system. Taxpayers – either individuals or businesses – are more likely to comply if they feel that they have been treated respectfully, honestly, and impartially.[97]

---

[96] Slemrod, J. (2004). The Economics of Corporate Selfishness. *NBER Working Paper 10858*. Cambridge, MA: National Bureau of Economic Research.

[97] Fjeldstad, O-H., & Tungodden, B. (2003). Fiscal corruption: A vice or a virtue? *World Development,* 31(8):1459-1467*;*Shapiro, M.D., & Slemrod, J. (2003). Consumer response to tax rebates. *American Economic Review,* 93(1): 381-396; Picciotto, S. 2007. "Constructing compliance: Game playing, tax law, and the regulatory state. *Law and Policy* 29(1):11-30.

One source of perceived unfairness in many developing countries is the fact that individuals, and some (particularly small) businesses, have limited understanding of the taxes that they are required to pay. In the most recent round of the Afrobarometer survey, over 55 percent of taxpayers reported that it was "difficult" or "very difficult" to find out what taxes they are supposed to pay to government.[98] This appears particularly true of local-level payments in lower-income countries, which may appear comparatively arbitrary. Recent surveys in Sierra Leone and the DRC both find that taxpayers report surprisingly limited understanding of the taxes that are due.[99] Discussions with small traders in Ghana, and elsewhere, similarly reveal significant difficulty in accessing information about the tax system,[100] while small firms often face substantial complexity and administrative hurdles to enter the formal sector.[101] Reflecting this concern, there has been mounting interest across countries in expanding taxpayer education.[102] However, an important distinction is needed. Tax administrations often conceptualize taxpayer education as an effort to teach taxpayers why paying taxes is important. However, what may be most needed to expand trust is taxpayer education that helps taxpayers to understand the taxes that they must pay, and how to do so.

A second source of unfairness is arbitrary or abusive enforcement – and extraction – by tax collectors. Surveys indicate that tax agencies are frequently among the least trusted institutions in many developing countries, and/or those most likely to be involved in corruption.[103] Particularly where face-to-face interactions between taxpayers and tax officials are common there is extensive evidence of tax collectors seeking to extract informal payments from taxpayers. There is some evidence that this extraction sometimes targets more vulnerable or less educated groups,[104] or areas in which tax collectors have greater leverage – owing, for example, to the ability to disrupt business operations[105] or access to key services.[106] But extraction is not limited to these groups. In trying to combat this source of mistrust in the tax system, one strategy has been to try to minimize face-to-face interaction between tax officials and taxpayers, or to minimize the scope for negotiation of tax payments. Automation has been one strategy for doing so. Another has been simplification, to remove discretion in the administration of tax laws. An alternative option is to seek to offer

[98] Afrobarometer Data, Round 6, 2014/15, available at http://www.afrobarometer.org.
[99] Jibao, S., Prichard, W., & van den Boogaard, V. (2017). Informal taxation in post-conflict Sierra Leone: Taxpayers' experiences and perceptions. *ICTD Working Paper 66*. Brighton: International Centre for Tax and Development.; Paler, L., Prichard, W., Sanchez de la Sierra. R., & Samii, C. (2017). Survey on total tax burden in the DRC, Final Report. Kinshasa: Department for International Development.
[100] Prichard, W., & van den Boogaard, V. (2017). Norms, power and the socially embedded realities of market taxation in Northern Ghana. *African Studies Review*, 60 (1):171-194.
[101] Joshi, A., Prichard, W., & Heady, C. (2014). Taxing the informal economy: The current state of knowledge and agendas for future research. *Journal of Development Studies*, 50 (10):1325-1347.
[102] OECD. (2015). *Building tax culture, compliance and citizenship: A global source book on taxpayer education*. Paris: Organisation for Economic Cooperation and Development.
[103] For example, Fjeldstad, O-H. (2005). Corruption in tax administration: Lessons from institutional reforms in Uganda. *CMI Working Paper 10*. Bergen: Chr. Michelsen Institute.
[104] Prichard, W., & van den Boogaard, V. (2017). Norms, power and the socially embedded realities of market taxation in Northern Ghana. *African Studies Review*, 60 (1):171-194.
[105] Hassan, M., & Prichard, W. (2016). The political economy of tax reform in Bangladesh: Political settlements, informal institutions and the negotiation of reform. *Journal of Development Studies*, 52 (12):1704-1721; Sequeira, S., & Djankov, S. (2016). Corruption, Trade Costs and Gains from Tariff Liberalization: Evidence from Southern Africa. *American Economic Review*, 106 (10): 3029-63
[106] Paler, L., Prichard, P., Sanchez de la Sierra, R., & Samii, C. (2017). Survey on total tax burden in the DRC, Final Report. Kinshasa: Department for International Development.

taxpayers greater opportunities to make complaints or appeals in cases of abuse by tax officials. This, in turn, needs to be coupled with tighter monitoring of abuses by tax officials.

A third source of unfairness lies in arbitrary or highly punitive penalties related to some taxes, both formal and informal. This often appears to be a particular problem with relatively smaller taxes, where enforcement can be highly punitive in some low-income countries.[107] Even for somewhat larger businesses, however, punitive enforcement measures – like closing down businesses – can be a double-edged sword. While they may sometimes be the only means to ensure payment from recalcitrant taxpayers, the application of these penalties can appear arbitrary when unevenly applied, and can give tax collectors enormous leverage in seeking to extract both formal *and* informal payments from taxpayers.[108] Here the reform goal is, in principle, simple: to put in place penalties sufficient to encourage compliance, but which are not excessive – and, which, critically, are consistently applied. However, there may be significant challenges on the ground. Where taxes are collected face-to-face, some discretion in tax collection may be hard to avoid, and also hard to monitor. Meanwhile, tax collectors may often defend strong penalties, owing to the rent-seeking opportunities they present, which creates a barrier to reform.

Particularly for businesses, the predictability of tax enforcement may figure centrally in compliance decisions. Research suggests that predictability – and not only related to taxation[109] – is very important for businesses, as predictability can facilitate planning and investment, while predictably equitable enforcement ensures a level competitive playing field.[110] Where tax laws are enforced fairly and consistently, firms seem more likely to declare tax obligations honestly based on the promise of avoiding informality, corruption and uncertainty. By contrast, where taxes are enforced inconsistently, firms have little incentive to declare honestly, as such honest behavior is not a guarantee of avoiding informality, corruption and uncertainty – and may disadvantage them relative to their competitors. Reflecting this logic, a recent OECD study goes so far as to use measures of "tax certainty" as a direct proxy for business tax morale, owing to the current absence of alternative measures and survey data.[111]

Inappropriate tax policies and problems with revenue forecasting sometimes lie at the root of unfair tax administration. In these cases, successful reform may need to happen "above" the level of administration. In some cases, unfairness is exacerbated by overly complex tax policies. This may be true where tax policies offer significant subjectivity in the assessment of tax liabilities – as with, for example, "market value" systems of property tax assessment, or presumptive tax systems based on administrative estimation of turnover. It may equally be true where tax policies are so

[107] Fjeldstad, O-H., & Therkildsen, O. (2008). Mass taxation and state-society relations in East Africa. in Brautigam, D., Fjeldstad, O-H., & Moore, M. (Eds.) *Taxation and state building in developing countries: capacity and consent.* Cambridge: Cambridge University Press; Fjeldstad, O-H., & Semboja, J. (2001). Why people pay taxes: The case of the development levy in Tanzania." *World Development*, 29 (12):2059-2074.
[108] This can be an issue even in relatively high capacity contexts. According to anecdotal evidence South Africa, for example, has seen increasing complaints from taxpayers about what they view as aggressive application of penalties – and sometimes extra-legal behavior by tax collectors.
[109] Campos, J. E., Lien, D., & Pradhan, S. (1999). The impact of corruption on investment: Predictability matters. *World Development*, 27 (6):1059-1067.
[110] Hassan, M., & Prichard, W. (2016). The political economy of tax reform in Bangladesh: Political settlements, informal institutions and the negotiation of reform. *Journal of Development Studies*, 52 (12):1704-1721.
[111] OECD. What is driving tax morale. *Public Consultation Document*. Paris: Organisation for Economic Cooperation and Development.

fragmented, and the number of formally taxed activities so extensive, that taxpayers have little hope of understanding all details – and tax collectors have ample opportunities for extraction.[112] A different problem can arise at the level of revenue forecasting. In many – if not most – cases, revenue forecasting is highly imprecise and achieved based not on objective assessment of actual tax capacity, but based on simple extrapolation from earlier years, or an assessment of revenue needs. Whatever the case, where revenue targets are set in ways inconsistent with economic and administrative realities, this can expand incentives for tax collectors to engage in arbitrary extraction to meet targets.[113]

**Equity**

Equity captures the extent to which the tax burden is felt to be fairly distributed across different taxpayers. There is now considerable evidence that taxpayers are less likely to comply – or to support higher taxes – when they feel that the distribution is unfair. Put differently, while taxpayers may be willing to pay their "fair share", they are more likely to oppose taxation when they feel that others are not paying enough. For individuals this may represent a form of principled resistance to bearing an unfair burden. For businesses the stakes may be more tangible and explicit: inequity in tax enforcement across firms operating in the same sector can generate an uneven competitive playing field and generate pressure on more compliant firms to reduce their tax burdens to match those of their less compliant competitors.[114]

The term "equity" captures two distinct dimensions: horizontal and vertical equity. Horizontal equity asks whether a taxpayer pays similar taxes to those in similar economic circumstances, or whether there are large differences in tax burdens among otherwise similar taxpayers owing to unequal tax policies, or unequal enforcement. Horizontal equity is similarly relevant to both individual and business taxpayers. Vertical equity asks whether the distribution of the tax burden is equitable across the wealth spectrum. This of course depends to an important degree on societal beliefs about what a "fair" vertical distribution of the tax burden looks like. In most countries there is a broad belief that individual tax burdens should be progressive -- that is, that the wealthy should pay more, as a share of income, than the less wealthy. The story for businesses is more complex. In most countries, corporate tax regimes apply a single tax rate to all firms, with a stated goal of ensuring competitive balance. However, effective tax burdens may vary owing to exemptions and incentives, while many countries apply special regimes for smaller firms, sometimes with the official goal of delivering somewhat lower burdens to those firms. Discussions of equity from the perspective of firms may thus focus on the relative balance of effective tax burdens across differently-sized firms.

The most conspicuous, and problematic, horizontal inequity in most countries appears to be the result of unequal enforcement of many taxes. Among those with enough income to be liable for individual income taxes, those whose primary income is from formal employment – and who thus

---

[112] Paler, L., Prichard, W., Sanchez de la Sierra, R., & Samii, C. (2017). Survey on total tax burden in the DRC, Final Report. Kinshasa: Department for International Development.

[113] Piracha, M., & Moore, M. (2015). Understanding low-level state capacity: Property tax collection in Pakistan. *ICTD Working Paper 33*. Brighton: International Centre for Tax and Development.

[114] Hassan, M., & Prichard, W. (2016). The political economy of tax reform in Bangladesh: Political settlements, informal institutions and the negotiation of reform. *Journal of Development Studies*, 52 (12):1704-1721.

are subject to withholding taxes on their salaries – generally bear dramatically higher effective burdens than those in self-employment, or with non-salary income.[115] Among firms, there may be sharp differences in burdens based on the level of formality, or the extent to which transactions are easily tracked – as with firms that do or do not use electronic tax registers, for example.[116] Among property tax payers, the failure to regularly update property valuations – and the frequently high levels of subjectivity in the valuation process – can result in hugely disparate assessments for similar properties, and in many properties being completely outside the tax net.[117] While difficult to document precisely, it is widely felt that those with strong connections within government and the administration are better able to minimize or avoid taxes.

An important source of such horizontally inequitable tax burdens may also lie in the international tax system. Firms that operate across borders may be better able to minimize their taxable profits through the use of complex tax structures, while national firms are less able to do so, while some sectors may also offer greater opportunities for evasion and avoidance.[118] Most writing about international tax evasion and avoidance has focused on its aggregate impact on revenues, and these continue to appear to be large in some sectors, led by the extractives sector. That said, the impact on competition across firms may be similarly important. The same is true of individuals, with wealthy individuals more able to exploit international opportunities to move wealth offshore to avoid local taxes. While precise figures are impossible to obtain owing to the inherently secretive nature of tax evasion, recent estimates suggest that 30 percent or more of financial wealth in developing countries is held offshore, free of taxes. This wealth is presumed to be held almost entirely by the very wealthy, and thus presents a major loss of revenue and of progressivity for developing country tax systems.[119]

In some cases, inequities may arise from national policy choices. At the national level, tax incentives and exemptions can generate substantial inequities across different businesses – with, in some cases, businesses in the same sector paying significantly different tax rates. This is a particular risk where government officials enjoy significant discretion in granting exemptions.[120] Special tax regimes granted to some extractive companies are a particularly prominent example.[121] However, such inequity is also possible where exemption regimes appear relatively transparent and rule-bound. Such regimes might, for example, create benefits for foreign companies over local companies. Alternatively, where incentives are time-bound, some firms may manage to extend

[115] Bird, R., & Zolt, E. (2005). Redistribution via taxation: The limited role of the personal income tax in developing countries. *International Tax Program Paper 0508*. Toronto: Joseph L. Rotman School of Management.
[116] These patterns are more likely to vary by country. Mascagni and Mengistu (2016) offer an example of an effort to estimate this variation in Ethiopia. Mascagni, G., & Mengistu, A. (2016). The corporate tax burden in Ethiopia: Evidence from anonymised tax returns. *ICTD Working Paper 48*. Brighton: International Centre for Tax and Development.
[117] Piracha, M. & Moore, M. (2015). Understanding low-level state capacity: Property tax collection in Pakistan. *ICTD Working Paper 33*. Brighton: International Centre for Tax and Development.; Khan, A., Khwaja, A., & Olken, B. (2016). Tax farming redux: Experimental evidence on performance pay for tax collectors. *Quarterly Journal of Economics*, 131 (1):219-271.
[118] This is a possible explanation, for example, for evidence that large firms pay lower effective tax rates than mid-sized firms in Ethiopia. Mascagni, G., & Mengistu, A. (2016). The corporate tax burden in Ethiopia: Evidence from anonymized tax returns. *ICT Working Paper 48*. Brighton: International Centre for Tax and Development.
[119] Zucman, G. (2014). Taxing across borders: Tracking personal wealth and corporate profits. *Journal of Economic Perspectives*, 28 (4):121-148.
[120] Klemm, A. (2009). Causes, benefits and risks of business tax incentives. *IMF Working Paper WP/09/21*. Washington: International Monetary Fund.
[121] Prichard, W., & Jibao, S. (2010). Building a fair, transparent and inclusive tax system in Sierra Leone. Freetown: Christian Aid Sierra Leone.

their incentives by creating the impression of new investment where none exists – for example through "sales" to offshore holding companies controlled by the same actors. Presumptive taxes on small businesses may sometimes have similar effects if the metrics used to calculate burdens are poorly calibrated.[122]

More extreme policy-driven inequities often arise at the local government level, owing to the often fragmented and opportunistic nature of local taxes. One ubiquitous example is comparatively high tax burdens on market traders, who have relatively low incomes but are an easily accessible tax base for local governments. Even within markets, flat rate taxes often mean that lower-income traders end up paying higher overall rates.[123] These inequities frequently also have strong gender dimensions, with market trade dominated by female traders.[124] In similar fashion, property taxes that are based entirely on the value of land may end up imposing the same tax on households with similar plots of land, despite one hosting a one bedroom home and the other a large mansion.[125] Local government revenue systems are also frequently (though decreasingly) characterized by large numbers of so-called "nuisance taxes" – highly idiosyncratic taxes on particular activities like brewing beer, raising livestock, holding a wedding, transporting certain goods and so forth. The result is that households with similar incomes may bear vastly higher tax burdens if they operate in an easily taxed sector.[126]

The significant vertical inequity within many developing country tax systems is receiving mounting attention amid growing concerns about inequality. Most, though not all, tax systems aim to be progressive in incidence among individual taxpayers, such that the share of income paid in taxes increases with overall income and wealth. To achieve this goal, most tax systems rely primarily on income taxes with progressive rates, while property taxes also have the potential to contribute to the overall progressivity of tax systems in the context of skyrocketing property values in many places.[127] However, these potentially progressive taxes are (by a significant margin) the least well-enforced major taxes in almost all low-income countries.[128] Historically, some countries

[122] This was the case, for example, in Ethiopia where highly detailed rates for different sectors, and at times subjective assessments, resulted in heavy burdens on some firms. Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining*. Vol. PhD Thesis. Cambridge: Cambridge University Press.

[123] Akpan, I., & Sempere, K. (2019). Hidden inequalities: Tax challenges of market women in Enugu and Kaduna states, Nigeria. *ICTD Working Paper 97*. Brighton: International Centre for Tax and Development.

[124] Prichard, W., & van den Boogaard, V. (2017). Norms, power and the socially embedded realities of market taxation in Northern Ghana. *African Studies Review*, 60 (1):171-194; Siebert, M., & Mbise, A. (2018). Toilets not taxes: Gender inequity in Dar es Salaam's city markets. *ICTD Working Paper 89.* Brighton: International Centre for Tax and Development.; Akpan, I., & Sempere, K. (2019). Hidden inequalities: Tax challenges of market women in Enugu and Kaduna states, Nigeria. *ICTD Working Paper 97*. Brighton: International Centre for Tax and Development.; Ligomeka, W. (2019). Expensive to be a female trader: The reality of taxation of flea market traders in Zimbabwe. *ICTD Research in Brief 35*. Brighton: International Centre for Tax and Development.

[125] Taxation exclusively of land is relatively uncommon, but exists, for example, in Kenya. In turn, in many other countries, valuations of improvements on land fail to capture their actual value, distorting tax liabilities.

[126] Paler, L., Prichard, W., Sanchez de la Sierra, R., & Samii, C. (2017). Survey on total tax burden in the DRC, Final Report. Kinshasa: Department for International Development.

[127] Goodfellow, T. (2017). Taxing property in the neo-developmental state: The politics of urban land value capture in Rwanda and Ethiopia. *African Affairs,* 116(475): 549–572.

[128] Kangave, J., Nakato, S., Waiswa, R., & Lumala Zzimbe, P. (2016). Boosting revenue collection through taxing high net worth individuals: The case of Uganda. *ICTD Working Paper 45*. Brighton: International Centre for Tax and Development.; Prichard, W. (2009). *Taxation and development in Ghana: Finance, equity and accountability*. London: Tax Justice Network; Fairfield, T., & De Luis Jorrat, M. (2016). Top income shares, business profits, and effective tax rates in contemporary Chile. *The Review of Income and Wealth*, 62(S1):S120-S144; Bird, R., & Zolt, E. (2005). Redistribution via taxation: The limited role of the personal income tax in developing countries. *International Tax Program Paper 0508*. Toronto: Joseph L. Rotman School of Management.

– primarily in the OECD – have also relied on broader taxes on wealth, including taxes on inheritance, though these taxes have rarely been significant in non-OECD countries and have been declining everywhere over time. The weakness of wealth taxes has further undermined progressivity.

With respect to business taxation, much discussion has focused on concerns that small informal sector firms may enjoy unfair advantages, but most evidence suggests that these concerns are overblown. In revenue terms, taxation of small and informal firms represents a tiny share of overall revenues and would be unlikely to generate large amounts of revenue even with stronger enforcement. Meanwhile, in equity terms it appears that small firms – including those classified as informal – often continue to bear significant formal fiscal burdens. Small firms are subject to fees, levies, local taxes or indirect taxes embedded in prices, as well as significant informal burdens.[129] More broadly, it remains unclear whether weak taxation of SMEs undermines broader trust in tax systems among the bulk of taxpayers. Torgler and Schneider present survey evidence that lower tax morale is associated with larger informal sectors. But the dominant interpretation is that causation likely runs from low morale to larger informal sectors, rather than the reverse.[130] It seems more likely that it is weak compliance among wealthy individuals and larger firms that poses a greater threat to trust in tax systems.

If there is a pervasive feeling that tax enforcement is inequitable, the challenge for governments is both to address the problem, and to gain the trust of taxpayers that they have done so. Increasing transparency around what people or firms pay in taxes may hold significant potential. In one example at the local level in Ethiopia, widespread concerns that small business taxes were being applied inequitably led some local governments to allow local business associations to participate in local tax assessments. Some simplified models of property tax valuation employ formulas based on observable characteristics of properties, so as to make the basis for valuations – and thus taxation – fully transparent to taxpayers.[131] In a very different example, advocates for more equitable taxation at the international level have argued for making country-by-country reports capturing tax payments by multinational firms publicly available – in order to ensure that all are paying their "fair share", create pressure for changes where they are not, and expand public confidence in the tax system. The most extreme example of tax transparency comes from Norway, which makes information on income, net worth and tax payments of every individual publicly available via a government web portal. The goal is to enhance trust in the tax system by demonstrating that everyone pays what is required under the law.

### Reciprocity

Reciprocity is perhaps the most intuitive of the four elements underlying trust in tax systems and lies at the core of the fiscal contract: the idea is that tax revenues will contribute to the provision of valued public goods and services. This concept is frequently at the heart of government outreach and education campaigns, which stress the need for taxes to fund national development. The

---

[129] Joshi, A., Prichard, W., & Heady, C. (2014). Taxing the informal economy: The current state of knowledge and agendas for future research. *Journal of Development Studies*, 50 (10):1325-1347.

[130] Torgler, B., & Schneider, F. (2009). The impact of tax morale and institutional quality on the shadow economy. *Journal of Economic Psychology*, 30 (2):228-245.

[131] Jibao, S., & Prichard, W. (2016). Rebuilding local government finances after conflict: Lessons from a reform program in post-conflict Sierra Leone. *Journal of Development Studies*, 52 (12):1759-1775.

operational question for governments is whether taxpayers believe that taxes are, in fact, used for national development – and, if not, how to build greater trust.

Surveys across the developing world suggest that taxpayers are, at least in principle, strong believers in the importance of taxation to fund government. Data from the Afrobarometer survey, for example, find that two-thirds of respondents on average believe that citizens should pay their taxes to support national development.[132] Faith in the general importance of taxes often exists even in areas of very poor service delivery. A recent survey in the Democratic Republic of Congo, for example, found that over 70 percent of respondents support taxation to fund national development.[133] It is occasionally suggested that developing country taxpayers may not understand, or value, the connection between taxation and national development. However, the empirical evidence shows unambiguously that broad support for effective taxation exists across a wide range of contexts.

Accordingly, there is mounting empirical evidence that if tax revenues are translated into public goods, this is associated with higher levels of tax morale and compliance. Recent survey and experimental evidence from Latin America offers clear support for a connection between perceived reciprocity and willingness to pay taxes.[134] This replicates more basic data from a variety of surveys from across the African countries.[135] An OECD survey conducted in 26 Asian countries showed that a majority of their citizens are in favor of tax increases if they are linked to more government spending and provision of public goods.[136]

While taxpayers express an in-principle commitment to taxation, they frequently harbor significant doubts about whether tax revenues are, in fact, used to support the broader public good. Survey respondents in the DRC, as noted above, expressed strong in-principle support for taxation, but 40 percent of respondents said that in practice they had refused or would refuse to pay taxes. This is a reflection of the strikingly low level of trust in the way the revenues are used, with 70 percent of respondents believing that the government is very likely to misuse tax revenue, and another 15 percent finding it somewhat likely.[137] While survey questions on this specific point are not widely available across countries, public concerns about use of government resources appear widespread.

The core challenge facing governments is thus to demonstrate to taxpayers that tax revenues are in fact being used to fund national development. Doing so is likely to require two things: (1) effective strategies for highlighting the connections between revenue and services for taxpayers; and (2) actual improvements in service delivery outcomes as revenue collection increases. While

---

[132] Aiko, R., & Logan, C. (2014). Africa's willing taxpayers thwarted by opaque tax systems, corruption. *Afrobarometer Policy Paper 7*. Afrobarometer.
[133] Paler, L., Prichard, W., Sanchez de la Sierra, R., & Samii, C. (2017). Survey on Total Tax Burden in the DRC, Final Report. Kinshasa: Department for International Development.
[134] Ortega, D., Ronconi, L., & Sanguinetti, P. (2016). Reciprocity and willingness to pay taxes: Evidence from a survey experiment in Latin America. *Economia*, 16 (2):55-87.
[135] Ali, M., Fjeldstad, O-H., & Sjursen, I. (2013). To pay or not to pay? Citizens' attitudes towards taxation in Kenya, Tanzania, Uganda and South Africa. *World Development*, 64:828-842.
[136] OECD. (2013). What drives tax morale? *Tax and Development*. Paris: Organisation for Economic Cooperation and Development.
[137] Paler, L., Prichard, W., Sanchez de la Sierra, R., & Samii, C. (2017). Survey on total tax burden in the DRC, Final Report. Kinshasa: Department for International Development.

improved communications alone may improve compliance or support for reform over the short term, it seems unlikely to be sustained in the absence of concrete improvements.

Assuming that governments are genuinely committed to improving services, increasing transparency is one strategy to achieve corresponding improvements in public trust. At the local government level this may mean publishing documents detailing revenue raised, and public expenditure by projects and categories. At the national level a growing number of countries publish – sometimes in newspapers – all public spending projects, thus allowing for more targeted public expenditure monitoring. In Kenya, for example, civil society groups have sought to explicitly link citizens' status as taxpayers to their expenditure tracking advocacy.[138]

However, there are important concerns about the efficacy of transparency initiatives alone. Most basically, the available information may be of limited immediate value to most taxpayers. It may be difficult to access, or difficult to understand, and thus may depend on intermediary groups – civil society and the media in particular - to "translate" it into a form that is useful to a broader group of taxpayers. These groups, of course, are frequently weak. While civil society and media engagement with spending issues is extensive, tax issues frequently remain less covered. And, of course, the availability of information is only likely to encourage trust if the information provided is evidence of effective government performance that meets popular expectations. Transparency about poor performance may, in fact, reinforce a lack of trust in public authorities.

A related option is to try to demonstrate connections between taxes and broader public goods more explicitly and directly. The increasingly common taxpayer education programs represent one channel,[139] and in a growing range of countries these are accompanied by call-in radio shows and public forums designed to create engagement between taxpayers and governments. Recent research presents evidence that well-designed taxpayer education programs can significantly increase tax knowledge, while also having positive effects on compliance – effects that appear largely attributable to facilitating compliance but may also reflect improved willingness to pay.[140] An alternative approach is targeted communication about tax-expenditure links. As noted above, an experiment in Rwanda found that letters to taxpayers stressing the connections between taxes and services were generally at least as effective as enforcement threats in increasing compliance.[141]

Still, communication-based interventions may have a limited ceiling, or diminishing returns. Telling taxpayers about the link between tax payments and public services is unlikely to be a

---

[138] Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining*. Cambridge: Cambridge University Press.

[139] OECD. (2015). *Building Tax Culture, Compliance and Citizenship: A Global Source Book on Taxpayer Education*. Paris: Organisation for Economic Cooperation and Development; Prichard, W., Beach, R., Mohiuddin, F., & van den Boogaard, V. (forthcoming). The micro-links between taxation and accountability initiatives. *ICTD Working Paper*. Brighton: International Centre for Tax and Development.

[140] Mascagni, G; Santoro, F. & Mukama, D. (2019). Teach to comply? Evidence from a taxpayer education programme in Rwanda. *ICTD Working Paper 91*. Brighton: International Centre for Tax and Development; Similarly, a World Bank project that combined tax infrastructure improvements with a comprehensive education program resulted in significant increases in tax revenue. World Bank, (2017). Modernization, Taxpayer Education Provide Good Foundation for Tax Collection in Tanzania. Washington, DC: World Bank Group. http://www.worldbank.org/en/results/2017/01/05/modernization-taxpayer-education-provide-good-foundation-for-tax-collection-in-tanzania

[141] Mascagni, G., Nell, C., & Monkam, N. (2017). One size does not fit all: A field experiment on the drivers of tax compliance and delivery methods in Rwanda. *ICTD Working Paper 58*. Brighton: International Centre for Tax and Development.

substitute for *actual* improvements in public services in a context where citizens are generally dissatisfied. A letter from the tax administration stressing the links between taxes and services may improve short term compliance – but what happens over the longer term if there are no subsequent improvements in services? Meanwhile, the increases in compliance reported in these studies, while certainly important, remain relatively small compared to overall revenue leakage. Perhaps reflecting these challenges, studies about such letter- and SMS-based communication campaigns seeking to highlight tax-expenditure links have produced somewhat inconsistent evidence across countries, suggesting that their effectiveness might be at least partly context-specific.[142]

If relying on transparency or communication-based initiatives seems inadequate to increase trust, earmarking revenues is an option. Earmarking is a way to more explicitly link specific revenue collection to specific public expenditures either formally or informally. Such earmarking can range from simple government declarations that new revenues will be used for specified purposes, to formal legal commitments. Legal commitments can be more or less binding in practice depending on the extent of budgetary fungibility.[143] When the commitments are genuine, a small but growing body of evidence suggests that they can increase taxpayer trust and support for expanded taxation, while also strengthening the translation of revenues into public services.[144] The best documented example comes from Ghana, where the government earmarked increases in the VAT rate for, respectively, a Ghana Education Trust Fund and the National Health Insurance Scheme, in both cases also creating new oversight mechanisms to ensure that these promises were executed.[145]

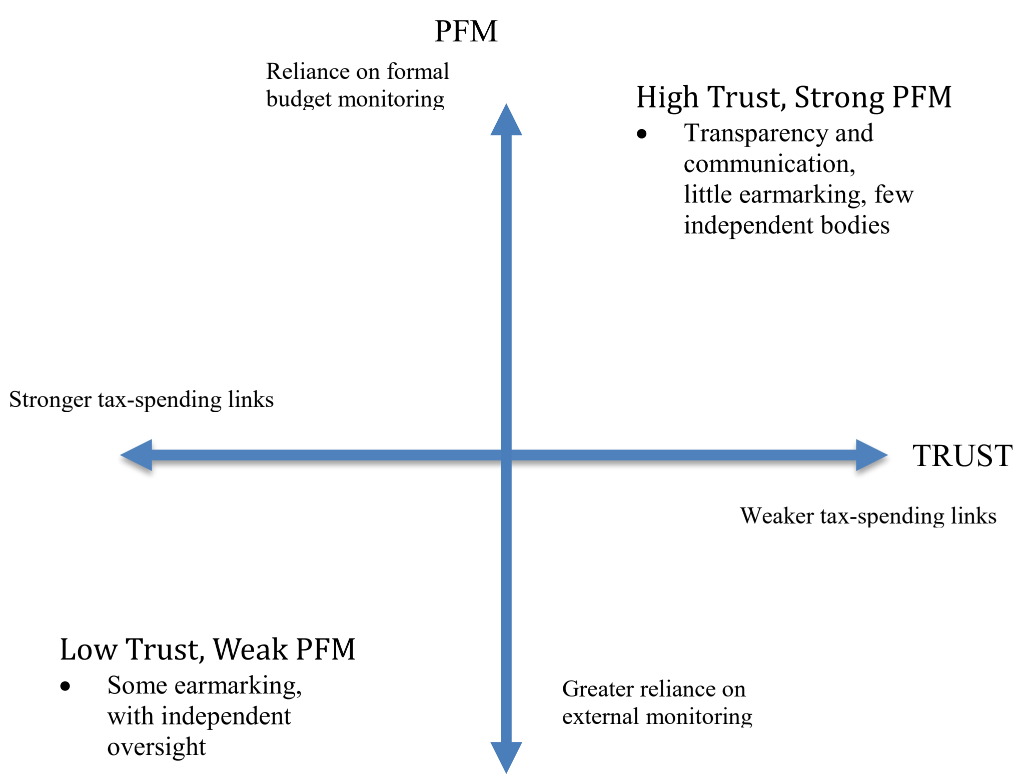
However, there are important trade-offs in drawing increasingly explicit ties between taxes and services. Conceptually, taxes are generally intended to be *unrequited* payments to government, and such earmarking risks creating expectations – particularly among the wealthy – that they should receive quite narrow and direct benefits from tax payments. More pragmatically, the expansion of earmarks can create problematic budget rigidity, while budget fungibility means that earmarks can become political theater, and complicate budget processes, without actually driving improvements in service delivery.[146] These risks are a reminder that earmarking almost certainly should be used cautiously, and with clear justification. This includes an emphasis on ensuring that earmarking is actually translated into increased spending on designated activities – including, potentially, through specific oversight functions that encourage public monitoring – and on using earmarks to support broad public benefits rather than narrow benefits to elite groups.

[142] Castro, L., & Scartascini, C. (2015). Tax compliance and enforcement in the pampas evidence from a field experiment. *Journal of Economic Behavior & Organization*, *116*, 65-82; Weigel, J. L. (2018). *The taxman cometh: A virtuous cycle of compliance and state legitimacy in the DR Congo*. Working Paper.
[143] Bird, R., & Jun, J. (2005). Earmarking in theory and Korean practice. *International Studies Program Working Paper 05-15*. Atlanta: Andrew Young School of Policy Studies, Georgia State University.
[144] Prichard, W. (2009). The politics of taxation and implications for accountability in Ghana 1981-2008. *IDS Working Paper 330*. Brighton: Institute of Development Studies; Flores-Macias, G. (2012). Financing security through elite taxation: The case of Colombia's "Democratic Security Taxes". *Studies in Comparative International Development*, 49 (4):477-500; Flores-Macias, G. (2016). Building support for taxation in developing countries: Experimental evidence from Mexico. *ICTD Working Paper 51*. Brighton: International Centre for Tax and Development.
[145] Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining*. Cambridge: Cambridge University Press; Cashin, C., Sparkes, S., Bloom, D., (2017). Earmarking for health: form theory to practice. *Health Financing Working Paper No.5.*
[146] Bird, R., & Jun, J. (2005). Earmarking in theory and Korean practice. *International Studies Program Working Paper 05-15*. Atlanta: Andrew Young School of Policy Studies, Georgia State University.

Ultimately, the case for drawing stronger connections between specific taxes and specific expenditures may be comparatively strong in countries where trust is very low, and at the subnational level. At very low levels of trust, the benefits of using tax-spending links to build some trust may outweigh the downsides of earmarking. At one extreme, policy makers could face trade-offs between remaining stuck in a low revenue equilibrium characterized by low compliance, trust and support for reform, or drawing stronger tax-spending links to mobilize political support for reform. Confronted with this choice, tighter tax-spending links, while imperfect, may hold important advantages. Meanwhile, the use of earmarking may be more meaningful at the subnational level, where clear links between revenues and public benefits are more straightforward and easier to monitor, including around highly visible spending on local markets, street cleaning, public toilets, bus services, basic sanitation, road maintenance and other small-scale services.

Figure 9 presents a basic framework for thinking about the contexts in which different types of tax-expenditure links may be appropriate. Along the horizontal axis, comparatively specific and binding tax earmarking may be more appropriate in contexts in which trust is more limited. This reflects the trade-off between the technical and conceptual costs of earmarking, and the benefits for trust promotion. Along the vertical axis, reliance on external monitoring of any earmarking – via new oversight institutions, specific transparency measures or the like – is likely to be more important where formal PFM and budget institutions are weak. In these contexts, external institutions for monitoring may be particularly important for ensuring that earmarking is meaningful, as opposed to a pure (and misleading) political exercise.

**Figure 9: Potential Role of Tax-Expenditure Links Across Contexts**



## Accountability

While the desire for reciprocity captures taxpayers' interest in receiving public goods and services, a demand for accountability captures the desire for an institutionalized voice in shaping how tax and spending decisions are made. Of course, the goals of reciprocity and accountability are overlapping: the goal of accountability is, often, to provide an institutionalized way for taxpayers to demand and ensure reciprocity. But they are also meaningfully distinct. Where reciprocity implies governments making potentially time-limited concessions to taxpayers, institutionalized accountability is intended to ensure that reciprocity is sustained. As importantly, accountability may have independent value to those who are granted a voice in shaping tax and spending decisions.

Evidence suggests that lower levels of corruption, as well as participatory budgeting and other forms of direct democracy, are associated with higher tax compliance. This underscores the importance of accountability in shaping trust in tax systems. For example, a recent cross-national survey experiment carried out by the World Bank finds that interventions which increase the salience of anti-corruption efforts and allow citizens to state their expenditure preferences to the government result in sizable and significant increases in tax morale relative to a control group.[147] Two studies from Brazil yield similar findings. In one the authors find that evidence of corruption reduces property tax receipts, and increases demands for participatory budgeting.[148] A World Bank study demonstrates that the presence of participatory governance institutions is closely associated with the ability of municipal governments to raise local tax revenue.[149] The research shows that Brazilian municipalities that voluntarily adopt participatory institutions collect significantly higher levels of taxes than other, similar municipalities without these institutions. Similarly, earlier research from Switzerland found that tax compliance is substantially higher in cantons with larger reliance on direct democracy, including fiscal referendums.[150] Somewhat more broadly, research has argued that tax collection and compliance often increase following the election of new governments, because of renewed popular trust following successful elections.[151]

The importance of accountability in shaping trust and tax compliance among business taxpayers has been comparatively under-researched, though some key messages have begun to emerge. In general, relative to individuals, businesses appear more concerned about the creation of specific, and comparatively narrow, forums for participation in shaping government action, as these forums may most directly address their core interests and concerns. In Ethiopia, concerns about the arbitrary application of presumptive taxes on small businesses led state governments to invite business associations to joint assessment committees.[152] In Ghana, initial efforts to tax the informal sector were pursued through the introduction of "associational taxation" by which tax collection

---

[147] Sjoberg, F., Mellon, J., Peixoto, Hemker, J., & Tsai, L., (2019). Voice and Punishment: A Global Survey Experiment on Tax Morale. .*World Bank Policy Research Working Paper 88558855.* Washington: World Bank.
[148] Timmons, J., & Garfias, F. (2015). Revealed corruption, taxation and fiscal accountability: Evidence from Brazil. *World Development*, 70:13-27.
[149] Touchton, M., Wampler, B., & Peixoto, T. (2019). Of governance and revenue: Participatory institutions and tax compliance in Brazil. *World Bank Group, Policy Research Working Paper 8797.* Washington: World Bank.
[150] Torgler, B. (2005). Tax morale and direct democracy. *European Journal of Political Economy*, 21:525-531.
[151] Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining.* Cambridge: Cambridge University Press.
[152] Ibid.

was conducted by associations themselves, and then revenues were remitted to government.[153] In many countries, governments seeking to encourage compliance among larger businesses have introduced consultative bodies with business associations.[154] In at least some cases, these are forums that allow businesses to pursue policy options in which they have a specific interest.[155] None of these efforts has rigorously sought to assess the link between such forums of accountability and compliance, but this anecdotal evidence – and the fact that governments have invested in creating such forums – is suggestive of their potential efficacy.

The role of accountability in strengthening trust, tax morale and tax compliance has been given less attention historically than other topics, but recent research has increasingly highlighted important links. The nature of these accountability links, and the strategies that states might pursue in strengthening them, have been highly diverse. The preceding examples range from broad attempts to strengthen democracy, or the introduction of participatory budgeting, to much more micro-level interventions related to transparency, taxpayer involvement in tax assessment, new oversight institutions for specific (sometimes earmarked) public spending, or specific bargaining institutions (for business in particular). A critical challenge for reformers thus lies in identifying the right kinds of local strategies for building trust.

## TAILORING REFORM: COMBINING ENFORCEMENT, FACILITATION AND TRUST TO STRENGTHEN FISCAL CONTRACTS

A key challenge for governments lies in finding the right combination of enforcement, facilitation and trust-building measures to achieve both revenue and broader development goals. Here existing research has comparatively little to say. While it is clear that all these factors matter, it is less clear how best they may be combined, prioritized or sequenced. Most likely, there is not a single answer to these questions. Instead the answer is likely to depend on understanding the specific objectives and constraints that exist in specific contexts, while thinking of enforcement, facilitation and trust as complementary, rather than distinct, strategies.

Central to successful reform is an understanding of enforcement, facilitation and trust as complementary—and necessary—components of a comprehensive reform strategy. Investments made exclusively in any one area are likely to be undermined by a lack of progress in other areas. Absent a measure of effective and equitable enforcement, it will remain difficult to raise levels of trust in tax authorities. Absent greater trust, it is likely to remain difficult to build quasi-voluntary compliance, and to mobilize the political will needed to dramatically improve enforcement. And both types of reform can be undermined by a lack of attention to facilitation, as difficulties in understanding tax liabilities and making payments can quickly undermine trust and compliance. Unsurprisingly, then, some of the best documented recent cases of relatively successful tax

[153] Joshi, A., & Ayee, J. (2008). Associational taxation: A pathway into the informal sector. In Brautigam, D., Fjeldstad, O-H., and Moore, M. (Eds.). *Taxation and State Building in Developing Countries: Capacity and Consent.* Cambridge: Cambridge University Press.

[154] Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining*. Cambridge: Cambridge University Press; Moore, M. (2014). Revenue reform and state building in Anglophone Africa. *World Development*, 60:99-112.

[155] In one documented case, in Ghana, business associations successfully pushed to have some of the revenue from a new tax devoted to a new venture capital fund; Prichard, W. (2015). *Taxation, responsiveness and accountability in developing countries: The dynamics of tax bargaining*. Cambridge: Cambridge University Press.

reform—such as those in Lagos and Edo, Nigeria—have combined parallel investments in enforcement, facilitation and trust.[156]

However, while the connections between enforcement, facilitation and trust are increasingly recognized, existing work has struggled to translate this broad insight into concrete strategies for strengthening reform. While individual research findings have pointed toward specific types of interventions that have been successful in specific contexts, a broader framework is needed in order to identify appropriate reform strategies that are likely to work in particular contexts. This would take into account the variations in starting points, objectives, and constraints. Such strategies need to be able not only to identify technical challenges and barriers to reform, but to analyze political barriers, to identify binding constraints on reform, and to adopt targeted strategies for building trust – and strengthening fiscal contracts – as part of holistic reform strategies.

International organizations have recently made considerable progress in assessing the policy and administrative barriers to improved performance. Tools such as TADAT and DIAMOND offer a nuanced understanding of what is not working in relation to various aspects of tax enforcement, while also offering a snapshot of some aspects of facilitation and taxpayer outreach. However, identifying what is not working is only the first step to identifying the appropriate target for reform. The latter requires understanding where reform is technically and politically feasible – and which areas of "dysfunction" are the most binding constraints on overall performance. For example, in the context of sharply limited human resources, broad-based capacity building for international taxation may face technical limits – and efforts at highly targeted enforcement, or policy simplification, may offer greater payoffs.

Reformers may consider an interconnected – but not necessarily linear – set of questions in guiding reform design. These are, of course, likely to vary by country, but offer a sense of how reform programs that are tailored to local contexts, and which combine enforcement, facilitation and trust, may be developed. First, what are the central objectives of reform? Second, what are the key political barriers to reform? Third, what are the binding constraints on reform? Fourth, how can investments in enforcement, facilitation and trust best be combined? What follows considers each element of potential reform strategies in turn.

*Social Desirability: What are the central objectives of reform?*

The starting point for any reform is a clear understanding of what the reform aims to achieve, and what broad strategies may contribute to that goal. Central to most reform efforts is a desire to increase revenue collection. However, reform is equally likely to be motivated, in varying degrees, by desires to increase economic efficiency, expand equity, improve trust in government and strengthen the fiscal contract. These latter objectives are critical to thinking about the development goals of reform. Expanded taxation is only socially beneficial if it translates into reciprocal benefits for taxpayers, while the extent of those social benefits will be much larger where tax and fiscal systems are fair, equitable and redistributive.

[156] Cheeseman, N., & de Gramont, D. (2017). Managing a mega-city: Learning the lessons from Lagos. *Oxford Review of Economic Policy*, 33 (3):457-477; Porter, D. & Watts, M. (2017) Righting the resource curse: Institutional politics and state capabilities in Edo State, Nigeria. *The Journal of Development Studies*, 53:2, 249-263.

Well-defined objectives should shape the targeting of reform in significant ways. Different objectives are likely to imply a focus on different segments, and different combinations of enforcement, facilitation and trust-building reforms. Over the past several decades, a focus on revenue mobilization and economic efficiency has frequently motivated a primary focus on enforcement reforms related to the VAT. A greater focus on equity and trust might, for example, imply more attention to income and property taxes. A concern with strengthening the fiscal contract at the sub-national level might lead to a focus on local-level taxes. Critically, varying objectives may not only shape the segments of the tax system to be targeted, but the specific approaches adopted within segments. Even among two countries interested in expanding taxation of businesses, specific focuses could vary substantially: a focus on revenue maximization may dictate an emphasis on maximizing collection from large and easily-identified firms, while a focus on equity might imply a focus on those who are outside the tax net – though whether the focus is on larger or smaller informal firms will, again, depend on the overall priorities of reform.

*Technical Appropriateness: What are the binding constraints on reform?*

Once goals have been defined, designing successful reform is likely to depend on identifying the *binding constraints* to progress– technical, social and political –within particular taxpayer segments. Tax systems are likely to vary in the extent to which weak compliance is driven by (a) a lack of technical capacity for enforcement; (b) high costs of compliance; (c) low trust and tax morale; or (d) political barriers to reform. And, of course, this may vary across tax segments, tax types and over time. If the goal of reform is, for example, to increase vertical equity through improved income tax enforcement, there is a wide variety of possible strategies available: changes to tax laws, expanded or improved audits, improved data sharing, introduction of new IT systems, stronger and more enforceable penalties and so forth. The challenge lies in identifying the most feasible and impactful focus for reform. Strategies to reduce compliance costs may similarly vary quite dramatically across segments of taxpayers. For example, some countries have introduced "tax fairs" of various kinds to attempt to register small informal firms. These "fairs" assume that the largest barrier to formalization is a lack of knowledge and the difficulty of reaching tax offices. But, while this may be true for some firms, for others the primary concern may be that formalization would expose them to new forms of informal harassment by tax officials, or unmanageable reporting requirements. Meanwhile, while reform diagnostics tend to focus on identifying technical steps, in many cases the binding constraint may actually be the absence of adequate political commitment – or public sector leadership – to put widely-understood reforms into practice. Selecting the appropriate strategy demands an understanding of the binding constraint in a particular country context.

More specifically, a binding constraints analysis generally consists of four steps. These include 1) defining a clear problem statement; 2) developing a decision tree that lays out all the potential causes of suboptimal performance;[157] 3) systematically identifying which causes are, in fact, most important; and 4) among these, identifying likely *binding* constraints. Because the potential barriers to reform are often diverse, and tax administrations are often characterized by a wide variety of overlapping weaknesses, a key challenge for reformers lies in pinpointing the most significant issues. Where there is a clear understanding of the binding constraint on reform this

[157] Drawing on existing tax diagnostic tools, like TADAT or DIAMOND, may be very valuable at this stage.

can allow for effective prioritization and targeted reform programs – often focused on the "basics" of improved performance – that reduce the scope and technical complexity of reform efforts, while increasing their political feasibility.

A particularly compelling illustration of the value of this kind of analysis comes from examining challenges in reforming IT systems. Donor programs have often identified major limitations of existing IT systems, and significant potential to achieve large improvements in outcomes, and have correspondingly made the introduction of sophisticated IT systems a central part of reform strategies. Yet these reform programs have frequently had significant delays, and upgraded IT systems have continued to be underutilized even after implementation. The most persuasive explanation for this underperformance is that while IT systems offered significant potential to improve outcomes, weak IT systems *per se* have often not been the binding constraint on reform. Instead, poor performance has been rooted more deeply in failures of process or politics that have prevented even relatively basic data sharing and audit measures that are, in principle, possible even without broader IT reform. Here again, knowing that existing IT systems are underperforming is not on its own an adequate guide to targeting reforms –a binding constraints analysis is likely to point toward the need to first, or in parallel, address other challenges essential to maximizing the impact of IT reform.

*Political Feasibility: What are the key political barriers to reform?*

What kinds of technical reform are consistent with existing political constraints, and how can political barriers to action be overcome, and/or how can support for reform be constructed and sustained? There is now near-universal agreement that political hurdles are frequently the most important barriers to reform – and thus agreement about the importance of problem-focused political economy analysis to inform reform efforts. A problem-focused political economy analysis aims to provide a sophisticated assessment of the politics of reform that anticipates likely challenges – both inside and outside of tax agencies – and potential strategies for confronting them. The starting point is an assessment of the extent of political support for reform and the configuration of political interests. The core concern is not with an exhaustive mapping of possible interests, but a focused interrogation of the interests that are likely to shape the prospects for the success of reform, with a view to (a) informing the design of reform that is most likely to succeed amid existing political constraints ("incentive compatible reform"); and (b) supporting the design of strategies to minimize resistance and build support for reform.[158]

The initial goal of political economy analysis is to assess the extent of political support, and the consequent feasibility of different reform options – but doing so can be complex. Government actors have strong incentives to express confidence in reform in order to access external support but may in practice lack sufficient political will to overcome entrenched resistance. However, tax reform provides unique opportunities for overcoming this challenge: it is often characterized by reform options that are low cost and technically simple, but politically costly – for example, expanding basic data sharing about high-income taxpayers. Jibao and Prichard have argued that government may "reveal" its underlying commitment to reform through its willingness to take

[158] Prichard, W. (2019). Tax, politics, and the social contract in Africa. *Oxford Research Encyclopedia of Politics*. Oxford: Oxford University Press.

such politically costly – but financially and technically manageable – reform steps, often without donor support.[159] Three types of actions stand out: improving the sharing and transparency of available data, pursuing enforcement actions against elites, and expanding genuine consultation with taxpayers.[160] If governments are unwilling to take financially low-cost steps of proven efficacy to improve enforcement, this may be an important signal of the absence of genuine political commitment to reform.

Assuming a baseline of political support for reform exists, the broader goal of problem-focused political economy analysis is to support governments in identifying strategies for minimizing opposition and building support for reform. Research by Fairfield has proposed six broad strategies for increasing the viability of tax reform specifically targeting elite groups.[161] On one hand, she argues for seeking to weaken resistance to reform by slowing the phase-in of reform, or obscuring its full impact; seeking to divide resistance by appealing to the importance of horizontal equity in enforcement; and providing some reciprocal shorter–term benefits to powerful groups resisting reform. On the other hand, she argues for seeking to build a broader-based constituency for reform, based on the commonsense observation that the lower income majority should, in principle, favor more effective enforcement among elites. This, she argues, can be pursued by stressing the virtues of a more vertically equitable tax system, and by clearly linking new tax revenue to popular public services.[162] These latter goals are, in the language of the framework developed here, aimed at building trust among taxpayers.

Whereas tax reform was once viewed as almost entirely the preserve of technical experts, the challenge of overcoming the political barriers to reform points to a need for broader public engagement. Over the past decade, increasingly independent business associations have become active in tax debates, as have a broader range of civil society organizations.[163] The expansion of public engagement in tax debates may in some cases increase barriers to reform, as businesses seek narrow tax benefits and a broader base of taxpayers resist tax reforms in systems that they do not trust. However, in the longer term, broadening public debate about taxation has the potential to shift the politics of reform in a positive direction by enabling the creation of coalitions in favor of expanded progressive taxation and greater reciprocity and accountability in the use of those revenues.[164] Critically, there is scattered evidence that the expansion of taxation that is fair, equitable, reciprocal and accountable can, indeed, become a political asset for governments. An

[159] Jibao, S., & Prichard, W. (2016). Rebuilding local government finances after conflict: Lessons from a reform program in post-conflict Sierra Leone. *Journal of Development Studies*, 52 (12):1759-1775.
[160] Adapted from ibid.
[161] Fairfield, T. (2013). Going where the money is: Strategies for taxing economic elites in unequal democracies. *World Development,* (47): 42-57.
[162] Ibid.
[163] Fjeldstad, O-H., Rakner, L. & Ngow, P. 2015. Shaping the tax agenda: Public engagement, lobbying and tax reform in Tanzania. *CMI Brief 14:5*, Bergen: Chr. Michelsen Institute; Fjeldstad, O-H., & Johnson, J. 2017. Governance challenges in Tanzania's natural gas sector: Unregulated lobbyism and uncoordinated policy. In Williams, A. & Le Billon, P. *Corruption, Natural Resources and Development: From Resource Curse to Political Ecology*. Cheltenham: Edward Elgar.
[164] Moore, M., Prichard, W. & Fjeldstad, O-H. (2018). *Taxing Africa: Coercion, Reform and Development*: Zed Books; Prichard, W. (2018). Improving Tax and Development Outcomes: What Next for Civil Society Engagement? *Transparency & Accountability Initiative*. Washington: OpenGov Hub.

effort to crack down on evasion in Italy has been shown to have yielded significant electoral benefits for local politicians.[165]

*Building Fiscal Contracts: How can investments in enforcement, facilitation and trust best be combined?*

The final reform challenge lies in identifying the right balance between investments in enforcement, facilitation and trust – while developing specific and detailed strategies for enhancing trust. Where the primary barrier to reform is a lack of technical capacity, there may be a case for greater investments in enforcement – but these may need to be matched by necessary investments in trust, to sustain necessary political support. Where a lack of political support for reform is the binding constraint, priority may be given to investments in trust. But government will need to establish what types of trust are most needed, and from whom – while investments in enforcement and facilitation are likely to be important elements of trust-building reforms. The adoption of such holistic approaches does not imply trying to reform all aspects of the tax system at once, but rather the strategic linking of mutually reinforcing interventions within well-defined reform areas, in order to root reform in the construction of a broad fiscal contract.

Particularly important is the need to move from a general focus on enhancing trust, and toward a specific, evidence-based and contextually appropriate set of strategies. There is now broad agreement that enhancing trust can be important to improving compliance and building political support for reform. However, existing evidence suggests that the importance of different aspects of trust is likely to vary across contexts, and over time, while different kinds of trust-building interventions – like communications programs – may have quite distinct impacts in different places. Success likely requires adopting strategies to understand (a) which kinds of trust, among which subset of taxpayers, are needed in order to support specific kinds of reform; (b) the particular roots of taxpayer mistrust in specific contexts; and (c) the potential of different kinds of interventions to improve outcomes. To date, many government initiatives for improving trust have been comparatively generic and have not accurately reflected taxpayers' particular views and concerns. One study in Ghana and Sierra Leone, for example, found that while governments have often emphasized general campaigns – like billboards – stressing the importance of paying taxes, alongside taxpayer education programs about how to pay taxes, taxpayers tend to be more interested in having access to detailed information about the links between revenue and spending, along with interactive forums for engagement with governments.[166]

In emphasizing the role of trust-building in reform design, the goal is not simply to maximize revenue, but also to develop strategies for strengthening the fiscal contract and building virtuous circles of reform. Research has provided a broad picture of the strategies that may be employed to empower taxpayer voices as part of tax reform, including expanding the political salience of taxation, improving horizontal equity in enforcement, strengthening transparency and the links between revenues and expenditures, and supporting institutional space for engagement between

[165] Casaburi, L., & Troiano, U. (2015). Ghost-house busters: The electoral response to a large anti–tax evasion program. *The Quarterly Journal of Economics*, *131*(1), 273-314.

[166] Prichard, W., Beach, R., Mohiuddin, F., & van den Boogaard, V. (forthcoming). The micro-links between taxation and accountability initiatives. *ICTD Working Paper*. Brighton: International Centre for Tax and Development.

taxpayers and governments.[167] All of these approaches overlap closely with strategies for increasing trust, compliance and political support for reform. As such, there is a clear argument for reformers to place greater emphasis on trust-building, not only to increase revenue collection, but to support the translation of new revenues into broader social benefits.

[167] Prichard, W. (2015). *Taxation, responsiveness and accountability in Sub-Saharan Africa: The dynamics of tax bargaining*. Cambridge: Cambridge University Press; Prichard, W., Beach, R., Mohiuddin, F., & van den Boogaard, V. (forthcoming). The micro-links between taxation and accountability initiatives. *ICTD Working Paper*. Brighton: International Centre for Tax and Development.