



Working Paper 84

Taxing Government: The Case of the Uganda Revenue Authority's Public Sector Office

Henry Saka, Ronald Waiswa and Jalia Kangave

October 2018

BILL & MELINDA
GATES *foundation*

 Institute of
Development Studies


ukaid
from the British people

ICTD Working Paper 84

Taxing Government: The Case of the Uganda Revenue Authority's Public Sector Office

Henry Saka, Ronald Waiswa and Jalia Kangave

October 2018

Taxing Government: The Case of the Uganda Revenue Authority's Public Sector Office
Henry Saka, Ronald Waiswa and Jalia Kangave
ICTD Working Paper 84
First published by the Institute of Development Studies in October 2018
© Institute of Development Studies 2018
ISBN: 978-1-78118-490-5



This is an Open Access paper distributed under the terms of the Creative Commons Attribution Non Commercial 4.0 International license, which permits downloading and sharing provided the original authors and source are credited – but the work is not used for commercial purposes. <http://creativecommons.org/licenses/by-nc/4.0/legalcode>

Available from:
The International Centre for Tax and Development at the Institute of Development Studies, Brighton BN1 9RE, UK
Tel: +44 (0) 1273 606261
Email: info@ictd.ac.uk
Web: www.ictd/en/publications

IDS is a charitable company limited by guarantee and registered in England
Charity Registration Number 306371
Charitable Company Number 877338

Taxing Government: The Case of the Uganda Revenue Authority's Public Sector Office

Henry Saka, Ronald Waiswa and Jalia Kangave

Summary

Virtually all the literature on taxation presents it as a relationship between government and non-government taxpayers. And even though in practice government organisations are – or should be – big taxpayers, very few revenue authorities treat these organisations as a separate segment of taxpayers. Different categories of taxpayers behave differently and so need to be treated differently to best encourage their compliance. With this in mind, in 2014, the Uganda Revenue Authority (URA) established the Public Sector Office (PSO) as a separate office to manage the affairs of government ministries, departments and agencies. Subsequently, the duties of the office were expanded to include the management of the affairs of politically influential individuals. Within the first year of its operation, the PSO had increased revenue collections from government organisations by 194 per cent when compared to the previous year. The PSO is now the second largest contributor to domestic tax collection in Uganda, after the Large Taxpayers' Office. Its revenue share as a percentage of total domestic revenue collections grew from only 5 per cent in financial year 2014/15 to 17 per cent in 2016/17. In this paper, we examine the reasons behind establishing the public sector as a separate taxpayer segment. We also look into the factors that have enabled the success of this office. We find that the PSO's successful performance is facilitated by a number of factors including having a proficient team of revenue officials; having the support of top URA management; collaboration and coordination with other key government offices; support from high-ranking government officials; and the use of 'soft compliance' strategies such as organising taxpayer workshops, making phone calls to relevant contact persons in government organisations and sending emails with reminders of due dates for filing tax returns and paying taxes.

Keywords: public sector office; Uganda Revenue Authority; ministries; departments; agencies; taxpayers.

Henry Saka is the Commissioner for Domestic Taxes at the URA. Henry has led several reforms at the URA including the establishment of the Public Sector Office and a High Net Worth Individual Unit.

Ronald Waiswa is a supervisor in Research and Policy Analysis at URA's Research, Planning and Development Division. He also heads research and training at Lida Africa.

Jalia Kangave is a Research Fellow at the Institute of Development Studies, and Capacity Building Manager of the International Centre for Tax and Development (ICTD). She also leads the Gender and Tax programme at ICTD.

Contents

Summary	3	
Acknowledgements	5	
Acronyms	5	
Introduction	6	
1 Tax administration reform in Uganda	7	
2 The Uganda Revenue Authority's Public Sector Office	8	
2.1 The public sector as a taxpayer	8	
2.2 Structure of the PSO	10	
2.3 Functions of the PSO	11	
2.3.1 Service management	11	
2.3.2 Compliance management	11	
3 What made the URA adopt the PSO model?	12	
3.1 The need to improve the efficiency of the LTO	12	
3.2 Reducing complacency in smaller URA offices	13	
3.3 Improving the tax compliance of the public sector	14	
3.4 To monitor the flow of money from government to the private sector	14	
3.5 The public sector needed specialised, high-quality engagement and service	14	
4 Achievements of the PSO	15	
4.1 Improvements in government declarations	15	
4.2 Revenue collection performance	17	
4.3 Improved tracing of transactions between government and private sector contractors	18	
4.4 Increase in compliance by politicians and other influential individuals	19	
5 Enabling conditions for the PSO's success	19	
6 Challenges faced by the PSO	20	
7 Conclusion	21	
References	22	
Tables		
Table 1	PSO taxpayer register and staffing	11
Table 2	Domestic tax collections by stations before and after PSO	13
Table 3	Number of staff declared in monthly returns by MDAs	16
Table 4	Domestic tax collections by tax office (in billions of Uganda Shillings)	18
Figures		
Figure 1	URA taxpayer segmentation reform	8
Figure 2	Criteria for inclusion or exclusion of government entities in PSO register	9
Figure 3	Structure of the PSO	10
Figure 4	Filing PAYE returns over time	15
Figure 5	Filing withholding tax returns over time	16
Figure 6	Annual revenue growth of public sector institutions	18

Acknowledgements

We are greatly indebted to the Public Sector Office team at the Uganda Revenue Authority (particularly Monica Tumukunde, Marion Namunyolo and James Etengu) and the management of the Domestic Tax Department for the wealth of information they shared with us, which enabled the writing of this paper. We thank Mick Moore and the anonymous reviewers for their useful comments on previous versions of this paper. Lastly, we thank participants of the 2017 ICTD annual meeting in Entebbe for their feedback on an earlier version of this paper.

Acronyms

CAO	Chief Administrative Officer
HNWI	High net worth individual
IMF	International Monetary Fund
IPPS	Integrated personnel payroll system
LTD	Large Taxpayer Department
LTO	Large Taxpayers' Office
MDA	Ministries, departments and agencies
MTO	Medium Taxpayers' Office
OECD	Organisation for Economic Cooperation and Development
PAYE	Pay as you earn
PSO	Public Sector Office
PSST	Permanent Secretary and Secretary to the Treasury
STO	Small Taxpayers' Office
TADAT	Tax Administration Diagnostic Assessment Tool
TCC	Tax clearance certificate
TIN	Tax identification number
UGX	Ugandan Shilling
URA	Uganda Revenue Authority
US\$	United States Dollar
VAT	Value added tax
VIP	Very important person

Introduction

'Why does the Uganda Revenue Authority need a Public Sector Office?' This is a question that URA officials are frequently asked. The short answer to that question is that government itself is – or should be – a big taxpayer. The long answer is provided in the discussion in this paper.

Over the past three decades, African countries have undertaken various reforms in tax administration in a bid to increase revenue collection. Perhaps the most fundamental of these reforms is the establishment of semi-autonomous revenue authorities that are independent of the civil service. Previously, most revenue authorities were structured according to tax type: individual offices were assigned to collect a specific type of tax (Moore 2013). This model had a number of shortcomings including: duplication of functions; high compliance costs for taxpayers who had liability for more than one tax type; encouraging unhealthy competition between tax offices; and lack of centralised information relating to taxpayers (OECD 2010). In a number of countries, the tax-type structure was subsequently replaced by a functional structure, which consists of having different units that deal with different functions of tax administration (such as taxpayer registration, audit and investigation, legal affairs, debt collection, dispute resolution and human resource management) (Moore 2013; Gill 2003). This newer model of tax administration has various advantages, including improving professionalism in revenue authorities by promoting specialisation; having a unified system of tax registration; more centralised access to taxpayer information; and enabling tax authorities to more effectively manage audits and debt collection (Terkper 1995; OECD 2010).

In various revenue authorities, the functional model is complemented with taxpayer segmentation (OECD 2010; Moore 2013). Taxpayer segmentation recognises the fact that different categories of taxpayers have different characteristics and behave differently. Each may be treated differently to best encourage compliance. The most common type of segmentation is by size: taxpayers are divided, for example, into large, medium and small taxpayers (Baum, Gupta, Kimani and Tapsoba 2017). More recently, a few revenue authorities in African countries such as Uganda, South Africa and Mauritius have added a new segment of taxpayers referred to as 'high net worth individuals' (HNWIs) (Kangave Nakato, Waiswa, Nalukwago, and Lumala Zzimbe 2018).

While government organisations have an obligation to pay taxes, most revenue authorities do not treat these organisations as a separate segment of taxpayers. Instead, the tax affairs of these government organisations are managed in the three 'traditional' taxpayer segments (small, medium and large). Similarly, virtually all the literature on taxation presents it as a relationship between government and non-government taxpayers. Yet in reality, there is a large intra-government dimension of taxation. In recognition of the importance of the government as a taxpayer, the Uganda Revenue Authority (URA) set up a separate office – the Public Sector Office (PSO) – to manage the tax affairs of government ministries, departments and agencies (MDAs). Since its establishment in 2014 the PSO has registered significant success. In the financial year 2015/2016, revenue collected by the PSO grew by 194 per cent over the previous year. In 2016/17, it increased by 106 per cent. The PSO is now the second largest contributor to domestic tax collection in Uganda, after the Large Taxpayers' Office (LTO). Its revenue share as a percentage of total domestic revenue collections grew from only 5 per cent in the financial year 2014/15 to 17 per cent in 2016/17.

In this paper, we examine the question: to what extent does the URA's PSO present a convincing case for having a separate segment for managing the taxation of public sector entities? Given that there are not many such specific offices for managing the taxation of government entities, there is hardly any published literature on these offices. This paper aims

to fill that gap. In the course of our research, we found out that Nigeria's Federal Inland Revenue Service (FIRS) has a similar office, referred to as the Government Business Tax Department. The department was established in 2012 to handle the tax affairs of government MDAs, agencies, states and local government councils (Federal Inland Revenue Services 2013a; Federal Inland Revenue Services 2013b). It is headed by a director and has a total of 37 offices, covering all the states in the country and the Federal Capital Territory. Its responsibilities include assessment and collection of taxes, compiling databases of government organisations and managing the tax debts that they owe. While the Government Business Tax Department started its operations in early 2013, we are not aware of any published study on its impact or effectiveness. It seems even more appropriate, therefore, to have a discussion on the impact of the URA's PSO in the hope that other revenue authorities can learn from its experience.

The paper is divided into eight parts, with this being the introduction. Part 1 provides a brief background on tax administration reforms in the URA. This is followed by a discussion in Part 2 of the structure of the URA's PSO, including the URA's definition of the public sector. Part 3 contains a discussion of the reasons why the URA established the PSO. In Part 4, we highlight the achievements of the PSO. Part 5 discusses some of the conditions that enabled the PSO to achieve this success. In Part 6, we highlight the challenges faced by the PSO. We conclude in Part 7.

1 Tax administration reform in Uganda

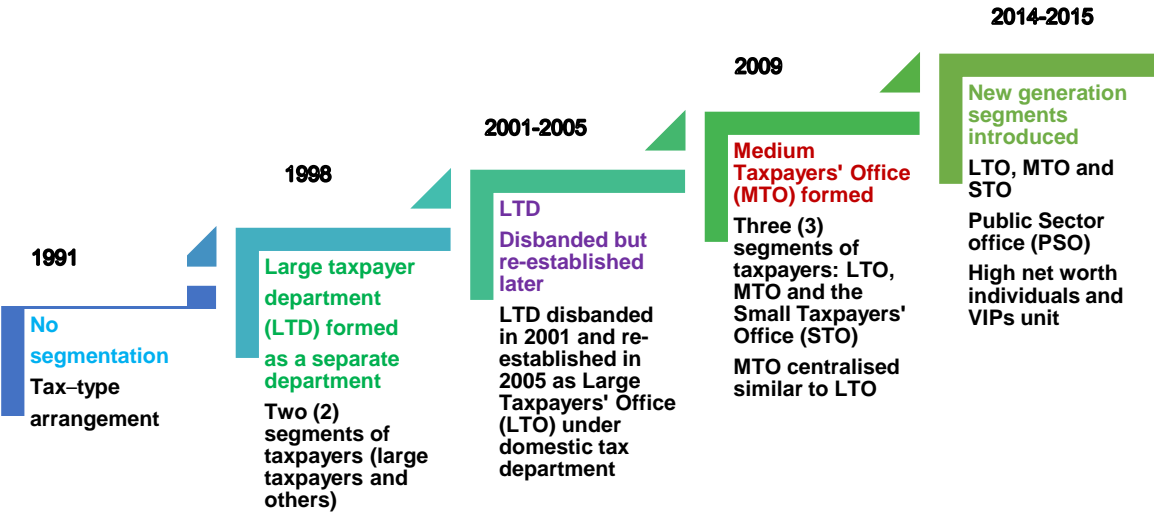
Before the establishment of the URA, central government taxes were collected by the Ministry of Finance. In September 1991, the URA was established as a semi-autonomous revenue authority. The government hoped to achieve two main objectives when it established the URA (Kangave 2005). First, it was hoped that, by removing tax collection from the Ministry of Finance, the newly established revenue authority would operate with limited political interference. Second, by being removed from the civil service, the URA would be able to offer better remuneration and thereby attract and retain competent staff. These reforms, along with the introduction of value added tax (VAT) in 1996 and the enactment of a new income tax law in 1997, registered initial success. The ratio of tax collections to Gross Domestic Product (GDP) increased from 7 per cent in 1991 to 10 per cent in 1997.

From its inception, the URA regularly adjusted its organisational structure to meet changing demands. In the early to mid-1990s, the URA was structured along predominantly tax-type lines such as the Income Tax Department, Excise Department, VAT Department and Customs Department. Following an International Monetary Fund (IMF) review, a Large Taxpayer Department (LTD) was established in late 1998 (Kuteesa, Tumusiime Mutebile, Whitworth and Williamson 2010). This resulted in the creation of two broad categories of taxpayers: large taxpayers and others. The LTD was an instant success in terms of revenue collection. In 1999/2000, it contributed approximately 74 per cent of the domestic tax revenue collections. However, it was not popular with large taxpayers, who complained that they were being harassed; a factor that contributed to its closure in 2001 (Kuteesa *et al.* 2010). Several structural changes were made in the period between 2000 and 2004, culminating in the establishment of a Department of Direct Taxes, a Department of Indirect Taxes and an Expansion and Collection Department. The LTD that was closed in 2001 was subsumed into the Direct and Indirect Tax Departments (Baum *et al.* 2017). It was reopened in 2005 as a division in the Domestic Tax Department and called the Large Taxpayers' Office (LTO) (Kuteesa *et al.* 2010).

In 2004, the URA underwent a major restructuring exercise which resulted in moving away from a tax-type organisational structure to a function-based structure, which was

complemented with taxpayer segmentation (Kangave 2005). Six departments were created: Domestic Taxes Department, Customs and Excise Department, Board and Legal Affairs Department, Commissioner General’s Office, Corporate Services Department and the Internal Audit, Tax Investigation and Internal Affairs Department. The Domestic Taxes Department and the Customs and Excise Department were the two core departments in charge of operations. The Domestic Taxes Department was responsible for the registration, auditing, assessment, collection and accounting of domestic taxes. By 2009, there were three categories of taxpayers: large, medium and small. Later, in September 2014, the URA established a specialised office to deal with the public sector. This Public Sector Office has three main segments of taxpayers: government organisations, HNWI¹ and very important persons (VIPs).²

Figure 1 URA taxpayer segmentation reform



2 The URA’s Public Sector Office

In this part, we define what is meant by the public sector for the URA’s purposes, document the structure of the PSO, and explain its functions.

2.1 The public sector as a taxpayer

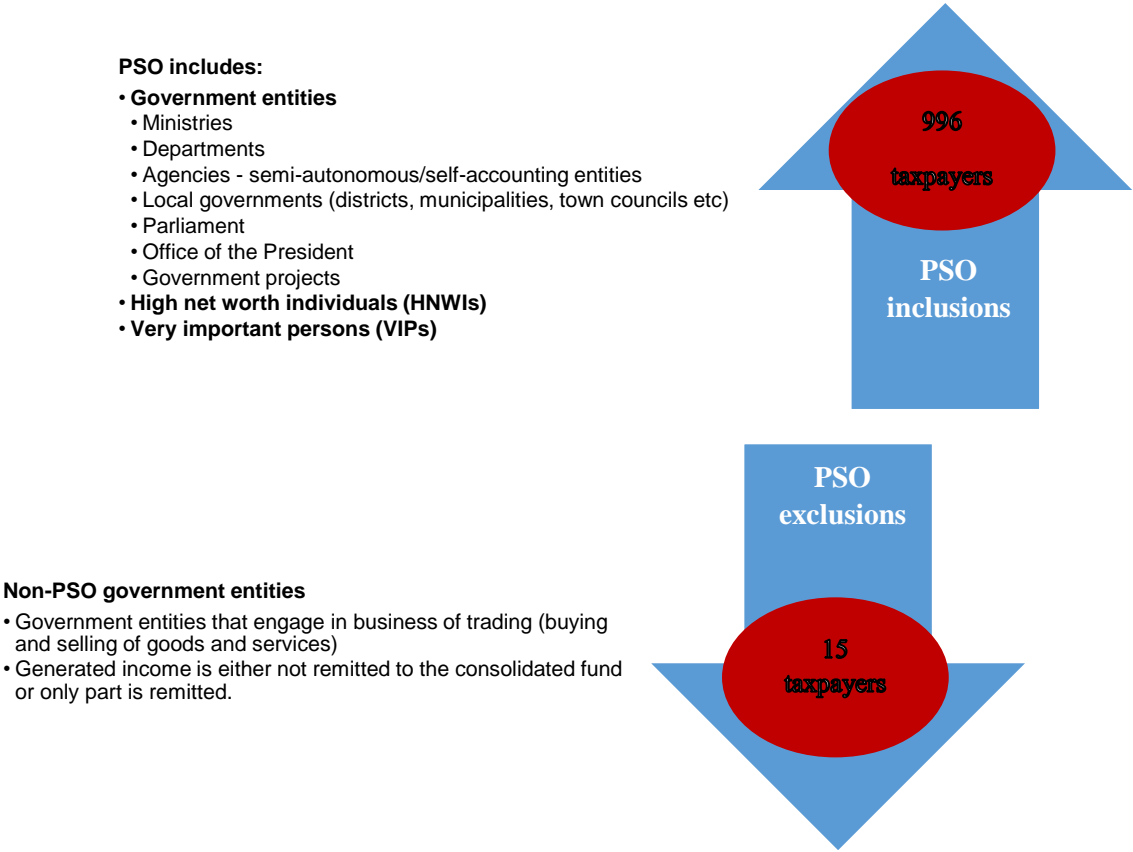
The public sector, as defined by the URA, includes all entities that constitute the three arms of government, namely the executive, legislature and judiciary. This includes the office of the president (not to be confused with the person of the president), the parliament, central government ministries and local government units. Where executive authority is delegated by law to semi-autonomous entities (such as the URA, the Electricity Regulatory Authority and the Petroleum Authority of Uganda), the URA treats these as part of the public sector. Specific exceptions are made where entities operate in a manner similar to private business entities, for example, buying and selling goods or services or letting/leasing property.

¹ See Kangave *et al.* 2018 for criteria defining a HNWI.
² VIPs consist of top government officials (such as the president, vice president, cabinet ministers, speaker of parliament, high-ranking judicial officers and heads of political parties and parliamentary committees) and influential figures (such as kingdom heads, heads of professional associations, religious leaders, influential journalists and heads of business associations).

Examples of such entities are the National Social Security Fund and the Uganda Wildlife Authority. In these cases, the incomes earned are usually either partially remitted to the Uganda Consolidated Fund³ or are not remitted at all. These exceptions are treated in the same manner as the URA would treat any other taxpayer. This rule also applies to limited companies owned by the government.

By design, and to the extent that any revenues of the public entities are remitted to the Uganda Consolidated Fund, the entities are not subject to income tax.⁴ As such, their tax compliance relates primarily to the declaration and remission of withheld income taxes (pay as you earn (PAYE) for their employees, and tax withheld on supplies made to government by private business). For VAT, a withholding mechanism was in operation until 2006 when it was formally abolished. Some government entities have continued to practise withholding, although it is contrary to government standing orders. If public sector entities enter into taxable transactions of a commercial nature – for example, when local governments rent out commercial markets – the transactions are subject to VAT. The public sector entities are therefore required to register as VAT taxpayers. In a few cases, such as the National Social Security Fund, public sector units are also subject to corporation tax. They are treated as normal businesses for tax purposes and are subjected to the standard segmentation rules.

Figure 2 Criteria for inclusion or exclusion of government entities in PSO register



³ The Uganda Consolidated Fund is the government account where all government revenues and funds are paid. It is also the account from which money is withdrawn to fund all government activities.

⁴ Our analysis of records shared with us by the Ministry of Finance revealed that between 2015 and 2018, only one entity – the Uganda Communications Commission – made contributions to the Uganda Consolidated Fund. On average, the contribution in this three-year period was about 1.2 per cent of the approved government budget.

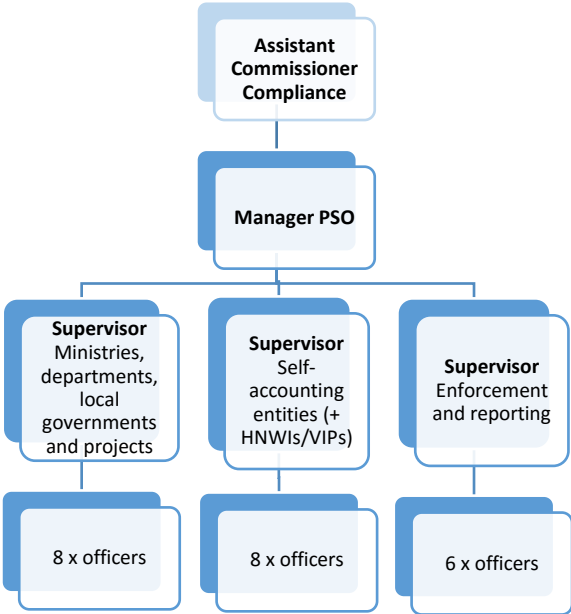
As at January 2018, the PSO managed a total of 996 taxpayers. 661 of these are government entities, while the remaining 335 are HNWI and VIPs. Only 15 government entities are not managed by the PSO.

Prior to the establishment of the PSO, public sector taxpayers were placed into two categories for tax management purposes. Government ministries, departments and agencies were managed by the LTO while the tax affairs of local government agencies were handled by the URA’s local offices in the geographical locations in which they were based. For example, the municipal council of Jinja town would be managed by the Jinja local tax office.

2.2 Structure of the PSO

The PSO is headed by a Manager, who reports to the Assistant Commissioner of Compliance in the Domestic Taxes Department. The office comprises three sub-divisions, covering: (a) ministries, departments, local governments and projects; (b) self-accounting entities (such as the URA), VIPs and HNWI; and (c) enforcement and reporting. The enforcement and reporting division is responsible for arrears management, receipting payments that come through the Bank of Uganda, consolidating reports from the other sub-divisions and performing the PSO’s general administration roles. The other two sub-divisions serve as client relationship managers, following up with normal flows of tax payments and filing, and educating taxpayers on their tax obligations.

Figure 3 Structure of the PSO



The PSO started operations in September 2014 as a pilot project with only seven staff members (a manager, a supervisor, and five officers) managing 379 public sector taxpayers (ministries, departments and district local governments). Between September 2014 and June 2015, the PSO collected UGX (Ugandan Shillings) 216 billion (approximately US\$ 77 million),⁵ surpassing the revenue target of UGX 142 billion (approximately US\$ 50 million) that the URA management had set for it. The results of the pilot were so impressive that the URA management decided to increase both the capacity and scope of the PSO. In July 2015, VIPs, public authorities and commissions were added to the register and the staff

⁵ Using a bank of Uganda exchange rate of US\$ 1 = UGX 2,823.22 for FY2014/15. This rate is used for all the conversions in this paper.

numbers were increased to 17.⁶ In July 2016, public universities, technical and vocational institutions, referral hospitals, national parks and self-accounting entities were also shifted to the PSO. Lastly, in January 2017, HNWI were moved from the LTO and added to the PSO register. This last move was considered necessary because the URA observed that a number of individuals on the HNWI register were also VIPs. Of the original 117 HNWI identified, for example, 21 per cent were VIPs and 11 per cent were former VIPs (Kangave *et al.* 2018). The URA also noticed that there were other similarities and overlaps between VIPs and HNWI: both groups tend to be politically and economically influential, and have busy lifestyles. The skills required to interact with them and manage their affairs are thus quite similar. The addition of HNWI to the PSO register brought the total number of taxpayers in the office to 981. Staff members were also increased to 26 as shown in Table 1.

Table 1 PSO taxpayer register and staffing

Taxpayer category	2014/2015	2015/2016	2016/2017
Taxpayer register	381	666	981
No. of PSO staff	7	17	26
Staff to taxpayer ratio	1:55	1:39	1:38

Source: URA databases

2.3 Functions of the PSO

The PSO has two core functions: service management (which includes taxpayer registration and education) and compliance management (review and enforcement of compliance). The two functions are in practice largely interwoven but we handle them separately here for discussion purposes.

2.3.1 Service management

The core activity of the PSO so far has been to establish and maintain an up-to-date register of public entities. Extensive cleaning of the existing register was undertaken, particularly as it relates to government projects and local government entities. Alongside the cleaning and expansion of this register was the need to strengthen taxpayer education. The PSO actively participates in government activities and meetings of various kinds to ensure that tax is consistently on the agenda of government agencies. PSO officials educate taxpayers on an ongoing basis by listening to and addressing their concerns, assisting with online compliance procedures and providing advice on taxpayer obligations. For VIPs and HNWI, functions that are ordinarily carried out within URA premises are sometimes conducted on a client’s premises. Due to the nature of the taxpayers, senior management will often get involved in interactions with taxpayers.⁷

2.3.2 Compliance management

To a great extent, the PSO employs a soft approach to improving compliance, with the emphasis being placed on taxpayer education and increasing the ease of complying. Enforcement is usually limited to cases where audits have been carried out. Recovery methods emphasise engagement and high professionalism.

The compliance management function examines compliance history and trends and takes corrective action through audit, management of arrears and enforcing collections. Key roles under compliance management include:

⁶ This includes 12 technical staff members and five support staff.
⁷ For more details on the URA’s treatment of HNWI and VIPs, see Kangave *et al.* 2018.

- Tracking government appropriations and fund releases to provide information to other tax offices when their clients have been paid by government. It also informs the Treasury Department when there are inconsistencies between the amounts filed in the tax returns and the funds that were released to the government entities.
- Examining contracts between business entities and government organisations, including keeping track of their implementation.
- Examining policies and laws and advising the Business Policy Division of the URA on possible changes.

3 What made the URA adopt the PSO model?

While there is no question about the formal legality of taxing the public sector, this is not always accepted in practice. And some public sector units have sufficient authority to resist. The public sector poses significant tax risks and leakages that need to be addressed through deliberate strategies. The URA chose to manage the public sector separately for the following combination of reasons.

3.1 The need to improve the efficiency of the LTO

Various assessments and external technical assistance missions had identified a number of inefficiencies in the LTO. For example, in 2014 and 2015, IMF missions identified high levels of non-compliance among large taxpayers. They found that of the 726 taxpayers on the LTO register, about half were making little or no revenue contributions, and less than 10 per cent of the taxpayers on the register contributed the bulk of the revenue collected by the LTO. The IMF recommended a review of the segmentation of taxpayers in the LTO and the Medium Taxpayers Office (MTO) to establish whether the criteria for allocating taxpayers between them should be adjusted. Similarly, the first Tax Administration Diagnostic Assessment Tool (TADAT)⁸ assessment carried out on the URA in 2015 identified a number of weaknesses in tax administration, including inaccuracies in taxpayer registration details and poorly structured mechanisms to identify, assess and prioritise risks. These findings and other internal URA assessments attributed the shortcomings in part to the lack of sufficient resources in the LTO and called for an increase in its technical personnel.

With no funds to hire additional staff in the short term, the URA management studied options to reduce the administrative burden on existing staff and to further specialise the operations of the LTO (interview with the management of Domestic Taxes Department). The LTO handles large taxpayers (companies) who by their definition have complex business and tax arrangements, and hence it requires specialised skills that were in short supply. As of July 2014, the LTO managed 722 taxpayers. Close to 30 per cent of these were either government organisations or were not large enough to be categorised as large taxpayers. Specifically, there were around 53 government organisations, constituting approximately 7 per cent of the LTO population (URA databases for 2014). The nature and operations of these public organisations were very different from private sector businesses. Handling the tax affairs of the public sector entities required different tax administration skill sets such as knowledge of public sector management/accounting and an ability to negotiate with public officials. It was perceived that a focus on both extremes – private businesses engaged in complex tax planning on the one hand and the much less complex but severely non-

⁸ The Tax Administration Diagnostic Assessment Tool (TADAT) is a tool developed by a number of international organisations (led by the International Monetary Fund) to assess the health of key components of a country's tax administration system. It focusses on nine performance indicators: accountability and transparency, integrity of the registered taxpayer base, risk management, supporting voluntary compliance, timely filing of declarations, timely payment of taxes, accuracy of declarations, effectiveness of dispute resolution and efficient revenue management. See <http://www.tadat.org/>

compliant public sector on the other hand – was stretching the resources of the LTO. The public sector entities were also skewing the performance of the LTO, making realistic analysis and design of compliance interventions difficult (URA internal report, undated). By June 2014, although all other taxpayers had migrated to the more efficient eTAX electronic system for tax declaration and payment, most payments of tax by the government were reflected through an older electronic cash book. Continuing use of the older system was causing significant revenue reconciliation challenges within the LTO.

3.2 Reducing complacency in smaller URA offices

URA management observed that a number of smaller URA field offices relied heavily on a relatively small number of public sector taxpayers to meet their revenue targets. Consequently, these offices did not put much effort into registering or collecting taxes from small taxpayers. It was perceived that removing the public sector entities from these jurisdictions would shift the focus to business taxpayers, particularly for purposes of expanding the taxpayer register. Initially, when public sector entities were removed from the control of the Small Taxpayer Offices (STOs), revenue collections dropped by 17 per cent in upcountry STOs in the financial year 2014/15 and by another 18 per cent in 2015/16. However, in 2016/17 their collections increased by 27 per cent. Interestingly, one of these upcountry stations (Pallisa) virtually collapsed after the removal of public sector taxpayers from its register. In 2014/15, following the removal, it collected only UGX 100,000 (approximately US\$ 35). URA management later made the decision to close it. Similarly, even the Kampala-based STOs registered a slump in their collections in 2015/16, followed by a recovery in the next year (Table 2).

Table 2 Domestic tax collections by stations before and after the opening of the PSO

Station	DT collections (UGX billions)				Growth rate (%)		
	FY2013/14	FY2014/15	FY2015/16	FY2016/17	FY2014/15	FY2015/16	FY2016/17
Kampala STOs	475	619	583	701	30%	-6%	20%
Upcountry STOs	264	220	180	228	-17%	-18%	27%
LTO	3,198	3,187	4,428	4,330	-0.4%	39%	-2%
PSO		216	628	1,291		194%	106%
MTO	467	494	776	929	6%	57%	20%
Grand total	4,404	4,736	6,595	7,479	8%	39%	13%

Source: Authors' computations based on URA payments databases.

3.3 Improving the tax compliance of the public sector

By 2014, URA management had observed that the public sector posed a range of unique challenges to tax administration. Tax payments by government organisations were driven by the frequency, or lack thereof, of government expenditure releases by the Treasury Department, rather than by the requirements of tax legislation. The likelihood of success of traditional enforcement measures was perceived to be low and the likelihood of resistance by the managers of these organisations was high. This created an incentive for accounting officers in these entities to ignore their tax obligations or to misuse the money earmarked for taxes by reallocating it to other unfunded needs. When tax arrears mounted, the government would simply waive the liabilities.

There were likely two main reasons for low compliance rates in the public sector: the knowledge that the URA found it difficult to enforce the law; and, in some cases, ignorance or uncertainty about tax obligations. Some public sector units perceived tax as the role of the URA and believed that the URA should recruit officers to file tax returns on their behalf (interview with PSO team).

Many entities were either not filing their tax returns at all or were filing and paying late. The public sector (as defined in Part 2 above) and the education sector (government schools, universities and technical institutions) were ranked the least compliant sectors for PAYE in a

2014 study conducted by the URA (URA report 2014). By October 2014, only 39 per cent of the PAYE returns of these public sector entities were filed on time. For tax withheld on business-to-government transactions, the on-time filing rate was 36 per cent (eTAX data). The few entities that were declaring tended to make significant errors in their declarations (PSO performance report 2016). Similarly, many senior government employees received benefits in kind which went largely untaxed. For example, contrary to the law, government vehicles used by these officials were considered tax free.

By June 2014 the government had accumulated tax arrears of UGX 598 billion (approximately US\$ 212 million). In the same year the URA had a record collection shortfall of just over UGX 400 billion (US\$ 141 million), a significant portion of which was attributed to non-compliance by government entities. The response was for government to waive most of the tax outstanding from the public sector. URA management was, therefore, looking for a way to make government bodies more compliant in the future.

3.4 To monitor the flow of money from government to the private sector

The URA's limited access to the government accounting and payments system (Integrated Financial Management System – IFMS) made it difficult to track transactions made between government and the private sector. This, compounded with the lack of other third party data sources (such as bank account information) was identified as a major weakness in tax administration. Considering that government is perhaps the biggest consumer of goods and services in the economy, understanding how it was spending its money would be essential to designing efforts to improve tax compliance. Similarly, the partial failure to collect taxes from businesses with government contracts was routinely raised by internal and external URA auditors (interview with the management of the Domestic Taxes Department).

Upon investigating into why there were huge tax arrears relating to government transactions, the URA found that a significant number of large and medium businesses who supplied goods and services to government were failing to pay taxes because they had not been paid by the government. This was especially the case with VAT, because the liability for tax arose as soon as the supply was made or an invoice was issued, and yet the government would take months, or even years, to pay the supplier. Sometimes, large taxpayers borrowed money to pay tax because the government had not yet paid them and yet interest was accruing on their tax arrears. Establishing a PSO would help URA management to create awareness of this problem by regularly highlighting it.

3.5 The public sector needed specialised, high-quality engagement and service

The tougher enforcement methods that the URA might occasionally use against private sector tax defaulters, such as seizures of assets or freezing bank accounts,⁹ are almost unusable against public sector defaulters. In the few instances in which the URA attempted to employ these measures, they were largely ineffective (interview with the management of the Domestic Tax Department). It was decided that the most feasible way to improve the compliance of public sector entities was to customise URA services to address their problems and expectations, win their trust, and thus be in a position to influence their behaviour as taxpayers.

⁹ Most government entities hold bank accounts at the Bank of Uganda, which is the central bank.

4 Achievements of the PSO

The establishment of the PSO has resulted in:

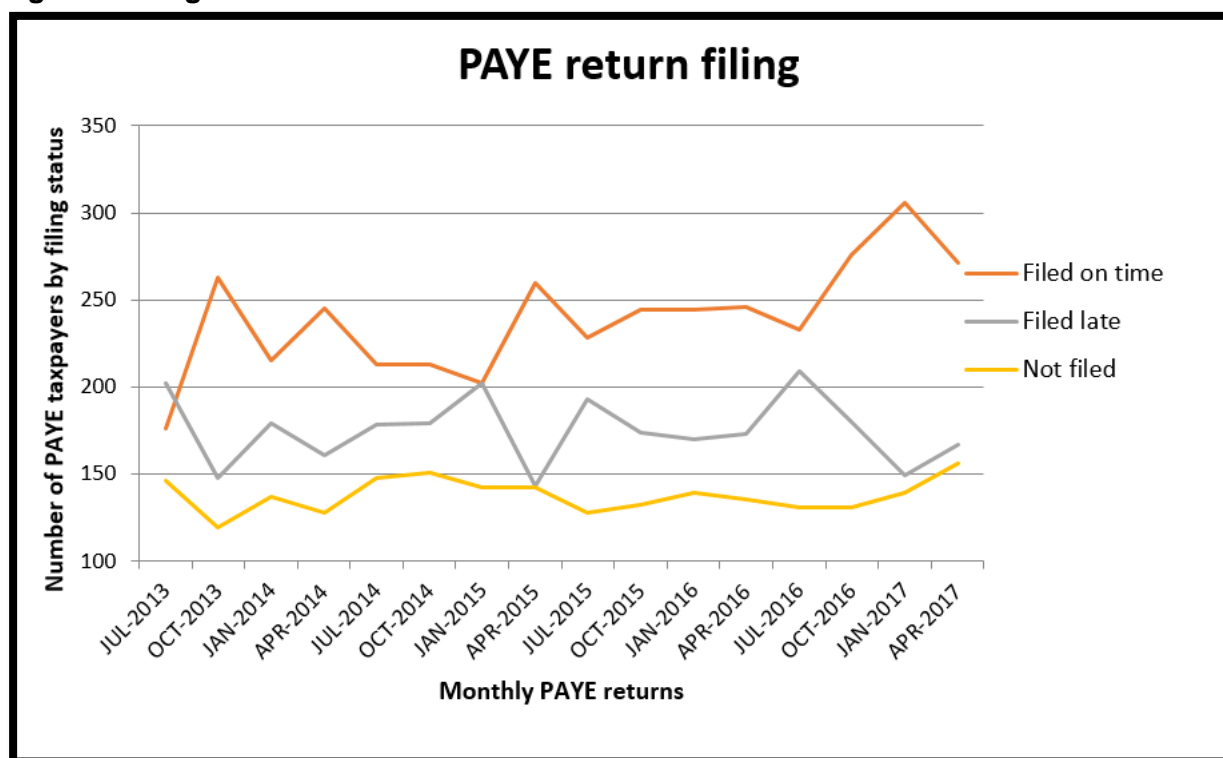
- Improvements in the quality and timing of tax returns filed by the public sector.
- Increased tax collections from the public sector.
- The installation of a system for tracing economic transactions between government and the private sector.
- Improved tax compliance on the part of influential people: politicians and those who are politically well connected.

We discuss each of these achievements below.

4.1 Improvements in government declarations

Following the establishment of the PSO and efforts to sensitise public entities about their tax obligations, there was an increase in the number of returns filed and the number of government employees declared in monthly tax returns (Figure 4 and Table 3).

Figure 4 Filing PAYE returns over time



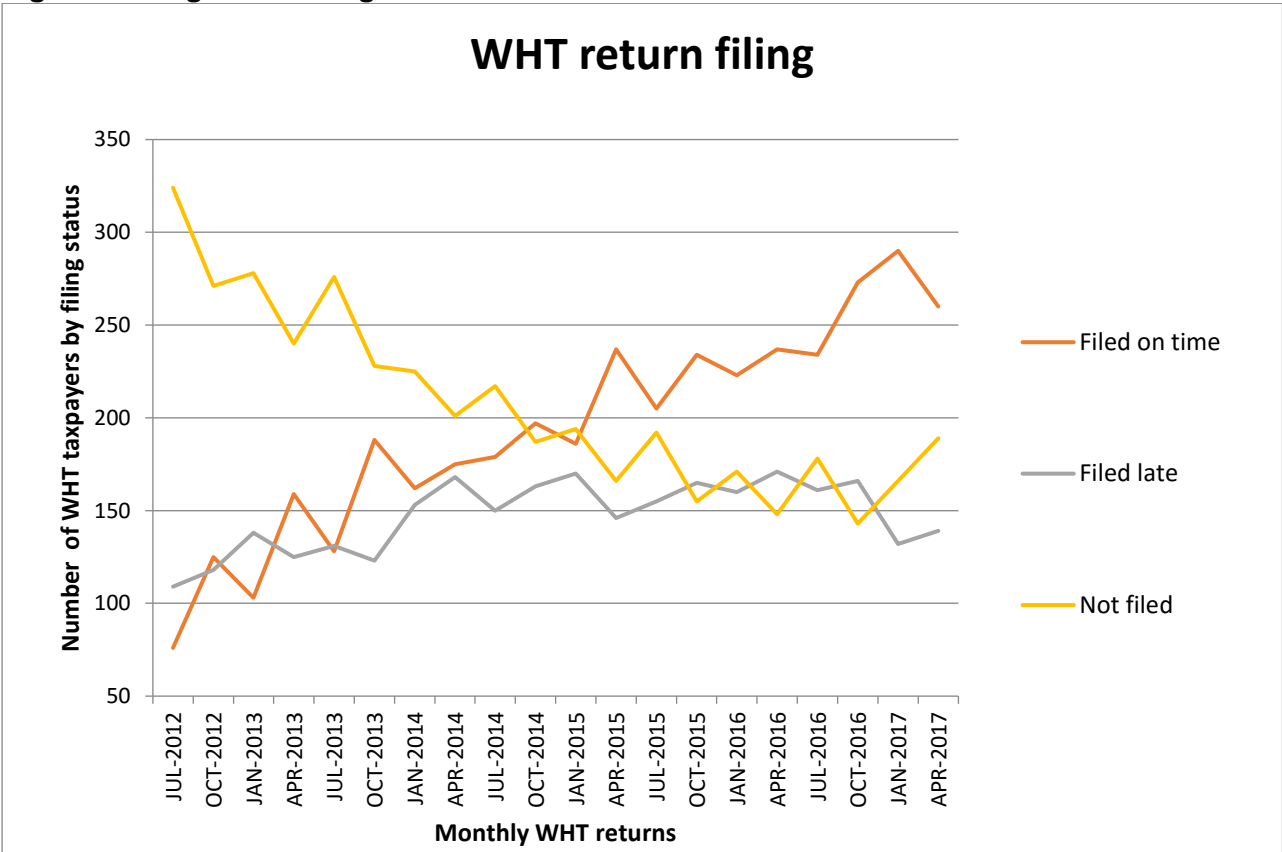
Source: URA databases

Table 3 Number of staff declared in monthly returns by ministries, departments and agencies

Financial year	Average no. of employees included in a monthly return	Growth rate
2015/16	31,359	45.86%
2014/15	21,499	34.50%
2013/14	15,984	103.05%
2012/13	7,872	69.14%
2011/12	4,654	

Despite these improvements, however, the number of late filers has remained much the same, and in 2017 there was even a small increase in the number of non-filers (Figures 4 and 5). There are two explanations for this shortcoming. One is that the PSO has a limited budget for its outreach activities, and had to suspend them entirely for a period in late 2015/early 2016. The other is that some of the staff of the government organisations who have been trained by the PSO team have been transferred elsewhere, creating a need for training new staff on how to handle tax obligations (interviews with PSO team).¹⁰

Figure 5 Filing withholding tax returns over time



Source: URA databases

There has been a significant improvement in the quality of returns that are filed. Shortly after establishing the PSO, the number of quality returns grew by 1,023 per cent by the end of 2015. In 2016, the quality returns submitted further increased by 56 per cent, and by 24 per cent in 2017 (PSO report 2017). According to the PSO, a 'quality return' is one where the taxpayer indicates the correct number of employees and suppliers in the PAYE and

¹⁰ This invariably suggests a lack of effective handover mechanisms in the government departments, which can be used to avoid business disruption.

withholding tax returns respectively; populates the tax identification numbers (TINs) of all employees and suppliers; assigns the correct TINs to the right owners; and also makes accurate revenue declarations (PSO report 2017, and interview with PSO staff).¹¹ To assess the quality of PAYE returns, for example, the PSO officials check whether the information submitted is consistent with that contained in the integrated personnel payroll system (IPPS). They also use URA systems such as eTAX and the data warehouse eHUB, which highlight inconsistencies in information that has been submitted.

The accuracy of returns was often compromised by a number of factors: (1) inability of government accounting officers to adequately glean data from the IPPS; (2) failure to convert this data into an Excel format that can be copied and pasted in the tax return form; and (3) an overall limited concern by government staff for the quality and consistency of their tax returns. The PSO team conducts training for government accounting officers on how to use the IPPS and how to file tax returns, and continuously sends filing reminders through phone calls, messages, emails and letters.

4.2 Revenue collection performance

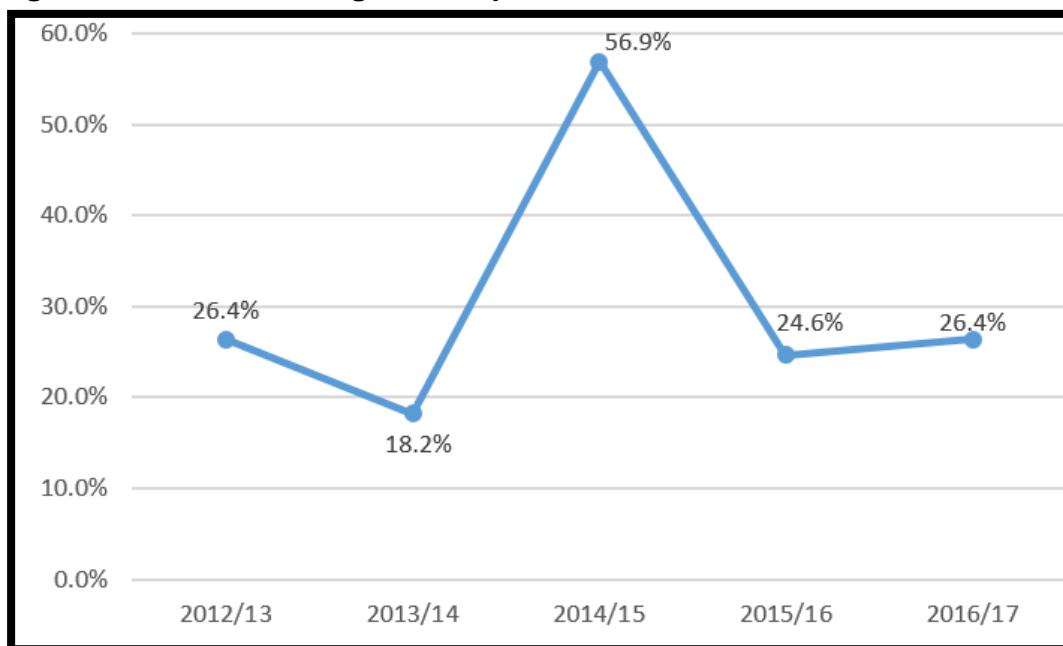
Since 2005, the URA has run an annual taxpayer appreciation day (TPAD) where it recognises the most compliant taxpayers. In the financial year 2016/2017, eight taxpayers were given awards. Of these, five were PSO clients: district local governments. This was the first time that local governments had received this award (TPAD analysis report 2016/17). Let us look at the statistics behind this.

As we have already noted, before the PSO was established, there were a number of public sector organisations that were not paying taxes. For example, internal URA records indicate that, in the financial years 2012/2013 and 2013/2014, there were 17 government organisations that did not remit any taxes. With the establishment of the PSO, these organisations started paying taxes.

Our research also reveals that even among those government organisations that were paying taxes, there were huge under-declarations. Some were paying as little as UGX 5,000 (approximately US\$ 1.77) per year. Shortly after the PSO was established, revenue contributions from public organisations shot up tremendously as evidenced in Figure 6 below.

¹¹ For example, previously, some income would be treated as exempt when it was in fact taxable.

Figure 6 Annual revenue growth of public sector institutions



Source: URA databases

The PSO is now the second largest contributor to domestic tax collection in Uganda after the LTO. It contributed 5 per cent of domestic revenue collection in 2014/15, a figure that had increased to 17 per cent by 2016/17 (Table 4).

Table 4 Domestic tax collections by tax office (in billions of Uganda Shillings)

Segments	% of domestic tax share		
	2014/15	2015/16	2016/17
LTO	67%	67%	58%
PSO	5%	10%	17%
MTO	10%	12%	12%
STO	18%	12%	12%
Total domestic tax share	100%	100%	100%

Source: URA revenue performance reports for 2014/15, 2015/16 and 2016/17.

The PSO has consistently surpassed the revenue targets set for it. As one top URA official stated: 'PSO is actually given a stretched target. We have kept increasing their targets but still they surpass them. The revenue collected from these entities is a big surprise to us.' (Interview with management of Domestic Taxes Department.)

4.3 Improved tracing of transactions between government and private sector contractors

Government entities are now required to submit a list of all their service providers to the URA. This information contains the identification details of the suppliers, the amount of money disbursed and the withholding tax deducted, if any. The information is then processed by the PSO team and shared with the URA compliance office, who verify whether the taxpayers have declared these amounts in their tax returns and take action if there are inconsistencies. While we do not have data on the impact of this information sharing on revenue collections in other URA offices, it is safe to assume that it has been positive. The efficiency of this tracing process has been increased with the introduction of the electronic

tax clearance certificate (TCC). For a long time, there was a requirement that any person who was going to supply goods or services to government should have a TCC, which would indicate that they are tax compliant. However, because the TCC system was manual, it was difficult to verify its authenticity. The electronic TCCs are now emailed to both the suppliers and the government purchasing organisations. The PSO team sensitises the latter on how to verify the authenticity of TCCs online. There are some benefits to the suppliers: faster clearance means they are paid more promptly. Finally, the URA can now access information from government about all those who bid for government tenders but end up being unsuccessful. This has helped enrich the URA's taxpayer register.

4.4 Increase in compliance by politicians and other influential individuals

In many African countries, one of the most difficult groups to tax is politicians and politically connected individuals (McCluskey 2016). A study that was conducted in 2016 on HNWI's in Uganda found that politicians constituted a significant percentage of the wealthy individuals in the country (Kangave, Nakato, Waiswa and Lumala Zzimbe 2016). An analysis of the tax compliance of 71 top government officials over the period 2011/2012 to 2013/2014 found that although all of these individuals had stakes in commercial enterprises, the majority were not paying personal income taxes. Neither were the companies that they were associated with complying with their tax obligations. Since the opening of the VIP unit in the PSO, compliance by this group of individuals has significantly improved. For the financial year 2015/2016, for example, 65 per cent of VIPs on the URA's register were filing returns (Kangave *et al.* 2018).

5 Enabling conditions for the PSO's success

A combination of factors have enabled the success of the PSO:

- a) Strong support for the PSO's activities within the URA: in addition to having a PSO team that is proficient and dedicated, there has been strong institutional support for the work of the PSO. In particular, URA senior management has been actively involved in the activities of the PSO, with leaders such as the Commissioner General and the Commissioner for Domestic Taxes being part of the meetings that the PSO team holds with taxpayers. Similarly, the management team of the Domestic Taxes Department participates in some of the taxpayer sensitisation activities. Lastly, there is good collaboration and coordination of activities between the PSO and other URA departments.
- b) Successful coordination and collaboration with key government agencies: the PSO is able to access budget execution data at an early stage, thereby enabling it to determine what tax liability different government organisations are likely to have. When the government releases funds to different agencies, the Permanent Secretary and Secretary to the Treasury (PSST) notifies the PSO. Once payments have been made to these agencies, the Bank of Uganda issues a statement to the PSO for analysis. If there are any inconsistencies between the funds that were released and the amounts that are subsequently declared in tax returns, the PSO notifies the Treasury Department of these inconsistencies.
- c) Related to the above is the support and cooperation that the PSO has received from high-ranking government officials, particularly the PSST and the Commissioner of Local Government Administration. The PSST, for example, issues circulars to different ministries, departments and agencies requiring them to comply with their tax obligations. Organisations that fail to comply risk missing government budget

releases on time. Similarly, the Commissioner of Local Government Administration started issuing an updated list of district Chief Administrative Officers (CAOs) to the URA. Where the PSO experiences difficulties in dealing with a particular CAO, the Commissioner intervenes. For example, there was an instance when one CAO refused for his staff to go for a PSO training session unless the URA paid them a per diem. The PSO engaged the Commissioner, who wrote the message below to the CAO:

'Please refer to forwarded email message from URA. I have also tried to call you over the same, but you are not picking. It is indicated that your office is not willing to send Officers for the training organized by URA in Mpigi unless URA shall pay them subsistence allowances in spite of the failure by your district to complete and submit the tax returns.

I wish to advise that you find means of sending the affected Officers to participate in the training which definitely they need instead of insisting on the issue of allowances. Please cooperate and I do not need to remind you of the repercussions of failing to do so.'

- d) Use of 'soft compliance' strategies: in addition to the taxpayer sensitisation exercises that are undertaken by the PSO on an ongoing basis, the PSO team employs alternative compliance mechanisms such as following up with contact persons in government organisations through short message service (SMS), emails, phone calls, physical visits and slots during workshops. The use of these soft approaches have proven to be quite instrumental in improving compliance.

6 Challenges faced by the PSO

Despite the success registered by the PSO, it still faces various challenges.

- Limited human resources: the ratio of staff to taxpayers in the PSO is 1:37. While this seems more than acceptable by normal URA standards (as the staff to taxpayer ratio in the whole organisation was 1:373 in 2015/2016) it is still relatively low for an office that deals with large taxpayers such as government organisations (Kangave *et al.* 2018). By comparison, the LTO has a staff to taxpayer ratio of 1:8. The staff shortage in the PSO is exacerbated by the fact that some of the staff members lack public sector accounting skills. Their ability to operate is also constrained by lack of sufficient resources (such as laptops and vehicles), which are essential for upcountry field visits.
- Sensitisation workshops for staff of other government agencies: the practice in most government agencies in Uganda is to give officials a per diem (daily allowance) to attend workshops. The URA does not do this. Consequently, attendance at some of the sensitisation workshops is very low.
- For local governments and town councils that are located in rural areas, compliance is undermined by poor internet connections.

7 Conclusion

Reforms in tax administration normally focus on increasing compliance among taxpayers in the private sector. Yet there is a significant component of intra-government transactions and transactions between government and the private sector that are – or should be – subject to tax. The compliance behaviour of government organisations is often quite different from that of private sector taxpayers. The URA case study demonstrates the benefits that other revenue authorities in Africa could accrue from establishing offices that are dedicated specifically to managing the tax affairs of public sector entities.

References

- Baum, A., Gupta, S., Kimani, E. and Tapsoba, S.J. (2017) *Corruption, Taxes and Compliance*, Working Paper WP/17/255, Washington, DC: International Monetary Fund
- Federal Inland Revenue Services (2013a) Government Business Tax Department: 2013 Departmental Operational Plan, unpublished
- (2013b) Operational Manual: Government Business Tax Department, unpublished
- Gill, J.B.S. (2003) *The Nuts and Bolts of Revenue Administration Reform*, Working Paper, Washington, DC: World Bank
- Kangave, J. (2005) 'Improving Tax Administration: A Case Study of the Uganda Revenue Authority', *Journal of African Law* 49.2: 145-176
- Kangave, J., Nakato, S., Waiswa, R., Nalukwago, M. and 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: Institute of Development Studies
- Kangave, J., Nakato, S., Waiswa, R. and Lumala Zzimbe, P. (2016) *Boosting Revenue Collection through Taxing High Net Worth Individuals: The Case of Uganda*, ICTD Working Paper 45, Brighton: Institute of Development Studies
- Kuteesa, F., Tumusiime Mutebile, E., Whitworth, A. and Williamson, T. (eds) (2010) *Uganda's Economic Reforms: Insider Accounts*, New York: Oxford University Press
- McCluskey, R. (2016) *African Governments Aren't Taxing the Rich: Why They Should*, The Conversation, April 3, <https://theconversation.com/african-governments-arent-taxing-the-rich-why-they-should-57162>
- Moore, M. (2013) *Obstacles to Increasing Tax Revenues in Low Income Countries*, ICTD Working Paper 15, Brighton: Institute of Development Studies
- OECD (2010) *Tax Administration in OECD and Selected Non-OECD Countries: Comparative Information Series (2010)*, Paris: OECD, <http://www.oecd.org/tax/forum-on-tax-administration/publications-and-products/comparative/CIS-2010.pdf>
- Terkper, S.E. (1995) *Ghana: Tax Administration Reforms (1985-93)*, Taxation Research Series No. 21, Cambridge, MA: Harvard Institute for International Development



International Centre for Tax and Development
at the Institute of Development Studies
Brighton BN1 9RE, UK
T: +44 (0)1273 606261
F: +44 (0)1273 621202
E: info@ictd.ac
www.ictd.ac