

---

This work is licensed under a  
Creative Commons  
Attribution – NonCommercial - NoDerivs 3.0 Licence.

To view a copy of the licence please see:  
<http://creativecommons.org/licenses/by-nc-nd/3.0/>

TAX SOURCES AND FISCAL POLICY FOR DEVELOPMENT.

Introduction:

The most urgent problem in the field of Public Finance faced by the public authorities in East Africa is the need to find additional revenue to finance ever-increasing public expenditure. The total expenditure of the East African governments has increased at a very fast rate in the post-war period. There are strong reasons to believe that this trend is likely to continue in the future. The main reasons for the strong upward trend in public expenditure in developing countries (not necessarily in their order of importance) are:

- (1) Heavy capital expenditure on development plans and the recurrent expenditure thereof.
- (2) Increasing pressure on governments to spend more on social services like health and education.
- (3) Increasing participation of the public sector in the economy.
- (4) Increase in population.
- (5) Increase in prices, wages and salaries.

Moreover, on the basis of past experience and prevailing views on the role of the public sector in the economies of underdeveloped areas, we may safely predict that the ratio of public expenditure to national income will show an upward trend. Given this situation, we are faced with the problem of devising a tax system which will be income-elastic i.e. will ensure a rising revenue from marginal increases in income, without at the same time having serious adverse effects on incentives to work, to save and to take risks. This is the long-run problem. In the short-run it is necessary to devise ways of increasing public revenue from a given national income. My research effort will, therefore, focus on the central problems of the imbalance between public revenue and public expenditure in East Africa, both in the short- and in the long-run, and the means to eliminate such imbalance. This project may further be sub-divided into three broad problems:

- (A) Future revenue requirements of the public authorities in East Africa, derived from a projection of public expenditure over the next five years, say from 1964/5 to 1968/9.
- (B) Estimates of expected revenue from existing sources on various assumptions about the future rate of growth of monetary GDP.; on appraisal of the existing as well as potential sources of revenue from the point of view of "economic efficiency"<sup>1</sup>; suggestions for improvement in the efficiency and income elasticity of the tax structure in East Africa.

1. "Economic efficiency" in this context is meant to refer to the usual economic criteria used to assess the efficiency of taxes: i.e. effect on incentives, stabilisation, equity, administrative costs.

- (C) Allocation of sources of revenue among different layers of government - local/regional/central; or local/regional/territorial/Federal.

(A) Projection of public expenditure: 1964/5 - 1968/9.

In many ways this is the most difficult part of the entire exercise. However, it is essential to attempt this projection in order to obtain a rough quantitative estimates of the revenue required by the public authorities. I have not so far been able to give much thought to the "techniques of projection" and will greatly welcome any suggestions from the group; as at this point my project merges with the others in the programme. At the outset, we have several guide-lines to go by, such as the past rate of growth of public expenditure, the capital and recurrent expenditure implications of the Development plans drawn up by the three East African Governments, the projections made by departments, ministries and planning commissions. These estimates will have to be revised with the help of more sophisticated techniques of projection. Finally, it will be necessary to use one's judgement about the expected magnitude of public expenditure in the light of the study of the important influences affecting the level of public expenditure.

(B) Sources of Revenue.

In this section it is intended to study the existing sources of revenue available to public authorities in East Africa. These may be divided into six broad groups:

- (1) Taxation;
- (2) Fees, departmental earnings etc.
- (3) Past surpluses.
- (4) Internal borrowing.
- (5) Foreign grants and loans.
- (6) Credit creation.

The scope for increasing revenue substantially from sources (2), (5) and (4) is rather limited in the present circumstances of East Africa. It is reasonable to expect that revenue from (5) will increase more rapidly in future; however, foreign assistance is not a source of revenue that can be relied upon with any degree of certainty for financing public expenditure. Credit creation has hardly been resorted to in East Africa; and under the present monetary system, it is difficult to see how deficit financing (credit creation) can make an important contribution to the solution of the fiscal problems of the East African governments. Even if there were no institutional barriers, excessive credit creation could easily lead to inflation and balance of payments problems. However, there can be little doubt that in future a certain amount of budgetary deficit may have to be met by credit creation.

An examination of all the possible sources of public revenue leads us to the conclusion that most of the increase in revenue will have to come from taxes of one sort or the other. Our main problem, therefore, is to find ways of increasing revenue from existing sources as well as to develop new ones. The following are the main tax sources in East Africa at the moment:

- |                           |                            |
|---------------------------|----------------------------|
| (1) Individual Income Tax | (4) Excise duties          |
| (2) Company Taxes.        | (5) Export taxes           |
| (3) Customs duties.       | (6) Graduated Personal tax |

- |                       |                        |
|-----------------------|------------------------|
| (7) Produce sales tax | (9) Rates on property. |
| (8) Cesses            | (10) Estate duties.    |

Other 'potential' sources are:

- |                      |                              |
|----------------------|------------------------------|
| (11) Sales Taxes     | (14) Capital gains taxation. |
| (12) Turnover Taxes  | (15) Land taxes.             |
| (13) Expenditure Tax |                              |

An important aspect of this project will be an assessment of the different tax sources from the viewpoint of their effect on the allocation and supply of resources, stabilization, administrative convenience and equity. Throughout our analysis, income-elasticity will be an important criterion in our assessment of different taxes. It is hoped that as a result of this analysis, some valuable suggestions will emerge for the improvement of the economic efficiency of the existing tax system in East Africa. We shall attempt to project revenue for the next 5 years from existing sources. A comparison of the public revenue and expenditure projections will reveal the probable size of the budgetary deficit. It is here that the above analysis of different taxes will prove most useful in suggesting changes in the tax system to close the budgetary gap.

(C) Allocation of sources of revenue.

So far we have not made any distinction between different layers of government. It has been possible to consider the revenue and expenditure of all public authorities in the aggregate. Here an attempt will be made to allocate sources of revenue to different tiers of government. The constitutional structure of the three East African countries shows sufficient diversity to tax the ingenuity of any fiscal expert. At one extreme we have Tanganyika, with its relatively simple and orthodox two-tiered governmental structure; at the other extreme there is Kenya with a novel, full-fledged three-tiered structure of government, with Uganda somewhere in the middle, partaking of the feature of both types of systems. The pattern of distribution of fiscal sources will depend on the division of functions among different layers of government and the extent of financial autonomy granted to lower tiers of government. Each tier of government will have some independent sources of revenue to itself. It will, therefore, be necessary to study the suitability of particular taxes at federal, national, regional and local levels. We shall also have to consider other methods of dividing revenue between different public authorities such as sharing in the proceeds from a common tax, grants from the Federal or territorial governments to regional or local authorities etc.

Conclusion.

In conclusion, I should like to emphasize that the above outline of my project is still very tentative. I shall greatly welcome any comments, suggestions and criticism from the group. In particular, I should like the comments of the group on the following points:

- (1) Is the project outlined above too ambitious ?  
More specifically, does it meet the requirements of  
a doctoral dissertation of an American University ?
- (2) Does the project focus on the 'right' problems in  
the field of Public Finance in the East African  
context ?
- (3) Are there other aspects of Public Finance which  
raise issues of theoretical and practical importance  
in the East African context ?

-----