



Working Paper 98

## **Democratisation in Tanzania: No Elections Without Tax Exemptions**

Ole Therkildsen and Ane Karoline Bak

June 2019

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ICTD Working Paper 98

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## **Summary**

A demand-supply framework has been developed and applied to Tanzania to explore the link between democratisation, economic liberalisation and the use of tax exemptions to fund political parties' electoral campaigns. In Tanzania, the demand for this type of money has increased since one-party rule was abolished in 1992. This led to reduced state subsidies to parties, while growing inter- and intra-party competition for political power through the ballot box increased the campaign costs of the last three elections. Political liberalisation also raised the cost of keeping together increasingly fragmented political elites. The increased supply of political funding for the ruling party is driven by mutual interest between the funding demands of political elites, the interests of companies and emerging capitalists for tax exemptions and other rents to succeed in business. This demand-supply framework helps to explain an increased use of tax exemptions for private companies and individuals around election years in Tanzania. The framework is also relevant to the analysis of political financing through tax exemptions elsewhere on the African continent.

**Keywords:** tax exemptions; political financing; political economy; Tanzania; Africa.

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# Introduction

The purpose of this paper is to explore the political rationales and mechanisms that help explain the extensive use of tax exemptions in many African countries during the 2000s. It focuses on exemption magnitudes and changes over the three most recent election cycles in Tanzania. There are three interrelated issues which motivated this decision.

Firstly, although political funding (i.e. the financing of party activities and election campaigns) has received some attention both globally (Bryan and Baer 2005; Falguera, Jones and Ohman 2014; Pinto-Duschinsky 2012) and in Africa (Butler 2010; Lodge 2011; Pottie 2003), 'few political scientists have investigated the political rationale for exemptions in a consistent fashion. We mostly have to guess the extent to which they are granted in exchange for broad political support, party and political funding or simple bribes' (Moore 2014: 22).

Secondly, the context in which political parties in African countries seek to fund their activities has changed significantly over recent decades. Competitive elections have become more common – although not necessarily freer and fairer (Ham and Lindberg 2018). Election campaign costs may have risen in some countries (Bryan and Baer 2005), but there is too little evidence to show that this is generally the case (Pinto-Duschinsky 2002: 84). Nevertheless, the demand for campaign finance raises concerns about the distortions of democracy that the donors of political finance may cause. Such influence includes the risk of political capture, the sale of government favours and other rent-seeking practices (Moore, Prichard and Fjeldstad 2018; Norris, Es and Fennis 2015; OECD 2016).

Large domestic companies appear to be the main suppliers of political party funding (Amsden 2009). In African countries, many have emerged since the 1980s, in the wake of economic liberalisation. In some countries, they also appear to be the main beneficiaries of tax exemptions (Gauthier and Reinikka 2006). Such access to state-provided rents is typically very important for business success in emerging capitalist economies (Khan 2005a; Rodrik 2008; Whitfield, Therkildsen, Buur and Kjær 2015). The mutual interest of contributors and recipients of political finance is a common theme in all research work in this field, in both rich and poor countries (Arriola 2013b; Mendilow 2012).

Thirdly, the use of tax exemptions has spread to an increasing number of countries in sub-Saharan Africa (Fuest and Riedel 2009: 49, Table 2). The money involved is substantial: Tanzania spent 2.5 per cent of GDP in 2010/11 on tax exemptions compared to 7.1 per cent in Burundi, 2.6 per cent in Kenya, 3.2 per cent in Rwanda and 1.2 per cent in Uganda. Similar levels of tax exemptions are found in West Africa (OECD 2013: 10, Table 6).<sup>1</sup> This indicates that the use of tax exemptions in Tanzania is fairly typical.

In the following, we develop a framework to improve understanding of the political economy of the demand and the supply of political financing. This is used to explore the pattern of tax collection and tax exemptions in Tanzania from the early 2000s to 2016. Three general elections were held in that period (2005, 2010, 2015).

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<sup>1</sup> The East Africa figures are from the World Bank, as quoted in CRC Sogema (2013: 30, Table 7). They are based on the same methodology and therefore comparable. This is not the case for the OECD figures.

The main argument is that, in the context of increasingly competitive elections and economic liberalisation, fluctuations over time in the volume of tax exemptions awarded to companies and individuals in Tanzania can be linked to the election cycle. Some of these fluctuations are driven, at least in part, by the demand for campaign financing and a corresponding willingness of companies and individuals to supply it.

Five main findings underpin this argument: (a) the cost of election campaigns has risen due to increased competition for political power since the 2000s – both within the ruling party and vis-à-vis the opposition; (b) the regulatory framework for political financing is not enforced and public access to information about tax exemption beneficiaries is unreliable, thereby providing ample opportunities to exchange exemptions for political funding for the ruling party; (c) the tax/GDP ratio has decreased around each of the three recent election years; (d) the volume of tax exemptions (in constant shillings) to ‘Private companies and individuals’ has increased around each of these three election years – although the total volume of tax exemptions has actually declined since 2011/12; and (e) although some of the donations given in exchange for tax exemptions may end up in private pockets, a significant share must go to the ruling party, otherwise it would be difficult to finance the continued rise in election campaign costs.

The exploratory analyses of the link between tax exemptions and political funding in Tanzania mainly focus on Chama Cha Mapinduzi (CCM) – the ruling party since independence in 1961, and the largest recipient of political funding from the private sector. Tax exemptions are usually defined as deviations from a benchmark tax system that give rise to tax revenue losses rather than direct expenditure (OECD 2010: 14). Tax exemptions occur in many forms, including reduced tax and customs rates, and they may be bound to certain geographic locations (tax free zones) or time spans (e.g. tax holidays) (Fuest and Riedel 2009: 46). Information on these is taken from official sources (especially time series data on tax exemptions from the Controller and Auditor General’s (CAG’s) annual reports and (limited) microdata on tax exemptions by beneficiaries), academic articles, newspapers, major recent reports by consultants and NGOs and interviews with various key informants during the period 2009 to 2018. Other uses of the tax system – and of the government apparatus and budgets in general – to influence election results are not analysed in this paper (but see examples in Kjær and Therkildsen (2012) and Prichard (2016)).

The rest of the paper is organised into six parts. Section 1 presents the demand-supply framework which links exemptions to political funding. Section 2 discusses the method and data, including sources, reliability and coverage. Section 3 presents analyses of the rising demand for political funding in Tanzania and, hence, the political importance of tax exemptions and Section 4 deals with the supply of political financing. All this provides some insight into the links between tax exemptions and political financing (Section 5) and, finally, in Section 6, some implications for the relations between taxation and democratisation are outlined in the conclusions.

# 1 A demand-supply framework for political funding

There is very limited research that explicitly explores how political funding, tax exemptions, democratisation and economic liberalisation in African countries are linked. However, the literature quoted in the introduction provides a useful basis for formulating a demand-supply framework that links tax exemptions to political funding. In the following, we will show how the ruling political elite, private companies and rich individuals develop mutual interests that influence political funding in the context of competitive elections and economic liberalisation. Such mutual interests fundamentally depend on the political incentives facing political elites and leaders (Booth and Therkildsen 2012: 1).

There are three main reasons why, in many African countries, the *demand* for political funding increases with democratisation. Firstly, in one-party states, the ruling party can in principle draw as much funding from the government budget as it pleases. With the introduction of multiparty elections, the overt use of this opportunity is reduced. Although some African countries now provide state subsidies to all parties that won seats in prior elections, these funds are typically quite limited (like in Tanzania) or are non-existent (like in Botswana and Ghana) (Biezen and Kopecký 2007: 244 Table 1; Pottie 2003). Furthermore, party membership fees typically only contribute a little. Political parties and individual politicians must therefore look elsewhere for political funding.

Secondly, the costs of election campaigns are likely to increase when elections become more competitive (Bryan and Baer 2005; Kulick and Nassmacher 2012).<sup>2</sup> Even in countries where the ruling party has won multiparty elections with large margins, as is the case for CCM in Tanzania during the 2000s (Collord 2016), the cost of running election campaigns can be substantial. Furthermore, the probability of accessing political power is much better for a candidate in a dominant ruling party than in weaker opposition parties. The bid for nomination in the primary election as a ruling party candidate is therefore often fiercely competitive and costly (Seeberg, Wahman and Skaaning 2018). In other words, the increased competition can intensify the party's, as well as the individual candidates', demand for political funding in primary, parliamentary and presidential elections.

Finally, in many African countries, political parties – including dominant ones – tend to be internally fragmented and even more so in the wake of competitive multiparty elections where each clientelistic party has 'its own personalistically-based support built on loyalty and linked with the direct exchange of services and material benefits' (Erdmann 2010: 1291). Whitfield et al. (2015), for example, found that elite fragmentation has become substantial in Ghana, Mozambique, Tanzania and Uganda. To maintain access to political power, political funding in exchange for access to rents is essential to keep a fragmented party or elite coalitions together and reduce defections to the opposition (Khan 2012). Provision of club goods and tax exemptions for individuals, groups, commodities or companies is among the important instruments available.

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<sup>2</sup> In Kenya, for example, 'particularly campaign financing, has increased [...] largely due to intense intra- and inter-party political competition' (Mwangi 2008: 283).

In short, maintaining the 'party of choice' status in contexts of increasingly competitive elections requires money for voter mobilisation and election campaigning as well as rents for building and maintaining the coalition.

Turning to the *supply* side, private businesses and wealthy individuals can be potentially important sources of political funding. One reason for this is that economic liberalisation and rent seeking have spurred primitive accumulation in poor countries (Gray and Whitfield 2014; Khan 2005a). Over the last two decades, this has contributed to the emergence of a small number of large companies and rich individuals who typically dominate the formal economy (Page and Söderbom 2015) and have the capacity and motivation to provide political funding. This contrasts with the 'missing middle' of small and medium scale enterprises in African countries (Gelb, Meyer and Ramachandran 2014).

Especially in newly liberalised economies, (aspiring) large capitalists typically depend on formal or informal access to state-provided rents to achieve success in business. Among the examples are (subsidised) access to land and licences, less stringent enforcement of particular policies and tax requirements, import privileges and/or restrictions and tax exemptions (Noman and Stiglitz 2012; Whitfield et al. 2015). This enhances the capitalists' interests in political financing of the ruling political elite in exchange for rents. Furthermore, because the government's ability to redistribute is severely constrained by limited fiscal resources, political stability cannot be achieved in an open and transparent manner. Instead, individuals or groups who have redistributive claims or who pursue political office must build factions with enough power to enable their access to scarce state resources – often 'a combination of fiscal, off-budget, and even illegal means' (Khan 2005b: 718). Mutual interests enable the matching of the private companies' need for rents with the party's need for political funding.

In addition, winning elections with a considerable margin will help undermine beliefs in the oppositions' ability to take power. This deters future opposition turnout and coordination (Simpser 2004) and reduces the incentives to donate funds to the opposition. As long as donors of political funding – entrepreneurs in particular – are beholden to the regime in power, the funding needed by the opposition politicians to successfully build multi-ethnic electoral coalitions is limited (Arriola 2013a). This is especially true for domestic capitalists. Multinationals are less dependent on host state rents. Their relations to the host state's ruling political elites are typically more ambiguous and less 'embedded' compared to the domestic capitalists (Amsden 2009). They are therefore less likely to exchange political financing for rents. Multinationals do seek rents too, but their strategy for obtaining them seems to be based more on their investment and technological capabilities, as well as their importance as major taxpayers, than on their willingness to donate to political financing.

Finally, although the supply of political funding is legally regulated in most countries, there are many loopholes. Neither the ruling nor the opposition parties in African countries have strong incentives to increase or consistently enforce the regulation of political funding (IDEA 2014; Mendilow 2012). Non-compliance gives the ruling party the added opportunity to attract more private sector donations in exchange for tax exemptions and other rents. Neither do opposition parties have a clear interest to push for better regulation of political funding. For example, requirements for disclosure of the contributors to political funding may actually reduce donations to opposition parties and candidates, because transparency in these matters will reveal who these businesspeople are and expose them to the risk of retribution (Arriola 2013b; Sarakinsky 2007).

## 2 Methods and data

In this paper, the focus is solely on the link between political funding and tax exemptions. Using available tax exemption data, the analytical method is simple: changes over time in the monetary value of exemptions are explored to identify a possible link between the demand for and supply of campaign financing. Variations around election years are especially important to study. However, some clarification of concepts, categories and data are required before this method is applied.

There is no agreed definition of ‘political funding’ in multiparty systems (Mendilow 2012). However, Mendilow suggests a narrow definition, which is also used in this paper: political funding is money donated to parties and their candidates for ‘electioneering’. But distinguishing campaign funding from routine party funding is difficult. Donations to the latter could therefore also be considered ‘political funding’. In addition, government election cycle spending to lure voters to support the ruling party is widespread (Prichard 2016), as is the ruling party’s use of state resources and money spent for its political purposes by legally distinct NGOs, media, lobbyists and other organisations (Pinto-Duschinsky 2002: 70). In Tanzania, political parties rarely publish their accounts and audits are problematic (Kimboy 2014). This further blurs the distinction between routine and campaign financing. In practice, the size of political funding therefore cannot be precisely estimated; it is only possible to make educated guesses.

The sources of political funding to parties and their candidates are numerous and often overlap, and their relative importance vary across countries according to a survey of African countries (Bryan and Baer 2005).<sup>3</sup> Domestic military organisations (Arriola 2013b), foreign foundations and foreign intelligence services (Roelofs 2007) may also be important sources, but they are omitted from the Bryan-Baer survey. In Tanzania, money from some major recent economic scandals is also believed to have contributed to CCM’s campaign financing (Cooksey and Kelsall 2011; Gray 2015).

All the aggregate tax exemptions data on Tanzania are from annual reports by the CAG.<sup>4</sup> They cover the 2002 to 2016 period,<sup>5</sup> including the 2005, 2010 and 2015 election years. Thirteen different categories of exemptions are reported by the CAG.<sup>6</sup> However, only one, ‘Private companies and individuals’, is analysed in this paper. There are several reasons for this choice.

Most importantly, this category captures exemptions granted at the discretion of a variety of government ministries for a wide range of reasons (and supposedly published in Government Notices).<sup>7</sup> This creates considerable room for bargaining between the taxpayer and the granting

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<sup>3</sup> In a sample of 13 African countries, Oxford Analytica (2008) found that only 26 per cent of funds are raised by the party, 20 per cent comes through direct public funds, while the rest is presumably provided by the candidates themselves through various legal/informal/illegal channels.

<sup>4</sup> The data differ by up to 10 per cent from figures by other sources (see CRC Sogema 2013: 26, Figure 5), but only the CAG provides annual data from a longer period.

<sup>5</sup> The CAG’s annual reports from 2002 to 2008 are no longer available on the internet. Data from that period are from Rutasitara et al. (2010). Exemption data around 2000 are problematic as pointed out by Levin (2005). Hence, only data since 2002 are analysed. The so-called ‘shadow’ exemptions (CRC Sogema, 2013: 5) are not explicitly defined in any legislation approved by Parliament, and the CAG therefore cannot track them.

<sup>6</sup> None of the categories are defined in the CAG reports (or elsewhere in public sources). They range from relatively small volumes of exemptions to military duty-free shops, religious institutions and NGOs to larger exemptions for investment promotions (mining, oil, gas, (export) manufacturing) and exemptions for VAT.

<sup>7</sup> A complete set of up-to-date Government Notices is not available to the public. In ‘what seems to be an old version of the Government Notices ... more than 500 exemptions were granted to various beneficiaries, including individual corporations and people’ (CRC Sogema 2013: 52-53).

authority, including bargaining over money contributions to the ruling party in exchange for tax exemptions. Moreover, this exemption type has been given for at least twenty years. Analyses of the pattern of exemptions around three election years are therefore possible. Finally, the volume of this type of tax exemption is substantial. During the 2002 to 2016 period, it was the third biggest after exemptions on value-added tax (VAT) and exemptions given through the Tanzania Investment Centre (TIC).

None of the other twelve exemption types has all these useful analytical features. Unlike exemptions to 'Private companies and individuals', exemptions through TIC, the Export Processing Zones Authority (EPZA), mining development agreements and strategic investors are, supposedly, linked to the promotion of investments. Since investment decisions are influenced by many factors, which vary over time, it would be difficult to separate investment-driven exemptions from those that may be driven by demands for political funding.

Furthermore, the identification of possible causes of variations in exemptions over time is obscured by major policy changes in some of the important categories. Exemptions for the mining sector and the oil/gas exploration first started in 2008 – as did the Export Processing Zones (EPZ) exemptions – while exemptions through TIC have dropped significantly. In 2015, they were only 13 per cent of their 2008 peak value.

Finally, VAT exemptions – the biggest in volume terms during the 2000s – are given to a very wide variety of businesses, including many small ones. The underlying legislation has changed frequently over the years.<sup>8</sup> Moreover, the recording of 'VAT exemptions' is ambiguous. If granted to companies in mining, for example, such exemptions could be recorded under that category – but also under 'Mining Companies' (similar classification problems exist for other exemption categories like TIC). Even the consultants hired by the Ministry of Finance and supported by donors to analyse tax exemptions could not clarify this: 'A clear answer would require information that was not made available' (CRC Sogema 2013: 31).

In addition, information about the names of beneficiaries and the value of exemptions given to them are not published systematically or as regularly as promised (see Section 5) and a general picture of non-transparency and data problems emerges. This is reflected in the empirical analyses below.

## 3 The demand for political funding in Tanzania

In this section, the demand side of the analytical framework is applied. Several factors raise the demand for political funding: the poor state of CCM finances, increasing costs of election campaigns and elite fragmentation, which augment the costs of building and maintaining the ruling coalition.

### 3.1 The poor state of CCM finances

The financial situation for political parties in Tanzania changed significantly with the introduction of competitive elections. During the one-party rule prior to 1992, party funding was aided by the

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<sup>8</sup> Before the 2014 amendments to the VAT Act, it contained many exemptions and zero ratings of goods and services, as well as certain person categories entitled to receive exempt supplies (Fjeldstad, Ngowi and Rakner 2015).

blurred lines between government and party. It meant that the Tanganyika African National Union (TANU) (and after 1977 the CCM) received generous government support endorsed by the party-controlled parliament.<sup>9</sup> To some extent, this is still the case. CCM often uses government staff and vehicles in their election campaigns, as has been repeatedly highlighted by observers (TEMCO 2010; TEMCO/REDET 2016: 96). Government subsidies to parties also still clearly favour CCM, as their size depends on voting results in the previous presidential and parliamentary elections. After the 2000 elections, for example, CCM's monthly subvention was more than ten times higher than the opposition's. CCM received an annual total of TSh 5.3 billion compared to the opposition's TSh 480 million in 2018 shillings (Sokomani 2005: 87). In 2012 and 2015, the difference was smaller but still considerable; subsidies to CCM were almost three times larger than to the opposition (United Republic of Tanzania 2015a: Vote 27).

The size of the CCM's other income sources is unknown. The party runs various enterprises, some in collaboration with the army. For example, it owns prime location offices and factory buildings, storehouses and sports stadiums in major cities, and it runs the Kiswahili newspaper, *Uhuru*.<sup>10</sup> However, these undertakings have not been economically successful (Cooksey and Kelsall 2011). The current president, Magufuli (2015- ), established a committee to investigate such CCM assets in 2017. This committee found that many had been stolen, but the report is confidential.<sup>11</sup>

Former President Jakaya Mrisho Kikwete (2005-2015) gave a rare glimpse into CCM's financial problems when he stepped down as the party chair in 2016 (an issue he had taken up on several occasions in the past). He told the Party Congress that the only stable source of income was state subventions. Membership fees amounted to just TSh 500 million annually – TSh 10.5 billion short of full payment (Eriksen 2018: 7). According to one party insider, the annual deficit was about TSh 12 billion and the party therefore had to rely on private sector donations.<sup>12</sup> Funding gaps were to be filled 'by ad hoc interventions of the leadership' according to Kikwete.<sup>13</sup>

### 3.2 Increasing cost of election campaigns

Perhaps motivated by the implications of the CCM's strained finances and increasing campaign costs, Kikwete told Parliament in 2008 that he wanted to 'keep businesspeople from politics and politicians from business'. Kikwete proposed that people entering politics should leave the running of their economic activities to a trust fund. However, he had to abandon this radical idea because of resistance within CCM (REDET 2010: 24-26).

A less radical measure was, nevertheless, taken. The Election Expenses Act (2010), in force for all elections since 2010, aims to reduce corruption by setting overall spending limits on election expenses.<sup>14</sup> Each party must also provide the Registrar of Political Parties with a documented

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<sup>9</sup> In 1973/74, for example, government subventions accounted for 39 per cent of the party's budget. In 1984/85 that percentage was nearly 93 per cent (Whitehead 2009: 199).

<sup>10</sup> CCM is also said to own some 350-400 properties in Dar es Salaam alone. For a public debate about this, see Daily News (2012) *Tanzania: No Change for CCM-Owned Stadia, Says Sports Minister*, 4 July.

<sup>11</sup> Confidential interview with author, September 2018. See also The Citizen 2018.

<sup>12</sup> Confidential interview with author, September 2018.

<sup>13</sup> Quoted from Eriksen (2018: 7). He refers to 'Hotuba ya Mheshimiwa Jakaya Mrisho Kikwete, Mwenyekiti wa Chama Cha Mapinduzi, Wakati wa Mkutano Mkuu aa CCM Dodoma, 23 Julai 2016' and to the Makala Zetu blog, <http://makalazetu.blogspot.com/2016/07/hotuba-ya-mheshimiwa-jakaya-mrisho.html>.

<sup>14</sup> In the 2010 elections, the limits were TSh five billion for the presidential election and from TSh 30 to 80 million for the parliamentary election depending on the constituency population, size, etc. The overall spending limit for each political party was TSh 15 billion (Babeiya 2011: 99). For the 2015 elections, the spending limits were TSh six billion for the presidential election and between TSh 33 and 88 million per constituency in the parliamentary election. (TEMCO/REDET 2016: 94). The overall spending limit

financial statement of all expenses incurred within five months of the election. The Registrar can then act if spending limits are exceeded or accounts are not submitted. However, compliance is poor, as the monitoring depends on the parties' and the candidates' own reporting of their campaign spending (Heilman and John 2013). In addition, the act does not apply to intra-party elections, which can also be expensive (Khisra, Msami and Therkildsen Forthcoming). Actual campaign spending is therefore difficult to establish, but indications are that they have become more expensive over time. For Tanzania's 2000 and earlier elections, Bryan and Baer observed that the 'high cost of elections has turned the political process into something that can only be accessed by rich and predominantly male candidates' (2005: 129). The Tanzania Election Monitoring Committee (TEMCO) (2006: 24) noted that the 'excessive use of money in the 2005 elections raises the question as to what candidates expect in return for their "investment"'.<sup>15</sup> Tsubura (2015: 23) found that 'more Tanzanians said they were offered election incentives in 2010 than in the 2005 elections', and during the 2010 elections, the 'campaign materials for the bigger parties, especially the ruling CCM, were clearly more elaborate and expensive ... than in previous elections. Even a casual observer of these campaign materials would not fail to conclude that this was a very expensive election and that some parties and candidates spent fortunes' (TEMCO 2010: 108). Nevertheless, in contrast to the opposition parties, CCM and its candidates did not seem to have problems financing their campaigns according to the European Union Election Observation Mission (2010).

All of this points to increasing campaign costs from 2005 to 2015. However, none of the above assessments is based on surveys of actual campaign financing. Khisra, Msami and Therkildsen (Forthcoming) did that for a sample of MPs who ran successfully in the 2010 and 2015 parliamentary elections. Estimates of their campaign costs based on self-reported figures by the interviewees rose from TSh 52 million in 2010 to TSh 58 million in 2015 (in constant 2010 prices). Estimates of the presidential campaign costs, calculated on limited and scattered data, indicate that costs grew from about TSh 13 billion for the 2010 election to about TSh 21 billion for the 2015 elections (in constant 2010 prices). These increases are consistent with the observations presented above.

### **3.3 Elite fragmentation and the cost of coalition building**

Since the 1960s, Tanzania's ruling coalition<sup>16</sup> has consisted of CCM, parts of the bureaucracy and the military as well as, increasingly, prominent and rich businesspeople (Therkildsen and Bourgouin 2012), but economic liberalisation and competitive elections have contributed to making the ruling coalition more fragmented over time.

Since 1995, CCM has won all elections at all levels with substantial – although declining – margins (Collord 2016: 30 Figures 1 and 2). This makes it the 'party of choice' for political entrepreneurs seeking political office.<sup>17</sup> As these continue to turn to CCM, consensus about the party line becomes more difficult.

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for each party was TSh 17 billion (European Union Election Observation Mission 2015: 25). There are no limits on corporate and individual contributions to a party provided that it records donations of more than TSh two and one million respectively with the Registrar. Moreover, corporate and individual contributions to individual candidates are permitted but no explicit limits or reporting requirements are stated in the act (United Republic of Tanzania 2010: §11).

<sup>15</sup> TEMCO is supported by the United Nations Development Programme (UNDP) and has followed elections since 1995.

<sup>16</sup> The ruling coalition refers to the ruling elites as well as the groups and individuals who are behind the rise of the ruling elites to power and who give them their support, typically in exchange for benefits.

<sup>17</sup> As Mukandala et al. (2005: 5) explained, 'over 90% of the talented and experienced politicians decided to remain in the CCM under multi-partyism'.

The factional nature of Tanzanian politics is often discussed in terms of the ideological divisions within the CCM that existed in the 1980s and 1990s. Yet, ideological conflicts over economic liberalisation or socialism are now less intense, as a growing private sector and primitive accumulation have become stronger features of the economy (Gray 2015). Instead, intergenerational and interpersonal conflicts over and competition for posts in the party, the parliament and government have intensified (Mmuya 1998: ix; Tucker, Hoffman, Mukandala and Billera 2010). Such positions can be economically rewarding as the line between politics and business has become increasingly blurred (Cooksey and Kelsall 2011). Indeed, in a clear break with the Leadership Code of the Arusha Declaration, the party's Zanzibar Resolution of 19s91 formally allowed CCM members to engage in 'capitalist activities'. All this contributes to a growing fragmentation of the ruling coalition.

According to Andreoni (2017: 16), the fragmentation of CCM is also partly driven by disagreements about the relationship between the mainland and Zanzibar and by a major 1995 corruption scandal in which the party was accused of allowing rich businessmen of Asian origin to capture wealth at the expense of poor Africans. Another trend is that factions of the ruling coalition – especially the local levels of the government administration and party machinery – gain political strength because they have become increasingly important for mobilising voters during the elections (Whitfield et al. 2015: chapter 8).

Indeed, competition within CCM for political office has been stronger than that with the opposition parties. About 57 per cent of the CCM parliamentarians in the 1995, 2000 and 2005 elections lost their primary elections – 31 per cent because they did not contest and only 11 per cent because they lost to an opposition candidate (Collord 2018: 293). The fragmentation of the ruling party extends to the present (see Ng'wankilala 2014 and Kisiangani and Lewela 2012) The 2015 election 'laid bare the entrenched factionalism within CCM. What was once a highly centralized, bureaucratic party is increasingly split by rival networks of competing political elites' (Collord 2015).

Gray (2015: 395) concludes that, '[b]ehind the formal constitutional rules, power is considerably fragmented even at the top of a dominant party system'. The party is effectively an organised election-winning machine for competing factions within the party. It has survived twenty years of competitive elections relatively unscathed despite a fluid political balance between contending factions within the ruling coalition. Nonetheless, access to rents and political financing is crucial for keeping the ruling coalition together, leading to substantial and increasing demands for political funding. Such demands cannot be met from the government's formal budget.

Thus, democratisation and increased electoral competition have created a paradoxical situation for Tanzanian politics. While CCM is strong enough to keep factions together, it is too weak to impose discipline on them. In this situation, tax exemptions and off-budget rents become important coalition building instruments.

## 4 The supply of political funding to the ruling party in Tanzania

Tanzania's economic liberalisation in the 1990s had far-reaching consequences. In the absence of effective regulation, it allowed well-placed politicians and civil servants to benefit from poorly

designed privatisations and deregulations. At the same time, it led to the rapid rise of a new class of economic elites with close connections to CCM (Gray 2015; Tucker et al. 2010). These elites are important for the supply side of the ruling party's political financing, as this section shows. Tanzania's narrow tax base leads to a financial dependency on very small segments of the business community and richer individuals. Moreover, there is a strong relationship between these capitalist segments and the ruling political elites which creates a clear interest of these businesspeople to provide political funding to the ruling political party and its candidates. The link between political funding and tax exemptions given in and around election years will be substantiated in Section 5.

Tanzania's economic growth has been high for the last 15 years (five to six per cent per year since the mid-1990s). From 2000 to 2016, its tax/GDP ratio fluctuated between nine per cent (in 2005) and 13 per cent (in 2016), as shown in Figure 1. This performance compares reasonably well with that of other African low-income countries (Haldenwang and Ivanyina 2012),<sup>18</sup> but as Cooksey (2011: 27) observed: 'Most Tanzanian adults do not pay taxes on their income, either because they are too poor, too distant from the tax-collector's dragnet, and/or successful in tax evasion'. Add tax exemptions to this quote, and the statement provides an accurate description of the situation.

Despite its approximate 50 million inhabitants, Tanzania had only about 400,000 registered taxpayers in 2007, growing to 1.3 million in 2013 (Ministry of Foreign Affairs of Denmark n.d.). This reflects an economic structure characterised by a very small formal sector.<sup>19</sup> Since all public employees (708,000 in 2014) are supposedly paying tax, the number of registered taxpayers in the private sector is, by implication, modest.<sup>20</sup> In addition, only about 4 per cent of small – typically sole proprietor – businesses were registered with the authorities in 2012. Few of them had a tax identification number (UNIDO 2013: 10). However, the most striking feature of taxation in Tanzania is that most domestic revenues are generated by very few businesses. In 2005, for example, almost 70 per cent of the domestic revenues came from just 286 large taxpayers (Fjeldstad and Moore 2008: 256). By 2008, about 400 large taxpayers accounted for 80 per cent of the revenues (African Development Bank Group 2011: 247). The economic and political liberalisation has arguably served to create 'a political and economic oligarchy at the top levels of society' (Tucker et al. 2010: 3).

If, as a reasonable first approximation, it is assumed that the political bargaining power of (groups of) taxpayers depends on the size of their revenue contributions (Timmons 2005), then large companies yield considerable political power in Tanzania – especially if they are also organised within or enjoy close connections to CCM. This makes such companies likely beneficiaries of state-provided rents such as tax exemptions, licences and non-market access to property (Wangwe 2010). In exchange for such rents, they may provide political funding to the ruling party.<sup>21</sup>

That close connections to the ruling party are important is illustrated by a clarification from the former Prime Minister Frederick Sumaye (1995-2005), requested by Makidara Mosi, a member of parliament for a major opposition party. In a public meeting, Sumaye reportedly said, 'if you want to do well in business you should join the CCM' (Therkildsen and Bourgooin 2012: 17).

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<sup>18</sup> Haldenwang and Ivanyina's (2012) assessment is based on data prior to the financial crisis in 2008.

<sup>19</sup> Tanzania has, together with Zimbabwe and Nigeria, one of the largest shadow economies among developing countries (60, 63 and 59 per cent respectively in the early 2000s) according to Schneider (2004: 10).

<sup>20</sup> Formal employment in the private sector was 1.4 million people (United Republic of Tanzania 2015b: ix).

<sup>21</sup> However, it may also tempt politicians to predate on private capital (Centre for the Future State 2010: 23). Cooksey (2011) deals with this issue.

Sumaye has denied this allegation, but it is a common view among businesspeople that connections with the CCM can be very helpful for business (see also Babeiya 2011: 95).

Connections between businesses and CCM are most evident when the CCM politicians themselves own – or have strong interests in – private sector companies. No systematic information on this exists, but some CCM politicians are, for example, known to be involved in a number of trucking companies, which have therefore become ‘politically powerful’ (Hoffman 2014: 3). From an election perspective, it is also interesting that at least ten CCM MPs have interests in radio/TV stations and newspapers, compared to only two opposition MPs (TEMCO 2010: 78). One prominent example of this is the former Speaker of Parliament, Pius Msekwa (1994-2005). From 2003 to 2005, he was also the non-executive chair of the board for Vodacom in Tanzania.<sup>22</sup> When the company was questioned about this unusual arrangement, it replied that the appointment of Msekwa was a prerogative of Vodacom’s Tanzanian partners (Brümmer 2007). Rostam Aziz (see below), who owned the most shares at the time, was prominent among them.

Generally, some of Tanzania’s largest domestic entrepreneurs have prospered substantially under CCM rule and are among its main donors according to author interviews with three CCM insiders.<sup>23</sup> The entrepreneurs have a clear incentive to help the incumbents retain power by contributing substantially to the party. With wide-ranging cross-sectoral business interests, they have incentives to donate election campaign funds to the party (including to the presidential campaign) to maintain the system that benefits them, while at the same time nurturing specific connections through targeted support to individual politicians.

Among the big business donors is an Asian-Tanzanian businessman-cum-politician, Rostam Aziz, who was the party’s treasurer from 2005 to 2007. He was also the campaign manager for Kikwete himself during the presidential elections in 2005. Aziz reportedly became the first Tanzanian dollar billionaire in 2013. He makes his money in constructions related to mining, telecommunications (Vodacom) and real estate. Other prominent and wealthy businesspeople supporting CCM are the Tanzania-based multinational Bakhressa group of companies (manufacturing, media, milling, maritime and land transport, retail, etc.): Ali Mfuruki (retail, software, telecommunications), the multinational Mohammed Enterprises<sup>24</sup> (agro-business, import and export trading, manufacturing, software), Subash Patel<sup>25</sup> of the multinational Motisun Group (infrastructure, manufacturing and services) and the Seif brothers (sugar factories, manufacturing, transportation, construction equipment, etc.).

In this perspective, Kikwete’s failed attempt in 2008 to reduce the influence of money in politics mentioned earlier is not surprising. According to several observers, his idea was not just motivated by high principles; it was also a reaction to public concern about corruption in politics and an attempt to prevent the then prime minister, Edward Lowassa (2005-2008), from using his wealth to run for the presidency in 2015 when Kikwete’s final term in office expired. Kikwete failed in the latter. Although Lowassa had to resign in 2008 due to his involvement in the so-called Richmond corruption scandal, he made a run for the CCM presidential nomination in

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<sup>22</sup> Vodacom is one of the largest telecommunication companies in Tanzania and it was conspicuously absent from the top ten list of tax-paying companies in Tanzania presented to Parliament in August 2009 by former Prime Minister Mizengo Pinda (2008-2015).

<sup>23</sup> Confidential interviews with authors in 2010 and 2018.

<sup>24</sup> The owner, Mohammed Dewji, was a Member of Parliament for CCM from 2005 to 2015.

<sup>25</sup> Elected chairman of the Confederation of Tanzania Industries in 2018 – a position always held by a party supporter.

2015, backed by his very considerable ill-gotten wealth.<sup>26</sup> When the party finally stopped his candidacy, Lowassa switched to the opposition and ran for presidency as the leader of the opposition. In addition, the CCM itself is believed to have partially funded its 2005 election campaign with money from the so-called External Payment Area corruption scandal of the early 2000s (Cooksey and Kelsall 2011; Gray 2015; Policy Forum 2016).

Thus, with economic liberalisation, a growing group of wealthy domestic entrepreneurs and businesspeople-cum-politicians has emerged. As shown below, they have brought serious money into Tanzanian politics.

## 5 Linking tax exemptions and political funding

The loss of the one-party regime's financial privileges and the increased cost of competitive politics have forced the ruling party to look hard for new sources of political funds. Donations to CCM and its candidates in exchange for tax exemptions is an important option. Evidence of such exchanges is not directly available but can be deduced by combining analyses of six pieces of publicly available information.

Firstly, opportunities for granting exemptions are abundant. In the beginning of 2013, a total of 122 sections in the Tanzanian legislation made it possible for a range of government organisations to grant them. The East African Community Customs Management Act adds another 38 provisions, which are administrated by the Revenue Authority in Tanzania. Exemptions are also given through Government Notices that do not need to be based on legislation approved by Parliament.<sup>27</sup> Prior to 2013, more than 500 were granted by a range of ministries to various beneficiaries, including individual corporations and people, but up-to-date lists are not available. 'This makes it almost impossible to collect relevant data, assess costs and report on a regular basis on these exemptions', wrote the consultant whom the Ministry of Finance itself had hired to do exactly that (CRC Sogema 2013: 4-5, 53-54).

In 2012, however, the government decided to reduce tax exemptions to below one percentage point of GDP by 2014 (United Republic of Tanzania 2012: 55). Accordingly, VAT exemptions, for example, were reduced and the total volume of exemptions declined significantly. Nevertheless, as shown below, specific types of exemptions are still substantial.

Secondly, up to this point, the granting of exemptions has remained opaque. This facilitates discreet rent bargaining between beneficiaries and government/party organisations. Regular up-to-date lists of each exemption-benefitting company are not available despite repeated government promises to publish such information quarterly.<sup>28</sup> They are only published sporadically on the Ministry of Finance (MOF) website. Analyses of the four available MOF tax exemption reports from 2015 show, for example, that while fifty different companies received tax exemptions linked to the EPZ, ten of these were not listed as EPZ companies by the EPZ

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<sup>26</sup> Lowassa had used his wealth to build a strong network in the regional and district level party organisations. He distributed, for example, 39 Toyota four-wheel drives to these organisations (confidential interview with author, CCM insider, Dar es Salaam, August 2012).

<sup>27</sup> Tax exemptions can also be granted through Mining Development Agreements, Oil and Gas Production Sharing Agreements and agreements between the government and strategic investors (CRC Sogema 2013: 1).

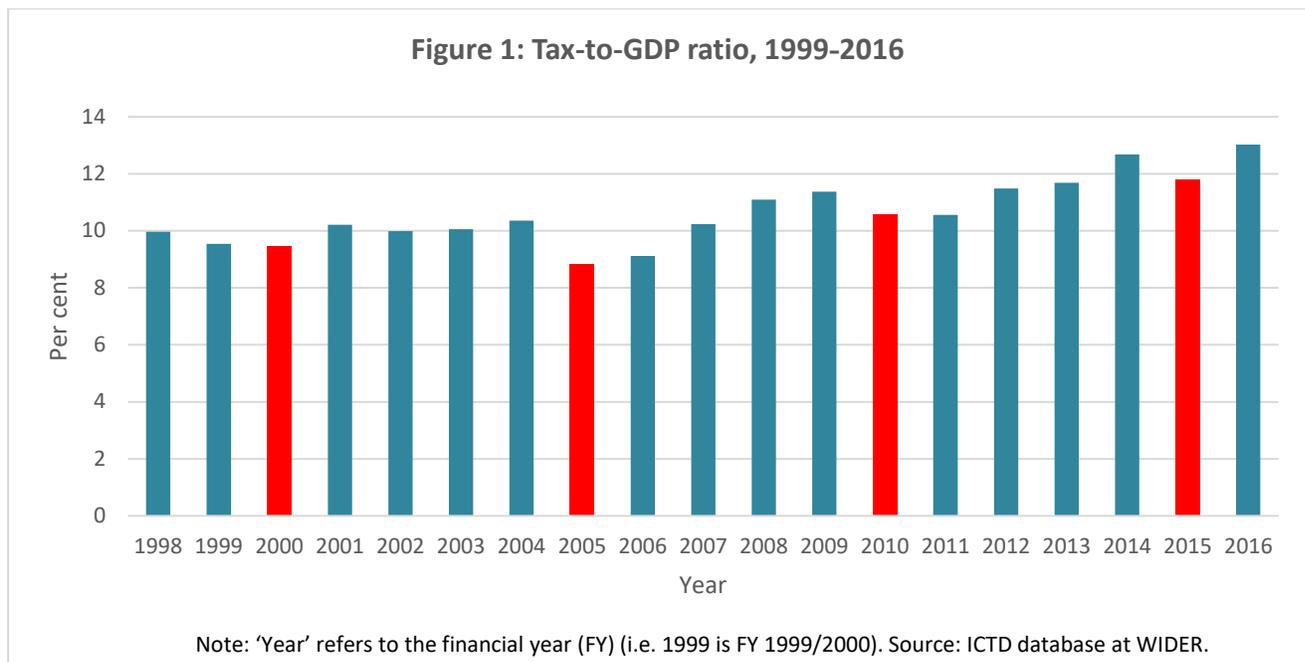
<sup>28</sup> See, for example, the Budget Speech 2009/2010 presented in Parliament by the Minister of Finance. A similar promise was made in the 2014/2015 Budget Speech. The CAG has made requests for this since the 2012/13 report. From 2013/14, the CAG also began to raise questions about exemptions to specific named companies.

authority (EPZA). Such unreliable public information facilitates illicit exchanges between private businesses, civil servants, public organizations and the ruling party, CCM.

The presence of this opportunity structure strongly indicates that tax exemptions are central to Tanzania's political economy. Even multilateral organisations that do not normally venture into such analyses have pointed this out. For example, the International Monetary Fund (IMF) stated that 'exemptions have unduly multiplied ... and could be usefully scaled down. The authorities noted they were aware of the issue but had run into political difficulties when attempting to curtail exemptions' (2011: 17). The African Development Bank explicitly concludes that Tanzania's tax effort will be constrained by two factors in the medium term: '(i) continued elite resistance to abolition of the prevailing extensive tax exemptions; and (ii) threat of increased high-level corruption in government agencies' (2011: 240).

Thirdly, little is known about how the actual bargaining for political funding occurs. One CCM inside source claimed that the top CCM leadership typically asked the ministers to mobilise party donations from their respective ministries. Each one simply got a money quota to meet. This is consistent with President Kikwete's quote mentioned earlier (see Section 3.1), which stated that the party' funding gaps had to be filled 'by ad hoc interventions of the leadership'. The extensive legislative opportunities for tax exemptions to individual companies must have helped ministers to meet their quota.

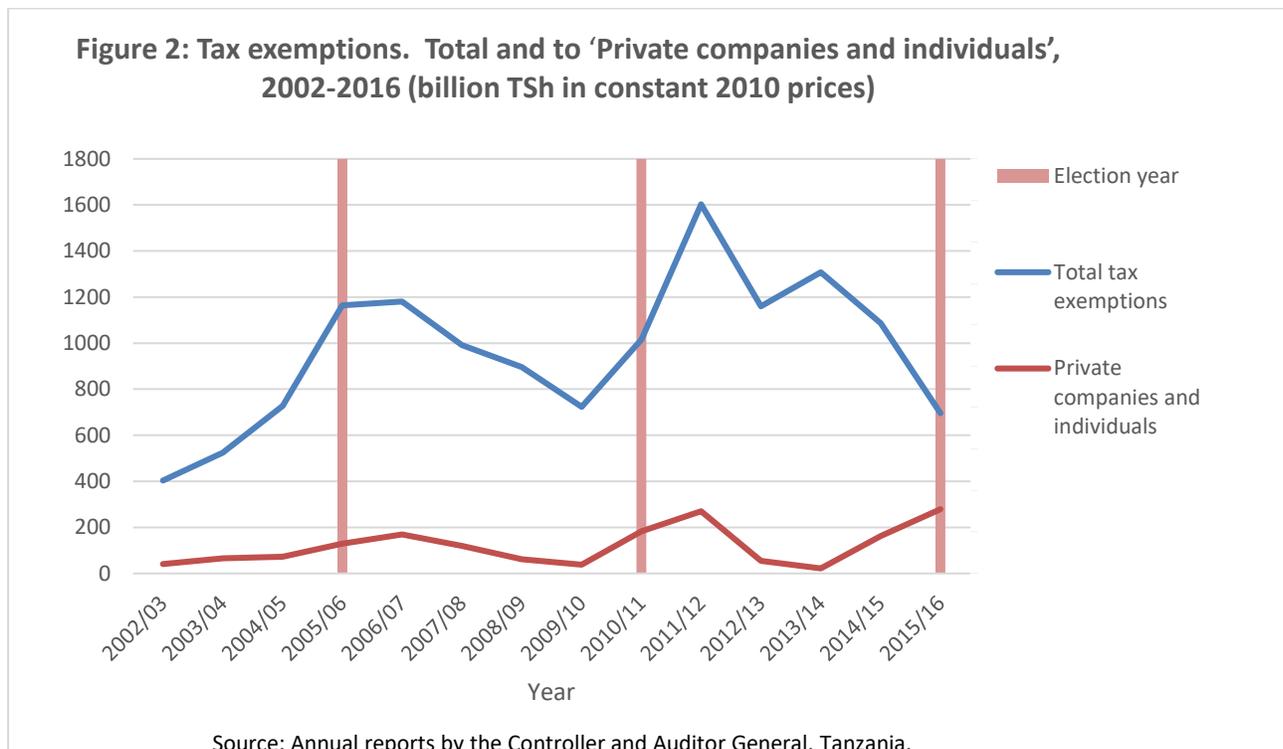
Fourthly, the level of tax exemptions correlates with the holding of elections. Figure 1 shows that the tax-to-GDP ratio has dipped in each of the last four election years (2000, 2005, 2010, 2015). Several factors may cause these systematic fluctuations: smuggling to avoid paying import tariffs on politically sensitive commodities (Levin and Widell 2014) – for example rice and sugar (Andreoni and Tasciotti: Forthcoming), less aggressive tax collections as well as more concerted taxpayer resistance in election years (see Prichard (2016) for a discussion of such issues) and, of course, tax exemptions.



Fifthly, Figure 2 focuses specifically on fluctuations in the substantial tax exemptions given to 'Private companies and individuals'. The reasons for analysing this category are presented in Section 3.

The observed changes in exemptions given to 'Private companies and individuals' clearly correlate with election years and can, therefore, by implication, be linked to political financing of the ruling party. The figure shows that their volume grows rapidly prior to the election year, only to fall in subsequent years. The peak of the total volume of exemptions also rises through the three election cycles observed (although data on 2016/17 are not available). As this is consistent with the observation that election expenses have risen during the 2000s, it clearly indicates that tax exemptions serve to facilitate a supply in response to an increasing demand for political funding. The pattern is remarkable because expenditures in this particular exemption category increase despite a significant decline in the total volume of exemptions since 2011 (Figure 2).

Sixthly, an important observation follows from this. Officials that negotiate and receive donations for the party do not retain all of it themselves. If they did, the party would – everything else being equal – have to reduce campaign expenses and evidence suggests that this has not happened. Likewise, the consistency over all three elections cycles in the correlation between the increasing peak value of exemptions and the increase in election expenses indicates that the party must be a main recipient of such donations.



Taken together, this evidence – substantiated by the changes in demand and supply of the political funding demonstrated above – strongly indicates a link between election-driven fluctuations in tax exemptions and political funding of CCM by individuals and companies.

## 6 Conclusions

As is typical of several other African countries, Tanzania annually loses substantial revenues due to tax exemptions. They amounted to approximately USD 1.16 billion at their peak in 2011 but have since declined to USD 0.47 billion in 2016.

Exemptions are officially given for a variety of reasons: to promote investments, further the work of NGOs and religious organisations, show support to the military, reduce the costs of essential goods consumed by the poor, etc. But tax exemptions can also be given in exchange for financial contributions to the ruling party's election campaigns to keep a ruling coalition together. Who receives what and under which conditions is, however, poorly understood.<sup>29</sup>

This paper contributes to a better understanding of the political economy of tax exemptions. Based on a simple demand-supply framework, this paper explores how, in the context of Tanzania's increasingly competitive elections and economic liberalisation, fluctuations over time in the volume of tax exemptions to companies and individuals are linked to the election cycle. Ruling elites need political funding to stay in power. Businesspeople need tax exemptions and other state-provided rents to be successful. Thus, mutual interests between major capitalists and the ruling political elite are central to the supply in the face of an increasing demand for political funding.

Exemption data from 2002 to 2016, covering three general elections, establish this link between tax exemptions and political funding. They show that peak volumes of tax exemptions to private companies and individuals co-vary with election years. The supply of donations from companies and individuals helps to meet the demand for campaign financing by the ruling party. Moreover, although the total volume of tax exemptions has fallen significantly since 2011, the peak volume of this type of exemption has increased from the 2005 to the 2015 elections. This is consistent with increasing costs of election campaigns during that period.

The Tanzanian case illustrates that democratisation since the 1990s has not undermined its clientelistic politics; instead, it has amplified it. This has also been observed in other countries studied by, for example, Whitfield et al. (2015), Khan (2005b) and the African Power and Politics Programme (Crook and Booth 2011). The explanation is that the organisation and mobilisation of clientelistic political coalitions are not driven by the absence of democracy, but by structural features of the economy and by the efforts of fragmented ruling political elites in order to maintain and strengthen the coalition that keeps them in power.

To serve this purpose, money has become increasingly important in Tanzanian politics. Consequently, this has driven the old self-proclaimed socialist party of workers and peasants into close engagement with a small segment of the business community, as well as people with money. If Moore (2007) is right in saying that states that rely on broad taxation have better incentives to practice better governance, then the short-term prospects for governance improvements are not good in such contexts. Democratic or not, there cannot be a meaningful inclusive fiscal contract in place in a country where the government depends on a very limited number of rich companies and individuals for its revenues and where the ruling party depends on such sources of income to run election campaigns. Thus, taxation and the granting of exemptions are instruments of rule as also emphasised by Moore (2014).

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<sup>29</sup> McMenamin (2012) makes a similar observation for rich countries.



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