International Journal of Economics, Commerce and Management
United Kingdom ISSN 2348 0386 Vol. X, Issue 6, June 2022

http://ijecm.co.uk/

AN EVALUATION OF UGANDA'S TAX SYSTEM USING THE CRITERIA OF A GOOD TAX SYSTEM

Tonui Vincent Kiplangat
tonuivincent82@gmail.com

Abstract

Most developing countries devote their attention to designing taxation policies that promote economic development, since taxation policy is a very important instrument for augmenting revenue if not the primary domestic revenue source. This paper aims to evaluate Uganda's tax system by subjecting it to principles of a good tax system and comparison with tax effort/performance from other sub-Saharan Africa countries. For the purpose of the study, the criteria of determining a good tax system border on effective administration, equity and fairness, convenience of payment, certainty, transparency and accountability, simplicity, efficiency, neutrality and one that has a minimum tax gap. The data sources include the Uganda's fiscal policy environment, legal framework on taxation and tax reforms. Study found that despite undertaking more favorable tax reforms over the last three decades, Uganda's fiscal policy is marked by high budget deficits, suffers substantial imbalance in the tax incidence, low impact and limited tax base, low levels of tax compliance and high tax evasion as well as tax avoidance. The study concluded that these characteristics of Uganda's tax system are synonymous with a country whose tax system falls below the criteria of a good tax system and may therefore need continuous review.

Keywords: Tax system, taxation policy, tax reforms, tax effort, tax performance, tax revenue

INTRODUCTION

Most developing countries devote their attention to designing taxation policies that promote economic development since taxation policy is a very important instrument for augmenting revenue if not the primary domestic revenue source. As a result, in most developing countries, the primary goal for fiscal policy is to increase revenue. Given the useful role played by fiscal policies in economic development, developing countries must ensure that they are operating a good tax system. This paper is an evaluation of Uganda's tax system by subjecting it to principles of a good tax system and comparison with tax effort/performance from other sub-Saharan Africa countries.

CRITERIA OF A GOOD TAX SYSTEM

The criteria of determining a good tax system border on effective administration, equity and fairness, convenience of payment, certainty, transparency and accountability, simplicity, efficiency, neutrality and one that has a minimum tax gap. The table below shows the guiding principles of good tax policy using four formulations of universal criteria to analyze tax systems.

Table 1: Criteria of a Good Tax System

AICPA Principles of Good Tax Policy	OECD Tax Principles	U.S. Joint committee on Taxation (JCT) Analysis Criteria	U.S. Government Accountability Office (GAO) Criteria for a Good Tax System
Equity and fairness	-	Is "the tax system fair? Does the tax system treat similarly situated individuals similarly? Does the tax system account for individuals' different capacities to bear the burden of taxation?"	Equity includes two principles: (1) ability to pay (horizontal and vertical equity), and (2) benefits received. "When making judgments about the overall equity of government policy, it is important to consider both how individuals are taxed and how the benefits of government spending are distributed."
Certainty	-	-	-
Convenience of payment	"Compliance costs for taxpayers and administrative costs for the tax authorities should be minimized as far as possible."	-	-

Effective tax administration	-	"Can the tax system be easily administered by the government and can it induce compliance by all individuals? Is enforcement costly? Can some individuals successfully avoid their legal liabilities?"	Administrability including "processing returns, enforcement, and taxpayer assistance."
Information security	Structural features should keep pace with technological changes.	-	-
Simplicity	"The tax rules should be clear and simple to understand so that taxpayers can anticipate the tax consequences in advance of a transaction, including knowing when, where and how the tax is to be accounted."	Is "the tax system simple? Is it costly for taxpayers to determine their tax liability and file their taxes?"	Simplicity in terms of the "compliance burden (record keeping, planning, return preparation, and responding to audits)."
Neutrality	"Business decisions should be motivated by economic rather than tax considerations. Taxpayers in similar situations carrying out similar transactions should be subject to similar levels of taxation."	-	The system should not distort economic decisions.

FISCAL POLICY ENVIRONMENT IN UGANDA

Legal Framework on Taxation

The legal framework includes the Ugandan Constitution, 1995; Income Tax Act (Cap 340) of 1997; (Mugalula, 2010). Value Added Tax (Cap 349); Excise Management Act (Cap 335); East African Excise Management Act (Amendment) Act, 2012; Tax Procedures Code Act, 2014; The Local Government Act (Cap 243) and other laws governing taxation at local government levels.

Tax Systems and Policy in Uganda

Uganda's revenue is primarily derived from indirect taxes, notably those related to international trade. This reliance on indirect taxes is mostly owing to the administrative and other constraints that limit income taxes. Currently, the country's tax system is comprised of:

i. Excise duties,
ii. Value Added Tax (VAT) at 18% (Almunia et al., 2017),
iii. Import duties,
iv. Income taxes (personal and corporate income tax at 30%),
v. Withholding tax (5%)
vi. Other small yield taxes such as fees and licenses, freight charges, airport tax and drivers' permits

Although indirect taxes are widely believed to be more regressive than income taxes, indirect taxes are unavoidable in Uganda. Food, for example, is exempt from taxes, and food accounts for a significant amount of the poor's budget. In Uganda, merit goods taxes, excise duties on alcohol based products and tobacco and import levies on petroleum products, are a key source of revenue, suggesting that high merit goods taxes may contribute to the country's regressive indirect tax structure. However, demerit may not be the primary reason behind the hefty taxation. Partial equilibrium analysis implies that taxing them is efficient due to their low price elasticity.

Since 1987, fiscal authorities have implemented several revenue enhancing and efficiency discretionary tax measures. These include; changing all excise and customs duties from specific to ad-valorem, minimizing the customs duty rates numbers, and increasing excise duties and sales tax rates on the primary revenue-generating domestic products e.g. cigarettes, beer, soft drinks.

Tax Reforms in Uganda

There have been evolutions in the tax systems, institutional changes and reforms especially around income tax and VAT. The usual rate of VAT, for example, was raised from 17 percent to 18 percent in 2005/06. Efforts to protect the poor have included zero-rating and exclusions of food items from VAT, as well as increasing the personal income threshold. In 2012, the PAYE level was increased from UGX 130,000 to UGX 235,000 (Elshout, 2020) The Ugandan government (GoU) passed the Tax Procedures Code Act in 2014 to harmonize and regulate the administrative procedures of existing tax legislation, making it easier for taxpayers to comply. Uganda Revenue Authority (URA) altered its organizational structure and operational departments as part of institutional adjustments to improve its performance, particularly in terms of international and domestic revenue mobilization. By 2015, the five original departments had been updated and enlarged to seven. These are: commissioner-general's office, corporate affairs, legal services and board affairs, tax investigations, domestic taxes, customs, internal audit and compliance.

Other changes were institution building for tax administration given top priority, creation of Uganda Revenue Authority in 1991, Establishment of EACU/Tarrif liberalization, enactment of new income tax law in 1997, widening excisable goods, establishment of Tax Appeals Tribunal (TAT). The efforts to extend taxation by introducing a uniform rate – VAT as a standard model of commodities taxation and the reorganization of income tax have been a prominent feature of current tax policy. Efforts to protect the poor have included zero-rating or exempting items from VAT and boosting the personal income level. Furthermore, since 1997, the corporation tax rate has been decreased from 60% to 30% in 1987/88 (Teera, 2003) and the maximum income tax rate has been lowered from 60% to 30% in 1987/88.

The tax system in Uganda includes taxes with a rate schedule that can be changed rapidly and with a level of certainty, affecting the private sector's purchasing power. These taxes have been used to raise or decrease private spending in to attain stabilization objectives concerning growth, price, or balance-of-payments. Tax system of Uganda is cluttered with a narrow tax base, revenue adjustment with the aim of stability has been achieved by piecemeal approaches, such as boosting rates on indirect taxes like sales tax, excises and import duties, which are thought to generate more money with better certainty and speed.

However, for more than a decade, Uganda's principal tax policy goal has been to increase income — the tax ratio has risen from around 4.5 percent in 1987 to around 11 percent now (Gandhi, 1987). Unfortunately, this was accomplished through ad hoc tax rate increases to meet the revenue target, with no attention for potential supply side consequences. There are challenges of adherence in a culture of tax avoidance, as there are in many other countries, notably but not only in the developing world. It's probable that the recent rapid spike in taxation has lowered compliance. This is something we'll try to investigate in our empirical research.

EXPERIENCE AND TRENDS IN FISCAL POLICY ENVIRONMENT IN UGANDA

Uganda has tax revenue to GDP ratio of 13% which is lower than Sub Sahara Africa's 21% (Mawejje et al., 2016) and OECD countries whose rate is 32%. The country's tax system has faced several economic shocks that have troubled the country since 1966. Tax collections are minimal causing to large fiscal deficits. The fiscal deficit in the Financial Year (FY) 2018/19 is forecasted at 4.8% of GDP which is 0.9 percentage point gain over 2017/18 level. Between FY 2017/18 and FY 2018/19, the deficit was covered mostly through non-concessional loans and concessional, with domestic borrowing growing from UShs 612 billion to UShs 1,690 billion.

The country has also struggled from an over-reliance on a limited number of tax revenue sources, which are susceptible to external shocks and continue to be a major issue in the tax system. In regard to the need for cash to support social and economic growth, there was a major reform to Uganda's tax system since May 1987. (Engle et al., 1987) To achieve fiscal discipline, the government intensified its efforts in the departments of expenditure reduction and tax administration. The Uganda Revenue Authority (URA), a semi-autonomous entity charged with tax policy implementation, was established by the government in 1991 (Kangave, 2001)

It was given the job of administering and collecting taxes for the federal government.

Other reforms include the exemptions partial elimination, customs duty rates standardization, tax rate bands narrowing, tax rate reductions, and new types of taxes introductions, that are reasonably simple to manage. The Value Added Tax (VAT) was implemented in 1996 with the goal of broadening the tax base by bringing all commodities and services into the tax net.

In comparison to the 1980s, a blend of excellent governance, effective tax administration, effective macroeconomic policies, among other discretionary tax approaches has led to the improvement of the tax to GDP ratio, though it remains low in comparison to other countries. The unsuccessfulness of the tax system to yield adequate revenue has led to unsustainable deficits in the government.

An Empirical Appraisal of Uganda's Tax Performance

Appraising the tax performance of Uganda in relation with other similar countries, Teera (2003) analyzed whether the development expectations to add tax revenue beyond the current level is achievable and which taxes were the best candidates. To do this, Teera (2003) calculated the tax effort index whose results are shown by Table 1 below.

Table 2: Tax Effort Indices for Total Tax Ratios and Individual Taxes for 18 Countries

Country	**Total Tax Ratios**		**Taxes on Income**		**Taxes on Goods & Services** [redacted]		**Taxes on International Trade** [redacted]	
	Tax ratio	Tax Effort Index	Tax ratio	Tax Effort Index	Tax ratio	Tax Effort Index	Tax ratio	Tax Effort Index
Togo	24.6	2.216	33.7	1.682	12.6	0.624	31.8	1.017
Kenya	18.8	1.698	31.2	1.554	37.6	1.868	18.6	0.595
Gambia, The	15.9	1.437	13.9	0.692	6.2	0.308	64.9	2.075
Malawi	15.6	1.404	34.9	1.741	29.3	1.456	18.8	0.601
Tanzania	15.1	1.365	27.4	1.364	42.2	2.095	16.0	0.512
Burundi	13.8	1.242	19.7	0.980	26.9	1.338	33.3	1.064
Ethiopia	12.4	1.118	24.8	1.239	23.6	1.175	26.8	0.856
Nigeria	12.2	1.102	60.0	2.991	6.5	0.324	14.2	0.454
Mali	10.7	0.961	15.9	0.793	29.7	1.475	23.2	0.743
Madagascar	10.3	0.927	14.9	0.744	28.3	1.406	37.9	1.211
Rwanda	10.3	0.925	16.6	0.825	21.3	1.059	43.8	1.400
Ghana	9.8	0.888	20.7	1.034	28.5	1.414	38.8	1.241
Sierra Leone	9.5	0.856	24.4	1.215	24.1	1.199	42.5	1.358
Burkina Faso	9.3	0.841	16.7	0.834	19.9	0.991	38.1	1.218
Uganda	**8.2**	**0.740**	**11.4**	**0.567**	**35.2**	**1.750**	**45.9**	**1.468**
Congo, Dem. Rep.	7.2	0.650	28.4	1.415	16.8	0.837	39.5	1.263
Guinea-Bissau	7.2	0.648	9.9	0.492	19.8	0.986	33.5	1.070
Chad	6.1	0.547	17.7	0.884	25.0	1.244	35.7	1.141
Average	**12.1**	**1.1**	**23.5**	**1.2**	**24.1**	**1.2**	**33.5**	**1.1**

Source: Teera (2003)

From the findings; Uganda's tax effort index for whole taxes and taxes on salary were below unity (1), whilst indices for international taxes and goods and services' tax are over unity (1). The general tax effort index of 0.7 for Uganda was too below the other compared countries, which was 1.1 and this shows that Uganda had exploited the suggested tax potential below average hence the chances of increasing tax revenue is possible. The low index for revenue taxes suggests that the country is supposed to elevate the efforts towards income taxes. The opposite was true for countries with tax effort indices above unity. Examples of those countries appear to be wisely using their tax bases to elevate revenue and vice versa. Countries with a tax effort over the unity can be used as operating on regions not allowed of the Laffer Curve (Abu-Hammour, 1997) hence a tax rate would benefit such countries in an aim to raise extra revenue (Gandhi et al., 1987). Additionally, countries with less than unity tax effort can be seen as working on a normal range of the Laffer curve so that an elevated tax rate would be feasible in order to elevate revenue

Challenges with Uganda's Tax System

Tax Evasion

Tax evasion is regarded to be a serious issue to those dealing with taxation issues of a country due to the harmful effects; it is assumed that to have on a tax system and revenue in general. An obvious effect of tax evasion on the government is the loss of tax revenue. The fact that some income becomes untaxed and also some indirect taxes such as VAT and expurgate duties are evaded; leading to the conclusion that tax revenues are lower than if everyone had paid their taxes.

Huge Shadow Economy

Over a period of time a growing amount of attention has been fixated on the conclusion that a significant and a growing hidden economy subsist. Several authors who have tried to deal with it have concluded to a common conclusion that the issue of the hidden economy cannot be laid off as quantitatively trivial, especially due to some of the analytical work done on the topic has revealed interesting issues.

The main inducement for the effort to measure the extent of the hidden economy has been dominated by the issues of fiscal authorities concerned with the cost of tax revenue through tax evasion. Efforts to estimate the quantity of the tax revenue loss have formed appalling numbers of lost tax revenue. Other issues include:

i. Uganda has a slim tax base where taxes can be gathered.
ii. Uganda Revenue authority (URA) has significantly improved the tax administration but there are several issues to be looked at in order for URA to gather taxes from all earning an income. A significant number of income earners especially in the agriculture region are not taxed. The government should develop a modern and rational and efficient tax system.
iii. Several businesses in Uganda are quite small but have profits and majority of the businesses are not taxed, including Matatu operators, bars, butchers among others.
iv. Women are significant in several businesses but there is no deliberate move in bringing women to the formal economy.
v. Several taxes are not understood by taxpayers and erstwhile y staff from URA thus creating resentment. There is a need for a constant awareness program being issued by the URA.
vi. Most workers in Uganda are usually employed in the agriculture or in informal, small enterprises. The economic activities in this sectors of the economy is generally not

recorded meaning that several people who work and earn an income here are not taxed therefore keeping a potential amount of the tax base out of the tax net.

vii. Corruption is a main issue in broadening the tax of base of Uganda, there are several cases of stolen public funds seen in the media.

viii. There are also issues of uneven income supply in Uganda. There are several Ugandans who do not earn a dollar per day.

ix. There is no clear way of accounting how taxes have been used hence taxpayers do not see the goodness of paying taxes.

x. Bureaucratic systems at URA. Delayed decision making by URA staff for instance some complaints which could have taken days end up taking months to be resolved. This is in spite of the reforms made at URA.

xi. Governmental systems at URA. Delayed decision making by the staff for example some complaints which could have be done days will take taking months to be resolved in spite of the reforms made at URA.

xii. Huge exemptions due to political benefaction. This has led to taxes being waived for the selected few yet other businesses are failing due to high taxes. In tax exemption there is no system criteria followed.

xiii. Thoughtful budget proposals designed at politicking. Some budget suggestions are approved politically rather than on economic grounds thus hindering revenue collection.

xiv. Non-accounting public utilities and goods. Though this is the best judgment of performance, delivering service in Uganda is still lacking, for instance, Roads that were budgeted for in previous financial years have not yet been competed without reasons. This makes it hard to persuade people to pay taxes and declare incomes because they are not seeing results.

xv. Some clearing agents and firms over charge their customers and make abnormal profits whilst paying less to URA. Thus both the customer and URA tend to loose.

xvi. FDI promotion opting for tax incentives resulting into gross loss of revenues as huge investments goes untaxed.

CONCLUSION

Despite undertaking more favorable tax reforms over the last three decades, Uganda's fiscal policy is marked by high budget deficits, suffers substantial imbalance in the tax incidence, low impact and limited tax base, low levels of tax compliance and high tax evasion as well as tax avoidance. It is worth noting that these are challenges that are also experienced by other neighboring countries in the East African region. Nevertheless, these characteristics are synonymous with a country whose tax system falls below the criteria of a good tax system and may therefore need continuous review. Recommendations are made to improve the country's tax system such as efforts to create tax awareness**,** impose stiff penalties for tax offenses such as tax evasion, ensure effective tax administration, proper tax collection mechanisms, and having independent and transparent tax authorities.

REFERENCES

Abu-Hammour, M. (1997), The Measurement of Taxable capacity in Jordan. Unpublished Thesis.

Almunia, M., Gerard, F., Hjort, J., Knebelmann, J., Nakyambadde, D., Raisaro, C., & Tian, L. (2017). An analysis of discrepancies in tax declarations submitted under value-added tax in Uganda. International Growth Centre Project Report.

Elshout, C. (2020). The impacts of a PAYE reform on taxable earnings in Uganda-Maria Jouste (University of Turku, UNU-WIDER).

Engle, R.F., and Granger, C.W.J. (1987), Co- integration and Error Correction: Representation, Estimation and Testing, Econometrica, 55(2), 251-276.

Gandhi, V.P. (1987), Supply-Side Tax Policy: Its Relevancy to Developing Countries. IMF.

Kangave, J. (2005). Improving tax administration: A case study of the Uganda Revenue authority. Journal of African Law, 49(2), 145-176.

Mawejje, J., & Francis Munyambonera, E. (2016). Tax revenue effects of sectoral growth and public expenditure in Uganda. South African Journal of Economics, 84(4), 538-554.

Mugalula, J. (2010). Anti-Tax Avoidance Provisions Under the Income Tax Act Cap 340: A Perspective Analysis. The Uganda Law Society-Lawyers' Voice.

Tanzi, V. and Zee Howell, H. (2000), Tax Policy for Emerging markets: Developing Countries, National Tax Journal, 53(2), 299-322.

Teera, J. M. (2003). Determinants of tax revenue share in Uganda. Centre for Public Economics Working Paper 09b-03, University of Bath.