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Tax Revenue Mobilisation in Malawi

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Submitted for the degree of Doctor of Philosophy in Development Studies

University of Sussex

July 2019

I hereby declare that this thesis has not been and will not be submitted in whole or in part to another University for the award of any other degree.

Signature.....

UNIVERSITY OF SUSSEX

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DOCTOR OF PHILOSOPHY IN DEVELOPMENT STUDIES

TAX REVENUE MOBILISATION IN MALAWI

Summary

This thesis was initially motivated and guided by a general interest in tax revenue mobilisation in Malawi, with a bias towards believing that levels of revenue collection were too low, and a tentative focus on the question of how they could be increased. As the research progressed, and particularly as more attention was paid to comparisons between Malawi and other African countries, my primary interests shifted. It became increasingly clear that Malawi is, in some respects, relatively successful in terms of the amount of tax revenue collected, and how it is collected. The thesis aims to answer three interrelated questions regarding this success:

- Why did the ratio of tax-to-GDP in Malawi increase significantly between 2005-2011, from 10% to 17.5% of GDP? (Note, it has remained high since 2011)
- Why, in recent years (since 2009), has the tax-to-GDP ratio been significantly higher in Malawi than in comparable sub-Saharan African (SSA) countries?
- Why and how, since 1964 – the first year for which relevant data is available – have the Malawian tax authorities been able to raise an unusually high proportion of total tax revenue (and total revenue) from direct taxes, i.e., taxes on income (especially Pay As You Earn and not corporate tax). These figures are high for Malawi compared to most SSA countries, and indeed to low-income countries generally.

I used a range of methods and approaches to address these questions. The most notable of which are as follows:

- A study of historical documents relating to taxation in Malawi.
- Cross-country intra-Africa comparisons of ‘tax morale’ using Afrobarometer data.
- A survey of business people in Malawi, aimed at understanding their tax morale.
- A series of interviews with staff of the Malawi Revenue Authority and other

specialists to try to understand how taxes are collected and processed by the Authority in practice.

- Statistical analysis to extend and update an influential paper by Mkandawire (2010) that suggests that differences in national tax performance in contemporary Africa, to a large extent, reflect the character of the colonial economy.

It was difficult to reach clear answers to the three main research questions. The conclusions of the study are as follows:

- The drastic increase in tax-to-GDP ratio between 2005-2011 in Malawi was significantly influenced by the introduction of value added tax (VAT) in 2005, which resulted in improvements in the collection of both direct and indirect taxes.
- The higher tax-to-GDP ratio in Malawi compared to other SSA countries since 2009 can be partially explained by the ability of the Malawi Revenue Authority to collect significant revenue from large companies and their employees, despite the use of tax collection methods that appear to be lagging behind technological frontiers.
- The ability of the Malawi Revenue Authority (and previous tax administrations) to collect significant revenue from large companies and their employees also explains the high reliance on direct tax in Malawi. This ability is facilitated by Malawi's economic structure, where income has been concentrated in the hands of a few businesses and individuals, during both the colonial and the post-colonial eras.

The thesis contributes to the debate on tax revenue mobilisation in SSA countries by providing evidence from Malawi on how a low-income country with a pattern of tax administration that by normal measures is considered ineffective, is effective in practice. In addition, it contributes to the meagre evidence on the role of the post-colonial political and economic structure in Malawi in making it possible for the government to continue to collect significant revenue, especially through taxing income.

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Dedication

This work is dedicated to my late mother and brother, Eluby Tsamila Ligomeka and Elijah Ligomeka, who would have been proud to see me get this far.

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List of Abbreviations

AGD	Accountant General Department
ATAF	African Tax and Administration Forum
ASYCUDA	Automated System for Customs Data
CIT	Corporate Income Tax
CSR	Centre for Social Research
DPP	Democratic Progressive Party
DTD	Domestic Tax Division
EFD	Electronic Fiscal Device
GDP	Gross Domestic Product
ICTD	International Centre for Tax and Development
IT	Information Technology
ITAS	Integrated Tax Administration System
IMF	International Monetary Fund
LMICs	Low- and Middle-Income Countries
LRE	Labour Reserve Economies
LTU	Large Taxpayer Unit
MCP	Malawi Congress Party
MK	Malawi Kwacha
MW	Malawi
MRA	Malawi Revenue Authority
NLRE	Non-Labour Reserve Economies
OECD	Organisation for Economic Cooperation and Development
PAYE	Pay As You Earn
PIT	Personal Income Tax
POA	Performance Outcome Area
SACU	Southern Africa Customs Union
SAP	Structural Adjustment Programmes
SSA	Sub-Saharan Africa
TADAT	Tax Administration Diagnostic Assessment Tool
VAT	Value Added Tax
WB	World Bank

WHT

Withholding Tax

WVS

World Value Survey

Glossary

Corporate Income Tax (CIT): Income tax on the profits of companies.

Customs Duties: Taxes on goods imported into a country.

Direct Tax: Taxes imposed on income, capital gains, and net worth (gift tax, death duties, and property tax are also considered direct taxes).

Hut Tax: Type of poll tax levied on inhabited dwellings or huts generally introduced at an early stage in the development of an economy when it is not feasible to introduce an income tax.

Income Tax: A tax levied on the income of individuals and/or corporations; may be applied to gross (total) income or net income (gross income less deductions for certain expenses).

Indirect Tax: Tax imposed on certain transactions, goods or events. Examples include value added tax (VAT), sales tax, excise duties, and stamp duty.

Input Tax: Term used in connection with VAT to denote the tax embodied in purchases made by a trader or entrepreneur who will usually be able to obtain credit for the tax that their suppliers have paid on the goods supplied to them, which form their 'input'.

Non-Taxes: Recurring income earned by the government from sources other than taxes.

Output Tax: Term used in connection with VAT to denote the tax payable on the sales of goods or services by those who are subject to the tax and in contrast to the input tax, for which credit will be available.

Personal Income Tax (PIT): A tax paid by people on the money they earn, as opposed to a tax that a company pays on its profits.

Poll Tax: A tax levied as a fixed sum on every liable individual.

Process Performance: A measure of how efficient or effective a process is.

Sales Tax: Tax imposed as a percentage of the price of goods (and sometimes services). The tax is generally paid by the buyer but the seller is responsible for collecting and remitting the tax to the tax authority.

Surtax: An additional tax rate added onto the rate of an existing tax.

Taxable Capacity: Refers to the predicted tax-to-gross domestic product (GDP) ratio

that can be estimated with the regression, taking into account a country's specific macroeconomic, demographic, and institutional features.

Tax Compliance: The degree to which a taxpayer complies (or fails to comply) with the tax rules of their country, for example by declaring income, filing a return, and paying tax in a timely manner.

Tax Effort: An index of the ratio between the share of the actual tax collection in gross domestic product (GDP) and the predicted taxable capacity.

Tax Evasion: Generally means illegal arrangements where tax liability is hidden or ignored, i.e., the taxpayer pays less than they are legally obliged to pay, hiding income or information from the tax authority.

Tax Morale: Taxpayers' perceptions of and attitudes towards paying and evading taxes.

Taxpayer: An individual who pays taxes.

Tax-to-GDP Ratio: A ratio of a nation's tax revenue relative to its gross domestic product (GDP).

Value Added Tax (VAT): a specific type of turnover tax levied at each stage in the production and distribution process. Although VAT ultimately applies to the individual consumption of goods or services, liability for VAT is with the supplier of the goods or service. VAT normally utilises a system of tax credit to place the ultimate and real burden of the tax on the final consumption and to relieve the intermediary of any final tax cost.

Chapter 1: Introduction and Thesis Overview

1.1 Introduction

I began the research for this thesis with a general interest in tax revenue mobilisation in Malawi, with a bias towards believing that levels of revenue collection were too low, and a tentative focus on the question of how they could be increased. As I progressed in the research, and particularly as I paid more attention to comparisons between Malawi and other African countries, my interests shifted. I came increasingly to appreciate that Malawi is, in some respects, a relative success in terms of the amount of tax revenue collected, and how it is collected. Accordingly, the thesis examines the issue of tax revenue mobilisation in Malawi by seeking to answer three interrelated questions about this relative success:

- Why did the ratio of tax-to-GDP (measured as total central government revenues divided by gross domestic product) in Malawi increase significantly between 2005-2011, from 10% to 17.5% of GDP? (Note, it has remained high since 2011)
- Why, in recent years (since 2009), has the tax-to-GDP ratio been significantly higher in Malawi than in comparable sub-Saharan African (SSA) countries?
- Why and how, since 1964 – the first year for which relevant data is available – have the Malawian tax authorities been able to raise an unusually high proportion of total tax revenue (and total revenue) from direct taxes, i.e., taxes on income (especially Pay As You Earn and not corporate tax). These figures are high for Malawi compared to most SSA countries, and indeed to low-income countries generally.

The literature (Gupta, 2007; Stotsky & WoldeMariam, 1997; Fjeldstad & Rakner, 2003; Keen & Mansour, 2010; Mkandawire, 2010; Moore & Wilson, 2017) suggests that some of the major factors that determine the level and structure of tax collection in SSA include: tax policy; the efficiency and effectiveness of the tax administration; the willingness of taxpayers; colonial legacy; and the introduction of value added tax (VAT). Accordingly, to answer the three main research questions of this thesis, I explore four hypotheses:

- The introduction of value added tax (VAT) in 2005 led to an increase in the collection of all taxes.

- Malawians are exceptionally good and willing taxpayers (i.e., tax morale is high) relative to the populations in other SSA countries.
- Malawi has an effective tax administration.
- Malawi's colonial history may have steered the country towards a relatively higher tax revenue performance.

1.2 Malawi Overview

Malawi is a low-income landlocked country in Southern Africa, bordered by Mozambique, Zambia, and Tanzania. It has an estimated population of 18.6 million people as of 2017 (NSO, 2019). The country had been colonised by the British since 1891 and gained its independence in 1964 (Thomas, 1975). Between 1964–1994, it was a one-party nation-state under the rule of Dr. Kamuzu Banda. In 1994, the country became a multiparty state; a total of six presidential elections have been held since the dawn of the multiparty era.

Malawi's economy is largely centred around rain-fed agriculture, which accounts for 80% of livelihoods, 64% of the country's formal work force, and 28% of its GDP (Government of Malawi, 2017; World Bank, 2018). The reliance on agriculture in Malawi dates back to the colonial era. During the colonial period, as the country did not have minerals and other natural resources (McCracken, 2012), few Europeans (settlers) settled there. The small community of settlers who, prior to 1891, were involved in ivory trade, turned to commercial farming (mainly coffee, cotton, tobacco, and tea) (McCracken, 2012). McCracken (2012) further notes that vast tracts of land were appropriated by the few settlers and turned into estates. The extant African population was then forced to work in the estates and not allowed to grow commercial crops. In addition, a hut/poll tax (see Chapter 6) was introduced to force the Africans to work on the estates, as they needed to find money to pay the taxes levied by the colonial state. Thus, the colonial state was politically oppressive and economically exploitative which resulted in continuous conflict between the settlers and the Africans.

After independence, President Banda's rule deepened political oppression and economic exploitation through a system of patronage, terror, and the promise of social and economic development (Kaunda, 1995). Kamuzu encouraged estate farming at the expense of the smallholder agriculture and promoted few private businesses owned by himself or his close allies (see Chapter 6). As of 2018, the private sector in Malawi was

still underdeveloped and mostly defined by parastatals (state-owned companies with political connections) and family businesses (such as Mulli Brothers, Siku Transport, OG Group of companies, and Crossroads Hotels). The agricultural sector has remained highly dualistic, with smallholder farmers growing mainly subsistence crops and the estates concentrating on producing tobacco, tea, and sugar for export. Another characteristic of the economy is its perpetual indebtedness, indicated by the tendency of the government to rely on domestic and foreign borrowing to finance its expenditures (Khomba & Trew, 2018)

Between 1964–1980, Malawi’s economic performance was good, with its average real GDP growth being 5% (Chipeta, 1998). However, in the 1980s, Malawi was affected by exogenous economic shocks and geopolitical events in the SSA region (oil shock, war in Mozambique, and droughts) (see Chapter 2), which led to a deterioration in Malawi’s development-oriented performance (Chipeta, 1998). In response, the country started pursuing the “good governance” agenda (putting in place policies to fight corruption, market liberalization, and democratic reforms) (Anders, 2009), with the aim of ensuring that the available resources would be well managed in order to achieve maximum economic development. Between 1994–2002, the country implemented far-reaching reform programmes under the guidance of the World Bank and the IMF. The reforms focused on privatisation, deregulation, and liberalisation (Anders, 2009). These reforms included the following: the establishment of the Medium-Term Expenditure Framework (MTEF) (the MTEF enabled the government to plan and prioritise expenditure in line with the available financial resources over a period of three to five years); the introduction of institutional development projects which aimed to eliminate “ghost workers” (fictitious employees existing only on the payroll); public expenditure reviews; institutional reviews; the privatisation of statutory corporations; the introduction of meritocracy and a retrenchment exercise; the introduction of the Malawi Revenue Authority, a semi-autonomous revenue collecting institution (Anders, 2009).

Thus, this thesis focuses on a country which is low-income, highly reliant on agriculture, where income concentrated in few businesses and individuals, and has been implementing various reforms to ensure good governance.

1.3 Background to the Research

When I began conducting my research for this thesis, my aim was to investigate the reasons for low tax collection in Malawi. I am employed by the Ministry of Finance

in Malawi in their Revenue Policy Division (RPD). The perception within the Ministry of Finance is that the country can collect more tax revenue than it currently does. Indeed, several studies have suggested that tax collection in SSA countries, such as Malawi, is lower than it should be (Stotsky & WoldeMariam, 1997; Fjeldstad & Rakner, 2003; Keen & Mansour, 2010; Moore & Wilson, 2017). Two problems related to tax collection in SSA are widely cited in the literature:

1. Low tax compliance due to problems including corruption and the large, hard-to-tax informal sector.
2. The tax administration is generally weak.

I initially aimed to understand these problems in more depth and find ways of overcoming them. However, in the course of writing this thesis, the perspective that tax collection in low-income countries in general and SSA in particular is low was found to be an exaggeration and simplification. Upon scrutinising this issue of tax collection in SSA, I found that tax collection performance in Malawi and other SSA countries is not as low as cited in the literature. Moreover, there are three positive factors relating to tax collection in SSA in general, and Malawi in particular:

1. The tax revenue as a share of GDP in SSA has been increasing steadily since 1996 (ICTD/UNU-WIDER, 2017) despite the fact that economic growth in SSA has primarily been focused on hard-to-tax activities that are small-scale, informal, and agricultural in nature (Jayne, Chamberlin & Benfica, 2018). The increase in tax collection in SSA within this context suggests that African tax administrations are gradually learning to raise significant amounts of revenue despite the pervasive informality of their economies. In Malawi, the increase in the tax-to-GDP ratio has been greater than the average increase in other SSA countries. From 1996-2011, the tax-to-GDP ratio in Malawi more than doubled, from 8% to 17.5% (see Chapter 2).
2. Relative to other African countries, Malawi's tax effort is high. Tax effort is defined as an index of the ratio between the actual tax collection and the taxable capacity (the predicted tax-to-GDP ratio that can be estimated using regression analyses, taking into account a country's specific macroeconomic, demographic, and institutional features) (Le et al., 2012). The estimated tax effort for Malawi is usually 1 or higher (Gupta, 2007; Mkandawire, 2010; Stotsky & WoldeMariam, 1997; Langford & Ohlenburg, 2015). By contrast, most countries in SSA have tax

effort estimates of less than 1 (Fenochietto & Pessino, 2013; Mkandawire, 2010; Stotsky & WoldeMariam, 1997; Langford & Ohlenburg, 2015).

3. As will be shown in Chapter 2, relative to other SSA countries and low-income countries in general, the share of total tax revenues accounted for by direct tax in Malawi (mainly PAYE) is high. Direct taxes in Malawi contribute approximately 44% of the total central government revenue, compared to the average of 32% for SSA (ICTD/UNU-WIDER, 2017). A high reliance on direct tax is normally difficult to achieve in low-income countries such as Malawi, due to factors such as low per capita income, the administrative challenges of administering direct taxes, and the political hurdles of taxing the rich and local elites (Aizenman & Jinjarak, 2009; Junquera-Varela et al., 2017).

These examples show that tax revenue collection performance in SSA generally, and in Malawi specifically, is relatively good. However, the initial assumption that there are many problems associated with tax collection in Malawi remains valid for various reasons, including: (a) estimated taxes equivalent to 12% of GDP in Malawi are not collected due to tax non-compliance (Yikona et al., 2011), and (b) the performance of the tax administration in Malawi, the Malawi Revenue Authority (MRA), was found to be below international best practices in almost all the areas assessed by the Tax Administration Diagnostic Assessment Tool (TADAT) in 2015 (TADAT Secretariat, 2015a) (see Chapter 6).

Given these factors, the main aim of this thesis is to understand the commonly cited problems related to tax collection in Malawi in more detail and suggest ways of overcoming them. However, it is also recognised that the system has positive components, and the objectives for tax policy in Malawi (and hence, this thesis) should include finding ways of sustaining these.

1.4 Motivation

Since 2011, the Ministry of Finance has been under pressure to find alternative sources of revenue following a drastic reduction in budget support from international donors. Prior to 2011, the international budgetary support accounted for 40% of the national budget; after 2011, this decreased to 15% (Khomba & Trew, 2018). The drastic reduction in budget support provided to Malawi was the result of donor concerns regarding governance (Cammack, 2017) and ‘Cashgate’, the systematic looting of

government funds by a syndicate involving government officials and the private sector (Kayuni, 2016; Majanga, 2015).

To compensate for the drastic reduction in aid, the Malawian Government relies on borrowing. However, Malawi's debt has increased from 30% of GDP in 2011 to 54.3% in 2017 (IMF, 2017). Clearly, the current means of augmenting government finances through borrowing is not sustainable, and longer-term methods of financing government expenditure must be identified. The most reliable alternative is to increase tax revenue collection (Akitoby, 2018). Accordingly, I was motivated to conduct research on tax revenue mobilisation in Malawi with the aim of exploring some of the measures the Malawian Government may implement to increase tax revenue collection, or at least to sustain the current levels of tax collection.

1.5 Significance of the Study

The study of tax revenue mobilisation in Malawi is important for three reasons:

1. Following the reduction in international budgetary support provided to Malawi, taxation is the only option available for reliable and sustainable government financing. Thus, any factor that undermines the efforts to collect more tax revenue also undermines the capability of the government to meet its financing needs.
2. There is a growing range of literature that supports the idea that states that rely heavily on taxation to fund their activities, as opposed to relying on natural resources, wealth, or foreign aid, are more likely to build strong state structures and be accountable to their taxpayer-citizens (Prichard, 2010; Moore, 2015). Malawi has been reliant on donor aid since it gained independence in 1964 (Khomba & Trew, 2018). However, in Malawi, government accountability to its citizens is low (Tambulasi, 2011; McNeil & Male, 2010). Thus, by encouraging domestic tax collection, the state may become more accountable to its citizens.
3. Some studies have suggested that the current level of tax collection and tax structure for most countries in SSA is affected by their colonial legacy (Mkandawire, 2010; Acemoglu et al., 2001; Austin, 2008; Bolt & Bezemer, 2009; Bowden et al., 2008; Engerman & Sokoloff, 2005; Grier, 1999; Lange, 2004.; Moradi, 2008). This study provides an opportunity to trace the mechanism through which the colonial legacy works to affect tax collection, drawing on the experience of Malawi.

1.6 Structure and Overview of the Thesis

This thesis is structured into five substantive chapters, Chapters 2 to 6. Then, Chapter 7 draws some broad conclusions.

The research begins, in Chapter 2, with a broad overview of the tax system in Malawi in terms of its structure and revenue performance since the country gained independence in 1964, and a comparative analysis of tax revenue performance in Malawi and other SSA countries between 1980-2015. In addition, this chapter explores whether the introduction of value added tax (VAT) had any impact on tax revenue collection in Malawi. The main contribution of this chapter to the literature is in providing a history of tax collection in Malawi, covering policy, trends, and the drivers of those trends. This information has not previously been available for the period considered. I have identified four distinct periods in tax revenue performance in Malawi:

1. From 1964 to 1989. During this time, tax revenue as a share of GDP remained relatively stable at 10%, despite many tax policy changes.
2. From 1990 to 1995. In this period, tax revenue as a share of GDP declined due to a combination of three factors: a reduction in all major tax rates; a prolonged drought that affected the key cash crop, tobacco, thereby affecting the profitability of most major companies; and political tension, as citizens demanded a move from a one-party state to a multiparty democracy.
3. From 1996 to 2005. This was a recovery phase, during which the tax-to-GDP ratio increased from 8% to 10%. The recovery was driven by favourable weather conditions and a stable political environment (see Chapter 6).
4. From 2005 to 2011. During these years, the tax-to-GDP ratio for Malawi increased drastically, from 10% to 17.5%. The main tax policy change for this period was the introduction of value added tax (VAT) in 2005. Considering that the introduction of VAT was the only significant policy change during this period, it seems likely that the increase in tax-to-GDP ratio during this period was due to the introduction of VAT.

I also find, in this chapter, that direct tax as a share of total revenue and tax effort in Malawi were considerably higher throughout the period under study (1964-2015) compared to the average for SSA countries. The reasons why Malawi performs better

than other SSA countries are explored throughout this thesis.

Having gained insights relating to the trends, structure, and level of revenue collection in Malawi relative to other SSA countries between 1964-2015, the subsequent chapters explore, in detail, the peculiarities of the Malawian tax system, specifically: the significant increase in the tax-to-GDP ratio between 2005-2011; the high tax revenue collection in Malawi compared to other SSA countries since 2009; and the high reliance on direct tax in Malawi since 1964.

Chapter 3 reviews the existing literature on tax morale. I focus on tax morale because the good tax revenue performance in Malawi relative to other SSA countries between 2009-2015 may be due to its high tax morale, which maybe translating into high tax compliance. The key research questions addressed in this chapter are: 1) what factors shape tax morale? 2) What methods can be used to study tax morale? 3) What do we know about tax morale in SSA? The literature shows that there are three main methods that can be used to study tax morale: surveys, simulation exercises, and field experiments. Each of these methods has particular strengths and weaknesses. In terms of factors affecting tax morale, the literature highlights several types of factors, including reciprocity motivation, peer influence, and economic factors. In addition, socio-demographic factors, such as age, gender, education, and income level also influence tax morale. Furthermore, the literature indicates that the factors that affect tax morale vary based on place (or country). The key gap in the tax morale literature is that the majority of existing studies focus on less pragmatic factors, such as the social-psychological or social-demographic factors influencing tax morale. However, for more practical or policy-oriented research, there is a need to focus more on more pragmatic factors, such as the differences in tax morale among different categories of taxpayers, as this would provide policymakers with a clear picture of which category of taxpayers they need to concentrate on to improve tax morale where it is low.

Chapter 4 is an empirical investigation of tax morale in Malawi and other SSA countries. To this end, two different pieces of analysis are presented in this chapter. The first compares Malawi's tax morale with the average tax morale for SSA countries.¹ I used survey data collected by the Afrobarometer to conduct a multivariate regression analysis to try to determine whether Malawians are any more or less willing taxpayers

¹ Only those countries that are included in Afrobarometer surveys are included in the analysis.

than the population in other countries, and what may explain the differences in tax morale (if there are any) between Malawi and the other SSA countries. Tax morale is measured as follows: people's views about whether it is "wrong and punishable," "wrong but understandable," or "not wrong at all" to not pay taxes owed to the government. The tax morale model that I developed as part of this study is tested using Afrobarometer survey data; Round 5 (R5) (conducted in 2012/13), Round 6 (R6) (conducted in 2014/15), and the merged R5 and R6 data. I used Afrobarometer data from R5 and R6 as well as the merged data because, while evaluating the Afrobarometer data for suitability for this analysis, I discovered that responses to both R5 and R6 surveys in Malawi and Madagascar were heavily influenced by the prevailing political and economic situation at the time the two surveys were conducted, such that there is significant variation in tax morale between the two rounds in these two countries. The huge variation in tax morale in these two countries during these rounds occurred because R5 surveys were conducted in the midst of political unrest, economic slowdown, and corruption scandals in both countries. This resulted in lower than normal tax morale in R5. By contrast, the R6 survey was conducted following a change in government in both Malawi and Madagascar, the economic challenges were being addressed, and the prosecution of most of the individuals involved in corruption was underway. This resulted in higher than normal tax morale in Malawi and Madagascar in R6. This finding suggests that the true level of tax morale (given a relatively stable economic and political environment in the country, as is usually the case) is somewhere in between the results for R5 and R6 for both Malawi and Madagascar. Accordingly, the merged data for R5 and R6 serves as an appropriate proxy for tax morale when the two countries (Malawi and Madagascar) are stable. The main finding from the regression analysis is that tax morale in Malawi is within the average for countries in SSA. This result suggests that Malawians are not any more or any less willing taxpayers than the populations in other SSA countries.

The second piece of analysis explores the potential differences in tax morale among business people in Malawi. It seemed plausible that, although the overall tax morale is not notably higher in Malawi compared to the average tax morale for SSA countries, it might be sufficiently high among certain business taxpayers within Malawi to at least partially explain the relatively high overall tax revenue performance. To test this hypothesis, I conducted a survey of businesses people operating in Lilongwe and Blantyre, the two largest cities in Malawi. Similar to the comparative analysis, I estimated

a regression equation with tax morale as the dependent variable and various factors, such as corruption and tax knowledge, as the independent variables. In addition, variables were included that would help identify variances in tax morale among the surveyed business people, such as the size of the business, where the business is located, whether the business is registered with the revenue authority or not, and the sector in which the business operates. The results showed that business people operating in Blantyre have a higher tax morale than those operating in Lilongwe; large businesses have a higher tax morale than small businesses; and businesses in the construction sector have a lower tax morale than businesses in other sectors. These results suggest that, while tax morale in Malawi is not significantly different from the average tax morale for countries in SSA, there are certain business people in Malawi who have a higher tax morale. While a higher tax morale (attitude) does not necessarily translate to tax compliance (behaviour), it is more likely that the taxpayers with high tax morale in Malawi (those operating in Blantyre, and taxpayers classified as large) may be partly contributing to the good tax revenue performance in Malawi.

Chapter 5 explores the question: to what extent do the tax administration processes followed by the Malawi Revenue Authority affect the level of tax revenue collection and tax structure in Malawi? This question emanates from the apparent paradox of the poor performance of the MRA even by the standards of low-income countries on the one hand, and the institution's effectiveness at capturing a relatively high proportion of taxes in GDP and the collection of a high proportion of direct taxes through corporate income tax (CIT) and personal income tax (PIT), on the other. The analysis is based on the Tax Administration Diagnostic Assessment Tool (TADAT) priority outcome areas (POA). However, due to data access limitations, only four out of the nine POAs are assessed, namely: taxpayer registration and data management; detection and prosecution of tax fraud through tax audit; handling of administrative appeals and complaints through a dispute resolution process; and provision of services and assistance to taxpayers, such as taxpayer education. The analyses presented in this chapter were based on qualitative data collected through semi-structured interviews with MRA officials, analysis of MRA documents (such as annual reports, strategic frameworks, and management reports), the TADAT report for Malawi, and information collected through a survey of business people in Malawi. The main finding of this analysis is that the paradox described above is largely explained by the relative efficiency of the Large Taxpayer Unit (LTU). The LTU is

responsible for only 2% of total taxpayers, yet collect 70% of total tax revenue. However, the LTU itself is not well-equipped from a technological perspective. It relies heavily on some very basic software for recording taxpayer information. However, the LTU staff interact closely with the staff of large companies, and understand their clients' businesses quite well, hence the success in collecting significant revenues from the small number of taxpayers. This brings me to a set of issues explored further in Chapter 6: the long-standing economic dominance in the Malawi economy of a few large firms; and the fact that, unlike in many countries, these firms have been unable to use their economic dominance to avoid taxes on a large scale.

Chapter 6 explores the hypothesis that Malawi's high reliance on direct tax relative to other SSA countries is due to its colonial legacy. The main question addressed in this chapter is how Malawi, a low-income country with weak tax administration, is able to collect more revenue from direct taxes than other countries in SSA.

A review of the literature shows that Malawi is not the only country in southern Africa that collects a high proportion of its revenue from direct tax, but part of a cluster. Other such countries include Zambia, Zimbabwe, Botswana, and South Africa. There are a number of explanations for the differences in tax collection and tax structure among African countries, including: influence of the Southern African Customs Union (SACU); size of the mining sector; institutional spill-over; and colonial legacy. The most plausible explanation among these is the colonial legacy theory, well-articulated by Mkandawire (2010). Mkandawire (2010) classified countries of Africa according to structures of colonial economic exploitation, with three categories: labour reserve economies, cash crop economies, and concessional companies. Of these, labour reserve economies are better able to raise revenue and more reliant on direct taxes. Mkandawire (2010) then carried out a statistical analysis for the period 1984-2004, using two categories, labour reserve economies and non-labour reserve economies (cash crop and concessional companies) for comparison, and found that the colonial-era difference in economic structure and consequent revenue potential endured into the post-colonial era.

Mkandawire (2010) classified Malawi as a labour reserve economy, which suggests that the high dependence on direct tax in Malawi stems from its colonial legacy. To determine whether this argument is valid in this regard, I explored and extended Mkandawire's theory in various ways. First, I looked deeper (1910-1960) into records of revenue-raising in Malawi and seven other countries in SSA and found that Mkandawire's

argument holds. Then, I looked at comparative revenue performance for 25 countries in Africa for a more recent period (2000-2015), and again found that Mkandawire's pattern holds, but is generally weakening. However, it holds more strongly for Malawi. The explanation for why that might be appears to lie in unusual pattern of ownership of major economic assets in Malawi after independence, where most assets were owned by either Dr Banda, the first president of independent Malawi, or his close allies. Broadly speaking, this was a continuation of a colonial-type economy. The ownership of assets by a few individuals created a situation where it was (and still is) possible for tax collectors to closely 'manage' the few large firms and collect a lot of direct tax from both their profits and from 'Pay As You Earn' (PAYE) on their employees. Thus, Malawi's history and its economic structure contribute significantly to explaining the high ratio of direct tax in total revenue.

Chapter 7 concludes this thesis with a summary of the findings, policy implications, contributions to the body of knowledge, and areas for further research. After exploring the four hypotheses, the main conclusions are that: 1) the introduction of VAT in 2005 significantly contributed to the drastic increase in tax-to-GDP ratio between 2005-2011 in Malawi; 2) the higher tax-to-GDP ratio in Malawi compared to other sub-Saharan African countries since 2009 can be partially explained by the ability of the Malawi Revenue Authority to collect significant revenue from large companies and their employees, despite the use of tax collection methods that appear to be lagging behind technological frontiers; and 3) the ability of the Malawi Revenue Authority (and previous tax administrations) to collect significant revenue from large companies and their employees also explains the high reliance on direct tax in Malawi. This ability is facilitated by Malawi's economic structure, where income has been concentrated in the hands of a few businesses and individuals during both the colonial and the post-colonial eras.

Other than providing the main conclusions from the various analyses conducted in this thesis, I also highlight one key issue that emerges from this thesis. The thesis raises a much broader question about revenue collection in low-income countries. It is shown in the thesis that a low-income country, namely Malawi, collects significant amount of tax revenue and is highly reliant on direct taxes even though its tax administration is weak and it has a large informal sector. This suggests that low-income countries with weak tax administrations can still collect significant amount of revenue from direct taxes

provided the government is committed and able to tax the sectors with the greatest potential for revenue generation, typically large businesses and individuals with a high income.

Chapter 2: Taxation in Malawi: A Comparative Perspective

2.1 Introduction

Taxes are conventionally divided into two categories: direct tax, a tax which is levied on the income or profits of the person who pays it, rather than on goods or services; and indirect tax, a tax on goods and services collected by an intermediary (such as a retail store) from the person who bears the ultimate economic burden of the tax (Obwona & Muwonge, 2002). In Malawi, the major direct taxes are corporate income tax (CIT) and personal income tax (PIT). Other direct taxes in Malawi include withholding tax (WHT)², rental income tax, tax on interest from banks, and turnover (presumptive)³ tax. The major indirect taxes in Malawi are value added tax (VAT), excise taxes (which are applied to selected items such as alcohol, cigarettes, and motor vehicles) and taxes on international trade transactions (i.e., import duty, import VAT, and import excise duties).

This chapter provides a historical overview of tax collection in Malawi, focusing on trends and policy changes made to both direct and indirect taxes since Malawi gained independence in 1964, and a comparative analysis of tax collection performance between Malawi and other SSA countries for the period 1980-2015. The main questions driving this chapter are:

- What are the major tax policy and administrative policy reforms that have been implemented by the Malawi Government since the country gained independence in 1964?
- How different is the tax revenue performance in Malawi from that of other sub-Saharan African (SSA) countries for the period 1980-2015?

There are four key findings:

- First, throughout the years following independence, direct and indirect taxes each accounted for approximately 50% of total tax revenue. By contrast, most SSA countries, and low-income countries in general, have a higher reliance on indirect

² A withholding tax (WHT) is an income tax to be paid to the government by the payer of the income rather than the recipient of the income. The tax is thus withheld or deducted from the income due to the recipient.

³ This refers to the income tax paid by businesses whose annual turnover is less than MK10 million (£10,000) in Malawi. The turnover tax rate is 3% of gross income while the standard income tax rate for businesses is 30% of profits.

taxes (Figure 2.3). However, Malawi is not the only country in SSA with this unusual characteristic; South Africa, Zimbabwe, Zambia, and Namibia are other countries in SSA with a higher reliance on direct tax relative to the average for SSA countries.

- Second, the tax-to-GDP ratio in Malawi from the time of independence until the mid-1980s was relatively stable, at around 10%. It fluctuated between 10% and 12% in the mid-1980s despite the dramatic increases in tax rates during this period, which indicates significant inefficiencies in the tax system. This was followed by a decline in the 1990s, when the tax-to-GDP ratio decreased to 8% due to political tension and a reduction of tax rates under the structural adjustment programmes (SAPs). Between 1995 and 2005, the tax-to-GDP ratio recovered to 10% and continued to increase thereafter, reaching 17.5% by 2011, due possibly to the introduction of VAT in 2005 and the establishment of the Large Taxpayer Unit within the Malawi Revenue Authority in 2007. The significant increase in tax-to-GDP ratio between 2005-2011 is unusual and provides an interesting insight, since most sharp increases in tax-to-GDP ratio are short-lived and unsustainable (Shalizi & Thirsk, 1990; Bird, 2013; Gaspar et al., 2016).
- Third, when compared to other SSA countries, Malawi has a slightly higher tax-to-GDP ratio, which has been higher than the average for both low- and lower-middle-income countries since 2009 (Figure 2.4).
- Fourth, Malawi's tax effort, the ratio between the share of the actual collected tax in GDP and the predicted taxable capacity – the predicted tax-to-GDP ratio that can be estimated with regression, taking into account a country's specific macroeconomic, demographic, and institutional features (Le et al., 2012) – is usually estimated to be close to 1 or above 1, when most SSA countries have a tax effort significantly below 1. This implies that Malawi utilises well its tax base to increase tax revenues (Stotsky & WoldeMariam, 1997).

The remainder of this chapter is organised as follows. The next section is a discussion of tax policy reforms undertaken in Malawi between 1964-2015. Malawi's tax structure and tax revenue performance are then compared to those of other SSA countries. The chapter concludes with a discussion of the peculiarities of tax collection in Malawi.

2.2 Tax Policy Reform Between 1964-2015

Malawi gained independence from Britain on 6 July, 1964 (Thomas, 1975). At the time of independence, direct (mainly CIT and PIT) taxes accounted for 50% of total tax revenue (Shalizi & Thirsk, 1990). Most of the PIT revenue came from workers in the public sector and large companies, while the CIT revenue came from a few large private firms in primary processing and distribution (Shalizi & Thirsk, 1990). However, between 1964-1979, the country was able to meet its revenue needs, as domestic revenues were supplemented by grants and concessional loans⁴ (Chipeta, 1998). Consequently, between 1964-1980, very few changes were made to the tax policy and tax administration (Chipeta, 1998). The main tax policy changes included an increase in CIT rate from 35% to 40% in 1970; an increase in excise tax rate on alcohol from 5% to 8% in 1971; the introduction of a sales tax (known as surtax) at 5% in 1971; an increase of surtax from 5% to 10% in 1972; and, an increase in CIT and PIT rates from 40% to 45% in 1978 (Chipeta, 1998).

More frequent tax policy changes commenced in 1979-1990 in response to a number of internal and external stressors. These stressors included: first, the drought of 1979-1980, which reduced food production and led to increased public expenditure on food imports (Chipeta, 1998). Second, the Mozambique Civil War, which was fought between 1977-1992 (Hanlon, 2003). During this war, the direct railway line between Malawi and Mozambique, which was used to conduct foreign trade, was destroyed. Consequently, Malawi had to use longer trade routes, such as through South Africa and Tanzania, which inevitably raised transport costs (Chipeta, 1998). The war in Mozambique also increased the spending on defence, as it was feared that the war may overflow to Malawi (Chipeta, 1998). Third, there was a global economic recession between 1973-1975, and again between 1980-1981 (Chamley et al., 1985). These periods of recession resulted in reduced availability of grants and concessional loans, such that the Malawian Government had to focus on domestic revenue mobilisation to meet its expenditure needs (Chipeta, 1998). In response, the Malawian Government began to increase all tax rates and introduce new taxes. Between 1980-1985, the surtax (or sales tax) rate increased from 15% to 25%, both CIT and PIT increased from 40% to 50%

⁴ This refers to the loans that are extended on terms substantially more generous than market loans. This concession is achieved in the form of either through interest rates below those available on the market, grace periods, or a combination of both.

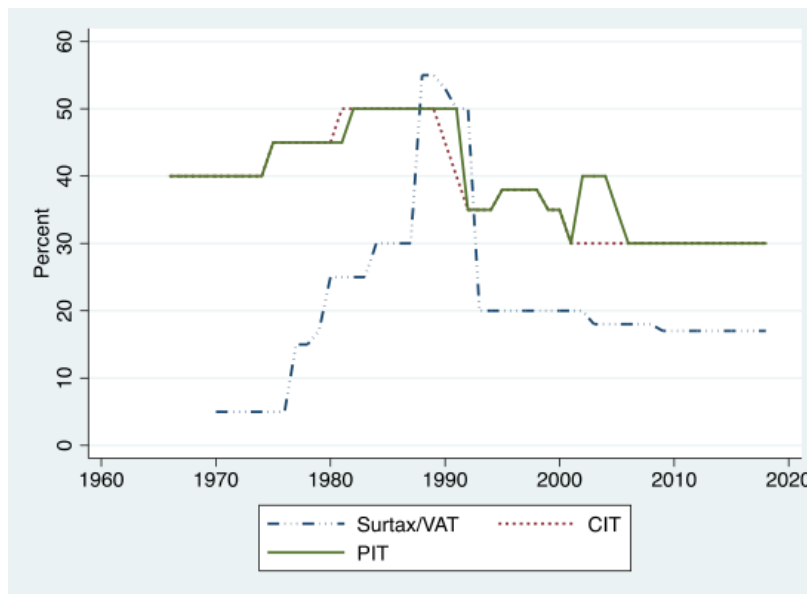
(Table 2.1), and trade taxes increased from an average of 40% to 85%. New taxes that were introduced included a temporary import levy and accommodation and refreshment tax in 1982, an export levy in 1984, and withholding taxes on non-wage incomes, which was levied on temporary workers, in 1985 (Chipeta, 2002).

Despite these changes, the tax-to-GDP ratio was volatile, increasing from 10% to 12% in 1985 and 1986, then reducing to 10% in 1987 and 1988, before rising again to 12% in 1989 (Table 2.4). In light of the volatility of tax collection in the 1980s it became clear to the Malawian Government that the tax system had several weaknesses that needed to be rectified (Chamley et al., 1985). The government therefore requested the assistance of the IMF and the World Bank (WB), who conducted studies on how to improve the tax system in Malawi (Chamley et al., 1985). Some of the main observations from the IMF and WB studies were that:

1. all tax rates were too high, which limited investment and consumption;
2. the tax system did not adhere to one of the important tenets of a good tax system of equity, whereby the rich should pay a higher rate of income tax than the poor;
3. the tax administration was weak because of, among other things, lack of a unique taxpayer identification system, no computerisation of certain processes, and a high number of unskilled officers.

Following these observations, in 1989, the Malawian Government, with assistance from the IMF and the WB, began reforming the tax system under the structural adjustment programmes (SAPs) (Shalizi & Thirsk, 1990).

The first phase of the reform programme involved the reduction of tax rates. Over a period of three years (1990-1993), the maximum marginal rates for all major taxes (PIT, CIT, surtax) were reduced by almost 50% (Figure 2.1).

Figure 2. 1: Evolution of rates of major taxes in Malawi (1970-2015)

Data source: Chafuwa, Kenani, & Kaunda (2017) and Chipeta (1998)

Figure 2.1 shows the movement in VAT, CIT, and PIT rates between 1969-2015. All the major taxes increased between 1970-1989. The surtax increased from 5% in 1971 to 55% in the late 1980s, before it was reduced significantly to 20% in 1991. Similarly, both CIT and PIT rates were increased in the 1980s from 40% to 50%, before being reduced to 35% in 1990.

Between 1995-2015, there were few tax policy changes. The most significant was the introduction of VAT in 2005 (Chafuwa, Kenani, & Kaunda, 2017). The type of VAT system introduced in Malawi is called invoice-based credit (Le, 2003). Under this method, a company at any stage of the production–distribution chain charges its customers the VAT on its output, submits the tax to the MRA, and then makes a claim for the VAT already paid on its input purchase. For example, if t_1 and t_2 are the tax rates on output and input VAT, respectively, then the tax liability is the difference between $(t_1 \times \text{output})$ and $(t_2 \times \text{input})$. In principle, invoice-based credit VAT is supposed to be self-enforcing, as a taxable business can claim for a refund on the input VAT only if the claim is supported by purchase invoices (Le, 2003). To a large extent, this mechanism provides strong incentives for firms to keep invoices of their transactions and is an efficient means for tax authorities to check and cross-check to facilitate enforcement (Le, 2003). However, in practice, it has been found that the tax is not fully self-enforcing: officers in

the MRA claim that they sometimes discover “ghost”⁵ invoices and false refund claims,⁶ indicating that either not all the VAT due has been paid, or the taxpayer may have over claimed the input VAT.

Until 1993, the focus of the reforms was tax policy and not tax administration. Thus, only minor changes were made to tax administration. These changes included the introduction of a withholding tax on wages and salaries called ‘Pay As You Earn’ (PAYE) in 1983, the computerisation of some activities (such as taxpayer registration) in 1990, and the establishment of a Tax Policy Unit in the Ministry of Finance in 1996 (Chafuwa, Kenani, & Kaunda, 2017). As a result, the second phase of the tax system reform programme, which began in 1995, focused on tax administration (Chipeta, 1998). The main tax administration reform was the creation of the semi-autonomous revenue authority, the Malawi Revenue Authority (MRA). The MRA Act was passed in 1998 and the institution started operating in 2000 (Chafuwa, Kenani, & Kaunda, 2017).

Since its inception, the MRA has continued the reform process, and has implemented the following:

1. The introduction of the Automated System for Customs Data (ASYCUDA) in 2002, for better management of customs data.
2. The introduction of the Large Taxpayer Unit (LTU) in 2007 to ensure that large taxpayers⁷ receive special attention tailored to their needs.
3. The merging of the Income Tax and VAT divisions in 2010 to form the Domestic Tax Division (DTD) to streamline functions.
4. The introduction of electronic fiscal devices (EFDs) in 2014 to enhance VAT collection.
5. The introduction of cargo scanners in 2014 to address smuggling and under-declaration of values of imported goods.
6. The introduction of e-payments in 2016 to reduce compliance costs by allowing online tax payments.
7. The interface of the domestic tax system and the Road Traffic Directorate in 2017

⁵ Fake invoices

⁶ The checking of VAT invoices is done randomly, as the process is manual. It is therefore very likely that not all “ghost” invoices are discovered.

⁷ See Chapter 6 for a detailed discussion regarding the classification of taxpayers according to the MRA

to address vehicle smuggling challenges.

Despite the various tax administration reforms, tax administration in Malawi is still considered weak (IMF, 2015). Indeed, a study conducted by the TADAT Secretariat found that MRA performance, in almost all of the 25 areas assessed, was below international standards (TADAT Secretariat, 2015a).⁸

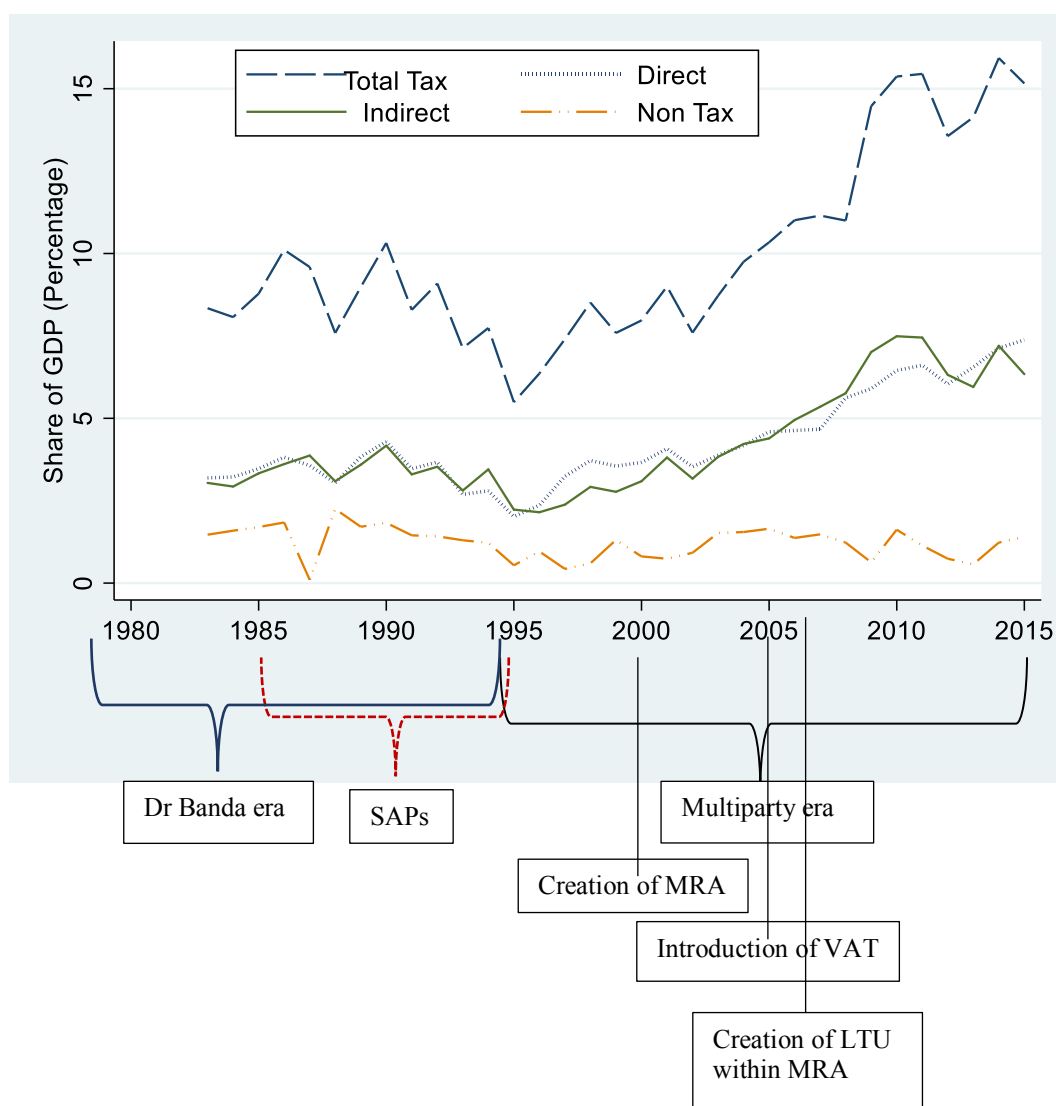
2.3 Tax Structure and Tax Revenue Performance in Malawi

2.3.1 Tax Structure

Taxes are the main source of domestic revenue in Malawi, the other source being non-taxes. By definition, non-taxes are recurring income earned by the government from sources other than taxes (Keen & Baunsgaard, 2005). Examples of non-taxes include police fees and fines, sale of government property, and fees for the processing of passports and driving licences. Between 2000-2015, taxes have contributed 92% of total domestic revenue in Malawi. During this period, the contribution of direct and indirect tax to total tax revenue was 44% and 48%, respectively. The remaining 8% was collected from non-taxes. Figure 2.2 shows the trends for total tax, direct tax, indirect tax, and non-taxes as a share of GDP between 1980-2015, and the various policy and administrative changes that occurred during this period. It should be noted that between 1964-1994, Malawi was under one-party rule by Dr Kamuzu Banda. From 1994 onwards, Malawi became a multiparty state.

⁸ Chapter 6 evaluates the performance of the MRA.

Figure 2. 2: Timeline of the changes in total tax, direct tax, indirect tax, and non-taxes in Malawi between 1980-2015 (all presented as share of GDP) and major political, tax policy, and tax administration changes that occurred during this period.



Source: Author's calculation using ICTD/UNU-WIDER Government Revenue Dataset (2017)

Figure 2.2 shows that, between 1980-1990, both direct and indirect taxes as a share of GDP were slightly below 4%. They both declined between 1990-1995 to approximately 2% of GDP, before gradually increasing between 1996-2004 to reach 5%, then significantly increased between 2005-2011 to reach 7.5%. Trade taxes, however, have been declining since 1990. As a share of GDP, trade taxes accounted for 2% of GDP prior to 1990, but declined thereafter to reach 1.6% of GDP in 2015. Similarly, the share of non-taxes in GDP declined from 2% prior to 1985, to 1.6% in 2015.

2.3.2 Tax Revenue Performance

One commonly used measure of a country's (tax) revenue performance is the tax-to-GDP ratio. To calculate the tax-to-GDP ratio, total tax revenue of a country is divided by its GDP (as highlighted in Chapter 1, in this thesis, tax-to-GDP ratio refers to the ratio of total central government revenue to GDP). Accordingly, when a country's tax revenues grow at a slower rate than its GDP, the tax-to-GDP ratio drops. By contrast, if tax revenue grows quicker than the GDP, the ratio increases. Figure 2.2 shows the trends in tax-to-GDP ratio in Malawi between 1980-2015, and the major drivers of changes in the tax-to-GDP ratio. The figure shows that Malawi's tax-to-GDP ratio has been volatile. Although the tax-to-GDP ratio averaged 10% between 1969-1985, it fluctuated between 10% and 12% between 1985-1990, before gradually declining to 8% between 1990-1995. From 1996 onwards, tax-to-GDP ratio increased, peaking at 17.5% in 2011.

The decline in tax-to-GDP ratio between 1990-1995 seems to have been driven by three factors:

1. Tax reform: As discussed in Section 2.2, Malawi began implementing SAPs in the late 1980s, and between 1990-1993, all major tax rates were halved. This sudden decrease in tax rates may have contributed to the decline in tax-to-GDP ratio.
2. Drought: In 1990 and 1991, Malawi experienced severe drought (Pauw et al., 2010); this affected agriculture, the key economic sector in Malawi. Agriculture and agricultural processing generate almost half of the GDP and 80% of total export earnings and employment in Malawi (Pauw et al., 2010). However, this sector is highly dependent on rain-fed agriculture (Nhamo et al., 2016), such that droughts affect agriculture productivity, which in turn affects the profitability of agro-based industries and, hence, tax collection.
3. Political tension: After independence in 1964, Malawi was a one-party state under the leadership of Dr Kamuzu Banda. However, in the late 1980s, a majority of the people were dissatisfied with Dr Banda's leadership; this dissatisfaction was attributed to his autocratic leadership (Moto, 1998). Moto (1998) observes that the judicial system was not independent, there were countless arrests and detentions without trial, and there was a lack of freedom of expression and association. It was estimated that, between the late 1960s and 1992, more than 2,000 Malawians were imprisoned in various parts of the country for political reasons (Moto, 1998). Dr Banda's autocratic behaviour, coupled with Malawi's poor economic performance throughout the 1980s, culminated

in political tension in the early 1990s (Chirwa, 2004). Citizens wanted the government to call a referendum so that they could choose to either remain in the one-party state under Dr Banda or move to a multiparty democracy. University students, urban workers, and political activists led frequent demonstrations and urban riots (Newell, 1995). The prolonged violence and riots between 1990-1994 affected the productivity of industries and revenue collection (Chirwa, 2004).

The years between 1995-2004 were a period of recovery in terms of revenue collection. Political stability returned, and the weather conditions were favourable (Chipeta, 1998; Chafuwa, Kenani, & Kaunda, 2017). The creation of the Tax Policy Unit within the Ministry of Finance in 1996, and the creation of the Malawi Revenue Authority which started operating in 2000, may also have helped the recovery by improving tax administration. However, no records on tax administration performance are available for this period (1995-2004) to support or dispute this theory.

The period between 2005-2011 was a turning point in the history of tax collection in Malawi. As shown in Figure 2.2, between 1964-2004, tax revenue as a share of GDP had only deviated by 2% from the average of 10%. However, since 2005, tax revenues as a share of GDP increased steadily by an average of 1% per year, reaching 17.5% in 2011. The ratio has remained relatively stable at 17.5% thereafter.

The drastic increase in the tax-to-GDP ratio in Malawi between 2005-2011 does not correspond to the rate of around 10% as was the case between 1964-2004. As Moore (2014) observed, not a single African revenue authority has exhibited a continually improving revenue performance for as long as a decade. It has also been noted that tax collection generally involves short periods of growth followed by a long period of inertia, and increases in tax-to-GDP ratio are achieved only in very small steps (Bird, 2013). Two other studies also point out that increases in tax-to-GDP ratio greater than 3% over relatively short periods (of less than five years) are usually difficult to sustain in the long term (Shalizi & Thirsk, 1990; Gaspar et al., 2016). Thus, the 7.5% increase in tax-to-GDP ratio in Malawi within six years, and its sustained stability, thereafter, is unusual. The most likely explanation for the drastic increase in the tax-to-GDP ratio during this period is the introduction of VAT in 2005 (Chafuwa, Kenani, & Kaunda, 2017). There are four avenues through which this may have been achieved:

- As already discussed, to a larger extent, the invoice-based VAT introduced in

Malawi is self-enforcing. This is because taxpayers have an added incentive to file a return to the revenue authority so that they can claim the input VAT. In addition, taxpayers are more likely to pay taxes other than just VAT once they start remitting VAT to the MRA.

- The possibility of crosschecking VAT documents to identify errors. On the 25th of every month, taxpayers who operate VAT in Malawi are supposed to submit a VAT return to the MRA. The VAT return shows all the transactions that the taxpayer has processed during that month and the amount of VAT to be remitted to the MRA. The MRA claims that the VAT returns are usually checked to ensure that the correct amount of VAT is remitted, and errors reported to the taxpayer for correction (MRA, 2016). The frequent checking of VAT returns may, therefore, be driving high tax compliance since taxpayers know that their VAT documents are frequently checked for errors, which may motivate them to ensure declarations of all their transactions, not just VAT, are correct.
- VAT generates more data to cross-check against other returns, such as corporate income tax. The VAT return contains additional information, such as the quantity of goods bought and sold in a month by a business. It is this information that the tax authority, the MRA claims to use (Chafuwa, Kenani, & Kaunda, 2017) to produce a rough estimate of profits, and hence the income tax to be paid by a taxpayer.
- When VAT refund claims exceed MK2 million (£2,000), the accounts are automatically flagged for audit before the claim is paid. However, in many instances, the audits are programmed to cover other taxes, not just VAT. Thus, enforcement of VAT indirectly leads to enforcement of other taxes, such as direct taxes.

The positive impact of VAT on revenue collection is not limited to Malawi. In an empirical micro study by Keen and Lockwood (2010) involving 143 countries over the period 1975-2000, it was also found that the VAT is a “money machine”: it had helped countries generate more revenues than they would had without the VAT in place. Accordingly, the significant increase in tax-to-GDP ratio between 2005-2011 is mainly attributed to the introduction of VAT.

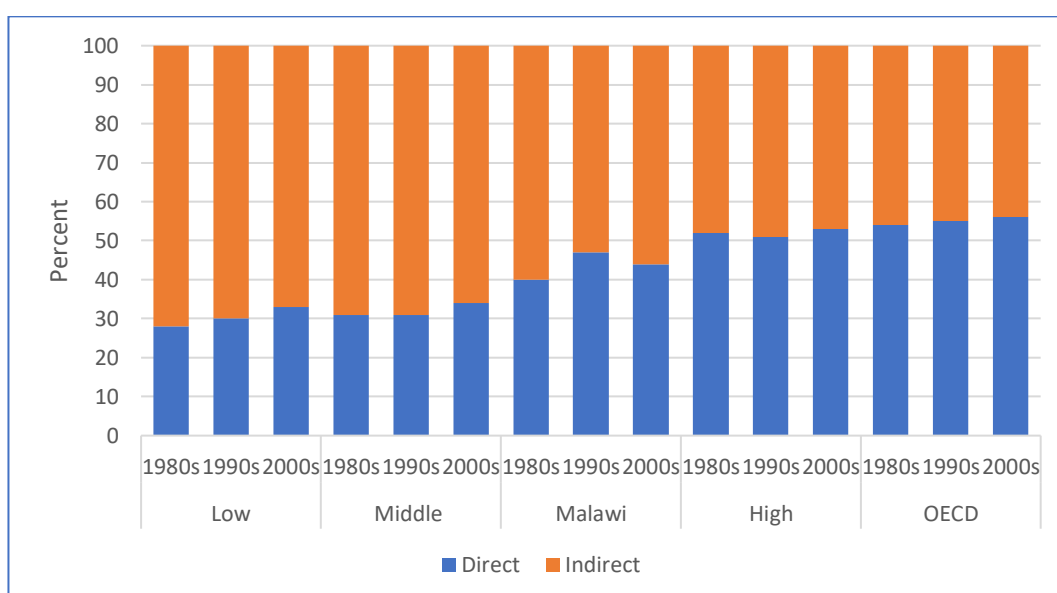
2.4 Comparative Analysis of Revenue Performance in Malawi and Other SSA Countries

In this section, the Malawian tax system is compared with those of other low-income SSA countries, focusing on three aspects: tax structure, the tax-to-GDP ratio, and tax effort.

2.4.1 Tax Structure

In general, low-income and middle-income countries rely more on indirect taxes than direct taxes compared to high-income or OECD countries which have a balanced reliance on direct and indirect taxes (Figure 2.3).

Figure 2. 3: Proportion of direct tax and indirect tax in total tax revenue by decade and income group



Source: Author's calculation, using ICTD/UNU-WIDER Government Revenue Dataset (2017)

Figure 2.3 shows that in low and middle-income countries, on average, direct tax collection averaged approximately 30% of total tax revenue between 1980-2015. By contrast, in Malawi, the contribution of direct taxes to total revenue was 40% in the 1980s, increasing to 48% in 1990, before declining to 44% during the 2000s. The level of direct tax collection in Malawi is well above that of low and middle-income countries but slightly below that of high-income and OECD countries, which collect a little over 50% of their tax revenue from direct taxes.

The literature suggests that the main reasons for low-income countries having low reliance on direct taxes are as follows:

1. In low-income countries, agriculture contributes a large share of GDP, and industry and manufacturing only a small share (Morrissey et al., 2016). The larger agricultural sector reduces taxable capacity, as agriculture is mainly a subsistence activity in low-income countries and is difficult to tax directly. On the other hand, a large industrial sector is easier to monitor and tax, and a larger share of manufacturing in GDP indicates economic development and a larger formal (taxable) sector. Thus, a low-income country with a high reliance on direct tax indicates that the tax administration is able to collect more direct taxes from a small-industry sector, i.e. the manufacturing sector, or the agricultural sector.
2. Low-income countries have low per capita income. Accordingly, income tax collection is low because the income tax base is small (ATAF, 2018).
3. There are a number of administrative challenges that hinder the effective enforcement and collection of income taxes, such as the political hurdles associated with taxing the rich or local elites (Junquera-Varela et al., 2017).

Focusing on countries in SSA, Table 2.1 shows the average proportion of direct, indirect, trade, and non-taxes in GDP for 30 African countries⁹ between 1980-2015. The countries are arranged in descending order based on their reliance on direct taxes (refer to column seven). Notably, only four countries (South Africa, Zimbabwe, Malawi, and Zambia) source more than 30% of their revenue from direct taxes. The other countries have a high reliance on either indirect taxes or non-taxes. Resource-rich countries, such as Botswana, Angola, Gabon, and Nigeria, collect over 80% of their revenue from non-taxes.

⁹ Countries were chosen according to the availability of the data; the countries included in this analysis had at least 27 years of data available.

Table 2. 1: Total revenue, direct tax, indirect tax, trade tax, and non-taxes as a share of GDP in various African countries (1980-2015 average)

Country	Total revenue /GDP (%)	Direct tax /GDP (%)	Indirect tax /GDP (%)	Trade taxes /GDP (%)	Non-tax /GDP (%)	Direct tax/total revenue (%)
South Africa	30.68	14.99	9.27	0.98	5.44	49
Zimbabwe	22.87	10.68	7.37	3.21	1.61	47
Malawi	11.15	4.21	4.14	1.58	1.22	38
Zambia	15.98	5.93	4.34	3.09	2.62	37
Namibia	31.03	8.95	7.22	10.32	4.53	29
Tanzania	11.32	3.12	6.07	1.13	0.99	28
Rwanda	11.81	3.22	4.69	2.75	1.15	27
Swaziland	23.17	6.26	2.4	13.31	1.2	27
Sierra Leone	7.62	2.01	2.17	2.64	0.8	26
Mozambique	13.07	3.36	6.07	1.68	1.96	26
Burundi	15.13	3.82	6.66	3.26	1.41	25
Uganda	9.62	2.32	5.27	1.32	0.7	24
Senegal	18.31	4.35	8.63	3.87	1.47	24
Benin	13.66	3.23	5.61	3.4	1.41	24
Togo	19.37	4.43	6.65	4.1	4.19	23
Mali	15.28	3.43	5.91	1.99	3.94	22
Central African Republic	10.06	2.24	3.6	3.05	1.17	22
Burkina Faso	11.6	2.58	4.35	3.11	1.55	22
Madagascar	10.24	2.16	2.77	4.84	0.48	21
Côte d'Ivoire	19.73	4.14	7.29	4.85	3.45	21
Gambia	15.43	3.17	5.1	4.68	2.48	21
Mauritania	20.42	3.94	5.42	2.86	8.19	19
Chad	9.6	1.82	1.92	1.54	4.32	19
Lesotho	40.4	7.05	6.69	22.2	4.46	17
Cameroon	16.39	2.62	5.6	2.15	6.02	16
Gabon	28.44	3.31	3.28	5.08	16.77	12
Guinea Bissau	8.66	1	1.82	2.66	3.19	12
Botswana	41.81	4.81	2.55	8.23	26.22	12
Nigeria	19.16	1.51	1.21	1.11	15.34	8
Angola	36.45	1.92	2.52	2.07	29.95	5
Average	18.75	4.34	4.96	4.23	5.22	24

Source: Author's calculation using data from the ICTD/UNU-WIDER Government Revenue Dataset (2017)

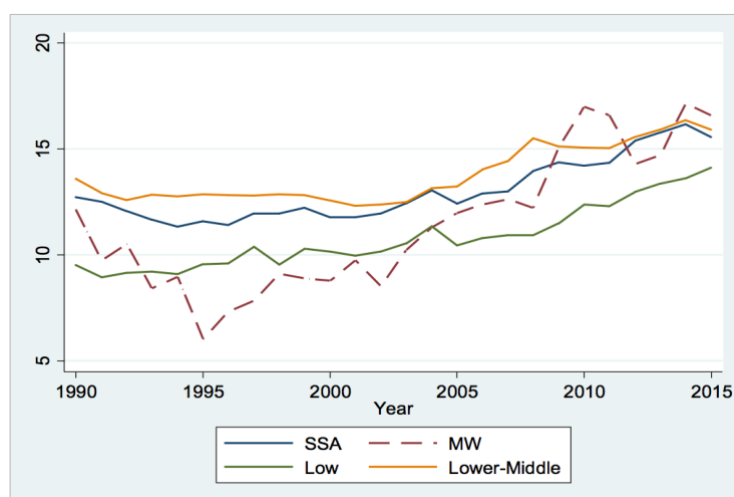
Table 2.1 shows that the average proportion of direct tax to total revenue from 1980-2015 for the countries under review was 24%. South Africa had the highest proportion of direct taxes in total revenue, followed by Zimbabwe, Malawi, and Zambia. It was expected that South Africa would have a high proportion of direct tax collection in

total revenue as it is classified as an upper-middle-income country by the IMF,¹⁰ based on gross national income (GNI) per capita. However, Malawi and Zimbabwe are classified as low-income countries, and Zambia is classified as lower-middle-income country. Therefore, it would be expected that these three countries would collect much more tax revenue from indirect taxes or non-taxes than from direct taxes, as is the case now. In Chapter 6, this phenomenon is explored in further detail to determine why some low-income countries, such as Malawi, Zimbabwe, and Zambia, are highly reliant on direct tax when the majority of low-income countries are more reliant on indirect tax or non-taxes.

2.4.2 Tax-to-GDP Ratio

The tax-to-GDP ratio in many regions, including low-income countries, lower-middle-income countries, and countries in SSA, has been increasing since the 1990s (IMF, 2011; Keen & Mansour, 2010). However, from a comparative perspective, the increase in tax-to-GDP ratio in Malawi since 2009 has been above average for SSA, low income and lower-middle income countries (Figure 2.4).

Figure 2. 4: Tax-to-GDP Ratio in low-income countries (low), lower-middle-income countries (lower-middle), SSA, and Malawi (MW) (1990-2015)



Source: Author's calculation using ICTD/UNU-WIDER government revenue dataset, 2017

Note: I define the abbreviations in Figure 2.4 as follows: SSA = Sub-Saharan Africa; Low = low-income countries; lower-middle = lower-middle-income countries; MW=Malawi.

Figure 2.4 shows that, prior to 1992, Malawi's tax-to-GDP ratio was slightly

¹⁰Refer to <https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups>

higher than the average for low-income countries but below the average for low, lower-middle income countries, and SSA countries. Malawi's tax-to-GDP ratio declined in the early 1990s, and by 1993 it had decreased to below the average for both low income, lower-middle income and SSA countries. However, the tax-to-GDP ratio began to increase in 1996. By 2005, it surpassed the average for low-income countries. In 2009, Malawi's tax-to-GDP ratio was higher than the averages for SSA, low-income countries, and lower-middle-income countries. Thus, in recent years, Malawi's tax revenue collection performance has been better than most countries in SSA, and better than low- and lower-middle-income countries.

2.4.3 Tax Effort

Tax effort is calculated and defined as actual tax collection as a share of expected tax collection, factoring in various features of the economy, such as level of development, share of agriculture in GDP, trade openness, and the share of GDP contributed by industry (Mkandawire, 2010). A tax effort greater than 1 indicates that the country is collecting more tax than the characteristics of the economy suggest it should. A tax effort of less than 1 indicates that, considering the prevailing characteristics of the economy, the country is collecting less tax than is potentially available.

Estimating tax effort for countries in SSA, including Malawi, is beyond the scope of this thesis. However, a review of the literature on tax effort estimates shows that, relative to other SSA countries, Malawi's tax effort is high. The estimated tax effort for Malawi is close to 1 or higher, whereas most countries in SSA have a tax effort estimate of less than 1. For instance, Fenochietto and Pessino (2013) estimated the tax effort for Malawi for 2012 to be 0.97, while the tax effort for other countries in SSA, specifically Madagascar, Tanzania, Uganda, and Ethiopia, were 0.62, 0.50, 0.64, and 0.62, respectively. Gupta (2007) on the other hand, estimated the tax effort of Malawi to be 1.55, while the tax effort for other low-income countries, specifically Madagascar, Mozambique, and Sierra Leone, were 0.72, 0.77, and 0.79 respectively.

2.5 Conclusion

This chapter has provided an overview of the current tax system in Malawi and presented the historical factors that have contributed to its current state. It has highlighted that Malawi has undergone numerous tax policy and administration changes since gaining independence in 1964. Soon after independence, a period of few tax policy reforms was followed by a period of increasing tax rates in the early 1980s, mostly driven by the need for more tax revenue as a result of various economic stressors. The changes in the tax policy undertaken in the late 1980s and early 1990s under the auspices of the IMF and WB were aimed at creating a fairer and more efficient system, promoting industrial development, securing revenue sustainability, and creating stability in the tax system (Chipeta, 1998). This was achieved by reducing the rate of import duties and income taxes, and by broadening the tax base. From the mid-1990s, the focus of reforms shifted from tax policy changes to improving tax administration. Administrative changes included the formation of the Tax Policy Unit in the Ministry of Finance in 1996, and the introduction of the semi-autonomous revenue authority, the Malawi Revenue Authority, in 2000.

The volatility of tax collection in Malawi over the years has also been noted. In general, the tax-to-GDP ratio averaged 10% between 1964-1990. This ratio declined to 8% between 1990-1994 due to several factors, including a significant reduction in tax rates; drought, which affected agricultural productivity, which in turn affected the profitability of agricultural industries; and political tensions that resulted in riots, which negatively affected the productivity of businesses, as production decreased during a period of protests and instability. The tax-to-GDP ratio began to gradually rise in 1996 due to greater political stability (when the one-party system changed to a multiparty democracy). Between 2005-2011, the tax-to-GDP ratio increased sharply, from 10% to 17.5%. Unexpectedly, this high tax-to-GDP ratio has been sustained ever since. Both indirect and direct taxes drove the increase in tax revenue from 2005, driven mainly by the introduction of VAT in 2005.

Aside from the dramatic increase in tax-to-GDP ratio between 2005-2011, the peculiarities of Malawi's tax structure has also been noted. Specifically, the country collects a considerably high amount of tax from direct taxes, despite being classified as a low-income country. While this phenomenon is unusual, it is not exclusive to Malawi. Other low-income SSA countries, such as Zambia and Zimbabwe, also see a high

proportion of their tax revenue collected from direct taxes (explored in further detail in Chapter 6).

This chapter has shown that Malawi's tax-to-GDP ratio between 2009-2015, and its tax effort between 1980-2015, are better than in most other SSA countries. The tax-to-GDP ratio is above average for countries in SSA, and for lower-income and middle-income countries more widely. Tax effort in Malawi is also higher than would be expected for a low-income country in SSA; it has been estimated to be close to 1 or above by two separate researchers, whereas in SSA and other low-income countries this ratio is generally much lower.

Overall, this chapter has highlighted and evidenced the following peculiarities in the Malawi tax system: a sharp increase in tax-to-GDP ratio between 2005-2011; a high tax effort, indicating that the majority of potential taxes are collected; and a tax structure with an unusually high dependence on direct tax for a low-income country. While the drastic increase in tax revenue is a more recent phenomenon, more likely a result of the introduction of VAT in 2005, the high reliance on direct tax has been present since Malawi gained independence in 1964.

Chapter 3: Understanding Tax Morale

3.1 Introduction

Four hypotheses are explored in this thesis, with the aim of finding answers to the main research questions. Chapter 2, while providing details about the peculiarities of the Malawian tax system, also explored how the introduction of VAT in 2005 may have significantly contributed to the increase in tax-to-GDP ratio in Malawi. This chapter and the next explore the second hypothesis, that Malawians are more willing taxpayers (i.e., tax morale is high) than the populations in other SSA countries. This chapter is a literature review of tax morale, while the next is an empirical investigation of tax morale in Malawi and other SSA countries.

It is first important to note that, as also highlighted by Kangave, Mascagni, and Moore (2018), researchers seeking to understand why some people pay taxes and others do not often use the phrase ‘tax morale’ interchangeably with the phrase ‘tax compliance’, yet these are distinct concepts. Tax non-compliance refers to the failure to freely and completely fulfil all tax obligations as per the law (James & Alley, 1999). Thus, tax compliance relates to the behaviour of taxpayers. Tax morale, on the other hand, refers to peoples willingness (or perceived moral obligation) to pay tax (Frey, 1997; Torgler, 2006; Alasfour et al., 2016; Kangave, Mascagni & Moore, 2018). Thus, tax morale relates to people’s attitudes. The relationship between tax morale and tax compliance is that high tax morale has been noted to be one of the key determinants of tax compliance (Torgler, 2006; Alm and Torgler, 2011; Luttmer & Singhal, 2014)

Tax non-compliance is a significant problem for many counties, including Malawi. Yikona et al (2011) estimated that taxes equivalent to 12% of GDP in Malawi are not collected as a result of tax non-compliance. In attempting to explain why some people choose not to pay taxes, Allingham and Sandmo (1972) assumed that taxpayers are rational individuals who seek to maximise the utility of their taxable income. They weigh the benefits and the cost of compliance with those of non-compliance. Individuals are more likely to be non-compliant when the expected penalty and probability of being caught are low in comparison to the benefits gained by non-compliance. Accordingly, Williams and Horodnic (2017) suggest that to increase tax compliance, tax administrations must ensure that the benefits of non-compliance are outweighed by the

cost of non-compliance through increased penalties and a high probability of detection of non-compliant taxpayers.

However, Slemrod (2007) found that reducing tax non-compliance is not a simple matter of applying higher penalties and/or increasing the probability of detection. This is because the percentage of taxpayers audited in a country is usually less than 1%, and the penalties for tax evasion¹¹ are only a fraction of the price of unpaid taxes (Slemrod, 2007). Even for fraudulent evasion, the penalty seldom exceeds more than the amount of unpaid taxes, and these penalties are infrequently imposed. In addition, civil penalties on non-fraudulent evasion are even smaller (Torgler, 2011). Alm et al. (1992) and Torgler (2007) also point out that the main issue regarding tax compliance is not why so many people are cheating the system (i.e., why some people do not pay taxes); instead, they argue that the real puzzle seems to be how little evasion occurs (i.e., why so many people do pay taxes).

The realisation that more people pay their taxes than is predicted by the Allingham and Sandmo (1972) model prompted the search for alternative factors that consider the non-pecuniary (non-economic or non-monetary) factors that might have an impact on tax compliance decisions. Alm and Torgler (2011) refer to the non-pecuniary influences on the tax compliance decision as tax morale. In this thesis, I adopt the definition of tax morale used by Frey (1997), Torgler (2006), Alasfour et al. (2016) and Kangave, Mascagni, and Moore (2018): to mean people's willingness to pay tax.

A high tax morale in Malawi relative to other SSA countries would suggest that tax compliance is also high. I chose to focus on tax morale and not on tax non-compliance because, like any other illegal activity, such as prostitution, studying tax non-compliance is difficult. Studies that attempt to study tax non-compliance usually rely on audit data. However, it would not have been possible for me to gain access to audit data for most (if not all) SSA countries, considering that disaggregated taxpayer data is normally confidential and only accessed in some instances by researchers after lengthy discussion with the revenue authority and the fulfilment of certain legal requirements by the researcher (Mascagni, Nell, & Monkam, 2017). Therefore, due to the impossibility of

¹¹ Tax evasion consists of illegal and intentional actions taken by individuals and firms to reduce their legally due tax obligations, under-reporting incomes, sales, or wealth, by over-stating deductions, exemptions, or credits, or by failing to file appropriate tax returns (Alm, 2012).

studying tax non-compliance, due to its illegal nature and the challenge of accessing audit data, I chose to focus on tax morale.

This review of tax morale will provide the foundation and framework for assessing tax morale in Malawi in the context of other SSA countries. Accordingly, the following literature review aims to answer the following questions:

1. How can tax morale be studied (methods used to study tax morale)?
2. What factors shape tax morale (the theoretical framework of tax morale)?
3. What is known about tax morale in SSA (the empirical evidence)?

Four main conclusions are drawn:

1. There are three main methods of studying tax morale: survey, simulation experiments, and field experiments.
2. Many factors impacting tax morale have been identified in the literature, and there is empirical evidence showing how the various factors impact tax morale.
3. The extent to which a factor impacts tax morale in different countries is not always the same.
4. Most of the studies of tax morale or compliance focus on the psychology of individual taxpayers (and hence assume that tax morale or compliance is an individual decision rather than an institutional decision), and on the personal attributes of taxpayers (e.g age, gender, education) rather than on the features of their business or occupation that might impact tax morale and tax compliance.

The remainder of this chapter is organised as follows. The next section is a review of the methods used to study tax morale. This is followed by a review of the different factors that have an impact on tax morale, the empirical findings related to these factors, and the empirical findings of tax morale studies conducted in SSA. The key findings of the literature review on tax morale are summarised in the conclusion.

3.2 Methods Used to Study Tax Morale

As mentioned above, three main methods are used to study tax morale: surveys, simulation exercises, and field experiments (Kangave, Mascagni, & Moore, 2018). These are addressed in detail in the following subsections.

3.2.1 Surveys

The use of surveys to investigate tax morale involves asking individuals about their experiences, perceptions, and attitudes towards the tax system, and can be conducted using questionnaires, interviews, observation, and content analysis (De Vaus, 2013). The main advantage of surveys in the study of tax morale is that they make it possible to obtain a wide range of information about respondents and examine whether and how a wide range of variables are correlated with the responses to questions. This allows researchers to investigate several hypotheses about the factors associated with tax morale (Torgler & Schneider, 2007). A critical limitation of surveys is that it is difficult to verify much of the information provided (Kelley et al., 2003), particularly when researching sensitive subjects, such as tax payments. Individuals may be cautious in their responses, wanting to avoid implicating themselves in any wrongdoing. Researchers studying tax morale have tried to circumvent this problem by using indirectly phrased questions about tax morale (Ali et al., 2013), which are more likely to elicit honest answers. Instead of asking respondents about their own tax behaviour, researchers ask questions about the behaviour of other people. For instance, the Afrobarometer (2014) used the question: “Why do some people choose not to pay taxes that they owe to the government?”

3.2.2 Simulation Experiments

In studies of tax morale that use simulation experiments, researchers place subjects in hypothetical situations and ask them to presume that they are taxpayers (Kangave, Mascagni, & Moore, 2018). They then observe subject’s behaviour when they are asked to make decisions related to paying taxes. Mascagni (2018) points out that the typical simulation experiment involves a group of students who are faced with the decision of how much income to report, based on a set of given variables including, for example, the tax rate, the probability of audit, and sanctions. The artificial setting allows the researcher to change these variables and to observe how the participants’ decisions vary in response. The key advantage of simulation experiments is that researchers can accurately detect actual behaviour because they have an idea of the (nominal) income and tax liability of each participant (Choo et al., 2014). In addition, behaviour is easier to observe in this artificial setting than in the real world because, in the real world, information about taxpayers’ assets, income, tax liabilities, and tax payments are often not observable (Franzoni, 1998). The main disadvantage of the simulated setting is

validation of the results, since the behaviour of participants in a simulated setting may not mirror their behaviour in reality (Torgler, 2003b). This is because, in the simulation experiment, the individuals involved know that they are part of a study and may behave differently than they would under the pressures of real life. As a result, behaviour in the artificial environment is likely to differ from actual decisions when faced with a real social context and real consequences of wrongdoing (Mascagni, 2018).

3.2.3 Field Experiments

Field experiments examine intervention in the real world (naturally occurring environments) rather than in artificial conditions, such as those used in simulation experiments (Mascagni, 2018). Field experiments on tax morale typically involve measuring the effects of interventions (such as messages sent to taxpayers) by the revenue authorities on actual taxpaying behaviour (Blumenthal et al., 1998; Hallsworth et al., 2014; Castro & Scartascini, 2015). An example of such a field experiment is where a researcher, with the help of the revenue authority, sends messages to taxpayers appealing to their conscience by, for example, informing them how the taxes they paid were used to build a school or a health facility. Responses to such messages, in the form of the actual tax paid, are then evaluated against the responses of a control group that does not receive any messages, or receives neutral messages, such as information about tax rates.

The advantage of using field experiments to study tax morale and taxpayer behaviour is that they are more likely to reflect real-life situations, due the natural setting (because the interface is the tax authority and not a researcher, the taxes indicate real money paid, and the consequences of wrongdoing are real sanctions and prosecution) (Mascagni, 2018). In addition, there is a lower likelihood of demand characteristics¹² affecting the results, as participants may not be aware that they are being studied (McCambridge, De Bruin & Witton, 2012). The main limitation of field experiments is that researchers can only experiment with a narrow range of variables that are under the control of the revenue authority and which it is willing to vary for research purposes (Mascagni, 2018).

There is no ideal method to study tax morale, as each of these methods has advantages and disadvantages. The method a researcher uses depends on several factors,

¹² Demand characteristics refers to an experimental artefact whereby participants interpret the experiment's purpose and subconsciously change their behaviour to fit that interpretation.

including:

1. The purpose of the research – to understand the drivers of tax morale and tax compliance, survey data may be more appropriate since survey responses reflect an individual's attitude. However, to investigate taxpayer behaviour (what people do) rather than just tax morale (people's attitudes), field experiments may be more suitable.
2. The accessibility of information – field experiments require the tax authority to cooperate in the study. The tax authority may not be willing to undertake certain exercises, such as sending messages to taxpayers using different formats (letters, or email, or phone calls) for fear that the taxpayers may later not respond to communication from the revenue authority if they find out that they were part of an experiment. The tax authority may also decline to be involved in the field experiment altogether. In such a case, other methods, such as surveys, may be more appropriate.
3. The available resources – field experiments and surveys are costly compared to simulation exercises, which can be conducted with, for instance, university students for a small or no fee at all. Thus, when there is a shortage of resources, simulation exercises may be the preferred method. In other cases, researchers may have access to secondary data from surveys, such as the World Value Survey (WVS)¹³ or the Afrobarometer data,¹⁴ which are freely available. In such cases, the researcher may opt to use the freely available data to save time and money.
4. The tax type – respondents of surveys such as the WVS and the Afrobarometer, are selected by targeting all adults of voting age. However, some taxes (such as corporate tax or PAYE) are paid by small proportions of the population. Thus, asking specific tax questions to individuals who are not subject to that particular tax may result in misreading findings. Thus, if the target is to understand factors that affect tax morale relating to a specific tax, data sources other than the secondary survey data produced by WVS or Afrobarometer should be used.
5. Time constraints – field experiments on tax morale or tax compliance take time, as they involve negotiating with the revenue authority. In addition, it typically takes at least 12 months to receive feedback once the experiment starts, as the

¹³ <http://www.worldvaluessurvey.org/wvs.jsp>

¹⁴ <http://afrobarometer.org/>

filing period for income tax, for example, is one year, and the basic method in field experiments involves comparing tax filings/declared taxes for the year the survey is conducted (T) with the previous year (T-1). By contrast, when using simulation experiments, the results are obtained within a shorter period.

3.3 Factors Affecting Tax Morale

The majority of tax morale studies are those that attempt to test whether and how certain generic features of human psychology or behaviour affect tax morale. Several factors are studied under this class of tax morale studies. The factors are usually categorised as: (1) economic deterrence; (2) fiscal exchange; (3) social influences; (4) comparative treatment; and (5) political accountability (Fjeldstad, Schulz-Herzenberg, & Hoem Sjursen, 2012).

Due to the multiplicity of factors that affect tax morale, in this chapter, I will only review those that are commonly cited in the literature and that I evaluate for Malawi and other SSA countries in Chapter 4. These factors are: economic deterrence factors; fiscal exchange factors; social influence factors; comparative treatment factors; political accountability factors; corruption; democracy; and some demographic factors, such as age, gender, and highest education level.

3.3.1 Economic Deterrence

Factors that fall under the economic deterrence category are those related to the economic model of tax compliance developed by Allingham and Sandmo (1972). As highlighted in the introduction, the economic model assumes that taxpayers are rational actors who seek to maximise the utility of their taxable income by weighing the benefits and cost of compliance against the utility of tax non-compliance. As such, they will be non-compliant when they can reasonably expect a penalty, and/or the probability of being caught is small relative to the utility gained from non-compliance. Accordingly, factors such as people's perception regarding tax rates, probability of audit, probability of being caught and punished for not paying taxes, and penalty rates fall within this category.

A number of studies have analysed the impact of deterrence factors on tax morale. For example, a field experiment undertaken by Castro and Scartascini (2015) in Argentina involving 23,000 taxpayers showed that deterrence messages had a positive impact on tax reporting. The researchers, working with the revenue authority, identified taxpayers and

divided them into four groups: the first group received deterrence messages (that non-payment of taxes would result in the tax authority taking action against them); the second group received messages pertaining to services that are provided by the municipality; the third group received messages asking taxpayers whether they were aware that only three out of ten taxpayers do not pay taxes; and the fourth group (control group) did not receive any messages. It was found that the group that received the deterrence message significantly increased their tax payments. These results are consistent with the findings of Fellner et al. (2013), who also conducted a large-scale field experiment to evaluate alternative strategies to enforce compliance in the payment of television licence fees in Australia. The researcher found a significant increase in tax compliance amongst individuals evading payment of television licence fees who received messages containing threats that indicated a high risk of detection. Several other studies have found a positive association between deterrence messages and tax compliance (Cummings et al., 2009; Ariel, 2012; Dwenger et al., 2016 ; Bott et al., 2017).

3.3.2 Fiscal Exchange

Factors that fall within the fiscal exchange category are those relating to the social contract between citizens and the government, where individuals are believed to pay taxes in exchange for the services they receive from the government (Ariel, 2012; Torgler, 2007). According to this theory, positive actions of the government will lead to an increase in social commitment by the taxpayers and, consequently, higher tax morale (Horodnic, 2018). There are at least two variants of the fiscal exchange theory. The first variant is cross-sectional; that is, taxpayers receiving more benefits from the government are likely to have a higher tax morale. For example, farmers who receive free or subsidised farm inputs, such as seeds and fertiliser from the government, are more likely to have a high tax morale than those who do not. The second variant is time-based, where a prolonged provision of goods or services by the government, such as schools, health facilities, roads, and so on, over time, would lead to higher tax morale, as individuals are able to see what their taxes are being used for.

Cummings et al. (2009) used survey data and simulation experiments to analyse the role of governance quality in influencing tax morale. The simulation experiments were carried out in Botswana and South Africa. These two countries have similar tax systems but different political histories and institutions, where Botswana is seen to have

a more accountable government and where the majority of citizens support their government, compared to South Africa (Mascagni, 2018). This means that the two countries offer a useful comparison for the investigation of the effects of tax morale stemming from perceptions of the government. Using the results from the simulation experiments and the survey data, the researchers found that perceptions of government fairness and efficacy were considerably higher in Botswana, and self-reported tax compliance also appeared to be higher than in South Africa. This confirmed the fiscal exchange theory that satisfaction with government provision of goods and services or governance leads to high tax morale.

In general, the empirical evidence shows that there is a positive correlation between people's satisfaction with the government's provision of goods and services and tax morale (D'Arcy, 2011; Ali et al., 2013).

3.3.3 Norms, Culture, and Social Influence

Some studies have suggested that human behaviour in regard to taxation is influenced by social interactions in much the same way as other forms of behaviour (Grasmick & Green, 1980; Grasmick & Scott, 1982). Thus, attitudes towards the tax system may also be affected by the norms, culture, and social behaviour of an individual's reference group, such as relatives, neighbours, business partners/acquaintances, and friends.

Various studies have found a link between social behaviour and culture, and tax morale (Schwartz & Orleans, 1967; Bobek et al., 2007). One of the early experiments to show the impact of social appeal to personal conscience on tax compliance was carried out by Schwartz and Orleans (1967). The researchers conducted a field experiment to understand the impact of personal norms and social influence on tax morale in the United States of America (USA). Four experimental groups of approximately 90 taxpayers each were included in the experiment. Each group received a different message (a message about sanctions for non-payment of taxes; a message about why it is good to pay taxes, which was an appeal to conscience; a neutral message; and no message). Before the filing of taxes commenced, the group that received messages about sanctions and the group that received messages appealing to their conscience were asked questions that aimed to identify their motives for tax payment. The results showed that emphasising patriotic considerations (the importance of paying taxes and the high number of people who pay

taxes) had a positive influence on tax payment, especially for middle-income individuals. However, a conceptual replication of this study by McGraw and Scholz (1991) did not find an equivalent effect on actual tax return data (i.e., the appeal to conscience did not have a significant impact on tax payment).

In a simulation study by Bosco and Mittone (1997), messages were sent to taxpayers emphasising the redistributive purpose of tax collection and that tax evasion would be at the expense of poorer taxpayers; a positive correlation was found between moral appeals and tax compliance.

A number of other studies based on survey data have also shown that general honesty (Porcano, 1988), ethical convictions regarding the payment of tax (Reckers et al., 1994), and the anticipation of guilt over non-compliance (Reckers et al., 1994; Scott & Grasmick, 1981) are positively correlated with tax morale.

3.3.4 Comparative Treatment

It has been suggested that individuals comply with the law if they perceive the process of implementing the law to be generally fair (McKerchar & Evans, 2009). Factors under the comparative treatment are those related to the fairness of the tax system (Bello & Danjuma, 2014).

Three types of fairness in taxation have been discussed by the OECD (2012):

1. Distributive fairness, which relates to taxpayers' perception that the government acts as a good custodian and wise spender of tax revenue.
2. Procedural fairness, which relates to the perception that tax bodies adhere strictly to established procedures and are fair in dealing with taxpayers.
3. Retributive fairness, which relates to the perception that tax authorities are fair in the application of punishments when tax rules or norms are violated.

Distributive fairness relates more to the equity of the exchange between the government and taxpayers, and can thus be linked with fiscal exchange factors. Factors that fall under the comparative treatment category are more related to the procedural and retributive fairness and can be influenced by tax administrations by emphasising fairness and transparency in the handling of tax matters (Walsh, 2012).

The importance of fairness in taxation is such that it is not significant whether the

outcome favours the individual taxpayer or not. Most taxpayers will still perceive a tax authority as fair and just even if it acts against them, provided it is in a fair manner (Bello & Danjuma, 2014). This predictably results in fewer complaints about the authority's decisions. Equity and fairness in tax matters also builds mutual trust and cooperation between tax bodies and taxpayers, thereby increasing voluntary compliance (Kirchler et al., 2008; Braithwaite, 2003).

A number of studies have examined the relationship between fairness and tax morale. For instance, using survey data collected from 2,292 taxpayers accused of tax avoidance in Australia, Rothstein (2011) found that the fairer the regulator's actions, the more taxpayers trusted their authority. In another survey-based study, Murphy (2005) found that when taxpayers were treated procedurally unfairly by tax officials, they were more likely to be non-compliant. Similarly, Giray et al. (2015), using survey data collected from 481 taxpayers in Turkey, found that tax morale is high when the tax administration is perceived to be fair in its dealings, when the tax system is considered to be efficient, and when taxpayers are satisfied with public expenditure.

3.3.5 Political Legitimacy

Political legitimacy is defined as belief or trust in authorities, institutions, and social arrangements as being appropriate, just, and working for the common good (Fjeldstad et al., 2012; Ali et al., 2013). The more trustworthy and effective a state is in providing public goods, the more legitimate it will appear, and the greater potential it will have in eliciting high tax morale (Cook, Hardin, & Levi, 2005; Rothstein, 2011). Various researchers (Levi, 1997; Rothstein, 2009; Tyler, 1990; Hechter, 2013) have argued that tax morale is high among taxpayers if they perceive the state to be legitimate; that is, if they believe that the state has the right to impose taxes and that citizens have the responsibility to pay these taxes.

Tyler (1997) proposed that if an organisation is perceived to be legitimate, people are generally more likely to follow and accept their decisions. In a study based on survey data for authorities in political, legal, managerial, educational, and family settings, Tyler (1997) found that authorities draw an important component of their legitimacy from their social relationships with group members. In another context, Tyler and Fagan (2008) found that legitimacy was important for encouraging cooperation with the police; using survey data collected from 830 New York residents, they found that the residents were

more likely to cooperate with law enforcement officials if they viewed the police as legitimate.

3.3.6 Corruption

Corruption in public authorities can severely harm tax morale (Jahnke & Weisser, 2018). From a theoretical point of view, corruption can discourage people from complying because of the perceived unfairness in the exchange taking place between the taxpayers and the state (Feld & Frey, 2007). Torgler (2006) found that countries with high levels of corruption lack the social norm of paying taxes to the government. Torgler (2006) analysed the correlation between Transparency International's Corruption Perceptions Index and tax morale and found it to be negative. Other studies have also found that widespread corruption is associated with lower tax morale (Alasfour et al., 2016; Gerstenbluth et al., 2012; Jahnke, 2015; Torgler, 2008; Williams & Krasniqi, 2017).

However, not all studies have found a negative correlation between corruption and tax morale. For instance, using Round 5 Afrobarometer survey data, Ali et al. (2013) analysed the impact of satisfaction with public services on the tax morale of individuals in Uganda, South Africa, Kenya, and Tanzania. The researchers used the perceived number of corrupt tax officials as a proxy for the citizens' satisfaction with the tax administration and found significant negative effects on tax morale in Uganda and South Africa, but not in Kenya or Tanzania.

3.3.7 Democracy

Tax morale may also vary based on the type of institutional setting. For instance, Prinz (2002) suggested that institutions that respect the preferences of their citizens will have more support from the people than a state that acts as a leviathan. Torgler (2005a) reported that the more able taxpayers are to participate in political decision-making through popular rights (such as voting), the higher their tax morale.

Empirical evidence also show a positive correlation between tax morale and democracy (Alm et al., 1999; Pommerehne & Weck-Hannemann, 1996; Feld & Tyran, 2002; Torgler, 2003; Torgler et al., 2003). Torgler (2005) analysed the impact of people's perception of democracy on tax morale in Switzerland, a country where participation

rights vary significantly across different cantons,¹⁵ using survey data from the International Social Survey Programme (ISSP, 1998); the findings suggested that democratic rights have a significantly positive effect on tax morale.

3.3.8 Tax Knowledge

Tax knowledge refers to the level of awareness or sensitivity of taxpayers to tax legislation (Holland, John & Pernill, 2009). The knowledge base of individuals regarding the types of taxes they pay and their rights and responsibilities as taxpayers may also have an impact on an individual's tax morale (Ali et al., 2013).

Oladipupo and Obazee (2016) studied the effects of tax knowledge and tax penalties on tax morale among small and medium enterprises in Nigeria, using survey data collected from 277 small and medium taxpayers. Multiple regression analysis was performed to assess the relative predictive power of the independent variables (i.e., tax knowledge and tax penalty) on the dependent variable (i.e., tax morale). The results showed a positive and significant correlation between tax knowledge and tax morale, corroborating the findings of previous studies by Kasipillai and Abdul-Jabbar (2006) and Kirchler et al. (2008).

3.3.9 Social Demographic Factors

Various studies have identified a relationship between sociodemographic variables and tax morale (Hofmann et al., 2017; Torgler & Schneider, 2007; Devos, 2008). Indeed, many studies of tax morale have integrated social and economic variables in models of tax morale (Alasfour et al., 2016; Ho et al., 2013; Devos, 2008). Commonly included sociodemographic variables include age, gender, education, employment status, and income level.

1. *Age* – Empirical studies have yielded conflicting results regarding the influence of age on tax morale. While some studies have found that older people have a higher tax morale compared to young people (Devos, 2008; Sipos, 2015; Torgler & Murphy, 2004), others have shown that young people have a higher tax morale than older people (Torgler & Schneider, 2007; Barone & Mocetti, 2011), or that there is no significant effect of age on tax

¹⁵ Cantons in Switzerland refers to the 26 member states of the Swiss Confederation.

morale (Ho et al., 2013).

2. *Gender* – There is no consensus on the relationship between gender and tax morale. Some studies, such as studies conducted in Pakistan (Marriott, 2017) and Russia (Alm et al., 2006) have found that women have a higher tax morale than men, whereas others find the opposite. Studies conducted in Romania (McGee & Preobragenskaya, 2006) and Turkey (McGee et al., 2011) have found a negative correlation between tax morale and gender (female), and a study conducted in Argentina (McGee & Rossi, 2008) found no correlation between gender and tax morale.
3. *Education* – Most studies of the correlation between education and tax morale have identified a positive correlation (Gupta & McGee, 2010; Roth et al., 1989).
4. *Employment* – Empirical evidence shows that self-employed or part-time employed individuals have lower tax morale compared to full-time employed individuals (Devos, 2008; Torgler & Schneider, 2007; Marriott, 2017). Furthermore, pensioners/retired individuals have been found to have a higher tax morale than non-pensioners (Cyan et al., 2016; Doerrenberg & Peichl, 2013; Feld et al., 2008; Sá et al., 2013).

The literature review has shown that various factors affect tax morale, and studies on tax morale have been conducted in both high-income and low-income countries, including SSA countries. Regardless of where the studies are conducted, the same factors are found to affect tax morale. Accordingly, there is no reason to suspect that factors that have an impact on tax morale in SSA countries are different from those that have an impact on tax morale in other regions. However, in the next section, I take a closer look at studies undertaken in SSA with the aim of understanding the main drivers of tax morale in these countries.

3.4 Tax Morale Studies in Sub-Saharan Africa

A number of studies on tax morale have been conducted in SSA. However, most (Ali et al., 2013; Cummings et al., 2009; Yesegat & Fjeldstad, 2016) are based on data collected through surveys. For instance, Cummings et al. (2009) studied how tax morale affects tax compliance in South Africa and Botswana using simulation experiments and Afrobarometer survey data, and found that the observed differences in tax morale in South

Africa and Botswana could be explained by differences in the fairness of tax administration, in the perceived fiscal exchange, and in the overall attitude towards the respective governments (political legitimacy). Ali et al. (2013) analysed the factors affecting tax compliance attitudes in Kenya, Tanzania, Uganda, and South Africa using Round 5 Afrobarometer data and found that tax morale is positively correlated with the provision of public services (such as health, education, and infrastructure). However, this correlation depends on the specific service in question and differs between countries. Finally, Yesegat and Fjeldstad (2016) examined factors that determine business people's attitudes towards paying taxes in Ethiopia, using data collected from a survey conducted in Addis Ababa, Ethiopia, and found that dissatisfaction with the tax administration led to low tax morale. Furthermore, the authors found that most of the factors identified in the literature as being correlated with tax morale, such as satisfaction with the government's provision of goods and services, and the impact of one's reference group (such as friends), were positively correlated to tax morale. A summary of the findings from different studies conducted in Africa and other low-income countries is presented in Table 3.1.

Table 3. 1: Empirical findings on tax morale from studies conducted in low-income countries

Reference	Demographic	Other Factors	Data source	Region
Yesegat and Fjeldstad (2016)	Education (+), female (-)	Corruption (-), satisfaction with revenue authority (+), penalty (+), audit (-)	Survey (own)	Africa (Ethiopia)
Ali, Fjeldstad and Sjørsen (2013)	Education (+)	Deterrence (+), fiscal exchange (satisfaction with provision of health and education (+), infrastructure (+), perceived compliance of others (-), corruption (-)	Survey (Afrobarometer)	Africa
D'Arcy (2011)	Female (-), literacy (-), primary education (+)	Fiscal exchange (handling and access to: health (+), education (+); deterrence (+), trust (+), and satisfaction with democracy (+)	Survey (Afrobarometer)	Africa
Levi and Sacks (2009)	Female (-), personal belongings, television, car, radio (+)	Satisfaction with: local gov. (+), efforts to combat corruption (+), enforcement of taxes (+) fair treatment (+)	Survey (Afrobarometer)	Africa
Daude and Melguizo (2010)	Age (+), female (-), economic problem (-) education (+), religion (+)	Satisfaction with: democracy (+) and services (+), corruption (+)	Survey (Latinobarometer)	Latin America
Gaviria (2007)	Age (+), female (+), savings (-), income (-)	Past mobility (-), future mobility (+), perception in meritocracy (-)	Survey (Latinobarometer)	Latin America
Hug and Spörri (2011)	Age (+), female (+) married (+), self-employed (-), retired (+)	Political legitimacy (satisfaction with incumbent (+)) confidence in the legal system (+)	Survey (World Value Survey)	Eastern Europe
Torgler (2003)	Age (+), female (+) married (+), self-employed (-), retired (+)	Political legitimacy (satisfaction with government (+))	Survey (World Value Survey)	Eastern Europe
Torgler (2004)	Age (+), self-employed (-), unemployed (-), upper class (-), financial satisfaction (+) India and Japan, same as above, religion (+)	Political legitimacy: Trust in: government (+), in legal system, (+), in democracy (+)	Survey (World Value Survey)	Asia (India and Japan)
Torgler (2005)	Age (+), female (+) married (+), religion (+), Financial fastification (+)	Satisfaction with national office (+), Trust in: President (+), in democracy (+)	Survey (World Value Survey and Lationobarometer)	Latin America

Note: (+) indicates a positive correlation between the variable and tax morale; (-) indicates a negative correlation between the variable and tax morale.

Table 3.1 shows that the factors that affect tax morale in different countries are not always the same. For instance, Yesegat and Fjeldstad (2016) found a negative correlation between tax morale and corruption within the tax administration in Ethiopia, while Daude and Melguizo (2010) found a positive correlation between tax morale and corruption in Latin America. The finding that factors that correlate with tax morale impact differently on tax morale depending on location suggests that findings from one study on tax morale cannot be generalised to another country. This is because knowing the factors that drive tax morale in one country does not provide knowledge of how the same factors will impact individuals' tax morale in a different country.

Table 3.1 also shows that most of the existing studies on tax morale focus on economic and social-psychological factors to understand tax morale. The researchers in these studies are mostly ignoring the effects of a wide range of other classes of variables, such as: the demographic characteristics of individual taxpayers; the type of tax in question; the type of business/enterprise; the structure of the tax system; or the behaviour of tax collectors.

3.5 Conclusion

The aim of this chapter was to understand how best to study tax morale. I have analysed methods used to study tax morale as well as factors and evidence regarding the factors affecting tax morale.

I find that there are three main methods of studying tax morale: surveys, simulation experiments, and field experiments. Each of these methods has strengths and weaknesses, and there is no ideal method. The literature also revealed that there are many factors that affect tax morale. There is empirical evidence supporting various factors that fall within fiscal exchange, economic deterrence, and peer influence. In addition, sociodemographic factors, such as age and education level, have also been found to have an impact on tax morale. In general, the empirical evidence shows that all the factors identified in the literature have an impact on tax morale. However, the impact of these factors differs according to place (or country).

As well as providing an overview of tax morale issues, the literature review has also shown that it is difficult to research tax morale in a deep and insightful manner due to the fact that the attitudes of individuals change depending on place or country.

It was also noted in this chapter that most of the existing studies on tax morale focus on economic and social-psychological factors and not on more pragmatic factors, such as differences in tax morale among different categories of taxpayers. This gap in the literature is addressed in Chapter 4, where I undertake an analysis of tax morale in Malawi focusing on differences in tax morale among different groups of businesses people.

Thus, in summary, this chapter has shown that: first, the tools to research tax morale/compliance are weak; second, and related, many different factors affect tax morale/compliance to some extent, but there is little knowledge on their importance relative to one another, either in same context or across contexts; third, much of the research on tax morale has focused on more variables derived from ‘big’ debates about what affects human behaviour, and not on more pragmatic concerns, such as informing tax collectors on how to better perform their role.

Chapter 4: What Can we Learn About Tax Morale in Malawi

4.1 Introduction

Chapter 3 explored the issue of tax morale, an umbrella term that captures the non-pecuniary motivations for tax compliance. This chapter is an empirical investigation of tax morale in Malawi and other SSA countries. The analyses presented in this chapter are based on the literature review in Chapter 3.

Given that tax revenue performance (measured by tax-to-GDP ratio) in Malawi has been higher in comparison to most SSA countries since 2009 (Chapter 2), it seems reasonable to assume that its tax morale will also be higher. Accordingly, in this chapter, I explore whether or not Malawians are exceptionally good and willing taxpayers (i.e., if tax morale is high) relative to the populations in other SSA countries. I explore this issue by undertaking research that answers the following interrelated questions:

- is tax morale in Malawi either higher than or in some other way significantly different from tax morale in other SSA countries?
- what are some of the factors that correlate with tax morale for individuals in SSA countries?
- are there significant differences in tax morale among different types of businesses in Malawi that might shed some light on the broader question of why tax collection, especially collection of direct taxes, is particularly high?

To answer these questions, I conduct three separate pieces of analysis.

In the first piece of analysis, I use Afrobarometer survey data to calculate average tax morale for countries surveyed by the Afrobarometer. Tax morale is measured based on people's views about whether it is "wrong and punishable," "wrong but understandable," or "not wrong at all" to not pay taxes owed to the government. Based on Round 5 (R5) (conducted in 2011/12) and Round 6 (R6) (conducted in 2014/15) Afrobarometer data, I note that there is a big apparent change in tax morale (based on the percentage of people who answered "wrong and punishable" in each country) between the two rounds in Malawi and Madagascar. This raised the question of whether or not the Afrobarometer data is accurate and reliable considering that the two survey (R5 and R6) were conducted within two years of each other hence the tax morale between the two

rounds were expected to be close to each other. In an attempt to understand what might be the problem with the data, I conducted a plausibility check involving looking at all countries surveyed by Afrobarometer which led to the conclusion that the high variation between tax morale in R5 and R6 in Malawi and Madagascar does not indicate a significant problem of the reliability of the Afrobarometer data, and that it was reasonable to use the merged data for R5 and R6 to calculate the “real” tax morale figure for Malawi. Based on the merged data for R5 and R6, I found that tax morale in Malawi is within the average for SSA countries. That is, Malawians are not any better, or more or less willing, taxpayers, when compared to people in other SSA countries.

Given that I had access to the original Afrobarometer survey data for individuals, I decided to conduct a second piece of analysis to investigate in more detail the factors that correlate with tax morale for individuals in SSA countries to see whether there might or might not be something distinctive about Malawian taxpayers that will help to shed light on my broader research questions. This analysis also showed that there is nothing special about Malawian taxpayers.

The third piece of analysis explored the differences in tax morale among different groups of business people in Malawi. I assumed that although the overall tax morale is not particularly high in Malawi compared with the average tax morale for SSA countries (based on the findings from the first analysis), it might be sufficiently high among certain groups of business people within Malawi to shed light on the good tax revenue performance in the country. This analysis is based on the survey data that I collected from business people in Malawi in January and February of 2017. Only one category of taxpayers (business people) was included in the survey due to time limitations meaning it was not possible to conduct a survey covering different taxpayer categories. However, business people in Malawi constitute a majority of taxpayers in terms of number as well as their contribution to revenues (see Chapter 5) hence they are a good representation of all taxpayers in Malawi.

A regression equation was estimated with tax morale as the dependent variable, and various factors, such as deterrence, fiscal exchange, corruption, and the following business taxpayer groups as independent variables: businesses operating in Lilongwe and Blantyre; formal and informal businesses; small/medium and large businesses (size based

on MRA classification of businesses)¹⁶; and businesses in different sectors (accommodation, manufacturing, construction, wholesale and retail, and transport).

The results of this analysis showed that business people operating in Blantyre had higher tax morale than those operating in Lilongwe; large businesses had higher tax morale than small businesses; and businesses in the construction sector had lower tax morale than businesses in other sectors. No variation in tax morale was found between formal and informal businesses; between businesses in manufacturing and other sectors; between businesses in retail and wholesale and other sectors; and between businesses in transport and other sectors. In addition, similar to the second piece of analysis presented in this chapter, I found that corruption, fiscal exchange, and deterrence factors are the main drivers of tax morale in Malawi.

The results from the three pieces of analysis suggest that, while tax morale in Malawi is not significantly different from the average tax morale for SSA countries, certain groups of business people in Malawi have a higher tax morale. Accordingly, the taxpayer groups with high tax morale (those operating in Blantyre, and taxpayers classified as large) may be partly contributing to the good tax revenue performance in Malawi as they may be more tax compliant. However, the extent to which the high tax morale among the groups of business people with high tax morale is translating into high tax compliance is unknown. This is because, as discussed in Chapter 3, tax morale only pertains to people's attitudes and not their behaviour.

The remainder of this chapter is organised as follows. I present the three pieces of analysis starting with the comparison of average tax morale of Malawi and other SSA countries, then the investigation of factors that correlate with tax morale in SSA based on the Afrobarometer data, and then the investigation of differences in tax morale among different business groups in Malawi. I conclude the chapter with a discussion of the results from the three analyses.

4.2 First Analysis: Comparative Analysis of Tax Morale Between Malawi and Other SSA Countries

In this analysis, I use Afrobarometer survey data to explore variation in tax morale

¹⁶ Two groups were created. The first group was for businesses with annual turnover of MK150 million (£150,000) which are classified as large. The rest were in the second group (hence comprised of small and medium taxpayers)

between Malawi and other countries in SSA based on country averages of tax morale.

Afrobarometer is an organisation that conducts public attitude surveys on democracy, governance, economic conditions, and related issues, in 37 SSA countries.¹⁷ The organisation has conducted seven rounds of surveys in the following years:¹⁸ 1999-2001 (Round 1); 2002-03 (Round 2); 2005-06 (Round 3); 2008-09, (Round 4); 2011-13 (Round 5); 2014-15 (Round 6); and 2017-18 (Round 7). The Afrobarometer data is cross-sectional and the rounds are not connectable in a panel¹⁹ since the respondents cannot be uniquely identified on the grounds of their being randomly selected from the whole population for each round. Afrobarometer surveys use national probability samples, which are designed to generate a sample that is a cross-sectional representation of all citizens of voting age in a given country. Every adult citizen has an equal chance of being selected for an interview. This is achieved by using random selection methods with a probability proportionate to the population size, to ensure that individuals in larger (i.e., more populated) geographic units have a proportionally greater probability of being chosen for the sample. A total of between 1,400 and 2,400 people in each country participate in these surveys, which are conducted using a structured questionnaire. The Afrobarometer survey data is freely available on the Afrobarometer website.

The question I use for tax morale is where the respondents were told: “I am now going to ask you about a range of different actions that some people take. For the following, please tell me whether you think the action is not wrong at all, wrong but understandable, or wrong and punishable: not paying taxes owed to the government.” Of all the rounds of Afrobarometer data, only the Round 5 (R5) and Round 6 (R6) surveys included this exact question. Given that only two years separated the R5 and R6 surveys, I expected to find that the level of tax morale (based on the percentage of people who answered “wrong and punishable” in a country) in Malawi and all the other countries within these two rounds to be either comparable, or that it would be slightly higher for R6 than for R5. This is because the two surveys were conducted at a time of relatively fast economic growth, considerable growth in tax revenues, and less political turmoil and

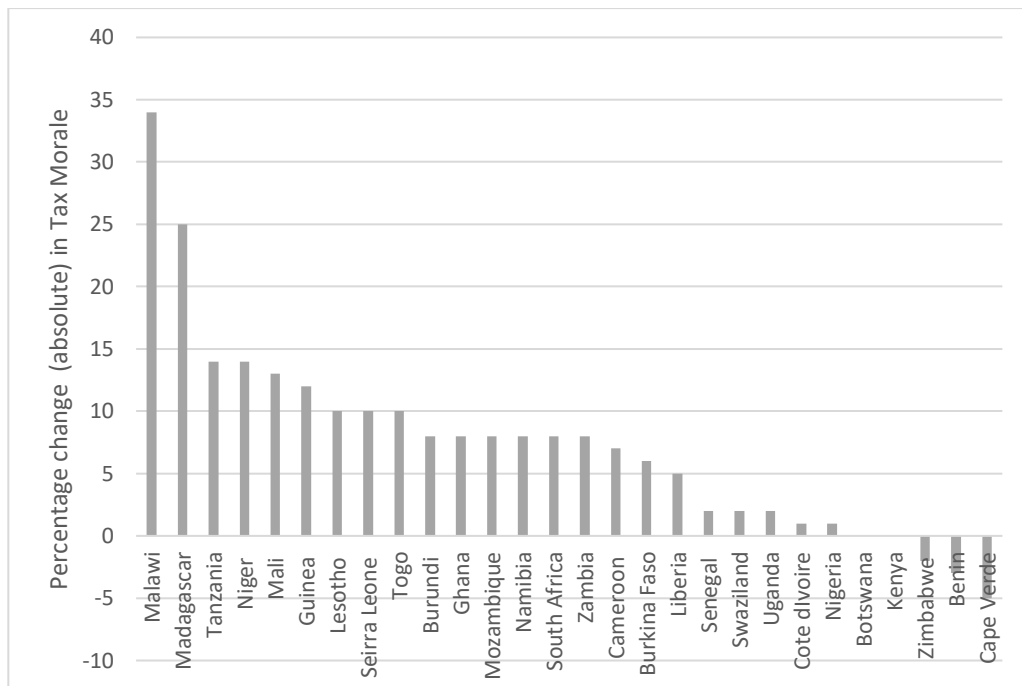
¹⁷See <http://www.afrobarometer.org>

¹⁸ Important to note that the years when the survey is conducted usually overlap in a country hence a range of years shown. This does not mean the surveys take more than 1 year. Also, a survey round, such as R5 surveys, are not always conducted in the same year in different countries. Accordingly, Afrobarometer include all the years that they took to complete a round in all countries included in their surveys.

¹⁹I was unable to create time series data by connecting different rounds.

conflict than in earlier decades, for most of the countries involved (Hong, 2015; World Bank, 2013). What I found was that the variation in tax morale (calculated as the percentage of people who answered “wrong and punishable” in R6 minus the percentage of people who answered “wrong and punishable in R5) in most countries between R5 and R6 ranged from -7% to +14% (Figure 4.1). However, in Malawi and Madagascar, the variation was 34% and 25% respectively. Figure 4.1 shows the absolute variation in tax morale between the two periods for each country.

Figure 4. 1: Absolute percentage change in tax morale between R5 and R6 in different African countries



Source: R5 and R6 Afrobarometer survey data, author's own calculations

Figure 4.1 shows that the increase in tax morale in Malawi and Madagascar was 34% and 25% respectively, more than twice that of most countries. For instance, the value for Madagascar alone is almost twice that for the next country down in this scale (Tanzania).

This huge variation in tax morale between R5 and R6 in Malawi and Madagascar raised the question of whether or not the Afrobarometer data is accurate and reliable considering that the two survey (R5 and R6) were conducted within two years of each hence the tax morale between the two rounds for each country was expected to be close to each other. In an attempt to understand what the problem with the data might be, I

conducted a plausibility check involving a review of the economic and political developments in all the countries surveyed by the Afrobarometer in R5 and R6 (Appendix 4.1). The results showed that the dramatic increase in tax morale in Malawi and Madagascar between R5 and R6 mirrored the prevailing economic and political situation at the time the surveys were conducted. In both Malawi and Madagascar, the R5 survey was conducted at a time of political and economic instabilities. In both countries, these instabilities included citizens protesting against the government and demanding the resignation of the president due to widespread corruption and poor governance; the withdrawal of donor support, which resulted in a shortage of various key products, such as fuel and food stuffs; and deterioration of government services, especially in health and education (Jackson, 2013; Ploch & Cook, 2012; Cammack, 2017; Dionne & Dulani, 2013; Gabay, 2014). By contrast, in both Malawi and Madagascar, the R6 survey was conducted when the government had just changed (with a change in president) and the new administration was addressing most of the economic problems, such as shortage of fuel and food stuffs, and a large injection of international donor funds, which allowed the government to address most of the challenges it was facing, especially in health and education (Jackson, 2013; Ploch & Cook, 2012; Cammack, 2017; Dionne & Dulani, 2013; Gabay, 2014). In general, during R6, there was jubilation in both Malawi and Madagascar as the political and economic situation was improving for the better. It is, therefore, very likely that it is these two extremely different political and economic environments in which the R5 and R6 surveys were conducted that resulted in the tax morale being very low in R5 and very high in R6, thereby resulting in a significant variation in tax morale between the two surveys in Malawi and Madagascar. No other country included in the R5 and R6 Afrobarometer survey had such different political and economic environments when the two surveys were conducted.

Considering that tax morale in R5 in Malawi and Madagascar was most likely abnormally low due to the prevailing political situation when the survey was conducted, and tax morale during R6 was most likely abnormally high due to the drastic change in the political environment, I found it reasonable to assume that the “real” tax morale for Malawi and Madagascar lies within the tax morale for R5 and R6. Accordingly, the merged data for R5 and R6 represents the “real” tax morale in the two countries in a stable environment. Accordingly, the comparison of tax morale for Malawi and other African countries was based on the merged data for R5 and R6.

The average tax morale value for all countries included in the survey was 47%, 53%, and 51% for R5, R6 and the merged data respectively. However, the average tax morale values for Malawi for R5, R6, and the merged data were 28%, 62%, and 48% respectively. While the average tax morale values for Madagascar for R5, R6, and the merged data were 36%, 60%, and 51% respectively. Thus, based on the merged data, the tax morale for Malawi (which was 48%) is within the average range of tax morale for SSA countries (which was 51%). This finding suggests that Malawians are not any better, or more or less willing, taxpayers, when compared to people in other SSA countries.

4.3 Second Analysis: Exploring Factors that Correlate with Tax Morale in Malawi and Other SSA Countries

Given that I had access to original Afrobarometer survey data for individuals, it seemed worthwhile to investigate factors that correlate with that morale for individuals across all countries covered by Afrobarometer. The aim of this exercise was to find out whether there might or might not be something distinctive about Malawi taxpayers that will help to shed light on my broader research question of why tax revenue performance in Malawi is better than in most countries in SSA.

4.3.1 Data

The analysis is based on the merged Afrobarometer data for R5 and R6. However, for comparison purposes, R5 and R6 data was also used.

4.3.2 Dependent Variable

The dependent variable, tax morale, is based on the question: “I am now going to ask you about a range of different actions that some people take. For the following, please tell me whether you think the action is not wrong at all, wrong but understandable, or wrong and punishable: not paying taxes owed to the government.”

Similar to other studies on tax morale (Fjeldstad, 2016; Ali, Fjeldstad & Sjørnsen, 2013; Yesegat & Fjeldstad, 2016), an individual was considered to have a higher tax morale if their response was “wrong and punishable,” and a lower tax morale if their response was either “not wrong at all,” or “wrong but understandable.” I created a dummy variable, tax morale, where a value of “1” was given to those who answered “wrong and punishable,” and “0” otherwise. This binary classification of the responses

reflecting high and low tax morale is consistent with how other researchers in similar studies have analysed survey responses (Yesegat & Fjeldstad, 2016). In addition, the binary classification of responses makes it easy to visually compare the results in a table when data from different rounds (R5, R6, and the merged data for R5 and R6) is used. However, to test the robustness of this classification, an analysis of tax morale based on each of the three responses (“wrong and punishable,” “wrong but understandable,” and “not wrong at all”) was also undertaken.

4.3.3 Independent Variables

A number of factors that have an impact on tax morale have been identified in the literature (see Chapter 3). However, in this study, only those factors that data was available for were tested. Table 4.1 provides descriptions of the independent (explanatory) variables, used in the analysis.

Table 4. 1: Description and measurement of independent variables

Variable	Description	Measurement
Deterrence (DETER)	The factors relevant to the economic deterrence theory of tax morale. Respondents were asked a question about their perceptions of how easy or difficult it is to avoid paying income or property taxes that they owe the government.	Responses ranged from 0 = “not applicable” to 4 = “very difficult.”
Fiscal exchange (FISCAL)	This captures people’s satisfaction with the government’s provision of goods and services. Respondents were asked about their satisfaction with the government’s	Responses ranged from 1 = “very satisfied” to 4 = “not satisfied at all.” To prevent the problem of multicollinearity, ²⁰

²⁰ Multicollinearity is a phenomenon in which one independent variable, in a multiple regression model, can be linearly predicted from the others, with a substantial degree of accuracy. In this situation, the coefficient estimate of the multiple regression may change erratically in response to small changes in the model or the data. Multicollinearity does not reduce the predictive power or reliability of the model as a whole, at least within the sample data set; it only affects calculations regarding individual, independent variables. That is, a multivariate regression model with collinear, independent variables can indicate how well the entire bundle of independent variables predicts the outcome variable, but may not provide valid results about any individual predictor, or about which predictors are redundant (Chong and Jun, 2005)

Variable	Description	Measurement
	handling of health, education, and maintenance of roads and bridges.	responses to these three questions were merged by taking a simple average to create a composite variable.
Comparative treatment (COMP)	This represents factors related to comparative treatment theory. Respondents were asked about how often people within their ethnic group were treated unfairly under the law.	Responses ranged from 1 = “never” to 4 = “always.”
Trust (TRUST)	This variable captures the degree of trust the respondent has in the tax administration. Respondents were asked about their perception of the trustworthiness of the tax administration.	Responses ranged from 0= “don’t trust at all” to 4 = “trust a lot.”
Corruption (CORR)	This represents the perception of corruption in the tax administration.	Responses ranged from 1 = “widespread” to 4 = “no corruption.”
Democracy (DEMOC)	Respondents were asked about their perception of how democratic their country is.	Responses ranged from 1= “very satisfied” to 5= “there is no democracy in this country.”
Tax knowledge (TKNOW)	Respondents were asked whether it is easy or difficult to know the taxes that they must pay.	The responses ranged from 1 = “Very difficult” to 4 = “Very easy.”
Age	Age of respondent.	Age ranged from 18 to 108.
Female	Gender of respondent.	Dummy variable “FEMALE” was used,

Variable	Description	Measurement
		where a value of 1 if respondent is a woman, 0 otherwise.
Education (EDU)	The highest level of education attained by the respondent.	EDU ranges from 0 = “No formal education” to 9 = “Tertiary education.”
Employment (EMP)	Respondents were asked about their employment status.	Dummy variable was created where “1” was given for respondents in full-time employment and “0” otherwise.
Urban (URBAN)	Where respondent lives; urban or rural area.	Dummy variable taking a value of “1” for those who live in urban areas and “0” otherwise.
Malawi	Malawi.	Dummy variable, taking a value of “1” if the country is Malawi, “0” otherwise.

4.3.4 Method

I used logit regression analysis to find the determinants of tax morale in Malawi and SSA, and the factors that drive it in that country. Logit regression analysis was used because the dependent variable, Tax Morale, takes only two values, “0” or “1”. Since the coefficients from the logit regression cannot be interpreted directly, marginal effects are presented. Marginal effects were interpreted just as is done under ordinal least squares regression (Wooldridge, 2003; Williams, 2006; Wolfe & Gould, 1998). The equation used in the analysis is presented below:

$$\begin{aligned}
TM_i = & \beta_0 + \beta_1 DETER_i + \beta_2 FISCAL_i + \beta_3 COMP_i + \beta_4 TRUST_i + \beta_5 CORR_i + \beta_6 DEMOC_i \\
& + \beta_7 TKNOW_i + \beta_8 FEMALE_i + \beta_{11} EDU_i + \beta_{12} AGE_i + \beta_{13} EMP_i + \beta_{14} URBAN_i + \beta_{15} MW \\
& + \beta_{16} DETER_i MW + \beta_{17} FISCAL_i MW + \beta_{18} TREAT_i MW + \beta_{19} TRUST_i MW + \\
& \beta_{20} CORR_i MW + \beta_{21} DEMOC_i MW + \beta_{22} TKNOW_i MW + \beta_{23} FEMALE_i MW + \\
& \beta_{24} EDU_i MW + \beta_{25} AGE_i MW + \beta_{26} EMP_i MW + \beta_{27} URBAN_i MW + \varepsilon_i
\end{aligned}
\tag{1}$$

In Equation 1: TM_i is the score for tax morale for a country; β is a vector of regression coefficients; ε is the error term; DETER is deterrence factors; FISCAL is fiscal exchange factors; COMP is perception about the treatment of one's ethnic group by the revenue authority; TRUST is level of trust in the revenue authority; CORR is perception of level of corruption in the revenue authority; DEMOC is level of democracy in the country; TKNOW is level of tax knowledge of the respondent; FEMALE is a dummy variable representing female; EDU is the highest education level attained by the respondent; AGE is the age of the respondent; EMP is the respondent's employment status; URBAN is a dummy variable taking a value of 1 for respondents in urban areas and 0 otherwise; MW is a dummy variable taking a value of 1 for Malawi and 0 otherwise; DETERMW is an interaction term used to find the impact of DETER on tax morale in Malawi compared to other countries in SSA; FISCALMW is an interaction term used to find the impact of FISCAL on tax morale in Malawi compared to other countries in SSA; TREATMW is an interaction term used to find the impact of TREAT on tax morale in Malawi compared to other countries in SSA; TRUSTMW is an interaction term used to find the impact of TRUST on tax morale in Malawi compared to other countries in SSA; CORRMW is an interaction term used to find the impact of CORR on tax morale in Malawi compared to other countries in SSA; DEMOCMW is an interaction term used to find the impact of DEMOC on tax morale in Malawi compared to other countries in SSA; TKNOWMW is an interaction term used to find the impact of TKNOW on tax morale in Malawi compared to other countries in SSA; FEMALEMW is an interaction term used to find the impact of FEMALE on tax morale in Malawi compared to other countries in SSA; EDUMW is an interaction term used to find the impact of EDU on tax morale in Malawi compared to other countries in SSA; AGEMW is an interaction term used to find the impact of AGE on tax morale in Malawi compared to other countries in SSA; EMPMW is an interaction term used to find the impact of EMP on tax morale in Malawi compared to other countries in SSA; and URBANMW is an interaction term used to find

the impact of URBAN on tax morale in Malawi compared to other countries in SSA. The analysis is based on merged data for R5 and R6. However, R5 and R6 data was also used for comparative purposes.

4.3.5 Empirical Results and Analysis

Descriptive Statistics and Correlations

The descriptive statistics for the variables in Equation 1, for 34 SSA countries²¹ (based on the merged data for R5 and R6) are presented in Appendix 4.4. The Pearson pairwise correlation coefficients for the dependent and independent variables used in this analysis are summarised in Table 4.2. Table 4.2 shows significant correlations ($p < 0.01$) between tax morale and all the independent variables included in Equation 1, with a stronger negative correlation between corruption and tax morale at -14 percentage points (i.e., a unit increase in corruption lowers tax morale by 14 percentage points).

²¹ The countries included in the analyses are: Algeria, Benin, Botswana, Burkina Faso, Burundi, Cameroon, Cape Verde, Cote d'Ivoire, Egypt, Ghana, Guinea, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritius, Morocco, Mozambique, Namibia, Niger, Nigeria, Senegal, Sierra Leone, South Africa, Sudan, Swaziland, Tanzania, Togo, Tunisia, Uganda, Zambia, Zimbabwe.

Table 4. 2: Pearson Correlation for Dependent and Independent Variables

Variable	1	2	3	4	5	6	7	8	9	10	11	12	13	14
TM	1													
DETER	0.14***	1												
FISCAL	0.05***	0.07***	1											
COMP	-0.03***	-0.07***	-0.19***	1										
TRUST	0.2***	0	0.19***	-0.12**	1									
CORR	-0.14***	-0.03***	-0.05***	0.05***	-0.36***	1								
DEMOC	0.02***	0.02***	0.23***	-0.28***	0.14***	-0.12***	1							
TKNOW	-0.03***	-0.43***	0.01*	0.09***	0.11***	-0.02***	0.02***	1						
FEMALE	-0.02***	-0.02***	-0.06***	0.16***	0	-0.08***	-0.13***	0.04***	1					
EDU	-0.02***	0.05***	0.02***	0.03***	0	-0.01***	-0.05***	-0.02***	0	1				
AGE	0.07***	0.05***	0.03***	0	0.09***	0	0.05***	0.07***	-0.08***	-0.15***	1			
URBAN	-0.05***	-0.23***	-0.09***	0.08***	-0.07***	0.06***	-0.02***	0.23***	0	-0.05***	-0.07***	1		
EMP	-0.01***	0.04***	0.01***	0	0.01**	0.01	0	-0.06***	0	0.29***	0	-0.06***	1	
MALAWI	-0.12***	-0.32***	-0.10***	0.17	0.00***	0.09***	-0.19***	0.2***	0.09***	-0.08***	-0.03***	0.21***	-0.01*	1

Notes:

1. TM_i is the score for tax morale for a country; DETER is deterrence factors; FISCAL is fiscal exchange factors; COMP is perception about the treatment of one's ethnic group by the revenue authority; TRUST is level of trust in the revenue authority; CORR is perception of level of corruption in the revenue authority; DEMOC is level of democracy in the country; TKNOW is level of tax knowledge of the respondent; FEMALE is a dummy variable representing female; EDU is highest education level attained by the respondent; AGE is the age of the respondent; EMP is the respondent's employment status; URBAN is a dummy variable taking a value of 1 for respondents in urban areas and 0 otherwise.
2. N = 61,300 for all variables.
3. *Significant at .10 level; **Significant at .05 level; ***Significant at .01 level.

Logit Regression Results

Equation 1 was estimated in STATA. Table 4.3 presents a summary of the binary logit estimation results for Equation 1, using data from R5, R6, and the merged data for the two. The standard errors are presented in parentheses.

Table 4. 3: Binary Logit Regression Results with Marginal Effects

Variable	R5	R6	Merged (R5+R6)
Fiscal exchange (FISCAL)	0.012 (0.004)***	0.008 (0.003)***	0.021 (0.004)***
Deterrence (DETER)	0.026 (0.004)***	0.029 (0.003)***	0.046 (0.003)***
Comparative (COMP)	-0.012 (0.003)***	-0.008 (0.002)***	0.015 (0.002)***
Tax knowledge (TKNOW)	0.032 (0.003)***	0.02 (0.003)***	0.009 (0.003)***
Democracy (DEMOC)	0.025 (0.003)***	0.021 (0.003)***	-0.0399 (0.002)***
Trust (TRUST)	0.021 (0.003)**	0.04 (0.003)***	0.085 (0.002)***
Corruption (CORR)	-0.017 (0.003)***	-0.012 (0.003)***	-0.037 (0.003)***
Education (EDU)	0.007 (0.001)***	0.031 (0.002)***	-0.033 (0.004)***
Age (AGE)	0.001 (0.00)***	0.001 (0.00)***	0.001 (0.00)***
Female (FEMALE)	-0.018 (0.006)***	-0.002 (0.006)***	0.029 (0.004)***
Urban (URBAN)	0.056 (0.006)***	0.027 (0.006)***	-0.016 (0.005)***
Malawi (MW)	-0.43 (0.095)***	0.7 (0.298)**	0.175 -0.124
FiscalMW	0.064 (0.014)***	0.007 -0.019	0.022 -0.021
DeterrenceMW	0.024 (0.015)*	-0.001 -0.021	0.098 (0.018)***
ComparativeMW	-0.057 (0.016)***	0.019 -0.018	-0.092 (0.018)***
TaxknowMW	0.021 -0.014	0.003 -0.022	-0.117 (0.018)***
DemocracyMW	0.004 -0.015	-0.033 -0.022	0.096 (0.02)***
TrustMW	-0.031 (0.014)**	-0.025 -0.017	0.132 (0.016)***
CorruptionMW	-0.029 (0.016)*	0.028 -0.019	-0.031 (0.019)*
EducationMW	0.025 (0.009)***	-0.083 (0.023)**	-0.004 -0.022
AgeMW	0 0	0 -0.001	0 (0.022)***
FemaleMW	0.049 (0.025)**	-0.014 -0.031	-0.184 (0.028)***
UrbanMW	-0.035 0.026	0.075 0.039*	0.069 0.038*
Obs.	27,139	33,086	40,226

Notes:

1. * Significant at 0.1 level; ** Significant at 0.05 level, and *** Significant at 0.01 level.
2. Dependent variable: tax morale; dummy taking the value of 1 if the individual thinks it is wrong and punishable not to pay taxes, 0 otherwise.

The results in Table 4.3 show that:

1. When R5 data is used (second column) the coefficient for the Malawi dummy (MW) is significant and negatively correlated with tax morale. This indicates that tax morale in Malawi in R5 was lower than the average for SSA countries by 3.5 percentage points. By contrast, the results of the regression when the R6 data is used (third column) show that MW is positively correlated with tax morale. This indicates that tax morale in Malawi in R6 was 7.5 percentage points higher than the average for SSA countries. However, when the merged data for R5 and R6 is used, the results show that MW is not significant. This indicates that tax morale in Malawi falls within the average range for countries in SSA. The statistical results from the merged data are in line with findings from the first analysis which was based on country average of tax morale, confirming that tax morale in Malawi is within the average for countries in SSA.
2. It is also noted that when the coefficient for the Malawi dummy (MW) is significant and negative (R5, column two), the coefficients for four interaction terms – comparativeMW, trustMW, corruptionMW, and urbanMW – are also significant and negatively correlated with tax morale. Specifically, the average impact in SSA countries of a unit change in the perception that one's ethnic group is not treated fairly is a six-percentage point reduction in tax morale. However, *in Malawi* the impact is a seven-percentage point reduction in tax morale ($-0.012 + (-0.057)$) (coefficient for comparative + coefficient for comparativeMW). The average impact in SSA of a unit change in trust in the tax authority *in SSA* is a two-percentage point increase in tax morale, whereas, *in Malawi*, it is a one percentage point decrease in tax morale ($0.021 + (-0.031)$). The average impact in SSA of a unit change in perception about corruption among tax officials is a two-percentage point reduction in tax morale *in SSA*, while the impact *in Malawi* is a one percentage point reduction ($0.017 + (-0.029)$). These results suggest that the lower tax morale in Malawi during R5 was driven by a higher perception that one's ethnic group is not treated fairly, a higher perception of corruption among tax officials, low trust in the tax administration, and low tax morale among individuals in urban areas. By contrast, when the coefficient for the Malawi dummy is significant and positive (when R6 data is used), the coefficient for two interaction terms – EducationMW and UrbanMW – are also significant. However, EducationMW has a negative coefficient, indicating that the impact of an increase

in the level of education on tax morale is lower in Malawi than the average for countries in SSA. In addition, people living in urban areas in Malawi had a higher tax morale compared to those living in rural areas, and their tax morale was higher than in the urban populations in other SSA countries. This suggests that the relatively high tax morale in Malawi in R6 was mainly driven by the high tax morale among the urban population.

3. The results also show that all the independent variables included in the analysis are significant and the direction of the correlation between the dependent and independent variables is consistent with findings in other tax morale studies (as discussed in Chapter 3). For example, the results of the regression analysis using R6 data (third column), reveals the following:
 - a. Positive correlation between tax morale and fiscal exchange. A unit increase in satisfaction with the government's provision of education, health services, roads, and bridges increases tax morale by one percentage point. This is in line with the fiscal exchange theory.
 - b. Positive correlation between tax morale and deterrence. A unit increase in a person's perception that it is difficult to avoid paying income or property taxes that one owes to the government increases tax morale by three percentage points. This is in line with the deterrence theory of tax morale.
 - c. Positive correlation between tax morale and comparative theory. A unit increase in a person's perception that their ethnic group is unfairly treated by the government reduces the person's tax morale by one percentage point. This is in line with the comparative treatment theory.
 - d. Positive correlation between tax morale and tax knowledge. A unit increase in a person's tax knowledge (TKNOW) increases tax morale by two percentage points.
 - e. Positive correlation between tax morale and democracy. A unit increase in a person's perception that the country is very democratic (DEMOC) increases tax morale by two percentage points.
 - f. Positive correlation between tax morale and trust. A unit increase in a person's trust in tax officials (TRUST) increases tax morale by four percentage points.
 - g. Negative correlation between tax morale and corruption. A unit increase in a person's perception that corruption is high among tax officials

(CORR) reduces tax morale by one percentage point.

- h. Positive correlation between tax morale and education. A unit increase in respondents' highest level of education (EDU) increases tax morale by three percentage points.
- i. Positive correlation between tax morale and age. A unit increase in a person's age (AGE) increases tax morale by less than one percentage point.
- j. Negative correlation between tax morale and female gender. Being female (FEMALE) reduces a person's tax morale by three percentage points.
- k. Positive correlation between tax morale and urban location. Living in an urban area (URBAN) increases tax morale by three percentage points.

In general, these findings are consistent with the findings of similar studies conducted in low-income and high-income countries (Yesegat & Fjeldstad, 2016; Alm, Martinez-Vazquez & Torgler, 2006; Frey, 2003). These results are also consistent with the univariate findings reported in Table 4.2.

Post-estimation Tests

Once Model 1 had been estimated, the Wald test and the Hosmer–Lemeshow Goodness of Fit post-estimation tests were conducted.

The Wald test is used to test the statistical significance of each coefficient (β) in a model (jointly or independently). If the coefficients are not significant, this suggests that removing them from the model will not substantially reduce the fit of the model (Agresti, 2003). The results of the Wald test on whether all the regressing coefficients are jointly zero (when R5, R6, and the merged data are used) show that the null hypothesis is rejected at a 1% level of significance ($p\text{-value} = 0.000$ in all regressions) (see Appendix 4.5-4.7). This implies that all the variables included in the regression create a statistically significant improvement in the fit of the model.

The Hosmer–Lemeshow Goodness of Fit test is similar to a chi-square test. It indicates the extent to which the model fits the data. The test compares observed and fitted frequencies using Pearson's formula, and the Pearson chi-square is reported. If this test result is not statistically significant, then the null hypothesis – that there is no difference between the observed and model predicted values – cannot be rejected. The

results of the Hosmer–Lemeshow test showed that all the regressions have good fit (p-value = 0.15, 0.44, and 0.18, respectively) (Appendix 4.8-4.10).

Robustness Check

Table 4.3 presents the results of the binary logit regression, where tax morale takes a value of “1” for individuals who responded that not paying taxes owed to the government is “wrong and punishable,” and “0” for those who responded “not wrong at all” or “wrong but understandable.” However, it is possible that individuals in the latter group might also have a high tax morale. Accordingly, another regression was estimated where the dependent variable, Tax Morale, took one of three possible values: 1 = “wrong and punishable,” 2 = “wrong but understandable,” or 3 = “not wrong at all.” The independent variables remained unchanged. Since the dependent variable has more than two responses, an ordered logit regression was used. The ordered logit model allows the analysis of responses to each category to be carried out separately (Williams, 2006; Wolfe & Gould, 1998).

Appendix 4.11 shows the results of the ordered logit regression using the merged data for R5 and R6. The results are consistent with the findings of the binary logit regression presented in Table 4.3. Specifically, Appendix 4.11 shows that there is a positive correlation between tax morale and: fiscal exchange; deterrence; comparative theory; tax knowledge; democracy; trust; education; age; and urban. There is a negative correlation between tax morale and: corruption; and female. This shows that the results from the binary logit regression are robust.

4.4. Third Analysis: Tax Morale Among Business People in Malawi

4.4.1 Data

This analysis draws on survey data that I collected from business people in Malawi. I conducted my own survey to capture additional variables not included in the Afrobarometer surveys. These were variables that would allow an exploration of the differences in tax morale among different groups of business people, such as businesses in different sectors, small and large businesses, formal and informal businesses, and businesses operating in different districts. In addition, I conducted my own survey because it was anticipated that this would reveal information about the relationship

between tax collectors and taxpayers that might be relevant to answering the main research questions of this thesis. In particular, I aimed to determine how often officers from the tax administration visit (for audit or other reasons) different taxpayers (small, medium, and large) and how these interactions impact the individual's taxpaying attitudes and behaviour with regards to taxation in Malawi. I made use of the insights gained from conducting my own survey in my review of the tax administration in Malawi (see Chapter 5).

The survey was conducted in Lilongwe and Blantyre – the two major cities in Malawi. Both businesses that are registered with the tax administration, the Malawi Revenue Authority (referred to as 'formal' businesses) and those that are not registered with the tax administration (referred to as 'informal' businesses) participated in the survey. Informal businesses operate illegally in terms of tax payments, as all businesses in Malawi are required to register with the revenue authority if their annual return exceeds MK3 million (£3,000). Over 90% of the informal businesses have annual turnover in excess of MK3 million (£3,000). A structured questionnaire was used (Appendix 4.10). The questionnaire was developed based on standard questionnaires used in the literature (those used by the Afrobarometer and the World Value Surveys). The survey was conducted with the assistance of two officers from the Centre for Social Research (CSR)²² and ten enumerators. All the enumerators were graduates of the University of Malawi, and some had conducted similar surveys for the CSR. The enumerators were trained for two days in all aspects of the survey, including project overview, review of survey objectives, interviewing techniques, field procedures, and all sections of the tax morale questionnaire. A pilot study was conducted, involving 40 formal and 20 informal businesses. Feedback on the pilot study informed the final questionnaire, and led to alterations (such as rephrasing, restructuring the format, deleting some questions, and introducing new questions) in 13 out of 32 questions. Preparation for the survey (including the development of the questionnaire, obtaining the taxpayer registry from the MRA, recruiting enumerators, training enumerators, and the pilot study) began in October 2016. The final survey was conducted between 3 January and 7 February 2017.

To sample businesses from the formal sector, taxpayer registration data obtained

²²A research institute based at the University of Malawi. Officers from CSR were specifically requested to assist in conducting the survey because they also conduct the Afrobarometer surveys in Malawi.

from the MRA was used.²³ As of October 2016, the MRA taxpayer registry had 32,000 taxpayers that had made a tax payment within the previous three years. These were the taxpayers that were targeted. Using the random function (RAND) in Excel, I randomly selected 300 businesses in each of the two districts (Blantyre and Lilongwe). Whenever a taxpayer refused to participate, additional taxpayers were randomly sampled. A total of 178 taxpayers did not participate for various reasons (including the outright refusal to participate or giving an excuse as to why they could not participate). Consequently, 50 taxpayers were additionally sampled, out of which 34 participated. The total number of formal taxpayers who participated in the survey was 456 from a sample of 650, representing a 70% participation rate.

To sample informal businesses, I used clustered random sampling in which the two districts were subdivided into clusters. Lilongwe was subdivided into 36 clusters, and Blantyre was subdivided into 19 clusters. I then randomly selected 10 clusters in each district (using the RAND function in Excel) from which informal businesses were interviewed. Additionally, the enumerators randomly interviewed participants in the selected clusters, interviewing every seventh informal business that they came across on the predetermined path within a cluster. The target was to interview representatives of 15 informal businesses in each cluster and 150 informal business in each district. I did not keep a record of the informal taxpayers who refused to participate, as enumerators simply moved to the next informal businesses without recording those who refused to participate. A total of 267 informal businesses participated in the survey. Appendix 4.11 provides more detail on the sampling method, how the survey was conducted, and data management procedures.

Eighteen questionnaires were excluded from the analysis because they were incomplete (for example, the participant may have decided to stop the interview before completion, or the participant skipped many questions). Thus, 705 completed survey questionnaires remained, representing 254 informal and 451 formal businesses.

4.4.2 Dependent Variables

Similar to the first piece of analysis, in the survey, I asked respondents the question: “Please tell me whether you think the action taken by some business people is

²³ The MRA has details such as the name of the business owner, the trading name, business size, and contact details.

not wrong at all, wrong but understandable, or wrong and punishable: not paying taxes owed to the government.” An individual was considered to have a higher tax morale if their response was “wrong and punishable,” and lower if their response was either “not wrong at all,” or “wrong but understandable.” I created a dummy variable, tax morale, where a value of “1” was given to those who answered “wrong and punishable,” and “0” otherwise. Similarly, as with the second analysis, to test the robustness of this classification, an analysis of tax morale based on each of the three responses (“wrong and punishable,” “wrong but understandable,” and “not wrong at all”) was also undertaken.

4.4.3 Independent Variables

Table 4.4 provides details of the independent variables used in this analysis.

Table 4. 4: Description and measurement of independent variables for the third piece of analysis

Variable	Description	Measurement
Deterrence (DETER)	The respondents were asked to rank their agreement with the following statement: “The consequences of not paying taxes, such as penalties and garnishment imposed by the tax administration, are harsh enough to deter the non-payment of taxes.”	Responses ranged from 0 = “not applicable” to 4 = “very difficult.”
Fiscal exchange (FISCAL)	Respondents were asked to rate their agreement with the statement: “I am satisfied with the level of goods (e.g., roads and bridges) and services (e.g., health and security) that I receive from the government.”	Responses ranged from 1 “Completely disagree” to 5 “Completely agree.”
Trust (TRUST)	Respondent were asked to rate their agreement with the statement: “the Malawi Revenue Authority is trustworthy in its operations.”	Responses ranged from 1 “Completely disagree” to 5 “Completely agree.”

Variable	Description	Measurement
Corruption (CORR)	Respondents were asked about the extent to which they agreed with the statement: “Most tax officials are not corrupt.”	Responses ranged from 1 = “Completely disagree” to 5 = “Completely agree.”
Tax knowledge (TKNOW)	<p>There were four questions relating to business people’s knowledge of the tax system. The respondents were asked to state their level of agreement with the following statements:</p> <ul style="list-style-type: none"> • “I am aware of my rights against unlawful search and seizure by the tax authority.” • “It is my right to claim a tax refund (if any) within specified timeframe.” • “It is my right to know the basis for assessment of my tax liability.” • “I am aware that I have certain rights if I have a problem with the tax office.” 	Responses ranged from 1 = “Completely disagree” to 5 = “Completely agree.” To avoid multicollinearity in the statistical analyses, responses to these questions were merged (a simple average) to create a composite variable.
Female	Gender of respondent.	Dummy variable “FEMALE” was used, where a value of 1 represents female, 0 otherwise.
Large businesses (LARGE)	Business size. Only two groups were created. Large, being those with turnover of more than MK150 million (£150,000), and others (small and	Dummy variable taking a value of “1” for large businesses and “0” for otherwise.

Variable	Description	Measurement
	medium where turnover is less than MK150 million).	
Formal (FORMAL)	Registration status of respondent. Where formal means registered with the revenue authority and informal means not registered with the revenue authority.	This is a dummy variable, taking the value of “1” for formal businesses, and “0” for informal.
Blantyre (BT)	The survey was conducted in Lilongwe and Blantyre.	This is a dummy variable. It takes a value of “1” for respondents who live in Blantyre and “0” for those who live in Lilongwe.
Blantyre (BT)	The survey was conducted in Lilongwe and Blantyre.	This is a dummy variable. It takes a value of “1” for respondents who live in Blantyre and “0” for those who live in Lilongwe.
Accommodation (ACCOM)	Classification of the business of the respondent.	Dummy variable Taking a value of “1” for businesses in the food and accommodation industry, “0” otherwise.
Construction (CONST)	Classification of the business of the respondent.	Taking a value of “1” for businesses in the food and accommodation industry, “0” otherwise.

Variable	Description	Measurement
Transport (TRANS)	Classification of the business of the respondent.	Taking a value of “1” for businesses in the food and accommodation industry, “0” otherwise.
Retail and wholesale (RETAIL)	Classification of the business of the respondent.	Taking a value of “1” for businesses in the food and accommodation industry, “0” otherwise.
Manufacturing (MANUF)	Classification of the business of the respondent.	Taking a value of “1” for businesses in the food and accommodation industry, “0” otherwise.

4.4.4 Method

Similar to the second piece of analysis, I used logit regression analysis to find the determinants of tax morale among business people in Malawi. The equation used in the analysis is presented below:

$$TM_y = \beta_0 + \beta_1 DETER + \beta_2 FISCAL + \beta_3 CORR + \beta_4 TKNOW + \beta_5 FEMALE + \beta_6 BT + \beta_7 LARGE + \beta_8 FORMAL + \beta_9 ACCOM + \beta_{10} CONST + \beta_{11} MANUF + \beta_{12} RETAIL + \varepsilon \quad (2)$$

In Equation 2, TM_y is the score for tax morale for individual y , β is a vector of regression coefficients, and ε is the error term. TM_i is the score for tax morale for an individual, β is a vector of regression coefficients, and ε is the error term. DETER refers to deterrence factors; FISCAL refers to fiscal exchange factors; CORR is perception of level of corruption in the revenue authority; TKNOW is the respondent's level of tax knowledge; FEMALE is a dummy variable representing female; BT is a dummy variable

taking a value of 1 if the respondent conducts their business in Blantyre, and 0 otherwise; LARGE is a dummy variable taking a value of 1 if the business is large; FORMAL is a dummy variable taking a value of 1 if the business is registered with the revenue authority, 0 otherwise; ACCOM is a dummy variable taking a value of 1 if the business is in accommodation services; CONST is a dummy variable taking a value of 1 if the business is in construction, 0 otherwise; MANUF is a dummy variable taking a value of 1 if the business is in manufacturing, 0 otherwise; RETAIL is a dummy variable taking a value of 1 if the business is in wholesale and retail, 0 otherwise. My own survey data was used to estimate this equation.

4.4.5 Empirical Results and Analysis

Descriptive Statistics and Correlation

Appendix 4.12 reports the descriptive statistics for the variables used in this analysis. The Pearson pairwise correlation coefficients for the dependent and independent variables in this analysis are summarised in Table 4.5. Table 4.5 shows that there are correlations between TM and some independent variables. Specifically: TM and DETER; TM and FISCAL; TM and CORR; TM and LARGE; and, TM and BT. However, no correlation was found between TM and TKNOW, or between TM and any of the various sectors of the economy (retail, manufacturing, construction, transport, and accommodation).

Table 4. 5: Pearson Correlations for Dependent and Independent Variables

Variable	1	2	3	4	5	6	7	8	9	10	11	12	13	14
1 TC	1													
2 DETER	0.22***	1												
3 FISCAL	0.14***	0.22***	1											
4 TKNOW	-0.06	-0.04	0.04	1										
5 CORR	(0.13)***	(0.25)***	(-0.29)***	(0.14)***	1									
6 LARGE	0.09***	0.07*	0.05	0.15***	-0.06	1								
7 BT	(0.19)***	(0.08)**	0.01	-0.07	(0.08)**	(0.08)*	1							
8 REGIST	0.04	(0.08)**	(0.07)*	0.28***	0.02	0.19***	0.02	1						
9 FEMALE	0.02	0.03	0.02	-0.02	0.04	(0.05	0.06*	(0.09)**	1					
10 RETAIL	-0.05	0	-0.01	(0.26)***	0.05	(0.15)***	0.13***	(0.34)***	0.07	1				
11 MANUF	0.04	0.06*	-0.04	0.03	0	0.16***	(0.01	0.05	(0.13)***	(0.2)***	1			
12 ACCOM	0.02	-0.05	0.03	0.03	0.05	-0.03	-0.05	0.07**	0.05	(0.027)***	(0.06)*	1		
13 CONST	-0.04	0	0	0.05	-0.03	0.09**	-0.01	0.1***	-0.3	(0.15)***	-0.04	(0.05	1	
14 TRANS	-0.01	0	0.03	0.01**	-0.02	0.17***	0.01	0.15***	0	(0.18)***	-0.04	-0.06	0.03	1

Notes:

- Variable definitions: TC, tax compliance; DETER, economic deterrence; FISCAL, fiscal exchange; TKNOW, tax knowledge; FEMALE, female; URBAN, urban; LL, Lilongwe; CORR, corruption; BSIZE, business size; BT, Blantyre; REGIST, business registration status; RETAIL, retail; MANUF, manufacturing; ACCOM, food and accommodation; CONST, construction.
- N = 704 for all variables
- *Significant at .10 level; **Significant at .05 level; ***Significant at .01 level.

Logit Regression Results

Logit regression was used to estimate Equation 2, using my own survey data.

Table 4.6 presents a summary of the binary logit estimation.

Table 4. 6: Binary Logistic Regression with Marginal Effects

Variable	Model 1A	Model 1B	Model 2
DETER	0.077 (0.019)***	0.032 (0.06)**	0.083 (0.023)***
FISCAL	0.018 -0.012	0.135 0.044***	0.001 -0.013
TKNOW	-0.048 (0.024)**	-0.048 (0.063)**	-0.029 (0.021)***
CORR	-0.032 (0.023)***	-0.011 (0.06)***	-0.041 (0.014)***
FEMALE	0.056 (0.046)	0.101 (0.099)	0.108 (0.056)*
BT	0.12 (0.025)***	0.203 (0.122)*	0.17 (0.048)***
LARGE			0.07 (0.035)**
FORMAL			0.018 -0.064
RETAIL			0.051 -0.103
MANUF			0.082 -0.131
ACCOM			0.052 -0.103
CONST			-0.269 (0.123)**
TRANS			-0.051 -0.095

Notes:

1. Variable definitions: TC, tax compliance; DETER, economic deterrence; FISCAL, fiscal exchange; TKNOW, tax knowledge; FEMALE, female; URBAN, urban; LL, Lilongwe; CORR, corruption; BSIZE, business size; BT, Blantyre, REGIST, business registration status, RETAIL, retail; MANUF, manufacturing; ACCOM, food and accommodation; CONST, construction.
2. *Significant at .10 level; ** Significant at .05 level; *** Significant at .01 level.
3. Dependent variable= dummy taking a value of 1 if individual thinks it is wrong and punishable not to pay taxes, 0 otherwise.

In Table 4.6, Model 1A is an estimation of tax morale, using my own survey data. For comparative purposes, Model 1B is similar to 1A, but was estimated using the average of R5 and R6 Afrobarometer data for Malawi. Model 2 is an estimation of Equation 2, as presented in Section 4.4.4, using my own survey data.

The results from Model 1A and 1B are broadly similar. The only difference is in the impact of fiscal exchange on tax morale, where FISCAL is not significant in Model 1A, but positive and significant in Model 1B. In both models (1A and 1B), DETER is positively correlated with tax morale, TKNOW is negatively correlated with tax morale, corruption is negatively correlated with tax morale, and Blantyre is positively correlated with tax morale. These results suggest that DETER, CORR, TKNOW, and BT businesses are some of the key factors driving business people's tax morale in Malawi. It can also be noted from Model 1A that DETER has the greatest impact on tax morale: a unit increase in DETER increases tax morale by eight percentage points, while a unit increase in tax knowledge and corruption decreases tax morale by five and three percentage points, respectively.

In Model 2, in addition to the variables included in Model 1A (or 1B), variables capturing the perceptions of business people in various groups were also included. The results were as follows:

- a. Tax morale among large businesses (LARGE) is seven percentage points higher than tax morale among small or medium businesses.
- b. Businesses operating in Blantyre (BT) have a 17-percentage point higher tax morale than businesses operating in Lilongwe.
- c. Businesses in the construction sector (CONST) have a 27-percentage point lower tax morale than businesses operating in other sectors.
- d. No variation in tax morale was found between businesses in formal (FORMAL) and informal, retail (RETAIL) and other sectors, manufacturing (MANUF) and other sectors, accommodation (ACCOM) and other sectors, and transport (TRANS) and other sectors.

Post-estimation Tests for Model 2 Regression

As was the case with the first analysis, once Model 2 had been estimated, the

Wald test and the Hosmer–Lemeshow Goodness of Fit post-estimation tests were conducted. The results of the Wald test – all the regressing coefficients are jointly zero – show that the null hypothesis is rejected at a 1% level of significance (p-value = 0.000) (see Appendix 4.13). This implies that all the variables included in the regression create a statistically significant improvement in the fit of the model. Similarly, the Hosmer–Lemeshow Goodness of Fit test showed that the model has good fit (p-value = 0.1834) (see Appendix 4.14).

Robustness Check

Similar to the comparative analysis, to check the robustness of the binary results, the ordered logit regression was estimated to separately determine the tax morale of people who answered, “wrong and punishable,” “wrong but understandable,” and “not wrong at all.” Appendix 4.15 shows the results of the ordered logit regression. The results are consistent with the findings of the binary logit regression presented in Table 4.5. Specifically, business people who perceive that they will be caught and punished for non-compliance were more likely to respond “wrong and punishable” than “wrong but understandable” or “not wrong at all.” Similarly, business people were less likely to respond “wrong and punishable” if they perceived that more tax officials are corrupt (more corrupt tax officials) than those who responded “wrong but understandable” or “not wrong at all.”

4.5. Discussion

Based on the country averages of tax morale, the first piece of analysis has shown that tax morale in Malawi is within the range for countries in SSA when the merged data for R5 and R6 is used.

Similarly, the results of the second piece of analysis using R5, R6, and the merged data for R5 and R6, showed that when R5 data was used, tax morale in Malawi is significantly lower than the average for SSA countries. The results of the regression when R6 data was used showed that tax morale in Malawi is significantly higher than the average for SSA countries. The results of the regression when the merged data for R5 and R6 was used showed that tax morale in Malawi is within the range for SSA countries. Based on the understanding that it is reasonable to believe that the results of the regression when the merged data was used are closer to representing the tax morale

in Malawi during a stable economic and political environment, these results show that tax morale in Malawi is within the range for SSA countries. Another important finding from the second piece of analysis was the various factors included in the model have an impact on tax morale in SSA. However, people's perception of corruption in the revenue authority, people's perception of being found and punished for non-compliance (DETER), and people's knowledge of the tax system (TKNOW) have a bigger impact on tax morale in Malawi compared to other SSA countries.

The results of the third piece of analysis, the analysis of business people's tax morale in Malawi, showed that the tax morale in Malawi is significantly higher among large businesses compared to small or medium-size businesses, and is higher for businesses operating in Blantyre compared to business operating in Lilongwe. However, businesses in the construction sector showed a lower tax morale compared to those in other sectors. The fact that large businesses in Malawi have a higher tax morale than small or medium-size businesses suggests that, although tax morale in Malawi is not higher than the average for SSA countries, the high tax morale among large taxpayers in Malawi and businesses operating in Blantyre may be translating to higher tax payments. This may partly explain the good tax revenue collection in Malawi.

It is surprising to find that business people operating in the district of Lilongwe have different levels of tax morale to those operating in Blantyre, considering that businesses in both areas are subject to a similar tax system. A possible explanation for the difference in tax morale between Lilongwe and Blantyre business people may be political affiliation and/or the lower visibility of MRA officers in Lilongwe compared to Blantyre. In terms of political affiliation, Malawi has two dominant political parties, the Malawi Congress Party (MCP) and the Democratic Progressive Party (DPP). The MCP is the most popular party in the central region, where Lilongwe is located, and the DPP is the most popular party in the southern region, where Blantyre is located. The DPP is currently the ruling party, winning the 2014 presidential election by a narrow margin (Patel & Wahman, 2015). Thus, it is possible that a large proportion of people in Lilongwe, who are mostly strong supporters of the MCP, have lower tax morale as a form of protest against a DPP government. In terms of higher visibility of MRA officers in Blantyre, the MRA headquarters are located in Blantyre, which may account for the difference in visibility of its officers compared to Lilongwe. The high number of officers in Blantyre may create a perception that taxpayers are being watched more closely.

Alternatively, due to the high number of officers in Blantyre, there may be more frequent interaction between MRA officers and taxpayers through random taxpayer visits or tax audits, which may also increase tax morale.

It is also surprising to find that businesses in the construction sector have lower tax morale than those in other sectors, considering that there is no variation in the level of tax morale between businesses in retail or manufacturing and other sectors. One possible explanation for this is that businesses in the construction sector are not closely monitored by the revenue authority, as is the case with retailers and manufacturers. Although all businesses in Malawi with an annual turnover of MK10 million (£10,000) operate electronic fiscal devices (EFDs) to account for VAT sales, businesses in retail and manufacturing are closely monitored (e.g., with random checks and mystery shopper programmes) to check if these EFD devices are being used with each customer. By contrast, businesses in the construction sector are not closely monitored because their sales transactions are less frequent.

4.6. Conclusion

This chapter has presented the results of three pieces of analyses conducted to explore tax morale in Malawi. The aims of this chapter were to: determine if Malawians are any more or less willing taxpayers than the people in other SSA countries; determine the drivers of Malawians willingness to pay taxes; and to explore tax morale among business people in Malawi in order to shed light on which of the different business groups are contributing to the good tax revenue performance in Malawi.

The three analyses conducted in this chapter were based on perception survey data from the R5 and R6 Afrobarometer surveys, and my own survey data. Both the Afrobarometer surveys and my survey included a series of theoretically rooted questions centred around individuals' and business people's attitudes towards taxation and tax morale. The key conclusions drawn from the three analyses presented in this chapter are as follows:

First, Malawians are not any more or less willing taxpayers than the populations in other SSA countries.

Second, the second and third pieces of analyses provide robust results supporting the following theoretically grounded determinants of tax morale:

1. Deterrence and enforcement: taxpayers have higher tax morale when they perceive that they will be caught and punished for evading taxes. This is in line with the deterrence theory of tax morale.
2. Fiscal exchange: there is also evidence supporting the idea that individuals and businesses that are more satisfied with public service provisions, such as health and education, have higher tax morale.
3. Comparative treatment: it was found that when individuals perceive that they are treated fairly, tax morale increases.
4. Corruption: the analyses revealed evidence that an increase in the perception that there is high corruption among tax officials reduces tax morale among individuals and businesses.
5. Tax knowledge: evidence suggested that individuals and businesses that are knowledgeable about tax issues have lower tax morale.

Third, this chapter has shown that, despite the fact that tax morale in Malawi does not differ significantly from other SSA countries, within the business community, there are certain groups of taxpayers with a higher tax morale. Specifically, businesses operating in Blantyre have higher tax morale than businesses operating in Lilongwe, and large businesses have higher tax morale than small or medium-size businesses. These groups of taxpayers may be partly contributing to the overall good tax revenue performance in Malawi. This conclusion is drawn while being mindful of the fact that tax morale relates to people's attitudes and not their behaviour. Thus, while studying tax morale can reveal factors that may improve an individual's morale, the extent to which that morale (attitude) translates into tax compliance (behaviour) remains unknown.

Finally, this chapter has shown that it is difficult to study tax morale in any meaningful way when using survey data. This is because survey data is cross-sectional (i.e., it measures individuals' attitudes at a given point in time). However, an individual's attitude at any given time is influenced by several factors and may not be reflective of their attitude over time. For example, had the first and second piece of analysis been based solely on the R5 Afrobarometer survey, the conclusion would have been that tax morale in Malawi is lower than the average for other SSA countries. On the other hand, had the analysis been based solely on the R6 Afrobarometer survey, the conclusion would have been the opposite. It was only because data from both periods (R5 and R6) was used, and further investigation was carried out on why the tax morale

for these two periods differed significantly, that I was able to determine whether the R5 and R6 results reflected the actual tax morale in Malawi under normal circumstances.

Chapter 5: Assessing the Performance of the Malawi Revenue Authority

5.1 Introduction

Tax administration plays an important role in ensuring that there is sufficient revenue for the smooth operation of the government. Tax administration involves the management, conduct, direction, and supervision of the execution and application of a country's tax law, tax legislation, and related statutes (Devas, Delay, & Hubbard, 2001). The core functions of a tax administration include, *inter alia* (Alink & Van Kommer, 2016; Kidd, 2010):

1. registration of taxpayers, including detection of non-registration and false registration;
2. assessment, billing and collection of taxes;
3. processing of tax returns, withholdings, and third-party information;
4. verification or examination of the correctness and completeness of the received information (including audit activities);
5. the process of enforced debt collection;
6. handling of administrative appeals and complaints;
7. provision of services and assistance to taxpayers;
8. detection and prosecution of tax fraud; and
9. internal anti-corruption.

As highlighted in Chapter 2, tax administration in Malawi is the responsibility of the Malawi Revenue Authority (MRA). Specifically, the MRA is responsible for the assessment, collection, enforcement, and accounting of tax revenues. It is governed by a board of directors and supervised by the Ministry of Finance. A Commissioner General heads the institution and is assisted by a management team comprising a Deputy Commissioner General, two commissioners (who are responsible for domestic taxes and customs and excise), seven directors, and three deputy directors (see Appendix 2.1 for an MRA organogram). When the MRA was formed in 2000, it was internally structured according to the tax type. However, this resulted in the duplication of work. Accordingly, in 2009, the structural arrangement was changed subsequently being based on function and taxpayer segment. At the beginning of the 2017/2018 fiscal year, the

MRA had 1,450 staff members and an operating budget of MK27 billion (£27 million) (3% of the MRA's annual tax revenue collection).

Mascagni, Moore and McCluskey (2014) suggest that the efficiency and effectiveness of a tax administration in undertaking its functions (i.e., process performance) is one of the contributing factors to low revenue collection in low-income countries compared to high-income countries. However, when judged by the standard criteria for effective tax administration, as done under the Tax Administration Diagnostic Assessment Tool (TADAT) (TADAT Secretariat, 2015a), the MRA appears to perform very poorly, even by the standards of low-income countries. These observations are in tension with the facts that the Malawi Revenue Authority (a) is rather effective at capturing a relatively high proportion of GDP in tax (Chapter 2), and (b) collects a high proportion of that through what is normally seen as a very challenging channel, i.e. direct taxes on corporate profits (CIT) and on employment income (PIT) (Chapter 6). Accordingly, the question explored in this chapter is: to what extent do the tax administration processes followed by the Malawi Revenue Authority affect the level of tax revenue collection and structure of the tax system in Malawi? I explore this issue by examining the MRA's process performance in four out of the nine areas assessed under TADAT, namely:

1. Taxpayer registration and data management
2. Detection and prosecution of tax fraud through tax audit
3. Handling of administrative appeals and complaints through a dispute resolution process
4. Provision of services and assistance to taxpayers, such as taxpayer education

The analysis is based on qualitative data collected through semi-structured interviews conducted with MRA officials, analysis of MRA documents (such as Annual Reports, Strategic Frameworks, and Management Reports), the TADAT report for Malawi, and information that I collected from carrying out a survey of business people in Malawi (as discussed in Chapter 4).

The main finding of this analysis is that the apparent paradox – the poor performance of the MRA even by the standards of low-income countries on one side, and the institution's effectiveness at capturing a relatively high proportion of GDP in

tax and collection of a high proportion of direct taxes on CIT and PIT on the other – is largely explained by the relative efficiency of the Large Taxpayer Unit (LTU). The LTU is responsible for administering only 2% of total taxpayers yet collects 70% of total tax revenues. However, the LTU itself is not well-equipped from a technological perspective. It relies heavily on some very basic software for recording taxpayer information. However, the LTU staff interact closely with the staff of large companies and understand their clients' businesses well. This has enabled the LTU to collect significant revenues from the large taxpayers. This brings me to a set of issues explored further in Chapter 6: the long-standing economic dominance in the Malawian economy of a few large firms; and the fact that, unlike in many countries, those firms have been unable to use their economic dominance to avoid taxes on a large scale.

The remainder of this chapter is organised as follows: Section 2 is a literature review focusing on the Tax Administration Diagnostic Assessment Tool (TADAT), the main tool used to evaluate tax administration performance in low income countries. Section 3 covers the methodology and analysis of the study findings. This section explains how the data used in the analysis was collected, and the findings for each of the four areas the MRA was assessed on. Section 4 is a discussion of the findings, and Section 5 concludes the chapter.

5.2 Assessing Tax Administration Performance in Low-Income Countries

In many countries, performance measurement has become one of the symbols of the transformation of governance (Le Galès, 2016). Davis, Fisher, Kingsbury, and Merry (2012) point out that there has been a proliferation in the use of indicators as policy instruments with various institutions (international development agencies such as the World Bank and the UN, national governmental aid agencies such as US governments Millennium challenge corporation, and global businesses and investors). One area in which there has been a development of performance measures is on tax administration. Since 2015, the Tax Administration Diagnostic Assessment Tool (TADAT) has been widely used as a tax administration performance measurement tool, especially in low-income countries. TADAT is not public and has no simple aggregate measure attached to it. However, there are other public and simple tools which are used to assess the tax administration performance. These include the following:

1. The public expenditure and finance accountability (PEFA) on which the TADAT was based. Using PEFA, a tax administration is assessed on the following aspects: the aggregate revenue outturn, which captures only negative variations and measures forecasting accuracy but does not identify the reasons why the forecasts might be inaccurate; the clarity and comprehensiveness of legislation and procedures; taxpayers' access to information, existence and functioning of an appeal mechanism; taxpayer registration, penalties for non-registration and non-filing, and planning and monitoring for audits and investigations; arrears and the collection ratio, the effectiveness of transfers to the treasury, and the frequency of reconciliations.
2. The OECD's comparative information series, which covers the following: institutional and organizational arrangements for tax administration operations; the description of management practices; a comparison of the tax filing and payment obligations for the major taxes (PIT, CIT and VAT); a summary of selected administrative powers given to revenue bodies to carry out their mandate; a comparison of the country's tax burdens.
3. The International Survey on Revenue Administration (ISORA), which is an extension of the OECD's comparative information series. It comprises a survey to collect tax administration data from national or federal tax administrations. It surveys tax administration operations and other characteristics based on common questions and definitions agreed by four partner organizations: The Inter-American Center of Tax Administrations (CIAT), the IMF, the Intra-European Organisation of Tax Administrations (IOTA), and the Organisation for Economic Co-operation and Development (OECD). The survey collects information in three areas of tax administration: (1) performance-related data, (2) profile data, and (3) data on administrative and operational practices. A country's participation in this survey is voluntary. One key limitation of ISORA is that it uses an online data collection platform. No verification regarding the accuracy of the available information is conducted.

The pioneering efforts of the TADAT Secretariat to collect comparative information about tax administrations in low-income countries has already started to bring positive change (Adam Smith International, 2018), and recent empirical studies on tax administration process performance in low-income countries are already drawing

on this new database (Moore & Wilson, 2017; Bogere, 2018). As it is the most comprehensive and widely used tool to assess tax administration performance in low-income countries, this review of tax administration performance in low-income countries will focus on TADAT.

5.2.1 TADAT Overview

TADAT is a standardised approach to diagnosing tax administration performance that pinpoints the relative strengths and weaknesses of a country's tax administration (TADAT Secretariat, 2015b). TADAT focuses on nine key performance outcome areas (POAs), which cover most of the functions, processes, and institutions of tax administration (Figure 5.1).

Figure 5. 1: TADAT Performance Outcome Areas

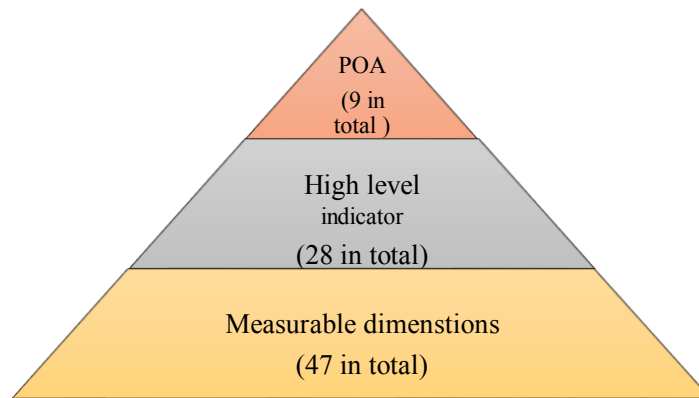


Source: TADAT Secretariat (2015)

As shown in Figure 5.1, the nine POAs are: integrity of registered taxpayer base, effective risk management, supporting voluntary compliance, timely filing of tax declarations, timely payment of taxes, accurate reporting in declaration, effective tax dispute resolution, efficient revenue management, and accountability and transparency.

The TADAT framework has a hierarchical, pyramid-style format (Figure 5.2):

Figure 5. 2: TADAT Framework



Source: Author's own depiction

Figure 5.2 shows that at the apex of the TADAT framework are the nine POAs. Based on these outcomes, the level of maturity of a tax administration system, in the context of international good practice, is ascertained. The POAs are linked (at the second level) to 28 high-level 'indicators' that are critical to tax administration performance. The 28 indicators are then linked to 47 measurable dimensions (third level), with detailed assessment criteria, that form the basis of evaluating the performance of the system of tax administration (see Appendix 5.1 for detailed information on the high-level indicators and the dimensions). A four-point ABCD scale is used to score each dimension and indicator, and scores are consolidated from the dimension to the indicator level. The POAs themselves are not scored. The scoring criteria for each indicator, and the methodology used to calculate the dimension scores, are detailed in the TADAT Field Guide (TADAT Secretariat, 2015b), as follows:

- A- Denotes performance that meets or exceeds international good practice. For TADAT purposes, good practice is taken to be a tested and proven approach applied by a majority of leading tax administrations. It should be noted, however, that a process does not need to be at the forefront of technological advancement to be considered good practice. Given the dynamic nature of tax administration, good practice – described throughout the field guide – can be expected to evolve over time, as technological advances and innovative approaches are tested and gain wider acceptance.
- B- Represents sound performance (i.e., a healthy performance but below the level of international good practice).
- C- Denotes weak performance, relative to good practice.
- D- Denotes inadequate performance and is applied when the requirements for a C

rating or higher are not met. Furthermore, a D score is given in certain situations where there is insufficient information available to assessors to determine and score the level of performance (e.g., in areas of filing, payment, and refund processing). The underlying rationale is that the inability of the tax administration to provide the required data is indicative of deficiencies in its information management system and performance monitoring practices.

5.2.2 TADAT Assessment Procedure

The TADAT manual (TADAT Secretariat, 2019) states that TADAT assessments are usually initiated by either a country's Ministry of Finance or tax administration, or by international/regional agencies (e.g. African Development Bank, African Tax Administration Forum, Asian Development Bank, European Commission, International Monetary Fund (IMF), Inter-American Development Bank, and World Bank). The TADAT assessments are conducted by an assessment team typically comprising 3–4 trained assessors. The analysis is conducted in four (4) phases. The first phase is when a formal request from the country authorities is made to the sponsoring organisation (e.g. IMF, World Bank), or directly to the TADAT secretariat. The letter indicates the desired timing of the assessment. The second phase is the assessment team's planning and preparation phase. The third phase constitutes the in-country assessment. The critical work of a TADAT assessment occurs during the third phase, which typically takes 2–3 weeks before the preliminary report is produced. The key tasks conducted during this phase include the following:

1. An opening meeting with the minister (if appropriate) and the head and senior management team of the tax administration. The aim of this meeting is to (1) acquaint the senior officials with the objectives, processes, and outputs of the TADAT diagnostic approach (this may entail a short presentation of the TADAT framework), (2) discuss the assessment team's work program; and (3) respond to questions and issues raised.
2. A series of meetings with tax officials. The aim of these meetings is to gather information and evidence regarding each indicator and measurement dimension. In conducting these meetings, the assessors use the checklists of questions and examples of evidence set out in the field guide. Follow-up meetings, including the validation of evidence, may also be conducted.

3. A walkthrough of the work processes of operational/field offices, including the large taxpayer office.
4. Scoring each dimension and indicator based on an analysis of the evidence gathered. Each dimension is scored based on the following key questions:
 - a. What is the TADAT's good practice standard or criterion?
 - b. Who, at the tax administration's head office, is accountable for communicating the good practice standard, its implementation, and the related monitoring of performance?
 - c. Are the tax administration's documented and approved standard operating rules, instructions, processes or procedures consistent with the good practice standard?
 - d. Is the good practice standard implemented uniformly across the tax administration as a whole, and not selectively or in a fragmented manner?
 - e. Did the tax administration provide or allow access to the good practice standard monitoring and impact analysis reports?

The fourth phase is the post-assessment phase. The TADAT report produced in phase three is finalised during this phase.

5.2.3 Summary of the TADAT Assessment Results

As of January 2019, 63 assessments had been conducted using TADAT. Out of the 63 assessments, 14 assessment reports are freely available on the TADAT Secretariat website.²⁴ The TADAT reports are confidential and are only published on the TADAT Secretariat website with consent from the government concerned.²⁵ Appendix 5.2 is a summary of the results of the 14 published and available TADAT assessment reports. As Moore and Prichard (2017) observe, if one assumes that the available reports cover a representative sample of countries, the results of the assessments, overall, show the following:

1. Tax administration performance in many low-income countries is poor, as the

²⁴ <http://www.tadat.org>

²⁵ Countries with their TADAT assessment report published on the TADAT website are: Alagoas (State of Alagoas, Brazil), Armenia, Burkina Faso, Georgia, Guatemala, Jordan, Kyrgyz Republic, Liberia, Peru, Rio de Janeiro, Trinidad and Tobago, Ukraine, and Zambia. A TADAT assessment was also conducted in Malawi.

scores given by assessors are generally low. Overall, the score allocation is as follows: A – 15%; B – 15%; C – 32%; and D – 38%. Peru has the strongest performance, receiving an A for 15 of the 28 items. No other country, out of the 14 available reports, received an A rating for more than six items. Liberia, Trinidad, Tobago, and Burkina Faso show the poorest scores, receiving a D for 19, 18, and 18 of the 28 items, respectively. Malawi was assessed on 25 items (instead of 28) and received Ds for 19 of the items assessed (see Appendix 5.2).

2. The digital management and accounting tools that are available to tax authorities are often underutilised. Comparing the scores for ‘use of electronic filing facilities’ and ‘use of electronic payment methods’ with the scores for ‘adequacy of the tax revenue accounting system’ for the 14 countries, out of the 28 scores for ‘use of electronic filing facilities’ and ‘use of electronic payment methods’: 50% are As; 7% are Bs; 21% are Cs; and 21% are Ds. By contrast, out of the 14 scores for ‘adequacy of the tax revenue accounting system’: 7% are As; 0% are Bs; 57% are Cs; and 36% are Ds.

Malawi had a TADAT assessment in 2015. Although the authorities have not consented for the assessment report to be published on the TADAT website, the recently published Development Finance Assessment for Malawi (Besharati & Loga, 2018) contains the results of the assessment. The results show that the MRA’s performance is very poor. The MRA scored a D in 19 out of the 25 indicators on which it was assessed. This result is surprising considering that the tax-to-GDP ratio for Malawi has been increasing since the MRA started operating in 2000. Since tax administration plays a key role in tax revenue collection performance, as argued by Bird et al. (2008), one would expect the increase in tax revenue in Malawi, especially that between 2005 and 2011, to be associated with good tax administration process performance. Based on the TADAT results, this does not appear to be the case for Malawi. Thus, this chapter will attempt to understand why Malawi has a high tax revenue performance compared to other SSA countries despite the lack of efficiency and effectiveness in its tax administration.

5.2.4 Benefits and Limitations of TADAT

I note that the key benefits of TADAT are that:

1. It provides a benchmark from which a revenue authority can set targets for improvement.
2. The results of the assessment can be used to facilitate a shared view on the condition of the system of tax administration among stakeholders (country authorities, international organisations, donor countries, and technical assistance providers).
3. It can help to monitor and evaluate reform progress by way of subsequent repeat assessments.

TADAT has at least three limitations:

1. TADAT does not offer solutions to challenges or weaknesses it identifies. The TADAT approach only provides an indication of how the country's administration deviates from what seems to be best practice, but does not provide ways of solving those problems.
2. TADAT assessments are standardised, which means all tax administrations are assessed using similar criteria. The challenge with the standardised approach is that how a tax administration performs in practice largely reflects several underlying determinant factors. These include the context of tax administration within the public sector, the economic environment (e.g., the size of the informal sector), the political environment (e.g., the degree of support for effective enforcement), the legal and regulatory framework, and the managerial system of the tax administration. Thus, simply assessing performance in specified institutional activities, and then comparing that performance to some subjectively established goal, does not provide a meaningful basis for diagnosing the problems with any particular administration, unless one also considers the environment in which the administration functions.
3. In some cases (as is the case of Malawi), high or low TADAT indicator scores do not correlate closely with tax revenue collection outcomes. Out of the 14 published TADAT reports, Malawi has the lowest scores for all indicators, yet its tax revenue collection performance is relatively good.

These limitations do not mean that TADAT is not a useful tool. Rather, they indicate that TADAT assessment reports must be interpreted with these limitations in mind.

5.3 Methodology

As indicated in the introduction, this analysis assesses the MRA's performance in four areas (taxpayer registration and data management, detection and prosecution of tax fraud, handling of administrative appeals and complaints, and provision of services and assistance to taxpayers). Only four of the nine POAs assessed in TADAT are assessed in this study, due to limited access to taxpayer information from the MRA. I was only granted access to aggregate taxpayer data (such as how much tax is collected from taxpayers classified as large) and not disaggregated taxpayer data (such as how much each of the taxpayers classified as large pays in a year). Under Malawian law, only tax officers have access to disaggregated taxpayer data (Section 6 (2), Malawi Taxation Act, 2006). I was therefore unable to have access to data related to some POAs, such as timely filing of tax returns, timely payment of taxes, and accurate reporting in declaration. Assessing the MRA's performance in fulfilling these functions would have required accessing individual taxpayer details. Nevertheless, the four functions analysed have been identified in the literature as being among the most important activities undertaken by a tax administration, if it is to be effective in raising revenue (Kidd, 2010; Ter-Minassian, 1997).

The analysis of the efficiency and effectiveness of the MRA in carrying out its functions is based on both primary and secondary data. Primary data was collected between October 2016 and April 2017 using semi-structured interviews (17 in total) with MRA officers, and a survey of business people that I conducted (see Chapter 5). From the MRA, interviews were conducted with the Commissioner General, the Commissioner for Domestic Taxes, the Deputy Commissioner for Domestic Taxes, technical staff in the Domestic Taxes Division (Technical Unit, Modernisation Unit, Large Taxpayer Unit, and Audit Unit), staff in the Policy Planning and Research Department, and staff in Taxpayer Education Services. Information from taxpayers was used to cross-check the information provided by MRA officers, as well as the information in various documents. Secondary data was obtained from the MRA's corporate plan, Acts (Taxation Act, Customs and Excise Act, Value Added Act, and MRA Act), and MRA documents (Annual Reports, Strategic Plans). This information was used as a reference to verify whether what happens on the ground is in line with what is specified in law.

5.4 Findings

5.4.1 Tax Registration and Data Management

Registration of taxpayers and management of the taxpayer registry underpins key administrative processes, such as filing, payment, assessment, and collection of taxes (Brondolo & Zhang, 2016). Thus, one of the most important functions of any revenue administration is to identify potential taxpayers, register them, and properly manage the collected information for easy access and use.

Registration

Anyone operating a business in Malawi is required to register with the MRA for tax purposes, either under the standard income tax regime²⁶ or the turnover tax regime.²⁷ Businesses whose annual gross income is below MK10 million (£10,000) are registered under the turnover tax regime, while those whose annual gross income exceeds MK10 million are registered under the standard scheme.²⁸ Taxpayers in the standard regime are further classified as either small, medium, or large.²⁹ A special department known as the Large Taxpayer Unit (LTU) within the Domestic Revenue Department manages large taxpayers. Initially, a business chooses the type of taxes to register for. Individuals operating a business that is not incorporated register for personal income tax (PIT) and ‘Pay As You Earn’ (PAYE) for their employees. Unincorporated businesses may also register for withholding tax (WHT),³⁰ value added tax (VAT), or excise tax, depending

²⁶ Businesses registered under the standard income tax regime are required to keep books of accounts, submit tax returns, and pay income tax at the rate of 30% on profits.

²⁷ Businesses registered under the turnover regime pay 2% income tax on their gross income. They are not required to submit detailed books of accounts.

²⁸ In principle, business registered under the turnover tax regime are graduated to the standard regime by the MRA once their annual turnover exceeds the threshold.

²⁹ The MRA classifies taxpayers as large, medium, and small. To qualify as a large taxpayer, either of the following conditions have to be met: a) have annual turnover of at least MK750 million (£750,000), b) paying cumulative taxes (Excise Tax, PAYE, Corporate Tax, VAT, etc.) of over MK450 million (£450,000) or above per annum, c) importing goods valued at MK750 million or above per annum, d) operating in a financial or mining sector, e) being an operator of Excise Tax, f) being an associated or related company whose parent company is a large taxpayer. Medium taxpayers are businesses whose annual turnover is between MK150 million (£150,000) and MK750 million (£750,000), while small taxpayers are those whose annual turnover is less than MK150 million.

³⁰ Withholding tax is an advance payment of income tax that is deducted from specified payments. The person making the payment deducts the tax. Any individual, partnership, trust, association, company, club, statutory body, council, government ministry or department, or any religious organisation, as long as it makes payments to any person, is eligible to register with the MRA and

on their turnover and the type of business they undertake.³¹ Incorporated businesses are registered for corporate income tax (CIT), PAYE, WHT, and VAT. They may also register for excise tax if they are supplying excisable goods.

In 2010, the MRA embarked on a project to register as many taxpayers as possible under the turnover tax regime. Over 200 temporary officers were hired to identify and register potential taxpayers. The MRA database shows that taxpayers registered under the turnover tax regime make up 35% of all registered taxpayers but account for just 1% of total tax revenue collected by the institution. Regardless, the MRA continues to register taxpayers under the turnover tax regime due to their senior officers' contract renewal being performance-based, where one measure of good performance is the number of new taxpayers that they register.

In total, more than 70,000 taxpayers are registered with the MRA. However, in the 2015/16 fiscal year, only 32,000 were classified as active. Taxpayers classified as active are those that have filed a tax return or made a tax payment within the past three years. MRA officers have suggested that some taxpayers register with the MRA so that they receive a registration certificate and a taxpayer identification number (TIN),³² which enables them to deal with government and other registered traders.³³ Once taxpayers have the MRA registration certificate, most do not pay the turnover tax. The MRA does not follow up with inactive registered taxpayers to determine whether they have stopped operating or whether they have just stopped paying taxes. One way of establishing whether taxpayers who do not file tax returns, or make any tax payment, are still economically active is by using third-party information, such as WHT receipts.³⁴ WHT receipts show details of taxpayers from whom the money is withheld, and the type

operate withholding tax. Withholding tax is deducted using specified rates. The rates are specified in the 14th Schedule to the Malawi Taxation Act.

³¹ Only business whose turnover is in excess of MK10 million (£10,000) are required to register for VAT.

³² Instead of using names to identify taxpayers, the MRA issues a unique number to each taxpayer on registration called the Taxpayer Identification Number (TIN).

³³ By law, the Malawi Government deals only with suppliers that have an MRA registration certificate. Private companies, on the other hand, are not governed by similar laws. However, most registered private companies also require an MRA registration certificate to deal with them, as a social responsibility to ensure that other businesses also pay tax. The MRA further indicates that dealing with other registered taxpayers also helps a company to easily qualify for a withholding tax exemption certificate, which allows the company to deduct withholding tax when they supply other registered companies.

³⁴ All registered taxpayers are required to withhold a specified percentage of money (depending on the goods or transaction being purchased) on payments made to suppliers and remit the money to the MRA. The supplier is issued with a Withholding Tax receipt showing the amount deducted, a copy of which is given to the MRA when the buyer is remitting the withheld money to the MRA.

of transaction involved.

Data Management

A capable tax administration must deal systematically with a high volume of information. Practitioners thus regard the use of information technology (IT) as a crucial feature of successful tax administration reform projects (Berman & Tettey, 2001).

Officially, the MRA uses four IT systems to manage taxpayer data for domestic taxes. However, in practice, five IT systems are in use. Below is a list of IT systems used by the MRA to manage taxpayer data:

1. The Centralised Self-Assessment System-2 (SAS2), which was introduced in 2014. This system is mainly used to generate TIN and record income tax (PAYE, CIT, WHT) payments. SAS2 is supposed to be the only system generating TINs; however, other systems (such as TACS) are also used to issue TINs.
2. The Tax Administration Computer System (TACS) was introduced in 1989. SAS2 was introduced as a replacement for TACS. However, the migration to SAS2 from TACS was never completed, after it was realised that some functions could not be performed in SAS2. Thus, both SAS2 and TACS are being operated, with TACS mainly used to record direct taxes (PIT, CIT, WHT). Although SAS2 and TACS perform similar functions, the two systems are not interfaced, often resulting in conflicting information. TACS, for example, has more than 67,000 taxpayers, while SAS2 has approximately 32,000 taxpayers.
3. The Centralised Self-Assessment System-1 (SAS1) was introduced in 2008 and is used to record VAT payments. It was intended to replace the Surtax Administration Computer System (SACS), which was introduced in 1989. However, some stations³⁵ still use SACS regularly, and the LTU uses it as a backup system.
4. SACS: as noted in point three above, SACS was introduced in 1989 to record surtax, a tax that was restructured in 2005 and renamed VAT. SACS is not officially recognised by the MRA, although some stations still use it.
5. Electronic Fiscal Device (EFDs): EFDs were introduced by the MRA in 2014

³⁵ There are 28 MRA stations spread across Malawi. All the stations are supposed to use the four officially recognised IT systems. However, some stations did not phase out SACS and thus use five IT systems.

for the management of value added tax (VAT). EFDs record VAT transactions in real time, whereas SAS1 and SACS record information from VAT returns.

All five IT systems operate individually, and are not interfaced. Table 5.1 is a summary of the five IT systems currently being used in the MRA, and the period over which they have been operating.

Table 5. 1: IT systems used in the administration of domestic taxes and their current status

	System	Primary function	Start date	Proposed end date	Current status
1	SAS2	Generating TINs Recording all tax payments from tax returns (CIT, PIT, WHT, VAT, Excise, etc.)	2014		Active
2	EFD	Recording VAT transactions in real time	2014		Active
3	SAS1	Recording VAT returns	2008	2014	Active
4	TACS	Generating TINs Recording income tax payments (CIT, PIT, WHT) from tax returns	1989	2014	Active
5	SACS	Recording VAT returns	1989	2008	Active (informally)

Source: Interviews with MRA officers, 12-27 November 2016; TADAT (2015a)

The numerous IT systems being used in the administration of domestic taxes has created a number of challenges. The following are some of the main challenges:

1. Duplication of work. For example, four of the five systems are used to record VAT transactions, yet the information in the different systems is often conflicting.
2. It is difficult for the MRA to trace some activities, such as taxpayer payments, because the systems are managed by different units. For example, an officer dealing with VAT payments using the EFD or SAS1 system would require authorisation to access income tax information from SAS2. The process of

getting authorisation can sometimes be rigid and complex. Officers therefore concentrate only on recording taxes under their mandate and ignore other taxes.

3. Issuance of multiple TINs. In principle, each taxpayer is supposed to have one TIN; yet in practice, it has been found that a taxpayer can have more than one TIN. During the survey of business people that I conducted, respondents were asked if their business is registered with the MRA, and if the business has one registration certificate or multiple certificates. At least three respondents out of the 450 taxpayers registered with the MRA indicated that they have more than one certificate (and therefore multiple TINs), for their business. The SAS2 is programmed to only issue one TIN per taxpayer, but it is possible to override the system, thereby allowing some taxpayers to be (illegally) issued multiple TINs. There are also instances where temporary TINs are issued outside of SAS2. An officer in the audit section of the MRA indicated that some taxpayers use different TINs to circumvent payment of tax arrears or penalties when filing a return. In some cases, taxpayers use multiple TINs to file more than one tax return for the same business, breaking their gross income into smaller amounts to avoid being classified as a large taxpayer. Businesses do not want to be classified as large taxpayers, since this group is closely monitored.

All MRA departments use the five IT systems outlined above. However, in addition to using these five systems, the LTU uses a sixth system. Noting the challenge of conflicting information generated from the various IT systems, the LTU hired dedicated officers to record and update taxpayer information and all their tax payments in a Microsoft (MS) Excel file.³⁶ This Excel file, developed and updated by LTU officers, is the MRA's most reliable and up-to-date registry for information related to taxpayers. All the details relating to a taxpayer, including their current physical address, phone numbers, and monthly tax payments by tax type, are stored in this file. However, only information and tax payments relating to taxpayers under the management of the LTU are recorded in the MS Excel file. While the MS Excel file is thought to be the most reliable source of taxpayer information in MRA, this format and process of storing taxpayer information is not formally recognised by the MRA because Excel files present

³⁶ There are no dedicated officers for taxpayer data entry in the divisions that manage small and medium taxpayers. Each officer enters the information on the tax return that they are handling into the IT systems.

a security risk, as they can be easily manipulated.

The MRA is aware of the challenges related to their IT systems. The MRA website specifically states that:

“The functionality of the domestic tax division current transaction computer systems is limited to the rudimentary registration and taxpayer accounting for assessment and payment. Most of the processes are executed in a manual environment and, consequently, the process data generated is also substantially manual. Manual processes and data present a myriad of challenges including security of data, access to the data, integrity of the data as well as extraction of the data for reporting and analysis.”³⁷

To resolve these problems, the MRA is in the process of procuring another system that it claims will replace the five IT systems. The new system, called the Integrated Tax Administration System (ITAS), is expected to be operational by April 2019.

5.4.2 Tax Audit

A tax audit occurs when the tax authority decides to closely examine a taxpayer’s tax return³⁸ to verify that it is accurate. A tax return is usually chosen for audit when something that is entered on the return is out of the ordinary. Tax audits allow the tax authority to monitor tax revenue losses from inaccurate filing, to deter non-filing of tax returns, and to identify areas of weakness in the tax system (OECD, 2010).

In terms of auditing, the key challenge for any tax authority is that it is not economically viable nor logical to audit each taxpayer. In Malawi, less than 1.5% of taxpayers are audited in a year (MRA, 2016). This audit rate is consistent with trends in both high-income and low-income countries, where less than 2% of total taxpayers are audited in a year (Lemgruber, Masters & Cleary 2015). Large taxpayers in Malawi have a higher probability of being audited than small and medium taxpayers. On average, between 14% and 33% of large taxpayers are audited in a year, compared to 1% of small and medium taxpayers (Table 5.2). Officers in the audit section of the MRA explained that they dedicate more resources to the auditing of large taxpayers because

³⁷ See <http://www.mra.mw/help-for-taxpayers/integrated-tax-administration-system-itas>

³⁸ A tax return is a form on which a taxpayer makes an annual statement of income and it is used by the tax authorities to assess liability for tax.

approximately 70% percent of revenue collected by the MRA is collected from large taxpayers. During the 2014/15 fiscal year, the MRA handled a total of 252 audit cases. The distribution of the audit cases was as follows: 45% comprehensive audits;³⁹ 48% issue-oriented audits;⁴⁰ 7% refund audits;⁴¹ and 0% desk audits.⁴² Similar proportions of audits were conducted in the 2015/16 fiscal year (Table 5.2).

Table 5. 2: Audit rates and revenues recovered in 2014/15 and 2015/16 by classification, based on turnover

Year	2014/15			2015/16		
Section	Number of taxpayers audited	Percentage of taxpayers audited	Revenue recovered (MK' billion)	Number of taxpayers audited	Percentage of taxpayers audited	Revenue recovered (MK' billion)
Large taxpayer office	67	33%	14.6	92	14%	22.3
Medium and small taxpayer office	185	1%	5.2	354	1%	4.6

Source: 2015/2016 MRA Annual Report

The MRA faces three challenges with respect to audits. The first is that cases for audit are selected randomly. To select a case for audit, the MRA is supposed to use a

³⁹Comprehensive audits are generally employed when significant anomalies are detected through a desk or issue-oriented audit, or identified by the risk management system. Usually, cases selected for comprehensive audit cover all taxes for one or more tax years.

⁴⁰ Issue-oriented audits are generally limited to check particular aspects of the return and cover a single tax. For example, in the case of VAT, an issue-oriented audit may deal with all of the activities reflected in a tax return, or it may focus on one particular aspect such as turnover, exports, invoicing, or excess credit.

⁴¹Refund audit is one form of issue audit. It has been highlighted because of the increase in refund fraud where taxpayers overstate the amount to be refunded (when the input VAT is greater than the output VAT, MRA refunds the difference). Prior to 2013/14, tax refunds were usually paid without audit.

⁴² Desk audits include: (1) a check that the returns filed are consistent, (2) a comparative analysis of returns for different taxes, (3) a comparative analysis of the main ratios against those for similar businesses in the same sector, and (4) a cross-check against information received from other government agencies and third parties.

risk matrix. The risk matrix is a systematic way of identifying the risk of tax non-compliance among taxpayers, and is intended to help officers in the audit section target their actions to the various identified risk categories, better allocate resources across different types of audits (comprehensive, issue-oriented, and desk audit), and improve the overall effectiveness of the audit function. However, officers in the audit section of the MRA pointed out that the risk matrix is largely ignored. A number of reasons for ignoring the risk matrix were raised. An officer in the audit section pointed out that a taxpayer can be selected for audit because the audit manager anticipates the recovery of a significant amount of money. Audits that do not raise money are seen as a failure by MRA management.⁴³ In other instances, the audit matrix is ignored because, when used, it will select taxpayers that the audit manager does not want to audit (either under instruction from senior officers in the MRA, or because the officer selecting the cases has been bribed by the taxpayer so that they are not audited during specific periods).

The MRA is aware that the audit matrix is largely ignored and the LTU is aware of the weaknesses in auditing. To ensure that all risky taxpayers are audited, the LTU formulated its own risk matrix. The LTU then submits the additional taxpayers to be audited to the audit division, and funds these additional audits using their divisional budget. The small and medium taxpayer units do not have a similar arrangement.

The second audit challenge is corruption of MRA officers. Often, the MRA discovers that audit officers have been colluding with taxpayers to settle audit cases outside of the normal channels or to ensure they are not audited in exchange for personal gains. To address this problem, one of the measures the MRA has taken is to require that auditors (and all senior personnel in all departments) declare their assets annually, to monitor the growth of their wealth. MRA employees are also required to declare all gifts that they receive from taxpayers. However, the likelihood of these measures deterring corrupt practices within the MRA is low, because officers can hide their wealth by investing in assets that cannot easily be traced back to them. However, what this practice appears to have achieved is to instil, among both taxpayers and some tax officials, the perception that tax officers are under surveillance for corrupt practices. During the survey of business people in Malawi, some taxpayers specifically pointed out that it has become difficult to bribe MRA officers because they are being closely

⁴³ The risk matrix also likely selects cases for audit with high potential of recovering taxes. The advantage of using a risk matrix over human intuition is that the process is systematic and unbiased.

monitored, such that they often refuse and report those attempting to bribe them to the police. These stories, though difficult to verify, suggest that the monitoring of MRA officers' wealth may reduce the likelihood of some taxpayers offering bribes to tax officers, or of tax officers accepting bribes.

The third challenge associated with auditing is that the information obtained from audits is not used to inform policy. I noted that auditors identify risks in the field, but that these risks are not being collated to inform any review of risk selection criteria or compliance improvement plans. Assessment of audit reports mainly focuses on the number of audits conducted in a year, and how much money is recovered from audits. In addition, no feedback is provided by the legal division to the audit division on the outcomes of different court cases that the audit division has handed over. For instance, when I asked officers in the audit division about the percentage of court cases that are ruled in favour of the MRA in a year, they could not provide any details but referred me to the legal division. It is evident that the audit system lacks a feedback mechanism, giving rise to this problem.

5.4.3 Dispute Resolution

From time to time, disputes arise between taxpayers and the tax administrator. Disputes typically emerge as a result of an administrative error on the part of the administration or the taxpayer. In addition, the outcome of a tax audit or investigation that identifies a discrepancy may be disputed by the taxpayer on the grounds of facts (the taxpayer may have material evidence to the contrary) or legal interpretation (Lemgruber et al., 2015).

It is, therefore, important for a tax administration to have a systematic, fair, fast, and effective dispute resolution process. An effective tax dispute resolution process can be said to be one that is based on a legal framework, is easily accessible, guarantees transparent independent decision-making, and resolves disputed matters in a timely manner (Okello, 2014). Such processes typically include an independent administrative appeals process within the tax administration, and a special tribunal that taxpayers can resort to if they are dissatisfied with the outcome of the administrative appeals process (Okello, 2014).

Tax dispute resolution processes that are not fair (or not seen to be fair), and/or

that take a long time to resolve a dispute, may have the following consequences (UN, 2017; Gangl et al., 2015):

1. Affect taxpayers' trust in the tax administration, and the judicial system.
2. Lead some taxpayers to challenge the tax authority's integrity.
3. Lead to higher costs for taxpayers, potentially making the country unattractive for conducting business.

According to the available TADAT assessment reports, in most low-income countries, the dispute resolution process is relatively good. Out of the 14 TADAT assessment reports analysed, for the indicator P7-19 (the existence of an independent, workable, and graduated dispute resolution process), 75% of the countries scored an A or B, meaning that 75% of the countries have a dispute resolution process that is in accordance with international best practice.

Malawi scored a "D" on this indicator. One key limitation in the law on dispute resolution in Malawi (which was also noted by TADAT assessors) is the lack of easy access to information about appeals procedures. Thus, although the Malawi Taxation Act (Section 95–101) states that when a tax dispute arises, a consensual dispute resolution process should first be attempted. The taxpayer makes an appeal for their case to the Commissioner General (CG). The CG, after consultation with technical staff, makes a decision. If the taxpayer is not satisfied with the CG's decision, they may appeal the decision to a special arbitrator (judges selected from the mainstream judicial system). Following the arbitrator's decision, taxpayers may appeal disputes of law to the High Court.⁴⁴ On paper, this dispute resolution process is comprehensive, providing recourse to independent arbitrators and the courts, instead of the MRA itself resolving all disputes. However, in practice, the tax dispute resolution process in Malawi does not follow all the steps outlined in the law. The majority of cases end with the MRA (i.e., they are not appealed). One of the contributing factors for MRA to usually remain the final judge is that most taxpayers are not aware of the dispute resolution process, probably due to the fact that it is difficult to find the dispute resolution procedures in the Malawi Taxation Act and that the MRA does not make this information available in other documents. Comparing the section dealing with appeals procedure in the Malawi

⁴⁴ The guiding law on appeals is the Taxation Act, Cap 41:01, Part X, Section 95-101 and Eighth schedule. The Malawi Revenue Authority also has a document highlighting the Appeals procedure.

tax law with those of Zambia and Uganda shows how the appeals procedure seems to be hidden in the Malawi Tax law (Table 5.3)

Table 5. 3: Comparison of appeals procedure as outline in Tax laws of Malawi, Zambia and Uganda

Malawi	Section 97 of the Malawi Taxation Act states that “A taxpayer who is aggrieved...may appeal to the Commissioner against such assessment, decision or determination”. Section 98 (1) states that “a taxpayer aggrieved by a decision of the Commissioner under section 97 may appeal to a Special Arbitrator appointed either generally or specifically for the purpose by the President” while section 101 (1) states that “Either party to proceedings before a Special Arbitrator under section 98 or a Traditional Appeal Court under section 100 may appeal in the prescribed manner to the High Court..”
Zambia	Section 107 sets up Appeal court while Section 108 states that “...within thirty days of the date of service of notice of assessment, the person assessed may make to the Commissioner-General a written statement of objection to the assessment setting out the grounds of objection, and the Commissioner-General shall give that person written notice of his decision concerning that objection” and Section 109 (1) states that “if a person assessed is dissatisfied with the Commissioner-General's decision concerning his objection to the assessment, that person may, by written notice to the Chairperson, within thirty days of the date of service of the written notice of the Commissioner-General's decision, appeal against the assessment to the tribunal and shall send a copy of the notice to the Commissioner-General”
Uganda	Section 99 (1) states that “A taxpayer who is dissatisfied with an assessment may lodge an objection to the assessment with the commissioner within forty-five days after service of the notice of assessment”. Section 100 (1) and (2) further states that “(1) A taxpayer dissatisfied with an objection decision may, at the election of the taxpayer— (a) appeal the decision to the High Court; or (b) apply for review of the decision to a tax tribunal established by Parliament by law for the purpose of settling tax disputes in accordance with article 152(3) of the Constitution and (2) An appeal under subsection (1) to the High Court shall be made by lodging a notice of appeal with the registrar of the High Court within forty-five days after service of notice of the objection decision”

Source: Taxation Act Malawi, Taxation Act Zambia, Taxation Act Uganda

It will be noted in Table 5.1 that both Zambia and Uganda provide details of procedures and timelines on how appeals should be conducted with regard to the main clauses of the Act, the Malawi law does not have similar details in the main clauses of its particular Act. This information is put in the eighth schedule, which is found towards the end of the Malawi Taxation Act. The procedures outlined in the eighth schedule are

in line with what is provided in the Zambia and Uganda Taxation Act. However, because the referencing to the procedures is not well-made in the main clauses, taxpayers may not easily find the information about the appeals procedures and the timelines regarding appeal. During the survey that I conducted in Malawi, business officials were asked what they (or others in similar businesses) did if they had reservations with the MRA ruling on a dispute. In total, 63% answered, “there is nothing a taxpayer can do but follow the MRA’s ruling,” 24% answered, “settle the case as proposed by the MRA,” 7% answered, “take the case to court or the Ministry of Finance,” and 6% declined to answer. This finding suggests that the majority of taxpayers do not know that they have the option to take tax disputes to court or to a special arbitrator. It was, therefore, not surprising to note that more than 90% of cases that go to court involve large taxpayers, because large taxpayers will typically have lawyers and well-qualified accountants who understand the law.

When investigating whether there are publicly available guidelines on the dispute resolution process, the MRA referred me to the Taxation Act, as there are no brochures or documents that detail the appeals process for the public. Other than what is contained in the Acts, there has been just one public notice (published in a newspaper in 2015) informing taxpayers that if they are not satisfied with the MRA’s decision, they can refer the matter to a special arbitrator and the courts.⁴⁵ However, the notice did not provide any details on how a taxpayer could do that. Internally, the MRA has an appeals procedure document, the existence of which is only known by officers in the legal department and some auditors. Due to taxpayers’ lack of awareness of the dispute resolution process, they often submit appeals to the Ministry of Finance, who usually refer the cases back to the MRA. Occasionally, the Ministry of Finance intervenes in the dispute resolution process, which adds further confusion to the dispute resolution process. Interviews with officers in the Ministry of Finance revealed that at least one appeal case on an MRA ruling is sent to them every month.

An interview with the head of the Society of Accountants in Malawi on the tax appeals process in Malawi revealed that the institution has been asking the Ministry of Finance to establish a tax tribunal to ensure that the system is fair. In the 2013/14 budget statement, the Minister of Finance announced that a tax tribunal would be introduced.

⁴⁵ The Malawi Revenue Authority Tax Update “Income tax objection” in Daily Times newspaper, 14 May 2015.

However, to date, none has been set up, and there are still no public documents that provide guidance on the appeals process. Commenting on the appeals process, one taxpayer described sending a 75-page appeal letter to the MRA with receipts and other documents attached to prove that the MRA's audit conclusions were not correct. The MRA sent a one-line response, stating that, "we maintain our earlier position." The taxpayer was extremely disappointed with the MRA's response, as no effort was made on the MRA's part to explain why they maintained their position after being provided with additional information. Instead of involving the special arbitrator or the court, the taxpayer referred the matter to the Ministry of Finance. The taxpayer claimed that he did not know that he could refer the case to a special arbitrator, and was not comfortable asking the MRA about the process.

The shortage of information on the dispute resolution process mostly affects small and medium taxpayers. Almost all large taxpayers have access to specialised tax advice and lawyers who are aware of the dispute resolution process.

5.4.4 Taxpayer Education

Taxpayer education refers to programmes that aim to teach taxpayers about: their tax rights; responsibilities; legal requirements; the importance of paying tax; and what taxpayers should expect of the government, in terms of accountability (Gitaru, 2017; Mascagni & Santoro, 2018). To ensure voluntary tax compliance, tax administrations are expected to provide tax information and support to taxpayers so that they can meet their obligations and claim what they are legally entitled to. Tax education is also provided because very few taxpayers use the law itself as a primary source of information (Gitaru, 2017). In addition, studies have shown that taxpayers often have little understanding of how tax systems work (Kira, 2017; Feldman et al., 2016). Thus, advice and assistance from the tax administration plays a crucial role in bridging the knowledge gap.

The MRA disseminates tax information to the public in a number of ways, though primarily through brochures, press releases, magazine articles, radio and television slots, and content on the MRA website. The MRA also conducts seminars and workshops for taxpayers, and awareness programmes in schools. In 2018, it introduced walk-in enquiries and phone services (including WhatsApp) to address taxpayer questions. In addition, every year, the MRA publishes on its website a list of tax policy

changes made by Parliament. The taxpayer education services are expansive and cover different types of taxes.

The primary limitation of the taxpayer education service provided by the MRA is that the publicly available resources and activities do not explain, in detail, the taxpayer's technical obligations and rules. The resources and information sessions provide basic information rather than full guidance or manuals. For instance, taxpayers are told that if they have a problem with how the MRA has handled a dispute, they can appeal to a special arbitrator. However, the advice does not contain detailed information on how to initiate the appeals process.

As mentioned previously, to ensure that large taxpayers have all the information that they need related to taxation, the LTU assigns a desk officer to each large taxpayer. The officer is a source of information on all matters relating to tax. This service is not available to small and medium taxpayers – these are many in number, meaning it is not feasible to assign officers to each.

5.5 Discussion

The assessment of the MRA's performance is based on four performance outcome areas, which are identified in the literature as being among the most important activities of a revenue authority, and are among the nine performance outcome areas assessed within TADAT. However, unlike in the TADAT assessment, the areas assessed were not scored. Rather, I identified strengths and weaknesses in each area based on what the MRA intends to achieve when undertaking that activity. To some extent, the findings are consistent with the TADAT assessment for Malawi, in that the efficiency and effectiveness of the MRA is found to be poor in all four areas assessed. The only exception relates to the LTU, within which efficiency and effectiveness was found to be good. Furthermore, unlike in the TADAT assessment, where a tax administration is evaluated as a whole on its efficiency and effectiveness in undertaking its function, I assessed the performance of the MRA by looking at process performance within specific departments. In addition, information obtained from documents and tax laws was cross-checked with actual performance and triangulated with information from taxpayers. This provided a comprehensive picture of the efficiency and effectiveness of the different departments of the MRA in undertaking their functions.

The first function assessed was the registration and management of taxpayer

data. In this area, I found that the MRA has good initiatives that ensure that eligible taxpayers are registered. However, the institution uses multiple IT systems to manage taxpayer data. This means that officers within the MRA cannot undertake data analysis tasks, such as disaggregating revenue performance by income group, occupation, and gender, predicting future risks for revenue, or cross-checking tax payments. Gray et al. (2001) suggest that taxpayers who default on direct taxes are more likely to evade indirect taxes, and vice versa. The MRA would not be able to make these connections, because the use of multiple IT systems has resulted in disaggregated taxpayer information. An exception was noted in the LTU, where efforts are made to maintain complete and up-to-date taxpayer information using an MS Excel file. While this initiative is commendable, keeping taxpayer data in this particular format is vulnerable to manipulation, which may compromise the quality and reliability of the data. In addition, as the number of taxpayers managed by the LTU grows, there is a need for a more advanced system to manage taxpayer data.

Next, I assessed the audit function. A positive result was that the audit rates and distribution of cases for auditing were found to be consistent with international standards. In line with other revenue authorities in low-income countries, the MRA has an audit plan that covers all core taxes and taxpayer segments. It was also noted that large taxpayers have a higher probability of being audited than medium or small taxpayers. This is expected of any revenue authority, considering the amounts of money involved with large taxpayers. This makes auditing large taxpayers critical to safeguarding revenue collection. While it is not necessary to match audit rates between large and small taxpayers, it is necessary for the MRA to ensure that it gives the impression that even small and medium taxpayers are audited. The fact that some small and medium taxpayers connive with tax officials to have multiple TINs suggests that small and medium taxpayers are aware that the probability of their being audited is very low. The MRA must find ways of addressing this problem. A negative result was that the risk matrix used for case selection is largely being ignored. In addition, there is no evaluation of the extent to which audits are detecting and deterring inaccurate reporting. To improve its audit function, the MRA must ensure that audit officers use the audit matrix, and must create clear channels through which information is transmitted (from auditors to decision-makers and other departments, then back to auditors).

Next, I assessed the dispute resolution process. Malawian law provides for a

reasonable dispute resolution process. However, the MRA, intentionally or not, does not publicise the dispute resolution process. This means the institution, in many cases, is the final judge. It seems it is only large taxpayers who make use of the extended dispute resolution process, which involves players other than the MRA. For the MRA to position itself as a legitimate and fair institution, thereby encouraging tax compliance, it needs to ensure that all taxpayers are fully aware of the dispute resolution process and that this process operates as intended. One way of achieving this is through publication of a detailed document on the dispute resolution process, made available on the MRA website. In addition, the creation of a tax tribunal should be facilitated. This would create a perception of fairness among taxpayers as the final decision on a tax dispute will be taken by the tribunal and not the MRA. This will provide positive incentive for tax compliance (Faizal et al., 2017; Smith, 1991).

Finally, I assessed the taxpayer education services. The MRA undertakes a number of initiatives to inform taxpayers and the public about taxation in Malawi. Walk-in enquiries, phone services, and the use of WhatsApp as ways to respond to questions from taxpayers and the general public are some of the positive initiatives that the MRA undertakes. However, the information provided should be sufficiently detailed to allow taxpayers to make a well-informed decision. This is not currently the case. Assigning MRA officers to individual taxpayers is effective in the LTU because the number of taxpayers classified as large is small. For the small and medium taxpayers, it is important for the MRA to provide sufficient information so that they can make informed decisions on their own. This will help to encourage tax compliance and legitimise the institution, as taxpayers become aware of their responsibilities and legal rights.

5.6 Conclusion

This chapter aimed to determine the extent to which the tax administration processes followed by the Malawi Revenue Authority affect the level of tax revenue collection and tax structure in Malawi. The analysis has shown that the MRA's process performance is mixed, with good performance in the LTU and weak performance in all other revenue-collecting departments. Given that the LTU is responsible for approximately 70% of the taxes collected by the MRA, the good tax revenue collection in Malawi, especially between 2005-2011, can largely be attributed to the effectiveness and efficiency of the LTU in undertaking its functions.

Only four out of the nine areas assessed in TADAT were assessed in this study. This may limit the extent to which conclusions can be drawn regarding the impact of the MRA's process performance on revenue collection. However, the findings for the four areas assessed are consistent with TADAT's assessment of the MRA, except where the LTU is concerned, and therefore seem to be a true reflection of the MRA's process performance.

Chapter 6: Why is Malawi so Successful in Collecting Direct Taxes?

6.1 Introduction

Malawi has a high reliance on direct taxes relative to other sub-Saharan African (SSA) countries, and to low-income countries in general. For example, between 1980-2015, direct taxes in Malawi accounted for 40% of total revenue, while the average for SSA countries was 32% (ICTD/UNU-WIDER, 2017). Shalizi and Thirsk (1990) argue that the share of total revenue accounted for by direct taxes in Malawi is more reminiscent of a developed country. Governments of low and middle-income countries rely more on indirect taxes than those of high-income countries (Besley & Persson, 2014; Junquera-Varela et al., 2017). The reason is that direct taxes are administratively difficult to collect in low-income countries for several reasons, including weak tax administrations and political hurdles relating to taxing the wealthy (Aizenman & Jinjara, 2009; ATAF, 2018). By contrast, the main reason for high dependence on direct taxes in high-income countries is that there are many people in formal employment such that there is high revenue from Personal Income Taxes (PIT), notably Pay As You Earn (PAYE) (Aizenman & Jinjara, 2009).

Malawi is among the 47 least developed countries in the world (UNCTAD, 2018). It has a tax administration which, when judged by the standard criteria for effective tax administration, appears to perform very poorly, even by the standards of low-income countries (see Chapter 5). Furthermore, approximately 89% of its working population is employed in the informal sector, and hence are not liable to pay income taxes (NSO, 2014). It is, therefore, unexpected for Malawi to have higher reliance on direct taxes than most SSA countries, and low-income countries in general. Accordingly, the aim of this chapter is to determine how Malawi, a low-income country with a tax administration that operates below international standards and a large informal sector, has been able to collect greater revenue from direct taxes than most other SSA countries. I explore this issue by undertaking research that answers the following questions:

- What are the reasons for Malawi's current high reliance on direct tax?
- How far back in history does Malawi's reliance on direct tax extend?

In Section 6.2, I briefly review a number of possible explanations for Malawi's high dependence on direct taxes, and find none of them plausible. Most of this chapter is devoted to explaining, reviewing, testing and extending a previous piece of research that gives us great insight into my central question: work by Thandika Mkandawire (2010) on the structure of the colonial economies of Africa. Mkandawire (2010) classifies African countries into three main groups according to the structures of colonial economic exploitation: Labour Reserve Economies, Cash Crop Economies, and Concessional Companies. For reasons that I explain below, the governments of the Labour Reserve Economies were better able and more motivated to raise revenues, and to do so by taxing incomes directly. Mkandawira (2010) shows that, for the period 1984-2004, the governments of the Labour Reserve Economies were better able to raise revenue and more reliant on direct taxes. He attributes this to the continuing legacy of colonial economic and revenue systems.

Malawi is classified as a Labour Reserve Economy. It is not a complete outlier as a successful generator of direct tax revenues. It is part of a group, consisting largely of neighbouring countries (including Zambia, Zimbabwe, Botswana, and South Africa). I test and build upon Mkandawira's research in three main ways:

- comparative country analysis, with more recent data. This analysis shows that the pattern still holds, but generally weakening, but somewhat more persistent in Malawi;
- history of tax in Malawi; and
- provide plausible explanation for Malawi's high reliance on direct tax by recounting the nature of the post-independence national politico-economic system.

I conclude that the initial question, on why Malawi is highly dependent on direct tax, is in part explained as a legacy of colonial political, economic and revenue structures, but that in Malawi's case, functionally-similar structures were perpetuated well into the post-independence era through the decisions of the first President, Dr Banda.

The chapter is structured as follows. The next section provides a review of the drivers of difference in level of tax revenue collection and tax structure in SSA. Then, I validate Mkandawire's (2010) theory by looking deeper into records of revenue raising

in Malawi and the other seven countries in SSA for the period 1910-1960. This is followed by an updating and testing of Mkandawire's theory for the period 2000-2015. Then, based on the finding that colonial histories may be playing a part in influencing current levels of tax collection and tax structure, I review Malawi's tax collection history from 1891 to 2015, with the aim of understating how direct tax collection in Malawi has been sustained over the years.

6.2 Drivers of Differences in Levels of Tax Collection and Tax Structure in Sub-Saharan Africa

In most SSA countries, formal taxation was introduced by colonial governments (Gardener, 2012). However, levels of tax collection and tax structures vary among countries in the region. It has been observed that southern African countries within SSA collect a significantly high amount of tax revenue as a proportion of GDP, and have a higher reliance on direct taxes, in comparison to other countries in the region (Mkandawire, 2010). There are several theories that seek to explain the differences in the level of tax-to-GDP ratio and the tax structure across SSA. The commonly cited drivers are the influence of the SACU, differences in the size of the mining sector, institutional spill-over, and colonial legacy. This section evaluates each of these possible explanations, and finds that none of them fully explains the differences in level of tax collection and tax structure in SSA. However, the colonial legacy theory goes a long way towards explaining these differences.

6.2.1 Influence of the SACU

Based on panel data on 43 SSA countries for the period 1990-1995, Stotsky and WoldeMariam (1997) found that countries in southern Africa have high tax-to-GDP ratios and tax effort indices. They constructed the tax effort index as the ratio of actual tax as a share of GDP to predicted (potential) share of tax-to-GDP. They found that the tax effort index for most southern African countries, including South Africa, Botswana, Lesotho, and Namibia was above 1, and the ratio in other countries was less than 1. They attributed the high tax effort for countries in southern Africa to the influence of the SACU.

Established in 1910, the SACU comprises five countries: Botswana, Lesotho,

Namibia, South Africa, and Swaziland.⁴⁶ The aim of the SACU is to maintain the free interchange of goods between the member countries through a common customs area, a common external tariff,⁴⁷ and a common excise⁴⁸ tariff. All customs duties and excise taxes collected in the common customs area are paid into South Africa's National Revenue Fund (SACU, 2002). The revenue is then shared among member countries in accordance with a revenue-sharing formula (SACU, 2002).

As of 2017, the tax-to-GDP ratio for SACU member countries averaged 25%, while the average tax-to-GDP ratio for countries in SSA was 16% (ATAF, 2018). In addition, all SACU member states are classified as middle-income countries, whereas most SSA countries are classified as low-income (World Bank, 2017). Thus, the high tax-to-GDP ratio in SACU countries may also be due to the effect of high income. In addition, some of the countries in southern Africa with high tax-to-GDP ratios, such as Zimbabwe (where the tax-to-GDP ratio as of 2017 was 26% (ICTD/UNU-WIDER, 2017)), are not members of the SACU. Thus, the SACU theory only partly explains the differences in level of tax collection among SSA countries.

6.2.2 Size of the Mining Sector

It has been suggested that countries in southern Africa have a relatively high tax-to-GDP ratio because they have a large mining sector (Laporte, Céline & Yannick, 2017). While this explanation seems valid for Zambia, Namibia, and Botswana, where the mining sector contributes significantly to tax revenue (Mkandawire, 2010), it does not apply to Malawi, which has had a relatively high tax-to-GDP ratio since 2009 despite not having a large or flourishing mining sector (Chapter 2). Thus, this theory only partly explains the differences in level of tax collection among SSA countries.

6.2.3 Institutional Spill-over

The high tax-to-GDP ratio in countries in southern Africa has also been attributed to institutional spill-over (Arizala et al., 2018). The institutional spill-over theory suggests that the tax administration practices of more advanced countries, in this

⁴⁶ See <http://www.sacu.int/index.php>

⁴⁷ The same customs duties, import quotas, preferences or other non-trade barriers apply to all goods entering the area, regardless of which country within the area they are entering.

⁴⁸ Excise is a form of tax that is charged mostly on luxury products, alcohol and tobacco.

case South Africa, has influenced neighbouring countries, either through a contagion effect where countries directly copy the tax policy and tax administration practices followed by South Africa, or through shared tax arrangements, as is the case for SACU member states. The spill-over effect may explain the good tax revenue collection performances of countries in the SACU. However, the literature does not indicate the factors influencing the extent of that spill-over. For instance, it is not clear why the tax-to-GDP ratio for Angola (which borders Namibia, a SACU member state) is much lower compared to that of SACU member countries. Because this theory has not yet been, and cannot be easily, tested, it is not possible to conclude the extent to which it has influenced the differences in the level of tax collection and tax structure in SSA.

6.2.4 Colonial Legacy

The colonial legacy theory pertains to how different colonial economic structures generated different tax levels, and how those colonial differences have persisted (Mkandawire, 2010). The theory is based on the observation that the colonial culture, forms of colonisation, legal systems, and institutional heritage shaped the initial conditions of African economies, and that they continue to have an impact on current economic performance in SSA (Grier, 1999; Mkandawire, 2010; Acemoglu, Johnson & Robinson, 2001; Austin, 2008; Bolt & Bezemer, 2009; Bowden & Mosley, 2008; Engerman & Sokoloff, 2005; Lange, 2004; Moradi, 2008).

Mkandawire (2010) convincingly describes how colonial history still influences tax collection in SSA in the post-colonial era. Mkandawire classified regional economic structures (using countries as the unit of analysis, due to data constraints) into three groups based on the form of incorporation of countries in certain regions into the colonial economic system. The three groups are: Cash Crop Economies; Concessional Companies; and Labour Reserve Economies (LRE)(Table 6.1).

Table 6. 1: Forms of colonial incorporation

Type	Countries
Labour Reserve	Angola, Botswana, Kenya, Lesotho, Malawi, Mozambique, Namibia, South Africa, Swaziland, Zambia, Zimbabwe
Cash Crop	Benin, Burkina Faso, Cameroon, Côte d'Ivoire, The Gambia, Ghana, Guinea, Guinea Bissau, Mali, Nigeria, Senegal, Tanzania, Togo, Uganda, Mauritania, Niger
Concessional Companies	Congo Kinshasa, Congo Brazzaville, Gabon, Central African Republic, Rwanda, Burundi

Source: Mkandawire (2010)

Mkandawire (2010) described each of the colonial economic systems as follows:

1. **Cash Crop Economies:** countries where production was left to peasants. Marketing was dominated by metropolitan mercantile houses or, later, by state marketing boards that enjoyed monopolistic positions in the economy. Taxation in these economies took place largely through marketing channels and hut or poll taxes (the hut tax was a type of tax applied on a per hut or per household basis. The poll tax was similar to the hut tax but was applied to individuals and not households (Massey, 1978)). There were few restrictions on the movement of indigenous labour and on informal activities in the urban areas. However, the movement of crops was highly regulated.
2. **Concessional Companies:** countries where the colonial power gave private companies concessions on vast areas of land, for the production of crops on large plantations, or for mineral extraction. These economies relied on forced labour, and there was virtually no development of peasant commercial farming.
3. **Labour Reserve Economies:** countries that were often associated with racial segregation (e.g., South Africa), migrant labour (e.g., Malawi), and ubiquitous townships or locations (e.g., Zambia). The labour reserve economies were sometimes within the national economies, as was the case in Angola, Kenya, South Africa, Namibia, Zambia, and Zimbabwe, or alternatively were entire

countries, assigned the LRE role through the colonial division of labour, for example Botswana (before the discovery of diamonds), Lesotho, and Swaziland. Two key features of labour reserve economies were their highly dualistic formal labour market and their migrant labour system that tied large numbers of peasants to the mining industry or plantation agriculture.

Using tax data from 1984-2004, Mkandawire (2010) showed that the LRE had a high tax-to-GDP ratio (on average, tax-to-GDP ratio averaged 23% during this period), and a high proportion of direct tax in total revenue (on average, direct taxes contributed 36% to total revenues during this period) compared to the non-labour reserve economies (NLRE)(cash crop economies and concessional companies), where the tax-to-GDP ratio and contribution of direct taxes to total revenues averaged 12% and 23%, respectively (Mkandawire, 2010)⁴⁹. According to Mkandawire, the reasons for the high tax collection and high reliance on direct taxes in LRE were threefold:

1. The state had the administrative and coercive capacity to impose high taxes. The labour reserve economies had a lot of labourers (most of whom were young men) who worked in mines or plantations. The labourers usually lived together in proletarian living conditions, which created a potential security problem as there was a risk of the labourers attacking the settlers (the Europeans who settled in the colonies) or even each other. The profitability of mining and plantation investment required this threat to be controlled. Accordingly, the state needed to have strong police and army security forces, and higher taxes were imposed to fund these security programmes. In exchange for a higher level of protection, the settlers were willing to pay high income taxes and to collect taxes from their workers on behalf of the government.
2. There was a low level of informalisation. In labour reserve economies, informal businesses were restricted and only the settlers could operate formal businesses. This resulted in a low level of informalisation, which made it easy for the state to collect taxes from the few formal businesses and the labourers.
3. There were high levels of inequality, coupled with a lack of redistributive expenditure. In labour reserve economies, ownership of land was concentrated

⁴⁹ Mkandawire aggregated the labour reserve and non-labour reserve economies. No reason is given for this. However, this may be due to a greater interest in showing that labour reserve economies have a high tax-to-GDP ratio and high reliance on direct tax compared to non-labour reserve economies.

to a few individuals who used it for estate farming. When tax was collected from either the estate owners or their workers, it was used to fund activities that benefited the estate owners (such as their security) and not the whole country. Thus, the few wealthy people were more willing to pay taxes (and collected taxes from their labourers on behalf of the government) because the benefits from the use of the tax revenue accrued directly to them.

6.3 Validating, Updating, and Testing Mkandawire's Classification of Economic Structure in SSA for the Period 1910-1960 and 2000-2015

Based on Mkandawira's (2010) classification of economic structure in SSA and statistical evidence regarding the economic structure in SSA for the period 1984-2004, it can be concluded that the colonial legacy theory largely explains the differences in tax structure and level of tax collection among SSA countries. However, 14 years have passed since Mkandawire tested the colonial legacy theory. Thus, although the theory seems to hold when tested using tax data for the period 1984-2004, it may not hold when more recent tax data is used (e.g., 2000-2015). In addition, Mkandawire only provided statistical evidence for the period 1984-2004, which does not include the colonial period (generally, 1900-1960 for most countries). Accordingly, this section aims at validating the colonial legacy theory with reference to statistical evidence for the period 1910-1960, and updating and testing the theory for the period 2000-2015.

6.3.1 Empirical Evidence on Mkandawire's Classification of Economic Structure in SSA for the Period 1910-1960

Mkandawire (2010) likely used tax data for the period 1984-2004 because, prior to 2015, tax data for the colonial period was not readily available. In 2015, the British Online Archives (BOA)⁵⁰ made some colonial documents, including financial statements and blue books, available online. These documents contain details about tax collection in British colonies. I was not able to locate similar detailed information about tax collection during the colonial period for countries that were not colonised by the British. Consequently, only British colonies are included in the analysis. Regardless, a sufficient number of African countries were colonised by the British to enable a large

⁵⁰ <https://microform.digital/boa/>

number of countries to be included in the analysis.

By grouping each tax type into either direct, indirect, or non-tax, the colonial tax structure was reconstructed using tax data for the period 1910-1960. Reconstructing the colonial tax structure is a challenging work as the names of taxes changed frequently during the colonial period, and countries had different names for similar types of tax. This required that I carefully check that each category had correct taxes or fees for each year. Consequently, for each country covered, approximately 30 financial statements or blue books were analysed (at least one financial statement or blue book for every two-year period covered). As a result, I was only able to reconstruct the colonial tax structures for eight countries: Malawi, Zambia, Zimbabwe, and Lesotho (for LRE), and Uganda, Tanzania, Gambia, and Ghana (for NLRE). Table 6.2 shows the composition of each tax category.

Table 6. 2: Classification of domestic revenue sources in colonial Africa (1910-1960)

Classification	Composition
Direct tax	Poll/hut tax, native tax, corporate income tax, companies tax, super tax, income tax, personal tax, officials' salary tax, alien tax, gold premium tax, excess profit tax
Indirect tax	Customs, export tax, import tax, excise, cotton tax, duty on various products (e.g., sugar, tea, tobacco), petrol tax, entertainment tax
Non-taxes	Court fees and fines, rent of government property, mining licence and fees, motor vehicle licence fee, railways fees, land sales, boarding fees, school fees, hospital fees, post office fees, telecommunication fees

Source: Author's Classification

Table 6.2 shows that taxes classified under direct tax included poll tax, company taxes, gold premium tax, and excess profit tax. The taxes included under indirect taxes were customs duties, import taxes, and petrol tax. Non-taxes included court fees, rent of government properties, land sales, and other user fees and fines.

Considering that even during the colonial period countries were at different levels of development, and hence the amount of taxes collected, in absolute terms,

differed markedly, the taxes and non-taxes were expressed as a percentage of the total revenue in each country. This ensured that only the proportion of direct tax, indirect tax, and non-taxes in total revenues were compared among the countries and not the actual amount of revenues collected. Another alternative would have been to express the total for each tax category as a share of GDP. However, GDP figures for African countries are highly unreliable, even more so for the colonial period – if indeed they can be found (Jerven, 2013).

Figure 6.1 and Figure 6.2 show the proportions of direct tax, indirect tax, and non-taxes in total central government revenues in Malawi, Zambia, Zimbabwe, and Lesotho (LREs), and in Tanzania, Uganda, Ghana, and Gambia (NLREs) for the period 1910-1960, respectively.

Figure 6. 1: Proportion of direct tax, indirect tax, and non-taxes in total central government revenues in Malawi, Zambia, Zimbabwe, and Lesotho (LRE) during the colonial period (1910-1960)



Source: British Foreign & Commonwealth Office (2015), Author's calculations

Figure 6.1 shows that, between 1910-1950 in LREs, direct taxes either contributed as much revenue as indirect taxes (as was the case in Malawi and

Zimbabwe) or were the main source of revenue (as was the case in Lesotho and Zambia (after 1935)). After 1950, the proportion of direct taxes in all LREs was much higher than either the proportion of indirect tax or non-taxes. For Malawi, Zambia, and Zimbabwe, the increase in the contribution of direct taxes to total central government domestic revenue was influenced by the formation of the Federation of Rhodesia and Nyasaland in 1953 (Rosberg Jr, 1956). At this time, some of the taxes categorised as indirect taxes became sources of revenue for the federal government (Gulati, 1960). Consequently, direct taxes became the main source of revenue. The proportion of direct taxes in total revenue in Lesotho was always higher than that of indirect tax or non-taxes during the colonial period. The main reason for this was that income was heavily taxed in Lesotho, and the British relied on the king to enforce the tax law. Because the king was very powerful, the citizens were very tax-compliant (British Foreign & Commonwealth Office, 2015b)

Figure 6. 2: Proportion of direct tax, indirect tax, and non-taxes in total central government revenues in Tanzania, Uganda, Ghana, and Gambia (NLRE) during the colonial period



Source: British Foreign & Commonwealth Office (2015), Author's calculations

Figure 6.2 shows that, during the colonial period, the proportion of indirect taxes in total revenues was always higher than direct taxes or non-taxes in Ghana and Gambia, while in Tanzania (Tanganyika) indirect taxes did not contribute much to total revenues until 1936. The construction of a railway line in the country, which promoted trade, was the main driver for the increase in the collection of indirect taxes after 1936 (British Foreign & Commonwealth Office, 2015d). In Uganda, the proportion of indirect taxes began to outweigh that of direct tax or non-taxes after 1949. The main driver for this increase was the greater demand for cash crops, such as cotton, coffee, and hides and skin. The export tax earned on these products increased by more than 800 times from £3,684 in 1948 to £2,967,986 in 1949, and the increase was sustained thereafter (British Foreign & Commonwealth Office, 2015e). In Ghana, direct taxes were introduced in 1944, while indirect taxes and user fees were being collected prior to this (British Foreign & Commonwealth Office, 2015a). However, the significance of direct taxes remained low, as the country was more reliant on indirect taxes, especially trade taxes.

To get a fuller picture of the tax structure in LREs and NLREs, I calculated the average proportion of direct taxes, indirect tax, and non-taxes for LREs and NLREs for the period 1911-1960. It should be noted that the proportion of a revenue category in total revenues might increase or decrease not because of a change in the amount of revenue collected from that revenue category, but rather because of a change in the other categories. For instance, in 1913, indirect taxes in Malawi amounted to MK13,000 (£13), accounting for 10% of total central government domestic revenues. In 1914, indirect taxes amounted to MK14,000 (£14) but accounted for only 7% of total central government domestic revenues. The decrease in the proportion of indirect taxes in total revenues was due to the fact that, in 2014, direct taxes had increased much faster than the growth in indirect taxes. Thus, the decline in the proportion of indirect tax in total revenue was due to the increases in the other revenue categories and not because the amount of revenue collected from indirect tax category declined. Regardless, this does not pose a problem for this study, as the focus here is on determining which of the different revenue categories (direct, indirect, and non-taxes) countries in SSA relied more on. Table 6.3 shows the 10-year averages for the proportion of direct tax, indirect tax, and non-taxes in total central government revenues during the colonial period in both LREs and NLREs.

Table 6. 3: Contribution of direct tax, indirect tax and non-taxes to total revenues (percentage) in LREs and NLREs for the period 1911-1960 (10-year averages)

Year	Direct Tax/Total Revenues (%)		Indirect Tax/Total Revenues (%)		Non-Tax/Total Revenues (%)	
	LRE	NLRE	LRE	NLRE	LRE	NLRE
1911-20	45		40		15	
1921-30	40	37	38	32	22	31
1931-40	39	38	38	37	23	25
1941-50	53	28	29	46	17	25
1951-60	52	18	31	60	17	22

Source: British Foreign and Commonwealth Office (2015)

Table 6.3 shows that, throughout the period under review, LREs were collecting more domestic revenue from direct taxes than indirect taxes or non-taxes. The LREs had been more reliant on direct taxes than NLREs, especially after 1941. The contribution of direct tax to total revenues in the LREs averaged 41% between 1911-1940, then increased to 53% between 1941-1960. By contrast, direct taxes in NLREs averaged 38% between 1921-1940, then reduced to an average of 23% between 1941-1960.

In general, during the colonial period, and especially after 1945, LREs relied more on direct taxes than indirect taxes or non-taxes, while NLREs relied more on indirect taxes than direct taxes or non-taxes. Thus, at independence, LREs inherited a tax system that was more reliant on direct taxes than indirect taxes. By contrast, NLREs inherited a tax system that was more reliant on indirect taxes than direct taxes.

The empirical evidence on the colonial tax structure as presented in Table 6.3 is consistent with the colonial legacy theory put forward by Mkandawire (2010) for this period, although Mkandawire presented no empirical evidence.

6.3.2 Empirical Evidence on Mkandawire's Classification of Economic Structure in SSA for the Period 2000-2015

To show that the colonial legacy continues to have an impact on current levels of tax collection and tax structure in Africa, Mkandawire (2010) used tax data from 1984-2004. Given the findings of the present study on the colonial tax structure in LREs and NLREs during the colonial period, and the analysis by Mkandawire for the period

1984-2004, it can be said that there is good evidence to suggest that the colonial legacy theory is valid for the colonial period and the earlier post-colonial period (1984-2004). However, this study seeks to determine how far the theory can explain the level of tax collection and tax structure in SSA in more recent years (2000-2015). To this end, I analysed tax data for LREs and NLREs (based on the country-level data presented in Table 6.1) using the ICTD/UNU-WIDER Government Revenue Dataset (2017). Of the countries listed in Table 6.1, only those that had fewer than four years of consecutive missing data and not more than eight years of missing data during this period were included in the analysis. Consequently, Angola and Zambia were not included for LREs, and Cameroon, Côte d'Ivoire, Mali, Niger, Nigeria, and Mauritania were not included for NLREs. This means a total of 25 countries were included in this analysis. Table 6.4 shows the comparison of the average tax structures for LREs, NRLEs, and Malawi for the period 1984-2004 (the period used by Mkandawire), and 2000-2015 (the period not covered by Mkandawire).

Table 6. 4: Average revenue structure in labour reserve economies, non-labour reserve economies, and in Malawi for the periods 1984-2004, and 2000-2015

Classification	Total Revenue / GDP (%)	Tax Revenue / GDP (%)	Direct Tax/ GDP (%)	Indirect Tax/ GDP (%)	Non- taxes/ GDP (%)	Direct/ Tax Revenue (%)
Labour reserve (1984-2004)	23.38	16.63	5.70	10.93	6.95	34
Labour reserve (2000-2015)	25.29	18.61	6.21	12.40	6.68	33
Non-labour reserve (1984-2004)	13.88	10.05	2.51	7.54	3.83	25
Non-labour reserve (2000-2015)	15.79	11.48	3.50	7.98	4.31	30
Malawi (1984-2004)	9.43	8.18	3.31	4.87	1.25	40
Malawi (2000-2015)	13.54	12.35	5.46	6.89	1.19	44

Source: ICTD/UN-WIDER Government revenue dataset, (2017)

Comparing tax collection and tax structure for 1984-2004 with 2000-2015 for LREs and NLREs as shown in Table 6.4 reveals that the proportion of revenue obtained from direct taxes increased much more in NLREs between the two periods, from 2.5% of GDP to 3.5% of GDP (an increase of 39%), than in LREs, where the increase was

only 9% (from 5.7% of GDP to 6.2% of GDP). This increase can also be seen in Table 6.4 (last column on the left), where the proportion of direct taxes in total revenues slightly declined, from 34% to 33%, in LREs between the two periods, while it increased from 25% to 30% in NLREs. Thus, although the statistical predictions from the colonial legacy theory still hold when more recent tax data is used, the extent of that influence is declining with each passing year.

In Malawi (bottom two rows in Table 6.4), the overall tax pattern in terms of tax structure is that of an LRE, where the reliance is on direct taxes. The average share of direct tax in total revenues in Malawi between 1984-2004 was 40%; this increased to 44% between 2000-2015 (see last column on the right in Table 6.4).

These findings show that Mkandawire's (2010) pattern of tax structure for LREs and NLREs holds, but is generally weakening. However, it holds more strongly for Malawi.

6.4 Review of Tax Collection History in Malawi Since Introduction of Formal Taxes in 1891

This section traces Malawi's tax structure from the time formal taxes were introduced in 1891 until 2015. The aim is to understand the mechanism through which the high reliance on direct tax in Malawi was sustained throughout this period.

6.4.1 Taxation During the Colonial Period (1891-1963)

Formal taxation was introduced in Nyasaland (present-day Malawi) by the British. Malawi became a British protectorate on 11 June 1891 and received independence on 6 July 1964 (Baker, 1975). During the colonial period, each colony was encouraged to find ways of funding their local expenses without assistance from the British Treasury (Gardener, 2012). The two main sources of revenue for the colonial governments were the trade tax and hut tax (Frankema & van Waijenburg, 2014). In Malawi, trade taxes did not contribute significantly to revenue, especially during the earlier years of the administration. This is attributed mainly to the following three factors:

1. Malawi is a landlocked country, which made transport of goods from inland to the coast slow and difficult, due to the poor road and rail infrastructure

(Nyasaland Financial Statement, 1911). This restricted the flow of trade and, hence, reduced collection of taxes from trade.

2. Malawi did not trade in any goods or mineral resources other than ivory, which was not taxable (Nyasaland Financial Statement, 2011).
3. During the early years of the colonial administration, the indigenous population was hostile to the white settlers in resistance to colonisation. One way in which they demonstrated this hostility was by blocking roads and rivers, thereby making it even more difficult to trade (Nyasaland Financial Statement, 1911; Morris, 2015).

The colonial administration thus concentrated on taxing the indigenous people through hut tax or poll tax. In addition to raising revenue, the hut/poll tax was used to stimulate the flow of wage labour (Massey, 1978). Individuals who could not afford to pay the poll tax were forced to work in farms for a specified period of time (usually one month) in a system commonly known as *Thangata*⁵¹ (unpaid work) (Prowse, 2013). This system worked to the advantage of the settlers because commercial farming was limited to the small community of white settlers,⁵² as the indigenous people were prohibited from owning farms or starting formal businesses. Throughout the colonial period, the hut/poll tax was the main source of revenue for the colonial government, contributing as much as 55% of tax revenue between 1911-1920 (Table 6.6).

The hut tax was first introduced in 1891. It applied to the indigenous population only, and was increased almost every year between 1891-1920 (Baker, 1975). In 1922, the colonial administration introduced corporate income tax (CIT), which applied to white businesses only (Nyasaland Protectorate, 1923). Between 1922-1930, CIT did not generate much revenue because there were few companies, which were also not very profitable⁵³ (Nyasaland Protectorate, 1930). However, the contribution of CIT to total

⁵¹ Thangata was an arrangement between the (European) estate owners and the indigenous people, where the estate owners would give the indigenous people a small piece of land to settle on and for subsistence farming in exchange for at least one month's estate labour and an additional month's protectorate hut tax.

⁵² The white population in Malawi has never been large. There were a total of 314 white settlers in 1901, 1,486 in 1921, 1,975 in 1931, and 1948 in 1945. The small community of white settlers was divided occupationally between farmers, those in trade and commerce, and government officials and missionaries (Palmer, 1985).

⁵³ Thomas (1975) reported that in 1952 there were only 11 companies in Malawi; one cigarette factory, one oil expression plant, two cloth factories, two blanket factories, one cement mill, two sweet factories, one soap factory, and one vehicle assembly plant.

domestic revenue increased at the onset of the Second World War in 1939. This was a result of increased demand for, and thus prices of, cotton and tea, which at that time were Malawi's primary agricultural products (Nyasaland Protectorate, 1941)

In 1953, Northern Rhodesia (Zambia), Southern Rhodesia (Zimbabwe), and Nyasaland (Malawi) were merged to form the Central African Federation (Rosberg Jr, 1956). To finance the running of the federal government, over 95% of the trade taxes and some non-taxes (e.g., postal fees) were re-assigned to the federal government (Nyasaland Protectorate, 1955). Consequently, between 1953-1963 (the period the federation existed), income taxes accounted for over 60% of domestic revenue in Malawi (Nyasaland Protectorate, 1961) (Table 6.6).

6.4.2 Taxation During Dr Banda's Presidency (1964-1994)

At independence, Dr Kamuzu Banda was elected president, a position he retained until 1994. During the colonial period, Malawians did not hold prominent positions in government and were not permitted to own commercial farms or formal businesses (Kydd 1988). Thus, to a large extent, Malawians did not have the technical and professional skills to run the government (Kaunda, 1995). To ensure a smooth transition from British rule to self-rule, Dr Banda retained a number of white settlers who had previously held senior positions in government, to enable skills transfer (Kydd, 1988; Kaunda, 1995).

As occurred during the colonial era, during Dr Banda's term of office, there was no promotion of smallholder farming. Instead, Dr Banda promoted commercial farming and gave many advantages to close allies, allowing them to own and run commercial farms and other large-scale businesses (Kaunda, 1995). To acquire the financial resources needed for the development of commercial farming, the marketing board, the Agricultural Development and Marketing Corporation (ADMARC), extracted resources from smallholders (especially those growing tobacco, cotton, and tea) both through controlled low prices and through formal commodity taxes (Kadyampakeni, 1988). Similar to the poll tax, the low prices offered to smallholder farmers rendered smallholder farming non-profitable, such that smallholder farmers were forced to seek work on commercial farms. Thus, the government practised a new variant of the colonial

practice of using taxes (and in this case, producer price controls) to force smallholder farmers to provide labour to the commercial sector at low cost. In addition, the profits made by ADMARC were invested in estate farming, not smallholder agriculture (Kadyampakeni, 1988). As a result, during Dr Banda's tenure, only a few large businesses emerged. Dr Banda specifically promoted three entities: Press Holdings Limited, the Malawi Development Corporation (MDC), and ADMARC (Kaunda, 1995). By the early 1970s, Press Holding Limited, a company wholly owned by Dr Banda, was the biggest contributor to GDP. At its peak, Press Holdings Limited accounted for one-third (33%) of Malawi's GDP, employed 10% of the wage-earning workforce, and paid more than 30% of the taxes collected by the government (Meredith, 2011; Cammack & Kelsall, 2011).

Dr Banda's policies on industrialisation were comparable to those of Mikhailov (the governor of Pskov Oblast, a region in north-western Russia) in the 1990s (Gehlbach, 2008). Mikhailov deliberately promoted a small number of large enterprises (vodka producers) to dominate the economy, as this sector was easy to tax and therefore would contribute more to the development of the region (Gehlbach, 2008). Pskov Oblast experienced significant economic growth as a result of this policy. Similarly, the promotion of a few big companies in Malawi allowed for greater operational control by Dr Banda (such as designating objectives and giving authoritative direction), since the large-scale commercial farms and big businesses were partly or wholly owned by Dr Banda, his close allies, or the government. Dr Banda also ensured that all companies in Malawi were tax-compliant (Van Donge, 2002); he encouraged tax compliance in his businesses, and those of his allies, as he wanted to serve as a role model for other entrepreneurs (Cammack & Kelsall, 2011). It is also reasonable to assume that Dr Banda encouraged tax compliance because he was the head of government. Thus, he needed funds for the running of the country.

It should be noted that the key factors that explain the continued reliance on direct tax during Dr Banda's tenure were two-fold. First was the economic structure, which was similar to that of the colonial period. As in the colonial period, economic activities were concentrated in the hands of a few individuals and companies. This made it easy for the tax-collecting agency to monitor the tax payments of these companies. Second was Dr Banda's determination to ensure that companies and organisations paid taxes. The support that Dr Banda gave to the tax-collecting department was key to the

success of the Malawi Government in collecting taxes.

6.4.3 Taxation in More Recent Years (1994-2015)

Malawi changed from a one-party state under Dr Banda, to a multiparty democracy in 1994. However, as noted in Chapter 2, this change did not have a significant impact on the *modus operandi* of the government. The biggest impact on the economy emerged four years before Dr Banda's rule of Malawi came to an end in 1990, with the implementation of the Structural Adjustment Programmes (SAPs). The SAPs involved changing most of the policies that Dr Banda had followed, such as removing the fixed price at which smallholder farmers could sell their products; liberalisation of agricultural marketing, thereby allowing more players to enter the system; and privatisation (either wholly or partially) of public holding companies, such as ADMARC. In addition, the privately-owned Press Holdings Limited was broken down to create small independent entities (Chipeta, 1998; Kalua et al., 1992; Kydd, 1988), thereby increasing the number of companies in the country.

These developments in the 1990s had an impact on the economic structure of Malawi, as the size of some companies was reduced, thereby, in theory, creating a more competitive environment. In addition, price and marketing liberalisation was, in principle, intended to ensure that smallholder farmers could flourish and create a more diversified economy (Chirwa, 2004). The change from Dr Banda's economic structure and the change from one-party to multiparty rule may have had a negative impact on direct tax collection in Malawi in two ways. First, the tax administration had to collect direct taxes from a significantly greater number of companies, making it more difficult to monitor all businesses. Second, the support that the tax administration had received from Dr Banda, who encouraged tax compliance, was lacking after his presidency ended.

Table 6.6 shows that direct taxes as a share of total revenue was slightly higher than indirect tax during the early Banda period (1964-80), averaging 45%, and then declined to 33% during the later Banda tenure and early post-Banda period (1980 to 1995). The decline in direct tax collection (and total tax revenue collection in general) between 1980-1995 reflects the political (change from a one-party to a multiparty system, a volatile period) and policy instability (SAPs) during this period (Chapter 2). The share of total revenue accounted for by direct tax increased to an average of 41% between 1995-2015. Given that Dr Banda was no longer president, and hence the

pressure that businesses were under from Dr Banda to be tax-compliant reduced, and the fact that most of the major SAPs were implemented in the late 1980s and early 1990s, the question arises of what explains the continued reliance on direct tax in Malawi in the more recent period (1995-2015).

There are three likely explanations for this continued reliance after 1994: the introduction of VAT in 2005 (discussed in Chapter 2), the structure of the Malawian economy, and close surveillance of large businesses. The latter two factors are discussed in this section.

Structure of the Malawian Economy

As has been confirmed in Sections 2 and 3 of this chapter, the economic structure, practices, and mindsets that led to the high collection of direct taxes during the colonial period and during Dr Banda's presidency persist in present-day Malawi. The administrative practices that prevailed during Banda's tenure have continued because minimal operational changes occurred during the transition from a one-party state (Banda's tenure) to a multiparty democracy (from 1994, with Dr Bakili Muluzi as the president). Cammack (2004) described the change from a one-party state to a multiparty democracy as "transition without transformation," as many systems and personalities did not change. Cammack (2004) further argued that the economic strategy articulated by the new United Democratic Front (UDF) government and President Muluzi conformed to that of the previous government. Thus, tax collectors continue to believe that they can collect a significant amount of revenue from direct tax, and this focus has not changed. In addition, the de-merging of companies such as Press Holdings Limited did not significantly impact the structure of the economy, since income is still concentrated in the hands of a few individuals and businesses. As noted in Chapter 5, less than 2% of businesses in Malawi are classified as "large", yet they contribute over 70% of the tax revenues.

Close Surveillance of Large Businesses

One of the major changes made to tax administration between 2000 and 2015 was the creation of the semi-autonomous revenue authority, the MRA. According to the former Deputy Commissioner General (DCG) of the Malawi Revenue Authority, the creation of the MRA boosted tax collector morale such that tax collectors worked hard

to ensure that more taxes were collected. Specifically, the former DCG pointed out that:

When the MRA was created and staff who worked in the tax departments in the Ministry of Finance in Lilongwe were moved to the Malawi Revenue Authority offices in Blantyre, salaries were more than tripled, training opportunities were available for almost everyone, equipment such as computers were made available, bonuses were introduced for beating the tax collection target, and better working conditions in general were offered. This greatly motivated the staff to work hard. (Interview with Mr C.C. Kulemeka, 13 December 2016)

Due to increased motivation, MRA staff believed they could collect more tax from big businesses, as they used to during the Dr Banda era, by re-establishing close surveillance of larger companies. This belief further led to the reorganisation of MRA functions, which resulted in the creation of the Large Taxpayer Unit (LTU) in 2007. Unlike other departments in the MRA, the operations of the LTU are highly efficient and effective (see Chapter 5). Table 6.5 shows the amount of taxes collected from large taxpayers by the LTU.

Table 6. 5: Average contribution of various taxes to total tax revenue in Malawi between 2000-2015

Tax Type	Tax Type/Total Revenues (%)
Direct Taxes	47
PAYE	28
o/w LTU	20
Corporate income tax	11
o/w LTU	10
Withholding tax	8
o/w LTU	6
Indirect Taxes	53
Customs duties (import duty, import excise, import VAT)	32
Other taxes (VAT, excise, etc.)	21
o/w LTU	16
Total Tax Revenue	100

Source: Malawi Revenue Authority, 2016

Note: LTU = Large Taxpayer Unit; VAT = value added tax

Table 6.5 shows that direct tax as a share of total revenue averaged 47% between 2000-2015. PAYE accounts for 60% ($28 \div 47$) of direct taxes, while corporate income tax accounts for 23% ($11 \div 47$) of direct taxes. Of the total direct taxes, 77% ($((20+10+8) \div 47)$) is collected by the LTU from large taxpayers. During the 2014/15 fiscal year, 32,000 taxpayers were registered and had made at least one tax payment to the MRA in the previous three years. Of the registered taxpayers, 451 were classified by the MRA as large taxpayers. Thus, 77% of direct taxes in Malawi is collected from less than 2% ($451 \div 32,000 = 1.4$) of the registered taxpayers.

I interviewed six officers working in the LTU to discover why they were more successful in collecting direct taxes than the small and medium taxpayer units. All the officers interviewed attributed the success to the close surveillance that the LTU maintains on large taxpayers. One officer in LTU explained that:

I do not blame the small and medium taxpayer units for failing to collect a significant amount of income taxes from their taxpayers. They manage too many taxpayers, such that closely following each taxpayer would not make sense. The result is that many taxpayers are either not paying income taxes or they are grossly under paying. By contrast, officers in the LTU manage few taxpayers and follow up with each taxpayer. For instance, one of the taxpayers that was giving us problems in paying PAYE was the Government. What we did was assign an officer whose main job it is to ensure that the government has made PAYE payments. On a monthly basis, when PAYE is due, this officer makes phone calls to remind officers in the Accountant General Department (AGD) to make the PAYE payment. Sometimes, the officer has to physically visit the AGD offices several times before the cheque for PAYE is written and given to us. We can afford to have this kind of follow-up with taxpayers because we manage few taxpayers. It would be too expensive for small or medium taxpayer units to implement similar close follow-ups. (Interview with an officer from LTU, MRA, 15th November 2016)

Aside from the collection of direct taxes, the LTU also collects indirect taxes, such as VAT and excise tax. Table 6.5 shows that 80% ($16 \div 20$) of the other domestic taxes (VAT, excise etc.) are collected from large taxpayers.

In general, taxes collected from large taxpayers in Malawi account for approximately 70% of the revenue collected by MRA (MRA, 2017). It is this high contribution of tax revenue from large taxpayers that forces the MRA to closely monitor the operations and tax payments of large businesses.

Table 6.6 shows the five-year average share of direct tax, indirect tax, and non-taxes in GDP in Malawi between 1911-2015. The table shows that tax collection declined during the later years of Banda's presidency and the early years of the multiparty era (1980-1995). Thereafter, tax collection began to increase. However, the increase in tax collection between 1995-2005 was a recovery of the slump of 1990-95. As discussed in Chapter 2 and the present chapter, the increase in tax collection between 2005-2015 was due to a combination of three factors: the introduction of VAT in 2005; the structure of the economy in Malawi, where income is concentrated in the hands of a few individuals and businesses, thereby making it tax administration easier; and the close surveillance of large taxpayers by the LTU.

Table 6. 6: Proportion of direct taxes, indirect taxes, and non-taxes in total central government revenues in Malawi (1911-2015) (five-year averages)

Year	Direct Tax/total Revenue (%)	Indirect Tax/Total Revenue (%)	Non-Tax/Total Revenue (%)
1911-1915	55	34	11
1916-1920	49	39	12
1920-1925	44	40	16
1926-1930	40	44	16
1931-1935	37	44	19
1936-1940	35	39	26
1941-1945	52	31	17
1946-1950	42	43	15
1951-1955	37	35	28
1956-1960	59	31	10
1961-1963	52	33	15
1966-1970	48	49	3
1971-1975	42	57	1
1976-1980	46	53	1
1980-1985	33	51	16
1986-1990	34	52	14
1991-1995	33	53	14
1996-2000	39	51	10
2001-2005	39	49	12
2006-2010	42	50	8
2011-2015	44	49	7

Sources: (Nyasaland Financial Reports and Statements, 1909; Nyasaland Protectorate, 1912; Nyasaland Protectorate, 1920; Nyasaland Protectorate, 1940; 1953; 1961⁵⁴; Chipeta, 1998 (1970-1980); ICTD/UNC WIDER Government Revenue Database, 2017).

6.5 Conclusion

This chapter aimed at identifying the reasons why Malawi is so successful in collecting direct taxes. The high reliance on direct tax for a low-income country like Malawi is

⁵⁴ The Financial Reports and Statements can be found on the British Online Archives website: <http://microform.digital/boa/collections/23/volumes/390/finance-1911-1966>

unusual given that empirical evidence shows that low-income countries with a weak tax administration and a big informal sector typically have a higher reliance on indirect taxes than direct taxes. In exploring this anomaly, I have assessed, tested, and updated an influential paper on the influence of colonial legacy on tax collection in SSA by Mkandawire (2010).

The analyses showed that, during the early years of colonisation, the only available source of revenue for the colonial government was taxation of the local people through the hut/poll tax. Throughout the colonial period, there were no policies to encourage entrepreneurship or industrialisation by the indigenous people, as the system was deliberately skewed to benefit large settler enterprises, mainly plantations. This resulted in the creation of few large, formal, labour-intensive businesses. The efforts of the government to tax individuals and the few formal businesses led to the high reliance on direct tax. Direct tax collection remained high in Malawi even after the country gained independence in 1964, and up to 1994, as its policy and economic structures remained broadly similar to those of the colonial period. In other words, the collection of direct tax by the tax administration was made easier due to the combination of concentration of income in the hands of a few individuals and businesses, and state determination and ability to tax large enterprises. The late 1980s and early 1990s brought a number of changes to the economic structure and administration in Malawi, including the implementation of SAPs, which resulted in the de-merging of large companies, such as Press Holdings Limited. Reliance on direct tax in Malawi initially declined between 1990-1994 but has since remained high compared to other SSA countries. This is attributed to income being generated by only a few individuals and companies, the introduction of VAT in 2005, and the close surveillance of large taxpayers.

Thus, in general, Malawi's history and its economic structure significantly contribute to explaining the high ratio of direct tax to total revenues.

This chapter contributes to the literature in three ways. First, it provides a review of the history of tax collection in Malawi since the introduction of formal taxes in 1891, until 2015. Second, it adds to the limited empirical evidence on how colonial history shaped, and continues to shape, the level of tax collection and tax structure in SSA, including in Malawi, by updating the most influential paper on the colonial legacy, authored by Mkandawire (2010). Third, it challenges the commonly held view that low-

income countries, which usually have weak tax administration and a large informal sector, are better placed to rely more on indirect taxes, as these are easier to collect than direct taxes. The evidence in this chapter points to the fact that these low-income countries can still collect significant revenue from direct taxes if the government is committed and able to tax the sectors with the greatest potential for revenue generation, typically large businesses, individuals with a high income, and the extractive industry.

Chapter 7: Conclusion

7.1 Introduction

Although the number of studies on tax revenue mobilisation in Malawi has increased over the years (Chamley et al., 1985; Chipeta, 1998; Chiumya, 2008; Chafuwa, Kenani & Kaunda, 2017) these studies have generally focused on tax policy changes and trends in tax revenue collection. To the best of my knowledge, no study has been undertaken to understand why tax revenue performance in Malawi, in terms of tax effort and tax-to-GDP ratio, has been better than in most SSA countries since 2009, or why there has been a high reliance on direct tax in Malawi compared to most SSA countries since the inception of formal taxes in 1891. This thesis is the first attempt to comprehensively address these issues; in doing so, it has provided some plausible answers to the following questions:

- Why did the ratio of tax-to-GDP in Malawi increase significantly between 2005-2011, from 10% to 17.5% of GDP?
- Why, in recent years (since 2009), has the tax-to-GDP ratio been significantly higher in Malawi than in comparable SSA countries?
- Why and how, since 1964, have the Malawian tax authorities been able to raise an unusually high proportion of total tax revenue (and total revenue) from direct taxes, i.e., taxes on income. These figures are high for Malawi compared to most SSA countries, and indeed to low-income countries generally.

Based on the understanding that level of tax revenue collection mainly depends on, among other things: tax policy; the actions of taxpayers; the actions of tax collectors; and the structure of the economy, the following four hypotheses were explored:

- The introduction of value added tax (VAT) in 2005 led to increases in the collection of both direct and indirect taxes.
- Malawians are exceptionally good and willing taxpayers (i.e., tax morale is high) relative to the populations in other SSA countries.
- Malawi has an effective tax administration.
- Malawi's colonial history has steered the country towards a relatively higher tax revenue performance.

In the next section, I reflect on the findings from the investigation of these

hypotheses. I then present the main conclusion of this thesis and its contribution to literature. Next, I discuss the implications of my findings for policy and practice, and what I have learned from carrying out this research. I conclude with a discussion of future possible research directions.

7.2 Reflection on Empirical Findings

7.2.1 Impact of the Introduction of Value Added Tax on Revenue Collection

In Chapter 2, I found that, after VAT was introduced in Malawi in 2005, the tax-to-GDP ratio began to increase, driven mainly by the increase in both VAT collection and other taxes. VAT started to be introduced in many low-income countries in the 1990s (Gbato, 2017). Based on a sample of 32 countries in SSA, Gbato (2017) found that, following the introduction of VAT in these countries, the share of indirect revenues rose from 27% in 1990 to 43% of total tax revenues in 2010. Gbato (2017) attributes this to the ease of implementation and the low economic cost of VAT as the main drivers of the mobilisation of significant revenue. Considering that the trend is largely similar in most countries in SSA, where the introduction of VAT leads to increased revenue collection, it is reasonable to attribute the significant increase in tax-to-GDP ratio in Malawi, especially between 2005-2011, to the introduction of VAT.

Indeed, aside from the role of VAT, I did not find any other explanation for why tax collection increased rapidly in Malawi between 2005-2011 and then plateaued. The political and economic stressors of 2011-2013 may have contributed to the plateauing of VAT collection and the tax-to-GDP ratio in general. However, both the political and economic environment improved after 2014 and yet VAT collection, and the tax-to-GDP ratio generally, has not changed. Investigating why the tax-to-GDP ratio plateaued in Malawi post-2011 is beyond the scope of this thesis, but represents an interesting avenue for future research.

7.2.2 Malawians are Willing Taxpayers

The second hypothesis I explored (Chapters 3 and 4) was that Malawians are good and willing taxpayers relative to the populations in other SSA countries. This hypothesis addresses the question of why the tax-to-GDP ratio in Malawi is unusually high compared to the average for SSA countries since 2009.

The cross-country analysis of tax morale in Malawi and other SSA countries showed that tax morale in Malawi does not significantly differ from the average tax morale in other SSA countries. In other words, Malawians are no more or less willing to pay taxes than the populations in other SSA countries. However, an analysis of tax morale among business people in Malawi showed that: large businesses have high tax morale compared to small or medium businesses; businesses operating in Blantyre have higher tax morale than those operating in Lilongwe; and businesses in the construction sector have lower tax morale compared to businesses operating in other sectors.

It has been shown in Chapter 6 that revenue collected by the LTU in Malawi accounts for approximately 70% of revenue collected by the MRA since 2000. Thus, although tax morale in Malawi is not significantly different from the average tax morale for SSA countries, the fact that large businesses and businesses operating in Blantyre have high tax morale may be contributing to the overall good tax revenue performance in Malawi. However, I did not conduct any statistical analysis to determine whether large taxpayers and taxpayers in Blantyre do indeed have higher tax compliance than small/medium taxpayers and taxpayers in Lilongwe, respectively. Thus, arguing that large business and businesses in Blantyre may be contributing to the high tax collection in Malawi because they have higher tax morale than other business groups is in no way arguing that high tax morale (which relates to attitudes towards taxes) automatically translates to high tax compliance (which relates to the behaviour of taxpayers).

7.2.3 The Effective Tax Administration in Malawi

The third hypothesis explored in this thesis relates to the effectiveness of the tax administration (Chapter 5). I conducted a detailed analysis of the efficiency and effectiveness (process performance) of the revenue collecting units in the MRA in four areas: taxpayer registration and data management, dispute resolution, tax audit, and taxpayer education. The overall performance was found to be mixed. Only one of the revenue collecting units, the LTU, was found to be efficient and effective in carrying out all the functions assessed; the small and medium taxpayer units were found to be ineffective and inefficient.

Although the results were mixed, they highlight an important feature of tax collection in Malawi. It was noted that the LTU was introduced in 2007 and has since become the key tax revenue-collecting unit, collecting as much as 70% of tax revenue.

It is therefore reasonable to attribute both the significant increase in tax-to-GDP ratio between 2005-2011 and the good tax revenue performance in Malawi relative to other SSA countries since 2009 in large part to the efficiency and effectiveness of the LTU. I recognise that most low-income countries have introduced an LTU within their tax administration (Tennant & Tracey, 2018). In general, the LTUs manage a small number of taxpayers but account for the highest share of tax revenue collected by tax administrations (Tennant & Tracey, 2018). Thus, the fact that the LTU in Malawi collects a significant amount of revenue is not on its own a sufficient reason to explain the good tax revenue performance in the country. However, when we consider the colonial and post-colonial political and economic history of Malawi (discussed in Chapter 6) and the importance of the close surveillance of large businesses promoted by Dr Banda between 1964-1994, the importance of the LTU becomes significant and can be noted to be the crucial factor influencing tax revenue collection in Malawi since 2007.

7.2.4 Colonial Legacy

In Chapter 2 and Chapter 6 it was noted that, at independence, Malawi inherited a tax system that was highly reliant on direct tax, a situation which has persisted to date. This suggests that there is something inherent to the history of taxation and/or the framework of Malawi's economy that has driven the country towards being more reliant on direct tax and generating higher tax revenue. Indeed, a well-renowned scholar from Malawi, Thandika Mkandawire, investigated the relationship between level of tax collection and tax structure in SSA and the region's colonial legacy (Mkandawire, 2010).

Mkandawire (2010) classifies countries of Africa according to structures of colonial economic exploitation (labour reserve economies, cash crop economies, and concessional companies). Malawi is classified as a labour reserve economy, and Mkandawire argues that these are better able to raise revenue and more reliant on direct taxes. This argument was based on statistical analysis for the period 1984-2004. I have expanded Mkandawire's theory in two ways. First, I looked deeper (1910-1960) into records of revenue-raising in Malawi and seven other countries in SSA and found that Mkandawire's argument holds. Second, I looked at comparative revenue performance for 25 countries in Africa for a more recent period (2000-2015) and again found that

Mkandawire's pattern holds, but is generally weakening. However, it holds more strongly for Malawi. Why has the colonial legacy had such a strong impact in Malawi? The likely answer to this question reveals the importance of and linkage between the colonial legacy and the close surveillance of large taxpayers in Malawi through the LTU. Since colonial period, Malawi has had an unusual pattern of ownership of major economic assets, where most assets are owned by a few individuals. It is, therefore, critical that those with high income and wealth are closely monitored by the revenue authority.

7.3 Main Conclusions and Contribution of the Thesis to Literature

It was difficult to reach clear answers to the three main research questions. The conclusions of the study are as follows:

1. The drastic increase in tax-to-GDP ratio between 2005-2011 in Malawi is partially explained by the introduction of value added tax (VAT) in 2005 (Chapter 2), which resulted in improvements in the collection of both direct and indirect taxes. It must be noted that, apart from the role of VAT, I did not find any other explanation for why tax collection increased rapidly between 2005-2011 and then plateaued.
2. The higher tax-to-GDP ratio in Malawi compared to other sub-Saharan African countries since 2009 is partially explained by the combination of the introduction of VAT in 2005 and the ability of the Malawi Revenue Authority to collect significant revenues from large companies and their employees, despite the use of tax collection methods that appear to be lagging behind technological frontiers.
3. The ability of the Malawi Revenue Authority (and previous tax administrations, even during the colonial period) to collect significant revenue from large companies and their employees explains the high reliance on direct tax in Malawi. This ability is facilitated by Malawi's economic structure, where income is concentrated into the hands of just a few businesses and individuals; this has been the case during both the colonial and the post-colonial eras.

Overall, the thesis makes two major contributions to the existing literature, in regard to both theoretical and empirical knowledge:

1. It contributes to the debate on tax revenue mobilisation in SSA by providing comprehensive evidence from Malawi on how a low-income country with a pattern of tax administration that appears to be ineffective by normal measures, is effective in practice.
2. It contributes to the limited evidence on the colonial legacy theory, which suggests that the current tax structure and level of tax collection in SSA stems from its colonial history. Due to data scarcity prior to 2015, no comprehensive empirical evidence on the tax structure and level of tax collection during the colonial era (prior to 1960) and more recent years (2004-2015) has been produced. This thesis has provided evidence related to this topic.

7.4 Implications for Policy and Practice

Having presented the main findings of this study in the previous section, it is important to illustrate how these findings could contribute to future policy formulation. If tax revenue collection in Malawi is to be enhanced, or at least sustained at existing levels, it is critical for policymakers to have a broad understanding of the dynamics of tax revenue mobilisation. Significantly, the results suggest that, as well as implementing policies that would lead to increased tax revenue collection, it is also important for the government to ensure that success is safeguarded and sustained. There are four key policy implications emanating from this study: 1) the need to improve tax morale among small and medium taxpayers, taxpayers in Lilongwe, and taxpayers in the construction sector; 2) the need to improve tax administration, especially for the small and medium taxpayer units; 3) the need to support the LTU to sustain the good tax revenue collection; and 4) the need to improve the efficiency of VAT.

- 1) **Improving tax morale among small and medium taxpayers and businesses in various sectors.** Tax morale has been found to be one of the key determining factors of tax compliance (Alm & Martinez-Vazquez, 2007; Torgler, 2007). The empirical evidence presented in Chapter 4 shows that tax morale is low among business people in Lilongwe compared to those in Blantyre, small and medium taxpayers compared to large taxpayers, and business people in the construction sector compared to those in other sectors. As one of the key determining factors of tax compliance, it is important that measures be employed to improve the tax morale of taxpayers in these categories.

- 2) **Improving tax administration, especially in data management, dispute resolution, and taxpayer education.** It was established in Chapter 5 that tax administration in Malawi is weak. Although the LTU is efficient and effective in fulfilling its functions, in many instances, it does so only by using unconventional measures that are less reliable, such as using MS Excel to store and update taxpayer data. Improving tax administration in Malawi may lead to an increase in tax collection; more importantly, it will also ensure that the good tax revenue performance is sustained. There are at least two interventions that the MRA could initiate to improve the efficiency and effectiveness of all the revenue collecting units. First, is improvement in taxpayer data management. The procurement of ITAS, a system aimed at improving taxpayer data management, should be supported and facilitated. Second, there is a clear need for the Malawian Government to introduce a taxpayer tribunal to deal with the bottlenecks in the dispute resolution process. A tax tribunal is an independent body that ensures that taxpayers' arguments are heard, and objective decisions are made. Having an independent body responsible for taxpayer disputes will improve taxpayers' trust in the tax authority. However, in the short term, the MRA should immediately produce a detailed information sheet about the dispute resolution process and make it available to all taxpayers, especially small and medium ones.
- 3) **Supporting the LTU.** It was noted in Chapters 5 and 6 that the good tax revenue performance in Malawi is partly due to the combined effect of the economic structure, where income is concentrated in the hands of a few individuals and businesses, and close surveillance of large businesses is carried out by the LTU. Thus, any weaknesses in the operation of the LTU will clearly have a significant impact on tax collection in Malawi. The MRA should therefore continue investing in the LTU to ensure that it fulfils its functions and operates effectively. Currently, the LTU utilises unreliable measures to address weaknesses in the tax administration. As the number of taxpayers administered in the LTU increases, it will become more difficult for the LTU to continue its reliance on these less dependable means. The biggest challenge with the LTU is data management, followed by weaknesses in audit case selection. Thus, supporting the operations of the LTU will involve improving the operations of other departments, such as the audit department.

- 4) **Improving the efficiency of VAT.** The introduction of VAT in Malawi has been key to the dramatic increase in the tax-to-GDP ratio between 2005-2011. However, the growth in VAT has stalled since 2011. There is, therefore, a need for the MRA to invest more in measures that will increase VAT collection.
- 5) **Improving the efficiency and effectiveness of the small and medium taxpayer units.** The bulk of tax revenue in Malawi is collected by the LTU. The MRA has therefore placed much emphasis on improving the operation of the LTU. However, there has been comparatively little focus on improving the operations of the small and medium taxpayer units. Improving these operations will achieve two things. First, more tax revenue would be collected, thus improving tax revenue mobilisation in Malawi. It has been noted that over 95% of taxpayers in Malawi are small and medium taxpayers; the importance of ensuring that as many as possible of these taxpayers make their tax payments cannot be overstated. The greatest potential for Malawi to increase the tax-to-GDP ratio lies in these categories of taxpayers, as they are currently not effectively or efficiently managed. The reluctance to put too much emphasis on the operations of the small and medium taxpayer units by the MRA is likely due to the high administrative costs associated with administration of this category of taxpayers (Evans et al., 2013; Coolidge, 2012). However, considering the advancements in information technology (IT), the MRA should explore the use of IT systems in the administration of small and medium taxpayers. Second, it will improve the tax compliance culture among small and medium taxpayers, thereby ensuring that they are more compliant if and when they graduate to become large taxpayers.

7.5 What I Learned From This Research

Over the past three and half years that I have been working on this thesis, I have learned various valuable lessons. In this section, I will highlight only two.

First, **to be wary of standardised approaches.** Assessment of tax administration performance in low-income countries is being carried out under TADAT. TADAT provides useful information based upon which countries can improve their administration. However, what I have learned from this research is that what is considered to be an ‘international standard’ with regard to process performance in

TADAT, does not necessarily translate to high tax revenue performance, as is the case for Malawi. There is a need to go beyond the standardised approaches such as TADAT and consider country nuances to better understand tax administration performance in low-income countries, such as Malawi, a country with a pattern of tax administration that, by normal measures, appears to be ineffective but is effective in practice.

Second, **to be wary of cross-sectional data**. Cross-sectional data provides information such as people's views and attitudes about an issue at a particular time. However, people's views and attitudes may change based on place and time. Accordingly, this means that the findings of any research that is based on cross-sectional data applies only to the time the survey was conducted. For example, using Afrobarometer data collected in 2011/2012 (R5) and in 2013/14 (R6) to analyse tax morale in Malawi yielded conflicting results. Therefore, the interpretation of the results of tax morale studies based on cross-sectional survey data should consider the prevailing political and economic environment at the time of data collection, and any other factors that may affect people's attitudes and behaviour.

7.6 Future Research Direction

This thesis has identified many opportunities for future research and for refining the analysis in this thesis. Below are some of those I hope to pursue further.

First, the analysis of tax morale conducted in Chapters 3 and 4 can be augmented through studies that consider the behaviour of taxpayers and not just their attitudes towards taxation. The analysis in this thesis has shown that, while tax morale studies provide insight into taxpayer attitudes, people's attitudes change with time; the significant variation between people's attitudes in R5 and R6 in Malawi is evidence of this. Accordingly, augmenting tax morale studies with studies that closely look at taxpayer behaviour, such as field experiments, would provide a more comprehensive picture of the drivers of tax compliance in a country.

Second, Chapter 4 has indicated that going beyond TADAT assessment to closely evaluate tax administration performance in the same areas assessed under TADAT can provide a better understanding of a tax administration's performance. I was only able to assess the MRA on four of the nine areas assessed under TADAT. It would be useful to assess the MRA on all nine areas for a more comprehensive understanding

of the challenges and weaknesses of the institution. Clearly, this would require gaining access to disaggregated taxpayer data, which was the key limitation preventing me from assessing all nine areas for this study. Convincing the MRA of the usefulness of undertaking such an assessment of the tax administration, as well as providing them with alternative suggestions for how the disaggregated taxpayer data can be accessed without compromising confidentiality, may lead to researchers being provided access to this data in the future.

Finally, although much has been written about the colonial legacy theory, due to data limitations, prior to this work, the tax structure and level of tax collection in the colonial period had only been assumed. I was only able to provide empirical evidence of the tax structure in both labour reserve and non-labour reserve economies based on eight countries, four labour reserve and four non-labour reserve. According to Mkandawire's (2010) classification of countries based on the nature of their incorporation into the colonial system, there are 11 countries classified as labour reserve and 22 countries classified as either cash crop or concessional companies. Accordingly, including more countries in the analysis of the colonial legacy theory and tracing the mechanism through which the colonial legacy has persisted in the post-colonial era to affect the level of tax collection and tax structure in different countries would provide greater insights into this theory and enhance the current understanding of tax revenue mobilisation in SSA.

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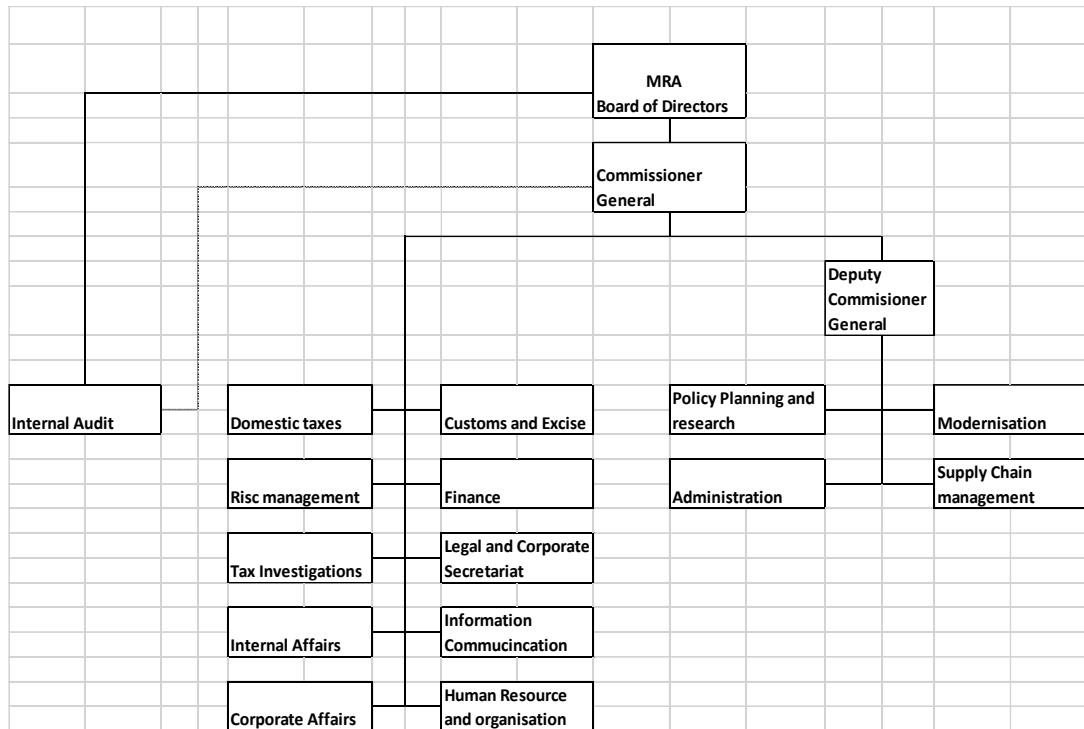
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Appendices

Appendix 2.1: MRA organogram



Appendix 4.1: Political and economic condition During R5 and R6

Country	R5	Political and economic situation during R5 survey	R6	Political and economic situation during R6 survey
Benin	2011	Stable	2014	Stable
Botswana	2012	Stable	2014	Stable
Burkina Faso				Relatively Stable- there were some protests when the president attempt to run for re-election for a third term in 2015 (the limit is two terms). However, peaceful elections were held in November 2015 where the ruling president did not participate.
	2012	Stable	2015	
		Relatively Stable- there were some violence between the ruling patty and opposition groups		Relatively stable: the violence between the ruling patty and opposition groups still existed
Burundi	2012		2014	
Cote d'Ivoire	2013	Stable	2014	Stable
Cameroon	2013	Stable	2015	Stable
Guinea	2013	Stable	2015	Stable-amidst Ebola outbreak
Kenya	2011	Stable	2014	Stable- amidst Al-Shabaab attacks
				Relatively stable: there was an attempted nonviolent coup that lasted for a few days in August 2014
Lesotho	2012	Stable	2014	
Liberia	2012	Stable	2014	stable

Country	R5	Political and economic situation during R5 survey	R6	Political and economic situation during R6 survey
		Unstable-increasing repression and physical and economic insecurity—including intimidation of journalists, violence in the south, and a rise in human trafficking—caused by ongoing political instability that began with a 2009 coup. Donors froze aid to the country which resulted to economic crisis. However, stability started to return in November after peaceful election		
Madagascar	2013	Unstable-government's violent suppression of public protests (which led to death of 18 people), intimidation of journalists, and threats to academic freedom were rife in 2011 and 2012. Consequently, donor froze aid and the country went into a high economic crisis which resulted in shortage of most commodities including fuel. In April 2012 and the vice president was sworn in. However, economic stability did not return into the country until late in the years when donor resumed aid		
Malawi	2012		2014	Stable
Mozambique	2012	Stable	2015	Stable
Namibia	2012	Stable	2014	Stable
Niger	2013	Stable	2015	Stable

Country	R5	Political and economic situation during R5 survey	R6	Political and economic situation during R6 survey
Nigeria	2013	Stable- amidst Boko Haram attacks	2015	Stable- amidst boko Haram attacks
Senegal	2013	Stable	2015	Stable
Sierra Leone	2012	Stable	2015	Stable- amidst ebola crisis
Swaziland	2013	Stable	2015	Stable
Tanzania	2012	Stable	2014	Stable
Togo	2012	Relatively stable-planned election were delayed beyond the planned year which led to some protests	2014	Stable
Uganda	2012	Stable	2015	Stable
Zambia	2013	Stable	2014	Stable
Zimbabwe	2012	Stable	2014	Stable

Notes on Table 1:

1. Source: Compiled based on the Freedom House Annual Reports and the UN Economic Commission for Africa annual country profile
2. “Stable” means there was no reports of political unrest or economic crisis reported for that country in that year. “relatively stable” means there were some political unrest or economic crisis” reported in that country. However, the crisis was not severe and did not lead to violent protests. “Unstable” mean there was political unrest or economic crisis reported in the country. His was accompanied with violent protests and calls for the president to resign

Appendix 4.2: Descriptive statistics: Afrobarometer data (merged for R5 and R6)

Variable	Obs	Mean	Std. Dev	Min	Max
Tax Morale	60,692	0.592	0.491	0	1
Deterrence	52,160	3.235	0.874	0	4
Fiscal	61,198	2.507	0.895	1	4
Unequal	61,565	1.686	1.077	1	4
Treatment					
Trust	58,904	1.543	1.056	1	4
Corruption	55,271	1.469	0.877	1	4
Democracy	58,112	2.346	1.079	0	4
Tax	55,165	2.102	0.958	1	4
Knowledge					
Female	63,585	0.503	0.499	0	1
Education	63,445	3.434	2.212	0	9
Age	63,290	27.986	14.007	18	105
Urban	62,985	0.389	0.487	0	1
Employment	59,777	0.246	0.431	0	1
Malawi	63,586	0.378	0.191	0	1

* Significant at .10 level.

** Significant at .05 level.

*** Significant at .01 level.

Appendix 4.3: Wald Test model 1 (R5 data)

Wald Chi2	677.10
Number of observations	27,139
Prob>chi2	0.00

Appendix 4.4: Wald Test, model 2 (R6 Data)

Wald Chi2	872.67
Number of observations	33,086
Prob>chi2	0.00

Appendix 4.5: Wald Test, Model 3 (merged data-R5 and R6)

Chi2	913.43
Number of observations	43,578
Prob>chi2	0.00

Appendix 4.6: Hosmer-Lemeshow goodness of fit test: Model 1

Number of observations	27,139
Pearson chi2	26,973
Hosner_Lemeshow Chi2 ()	11.98
Prob > chi2	0.2159

Appendix 4.7: Hosmer-Lemeshow goodness of fit test: Model 2

Number of observations	33,086
Number of covariate patterns	32,595
Pearson Chi2	(32613.07)
Prob > chi2	0.4351

Appendix 4.8: Hosmer-Lemeshow goodness of fit test: Model 3

Number of observations	42,145
Number of covariate patterns	40,344
Pearson Chi2	40,133
Prob > chi2	0.3159

Appendix 4.9: Ordered Logit Regression, Equation 1, merged data

Variable	<i>Not wrong at all</i>	<i>Wrong but understandable</i>	<i>Wrong and punishable</i>
Deterrence	-0.04 (0.01)**	-0.02 (0.01)**	0.05 (0.02)**
Fiscal	-0.01 (0.01)	-0.01(0.00)	0.02 (0.01)
Tax Knowledge	0.08 (0.02)**	0.02 (0.01)**	-0.05 (0.02)**
Corruption	0.01 (0.01)*	0.00 (0.00)*	-0.1 (0.01)*
Business size	-0.08(0.05)**	-0.04 (0.03)**	0.12 (0.08)**
Lilongwe	0.12 (0.03)***	-0.05 (0.02)***	-0.17 (0.04)***
Registration status	-0.03 (0.04)	-0.01 (0.02)	0.04 (0.06)
Female	-0.03 (0.03)*	-0.01 (0.01)*	0.04 (0.05)*
Retail	0.01 (0.03)	0.00 (0.02)	-0.01 (0.05)
Manufacturing	-0.04 (0.07)	-0.02 (0.03)	0.07 (0.11)
Accommodation	-0.03 (0.06)	-0.01 (0.03)	0.05 (0.09)
Construction	0.13 (0.08)*	0.06 (0.04)*	-0.19 (0.12)*
Transport	0.05 (0.07)	0.02 (0.03)	-0.07 (0.11)

* Significant at .10 level.

** Significant at .05 level.

*** Significant at .01 level.

Appendix 4.10: Survey Questionnaire

QUESTIONNAIRE : TAX COMPLIANCE IN MALAWI

Questionnaire number _____

Interviewer _____

Interviewer: When you arrive at the interview location please introduce yourself using the following script. You must learn this introduction so that you can say it exactly as it is written below.

Good morning/afternoon. My name is _____. I am conducting a survey on behalf of Mr. Wazona Ligomeka. Mr. Ligomeka is a PhD student at the University of Sussex in the United Kingdom. As part of his studies, he is conducting a survey on the experiences and views of business people in Malawi on the Malawi tax system. As a business person/company operating in Malawi, we would like to request your participation in this survey. Your participation will assist Mr. Ligomeka in completing his PhD and also in making recommendations to the Malawi Government on how to improve the tax system. Participating businesses in the survey have been selected from Lilongwe and Blantyre and your business has been chosen at random. Your participation is voluntary and the information that you provide will NOT be shared with any institution including government agencies. The interview will take approximately 30 minutes and there is no penalty for refusing to participate. If you agree to participate, you can skip any question that you do not want to answer or terminate the interview at any time during the interview. I would like to know now if you have any questions and if you would like to proceed with the interview.

(Interviewer: Proceed with interview only when any concerns have been addressed and the respondent agrees to proceed. Before proceeding ask: “We can do this interview in English or Chichewa. Please, tell me which language you would like to use?”)

Begin interview

The questions that I will ask you will mainly relate to the 2016 (or 2015/16) tax year.

A. Respondent and businesses profile

Q1a. What is your position in the business?

Owner /Partner	1
Chief Executive Officer	2
Accounts personnel	3
Other: Specify.....	4

Q1b. How old are you?.....

Q1c. How long have you been working in this business?

.....years andmonths

Q1d. Are you involved in accounting or book-keeping in this business?

Yes	1
No	2

Q2a Is this business registered with the Malawi Revenue Authority (MRA)?

Yes	1
No (skip Q2b)	2
Don't know (Skip Q2b)	0

Q2b Which year did you register with the MRA and receive your Tax Payer Identification Number (TPIN).....

Q2c. Has this business filed (submitted) a tax return to the MRA in the last five years?

Yes	1
No	2
Don't know	0

Q3. Including yourself and family members, how many:

a- Full-time workers are employed by this business (*A worker is considered to be working full time if they work 40 hours a week or more, regardless of whether paid or not*)? _____

b- Part-time/ seasonal workers are employed by this business (*A worker is considered to be working part time if they work less than 40 hours a week, regardless of whether paid or not*)? _____

Q4. What is the current legal status of this business? (*Interviewer: Accept only one answer.*)

Sole Proprietorship	1
Partnership	2
Limited Liability Company	3
Closed Stock Company	4
Public Company	5
Other (specify): _____	99

(Interviewer: for question 5a, 5b and 5c, use table below for the responses)

Q5a. What would you say is the main activity of your business?

Q5b. What would you say is the second main activity of your business?

Q5c. What would you say is the third main activity of your business?

	Q5	Q6	Q7
Agriculture, forestry and fishing	1	1	1
Mining and quarrying	2	2	2
Manufacturing	3	3	3
Electricity, gas, steam and air-conditioning supply	4	4	4
Water supply, sewage, waste management and remediation activities	5	5	5
Construction	6	6	6
Wholesale and retail trade, repair of motor vehicles and motorcycles	7	7	7
Transportation and storage	8	8	8
Accommodation and food services	9	9	9
Information and communication	10	10	10
Financial and insurance services	11	11	11
Real estate activities	12	12	12
Professional scientific and technical activities	13	13	13
Administrative and support services	14	14	14
Education	15	15	15
Human health and social work	16	16	16
Arts and entertainment and recreation	17	17	17

B. General tax compliance and taxpayer experience

Q6. Who prepares the books of accounts and tax returns?

Self /owner (skip Q6b)	1
Part time accountant (skip Q6b)	2
Full time accountant (Skip Q6b)	3

None	0
------	---

Q6b What is the reason for not doing any type of book-keeping?

It is too expensive for our business	1
I do not know how to do it	2
Why should I? Nobody is forcing me	3
I do not want to keep books because of the risk of books falling into the tax authority's hands	4
Other (specify).....	5
N/A	0

Q7. I would now like to read out some statements about record-keeping in your business.

Using a scale of 1 to 5, where 1 is "Not at all" and 5 is "All the time," to what extent does your business . . .

		Not at all	Almost never	Sometimes	Most of the	All the time
A	Keep all physical receipts in an organised manner (such as sales slips, invoices receipts etc)	1	2	3	4	5
B	Practice manual book-keeping to record revenue and expenses in an organised manner	1	2	3	4	5
C	Record income and expenses in an organised manner using a computer	1	2	3	4	5

Q8a. How many times in the past 12 months has the business been visited by tax

officials (*Interviewer: Explain difference between Tax Authority officials and other officials that might visit a business such as Ministry of Finance Officers, Local Council, etc.*)? _____

Q8b. Out of all the times the business has been visited in the past 12 months, how many times was the business audited by tax officials (*Interviewer: clarify that you are not referring to informal checks conducted by MRA officers but actual audits*)? _____

Q8c. Has this business been fined by the Tax Authority

Yes	1
No	2
Don't know	0

Q8d. Apart from a fine, has this business suffered any other negative consequences after a visit by a tax official?

Yes	1
No	2

Q8e. Can you provide us an example of what the fine was in connection with, or the negative consequence that you suffered?

Q9a. Have you appealed against any of the fines or negative consequences suffered?

Yes	1
No (<i>skip Q10</i>)	2
N/A (<i>skip Q10</i>)	0

Q10a. On a scale of 1 to 5, where one is "Not satisfied at all" and 5 is "very satisfied" how satisfied were you with the MRA's appeal process?

Not satisfied at all	1
Not satisfied	2
Neither satisfied nor dissatisfied	3
Satisfied	4
Very satisfied	5
N/A	0

Q10b. What do you (or others in similar business) do if you (or they) are not satisfied with the MRA's ruling on your appeal? (if they have never been in this situation or they don't know anyone who has been in this situation, ask them what they think they would do if they were in this situation) **(do not prompt)**

Settle the case as proposed by MRA	1
There is nothing I can do, I just follow MRA ruling	2
Write to Ministry of Finance	3
Take the case to court	4
Other.....(specify)	5
Declined to answer	6

Q11a. Do you think business like yours are sometimes asked by tax officials to pay them money so that their cases are closed without using formal channels?

Yes	1
No <i>(skip Q11b)</i>	2
Don't know <i>(skip Q11b)</i>	0

Q11b. If so, how often?

Never	1
Rarely	2
Sometimes	3
Most of the time	4
All the time	5
Don't know	0

*(Interviewer: for Questions 12a, 12b and 12c use table below. **Do not prompt**)*

Q12a. What do you think are the main reasons businesses like yours give gifts or bribes to tax officers?

Q12b. How about the second most important reason?

Q12c. How about the third most important reason?

	Q12a	Q12b	Q12c
To prevent excessive tax payment	1	1	1
To avoid penalties	2	2	2
To reduce the amount of tax they should pay	3	3	3
To stop Tax Authority officers' harassment	4	4	4
To reduce time and money spent on various tax-compliance tasks	5	5	5
None of the above. The tax officer was nice and fair, and generally they are underpaid	6	6	6
Other (please specify).....	99	99	99
None	0	0	0

Q12d. How frequently do you think taxpayers evade taxes?

Very frequently	1
Frequently	2
Not often	3
Sometimes	4
Never	5
Don't know	0

Q12e. Please tell me what you think about people who do not pay taxes that they owe the MRA. Is that behaviour wrong, wrong but understandable or wrong and punishable?

Not wrong at all	1
Wrong but understandable	2
Wrong and punishable	3
Don't know	0

Q13. Please rate your agreement with the following statements using a scale of 1 to 5, where 1 is “Completely disagree” and 5 is “Completely agree.”

Question #		Completely disagree	Somewhat disagree	Neither agree nor disagree	Somewhat agree	Completely agree	Don't know or N/A
A	I am satisfied with the level of goods (e.g roads and bridges) and services (e.g education and security) that I receive from the government	1	2	3	4	5	0
B	There is a culture of tax evasion in Malawi	1	2	3	4	5	0
C	If the tax rates were lower, businesses would be more willing to pay all taxes due	1	2	3	4	5	0
D	The risk of getting caught evading tax is very low in Malawi	1	2	3	4	5	0
E	The potential consequences (e.g. fines and penalties, public naming, prosecution) of getting caught are serious enough to stop people from avoiding paying their taxes	1	2	3	4	5	0
F	The Malawi Revenue Authority is trustworthy in its operations	1	2	3	4	5	0
G	I have access to reliable information on the tax rates, laws, and regulations relevant to my business	1	2	3	4	5	0
H	Business would be willing to pay more tax if corruption was not prevalent	1	2	3	4	5	0
E	Most tax officials are not corrupt	1	2	3	4	5	0

14. Apart from taxes, what other fees and charges do you pay to government

Annual business licence	1
Market fee	2
TEVETA levy	3
Tourism levy	4
MBS	5
ODPP	6
Other (specify).....	7

C. More on VAT

I will now ask a few more questions about Value Added Tax (VAT).

Q15. *Are you registered for VAT?*

Yes (skip Q16)	1
No	2

Q16. What, if anything, would encourage you to register for VAT?

When I reach the VAT registration threshold	1
If I start dealing in exempt supplies	2
To deal with other VAT registered businesses	3
If tax compliance procedures were less complicated	4
If there were no frequent inspections by the MRA	5
If there was no harassment by MRA officers	6
Other (specify).....	99
NA	0

Q17. Do you use Electronic Fiscal Device (EFD) machines?

Yes (skip Q18)	1
No (skip Q19, Q20, Q21, Q22, Q23)	2

Q18. What is the reason for not using EFD Machines? (*Interviewer: do not prompt*)

Not registered for VAT	1
Cost of buying machine is too high	2
Electricity/internet interruptions	3
High maintenance cost	4
Difficult to use other options when it is not working	5
Require training workers	6
Limited maintenance service providers	7
Bigger tax burden	8
Other(specify).....	9
N/A	0

Q19. What are the advantages of using EFD machines?

Updated and easily available information	1
Easy to comply with tax requirements	2
Better sales and inventory control	3
Saves time	4
Improves business reputation	5
Able to get VAT credit (refund)	6
Less opportunity for theft by employees	8
Other (specify).....	9

Q20. Have you ever applied for a VAT refund in a relevant situation?

Never	1
sometimes	2
All the time	3
I don't know	0

Q21. If you have never applied or only apply sometimes, what is the typical reason for not applying for a VAT refund?

It was not worth it because the refund was too small	1
We would not get the refund anyway	2
The refund takes too long to come	3
It may induce a tax audit of the business	4
Complicated formalities for refund	5
Other (specify).....	0

Q22. How long does it take for you to get a VAT refund? (*Interviewer: do not prompt*)

Less than 3 months	1
Between 3 and 6 months	2
Between 6 and 12 months	3
Between 1 and 3 years	4
More than 3 years	5

Q23. If you compare businesses registered for VAT to businesses not registered for VAT, would you say that registered businesses are, overall (*Interviewer: Read out and circle appropriate response.*)

In a much worse position	1
In a worse position	2
In the same position	3
In a better position	4
In a much better position	5
N/A	0

D. Access to Information

Q24a. In the past, have you used any of the following services to contact MRA?

Phone	1
Sent an email enquiry	2
Sent a letter or fax	3

Visited in person	4
Other (specify).....	5
Never contacted the MRA (skip Q24b)	0

Q24b: What kind of information did you seek from the taxpayer services office of the MRA?

Q24c. In the past, has the MRA contacted you?

Yes	1
No (skip Q 24d)	2

Q24d. How did the MRA contact you?

Phone	1
Sent an email quarry	2
Sent a letter or fax	3
In person visit	4
Other (specify).....	5
N/A	0

Q25. Please rate your agreement with the following statements using a scale of 1 to 5, where 1 is “Completely disagree” and 5 is “Completely agree.”

Question		Completely disagree	Somewhat disagree	Neither agree nor disagree	Somewhat agree	Completely agree	Don't know
A	I am treated the by MRA staff with respect and dignity	1	2	3	4	5	0
B	The MRA staff are fair in thier dealings	1	2	3	4	5	0
C	The MRA staff are cooperative	1	2	3	4	5	0
D	I am satisfied with the time the MRA take to respond to my queries and problems	1	2	3	4	5	0
E	The MRA takes appropriate measures to ensure access to and availability of tax officers	1	2	3	4	5	0

(Interviewer: For Q26a, Q26b, Q26c, use table below)

Q26a. We would like to know a little bit about the channels of communication through which you find out about tax laws, regulations, and practical tax information and advice. What channels do you access information through?

Q26b. What would be the most important one?

Q26c. And what would be your most preferred channel through which you would like to access information about government laws and regulations?

	Q26a All channels	Q26b Most important	Q26c Preferred
Television	1	1	1
Radio	2	2	2
Newspapers and magazines	3	3	3
Internet	4	4	4
Friends and family	5	5	5
Talking to other people in my	6	6	6
Billboards	7	7	7
Trainings and seminars	8	8	8
Official Gazette	9	9	9
Our lawyer	10	10	10
Email	11	11	11
SMS	12	12	12
Telephone	13	13	13
Specialist tax consultants/ accountants/ bookkeepers	14	14	14
Taxpayer Services Office in the Tax Authority	15	15	15
Other (please specify):	16	16	16
None	0	0	0

E. Knowledge of taxpayer rights

Q27. Please rate your agreement with the following statements using a scale of 1 to 5, where 1 is “Completely disagree” and 5 is “Completely agree.”

question		Completely disagree	Somewhat disagree	Neither agree nor disagree	Somewhat agree	Completely agree	Don't know or N/A
A	I am aware of my rights against unlawful search and seizure by the tax authority	1	2	3	4	5	0
B	It is my right to claim tax refund (if any)	1	2	3	4	5	0
C	It is my right to know the basis for the assessment of my tax liability	1	2	3	4	5	0
D	I am aware that I have certain rights if I have a problem with the tax office	1	2	3	4	5	0

Q28. What was the approximate sales profit of this business in 2016?

Below MK100,000	1
Between MK100,000 and MK500,000	2
Between MK500,000 and MK1 million	3
Between MK1million and MK5 Million	4
Between MK5 million and 10 million	5
Between MK10million and MK50 million	6
Between MK50 million and MK200 million	7
Between Mk200 million and MK500 million	8
Between MK500 million and MK1 billion	9
Above MK1 billion	10
Made a loss	11

Q29. Apart from provisional tax, have you ever been asked by the MRA to make an advance payment on your taxes?

Yes	1
No (skip Q 30)	2

Q30. How often does the MRA make a request for non-provisional advance payment of taxes in a year? _____

Q31. Lastly, do you have any recommendations for how the Malawi tax system can be improved?

END

Thank you for your time.

(Interviewer: after the interview, complete these two additional questions)

Q32. Respondent gender:

Male	1
Female	2

Q33. District where the business is located...

Lilongwe	1
Blantyre	2

Appendix 4.11: Sampling method and data management for the survey in Malawi

1. Registered businesses (Formal)

To sample registered businesses, data from the tax administration, the Malawi Revenue Authority (MRA), was used. The MRA data shows that, in 2015, a total of 32,342 active⁵⁵ businesses were registered with the institution. Of the active registered businesses, 11,443 operated (have their headquarters) from Blantyre, while 12,601 businesses operated from Lilongwe, and 2,345 operated from Mzuzu. Thus, over 80% of all active businesses registered in Malawi in 2015 had their headquarters in the three districts of Lilongwe, Blantyre, and Mzuzu, with Lilongwe and Blantyre accounting for approximately 75% of the businesses. In total, there are 28 districts in Malawi. To classify business size for sampling purposes, the study partly followed the MRA classification of businesses⁵⁶ (large, medium, and small). In 2015, there were 434 large businesses in Blantyre, and 225 large businesses in Lilongwe. A total of 217 businesses participated in the survey in Blantyre, comprising 41 large businesses and 176 small and medium businesses. In Lilongwe, a total of 37 large businesses and 188 small and medium businesses participated. The MRA provided a telephone number, email address, and physical address for each business. Using an Excel function (RAND), business were randomly selected to participate in the survey. A dedicated individual then made calls to the sampled businesses to arrange the interviews. In other instances, I physically visited the business premises to arrange an interview date and time. Table 1 shows the distribution of the sample.

⁵⁵ Those that had filed a tax return in the past three years.

⁵⁶ The MRA groups businesses into large, medium and small. To qualify as a large taxpayer, one of the following conditions have to be met: a) have an annual turnover of at least MK750 million (£750,000); b) be paying cumulative taxes (excise tax, PAYE, corporate tax, VAT etc.) of over MK450 million (£450,000) or above per annum; c) be importing goods valued at MK750 million or above per annum; d) be operating in a financial or mining sector; e) be an operator of excise tax; f) be an associated or related company whose parent company is a large taxpayer. Medium taxpayers are businesses whose annual turnover is between MK150 million (£150,000) and MK750 million, while small taxpayers are those whose annual turnover is less than MK150 million. However, the study grouped medium and small business together after noting that although the MRA has a “medium” taxpayer classification, there is no division dedicated to this group, as is the case with large taxpayers, such that the medium and small business are treated the same.

Table 1: Sample size for formal businesses based on location and size

District	Blantyre	Lilongwe	Total
Number of businesses	11,443	12,601	24,044
<i>of which are large businesses</i>	434	225	659
Sample size	219	237	456
<i>of which are large business</i>	43	37	81

Source: The MRA, my own calculations

2. Unregistered businesses (informal)

In respect of informal businesses, the sampling technique adopted was a clustered, multi-stage random sampling method. In the two districts where the survey was conducted, the sample was taken from the urban areas. This done deliberately to ensure that both the registered and non-registered businesses came from within the same area, and thereby were likely to be subjected to a similar environment and hence have comparable experiences. The urban area subdivisions (or clusters) were listed in accordance with the city assembly town plans in each district. Some of the areas in Lilongwe include Area 1, 2, 3, 4, Kawale, etc. In Blantyre, the areas include Zingwangwa, Mkolokosa, Limbe, etc. The areas were listed and five areas in each district were chosen at random (using the Excel random function). In Lilongwe, the following areas were chosen: Chinsapo, Area 3, Kawale, City Centre, and Old Town. In Blantyre, the study was conducted in Zingwangwa, Limbe, Blantyre, Mkolokosa, and Angelogoveya. The sample size for each district was proportional to the population size. The estimated population size for Blantyre and Lilongwe as per the most recent available Malawi Integrated Household Survey (IHS3) 2010/11⁵⁷ conducted by the National Statistics Office (NSO) is 900,000 and 1,100,000, respectively. Representatives of a total of 267 informal businesses were interviewed; 123 unregistered businesses were sampled from Blantyre, and 144 were sampled from Lilongwe. The non-registered businesses included hawkers, motor vehicle

⁵⁷ It is noted that population figures from the Population and Household Survey conducted by NSO would have been more appropriate to use in this survey. However, the most recent Population and Housing Census was conducted in 2008, and hence would not provide a true picture of the current population size in these districts.

mechanics, tailors, carpenters, welders, small cross-border traders, bus/minibus owners, taxi and car hire operators. The interviews were restricted to non-registered businesses that had some kind of “permanent establishment” such as shop, house, or shack from which they conducted their businesses. This meant that street vendors, vegetable sellers, and other micro businesses were not included in the survey. Approximately 20 interviews were conducted in each area.

3. Data management

Once collected, survey data was encoded by using ‘Microsoft Excel’ spreadsheets prepared with data fields and codes. After entry, I worked with a research assistant who, using the questionnaire, read aloud the questions and responses while I confirmed the correctness of the responses on the spreadsheet. Changes were made as appropriate. Next, the data was analysed using STATA 15.1 to identify responses outside of expected ranges, including potential inconsistencies across variables. At each stage, copies of the data were maintained. The actual questionnaires with the responses are stored and will be available at least until the completion of the thesis.

Appendix 4.12: Descriptive statistics: My survey data

Variable	Mean	Std. Dev	Min	Max
Tax Morale	0.606	0.489	0	1
Deterrence	3.891	1.670	0	5
Fiscal	3.915	1.567	1	5
Tax knowledge	-0.00	1.00	-1.8	0.62
Corruption	4.2	1.29	1	5
Business size	1.083	0.333	1	3
Lilongwe	0.47	0.499	0	1
Registration status	0.645	0.479	0	1
Female	0.703	0.457	0	1
Retail	0.454	0.498	0	1
Manufacturing	0.046	0.211	0	1
Accommodation	0.078	0.268	0	1
Construction	0.025	0.158	0	1
Transport	0.038	0.192	0	1

Source: Business survey, My calculations

Appendix 4.13: Wald Test, equation 2 (my survey data)

Wald Chi2	677.10
Number of observations	703
Prob>chi2	0.00

Appendix 4.14: Hosmer-Lemeshow goodness of fit test: equation 2

Number of observations	703
Number of covariate patterns	619
Pearson Chi2 (603)	630.03
Prob > chi2	0.2159

Appendix 4.15: Ordered Logit Regression, Equation 2 (my survey data)

Variable	<i>Not wrong at all</i>	<i>Wrong but understandable</i>	<i>Wrong and punishable</i>
Deterrence	-0.04 (0.01)**	-0.02 (0.01)**	0.05 (0.02)**
Fiscal	-0.01 (0.01)	-0.01(0.00)	0.02 (0.01)
Tax Knowledge	0.08 (0.02)**	0.02 (0.01)**	-0.05 (0.02)**
Corruption	0.01 (0.01)*	0.00 (0.00)*	-0.1 (0.01)*
Business size	-0.08(0.05)**	-0.04 (0.03)**	0.12 (0.08)**
Lilongwe		-0.05	
	0.12 (0.03)***	(0.02)***	-0.17 (0.04)***
Registration			
status	-0.03 (0.04)	-0.01 (0.02)	0.04 (0.06)
Female	-0.03 (0.03)*	-0.01 (0.01)*	0.04 (0.05)*
Retail	0.01 (0.03)	0.00 (0.02)	-0.01 (0.05)
Manufacturing	-0.04 (0.07)	-0.02 (0.03)	0.07 (0.11)
Accommodation	-0.03 (0.06)	-0.01 (0.03)	0.05 (0.09)
Construction	0.13 (0.08)*	0.06 (0.04)*	-0.19 (0.12)*
Transport	0.05 (0.07)	0.02 (0.03)	-0.07 (0.11)

* Significant at .10 level

** Significant at .05 level

*** Significant at .01 level

Appendix 5.1: TADAT Performance Outcome Areas (POA), Indicators, and Dimensions

POA	Indicator	Dimension
POA 1: Integrity of the Registered Taxpayer Base	P1-1 Accurate and reliable taxpayer information	1) The adequacy of information held in respect of registered taxpayers and the extent to which the registration database supports effective interactions with taxpayers and tax intermediaries
		2) The accuracy of information held in the registration database
	P1-2 Knowledge of the potential taxpayer base	3) The extent of initiatives to detect businesses and individuals who are required to register but fail to do so
		4) The extent of intelligence gathering and research to identify compliance risks in respect of the main tax obligations
	P2-3 Identification, assessment, ranking, and quantification of compliance risks	5) The process used to assess, rank, and quantify taxpayer compliance risks
	P2-4 Mitigation of risks through a compliance improvement plan	6) The degree to which the tax administration mitigates assessed risks to the tax system through a compliance improvement plan
	P2-5 Monitoring and evaluation of compliance risk mitigation activities	7) The process used to monitor and evaluate the impact of compliance risk mitigation activities
	P2-6 Identification, assessment, and mitigation of institutional risks	8) The process used to identify, assess, and mitigate institutional risks
POA 2: Effective Risk Management		

POA	Indicator	Dimension
POA 3: Supporting Voluntary Compliance	P3-7 Scope, currency, and accessibility of information P3-8 Scope of initiatives to reduce taxpayer compliance costs	<p>9) The range of information available to taxpayers to explain, in clear terms, what their obligations and entitlements are in respect of each core tax</p> <p>10) The degree to which information is current in terms of the law and administrative policy</p> <p>11) The ease with which taxpayers obtain information from the tax administration</p> <p>12) The time taken to respond to taxpayer and intermediary requests for information</p>
		13) The extent of initiatives to reduce taxpayer compliance costs
	P3-9 Obtaining taxpayer feedback on products and services	14) The use and frequency of methods to obtain feedback from taxpayers on the standard of services provided
		15) The extent to which taxpayer input is taken into account in the design of administrative processes and products
POA 4: Timely Filing of Tax Declarations	P4-10 On-time filing rate	<p>16) The number of CIT declarations filed by the statutory due date as a percentage of the number of declarations expected from registered CIT taxpayers</p> <p>17) The number of PIT declarations filed by the statutory due date as a percentage of the number of declarations expected from registered PIT taxpayers</p> <p>18) The number of VAT declarations filed by the statutory due date as a percentage of the number of declarations expected from registered VAT taxpayers</p>

POA	Indicator	Dimension
		19) The number of PAYE withholding declarations filed by employers by the statutory due date as a percentage of the number of PAYE declarations expected from registered employers
	P4-11 Use of electronic filing facilities	20) The extent to which tax declarations are filed electronically
	P5-12 Use of electronic payment methods	21) The extent to which core taxes are paid electronically
	P5-13 Use of efficient collection systems	22) The extent to which withholding at source and advance payment systems are used
	P5-14 Timeliness of payments	23) The number of VAT payments made by the statutory due date as a percentage the total number of payments due 24) The value of VAT payments made by the statutory due date in percent of the total value of VAT payments due
POA 5: Timely Payment of taxes		25) The value of total core tax arrears at fiscal year-end as a percentage of total core tax revenue collections for the fiscal year 26) The value of collectible core tax arrears at fiscal year-end as a percentage of total core tax revenue collections for the fiscal year 27) The value of core tax arrears more than 12 months' old as a percentage of the value of all core tax arrears
	P5-15 Stock and flow of tax arrears	
POA 6: Accurate Reporting in Declarations	P6-16 Scope of verification actions taken to detect and deter inaccurate reporting	28) The nature and scope of the tax audit programme in place to detect and deter inaccurate reporting 29) The extent of large-scale automated crosschecking to

POA	Indicator	Dimension
		verify information reported in tax declarations
	P6-17 Extent of proactive initiatives to encourage accurate reporting	30) The nature and scope of proactive initiatives undertaken to encourage accurate reporting
	P6-18 Monitoring the extent of inaccurate reporting	31) The soundness of the method/s used by the tax administration to monitor the extent of inaccurate reporting
		32) The extent to which an appropriately graduated mechanism of administrative and judicial review is available to, and used by, taxpayers
		33) Whether the administrative review mechanism is independent of the audit process
	P7-19 Existence of an independent, workable, and graduated dispute resolution process	34) Whether information on the dispute process is published, and whether taxpayers are explicitly made aware of it
	P7-20 Time taken to resolve disputes	35) The time taken to complete administrative reviews
POA 7: Effective Tax Dispute Resolution	P7-21 Degree to which dispute outcomes are acted upon	36) The extent to which the tax administration responds to dispute outcomes
	P8-22 Contribution to government tax revenue forecast- ing process	37) The extent of tax administration input to government tax revenue forecasting and estimating
	P8-23 Adequacy of the tax revenue accounting system	38) Adequacy of the tax administration's tax revenue accounting system
POA 8: Efficient Revenue Management	P8-24 Adequacy of tax refund processing	39) Adequacy of the VAT refund system
		40) The time taken to pay (or offset) VAT refunds
POA 9: Accountability and Transparency	P9-25 Internal assurance mechanisms	41) Assurance provided by internal audit
		42) Staff integrity assurance mechanisms

POA	Indicator	Dimension
	P9-26 External oversight of the tax administration	43) The extent of independent external oversight of the tax administration's operations and financial performance 44) The investigation process for suspected wrongdoing and maladministration
	P9-27 Public perception of integrity	45) The mechanism for monitoring public confidence in the tax administration
	P9-28 Publication of activities, results, and plans	46) The extent to which the financial and operational performance of the tax administration is made public, and the timeliness of publication
		47) The extent to which the tax administration's future directions and plans are made public, and the timeliness of publication

Source: TADAT Field Guide (2015)

Appendix 5.2: Summary of TADAT assessment reports

Indicator	Jordan	Liberia	Georgia	Zambia	Armenia	Kyrgyz	Peru	Alagoas	Trinidad and Tobago	Guatemala	Burkina Faso	Malawi	Ukraine	Rio De Janeiro
P-1 Integrity of the registered taxpayer base														
P1-1 Accurate and reliable taxpayer information	C	D	D	D	D	D	B	C	D	D	C	D	C	C
P1-2 Knowledge of the potential taxpayer base	B	C	C	C	B	C	A	C	C	D	D	C	C	C
P2- Effective risk management														
P2-3 Identification, assessment, ranking, and quantification of compliance risks	D	D	C	C	C	C	A	D	C	D	D	D	C	D
P2-4 mitigation of risk through compliance improvement plan	D	C	C	C	D	C	A	D	D	C	D	D	D	D
P2-5. Monitoring and evaluation of compliance risk mitigation activities	D	D	C	C	D	C	B	D	D	D	D	A	C	D
P2-6. Identification, assessment, and mitigation of institutional risks	A	D	D	A	C	D	D	D	D	D	D	C	C	D
P-3 Supporting voluntary compliance														
P3-7. Scope, currency, and accessibility of information	C	D	B	C	A	B	A	C	D	B	D	C	B	B

Indicator	Jordan	Liberia	Georgia	Zambia	Armenia	Kyrgyz	Peru	Alagoas	Trinidad and Tobago	Guatemala	Burkina Faso	Malawi	Ukraine	Rio De Janeiro
P3-8. Scope of initiatives to reduce taxpayer compliance costs	B	D	B	B	B	C	A	B	D	D	D	D	B	C
P3-9. Obtaining taxpayer feedback on products and services	A	C	C	B	B	B	A	D	C	C	C	D	B	D
P4 Timely filing of tax declaration														
P4-10. On-time filing rate	B	D	C	D	C	B +	C	D	C	D	D	B+	D	
P4-11. Use of electronic filing facilities	D	D	A	B	D	A	A	D	A	D	B	C	A	
P5- Timely payment of taxes														
P5-12. Use of electronic payment methods	C	C	A	C	A	A	A	A	C	A	C	D	A	A
P5-13. Use of efficient collection systems	C	A	B	A	A	A	A	A	A	A	A	C	A	A
P5-14 Timelines of payments	C	D	B	B	D	A	C	D	D	C	D	D	A	C
P5-15. Stock and flow of tax arrears	D+	D	D +	D+	D+	B +	D	D	D	D+	D+	D	B	D
P6 accurate reporting in declaration														
P6-16. Scope of verification actions taken to detect and deter inaccurate reporting	C+	D	C	C	C	C	C+	D	D+	D+	D+	D	D+	D+

Indicator	Jordan	Liberia	Georgia	Zambia	Armenia	Kyrgyz	Peru	Alagoas	Trinidad and Tobago	Guatemala	Burkina Faso	Malawi	Ukraine	Rio De Janeiro
P6-17. Extent of proactive initiatives to encourage accurate reporting	D	D	B	D	C	D	B	B	D	D	D	D	B	B
P6-18. Monitoring the extent of inaccurate reporting	C	D	D	C	C	D	A	D	D	C	C	D	D	D
P7 effective tax dispute resolution														
P7-19. Existence of an independent, workable, and graduated dispute resolution process	B+	A	A	B	B	B +	B	A	A	B+	C+	C	A	A
P7-20. Time taken to resolve disputes	B	D	C	C	A	C	D	D	D	D	D	D	B	D
P7-21. Degree to which dispute outcomes are acted upon	D	C	C	B	C	B	A	C	B	C	C	D	A	C
P8- Effective Revenue Management														
P8-22. Contribution to government tax revenue forecasting process	B	B	C	B	C	C	A	C	C	C	C	D	B	A
P8-23. Adequacy of the tax revenue accounting system	A	D	C	D	C	C	C	D	D	C	D	C	C	C
		N /												
P8-24. Adequacy of tax refund processing	C	A	D	C	C	D	C+	D	D	D	D	C	C	D
P9- Accountability and transparency														
P9-25. Internal assurance mechanisms	B	D	D	B+	C	C	A	C+	D	B+	C	B	B	C+

Indicator	Jordan	Liberia	Georgia	Zambia	Armenia	Kyrgyz	Peru	Alagoas	Trinidad and Tobago	Guatemala	Burkina Faso	Malawi	Ukraine	Rio De Janeiro
			+			+								
P9-26. External oversight of the tax administration	C	D	C	C+	D+	C	B	B	C	C	D	D	B	A
P9-27. Public perception of integrity	A	D	C	C	B	C	A	D	D	D	C	A	C	D
P9-28. Publication of activities, results, and plan	A	D+	D+	B	C+	C+	A	C+	C	A	D	N/A	A	D