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Domestic Resource Mobilization
for Poverty Reduction in East Africa:

Rwanda Case Study

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Table of Contents

	Table of Contents	i
	List of abbreviations	ii
	Preface	iv
	Acknowledgements	Error! Bookmark not defined.
	Executive summary	v
1	Context – political economy and fiscal legacies	1
	1.1 Colonial legacies and the 1994 genocide	1
	1.2 Post-genocide economic recovery and development drive	2
	1.3 Development financing mix and challenges	3
	1.4 Political economy dynamics underpinning domestic resource mobilisation.....	5
	1.5 Fiscal governance drivers, results and trajectory.....	8
2	Trends in the tax system	10
	2.1 Changes in tax policies over the years	10
	2.2 Institutional changes.....	12
	2.3 Changes in administrative systems	15
	2.4 Fiscal decentralisation and taxation by local governments.....	16
	2.5 Reforms sequencing, implementation and results	18
3	Domestic revenue performance.....	22
	3.1 Domestic revenue performance trends.....	22
	3.2 Tax administration performance benchmarks.....	24
	3.3 Summary of overall trends.....	27
4	Challenges and issues.....	29
	4.1 Introduction.....	29
	4.2 Achieving a cost-effective strategy to widen the tax net	29
	4.3 Rationalising the collection of central and local government t taxes.....	29
	4.4 Developing and maintaining capacity for tax policy management	30
	4.5 Building and sustaining management capacity in RRA	30
	4.6 Putting a cap on tax incentives and exemptions.....	31
5	Lessons of experience.....	32
	5.1 Explicit and strong top political leadership support matters	32
	5.2 Developing and retaining effective capacity is a long-term undertaking.....	32
	5.3 Long term and flexible technical assistance support enables rapid and sustained capacity development.....	33
	Annex A: Key informants	34
	Annex B: Bibliography	35
	Annex C: Select indicators.....	40
	Annex D: Glossary of definitions of select terms	46

Annex A – List of key informants.....	A1
Annex B – Literature reviewed.....	B1
Annex C – Select indicators.....	C1

List of abbreviations

ACBF	Africa Capacity Building Foundation
AfDB	African Development Bank
APRM	African Peer Review Mechanism
ARA	Autonomous Revenue Authority
ASYCUDA	Automated System for Customs Data
BMS	Block Management System
BNR	National Bank of Rwanda
CAGR	Compounded Annual Growth Rate
CED	Customs and Excise Department
CED	Customs and Excise Department
CET	Common External Tariff
CIT	Corporate Income Tax
CITPROD	Corporate Income Tax Revenue Productivity
COMESA	Common Market for East and Southern Africa
CPAF	Common Performance Assessment Framework
CPI	Consumer Price Index
CTL	Commercial Transaction Levy
DAD	Development Assistance Database
DFID	Department for International Development
DPAF	Development Performance Assessment Framework
DRC	Democratic Republic of Congo
DRM	Domestic Resource Mobilization
DTD	Domestic Tax Department
EAC	East African Community
EASSy	Eastern Africa Submarine Cable System
eFiling	Electronic Filing
FDI	Foreign Direct Investment
FTSE	Financial Time Stock Exchange
GBS	General Budget Support
GDP	Gross Domestic Product
GoR	Government of Rwanda
GP	General Public
HIPC	Heavily Indebted Poor Countries
ICT	Information and Communication Technology
ID	Identification
IDO	International Development Organisation

IMF	International Monetary Fund
ISO	International Standards Organisation
ITU	International Telecommunications Union
LTO	Large Taxpayers' Office
M&E	Monitoring and Evaluation
MDG	Millennium Development Goal
MDRI	Multilateral Debt Reduction Initiative
MINECOFIN	Ministry of Finance and Economic Planning
MTEF	Medium Term Expenditure Framework
NDP	National Development Plan
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development
PIT	Personal Income Tax
PITPROD	Personal Income Tax Revenue Productivity
PS	Permanent Secretary
PSF	Private Sector Federation
PwC	PricewaterhouseCoopers
RADDEX	Revenue Authority Digital Data Exchange
RDB	Rwanda Development Board
RPD	Revenue Protection Department
RPF	Rwandan Patriotic Front
RRA	Rwanda Revenue Authority
Rwf	Rwanda Franc
SAP	Structural Adjustment Programme
SIGTAS	The Standardized Integrated Government Tax Administration Systems
SME	Small and Medium Enterprise
SMTO	Small and Medium Taxpayers' Office
SSA	Sub-Saharan Africa
TAXSTAFF	Ratio of Tax Staff per Population
TIN	Taxpayer Identification Number
UK	United Kingdom of Great Britain and Northern Ireland
UNCTAD	United Nations Conference on Trade and Development
VAT	Value Added Tax
VATGCR	VAT Gross Compliance Ratio
WTO	World Trade Organisation

Preface

The African Development Bank (AfDB) has partnered with the African Tax Administration Forum (ATAF) and the East African Secretariat on a project aimed at sharing lessons of experience from Domestic Resource Mobilization (DRM) through case studies for the East African Community partner states (EAC), South Africa and South Korea. For the purposes of this work, DRM is defined to include only tax policy and administration and excludes other possible components of DRM such as domestic financial markets.

The overall objective of this project is to make recommendations, for the participating countries of the EAC, on the priority reforms and ways to sequence and implement them, in order to significantly enhance DRM. As such, the primary beneficiaries of the project are both the Ministries of Finance and the Revenue Administrations of the EAC.

This paper seeks to respond to the following question: *What key factors have contributed to or inhibited DRM in Rwanda?* This case study has been prepared following an extensive review of available literature, interviews with key informants in Rwanda, the collection of quantitative data, and the analysis of both primary and secondary data. Its development has also been informed by a methodological framework designed by the AfDB. The core principle of the methodological framework is to analyse tax performance as a result of tax systems, reforms and the political economy. The study adopts an explanatory case study approach to match patterns from our analysis of the literature and key informant interviews.

The achievements and lessons of experience contained in this and other country papers will provide primary inputs for a policy note. The policy note will seek to address the following questions: *What are the priority reforms for EAC countries and the EAC? How should reforms be sequenced and implemented?*

Chapter 1 of this case study paper begins with an examination of Rwanda's political economy and fiscal legacies. Thereafter, Chapters 2 and 3 explain and analyse the trends in the tax system and their impact on domestic revenue performance respectively. The final chapters highlight the challenges and issues currently faced by government (Chapter 4), and lessons of experience for consideration by the EAC member states (Chapter 5).

Acknowledgements

The Rwanda Case Study was prepared under the overall supervision of Mrs. Diarietou Gaye (Regional Director, Department East A, OREA) and Catherine Baumont-Keita (Lead Economist, OREA). Core team members were Edward Sennoga (Macro Economist, UGFO and Task Manager, Richard Walker (Country Economist, KEFO) and Christian Lim (Private Sector Specialist, OSGE). The external consultants were led by Elizabeth Kariuki and Kithingi Kiragu (PricewaterhouseCoopers).

Mr. Aloysius Ordu (Vice President, Country and Regional Programs), Mr. Steve Kayizzi-Mugerwa (Director, Operational Resources and Policies), and Ms. Radhika Bharat (Investment Officer) initiated the project and were involved in the early design of the study.

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There is not enough space here to name each and every one of those who have contributed immensely to the successful completion of this case study; however, Annex A lists some of the key contributors to this report. In addition, we seek the indulgence of all the contributors in accepting this blanket acknowledgement and appreciation of their efforts and contribution. We are indeed very thankful.

Executive summary

1. Context-Political economy and fiscal legacies

As expounded in an Africa Capacity Building Foundation (2003) sponsored review, at independence, in 1962, Rwanda inherited weak human, institutional and societal capacity to cope with the challenges of development management. The economic crisis of the mid-1980s, followed by genocide and war in the 1990s served to further undermine the limited progress that had been made (Rugumamu and Gbla, 2003). The 1994 genocide did not only result in the unprecedented loss of human lives and disruption of the social fabric, but also the virtual destruction of the already weak economy and socio-economic institutions. Real GDP in 1996 remained at only 72% of its 1990 level. Five years later, over 60% of households lived below the poverty line, compared to about 40% in 1985.

The post-genocide government committed to rapid economic recovery; with prudent fiscal and monetary policies, liberalisation of the economy, and institutional capacity building. The economy rapidly rebounded - growing by about 80% between 1994 and 1998. After a temporary set-back in 2003 (when the real GDP growth rate fell to 2.9%), high rates of growth have been recorded since 2004. Since 2005, Rwanda's annual real GDP growth has exceeded 9% every year (except in 2007 when it dropped to 7.7%). In 2008, the economy experienced its first double-digit real growth rate in over five years, at 11.6%.

Three political economy factors underpin the Government of Rwanda's (GoR's) zeal to maximise DRM. First, Rwanda's defense budget, which cannot be supported by Official Development Assistance (ODA) will remain comparatively high because the country remains in a defensive "war" standing since the genocide. Second, while the ODA contribution to the budget is substantial, there have been intermittent threats, and two incidences of actual withdrawal or cut-back of aid by European countries because of Rwanda's engagements in the conflicts in the DRC. Rwanda's involvement in these conflicts has been justified by the need to fend off the continued insecurity posed by former genocide perpetrators. Third, substantial and sustained increases in development financing are needed to achieve the ambitious goals of Rwanda's Vision 2020.

2. Tax reforms: Sequencing, implementation and results

The history of tax reforms in Rwanda is comparatively short. From a sequential perspective, six distinct albeit short phases of reforms can be identified:

- First - *institutional reforms and capacity building*, which correspond to the period beginning with the establishment of Rwanda Revenue Authority (RRA) in 1997 and the subsequent three years;
- Second - *widening the tax base*. The hallmark development in this phase was introduction of the VAT in 2001;
- Third – *streamlining the tax regime and administration*. This was effected by widening the mandate of RRA to cover non-tax revenues, and rationalisation of income tax rates, in 2003 and 2005 respectively;
- Fourth – *aligning the tax system to development policy priorities*, through the introduction of a new income tax law, investment and export promotion legislation and tax code, in 2005;
- Fifth – *strengthening the compliance enforcement regime* by enacting law number 25 of 2005 to cater for, among other measures, tax audits, appeals and penalties for evasion; and introducing penalties for taxpayers who fail to comply with provisions for consumption taxes (in 2006);
- Sixth – *harmonising Rwanda's tax regime and administration with that of the EAC* (in 2009 and 2010).

In a nutshell, the Rwanda tax system has undergone several reforms since 2001. Nonetheless, the reforms have been systematic and sequenced. More significantly, through the reforms, Rwanda has made major strides in efficiency improvements and modernisation of the tax administration system. Highlights of these results include:

- The ongoing major initiative to widen the tax base by establishing the Small and Medium Taxpayers Office and embarking on implementation of the block management system;
- Timely auditing of refund claims by the RRA. Also, unlike some EAC countries, in Rwanda, RRA has the full mandate to administer the refunds;

- Compliance levels have significantly improved with as many as 97% compliant large taxpayers (who contribute approximately 75% of total domestic taxes);
- Over 90% of revenue is collected by banks;
- In 2010, Rwanda and Uganda launched a 24/7 one-stop border service at Gatuna;
- RRA has contributed to the dramatic improvement in Rwanda's 2010 "Doing Business" ranking, by spearheading the introduction a number of tax legislation reforms;
- RRA became International Standards Organisation 9001 certified in 2009.

Although Rwanda faces the same fiscal decentralisation challenges that are encountered by other countries, the social context for decentralisation reform in the country provides a degree of vibrancy and innovation in its reform efforts that sets it apart from other countries in the region. The goal of the Government's Fiscal and Financial Decentralisation Policy (2006) is not only to pursue efficiency in the provision of services at the local level, but also sustainable development, economic growth and the reduction of poverty. The *Law on the Organization and Functioning of the District* (2006) assigns local governments in Rwanda a series of tax and non-tax revenue sources. However, while local governments have a degree of discretion in determining tax rates, they are not permitted to create new taxes or define the tax base for local revenue sources. This ensures coordinated implementation of tax policy and minimizes distortion/ disruption of economic activity.

3. Domestic revenue performance

Rwanda's total domestic revenue as a percentage of GDP rose from 8.4% in 1993, to 14.2% in 2008. In 1994, however, total domestic resources as a percentage of GDP fell to a dismal 3.6% on account of the genocide. Tax growth has ranged between 0.25% and 0.3% of GDP every year from 1997 (IMF 2009c).

Over the years, taxes on goods and services have formed the largest proportion of total domestic revenues – at about 48% of the total tax revenue. Since 2001, and with the exception of 2004, the contribution to total taxes from direct taxes has been on a steady rise – in 2008 the share of direct taxes peaked at 37.5%. The share of taxes on international trade to total tax revenues has steadily decreased from a high of 41% in 1995, to just over 10% in recent years. This reduction is explained by an

initial reduction in import duty rates – “with the maximum rate declining from 60% to 40%” (IMF, 2000). Furthermore, “Rwanda’s weighted average tariff rate was 11.3% in 2008”¹. In the short to medium term, significant rises in real tax revenue growth are more likely to come from measures to raise and sustain compliance by the existing taxpayers and improvements in tax administration efficiency.

4. Challenges and issues

In the short to medium term, significant rises in real tax revenue growth are more likely to come from measures to raise and sustain compliance by existing taxpayers and improve administration efficiency. In this regard, the main challenges and issues to be addressed include the following.

- *Achieving a cost-effective strategy to widen the tax net:* Widening the tax net entails capturing small and micro enterprises that are largely in the informal sector, and getting them to pay taxes. This can be associated with high administrative costs in the short term;
- *Rationalising the collection of central and local government taxes:* In line with GoR’s decentralisation policy, property and rental income taxes are collected by local government authorities. However, experiences from countries such as Kenya and South Africa suggest that RRA would be more effective than local governments in collecting property taxes and taxes on rental income, and in some countries such as Tanzania, the revenue authority collects property taxes on behalf of local government authorities;
- *Developing and maintaining capacity for tax policy management:* The tax policy function is much weaker relative to tax administration. This is to a significant extent, explained by the fact that the organisation and staff in tax policy remain in a bureaucratic and poor incentive environment;
- *Building and sustaining management capacity in RRA:* especially technical and professional skills, will remain a major challenge to RRA for well into the long run. RRA’s capacity to develop and retain the required human resources remains contingent on its ability to offer competitive remuneration packages;
- *Putting a cap on tax incentives and exemptions:* In the pursuit of the policy goal of making Rwanda a preferred foreign investment destination, and to attract particular investors to establish in Africa, GoR has legislated tax

¹ <http://www.heritage.org/index/Country/Rwanda> [Accessed 18 April 2010].

incentives and granted tax exemptions to some businesses. Yet, there is a body of knowledge that suggests that these incentives can be counter-productive.

5. Lessons of experience

In confronting the challenges of design and implementation, three major lessons of experience, are worth sharing as follows:

- *Explicit and strong support of top political leaders matters:* There is a shared view that strong support from the top political leadership of the country, especially the President, and successive Ministers of Finance was the most crucial driver for change;
- *Developing effective capacity is a long-term undertaking:* In spite of decade-long consistent and determined efforts of RRA's top management to rapidly achieve required capacity, considerable capacity gaps are still prevalent. The IMF (2009b) suggests the priority gaps to be closed are strengthening audit and enforcement capacity, as well as management support functions such as ICT systems management, human resource management and financial management;
- *Long term and flexible technical assistance support enables rapid and sustained capacity development:* DFID has provided substantial support to the RRA since 1998. Although DFID's support has significantly been reduced in recent years, and it is now being phased out, there is no doubt that the long term orientation, predictability and flexibility of this support has enabled RRA to rapidly and sustainably improve its capacity.

1 Context – political economy and fiscal legacies

1.1 Colonial legacies and the 1994 genocide

Rwanda has had uniquely chequered colonial as well as post-colonial legacies. It was part of the German East African colony from 1890 until it was occupied by Belgium in 1916, which in 1923 was given a League of Nations mandate to govern Ruanda-Urundi². Rwanda became independent in 1962. However, French neo-colonial influence was not only more pronounced than Belgian in the immediate post-independence period but preeminent, until the 1994 genocide. More significantly, the colonial powers did little to develop the economy and institutions of the country, and yet accentuated the ethnic divide and promoted the tensions that created the conditions for the genocide (Mamdani, 2001).

As expounded in a 2003 Africa Capacity Building Foundation (ACBF) sponsored review, Rwanda inherited weak human, institutional and societal capacity to cope with the challenges of development management. It faced severe capacity constraints in literally all sectors, characterised by a shortage of skilled staff, under-utilisation of the available resources, weak institutional environments, inadequate incentive structures, as well as a lack of capacity retention strategies. Despite various efforts to promote the social sector, neither institutional nor human capacity grew fast enough to keep pace with the requirements of rapidly changing social-economic circumstances. The advent of the economic crisis of the mid-1980s, as well as war and genocide, undermined the limited progress that had been made (Rugumamu and Gbla, 2003).

The 1994 genocide did not only result in the unprecedented loss of human lives and disruption of the social fabric, but also, the virtual destruction of the already low economy and weak socio-economic institutions. Per capita GDP dropped to less than US\$200, and poverty levels worsened. Real GDP in 1996 remained at only 72% of its 1990 level. Five years later, over 60% of households lived below the poverty line, compared to about 40% in 1985. In economic terms, Rwanda saw its GDP fall by 50% in 1994, and the rate of inflation increase by 64%. Rwanda remains one of the poorest countries in the world, with a per capita GDP of under US\$500 in 2008.

² <http://news.bbc.co.uk/1/hi/world/africa/1070329.stm> [Accessed 4 June 2010].

1.2 Post-genocide economic recovery and development drive

The post-genocide government made a commitment to ensure rapid economic recovery, with prudent fiscal and monetary policies, liberalisation of the economy, and institutional capacity building. Backed by substantial external resources, the new government successfully delivered on its commitment. The economy rapidly rebounded, growing by 7.0% between 1994 and 1997, and 8.9% in 1998, fuelled by large inflows of external resources for relief and reconstruction, and supported by the stabilisation and liberalisation of the economy. Inflation reduced from 17% at the end of 1997, to an average of 6.8% in 1998.

After a temporary set-back in 2003 when the real GDP growth rate fell to 2.9% (IMF, 2004), high rates of growth have been recorded since 2004³. Yet, as observed by Rugumamu and Gbla (2003), the pre-1994 structural economic problems still persist and will take decades to resolve. Weakness in the Rwandan economy stems from a lack of natural resources, poorly developed human resources, a high population density, antiquated agricultural practices, environmental degradation and difficulties in economic management. Both the private and public sectors remain small and neither has been developed to meet the population's needs.

As already stated, in recent years, except in 2003, Rwanda has had comparatively high rates of economic growth. In 2008, however, the economy experienced its first double-digit real growth rate in over five years, at 11.6%. The strongest contribution came from export crops which grew at 29%. The industry and service sectors also delivered high growth rates of 15% each⁴.

On the whole, there has been an acceptable degree of macro-economic and fiscal stability since the late 1990s. Over the same period, for example, an overall fiscal surplus was recorded. This steady progress was interrupted in 2007 by firstly steep rises in the prices of imported petroleum products and other commodities which impacted negatively on budget execution. Secondly, there was an earthquake. Disaster and the reconstruction needs afterwards together with the policy to provide additional emergency as well as investment resources to improve food security increased expenditures significantly (see **Table 1.1**).

According to GoR's Budget Framework Paper for 2009 to 2012, by early 2009, there were signs that the global financial crisis was beginning to have an impact on Rwanda. Whilst inflation had begun to decline, due to falling world prices and domestic policies, there were downsides. The balance of payments projections for

³ In 2004, Rwanda recorded an economic growth rate of 4% (IMF, 2005).

⁴ <http://statistics.gov.rw/images/PDF/GDP%20FINAL%20REPORT.pdf> [Accessed 4 June 2010].

2009 (as a result of performance seen in early 2009) were not good. The fiscal deficit was set to rise to 1.7% of GDP before shrinking “to 0.5% in 2011/12” (GoR, 2009).

Table 1.1: Fiscal performance indicators (in percentage of GDP)

	2006	2007	2008
Revenues and Grants	23.7	23.8	27.8
Total Revenues	13.1	13.8	14.0
Tax Revenues	12.2	13.0	12.9
Grants	10.9	9.9	13.8
Expenditure and Net Lending	23.9	25.4	28.4
Current Expenditure	15.8	17.1	17.6
Capital Expenditure	7.1	8.8	11.1
Overall Deficit including grants	-0.2	-1.7	-0.6
Overall Deficit excluding grants	-10.9	-11.6	-14.4

Source: GoR (2009)

1.3 Development financing mix and challenges

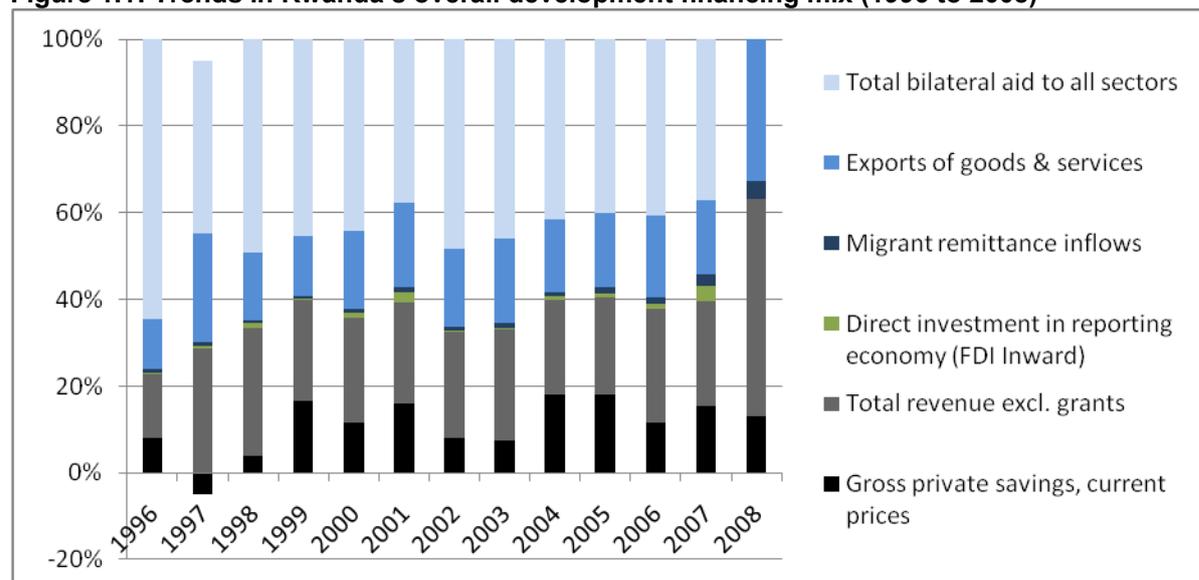
Figure 1.1 shows trends in the overall development financing mix for Rwanda between 1996 and 2008. The largest source of financing during that period was Official Development Assistance (ODA). Following the genocide, Rwanda received large injections of external aid. As would be expected, much of this aid was for emergency food aid and other humanitarian needs. However, by about 1998, humanitarian aid was considerably reduced, and external resources were increasingly focused on economic development and building of institutions. Between 2000 and 2008, total ODA to Rwanda averaged around US\$460 million p.a.

Still, as noted in a 2005 review of Rwanda’s international relations, donor support remained largely uncoordinated (Killick 2005). Furthermore, when for example, compared to several other countries in Eastern Africa (Ethiopia, Mozambique, Tanzania, and Uganda), Rwanda’s external assistance remained transitional and its effectiveness constrained by institutional weaknesses. In 2006, in consultation with its development partners, GoR promulgated “Rwanda’s Aid Policy - Implementing Change to Maximise the Impact of Aid on Poverty Reduction and Economic Growth”. In that year, Rwanda received US\$586 million in ODA, representing about 21% of GDP.

From, 2006 onwards, Rwanda has benefited from debt relief under the Heavily Indebted Poor Countries (HIPC) initiative. Since then, use of debt in budget financing is on the whole confined to project loans on concessional terms, and the sale of treasury bills (domestic borrowing). In the backdrop of a combination of debt

relief and more predictable commitments by development partners, in 2007, Rwanda raised its total annual budget by 33%, to Rwf 528 million. Also, the budget for FY2009/10 was 20% above that for 2008/09. The reduction in external debt and the overall increase in available resources have enabled GoR to allocate a higher proportion of its development resources to pro-poor expenditures.

Figure 1.1: Trends in Rwanda's overall development financing mix (1996 to 2008)⁵



Source: Africa Economic Outlook (AEO) 2010 data

Domestic revenues and exports of goods and services constitute Rwanda's second and third largest sources of development financing respectively. Revenues from Rwanda's exports grew at an average rate of 11.3% from 2002 to 2008, "with the share of traditional exports, coffee and tea, declining to about 50%" (AfDB, 2008). Coffee and tea are two export commodities, which over the years have been exposed to variations in global commodity prices. Therefore, this is likely to be the case in future. At the moment, World prices for both commodities are high. In this context, as well as in pursuit of more rapid and broad-based economic growth, GoR has an array of initiatives for the diversification of its export base to cover areas such as tourism, mining and business process outsourcing. These initiatives will again serve to consolidate Rwanda's benefits from globalisation.

GoR is aggressively promoting Rwanda as a foreign direct investment (FDI) destination. As a result, for the post-Monterrey period (2002-2008), FDI grew at an

⁵ Data on ODA for 2008 is not available.

average rate of 112%. In a 2009 interview, President Paul Kagame is quoted to have stated that “investment is the key to developing our industrial and service sectors” (Kitaoka, 2009). This initiative is bearing fruit. In 2009, Rwanda attracted a record US\$600 million in FDI, surpassing Rwanda Development Board’s (RDB’s) target of US\$200 million (Oluoch-Ojiwah, 2009). This was also the year when Rwanda was ranked the best performer in the EAC in the World Bank’s Doing Business ranking – in particular it was ranked: 67th out of 183 countries in terms of ease of doing business; and as the top reformer globally. Significant efforts have gone into improving Rwanda’s regulatory and legislative environment. “For example, the passing of the Company Law has reduced [the time taken to start a] business from 14 days to 2 days” (Ruburika, 2009).

1.4 Political economy dynamics underpinning domestic resource mobilisation

The synopsis of the political economy legacies that have impacted DRM, as presented in the subsections below, is based on Brautigam’s (2008) analytical framework⁶, which consists of the following five facets: (1) level of economic development and economic structure; (2) societal factors: culture, values, trust and ‘tax morale’; (3) war and taxes: bureaucratic modernisation as a response to threat; (4) political institutions and tax systems; and (5) taxation and the fiscal contract.

1.4.1 High rates of economic growth in recent years but poverty levels remain high

Since 2005, Rwanda’s annual GDP growth has exceeded 9% every year (except in 2007 when it dropped to 7.7%). In 2009 GDP growth was expected to slow down to 6%. In the previous decade, the average annual growth rate was more than 5% (GoR, 2009).

Despite the impressive rate of economic growth since late the 1990s, the vast majority of Rwandans remain poor, and the economy is predominantly agriculture-based. Real GDP per capita is below US\$500. However, the structure of the economy is changing (see **Annex C: Table C14**). In other words, there are good signs of progress in the modernisation of the economy. The manufacturing and construction sectors’ contribution to real GDP growth is steadily rising, while that of agriculture is shrinking.

⁶ Brautigam’s framework is adopted because compared to others that were examined; it is judged to be more comprehensive and elegant. However, like most others, its historical perspective derives too much from emergence of the modern European state to be linearly applied in states that are legacies of colonial rule, such as Rwanda.

In the medium-term, GoR projects an annual growth rate of at least 8%, and great strides in modernisation of the economy, especially through intensive exploitation of ICT. Still, the economy will remain largely agricultural based in the foreseeable future. Although agriculture contributes only about 35% of GDP, it provides more than 90% of employment. The large rural (agricultural) informal sector constitutes a vast reservoir of potential taxpayers but one that is not readily accessible. Therefore, for the foreseeable future, Rwanda will rely on a comparatively narrow tax base.

1.4.2 Seeds of trust in government as a basis for a ‘tax morale’ are now evolving⁷

The 1994 genocide was a culmination of decades of intense ethnic distrust, tensions and hatred among sections of Rwanda’s population – which also contributed to a non-compliant tax culture. Mamdani (2001) and Gourevitch (1998) argue that, while colonialists had a major influence on these developments, the traditional (pre-colonial) culture had feudal strains that also contributed to the distrust and conflict just before independence in 1959, and in the next three and a half decades. It has also been suggested by Rugumamu and Gbla (2003) that Rwanda’s past monarchical and authoritarian regimes promoted a social culture of fear, sectarian hatred and other negative social values that are inimical to tax morale.

An independent review by the AfDB/OECD (2007) suggests that the new regime:

“Has chosen the path of reconciliation, unity, social cohesion and development as national priorities. In October 2008, steps were taken to strengthen all Rwandan political parties to enable them to engage in interparty dialogue and improve their capacity to organise, communicate, and reach out to constituents at the grassroots level. ... the ruling RPF won 78.6% of the vote, with the Social Democratic Party and Liberal Party sharing the remainder of the seats. The elections also resulted in women taking 56% of all parliamentary seats, making Rwanda’s Chamber of Deputies the first in the world with a female majority. The elections were endorsed by international observers, and will enable the incumbent president to pursue other pressing social development matters if he is re-elected in 2010”.

In addition, “a study commissioned by the Regional Centre on Small Arms has shown 96% and 94% respectively of Civil Society and the General Public declare

⁷ In a society where “tax morale” is high, there are low levels of tax evasion and avoidance. It is only in a social culture where citizens generally appreciate their responsibility for sustaining state services and where they have a trust in their state institutions and leaders that a “tax morale” evolves.

high level of trust and satisfaction about security organs and their effectiveness in providing security to citizens” (Kagire, 2009). It is this kind of citizen experience which eventually builds trust and confidence in a government, and thereby enhances its legitimacy, and stimulates tax morale among the citizens. However, as recently as in 2007, the Rwanda Revenue Authority (RRA) Commissioner General is cited in a local daily to have observed that most of the potential taxpayers evade paying taxes (The New Times, 2007).

1.4.3 Continuing threat of war and reduced external aid impel bureaucratic modernisation for growth in DRM

Since the genocide, Rwanda has remained in a “war” standing because large numbers of those responsible for the genocide killings fled into the jungles of neighbouring Democratic Republic of the Congo (DRC), and the threat of their reprisals remain real. At the same time, while external aid contributions to the budget are substantial, Rwanda has been intermittently under the threat of withdrawal of aid by European countries because of its engagements in the conflicts in the DRC that have to do with fending off the external threat. Also, the IMF (2009a) underscores the need for GoR to formulate “an exit strategy from aid dependence over the long-term”. These factors underpin the GoR’s zeal to maximise DRM, especially by ensuring the capacity, efficiency and effectiveness of the RRA.

1.4.4 Top political leadership keenly follows developments in the tax system

On assuming power, the RPF regime immediately realized that major institutional reforms, beginning with the establishment of an autonomous revenue collection agency, RRA in 1997, were crucial to strengthening and developing its fiscal framework. In recent years, it is observed that the ‘National Taxpayers Day’ is one of the two most important national events that the President of Rwanda must personally grace. The other is the annual leadership retreat. According to Torero et al (2006):

“From the outset the RRA has been able to count on the personal support of the President, who has gone on to play a major part in the campaign to change public attitudes towards paying taxes and related challenges such as corruption. The President has underlined the importance of the RRA as enabling the country to finance poverty reduction expenditure, and to reduce its dependence on outside assistance. ... The President has also publicly stressed the importance of creating an enabling environment for investment, which has stimulated the RRA in making considerable effort at outreach to the private sector”.

1.4.5 Government leaders are promoting the principle of a “fiscal contract”⁸

According to Torero et al (2006), the principle of the ‘fiscal contract’ is well upheld by Government leaders in Rwanda, who advocate for RRA to be seen to “contributing to developing a culture of participation and citizenship as part of a wider process of establishing the norms and practices of democratic governance, and of bringing government closer to the people”. In this regard, the leaders are proactively seeking to persuade the public to buy into the latter’s motto, ‘taxes for growth and development’. This is the beginning of a “fiscal contract” between a government and its citizens.

1.5 Fiscal governance drivers, results and trajectory

The authors suggest that there are four key fiscal governance drivers for Rwanda in the medium to long-term. First, GoR has an ambitious vision and goals to transform the nation to a middle income country, free of poverty by 2020. To this end, besides achieving the MDGs, there are grand plans to modernise the physical economic structure and institutions, and make Rwanda the ICT hub of East and Central Africa. According to the IMF (2009b), although Rwanda has made significant progress in achieving universal primary education, gender equality and women’s empowerment, and reducing child mortality, it may not meet some of the MDG targets. Still, Rwanda’s leadership does not waiver on its commitment to achieving the MDGs. It can therefore be expected to sustain high levels of public expenditure allocations to social services. GoR is also geared to making high investments in infrastructure development. In the circumstances, GoR looks to RRA’s improved tax effort to close any fiscal shortfalls.

The second driver is international development organisations’ influence given the comparatively high level of ODA in the budget. Total grants are shown at Rwf 285.2 billion (about US\$ 485 million) in 2008/09 and rising to Rwf 405.7 billion (about US\$ 690 million) in 2011/12 (subject to additional donor commitments). Fiscal expansion has allowed increases in priority spending especially in the areas of: infrastructure; and the social sectors particularly education, health as well as social protection. It is expected that this scaling-up will continue despite the international financial crisis. However, support from international development organisations’ (IDOs’) is problematic in particular due to the unpredictability forward commitments. For instance, the fiscal projections in the budget framework paper for 2009/10 to

⁸ Fiscal contract has its genesis in agreements between European monarchies and the propertied class and merchants that the latter would contribute to state coffers especially to fund war in return for specific benefits. In modern times a fiscal contract would be characterised by government pledges of specific socio-economic benefits to justify taxation. This is a more realistic proposition in a democratic dispensation.

2011/12 show a gap of Rwf 168.5 billion (US\$294.5 million) in grants over the medium term (GoR, 2009).

The third fiscal governance driver which relates to the second driver, emanates from the conditionalities imposed on Rwanda by IDOs to continue to access debt relief under HIPC. Specifically, Rwanda's access to non-concessional borrowing is restricted. Moreover, given the macro-economic and fiscal regimes that GoR has agreed with the IMF, which serve to confirm compliance with HIPC conditionalities, the fiscal space is quite restricted. This therefore implies that fiscal expansion can only be achieved with increased DRM.

Finally, although Rwanda's accession to the EAC is expected to yield considerable economic benefits in the long-term, and even facilitate the timely achievement of the nation's Vision 2020, this membership imposes fiscal restraints. The member states of the EAC, are expected to observe monetary and fiscal convergence. Furthermore, in the medium-term, Rwanda will experience a reduction in customs revenue arising from the lower external tariffs. These have been estimated at Rwf 23.3 billion (US\$41.2 million) for the three year period.

Although a high rate of economic growth and a substantially improved tax effort are projected for Rwanda in the medium-term, there are pointers which suggest that GoR's fiscal governance trajectory could be precarious in the medium to long-term (IMF, 2009b). Tax to GDP ratio is projected to reach 15% of GDP by 2013. But, the level of grants is expected to decrease from a peak of 13.6% of GDP in 2009 to as low as 7.4% in 2013. At the same time, as earlier indicated, HIPC conditionalities, will restrict Rwanda's options for alternative resource mobilisation. In this scenario, Rwanda may not afford a fiscal framework that is consistent with achieving its development goals, especially as anchored to the National Vision 2020, unless tax effort is raised rapidly and considerably.

2 Trends in the tax system

2.1 Changes in tax policies over the years

2.1.1 The rudimentary legacy tax system of the 1960s

Rwanda inherited a rudimentary tax legislative and institutional structure at independence. The first tax legislation included the Ordinance of August 1912, which established graduated tax and tax on real property. In November 1925, there was another Ordinance adopting one issued in Belgian Congo in June 1925, to establish a profits tax. After independence, taxes were formally introduced in Rwanda by a law of June 1964 concerning profit tax. Customs and excise duties were introduced later by law in July 1968⁹. Apparently, there were minimal improvements until the time of the RPF regime, in 1994.

2.1.2 Tax policies immediately following the genocide and RRA formative years

When the RPF assumed power, as a temporary measure, it introduced an export tax on coffee. GoR also took steps to reduce the level of tax exemptions (e.g. around imports and waivers given to public enterprises, NGOs and faith groups), and curb tax evasion. In 1996, GoR imposed a “presumptive income tax of 3% of annual turnover on all enterprises...[and increased] specific consumption taxes on alcohol, petroleum and soft drinks” (IMF, 2000).

The establishment of RRA in 1997 was underpinned by the policy objective to maximise domestic revenue so as to reduce Rwanda’s dependence on foreign aid. There were no immediate major tax policy measures for the next three years and focus was apparently on building administrative capacity as GoR:

“Benefited from a long-term [IMF] resident adviser in tax policy, legislation and administration. Particular emphasis was placed on the establishment of the Large Enterprise Unit (in MINECOFIN), taxpayer registration and identification, including the introduction of taxpayer identification numbers, arrears collection, tax audits, and the introduction of presumptive taxation” (IMF, 2000).

2.1.3 Major developments in tax policies beginning 2001

The first major policy initiative of the post-genocide regime was the introduction of the Value Added Tax (VAT) in 2001. VAT replaced the sales tax (ICHA) through

⁹ http://www.devpartners.gov.rw/index.php?option=com_content&task=view&id=36&Itemid=56
[Accessed 21 February 2010].

Law No. 6 of 2001. ICHA was considered to offer too many exemptions and was difficult to administer¹⁰. The standard rate of VAT levied was initially 15% in 2001 but it is now 18%. Purchases by privileged persons (e.g. diplomats) as well as IDO financed projects are zero rated. Furthermore, certain supplies are exempt from VAT such as agricultural products, health services and supplies, education materials and services, transport services and water supplies.

In 2003, another major policy move was made when RRA was assigned responsibility for collecting non-tax revenues such as: fines and fees; revenue from public property and assets; proceeds from the sale of government vehicles. This was expanded with the addition of administrative fees in 2007.

Two years later, in 2005/06, further major policy and legislative measures were taken, comprising:

- New income tax legislation, through Law No. 16 of 2005. The top marginal corporate and personal income tax rates are 30%. Personal income tax rates are progressive with income categorised into three brackets with marginal rates of 0%, 20% and 30%¹¹, The law also provides for a: 4% annual turnover tax on 'intermediate' business owners; and dividend withholding tax. Also, depreciation allowances on capital assets were rationalised and simplified in the Income Tax law of 2005;
- A new tax code and investment and export promotion code as well as a new schedule for investments under customs through legislation. "These laws provide fiscal incentives to investors... There is a high threshold to meet this classification – US\$250,000 for foreigners and US\$100,000 for local investors" (USAID, 2008);
- Law No. 25 of 2005, which was enacted to: improve tax collection; set-up audit procedures, and a tax appeals process; and introduce speedy sanctions and penalties for tax evasion;
- Law No. 26 of 2006 was passed "determining and establishing consumption tax on some imported and locally manufactured products [and] provide penalties to taxpayers [who] fail to observe the required provisions"¹² – in

¹⁰ <http://www.gov.rw/economy/vat.htm> [Accessed 4 June 2010].

¹¹ http://www.rra.gov.rw/rra_article256.html [Accessed 16 April 2010].

¹² http://www.rra.gov.rw/rra_article252.html [Accessed 16 April 2010].

other words excise duties. Soft and alcoholic drinks, cigarettes, telephone communication, fuel, vehicles etc. are all subject to varying excise duty rates.

After a lull of another four-five years, the following tax policies were introduced:

- Rwanda became a signatory to the EAC Customs Union protocol in July 2009. The EAC Customs Union protocol is enshrined into the East African Community Customs Management Act of 2004. The protocol establishes common external tariffs (CETs), eliminating internal tariffs;
- Tax incentives for liquefied petroleum gas and energy saving devices. The policy objective is to make these devices more affordable in order to increase penetration of their use by households and industries. GoR estimates that this policy will result in a temporary loss of revenue of Rwf 300 million;
- The removal of the sugar surcharge in Law No. 71 of 2008. This surcharge was removed in tandem with the provisions of the EAC Customs Union leading to an estimated revenue loss of Rwf 2.2 billion per annum;
- A reversal of the VAT charge on transport. This was a tax on foreign trucks transporting goods in and out of Rwanda. It was introduced to ensure the competitiveness of Rwandan transporters. However, research has shown that the current capacity of Rwandan transporters is insufficient to satisfy demand. Furthermore, this tax was applied to transporters from Uganda, Tanzania and Kenya, and thus the tax increased the comparative cost of doing business in Rwanda. Therefore, the government reversed it, although about Rwf 370 million revenue per annum will be lost;
- A specific value fuel tax replaced the flexible ad valorem levy. This policy removed an implicit subsidy on fuel pump prices, and an intervention aimed at keeping pump prices stable. Also, the change in tax policy was due to the desire to align Rwanda's tax system with EAC practices. This entailed a shift from a flexible ad-valorem taxation rate to a specific tax set at a nominal Rwandan Franc value per litre. A key benefit of the new policy is that the government can have guaranteed revenue per litre sold which is independent of the international oil price (GoR, 2009).

2.2 Institutional changes

The establishment of the RRA as an autonomous agency in 1997, and the wide-ranging policy and legislative measures effected since 2001 have gone a long way

to transforming and modernising the institutional environment for DRM in the country. RRA enjoys strong political support for both its mandate and administrative autonomy. Government has provided an ultra-modern building for RRA to share with the National Electoral Commission and the Auditor General. RRA is allowed to retain 3% to 3.5% of its total revenue collection to meet its administrative costs. The actual budget is determined by the Board of Directors and approved by the Minister of MINECOFIN.

The staff of the RRA have been completely delinked from the civil service. The staff are better remunerated than civil servants, compensation includes a performance bonus of 5% of total revenue collected in excess of the target agreed with MINECOFIN. This is so far, regularly received, and paid to every staff member of the authority, in three or four instalments every year. The bonus is equal to 80 to 100% of individual staff salaries. This ratio is generally higher for junior staff and lower for the senior staff. It is considered to be a critical element of staff compensation because, according to RRA staff, it promotes retention of staff, and reduces any temptation to resort to corrupt practices.

More significantly, the RRA has the full and autonomous mandate for tax administration. Direct strategic leadership and oversight of the operations and performance of the authority is exercised by a Board of Directors comprising: a Chairman appointed by the Prime Minister with the approval of the Cabinet; a Vice-Chairperson who is the Permanent Secretary (PS), MINECOFIN; Governor of the National Bank of Rwanda (BNR); three professionals from the private sector; the PS, Ministry of Trade and Industry; and the PS, Ministry of Public Service and Labour. The chief executive (Commissioner General) and his/her deputy are appointed by the Cabinet. The Commissioner General, like the Chairman of the Board is required to sign a performance contract with the Minister. In the context of the performance contract, both officers are required to submit quarterly performance reports to the Minister. The role and mandate for policy-making and progressing of legislative measures for DRM remain with the MINECOFIN.

Structural reforms in RRA started in earnest in 2003, when a new structure was introduced. Until then, the tax administration was organised on the basis of tax categories, (i.e. Income tax and VAT departments). In that year, the Domestic Taxes Department (DTD) was established to further improve tax administration.

Today, the RRA has offices in all the provincial headquarters, and in 11 out of the 30 districts. In addition, RRA operates 32 customs offices and 8 border posts. It employs 875 staff, most of who are based at RRA's headquarters. At headquarters, the authority has two main operational departments:

- The Customs and Excise Department (CED): CED's mission is to contribute to the achievement of RRA's objectives by maximising the collection of all revenues due on imports, at minimum cost; and to facilitate trade through providing a responsive and efficient service to stakeholders. The department works to ensure that all legally chargeable revenues are paid through effective administration of the relevant laws. Specifically, CED is mandated to facilitate both international and national trade so as to support local and foreign investment, while ensuring that local society is protected from importation of hazardous and contraband material/goods;
- The DTD, which was established in order to create a one-stop, efficient and customer-oriented tax office. The basic objective is to increase and coordinate control over the largest taxpayers and improve large taxpayers' compliance and revenue yield to the government. The DTD is comprised of two offices - the Large Taxpayers' Office (LTO) and Small and Medium Taxpayers' Office (SMTO). The LTO accounts for over 50% of total RRA revenue collections. In July 2009, RRA's assumed responsibility for the audit, collection and enforcement of social security contributions from employers. This discharge of this function by RRA commenced in July 2010.

In addition to the two main departments, RRA has the following supporting departments: Revenue Protection Department (RPD); Quality Assurance; Taxpayer Services; Planning and Research; Legal and Board Secretariat; Human Resources and Administration; Information Technology; Finance Department; and RRA Training Centre.

It is noteworthy that fraud prevention and investigation support functions and activities at RRA are carried out by the RPD outside the core operations of the authority. The focus is on cases of complex tax fraud. The department's initiatives and activities respond to either the results of its risk research and analysis, or cases of suspected fraud identified by the DTD and CED, or its "intelligence agents" (informers). Informers are paid 10% of the revenue collected/recovered on any case they report on.

Prior to the establishment of RRA, the fraud prevention and investigation functions were handled purely as "military surveillance" and were carried out under MINECOFIN's Audit department. Then, all staff were seconded from the armed forces but were not under the command of MINECOFIN. Following the establishment of the RRA, armed officers seconded to the fraud prevention unit are accountable to the RRA management.

2.3 Changes in administrative systems

RRA's modernisation and development of its administrative systems, have since its establishment, been guided by strategic planning. This planning has recently taken to the state of the art, by adopting a balanced score card. The strategic vision of RRA is "*to become a world class efficient and modern revenue agency, fully financing national needs*". The current strategic plan, which has been prepared with a focus on the integration of Rwanda into the EAC, comprises 34 strategic objectives, and includes the following key targets:

- Assume the collection and audit of social security contributions by January 2010—RRA started collecting these contributions in July 2010;
- Support the government to widen the tax base with a target to achieve tax revenue collections of 15% of GDP by June 2010 – within a long term goal of 18% of GDP;
- Implement an anti-smuggling strategy, especially in the area of evasion of customs and excise duties;
- Substantially increase staff productivity, in terms of revenue per employee, and the improvement in the overall cost-of-collection ratio;
- Strengthen RRA's presence in the regions and computerise all regional offices. Also, provide a twenty-four hour, seven day (24/7) service at the border posts;
- Obtain the International Standards Organisation (ISO) 9001 certification by 2010.

Modernisation of administrative systems has been at the core of the changes pursued by RRA since it was established. In 2004, RRA commenced with the modernisation of its revenue collection systems. Computerisation focused on piloting systems with large taxpayers. The initiative covered the implementation of:

- The Standardized Integrated Government Tax Administration Systems (SIGTAS) in DTD. SIGTAS is a business analysis software introduced in 2003. It supports data management for each taxpayer, and facilitates tax returns processing, enforcement and audit;

- Automated System for Customs Data ++ (ASYCUDA++) for customs operations developed by the United Nations Conference on Trade and Development (UNCTAD). ASYCUDA allows for direct trader input so that importers can lodge declarations from their bases, and to minimise the build up of documents;
- PEODESY for human resources management and an enterprise resource planning system, Sage-Pastel Evolution for financial management;
- 'I.D.E.A' software for taxpayer audit purposes. According to key informants, RRA has a comparatively strict and punitive regime for enforcing tax collection by both large and small taxpayers, when the latter have been identified;
- A Revenue Authorities Digital Data Exchange (RADDEX) system – which has been jointly developed by the revenue authorities of East Africa to support coordinated management of transit of goods;
- E-doc for internal correspondences and a “one-to-one” laptop project for RRA staff.

The end-stage in the modernisation process will be the introduction of electronic filing (eFiling). However, according to RRA's management, 80% of the computerisation of the large taxpayers processes and systems is complete. The remaining and planned areas of modernisation include:

- eFiling, preparations for which started in early 2010, and should be complete in 2011;
- Electronic tax registers – funds for this initiative have not yet been identified;
- Social security funds collections, which commenced in July 2010.

2.4 Fiscal decentralisation and taxation by local governments

Rwanda's National Decentralisation Policy, officially adopted in May 2000, set out a new course of citizen participation through elected organs at the local level. Territorially, the subnational government structure of Rwanda is not unlike its neighbours in East Africa: the country is divided into 30 districts plus the City of Kigali. The district level is led by elected District Councillors and forms the main platform for subnational service delivery. Over the past ten years districts have been

accorded a greater role for service delivery across all sectors. It is the government's intention for sub-district *Secteurs* (of which there are 416) to increasingly become the nodes for subnational public service delivery. The *Secteurs* will enhance service delivery by assisting the district leadership in identifying, coordinating, and implementing development plans and programmes.

Although Rwanda faces the same fiscal decentralisation challenges that are encountered by other countries, the social context for decentralisation reform in the country provides a degree of vibrancy and innovation in its reform efforts that sets it apart from other countries in the region. The goal of the Government's Fiscal and Financial Decentralisation Policy (2006) is not only to pursue efficiency in the provision of services at the local level, but also sustainable development, economic growth and the reduction of poverty (Republic of Rwanda 2006).

The *Law on the Organization and Functioning of the District* (2006) assigns local governments in Rwanda a series of tax and non-tax revenue sources. The main local tax sources include the property tax, the trading license tax, and rental income tax, which were formerly collected by the central government and subsequently devolved to the local level. While local governments have a degree of discretion in determining tax rates, they are not permitted to create new taxes or define the tax base for local revenue sources. This ensures coordinated implementation of tax policy and less distortion/ disruption of economic activity.

Thus local governments in Rwanda are funded by a combination of conditional and unconditional grants, as well as by an assortment of local revenue sources. Between 20 and 25% of all public expenditures take place at the subnational level; this is similar to the share of the budget provided to the local government level in Tanzania, but below the level provided to the local government level in Uganda. In contrast to either Uganda or Tanzania, local governments in Rwanda contribute a larger share in local resources through own source revenues (see **Annex C: Tables C15 and C16**).

A 2004 assessment of alternative local revenue sources identifies numerous unexploited local user fees and charges as well as public-private partnerships that could generate revenue benefits for the local government level (ARD, 2004). However, concern has been raised about the capacity of local governments to engage in substantial broad-based revenue mobilisation (Tumukunde, Kiessel, and Khawar, 2008). Tumukunde et.al also observed numerous innovative community-based local revenue generation initiatives whereby community contributions were linked closely to improvements in public service delivery.

2.5 Reforms sequencing, implementation and results

The history of tax reforms in Rwanda is comparatively short. From a sequential perspective, six distinct albeit short phases of reforms' implementation can be identified:

- First - *institutional reforms and capacity building*, which correspond to the period beginning with the establishment of RRA in 1997 and the subsequent three years;
- Second - *widening the tax base*. The hallmark development in this phase was introduction of the VAT in 2001;
- Third – *streamlining the tax regime and administration*. This was effected by widening the mandate of RRA to collect non-tax revenues, and rationalisation of income tax rates, in 2003 and 2005 respectively;
- Fourth – *aligning the tax system to development policy priorities*, by introduction of a new tax, investment and export promotion legislation and tax code, in 2005;
- Fifth – *strengthening the compliance enforcement regime*; by enacting law number 25 of 2005 to cater for, among other measures, tax audits, appeals and penalties for evasion; and introducing penalties in 2006 for taxpayers who fail to comply with provisions for consumption taxes;
- Sixth – *harmonising Rwanda's tax regime and administration with that of the EAC* (in 2009 and 2010).

In a nutshell, the Rwanda tax system has been through several reforms since 2001. Nonetheless, the reforms have been systematic and sequenced.

On the whole, RRA and thereby DRM efforts of GoR are a success story. Tax revenue collected has considerably improved over the past decade, from 9.7% of GDP in 2000 to a projected 13.8% in 2010. The aim is for this ratio to grow at 0.2% or higher p.a. in the medium to long-term.

While the tax revenue to GDP ratio shows a comparatively modest level of performance, there are independent indicators that RRA has over the decade made commendably steady progress in capacity development. One such indicator is the uniquely sustained support that RRA has received from DFID over the years. RRA

is currently benefiting from the sixth successive DFID technical assistance and other capacity building support. At the end of each tranche of support, a comprehensive evaluation has been undertaken, and it is on the basis of the results of such evaluation that subsequent support has been provided. This support has been broad-based and flexible. It has been driven by RRA's strategic plans and reflects the priorities of MINECOFIN's and RRA's top management, as consistent with the Economic Development and Poverty Reduction Strategy. By 2005, DFID was funding as much as 34% of RRA's total budget. But amounts were reduced to about 10% in 2009.

RRA has also made noteworthy strides in modernisation and efficiency improvements of the tax administration system. Highlights of these results include:

- The ongoing major initiative to widen the tax base by establishing the Small and Medium Taxpayers Office (SMTO) and embarking on implementation of the block management system (BMS) to facilitate “the registration of more taxpayers through education, close monitoring and audit from their proximity” (Kiregu, 2009). In 2007, RRA reports that the SMTO had registered 9,662 taxpayers, undertook 455 audits (compared to 480 planned audits) and raised Rwf 3.2 billion (about US\$ 5.4 million) in tax revenues. However, “the average compliance rate in SMTO for returns filing during 2008 was about 49%. Filing compliance for SMTO remains below the average and requires more efforts” (RRA, 2008);
- RRA is also credited with a comparatively efficient system for the administration and payment of tax refunds. There is timely auditing of refund claims by the RRA. Also, unlike some EAC countries, in Rwanda, RRA has the full mandate to administer the refunds. In other countries, such as Kenya, the refunds require approval of their ministries of finance, and sometimes specific budgetary allocations. In the latter cases, payment of refunds sometimes taked more than a year after validation by the revenue authority. In Rwanda, refunds are usually paid within 30 days for claims below certain thresholds (see **Section 3.2.1**);
- Compliance levels have significantly improved with as many as 97% compliant large taxpayers (who contribute approximately 75% of total

domestic taxes¹³). Compliance rates are lower in the medium and small taxpayers;

- Improved administration of collection and cash management - Collection of revenues is mainly undertaken by commercial banks. Over 90% of revenue is collected by banks;
- In 2010, Rwanda and Uganda launched a 24/7 one-stop border service at Gatuna. Rwanda's PS in the Ministry of East African Community Affairs is cited as having said, "The one stop border point shall benefit the private sector, by providing quality and quick service delivery of goods and services across EAC" (Gahene, 2010);
- RRA has contributed to a dramatic improvement in Rwanda's ranking in the World Bank's 2010 global "Doing Business Index", by spearheading the introduction a number of tax legislation reforms. Rwanda's ranking rose to 67 in the latest ranking (2010) from 143 in 2009¹⁴;
- RRA became ISO 9001 certified in 2009. "According to RRA Commissioner General, Mary Baine, ISO certification demonstrates RRA's ability to enhance customer satisfaction through effective application of quality systems"¹⁵.

On the other hand, there are suggestions that Rwanda may have been doing significantly better in tax revenue generation if did not extend the kind of tax incentives and exemptions it introduced from 2005 with the objective of attracting foreign investors to the country. In this regard, for example, the IMF (2007a) observed that tax incentives may be counterproductive or ineffective because: (i) they distort the investment climate and discriminate against investments by domestic and/or small and medium enterprises; (ii) there is evidence that such other factors as infrastructure, property and commercial legal system, efficiency and integrity of the public service, etc. are ranked higher by investors in the choice of their investment locations; and (iii) what the investor's host country fails to tax ends up being taxed in the country of the investors' domicile. In other words, the tax

¹³ The large taxpayer segment constitutes less than 5% of the total tax paying community (Musoni, 2009).

¹⁴ http://www.devpartners.gov.rw/index.php?option=com_content&task=view&id=36&Itemid=56 [Accessed 21 February 2010].

¹⁵ http://www.rra.gov.rw/rra_article521.html [Accessed 18 April 2010].

policies of the country of origin of the investor may cancel out the presumed local tax advantage.

3 Domestic revenue performance

3.1 Domestic revenue performance trends

Rwanda’s total domestic revenue as a percentage of GDP rose from 8.4% in 1993, to 14.2% in 2008 (see **Figure 3.1**). In the year that the genocide took place (1994), however, total domestic resources as a percentage of GDP fell to 3.6%. In the period between 1993 and 2008, on average the split between tax and non-tax revenues was 93.3% to 6.3%. Observations made by the IMF (2009c), are that tax growth has ranged between 0.25% and 0.3% of GDP every year from 1997. Furthermore, the mission team indicates that in line with GoR’s aspirations in Vision 2020 to be less dependent on IDOs, “tax effort needs to be scaled up”¹⁶. It is also noteworthy that when GoR embarked on tax reforms in 1998, it aimed to increase “the revenue-to-GDP ratio by 0.5% p.a.” (IMF, 2000).

Figure 3.1: Tax and non-tax revenue contribution as a percentage of GDP (1993 to 2008)



Source: Various IMF staff reports. Also see Annex C: Table 14

There are three main categories of domestic revenue sources: taxes on goods and services (comprising VAT and excise duty), direct taxes (including PAYE, corporation income tax, personal income tax and tax imputed on turnover), and tax on international trade. As shown in Fig. 3.1, taxes on goods and services have

¹⁶ http://www.devpartners.gov.rw/index.php?option=com_content&task=view&id=36&Itemid=56 [Accessed 21 February 2010].

formed the largest proportion of total domestic revenues – at about 48% of the total tax revenue (see also **Annex C: Table C6**). Since 2001, and with the exception of 2004, the contribution to total taxes from direct taxes has been on a steady rise – in 2008 the share of direct taxes peaked at 37.5%. The share of taxes on international trade to total tax revenues has steadily decreased from a high of 41% in 1995, to just over 10% in recent years. This reduction is explained by an initial reduction in import duty rates – “with the maximum rate declining from 60% to 40%” (IMF, 2000). Furthermore, “Rwanda’s weighted average tariff rate was 11.3% in 2008”¹⁷.

A key reason for comparative underperformance of domestic revenue in Rwanda is that whilst agriculture is a significant means of production, farmers and other traders operate on an informal basis and are largely not captured within the tax net. “According to the Private Sector Federation [PSF], about 0.3% of taxpayers contribute 48% of Rwanda’s tax revenue” (Godbout, 2009). The IMF (2009c) estimates that between 2002 and 2009, the informal sector contributed an average of 6.25% of GDP. The IMF (2009c) also suggests that by formalising such enterprises and monetising the economy, there would be huge pay-offs in terms of increased levels of DRM¹⁸. Therefore, RRA’s “onus should be on widening the tax net to the informal sector and ensuring that tax laws are applied evenly and fairly” (IMF, 2007b).

In recent years, there have been continuous efforts by the RRA to improve its reach of the informal sector, and small and medium enterprises (SMEs). In 2008, for example, the RRA pronounced changes in the system of taxing commercial vehicles. The change was aimed at bringing fairness in tax collection whereby taxes on a vehicle would be paid according to its load capacity by tonnage or number of passengers. Also, in 2009, the Minister of Finance and Economic Planning, talking of the potential of the informal sector and SMEs to contribute to revenue, is quoted to have stated that, “we are closing in on this very large and yet elusive informal sector. The large taxpayer segment constitutes less than 5% of the total tax paying community but from which over 75% of the total tax revenues are collected” (Musoni, 2009).

¹⁷ <http://www.heritage.org/index/Country/Rwanda> [Accessed 18 April 2010].

¹⁸ http://www.devpartners.gov.rw/index.php?option=com_content&task=view&id=36&Itemid=56 [Accessed 21 February 2010].

3.2 Tax administration performance benchmarks

3.2.1 Performance efficiency

Cost of collection. Between 2003/04 and 2007/08, RRA's operating costs (including capital expenditure) as a percentage of total revenue collected averaged at 3% (see **Annex C: Table C2**). The IMF rates this result as comparatively higher than what is considered typical for modern revenue administrations, which would be less than 2% (IMF, 2007a). In particular, in the same IMF review, Rwanda's collection costs as percentage of total tax revenues were observed to be higher than for other countries in the region – Kenya (1.7%), Malawi (2.8%), Tanzania (2.8%) and Uganda (2.8%). Furthermore, during the four year period to 2007/08, RRA's tax administrative costs grew at an average annual growth rate of 27%.

Organizational structure. RRA is organised along functional lines. It established a LTO in 2006. In 2010, the LTO served 307 large taxpayers. Large taxpayers comprise individuals, corporates, government bodies and ministries, who meet one or more of the following criteria: (i) their activities are complex and turnover exceeds Rwf 200 million p.a.; (ii) they pay excise duties; (iii) they are registered with RDB and have invested over Rwf300 million; and (iv) they are gauged to have growth potential; and their PAYE costs exceed Rwf600 million p.a.¹⁹. In the same year, the SMTO was established, and by 2007 had 9,662 registered taxpayers who contributed 16% of total revenue collections (RRA, 2008).

Ease of paying taxes. Rwanda has the best rating among the EAC countries, in terms of the World Bank's Doing Business Ranking with respect to, ease of paying taxes – ranking 59th out of 183 countries in 2010. However, Rwanda dropped one place from its position in 2009 of 58th place. According to the World Bank's 2010 Paying Taxes report, a company is required to make 34 payments a year which are below the SSA average of 37.7 p.a., but above the OCED average of 12.8 a year.

Tax arrears. Information on tax arrears was only available for 2006/07 and 2007/08. Tax arrears as a percentage of total tax collections in 2007/08 amounted to 16.4%. According to the IMF (2007a), "significant progress was made by the RRA in 2006 to reduce the stock of tax arrears, particularly for corporate profits tax where Rwf 17,334 million was collected during the year. The number of debtors at the end of 2006 was less than 400, with around Rwf 8,500 million outstanding (i.e., 4.4% of total 2006 collections)".

¹⁹ International Tax Dialogue Survey – 2009.

VAT payment system. In 2008, RRA streamlined the VAT refund process. It set various monetary refund limits which small (below Rwf 50,000), medium (below Rwf 100,000) and large (below Rwf 200,000) taxpayers can automatically deduct from their next month's VAT return – in other words VAT refunds for eligible amounts are made within 30 days. Refunds above the prescribed thresholds are subject to further conditions including for example the need: to have deposited a payment at the Treasury; for a taxpayer to submit honest and accurate returns; and for an audit over a prescribed threshold.

Tax compliance. Rwanda has a low VAT gross compliance ratio (VATGCR) of 30.30 in comparison to World and SSA averages of 65.48 and 38.45 respectively²⁰. Measures from the same source compute corporate income tax (CIT) revenue productivity (CITPROD) and personal income tax (PIT) productivity (PITPTOD) of 0.06 and 0.09 which indicate that Rwanda uses the taxes less efficiently in generating revenue than World averages of 0.13 and 0.14 for CITPROD and PITPROD respectively.

Compliance by large taxpayers is generally high because the LTO closely monitors each of them. There is continuous audit of large taxpayers whose monthly dues of VAT, PAYE and withholding tax are audited and agreed before payment. The audits are also comparatively quick but thorough. To this end, RRA has its audit staff literally camped at taxpayers' premises. However, compliance by others remains weak. According to the IMF (2007a), about a third of corporate and non-corporate tax returns were filed late, and 15% of VAT payers failed to file returns on time.

3.2.2 Allocative efficiency

In 2006, a review of tax incentives highlighted “revenue losses of about 3% of GDP” (IMF, 2006). Furthermore, the IMF (2007a) raised concerns about potential allocative inefficiencies arising from use of tax holidays and other incentives to attract foreign investors. The same review observed that for Rwanda they should be avoided (see **Box 3.1**).

Box 3.1: The IMF's rationale for avoiding tax holidays

“Tax holidays as a policy instrument should be avoided for three main reasons. First, such instruments are in direct conflict with goals to increase tax revenues and therefore place greater pressure on tax-base broadening in the medium and small taxpayer segments where greater effort is required for much lower yields. Second, tax is generally a second order issue to investors eclipsed by such factors as the rule of law, a working judicial system, security of property ownership, good infrastructure and as little bureaucracy in doing business as possible. Third, and

²⁰ http://www.fiscalreform.net/index.php?option=com_wrapper&Itemid=132 [Accessed 2 February 2010].

closely connected to the second point (in the sense that tax is not a factor) is that most investor countries' tax systems operate on a residence basis, and hence perversely, where taxable income is subject to no tax in Rwanda as a result of a tax holiday, the businesses' country of residence acquires a taxing right to this income instead... It is important for the RRA to ensure that it adequately records revenue forgone by ensuring that businesses subject to tax holidays file tax returns, like any other business, so that the quantum of lost revenues can be reported to the ministry of finance. Equally important is the need to ensure that investors already established in Rwanda do not have access to this regime and that businesses cannot qualify for renewed tax holidays for substantially the same investment through restructured business entities or convoluted schemes".

Source: IMF (2007a)

3.2.3 Performance equity

Rwanda has a regressive income tax regime by any standards. 2009 personal income tax rates show that the minimum monthly taxable income attracting the highest PAYE rate of 30% is as low as RwF 100,000 (equivalent to US\$175). This is about a third of threshold levels for Kenya (US\$523) and Tanzania (US\$542). Yet, even the latter two countries fall in the category of the majority of African countries that have been described as having regressive tax rates on income. For instance, thresholds for the maximum personal income tax rate in the Republic of South Africa and Botswana are about US\$1,318 and 1,515 respectively (Institute of Economic Affairs, 2010).

However, as with other countries in the region, Rwanda's VAT system does provide for tax concessions for certain basic goods and services consumed by poor households. Similarly, excise and import duties are generally levied on luxury items or goods which contribute to negative public health externalities.

In the case of corporate business income, the World Bank's 2010 Paying Taxes report indicates that the 'total tax rate' as a percentage of profit of 31.3% is significantly lower than the OECD average of 44.5%, and is lower than the SSA average of 67.5%. However, RRA is reputedly tough with taxpayers. It has forced the closure of businesses where tax evasion went on for a long time. Furthermore, we understand that there have been many instances in the past, when MINECOFIN has had to restrain the RRA from taking coercive action against taxpayers with payments in arrears.

Another indicator of the tax burden has to do with the amount of time taken by taxpayers to comply with the major types of taxes. In this regard, the 2010 World Bank paying taxes survey indicates that, the time taken by companies in Rwanda to comply with major taxes is 160 hours, which is much lower than the OECD and SSA averages of 194.1 hours and 306.0 hours respectively.

3.2.4 Performance effectiveness

RRA's performance effectiveness is modest in terms of tax effort and tax gap (see **Annex C: Table C13**). At 61.4% in 2008, Rwanda's tax effort was lower than that in Tanzania 71.6%, but higher than in 2001 (51.2%). However, Rwanda's tax gap was 9.9% in 2005, and higher than that recorded for Kenya, Tanzania and Uganda of 2.0%, 5.9% and 7.8% respectively during the same period.

At an operational level, to enhance its performance effectiveness, RRA's management considers that it has been successful in establishing a good relationship with the main taxpayers. The RRA has enabled regular dialogue with representatives of the private sector. There is a quarterly Tax Issues Forum which is jointly chaired by the Commissioner General of RRA and the Chief Executive of the PSF. Participants comprise taxpayers and senior staff of RRA. The forum has a standing technical committee with representation by both taxpayers and RRA staff, which facilitates collaborative dialogue and analysis of the issues prior to the quarterly forum. In addition, RRA welcomes taxpayer feedback through an online customer satisfaction feedback questionnaire.

However, there is an independent perspective that RRA has not been responsive to the specific needs of small taxpayers; this sentiment is especially cited in terms of outreach and education. From a study on the informal sector in Rwanda, 53% respondents mentioned tax as the most troublesome regulation. In any case, it is not easy to reach many of the SMEs because they are rural based and thus have limited access to urban infrastructure, markets and technology (Hategeka, 2009). PSF members have previously complained that RRA does not pay attention to small businesses, which account for over 80% of employment (Torero et al, 2006). However, a study by the federation also confirmed the difficulties in bringing the SMEs and other informal sector entities into the tax bracket. It was also noted that, in Rwanda, as in most African countries, most SMEs are run by illiterate and semi-literate owners/families.

3.3 Summary of overall trends

Rwanda has a relatively short history of policy, institutional, legislative and capacity development and reforms, which date after the 1994 genocide. The implementation of changes has been rapid but systematic and overall quite successful. Rwanda's total domestic revenue as a percentage of GDP rose steadily from 9.7% in 2000 to 14.2% in 2008. The ratio is projected at a lower 13.8% in 2010, but this is generally explained by failure of tax revenue growth to keep pace with the high real GDP growth rate, as discussed in **Chapter 1**.

Although the tax to GDP ratio for Rwanda is significantly lower than that of, for example Kenya, Tanzania and South Africa, target growth rate for this ratio is also fairly low, at about 0.2 annual percentage points. This comparative underperformance of domestic revenue and conservative target growth rate is explained by the fact that the economy remains agriculture-based; with dominance of smallholder farmers. The other significant potential pool of taxpayers constitutes of small-time traders who largely operate informally. Such farmers and traders are not easily captured into the tax net. However, RRA has an aggressive programme to draw several of the informal market participants into the tax net through the implementation of the BMS.

4 Challenges and issues

4.1 Introduction

At the end of the previous chapter, it was pointed out that the structure of the Rwanda economy today (i.e. preponderance of smallholder farmers and informal traders) poses a near-binding constraint to rapid enhancement in the overall tax revenue base. Therefore, in the short to medium term, significant rises in real tax revenue growth are more likely to come from measures to raise and sustain compliance by existing taxpayers and improve administration efficiency. With a long-term perspective, efforts to widen the tax net will also continue to be implemented. Nonetheless, on both prongs, there will be challenges and issues to be addressed. The more significant of these challenges are highlighted below.

4.2 Achieving a cost-effective strategy to widen the tax net

Widening the tax net entails capturing small and micro enterprises that are largely in the informal sector, and getting them to pay taxes. This will not be easy. As a survey by PSF reports, “small and micro business operators in Rwanda generally have low literacy and numerical skills, and have limited understanding of both the tax system and business record keeping...and understanding of tax matters is weak” (Hategeka, 2009). Furthermore, it can be costly to apply conventional approaches such as audits to bring these enterprises into the tax net, and to enforce compliance. Therefore, RRA needs to develop strategy, knowledge and other capacity to successfully and cost-effectively implement alternative interventions. The approach to adopt should be considered on a case by case basis. In particular, RRA has done well to study the experiences of Tanzania in the implementation of the BMS. The RRA may also benefit from Kenya’s experiences, for instance with electronic tax registers for VAT. Moreover, relevant taxpayer education will remain a critical feature of whatever strategy or modality is identified or designed.

4.3 Rationalising the collection of central and local government taxes

In line with GoR’s decentralisation policy, the mandate for collecting taxes from property and rental income lies with the local government authorities (Kigali City Council and districts councils). However, experiences from countries such as Kenya and South Africa suggest that RRA could be more effective than local governments in collecting property taxes and taxes on rental income because of its expertise, resources and institutional arrangements. Also, in some countries such as Tanzania, the revenue authority collects property taxes on behalf of local government authorities. There is a distinct prospect that in some districts the local

elites will collude with tax staff in councils to evade taxes. There is also a risk that some councils will not handle taxpayers with any courtesy. Nor are the councils likely to undertake any taxpayer education. Furthermore, given that local governments have been assigned a range of taxes, (i.e. property tax, tax on rental income, fees and levies on quarries, markets, etc), there is a risk that the need to file taxes to multiple tax collection agencies could increase taxpayer compliance costs, and potentially increase the temptation to avoid and evade taxes. Therefore, the challenge to rationalise the tax collection functions between RRA and local governments can be anticipated.

4.4 Developing and maintaining capacity for tax policy management

One important consideration in the establishment of RRA and the transfer of the tax administration function out of MINECOFIN, was the exigency to minimise bureaucratic red-tape, low staff morale and poor performance in the discharge of functions. Under a quasi-autonomous revenue agency: processes and procedures are restructured and re-engineered to eliminate resource and time-wasting routines; salary and incentive frameworks are put in place so as to attract, retain and motivate revenue collection officers, and enhance their integrity etc. On the basis of the latter, substantial and reliable institutional and human resources capacity for rapid growth and efficient revenue collection could be developed.

There is still another very important factor that should have underscored the creation of RRA from the revenue collection departments of MINECOFIN. That factor is the case for separating tax policy from administration (DFID, 2008a). The institutional and organisational developments are in the right direction. However, it appears that the tax policy function is much weaker relative to tax administration. This is to a significant extent, explained by the fact that the organisation and staff in tax policy remain in the bureaucratic and poor incentive environment of MINECOFIN. Therefore, only a strategic and deliberate effort to build capacity for tax policy functions will ensure that the necessary capacity is installed.

4.5 Building and sustaining management capacity in RRA

Building and sustaining adequate capacity, especially technical and professional skills, will remain a major challenge to RRA for well into the long run. Land (2004) observed that:

“The RRA is no longer the employer of choice, and is finding it increasingly difficult to remain competitive in the labour market. Once the standard bearer for conditions of service, a growing number of private and quasi-public institutions as well as international agencies now offer more competitive

remuneration packages. It is therefore becoming more difficult to attract and retain good personnel. Constrained by budget ceilings, the RRA will have to work at improving efficiency so that resources can be freed up to offer more attractive salaries linked to performance”.

The difficulties entailed in human resources capacity development and retention is exacerbated by the proliferation of ICT applications for both core business processes as well as management support services. The technologies for these applications keep changing with short time spans, and the competition for the skills is ever intense, because the market is not confined to the boundaries of Rwanda. It is definitely regional and increasingly global. In this regard, RRA will need technical assistance to sustain the modernisation momentum in key areas such as: (i) risk management for tax and customs administration; (ii) an assessment of SIGTAS and ASYCUDA ++ to support risk management approaches, particularly automatic profiling of taxpayers; (iii) developing a “super” green/gold card trader facilitation programme, including an importer self-assessment instrument and guidelines; and (iv) developing RRA processes and procedures in readiness to collect social security contributions.

4.6 Putting a cap on tax incentives and exemptions

In the pursuit of the policy goal of making Rwanda a preferred foreign investment destination, and to attract particular investors to establish in Africa, GoR has legislated tax incentives (see **Sections 2.1.3** and **3.2.2**). It has also granted tax exemptions to some businesses. Available data suggests that the impact of these exemptions and incentives in terms of tax revenues foregone is significant. Moreover, there is a body of knowledge that suggests that these incentives are counter-productive in terms of: (i) distorting the investment climate and discriminating against investments by domestic and/or small and medium enterprises; (ii) there is evidence that such other factors as infrastructure, property and commercial legal system, efficiency and integrity of the public service, among others, are ranked higher by investors in the choice of their investment locations; and (iii) what the investor’s host country fails to tax ends up being taxed in country of the investors’ domicile. In other words, the tax policies of the country of origin of the investor may cancel out the presumed local tax advantage. Despite such arguments, however, political leaders may not be easily persuaded not to grant tax favours in their courting of brand international investors. This remains a challenge for Rwanda.

5 Lessons of experience

The outcomes and impact of the wide ranging policy and capacity development measures that Rwanda, and RRA in particular, have implemented since the establishment of the RRA in 1997, are yet to yield the expected results. Nonetheless, in confronting the challenges of design and implementation, three major lessons of experience, which are presented below, are worth sharing.

5.1 Explicit and strong top political leadership support matters

Rwanda has gone through a marathon of policy, institutional, legislative and capacity development changes with the goal of achieving rapid growth in tax revenues over the past decade or so. Many of the key informants to this study were emphatic in sharing the view that strong support from the top political leadership of the country, especially the President, and successive ministers of finance was the most crucial driver for change. This is collaborated by Land (2004):

“The RRA was granted a clear and unequivocal mandate and a strategic role to play within government's wider strategy of national reconstruction, poverty reduction and good governance. As the centrepiece of the country's domestic revenue generation effort, it has been expected to play a key role in meeting the aspirations of the Rwandan government and its international partners to the reduce dependency on aid and to shift towards a country-driven transformation process. Accordingly, from the outset the RRA enjoyed a high degree of legitimacy and backing from official circles - there were equally high expectations placed on the nascent organisation to perform”.

5.2 Developing and retaining effective capacity is a long-term undertaking

RRA has benefited from strong government as well as IDO (especially DFID commitment) to provide the resources needed to rapidly develop its capacity. Furthermore, the authority's strategic plans reflect that there has also been determination to expeditiously develop capacity, and improve performance on the part of the top management of RRA. Yet, considerable gaps in capacity are prevalent, even after a decade of consistent efforts. The IMF (2009b) suggests the priority gaps to be closed are strengthening audit and enforcement capacity. The IMF also suggests that management support functions such as management of ICT applications, human resource management and finances deserve as much attention especially because technical and professional staff in the latter skills areas are in high demand in the local, regional and global markets.

5.3 Long term and flexible technical assistance support enables rapid and sustained capacity development

DFID has provided substantial support to the RRA since 1998. As mentioned earlier, by 2003, it was 34% of the total RRA budget, and for the subsequent four years ranged between 31% and 20%, before dropping to about 11% in 2008 (DFID, 2008b). While that support is now being substantially phased out, the following observation by a DFID independent review mission is noteworthy:

“There is a clear and direct link between DFID’s support and RRA’s revenue collection performance. The major share of the funding has been invested in IT hardware and software, primarily for installation and the development of SIGTAS and ASYCUDA the main IT systems supporting the improvement of the operations at the RRA. Furthermore, the spending on training has strengthened the skills across a broad range of RRA’s operations. Although DFID’s share of the total annual funding of the RRA has reduced over the years, the contribution remains significant in the context of the non-salary expenditures” (DFID, 2008b).

Annex A: Key informants

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Eugene Mugnai Torero (Mr), Deputy Commissioner General & Commissioner for Customs Services, Rwanda Revenue Authority

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Jeremy Armon (Mr), Senior Governance Adviser, UK Department for International Development

Michael Minega Sebera (Mr) International Legal and Agreements expert, Ministry of Finance and Economic Planning

Mugo W. Maringa (Mr), Country Manager, Tourism Promotion Services (Rwanda) Limited

Noah Oluoch (Mr), Chief Accountant, Tourism Promotion Services (Rwanda) Limited

Obald Hakizimana (Mr), Head of Macroeconomic Policy, Ministry of Finance and Economic Planning

Pierre Celestin Bumbakare (Mr) Commissioner Domestic Taxes, Rwanda Revenue Authority

Richard Dada (Mr), Deputy Commissioner of Small and Medium Taxpayers Office, Rwanda Revenue Authority

Seth Muhirwa (Mr), Director of Revenue Protection Department, Rwanda Revenue Authority

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Annex C: Select indicators

Table C1: Tax policy – Maximum marginal tax rates

Fiscal year	PIT	CIT	VAT
2000/01	-	-	18%
2001/02	-	-	18%
2002/03	-	35%	18%
2003/04	-	35%	18%
2004/05	-	35%	18%
2005/06	30%	30%	18%
2006/07	30%	30%	18%
2007/08	30%	30%	18%

Source: RRA

Table C2: Tax administration costs (1998/99 to 2007/08)

Fiscal year	Operating cost (RwF)	Operating cost as a % of tax revenue
2003/04	4,343,432,497	3.2%
2004/05	4,919,010,000	2.8%
2005/06	6,996,670,000	3.4%
2006/07	7,575,300,000	3.0%
2007/08	9,418,400,000	2.7%

Source: Various RRA annual reports

Table C3: Ratio of tax staff per population (TAXSTAFF)

Indicator	Rwanda's measure	World's measure	SSA's measure	Low income economies' measure
TAXSTAFF	-	0.82	0.37	0.20

Source: http://www.fiscalreform.net/index.php?option=com_wrapper&Itemid=132 [Accessed 2 February 2010].

Table C4: National government revenue and deficit as a percentage of GDP (1993-2008)

Year	Revenue (tax plus non-tax)	Total revenue including grants	Budget deficit before grants
1993	8.4%	9.1%	-14.5%
1994	3.6%	3.6%	-12.4%
1995	6.1%	6.9%	-13.3%
1996	8.4%	9.1%	-13.1%
1997	9.8%	10.3%	-9.9%
1998	9.9%	10.4%	-10.8%
1999	11.8%	19.8%	-12.3%

Year	Revenue (tax plus non-tax)	Total revenue including grants	Budget deficit before grants
2000	12.1%	25.3%	-12.5%
2001	13.8%	25.7%	-12.5%
2002	15.0%	19.4%	-11.9%
2003	13.5%	21.6%	-10.3%
2004	13.9%	25.9%	-12.1%
2005	15.1%	29.2%	-13.4%
2006	13.3%	24.0%	-11.1%
2007	13.6%	23.4%	-11.3%
2008	14.2%	27.1%	-11.0%

Sources: Various IMF staff reports

Table C5: Split of total budgeted tax and non-tax revenue as a percentage of total domestic revenue (1993- 2008)

Year	Tax revenue	Non-tax revenue
1993	92.3%	7.7%
1994	100.0%	0.0%
1995	93.9%	6.1%
1996	91.9%	8.1%
1997	94.7%	5.3%
1998	94.8%	5.2%
1999	95.0%	5.0%
2000	95.2%	4.8%
2001	92.2%	7.8%
2002	93.5%	6.5%
2003	93.7%	6.3%
2004	91.6%	8.4%
2005	90.2%	9.8%
2006	93.0%	7.0%
2007	94.0%	6.0%
2008	86.3%	13.7%

Source: Various IMF staff reports

Table C6: Composition of national government tax revenues (1993 to 2008)

Year	Direct taxes	Taxes on goods and services	Taxes on international trade
1993	26.8%	43.1%	30.1%
1994	26.2%	37.7%	36.1%
1995	13.4%	45.6%	41.0%
1996	28.5%	39.8%	31.8%

1997	26.5%	39.8%	33.6%
1998	29.2%	45.5%	25.2%
1999	26.2%	55.6%	18.2%
2000	28.3%	53.9%	17.8%
2001	30.8%	51.6%	17.6%
2002	32.2%	50.1%	17.7%
2003	30.6%	50.1%	19.3%
2004	28.4%	52.1%	19.5%
2005	31.2%	51.0%	17.8%
2006	33.3%	49.3%	17.4%
2007	36.1%	50.9%	13.0%
2008	37.5%	49.2%	13.4%

Source: Various IMF staff reports

Table C7: Contribution of major direct, consumption and international taxes to overall tax revenue collections in Rwanda (2006 to 2008)

Year	Tax on profit	PAYE	VAT	Excises	Customs duties	Total
2006	14.1%	17.7%	33.9%	11.7%	15.5%	100.0%
2007	13.5%	18.1%	32.2%	11.1%	14.0%	100.0%
2008	16.1%	18.0%	33.2%	10.6%	11.4%	100.0%

Source: RRA annual reports

Table C8: Amount of previous year's arrears collected as a percentage of total amount of tax arrears at beginning of year

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08
Tax arrears at the end of the financial year as a percentage of fiscal collections	-	-	-	-	-	16.4%

Source: RRA annual reports

Table C9: CIT and PIT revenue productivity and VAT gross compliance ratio (2008/09)

Indicator	Rwanda's measure	World's measure	SSA's measure	Low income economies' measure
CITPROD	0.06	0.13	0.09	0.08
PITPROD	0.09	0.14	0.08	0.07
VATGCR	30.30	65.48	42.3	38.45

Source: http://www.fiscalreform.net/index.php?option=com_wrapper&Itemid=132 [Accessed 2 February 2010].

Table C10: World Bank Doing Business indicators on the tax burden (Rwanda only)

Indicator	Year		
	2008	2009	2010

Rwanda's global ranking	-	58	59
Number of tax payments a year	34	34	34
Time taken to comply with the major tax types	168	160	160

Source: <http://www.doingbusiness.org/ExploreEconomies/?economyid=185> [Accessed 10 March 2010]

Table C11: World Bank Doing Business indicators (2010) on the tax burden (Rwanda vis-à-vis the OECD and SSA)

Indicator	Region		
	Rwanda	OECD	SSA
Number of tax payments a year	34	12.8	37.7
Time taken to comply with the major tax types	160	194.1	306.0
Total tax rate as % of profit	31.3%	44.5%	67.5%

Source: <http://www.doingbusiness.org/ExploreEconomies/?economyid=185> [Accessed 10 March 2010]

Table C12: Growth of registered taxpayers (2002/03 to 2007/08)

Registered for	Total number			Percentage increase (2006 to 2008)
	2006	2007	2008	
VAT	2,637	3,741	4,644	76%
PAYE	4,495	9,285	8,929	99%
Profit taxes	4,205	11,842	20,676	392%
Large taxpayers	284	289	311	10%

Source: RRA annual reports

Table C13: Tax gap and tax effort for select EAC countries and South Africa (select years)

Country	Year	Tax revenue (A)	Estimated potential tax revenue (B)	Tax gap (B) – (A)	Tax effort (A)/(B) as a %
		As a % of GDP			
Kenya	2001	17.8	20.8	3.0	85.5
	2005	18.6	20.6	2.0	90.5
South Africa	2001	24.8	26.7	1.9	92.9
	2005	27.4	27.0	-0.4	101.4
Rwanda	2001	10.7	20.9	10.2	51.2
	2005	12.2	21.4	9.9	57.0
	2008	13.5	22.0	8.5	61.4
Tanzania	2001	9.7	20.0	10.3	48.5
	2005	11.2	20.5	9.3	54.4
	2008	15.0	20.9	5.9	71.6
Uganda	2001	10.4	19.2	8.8	54.3
	2005	11.8	19.5	7.8	60.3

Source: IMF (2009c)

Table C14: Value added by sector as a percentage of GDP

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Agriculture	37%	37%	37%	35%	38%	39%	38%	38%	36%	32%	34%
Industry	15%	14%	14%	14%	13%	14%	14%	14%	14%	15%	14%
Services	42%	44%	43%	44%	42%	41%	41%	42%	45%	46%	46%
Adjustments	6%	5%	6%	7%	7%	6%	6%	6%	6%	6%	6%

Source: GoR

Table C15: Aggregate provisional local revenue budget for Rwanda, 2008 (in Rwandan Francs)

	Amount	Percent of total	Percent of total own revenues
Own revenues			
Property tax	4,225,191,332	4.1	31.0
Administrative fees	6,602,246,477	6.4	48.4
Concessions for mines	313,533,408	0.3	2.3
Other revenues	2,452,826,228	2.4	18.0
Interest	42,524,160	0.0	0.3
Total own revenues	13,636,321,605	13.2	100.0
Transfers from central government			

Block grants	11,507,008,328	11.2	
Conditional grants	77,972,942,498	75.6	
Total transfers	89,479,950,826	86.8	
Grand total	103,116,272,431	100.0	

Note: The financial data covers Rwanda's 30 Districts, excluding the City of Kigali.

Source: Computed by author based on data from MINECOFIN²¹.

Table C16: Key fiscal decentralisation indicators

	Kenya	Rwanda	Uganda	Tanzania	South Africa
Functional assignment: local government level responsible for delivery of national social services (education and health)?	No	Yes	Yes	Yes	No
Functional assignment: local government level responsible for basic municipal functions?	Yes	Yes	Yes	Yes	Yes
Percentage of centrally collected revenue transferred to local government level	2.2	27.1	36.0*	29.1	5.5
Percentage of public revenues represented by local own source revenues	2.8	3.5	1.2*	2.1	13.7
Percentage of local financed represented by local own source revenues	57.1	11.7	5.0	7.0	74.3
Is there a constitutionally (or legally) established agency/mechanism for vertical revenue sharing?	Yes	Yes	Yes	No	Yes
Is there a fixed horizontal revenue sharing formula for the main transfer schemes?	Yes	Yes	Yes*	Yes*	Yes

Note: An asterisk (*) reflects a partial or qualified finding.

Source: Various governments

²¹ Note: The financial data covers Rwanda's 30 Districts, excluding the City of Kigali.

Annex D: Glossary of definitions of select terms

CITPROD	CITPROD indicates how well CIT does in terms of producing revenue, given the prevailing tax rate. It is calculated by dividing total corporate income tax revenues by GDP and then dividing this by the general corporate income tax rate.
PITPROD	PITPROD attempts to provide an indication of how well the personal income tax in a country does in terms of producing revenue. It is calculated by taking the actual revenue collected as a percentage of GDP, divided by the weighted average PIT rate.
Tax effort	Actual tax revenue as a percentage of estimated potential tax revenue
Tax gap	The difference between estimated potential tax revenue and actual tax revenue
VATCGR	This is a measure of how well the VAT produces revenue for the government. It is computed by dividing VAT revenues by total private consumption in the economy and then dividing this by the VAT rate.