The Effect of suspending Graduated Tax in Lower Local Government: A Case Study of Mukono District.

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DEDICATION

This report is dedicated to Compassion International for educating me right from primary up to university, my uncle and brother for taking care of me after the death of my mother and my supervisor Prof. Foster Byarugaba for the guidance and support given to me during the compilation of this report.

God bless you so much!

DECLARATION

I, Ndawula James, declare that the work presented herein is my original work and has never been presented any where for the award of a degree in any institution or University whatsoever.

Signed…………………… Date……………………….

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STUDENT

Signed…………………………… Date……………………………

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I thank the almighty God for keeping me alive as well as giving me the necessary resources that have enabled me complete this report successfully.
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Thank You All For Being a Blessing to Me at the University!

LIST OF ACRONYMS

CAO	Chief Administrative Officer
CBOs	Community Based Organizations
CFO	Chief Finance Officer
CSC	Community Services Charge
CSO	Civil Society Organization
FREQ	Frequency
FY	Financial Year
GPT	Graduated Personal Tax
GT	Graduated Tax
HLG	Higher Local Government
LCs	Local Councils
LLG	Lower Local Government
LLGs	Lower local governments
LGs	Local governments
LGDP	Local Government Development Program
LGFC	Local government finance commission
LRR	Locally Raised Revenue
MOLG	Ministry of local government
NAADS	National Agricultural Advisory Services
NGO	Non government organization
NO	Number
PAF	Poverty Alleviation Fund
PAYE	Pay As You Earn
%	Percentage
PMA	Plan for Modernization of Agriculture
UBOS	Uganda Bureau of Statistics

UPE	Universal Primary Education
URA	Uganda Revenue Authority
VAT	Value Added Tax

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ABSTRACT

The objective of the study was to assess the effects of the suspension of graduated tax in the lower local governments. The findings reveal that GT formed a major source of the local revenue collection and this made it easy for the lower local governments to deliver some services to the people without depending so much on the central governments as it is today. GT was used to fund schools (both government and private), pay workers, garbage collection, routine road maintenance, buy medical equipment and furniture among others. GT was crucial for the functioning of lower local governments. Its suspension brought a very big task of finding about 59.0 billion Uganda shillings to replace it.

With the suspension of GT, there were many negative effects that were faced by the lower local governments and these were: failure by the local councils to effectively collect garbage, low tax bases, council budgets were affected leading the councils to leave out some activities like contributions to the youths and the disabled, poor revenue generation, introduction of indirect taxes which are in a form of increased prices of various commodities like fuel and others. In order to minimize the effects associated with the suspension of GT, the researcher recommends that new sources of revenue for the lower local governments should be established. These include land tax, property tax, parking fees, taxes on charcoal and cattle, introduction of indirect taxes on essential household consumption, VAT, introduction of local government matching grant and others. However, the researcher suggests that the new introduced taxes should have a wide tax base, be acceptable and should be easy to collect in order to avoid the weaknesses that were associated with GT that led to its suspension. The dissertation is presented in five chapters.

CHAPTER ONE

1.0 DECENTRALIZATION

Decentralization is the transfer of responsibility for planning, management, and resource raising and allocation from the central government to field units of central government ministries or agencies, subordinate units or levels of government, semi-autonomous public authorities or corporations, area-wide regional or functional authorities, or organizations of the private and voluntary sector.(Rondinelli, D. 1981).

The process of decentralization in Uganda traces back to the establishment of the Resistance Council System in 1986 on-wards. In October 1992, the President launched the decentralization programme. Since then, the policy of decentralization has been included in the new Ugandan Constitution, and in 1997, a Local Government Act was enacted. These two legal instruments have dramatically changed the central government framework within which its local governments operate. It is expected that districts, under decentralization, will have more power, resources, more responsibilities and more decision-making autonomy. Also, their performance will thus be increasingly important for growth, poverty eradication and long-term rural development prospects.

After the launching of decentralization in October 1992, 13 pilot districts became decentralized. Their performance led to the enactment of the Decentralization Statute of 1993. To harmonize the provisions of the Constitution of 1995 with decentralization, the Local Governments Act was passed in 1997. The Local Government Act of 1997 gave effect to the implementation of decentralization. The emphasis of the Act is to devolve powers to the district and the lower levels of local governments and the democratization of decision-making. Under the Act the district and the sub-county have been made local governments that are body corporate, capable of suing and being sued. They are no longer required to forward their budgets to the minister for approval. The councils, themselves, have complete responsibility for their budgets. The centre no longer approves bye-laws of these local governments. Except if such bye-laws are not consistent with the constitution or any other law made by the legislature.

The minister responsible for local governments has no powers to terminate the mandate of a councilor. The revocation of a mandate of a councilor is constitutionally vested in the electorate who can initiate the removal of any councilor through petitioning the Electoral Commission. Neither does the minister have powers to dissolve councils-until their statutory term of office expires. This can only happen when it is clear that a council is unable to exercise its duties. When such a situation arises, the President, with the approval of two thirds of all members of parliament, assumes the executive powers of any district.

But the following conditions must first be met: Where the district council so requests and it is in the public interest to do so, where a state of emergency has been declared in that district or in Uganda in general (Mtafiti Mwafrika: 1999) and where it has become extremely difficult, or impossible, for a district government to function. These administrative changes are supposed to enhance local autonomy and bring decision-making at the place where people affected want it, including the decisions in district human-power development.

1.1 ASPECTS OF DECENTRALIZATION

The different aspects of decentralization include: fiscal decentralization, post-constitutional regulatory decentralization and constitutional decentralization.

Fiscal decentralization

Fiscal Decentralization refers to an intergovernmental system where the balance of power moves towards the sub national government sector. (www.jposc.org).

Principles of Fiscal Decentralization

The assignment of expenditure responsibilities to different government levels i.e. what are the functions and expenditure responsibilities of each level of government?, The assignment of tax and revenue sources to different government levels i.e. once sub-national governments are assigned certain expenditure responsibilities, which tax or non-tax revenue sources will be made available to sub-national governments in order to meet those responsibilities?, Intergovernmental fiscal transfers i.e. in addition to assigning revenue sources, central governments may provide regional and local governments with additional resources through a system of intergovernmental fiscal transfers or grants, Sub-national borrowing i.e. local governments can borrow (in a variety of ways) to finance revenue shortfalls.

1.2 FISCALTRANSFERS

In Uganda central government transfers to LGs began in the FY 1993/94, as part of the decentralization process. All local governments in Uganda were receiving block grants, from the central government by 1995/96. These grants were meant for the different services that were devolved to the Local governments. The size of LG share of the total public sector has increased significantly along with the transfers of new tasks and responsibilities from central to local governments.

Over the last seven years transfers from the central to local governments are estimated to constitute about 36.3 % in FY 2002/03.

If one is to use the indicator of share of local government transfers as a percentage of the national budget, Uganda is very far ahead and it could claim to be one of the most decentralized countries in Africa. According to the 1995 Uganda Constitution, Article 193, financial grants are classified as Unconditional, Conditional and Equalization Grants. The Constitution under Article 193, stipulates that:

Unconditional grant is the minimum grant that shall be paid to local governments to run decentralized services and shall be calculated in a manner specific in Seventh Schedule to this Constitution, **Conditional grants** shall consist of moneys given to local governments to finance programs agreed between the Government and the local governments, and shall be expended only for purpose for which it was made and in accordance with the conditions agreed upon, **Equalization Grant** is money to be paid to local governments for giving subsidies or making special provisions for the least developed districts, and shall be based on the degree of which a local government unit is lagging behind the national average standards.

1.4 LOCAL REVENUE SOURCES

A tax base, which is capable of sustaining national economy, should be able to sustain national requirements of production, distribution and consumption of both public goods and services. As you all know, the professional middle name of Uganda's Economy is "Professor Lack of Resources". This problem of lack of resources, budget deficits, budget cuts and unfulfilled pledges of public works or private bailouts are too well known and are too many to list here. What this emphatically means is that the Uganda Tax base is insufficient to sustain its economy. Below are some of the major sources of local Revenue.

Taxation

Local Governments generate local Revenues through taxing different businesses such as markets, schools, hospitals, tenders depending on the possessions or what they have in their localities.

Borrowing

At times when local governments can not raise enough Revenue to finance the delivery of social services, they can resort to borrowing though this may be done through the central Government and such sources they can borrow from may include the World Bank.

Investment

This ensures viability of the investments (Higher returns on the investment capital). When we have a lot of investments like industries, hospitals in Mukono District, it means that all these investments are taxable whereby in the end we can generate local Revenue that can fund the delivery of services within the District. This will in the end solve some of the financial challenges the District is going through and in the end increase the level of local service delivery.GT is supposed to be the most important internally generated source of revenue for local government.

1.5 GRADUATED TAX

Graduated tax (http//www.kcc.go.ug) is defined as the head-cum-property tax which was paid annually after assessment. (Davey, 1974) Graduated Tax (GT) has a long history in Uganda and is a successor of the Hut tax introduced during colonial times. It was introduced in Uganda at about 1900. It evolved from hut tax (1900) to poll tax in 1905. Both taxes were paid to central government at flat rates in a bid to increase progressiveness in the tax.

In 1954 GT was introduced for all local authorities in Uganda. Since then, Graduated Tax (GT) has had its roots in Uganda. It was started by the colonial government as a hut tax in 1900 and later in 1953 transformed to GT in a bid to increase progressively and allow those with higher incomes to contribute to the cost of provision of services at the local level. The Uganda protectorate agreement signed in 1894 between Sir Gerald Portal (then the British commissioner to Uganda) on behalf of the British Crown and Kabaka Mwanga of Buganda appears to have been the start of central government and local government structure.

GT was assessed and collected by local governments under the Local Governments Act 1997:148 and was (Godfrey Baiigwa, Policy brief NO1:2) payable by every able bodied male adult, and women who were in gainful employment. Note that it did not matter whether a male was employed or not. In practice most women did not pay this tax unless they were in formal government or private sector. There were two preconceived objectives for this tax system; Raising revenues for local services and bringing Africans into a monetary economy by pushing them to seek employment to get money to pay these taxes. A prelude to the tax was when the Colonial administrators instituted a system of compulsory physical contribution to public works for all adults.

Women were eventually exempted on account that they were already involved in a lot of domestic works. The option of paying cash instead of physical works encouraged or assuaged the majority of the peasant natives to increase output from their farms and to sell surplus to markets and pay taxes rather than do manual labour which would usually be long hours and whose value was difficult to quantify.

The outcomes of these activities were increased crop production, particularly after the introduction of cotton and coffee in most areas of Uganda. In turn this output supported industries in Britain.

To ensure adequate Tax compliance, the colonial government relied upon local chiefs for tax collection who in turn applied the carrot and stick approach. On what became the downbeat side of tax policy, defaulters would be exposed and subjected to embarrassment and humiliation. They would be bundled on a single rope, stripped half-naked and taken around the villages.

This did not only embarrass them but also their entire families, including wives and children. On the extreme, defaulters were committed to jail terms, which involved hard conditions and forced community labor in government plantations and public infrastructures like roads. Jail terms resulted into family break ups and other social stress on women and children. Peasants soon realized that to avoid being subjected to this shame it was better to devote energies in their own gardens or seek employment.

This revenue Mobilization strategy was eased and popularized by an effective sensitization campaign by the colonial chiefs among peasants.

They were made to believe and actually appreciate that their tax was after all put to proper utilization in provision of essential social services like health, civil servants' salaries, maintaining law and order as well as road construction. When Peasants physically saw government services, they came to appreciate the tax. There was service visibility and low incidences of corruption and theft of taxes and this popularized the tax.

Without widespread corruption, (only a few cases of corruption existed among the local chiefs, and even then such cases never came to the peasants' knowledge) and

good accountability and governance, those who resisted were regarded as saboteurs of development, especially under colonial Kingdom systems.
There was no more respect and sympathy for defaulters. Failure to pay was seen as spite for the powerful chiefs or Kings. With public sympathy and support among peasants, it became part of the people's culture to oblige with the policy. It is also possible that the support was due to lack of knowledge about possible misuse of tax money by chiefs. For example there were persistent attempts by the colonial regime to audit Mengo's books of accounts. Mengo Ministers rejected it for fear of public exposure. In 1923 for example, Kabaka's chiefs became transferable resulting in unprecedented rise in revenue, an increase by three fold. (LGFC)

However, as long as service delivery continued to flow, the peasants never saw any reason to default the tax, which became to be perceived as part of their culture. Worth of noting is that this tax was properly evaluated and assessed. Chiefs used to count coffee trees and animals in case a person had any and reached a proper income level of an individual in an open forum. Since the tax imposed was perceived to be proportional to one's income, peasants found it most convenient to comply.

Payment coincided with the season whereby farmers sold their crops, deducted tax payments, domestic needs and paid their laborers who also were able to pay graduated tax. This created an automatic relief when crops failed. In 2005, the Government of the Republic of Uganda suspended Graduated Tax. This was because although Graduated Tax was the main source of revenue for the Local Governments, contributing more than 80% of all local revenues, it was seen as regressive to the poor.
The suspension of GT was a major challenge to local governments since it was its major source of internal Revenue. This study is therefore about the effect of its suspension in Mukono district.

1.6 STATEMENT OF THE PROBLEM

GT was the most important source of Revenue, it accounted for 7,797,259,792/= from 1999/2000 to 2004/2005 financial years in Mukono District when it was suspended. Its suspension therefore was likely to have significant effects not only on the autonomy of local governments but also their capacity to plan according to their own needs and also to provide social services.

1.7 OBJECTIVES OF THE STUDY

1.7.1 GENERAL OBBJECTIVE

To assess the effects of the suspension of GT on social service provision in Mukono

1.7.2 SPECIFIC OBJECTIVES

1. To understand the percentage contribution of GT in Mukono before it was suspended
2. To examine the major services funded by Revenue from GT.
3. To Assess peoples' attitudes towards the suspension of GT in Mukono
4. To Evaluate alternative sources of local Revenue

1.9 SCOPE OF THE STUDY

In terms of scope, the study was carried out in Mukono District. Mukono District was chosen because it is one of the peri-urban Districts located in central Uganda. This helped make good generalizations of the findings to the rest of the country as data was collected from both rural and urban areas.

The study took a period of four months i.e. from may 2007 to September 2007. This was sufficient time to collect data in the chosen sub counties. The sub counties were

Lugazi, Kawolo, Njeru, Ngogwe, Kasawo and Seeta-Namuganga. These sub counties chosen were both urban and rural and were randomly chosen.

1.10 JUSTIFICATION OF THE STUDY

Three points justify the need to study this problem:

The study will help decision makers to learn the new possible sources of the local revenue to replace Graduated tax.

The study will also provide information on the hardships and copying mechanisms after graduated tax suspension in the Lower Local Government of Mukono District. Although the study will be located specifically in Mukono District, the information/findings will be generalisable to other Districts in Uganda since they have similar conditions.

The study will advise policy makers to always critically evaluate the consequences of the new policies they initiate before passing them for implementation. A fire brigade approach to public policy making should be avoided in future.

CHAPTER TWO

LITERATURE REVIEW

2.0 INTRODUCTION

This chapter examines the underlying debates supporting and opposing fiscal decentralization, benefits of fiscal decentralization, the theoretical frame work for fiscal decentralization, debates and policy issues concerning Graduated tax.

2.1 FISCAL DECENTRLIZATION

The main aim of fiscal decentralization is to ensure that at all levels of government there are sufficient financial resources to match the responsibilities assigned to each level of government. Allocating local sources of revenue to local governments that can yield sufficient revenue to meet their expenditure needs would be the ideal solution. These are referred to as local/own sources of revenue.

In reality however, this is not practical. This is because the revenue/tax bases are not uniform countrywide. Charging local governments with the task of locally mobilizing all the revenues they need would result into significant differences in revenues per capita mobilized and thus, in the ability of the various local governments to finance service provision in their jurisdictions.

Secondly, for reasons of maintaining macroeconomic stability, it is essential for the centre to retain a significant level of influence on the amount of public revenue raised. This can only be done by maintaining central mobilization of revenue from some of the taxes. Thirdly, given the nature of their bases, some taxes can only be collected efficiently and cost-effectively by the centre for example import duty.

In essence therefore, tax administration and collection should only be decentralized if the nature of their bases is such that:-

- Local governments are in a better position (to ensure compliance) to collect revenue from these sources as compared to the central government e.g. market dues.
- They promote horizontal fiscal balance. That is, they do not, significantly, introduce inequities in the level of local revenues mobilized by the local governments.
- They promote vertical fiscal balance by strengthening local fiscal autonomy. This means that yields from those taxes are relatively high while the costs of administration and collection remain relatively low.

For the reasons mentioned above, it is not possible to decentralize completely, revenue mobilization. A significant amount of public revenue will continue to be mobilized centrally.

Hence, a System of Intergovernmental Fiscal Transfers has to be put in place to ensure that some of the centrally mobilized revenues are passed onto the sub-national governments for subsequent allocation and management. These transfers are in form of central grants. Central grants can be used effectively to offset differentials in tax bases thereby promoting vertical and horizontal equity.

For such a system of fiscal decentralization to be successful, it must conform to the principles that:-

- The fiscal autonomy of Local Governments is strengthened without ceding central ability to ensure macroeconomic stability.
- Horizontal equity is established without killing off local initiative in revenue generation.

- Vertical equity is established without impairing the ability of Central ministries to perform their role of policy formulation, monitoring and evaluation as well as quality assurance.

2.2 ARGUMENTS FOR FISCAL DECENTRALIZAYION

The theoretical case for fiscal decentralization dates from 17th and 18th Century philosophers, including Rousseau, Mill, de Tocqueville, Montesquieu and Madison. Central governments were distrusted and small, democratic governments were seen as the principal hope to preserve the liberties of free men (Faquet, 1997). The modern case for decentralized government was articulated by Wolman (in Bennet, 1990). Wolman divided the proponents' arguments under two headings: Efficiency Values and Governance Values.

Efficiency Values

Efficiency is an economic value seen as the "maximization" of social welfare. The public sector does not contain the same price signals as the private sector, to regulate supply and demand. Public sector allocation of goods and services are inherently political; however, as nearly as possible tax and service packages should reflect "the aggregate preferences of community members." (Wolman 1997, p. 27)

However, within any political jurisdiction, some people will prefer more, some less, public services. As a result there is a "divergence between the preferences of individual community members and the tax and service packages reflecting the aggregate community preferences" (Ibid). Since such divergence reduces social welfare, it is desirable to hold those to a minimum and they will be less in smaller communities (e.g., municipalities) than in larger, more heterogeneous areas (the nation).

Governance Values

Governance values include responsiveness and accountability, diversity, and political participation (Wolman, 1997). Decentralization places allocation decision making closer to the people. This fosters greater responsiveness of local officials and greater accountability to citizens. This is because we expect local decision makers to be more knowledgeable about the problems and needs of their local area than centralized decision makers. Further, to the extent that there is accountability through local elections, those elections are more likely driven by issues of local allocation, whereas national elections are seldom focused on local service delivery.

Diversity in public policy is a second governance argument for fiscal decentralization. It is valued because it offers citizens a greater choice in public service and tax options when they are deciding where to reside (Tiebout, 1956). In addition, it helps to create "laboratories" for innovation and experimentation, which sometimes serve as models for later implementation by the central government or by example to other local governments. While there is no theoretical reason why a central government could not be diverse in its solutions, there is great pressure on the central government towards uniform policies and procedures.

Finally, fiscal decentralization is thought to enhance political participation at the local level. This has the potential to enhance democratic values and political stability at the local level. It provides a forum for local debate about local priorities, and can be a proving ground for future political leaders.

Bahl (1999b) argues that in developing countries personal income taxes are primarily wage taxes that can be monitored and enforced at the local level. A compromise model would have the central government be the principal actor with local governments piggybacking a local rate and possibly collecting the tax.

The VAT makes a good shared tax. It can be collected at either the national or regional level. It is more stable than the income tax and thus provides a more assured revenue stream for regions and/or local Governments. Sharing natural resource taxes is appropriate because in one sense oil, gas and coal reserves are a national resource; yet, in another sense, the exploitation of those resources imposes costs on local governments. What does not seem appropriate is windfall profits to one region at the expense of other regions.

The property tax is a good local tax. Real property is immobile and local assessment of valuation is appropriate. Business taxes, charges and fees are often closely related to specific services provided by state or local government and thus are good from a standpoint of allocation efficiency. Some would argue against allowing state or local gaming taxes because it leads to exportation of local taxes (and hence lowers the real price for local services); however, there are governmental costs associated with this revenue source.

Regional governments might rely on a piggybacked source of revenue, such as on a national income tax or VAT, or on excise taxes (gasoline, alcohol and tobacco, for example).

2.3 BENEFITS OF FISCAL DECENTRALIZATION

During the last decade, there has been a tendency towards regional and economic integration. The most prominent example is certainly the European Union, granting free migration of goods, services, capital and labor since the Single Market was established on January 1st, 1993. Enhancing the mobility of goods and factors, liberalization is expected to improve the allocation of resources. However, increasing economic integration also means an increasing mobility of tax bases.

Authors like Oates (1972), Wilson (1986) and Zodrow and Mieszkowski (1986) emphasize that governments provide an inefficiently low level of local public goods in response to tax competition. On the other hand, tax competition serves to limit the taxing power of politicians who, following Niskanen (1971), seek to maximize their tax revenues. This argument brought forward by authors like Brennan and Buchanan (1980) and McLure (1986) is in remarkable contrast to the first one.

However, on closer inspection these sharply differing views reflect equally different perceptions of government policy–making. While the first strand of literature assumes that governments are benevolent utility maximizers, the Leviathan government is supposed to be wholly self–interested. In a recent study Edwards and Keen (1996) try to reconcile both views by assuming that governments are neither entirely benevolent nor fully self–interested. In this framework, starting from a non–cooperative equilibrium, they analyze whether a representative citizen benefits from or is harmed by some degree of tax coordination. They conclude that it is an empirical question whether less tax competition, that is, less fiscal decentralization, is beneficial or not.

The gains of an increased supply of public goods must be compared with the disadvantage of weaker competition among self–interested policy–makers wasting tax while using a similar model, this study reveals an important condition for welfare gains of fiscal decentralization. Governments must be constrained to finance their See, for instance, OECD (1992), Owens (1993) and Sorenson (1994). Expenditures by a tax on a mobile factor like capital. If politicians have an undistortive tax at their disposal they will abstain from taxing mobile factors in the case of identical regions.

Hence, as emphasized by authors like Sinn (1997) and Wellisch (1999) there is in fact no tax competition and no welfare gain of fiscal decentralization. This, in turn, is in sharp contrast to the conclusions drawn in the literature analyzing the behavior of entirely benevolent governments. There, the condition that policy–makers are able to levy undistortive taxes is necessary to ensure that decentralized decision making results in an efficient allocation. If, on the contrary, politicians are partly self–interested, the absence of undistortive taxes is a necessary condition for fiscal decentralization being beneficial. In addition, if the gains of limiting the taxing power dominate the negative effect of under provision of public goods, tax competition is in the interest of the citizens.

2.4 THE THEORETICAL FRAME WORK FOR FISCAL DECENTRALIZATION

The "proper" distribution of tax authority and expenditure responsibility is an extremely complex issue. Economists generally focus on issues of efficiency and equity, while public administration and political science scholars tend to focus on distribution of powers, responsiveness and accountability, and tax competition and coordination. Economist Richard Musgrave's framework for analyzing roles or functions is widely accepted (Musgrave, 1959, 1961; see also Oates, 1977).

The Stabilization Function involves the role of tax and spending policies and monetary policy in managing the overall level of economic activity. It is widely agreed that this macroeconomic function should be assigned to the national government. This suggests that the national government must have a broad-based tax suitable for this role.

However, Oates' (1993) analysis of 58 countries demonstrated a positive relationship between economic growth and fiscal decentralization suggesting some role for local governments, especially infrastructure development.

The Distribution Function involves the role of government in changing the distribution of income, wealth or other indicators of economic well being to make them more equitable than would otherwise be the case. The case for assigning this function to the national government rests on two assumptions: 1) that the national government's broad taxing powers can more easily redistribute income; and 2) that the ability of taxpayers to move from one jurisdiction to another to take advantage of more attractive spending and taxation policies weakens local government's ability to "soak the rich and redistribute to the poor." The case for regional and local redistributive policies rests on the fact that sub national levels of government provide the services most used by low-income families. However, most economists view the national role as primary.

The Allocation Function is government's role in deciding the mix of public and private goods that are provided by the economy or by government. Each level of government may be more efficient in delivering certain governmental goods and services. The superiority of the national government in delivering national defense or national health research is obvious as is the likelihood that certain services such as fire and police protection are more suitable for local government. In attempting to match local revenues and expenditures in the allocation process, economists are concerned about efficiency, vertical imbalances (mismatches between revenues and expenditures), horizontal equity (fiscal capacity among regions), externalities (spillovers), and tax exportation.

Additional public management concerns have to do with overlapping of taxes and roles, and responsiveness and accountability for service delivery.

This framework is most helpful in thinking about which taxes are levied at each level of government and the total tax authority of each level. A commonly cited public finance principal is "finance should follow function." If certain expenditure roles are assigned to a level of government, that level must have the resources to meet those responsibilities. Taxes are the principal source of "own-source" revenue for governments at all levels. If tax collections or fiscal capacity falls short expenditure responsibilities, then that level of government must have additional taxing authority, develop user fees, or rely on intergovernmental transfers (such as grants and shared taxes) to support its expenditures.

2.5 FISCAL DECENTRALIZATION: THEORY AS REFORM

The last decade has seen a renewed interest in the concept of fiscal decentralization or fiscal federalism. This comes after a half-century of fiscal centralization in most developed and developing nations.

Fiscal Decentralization also has become part of a world-wide "reform" agenda, supported by the World Bank, USAID, the Asian Development Bank, and many others, and has become an integral part of economic development and governance strategies in developing and transitional economies (Bahl, 1999a). Along with "globalization," fiscal decentralization and the desire for local discretion and devolution of power is seen by the World Bank as one of the most important forces shaping governance and development today (World Bank, 1999).

Fiscal decentralization is the devolution by the central government to local governments (states, regions, municipalities) of specific functions with the administrative authority and fiscal revenue to perform those functions.

The theoretical case for continuing the efforts to find the right mix of tax and revenue sharing for sub national governments is the following.

When regional and local governments are involved in financing their own expenditures, at least at the margin, they will be more accountable to their citizens (and the central government) for the efficient delivery of public services. In contrast, when the bulk of financing of local services comes from revenues transferred from a higher level of government, local governments are less likely to be parsimonious with those expenditures. Thus, tax sharing formulas need to be constructed in a fashion that encourages (or at least does not discourage) local governments from developing their own-source revenues.

The case for local tax administration and at least some local discretion on tax rates is to place greater responsibility on local government to collect taxes owed and to use discretion as to tax rates to provide discretionary services or to use for economic development purposes. The goal is to provide the greatest stake in the success of local governments with the local officials and to take away the excuse that they are "bound" and therefore unfairly limited by national legislation.

Why interest in fiscal decentralization as reform? There are three basic reasons:

- Central governments increasingly are finding that it is impossible for them to meet all of the competing needs of their various constituencies, and are attempting to build local capacity by delegating responsibilities downward to their regional governments.
- Central governments are looking to local and regional governments to assist them on national economic development strategies.
- Regional and local political leaders are demanding more autonomy and want the taxation powers that go along with their expenditure responsibility.

Fiscal decentralization is now seen as part of a reform agenda of many nations to strengthen their regional and local governments to meet the challenges of the 21st Century.

2.12 PERSPECTIVES ON GRADUATED TAX

The quid-pro-quo approach

The quid-pro-quo approach on taxation rests on the notion that taxation systems are based on reciprocity between taxpayers and authorities. It is argued that since tax enforcement is costly, rulers are likely to encourage situations in which tax payers choose to pay voluntarily and only if they do not pay, they will be forced to do so by coercion. This is what has been termed as quasi-voluntary compliance.[1] It is argued that revenue production is a result of a bargaining process in which a fiscal contract is written. Hence if rulers fail to deliver on the part of the bargain, tax defection is likely to increase. To ensure voluntary compliance to it, tax administrators need to provide reassurance of provision of services. Non-compliance will therefore increase if tax payers begin to feel that their taxes are misused or end up in the hands of a relatively small group of people who misuse them. Similarly, compliance may result from a sense of paying relatively high tax compared to income.

Moore also advances a reciprocal relation between the tax payer and administrator[2]. Moore argued that earned income tends to foster improved accountability relations between citizens and government. The extent to which a governments' income is earned depends on (i) the organisational and bureaucratic effort by the state to raise revenues and (ii) the degree of reciprocity between citizens and the state, i.e. real services in exchange for tax payment. Moore further contends that if the state depends

[1] Margaret Levi, (1988) Of Rule and Revenue, Berkeley: University of California Pres [1] See article 191 of the 1995 constitution and The Local Government Financial and Accounting Regulations, 1998

[2] Mick Moore, (1997) "Death without taxes: Democracy, state capacity and aid dependence in the fourth world," In Gordon White and Mark Robinson eds., *Towards a Democratic Developmental State* (Oxford: Oxford University Press)

upon its citizens for income, it will tend to secure compliance through the establishment of negotiated, reciprocal relations in which tax payers receive a return.[3]

In Mukono a quid-pro-quo explanation appears highly plausible, since revenue collection in the district declined over time as services also declined. The colonial administration did not use this perspective because its objectives were different in that they wanted to ensure that graduated tax contribute to the cost of provision of services at the local level.

The institutional approach on taxation

The institutional approach is based on the underpin that Institutional choices affect present choices about tax policies and their implementation. According to Steinmo the configuration of political institutions for tax policy matter for the kind of tax system adopted. Institutions are both formal organisation and informal rules and standards operating procedures that structure individual relationships[4]. To Steinmo, the reciprocity element is not essential. The fact that citizens want higher public spending and lower taxes (even if services were improved they would be willing to pay taxes).

Steinmo explanation is based on the post-war era in Europe where citizens were not interested in paying taxes, partly because they did not have the resources to do so. It is also important to note in the case of Uganda that institutions that are charged with taxation and tax policy formulation are neo-patrimonial in nature and normally represent interests of the political elites not the general citizenry.

[3] ibid
[4] Sven Steinmo, (1993) *Taxation and Democracy: Swedish, British and American Approaches to Financing the Modern State*, New Haven: Yale University Press

Similarly as Van de Walle contends low taxes in Mukono can be partly explained by corruption in the institutions mandated with tax collection and administration[5]. What the institutional approach helps us to understand is power institutions have over taxation. In Uganda this was clearly displayed by the president in 2005, when he suspended GT. It is imperative to note that institutions in Uganda represent interests of political elites, as already mentioned. Because of this their work is structured around the interests of the political elites. The outcome of this same is intended to appease the political elites not the citizens. As such payment of taxes is not seen as benefiting the citizens but the political elites who can decide on the usage of the same taxes. Indeed when GT was suspended there were a number of consequences in Mukono district, especially how the district was to deliver services. It is true in Mukono that the taxation policies represent the political elite as the citizens in the district were not consulted on the likely consequences of the suspension of graduated tax and in addition, there was a lot of corruption in the process of collecting G.T. by the tax collectors were by some of the money that was collected went in the pockets of its collectors which was not the perspective during the colonial administration whose aim was to see G.T. collections benefiting the citizens through local service financing/provision.

Traditional theory

The traditional theory of public finance has made a strong case for a major role for fiscal decentralization. This case is based on an improved allocation of resources in the public sector. And it has four basic elements. First, regional or local governments are in a position to adapt outputs of public services to the preferences and particular circumstances of their constituencies, as compared to a central solution which

[5] Nicolas van de Walle, "Economic reform in a democratizing Africa," *Comparative Politics*, 32, 1 (1999), 21-42 Cambridge: Cambridge University Press

presumes that one size fits all. Second, in a setting of mobile households, individuals can seek out jurisdictions that provide outputs well suited to their tastes, thereby increasing the potential gains from the decentralized provision of public services (Tiebout 1956). Third, in contrast to the monopolist position of the central government, decentralized levels of government face competition from their neighbors; such competition constrains budgetary growth and provides pressures for the efficient provision of public services. And fourth, decentralization may encourage experimentation and innovation as individual jurisdictions are free to adopt new approaches to public policy; in this way, decentralization can provide a valuable Laboratory for fiscal experiments. However, this basic economic rationale for decentralization of the public sector is not quite so simple and compelling as it appears. Some of the more recent literature provides, first, a thoughtful and provocative critique of the traditional view of fiscal decentralization, and, second, some new approaches that reveal its dark side, especially in practice. There is emerging, in short, a broader perspective on fiscal decentralization that raises some serious questions about its capacity to provide an unambiguously positive contribution to an improved performance of the public sector.

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 INTRODUCTION

This section gives the methodology, which was used in the study. It outlines the research design, study area, population, sampling procedure, and methods of data collection and data analysis.

3.1 RESEARCH DESIGN

The researcher used a case study research design while carrying out research. A case study can be defined as an intensive investigation of a particular unit under investigation.

A case study is used by choosing one specific area and studying it intensively and exhaustively and thereafter generalizes the findings. The researcher used a case study because it enabled the generalization of the findings to other districts and eventually to the whole country and in addition to that, the study can use more than one method for data collection.

3.2 GEOGRAPHICAL AREA OF STUDY

Mukono district lies in the central region of Uganda, sharing boarders with the districts of Jinja in the East, Kayunga along river Sezibwa in the North, Luwero in the North West, Kampala and Wakiso in South West, Lake Victoria in the south with the Islands of Koome and Buvuma as part of the district. Its district headquarters are in Mukono town, situated along Kampala-Jinja road (21kms East of Kampala City).

Mukono town serves as an administrative and commercial center and other urban centers include Lugazi, Njeru, and Nkokonjeru town councils. The District has four counties namely: Nakifuma, Buvuma Islands, Mukono and Buikwe, 28 sub counties, 144 parishes and 119 villages. The study was carried out in the sub counties of: Lugazi, Kawolo, Njeru, Ngogwe, Kasawo and Seeta-Namuganga. The sub counties visited were chosen randomly and four sub counties were chosen so as not have a very big area of coverage that could not be covered while collecting data.

3.3 TOPOGRAPHY OF MUKONO DISTRICT

The northern part of the district is flat but the southern region consists of slopping land with great many undulations; 75% of the land is less than 60 degrees in slope.

Knowing the Topography of the district helped the researcher know the nature of the land for easy movements as well as knowing the climatic conditions for easy accessibility of respondents.

3.4 THE STUDY POPULATION

The study focused on the chairpersons, councilors, the finance sections, and other administrative staffs.

3.5 SAMPLE SIZE AND SAMPLING PROCEDURE

Because this was a case study, a sample size of 42 respondents was considered where by 7 respondents were randomly selected from each sub county that is Lugazi, kawolo, Njeru, Ngogwe, Kasawo and Seeta-Namuganga using simple random sampling. The information obtained was used to generalize to the rest of other lower local governments. Both qualitative and quantitative data were collected and thereafter the Data was analyzed.

3.6 DATA COLLECTION TECHNIQUES

In terms of data collection, the study used both qualitative and quantitative data collection methods. Qualitative methods were used in collecting data that did not have figures and where applicable, tables were used to present quantitative data. The study used the following different methods namely:

Documentary, the study looked at the documents concerning taxation (primary and secondary) as the first source and tool of information. Such tools included and not limited to, policy statements, press statements in newspapers and journals, ministry of local government reports and other statutory instruments and thereafter wrote down the findings.

Interviews, the study carried out face-to-face interviews to respondents who were easily accessed (an average of six interviews were carried out per day) and written interviews in form of self administered Questionnaires to respondents who were not easily accessed due to their busy schedules. Some respondents wrote down the answers on the questionnaires and pieces of papers that were provided by the researcher and handed in the filled in questionnaires at the end of the day and there after the researcher scrutinized them.

3.7 DATA ANALYSIS AND PRESENTATION

After data collection, different types of data were compiled and there after, a content analysis was done. For the quantitative data, descriptive statistics was presented in a table form while in the qualitative data questions that were not well answered, the researcher sought clarification from the respondents and those ones with accurate answers were considered with no further clarification. Findings were also presented and discussed.

3.8 ETHICAL CONSIDERATIIONS

The researcher made sure that he gets the consent of the respondents first while carrying out research. The researcher also made sure that he does not force respondents to give him answers as well as maintaining the confidentiality of the answers they gave him in the process of data collection. In addition to this, he made sure that he collects data at the respondents' convenient time.

Time Frame

This research was carried out with in a period of four months.

3.9 PROBLEMS ENCOUNTERED IN THE STUDY

Some respondents were too busy. This made the researcher travel several times to their offices hence costing a lot of time and money, at times the researcher was even made to sit and wait for longer hours. The frequent postponement of meeting busy respondents made the researcher incur more costs that were not budgeted for.

The researcher had to look for more money to cater for other days he traveled which had not been budgeted for and in addition to this, he had to follow the schedule given to him by the respondents and he was patient to wait until was attended to.

Some respondents were not willing to release certain information especially in the finance departments this affected the researcher in that he had to spend more time than anticipated explaining to the respondents the significance of the study and there fore this was resolved by the assuring the respondents that information obtained from them will be for academic purposes only.

The researcher did not have enough money by the time data was collected and the increment in the days to meet respondents as a result of some respondents telling him to come some other days even made it worse. This was solved by the researcher getting a loan from friends whom he had to pay back after a certain period of time.

It was hard to collect data from some respondents as most of the time were out of their offices to the fields and this was solved by obtaining data from the district since some data was already submitted there while handing in their budgets for approval and funding. All in all, the above problems encountered did not affect the quality of this study.

CHAPTER FOUR

PRESENTATION AND ANALYSIS OF FINDINGS

4.0 INTRODUCTION

This section presents and discusses the findings from the study. The Discussion is based on three issues. First is the tax revenue collected by Mukono district before and after the suspension of G.T. The emphasis is to establish the financial gap created by GT suspension. Second is a discussion on the effects of GT suspension on service delivery in Mukono district and lastly is a discussion on the copying mechanisms the district has devised in the face of decreasing financial resources. Until 2005 when it was suspended, GT was levied on the basis of the constitution and the Local Government Revenue Regulations.[6] It was calculated on the basis of estimated earnings from agriculture or livestock and annual income if the tax payer was in salaried employment. The tax started as a hut tax that was introduced during colonialism. Improved services in Mukono district might have increased tax compliance especially in the township, while in rural sub-counties poor delivery of services may have rendered it difficult to uphold high tax collections.

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[6] See article 191 of the 1995 constitution and The Local Government Financial and Accounting Regulations, 1998.

4.1.1 Levels of Local Revenue collection before and after Revenue suspension

Table 1: Local Revenue collections at the District before G.T suspension

Financial Year	Total GT Tax Revenue	Totals of other Sources of Local Tax Revenue	Total Local Tax Revenue
1999/2000	1,365,693,362	692,548,442	2,058,241,804
2000/2001	437,631,934	619,794,587	1,057,426,521
2001/2002	529,062,968	575,885,330	1,104,948,298
2002/2003	558,099,300	526,021,298	1,084,120,598
2003/2004	939,648,602	689,396,653	1,629,045,255
2004/2005	888,370,314	918,638,580	1,807,008,894
2005/2006	0	682,776,422	682,776,422

Source: Mukono District Council statements of final accounts

It can be noted from table 1 above that before G.T. was suspended by the central government, Mukono District could raise more money locally to help finance the local services with out waiting much to receive money from the central government. This was because Graduated Tax was a major source of local Revenue generation to the District.

In addition to the above, one of the reasons for the highest contribution of G.T was due the fact that it was a well known tax by all tax payers as they had got used to it and one had to work very hard to see to it that he/she pays before being arrested for non payment. Now that it was finally suspended, the district finds it hard to locally raise revenue and relies much on central transfers yet they have problems associated with them as exposed by this study.

Table 2: Revenue Collections at the District after G.T. suspension

Income	Amount in ushs for 2005/2006	Amount in ushs for 2006/2007	Amount in ushs for 2007/2008
Local revenue	682,776,422	589,358,460	410,623,716
Un conditional grant-district	2,671,253,999	2,238,080,745	3,035,792,843
Graduated tax compensation- district	1,021,252,470	1,318,316,170	397,476,358
Un conditional grant - urban authorities	801,264,111	810,476,000	1,149,859,700
Graduated tax compensation-urban authorities	279,224,681	360,446,331	111,748,370
Conditional grant – wage	14,111,486,021	16,145,947,675	16,788,888,166
Conditional grant – non wage	3,289,986,812	3,666,290,227	3,801,754,911
Conditional grant-development	5,429,863,000	4,982,288,656	4,354,360,555
Donor and NGO funds	1,770,871,570	1,856,046,788	1,038,051,256
TOTAL REVENUE	**30,057,979,086**	**31,967,251,052**	**31,088,555,875**

Source: Mukono District Council statements of final accounts

From table 2 above, it can be noted that ever since G.T. was suspend, local revenues went on reducing in all financial years which creates a big gap of the total local Revenues collected before G.T suspension as compared to the ones collected after its suspension which is not healthy for Mukono district as far as local service delivery is concerned.

In the collection of these taxes, the Lower Local governments found that they could not get 100% of what was expected. The following were the range of reasons respondents gave to explain the poor revenue collection performance in the District; Political pronouncements and interference, each time the District came up with new sources of local revenue generation, the central government especially during campaigning time interfered with the strategies laid down as a way of collecting local taxes. For example that because the central government wanted to win the voters' votes, government abolished some taxes which included taxi and market dues and this in the end made many tax payers resent many of the taxes that were inflicted on them saying that President Museveni removed all the taxes and therefore could not see reasons of paying which made it very hard for the lower local governments to collect taxes hence making local revenues keep on reducing as exemplified in table 2 above.

Problems faced in revenue collection in Mukono District

Political pronouncement or interference which is in most cases through issuing directives of collecting local revenue for example, abolishing many forms of local taxes without consulting sub county officials first e.g. Some politicians from higher offices removed the proposed Boda-Boda taxes without consulting the lower local governments first.

Low motivation of tax collectors, which prompts them to steal the money, they collect. Not enough money to carry out many activities geared towards delivering services to the local people like carrying out immunization and sensitization. This is due to the fact that many sub counties don't go especially to the villages to carry out those activities as there is no facilitation for them for example they are not given fuel to ride motor cycles unless they use their personal money and nobody is willing to use his or her personal money to render services to the community.

Retarded general development, the researcher was told that in Kasawo Sub County, GT made people work because they knew that if they don't work to raise money to pay taxes, they would be imprisoned. With the suspension of GT, people's zeal to work has reduced as many people now spend the whole day drinking saying there is no need to work hard because there is free primary education (UPE), free medical services at the health centers. It has reduced the capacity of sub counties to construct feeder roads, class rooms, provision of clean water through digging shallow wells and motorized wells.

4.1.2 Intergovernmental Fiscal transfers

In Uganda, local governments receive a number of central grants in addition to locally mobilized revenues. These are designed to achieve the three objectives stated above; that is vertical and horizontal equity as well as local autonomy.

Clause 1 of Article 193 of the Constitution of the Republic of Uganda, 1995 states that for any given year, local governments are to receive three grants namely Unconditional, Conditional and Equalization grants. Clauses 2-4 of article 193 define what is meant by each of these.

Unconditional grants are defined as the minimum grant that shall be paid to local governments to run decentralized services and are calculated based on the costs of running those services, Conditional grants on the other hand consist of monies paid to local governments to finance programs agreed upon between the central government and the local governments and expended for the purposes for which they are made and in accordance with the conditions agreed upon. Evident within this law is the need for the centre and local governments to arrive at a consensus through negotiations.

The distribution of Conditional and Unconditional grants as provided for in the definition above does not take into consideration the historical distortions which resulted into unequal distribution of social and economic infrastructure. Secondly, it also does not take into consideration differences in resource endowment among local governments as is evidently the case in Uganda.

In a recent survey made by the Local Government Finance Commission, Chief Administrative Officers (CAOs) confirmed that there indeed existed inequities among local governments. They identified three major factors as the main causes of inequalities among local governments. These were: - uneven social and economic infrastructure coverage, differences in revenue potential/resource base and differences in the demand for the services delivered by them due to differences in their demographic structures.

4.1.3 Inter-Governmental Fiscal Relations:

The decentralization of fiscal authority to lower level jurisdictions contributes to the efficient delivery of public services, but conflicts with national objectives.

Virtually all nations—federal or otherwise—have more than one tier of government, each with its own set of fiscal responsibilities. At the same time, the tiers are inter-connected by a system of fiscal relations. The fiscal relations in various countries generally reflect three common features of multi-tiered government, features that vary in their specifics from one nation to another.

The first common feature is that the provision of many important public services is decentralized to lower tiers of government. Although some of these services are of purely local concern, some of them are of important national concern. Examples include education, health and welfare services. Moreover, this decentralization of expenditure responsibilities is typically not accompanied by equivalent revenue-raising responsibility. There is a vertical fiscal imbalance (VFI) that is covered by transfers from upper-level governments.

The second common feature is that transfers from upper to lower levels of government are typically conditional in nature. The recipient jurisdictions are typically required to use them to meet some objectives of the donor government. This reflects in part the fact that the upper-level government has some interest in the manner in which lower governments carry out their expenditure responsibilities.

The third common feature concerns the equalizing nature of transfers that are used to close the vertical fiscal gap. Relatively more is transferred to those jurisdictions that are less able to carry out their fiscal responsibilities. The extent of equalization includes that arising from the jurisdictional incidence of tax revenues raised to finance the transfers, which falls disproportionately on the better-off jurisdictions. While these three general features—decentralized provision of important public services, conditionality and equalization—characterize the inter-governmental fiscal arrangements. This literature will find out whether this is the case in Mukono District.

4.1.4 Debates and policy issues concerning Graduated Tax

Graduated Tax (G-Tax) has a long history in Uganda and is a successor of the Hut Tax introduced during colonial times (Davey, 1974). It is the most important locally generated revenue source, and is levied on the majority of adult Ugandans. On average, G-Tax contributed about 67% of total own revenues collected in District councils and about a third of revenue collected in District councils and about a third of revenue collected in town councils in 1997/1998-1999/2002 (LGFC,2002).

However, in the election year 2001 there was a substantial drop in the Graduated tax contribution, and the Graduated tax share fell to about 40% of total own revenues in rural councils in 2000/2001. The corresponding figure for urban councils dropped to 18%.

Local councils are in general heavily dependant on transfers from the central level. On average, almost 90% of total expenditures in local authorities are funded by the central government, although this reliance varies among Districts. During the mid 1990s central government transfers expanded in line with increasing responsibilities, and they more than doubled in the four years prior to 1996/97 (Livingstone and Charlton2001:83). At the same time since, the late 1990s there has been a decline in the local revenue generation. From 1997/98 to 2000/01 local revenue declined slightly from about Uganda shillings 45.3 billion (LGFC, 2003).

The drop in the revenue collection for Graduated tax in 2001 was prompted by political intervention during Presidential campaign. The opposition candidate, Kizza Besigye campaigned for the abolition of Graduated tax while President Museveni promised to reduce the minimum level of Graduated tax from Uganda shillings 11,000 per year to 3,000 per year. This political intervention understandably caused confusion among tax payers regarding the legitimacy of Graduated tax.

After the 2001 election, the President's promise was implemented and the minimum Graduated tax rate reduced to Uganda shillings 3,000. This led many tax payers to pay only the minimum rate arguing that the President assessed all of them in 2001 (Bahiigwa et al, 2003). For instance, in Butiru sub county (in Mbale district) and independent of their income levels, over 98% of the tax payers who complied with the tax in 2002/03 paid the minimum rate. However, despite this, compliance was less than 60% in Butiru Sub County in 2002/2003 fiscal year while before the rate reduction it was 90%. This is due to grater resistance to pay Graduated tax by the tax payers combined with lax enforcement than before the election.

A variety of sources including regular news paper articles revealed that, the Graduated tax is in a mess in Uganda. On the one hand, local politicians often discouraged tax payers from paying, especially close to election times. On the other hand extensive use of force in Graduated tax collection had been reported across the country. The suspension of Graduated tax had been raised on several occasions in recent years. In August 2003, some MPs suggested that Graduated tax should be suspended altogether. They argued that Graduated tax was a regressive tax which imposed extra hardships on poor people.
Moreover, it was argued that Graduated tax was costly to administer and implied a double taxation on personal income tax payers in the formal sector who had to pay both PAYE to the central government and Graduated tax to the local authority.

4.1.5 A case in support of Graduated Tax

The arguments in support of continuation of GT were based on the dominant share of GT in local revenue budgets and the perceived absence of immediate viable alternative sources to replace it in a majority of rural districts. The suspension of GT without a viable and acceptable source of revenue would automatically cripple the capacity of local governments to contribute towards sustaining the policy of decentralization and service delivery unless there was a commensurate plan to compensate the loss with real transfers from the Government.

The need to finance local administration and political representation

GT had to be retained so as to meet the need for the Public to finance and maintain Local Administration and Political Representation. The biggest portion of local revenue was allocated towards expenditures on political representation (Councilors' allowances and emoluments of the Chairperson and Executive Committee) and cost of local administration (Offices of CAO, CFO, Heads of Departments and payment of salaries).

Although it may be argued that this expense was at the cost of services, political representation at the local level was the important pillar of good governance. The local leaders were responsible for the formulation of policy and taking major decisions (prioritization, allocation and approval of resources) through the development activities.

Local governments need to allocate funds towards operation and maintenance of Assets

In the process of implementing the decentralization policy both the Central Government and Local Government have allocated substantial resources towards creation of assets. The need to allocate funds towards operation and maintenance arises because most of the conditional grants to local governments do not provide for Operation and maintenance and there are specific areas of spending that must be locally funded, e.g. school inspections. (Godfrey Bahiigwa, Frank Elis, OddHelgeFjeldstad, Vegard Iversen: 2004).

There are differing sector policies towards Operation and maintenance with some sectors preferring to provide funds for construction of facilities to costs for maintaining them. The onus therefore, is on the LGs to provide Operation and maintenance funds out of their, own local revenue. On the other hand provision of Operation and maintenance funds will greatly enhance a sense of ownership and utility on the part of local governments.

Local governments are mandated to finance local investments and deliver services

Decentralization can positively contribute to the enhancement of the quality of life of the citizens through investment in delivery of services. (The Local government Act 1997). The ability of local governments to invest in service delivery will depend on the amount of funds available to it after meeting costs of local representation; administration and operation and maintenance.

Local Governments with a strong local revenue base have greater flexibility and freedom to allocate funds towards investment and service delivery. An important aspect of local government financing service delivery which was emphasized was local ownership of the investment.

Local contribution to Development Programs

A number of development programs have been designed incorporating a component of local contribution by local governments. Such programs include the Local Government Development Program (LGDP), Plan for Modernization of Agriculture (PMA), National Agricultural Advisory Services (NAADS), etc.

Local leaders pointed out that LGs could not access the above programs and others without spending part of their revenue as counterparts funding. In LG where bilateral or NGO Donor programs were being jointly implemented, LG had been clearly told that it was not proper for citizens in donor countries to be taxed in order to finance development programs in Uganda while Ugandans did not make their fair contribution to those programs.

4.1.6 Reasons for poor local Revenue collection

In practice, payments to the lower levels of government sometimes are not made or only partially made; Cost of collection had gone much higher relative to tax revenue having lowered the threshold and tax band mode to shs3000; Failure to deliver tangible or visible services; Poverty (poverty levels have actually increased especially in the rural areas); Frequent transfer of sub-county/parish chiefs.

To this was added the problem of unfilled posts at the parish level. Employing staff from outside a particular LLG affects revenue collection; Prolonged drought/ delayed rains led to decline in crop and animal yields; Negative attitude toward paying tax; Sickness/General morbidity especially HIV/AIDS; Narrow and low tax base; Declining commodity prices; Change of financial year while taxpayers had been used to the calendar year; Fish poisoning in Lake Victoria during FY 2002/03 which led to a ban or suspension of fishing for a period.

This affected fees from landing sites; Lack of accurate planning data; Lack of sensitization of tax payers due to lack of or limited facilitation of staff; Delays in tender award; Poor performance of tenderers/Declining market values, Un-coordinated and/or poor enumeration and assessment of taxpayers. It should be noted that the suspension of graduated tax is a complex issue and has attracted a lot of debates from both academicians and politicians.

According to the study carried out by the development consultants international Limited about the implications of the proposed suspension of graduated tax on local governments financing and decentralization process in Uganda (draft final report submitted to the secretary, local government finance commission on 17th march 2005), it is noted that during the Presidential and Parliamentary campaigns of 2001, some candidates called for the suspension of Graduated tax under the pretext that it was burdensome, particularly on the rural poor.

The tax was also castigated for being an outdated colonial legacy, for its brutal collection methods and regressive assessments. Some legislators presented petitions for suspension of the tax following several riots in Iganga, Busia and loss of lives during tax operations. The central Government reduced the minimum threshold to shs 3,000. This gesture was apparently misconstrued to mean a blanket reduction to shs 3,000 for all the rural and urban poor irrespective of the amount assessed. Since then, there had been growing political pressure to suspend GT all together. The climax came in April 2004 when a Private Member's Bill seeking to suspend Graduated Tax was put on the Order Paper of Parliament.

It was at this time, and particularly because of the intensified lobbying against Graduated Tax when the Government announced its intention to suspend Graduated Tax for 10 years effective 1st July 2005 to allow a series of comprehensive studies to facilitate a conclusion as to whether to suspend or retain it. The reasons which Government advanced for the suspension of GT included the tax being regressive, its brutal methods of collection, lack of fairness in its assessment, the impact on the poor being higher and that there were no visible services to justify the payment of the tax.

Local Governments and other stakeholders had expressed concern about the effects of suspending GT on the capacity for local service delivery as well as the sustainability of the entire decentralization process. Concern was expressed on the autonomy and discretion of local governments to plan and finance decentralized services; the capacity of local governments to operate and maintain decentralized services; the ability of local governments to effectively carry out administrative and management services at the local level; and the capacity of local governments to co- finance and contribute to development programs in conjunction with the Central Government and/or Civil Society Organizations (CSO).

Article191 (1) in the constitution of the republic of Uganda 1995 states that the lower local governments shall have the power to levy, charge, collect and appropriate fees and taxes in accordance with any law enacted by parliament by virtue of article 152 of this constitution. Article 152 states that no tax shall be imposed except under the authority of an Act of Parliament (1), where a law enacted under clause (1) of this article confers powers on any person or authority to waive or vary a tax imposed by that law, that a person or authority shall report to parliament periodically on the exercise of those powers, as shall be determined by the law (2). Parliament shall make laws to establish tax tribunals for the purposes of settling tax disputes (3).

Article 191 (2) states that the fees and taxes to be levied, charged, collected and appropriated under clause (1) of this article shall consist of the rents, rates, royalties, stamp duties, personal graduated tax, cess, fees on registration and licensing and any other fees and taxes that parliament may prescribe. Article 191(4) states that parliament shall by law make provision for tax appeals in relation to taxes to which this article applies. Article 192 states that parliament by law shall provide for;

- The taxes that may be collected by a lower local government for or on behalf of the government for payment into the consolidated fund;
- For a local government to retain for the purposes of its functions and services, a specified proportion of the revenues collected for or on behalf of the government from the district.

In the above, we note that there is a problem of giving powers to the lower local governments on one hand and taking them away on the other hand which creates a gap that needs to be bridged if lower local governments are to have power to levy taxes. Regan (2001:276) contends that political devolution involves the vesting of the rule making or law making powers in locally elected bodies if power was decentralized to the lower local governments.

It should also be noted that there are many forms of political devolution ranging from local councils which can make bylaws subject to national government approval through highly federal systems where the sub national units have some exclusive legislative and taxation powers of course including graduated tax collection.

Regan (2001) further contends that the administrative aim of decentralization is to enable the lower local governments mobilize local resources (sources including graduated tax) in more self reliant local development efforts more likely to be sustained by an involved population once central government or donor funding ceases. In the same book on page 326, one of the major changes following the decentralization process is the new grant system for local government and in line with the decentralization objectives central government grants will in the future take the form of block grants and equalization grants based on objective criteria. Local finance will thus consist of own revenues (graduated personal tax plus various fees and dues) plus a grant from central government. This grant will on average contribute at least 70% of all local revenue.

The issue of block grants has been one of the most controversial issues in the Ugandan lower local government reform. The Local Government Act, 1997 provides for sharing of local revenue among local governments. In rural areas sub counties (not districts), collect revenue, retain 65% of their collections and remit the balance to their respective districts. The sub counties, in turn, are required to remit 25% of what they have retained to village councils, 5% to their respective county councils. In urban areas, municipal divisions are required to remit 50% of their local collections to their respective municipalities. Like wise, Kampala City divisions must remit 50% of their collections to Kampala city council.

To ensure that remittances take place, money collected is banked on 'collection accounts' to which sub county/division lower local governments are joint signatories with their district/municipal/city counterparts. However, enforcement is not always total, and there have been numerous complaints over non-remittance. We intend to check this fact in Mukono District.

Nakanyike (2001:7) noted that lower local governments have severe resource constraints owing to their narrow revenue bases and weak collection capacities, in addition to the inadequate transfer from the center, and cannot reasonably be expected to effectively discharge their responsibilities.

4.1.7 Positive elements of Graduated Tax

- Graduated tax is a tax in which local governments derive financial autonomy as most of them use it to finance activities. It is even more important in lower level councils, which finance most of their activities using collections from graduated tax.

- Graduated tax is an old and popular tax within the community and most taxpayers annually plan when to pay. This means that the level of expenditure required for tax education and mobilization may not be as high as it would be if knowledge about the tax amongst taxpayers were poor.
- Graduated tax has proved to be a dependable avenue for collecting other incomes such as development and education taxes.
- The degree of graduated tax evasion amongst the poor are generally believed to be lower as they use the tickets as a way of identification and a sign of patriotism. Moreover, graduated tax has room for appeal and review.
- Graduated tax imputed from agricultural outputs reduces redundancy of citizens as they work hard to produce enough for self and for the tax.

4.1.8 Change of people's attitudes

The otherwise positive attitude towards GT changed soon after independence. The security of persons and their properties went with the colonial government in many independent African countries. In order to undermine the government, the opposition parties encouraged peasants to resist tax payment to cripple government's services and to weaken government. The change from colonial systems in many cases showed a sudden change in the level of local services that appeared routine then. Peasants started to see misuse of money and saw no or little reason why they should be taxed. Government agents and political party activists of the ruling party, even in areas where a ruling party lacked support replaced old chiefs who were respected.

In Uganda for example, Amin's opponents deliberately encouraged the uprooting of coffee trees in the 70s to deny him revenue from the coffee boom at the time to cripple his government. Removal of traditional rulers reduced the perceived relationship of social responsibility to pay taxes since the administration appeared more far removed from them. The new chiefs had no immediate allegiance to the people and appeared more interested in personal gains, abandoned the old participatory assessment and evaluation process ending up overtaxing the peasants. Resistance could often be thwarted with violence since such rejection to pay was now perceived as political resistance and attempts by the opposition to embarrass government. In fact denying government revenue became a political trick on the part of the opposition.

The system of tracing defaulters through their village chiefs was replaced by haphazard road checks at the inconvenience of even the tax abiding citizens and often realizing no viable results apart from even maiming suspected defaulters. Tax payers were suddenly confronted by strangers who knew nothing about their well being and status in society. In graduated tax swoops, people who were arrested bought their way out by bribing the collectors with money which did not reach the authorities. These swoops corresponded with big religious holidays, market days, or even school opening. The immediate impression was that they were intended to get money for the bosses.

Finally, (UNDP: 2005) under decentralization, levels of local governments retained a certain percentage from their collections. What this meant was that the more they collected, the bigger the percentage they retained. In order to share more, they would obviously extort more from the peasants. Interestingly, since the percentage reduced the higher it went up to the district, there was nothing meaningful that could be used for it. In many cases the committee or the local council shared it. Since tender boards had been said to favor themselves in tender awards, the situation did not help. Worse still many districts did not accept or even encourage appeals. Local government leaders did not appear to be bothered by the mistreatment of suspected tax defaulters.

4.1.9 A case for suspending Graduated Tax

In 2005, the Government of the Republic of Uganda suspended Graduated Tax. This was because although Graduated Tax was the main source of revenue for the Local Governments, contributing more than 80% of all local revenues, it was seen as regressive to the poor. The Government assured the Nation that Local Governments would be compensated for the tax loss until an appropriate replacement for the Graduated Tax was suspended. In the financial year 2005/06, Government released shs34bn to the LGs for the compensation for Graduated Tax and in 2006/07, Government released shs45bn (Uganda Local Governments Association Report: 1).

However, on 14th June 2007 the Hon. Minister of Finance, Planning and Economic Development, Hon. Ezra Suruma, announced in his Budget Speech that Government had decided to suspend the Graduated Tax Compensation. He gave the reason as "Government has approved new revenue sources for Local Governments to broaden their revenue base …….the new taxes for Local Governments to take effect on 1st July 2007. With these new taxes in place, there should be less pressure for Graduated Tax Compensation". (Uganda Local Governments Association Report: 1).

Despite the significance and importance of Graduated Tax to local governments there was pressure from some politicians to abolish the tax all together, arguing that it is primitive and crudely collected. The arguments supporting the suspension of GT were based on existing difficulties in assessing, collecting, enforcement and use of funds generated out of Graduated Tax.

Graduated Tax Becoming Very Unpopular and Controversial

(The New Vision 27th October 2008). The thrust of this argument was that the taxpayer's attitudes and minds had been so negatively influenced that it was difficult to collect the tax effectively. It was a direct tax, thus the taxpayers easily perceived it as loss of income, but so was PAYE which had even higher rates. Historically the method of enforcement had been "brutal" or unfriendly thus making it more unpopular.

The fear instilled by tax payment enforcers had in many times driven defaulters away from home and abandoned work on their subsistence farms to the detriment of household incomes and welfare. Still one could argue that it was due to repressive governments that gave no opportunity to people to exercise their human rights.

It was open to political interference because of its inherent weakness in enumeration, assessment and collection that could easily be exploited. Favoritism and political patronage were known to be a common problem. It was difficult to guarantee that politicians both at the Central and local levels could refrain from interfering with G.T for political gains.

It was inequitable to the extent that only able bodied- men are taxable leaving out able bodied- women who could even be having more incomes than men. In this respect it undermined the human rights of women to have a sense of equality in status to men. The local leaders holding the above views pointed out that it would be difficult for any leader to advocate for G.T without risking losing an election. For the civil servants they emphasized the difficulty in collecting and enforcing G.T. payment if there is no political will.

The proponents of suspension propose to finance political representation through financial transfers. The perceived advantages of central funding include; Releasing of financial resources to support service delivery; A guarantee that a fair, equitable and transparent remuneration to local council leadership; Continuing to attract well educated and competent personnel; Lastly payment from the Central Government will contribute towards unity of purpose and achievement of mission in leadership throughout the country.

It may also increase level of willingness to pay other taxes and licenses since the perception that taxes are used to merely enrich officials will no longer be the case. However the majority of local leaders and officials were not in favor of the Central Government paying for local political representation as it would compromise their autonomy and make them dependent on the central government. Central government transfers have progressively provided the source of funding for the bulk of service delivery in local government. Overall transfers have grown from shs 31 billion in 1993/94 to shs 805.5 billion 2004/05.

The question we need to ask ourselves is: Should a tax be suspended because people run away? The system could be modified so that small income earners or persons with no known means of earning be directly taxed by LC11 councils and 100% collection retained for local programs. The HLGs would then benefit from remittances of salaried people at little administrative cost and less friction with the difficult non-salaried residents. The problem foreseen is that, as has been a usual practice, the rich business persons may evade payment.

Comments on Good Governance and Independence of Local Governments

Some of the stakeholders advocating for suspension of GT point out that the argument of local government independence is becoming progressively weaker in view of the declining share of local revenue (due to the growing share of transfers from Central Government) in local government service delivery. What is important is commitment to and strengthening the unity of purpose (i.e. delivery of services and poverty reduction) on the part of the Center and local governments. It is important for both the Center and local governments to observe the principles of mutual respect and non-subordination recognizing the roles of one another. Local leaders and technical officers therefore called for the change of attitude of Central Government officers towards local governments especially with regard to providing funds for local government programs.

4.2 Effects of GT suspension on Service Provision

The second schedule of the LGA, 1997 stipulates functions and services that are under the jurisdiction of the central and local governments. Article 191 of the 1995 constitution empowers districts to levy, charge, collect and appropriate fees and taxes, as a source of revenue. Article 193 of the 1995 constitution, puts in place a grant (conditional, unconditional and equalization) system for funding central government decentralized services. Local revenue collections mainly funds district programmes, while grants from the central government fund services initially delivered by the central government.

The suspension of GT was conceived to be political although this tapped in the tax's unpopularity. The question of alternative sources of revenue was widely debated, by the Local Government Finance Commission (LGFC), Uganda Local Government Association (ULGA) and other Local Government Associations. GT had earned local Governments a sum of 80 billion ($4.5 million) per year[7]. Officials both at national and local level rushed to find alternative sources of funding. The central government decided a compensation fund and imposing an airtime for cell phones, cattle and fuel, local service and hostel taxes. Government compensation since 2005 has been in the

[7] Cammack, et al 2007

range of 30-40 billions, and the other alternatives have not improved the financial situation in the districts. This uncertainty in the financial situation has had ramifications in Mukono district. In 2005/2006 the district planned to construct and improve roads as well as increasing water coverage. It intended to accomplish some road works, build protected springs, dig wells, and construct motorized wells.

However, this would not be completed; it is indicated in tables 3 and 4.

Table 3: Planned and completed Roads in 2005/2006 in Mukono District.

AREA OF CONCERN	PLANNED FOR	KMS COMPLETED
Road improvement	78.0km	49km
Periodic maintenance	40.8km	22km
Routine maintenance	23,226 work days	27,910 work days
Road rehabilitation	129km	19km

Source: Mukono District Planning Unit, Plans and Budgets 2005/2006

From the table, we note that there was a sluggish rate of implementation due to delayed release of funds from the central government. In fact most of the planned for activities were not achieved and this forced the District to re-plan for them in the next financial year 2005/2006 which in the end affected other important programs that could not be accommodated in the Budget due to financial constraints.

Table 4: Performance of Water Development Activities

PLANNED COMPONENT	PLANNED TARGET	STATUS	PERCENTAGE COMPLETED
Spring protection	61	49 completed	80.3
Hand dug wells	31 sources	25 completed	80.6
Motor drilled wells	33 sources	14 completed	42.4
Designs for piped water systems	2 designs	2 designs completed	100
Ferro-cement rain water tanks	20	10 completed	50
Construction of pit latrines	2 latrines	1 completed	50

Source: Mukono District planning unit. Plans and Budgets 2005/2006

From the above table, there is an indication that apart from the designs for piped water systems of all the planned targets, not all the planned activities were 100% met and the reason was due to insufficient funds. Some of the functions that were supposed to be performed by the finance and planning department at the district included the following: Coordination of revenue mobilization role; Ensuring adherence to financial management principles by all sectors; Coordination of the planning and budgeting process; Ensuring financial accountability and Production of quarterly financial and plan implementation reports.

However, in its efforts to mobilize resources, a number of setbacks led to its poor performance. Critical was the politicization of the revenue mobilization process due to government pronouncement of suspension of graduated tax and later pronouncement on market dues. This has put the district in a testing moment. Major limitations which led to the non-implementation of the above included: Some of the investments were under funded. Since the district registered poor performance in that area, most works were not realized; Budget cuts at national level hampered planned works and untimely release of funds by the central government.

With the suspension of GT, central government transfers to the district and yet these transfers have major risks associated with them as listed below:
Untimely release of funds especially locally generated revenue. The LGA, 1997 section 86 (2) stipulates that "in rural areas revenues shall be collected by the sub county councils and sub county councils shall retain 65% or any other higher percentage as the district council will approve of the revenue collected by it and pass the remaining percentage to the district".

Failure to meet co-financing obligations halts disbursements from the center, implies that when things are not done in the right time, it distorts all the plans and time can catch up with the service providers hence sometime doing away with those services completely and/or postponing others. This is due to the fact that lower Local Governments have very few sources of revenue generation and sometime when they identify new sources, the Government interferes and stops them from collecting these taxes hence becoming a big problem to provide or deliver services to the people for example the scrapping of Boda Boda fees in Lugazi town council during the presidential campaigns of 2006.

Whereas, government may have managed to offer alternatives to GT suspension, central government to districts normally has limitations. The Funds are in most cases released late hence affecting the lower local government plans for example, facilitation of health services like immunization, primary health care from government is sent quarterly and sometimes takes over two quarters without being sent to the lower local governments. Little money is sent by the central government, the money that is sent to the Lower Local Governments by the central Government is usually lower than what was being expected which hinders them from providing quality reliable services to the people for example in Njeru town council.

The greatest impact of GT suspension is on basic administration of the Local Councils and facilitation of local Councillors. Mukono district cannot pay councillors' allowances. This had halted budgeting and planning in the district. Without councils meeting and taking decisions, the district and the sub-counties cannot execute programmes since the administrative elites do not have the endorsement of council. This has further weakened the implementation of decentralisation and popular participation and in the end increase dependence of LGs on the centre. Sub-counties that had limited local revenue collection, had not convened council meetings as regularly as required

Poor motivation of workers especially in terms of allowances and this has de-motivated the affected workers and therefore affecting the results produced.
In addition to this, the 20% contribution of the council to the villages is no longer being sent as there is no money to do so. Budgets of the council were also affected negatively for example, contributions to the youth and disabled activities are no longer being sent there.

Low tax bases; Poor local revenue generation, this is sometimes due to the fact that tax payers don't want to pay whatever kind of tax being proposed or levied saying that the president for gave them from paying any tax. With that kind of Attitude; it was very difficult for the tax collectors to collect taxes which affected the financing of services that were financed by GT before it was suspended e.g. failure to rehabilitate class rooms. In addition to the above, people are also generally poor and can not effectively afford to pay all the taxes.

In a sub county like Lugazi town council, the effect was that the 20% to parish and 5% to village level remittance income that used to be taken to the villages for service delivery, was no longer there. General reduction in service delivery e.g. construction of roads, was constrained by finances. Some local authorities cannot even afford to pay their workers.

A non systematic suspension of the graduated tax without developing a viable alternative replacement source of own revenue source to local governments in general undermined the decentralization process and in particular implied some of the following:

- Those sub-counties, divisions and lower level councils who depended entirely on local sources of revenues (graduated tax being the predominant) were crippled and did not have sufficient funds for operation, grass-root development and mobilization – the way they had it then.
- That alternative source of finance to fund costs of administration, council expenses and allowances and operation of some statutory bodies such as the district tender board had to be found. Yet these were funded by Graduated tax.
- That greater pressure was exerted on the already highly constrained consolidated fund as the Ministry of Finance was made to immediately find alternative finance to bridge the gap that was created by suspending graduated tax. Pressure on the consolidated fund meant that government had to cut its expenditures in some sectors.

- That government had to bear an added cost of transferring money to local governments and had to face a number of equity related challenges of transfers especially given that the present set-up of revenue sharing still have a lot of shortcomings yet to be addressed.
- If local governments are brought up relying on central transfers, it will mean that they will adopt accountability for the central government practices rather than practicing accountability and good governance for the populace.

In this way transparency might be compromised and the whole essence of decentralization will be put to question.

The suspension of GT was a major challenge to local governments since it was a major source of internal revenue. When the current decentralization policy was launched in 1992, lower local governments were given the responsibility to undertake specific functions and provide functions and services as included in the Local Government Act of 1997. In part two and five of the Act, the Lower local governments assumed a number of functions which included, political administration, judicial services involving minor cases and maintenance of community development projects like the rehabilitation of roads. (The Local Government Act Cap.243:600).

To perform the above functions, Lower Local governments need funds which they have to raise from local sources. The major source of lower local revenue was the suspended Graduated tax. According to the studies carried out by the Local Government Finance Commission in the Ministry of Finance, graduated tax contributed about 75% to local revenue that accrued to rural lower local governments in 1997/1998 and about 35% of revenue to urban ones in the same year. (LGFC: 2005). The suspension of GT was directly denying LLGs this source of such a big amount.

The Local Government Finance Commission carried out research in 2005 on the likely effects of the proposed suspension of GT on Local Governments Financing and Decentralization process in Uganda. This Study was undertaken in view of the concerns of various stakeholders following persistent decline in Local Revenue over the past four years and the ever increasing dependence of Local Governments on Central Government transfers to finance service delivery. This was to warn Government on the likely problems that would arise in case G.T. was suspended. Unfortunately the advice was not heeded.

It is true that there was inefficiency in the collection of this tax and some of the methods to collect it were crude. What needed attention was to address this inefficiency and collect it without causing hardships to the payers. The suspension of GT at the beginning of 2005/06 implied that immediate steps needed to be taken to find the revenue to compensate local governments for the loss of Shs 59.0 billion which G.T. used to bring if the functions of the LGs as defined in the Second Schedule of the Local Governments Act were to continue. If the revenue was not found, decentralization would be greatly affected negatively.

4.3 Coping mechanisms without GT

It appears that Mukono district, has failed to implement a number of programmes due to the suspension of GT. The district has however attempted to copy by instituting new sources of revenue. Table 4 shows how the different sub-counties have responded to GT suspension.

Table 5: New sources of local revenue by sub-county

Name of sub county	Source of revenue collected
Kasawo	Licenses and permits from fishing on the Island, traditional healers, Birth attendants, Sand deposits etc.
Lugazi	Licenses and permits from shops, clinics, factories, petrol stations, market and Bodaboda fees etc.
Kawolo	Licenses and permits from shops, clinics, petrol stations, market and Bodaboda fees etc.
Njeru	Licenses and permits from shops, clinics, factories, petrol stations, market and Bodaboda fees etc
Ngogwe	Licenses and permits from fishing on the Island, traditional healers, Birth attendants, Sand deposits etc.
Seeta-Namuganga	Licenses and permits from shops, clinics, factories, petrol stations, market and Bodaboda fees etc

Source: interview notes

The above table illustrates the different sources of revenue collected from different sub counties as a way of raising local revenue to finance service delivery to the local people in Mukono District. With the suspension of G.T. by the central Government, lower local Governments in Mukono District did not just sit and watch how services would be rendered to the local people but instead came up with new mechanisms of financing local services.

Such mechanisms that were put in place included,

Issuing of licenses to people engaged in gainful activities within the District for example, among the people that were issued with these licenses were the traditional healers, shops, clinics, petrol stations and sand deposits.

Different lower local governments with in the District collect different revenues depending on the nature of the revenue bases in their localities as represented in table 6 above. These licenses bring in different revenues that are being used to finance the delivery of services to the local people.

Market dues, it was discovered by the researcher that the District is copying up with financing service delivery through charging and collecting market dues where by the bigger and activeness of the markets, the more the revenue collected. More revenue is collected from urban markets which are bigger with more buyers compared to village markets which are smaller with fewer buyers.

BodaBoda and park fees, the District is also surviving collecting revenue from bodaBoda cyclists and Taxi operators. This revenue collected is used to finance service delivery hence making the provision of local services continue after G.T. suspension. Other licenses that have helped Mukono District to thrive in financing and providing services include business licenses in fisheries/boats, the introduction of vanilla license have all increased revenue generation to the District hence the enablement of the District deliver services.

Tender fees, this has brought in some revenue to the District that has been very helpful in financing the delivery of services where by the business people who want to supply commodities or be awarded contracts have to pay a non refundable fee to the district as they submit their applications and whether they have been or not successful, the money they have paid is not refunded to them hence enabling the district take up such money in form of revenue that can be used to fund the delivery of services.

Lands registrations, Bill boards, Development Tax, NAADS service providers registration fees have also played a very big source of revenue in Mukono District to help in the financing of service delivery hence helping the District cope up with the situation after the suspension of Graduated tax.

The local service tax

Under this Tax, all practicing professionals such as lawyers, teachers, doctors, engineers are required to pay this tax which ranges from Shs5000 to Shs100, 000 per person per year. The argument in support of the tax is that the suspension of Graduated Tax created a funding gap in the local governments with in Mukono District. Therefore the Local Service Tax is to cure this problem. Under the new law, the non-professionals who are required to pay the Local Service Tax are people who are carrying out commercial farming on more than two acres of land or have more than 20 cows.

Hotel tax, the introduction of the hotel tax to the hotel occupants has also generated revenue to the District which has helped it to continue rendering services. Each hotel/Lodge occupant is asked to pay 1,000 Uganda shillings per stay in the hotel room or eats from there. The money is collected from the occupants by the hotel operators and there after collected from them by the tax collectors until it reaches the District. The Operationalization of both the Hotel and local service taxes took effect in July 2008.

In addition to the above mechanisms, the district is coping up by the help of the central government transfers that have supplemented the District efforts to raise money to service local service provision. We do thank the central government for that support.

4.4 Increasing local revenue base

With limited local revenue, the level of service provision in Mukono has deteriorated. As such there is a need to look into other sources of revenue.

Land Tax

The range of issues that concern taxation of land includes existence of varying land tenure systems. The proposal for introducing land tax is a good one in generating local revenue. This is because, majority of the people especially in rural areas have a lot of land that they use to carry out economic activities such as farming while other land is underutilized or not utilized at all so when this land is taxed, people are going to increase on their level of production to look for money to pay the tax levied on them and the more produce realized, the more the local revenue will be generated. Since land is found both in rural and urban setting, land will have a wide tax base i.e. the tax will be applicable to and paid by all land owners in the lower local governments.

At present rural land is not widely taxed but through GT there was an attempt to assess the income from land and tax that income. Since GT was suspended, taxation of rural land may be an attractive alternative because the majority of the citizens own land in one form or another.

The Local leaders held the view that the proposal could work since the prospective taxpayers could be easily identified. Nevertheless, if the responsibilities to pay the tax were to be shouldered by the land owners, there would be resistance if the rate fixed by the local government were to exceed the statutory shs 1,000/- which the Land Act 1998 requires the tenant to pay to the landlord. The Government would need to move very cautiously after a lot of sensitization and education of the taxpayers.

On the technical side, the Local Officers pointed to the difficulties that are likely to be encountered in valuing rural land. First the numbers and the capacity of competent land valuers including equipment and logistics that are necessary to carry out the exercise of valuation cannot be attained in time for the land tax to replace GT.

However, the following are the issues which should be put into very serious consideration if a land tax in the rural areas is to be implemented:
First issue is whether all types of land holding in the rural areas should be taxed. The majority of land holding in Uganda is Smallholder of less than 5 acres. Since over 90% of land holdings in Uganda are Smallholder, this would give the tax the broad base quality. However, there are political and valuation limitations to taxing smallholder farmers. If smallholder farmers were exempted, then taxation of rural land would apply to only comparatively few medium and large-scale landowners.

Second issue is how rural land should be valued. Three alternative approaches were suggested, namely using the imputation values as used during GT assessment; simplifying the existing system of valuation; or treating all rural land equally irrespective of value.

Third issue is what kind of rural land should be taxed. This issue relates to the type of economic activity being carried out on the land (farming, ranching, plantation or forestry). Likewise it will need to be decided who to pay for the cost of valuation between the tax payer and local government.

Fourth issue is who should pay the land tax. In areas where Mailo or private landownership applies, the choice would be between the landowner and the tenant.

Lastly is the issue of the tax rate to apply. It would be most appropriate for the local government to decide on the appropriate rate as long as it is politically acceptable.
The advantage of this Tax is that, it is easy to collect since it is easy to identify land owners and more so land will always be there without being carried away or hiding it or even dodging it like in the case of GT and in addition to this, the value for land keeps on increasing and this makes the process of assessing the tax to be paid easy. This particular tax has merits that include; It is easy to assess income that will be received from taxing land as majority of the people especially in the villages own land in one or the other. It is very easy to the payer and also maximizes the usage of land; it further appears easy to identify people to pay this tax.

Property Tax

Even though property is unevenly distributed with some people having more property than others especially in towns where we have the majority of people having more property in terms of buildings, cars and other wealth with much higher values compared to the ones in the rural areas where a number of properties owned have low values attached to them, levying taxes can vary depending on where the property is owned. In this case, those ones in towns where property has more value will of course pay more taxes while those ones where the property is of low value will of course be levied upon low taxes so as not to feel the burden of paying such taxes very much and in the end most of them will be willing to pay hence generating local revenue for the lower local governments.

The tax has advantages in that its base is potentially wide and easy to collect. It has a wide base as the majority of the people own property. In Urban areas like Mukono Township it is easy to assess especially, and this is where most of the valuable investments like schools, Hospitals and clinics can easily be identified.

The reactions of most local leaders consulted during the study about taxing rural property were generally positive. But many of them preferred to limit taxing only commercial buildings. The predominant issues would be how to handle owner occupier real estate where owners may not have a reliable source of Income now, but have a high value property like cattle.

Since Government decided to suspend GT, the new replacement tax to GT will necessarily have to be increment in the indirect taxes in order to avoid the pitfalls of GT. This however does not mean that people are exonerated from contributing to their development through payment of Taxes. A tax introduced on basic goods at an average of 4% on the final sales price on specified commodities including basic commodities ensures that the majority as households and not as individuals come into the tax net or contributes to their local service costs.

Commodities such as fuels which may have a minimal impact on transport and consumption, Soap, Sugar, match boxes, salt etc could serve a good example of those goods whose prices can be increased. When indirect taxes are introduced to the tax payers, the advantages to the lower local governments in their endeavours to collect taxes will include: The tax burden to the individual will be seen reducing or reduced. The tax base will be widened enough so that the majority of residents contribute to their own social-economic development and not to directly rely on donor money or direct Government transfers. The tax will be discrete, with a small impact on individual social well-being and have a fair elasticity to the base to ensure an adequate yield. A fair spread of the burden without reducing the living standards. Be convenient to pay, collect and account for.

Cost sharing in the delivery of services

Another source of local revenue generation can be through cost sharing where by the government pays for a particular portion of costs to some services and the rest paid by the service users. This for example can be applied in hospitals where by the government can pay the doctors and maintain the hospital facilities while the patients can buy the medicines prescribed to them by the doctors. This can in the end save lower local governments a lot of money they would have used to buy medicine for their people when they visit hospitals and hence can use the saved money to finance other services like the construction of roads.

Airtime Tax

All airtime cards sold in Uganda can have a surcharge component of Ush50 per Ush5000 of airtime. This can be collected by the service provider and there after the money can be remitted to the lower local governments through agreed transfer channels. An example of this revenue would be examining MTN, which has about 500,000 subscribers. On the assumption that each subscriber buys two airtime cards per month of Ush5000 each, this charge can raise about 600,000,000 shillings a year. The benefits of the charge are that users of luxury services pay it and it has no collection costs for local government. With a small tax on a high demand item, the resistance from the payer can be small.

Increment in the Taxes charged on incomes

Income tax is a Tax on income accrued from ones work or wealth. The different categories of incomes that can be taxed include:

Employment Income

Taxable income from employment is widely defined to mean any income derived by an employee from any employment. PAYE (Pay As You Earn) is a system of deducting at source (withholding) tax from incomes of employees.

The deduction is made by the employer at the time of paying the employees.

Traveling, entertainment and other allowances, unless representing solely the reimbursement of expenses incurred in the production of income, benefits in kind from employment should also be taxed, unless their aggregate value does not exceed Ushs.10, 000 per month. Here what the local government should do is to calculate the benefits given to workers in kind like food and add it to the Gross salaries they get and then tax it at once. The advantage in doing this will be that the workers will pay a higher tax than what they have been paying and in the end more revenue will be collected. The law obliges the employer to remit (pay over) to Uganda Revenue Authority which can assist transfer that using the existing money transfer mechanisms to the local governments.

Rental Income

Rental Income is defined as income earned by a person from letting out property. Rental Income earned by a landlord/landlady other than a limited company or trust is termed as Individual Rental Income. Under the Income Tax Act (1997), Individual Rental Income is taxed separately from other income of the landlord/landlady, as though it were a sole source of income basing on corporate income tax rate. Rental income earned by an individual should be separated from income earned from other sources and taxed separately under rental tax rates that can be set by the local governments.

Computation of tax on Individual Rental Income - Procedure:

All rents earned by the individual from rented properties during the year are summed up to obtain gross rental income. A flat percentage rate of the gross rental income is granted annually as a deduction to obtain income chargeable to tax. A fixed rate is applied to the net figure (taxable income) to determine the tax payable. An individual whose gross rental income does not exceed the threshold pays NIL rental income tax. Similarly an Individual whose net rent after the deduction does not exceed the threshold pays No rental Income tax.

Interest Income

Tax on interest received from financial institutions and government bearer bonds earned by individuals should also be taxed for example when an employee has been given a bonus for appreciating his or her work, this appreciation which may be in form of money should be taxed. In the above, in case taxes have not been levied, then they should be introduced and those ones who have been paying it need to increase the amount paid but the increment should not be alarming so as to resist paying it by the one paying for it.

Fines

Another way of local governments raising local Revenue is through levying fines to culprits that have been convicted of breaking the law. For example those who don't want to pay taxes and others that have committed offences whether small or big should be asked to pay a certain amount of money by the courts in which they are convicted. The amount can be charged basing on the financial status or the kind of work the convicted does. Since there are many law breakers among which may be Boda-boda cyclists and motorists, this will increase Revenue for the lower local governments.

Market Dues

Market dues are a very important source of local revenue. The contribution of market dues to local revenue has not only been varying widely from year to year within the same district, but also from district to district within the same year. This is in conformity with the fact that market sizes (sizes of local economies) vary a lot resulting in collectable dues to fluctuate accordingly, In addition, the rural economies are agricultural in nature, and because of seasonality in agriculture, volumes of tradable commodities also fluctuate by the seasons resulting in variations in collectable dues. Other factors such as the management of a market (private or public) may also affect revenue collections.

Therefore, there will be more revenue collections in the local governments with bigger markets compared to small ones and during harvests especially in the rural areas more taxes will be obtained though it will reduce during the drought season but this will increase local revenue.

Licenses and permits

These can be levied on people wanting to enter business or who want to carry out any economic activity. This can best be applied to shop keepers and those selling any kind of commodities for the case of guaranteeing a license for them to operate, it can be enforced by not allowing people without licenses to execute their operations and for the case of permits, these are issued to motorists who are both engaged in transportation businesses as well as those ones not involved transportation businesses but do have cars. For example, one can be required to pay a certain amount of money to obtain a permit to drive his or her car and this can also be applied to other people doing this kind of business like Taxi, Pickup, Buses, special hire drivers and Bodaboda cyclists.

Transaction Tax

Another possible tax and charges that can be levied are the banking transactions tax, airtime and user charges. All licensed banks and other financial institutions in Uganda with the exception of government and diplomatic accounts can apply a scaled charge on every account that has monthly receipts in excess of a specified amount. These amounts can be collected by the banks in a separate account on the last day of the month and then transmitted direct to local governments.

The split could be on the basis of the address of the account holder, or in direct proportion to the local government populations as determined by UBOS from time to time. The benefits of such a tax and charges are that there are no collections costs incurred by local governments and the wealthy are the ones who pay and Small accounts can be exempted. The cost of the bank administration is a legitimate charge by the banks on all accounts that pay the charge.

CHAPTER FIVE

SUMMARY OF THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.0 INTRODUCTION

This chapter presents summary of study findings and recommendations based on the findings and study objectives as well as the conclusions. It also makes policy recommendations and suggests areas for further research.

5.1 SUMMARY OF FINDINGS

The objectives of the study were:

- To establish the level of Revenue collection before and after G.T suspension
- To establish the coping mechanisms of Mukono district to graduated tax suspension
- To identify other new sources of local revenue generation

The study found out that since G.T formed the main source of revenue generation; its suspension had a lot of negative consequences in the lower local governments which included among others the following:

- Reliance of the lower local governments on central government transfers that are associated with problems
- Low budget realization
- Limited local revenue collection
- Introduction of new taxes such as the local service and hotel taxes
- General reduction in service delivery

- General attitude of people not wanting to pay taxes thinking that all taxes were abolished by the President and
- Increment in indirect taxes through increased prices of commodities
- The new proposed sources of local revenue generation are: Land, property, income, Air time, transaction, fines and market taxes.

5.2 CONCLUSIONS

The percentage contribution of GT to locally raised revenue at LLG was significant and crucial for the functioning of LGs. Therefore in terms of locally raised revenue the role of GT was critical for the sustainability of the LGs. Since government suspended GT, it will be an uphill task to find about shs 59.0 billion which represented net GT at a national level to replace it.

On the side of expenditure, locally raised revenues principally finance day to day routine administrative services, council allowances, and co-funding for programs such as Local development Grant under LGDP II expenditures. The suspension of graduated tax undermined service delivery by the local authorities. Government needs to sensitize the people about the need of paying taxes such that the thinking in the people that all the taxes were removed by the president is removed and before introducing the new taxes it will be good for the government to first teach people these taxes such that they understand them for easy acceptability.

5.3 RECOMMENDATIONS

The study recommends that the following should be considered if service delivery is to be enhanced in lower local governments effectively.

1. Sensitizing the citizens on the importance of paying taxes

2. Timely disbursement of GT compensation by the central government.
3. Streamlining the collection and administration of taxation in the districts.
4. The central government should empower and facilitate the districts to collect taxes without political influence.
5. Reduce the burden of local revenues financing large administrative and political structures. At LC1 and LC2 there should not be full time Executive Committee members and the number of civil servants should be small.
6. The central government needs to give equalization grants to lower local governments that have the least tax bases such that they match with those with bigger tax bases. This grant will help to reduce the differences in the fiscal capacities of local governments to finance their service needs. There is therefore a need to continuously review the other financing schemes (unconditional and conditional grants) to ensure that they are distributed on a fair and equitable basis in order for the equalization grant to be effective. This is because the equalization grant is meant for “filling in of potholes” of the disadvantaged local governments which Results in a significant transfer of more financial resources to the local governments. There are concerns however that if the mechanisms put in Place for the transfer of these resources do not promote equalization; they may introduce new inequalities among the local governments.
7. There is therefore a need to look at the mechanisms for the transfer to ensure that they do not either introduce inequalities thus undoing the impact of the equalization grants or do not duplicate the equalization mechanism already in place. It has been observed that there are horizontal inequalities existing among local governments. Thus, much as the equalization grant is expected to address the vertical imbalances and to some extent the horizontal imbalances among the recipients, the horizontal imbalances among the lower

level local governments (especially sub-counties) remain largely unaddressed these imbalances therefore need to be addressed.

To supplement the above effort, the local governments can also generate the necessary matching funds by introducing a Community Services Charge (CSC) at the parish level. The CSC, while generating revenues for service delivery in the community it will address the following major weaknesses which have been associated with GT namely; The CSC will be spent within the community i.e. LC1 and LC2 thus enhancing the participation of the community in planning and management of service delivery and in so doing increase ownership of development programs in the community. Increase the visibility of services financed by CSC and in so doing increase the willingness of the community to pay taxes.

Need for Equalization

It is as a result of these inequities that the need for equalization arises. Equalization is the desire by the central government to provide extra funds to those local governments whose revenue raising capacities are weak and expenditure needs great (as compared to other local Governments) to enable them provide a "minimum" level of service to their constituents. The main vehicle for channeling these funds to those "needy" local governments is the equalization grant. Clause 4 of Article 193 of the 1995 Constitution (elaborated on in Section 84 of the Local Government Act of 1997) defines the Equalization Grant as "...Money to be paid to local governments for giving subsidies or making special provisions for the least developed districts; and shall be based on the degree to which a local government is lagging behind the national average standard for a particular service".

By implementing the equalization grant scheme, it is expected that local governments which are disadvantaged either in terms of high expenditure need or low revenue potential will be subsidized to a level where they can at least provide a "minimum level of service delivery".

Calculation of Fiscal Equalization Grants

A typical formula that considers only the equalization of fiscal capacities and based on the Representative tax system can be given as follows: $TRi = Pi\ (B/P - Bi/Pi)^{*}\ t$ where

TRi = Fiscal Equalization grant to local authority i,

Pi = Population for the local authority,

Bi = Tax base of the local authority,

P = Total population of the country,

B = Total tax base of the country,

t = the country's average effective tax rate on the tax base.

$B/P - Bi/Pi$ measures the gap between the national average per capita tax base and the per capita tax base of local government i. This formula states that the central government transfer will bring the fiscal capacity of local governments below average up to the national average that is, assuming 100% equalization.

As regards determination of equalization according to expenditure needs, it is important for the stakeholders to agree on the following: -Which services to equalize. The criteria for equalizing those services should be objective and not easy to manipulate.

Improvement of Existing Tax Administration Systems

The government needs to conduct studies in the following areas; Improving tax administration (assessment and valuation), Improved Tax collection methods e.g. privatization, Tax data management and use, Accountability and good governance, Expenditure rationalizations i.e. review the major sectors and activities to which local revenue is allocated including political and administrative structures.

The Parish can be the main collection centre and the Parish Chief can act as accounting officer. All persons who will be deemed below an established poverty line for the District can be exempt. The powers to exempt a taxpayer can be vested in the LC1 Council on the advice of the Parish Chief. The LC1 can be required and facilitated to keep and maintain a simple taxpayer register at the LC1 level. The LC1 taxpayer's registers can be consolidated by the Parish Chief.

The extract of the tax payment register can be published or displayed permanently on LC Notice-boards every quarter. Likewise accountability for use of funds collected should also be displayed for each quarter. The local governments can use existing guidelines and other guidelines developed by MOLG and LGFC for assessment.
There is need for further research on the effects of the newly proposed taxes on the tax payers in the lower local Governments.

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APPENDICES

Appendix 1 INTRODUCTORY LETTER

Appendix 2 INTERVIEW GUIDE

Dear Respondent,

The Researcher is a student of Master of Arts in Public Administration and Management in the Department Of Political Science And Public Administration, Makerere University. He is undertaking a study entitled ''**The Effects of suspending Graduated Tax in Lower Local Government: A case Study of Mukono District''.** You have been chosen because we feel that you are most suited to provide data to the above-mentioned topic. The answers to the questions are for academic purposes and will be treated with confidentiality**.**

Thanks for your co-operation!

Appendix 3 QUESTIONNAIRE

THE EFFECTS OF SUSPENDING GRADUATED TAX IN LOWER LOCAL GOVERNMENTS: A CASE STUDY OF MUKONO DISTRICT

Objective one

1. What kind of taxes do you collect?
2. How much do you get from these taxes?
3. How was tax collected before it was suspended?
4. What problems do you face in collecting Local revenue?
5. In your view what could be the solutions to the above-mentioned problems?
6. What other sources of income do you have?
7. How much does the district get from the above sources?
8. How much money did you loose from GT when it was suspended?
9. What was GT used for?
10. How much in percentage did the district receive from government as conditional, unconditional and equalization transfers from the financial years 2000 to 2005
11. What problems are associated with the above?
12. Suggest ways of how the above can be rectified
13. What percentage was GT contributing to the district income?
14. How has the government interfered with your independence of collecting taxes?
15. What steps can government take to rectify this problem?

Objective two

1. What services does the district miss or cannot provide because of GT suspension?

2. What percentage of the budget is funded from district tax collections?
3. How much does the district spend on medical services since 2005?
4. How much does the district spend on water and sanitation since 2000?
5. How much does the district spend on work/roads?

Objective three

1. What new strategies does the district use to get income as a result GT suspension?
2. How does the district apportion transfers from government meant to recover GT suspension?
3. How is the district copying up with the new income strategies?
4. What is the district doing to reduce dependence on government transfers?