THE PUBLIC SECTOR TAX SEMINAR

THEME
Tax Transparency for Accountability and Shared Prosperity

TOPIC
Outsourcing Tax Collection: The Good, Bad and Ugly

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Outsourcing Tax Collection
“The Good, Bad and Ugly”

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The Constitution of Kenya

PREAMBLE

WE, THE PEOPLE OF KENYA -

ACKNOWLEDGING the supremacy of the Almighty God of all creation:

HONOURING those who heroically struggled to bring freedom and justice to our land:

PROUD of our ethnic, cultural and religious diversity, and determined to live in peace and unity as one indivisible sovereign nation:

RESPECTFUL of the environment, which is our heritage, and determined to sustain it for the benefit of future generations:
COMMITTED to nurturing and protecting the well-being of the individual, the family, communities and the nation:

RECOGNISING the aspirations of all Kenyans for a government based on the essential values of human rights, equality, freedom, democracy, social justice and the rule of law:

EXERCISING our sovereign and inalienable right to determine the form of governance of our country and having participated fully in the making of this Constitution:

ADOPT, ENACT and give this Constitution to ourselves and to our future generations.

GOD BLESS KENYA
BIG QUESTION?

“Should Tax Collection be left solely to “WE THE PEOPLE OF KENYA”? And not to profiteers / millionaires!
PROVISIONS

- The PFM Act legal framework is anchored in Article 201 of the Constitution of Kenya 2010.

- Article 189 of the Constitution of Kenya 2010 requires national and county governments to have autonomy in the management of their finances and setting priorities.
Purpose of the PFM Act

Effective management of public finances by – the national and county governments

The Cabinet Secretary shall, in writing, designate persons as receivers of national government revenue and who shall be responsible for receiving and accounting for such national government revenue provided in any law or in regulations as the Cabinet Secretary may specify in the letter of appointment.(Section 75(1)).

DESIGNATED .... KRA ?
A receiver of the national government revenue may authorise a public officer employed by the national government or any of its entities to be a collector of revenue for the national government and remit it to the receiver.(Section 76(1)).

The County Executive Committee member for finance shall, in writing, designate persons to be responsible for collecting, receiving and accounting for such county government revenue as the County Executive Committee member for finance may specify in their letters of designation.(Section 157(1)).
The County Executive Committee member for finance may authorize the Kenya Revenue Authority or appoint a collection agent to be a collector of county government revenue on such terms and conditions as may be agreed in writing in accordance with regulations. (Section 160).
OUTSOURCING TAX COLLECTION

- Outsourcing involves the contracting out of a business process to another.

- Outsourcing can also be viewed as any assistance from an intermediary that is more capable of or familiar with certain practices than the “main player” – The Tax Collector.
ADVANCE APOLOGIES!!

- No offence intended to anyone or any office!

- It is an educational forum ON A TOUCH SUBJECT!
JUSTIFICATION FOR OUTSOURCING

Problem in Tax administration to require outsourcing

1. Incompetent personnel in charge of tax administration.

2. Low salaries to tax administration personnel making corruption inevitable
Corruption and inefficiency in the tax and customs administration causes the citizens to lose confidence in their government – therefore good to outsource.
1. Greater professionalism in tax administration.

2. Efficiency and neutrality

3. Outsourcing allows for expertise in manpower and scrutiny on the work done because individual responsibility and liability is attached.

4. Expanded use of tax professionals would reduce errors as outsourced tax officials will do their job more carefully because they own it.

5. Private tax professionals will be more neutral in their analysis because they are paid for it, their work is subject to review, and future work is conditioned on satisfactory performance.
6. Technology – Computers in Tax Administration - The logic is that computers are so critical that the most capable computer experts should be utilized, and they are in the private sector.

7. In certain areas such as data entry, a private contractor will have more flexibility to provide the necessary incentives for quick and accurate performance.

8. The private sector can adapt to advances in computer technology more rapidly than the public sector, and greater use of private contractors will make the advances available for use more quickly.
9. Quality Audit

The audit function goes to the very heart of tax administration.

Close contact between public auditor and taxpayer, combined with the low wage scale for tax inspectors, provides a perfect environment for corruption.

Outsourced “tax officers” help in reviewing the performance of the public auditors with care.

Such control is more effective because there is more distance between the auditor and the reviewer. The private auditor may consider his professional reputation more important than government tax agents do.
10. Outsourcing reduces corruption at the collection point.

Private collectors have stronger personal interest in the collection results and more effective mechanisms for penalizing poor performance. You lose the work!
Tanzania Case Study (2008)

11. Cost Effectiveness and Predictability

a) Before outsourcing, Council Treasury staff spent a lot of time on tax collection but after outsourcing the council staff were released to other responsibilities.

b) Many revenue sources were seasonal thus inputs required for tax collection also fluctuate. Employment of staff means costs are fixed throughout the year. Outsourcing will bring in flexibility thus lowering administrative costs.
Effects and Resistance

- It was reported that the Council staff refused to support the private agents with information required to collect the tax.

- Individual Councilors resisted revenue collection in some locations.

- Reported cases of political interferences.
1. Disclosure of Information to 3rd Parties

- Confidential information often will be part of a project, and disclosing this information to a private contractor can be dangerous.

- Outsourced tax Collectors are profit-making businesses, and their success is primarily dependent on how much revenue they collect. (shortcuts or employ aggressive practices giving the government a bad name).
THE BAD

- If the outsourced agents are also collecting against same individuals on behalf of businesses, they may be tempted to use the government information for the collection of other debts.

- The data that can be used to commit identity theft.

- Need to amend the Official Secrecy Act?
2. Tax Retained (Brookers’ Waterloo)

Tax collected retained by agents to cover their costs and profits.

Data from Mwanza Tanzania showed that on average, 32% of the reported revenues collected were retained by the outsourced agents as amounts in recovery of their costs and profits.
3. Corrupt Arrangements

- Potential profits connected with private collection contracts may encourage corrupt arrangements

- May seriously undermine the credibility and working of the outsourcing system.
4. Monitoring the Agents

Outsourcing of incompetent and or dishonest agents; some outsourced agents did not comply with the terms and conditions of their contracts (Tanzania).

They submitted less money than was collected or submitted none at all.

In Kinondoni and Mwanza Tanzania, it was reported that the problems were due to the agents’ lack of experience, reflected in overambitious bids, and partly because the agents in some cases did not pay their own collectors properly which reduced their incentives to collect.
5. **Biased Accessibility (Selective Targeting)**

Temptation by outsourced agents to focus on most easily accessible (or soft targets) taxpayers to minimize their collection costs.

This method does not contribute to expanding the revenue base as intended and also leads to complaints from taxpayers who are approached for tax collection when others are not.
6. Value Added Tax

Outsourced services previously provided 'in-house' will give rise to VAT charges where no such charges previously arose. This will cause an additional burden on cash flow and swirl in transactions with the Exchequer.
7. Withholding Taxes

The cross-border nature of many outsourcing arrangements means that withholding taxes may apply to payments made between the parties.

Again, this may reduce cash receipts to the exchequer.
8. Taxable Presence

For cross-border outsourcing arrangements, in particular those involving outsourcing in different jurisdictions - may give rise to a “permanent establishment” for the customer in the service provider's jurisdiction.
9. Conflicting Objectives

The government’s objective of maximizing long-term compliance without causing financial hardship for taxpayers is fundamentally different from the profit-maximizing objective of a private collection agency.
10. Killing the Goose

Outsourced agents get paid by extracting the maximum amount from taxpayers with respect to a fixed liability.

- Regardless of whether collection reduces the likelihood of the taxpayer being compliant in future or creates a fatal financial hardship to the goose “that lays the golden egg every so often”.
11. Where outsourcing undermines effective tax administration, jeopardizes taxpayer rights, protections, and may not accomplish its intended objective of raising revenue.

- Program may end up causing more loss in cash.

- Tax cash moving from the government to the pockets of Agents in droves!
12. Danger of Corrupt Agents: large sums through corrupt activities. Taxpayers are happy because they can minimize their tax liability through unofficial payments to Agents.
13. Political Interference:-

Tax and Customs work appointments are used as resources for political patronage. Turnover due to political changes discourages professionalism, especially because political supporters traditionally seek such positions because of the opportunities for illicit activity.

14. Pressure to Increase other Taxes – When Agents Fail

Ineffective tax and customs administration causes upward pressure on rates and levies to be increased by the government to make up for lost revenues. Not good for the people.
THE UGLIEST FORMS OF TAX OUTSOURCING

15. INDIRECT TAXES IN THE FORM OF LEVIES

- Levies / Fee charges qualify as “Appropriations In Aid”. Takes the place of direct state funding.
- When allowed to be exercised by a body under the National or County Government, amounts to OUTSOURCED INDIRECT TAXATION!

New (Current) Examples in Kenya

i. Proposed increases in NHIF Rates?

ii. Commission for University Education (CUE) Regulations (Legal Notice No. 8477 of 21 November, 2014)
The Ugliest forms of Tax Outsourcing ..... Cont’d.....

CUE Levies

- Quality Assurance Charges per student enrolled per year – Bachelors Degree – Kshs 1,000/= 
- Diploma per student enrolled per year – Kshs 800/= 
- Quality Audit Charges – Institutional – 1,800,000/= (quoted as 1,8000,000/= in the Gazette Notice) 
- To approve a new course – Each Academic Programme - Kshs 640,000/= 
- Campus – Kshs 300,000/=
Such forms of Outsourced Indirect Taxation are extremely dangerous to the Government of the day

- Makes the government unpopular with the affected public
- Rich grounds for creating disaffection against the National or County government
- Provides fresh “fishing” grounds for corrupt practices / waste
- Many times such levies are / can be challenged under the constitution e.g. CUE levies will go against the Governments vision / drive for universal education, will disfranchise the poor as levies get passed on to the students, many of whom are already struggling.
NOT TOO UGLY

Existing types of Tax Administration Outsourcing

i. Withholding Tax (WHT) arrangements: you deduct (collect) as an Agent of KRA and remit to KRA once a month.

ii. Self Assessment Tax Return System: You assess yourself to tax and pay it to KRA
CAUTION

ANY FORM OF OUTSOURING OF DIRECT OR INDIRECT TAXES MUST TAKE AND CAREFULLY CONSIDER THE SOCIO-POLITICAL RAMIFICATIONS OF SUCH A MOVE!
1. Tax Payer Protection and Guarantees

The law has not imposed deterrent penalties on government tax collection employees who are abusive to taxpayers.

Tax Payer Rights are not sufficiently safe guarded by the Tax Payer’s Charter. There has to be meaningful consequences for violation of Tax Payer Rights.

Lack of such consequences for misbehavior leads to distrust of the government and the justice system.
2. Public Education on why we should pay tax / levies

- A significant part of any tax administration's duty should be facilitative compliance driven.

3. Increase confidence in the government by promptly punishing corruption and all manner of public waste

4. Allow the public to see the benefit of their taxes – when some areas are “super developed” while others are “abandoned”, we are creating rich grounds for tax / levy resistance – County and National Level.
5. Assessment Capacity

- Ensure capacity of the local government revenue administration to assess the actual local revenue base.

- National Government should place experienced officers particularly Economists, Tax Administrators and Planners to support each County. (Assuming Counties will Accept ?!)
6. Reporting (If Outsourced)

- Outsourced tax agents to submit revenues daily or weekly - reduce chances of default and embezzlement

- Similarly, the outsourced agents’ contracts should be for a limited period of time on renewal basis to encourage competition and healthy bidding.
7. Political Commitment

VAT Bill 2012 – Bring back Article 62 which said :-

i. “No Officer shall be personally liable for any act or omission done or omitted to be done in the performance of his functions under this Act unless, having regard to the circumstances of the case, such act or omission is found to be:-

ii. done or omitted to be done willfully or dishonestly by such officer;

iii. attributable to the negligence of such officer; or
iv. done or omitted to be done by such officer in contravention of any provision of this Act or the regulations”.

- Public Officers need to know (by law) that there are direct consequences for improper behavior on the individual.

- Clear sanctions against Public Officers are required in all taxing laws at National and County levels.
8. Policy to guard Taxpayers with economic hardships.

9. Express RIGHTS and NOT DISCRETIONARY rights to enter into compromise and installment arrangements – SHOULD NOT BE A FAVOUR by a National or a County Officer whether at KRA or at any other level.
“WE THE PEOPLE OF KENYA”

FINALLY

The power of tax collectors should always be a power afforded to a government that’s answerable to “We The People”. (Thom Hartman, 2013)
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Analysis


END

Thank You!

Questions / Comments?

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