

MANAGING THE TAXATION OF INFORMAL BUSINESS SECTOR IN MOGADISHU

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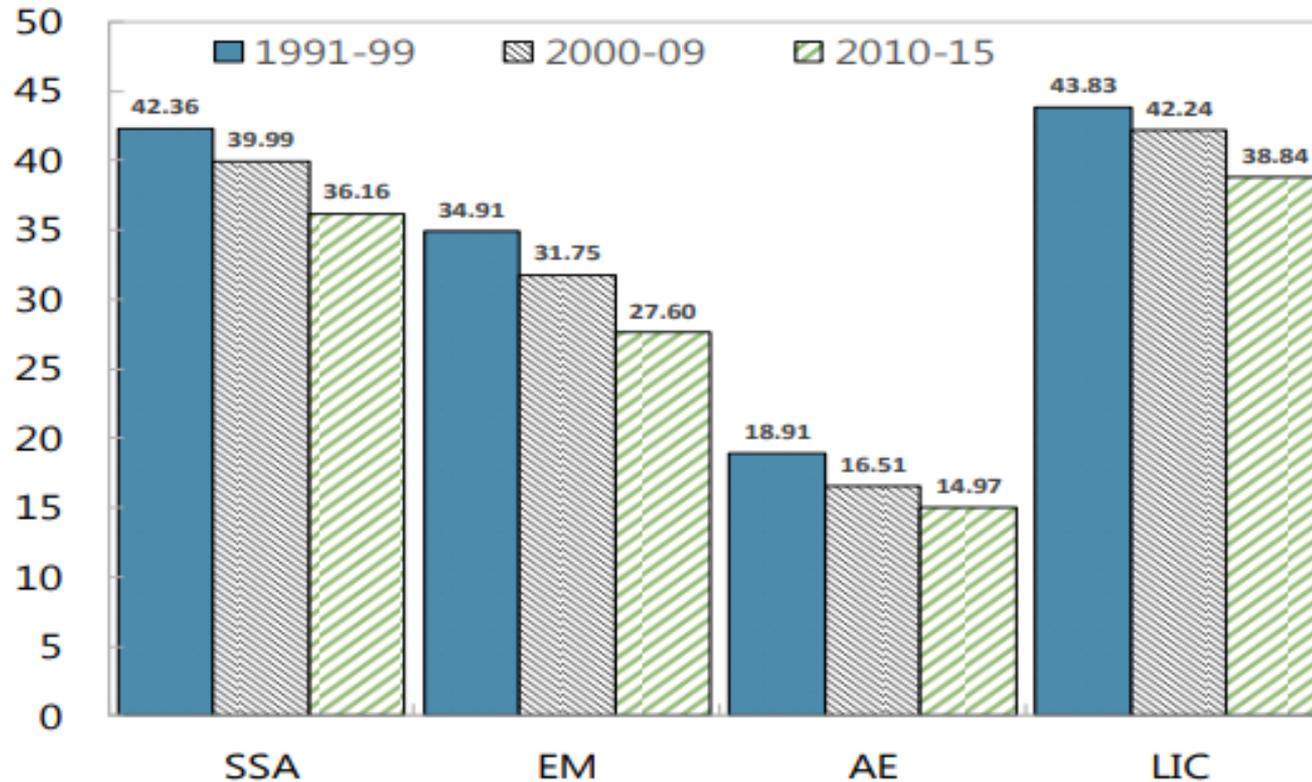
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INTRODUCTION

- The issue of taxation of the informal business sector in developing and transition countries has received increasing attention in recent years.
- Difficulties of taxing informal business sector comprises of limited revenue potential, high costs of collection, opportunities for corruption and potentially perverse impacts on small firms,
- As the benefits of informal taxation are accountability of government to more of its people, economic growth, important source of local government revenue, governance, tax compliance and Taxpaying culture.

Shadow Economy by income level (average, percent of GDP)



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- Somalia experiences presence of extensive informal sector, even though there is no country statistical data for this issue.
- Schneider, (2005) identifies that shadow economy's portion of the GDP accounts 42% in Ethiopia, 36% in Kenya and 45% Uganda as average Sub-Saharan African countries where Somalia includes has above 36%.
- The neighbor and regional countries' share of informality is very high. This gives that Somalia's case can be worsening due to severe fragility (Kalyundu & Norregaard, 2020).

Literature (Ways of Taxing Informal Sector)

- Through consumption (VAT, Import and Export Duty) Action Aid, 2018.
- In Zambia Presumptive Tax on taxis and minibuses, the Turnover Tax on small-scale enterprises, a Base Tax on marketers, Advance Income Tax (AIT) for cross-border traders were introduced Phiri & Kabaso, 2012
- Tanzania also has a turnover tax and presumptive taxes, it is progressive, and its threshold is much lower than in Zambia. They collected the presumptive tax through a Block Management System (BMS) Oduwole & Sanni, 2014,

Literature (Ways of Taxing Informal Sector)

- United Nations recommended presumptive tax in developing countries
- Kenya implemented a turnover tax (TOT) in 2008 at a rate of 3% for SMEs with less than 5million shillings but more than 500,000 shillings annual turnover to replace both income tax and VAT Ndaka & Katee, 2017
- In Ghana the government collects turnover tax of 3 per cent for small firms to replace standard VAT, while microbusinesses are covered by a tax stamp regime, in which a fixed tax is paid on a quarterly basis

Objective and Methodology

- This paper aims to present the how the concerned tax offices managed to tax the informal sector in Mogadishu which is the seat of the federal government.
- The study employs mixed types of data – in qualitative way;
- Firstly, it uses available business data from the ministry of finance archive. Secondly, it interviews economists, tax officials and owners of small scales businesses in order to have their views in different angles and cover gaps coming from the data of the tax offices.
- With this regard, the study identifies some key pressing challenges and finally it recommends several possible solutions.

DISCUSSION OF THE RESULTS

- The taxation culture officially came to Mogadishu in 2012 after 1991, started dealing with informal businesses through ad hoc fiscal system including disorganized tax collection;
- The situation turned into fixed or negotiated amount of payments;
- The ministry of finance reached a time of applying existing laws due enlarged fiscal muscle, 2017;
- Tax base extended and developed a policy of taxing informal sector indirectly; sales tax of imports at customs points 2018;
- Taxpayer registration and improved management started in 2018;
- The government of Somalia is planning to implement a turnover tax in Mogadishu in next year 2021.

INFORMAL SECTOR IN MOGADISHU

- The country's current nature of economy supports the existence of a huge informal sector, as informality widely exists in the region;
- The activities of most dominant (agriculture-fishery-livestock) sectors of the economy are informal and are legally tax heaven;

INFORMAL SECTOR IN MOGADISHU

- The weakness of administrative and enforcement capacity let the informal sector exist in a widespread.
- Most of SMEs in Mogadishu city stay informal because of too high cost to access and stay formal. In the doing business report of 2020, Somalia ranked the lowest country in 190 economies (World Bank, 2020). Studies by (Loayza, 1997) and (Soto, 1988).
- Extremely little engagements of the business community have historically existed.

CONCLUSION

- Somalia's tax system has been recovering rapidly in **Mogadishu** and slightly in other **sub-national states**. Having too informal businesses really burdened on the nation's tax collection in both levels.
- Informal sector, which comprises a wide range of small scales businesses and agricultural sector operators was not properly taxed in Somalia and Mogadishu particularly.

RECOMMENDATION

- To develop joint tax policy, administration and enforcement strategies that reduce the extent of informal activities happening out of tax net. This is also suggested by (Kalyundu & Norregaard, 2020).
- Study recommends setting prioritizing and sequencing of reforms, since recent tax reforms can be simply defined being a basic level, hence tax administration need to be integrated though getting sequenced tougher reforms. IMF's (2017) also highlighted this importance.

RECOMMENDATION

- Making the tax system very simple, understandable to stakeholders and is not damaging the businesses. In other words Fjeldstad et al, (2018) recommend “do not harm” and Bird, (2015) suggests “keep it simple”. These two strategies together build a proper tax administration in fragile countries.
- Better taxpayer services can improve the necessary engagements of the business community as it reduces the long term existing gap between authorities and taxpayers.
- The government should friendly incentivize the SMEs in Mogadishu and simplify the formalizing process and reduce the burden of payments and complex process.

Thanks for your attention

