



Taxing the Informal sector: A case of Dar es Salaam street vendors

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Key Messages

- Most street vendors in Dar es Salaam town centres are eligible and willing to pay presumptive income tax.
- The legal requirements for a recognized physical address as a necessary condition to acquire business licenses from respective municipalities hinders the participation of street vendors in payment of presumptive tax.
- The recognition and authorization of street vendors by the government in 2016 and later the introduction of petty traders' Identity Cards ("Machinga IDs") in 2018 has attracted some formal traders to directly or indirectly join street vending to avoid costs of operating formally.
- There is recognizably lower tax morale among formal enterprises that poses a challenge in the enforcement of the EFD Act for tax compliance.

Introduction

Recognizing the crucial role that domestic revenue mobilisation plays in financing sustainable development, governments in developing countries have increased interest in taxing the informal businesses to increase domestic revenue collections (Joshi & Ayee, 2008). However, the sector is often characterized by unregistered businesses and poor tax administrative systems, resulting in a substantially reduced tax basis.

The sector forms a large proportion of the economy in both transition and low-income countries. In Africa, for instance, it is recorded that every 8 out of 10 people work informally (ILO, 2018)¹. According to Medina *et al.*, (2016), the segment of informal economy in Sub-Saharan Africa (SSA) remains among the largest in the world, even though this share has been gradually declining, as seems to be the case globally. There is significant heterogeneity in the size of informality in SSA, ranging from a low of 20 to 25 percent in Mauritius, South Africa, and Namibia to a high of 50 to 65 percent in Benin, Tanzania, and Nigeria (Medina, *et al.*, 2016).

Looking back on revenue collection from the informal street vendors, in 1983, Dar es Salaam city introduced "Nguvu kazi" minor license² and later abolished in 2004. In July 2000, the Tanzania Revenue Authority (TRA) introduced a new simplified tax schedule for small taxpayers (as well as simplified balance sheets and tax declaration forms), as part of a drive to make it easier for informal sector operators to formalize and start paying taxes.

¹ ILO (2018). *Women and Men in the Informal Economy: A Statistical Picture (Third Edition)*

² In response to collect more revenues, the government enacted the 1983 Human Resources Deployment Act, which required every able-bodied person to be productively engaged. To facilitate that engagement, the law provided for local authorities to issue minor licenses ("nguvu kazi license") for which they paid a one-off annual fee.

Further, as part of the Business Environment Strengthening for Tanzania (BEST) Programme³ reforms, the requirement for annual renewal of business license was discarded in 2004 and re-instated in 2014, without re-instating the minor license (Olomi & Charles, 2016; WBG, 2010)⁴.

In July 2004 the government of Tanzania through the Income Tax Act 2004, later amended in 2006, formalized a presumptive tax scheme by introducing a new simplified taxation schedule for small business taxpayers as part of a drive to make it easier for informal sector operators (including start-up businesses) to register, formalize and start paying taxes. A presumptive tax system is one where informal traders are taxed based on their annual turnover (ATAF and GIZ, 2014)⁵. Taxpayers under this system are not obligated to prepare and submit audited accounts to the revenue authorities.

The adoption of the presumptive scheme is consistent with the objectives of the National Small and Medium Enterprise Sector Policy of 2003. The scheme includes an opt-out for micro, small and medium scale enterprises (MSMEs), allowing them to prepare audited accounts and pay tax based on profits (TRA, 2011)⁶. The turnover bands and their tax rates range from Tshs. 0 for annual turnover less than 4,000,000 to 450,000+3.5% of the turnover in excess of Tshs. 14,000,000 but does not exceed Tshs. 100,000,000.

However, the position of street vendors is not openly documented in the Act. In order to address the challenge of taxation of the informal sector, TRA under the department of domestic revenue introduced a presumptive tax scheme to simplify the taxation of operators in the informal sector previously underrepresented in the formal tax registry. TRA has operated a presumptive income tax through the Block Management System (BMS) since 2005 (ATAF & GIZ, 2014) with the aim of promoting compliance and registration of all eligible small and medium scale enterprises. The BMS captures information related to business type, sector, geographical area, and level of economic activities among others (TRA, 2011) in order to be able to deal with the heterogeneity characteristics of informal businesses and operating environment.

Business regulations however require that any business to be able to pay tax should get Tax Identification Number (TIN) from TRA and business license from respective municipalities.

Key requirements being physical address and introduction letter from “Mtaa” office. Alternatively, vendors have to trade from designated market places and pay stipulated charges as outlined by respective municipal by-laws. However, the practice has been contrary, as street vendors operate in undesignated areas due to easy access to customers and non-payment of rentals.

Street vendors, an important group in the informal sector, has been changing in its size and capital over time in Tanzania (Msoka, 2007). In the past, street vending was to a large extent a survival or a coping strategy against disruptions to livelihoods in urban centres, it has now become an admired and profit-making sector (Msoka, 2007). This is so because operating informally is considered more affordable since costs such as formality entry costs (registration and licensing) and recurrent costs (rent, taxes, and other contributions) are not incurred (Joshi, *et al.*, 2014).

However, the government has gradually began to review its understanding of the occupation following observed uptick in the value of items it trades and the size of capital deployed (Msoka, 2007; TRA, 2011). This created the appetite to target the group for tax, though difficult to find documented achievements. In recent years there has been an increase in the number of street traders permitted by the government to operate outside market places and formally built structures.

This raises questions in relation to charges, taxes and street vendors’ eligibility to operate and how they affect government efforts to implement a presumptive taxing system. It was therefore important to explore revenues collected from street vendors by the government, their willingness and the potential of them entering into the presumptive tax system. This brief therefore documents the operationalisation, opportunities and challenges of street vending in Tanzania.

The study was conducted in Dar es Salaam city, using three main independent methods of data collection that complement each other: documentary review, in-depth interviews, and Focus Group Discussions. Purposive sampling technique was applied to obtain a total of twenty (20) street vendors for (4) FGDs comprising five (5) participants each, together with eight (8) key informants for in-depth interviews. Fieldwork for this study was undertaken at different times between August 2017 and August 2019. The qualitative data from interviews and FGDs were analysed through a thematic approach inductively deriving themes from the data.

Findings

Table 1: Breakdown of estimate payments by street vendors

Type of payment	Maximum per day (Tshs.)	Maximum per month (Tshs.)	Responsible institution
Daily space rent	1000	30,000	Municipality
Waste collection	500	15,000	Municipality
Security	500	15,000	Self
Total		60,000	

Source: Field data 2017 from Kariakoo, Mwenge, Manzese

³ One of the initiatives to address the challenges identified in the National Economic Empowerment Policy. The Programme started in February, 2005 and aims to: i. reduce the burden of doing business in Tanzania especially SME by reforming and eliminating regularly, procedural, and administrative barriers; ii. enhance efficiency in service delivery by the Government to the private sector, including timely resolution of commercial disputes; and iii. Promote and maintain better partnerships between public and private sector.

⁴ World Bank Group Report on Better Regulation for Growth, Governance Frameworks and Tools for Effective Regulatory Reform: Regulatory Capacity Review of Tanzania.

⁵ African Tax Administration Forum (ATAF) and German Cooperation (GIZ). Taxation of SMEs in Africa, Good Practices and Lessons Learned from Block Management System (BMS) in Tanzania.

⁶ Tanzania Revenue Authority Report on Review of Informal sector for Taxation Purposes

Table 1 indicates that the payments by street vendors before the introduction of Machinga IDs are estimated at up to Tshs. 60,000 per month. Of this total, Tshs. 45,000 i.e. space rent and waste collection levy went to the municipality/government. On the other hand, registered and licensed traders pay a minimum of Tshs. 54,100 (presumptive tax, license fee, waste collection and fire charges) per month to the government (see table 2). That is to say, the two groups pay almost similar amounts to the government. However, formal businesses pay more due other recurrent costs such as rents to landlords.

Table 2: Estimate payments by a formal business in Kariakoo

Type of payment	Per month (Tshs.)	Per Year (Tshs.)	Responsible institution
Premise rent	250,000-2,000,000		Landlord
Presumptive tax	8,300	100,000-3,460,000	TRA
License fee	12,500	150,000 - 300,000	Municipality
Waste mgt.	30,000		Municipality
Fire	3,300	40,000	Municipality
Security	20,000		Self
Total	Min 304,100		

Source: Field data 2020; Finance Act 2019; TRA, 2019 (researchers' calculation)

Street vendors willingness to pay presumptive tax

Findings from both FGDs and in-depth interviews suggest that despite that street vendors are capable and willing to pay presumptive income tax, they are constrained by several recurrent costs including lack of adequate designated business premises (physical address) in the high human traffic areas. This is supported by one vendor during FGD; *“for your information, 90% of us can pay for business licenses and more taxes but the government has not decided to give us a good business area around Mwenge.”* A related confirmation was given by one VIBINDO Society⁷ staff:

“I know my people very well; they are rich and capable of paying taxes, but both the Local and Central Governments have not decided to listen to us and implement our ideas to formalize and tax these people. We need to identify, assess and find a proper place that is accessible to customers with necessary infrastructures for vendors to conduct their businesses. Slowly they will pay taxes. Let the government stop taking short time solutions and be ready to incur costs to prepare friendly trading places”

The results from street traders and their representatives suggest that there is a need for incentive for businesses to formalize and pay the required taxes/costs. Jaramillo (2009) in Lima, Peru, reported that a group of firms were offered free business licenses and support with the registration process, but only one in four firms was willing to formalise even with registration costs largely eliminated. He attributed that to recurrent costs of being formal along with low perceived benefits of formalisation.

Governments need to develop policy measures that provide such sustainable incentives to informal enterprises to formalize and remain formal. It was further found that in the absence of a streamlined governance framework for informal business activities and business sites, opportunist actors have taken the role of informal landlords, protectors and tax collectors. Findings indicate that there were places in the town centres that were “ruled” by opportunists, who must be paid daily, weekly or monthly by informal operators in a particular street or location.

“In some areas in the past including Mwenge, there have been private people who conspired with some unfaithful government officials and conducted illegal taxing of street vendors in return of protection from our by-laws.” (Interviewee)

This “extortion” was practiced by one or multiple actors on a single business. Taxtortionists range from local government (mtaa) leaders, security guards/police, owners or workers of adjacent properties, guys who claim control of a street, area or site. It is usual for initial occupiers of sites to “lease it out” to subsequent users regardless of whether they have a formal right to it. The daily rates range from Tshs. 2000 per week to Tshs. 5,000 per day (Olomi & Charles, 2016). Around busy bus terminals and adjacent to market centres, the charge is at least 1,500 per day.

Currently, following the introduction of the small entrepreneur IDs in 2018 petty traders pay only 20,000Tshs. per year with no additional costs, which allow them to operate in public places freely. The amount is paid to the TRA through their respective local government offices. Further noted that there were complaints among formal business traders and municipal officials for street vendors no longer contributing to the waste collection charges. They were termed as main producers of wastes in their areas. This has posed a critical challenge to the municipality in dealing with waste management. However, street vendors were implementing what government leaders ordered.

Street vendors eligibility for paying presumptive tax

The findings show that TRA has set the lowest rate for presumptive income tax (Tshs. 100,000 per annum) payable in four installments as a drive to make it easier for informal sector operators (including start-up businesses) to register, formalize and start paying taxes (TRA, 2019; TRA, 2011). This rate applies to businesses with an annual turnover of more than Tshs. 4,000,000 but less than Tshs. 7,000,000 and do not have complete records.

The findings suggest that street vendors’ eligibility for presumptive tax is subject to the area of operation (the busier the streets the higher the turnover), majority street vendors in town centres like Kariakoo and Mwenge have an annual turnover exceeding four million (Tshs. 4,000,000) hence qualified for presumptive income tax. Since physical address is a necessary requirement for a business to be issued with a business license from the respective municipalities and start paying taxes, this has become an obstacle to street vendors who operate their activities from undesignated areas.

⁷ An umbrella organization of informal economy operators in Tanzania.

Street vending impact on presumptive taxing system

The introduction of Machinga IDs in 2018, on one hand, has helped in solving the challenge of taxtortionists and harassment to the street vendors by authorities. On the other hand, findings suggest that the presence and recognition of street vending from restricted areas with the requirement of possession of an ID have stimulated some of the licensed and presumptive taxpayers to join street vending. The reason being the costs of becoming and remaining formal are higher. In addition, some formal business enterprises/companies silently enter into a deal of giving merchandise to street vendors to sell to avoid paying taxes. The following statement from TRA official substantiates:

“Nowadays the government is experiencing shrinking of revenue collection in Kariakoo and closing down of some shops. The investigation discovered it’s partly due to many taxes and some enterprises using street vending in their operations.”

The recognition of street vendors in the restricted areas is however associated with political interest. The situation has again posed a challenge to TRA staff in the enforcement of tax compliance through the use of the “Electronic Fiscal Device”. It has become difficult for TRA staff to differentiate buyers from licensed enterprises who should be offered with EFD receipt unlikely from the street vendors.

Findings also suggest that there is a risk of lowering the tax morale of formal businessmen in the respective places. Their places of operations have been invaded by street vendors who pay less to the government and other operational costs, selling goods at a cheaper price and competing for the same customers.

Conclusion and Policy Recommendations

Taxation plays an important role in raising revenue to sustainably finance development for economic growth. It is argued that the taxation of the informal sector in Tanzania is important given the large size of the sector and as a way of preserving the incentive system and promoting one of the canons of taxation, which is equity. The presumptive income tax system has been regarded as an effective way that facilitates administrative efficiency; minimizes time for tax collection; enhances compliance; eliminates chances of tax evasion, rationalizes the turnover tax regime and increases revenue.

The study suggests that the majority of street vendors in Dar es Salaam town centres are capable and willing to pay presumptive income tax. However, the lack of a proper

regulatory framework to accommodate the use of urban spaces have affected the implementation of the presumptive taxing scheme.

The following recommendations are made to nurture the eligible and growing tax base for smooth operation of the existing presumptive taxing system:-

First, there is a need to conduct a survey to obtain statistics of street vendors. This includes a thorough assessment of the type, capital size, location and earnings. This will enable the effective allocation of resources to enhance businesses to flourish but also enhance tax collection targets in accordance with the capacity of the identified informal sector operators.

Second, is building the capacity of street vendors’ associations/representatives to affect the activity of registration and taxing (indirect formalization).

Third, government in collaboration with vendors’ associations to set up a good working environment for vendors by redesigning the urban land-use plan to accommodate street traders by providing workspace and construction of business premises in town centres and be operated by vendors’ associations or other private investors.

Finally, providing tax education and other incentives including provision of loans, training, and strengthening deterrents (fines, restrictive law enforcement) for street vendors to opt for formalization of businesses.

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