

Modern Cooperativism: Solution for formalization and broadening the tax base?



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Background

The Tax Authority of Mozambique (AT) has recently launched the cycle of training courses under the National Cooperative Development Program - PNDC, in partnership with the Mozambican Association for the Promotion of Modern Cooperativism (AMPCM).

The program's main objective is to "boost a ho-

listic economic organization, where the cooperative model is the base for the transformation of the informal sector and national economic integration." Fundamentally, what is at stake is an organization and structuring of the national informal sector which, according to the President of the AT, quoted by the newspaper O País, edition of

July 7, 2022, has been a factor of macroeconomic distortion and fertile ground for the proliferation of unfair competition and stimulus to tax evasion, including the development of tax and economic crimes, such as counterfeiting, smuggling, embezzlement and tax elision in domestic operations and in flows resulting from foreign trade.

Because the program in question targets,

among others, a sector that has served as a source of livelihood for millions of Mozambicans in vulnerable situations, this Development Review reviews some of the merits and demerits of the program, existing expectations, and its potential contribution to transforming the country into a “middle-income economy by 2035.

Cooperativism for broadening

the tax base: starting the house from the roof?

As in most developing countries, the Mozambican economy is based on informality, with 90% of

the population working in the informal sector¹.

Leaving aside the lack of consensus on whether formalizing this sector should in fact be a major priority for the government, the reality is that due to the high collection costs, the AT has been facing major challenges in taxing it.

Attempts to tax this sector by tax administrations in developing countries have repeatedly resulted in extremely high administrative costs in relation to the potential revenue to be collected². It is in this context that the strategies for formalizing the sector have favored approaches that not only reduce collection costs, but also tax compliance by economic agents. By their “agglutinating” nature, gathering several individual agents into a single formal entity, cooperatives have been a viable option in this sense.

The cooperative model is not a new concept in the national economic reality. The model goes back to the post-independence period, having only changed its configuration, taking on the designation “modern cooperatives” to differentiate the more current models in the context of the modern, more competitive economy from those of the socialist economy period. Currently, there are 201 active modern cooperatives in the country³.

It is in this context that, capitalizing on the work that has been done for a little over a deca-

de by the AMPCM, the Government, through the PNDC, sees this model as an element to overcome the high costs that would be incurred in the direct collection of taxes from the different economic agents/small businesses in the informal sector, by charging a representative entity and thus broadening its tax base.

Without lessening the initiative’s merit, we must recognize that the conditions are not yet created so that, more than a broadening of the tax base, the cooperativism promotes the transformation of the informal sector in the most consistent and efficient way possible⁴. The truth is that the model that now appears as the AT’s trump card for formalizing and broadening the tax base remained for a long time with an incomplete legal framework. In fact, this is a situation that still exists today.

The country took an important step with the approval of the Cooperative Law, Law 23/2009, of September 8, adjusting it to the new constitutional framework marked by an increasingly competitive reality. However, and showing some lack of interest from the Government in the matter, a little more than 13 years after its approval, it has not yet been regulated. A process that, according to article 98 of the referred Law, should have been solved within 180 days of its publication.

The resolution of this omission by the Gover-

¹ <https://jornalvisaomoz.com/ciencia-dos-dados-para-melhorar-os-meios-de-subsistencia-dos-trabalhadores-informais-em-mocambique/>

² <https://www.ictd.ac/publication/taxing-the-informal-economy/>

³ <http://www.at.gov.mz/por/Noticias/MOCAMBIQUE-APRESENTA-CONDICOES-VANTAJOSAS-PARA-UMA-MELHOR-ORGANIZACAO-ECONOMICA>

⁴ https://salcaldeira.com/index.php/pt/component/docman/doc_download/165-lei-n-14-2012-de-8-de-fevereiro-de-2012-lei-organica-do-ministerio-publico-e-o-estatuto-dos-magistrados-do-ministerio-publico

nment has been recurrently demanded by the cooperatives operating in the country, more particularly by AMPCM, but without success⁵. In addition to the lack of regulation, there is the absence of a special fiscal framework for cooperatives, and they are normally taxed under the cur-

membership of informal people in cooperatives

to two different approaches of analysis. The first is the empowerment approach. In this view, the non-formalization of enterprises through the cooperative model would be justified by factors such as lack of information and illiteracy. In this case, the training cycle now launched on a national scale would be sufficient to formalize a good part of the informal ones.

In the second, formalization is seen as a rational choice resulting from a cost-benefit analysis in which respect for standards provides access to a set of benefits but entails costs⁶. The benefits usually take the form of access to credit and capital markets, government procurement contracts, other foreign markets, and services and facilities provided by the state. And in the particular case of the domestic market, this set of benefits also includes avoiding the frequent costs of informality, including the payment of bribes and the need to provide free services, relocate, or close businesses to avoid taxes.

In this perspective, the establishment of a clear regulatory framework, the facilitation of the legalization process of cooperatives (reducing bureaucracy and costs) and the creation of a fiscal

regime adequate to the reality of cooperatives, accompanied by training/capacity building actions, would have a relatively more catalyzing impact on the formalization of the sector.

But why should these factors be taken more seriously?

From a theoretical point of view, the weak

can be explained by two main reasons that refer

regime adequate to the reality of cooperatives, accompanied by training/capacity building actions, would have a relatively more catalyzing impact on the formalization of the sector.

These mechanisms for reducing the perceived costs of formalization become particularly relevant taking into consideration the inhomogeneous character of the informal sector. In fact, besides including a relatively more financially robust segment of small and medium enterprises, this sector also includes subsistence enterprises operating with low profit margins where tax incidence would likely be more regressive.

This heterogeneity puts into a different perspective the nearly 10 million dollars that, according to the AT, were lost in the first quarter of this year due to the informal sector. Because more than resources that the tax authorities could not "capture", a good part of them represent an indispensable part of the low income of families that have their subsistence base in the informal sector.

More than taxing, it is necessary to ensure that the

⁵ <https://www.opais.co.mz/cta-e-ampcm-juntos-pela-reducao-da-informalidade-e-alargamento-da-base-tributaria/>

⁶ <https://opendocs.ids.ac.uk/opendocs/bitstream/handle/20.500.12413/2309/ICTD%20Working%20Paper%204.pdf>

resources mobilized finance the development process

The Government's expectation is that, with the organization of these productive sectors, the na-

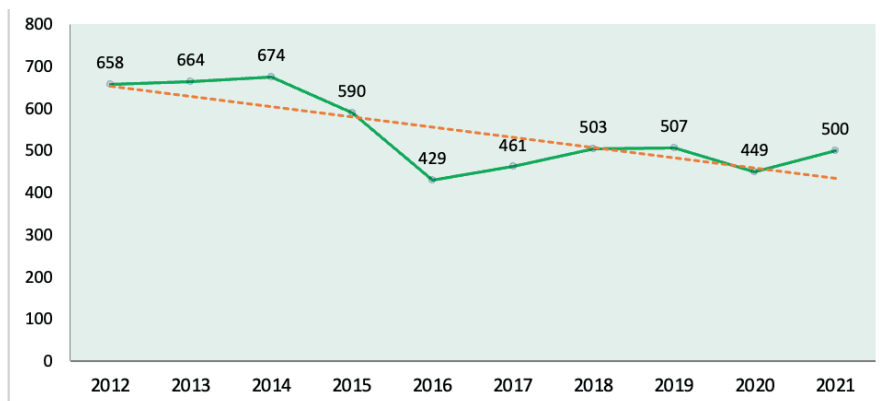
tional economy will be catapulted from a subsistence economy to a "middle-income by 2035" economy, in line with the National Development Strategy 2015-2035.

At first glance, this seems to be an easily achievable goal, but when analyzing the most recent trend of the economy in the matter, it is easy to see that it is nothing more than an "aspiration", mere rhetoric, and that the expectations on the program are, to some extent, unrealistic. In fact, instead of a convergence to the develop-

ment goal of a per capita GDP of USD 2,957.4 by 2035, in general, and due to the unreported debt crisis, the most recent trend has been a reversal of the gains achieved in the period prior to the approval of the strategy. Starting from a per capita GDP of around USD 600, seven years after the strategy was approved, the figure has reduced to close to USD 500, just 17% of the target set.

The challenges will be particularly greater considering that the gains will result, fundamentally,

Graph 1: Evolution of GDP per capita over the last decade (2012-2021)



Source: Bank Mundial (<https://data.worldbank.org/indicator/NY.GDP.PCAP.CD?locations=MZ>)

from better economic organization of the informal sector with its structuring into cooperatives, and few results can be expected from the allocation of the additional resources that will be collected from the broadening of the tax base. The reason is simple and lies in the way the Government applies the resources in order to promote development.

Ideally, public investment should play a major role in stimulating the economy and creating the conditions for private investment to take place. Meanwhile, government action has two ambiguous effects on economic growth and development⁷: On the one hand, through the positive externalities on private capital (productive spending) and, on the other, by the fact that they

necessarily imply an increase in the tax burden, reducing the resources available to the private sector and the growth of the economy.

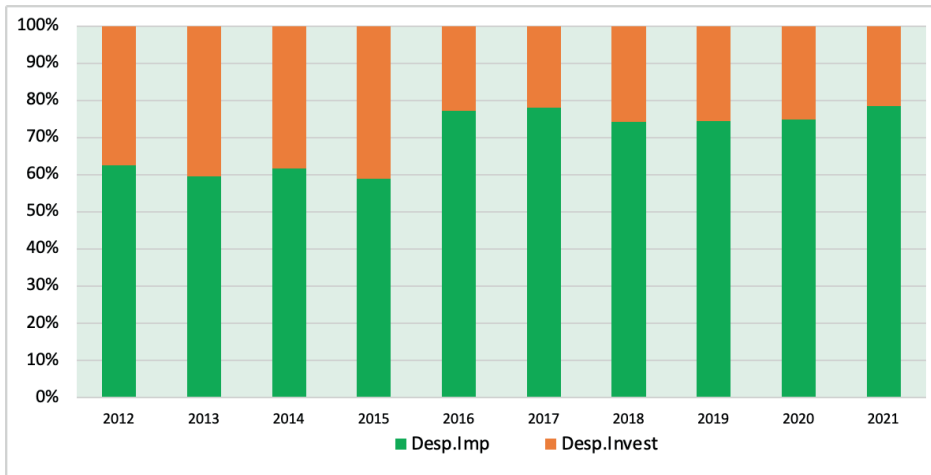
In the case of the national economy, the analysis of the composition of expenditure in the most recent period reveals that the resources mobilized have been mostly channeled to unproductive expenditures (operating expenses and debt service), which do not affect long-term growth, to the detriment of expenditures that are positively related to long-term economic growth, such as investment expenditures, with a weight of less than 10% of the total.

Conclusion

This Development Review analyzed the me-

⁷ https://dash.harvard.edu/bitstream/handle/1/3451296/Barro_GovernmentSpending.pdf
<http://www.repositorio.uem.mz/bitstream/258/159/1/2019%20-%20Garrine%2C%20Edson%20Zeca%20de%20Oliveira.pdf>

Graph 2: **Public expenditure composition in the last decade (2012-2021)**



Source: **General State Account (various years)**

rits and demerits of the National Cooperative Development Program, the existing expectations,

and its potential contribution in transforming the country into a “middle income economy by 2035”. The results of the analysis study point to the following:

- Despite its merits - opening space for greater capitalization of the opportunities of transforming the informal sector into cooperatives, the success of the program, and especially in protecting the most vulnerable segment of the informal economy, is contingent on creating a regulatory and fiscal environment that actually maximizes the net benefits of for-

malization.

- The program will have a relatively limited role in transforming the country into a “middle income economy”. The policy of revenue mobilization must be complemented by public investment in activities to increase productive capacity and generate linkages and externalities for action by the other sectors of the economy.



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