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LOCAL ECONOMIC GOVERNANCE IN MYANMAR

JARED BISSINGER

Policy Dialogue Brief Series No. 10

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Yangon

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ONE: INTRODUCTION

Reforming local economic governance is essential if the public is to enjoy the benefits of Myanmar's transition, and given their substantial exposure to public criticism when expectations are not met, actors at this level have strong incentives for reform. Nonetheless, local governance actors have been slow to pursue reforms, due to their lack of authority and capacity, the presence of vested local interests, and the many administrative layers separating them from the country's top leaders.

The township level of government is a key point of interaction for most people in Myanmar. Local governing authorities have a wide range of economic powers, from collecting revenues, to awarding concessions, to authorizing certain economic activities. They possess functionally decentralized powers, and often have significant discretion over the implementation of laws and rules, and they have also been given some authority to experiment, as long as they remain within their remit. Where they work with business, local governments' responsibilities emphasize licensing and taxation rather than regulation and service provision, and the tax structure is skewed heavily towards an up-front, fee-for-permission system – the legacy of an authoritarian state.¹

This policy brief begins by examining the relatively broad concept of “local economic governance,” then explores the decentralization of economic authority. The second section examines governance structures, with a particular emphasis on development affairs organizations (DAOs). The third section looks at subnational government revenue, and the fourth at licensing of selected economic activities through auctions. The brief concludes with recommendations on a number of local economic governance issues.

1.1 Defining Local Economic Governance

This policy brief focuses on the governance of private economic activity, conceptualized broadly to include both individual entrepreneurs and formal businesses. This broad definition covers a range of governance activities, including but not limited to:

- **Granting permissions and licenses:** business operating licenses (non-exclusive and exclusive), sector/activity-specific licenses, construction permits, land registration, and permission letters;
- Collecting revenue: taxes, fees, fines, and other revenues;
- Providing services: local infrastructure and services, sector-specific services, business development programs, state-administered loan programs, and resolution of disputes;
- Regulation and monitoring: setting rules and standards that influence business operations, and conducting inspections;
- Engagement and dialogue with business: constituent engagement, providing information.

1.2 Administrative Decentralization and State/Region Governments

The 2008 Constitution created new state/region (S/R) governing structures, including a chief minister, a “cabinet” of S/R ministers, and a unicameral *hluttaw*, with authorities defined in Schedules 2 and 5.² The practical implication of this change is that S/R governments have final authority for licensing and oversight in sectors where S/R parliaments make laws and collect revenues.³ Though S/R governments lack authority to issue licenses in areas where the Union government collects revenues, Union ministries often work through the state or region ministry in these areas.⁴

This points to a key characteristic of the decentralization process in Myanmar: *It is a process of decentralizing authority within the existing structure, instead of a decentralization of structures themselves.* The structures of the S/R government report both to S/R ministers, and to the Union government by way of the S/R ministers. The level with decision-making authority in this relationship depends on the specific economic activity in question. This form of decentralization is evident in the functioning of administrative bodies at the S/R, district, and township

¹ The system of advance payments helps the state circumvent the pervasive issue of poor compliance.

² These schedules, which are the S/R legislative list and the S/R revenue list, respectively, also guide the division of administrative authority over economic activity, though this is not explicit in the Constitution.

³ For example, licenses for freshwater fisheries (an area that falls under the S/R authority in Schedule 2 of the Constitution) need to be approved only by the S/R government, not the Union-level Ministry for Livestock, Fisheries, and Rural Development.

⁴ S/R ministers, for example, have various responsibilities for Union-level activities, including “submitting reports to Union ministries, monitoring, coordinating plans mandated by the central government, and assisting the Union government.” Jared Bissinger and Linn Maung, *Subnational Governments and Business in Myanmar* (Yangon: The Asia Foundation and Myanmar Development Research Institute-CESD, February 2014), 15.

levels, which are tasked with implementing on behalf of *both* the S/R and the Union. Despite their Union ministry connections, these bodies collect (or assist in the collection of) revenue for the S/R governments.⁵ Though the S/R governments receive revenue directly, the Union government retains influence via budget proposal oversight and the role of the General Administration Department (GAD) in decision-making.

TWO: MAPPING LOCAL ECONOMIC GOVERNANCE

At the S/R level, a range of institutions fall under the authority of S/R ministers.⁶ Fewer department offices exist at the township level, though core administrative departments are present across all townships, including the GAD, Internal Revenue Department (IRD), Department of Agricultural Land Management and Statistics (DALMS), and Myanma Economic Bank (MEB).⁷ Three government actors (DAOs, the GAD, and the IRD) have the most regular and meaningful township level interactions across economic sectors. DAOs have a range of economic authority, including a strong focus on urban service provision and licensing. The GAD is the most powerful authority at the township level, and plays a key role in coordination and oversight, while the IRD is focused on revenue collection.⁸

Line ministries are often present at the township level – albeit with small offices – to engage businesses in their sector.⁹ Some townships have industrial zones, governed by management committees that have some quasi-governmental functions. Sector-based departments – those besides DAO, GAD, and IRD – have a strong

focus on licensing and taxation, which are approved at higher levels. Despite significant overlap between government departments tasked with similar responsibilities,¹⁰ local coordination does exist, for example through weekly interdepartmental meetings at the township level that are generally orchestrated by the GAD.

2.1 Development Affairs Organizations

Development affairs organizations are the primary urban governance bodies and provide both a range of government services and oversight in various economic sectors. DAOs are the only department of the former Union government to have been completely decentralized, and their legal mandate stems directly from S/R governments, all of which have passed DAO laws since 2012.¹¹ DAOs thus have no affiliated Union ministry, and report only to the S/R ministers for development affairs, who, through the Department of Development Affairs, “coordinate and supervise township DAO offices.”¹² Of the various services provided by DAOs, the most important are urban road construction and maintenance, sewage and sanitation, street lighting, and urban water supplies.¹³ DAOs also issue business and “dangerous goods” licenses and run annual auctions for business licenses in certain sectors such as slaughterhouses, ferries, and pawnshops.¹⁴ Finally, the DAO is engaged in the permitting process for both public and private construction projects.

Licensing: Issuing business licenses is a key economic governance function for DAOs. In general terms, there are two different types of DAO licenses: non-exclusive business operating licenses (i.e., there is no limit on the

⁵ They receive funds from the S/R government to cover some of their operating expenses, though many of these funds are provided to S/R governments through transfers from the Union fund.

⁶ Though all of Myanmar’s S/R governments have largely the same departments, the structure varies somewhat between different states/regions because it is up to the S/R to determine the configuration.

⁷ Others are present in only a few townships, a variation due to differences in local economic circumstances. Some departments, such as the DAO and the Housing Department, are urban focused and therefore play a more important role in heavily urbanized townships. In rural townships, other departments, such as the Department for Rural Development, the Department of Agriculture, and the Department of Forestry, play a more central role. There is also variation in township-level departments based on geographical characteristics.

⁸ Of course, DAOs and the GAD also have important revenue collection functions, as do the vast majority of ministries involved in economic governance. The major difference is that for DAOs, the GAD, and others, revenue collection is one of the many duties in their mandate, whereas IRD is solely concerned with collecting taxes, which form a significant part of the country’s overall budget.

⁹ Note that the government departments covered in this report represent many but not all departments that engage with business. Within any given S/R government, there may be as many as 90 government departments.

¹⁰ For example, in urban areas DAOs are responsible for road construction, though in rural areas that responsibility lies with the Department for Rural Development or the Department of Highways, depending on the type of road. In border areas, the Ministry of Border Affairs is responsible.

¹¹ However, these laws either are all identical, or bear very close resemblance to the former Union-level SLORC law for DAOs, SLORC Law No. 5/93. Yet because they are passed at the S/R level, the legal mandates of DAOs can theoretically differ between different states/regions.

¹² Direct implementation is handled by township DAO offices, to which the S/R office delegates many responsibilities, including “annual planning, designing activities, crafting budgets, and routine municipal management and service provision.”

¹³ Other services include issuing business licenses to many different types of businesses, including restaurants, small shops, local lodging houses, skilled businesses, slow-moving vehicles, and others.

¹⁴ Information provided by the DAO, Taunggyi Township, Shan State.

number of businesses that may obtain this type of license) and auction licenses. Licensing for cattle markets, slaughterhouses, privately owned markets, small loan businesses (pawnshops), and ferries is generally handled through auction licenses, while licenses for roadside stalls, bakeries and restaurants, dangerous trades, and slow-moving vehicles are non-exclusive.¹⁵ Obtaining non-exclusive DAO licenses requires only a completed application form, an ID card copy, a household list, and the ward administrator's recommendation to the DAO. DAOs also have oversight of billboards in urban areas, with the authority to license and collect revenue from them; however, the approval process goes higher.

Construction permits: Construction permits involve numerous departments and usually require 14 to 23 days for DAO approval, depending on the scale of the project. While the cost to developers of the DAO's "supervision fee" appears significant (1 percent of the building cost), construction permits account for only a small portion of the DAO budget – generally less than 10 percent. DAO engineers are the primary inspectors.

Public construction projects tendered via government have a different process,¹⁶ involving the township administrator (GAD), the DAO director, an engineer from the Ministry of Construction, and a relevant sector ministry official (e.g., school construction would involve the Ministry of Education). Unlike commercial construction projects, engineering responsibility lies with the Ministry of Construction. Some regional governments exempt public projects from supervision fees.

Revenue: DAOs are unique in relying on local revenue for a significant majority of their budget. They receive no funding from the Union government, and the business license auction has emerged as one of the most important sources of DAO revenue.¹⁷ Non-auction business license and commercial billboard fees are also significant income sources for many DAOs, while taxes and fines remain small or negligible contributors to their budgets. Fines

are often unworkable due to the costs and administrative challenges of enforcement, leading to negotiations, which make a poor deterrent to illegal behavior.

DAOs also benefit from revenue sharing, such as their receipt of 5 percent of the total income tax collected by the IRD at the township level.¹⁸ A second sharing of revenue occurs via transfers between DAOs in the same state/region.

2.2 General Administration Department

The General Administration Department is the most powerful authority at the township level, and has regular interactions with the public. As the coordinating township office, the GAD is responsible for organizing interdepartmental meetings with other government offices, dispute resolution, and overseeing the collection and aggregation of population registration data. The GAD's primary economic and business role is focused on licensing and certification, whether for the sale of restricted goods (such as alcohol or property) or for activities such as land transfers or construction.¹⁹ The GAD is responsible for collecting four taxes: land, excise, mineral, and irrigation.

2.3 Internal Revenue Department

The Internal Revenue Department (IRD) is the Union government's taxation agency, and generally has a township office. The IRD collects the two most lucrative taxes, the commercial and income taxes, as well as stamp duties and other revenues. The commercial tax is sector specific, fixed at 5 percent of total sales for most goods and services. While the cost of intermediate goods is theoretically deductible, this rarely occurs.²⁰ Township IRD offices gather information and determine a tax amount based on observable characteristics, including the amount of tax paid last year, the size of the business, and the number of employees. The income tax is the other major tax, and is theoretically based on a net income schedule.²¹ In practice, though, income tax

¹⁵ This is not an exhaustive list, but a compilation of the major non-exclusive and exclusive licenses.

¹⁶ For government projects, inspections are conducted by a group of government officials when 25 percent, 50 percent, 75 percent, and 100 percent of the construction has been completed.

¹⁷ Generally, auction licenses account for 35-70 percent of revenue.

¹⁸ Note that these transfers technically happen between the S/R IRD and the S/R Department for Development Affairs, which then assigns the funds to the respective township DAO. Interview 032 with government, July 16, 2015, and Interview 038 with government, July 20, 2015. For some DAOs, these transfers can contribute a significant portion of their income, and in others the income tax transfer is worth less than 1 percent of total revenue.

¹⁹ Because the GAD plays the supervisory role at the township level, it often must give permission before businesses can proceed with their engagement with other authorities.

²⁰ In some sectors, notably garment manufacturing, businesses are able to deduct the cost of imported inputs from their commercial tax bill, but they need to obtain specific paperwork documenting the value of their imports and include that with their filings in order to receive the credit. Because of this, the commercial tax can be hugely burdensome for many businesses, and therefore it is almost always negotiated at the local level.

²¹ Because of poor compliance and a relatively high threshold for the income tax, the vast majority of wage earners do not pay any income tax to the IRD.

collections can also be negotiated. The IRD collects revenue only for the Union government.

2.4 Union-Level Sectoral Ministries and Industrial Zones

A wide range of sectoral ministries and their departments have important and varied roles dealing with Myanmar's private sector. Some, like the Department of Forestry and the Department of Fisheries, illustrate the way government administration at the township level is shared between the S/R and the Union. Others remain under the sole control of the Union government. Township-level offices of these ministries often play an important role in ensuring compliance with licenses and taxation agreements, at either the S/R or Union level.²²

Department of Forestry: The Department of Forestry is the key administrative body governing Myanmar's forests, and falls under the Ministry for Natural Resources and the Environment. The Department engages with various parts of the private sector, including logging companies and secondary businesses such as sawmills, furniture makers, and timber traders. Its most important role is in taxation.²³ Like a number of other departments, the Department of Forestry has oversight responsibilities from both the S/R and the Union,²⁴ though obtaining a license to harvest some products requires approval only at the S/R level.

Township Forest Department officers monitor the harvesting of trees, bamboo, and other forest products.²⁵ Fees for these products are not collected by inspectors, but are paid directly to Myanmar Economic Bank (MEB) before the harvesting begins. Fees are paid either to the Union or the S/R government, depending on the type of product. Township officers noted that the Union ministry never gives instructions directly to the township, instead passing them through the S/R government.

Department of Fisheries: The Department of Fisheries has the responsibility to govern offshore fishing, inland fishing, and aquaculture businesses such as fishponds. It oversees a licensing regime that requires separate permissions and payments for numerous different aspects of the fishing process. Revenue from licensing is the primary source of the Department's budget, and license administration is the Department's primary responsibility.²⁶ The S/R government has authority over fishing in territorial waters, as well as oversight of inland fisheries.²⁷ The budget for the Department of Fisheries is split between the Union and S/R governments.²⁸

Department of Livestock: The Department of Livestock has a regular presence at the township level, with a greater focus on service delivery than some other departments. Township officials noted that the Department did not run a licensing regime, but did implement a registration system for people who raise animals.²⁹ Registration rates remain low.

Department of Agriculture: While the Department of Agriculture plays an important role in Myanmar's rural economy, it has few responsibilities related to business. Like many other ministries, though, it does have selective authority over licensing.

Department of Agricultural Land Management and Statistics: The DALMS is the key government ministry for land registration and management. Its responsibilities include administering farmland tax by preparing vouchers and then passing those to GAD, which oversees collection. It also prepares irrigation tax vouchers for the Department of Irrigation and the GAD, and collects tax on selected types of urban land. For businesses, the most relevant role of DALMS is the registration and transfer of land and buildings in urban areas.

Transfers of land are assessed by a board of government

²² Some licenses in Myanmar are given with specific conditions, and township officials are often tasked with monitoring the licensees. For example, licenses to cut bamboo will stipulate a specific amount of bamboo that can be harvested, and the township forestry officer monitors licensees to ensure they do not exceed the limit. When licensees reach the limit stipulated in their license, they must pay additional fees to increase the limit.

²³ It collects: a tax on hardwoods (to Union government); a tax on forest products such as bamboo, some softwood trees, etc. (to S/R government); a tax on shops that sell furniture made of timber or forest products; and a tax on elephants used in timber production.

²⁴ While teak and hardwoods fall under the jurisdiction of the Union government, other forest products such as bamboo, firewood, soft wood trees, thatch, and bark fall under the S/R government.

²⁵ Once the licensee reaches the limit, they are required to either stop cutting or pay additional money.

²⁶ Fishing licenses issued by the Department include fees for two components (and their associated subcomponents) – licenses for fishing boats, and licenses for carrier boats that transport the fish to shore.

²⁷ This authority includes: auctions of licenses to raise fish in natural ponds, tenders for fishing rights on inland waterways, fees on freshwater fishing equipment, and licensing of existing artificial fish ponds.

²⁸ The budget for offshore and other activities that fall under the authority of the Union comes from Nay Pyi Taw, while the budget for fisheries work in coastal and inland areas, which falls under the authority of the state/region government, comes from the S/R.

²⁹ For example, people who raise anywhere from one to 200 chickens pay the lowest fee of 50 kyat per year (US\$0.04), while people raising 10,000 chickens or more pay 1,000 kyat per year (US\$0.78).

officials, called the Land Appraisal Board.³⁰ This board is tasked with determining the value of the land to be transferred, after which taxes and a stamp duty are assessed.³¹

Department of Highways: The Department of Highways is the department responsible for Union roads and is frequently present at the township level. This department was formerly part of Public Works, an erstwhile state owned enterprise under the Ministry of Construction, which has since been split into four departments: the Department of Highways, the Department of Bridges, the Department of Buildings, and the Urban and Housing Department.

At the township level, the Department of Highways is tasked with assisting road construction and monitoring the implementation of road projects. As part of this work it tenders for construction materials. The Department also supports the implementation of build-operate-transfer (BOT) highway concessions.³² S/R departments have little role in granting these concessions, though they do oversee companies' work.

Ministry of Hotels and Tourism: The Ministry of Hotels and Tourism (MoHT) is responsible for oversight of the tourism sector. It has a presence at some townships. Licensing is an important part of the Ministry's engagement with business: issuing licenses to hotels and guesthouses,³³ for transportation (vehicles and boats receive "blue plates" from the MoHT), and to tour guides and tourism companies. Companies first register with the Directorate of Investment and Company Administration (DICA) and then apply to MoHT for licenses. The extra step of providing the MoHT business documentation was identified by Ministry staff as hindering additional investment in the sector.

Directorate of Industrial Supervision and Inspection: The Directorate of Industrial Supervision and Inspection (DISI), part of the Ministry of Industry, conducts

inspections and registration of industrial businesses subject to the 1990 Private Enterprise Law (exempting SOEs, military companies, and joint ventures with these entities). Unlike many other government departments, however, DISI does not issue licenses, as they are already a prerequisite for registration with DISI. DISI also plays a key role in intergovernmental coordination regarding industrial enterprises, and is responsible for ensuring that businesses "follow procedures."

Ministry of Mines: The Ministry of Mines is a Union-centric ministry, with a local presence generally only at mine locations. The Ministry has a range of engagements with business, including the signing of production-sharing contracts with private companies operating in the sector. Local mining companies pay 30 percent of their revenues to the Ministry, and foreign companies pay 35 percent. The Ministry has no operating responsibilities, and is only responsible for giving permission to the business to operate, and monitoring and supervising the business according to the contract.³⁴

Transport Division of Operator License Supervision and Coordination: The Transport Division of Operator License Supervision and Coordination, part of the Ministry of Rail Transportation, is responsible for licensing commercial vehicles that transport cargo or passengers.³⁵ The Transport Division is completely controlled by the Union government.³⁶

Trade Promotion and Consumer Affairs Department: The Trade Promotion and Consumer Affairs Department is the key part of the Ministry of Commerce at the local level. The Department often has officers at the township level.³⁷ At the S/R level, the Department tracks the flow of commodities between various states/regions. These efforts are driven by the government's concern about food security and are conducted twice a month.

Industrial Zones: Industrial zones (IZs) are managed by an extensive hierarchy of government and business, and

³⁰ The board includes: the Internal Revenue Department, the State Land Records Department, the Department of Planning or the Department of Livestock (depending on township), the Myanmar Police Force, the General Administration Department, and the Development Affairs Organization.

³¹ If there is a disagreement, then there is generally a negotiation between the parties, though determination of the final rate is at the discretion of the board.

³² The Union-level highway concessions are for thirty years, though despite being called BOT concessions they often do not require companies to build new roads. Instead, concession holders are only obligated to expand and improve existing roads and do regular maintenance.

³³ DAOs also can give licenses for guesthouses; however, foreigners are only allowed to stay in accommodations licensed by MoHT.

³⁴ Businesses must also pay license fees, which depend on the size of the mine and are decided on a case-by-case basis. Fees are determined by a pre-negotiated level of production agreed by the ministry and the company. The company must pay these fees regardless of whether or not production meets these levels. Licenses are short term – generally three years – though larger mines can get longer contracts. Gold mines receive only a one-year contract.

³⁵ This includes local public transportation such as taxis and city buses, as well as intercity transportation.

³⁶ However, licenses are only valid in the S/R in which they are issued, so bus operators that want to pick up or drop off passengers in a different S/R must also obtain the same public transportation license from that state/region.

³⁷ The main function of the Department at the township level is to collect data on commodities such as rice, beans, maize, and sesame. Special emphasis is given to paddy, as this is the top question asked by senior officials and the most important issue for the Department.

are ultimately controlled by the government under the Ministry of Industry's DISI. Each industrial zone under DISI has a supervision committee (IZSC) that supervises the zone, and a management committee (IZMC)³⁸ that is responsible for its operation. IZs also issue operating licenses, from which they collect fees. They generally do not receive revenue from outside sources, meaning that many IZs are often short of money. Inside the industrial zones, then, IZMCs are analogous to DAOs.

THREE: THE STRUCTURE OF LOCAL REVENUES

State/region and township governance of economic activity is often characterized by a “fee-for-permission” structure, requiring license payments in advance of business activities. These characteristics can contribute to a revenue base that is broad and regressive in nature, and can have unintended negative consequences.³⁹ While there are a few subnational taxes with broad bases, such as the land tax and the building tax, direct taxation accounts for a minority of local government revenues. Together, fees and indirect taxes contribute to a regressive system that imposes arbitrary and unequal burdens on similar members of society.⁴⁰ By making these barriers to participation in the economy high, economic activity is discouraged and the range of economic actors is limited.

3.1 Fees and the Cost of Service Provision

Fees are common at the local level, and many of them bear little resemblance to the cost of the service provided. Instead, fees are used to generate revenue. Two observations reveal the disconnect between licensing fees and the actual cost of licensing. First, because licensing procedures tend not to vary significantly for businesses of different sizes, license fees should also vary only slightly. However, data from DAOs found major differences in these fees, suggesting that their purpose is often not simply to recoup the costs of the licensing

service. Second, fees for the same license vary from township to township, again suggesting that license fees are unconnected to actual costs, but are being used as a source of revenue.

3.2 Taxes

The two most common locally imposed taxes are the land tax and the property/building tax. Both are low compared to other countries, account for only a small portion of the revenue collected at the local level, and have major shortcomings in their design and implementation.

Land Tax: Taxes on land are generally low, largely for political reasons.⁴¹ Unlike commercial and income taxes, which depend on confidential information about individual or business finances, the land tax is verifiable, because land ownership is generally known within the community. Changing the land tax is mired in politics, however, due to the perception that raising land taxes would hurt the poor and farmers. One solution would be to establish a minimum acreage below which farmers' landholdings would be exempt from the tax.

Property Tax: Property taxes are collected by DAOs; however, they are a relatively small source of revenue in most townships. “Property tax” is used as a general term for a group of four taxes related to property – a building tax, a garbage tax, a water supply tax, and a street lighting tax (where applicable). Though the benefits of increasing these taxes and changing their structure are clear, there are numerous challenges to implementation. Building taxes may vary state by state, but are generally around 10 percent of the “standard rental rate” for the property. The rate is prescribed in the S/R DAO law, and change would therefore require approval by state/region parliaments, though some DAOs have classified properties into categories and set a minimum and maximum rate for each category. This inadvertently results in a cap on the amount of building tax for which one can be liable.

³⁸ The IZMC includes government and the private sector, though prior to 2014 it included only government.

³⁹ A broad revenue base means that a significant percentage of the population pays revenue in some form. A regressive revenue base is one in which the percentage of income paid decreases as the total income increases. It is important to clarify that this refers not to the total amount paid by a taxpayer, but instead to the percentage of total income paid. In contrast, a progressive revenue base is one in which the percentage of income paid increases as total income increases.

⁴⁰ While taxes and fees are often linked, and are regularly conflated by the Myanmar government, they are fundamentally different concepts. It is essential to disaggregate “taxes and fees” so as to make this joint usage more than simply a synonym for “revenue.” Unlike fees, taxes are generally not voluntary or directly linked to a service. They are often distinguished by three characteristics: “(1) A user fee is designed to defray the costs of a regulatory activity (or government service), while a tax is designed to raise general revenue; (2) a true user fee must be proportionate to the necessary costs of the service, whereas a tax may not be; and (3) a user fee is voluntary, whereas a tax is not.” This distinction is important in Myanmar, because, especially at the local level, significant revenue is raised through “fees.” Despite the name, though, some fees are taxes in disguise, used for raising general revenue. Michigan Supreme Court, quoted in Foundation for Economic Education, *A Tax Is Not a User Fee*, <http://fee.org/freeman/a-tax-is-not-a-user-fee/>.

⁴¹ In the 2008 Constitution, land taxes were decentralized to the authority of the S/R governments and remained low until FY2013-14, when many states/regions increased them significantly.

Noncompliance, largely driven by enforcement challenges and the lack of a coherent enforcement strategy, is a significant problem.⁴² Moreover, the DAO, which collects property taxes, must depend on other government departments for enforcement, meaning that interdepartmental cooperation is essential. When property taxes are not paid, the township DAO's executive officer reports non-payment to the regional DAO office, which gives the township office "collector power," akin to a warrant, to take control of and auction off the tax debtor's property to recover the debt.

The challenges of implementation and enforcement are exacerbated by the lack of incentives for building owners to pay on time. DAO officers note that they do not charge any penalties or interest for late payment of property taxes, even though they have the authority to do so in some townships. This encourages late payment, and effectively constitutes an interest-free loan by the government.

3.3 Indirect Taxes and Other Issues

Myanmar has a number of fees that function as indirect taxes. A common example of this is auction licenses, which require large payments by businesses that are not proportionate to the license's cost to government. Although businesses recoup these license fees from their customers, the effect is to create an indirect tax through the auction-license system.

Concentration of Income Tax Contributions in Urban Areas: DAOs receive a portion of their revenue via transfer from the IRD.⁴³ Budget analyses suggest that the transfers received by each township DAO equal the income taxes collected from that township (i.e., there is no redistribution at the S/R level). This system has the unintended shortcoming of recycling tax dollars into the development of S/R capital cities, which are generally among the best-off cities in each S/R. This is largely due to the fact that income tax compliance in Myanmar is poor. Income tax revenue is collected largely from civil servants, whose salaries are funded by the Union government. As a result, tax revenues get recycled back into the development of cities with large numbers of civil servants, instead of being distributed more equitably across the S/R.

Rural-to-Urban Transfers in DAO Revenue: Recent government restructuring has led to a redistribution of authority between different ministries, resulting in unintended rural-to-urban transfers through DAOs. At present, DAOs retain the authority to issue business licenses (and therefore raise revenue), as well as to oversee and retain the revenue from auction licenses, in both rural and urban areas. These fees and indirect taxes constitute a significant part of the DAOs' funding. Yet the Department for Rural Development has displaced DAOs as the agency responsible for a number of rural development activities, including the construction and maintenance of secondary rural roads, small rural bridges, and water supply in rural areas. As a result, revenues collected from rural businesses and individuals flow to an organization (the DAO) that has no mandate to spend those revenues on the people from whom they were raised. Therefore, they constitute a transfer from the (generally poorer) rural areas to the (generally richer) urban areas.

Implementation Challenges with the Commercial and Income Taxes:

Commercial and income taxes are the most important taxes by a significant margin. The vast majority of these are collected through township IRD offices and are often incorrect, arbitrary, or unaccountable. These problems are closely tied to the longstanding distrust between business and the state.⁴⁴ Taxation, licensing, and other aspects of business-government engagement are arbitrary and often perceived by businesses as unfair. Because of this history, government officials at the township level note that businesses are not truthful about their taxes. As a result, these officials have to use various methods to attempt to estimate tax due. The end result is that, even though the IRD purports to use a "self-assessment system," officials can override that self-assessment at any time. This type of system has significant room for negotiation. Despite this, many businesses thought that their tax was too high and negotiated a new tax rate based on the shop size.

Stamp Duties: Stamp duties are a common source of revenue for the IRD, and official stamps are required for legal certification of a wide range of documents. Much like the taxes noted above, the final price of stamps needed for some items, such as contracts, is administratively determined by the board, which is headed by the township IRD officer.

⁴² DAOs note that people think they should not have to pay a tax on something that they already own.

⁴³ This is administered at the regional level, as the S/R IRD transfers 5 percent of total income tax receipts to the S/R DAO.

⁴⁴ During Myanmar's socialist era, from 1962 until 1988, many types of businesses were not legal – people had to hide their economic activity for fear of arrest or worse. During the military era, many types of businesses remained illegal, though other sectors were liberalized and opened to private participation.

FOUR: AUCTION LICENSES

Annual license auctions in specific sectors are a key source of revenue for many government departments and organizations, especially DAOs. At present, many states and regions use legislation to create monopolies and oligopolies. They then license out these monopolies through auction licenses, which enable the government to extract part of the subsequent rents. Consumers and suppliers bear the burden of this indirect tax system, which in some cases removes market characteristics and creates a largely planned system for selected sectors. Nonetheless, it is in the auction-license system that local-level licensing experimentation has occurred – enabled by the decentralization of authority to S/R governments.

4.1 The Auction Process

While the auction-license system is common across Myanmar, state and region level oversight means some variations in auction processes occur across the country. Generally, auctions are announced publicly and are open to bids from anyone, though winners must be in compliance with the rules and regulations for the license. Some DAOs set price floors for auction licenses, which are announced prior to the auction.⁴⁵ The winner is then required to put down a deposit on the license on the day of the auction.⁴⁶

4.2 Slaughterhouse Licenses

Slaughterhouse licenses are one of the most important and lucrative auction licenses overseen by DAOs.⁴⁷ However, the true value of these licenses lies in the administrative restrictions accompanying them, which create artificial monopolies with state-mandated prices. This generates rents that are shared between the DAO and the licensee, leading to reduced farm-gate prices for livestock and higher retail prices for meat. These consequences have been noticed by many local policymakers, and in some locations have led to changes due to perceptions that the current system harms the public interest.⁴⁸ Meat prices (mutton, beef, and pork) in

many townships are determined by the DAOs and do not reflect the actual market.

The auction-license system presents a number of problems. First, the system causes price inflation not linked with the inflation rate of the broader economy. Second, the license restrictions create artificial monopolies that prevent competition and allow businesses to capture economic rents. The monopolistic licenses segment the market, and discourage businesses from expanding their operations and reaping improved efficiencies from economies of scale. Restrictions on trading between townships compound these issues. Another problem created by the system is that it probably lowers the prices that farmers can demand for live animals, because it removes competition among buyers.⁴⁹ Fundamentally, the license system removes many market-related characteristics from the sale of pork, beef, and mutton, and instead closely resembles a government-planned system.

Businesspeople in townships where the auction system has been changed noted that there are now more competitors, and that wholesale and retail prices for meat have decreased. Income for the DAO has also decreased, suggesting rent dissipation. Since the removal of auction licenses, the prices for live animals have increased. On the other hand, the current licensing system has a number of benefits, including creating business opportunities for locals of each township, and keeping meat prices stable.

The tightly regulated markets for pork, beef, and mutton stand in marked contrast to the relatively open markets for chicken and fish. The revenue-raising nature of pork, beef, and mutton licensing also raises the question of why consumers and suppliers of these meats, who are often from rural areas, should bear the burden of taxation while vegetarians do not. Not only is the indirect taxation that occurs through these auction licenses arbitrary, it may also be regressive, as the poor tend to spend a greater proportion of their income on food.

⁴⁵ Interestingly, though floor prices are given, some final auction-license prices were below the floor, because no bids were received at or above the floor price.

⁴⁶ In some townships, businesses that receive auction licenses with a cost of greater than 500,000 kyat may pay in installments, though licenses below this amount must be paid up-front. To enter a bid, businesses complete a form with a secret bid and submit it in a closed envelope to the auction committee, which is comprised of Township Development Affairs Committee (TDAC) and DAO staff.

⁴⁷ In some townships, they account for a significant portion of revenue (up to 50 percent in some townships).

⁴⁸ There are specific restrictions in DAO bylaws that expressly prohibit license holders from one township from selling meat in another. These restrictions on moving slaughtered meat between townships mean that consumers in one township cannot benefit from lower prices in nearby townships. Some DAO bylaws also prescribe the number of animals to be slaughtered in a day. Furthermore, DAO bylaws call for the submission of biographies, registration data, household lists, and police recommendations for each slaughterhouse manager, staff person, sales clerk, or related laborer.

⁴⁹ The licenses also contain a clause that sellers must have “good character” and “deal well with purchasers.” Those deemed not to have met this standard may have their licenses revoked, a source of uncertainty for licensees because of the vague nature of the clause.

4.3 Ferry Licenses

Ferry licenses are another important form of auction license, and share structural similarities with slaughterhouse licenses. A ferry license grants geographical exclusivity to a single operator, who operates the concession for a one-year term at a fixed price, under the regulation and oversight of the DAO.⁵⁰ Compared to other businesses in the auction-license system, however, the operation of ferries requires significantly greater capital outlay. Operators must purchase ferries, and sometimes build piers and shelters (if these do not already exist).⁵¹ Ferry license holders are aware of the insecurity of their investments and take steps to try to mitigate that insecurity. The nearly universal limit of ferry licenses to one-year terms is a direct and significant disincentive to long-term planning and development.⁵²

4.4 Other Auction Licenses

There are many other types of DAO licenses, with many different characteristics. Pawnshops, like slaughterhouses, enjoy a DAO-sanctioned monopoly to operate in a designated area. Many other auction licenses function as subcontracts to collect revenue on behalf of the state. For example, instead of the DAO having its own personnel collect revenue from street vendors in the market, some townships subcontract this responsibility. Auction licenses that fit this description include the wheel tax collection license, the public toilet and bathroom fee collection license, and the market fee collection license. Instead of giving the contractor a share of total revenue collected, the contractor pays a flat fee and keeps all revenue collected in excess of that fee. In some cases, this leads to DAOs capturing a significant share of the revenue, while in others they capture only a small portion.

FIVE: POLICY CONSIDERATIONS

5.1 Key Recommendations

Given the challenges posed by the current system of local

economic governance described above, the following recommendations have been developed. While these recommendations collectively may raise revenue, some individual recommendations (especially those addressing aspects of the auction-license system) will reduce revenue. This is especially problematic given that some local authorities, such as DAOs, are heavily dependent on licensing revenue. Therefore, it is essential that *reforms to the auction-license system happen in tandem with changes in the building-tax system*, to prevent a significant drop in DAO revenues and a serious degradation of essential local services. With this in mind, the recommendations are:

- Further decentralize local economic governance to give S/R governments the flexibility to reform licensing regimes⁵³ and to encourage experimentation with policy reforms.
- Work with S/R and township-level governments to develop location-specific, multi-year reform strategies based on a transparent and consultative process that builds trust and understanding of the reforms before they take place.
- Work with government to develop effective communication strategies to explain current and future local economic governance systems to communities.
- Reform the auction-license system to minimize the creation of rents and reduce the harmful effects of annual price increases and the negative economic consequences of fixed prices.
- In cases of natural monopolies, revise auction-license terms to incentivize improved service and investment and increase the government's share of the revenue.
- Reduce the use of one-year licenses, which increase costs for consumers by creating uncertainty for business that discourages long-term investment.
- Reform the system of advance license payments to allow for incremental payments throughout the

⁵⁰ Floor prices for ferry auction licenses also have increased at a DAO-mandated 10 percent per year, though there are exceptions to the floor price.

⁵¹ If a new operator wins a license, they are free to negotiate with the former operator to purchase their existing capital. However, there are no provisions for the transfer of capital between old and new license holders, which creates significant uncertainty for existing operators. If the old license holder does not reach an agreement with the new one, the old license holder can take down their infrastructure and remove it.

⁵² With this limit in place, businesses cannot justify or afford significant investments in infrastructure (nor is such investment a condition of the license).

⁵³ Note that, despite the theoretical decentralization of authority, there is sometimes informal Union-level influence in these areas. It is not possible to quantify this influence, however, and S/R governments still exercise significant autonomous decision-making authority. Decentralization of additional authority has been mentioned repeatedly by Parliament and other government bodies, including the decentralization of licensing for foreign and citizen investment below a set amount. This would presumably be done by the minister of planning at the S/R level.

duration of the license.

- Improve enforcement of sanitation and safety conditions for licensees.
- Reform the building tax to make it a more significant source of general revenues for DAOs.
- Revise the land tax, and consider introducing a minimum acreage below which no landowner's holdings are subject to the tax.
- Reduce S/R and local-level administrative barriers to trade, including but not limited to the prohibition on moving slaughtered meat between townships.
- Eliminate arbitrary barriers to entry for local business, such as the "Disciplinary Committee on Buses" or various hotel requirements from the Ministry of Hotels and Tourism.
- Charge penalty fees for late payment or non-payment of land and building taxes.
- Increase publicly available information, including local laws, rules, regulations, and bylaws that spell out the governance framework for local businesses.

As many of the economic powers are under the authority of subnational governments, especially auction licenses, some local officials are already aware that the existing system is problematic and can be improved. Because it does not require Union-level approval, local-level reform may be easier and less time-consuming, while enabling local experimentation with economic policy. Reforms also may be more feasible because they focus on improving the functioning of relatively small-scale local systems. Finally, local governments have significant flexibility to improve the implementation of laws and rules under their control.

With this in mind, not only are the recommendations detailed above much needed, but they are also realistic for policymakers in the short-to-medium term.

SIX: KEY QUESTIONS AND FURTHER READING

Discussion Questions

- What are the strengths and weaknesses of the current system(s) of local economic governance across the different states and regions of Myanmar?
- What are the steps that DAOs and other local economic governance institutions should take to improve local licensing procedures?
- How should local economic governance actors build on recent reforms and decentralization?
- What steps should the Union government take to reduce local governance actors' reliance on regressive revenue structures?
- What are the national-level structural changes required to improve regulatory and licensing procedures for businesses, government actors, and consumers?
- What lessons can be learned from comparable regional and international examples of local economic governance reform?
- What are some of the key risks of local economic governance reform in Myanmar?

Further Reading

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