

## **Building Fiscal Capacity**

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### **Project description**

Fiscal capacity—the ability of governments to raise revenue from broad tax bases—is a crucial determinant of economic growth and democratic outcomes. A well-functioning fiscal administration is a key element of fiscal capacity. However, surprisingly little is known about how an efficient fiscal administration can be built in places where it does not yet exist and about the consequences of capacity building.

The aim of our project is to improve our understanding of capacity building in the fiscal administration. We study empirically the measures taken to build the fiscal administration in the territory of the former German Democratic Republic after the fall of the Berlin Wall and evaluate their impact in the short and long run.

We have collected unique detailed information on the elements of administrative aid provided by West German tax offices to East German tax offices after reunification: on-the-job-training of East German personnel, secondments of West German officials as well as permanent transfers.

The project aims at understanding the effectiveness of the different strategies for capacity building in the fiscal administration. Administrative aid is usually tailored to the needs of the receiving tax office and thus endogenous. We exploit the unique historical setting after German reunification for identification: East German states were partnered with West German states; the administrative aid depended on the financial and personnel situation of the West German partner, which was exogenous to the East German tax office. The project thus provides the first causal empirical evidence about fiscal capacity building at the tax office level.