

Tax and Non-tax proposals for the 2012 National Budget

Joint Civil Society Paper

Submitted to

Ministry of Finance and National
Planning (MoFNP)



JCTR

CARITAS



Contents

Introduction 4

Background.....4

Review of Current Tax System.....5

Zambia’s Economic Outlook and Revenue Performance.....7

PROPOSED REVENUE MEASURES 8

Tax Measures 8

Income Taxes8

 Concessions..... 8

 Compensating Measures 10

Consumption taxes.....11

 Concessions..... 11

 Compensating Measures 12

Trade Taxes.....12

 Concessions..... 12

 Compensating Measures 12

Non Tax Measures 12

 Concessions..... 13

 Compensating measures..... 13

Conclusion..... 17

Annex 19

ABBREVIATIONS AND ACRONYMS

CSOs	Civil Society Organizations
GDP	Gross Domestic Product
CSPR	Civil Society for Poverty Reduction
CTPD	Center for Trade Policy Dialogue
EAZ	Economics Association of Zambia
JCTR	Jesuit Centre for Theological Reflection
MoFNP	Ministry of Finance and National Planning
MTEF	Medium Term Expenditure Framework
NGOCC	Non-Government Organizations Coordinating Council
PAYEE	Pay as you earn
PSP Zambia	Platform for Social Protection Zambia
SNDP	Sixth National Development Plan
USD	United States Dollars
ZMK	Zambian Kwacha
ZRA	Zambia revenue Authority
VAT	Value Added Tax

Introduction

The following submission is a joint response by Civil Society Organisations (CSOs) to the invitation by the Ministry of Finance and National Planning (MoFNP) to all Zambians to make submissions on Tax and Non-Tax Revenue Policy proposals which they hope to see in the 2012 National Budget and the 2012 Medium Term Expenditure Framework. The paper was put together by a consortium of CSOs working in the development sector in Zambia. The document merges the several compilations of specialized CSOs into a comprehensive submission for government consideration in the preparation of the 2012 national budget.

CSOs have over a long period of time been engaging government on alternative approaches to development in order to make development processes more inclusive and responsive to realities on the ground. CSOs have welcomed this opportunity to make contributions to the revenue side of the budget looking particularly at tax and non tax revenue measures for the 2012 National Budget. The intention of CSOs in making this submission is twofold; namely: to have a more progressive tax regime that will make revenue accumulation more sustainable for Zambia and to have a budget that tackles poverty and benefits the poor of Zambia

The parties to this submission include:

- Economics Association of Zambia (EAZ)
- Jesuit Center for Theological Reflection (JCTR)
- Center for Trade Policy Dialogue (CTPD)
- Civil Society for Poverty Reduction (CSPR)
- Platform for Social Protection Zambia (PSP Zambia)
- Caritas Zambia
- Non-Government Organisations coordinating Council (NGOCC)
- Participatory and Ecological Land Use Management (PELUM)

Background

Taxes world over are levied to finance government development agendas. While governments can use other means to finance development, like debt, aid and remittances taxes are the most reliable and sustainable source of government revenue. In Zambia, taxes make up to 70 percent

of the domestic revenue base (2011 National budget). Taxes have a duo function of raising government revenue and the important yet often underplayed function of redistributing wealth or income and thereby reduce disparity between the rich and the poor. So while a tax system must remain efficient to ensure enough tax revenue for government is collected without hampering economic growth, it must be equitable. Taxes therefore play a critical role in raising government revenue, encouraging economic growth, enhancing equity and reducing poverty.

Zambia is facing particular tax performance challenges that need to be addressed urgently. The ratio of tax revenue to Gross Domestic Product (GDP), often used as a basic measure of the performance of a tax system, has been on the decline, from 19.2 percent in 2000 to 15 percent in 2009,¹ though with some improvement to about 17% in 2010 (SNDP). Underlying this overall decline is the change in the structure of tax revenue (i.e. the different sources of tax revenue). The performance of trade taxes that previously were the major contributors to the tax revenues have declined while consumption taxes have also declined. This has left government to rely on income taxes, particularly Pay As You Earn (PAYE) which has raised issues of equity.

The tax administration system in Zambia faces several challenges, such as a large informal cash economy; low taxpayer compliance; complexities associated with taxation of international transactions; poor traceability of taxpayers; smuggling; and challenges facing Zambia Revenue Authority (ZRA) including human resource and technology which limit their ability to collect taxes more efficiently, for infrastructural and technological development.

Review of Current Tax System

The tax system in Zambia generally consists of three broad tax types: Income taxes (i.e. Pay As You Earn, Corporate tax etc), Consumption taxes (domestic VAT, Import VAT and Excise Duty) and Trade taxes (Customs and Export Duty). Among the three broad tax categories, income taxes are the largest contributors to the tax revenue base followed by consumption taxes and lastly trade taxes (contributing approximately 35%, 25% and 10% respectively to the 2011 national budget). The other percentage of the budget, 30% will be financed by debt (internal and external), aid and non tax revenue sources.

¹ Jesuit Centre for Theological Reflection Tax Study Report 'Taxation System in Zambia'

It is important to note that under income taxes, the formal sector bears much of the tax burden and even then only a few firms and individuals in selected economic sectors are bearing this burden. The performance of Consumption (largely VAT) and Trade taxes has deteriorated due to a number of challenges. For consumption taxes, administration of VAT especially management of refunds to the mines must be improved as these have dictated the performance of VAT. It should also be noted that best practices on revenue mobilization recommends that a tax system should rely more on consumption taxes than income and trade taxes as these are more volatile. Issues of equity on reliance on consumption taxes can be addressed by making VAT more progressive by for example excluding goods and services on which the poor segment of society spend their income from VAT.

Government also traditionally relies on other sources of revenue beside taxes, such as debt (foreign and domestic) and aid which currently constitute about 16% and 8% of the 2011 budget respectively. However, there are other sources of revenue that government has not fully exploited such as local government levies, wealth taxes, remittances etc. These alternative sources of revenue have challenges that need to be addressed if they are to be reliable and predictable sources of revenue.

Notwithstanding, the tax system has improved having undergone several administrative and policy reforms which have seen tax revenue contribution to the budget increase from around 50% in 2001 to around 70% in 2010. However, there is room for improvement especially if the tax revenue is viewed in light of economic growth. The growth in tax revenue has not kept pace with economic growth as shown by the decline in revenue to GDP ratio from 19.2% in 2000 to 15% in 2009. The number of tax types and rates should be reduced to make the tax system more effective and easier to manage. In its current state, the tax system is complex and difficult to administer. The many tax types and rates also result in high effective tax which may lead to lack of compliance on the part of tax payers.

On the tax formulation process, the system has become more inclusive as the private sector and Civil Society Organizations are regularly invited to make their submission on revenue and non revenue measures to Ministry of Finance and National Planning to feed into the budget process. This process however still has some challenges as the invitation is at the mercy of government.

The process can be enhanced by making it legally binding for government to include the participation of non state actors in the process so that government discretion is not subject to abuse as the current system is.

Zambia's Economic Outlook and Revenue Performance

The fiscal performance (revenue) of any country is intrinsically tied to the performance of the economy. As the economy grows, tax revenue being collected is expected to grow in response to the growth in the economy. This is because the economy is the base on which tax revenues are collected and therefore dictates the performance of tax revenue.

It should however be recognized that tax administrative reforms are often highly political processes that will inevitably pose a threat to important domestic stakeholders and revenue performance. The successful implementation of fiscal reforms requires political will and support from the highest level of government. The reforms/ measures are unlikely to succeed if the main source of energy and leadership comes from outside government.

The performance of the Zambian economy has been favorable in the last five years (FNDP period) recording annual average GDP growth rate of 6.1%. The growth has largely been driven by Agriculture, Construction and the Mining sectors.

The macroeconomic performance was generally mixed; recording single digit inflation, unstable Kwacha against major currencies and an unstable lending interest rate. In the external sector, the balance of payment position improved resulting largely from trade surplus. These factors among others led to improvements in international reserves position, reaching 4.8 months of import cover at the end of 2009 (2009 Economic Report). External debt also remained sustainable at 9% of GDP (SNDP). External debt position increased but remained sustainable.

With Zambia's economic prospect expected to remain positive during the SNDP, with GDP growth rate estimated at between 6 and 7 percent aided by growth in the Mining, Agriculture, Tourism, Construction and energy sectors; it is the hope of CSOs that tax revenues will respond more favorably than they did during the FNDP. Tax revenues as a share of GDP actually

recorded a decline as already alluded to during the FNDP period. The decline however can partly be explained by the global economic crisis of 2008. Higher tax revenue to GDP ratio above the internationally accepted minimum of 20% should be achieved than the anticipated annual average of 18.6% over the SNDP period. As more sectors grow and increase their contribution to GDP, their contribution to tax revenues must proportionally increase.

PROPOSED REVENUE MEASURES

Despite significant revenue contribution to the government budget following reforms in the taxation system that were first instituted in 1994 with the establishment of ZRA, the major problem that remains is that of broadening the tax base. The few Zambians in the formal sector contribute almost a third of total domestic revenues through PAYE. This is in addition to other indirect taxes incurred through purchase of goods and services. Although government is committed to reducing the tax burden on employees, there is still need to devise a clear strategy of achieving this. The government through the Zambia Revenue Authority should engage stakeholders to develop strategies of broadening the tax base and government should commit itself to implementing the strategy.

Tax Measures

Income Taxes

We propose the following tax measures under direct taxes:

Concessions

An adjustment to the exempt PAYE threshold from the current K 1, 000, 000 per month to K1, 300, 000 per month and an adjustment of income bands as specified in the table below.

Proposed PAYE Regime		Current PAYE Regime	
Income Bands	Tax Rates	Income Bands	Tax Rates
K 0 – K 1,300,000	0%	K 0 -K 1,000,000	0%
K1,300,001 – K 2, 300,000	25%	K1,000,001-K1,735,000	25%
K2,300,000 – K 5,000, 000	30%	K1,735,001-K4,200,000	30%

Above K5,000,000	35%	Above K4,200,000	35%
------------------	-----	------------------	-----

This proposal is intended to give relief to workers especially those earning lower incomes. Increasing the exempt threshold will provide greater relief to those on low incomes, while adjusting the bands upwards will enhance the progressive nature of the tax system.

Increase the exempt portion for income paid upon the termination of employment from the current K35 million to K50 million.

This measure is intended to mitigate the high cost of living and give further relief to those whose formal employment has been terminated.

Increase Tax credit for differently-abled persons from the current K3 million per annum to K6 million per annum.

This measure is intended to provide additional relief to the differently-abled persons and offset extra costs such as transport costs and other personal costs (guides, readers, sign language interpreters etc).

Income from part time employment must be taxed at the appropriate rate under the PAYE regime for people who have no other full time jobs.

The current system where every income from part time employment is taxed at 35% with the recourse action of filing a tax return for refund at the end of the charge year is unfair for people who rely on part time income as their only income. Employers should be verifying whether a part time employee has a full time job and then tax them appropriately

Tax allowable band

The tax relief allowance under section 7 of the Income tax Act be revised to reflect an amount that would encompass the NAPSA contribution and some portion of the contribution being made by a member towards an occupational pension scheme. This will enhance and encourage

individual and national savings as well as firmly entrench the culture of and faith in long term savings like pensions.

Treat gratuity paid after one year as qualifying gratuity and subsequently tax it like any other qualifying gratuity

The current system of taxing gratuity paid after one year of working as non-qualifying for lower tax rate like qualifying gratuity paid after at least one year is punitive. In this age of casualization where people are given short contracts, it is unfair to treat gratuity arising from such jobs as un-qualifying and thus taxing them at higher rates.

While the above measures imply loss of revenue to government, the following measures are proposed under income taxes to compensate for the loss of revenue. It should be noted also that even though some of these concession proposals imply loss of revenue to government, much of it will remain in the hands of ordinary people.

Compensating Measures

Change the tax structure for the construction sector, so that profits of K250 million or below are taxed at 35 percent while any profits above K250 million are taxed at 40 percent as the banking and telecommunication sectors are taxed

This measure is meant to align the construction sector with the banking and the telecommunication sectors' tax regimes as the sector has been noticed to be making supernormal profits

Increase tax rate on company income of mining companies holding a large mining license carrying on the mining of base metals from 30% to 35%

This will align company tax of mining companies with other companies in other sectors that pay tax at 35% and ensure that tax leakages are minimized through tax incentives

Increase tax rate paid ON DIVIDEND by mining companies holding large scale mining license and carrying on mining of base metals from 0% to 15% like any other dividend.

Reduce capital allowance on mining equipment and other capital expenditures from 100% to 25% as it applies to other sectors

The 100% capital allowance was introduced in the wake of the global financial crisis to enable mining companies withstand the impact of the crisis. Since the financial crisis is passed and copper prices have rebounded, there is **no** need to maintain the 100% capital allowance.

Increase mineral royalty tax from the current 3% to 5% which is closer to the international applicable rates of between 6% and 10%

Because of the evasive nature of mining profits and hence profit based taxes, this submission recommends that mineral royalty should continue to be paid based on gross sales and as a compensation that mining companies must pay for their exploitation of wasting assets

Reintroduce windfall tax as opposed to variable profit tax

In light of a variable tax that has failed to effectively collect tax revenues from the mining sector, windfall tax is the best alternative. International transactions such as mining are difficult to tax as they are prone to understating their profits through mechanisms such as transfer pricing for which our tax administration has no capacity to handle.

Consumption taxes

Concessions

Zero rating of VAT on accommodation in other towns beside Livingstone.

This proposal will ensure that tourism sector develops even in other towns outside Livingstone. There are a lot of small towns that have ventured into tourism by putting up lodges and the lodging fees are very high.

Consumption tax needs to become progressive and removed from basic goods. In this way basic goods are affordable to poor people

Compensating Measures

No measures were proposed

Trade Taxes

Concessions

No measures were proposed

Compensating Measures

Increase of Excise Duty on Plastics from 10% to 20%

Following the introduction of 10% duty on plastic bags in 2010 budget, the level of plastic litter has not abated as anticipated. Floods, partly caused by plastics have continued to rake havoc and thus the 20% customs duty on plastics is expected to be deterrent enough to promote environmental sound behavior and also raise revenue for government

Increase of Customs Duty on Processed Foods from 25% to 35%

Import duty on processed food items like peanut butter, margarine, orange juice is 25%. To encourage local production and raise revenue we propose that this be adjusted to 35%. There are many local players in the food market and it is important that they are encouraged to compete favorably and enter the regional market.

Readjust customs duty upward on heavy fuels for the mining sector from 15 to 30 percent.

Since the reduction in customs duty on heavy fuel was enacted to reduce the operating costs of mines during the global financial crisis which is already behind us, we propose that the duty be reintroduced.

Non Tax Measures

In addition to direct and indirect taxes, the Government of Zambia can maximise its available resources to support national development through creative non tax revenue measures. We have put together a compilation of several non tax revenue measures, the benefits and potential drawbacks of which should be considered in more detail by relevant Government agencies.

Concessions

Ground Rent – Peri-urban

Ground rate - charges for peri-urban communities are collected as ground rent from plot/home owners in peri-urban areas of Lusaka. We recommend that Government review its land rent policy to ensure compliance and prudent management.

Road Levy

The Government should consider granting 50 percent exemptions, on application, to all institutions that do not use roads directly. This exemption would lead to decongestion of our roads, and also help resuscitate our rail systems

Abolition of Medical Levy

We suggest that the government scraps the 1 percent medical levy on savings as it discourages savings. It is also unfairly applied and expensive to administer.

Compensating measures

Toll Gates

The government should consider the introduction of toll gates on busy roads, including Great East Road and Great North Road. The introduction of toll gates would help raise funds to maintain and develop our roads. The toll gates are likely to be equitable, in that it would apply more to people able to pay (vehicle owners) than those who cannot pay (lower-income Zambians without vehicles).

In conjunction with this, Government should apply a fixed levy on transit and long distance trucks entering Zambia to ensure they contribute to road maintenance. Most truckers do not buy fuel in Zambia as they consider it to be expensive, and thus they use our roads free of charge. K250, 000 per truck would be fair. South Africa charges toll fees.

With the current high production in the construction and mining industry, it has been observed that many inland roads have been damaged by heavy load trucks especially in the mining towns. We propose that road user charges be levied on any motor vehicles carrying construction and

mining products such as, copper, cobalt in excess of 20 tones instead of the current allowed tonnage of 30. This will ensure that revenue raised could be used for road rehabilitation.

Raise Parking Fees

Government should consider raising parking fees. The objectives of parking fees in town are to decongest vehicles and to raise funds to clean our towns. We propose that the existing fees be raised to K5,000.00. This will act as an incentive to decongest our town centres, without overly burdening the most impoverished Zambians.

Rural Electrification Levy

The rural electrification levy is currently set at 5 percent. We are aware that only 20 percent of the population has access to electricity. We should increase the rural electrification levy to 10 percent to speed up the process of rural electrification. To ensure that the increased levy does not disproportionately affect the poor – the majority of whom are the aged and women – Government could consider adopting the model of South Africa’s Department of Water Affairs and Forestry, which sets a low tax for low-consumption (usually poor) water users, a medium levy for normal consumption users, and a high levy for high consumption users.² A similar system – whereby high consumption users subsidize low consumption users – could be piloted in the electricity sector in Zambia.

Reduce the Size of Cabinet

This high number of Cabinet members is totally unjustified, given that the country has a little over 20 government ministries. The problem is that each ministry has duplication of functions among the top personnel, with about 2 to 3 deputy ministers per ministry. Each of them has a minimum of two cars. The waste of resources associated with the cumbersome Cabinet can and must be applied to more socially useful purposes, such as development of core social service sectors. We feel that the position of Deputy Minister is unjustified and should be removed from the system.

² See *Budgeting for Women’s Rights: Monitoring Government Budgets for Compliance with CEDAW*, UNIFEM, 2006, p.99.

Reduce Presidential Trips

The government should reduce the presidential trips and also the size of government delegations that travel to conferences and official visits. The delegation should not be more than 10 people. This will serve the much needed resources. We understand that a minimum of three days per diem for 20 people, as usually is the case, results in wasteful expenditures of US\$5,260 per week, reaching a figure of US \$273,520 (K128 million) a year. This wasted revenue is outrageous, considering an average basic school gets an allocation of only K4.8 million a year.

Resource Leakages and Losses

We realise there has been a lot of resource leakage through misallocation of funds and budget overruns, misappropriation, poorly conceived tender contracts and corruption. The report (Auditor General, 2009) also shows unaccounted for revenue under some departments including the police and immigration. The Government needs to expedite follow up and prosecution of cases identified in the Auditor General's Reports. This will help in the speedy recovery of public funds, donor funds, and also deter people from engaging in activities that demean the meaning of accountability and transparency.

Ghost Workers

The issue of ghost workers is real and the government should continually update its payroll, as tax payers are losing millions of kwacha every month to non-existent employees.

Restrict Use of Public funds for Party Use

The government should refrain from using public resources for use for their party affairs. The government vehicles should be parked by 17:00hrs and phone numbers should be written on the vehicles in case this is not followed. This cost should be avoided for both fiscal and political integrity. There is need to separate ruling party needs and government needs.

Strengthening Revenue Administration

Strengthening the Zambian Revenue Authority (ZRA) is critical, especially in light of the recent decline in VAT yields. The ZRA has embarked on a modernization program, and the 2007 Budget provided the ZRA with additional funding to strengthen tax enforcement and revenue collection. Consideration should be given to providing additional support to the ZRA.

Additionally, a dedicated unit for auditing large enterprises, such as those in the mining sector, should be established in the ZRA. Capacity should be increased in related institutions with specific focus on the mining companies. This should accompany revisions to how tax is calculated for the mining sector, so as to avoid transfer pricing and increase tax collection. To enable these reforms, some form of a norm price system should be introduced in the taxation of mining activity. The authority needs to build capacities within itself to audit the mines and consider having staff represented at the mining sites

Reduce the tonnage of vehicles liable to road user charges from the current 30 tones to 20 tones.

With the current high production in the construction and mining industry, it has been observed that many inland roads have been damaged by heavy load trucks especially in the mining towns. The proposed measure will ensure that revenue raised could be used for road rehabilitation. The government should increase focus on road maintenance

Increase industrial pollution fine from the current upper limit of K180 million to K500 million

While we commend government for increasing industrial pollution fine in the recent enacted Environmental Management Act Number 12 of 2011 to the current K180 million, the penalty is not punitive enough to deter pollutants from polluting our environment. Other countries like Kenya have stronger pollution laws compared to ours. Considering the level of mining activities going on in the country, it is important that stronger pollution regulations are put in place.

The power of the Minister of Finance to exempt, remit or suspend the whole or part of the tax payable by any person must be subjected to parliamentary approval

This is in order to curb abuse of the provision and maximize on tax revenue lost through the exercise of the provision. For instance in 2009, the Minister remitted export duty payable by

mining companies on exports of copper ore and concentrates to the tune of K300 billion. Similarly the suspension of excise duty on gas oil in the same year resulted in a revenue loss of about K190 billion.

Presumptive tax on taxis and minibuses should be paid through RATSA together with road license fees.

The current system of paying on a daily basis is subject to corruption and evasion. While the system allows operators to pay tax only on the day when income has been made unlike the quarterly system, where they pay even for days they have not operated, it is true that a lot of people do not pay even when they have operated. Quarterly payment will therefore ensure increased revenue collection from this tax type which has not performed well since its introduction. The low levels of staffing at ZRA makes policing taxi and minibus drivers difficult and therefore the proposed system is superior.

Conclusion

Zambia can equitably and efficiently raise enough resources through taxation to finance development, address the needs of the poor and improve social justice. All that is needed are sound tax and non tax policies and effective tax administration structures to ensure improved government revenue.

The move to allow more participation in the budgeting process is a positive one but in order to enhance meaningful and effective participation in budget processes it is necessary to broaden knowledge and understanding of all the key actors including the civil society and the general public. Our engagements with a number of CSOs and communities indicate that this is still far from reality in Zambia despite budget themes like “people’s budget”. Our recommendation on ensuring a truly people’s budget is to have meaningful and effective participation in determining how and on what resources should be spent and how it should be generated.

The SNDP’s ambitious plan of sustaining economic growth and reducing poverty will not be realized without putting in place an efficient and equitable tax system. While the current tax system might be argued to be delivering economic growth, it is an undeniable fact that it has not done much on poverty reduction. The CSOs that are part of this submission believe that it is

possible to have a tax system that both enhances economic growth and at the same time ensures equity in terms of tax burden distribution. It is therefore our earnest appeal that our proposals be considered and reflected in both the 2012 budget and the 2012 – 2014 Medium Term Expenditure Framework (MTEF).

It should be realized that in order for the aspirations outlined in various government documents including the SNDP and vision 2030 to be realised, increased revenue mobilization resulting from an efficient and equitable tax system must be complemented with a strong public finance mechanism to ensure good utilization of resources.

CSOs also urge government not to be only concerned about the rate of growth of tax revenue in relation to economic growth but the manner of growth of tax revenue. Even though company tax has shown improvement in its contribution to the budget since 2004, it still falls below PAYE which has remained the largest contributor to tax revenues leaving people in formal employment to bear the brunt of paying tax. 2012 budget must endeavor to be more equitable by having fast growing economic sectors contribute more to the tax base and increase the tax free threshold. This might call for government to scale down tax incentives as they act as tax leakage channels. Tax administration must also be improved by increasing funding and technical capacity of Zambia Revenue Authority so as to widen the tax base and curb tax evasion and avoidance.

Annex

Sector Submissions

In view of the proposed revenue changes, CSOs anticipate that government will manage to broaden and consequently increase its revenue collection through the proposed measures above. As mentioned earlier, the interest of CSOs in engaging with government on the revenue side of the budget is ultimately to see more equity in resource use in the country. Zambia is endowed with minerals, land, and water resources. Exploitation of these resources is leading to better macro-economic targets in terms of growth rates, these resources need to be redeployed strategically to reduce high poverty levels. We have therefore proposed some ways in which some of the resources can be used to enhance equity in income redistribution in the country. These include the following:

Gender – A call for Gender Budgeting

Given that the national budget determines how the Government mobilizes and allocates public resources, Government's efforts of reducing poverty in Zambia must consider the problem of gender inequalities through the budget. Gender inequality contributes to major losses in economic efficiency and human development. Therefore gender budget initiatives can reconcile the objectives of gender equality, human development and economic efficiency.

Gender Budgeting is a strategy for ensuring gender sensitive resource allocation and is a tool for engendering macro-economic policy. Gender Budgeting is a mechanism that recognizes the fact that men generally benefit more from budget allocations than women. It thus intends to improve women's poor socio-economic status by providing them with resources that promote their well-being and empowerment. It is not a separate budget for women, but a general budget analyzed or constructed from a gender perspective which involves analyses of actual government expenditure and revenue on women and girls in comparison to that of men and boys and in comparison to their unique needs.

In order to strive for an egalitarian, society capable of promoting social and economic development, the Ministry of Finance and National Planning must address how the various budget allocations have a different impact on women and men. Gender disaggregated data

becomes very crucial here and needs to be provided. It must further be examined how vulnerabilities can be reduced; abilities of women and men strengthened and how equal access can be ensured in order to effectively fight poverty, disease and strengthen the social infrastructure and hence actively work for the development of Zambia.

Social Protection – A call for increased budgetary allocation towards social protection

Social protection in relation to the budget, promotes economic models that are based on equity in revenue distribution, social inclusion, improved income and structural policies, as well as strong linkages for both urban and rural populations. The way to achieve this is by including fair, inclusive social policies in development agendas that focus on supporting vulnerable groups.

The funding of social protection is the quintessential core of social protection systems and reflects on the goodwill of the state to protect and support its poorer populations. Funding of social protection schemes fulfills functions of redistribution, insurance, sustaining, promoting development and social justice. CSOs have observed that social spending has remained worryingly low in Zambia with Social Protection managing to command a paltry 2.3% of the national budget in 2011; which itself is a misrepresentation as a considerable share of the percentage (65%) is actually paid towards pensions arrears (PSP Zambia, 2010: p2).

The funding of social protection has important ramifications for both public and private sectors. In the public sector, the composition of expenditures and percent of tax revenue over national income reflect not only the commitment but the degree and type of government intervention. Social protection expenditures come from and go to the general circular flow of the economy thus generating a virtuous cycle of economic activity.

Government should therefore assess the range and level of social protection it renders and identify if the funding is fairly distributed. Government should take measures to improve the equity of the system and reduce or eliminate coverage gaps. Research has shown, again and again, that progress is intimately and directly related to equity in the distribution of income, assets and opportunities for all.

Social Protection has several important socioeconomic and political consequences such as development of domestic markets and the relative size of the private sector. Social protection

also modifies the financial structure of health-care, education and nutrition as well as old age and child coverage, for example. With this wider view of social protection social protection cannot be limited to a single budget category. In formulating the budget therefore, government should ensure the impact of social expenditure on achieving social protection by analyzing both the proportion and the impact of social expenditure within overall government spending.

Mobilization of resources for social development is difficult without strong and sustained economic growth, although economic growth without a strong social development agenda undermines poverty reduction efforts which are the desired outcome of economic growth.

There are various options available for mobilizing the resources for financing social protection. These have been discussed in other parts of this document and will thus only be listed:

- (a) Taxes: extending the tax base and raising of extra resources by reducing tax avoidance and tax evasion;
- (b) Discriminating user fees and consumption tax: Improvement in social services so that the better-off pay for the services, the poorer sections pay nothing more than nominal fees
- (c) Reallocating budgetary resources within sectors: Shifting expenditure from low priority to high priority uses putting emphasis on Social Protection spending within sectors
- (d) Disincentive effect; reordering budgetary priorities across sectors: Shifting expenditure to social sectors.

Agriculture – A call for increased budgetary allocation and well targeted incentives

The Agriculture sector contributes about 20% of GDP. About 70 percent of the Zambian labor force are employed in agriculture. Agriculture is a primary source of income for the poor and yet there is low productivity and profitability which are closely associated with poverty incidence.

Despite recent bumper maize harvests, the sector has underperformed over the past decade; with average growth standing at 1.3%/yr. This lags far behind population growth of 3%/yr and way below the required 6% under Maputo declaration to address high levels of poverty. There is need for urgent sector policy review, from the budget side the allocation to the sector should be increased and particularly to the following areas:

- Irrigation: Irrigation development has remained funded by donors³ There is need to increase allocations to small irrigation systems as they have indicated to benefit many small holder farmers and are cheaper for government.
- Marketing. Government re-introduction agriculture marketing bill to enhance small holder's market access and to include warehouse receipting. The FRA should revert to its original mandate of securing reserves for the nation.
- Livestock and fisheries production: Government commitment should go beyond policy formulation and analysis and establishing disease free zones.
- Research: Support to agriculture research and training centers such as Mount Makulu and National Resource Development College should be given due attention so as to enhance research in the sector.
- Extension services (crop and livestock): enhance knowledge on farming techniques like conservation agriculture and animal husbandry to reduce farmer dependence on maize.
- Agriculture statistical information- Post-harvest data have not been available since 2004 (due to lack of funding for data cleaning and processing). This should be provided for in 2012 budget.
- Review FISP/FRA programme: Have targets to enhance private sector involvement in the programmes so as to free up government funds to finance core agriculture functions that are currently under funded. FISP and FRA consume 45 to 65% of the agriculture budget and only provides services to maize production.⁴
- Economic empowerment of women and the mainstreaming of gender into policies and programs including budget remain inadequate in scope and ineffective in execution. Their contribution to the agriculture sector is enormous and this should be reflected in policies and programmes in the ministry.

³ 2011 Yellow Book

⁴ M Muleba and P Chaaba, "Study on the impact of Farmer Input Support Programme and Food Reserve Agency Marketing Arrangement" 2011

- **Manufacturing - A call to develop the sector**

This sector has not really been developed as compared to other countries in the region such as Zimbabwe and South Africa. This is evident in the number of processed food items from these countries on our local market. The development of Multi Facility Economic Zones (MFEZ) is therefore a welcome move in ensuring that there is value addition to raw materials. However, government needs to ensure that investing in these zones is affordable to allow for local investors to have the opportunity to compete with foreign investors in these areas. The current 500,000 US dollars required as minimum amount worth of investment is quite high for most start up local businesses. Furthermore, to ensure that local entrepreneurs participate favorably with foreign investors, there is need for the government through the Zambia Development Agency (ZDA) to put legislation where foreign investors are required to partner with local businesses.

Infrastructure Development – A call for accelerated rural infrastructure development

Effective infrastructure development is the key for affordable services and goods. Zambia lags behind in terms of good infrastructure like roads, rail network, airports, to mention but a few. It is a fact that, the poor state of infrastructure makes Zambia a high cost area to do business and as such, the price of essential goods and services are high in Zambia than in other countries in the region. The encouragement of Public Private Partnerships (PPP) is yielding good results, for instance, the recently commissioned Kasumbalesa Border Post is one such example. While we appreciate the government position in strengthening the (PPP's) and funding a lot of road projects in last year's budget, a challenge still remains on rural road network. To address the issue of rural development, government needs to improve on the funding of Provincial Rural Roads Unit from the current K 6 billion kwacha, per province to at least K20 billion or more.

Informal Sector – A call for formalization and effective taxation of the informal sector

The informal sector includes the vast majority of individuals and firms involved in subsistence or near subsistence activities; and those that deliberately avoid inclusion in the formal tax and levy systems.

As the economy is growing, the informal sector is growing also but its contribution to tax revenue has remained poor, contributing only 1.8% to the total income tax in 2009 (JCTR Tax

Study Report). Although ZRA has in place specific taxes targeted at the informal sector (Turnover Tax, Advance Income Tax, Presumptive Tax and Base Tax) many potential taxpayers still remain outside the tax net. In order to meet the ever-growing demand for social services and development there is need to effectively tax the informal sector. This will enhance tax revenue generation and attain equity in bearing the tax burden.

It is generally argued that formalizing the informal sector and subjecting it to tax can drive a lot of people further into poverty. However, it should be noted that there are benefits for the formalization of the informal sector both to the government and the informal sector. While formalization of the informal sector increases tax revenue to government coffers and reduces the inequitable tax burden on the formal sector, it opens doors for the informal sector to the business world where they can receive financial and other services. In the informal sector for example, it is difficult to access bank credit.

The challenges in taxing the informal sector include a cash-based economy that reduces ability to audit transactions; Lack of resources or skills for proper record keeping; the labour intensive nature of tax administration; bias towards cost effective taxation of the formal sector by Zambia Revenue Authority; and susceptibility to political interference. CSOs propose the following measures to enhance the sector's contribution to tax:

- ZRA must consider contracting the collection of informal sector taxes to formal institutions, such as local councils, that have some degree of legitimacy and can exercise control and sanctions in case of non-compliance.
- ZRA must consider utilizing informal sector business associations, such as cross border traders and similar representative bodies, to promote compliance using peer pressure and coherence
- ZRA needs to continue developing innovative approaches that can provide less costly taxpayer services, such as e-payment and e-filing and improve taxpayer education to the informal sector
- Consider reducing business fees and levies imposed by local councils.
- Enforce use of cash registers for all traders and educate buyers on the need to demand receipts/invoices once they purchase a good or service

Mining – A call for effective taxation of the mining sector

Zambia's mining sector is said to have been the driving force behind the recorded economic growth during the FNDP period and is expected to continue driving the projected GDP growth, which is expected to expand to 6.5% and 6.7% in 2011 and 2012 respectively. Copper production figures increased to 740 000 tonnes in 2010, a level not seen since 1973, and up 8.0% from the 696 900 tonnes in 2009 and are further expected to rise to 7.5% and 8.5% higher in 2011 and 2012, respectively.

CSOs believe that mining sector can contribute significantly to Zambia's economic development through providing opportunities for foreign investment, private sector development, government tax revenues, foreign exchange earnings and quality employment. However, under the current revenue system, it is apparent mining companies are not making adequate contribution to the national purse. Mining taxes measured against the total tax revenue, total mineral sales and GDP all confirm that mining taxes are making only small contributions. Comparisons with other countries and regions of the world reveal that mining companies in Zambia are contributing less tax than mining companies in a number of these countries including Africa and Latin America.

Even though mining companies have argued that they contribute to economic development by creating jobs, it should be noted that in a country like Zambia, tax revenues are by far the largest benefit from mining. This is because of the following: employment generation is quite small; the manufacturing base is not advanced enough to supply the mines with their inputs; the benefits of increased technology are limited by the low level of industrial activity; and even foreign exchange earnings are not as large as they seem since the mines use about 40% of these earnings to fund their own imports. Furthermore, tax revenue today is of more value than tax revenue tomorrow because it can be invested in its economic and social infrastructure, which will in time lead to increased revenue in the future.

Therefore, one of the biggest dilemmas facing the Zambian government with regards to the mining tax regime is how to balance two seemingly competing interest; the need for high returns and security of the mining companies; and ensuring maximum social & economic benefits for the country on the other. CSOs however feel that it is possible to improve current levels of mining taxation in a way that strikes a balance between the development needs of the country

and the requirements of mining companies for stability and adequate return on investment. A number of proposals which attempt to achieve these twin objectives are outlined below

- Quick implementation of the revenue sharing mechanism with local authorities in which the mining activities take place as provided for under the 2008 mining and minerals act. This is one way of maximising benefits from the mining sector.
- **Integrating mining taxation into a coherent national development Policy** - an adequate and complete mining tax regime can only evolve from an integrated approach that treats taxation as part of Zambia's national development agenda. Taxing levels, incentives and tax concessions must be weighed against the country's needs to raise revenue for its development. These and any future Mining Development Agreements to must be subjected to parliamentary scrutiny and due process which carefully examines their long term impact on development.
- **Mainstreaming the gemstone industry** - the structure under which gemstones are produced and marketed is failing to maximize revenue for government and is instead leading to losses through under declaration and smuggling. If the industry is appropriately regulated, export earnings from gemstones and subsequent tax revenue generated can be substantial. But to achieve proper regulation will require the enactment of a separate law from the law that governs base metals.
- **Building capacity in the ZRA:** an important step in removing real or suspected tax avoidance or evasion by mining companies lies in building the capacity of the ZRA to effectively audit and verify mining company accounts. Special audits cannot take over ZRA's routine function of auditing companies. ZRA is reported to have created a special unit dedicated to the auditing of mining companies and has already embarked on the training of its staff in the required specialist skills. This development will make it better prepared to deal with cases of transfer pricing and manipulation of financial information as and when they occur. In addition to capacity building, the ZRA must become part of

the global network of tax authorities who share information across countries to reflect the transnational nature of the operations of large mining corporations. Currently, international accounting standards do not require multinational companies to report where they make their profits and what they remit to government. To audit them effectively, authorities need to access country by country financial reports relating to the countries in which they operate. Zambian authorities are encouraged to join the campaign for new international standards that would require companies to make these country disclosures.

- **Enhancing transparency in the mining industry** - the mining companies through the Chamber of Mines and the government have signed a memorandum of understanding expressing their desire to sign up to the Extractive Industries Transparency Initiative (EITI). Although Zambia announced its intention to become a compliant country in 2008, it will only be validated as EITI compliant in 2014. In the meantime it has taken the first step to becoming compliant by undertaking a reconciliation of selected payments paid by mining companies. The first report by Pricewaterhousecoopers based on the 2008 payments has been completed and released in February 2011. Government has the agreement of all the mining companies to proceed along with this initiative.
- **Revisit government position on the payment of windfall tax** - the decision to abolish the payment of windfall tax in favor of variable profit tax needs to be revisited by government. To date no variable profit tax has yet been paid by the industry to government. This is hardly surprising because between charging tax incentives and concessions to taxable income and the possible manipulation of profit figures by companies, reaching the threshold at which variable profit tax becomes payable is quite a challenge. During this period when the price of minerals has reached levels never experienced before, it is windfall tax and not variable profit tax that should be generating the revenue expected from extraordinary price levels. By refusing to charge windfall tax, Zambia risks permanently losing the limited and time bound window of opportunity to raise substantial sums of money. Mineral prices are not going to remain until the companies are ready to declare profits. And also while the country is faced with an

inadequately equipped ZRA, windfall tax presents the most practical and equitable option under which Zambia can get its share of windfall profits arising from the current high prices of minerals. This tax can be treated as a transitory tax to better position to effectively monitor and verify mining profits.

- Government should no longer allow hedging transactions to be treated as part of mining income for tax purposes.
- Government should release the results of the financial audit that has been conducted on Mopani and other mining companies for purposes of informing an updated tax assessment by ZRA.
- Government should reveal to the public details of the recently sign stability clause with the mining companies.
- Government should increase its share holding in mining companies to allow it to be major in decision processes.