

DOMESTIC RESOURCE MOBILIZATION

MISELO BWALYA - RESEARCHER - PMRC
THURSDAY 18TH JANUARY 2018
PARLIAMENT LUSAKA

START

Introduction

- Domestic Resource Mobilization (D.R.M.) refers to the generation of savings from domestic resources and their allocation to economically and socially productive investments. Such resource allocation can come from both the public and private sectors. The public sector does this through taxation and other forms of public revenue generation.





Sources of Domestic Revenue

Resource Envelope			
Total Domestic Revenue	Income Tax		<ul style="list-style-type: none"> • Company Income Tax
			<ul style="list-style-type: none"> • PAYE
			<ul style="list-style-type: none"> • Withholding & Other
			<ul style="list-style-type: none"> • Mineral Royalty
	Value Added Tax		
	Customs and Exercise Duties		<ul style="list-style-type: none"> • Customs Duty
			<ul style="list-style-type: none"> • Excise Duty
			<ul style="list-style-type: none"> • Export Duty
	Other Revenues		<ul style="list-style-type: none"> • Tourism Levy
			<ul style="list-style-type: none"> • Premium Levy
			<ul style="list-style-type: none"> • Skill Development Levy
	Non- Tax Revenues		<ul style="list-style-type: none"> • Fees collected by RTSA
			<ul style="list-style-type: none"> • Fees by collected Zambia Police



Informal Sector Taxes

Turn Over Tax	Applicable to business with a Turnover of K 800,000 or Less (3% + Presumptive amount.
Base Tax	Collected in the markets
Advance Income Tax	Charged at Point of Import, waived off for Tax Compliant Individuals
Presumptive Tax on Minibuses & Taxis	E.g. 64 Bus seater and above – K7200 per annum





Tax Administration and Policy

- Upward adjustment of the presumptive tax rates to **50 %**.
- Upward adjustment of Base Tax rate from **K150 to K365** per year.
- Introduction of introduced a surtax on selected imported products that are locally produced in order to support the growth of the domestic industry
- Upward adjustment on Customs duty on electric geysers and stoves to **40%** percent from **25%** percent.
- Introduction of penalties in the VAT Act, and the Customs and Excise Act for taxpayers that fail to furnish records upon request.
- Amendments to the Income Tax, the Property Transfer Tax, the Value Added Tax, the Customs and Excise, and the Skills Development Levy Acts. These are to harmonize tax legislation to make tax administration more effective. These measures are revenue neutral

Non Tax Measures

- Introduction of landing rights charge at the rate of K3,150 per Television channel which has less than 35% local content except for educational and scientific channels





Domestic Revenue Mobilization Strategies

- **Modernization and Automation of Revenue Collection Processes:** The tax administration measures being implemented include the introduction of enhanced information technology solutions to improve Value Added Tax (VAT) collection. In particular, the use of electronic devices such as fiscal cash registers will continue to be rolled out in 2018.
- **Rationalization of Tax Incentives and Processes for Facilitation:** During the medium term, Government will continue to streamline the tax incentive structure. e.g. Discontinuation of the 5-year income tax holidays that is facilitated through the Zambia Development Agency
- **Informal Sector Taxation:** Over the medium term, Government will partner with various stakeholders such as local authorities to develop practical mechanisms of improving tax compliance in the informal sector.
- **Appointment of Revenue Collecting Agents to improve efficiency:** In an effort to improve efficiency in collecting revenues, Government will appoint agents to collect other taxes, in addition to VAT. These additional taxes will include withholding taxes on rentals, turnover taxes, presumptive taxes, base tax and other fees collected by Government institutions.





Challenges to Domestic Revenue Mobilization

- **Burdensome tax policy regimes.** For the taxpayer, getting an agreement with the tax authorities as to how much tax is due, and how and when it is to be paid, can be quite an administrative burden. Many resource organizations have even to hire experts to assist in handling tax matters.

Example : In Zambia it takes our case study company 157 hours to comply with its taxes, it makes 26 payments and has an average Total Tax Rate of 18.6%.

- **A large and hard-to-tax informal sector of the economy.** The size of the informal sector (also known as shadow) economy in many Sub-Saharan African (SSA) countries is significant. A large informal sector tends to be prevalent in countries where the economy is largely dependent on subsistence agriculture. Many studies have shown that the size of the informal sector has an inverse relationship with revenue collection.

Significant tax revenues are lost through Zambia's informal sector which amounts to 83.9% of aggregate employment, totaling 4,491,943 people outside the tax net in 2012.

2016



K 573 million
ZRA Uncollected Revenue



- **In the Case of Zambia, the Revenue Authority in the year ending 2016 due to various inefficiencies resulted in the under collection of revenue which amounted of K 573 million**

Challenges to Domestic Revenue Mobilization (Contd)

- Low tax moral and absence of a fiscal contract. The large size of the shadow economy in most SSA countries suggests low levels of tax moral. Similarly, taxpayers are unlikely to be willing to pay taxes when a government offers tax exemptions to a select few.
- **Research reveals that Zambia has a generally low tax morale as shown through levels of tax evasion, avoidance and non-compliance.**
- Revenue losses through excessive tax exemptions and incentives. In order to attract investments in certain areas of the economy. Government offers tax exemptions and incentives such as tax holidays , tax credits, reduced income tax rates, accelerated depreciation allowances, concessions in export processing zones and import duty waivers.
- An IMF study reveals that exemptions and incentives are not critical to investment decisions, especially when other dimensions of the operating environment (e.g. physical infrastructure, the financial system, labor laws, property rights etc.) are in poor shape.
- **Corruption in tax administrations.** Corruption in public service plagues many countries in our region. “The level of corruption generally parallels that in the public service as a whole” and generally contributes revenue leakage (Purohit, 2007). Anecdotal evidence shows that Revenue Authorities use their discretionary powers to interpret complicated tax laws to their advantage, and/or looking the other way when it comes to taxing the elites.



Challenges to Domestic Revenue Mobilization (Contd)

- Zambia has a very large informal sector and underground economies where cash transactions do not need any audit trails for tax purposes. It will therefore, be important to find ways of taxing the informal sector. Need for effective administrative mechanisms aimed at reducing tax evasion and tax avoidance which will broaden the tax base.
- Promote diversification within the **Agriculture and Manufacturing** sector. Diversification in the Agriculture sector should include **crop, forestry, fisheries, horticulture, and livestock** products while diversification in the manufacturing sector should focus mainly on the mining products and other non food commodities to improve on the quality and value of exported products
- Investments in renewable and alternative energy such as **solar, wind, biomass and geothermal energy** to increase power supply which will impact positively on productivity.
- Invest in other forms of cheaper transportation such as rail for heavy vehicles to reduce on the cost of road maintenance and reduce the cost of production incurred through transportation
- Promotion of credit growth within the private sector through effective monetary policy to to reduce lending rates
- Investment in technology within all aspects of the economy as it is regarded as a primary source in economic development as the various technological changes will contribute significantly to the country's GDP





THE NATIONAL BUDGET AND THE GROWING INEQUALITY IN ZAMBIA

AKABONDO KABECHANI- HEAD OF MONITORING & EVALUATION - PMRC

THURSDAY 18TH JANUARY 2018

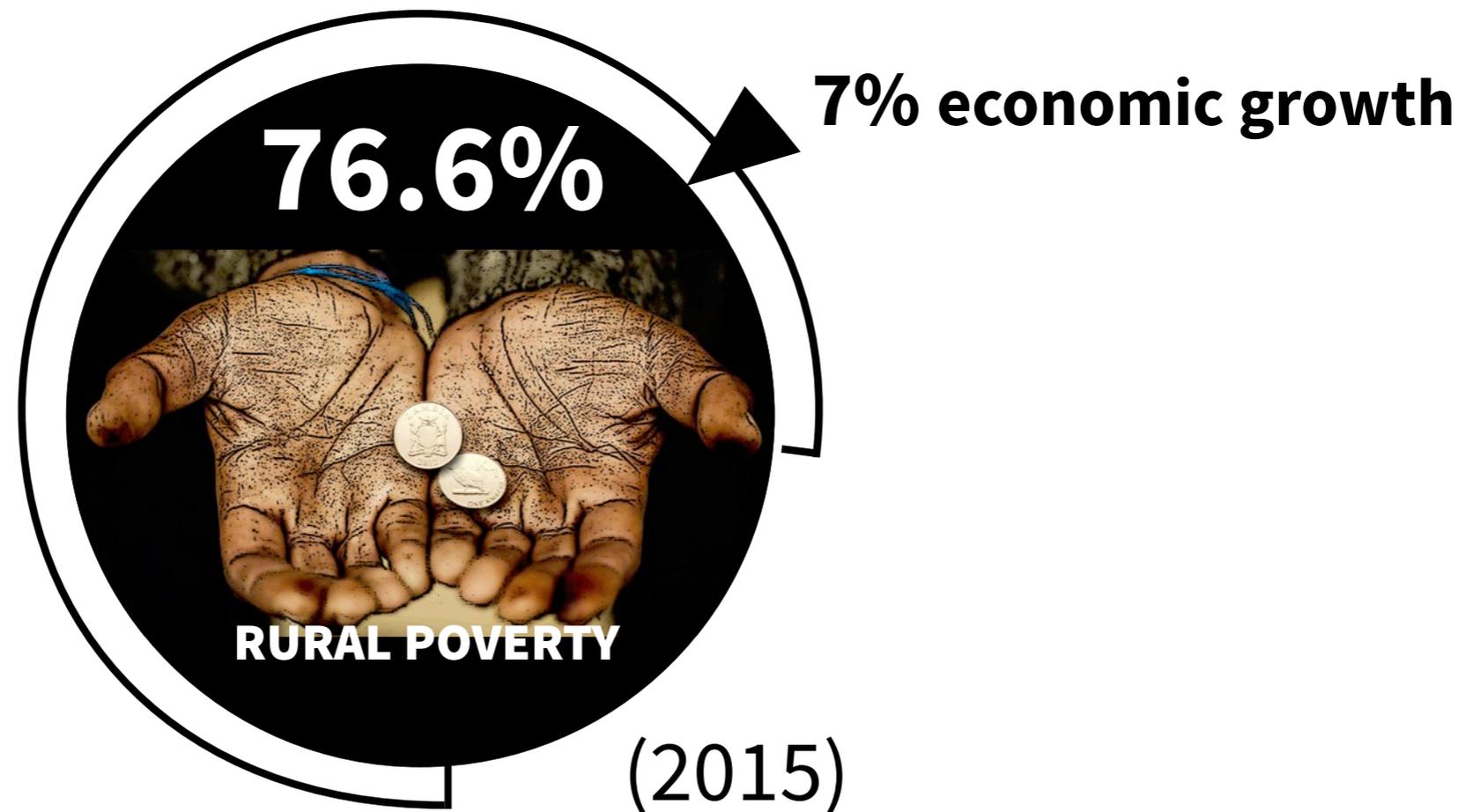
PARLIAMENT LUSAKA

START



Introduction

- **1. Strategies that the government has put in place to ensure inclusive growth and reduce growing inequality**
- Zambia has recorded an average of 7% economic growth in the recent years.
- Poverty levels are still high at 54.5%, with rural poverty at **76.6%** (2015).
- 2015 Living Conditions Monitoring Survey, shows gap between the rich and the poor in Zambia is widening with the Gini coefficient as at 2015 standing at **0.69** from **0.65** in 2010 (African average of approximately 0.43) 0.69 Gini Coefficient for Zambia reflects the country's inability to distribute its economic growth fairly across the population.





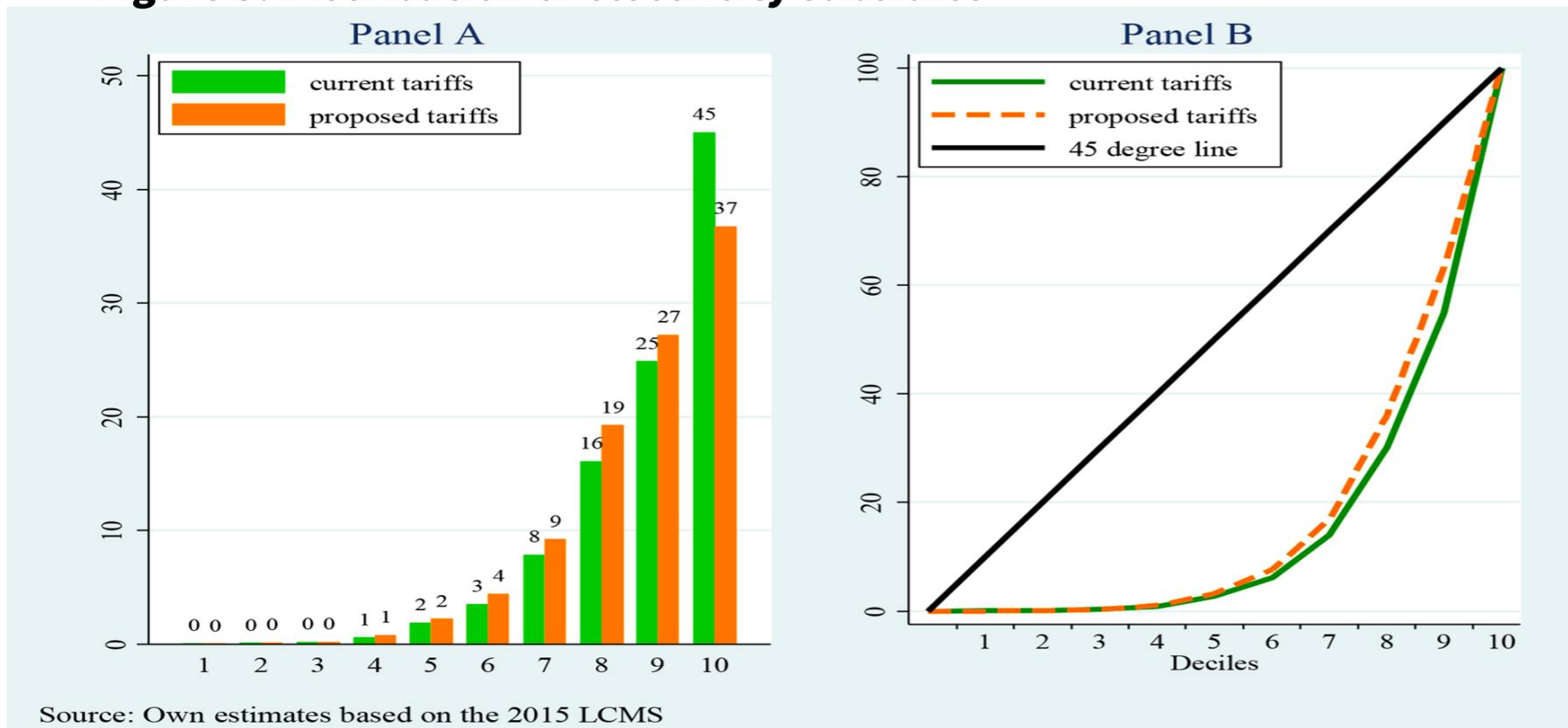
■ **Strategies to Curb Inequality Include:**

- **Minimum wage policy**- this is a useful income redistribution mechanism that government introduced with an expectation of raising income levels of those groups of people employed for improvement in living standard.
- **Social welfare schemes**- Effective in reversing inequality in the country. The social cash transfer scheme which government has been implementing since 2003 has been a commendable income reallocation mechanism. Over the past two years government has increased the allocation to social protection by **87% from 2.4% in 2016 to 4.2%** of the total 2017 budget.
Increase in **pension benefits** from **ZMW 805 million** in 2016 to **ZMW1.7 billion** in 2017 was significant and commendable.
- Government further increased the allocation and coverage to social cash transfer from **ZMW 302 million to ZMW 552 million** in 2017.
- Nominal reduction of 15% from **ZMW 2,693,210,000 in 2017 to ZMW 2,301,259,752 in 2018**. Despite this reduction the allocation to Social Cash Transfer has increased by 31% with the number of Social Cash Transfer beneficiaries increasing to **700,000 from 590,000** in 2017.
- Supported by Government's full migration to an electronic social cash transfer system
- **Infrastructure development**- the government has since 2011 embarked on massive economic and social infrastructure development both in urban and rural areas. Government has made positive strides in the development of infrastructure in order to increase access to social services.
- **National Development Plans**- Zambia's 7NDP aims to create a diversified and resilient economy for sustained growth and socioeconomic transformation driven, among others, by agriculture, tourism, manufacturing and mining through economic diversification and job creation; poverty and vulnerability reduction; reduced developmental inequalities; enhanced human development; and an enhanced governance environment for a diversified and inclusive economy.

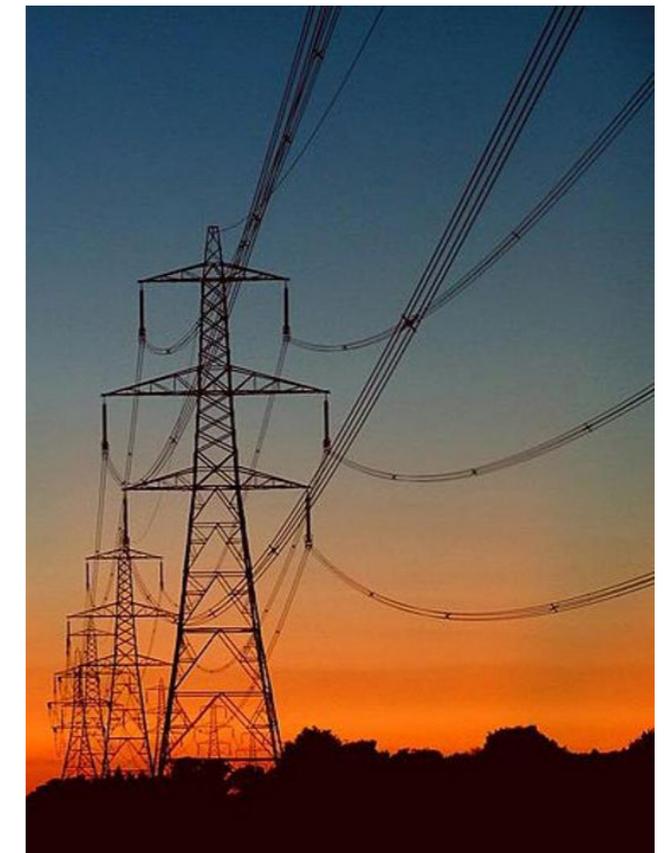


- **Removal of subsidies in the electricity and fuel sector-** Subsidies have been the third-largest component by economic classification and increased from **6.6% in 2012** to **13.9% in 2015**. Removal of subsidies in the two sectors and subsequent scaling up of social cash transfer is aimed at reducing inequality because subsidies have been generally regressive and poorly targeted resulting benefits largely accruing to the wealthier in the Zambia population (Please refer to figure 3 below from PMRC study on **Energy Policy Reform and Effects of Removal of Electricity Subsidies**).

- **Figure 3: Distribution of electricity subsidies**



Source: Own estimates based on the 2015 LCMS



- Subsidies are highly **regressive**, with the **richest 20%** of the income distribution receiving about **70%** of the electricity subsidies while the poorest **20%** receive less than 1% of the electricity subsidies. A look at the entire distribution actually shows a particularly striking pattern – nearly all the electricity subsidies accrue to the richest **50%** of the population, with less than **4%** of the benefits received by the bottom **50%** of the population.

2. What are the challenges of ensuring inclusive growth

■ **Inadequate and poor infrastructure-**

One of the major areas that have aggravated the levels of inequalities in rural is infrastructure deficits which has limited their competitiveness in economic activities. Most rural parts of Zambia have low access to electricity and poor road networks to attract needed investment in order for them to contribute to economic growth and job creation.

■ **Limited financial inclusion-** this has worsened the level of income inequality in the country. According to the 7NDP more than **60% of Zambians do not have a bank account** while only **5%** borrow successfully from the formal financial institutions. Those who borrow are usually large firms and wealthier households. Small businesses and poor households continue to face credit constraints due to prohibitive bank requirements thereby exacerbating inequalities.

■ **Limited formal high paying jobs-** the majority of Zambians are employed in the informal sector (**83.9%**) such as the agricultural sector which is characterised by low productivity and low disposable income at household levels.

Formal employment (16.1%) characterised by high incomes than those in the informal sector.

■ **Limited access to social amenities-** High inequality deprives low income households of the ability to afford **basic necessities** like education, health care, food and housing. Low Spending on Social Benefits- Spending on Social Benefits declined from **3.1% to 1.6%** of total spending in 2015.

■ **A lack of access to markets** - whether due to poor infrastructure or productivity, limited education, or insufficient information - prevents access to both labour and capital.

In many rural societies, there are few job opportunities outside of agriculture, often resulting in food and income insecurity due to the precarious nature of farming. **Rural workers are largely concentrated in jobs such as owners-cultivators, tenant farmers, informal care workers,**

agricultural day-labourers, and livestock herders.

Without access to other labour markets, rural workers continue to work for extremely low wages in agricultural jobs that tend to have seasonal fluctuations and thus little income security.

3. The effectiveness of the budget process in ensuring inclusive growth and reducing inequality Inadequate and poor infrastructure

- The extent to which the government budget is realistic and implemented as passed by the legislature is measured by comparing actual revenue and expenditure with the original budget. Assessments covering 2013, 2014 and 2015 do not support achieving inclusive growth and reduction of inequality.
- **The aggregate results (2013-2015) show a reasonably good performance in achieving fiscal outcome, but in respect of allocating resources and delivering services the substantial variances in economic type, which are also present in the results for administrative heads, the budget is has not been reliable.** There have been some consequential fiscal discipline issues regarding expenditure control as Ministries, Provinces and other Spending Agencies override commitment and cash controls and incur excess expenditures through supplier credit to carry out their functions. This has resulted in expenditure arrears that are proving difficult to eradicate.

■ 4. The role of the national budget as a tool for inclusive growth

The budget is an important tool that the government can use to ensure inclusive growth of an economy.

It is through the budget that a government can promote implement policy interventions that enforce inclusive macro-economic agenda of a country.

Most important policy intervention the government can implement through the budget is to ensure that all sectors in the economy contribute to the growth of the economy which will in turn result in a substantial reduction in poverty.

Interventions the government can implement through the budget to ensure inclusive growth are;

- **Investment in infrastructure** –there is need to invest in both social and economic infrastructure especially in rural areas. Lack of infrastructure in rural areas has led to the rural economies not contributing significantly to the economy.
- **Investment in skills development** – there is need to invest in appropriate skills development to bridge the skills gap that the country is experience such as those in ICT, entrepreneurship and research and development.
- **Fair tax pronouncements** – there is need to have a tax system that is inclusive and fair to all salary bands in the country.

5. Explain the factors that may have led to poverty disparities between the rural and urban areas-Inadequate and poor infrastructure-

- Limited access to finance – the availability of finance is low is low, with the rural population being affected more than their urban area counterparts. The limited in finance has led to low productivity in rural areas because they have less money to invest into the rural productive sectors.
- Inadequate infrastructure – most rural parts of Zambia face poor infrastructure services such as roads, hospitals, schools, markets and water and sanitation. The absence of this type of infrastructure has further contributed to poverty and vulnerability among rural areas.
- Limited access to services-limited access to social services is a constraint in the rural areas of Zambia. Not only are social services inadequate, but where they are available, financial constraints often limit the extent to which rural communities can access them.
- Poor access to education- In many rural societies, a lack of access to education and limited opportunities to increase and improve one's skillset inhibit social mobility.
- Low levels of education and few skills result in much of the rural poor working as subsistence farmers or in insecure, informal employment, perpetuating the state of rural poverty.
- Inadequate education regarding health and nutritional needs often results in under-nutrition or malnutrition among the rural poor.
- Social isolation due to inadequate roads and poor access to information makes acquiring health care (and affording it) particularly difficult for the rural poor, resulting in worse health and higher rates of infant mortality.



6. Factors that may have led to failure by small scale businesses to graduate into big businesses

Many factors have contributed to the stagnation of Small Scale Businesses in Zambia. These include;

- Pre-Start Capital
- Working Capital
- Capital Investment Capital.
- Poor Customer Repayment
- High and Multiple Interest
- Rates
- Unstable Foreign Currency
- Unfair Market Competition due to Subsidised and Smuggled Imports
- Inaccessible Government Tenders
- Unfair market Competition from Foreign Owned Firms

7. Explain the extent of local ownership of business Industries in Zambia (2017 Company Ownership in Zambia)

Companies with Zambian Ownership	11,0170
Companies with Foreign ownership	38,096
Companies with both Zambian and Foreign Ownership	22,853
Companies with majority Zambian Ownership for those with both Zambian and Foreign Ownership	17,630

Source: Patents and Companies Registration Agency 2017

- Current data provided by the Patents and Companies Registration Agency shows a total of companies with full Zambian ownership at 110,170, foreign ownership at 38,096, Zambian and foreign ownership at **22,853** out of which 17,630 have majority Zambian ownership representing **77.1%** penetration by Zambians in this category. The data provided does not include business names.
- PMRC had submitted a reform proposal on the Companies’ Bill to the Ministry of National Development Planning to address challenges faced in trying enhance local participation and wealth creation for Zambians. The Companies Bill is currently at ‘assent’ stage in the legislation process.



8. What measures (incentives) has Zambia put in place to promote the participation of Zambians in manufacturing

- In order to enhance full participation of SMEs in the economy the Zambian government established Zambia Development Agency (ZDA) to carry out the following functions for SME development:
- **Local Economic Development**; involves programmes on the utilization of local resources through value addition. It encompasses development of n Cluster Development to stimulate local (Rural and peri-urban) resource utilization and value addition. Under this component Guidelines and incentives for business environment development are provided.
- **Business Linkages Programme** - The programme involves Fostering business linkages between large corporations and local MSMEs which stimulate commercial solutions for both parties. The business linkages intervention strategy is premised on the rationale that such linkages can provide commercial market/demand led business solutions for both large companies and MSMEs. Business linkages seek to identify real market opportunities within the value chains of large corporations for local enterprises on one hand and to help lower procurement and distribution costs for large corporations on the other hand.
- Revisions to the Zambia Development Agency Act and the Companies' Bill



9. What measures has the government provided to protect local industries and promote consumption of local products

In order to protect local industries and promote the consumption of locally produced good, the government has implemented various measures among them;

- At policy level, the government through the Ministry of Commerce, Trade and Industry has formulated and implemented the commerce, trade and industrial policy. One of the objectives of the policy aimed at promoting the consumption of locally produced goods. The policy prescriptions for this policy objective are encouraging the branding of locally produced goods and services and maintaining support for the 'Buy Zambia Campaign', in order to ensure that locally manufactured goods and services compete favourably in the domestic market, while becoming competitive on the international markets. The campaign seeks to encourage Zambians to buy Zambian products and services.
- The Citizens Economic Empowerment is another opportunity available to SMEs. The objectives of this reform programme are to unlock the growth potential of citizens through business development support and empowerment initiatives (Ministry of Commerce, Trade and Industry, 2005). This programme can be taken advantage of by Zambian SMEs to ensure that they benefit from the funds available for entrepreneurs to develop their businesses
- The ministry of Commerce, trade and industry has been hosting manufacturing expos where they encourage upcoming Zambian SMEs to participate for their production promotion and business opportunities.

10. What is the level of participation by Zambians in multinational companies (both in management and supplier of goods and services);

- Data on level of participation by Zambians in MNCs in management and supply of goods is scanty and unreliable. This presents challenges in prescribing correct policy interventions and will require a full scale research project to present reliable and up-to-date information.

11. Recommendations.

- Actualise pillar number two and three of the 7NDP which aims at reducing poverty and vulnerability; and developmental inequalities in a joint manner by integrating of policies aimed at targeting poverty reduction and those looking to address inequality. Such an approach would help to ensure that policies in the two areas reinforce each other and that together, they are more effective in achieving the two objectives.
- Raise income in the agriculture sector by raising productivity and incomes specifically for the self-employed. This will impact significantly on both inequality and poverty due to the large proportion of households with access to this type of income.
- Feeder roads infrastructure is very important in developing and supporting agriculture in rural areas and Government must enhance rural connectivity. Government must prioritise the increased access to social services and completion of on-going education, health and water and sanitation infrastructure in rural areas. **However, the budget allocations towards Housing and Community Amenities shows 42% of this budget going towards Lusaka Sanitation Project.** In order to rebalance the allocations in this sector, the Government must allocate more resources towards rural sanitation to achieve objectives set out in Reducing Development Inequalities under Pillar 3 of the 7NDP.
- Planning and Budgeting Bill must be enacted to ensure adherence to planned programmes and enhance budget credibility.
- Government must ensure the full roll out of Integrated Financial Management Information System (IFMIS) so that no MPSAs shall be allowed to spend outside the system. This will curb accumulation of arrears.
- Government needs to align spending in the agriculture sector to support key drivers of growth in the sector that include extension services, research and development, livestock management and production, disease control and irrigation. These measures have the potential to grow the agriculture sector and reduce inequalities.



11. Recommendations Cont'd.

- Enforce measures outlined in the Companies' Bill to increase local participation by Zambians in business.
- Fully implement the budgeting process based on the 7NDP as opposed to the 'silo' sector based budgeting process.
- Increase budget support to functions that support industrialisation. Economic affairs by function covers mining, energy, agriculture, manufacturing, construction transport, communications, forestry and other industries. **Given the desire by government to diversify the economy and support objectives of the 7NDP, the reduction in spending here from ZMW 20,132,600,00 in 2017 to ZMW 17,258,329,480 in 2018 National Budget is likely to hinder diversification and job creation.**
- Government must ensure that **major revenue collection processes** are fully automated to minimise revenue leakages associated with the manual process. This measure needs to be supported by strong IT infrastructure to minimise disruptions and ensure efficiency.
- Priority must be given to the reforms listed in the **MTEF** that have be made to ensure **smooth implementation of the National Budget and the 7NDP**. Further, there will be need for communication tools to be developed and distributed across all ministries and spending agencies across the country to ensure that the multi-sectoral approach of development as outlined in the **7NDP** is realised.

THANK YOU

Unlocking Zambia's Potential

Response to this presentation can be sent to:

info@pmrczambia.net

Policy Monitoring and Research Centre (PMRC)
Plot No. 36c Sable Road, Kabulonga, Lusaka, Zambia
Private Bag KL 10

Tel: +260 211 269 717 | +260 979 015 660

www.pmrczambia.com



END