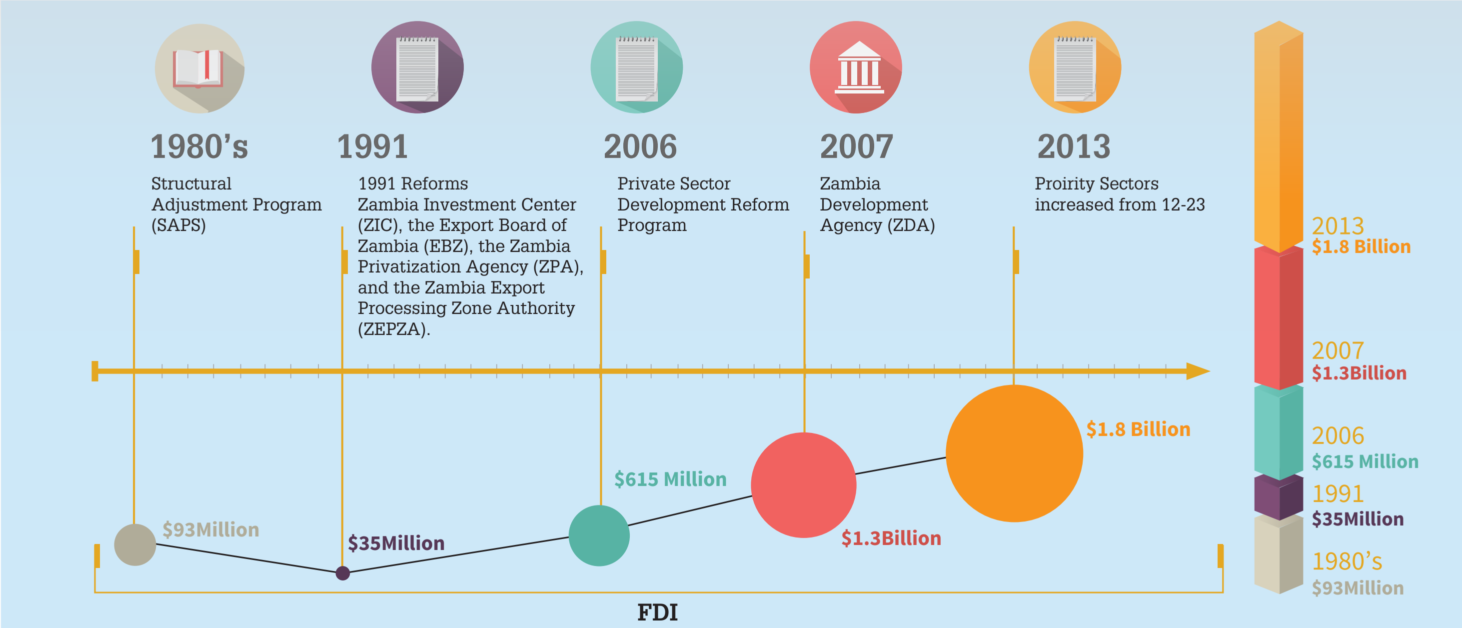
PMRC TAXATION SERIES

The Role of Efficient Tax Incentives in Enhancing Investment

Tax incentives are tools used increasingly by many developing countries to attract Foreign Direct Investment (FDI) and promote economic growth. Tax incentives can be defined as special exclusions, exemptions, or deductions that provide special credits, preferential tax rates or deferral of tax liability.

INVESTMENT TIMELINE:

In 1991 reforms were introduced that led to the creation of a number of institutions to achieve the objectives of the Structural Adjustment Program (SAP) and promote trade and investment. ZIC was later merged with the other statutory bodies to form the Zambia Development Agency (ZDA) through the enactment of the ZDA Act No.11 of 2006 as a result of the Private Sector Development Reform Program (PSDRP). An intial 12 priority sectors were identified in 2006 and these have increased to 23 in 2013 through the introduction of stautory instruments.



Source: Adapted by Policy Monitoring and Research Centre (PMRC) from Highlight of the Policy Framework for Investment in Zambia, April 2011

Despite Zambia's heavy investment in the provision of tax incentives, investment obligations such as employment creation have not been achieved. The provision of tax incentives has faced the following challenges:

Lack of targeted incentives
The increase of priority sectors from 12 in 2006 to 23 as of 2013 implies that tax incentives are used in general and not targeted to promote identified growth sectors, calling into question their efficiency.

Unrealistic investment costs for local investors
The minimum capital investment of US$500,000 is viewed by private sector as too high citing the lack of access to capital finances as a major challenge

US$ 175 Million
LOST IN 2012

Erosion of the tax base
The International Monetary Fund (IMF) have estimated that Zambia lost approximately US$ 175 million in 2012, equivalent to 1.41% of GDP due to tax incentives.

Lack of employment and economic growth benefits
The Ministry of Finance acknowledged in 2013 despite the issuance of tax incentives, investment has not created sufficient employment.

Lacks of consistency in supporting policies
Policy reversals in the recent past have affected the stability of the investment environment.

WHAT DO EFFICIENT TAX INCENTIVES MEAN FOR ZAMBIA AND ZAMBIANS:

- Enhanced flow of FDI
- Reduced tax expenditures
- Enhanced participation of local investors
- Enhanced employment creation and economic growth benefits
- Increased investor confidence

PMRC RECOMMENDATIONS

1. **Comprehensive Cost-Benefit of Tax Incentives:** The need for assessment to understand the benefits and cost implications of offering incentives.
2. **Stabilisation of the Investment Environment:** Stable financial and economic policies and conditions will encourage investor confidence.
3. **Formulation of an overall Investment Policy:** This will guide the focus and direction of investment in the country.

PMRC
Policy Monitoring and Research Centre

info@pmrczambia.net | www.pmrczambia.com

Plot No. 32 Sable Road, Bishop Road Kabulonga
Lusaka, Zambia Private Bag KL 10
Tel: +260 211 268 385 | +260 979 015 660