REPORT OF THE COMMITTEE ON ESTIMATES FOR THE FIRST SESSION OF THE ELEVENTH NATIONAL ASSEMBLY APPOINTED ON THURSDAY, 20TH OCTOBER, 2011

Consisting of:

Mr H H Hamududu, MP (Chairperson); Mr E M Sing'ombe, MP; Mr D Phiri, MP; Ms D Siliya, MP; Mr R L Mpundu, MP; Mr G Kunda, MP; Mr A L Lufuma, MP; Mr C Matafwali, MP; and Mr L Chabala, MP.

The Honourable Mr Speaker
National Assembly
Parliament Buildings
LUSAKA

Sir,

Your Committee has the honour to present its report on its deliberations for the year 2012.

Functions of the Committee

2.0 The functions of your Committee are as follows:

(a) to examine the Estimates and Excess Expenditure Appropriation Bill;

(b) to report on the economics, improvement in organisation, efficiency or administrative reform, consistent with the policy underlying the estimates, examine whether the money is well laid out within the limits of the policy implied in the estimates;

(c) to suggest alternative policies in order to bring about efficiency and economy in administration;

(d) to carry out regular examination and scrutiny on budgets, estimates and management thereof, and conduct budget hearings; and

(e) to make recommendations in a report to the House for consideration and implementation in future budget estimates.

Meetings of the Committee

3.0 Your Committee held fifteen (15) meetings to consider submissions from various stakeholders on the budget process in Zambia and the impact of the Euro-zone debt crisis on the European Union (EU's) budget support to Zambia.

Report of your Committee

4.0 This Report is in five parts. Part I deals with the budget process in Zambia while Part II highlights the impact of the Euro-zone debt crisis on the EU's budget support to Zambia. Part III highlights the findings arising from the tour to Kazungula, Katimamulilo and Victoria Falls border posts. Part IV of the Report highlights your Committees observations and recommendations and Part V is the Conclusion.

PART I

THE BUDGET PROCESS IN ZAMBIA

5.0 Your Committee was privileged to study in detail the budget process in Zambia. The study was necessitated by concerns from various stakeholders that the preparation of the budget was not consultative enough and that the role of Parliament in the budget process was limited to approval only while the power of the Executive in this regard was overbearing. There was also a concern that the legal framework governing the budget process was inadequate and in some cases outdated. In undertaking this study, your Committee was expected to achieve the following objectives:

a. appreciate the budget process in Zambia;
b. establish the role of Parliament in the budget process;
c. establish the role of Civil Society Organisations (CSOs) in the budget process;
d. appreciate the legal framework governing the budget process;
e. establish challenges facing the budget process in Zambia; and
f. recommend measures to improve the budget process.

In order to gather adequate information on this subject, your Committee sought written memoranda and oral submissions from the Ministry of Finance and National Planning, the World Bank (WB), the European Union (EU) Delegation to Zambia, Caritas Zambia, Civil Society for Poverty Reduction (CSPR), Jesuit Centre for Theological Reflection (JCTR), the Economics Association of Zambia (EAZ) and the Zambia Institute of Chartered Accountants (ZICA). The summary of the findings of your Committee is set out here below.

THE ANNUAL BUDGET

5.1 Your Committee was informed that the Budget is a document containing various government activities or work programmes expressed in monetary form. Thus, the budget is an important economic policy tool for macroeconomic management and resource allocation. It provides a comprehensive statement of the nation's economic priorities.

Recent Budget Reforms

The Committee was informed that in 2003, the Government embarked on planning and budgeting reforms. One initiative from these reforms was the introduction of the Medium-Term Expenditure Framework (MTEF). The MTEF is a broad Public Expenditure Management (PEM) tool which covers budget preparation, implementation, monitoring and evaluation. It is a three-year framework within which available resources are divided between sectors with a view to achieving government objectives. The MTEF was introduced in Zambia to address previous weaknesses in the planning and budget processes, with the following objectives:

i. to ensure the efficient allocation and management of public resources;
ii. to develop and maintain fiscal discipline in planning and management of public resources;
iii. to ensure commitment to budget priorities at the national and sector levels;
iv. to improve accountability of national resources; and
v. to improve predictability of resources.

THE STAGES OF THE BUDGET PROCESS AND THE EXTENT TO WHICH ZAMBIA CONFORMS TO THESE STAGES

5.2 Your Committee was informed that the budget cycle generally consists of four stages, namely, *Formulation (Drafting), Enactment, Implementation and Auditing.* These stages in relation to the Zambian context are discussed in turn here below.

i. Budget formulation (Drafting) Stage

Your Committee was informed that the initial stage in the budget process was the drafting of the budget. Through this process, the Ministry of Finance and National Planning (MoFNP) develops a national budget every year. Normally, the drafting of the budget goes through the stages set out hereunder.

(a) Preparation of a Consultation (Concept) Paper for Cabinet

Your Committee was informed that the starting point in the drafting of the budget was the preparation of the Concept Paper. The Concept Paper seeks guidance from Cabinet at an early stage concerning emerging Government developmental objectives and policy interventions that were likely to impact the way resources would be allocated over the subsequent budget year and the medium term period. It further seeks Cabinet's approval of key budget principles or fiscal policies to be followed so as to achieve overall government objectives.

(b) Update of the Macro-Fiscal Framework for the Forthcoming three years and Draft Green Paper

After receiving policy guidance from Cabinet, the Ministry of Finance and National Planning prepares the macro-economic and fiscal frameworks for the forthcoming three financial years using the latest real sector monetary and fiscal data. On the basis of this framework, the Ministry then prepares the Medium Term Expenditure Framework (MTEF) in which it allocates expected resources from taxes, non-tax revenues, grants and loans to Ministries, Provinces and Spending Agencies (MPSAs). This leads to the formulation of a "Green Paper" also called the MTEF which outlines Government's macroeconomic policies and objectives, and fiscal policies and strategies as well as expenditure allocations.

On the revenue side of the budget, the inter-ministerial Tax Policy Review Committee (TPRC) invites various stakeholders including the private sector and civil society to make tax proposals for the next budget. The TPRC sometimes meets some of these stakeholders, if further clarification was required. It evaluates all the submissions and makes recommendations to Cabinet for consideration during the preparation of the Draft Budget (Yellow Book).

(c) Cabinet Approval of the Green Paper and Dissemination of Budget Guidelines (Call Circular)

After the approval of the draft Green Paper by Cabinet, the Ministry of Finance and National Planning issues the Green Paper as a "consultative document" to various stakeholders including the National Assembly through the Estimates Committee, civil society groups, cooperating partners and the general public for comments for possible inclusion in the final budget. The Ministry of Finance and National Planning also issues a Call Circular to MPSAs providing them with the guidance on how to prepare their budgets and the resource ceilings allocated to them. These ceilings are disaggregated into Personal Emolument and Non-Personal Emoluments components, with some resources being earmarked for specific key government programmes such as, Farmer Input Support Programme (FISP). The "Call Circular" also acts as a guide to MPSAs on how the estimates of revenues and Expenditure should be prepared.

(d) Budget Hearings on the Draft Budget Estimates of MPSAs

After receipt of the "Call Circular", MPSAs prepare their draft budget estimates and submit them to the Ministry of Finance and National Planning. Budget hearing meetings are then held to discuss draft estimates of each MPSA. These interactive meetings provide an opportunity for the Ministry of Finance and National Planning to ensure that the Budgets for the MPSA’s were aligned with their expenditure priorities.

Changes in tax policy are analysed by the Tax Policy Review Committee chaired by the Director of Budget. The Committee comprises officials from within the MoFNP and key line ministries, such as the ministries of Justice, Trade and Industry, Mines, and Home Affairs. Others on the Committee include the Zambia Development Agency, the Bank of Zambia and the Zambia Revenue Authority. Also included are Government institutions and departments that collect or generate revenue. The task of the Committee is to analyse submissions on revenue proposals received from the various stakeholders in the economy and recommend to the MoFNP possible proposals to be considered for inclusion in the budget. The Committee is divided into four Working Groups, namely the VAT, Customs and Excise, Direct Taxes and Non-Tax Revenue. The Committee assesses the viability of the suggested measures and the capacity of the concerned institutions to generate the projected revenue.

Once all submissions and reviews have been discussed and concluded, the Budget Office processes the data and compiles a consolidated report which was sent to the Permanent Secretary and the Secretary to the Treasury at MoFNP. In addition, in the light of the proposed decisions during the budget hearings, MPSAs are required to conclude their budget estimates and thereafter, the Ministry of Finance and National Planning consolidates all the estimates of Revenue and Expenditure into a draft Budget "Yellow Book" for submission to Cabinet.

(e) Cabinet Approval of the Draft Budget and Budget Speech

Your Committee was informed that the MoFNP prepares a Cabinet Memorandum on the Budget for consideration by Cabinet indicating proposed revenue measures to support the budget. Cabinet extensively discusses the budget proposals and made relevant adjustments. The discussions further provided ministers with a chance to defend their ministries' allocations. Once Cabinet approves the budget proposals, a printed document of estimates of expenditures and revenue referred to as the Yellow Book is published.

ii. Enactment or Authorisation Stage

Your Committee was informed that the second stage of the budget process is the enactment of the national budget. This starts from the point when the Minister responsible for finance presents the budget statement to Parliament. The *Constitution of the Republic of Zambia* mandates the Minister of Finance and National Planning to present the Budget to Parliament. *Article 117(1) of the Constitution of the Republic of Zambia* stipulates that "*the Minister responsible for finance shall cause to be prepared and shall lay before the National Assembly within three months after the commencement of each financial year estimates of the revenues and expenditure of the republic for the financial year".*

This provision was, however, amended through the *Constitution of Zambia (Amendment) Act No. 20 of 2009*. *Article 117* of the *Constitution of the Republic of Zambia* was amended by repealing clause (1) of Article 117 and replacing it with a new clause (1) which requires the Minister responsible for finance to cause to be prepared and lay before the National Assembly estimates of revenue and expenditure *within ninety days* before the commencement of the next financial year.

The presentation of the budget is basically a motion moved by the Minister responsible for finance for the House to resolve into the *Committee of Supply* on Estimates of Revenue and Estimates to approve expenditure proposals. This is traditionally referred to as Budget Address.

After presentation, the Budget is referred to the Expanded Committee on Estimates, for consideration. This is an *ad hoc* committee which consists of the Committee on Estimates, all Chairpersons of portfolio and general purposes Committees and the Chairperson of the Reforms and Modernisation Committee. The inclusion of Chairpersons of these Committees of Parliament is based on the understanding that all sectors should be represented during the budget analysis. In considering the Budget, the Committee invites submissions from various interest groups and members of the general public. The deliberations of the Committee are open to the public and to the members of the press.

The Committee is required to prepare a report for debate in the main House. Similar to reports by Committees on Legislation, this report is not adopted by the House, but is used to assist shape the debate in the House.

The approval of the Budget is one of the core functions of Parliament and the *Constitution of the Republic of Zambia* mandates Parliament with the sole authority of approving expenditure from the general revenues. *Article 114 of the Constitution of the Republic of Zambia* empowers Parliament to consent on the imposition of any form of taxation. To achieve this purpose, taxation measures are considered in the *Committee on Ways and Means*. Bills to effect the proposed changes in the budget are presented before the House for enactment. These Bills are also referred to the Committee on Estimates. The Committee consults various stakeholders before presenting a report to the House. The Report on the Bills is also not adopted but used for debate on the tax Bills.

When the estimates of the expenditure have been approved by the National Assembly, the Heads of the estimates in the Yellow Book together with the amounts approved in respect of each vote are included in the Appropriation Bill. This Bill is introduced in the National Assembly for enactment.

iii. Execution or Implementation stage

Your Committee was informed that after the enactment of the Budget, the President signs a General Warrant authorising controlling officers in the budget units to start implementing the Budget.

In order to provide for activities that are unforeseen, your Committee was informed that the Constitution of Zambia provides for supplementary expenditure. *Article 117 (4) of the Constitution of the Republic of Zambia* provides that: '*where any supplementary expenditure has been **authorised** in respect of any financial year for any purpose and an amount has **not been appropriated** for that purpose under any head of expenditure by the appropriation Act for that financial year; or the amount of the supplementary expenditure is such that the total amount expended for the purposes of the head of expenditure in which expenditure for that purpose was included is in excess of the amount so appropriated under that head, the Minister responsible for finance shall introduce in the National Assembly not later than fifteen months after the end of that financial year or, if the National Assembly is not sitting at the expiration of that period, within one month of the first sitting of the National Assembly thereafter, a Bill, to be known as **Supplementary Appropriation Bill confirming the approval** of such expenditure, excess expenditure as the case may be'.* According to this provision, expenditure may take place without passing the appropriation law provided that Parliament has approved such expenditure.

Furthermore, your Committee was informed that the Constitution of the Republic of Zambia provides for expenditure without authorisation by Parliament. Article 117 (5) of the Constitution of Republic of Zambia provides that:

'*where in any financial year, expenditure has been incurred **without authorisation of Parliament**, the Minister responsible for finance shall, on approval of such expenditure by an appropriate Committee of the National Assembly, introduce in the National Assembly, not later than thirty (30) months after the end of that financial year or, if the national assembly is not sitting at the expiration of that period, within one month of the first sitting of the National Assembly thereafter, a Bill to be known as the **Excess Expenditure Appropriation Bill**, **for the approval** of Parliament of such expenditure'.*

Most of the stakeholders contended that this provision was not in line with the principles of transparency and accountability and as such was prone to abuse. While implementation of the Budget is the preserve of the Executive, Parliament through the Committee on Estimates has power to provide oversight on its implementation. The Standing Orders No.155 (IV) of 2005 empowers the Committee on Estimates conducts regular examination and scrutiny of the budgets, estimates and management thereof and conduct budget hearings.

iv. Accountability (Audit stage)

The Audit is the last stage of the budget process. Section 10 (2) of the Public Finance Act of 2004 empowers the Controller of Internal Audits to be responsible for the internal audit of every Ministry, department and statutory corporation. In addition, the Government accounts and financial statements were audited by an independent audit institution namely, the Auditor General. This process is normally followed by the presentation of the audit report to Parliament and its consideration by the Public Accounts Committee (PAC).

In order for the Auditor-General's Office to carry out its functions of ensuring accountability of public resources, *Article 121(2) of the Constitution of the Republic of Zambia* empowers the Office to audit accounts related to general revenues. The Report of the Auditor-General on the audit findings is presented to the President not later than twelve months after the end of each financial year. *Article 121 (4) of the Constitution of the Republic of Zambia* provides that the Auditor-General (AG) should within 12 months after the end of each financial year submit a report to the President, who in turn is obliged to cause the AG's report to be laid before the National Assembly not later than seven days after the first sitting of the National Assembly.

The Public Accounts Committee is charged with the responsibility of scrutinising the Auditor-General's Report. Thereafter, it is required to prepare a report on the findings contained in the report of the Auditor-General. The report is adopted on the floor of the House for onward transmission to the Executive for corrective action. However, the role of the Committee in this regard is limited to making recommendations only.

LEGAL AND INSTITUTIONAL FRAMEWORK GOVERNING THE BUDGET PROCESS AND ITS LIMITATIONS

5.3 Your Committee was informed that the legal framework guiding the Budget Process in Zambia is the Constitution of Zambia, which gives power to Parliament to approve any taxation and expenditures from the general revenues in the country. The Zambian Constitution authorises the Minister responsible for finance to prepare the budget and spend the funds in accordance with the budget as approved by Parliament.

The Constitution also authorises the Executive to raise the required funds, but only with the approval of Parliament. After the approval of the Estimates of Expenditure, the Heads of Estimates and the corresponding approved amounts are included in the Appropriation Bill for enactment. Once the Appropriation Act is passed by the National Assembly, the President signs a General Warrant which empowers Controlling Officers in the budget units to start spending their allocations on current and capital projects. The Permanent Secretary, MoFNP applies the General Warrant to apportion funds with respect to the requirements of the budget units and notifies them by issuing the Treasury Authority for recurrent expenditure and Capital Requisition for capital spending. Once Treasury Authority is received, the Controlling Officers in the budget units responds by issuing the Expenditure Warrant which indicates the allocation for recurrent and capital expenditure. The MoFNP is then ready to start releasing funds.

Your Committee was informed that while the Constitution provides for the presentation and approval of the budget, there was need to put in place a comprehensive subsidiary piece of legislation to provide for the consultative process in the budget process. Currently, while there is a general conformity to the stages as outlined in this Report, conformity in particular with regard to stakeholders' consultation sometimes tends to be compromised due to exceptional circumstances such as administrative delays at earlier stages in the process. Further, the capacity of the National Assembly, as the principal oversight institution, to analyse the "Green Paper" and present a formal response was weak partly because there was inadequate technical staff of budget analysts to assist Members of Parliament.

Regrettably, the practice of bringing detailed debate on the expenditure estimates to the full House and the consequent lack of use of the portfolio committees to scrutinise in parallel sessions the estimates of their relevant MPSAs, means that the time taken to scrutinise individual Heads of Expenditure is reduced and the level of expertise used to undertake this scrutiny is diluted. As a result, the National Assembly's ability to oversee the operational efficiency within MPSAs in achieving their institutional objectives as opposed to the allocative efficiency of the whole Budget was weakened.

Your Committee was, however, assured that the Ministry of Finance and National Planning was in the process of preparing the Planning and Budgeting Act and that this piece of legislation would address the current weaknesses in the process and enhance effective participation of various stakeholders in the country.

It was reported that the Ministry of Finance and National Planning has set up a Monitoring and Evaluation Department which performs a coordination function of monitoring the budget implementation process in liaison with sector ministries. The department is developing a framework which would be used by MPSAs in the implementation, monitoring and evaluation of programmes and projects in the budgets.

Apart from legislation that was aimed at formalising the measures contained in the budget speech, two other Bills are prepared and presented in Parliament by the Minister of Finance. These were the ***Supplementary Appropriation Bill*** and the ***Excess Expenditure Appropriation Bill.*** The ***Supplementary Appropriation Bill*** formalises the supplementary expenditure approved by Parliament in the previous year. In most cases, supplementary estimates accommodate items such as Grants or loans received from donors after the budget has been finalised by Parliament; and Variation of funds from one sub-head to another within the budget amounts already approved.

The Excess Expenditure Appropriation Bill formalises the unconstitutional expenditure report in the Auditor-General's report. This follows clearance by the Public Accounts Committee for unconstitutional expenditure to stand as a charge to the general revenues of the republic.

THE ROLE OF PARLIAMENT IN THE BUDGET PROCESS

5.4 The drafting stage was largely the preserve of the Executive involving line ministries and other spending agencies agreeing with the Ministry of Finance and National Planning on how available funds will be allocated in the next year’s budget. Nonetheless, Members of Parliament were free at this stage to participate during the consultative process at District and Provincial level as members of the District Development Coordinating Committee (DDCC) or the Provincial Development Coordinating Committee (PDCC). However, these meetings were normally not well planned and Members of Parliament ended up being excluded. Therefore, Parliament’s role in the budget process was clearly defined at the approval stage when it scrutinised the executive’s expenditure and revenue proposals.

After Parliament’s approval of the Budget and the passing of the Appropriation Act, the Executive begins to implement the Budget. The Ministry continuously reviews the budget during the year through an internal audit process. The feedback from the post-budget reviews becomes valuable input for the subsequent year's budget. After the fiscal year has elapsed, the Minister responsible for finance was required to cause to be prepared and lay before the National Assembly a Financial Report in respect of that year, not later than nine months after the end of the financial year.

Various stakeholders advocated that Parliament should closely monitor budget implementation through scrutiny of information on actual spending during the budget execution. They argued further that there was need to expand or enhance the scope of the Committee on Estimates to compel the Accountant General, just like PAC receives reports from Auditor-General’s Office, to present the quarterly budget execution reports to the Committee.

THE ROLE OF CIVIL SOCIETY ORGANISATIONS (CSOS) IN THE BUDGET PROCESS

5.5 Your Committee was informed that over the past few years, civil society has become important in influencing the course of political events in the country, including the budgetary process. There was no constitutional obligation on the part of the Government to allow civil society input into the budget process. However, for the purposes of inclusiveness and transparency, the Government had encouraged civil society to participate in the process.

There were many civil society organisations engaged in the budget process. Some of these organisations present submissions to Government during the drafting stage and have budget discussion meetings with the MoFNP while others attempt to monitor budget implementation throughout the year and share their findings with interested stakeholders, including the Government.

COMMUNITY INVOLVEMENT IN THE BUDGET PROCESS IN ZAMBIA

5.6 Regarding the involvement of the Community in the budget process, your Committee was informed that public availability of budget information was a fundamental requirement for fiscal transparency and accountability. The information ought to be comprehensive, reliable and useful. The community's involvement in the budgetary process was largely through the representation by civil society organisations. Further, the Ministry's invitations for submissions extend to individuals who are also free to make submissions on the budget. However, there remained greater scope for the involvement of the public in the budgetary process from constituency level.

PART II

THE EFFECTS OF THE CURRENT EURO-ZONE DEBT CRISIS ON EU's BUDGET SUPPORT TO ZAMBIA

6.0 Your Committee considered the effects of the current Euro-zone debt crisis on the EU's budget support to Zambia. The study was based on a quick research highlighting that a significant portion of the donor budget support was funded by the European Union. However, this situation was being threatened by the sovereign debt crisis that was currently being experienced in the European Union that had put considerable pressure on the budgets of most of the member states in the Union.

Stakeholders were concerned that the situation might lead to reduced budget support to Zambia which would have adverse effects on deficit financing and consequently constrain project implementation. This would further derail the attainment of the Millennium Development Goals (MDGs) by 2015. In undertaking the study, your Committee's objectives were as follows:

a. to establish the effect of the euro-zone sovereign debt crisis on the EU's budget support to Zambia;
b. to appreciate challenges facing the Government in resource mobilisation; and
c. to recommend the way forward in ensuring sustainable resource mobilisation.

In order to gather adequate information on this subject, your Committee sought written memoranda and oral submission from the Ministry of Finance and National Planning, the World Bank (WB), the European Union (EU) Delegation to Zambia, Caritas Zambia, Civil Society for Poverty Reduction (CSPR), Jesuit Centre for Theological Reflection (JCTR), the Economics Association of Zambia (EAZ) and the Zambia Institute of Chartered Accountants (ZICA). The summary of the findings of your Committee are set out below.

BACKGROUND TO THE EURO-ZONE DEBT CRISIS

6.1 Your Committee was informed that the European sovereign debt crisis emanated from a combination of factors: globalisation of finance, easy credit conditions during 2002-2008 which encouraged high risk lending and borrowing practices; international trade imbalances; real estate bubbles that have since burst; slow economic growth since 2008; high fiscal deficits; and the approaches used by countries to bail out troubled banking industries and private bondholders.

Your Committee was further informed that during the period 2002-2008 a number of EU member countries borrowed heavily and were able to hide their deficits and debt levels through the use of complex currency and credit derivatives structures designed by prominent US investment banks. However, with the onset of the financial crisis which led to global economic slowdown, this resulted in unsustainable government debt levels for certain European countries, including Greece, Portugal, Spain and Italy. Concern about the rising government debt levels combined with the downgrading of government debt for these countries created uncertainty in financial markets.

Therefore in May 2010, Europe's Finance Ministers approved a rescue package and proposed a series of austerity measures aimed at ensuring financial stability across Europe by creating the European Financial Stability Facility (EFSF). In October 2011, the Eurozone leaders meeting in Brussels agreed on a package of measures designed to prevent the collapse of member economies due to their spiralling debt.

EFFECTS OF THE EURO-ZONE DEBT CRISIS

6.2 Your Committee was informed that foreign component in budget support for Zambia has been declining over the last few years, putting pressure on Government to source financing from the domestic market. As the economy is growing the need for financing of infrastructure projects (roads, schools, hospitals and extending power generation) was rising. The Government had to look beyond the domestic market for financial resources and was now considering issuance of a bond to finance these projects.

It is a well known fact there were strong economic links between Zambia and the EU. Therefore, the possible effects of the Euro-zone debt crisis on the budget support to Zambia were identified as set out below.

i. Less Overseas Development Aid

Your Committee was informed that the EU and European Governments could be forced to reduce aid to Zambia as a result of the debt crisis. The EU has been a major source of direct budget support and project support, therefore, projects related to social service delivery and poverty reduction might also be derailed.

ii. Reduced Trade

Regarding the trade channel, it was highlighted that while strict austerity measures were being undertaken to resolve the European debt crisis, most developed countries including the United Kingdom, USA and France were also undertaking similar fiscal measures. As a consequence, global GDP growth rates could be constrained in the coming years and aggregate demand may fall, thereby, negatively affecting commodity prices and import demand levels. This may, in turn, negatively affect Zambia’s exports, leading to deterioration of the current account balance, exchange rate volatility with inflationary consequences and lower growth prospects. A fall in the demand for exports would also adversely affect tax revenues, especially through trade and resource related tax revenues, which could make it difficult for Zambia to maintain the planned levels of public expenditure including long-term infrastructure investment.

iii. Decline in Tourism

Given the strong linkages with European markets, the overall negative impact of the Euro-zone debt crisis on Zambian tourism would be substantial. The decline in tourism from Europe would result in decline in income and tax revenues which could make it difficult for Zambia to maintain the planned levels of public expenditure including long-term infrastructure investment.

iv. Reduction of Tax Revenue

The debt crisis in Euro-zone countries might indirectly reduce tax revenues of countries that exported to the Euro-zone. The slowdown in economic growth has implied lower demand for imports. Reduced exports by countries such as Zambia that export to Europe means reduced Government revenue through trade and other taxes. This could make it difficult for Zambia to maintain the planned levels of public expenditures including long term infrastructure investment.

v. Increased cost of borrowing

In order to insure investment against high risks of default that have arisen with the occurrence of debt crisis in Europe, investors would demand higher interest rates. Therefore, emerging economies such as Zambia that were about to issue their sovereign bonds were likely to borrow at higher interest rate due to heightened risk averseness and unwillingness to invest.

vi. Reduced inflow of Foreign Direct Investment (FDI)

The effects of European debt crisis could also be transmitted through foreign direct investment and short term portfolio investment. If European banks which were the major players in the project finance, in sectors such as mining face liquidity shortage and start reducing their exposure to emerging countries, Zambia would be affected. Zambia's economic growth in the recent past has been propelled by foreign investment and any disruption to the flow of investment would have adverse effects on the economy.

vii. Reduced Remittances

While statistics on remittances to Zambia were not readily available, it was a fact that a lot of Zambians were living in the Diaspora and remit substantial amounts of financial resources to their relatives. The Debt crisis has resulted in economic recession in the Euro-zone and massive lay-offs especially of unskilled labour. This would significantly reduce the flow of remittances.

viii. Depreciation of the currency

Reduced trade as a result of the crisis would adversely affect foreign currency flows to Zambia thereby putting pressure on the local currency. The debt crisis has also forced a lot of investors who were risk averse to demand more US dollar based assets in the international market thereby putting pressure on the local currency.

ix. Inflation

The depreciation in the local currency would translate into increased cost of doing business and ultimately increased inflation.

x. Trade deficit

Depreciation in the local currency implies that the cost of imports would increase thereby result in a trade deficit and thus cause balance of payment problems.

EFFECTIVENESS OF THE EU AID TO ZAMBIA

6.3 The Committee was informed that external assistance to Zambia was provided either in form of budget support or project support. This has been of great assistance to Government especially in areas of capacity building, technical assistance and social service delivery. The Government could not fund all the required expenditure on its own due to limited sources of domestic revenue, therefore, Official Development Assistance (ODA) has played a role in filling the financing gap effectively over the years.

Most projects have focused on up-lifting the standard of living or poverty reduction. Therefore, focus on raising health and education standards such as specialised training, provision of equipment, drugs, immunisation, maternal health care, materials, building, water and sanitation, empowerment of women, seed and agriculture and pollution throughout Zambia.

CHALLENGES OF DOMESTIC RESOURCE MOBILISATION IN ZAMBIA

6.4 Your Committee was informed that the use of domestic resources for development purposes was becoming more and more important as access to foreign resources was increasingly becoming difficult. Such resource mobilisation could come from both the public sector and the private sector. However, the following are the challenges of Domestic Resource Mobilisation:

i. limited savings were being generated to facilitate the required investment, and in addition, the types of savings available did not easily make financial intermediation possible, due to low and stagnant savings rates;

ii. low use of the Information Technology in collecting revenue;

iii. taxing the informal economy also continued to be a major challenge as in Zambia's informal economy, workers and companies operate outside the reach of the law or public administration, and this was a major obstacle to the broadening and deepening of the tax base; whilst the Zambia Revenue Authority did not have the capacity to capture all the economic activities going on in the informal sector; therefore, low contribution of tax revenue by the informal sector has contributed to the poor performance of taxation as a resource mobilisation mechanism;

iv. administrative capacity constraints were generally known to be major obstacles to improving tax policy in that they limit policy options, whilst ZRA is understaffed and has limited skilled staff thereby impeding tax collection;

v. transfer pricing in which the main beneficiaries are assumed to be tax havens and the multinationals;

vi. rampant corruption in revenue collecting institutions; and

vii. the Zambian government gives out a lot of tax incentives especially in the mining sector and thus tax revenue was foregone through these tax incentives and, requires better management.

PART III

FIELD-BASED OVERSIGHT ACTIVITIES

7.0 Your Committee was privileged to undertake field-based oversight activities to Katimamulilo, Kazungula and Victoria Falls border points from 1st to 5th April 2012. The tour provided an opportunity for your Committee to appreciate the strategies in place to increase domestic resource mobilisation in view of the anticipated decline in the EU budget support to Zambia arising from the EU debt crisis. The findings of your Committee are set out here under.

(1) The revenue drivers at *Katimamulilo Border* are alcohol, meat products and frozen fish (Tilapia). Others were second hand vehicles from the United Kingdom (UK) and the United States of America (USA).

(2) The main revenue drivers at *Victoria Falls Border* are grinding balls imported by Lumwana and Kansanshi Copper Mines, Coal by Konkola Copper Mines, Steel, Refrigerators and mixed juices. Others products are blankets, clothes, wax and washing powder.

(3) The main revenue drivers at *Kazungula Border* are machinery parts, pumps, transmission shafts, salt and freezers.

(4) The 2011 annual revenue target for *Katimamulilo Border* was K24.4bn while the actual collection was K31.2bn representing a collection surplus of about 28 percent.

(5) The 2011 annual revenue target for *Victoria Falls Border* was K69.6bn while the actual was K78bn representing 12 percent increase.

(6) The revenue target for *Kazungula Border* fell below by 15.5 percent from the target K355million to the actual of K300 million. The situation later improved following the introduction of a commercial pontoon by Botswana bringing the number of operational pontoons to three which increases traffic volumes that in turn translated into increased revenue outturn.

(7) *Kazungula Border* has been facing a problem of continuous breakdown of the pontoons thereby, negatively affecting revenue collection. The Commissioning of the refurbished third Zambia pontoon in February 2012 bringing the number of the operational pontoons to four and the enhancement of payment system through e-payment improved the situation.

(8) There were no banking facilities at *Kazungula and Katimamulilo Borders* contributing to delays as ZRA and tax payers had to travel to Livingstone town to access these facilities.

(9) The Borders at *Katimamulilo* and *Kazungula* were porous leading to rampant smuggling.

(10) There were limited resources to conduct both inspections and patrols at the border points and intermitted systems failure due to power surges negatively affected revenue collection.

(11) There was limited staffing levels particularly at Kazungula and Katimamulilo Borders.

PART IV

COMMITTEE'S OBSERVATIONS AND RECOMMENDATIONS

8.0 After carrying out an in-depth study on the budget process in Zambia and the impact of the Euro-zone debt crisis on budget support to Zambia and the subsequent field-based oversight activities to Katimamulilo, Kazungula and Victoria Falls Border points, your Committee makes the observations and recommendations set out hereunder.

(a) Enactment of the Budget and Planning Law

Your Committee observes that the Budget Act is an important piece of legislation needed to guide the budget process in Zambia. This piece of legislation will enhance the consultative process among the various stakeholders involved in the budget process. Wide consultations will enhance ownership, participation and accountability of budget implementation. Your Committee is aware that *Article 118A of the Constitution Amendment No. 20 of 2009* empowers Parliament to enact the budgeting and planning legislation and as such, Parliament does not need to wait for the enactment of the Draft

Constitution.

In this regard, your Committee reiterates the recommendation by your previous Committee that the Executive through the Ministry of Finance and National Planning should present this important piece of legislation to Parliament for enactment.

(b) Review of the Legal Framework Governing the Budget Process in Zambia

Your Committee observes that some legal provisions on the budget are not in keeping with the principles of transparency and accountability. In this regard, your Committee observes that while Article 117 (4) of the Constitution provides for Supplementary Expenditure, it does not explain the type of activities that qualify for such expenditure and as such is prone to abuse. Ideally, supplementary expenditure is supposed to meet unforeseen expenditure such as disasters, but this has not been the case in the past. Your Committee is saddened that some expenditures incurred in the past which were treated as supplementary were purely as a result of poor budgeting as they should have been planned for.

Furthermore, your Committee is uncomfortable with Article 117 (5) of the Constitution of the Republic of Zambia which provides for excess expenditure without approval and authourisation by Parliament. This undermines the principle of democratic accountability and Parliament's role of approving and enacting the Appropriation Bill. Your Committee is of the view that the supplementary and excess expenditure budgets are merely being used to finance activities over and above what Parliament approves, thereby derogating from the power of Parliament to deliberate on and approve all public expenditures.

In this regard, your Committee strongly recommends that this matter be carefully scrutinised during the Constitution review process so that the Supplementary Appropriation Bill and the Excess Expenditure Appropriation Bill should be enacted before expenditure is incurred.

(c) Inadequate Time for Consideration of the Budget

Your Committee observes that the time required by Parliament to study and approve the budget is limited. Limited time coupled with inadequate in-house expertise to provide technical and unbiased advice on the budget to Members of Parliament adversely affects the quality of the debates on the floor of the House. Your Committee, therefore, recommends that the amount of time needed to analyse the budget should be extended by allowing Parliament to scrutinise the draft budget. The analysis of the budget should be enhanced by establishing an independent budget office in Parliament. This will improve the quality of debate and reduce on the amount of time required to debate and approve the budget when it is formally presented to Parliament.

(d)Lack of Transparency

Your Committee observes that there is lack of transparency by the MoFNP when disbursing funds. In other jurisdictions, the community was informed of the disbursements by displaying relevant information on the notice board in respective local areas. In this regard, your Committee recommends that the Government should be open by publicly displaying the disbursements to various Spending Agents. Further, the Government should expedite to roll out the implementation of the Integrated Financial Management Information System (IFMIS) programme to other provinces and districts.

(e) Inadequate Human and Financial Capacity by the Zambia Revenue Authority (ZRA)

Your Committee observes that domestic resource mobilisations has been hampered in part by inadequate capacity by the ZRA as evidenced during the tour where most borders were not adequately funded and had limited staffing levels. Your Committee recommends that the staffing levels and funding to the Authority, particularly to collecting points such as borders should be increased.

(f) Deepening and Broadening of the Tax Base

Your Committee notes that the Euro-zone debt crisis may have adverse effects on the budget support to Zambia especially that the tax base is still narrow. Your Committee notes with concern that the informal sector which has the potential to contribute favourably to the broadening of the tax base continues to be excluded from the tax net. In this regard, Your Committee strongly urges the Government to seriously explore various ways of broadening and deepening the tax base including capturing the informal sector into the tax net.

(g) Fiscal Decentralisation and Local Tax Mobilisation

Your Committee observes that local authorities are a major source of revenue. They are better placed to collect certain taxes than central Government such as taxes from the informal sector. In this regard, the Zambian Government should speed up the process of fiscal decentralisation that will empower local authorities to collect certain taxes beyond the levies they are currently collecting to make them financially sustainable.

(h) Rationalisation of Tax Incentives

Tax policy measures which may include tax exemptions, deductions and tax credits, deferrals of tax payments or subsidies are provided to stimulate both domestic and foreign investments in the hope of mobilising needed financial resources. While such incentives may promote investment in the short and medium term, their long term economic effectiveness can be limited as they tend to dampen tax efforts. Sometimes even the anticipated job creation, backward and forward linkages and knowledge transfer for which tax incentives are given may never be realised.

For Zambia, the sectors in which foreign capital is mainly invested such as mines are highly mechanised and thus create fewer jobs. Little of forward and backward linkages and skills transfer may be created as foreign investors keep outsourcing both labour and capital from abroad thereby creating little impact on the local economy. Tax exemptions and incentives may also just undermine equity and fairness in the way tax burden is distributed.

In view of the above, your Committee strongly urges the Government to review its tax incentives including those earmarked for Multi Facility Economic Zones (MFEZ) investment.

(i) Improved Fiscal Management

Your Committee observes that the Government collects taxes on the basis that it will provide specific socio-economic benefits to the people. Therefore, mismanagement of public resources which might be caused by corruption, lack of willingness to fight corruption, social economic decline and overall deterioration in public service undermines public confidence in a government and thus endangers tax compliance.

In this regard, the Government should show great commitment to reducing waste in public expenditure management as a matter of priority. This will not only free up resources that can be devoted to productive public expenditures but also enhance tax compliance.

(j) Shield the Economy from External Shocks

Your Committee observes that the Zambian economy is prone to external shocks because it depends heavily on copper which is affected by the fluctuations in the international prices.

In this regard, your Committee recommends that the Government should be proactive by putting measures to counter the adverse effects of external shocks such as diversification of the economy.

PART V

CONCLUSION

9.0 Your Committee wishes to pay tribute to all stakeholders who appeared before it and tendered both oral and written submissions. It also wishes to thank you, Mr Speaker, for affording it the opportunity to serve on the Committee for the year 2012. Your Committee also appreciates the services rendered by the office of the Clerk of the National Assembly. Your Committee is very hopeful that the observations and recommendations contained in this Report will go a long way in improving the budget process in Zambia.

June 2012	Mr H H Hamududu, MP
LUSAKA	**CHAIRPERSON**