REPORT OF THE COMMITTEE ON ESTIMATES APPOINTED TO SCRUTINISE THE INCOME TAX (AMENDMENT) BILL, NAB 1/2009, THE CUSTOMS AND EXCISE (AMENDMENT) BILL, NAB 2/2009, THE VALUE ADDED TAX (AMENDMENT) BILL, NAB 3/2009, THE PROPERTY TRANSFER TAX (AMENDMENT) BILL, NAB 4/2009 AND THE ZAMBIA DEVELOPMENT AGENCY (AMENDMENT) BILL, NAB 5/2009

The Honourable Mr Speaker
National Assembly
Parliament Buildings
P O Box 31299
LUSAKA

Sir,

Your Committee on Estimates have the honour to present their Report on their consideration of the Income Tax (Amendment) Bill, NAB 1/2009, the Customs and Excise (Amendment) Bill, NAB 2/2009, the Value Added Tax (Amendment) Bill, NAB 3/2009, the Property Transfer Tax (Amendment) Bill, NAB 4/2009 and the Zambia Development Agency (Amendment) Bill, NAB 5/2009 referred to them on Thursday, 26th February, 2009.

Terms of Reference

2. The terms of reference of your Committee on Estimates are as follows:

(a) to examine the Estimates and Excess Expenditure Appropriation Bill;
(b) to report on the economies, 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 and report to the House for the formulation and implementation of future Budget Estimates.

Membership

3. Your Committee, as constituted, comprised the following members:

Mr B Imenda, MP (Chairperson);
Mr J P L Mulenga, MP;
Mr E M Hachipuka, MP;
Mr H H Hamududu, MP;
Ms J Kapata, MP;
Mr S Chisanga, MP;
Mr E M Sing'ombe, MP; and
Mr A M Nyirenda, MP.

Meetings of and Procedure Adopted by the Committee

4. To give effect to the measures for revenue required in the 2009 fiscal year, a range of budget legislation was presented to the House and this was considered in detail by your Committee. Your Committee, in considering the proposed legislation, held six meetings and interacted with various stakeholders and examined in detail all the submissions presented before

them. The list of witnesses who gave oral and written evidence to your Committee is at Appendix I of this Report.

CONSIDERATION OF THE BILLS

5. Your Committee considered the legal ramifications of the Bills referred to them. A summary of the submissions made by officials from the Ministry of Justice is outlined in this paragraph.

(i) THE INCOME TAX (AMENDMENT) BILL, NAB 1/ 2009

This Bill sought to achieve several objectives, some of which were to:

(a) increase the tax free income threshold for individuals from seven million, two hundred thousand kwacha per annum to eight million four hundred thousand kwacha per annum;
(b) increase the exempt portion of terminal benefits from twenty million to twenty five million kwacha;
(c) increase tax credits for persons with disabilities;
(d) increase the advance income tax rate from three per centum to six per centum;
(e) increase the allowable pension contribution from one million, six hundred and twenty thousand kwacha to one million, eight hundred and sixty thousand kwacha;
(f) abolish windfall tax;
(g) provide for the increase in the capital allowance rate for persons carrying on mining operations; and
(h) increase the period for carry forward of losses for hydro and thermo power generation from five years to ten years.

Clause 1 - Short Title and Commencement

This clause provides the short title and commencement date for the Bill, which is 1st April, 2009.

Clause 2 - Introduction of new definitions and amendment of existing definitions

This clause seeks to amend section 2 of the Act in order to introduce new definitions such as “hydro and thermo power generation” “public benefit activity” and “public benefit organisation.”

Clause 3 – Increase of exempt portion of terminal benefits

This clause seeks to amend section 21 of the principal Act in order to increase the exempt portion of tax on terminal benefits from twenty million kwacha to twenty-five million kwacha. This measure is intended to cushion the effects of inflation and provide more relief to retiring workers.

Clause 4 - Increase of carry forward period for losses in hydro and thermo power generation

This clause seeks to amend section 30 by inserting a proviso which allowed for the carrying forward of a loss in hydro or thermo power generation for up to a period of ten years. The measure also is intended to treat any losses arising from Hedging income as mining losses.

Clause 5 - Increase of allowable pension contributions

This clause seeks to amend section 37 and increased the amount of allowable pension contributions from one million six hundred and twenty, thousand kwacha to one million eight hundred and sixty thousand kwacha. This translates into an increase from one hundred and thirty five thousand kwacha to one hundred and fifty five thousand kwacha per month. This measure is intended to cushion the effects of inflation and provide more relief to retired workers.

Clause 6 - Introduction of Public benefit organisations

This clause seeks to repeal and replace section 41 and make provision for dealing with tax relating to public benefit organisations, which were wider in scope, as opposed to the repealed section which referred to charities. These organisations include a company limited by guarantee, a trust, an association, educational institution, health institutions, amateur sporting association or any organisation or association registered under the laws of Zambia. The measure is intended to make donations to public institutions allowable as a deduction for income tax purposes in order to encourage donations to public institutions and to further streamline the provisions of the section regarding organisations that enjoyed tax relief.

Clause 7 - Abolition of windfall tax
This clause seeks to amend section 46 so as to abolish the requirement to pay windfall tax in mining.

Clause 8 - Documents in support of returns
This clause seeks to amend section 56 in order to provide for the use of audited accounts among the requisite supporting documents from a company. The measure is meant to bring the requirement in line with the *Companies Act*, thereby improving compliance.

Clause 9 - Repeal of Section 64B
This clause seeks to repeal section 64B which related to windfall tax assessment.

Clause 10 - Abolition of windfall tax returns
This clause seeks to amend section 77 by removing provisions relating to the filing of returns for windfall tax.

Clause 11 - Abolition of penalty for non payment of windfall tax
This clause seeks to amend section 78 so as to abolish the penalty for non payment of windfall tax.

Clause 12 - Sale by sealed tender
This clause seeks to amend section 79A so as to include the disposal of goods and chattels by means of sealed tender bids in the event of failure to pay tax by a person or partnership. The measure is meant to harmonise the procedure of disposal of such goods between this Act and the *Value Added Tax Act*, where such goods could be disposed of through sealed tenders and bids.

Clause 13 - Amendment of references to Mines and Minerals Act
This clause seeks to amend the Act generally in order to delete all references to the *Mines and Minerals Act,* which have since been repealed, and replace them with references to the current Act, the *Mines and Minerals Development Act.*

Clause 14 - Amendment of references to Small Enterprises Development Act
This clause seeks to amend the Act generally in order to delete all references to the *Small Enterprises Development Act* and replace them with references to the *Zambia Development Agency Act.*

Clause 15 - Amendment of Second Schedule
This clause seeks to amend the Second Schedule to the Act by deleting the reference to the *Investment Act* and the replacement with a reference to the *Zambia Development Agency Act* and to regularise and harmonise the taxation of income tax of some statutory bodies with the provisions of other relevant Acts.

Clause 16 - Amendment of Fifth Schedule
This clause seeks to amend the Fifth Schedule to the Act in order to provide for the increase in the capital allowance rate for persons carrying on mining operations.

Clause 17 - Repeal and replacement of Tenth Schedule
This clause seeks to repeal and replace the Tenth Schedule so as to define public benefit activities, which are wider in scope than those previously provided for under the repealed Schedule which dealt with charities and was more limited in application.

Clause 18 – Amendment of Charging Schedule
This clause seeks to amend the charging schedule so as to increase the tax free income threshold for individuals from seven million, two hundred thousand kwacha per annum to eight million four hundred thousand kwacha per annum; to provide for the zero rating on tax deductible from management, consultancy or other fees payable by a person developing a Multi-facility Economic Zone or an Industrial Park as an incentive in order to encourage the development of priority sectors and products. The amendment also seeks to increase the amount of advance income tax payable from a rate of three per centum to six per centum in order to improve the revenue collection on the part of the Government. The amendment is also meant to increase the tax credit applicable to persons with disabilities from six hundred thousand kwacha to nine hundred thousand kwacha per annum. This is meant to be additional relief to what had been proposed under PAYE.

In terms of specific adjustments to individual income tax, the purpose of the amendment is to increase the threshold of exempt income from seven million two hundred thousand kwacha per annum (six hundred thousand kwacha per month) to eight million four hundred thousand kwacha per annum (seven hundred thousand kwacha per month) and to set the rate of tax on an individual's income between eight million four hundred thousand kwacha per annum (seven hundred thousand kwacha per month) and sixteen million and twenty thousand kwacha per annum one million three hundred thirty-five per month), at 25 percent per, income between sixteen million and twenty thousand and one per annum (one million three hundred thirty-five and one kwacha per month) and forty-nine million two hundred thousand and one kwacha per annum (four million one hundred thousand and one kwacha per month), at 30 percent and income above forty-nine million two hundred thousand and one kwacha (four million one hundred thousand and one kwacha per month) at 35 percent. The adjustments were meant to increase the disposable take home pay for workers and make the PAYE system more progressive.

(ii) THE CUSTOMS AND EXCISE (AMENDMENT) BILL, NAB 2/2009

This Bill seeks to achieve several objectives, namely: to reduce excise duty on heavy fuel oils; reduce duty on major capital goods; revise the rates of customs, export and excise duty payable on certain goods; and provide for matters connected with or incidental to the foregoing.

Clause 1: Commencement date of the Bill
This clause provides for the short title and commencement date which is 31st January,2009.

Clause 2: Amendment of Section 34
Section 34 provides for post-assessment payment of import duties to be made within five days from the date of issue of an assessment notice.

Clause 2 seeks to introduce some flexibility so as to allow importers to register electronically and make payment of import duties prior to the arrival of the goods or make payment of import duties within five days from either the date of such registration or the date of issuance of an assessment notice.

The proposed amendment to Section 34 is in response to the growing need for effective and efficient facilitation of legitimate trade across Zambia's borders and also mitigating the challenges associated with congestions at the borders.

Clause 3: Amendment of Section 88
Currently, the *Customs and Excise Act* does not provide for a head of power in the valuation of services rendered in Zambia for purposes of excise duty determination. 'Head of power' in this context meant the authority to effect the particular tax measures. Clause 3 seeks to provide a head

of power in order to avoid nullification, through litigation, of valuation for excise duty determination.

Clauses 4, 5 And 6: Amendment of Section 139
These amendments are intended to delete the words "talk time" and substitute them with the words "air time" in order to broaden the definition of air time to include all services derived from the usage of mobile cellular telephone for purposes of excise duty imposition. This amendment would include all services such as voice mail, short message service (sms) multimedia service, internet and other services as may be consumed through a mobile cellular telephone. This amendment would also remove any doubt in the interpretation of "talk time".

Clause 7: Amendment of Section 171
Clause 7 seeks to introduce a provision for the writing off of bad debt. The amendment would empower the Minister responsible for Finance to write off such bad debt and ensure that treasury accounts reflected the correct position. The amendment would also provide for conditions under which such debt would be deemed as bad debt, such as bankruptcy, winding up or other factors beyond the control of the Authority.

Clause 8: Amendment to the First Schedule
Clause 8 seeks to remove duty on gray fabric, including loomstead, specially imported for further processing in the textile industry of headings to reduce the cost of production in the textile and clothing sectors. This would also enhance competitiveness of the sector.

Clause 9: Amendment to the Second Schedule
The intention of this clause is to reduce excise duty on clear beer from seventy-five percent to sixty percent. Excise duty on clear beer at 75 percent made the locally produced beer more expensive than the average in the region. As a result, consumers of alcohol have resorted to illicit brews while importers of clear beer had resorted to smuggling. This situation has in turn curtailed efforts to encourage profitable investments in the sector and gains from benefits that may accrue in the chain of distribution such as employment creation and higher taxes from VAT, PAYE and corporate income tax.

The aim of this measure is to stimulate demand for the locally manufactured beer; it is expected that the sector would increase investment, create more jobs and in the medium to long terms, create and develop a market for barley farmers through out-grower schemes.

Clause 10: Amendment to the Fourth Schedule
Clause 10 seeks to exclude vehicles propelled by non-pollutant energy sources, such as hydro carbon fuels, from payment of carbon tax. Currently, the law provides for charging and collecting of carbon tax on all vehicles, excluding ambulances and prison vans. As a result, vehicles that are propelled by energy sources that do not emit any carbon monoxide are also charged carbon tax. The objective of this measure, therefore, is to exclude vehicles propelled by non-pollutant energy sources from payment of carbon tax.

Clause 11: Amendment to the Sixth Schedule
This amendment seeks to remove the current administrative arrangement applicable to selected manufacturers of spirits and regularise it to make it applicable across the industry. In so doing, for local manufacturers of spirits, excise duty to be paid on the finished product (spirit), would not be based on the selling price, but instead be based on the taxable value of the input alcohol. This measure would ensure that the tax base for local manufactures is not any higher than would apply for importers of the manufactured product.

Clause 12: Repeal and Replacement of the Seventh Schedule
Clause 12 seeks to introduce a new section that would provide for the valuation of services for the purpose of excise duty determination. Currently, the *Customs and Excise Act* did not provide for a

head of power in the valuation of services for purposes of excise duty determination. The aim of this measure is, therefore, to provide a head of power in order to avoid nullification, through litigation, of valuation for excise duty determination.

Clause 13: Amendment of the Ninth Schedule
This clause is aimed at discouraging export of cotton seed to increase local value addition in view of the increased capacity to process it locally.

(iii) THE VALUE ADDED TAX (AMENDMENT) BILL, NAB 3/2009

The Bill seeks to achieve several objectives, namely:

(a) to provide the requirement for registered suppliers to maintain business records in English and extend the prescribed period in which to preserve such records to six years;
(b) to provide for the determination of minimum taxable values for specified goods;
(c) to introduce the requirement for suppliers or manufacturers of specified goods on the minimum taxable value scheme to submit a schedule of recommended retail selling prices by product category; and
(d) to introduce a Third Schedule in respect of specified goods on the minimum taxable scheme.

Clause 1: Short Title and Commencement
This clause specifies the short title and commencement date which was deemed to be 31st January, 2009.

Clause 2: Definition of Industrial Park and Multi-Facility Economic Zone
The measure seeks to include definitions for the terms "industrial park" and the "multi-facility economic zone". An industrial park means any area or premises in Zambia, which is at least fifteen acres in extent that has been declared an industrial park under section eighteen of the *Zambia Development Agency Act* and multi-facility economic zone means any area or premises in Zambia that have been declared a multi-facility economic zone under section 18 of the *Zambia Development Agency Act.*

Clause 3: Taxable Value of Supplies and Importations

The insertion of the new sections was being proposed in order to provide for determination of minimum taxable values for specified goods and introduce the requirement for suppliers or manufacturers of specified goods on the Minimum Taxable Value Scheme to submit a schedule of recommended retail selling prices product category. This would empower the Commissioner-General of the Zambia Revenue Authority (ZRA) to prescribe the manner and form of the schedule of the recommended retail prices of the specified goods. This clause seeks to strengthen the law so as to compel manufacturers and suppliers of goods listed under the Minimum Taxable Value Schedule (Third Schedule), to submit to ZRA a schedule of recommended retail prices of these products as and when there were changes in prices, on registration or any other time as the Commissioner-General may determine. The amendment would contribute to maximising the VAT collections on selected goods like cement, beer, cigarettes, soft drinks and cell phone airtime which were usually supplied in the informal sector.

Clause 4: Maintenance of Records and Accounts

The deletion of subsection and substitution, therefor, of a new subsection was being done in order to provide for the requirement for registered supplies to maintain business records in English and extend the prescribed period in which to preserve such records from five years to six years. This would also empower the Commissioner-General to further extend the period and this has to be done by a notice in writing.

This amendment would facilitate easier audits because there would be no need to have books taken for interpretation at the Ministry of Foreign Affairs. Currently, tax audits took unnecessarily long and were costly when books were not maintained in English as there was a charge for interpretation and, above all, they may be ineffective as the interpretation may lack precision and accuracy. The extension of the period to six years would also help harmonise the duration provided for in *Value Added Tax Act* and the duration provided for in the Income Tax Act.

Clause 5: Amendment to the Third Schedule
This clause seeks to amend the Third Schedule in order to list goods which qualified for the Minimum Taxable Value Scheme.

(iv) THE PROPERTY TRANSFER TAX (AMENDMENT) BILL, NAB 4/2009

The Property Transfer Tax (Amendment) Bill seeks to ensure that valuation of shares was at arms' length. This would entail that where a transaction was between two people who were related or otherwise connected in such a way that they may undervalue shares for the purposes of assessment of realisable value, ZRA would have the power to examine the transaction and make an independent assessment in order to avoid the undervaluation.

Clause 1 : Short Title and Commencement
This clause provides for the short title of the Bill and commencement date which was 1st April, 2009.

Clause 2: Realised Value of Shares
This clause provided for the valuation of shares at arms' length. This would entail that where a transaction was between two people who were related or otherwise connected in such a way that they may undervalue shares for the purposes of assessment of realisable value, ZRA would have the power to examine the transaction and make an assessment in order to avoid the undervaluation and consequent avoiding of payment of tax.

(v) THE ZAMBIA DEVELOPMENT AGENCY (AMENDMENT) BILL, N.A.B 5/ 2009

This Bill seeks to declare industrial parks, which were smaller in scale than multi- facility economic zones and were meant to accommodate small scale enterprises and encourage the development of small to medium sized businesses by providing incentives to such businesses.

Clause 1 - Short Title and Commencement
This clause provides the short title and commencement date for the Bill, which was deemed to be 31st January, 2009.

Clause 2 - Introduction of definition of industrial park
This Clause seeks to amend section 3 of the Act in order to introduce the definition of an "industrial park" which is an area or premises declared as such where small and medium enterprises could operate.

Clause 3 - Functions of Zambia Development Agency in Relation to Industrial Parks
This clause seeks to amend section 5 so as to provide for the application of the section to industrial parks. The section outlines the functions of the Zambia Development Agency in relation to Multi- Facility Economic Zones and, with this amendment, Industrial Parks.

Clause 4 - Declaration of Industrial Parks
This clause seeks to amend section 18 to include the declaration of industrial parks based on the listed criteria and conditions, including the limits of the area, premises or building declared as a Multi-facility Economic Zone; facilities to be provided and maintained within a Multi-facility

Economic Zone; terms and conditions under which such goods produced and services provided in a Multi-facility Economic Zone may be sold, exported or otherwise disposed of; and activities which are prohibited within a Multi-Facility Economic Zone.

Clause 5 - Incentives for Industrial Parks
This clause seeks to amend section 57 of the Act to provide for incentives to be extended to developers of industrial parks so that they enjoy exemption from duty as specified by or under the *Customs and Excise Act*.

Clause 6 - Exemption of Duty
This clause seeks to amend section 60 of the Act so as to empower the Minister of Finance and National Planning to determine which investors were eligible for tax exemption. Previously, this was done by the Commissioner- General.

Clause 7 – Power to Make Regulations
This clause seeks to amend section 82 in order to allow the Minister to make regulations for matters connected with industrial parks.

THE 2009 BUDGET: IMPLICATIONS OF PROPOSED TAX CHANGES

6. Your Committee's general observations as regards the economic and financial implications of the proposed tax changes in the 2009 budget. As set out hereunder.

Resource Outlook for 2009

Based on the pronouncements contained in the 2009 budget speech, the resource outlook for 2009 is as shown in the Table below.

Resource Outlook for 2009

Revenue Estimates for 2009 (in billions of Kwacha)		
Tax revenue		10191.6
Direct taxes	4530.0	
o/w Company tax	1104.0	
PAYE		2692.5
Other income taxes	579.0	
Value added tax		2549.9
Customs and excise duties	3111.6	
o/w Customs duty		1452.5
Excise duty	1659.1	
Non-tax revenue	454.3	
o/w User fees and charges		353.3
Exceptional revenue		34.8
Dividends, interest, etc	66.2	
Total domestic revenues	10645.8	

Sources: Budget Speech and Medium-Term Expenditure Framework, 2009-2011.

Arising from the above Table, your Committee noted the following:

- it is very clear that the financing of the Government budget is still principally dependent on taxation. This is evident in the fact that domestic revenues are equivalent to about nineteen percent of GDP while tax revenue is eighteen percent. These percentages show that there has been no shift in the relative contributions of domestic revenues and tax revenue to national income;

- according to the medium-term expenditure framework for the period 2008-2010 on the revenue side, Government policy would be to increasingly reduce taxes on trade and move towards taxes on consumption. In the 2007 budget, trade taxes accounted for thirty-two percent of total domestic revenues while in the 2009 budget, the Government estimated that the proportion of trade taxes in total domestic revenue would decline marginally to twenty-nine percent. While still quite small, this reduction was a commendable effort because it pointed to the start of the restructuring of the taxation system;

- the 2009 budget legislation proposals did not point towards a shift in Government policy with regard to the distribution of the tax burden. As before, individual and household incomes would bear the burden of taxation by paying almost twenty-seven percent of total tax revenue while corporate tax payers, including the mining companies, would only pay ten point eight percent. Meanwhile, the Government appeared to have succumbed to pressure to remove windfall tax from the statute books. It was also not clear what would happen to some mining companies that had defaulted on their windfall tax payments; and

- in addition, as further evidence of the fact that the distribution of the tax burden was heavily weighed against the individual taxpayer, about sixty percent of the total direct taxes in 2009 were expected to be contributed by PAYE. Clearly, this was worrying as workers were expected to continue to carry the burden even at an economically lean time such as now when they needed considerable relief. There was also a real danger that the tax relief offered by the proposed change to PAYE would be cancelled out by the sixteen point one percent rate of inflation. In fact, your Committee noted that for an individual earning one million five hundred thousand kwacha per month, the proposed change in the tax exempt threshold translated into tax relief of thirty thousand kwacha as illustrated in the computation below. If the figure was corrected for inflation, the relief may actually be much lower than this in real terms.

CURRENT SYSTEM (SCENARIO A)	
Income Bands	**Tax Rates**
0-K600,000 per month	0%
K600001-K1235000	25%
K1235001-K4,000,000	30%
Above K4000,000	35%

PROPOSED SYSTEM (SCENARIO B)	
Income Bands	**Tax Rates**
0-K700,000 per month	0%
K700,001-K1,335,000	25%
K1335,001-K4,100,000	30%
Above K4,100,000	35%

A

	Income	**Rate%**	**Tax(K)**
	1,500,000.00		
1st Band	**600,000.00**	**0%**	**0**
	900,000.00		
	1,235,000.00		
	600,000.00		
2nd Band	**635,000.00**	**25%**	**158,750**
	900,000.00		
	635,000.00		
3rd Band	**265,000.00**	**30%**	**79,500**
	Total Tax Burden		**238,250**

B

Income	**Rates %**	**Tax (K)**
1,500,000.00		
700,000.00	**0%**	**0**
800,000.00		
1,335,000.00		
700,000.00		
635,000.00	**25%**	**158,750**
800,000.00		
635,000.00		
165,000.00	**30%**	**49,500**
Total Tax Burden		**208,250**

The difference between the two scenarios, which is only thirty thousand kwacha, presents the relief that the worker who is getting one million five hundred thousand kwacha would get. This amount is insignificant and will not provide the intended relief.

- The current fiscal incentive structure in Zambia was a source of considerable worry for your Committee. They were of the view that a neutral structure of incentives was an important first step toward a fairer society. Instead, the 2009 budget provided substantial incentives to foreign investors, while struggling local investors were expected to benefit from possible trickle-down effects.
- Your Committee observed that while large increases in the country's public revenues were potentially available from full cost pricing of various public services, user fees remained below cost recovery and the Government had continued to rely heavily on tax revenues, particularly personal tax through PAYE, placing an inordinately heavy burden on the individual taxpayer. In this regard, your Committee noted that non-tax revenue was forecast at four hundred fifty-three point three billion kwacha against actual collections of five hundred sixty-seven point three billion kwacha in 2008. This was

indicative of problems in administering user fees and charges which included, but were not limited to, revenue leakages through corruption.

ISSUES AND CONCERNS RAISED BY STAKEHOLDERS

7. The stakeholders who appeared before your Committee noted, that essentially, apart from the tax system being asked to achieve the revenue mobilisation objective, it was also expected to facilitate compliance and collection through efficient administration. The system must also be seen to spread its burden equitably. Further, to avoid resource misallocation, the tax system should not distort the patterns of production, trade, consumption, saving, and investment. The tax system was also being used to offer incentives to investors. In sum, it was expected to achieve multiple objectives. Various stakeholders who appeared before your Committee expressed concerns about the 2009 budget legislation, a synopsis of which is provided below.

(a) The Income Tax (Amendment) Bill

- *Tax Relief for Personal Income Tax (PAYE)*

Some tax relief was being offered to individual income taxpayers by adjusting the PAYE income tax bands so that the tax free portion was raised by seventeen percent. It was claimed that this was seven percent above the targeted rate of inflation of ten percent in 2009. Stakeholders considered this to be grossly inadequate given the current rate of inflation which cancelled out this relief. Also, it was unrealistically optimistic to hope that the inflation target of ten percent would be achieved in 2009 in view of continued deterioration in the economy.

- *Other Types of Tax Relief*

Under the Income Tax (Amendment) Bill, there was also tax relief proposed for various other types of incomes. Stakeholders welcomed this but expressed the following concerns:

- extension of tax exempt income under PAYE to gratuities with the balance to be taxed at the flat rate of twenty-five percent. While the intention to recognise final payments at end of contract employment and the fact that the recipient may remain unemployed for a prolonged period or permanently was commendable, this was a one-off tax relief and would in reality be marginal;
- the increase of the tax exempt portion of terminal benefits by twenty-five percent from twenty million kwacha to twenty-five million kwacha was a welcome decision. However, for a retiring worker who virtually had to start a new life, this would hardly provide a cushion against inflation at the current rate.
- the increase in the tax credit for the disabled was welcome although the amount was inadequate given the rate of inflation and the size of income to meet basic needs; and
- in the present situation of an energy deficit, raising the period for carry over of losses constituted an incentive for investment in new hydro and thermal power generation facilities. The exclusion of wood sources of power for conservation purposes was welcome.

- *Concessions for the Mining Sector*

Stakeholders expressed the belief that the investment environment, especially the fiscal regime that was created for the mining sector, was too generous to foreign investors and did not adequately protect the country’s interests. Relations with foreign mining companies had generally not been smooth and foreign mining companies had not always dealt fairly with the country in sharing the revenues of profitable mining operations during the recently ended mineral price boom. Thus, it was worrying that the Government proposed to extend further concessions to the mining sector in the 2009 budget. One of the incentives provided reversal of the provision which separated hedging operations from mining operations. The previous provision prevented mining companies from offsetting hedging losses against mining income. In effect, this amounted to restoration of the position in the Development Agreements. Further, hedging programmes included certain financial transactions so as to insulate the company's financial returns from fluctuations in, say, the spot price of copper or currencies. Hedging techniques generally involved the use of complicated financial instruments known as derivatives, the two most common of which are options and futures. It was pointed out that there could be both gains and losses from hedging. Of major concern in this regard was the capacity of the Zambia Revenue Authority (ZRA) to effectively monitor these transactions in order for the country to benefit fully from mining operations.

- *100 percent Capital Allowances for Mining Companies*

This incentive for mining companies would allow the costs of capital assets to be written off against their taxable profits within one year and not in four years as at present. Effectively, capital allowances take the place of depreciation in the commercial accounts. This will enable mining companies a greater proportion of the capital expenditure on their assets to be set against the business profits of the period during which investments could be made. This was a very generous incentive which would alleviate the cash flow problems that the companies had been complaining about. By the same token, it was hoped that the mining companies would not hold the Government to ransom as had been witnessed during the impending closures of some of the mines or placement of others on a care and maintenance basis with consequent losses of jobs for Zambian people. In any case, it was hoped that this would be a temporary measure as no other industry enjoyed this kind of concession. It was noted that, under normal circumstances, capital allowances schemes were ordinarily introduced to encourage new investment or for expansion projects.

- *Abolition of Windfall Tax for the Mining Sector*

Stakeholders noted that windfall tax was levied on the mining companies when economic conditions allowed them to make excess profits. The windfall tax was primarily imposed on the mining industry which had benefited the most from the economic windfall from the unprecedented high copper prices that prevailed until 2008. As with all tax initiatives instituted by the Government, the mining companies were vehemently opposed to windfall tax. It was now proposed that this tax be abolished because the mining companies claimed that it had made the fiscal regime punitive, particularly for high cost mines. The mining industry contended that the existing variable profit tax was sufficient tax the excessive profits for which windfall tax was designed.

- *Increase of Company Income Tax on Cotton Export Earnings*

This measure was intended to increase company income tax from fifteen percent to thirty-five percent on earnings from the export of cotton lint without an export permit from the relevant ministry. It was expected to discourage the export of raw cotton in order to stimulate local value added processing for which there was ample local capacity. While this was a plausible objective, care should be taken not to drive out local farmers from cotton production to other crops. This was especially relevant given the exchange rate which made such exports extremely profitable and competitive in the export markets.

(b) The Customs and Excise (Amendment) Bill

Stakeholders expressed serious concern that this Bill proposed to amend the *Customs and Excise Act* almost exclusively for the purpose of offering incentives essentially to foreign investors through a wide range of concessions on various imported items. They observed that that international trade taxes could be collected from imports without driving a wedge between the price of imports and competing domestic products, provided the tax on imports has a counterpart in domestic production. However, taxes on imports could be used not only to raise revenue but also to protect domestic production. Therefore, because of these multiple objectives, Zambia's import tax regime was complex and could not be transparent. Specifically, the following observations were made:

- *Removal of Customs Duties on vegetable oils*

This measure was ostensibly intended to harmonise duties with the main competitors so as to level the playing field so that local firms could increase their share of the regional market and that this would lead to job creation. This assertion was difficult to understand as the measure would result in a greater influx of imported vegetable oils. In any case, Zambia did not produce palm oil and there were substantial imports of soybean and sunflower oils. The removal of import duties would simply make it easier to import these items for repacking and possibly some further reprocessing which could not lead to a significant increase in employment. This concession would clearly only benefit importers.

- *Reduction of Excise Duty on Clear Beer*

Excise duty on clear beer had been reduced from 75 percent to 60 percent. Stakeholders' understanding was that this would make locally produced beer cheaper in the region. This would increase the demand for local brews, discourage smuggling of imported beer and improve tax compliance. However, it was not clear that in the short to medium term, this measure alone would result in an increase in investment in this industry or that there would be a surge in the production of barley in the country.

- *Removal of Customs Duty on Gypsum*

Stakeholders recalled that gypsum had always been produced at Lochinvar near Monze in the Southern Province. It was, therefore, surprising that the Government had found it necessary to propose the removal of customs duty on gypsum, unless this industry had since been abandoned by the then Chilanga Cement and its successors. If gypsum was still being produced in the Southern Province, then this concession was misplaced and should be reversed. It could only be the product of lobbying by powerful entities that would profit from importing gypsum.

- *Reduction of Excise Duty on Heavy Fuel Oil*

This concession appeared to be another one in response to the demands of the mining industry. Perhaps, the overriding consideration was that sales of heavy fuel oil to the mining industry and manufacturers of tar-macadam was vital. This should reduce the cost of road surfacing and generally assist the mines to cut costs and, maybe, slow down job losses. The concession was, therefore, welcome.

- *Removal of Customs Duty on Paper Packaging Materials*

Stakeholders believed that the impact of the removal of the 5 percent duty on the local manufacturing cost of this item would be minimal because the bulk of the cost included a significant amount of imported inflation since all the paper board used in the production process was imported. It was also worrying that instead of encouraging local production, the Government appeared to be encouraging import dependency by introducing this measure.

- *Removal of Duty on Imported Gray Fabric used in the Textile Industry*

Stakeholders were concerned that this measure was intended for a textile industry which depended entirely on imports and this was expected to make the sector more competitive. It would, however, be difficult to compete effectively with established regional textile exporters. It would have been more realistic to assist the sector to produce gray fabric from locally grown cotton as this would also encourage local farmers to increase their output.

- *Reduction of Customs Duty on Various Items*

With regard to other concessions in terms of reduction of duty on refrigeration equipment, forklift trucks, track laying bulldozers and angle dozers, graders and levelers, tamping machines, road rollers, pile drivers and survey equipment, stakeholders noted that some of these concessions, while ostensibly aimed at reducing the cost of doing business in Zambia, appeared to be generally biased towards foreign businesses, particularly foreign contractors in road construction and other large construction projects, especially shaft sinking and mineral exploration.

- *Removal of Duty on Trucks (Mechanical Horses)*

This measure was a welcome concession as long as Zambian investors were not crowded out by foreign investors taking advantage of purchasing trucks more cheaply than elsewhere. Foreign investors could be mobile across border itinerants.

- *Removal of Duties on Special Purpose Motor Vehicles and Certain Aircraft*

Stakeholders considered these measures to be specific to certain requests by individuals and some business operators and to have no significant impact on Zambia's overall economic activities. The items involved were not traded in large numbers and were, therefore, not strategic to the country's development.

- *Exclusion of Non Pollutant Energy Using Vehicles from Payment of Carbon Tax*

This measure was a welcome incentive although the market for such vehicles was arguably small.

- *Removal of Customs Duty on Copper Powder, Copper Flakes and Copper Blisters*

The concession was clearly for the mining sector and could result in increased job losses in the mining industry as some of the mining companies would like to place their mines on a care and maintenance basis and concentrate on processing the materials imported from other countries.

- *Increase in Export Duty on Cottonseed and Customs Duty on Cellular Phone Handsets*

To compensate revenue losses arising from all the concessions on customs and excise duties on various imported items, the Government had proposed increases of export duty on cotton seed from 15 percent to 20 percent and the increase of customs duty on cellular phone handsets. However, it appeared that these measures were yet another example of lobbying by powerful interest groups and were aimed at protecting those specific groups because they were not strategically designed to promote development of the sectors involved.

(c) The Value Added Tax (Amendment) Bill

It was noted that this amendment Bill provides for concessions only, and some of these are discussed below.

- *Zero Rating of Windmills and Maize Dehullers*

Stakeholders welcomed this measure in the light of the fact that VAT was expensive to administer, especially for small scale farmers and it was hoped that this group would ultimately benefit from the measure.

- *Zero Rating of Two Wheel Tractors and Accessories, Tractors up to 60 Horsepower Ploughs, harrows, Disc Harrows, Planters, Seeders, Rippers/sub Soilers, Cultivators, Pump Sets and Agricultural Knap Sack Sprayers*

If, as stakeholders had been made to believe, this concession was intended to allow those farmers who were not registered for VAT purposes to claim input VAT on the listed equipment, it may result in reduced input costs and promote increased production. However, considering the matter realistically, this concession would only benefit the large farmers who could afford most of these items. Moreover, the main beneficiaries may essentially be the importers trading in these items.

- *Extension of the Deferment Scheme to Include Copper and Cobalt Concentrates*

Stakeholders believed that this was another concession to the mining sector and tied in with the customs and excise duties concession on copper powder, copper flakes and copper blisters.

(d) Property Transfer Tax (Amendment) Bill

Stakeholders noted that, currently, interest on related party loans for the purchase of shares was included in current liabilities, even where such transactions were not carried out at arm’s length. This constituted a loophole for undervaluation and potential loss of revenue to the Treasury. Accordingly, interest accruing on loans from related parties would henceforth be excluded from current liabilities for purposes of Property Transfer Tax as long as such transactions were not at arm’s length.

(e) The Zambia Development Agency (Amendment) Bill

Stakeholders noted that further tax incentives were being extended to developers of and investors in MFEZs and Industrial Parks under the *Zambia Development Act*. These tax concessions included:

- removal of withholding tax on management fees, consultancy fees and interest repayments for foreign contractors;
- zero rating of supplies to developers of MFEZs and Industrial Parks;
- exemption of foreign suppliers to MFEZs and industrial parks from reverse VAT charges; and
- exemption from payment of customs and excise duties on materials, equipment, machinery and accessories imported for the development of MFEZs and Industrial Parks.

The purpose of these tax concessions was stated to be the expansion of Zambia’s industrial base and to increase the competitive edge of Zambian companies in the Southern African region. However, stakeholders felt that this remained to be seen. Importantly, though, it was clear that the Government had decided to develop manufacturing on the basis of MFEZs and Industrial Parks whose developers and investors would invariably be foreigners, and very generous tax concessions had been granted to these investors. The other problem that may arise in these foreign-dominated manufacturing enclaves would be transfer pricing and any measures to curb this would be difficult to enforce.

COMMITTEE'S OBSERVATIONS AND RECOMMENDATIONS

8. Having taken time to seriously analyse the submissions made to them by various stakeholders, your Committee note that the 2009 budget is dominated by a very wide range of tax concessions given as incentives to foreign investors. As a result, the tax incentives may overload the tax instruments with multiple goals and there is the danger that they will complicate compliance, trigger unproductive efforts to obtain their benefits and may be difficult to administer. Further, because the incentives are extensive, the erosion of the tax revenue base will be significant. Specifically, your Committee wish to make the following observations and recommendations:

Structure and Purpose of Tax Incentives

Your Committee note that, despite the fact that Zambia has a pressing need for increased revenues, the Government has continued to offer tax incentives to foreign companies in a bid to entice foreign investors to invest in the country. However, your Committee wonder whether the objective is merely to attract foreign investors in the country with the sole objective that they will provide employment to the Zambian people without contributing to the development of a strong local entrepreneurial base through joint ventures with local entrepreneurs or, indeed, contributing significantly to the revenues of the Republic through payment of various taxes. They note that, as a matter of fact, the revenues that Zambia foregoes through these tax incentives are collected by the countries of origin of these investors, and these funds may end up being lent to Zambia as budget or programme support. It is even more worrying to note that these investors are allowed to externalise their earnings in full. Your Committee, therefore, recommend that the incentive structure be critically and holistically reviewed with a view to minimising the incentives or restricting them to those investors who will contribute more to Zambia's long term goals. Your Committee find it unacceptable that Zambia can continue offering incentives to investors whose only benefit is to offer lowly paid employment to a few Zambians. It would be important, for example, to evaluate the trade gains that may arise from MEFZs and Industrial Parks by analysing the relationship between Zambia's GDP and GNP. It should be noted that the distinction between gross domestic product (GDP), which is a measure of the value of output generated within the geographic boundaries of Zambia, and the gross national product (GNP), which measures the income actually earned by Zambian nationals, is extremely important. To the extent that the export sector, or any sector of the economy, is foreign owned and operated, GDP will be that much higher than GNP, and few of the benefits of trade will actually accrue to Zambian nationals. It may even be possible for the value of exports to be greater than GNP, meaning that foreign export earnings may exceed the total value of domestically accrued income.

The Customs and Excise (Amendment) Bill

It has become clear over the years that in Zambia one of the most important stimulants of sustainable economic growth and meaningful employment is the growth of the local manufacturing sector. In this regard, it is disappointing that despite the large quantity of incentives provided in the 2009 budget legislation, these are largely restricted to foreign dominated sectors such as MFEZs and mining, while very little attention is paid to local manufacturing. In fact, the only fiscal incentives offered to local manufacturers appear to be piecemeal and not based on any strategic long term economic considerations. For example, the reduction of duty on vegetable oil, packaging material and gypsum, all of which have been locally produced before and can still be locally produced if appropriate incentives are given to manufacturers, suggests that the Government is not keen to support local manufacturers. On the contrary, it suggests a bias towards imports to the detriment of local manufacturing. Your

Committee wish to echo the call made by the Republican President during the Opening of the Third Session of the Tenth National Assembly to diversify the Zambian economy and implore the Government to implement this important economic policy by giving support to the local manufacturing sector. For example, the Government must coordinate and promote the exploitation of the gypsum reserves in the country so that Zambia can export this product.

Income Tax (Amendment) Bill

***(a) The Mining Sector* -** Your Committee wish to reiterate their concern over the fact that the mining industry appears to have been singled out for special favourable treatment in the 2009 budget. While they appreciate the important role that the industry plays in Zambia's economy, they are of the view that for a country that has proclaimed itself to be on the path to diversification, it is imprudent to continue to offer such substantial incentives to the very sector from which it seeks to diversify. In this regard, your Committee are concerned about the proposal to abolish windfall tax. This is even more worrying in the light of the fact that the capacity of the Zambia Revenue Authority to monitor mining transactions for the purpose of enforcing tax legislation is still not well developed, while the mining companies have well developed and sophisticated operational methods. Your Committee's position is strengthened by the fact that the Government conceded that they did not know the actual cost of production in the mining industry and had since engaged a consultant to undertake a study on three mines which had high, medium and low cost profiles, respectively. In the same vein, without knowing cost profiles, your Committee wonder how the Government can effectively evaluate the genuineness of claims by the mining companies to the effect that the mines are unprofitable at the prevailing metal price levels and there is need to place them on care and maintenance. Further, your Committee feel that since windfall tax is self-adjusting, it does not place an extra burden on the mining companies during times when the metals prices are below the threshold at which it becomes applicable, as is presently the case. Your Committee are also mindful of the fact that the copper prices will certainly rebound in the next few years and Zambia will still need to benefit from such a boom. In the light of these observations, your Committee strongly recommend that the windfall tax be retained, even though it will be in a redundant state until the metal prices improve. As regards the contention that windfall tax is punitive, your Committee recommend that the tax should be reviewed to make the thresholds less punitive and it should be made deductible for corporate tax purposes. For the reasons outlined above with regard to the capacity of the ZRA, your Committee also do not support the proposal to allow hedging income to be part of mining income for tax purposes. They fear that without proper monitoring, the practice of transfer pricing will result in Zambia getting very little revenues out of the mining industry.

***(b) Pay-As-You-Earn (PAYE)* -** Your Committee totally agree with stakeholders that the budget failed to relate the cost of living to the tax exemption that had been provided to individual taxpayers. It is clear that little consideration was given to the minimum amount required to meet the basic needs of a poor family in Zambia. Your Committee argue that in establishing the tax exempt threshold, cognisance must also be taken of the fact that the individual tax payer will bear the burden of paying twenty-six point four percent of total tax revenue compared with ten point eight percent from the corporate sector and one point five percent as mineral royalty tax. This raises serious questions of equity of the tax system. It is now established from these numbers that taxes in Zambia do little to change the overall burden distribution. Your Committee implore the Government to, in future, consider using indexation in the computation of PAYE to protect the purchasing power of the public. They, further, call for a review of the tax exempt threshold in order to give meaningful relief to the Zambian worker by ensuring that the levels of tax free income as provided by personal exemptions and deductions should be above the poverty line as the cost of living based on the cost of essential food items and non-food items for a family of six in Zambia is currently around one million five hundred thousand kwacha per month.

Value Added Tax (Amendment) Bill

There has been a consistent call for the Government to review downwards the rate of Value Added Tax (VAT) in order to bring it in line with the rest of the region. Your Committee strongly recommend that the Government undertake such a review as soon as possible, even using gradual reductions over a period of time. There have also been concerns raised that the 21 day period given for payment of VAT was too short and resulted in cash flow problems for many businesses who were required to pay the VAT within this period even though they may not have actually received payment for the transaction in question. Since most business transactions in Zambia had a credit period which could be anything between 45 to 60 days, or even longer in the case of Government institutions, business entities were sometimes compelled to borrow from financial institutions at very high cost, which added to their already high operational costs. Your Committee are of the strong view that this issue must be revisited by extending the VAT payment period to at least 60 days.

The Zambia Development Agency (Amendment) Bill

The proposed amendments to this Act have raised some serious concerns for your Committee. Firstly, as earlier stated, the incentives offered in these amendments are primarily targeted at non-Zambians. This in itself is a matter of grave concern as your Committee are not convinced that the expected benefits for Zambians will be substantial, while the Government will suffer revenue losses through these fiscal incentives. In recognition of the fact that Zambian investors face well known constraints in accessing capital, your Committee recommend that a special (lower) threshold be established for Zambian investors to enter MFEZs, and that partnerships between foreign investors and local entrepreneurs be made a requirement for entry into MFEZs. The Government must also include a requirement in MFEZ regulations that the investors must satisfy a specified criteria with regard to the number of permanent and temporary tools their projects will generate before they can be eligible for the incentives.

Further, your Committee are concerned that there is clear discrimination against Zambians who will provide consultancy and management services to operators in MFEZs. They find it unacceptable that the Government sees the need to make the cost of such services competitive only if these services are being offered by foreign contractors. In fact, they reiterate their earlier contention that it is imprudent to allow foreign investors (and, in this case, contractors) to externalise all their earnings tax free only to go and seek donor support from their countries of origin who would have collected taxes on the money earned in Zambia. Your Committee emphasise that with this kind of approach, Zambia will never be able to earn enough to sustain her budgetary requirements and will perpetually remain a begging nation. Your Committee, therefore, stress the need to review the proposal to exempt only foreign contractors from payment of withholding tax on consultancy and management fees and extend this relief to Zambian contractors.

Property Transfer Tax (Amendment) Bill

Your Committee strongly support the proposed amendment as it seeks to make the valuation of shares in related party transactions more objective so as to reduce the possibility of tax planning.

CONCLUSION

9. Sir, your Committee concluded their deliberations within their terms of reference. Your Committee could not have succeeded in carrying out their work if it had not been for the cooperation of various stakeholders from whom they sought comments and reactions to the proposed budget legislation for 2009. Although the time given to your Committee to conclude

these consultations was limited, your Committee are grateful that the stakeholders made an effort to make both oral and written submissions to your Committee. For the support and cooperation received from these stakeholders, Sir, your Committee wish to record their profound gratitude. They also wish to thank you, Mr Speaker, for affording them an opportunity to scrutinise the budget legislation for 2009 and to convey their appreciation for your guidance throughout their deliberations. They, further, thank the Office of the Clerk of the National Assembly for the unfailing assistance and advice throughout their deliberations.

We have the honour to be, Sir, your Committee on Estimates mandated to consider the Income Tax (Amendment) Bill, NAB 1/2009, the Customs and Excise (Amendment) Bill, NAB 2/2009, the Value Added Tax (Amendment) Bill, NAB 3/2009, the Property Transfer Tax (Amendment) Bill, NAB 4/2009 and the Zambia Development Agency (Amendment) Bill, NAB 5/2009.

Mr B Imenda, MP
(Chairperson);
Mr J P L Mulenga, MP
(Member);
Mr E M Hachipuka, MP
(Member);
Mr H H Hamududu, MP
(Member);
Ms J Kapata, MP
(Member);
Mr S Chisanga, MP
(Member);
Mr E M Sing'ombe, MP
(Member); and
Mr A M Nyirenda, MP
(Member).

APPENDIX I
WITNESSES

MINISTRY OF JUSTICE
Mrs P D Jere, Acting Chief Parliamentary Counsel
Mrs M M Katongo, Acting Principal Parliamentary Counsel

Mr A Nkunika, Parliamentary Counsel
Ms Y K Chirwa, Parliamentary Counsel
Ms B L Musopelo, Parliamentary Counsel
Ms P Goma, Parliamentary Counsel

ZAMBIA INSTITUTE OF CHARTERED ACCOUNTANTS (ZICA)
Mrs C Zimba, Taxation Committee Chairperson
Mr H Kabeta, Secretary and Chief Executive

ENERGY REGULATION BOARD
Mr S H Hibajene, Executive Director
Mr B Sitali, Chief Legal Counsel

ZAMBIA BUSINESS FORUM

Mr R K Mfula, Chief Executive Officer
Mr M Sichula, Executive Secretary
Mr C Msoka, Research and Policy Officer
Mr B Lwando, Information Officer

ECONOMICS ASSOCIATION OF ZAMBIA

Mr I Ngoma, National Secretary
Mr A Chileshe, Executive Director

ZAMBIA DEVELOPMENT AGENCY

Mr A Chipwende, Director General
Mr M Lungu, Director RPP

MINISTRY OF COMMERCE, TRADE AND INDUSTRY

Dr J Mulungushi, Permanent Secretary
Mr J Mulongoti, Chief Economist
Ms E C M Soko, Data Manager

MINISTRY OF FINANCE AND NATIONAL PLANNING

Mr L Ndalamei, Secretary to the Treasury
Mr E Ngulube, Permanent Secretary (BEA)
Mr D K Chisenda, Director, Budget Analyst
Mr M Masiye, Principal Budget Officer
Mr F Nkulukusa, Chief Budget Analyst
Mr C Mwansa, Commissioner General, Zambia Revenue Authority
Mr W Nhekairo, Commissioner, Domestic Taxes, Zambia Revenue Authority
Mr R Kunda, Assistant Commissioner, Zambia Revenue Authority
Mr D Mulima, Assistant Director, Zambia Revenue Authority

APPENDIX II

List of Officials
Mr S M Kateule, Principal Clerk of Committees
Mr G Lungu, Deputy Principal Clerk of Committees
Ms M K Sampa, Committee Clerk (FC)

Ms C Musonda, Assistant Committee Clerk
Mr S Mtambo, Assistant Committee Clerk
Mrs D Mukwanka, Assistant Committee Clerk
Mr C Chishimba, Assistant Committee Clerk
Mrs J M Phiri, Personal Secretary I
Ms S Mwale, Stenographer
Ms K Chisenga, Typist
Mr R Mumba, Committee Assistant
Mr M Likunyendo, Parliamentary Messenger