Contribution by the Tanzania Tax Justice Coalition on Tax Reform in Preparation for 2016/17 Budget

1. WHO ARE WE?

Tanzania Tax Justice Coalition is a loose coalition of NGOs interested in tax justice. The group was started in 2013 under Policy Forum. The group comprises of Policy Forum, Action Aid Tanzania, Kepa, Youth Partnership Countrywide (YPC), Tanzania Coalition on Debt and Development (TCDD), Tanzania Trade and Economic Justice Forum (TTEJF), Tanzania Youth Vision Association (TYVA), Governance and Economic Policy Centre, Tanzania Education Network (TenMet) and Norwegian Church Aid (NCA).

2. OUR PROPOSALS FOR TAX AND NON-TAX REVENUES

Our tax reform proposals in Preparation for 2016/17 Budget on both tax and non-tax revenues are aimed mostly at increasing revenues that are crucial for financing economic and social services, thus fueling national development. Cognizant of the fact taxation is a critical aspect of state building, we place emphasis on the removal of harmful tax incentives that are an unnecessary loss of revenue considering anticipated decline in foreign aid transfers. The recommendations are as follows:

i. **Simplify tax revenue collection:** Tanzania has normally quite a low tax revenue yield and FY 2015/16 and recent years were no exception as tax revenue collection targets were missed including on import duties, value-added tax, excises, income tax, and other taxes resulting in revenue pressures for Tanzania. At around 12% its GDP, Tanzania's tax revenue collection is one of the worst in the world and insufficient to fund the budget and the country's ambitious development plan.

   This has partly been due to policy and administrative challenges recently exemplified in the difficult rollout of the Electronic Fiscal Device EFD/mobile devices for tax payment from small businesses and Tanzania's poor showing in "ease of paying taxes" indicator in the World Bank's Doing Business survey and the WEF's Travel and Tourism indicators, which in the latter it ranked 111th out of 141 countries surveyed. The government should simplify the costs of transaction for businesses to improve tax compliance if revenue collections are to rise. It is important to bear in mind; however, that simple embrace of technology in the collection of taxes will not be the panacea. Due to the ad hoc way in which the Tanzanian tax administration system has been formulated over many years, the longer term solution would be to establish a 'bottom-up' and inclusive process to overhaul it which will involve all tax stakeholders to enhance a robust social contract between the State and its taxpayers which is currently inadequate as not all stakeholders are on board.

   A related recommendation that will help support high levels of overall tax compliance is helping businesses spend less time on tax and more on being productive. The huge amount of time spent on following up taxpayer rulings and disputed debts, slow response time of taxpayers to

documentation requests, the difficulty in paying penalties and difficulty in correcting errors are some examples of time-consuming tax related work.

ii. **Expand the Non-Tax Revenue space**: Excluding LGAs own sources of revenues, the non-tax revenues we are referring to are the royalties on mining, fines, charges, levies and fees mobilized by the government which are not derived from taxes. These include, but are not limited to, contributions and dividends from public corporations, revenues from investment funds, fees for permits and revenues from the sale of state assets. The contribution of non-tax revenues, however, remains consistently low whereby the average yield over the past six years hovering around 1% of GDP[1] and non-tax revenues account for less than 2% of total Government revenue. For the financial year 2015/16, the estimated non-tax revenue was only TZS 12.7 billion.

The government, hence, should find interventions, both regulatory and administrative, for FY 2016/17 that would be geared towards strengthening the effectiveness in mobilizing revenues from this fiscal space of non-tax revenue. This should include concretizing government plans to integrate and harmonize non-tax revenue collection systems, local authorities, public institutions and agencies remitting 10% of collected gross non-tax revenue to the Exchequer as well as introducing electronic payment systems as a way of minimizing leakage of revenues.

Alternatively, the government could consider the idea that all royalty payments from natural resources be paid through the Tanzania Revenue Authority instead of parent ministries.

iii. **Harmful tax incentives**: Ending harmful tax incentives that do not have policy-based underpinnings. Multinational companies are receiving too extensive tax exemptions and not paying their fair share of tax while citizens are bearing a disproportionate tax burden due to an over reliance on consumption taxes in revenue collection such as Value Added Tax (VAT) and Pay As You Earn (PAYE) which was reduced from 12% in 2014/15 to 11% 2015/16.

The government should consider restraining from further developing Economic Free Zones. For example, the Global Financial Integrity has estimated that Tanzania lost 2.5 billion euros in 2002-2011 only due to trade and transfer mispricing by multinational companies. One of the main reasons behind increased illicit outflows is the existence of Export Processing Zones/Special Economic Zones (EPZ/SEZ)[2]. Despite this, the Government continues to commit to further development of such zones within its budgetary framework.

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[1] tax revenue collection is approximately 12% of GDP at TZS 12,363 billion which also very low compared to the collection in neighbouring countries. The target is to increase to increase tax revenues to reach 13.1% of GDP Source, 2015/16 Budget Speech:
http://www.tra.go.tz/documents/BUDGET%20SPEECH%20MINISTER%20OF%20FINANCE%20FINAL%20FINAL.pdf

[2] Global Financial Integrity (2014): Hiding in Plain Sight: Trade Misinvoicing and the Impact of Revenue Loss in Ghana, Kenya, Mozambique, Tanzania, and Uganda: 2002-2011
http://www.gfintegrity.org/report/report-trade-misinvoicing-in-ghana-kenya-mozambique-tanzania-and-uganda/

Tax exemptions alone deprive our country of the so much needed resources to finance public expenditure. These annual revenue losses are approximately 4% of GDP which in FY 2011/12 for example, amounted to over Tshs 1 billion which was about 18% of the total tax collections. Different studies including one by the International Monetary Fund (IMF) have actually noted that investment incentives and particularly tax incentives are not an important factor in attracting foreign investment.

Where government finds it imperative to grant exemptions as a result of evidence-based policy prescriptions, they should be issued in a transparent manner and the mechanism for monitoring and evaluating them should be robust. This should also include parliamentary scrutiny before the incentives are granted. This should be supported by issuing annual tax exemption reports which will detail the beneficiaries and the reasons for their provision.

iv. **Tax treaties:** Ending harmful tax treaties that limit the ability for Tanzania to raise revenue to fund quality public service delivery. Tax treaties are intended to prevent multinational companies and individuals from paying tax twice in two countries, but instead exploitation of these treaties with poor terms for "source countries" are leading to Tanzania potentially losing revenues.

The government should invest more in other measures to attract FDI and winning investor confidence instead of heavily relying on double tax treaties as a tool for FDI attraction. As suggested by Baker (2012) and Irish (1974) the absence of assurances which double taxation agreements provide to foreign investors can be overcome to a substantial extent by the government agreeing with individual investors to restrict their tax rates to particular levels and by providing non tax preferences to investors. Such non tax preferences could take the form of government participation in an investment with guaranteed return to the investor prior to any return to government, preference in import permits or exchange controls and robust steps to insure absence of a double taxation agreement has no detrimental effect on foreign investment. Where Double Taxation Agreements are important, the government should ensure that she benefits first. This can be achieved through conducting cost benefit analysis of the agreements before signing them. This will also inform on whether the government should renegotiate or cancel the agreements.

v. **Enhance TRA's capacity:** There is a strong reason to sustain current government efforts to increase resources to the Tanzania Revenue Authority (TRA) to oversee and collect revenue from multinational companies. Multinational companies possess sophisticated skills that make it easy for them to avoid and/or evade tax. It is therefore important that our revenue authority progressively increases the number of competent staff that can oversee and collect fair share of revenue from these companies. A particular area under this is the enhancement of transfer pricing expertise at TRA's International Taxation Unit (ITU) so that they are able to undertake audits. Although there is tremendous transfer pricing manpower and technical expertise

improvements at the ITU, more needs to be done to bolster their industry-specific expertise (eg specific training on mining, oil & gas, etc) and ability to access to information from across the extractive industries value chain. There is also need to improve the technology and infrastructure to enhance their efficient work on curbing transfer mispricing.

Enhancing TRA's capacity goes hand in hand with improving its image to the general public. It is widely believed that officials in TRA are highly involved in corruption. This is supported by a survey done by REPOA last year in which one third of those interviewed considers tax officials as the most corrupt in the population. With this belief amongst citizens, compliance is in some ways compromised.

vi. **Commit to tackling international tax avoidance and evasion** through implementing the recommendations set out in the African Union High Level Panel report on Illicit Financial Flows from Africa. The HLP report estimated that Sub-Saharan Africa loses more than 50 billion dollars annually (average of 2001-2012). This is more than the combined total of foreign direct investment (FDI) and net official development assistance (ODA), which these economies received in the same year. Among the various commitments are robust regulation for increased transparency, which includes disclosure of companies' annual financial statements and the establishment of a public beneficial ownership registry. In addition to these policy measures, we urge the Government to support the establishment of an intergovernmental tax body that is tasked with addressing global tax policy, rather than the current Organization for Economic Cooperation and Development (OECD) led process that does not equally include all countries, including Tanzania. A cohesive global system will make it simpler for tax administrations across the world to communicate and cooperate and remove the existing complicated web of thousands of bilateral tax treaties in the international tax system and streamline the diverse parallel international systems.

vii. **Widening the tax base by accelerating the formalization of the informal sector:** although it is assumed costly to collect revenue from the informal sector, cumulative tax revenue collection from such a sector is beneficial to the country in the medium to long term. There is value and justification to create conducive, efficient and effective structures and systems to progressively tax the informal sector while improving their work infrastructure. These range from sustaining morale and compliance amongst taxpaying small and medium businesses in the formal sector, strengthening the nexus between taxes and accountability through improved governance All this is aimed at accelerating economic and social growth The informal sector needs to be formalized by developing a database which will enhance payment of taxes in a fair manner. It is also evident that the formal sector still needs to be adequately addressed by ensuring that all individuals pay withholding tax. Most of the property owners including their agents do not pay the required taxes. Devising mechanisms that ensure capital gain tax as well as withholding taxes are paid will earn the government substantial revenue that would help in funding different development projects. The government should explore ways in which taxation of the informal economy can be done effectively.