



# Evaluation of PARPA II – Impact of Tax Policy

Debriefing Presentation  
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Maputo, Mozambique

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## Terms of Reference

- General objective: Analyze tax system impact on:
  - Sustainable revenue
  - Broad-based econ growth
  - SME development
  - Other PARPA II priority objectives
- Specific objectives:
  - Development of revenues
  - Regional and international perspectives
  - Recommendations on priorities for PARPA III
  - Trade-offs: increasing revenue vs. impact on private sector development
- Synthesize findings and recommendations

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## The study team

- Bruce Bolnick, Team Leader
- Bruce Byiers
- Egildo Massuanganhe
- Field assistance from TIPMOZ staff
- Research support from Nathan headquarters

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## Methodology

- Review relevant legislation, data, documents, studies
- Interview key organizations and stakeholders
  - Government (10 meetings)
  - Private sector (12 meetings)
  - Donor organizations (9 meetings)
- Examine tax administration practices
- Compare with regional and international standards

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## Provisional outline of report

- Introduction
- Background – baseline tax system, pre-PARPA II; reforms during PARPA II period
- Revenue trends and collection performance, including international benchmarks
- The current tax system
- Impact of the tax system on PARPA II objectives
- Major tax issues: 2009
- Conclusions and priority recommendations
- Technical appendices

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## Revenue performance (% GDP)

	<u>2005</u>	<u>2008</u>
Domestic Revenue	13.8%	16.0%
Tax Revenue	11.1	13.5
Income Tax	2.9	4.9
VAT	4.5	5.4
Excise	1.0	1.1
Import duty	1.9	1.5

Predicted value of revenue ratio (regression estimate) = 16.6%

Predicted normal range (50% band) = 15.4% - 17.8%

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## Revenue buoyancy with respect to GDP

	Ave. 00-08	Ave. 06-08
Receita Total	1.38	1.34
Receitas fiscais	1.32	1.48
<i>Impostos sobre Rendimentos</i>	1.97	2.35
<i>Imposto s/ rendimentos de pessoal</i>	2.00	1.65
<i>Imposto s/ rendimentos de empresas</i>	2.05	3.49
Impostos sobre Bens e Serviços	1.22	1.18
<i>IVA Operações internas</i>	2.16	2.00
<i>IVA Importação</i>	2.00	1.58
<i>Imposto s/ Consumo Especifico - Prod.s Nacionais</i>	1.15	1.15
<i>Imposto s/ Consumo Especifico - Prod.s Importados</i>	1.17	1.28
<i>Direitos Aduaneiros + sobretaxa de acucar</i>	0.97	0.52
<i>Imposto s/ Combustíveis</i>	1.06	0.78

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## SADC Comparison

Fiscal Indicators, three year averages 2006-2008 (all figures express as % GDP)				
	GDP per capita (current USD)	Government Revenue (excluding grants)	Overall Fiscal Balance (including grants)	Overall Fiscal Balance (excluding grants)
Angola	3,813	46.9	12.9	12.9
Botswana	7,011	35.7	4.6	3.9
Congo, Dem Rep	165	15.4	-0.7	-5.8
Lesotho	666	59.8	11.8	10.3
Madagascar	373	12.1	10.6	-8.3
Malawi	273	18.7	-2.4	-5.2
Mauritius	5,803	20.0	-4.3	-4.5
Mozambique	408	15.8	-3.7	-13.5
Namibia	4,146	30.3	1.0	0.8
Seychelles	10,943	37.8	-4.4	-6.2
South Africa	5,686	26.6	0.2	0.2
Swaziland	2,750	41.0	5.8	5.3
Tanzania	442	13.2	-2.8	-8.1
Zambia	1,002	18.2	5.7	-5.8
Zimbabwe <sup>1</sup>	na	na	na	na
SADC Mean	3,106	28.0	2.4	-1.7
SADC Median	2,750	26.6	1.0	-4.5

Source: IMF, Sub-Saharan Africa Regional Economic Outlook, April 2009; World Economic Outlook April 2009

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## Major reforms 2006-2009

- Revenue Authority act– 2006
  - All sources see major improvements in tax administration since AT established
- General law on taxation – 2006
- Revised codes for IRPC, IRPS, IVA – 2007
- Revised mining and petroleum Laws – 2007
- Municipal finance law – 2008
- “Rationalized” code of fiscal benefits – 2009
- Simplified tax (ISPC) – 2009
- Revised excise tax code – 2009

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## The new simplified tax regime (ISPC)

- Enterprises with turnover up to 2,500,000 MT may register.
  - Exclusion from VAT, IRPC and IRPS on ISPC income
- Enterprises with turnover up to 36 x highest minimum wage are exempt from tax.
- Applicable tax rate = 75,000 MT per year, or 3% of sales volume
  - Tax reduced by half for new businesses in first year of operation
- Simplified registration, bookkeeping, receipt books
  - Broad geographical access - logistics being planned
  - In June 2009 (month one), 1800 new taxpayers registered
- Widely seen as a major instrument for broadening the tax base and facilitating formalization
  - But large gain in revenue *very unlikely*

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## The new Fiscal Benefits Code (CBF)

- Ends the special negotiation regime for mega projects (!!)
- Large projects are now covered by IRPC
- Customs and duty exemptions on “K” goods remain
- Scales back generosity of many benefits
- See HANDOUT on generic benefits: 2009 vs 2002
- Income tax reductions still available for
- Agriculture, until 2025
- Science and technology parks, up to 15 years
- Industrial Free Zones, for life of project
- Special Economic Zones, up to 15 years
- New evidence on effectiveness of fiscal benefits
- Bolnick (2009) at [www.tipmoz.com](http://www.tipmoz.com)
- Ongoing research at the IFC

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## Can “small” domestic businesses benefit?

- \$5000 threshold for domestic enterprises
- Evidence of management and financial capability
- Procedures and information requirements

Category	2006	2007	2008
<b>Total approved investments</b>	<b>157</b>	<b>192</b>	<b>--</b>
<b>FDI only</b>	<b>72</b>	<b>97</b>	<b>--</b>
<b>JV</b>	<b>56</b>	<b>63</b>	<b>--</b>
FDI majority share	49	53	--
National majority share	3	5	--
Equal shares	4	5	--
<b>National only</b>	<b>29</b>	<b>32</b>	<b>--</b>
Equity < \$50,000	10	10	--
\$50,001 to \$100,000	3	4	--
\$100,001 to \$250,000	4	7	--
> \$250,000	12	11	--

Source: Calculations based on data provided by CPI

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## Impact on PARPA objectives

- Sustainable revenue growth
  - Major issue: medium-term revenue targets
  - Limited scope for base broadening via tax policy
  - Huge potential via improvements in tax administration
  - Natural elasticity of tax base relative to GDP
  - Enormous problems with evasion, false invoicing, smuggling, corruption
- Investment
  - Non-tax elements of the investment climate are far more important
  - Incentive regime reasonably attractive for internationally mobile investments (IFZ provisions)
  - Government *should* be seeking maximum domestic benefits from resource-based projects
  - Note: high METR reported in earlier studies mainly driven by double taxation of dividend income: easily fixed

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## Impact (2)

- Private sector development
  - Tax rates are not the main issue
  - Complexity of the tax code → high compliance costs
  - Ambitious revenue targets → punitive & arbitrary enforcement
  - VAT refund problems! Excessively complicated requirements
- Growth of SMEs
  - ISPC as new era ?? Depends on implementation
  - PSD issues most difficult for SMEs
  - Withholding tax inhibits development of linkages
- Employment
  - Job creation driven by impact on investment, PSD
  - And impact on capital intensity

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## Major issues (a sampler)

- Target tax ratio (tax/GDP)
  - Balance between growth and revenue requirements?
- Simplification and public information
- e-Taxation
  - Great need, great potential & *great pitfalls*
- Risk-management practices by the AT
  - Focus on operational efficiency, performance indicators
- Need to develop *service culture* within the AT
  - And *culture of paying taxes* on the part of the public
- Training for tax officials
  - And private sector accountants
- Donor coordination in assisting the AT

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## Preliminary recommendations

- The gorilla in the room: the revenue target ??
  - 0.5% per year target is arbitrary, with serious repercussions for the private sector
  - International comparisons, taking into account economic conditions → target in vicinity of 18% [preliminary]
  - Reduction in tax rates must be packaged with base broadening measures
  - Annual targets should be based on analysis of revenue effects of tax reforms, and underlying revenue elasticity
    - Need for Tax Policy Analysis capacity
- Large number of other issues as potential priorities
  - See HANDOUT

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## Schedule

- Field work June 28 – July 17
- Submission of draft July 31 (on or about)
- Final report Soon after comments received

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