

TANZANIA NATIONAL BUSINESS COUNCIL
FISCAL POLICY SUBCOMMITTEE OF THE FINANCE
WORKING GROUP REPORT

1.0 Fiscal Policy as Instrument of Stirring up Economic Growth

The Fiscal Policy Subcommittee (FPS) of the Finance Working Group agrees that fiscal policy can be used, among others, as an instrument to stir economic growth. The Budget is the main instrument of execution of fiscal policy, itself containing taxation policy and expenditure policy. For a long time the tax policy has taken the centre stage as growth-stirring instrument of fiscal policy through designing a lucrative incentive policies package aimed at attracting investment. Expenditure policy has not been prominently emphasised by investors as an instrument of economic growth, although it is always the more potent instrument than tax policy. Expenditure is the easier to target intended beneficiaries and measure its expected results than tax policy. It is therefore important to bring expenditure policy on board when using fiscal policy as instrument of economic growth.

Measuring the gains of the fiscal sacrifice the nation incurs through incentives granted is a highly elusive subject. Existing empirical evidence shows that tax incentives are important, but not the most important variable in determination of investment flows and hence economic growth. Being one of variables influencing economic growth, tax policy will continue to form part of policies recipe proposed by FPS for stirring up national economic growth.

2.0 Fiscal Policy Issues for Economic Growth - Agriculture

The Government of United Republic of Tanzania is committed to promoting agricultural revolution as it is a key sector to the realisation of its efforts on eradication of poverty and achievement of sustainable economic growth. Implementation of agricultural revolution is about commercialisation and modernisation of the sector. Fiscal policy also needs to orient towards facilitating agricultural revolution.

The Fiscal Policy Subcommittee (FPS) of the Finance Working Group has earmarked a few fiscal policy interventions needed to assist the agro revolution process as follows:

(i) Produce Cess

Subcommittee appreciates that as a civic responsibility, every national must pay their taxes. Process Cess is the main tax paid by small peasants. However, produce cess is not charged on small peasant alone but is also applicable on corporate entities. These

pay corporate tax as well on top of the produce cess. The applicable rate of 5% for produce cess is high given that agricultural sector is a low profitability business. A number of countries have abolished produce cess, while Tanzania has retained it at farm gate level. While the Subcommittee does appreciate the need for nationals to contribute to national development, as a sign of good governance and accountability, a turnover tax at 5% for agricultural business is likely to take away all the profit from a business with profit margin as low as agriculture. The Subcommittee recommends that produce cess charged by Local Authorities should be capped at 1% of farm gate price.

The Subcommittee supported the recommendation to review the produce cess from 5% to 1% to be charged at a single point-farm gate level.

(ii) Fuel Taxation

Subcommittee has noted that fuel levy imposes a heavy tax burden on farm use and agricultural processing. Farmers using fuel on their farms ought not to pay Fuel Levy, which is specifically earmarked for development of roads. On the basis of administrative complexities involved in monitoring fuel exemptions, the Subcommittee recommends possibility of adopting expenditure policies to subsidize fuel for farming activities with a view to alleviating the heavy burden fuel taxes impose on agriculture.

The exemption of petroleum products from Value Added Tax (VAT) makes input VAT paid by agricultural sector ineligible for credit. The VAT built in the product becomes part of production cost and hence chargeable to VAT at higher stages of production process. This produces cascading, i.e. tax on tax, a problem which VAT was meant to be superior to sales tax.

It was clarified that excise duty and fuel levy are the only taxes charged on petroleum products, confirming that there is no input VAT charged in this regard.

(iii) Land Rent

Land is the main resource for agriculturists. Tax on ownership of land in Tanzania however is a heavy burden on title holders. Land rent is chargeable at the rate of Sh. 200 per acre. The land rent rate is not only high but also inequitable as it is only chargeable on title holders. The rate means owner of a ranch with about 48,000 hectares pay land rent of Shs. 24.0 million per year. The flat rate of Shs. 200 per acre irrespective of the location of land is economically unjustifiable. This is applicable to all producers irrespective of the gestation periods of the farm product. In order to ease the burden imposed on land ownership it is proposed to reduce land rent from Shs. 200 per acre to Shs. 20 per acre.

It was suggested that land should be classified into two main categories and be charged as follows:

- *For land not utilised, the rent should be increased from TShs. 200 to TShs 500 per acre. Continuous non-utilisation of the land should empower the Government to revoke or cancel ownership,*
- *Exempt the rent for land under production, noting however that the existing rent of Tshs 200 under discussion was rather small.*

(iv) Payroll Taxes

Payroll taxes are another burden on agriculture. The removal of Skills Development Levy on agricultural employment means that only one payroll levy remains, that is contributions to social security funds. These too are a big cost to agricultural business. Our recommendation is that, as is the practice in some countries, contributions to social security funds should be capped at Shs. 50,000 per employee. The proposal is aimed at lessening the disincentive to employ which these levies cause at the moment when there is massive unemployment and underemployment.

It was suggested that the agricultural sector should be exempted from Payroll Levy. Nevertheless, farms of more than 500 acres should observe the National Social Security Policy for their employees.

(v) Corporate Tax

Agriculture in Tanzania is starved off investments, with a great deal of it being primarily peasant-based. To be able to realise agricultural revolution large scale commercial farming is prerequisite. In order to attract both local and foreign investments, the Government should reduce the current corporate tax rate from 30% to 10% as is applicable in Mozambique.

It was recommended to reduce corporate tax on the agricultural sector by fifty per cent, from 30% to 15% for the first 5 years of the investment.

(vi) Import Duty on Substitutes

Imports from the rest of the world, especially from highly subsidized countries, endanger sustainability and competitive edge of domestically produced substitutes. In order to encourage domestic production the Government should consider imposing import tariffs on products with potential of creating a threat to domestic industries through imported subsidy or endangering domestic industries market of inputs and raw materials. These include oil seeds, dairy and poultry products and vegetables.

It was suggested to impose import duty (countervailing) on products dumped into the Tanzanian market which are locally produced in the endeavour to protect domestic industries.

(vii) VAT on Agricultural Products

Many agricultural producers and processors are small-scale operators. VAT paid by small holders' sugarcane farmers and small holders, cotton, cashew nut farmers who in their legal status have revenue below the threshold of Shs. 40 million cannot qualify for input VAT refunds. Big farmers, plantation owners of similar crops qualify and have VAT refunded.

Smallholder sugarcane farmers unlike their counterparts in coffee and tea are taxed VAT on land preparation (ploughing, harrowing, and furrowing), cane cutting, cane loading and transportation to the factories. These farmers are not VAT registered because their incomes do not qualify them for VAT registration. In neighboring countries like Malawi which is a member within the SADC trading block, smallholder sugar cane farmers are exempted from paying VAT on those services.

In the dairy industry, VAT on imported dairy processing equipment is contributing significantly to the increase in production costs. Important equipment which should be seriously considered for VAT exemption are: milk cooling machines, pasteurizers, milk separators, homogenizers, milk packing machines, cheese making and packing machine and butter churners. Removing this tax burden on this infant industry would enable dairy farmers to build capacity to increase the local market share which is now dominated by relatively cheaper imports. Ultimately, this would enable them to compete with their counterparts in the regional and international markets.

- *It was noted that capital good are import duty zero-rated and VAT relieved.*
- *It was recommended that VAT on services to sugarcane out grower schemes should be exempted*
- *It was recommended that supplies of those equipment to milk processors should be relieved from VAT.*

3.0 Fiscal Policy Issues for Economic Growth – the Budget

Fiscal Policy as an instrument of economic growth needs to be holistic, extending *beyond the boundaries of sectoral scope. The holistic approach to fiscal policy as an instrument of economic growth is the budget.* The Subcommittee has emphasised on agriculture on account of its massive potential and centrality for realisation of Government's resolve to combat income poverty and spearhead economic growth.

Expenditure policy can stir growth. A great deal of expenditure management in that direction has already been implemented but more exist. Reviews and monitoring of budgetary allocations to sectors with high spill over effects, such as infrastructure- both fiscal and human, science and technology as well as defence and security are critical to economic growth.

It was recommended that the Government should strive to comply with the Maputo Agreement to allocate at least 10% of the Budget to the agricultural sector.

Fiscal Policy Subcommittee of the Finance Working Group

ISSUE	CHALLENGES	ACTION TAKEN	RECOMMENDED ACTION TO BE TAKEN	RESPONSIBILITY	TIME FRAME
1. Orient Fiscal policy Towards facilitating agricultural revolution. Taxes covered include Produce Cess, Fuel Levy, Land Rent, Pay Roll Taxes, Import Duties and Value Added Tax	1.1 Applicable rates of 5% for produce cess is high given that agricultural sector are a low profitability business. A number of countries have abolished produce cess, while Tanzania has retained it at farm gate price. While the Subcommittee does appreciate the need for nationals to contribute to national development, as a sign of good governance and accountability, a turnover tax at 5% for agricultural business is likely to take away all the profit from a business with profit margin as low as agriculture. The rate applicable under produce cess needs to be revised.	-	Review the produce cess from 5% to 1% to be charged at a single point-farm gate level	Ministry of Finance and Economic Affairs (MOFEA)	2009/10 fiscal year
	1.3 Land is the main resource for agriculturists. Tax on ownership of land in Tanzania however is a heavy burden on title holders. Land rent is chargeable at the rate of Sh. 200 per acre. The rate is irrespective of its location and gestation period. There is need to review taxation policy for land ownership.		It is suggested that land should be classified into two main categories and be charged as follows: (a) For land not utilized, the rent should be increased from TShs. 200 to TShs 500 acre. Continuous non-utilization of the land should empower the Government to cancel ownership, (b) Exempt the rent for land under production, noting however that the existing rent of Tsh 200 under discussion was rather small.	MOFEA/Sector Ministry	2009/10 fiscal year

ISSUE	CHALLENGES	ACTION TAKEN	RECOMMENDED ACTION TO BE TAKEN	RESPONSIBILITY	TIME FRAME
	1.4 Payroll taxes are another burden on agriculture. These are a big cost to agricultural business and act as a disincentive to employment creation in the sector. Measures should be taken aimed at lessening the disincentive to employ which these levies cause at the moment when there is massive unemployment and underemployment.	The Government has removed Skills Development Levy on agricultural employment	Agricultural sector should be exempted from Payroll Levy. Nevertheless, farms of more than 500 acres should observe National Social Security Policy for their employees	Ministry of Labour, Employment and Youth Development	2009/10 fiscal year
	1.5 Agriculture in Tanzania is starved off investments, with a great deal of it being primarily peasant-based. To be able to realise agricultural revolution large scale commercial farming is prerequisite. The challenge here concerns designing a fiscal policy incentive that can encourage commercial farming, in particular to make the sector more attractive		Reduce corporate tax on the agricultural sector by fifty per cent, from 30% to 15% for the first 5 years of the investment.	MOFEA	2009/10 Fiscal Year
	1.6 Imports from the rest of the world, especially from highly subsidized countries, endanger sustainability and competitive edge of domestically produced substitutes. In order to encourage domestic production the Government should consider imposing import tariffs on products with potential of creating a threat to domestic industries through imported subsidy or endangering domestic industries market of inputs and raw materials. These include oil seed, dairy and poultry products, vegetables etc.		Impose import duty (countervailing) on products dumped into the Tanzanian market which are locally produced in the endeavour to protect domestic industries.	MOFEA	2009/10 Fiscal Year
	1.7 Many agricultural producers and processors are small-scale operators not	Government has relieved from VAT	• Exempt VAT on services to sugarcane out grower	MOFEA	2009/10 Fiscal

ISSUE	CHALLENGES	ACTION TAKEN	RECOMMENDED ACTION TO BE TAKEN	RESPONSIBILITY	TIME FRAME
	<p>registered under VAT. These cannot claim VAT paid on their inputs while big farmers and plantation owners of similar crops qualify and have VAT refunded. Sugarcane out growers are taxed VAT on land preparation (ploughing, harrowing, and furrowing), cane cutting, cane loading and transportation to the factories and cannot claim input VAT.</p> <p>Imports for milk industry, including milk cooling machines, pasteurizers, milk separators, homogenizers, milk packing machines, cheese making and packing machine and butter churners are attracting VAT.</p> <p>Removing this tax burden would enable to build capacity to increase the local market share which is now dominated by relatively cheaper imports.</p>	<p>purchase of that capital good are import duty zero-rated and VAT relieved.</p>	<p>schemes</p> <ul style="list-style-type: none"> • Relieve from VAT supplies of milk processing equipment to milk processors 		<p>Year</p>
<p>2. Fiscal Policy Issues for Economic Growth – the Budget</p>	<p>Fiscal Policy as an instrument of economic growth needs to be holistic, extending beyond the boundaries of sectoral scope. The holistic approach to fiscal policy as an instrument of economic growth is the budget. The Subcommittee has emphasized on agriculture on account of its massive potential and centrality for realization of Government’s resolve to combat income poverty and spearhead economic growth. Measures should cover other areas as well.</p>		<p>Government should strive to comply with the Maputo Agreement to allocate at least 10% of the Budget to the agricultural sector.</p>	<p>MOFEA</p>	