

# Tanzania's Tax Exemptions:

Are they too high and making us too dependent on foreign aid?



## 1. Introduction

Every year the Parliament of Tanzania carefully scrutinizes the Government's budget. Tax exemptions, on the other hand, do not receive the same attention in the Parliament, effectively making them hidden expenditures. Tax exemptions involve very large sums of money. In 2009/10 alone, 2.3 percent of GDP or TZS 695 billion was granted in tax exemptions. The sheer size of the amount involved raises questions about the purpose these incentives serve and whether the amounts spent on them are justified.

Could it be that tax exemptions are too high for a country that is struggling to collect sufficient resources to finance its budget? Could it be that Tanzania would be better off if fewer tax exemptions were granted and more money was spent on health, water or education? And why is information on who benefits not publicly available?

This policy brief does not take a position on these questions. Instead, by providing nine key facts about tax exemptions in Tanzania, it aims to contribute to a debate on whether the current practice is desirable. The analysis is based on information contained in Revenue Reports obtained from the Tanzania Revenue Authority (TRA)<sup>1</sup>. It shows that:

- The size of tax exemptions increased substantially in the second part of this decade (2006–2010).
- If tax exemptions were harmonized with what is practice in Kenya (1 percent of GDP) the existing shortfall in tax revenue would have been avoided.



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- TRA grants twice as much in tax exemptions in Zanzibar as it does on Mainland.
- Tax exemptions benefit mainly multinational investors with certificates of incentives from the Tanzania Investment Centre (TIC) and Zanzibar Investment Promotion Authority (ZIPA).

## 2. Why tax exemptions are granted

Tax exemptions are granted for a variety of reasons. In Tanzania, exemptions may be given for the following reasons:<sup>2</sup>

- Where the foreign or official nature of the item in question doesn't warrant a tax – for example, consumption on internationally bound aircraft or goods consumed by the armed forces and diplomatic missions.
- Where activities of certain organizations do not earn them a profit but have a direct benefit to society which the Government may not be able to otherwise procure. This basis is used to grant exemptions to charities including religious organizations.
- Where consumption of certain goods are deemed to have direct benefit to society. For example, certain human and veterinary medicines are exempt from VAT, as are firefighting vehicles. Exempting such goods from taxes increases their consumption, which in return brings greater benefits due to their positive effects on society.
- Another reason exemptions are granted is to stimulate economic growth. These exemptions should normally lead to increased investment, employment, output growth and thus lead to more tax revenues in the long run. Groups of companies granted wide-ranging exemptions such as favourable corporation taxes on profits and reduced import duties fall under this category. Most notable among these are companies established under the Export Processing Zones Authority (EPZA) Act, mining companies and other companies which hold certificates of incentives from TIC and ZIPA.

## 3. Nine facts about tax exemptions in Tanzania

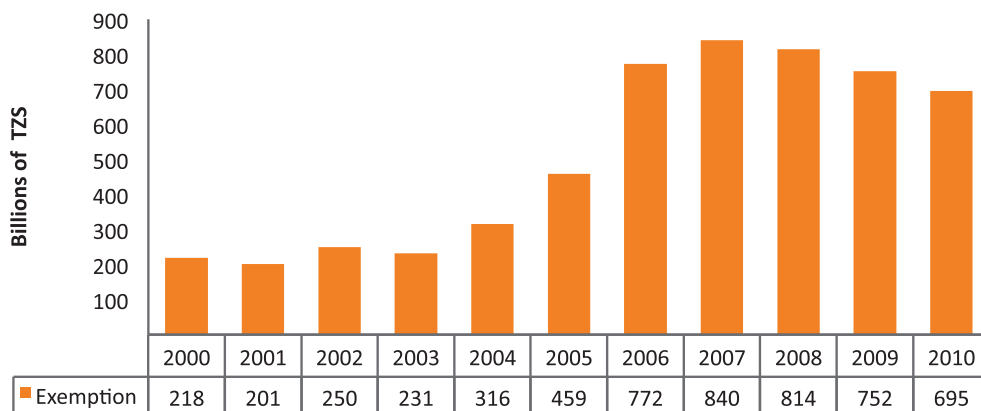
### Fact 1: A significant amount of revenue is forgone

The amount of money Tanzania gives away in tax exemptions has always been substantial but has increased rapidly in the middle of this decade. At its peak growth, tax exemptions almost doubled in one year, rising from TZS 459 billion in 2004/05 to TZS 772 billion in 2005/06.

In 2009/10 tax exemptions amounted to TZS 695 billion. This amount is more than half the TZS 1.3 trillion the Government plans to borrow from commercial sources

for infrastructure financing in 2010/11. Had it been collected, it would have provided 40 percent more resources for education or 72 percent more resources for health in 2009/10.

**Figure 1: Tax exemptions in Tanzania, fiscal year 2000-2010<sup>3</sup>**



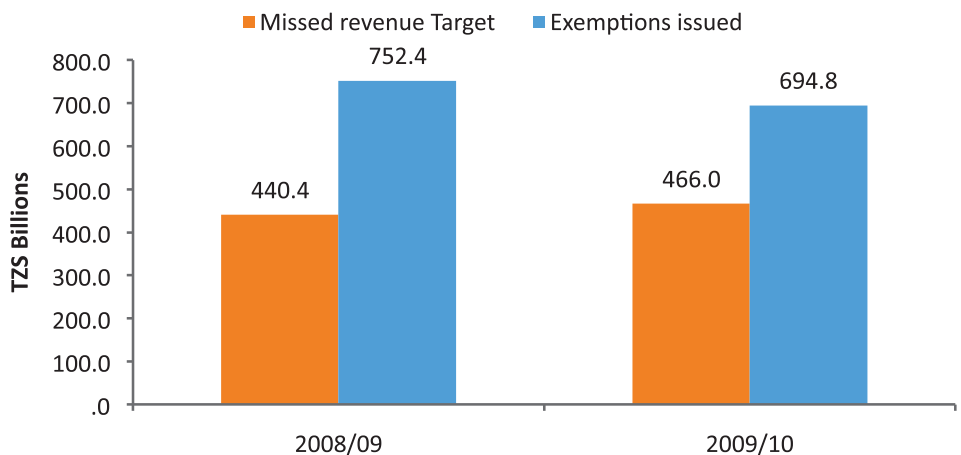
**Source of data:** Tanzania Revenue Authority (TRA) revenue reports

### **Fact 2: Tanzania grants more tax exemptions compared to its neighbours**

The level of tax exemptions in Tanzania is high. This can be seen by comparing the level of exemptions granted in Tanzania with that in Uganda and Kenya. In Tanzania, between 2005/6 and 2007/08 tax exemptions averaged 3.9 percent of GDP. In 2008/9 tax exemptions were 2.8 percent of GDP and in 2009/10, 2.3 percent. In comparison, in Kenya and Uganda exemptions amounted to 1 percent and 0.4 percent of GDP respectively.<sup>4</sup> If Tanzania would harmonize its tax exemptions with the level achieved in Kenya, more than TZS 600 billion would have been saved in 2007/08 alone.

The significance of the amount granted in exemptions can be illustrated by comparing it to missed tax revenue targets. In 2008/09 and 2009/10 the Government missed its revenue target by TZS 453 billion on average. In the same period, tax exemptions granted averaged TZS 724 billion per year. If tax exemptions had been brought in line with the level of exemptions granted in Kenya, TZS 484 billion would have been saved in 2008/9 and TZS 302 billion in 2009/10. In other words, the shortfall in revenue collection would have been largely offset.

**Figure 2: Missed revenue target vs. amount of exemptions granted in 2008/09-2009/10**

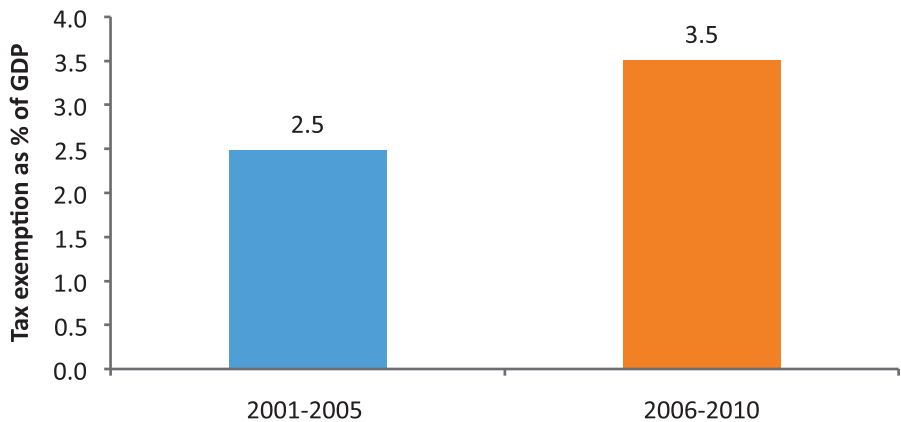


**Source of data:** Tanzania Revenue Authority revenue reports

**Fact 3: Under President Kikwete exemptions have grown rapidly**

A significant growth in tax exemptions occurred in the last five years. During President Kikwete’s five year term (2006-2010), tax exemptions were about 1 percent of GDP (or 40 percent) higher than during President Mkapa’s second five year term (2001-2005).

**Figure 3: Tax exemptions in President Kikwete’s first term vs. exemptions in President Mkapa’s last term**



**Source of data:** Tanzania Revenue Authority revenue reports

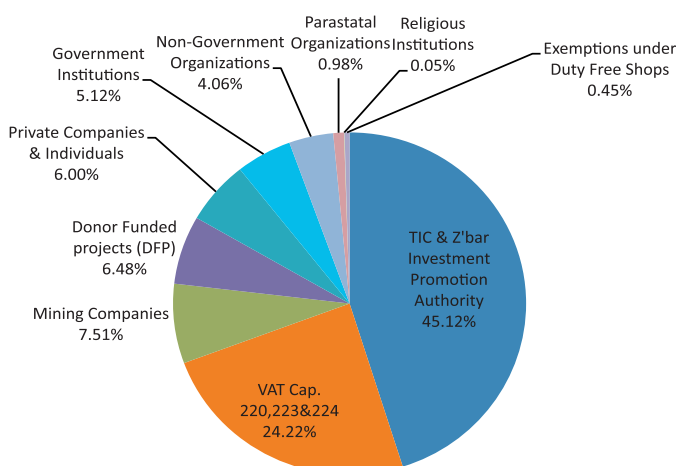
**Fact 4: Large, multi-national investors receive most exemptions**

TRA revenue reports show that a wide range of items and organizations are tax exempt. Three groups gain most of the exemptions. These are companies with certificates of incentives provided under the Tanzanian Investment Act and Zanzibar Investment Promotion and Protection Act; recipients of Value Added Tax exemptions under Cap. 220, 223 and 224; and mining companies under the Mining Act. At the bottom of the list

of beneficiaries are purchases made at duty free shops and import related exemptions granted to religious institutions.

Most of the exemptions granted through the investment promotion agencies, as well as those granted to mining companies accrue to multinational companies.

**Figure 4: Exemptions granted in 2008/09-2009/10 by recipient category**

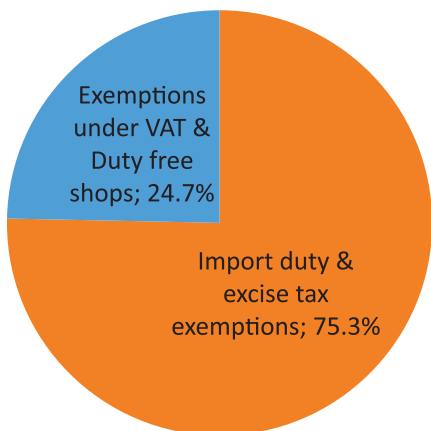


**Source of data:** Tanzania Revenue Authority revenue reports

**Fact 5: Exemptions on imported goods constitute 75% of all exemptions**

Exemptions processed by the TRA fall into two main categories: exemptions on customs related taxes (import duty and excise taxes) and exemptions under the Value Added Tax (VAT) codes. In the last two years, import taxes and excises on imports have constituted the bulk of tax exemptions. On the other hand, VAT and tax exemptions permitted by way of purchases from duty free shops together made up 25 percent of all the exemptions granted in the last two years.

**Figure 5: Exemption types by shares in the last 2 years (2009-10)**

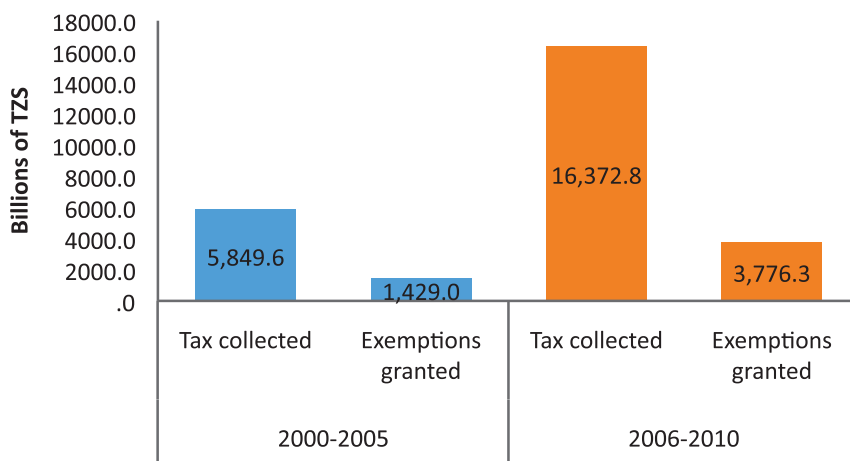


**Source of data:** Tanzania Revenue Authority revenue reports

### Fact 6: Zanzibar grants twice as much in exemptions as Mainland

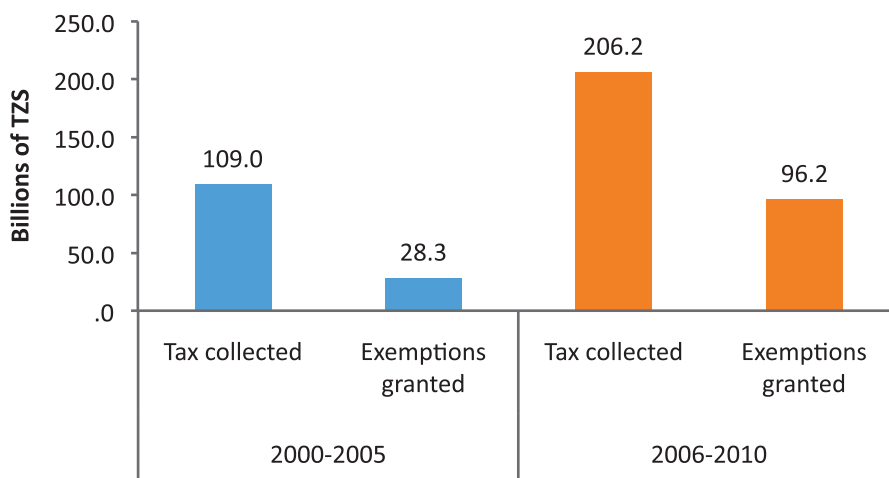
Tax exemptions are processed on both sides of the Union. As Figure 6.1 and 6.2 demonstrate amounts granted in tax exemptions have grown considerably in both the Mainland and Zanzibar. However, as a proportion of revenue collected, tax exemptions have increased particularly rapidly in Zanzibar. In the period 2006-2010 tax exemptions granted in Zanzibar were close to 46 percent of revenue collected, compared to 26 percent in the period from 2001 to 2005. On the other hand, exemptions issued by TRA Mainland were about 23-24 percent of revenue collected throughout that period.

**Figure 6.1: Tax collected and exemptions granted: Tanzania Mainland**



**Source of data:** Tanzania Revenue Authority revenue reports

**Figure 6.2: Tax collected and exemptions granted: Zanzibar**

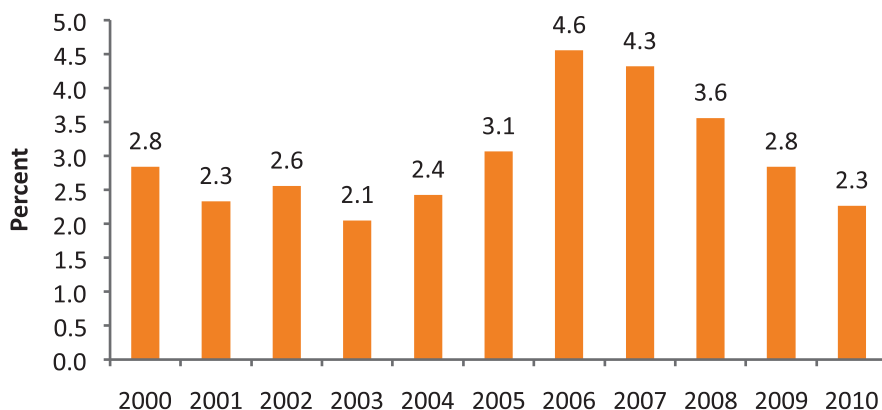


**Source of data:** Tanzania Revenue Authority revenue reports

### Fact 7: Exemptions have started to decline

The Government, through the Minister for Finance, has indicated that it would like to reduce tax exemptions. Indeed, tax exemptions have fallen from a peak of TZS 840 billion (or 4.3 percent of GDP) in 2006/07 to TZS 695 billion or 2.3 percent of GDP in 2009/10. Whereas this is a positive development, at 2.3 percent of GDP, tax exemptions in Tanzania are still between 2 and 6 times higher than in Kenya and Uganda.

**Figure 7: Tax exemptions as percent of GDP**



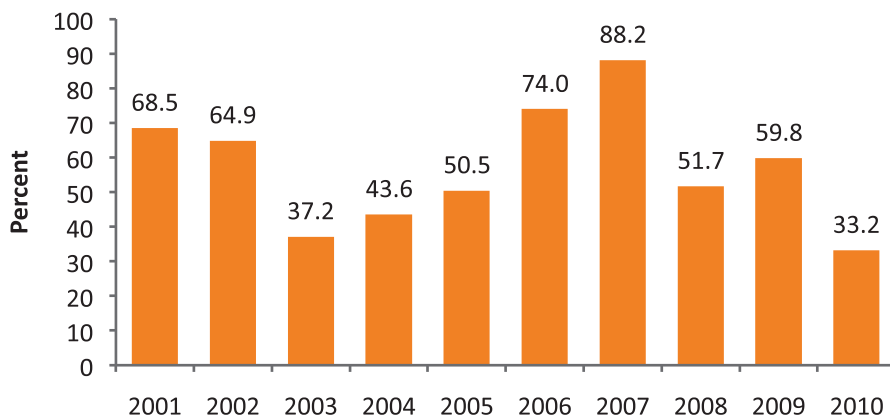
**Source of data:** Tanzania Revenue Authority revenue reports

### Fact 8: Reducing exemptions further would reduce dependence on aid

One reason Tanzania continues to rely heavily on foreign aid is because it fails to raise sufficient revenue. However, by comparing amounts of exemptions granted each year with grants received to fill the resource gap in the budget, it is evident that dependence on aid could be reduced significantly if exemptions were granted more prudently.

At its peak in 2005/06 and 2006/07 the ratio of exemptions to foreign budgetary grants was more than 70 percent. There has been a decline since then mainly as a result of a sharp rise in foreign grants rather than a decline in exemptions. In 2009/10 tax exemptions were estimated to be at 33 percent of the budgetary grants. By reducing the exemptions by 50 percent, the Tanzania Government could reduce its dependence on foreign grants by roughly 16 percent. In terms of public finances, such a reduction would be an impressive accomplishment.

**Figure 8: Tax exemptions as a percent of budgetary grants**



**Source of data:** Tanzania Revenue Authority revenue reports

**Fact 9: Exemptions for NGOs and Large investors declined; but increased for donor funded projects and Government institutions**

Between 2008/9 and 2009/10 the amount granted in tax exemptions declined from TZS 752 billion to TZS 695 billion. Table 1 below shows the change in the amount of exemptions granted across different categories of recipients for the last two years. It shows that the largest reductions were related to imports and involved exemptions to companies with certificates of incentives from the TIC and ZIPA. This is followed by reductions in exemptions for NGOs, and private companies and individuals. At the same time more import related tax exemptions were granted to donor funded projects and government institutions. On local taxes, exemptions under the 3<sup>rd</sup> schedule of the Value Added Tax also increased by a substantial amount.



**Table 1: Tax exemptions by category 2008/09 and 2009/10**

	2008/09	2009/10	Change 2009-2010	
			Actual change (TZS Millions)	% Change
<b>Customs Department</b>				
TIC & ZIPA	380,090.5	272,971.3	(107,119.2)	-28.2
Non-Government Organizations	37,237.8	21,503.0	(15,734.8)	-42.3
Private Companies & Individuals	51,233.4	35,639.7	(15,593.7)	-30.4
Mining	59,140.7	49,588.7	(9,551.9)	-16.2
Religious Institutions	408.0	260.3	(147.7)	-36.2
Parastatal Organizations	7,125.6	7,046.1	(79.5)	-1.1
Regional Trade arrangements	3.0	-	n/a	n/a
Government Institutions	21,617.3	52,481.6	30,864.3	142.8
Donor Funded projects (DFP)	21,552.7	72,257.8	50,705.1	235.3
<b>Sub - Total</b>	<b>578,408.9</b>	<b>511,748.5</b>	<b>(66,657.4)</b>	<b>-11.5</b>
<b>Domestic Revenue Dept. 3<sup>rd</sup> Schedule</b>				
VAT 220	13,249.6	217.0	(13,032.5)	-98.4
Exemptions under Duty Free Shops	3,892.4	2,691.6	(1,200.8)	-30.8
Exemptions under VAT 223/224	156,847.9	180,192.6	23,344.6	14.9
<b>Sub - Total</b>	<b>173,989.9</b>	<b>183,101.2</b>	<b>9,111.3</b>	<b>5.2</b>
<b>GRAND TOTAL</b>	<b>752,398.8</b>	<b>694,849.7</b>	<b>(57,546.1)</b>	<b>-7.6</b>

**Source of data:** Tanzania Revenue Authority revenue reports

#### 4. Once granted, tax exemptions are hard to revoke

Tax exemptions are privileges permissible by law. It means that before exemptions can be granted or claimed a law is needed to identify which categories of individuals, organizations or products are exempt from taxes. Once in place, these privileges are hard to revoke as the beneficiaries are likely to lobby for their continuity. Recent attempts by the Government of Tanzania to do so have shown how difficult it is to undo existing tax exemptions:

- During 2009/10 an attempt to revoke VAT special relief to charities, religious organizations and NGOs, citing its abuse to back up the proposed measure, was heavily criticized by religious leaders, leading to a media outcry and eventual rejection by Parliament.

- In 2009/10 the Government made a change in the tax laws to revoke the practice of classifying certain goods intended for use in specific investments as “deemed capital goods” for the purpose of claiming tax relief by investors. In 2010/11, the practice was reinstated.
- In 2009/10 the Government introduced changes in tax laws to revoke Government Notice No. 99 of 2005 that granted partial fuel levy exemptions to mining companies. Still it had to enter into negotiations with some investors before the revoked law could be applied on them since their Mining Development Agreements with the Government included specific provisions to grant them such exemptions.

These cases suggest that a prudent way for Tanzania to stem the amount in tax exemptions is by being extremely careful in granting these exemptions in the first place. And, where granted, exemptions could be time bound without option for extension.

## 5. Conclusion

One reason why Tanzania has remained both heavily aid dependent and unable to invest faster in its own development is because of its low domestic revenue collections. This brief has shown that tax exemptions in Tanzania (both Mainland and Zanzibar) are generous relative to its neighbors Kenya and Uganda and largely benefit large scale investors with certificates of incentives from investment promotion centers.

Becoming self sustaining in resources is priority for the Government, and could be supported by granting exemptions more prudently. This can be achieved by:

- Reviewing various laws granting exemptions;
- Introducing new exemptions less liberally and making them time bound; and,
- Improving enforcement.

Moreover, it is not possible at the moment to establish how such high levels of exemptions benefit Tanzania. With more transparency, for example by consistently disclosing individual exempt companies and exemptions amounts granted on the internet, such analyses may be possible. This kind of information is at present not fully available to the public, even though tax exemptions are just another form of Government ‘*expenditure*’. Just like expenses on health, water or education, tax exemptions should be subject to the scrutiny of Parliament and taxpayers.

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(Endnotes)

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## Notes

- <sup>1</sup> All tables and charts are based on data obtained from the Tanzania Revenue Authority (TRA), revenue reports 1997/98-2009/10.
- <sup>2</sup> A list of tax exemptions can be found on the Ministry of Finance website for Tanzania (<http://www.mof.go.tz/>)
- <sup>3</sup> All data is presented in fiscal years. For example, 2005 stands for fiscal year 2004/05
- <sup>4</sup> Maliyamkono T, Mason H., Ndunguru, A., Osoro N. E., & Ryder, A., (2009). Why Pay Tax? Dar es Salaam, Tema Publishers and Siyaya Publishing (Pty) Ltd.

