Commentary

Overall review of the Finance Minister's speech

Agriculture is the key focus – "Kilimo Kwanza"!

Adverse changes for the Mining sector in relation to taxes on fuel and VAT.

VAT rate reduced to 18%, but concern over treatment of leased residential buildings.

7.5%increase in specific excise tariffs on alcohol, tobacco, carbonated drinks.

Significant revenue shortfall projected in the year to June 2009.

Abolition of 405 Government Notices granting exemptions.

The global financial crisis provided the backdrop to this year's Budget speech with the most affected sectors identified as agriculture, mining and tourism, as well as manufacturing.

Agriculture was a particular focus with a Budget theme / motto of "Agriculture First" (or as spoken in Kiswahili "Kilimo Kwanza" for better alliterative effect). Measures mentioned included the following:

- A 30% increase in the budgetary expenditure allocation, to cover various initiatives including a drive to ensure timely availability of agricultural inputs, strengthening of the Strategic Grain Reserve, as well as improvement of the rural road network, of irrigation infrastructure and of storage facilities.
- A number of measures to redress adverse impacts of the global economic crisis, for example compensation of losses incurred by crop buyers such as in the cotton sector.
- A reduction of the cap / ceiling on cess (a local Government tax) to 3% from the current 5%, to take effect from 2010/2011.
- A number of VAT and customs duty changes to promote the dairy sector.

There was also explicit recognition of the need to identify and survey land for large scale food crop farming to take advantage of the existing opportunity in terms of local and world market demand.

Notwithstanding the dramatic downturn in the global mining climate, there was no good news for the mining sector with a number of adverse fiscal measures announced including:

- Removal of VAT special relief given to the mining sector, which will now be limited to cover only prospecting and exploration activities only. This relief was never an exemption in the sense of the Government giving up tax that it could use, but merely a means of mitigating cash-flow costs for mining companies that otherwise arise when VAT is paid on inputs, and then has to be refunded. The changes made, which will increase the VAT refunds to the sector, will

adversely affect the cash-flow position of mining companies.

- Abolition of exemption of taxes on fuel for mining companies, other than fuel levy exemptions in existing Mining Development Agreements (in the case of which it is stated that the Government intends to enter into a dialogue with the mining companies with the aim of amending the agreements to remove such exemptions). The implication from the speech appears to be that excise duty (unlike fuel levy) is not protected by such agreements – something that may be a matter for debate. The overall economic concern with loading these additional tax costs is that it will discourage the exploitation of more marginal ore bodies. Irrespective of this, one would have thought that as a minimum an exemption would still apply for fuel used to generate power, a cost only incurred in the case of lack of infrastructure to connect to the grid, something that is no fault of the relevant mine.

For tourism, there was mixed news. Adverse changes include the removal of the VAT exemption on air charters. This sector will also be particularly affected by the removal of the notion of "deemed capital goods", something that had enabled the industry in the past to import free of import duty and VAT a significant amount of material required for setting up tourism facilities such as hotels. On the plus side, there is the removal of import duty from 4 wheel drive vehicles specifically designed and built for tourist purposes, and some rationalisation in relation to visa costs.

One of the major announcements in this year's Budget was the reduction of the standard VAT rate from 20% to 18%. This will be appreciated by manufacturers selling into the domestic market, who will also be relieved that the increase in specific excise duties is no higher than 7.5%, stated to be the average inflation rate during the period. Certain sectors of manufacturing will benefit from reductions in customs duties on various inputs.

Other sectors to benefit from the VAT rate reduction will be businesses that make VAT exempt supplies - such as banks, insurance companies, and fuel retailers – as these businesses can not recover VAT input costs. So any reduction in VAT is a real reduction in their costs.

For most transactions, VAT is a tax only on the ultimate consumer. So, consumers will be the prime beneficiaries of the reduction. However, for individuals the Budget is a mixed bag. Yes there is a VAT rate reduction, and limited excise duty increases, as well as the removal of import duty on pharmaceuticals. On the other hand, there is no increase in the personal tax brackets. In addition, there will be some anxiety as to the possible adverse impact of changes to the VAT treatment of leased residential buildings as well as in relation to the removal of exemptions for charities and NGOs, particularly given the role played by religious bodies in relation to education and health.

An overriding concern for individuals and businesses is the reliability of projections for macro-economic variables such as inflation, lending rates and the exchange rate – especially, given the experience this year of a

significant revenue shortfall, estimated to be 10% short of target, not to mention a general election on the horizon. In addition, the Minister has confirmed that the Government will borrow significant funds from the domestic market, albeit that it is stated that this will be done on a basis consistent with monetary policy requirements. One cushion for the coming year is the support committed by donors, which will be 30% up on the level of loans and grants in the previous budget. There is also a pledge from the European Union and World Bank to provide additional financing to support agricultural food production.

In terms of revenue shortfall, the greatest deficit has been on Customs and Excise collections (21% down on budget), and whilst there is a commitment given to "continue strengthening supervision and operations in the Customs and Excise department" there is no further articulation of how this objective will be achieved. This is a matter for concern as Customs and Excise collections were also below expectations in the preceding year.

A significant contributor to Government revenues, but an area where there is an acknowledgement of significant evasion, is in relation to fuel. Again here there is a commitment to "strengthen monitoring of fuel import by ensuring flow meters operate all the time" – which begs the question, if the flow meter system has not worked to date, why do we believe it will work now. One controversial initiative for the sector, already much debated, and restated in the Budget speech is the proposal to establish a fuel bonded warehouse using TIPER facilities for bulk importation of fuel, which is seen amongst other things as a means to curb evasion. Before commenting further on this proposal, it would be interesting to know what the practical cost implications are of the introduction of such a system.

In seeking to clamp down on loopholes, the speech announces the immediate abolition of 405 Government notices issued between 1964 and 2005. It is not yet clear what the process will be for publicising the revoked notices, but one suggestion would be to have the relevant notices published on the internet so that taxpayers can assess the implications, if any, for them.

The speech rightly emphasises the importance of infrastructure and makes reference to the planned finalisation of a national policy on Public Private Partnership in order to enable the private sector to participate in infrastructure projects. Hopefully, this will presage a more positive experience and engagement with the private sector on infrastructure projects.

This Budget speech was given against the very challenging background of the global economic crisis. By definition this background has made the whole planning process challenging. Whilst we have queried certain aspects of the proposals, the overall thrust of "Kilimo Kwanza" is one to be supported.

The Economy

Highlights based on speeches by the Minister of Finance and Economic Affairs on 11 June 2009.

Past Performance 2008/09

The economy of Tanzania is estimated to have attained real GDP growth of 7.4% during year 2008 compared with the growth rate of 7.1% attained in year 2007.

The increased growth rates is attributed to an increase in economic activities in the following key sectors: Agriculture (4.6%), Fisheries (5.0%) and Services (8.5%). In addition, significant growth was also observed in communications (20.5%), financial intermediation (11.9%), construction (10.5%) and manufacturing (10%).

The economy has experienced higher inflationary pressure as compared to last year emanating primarily from the rise in food prices. The annual rate of inflation for 2008 was 10.3% as compared to 7% for 2007. The rate of inflation reached 13% by the end of March 2009. Monthly headline food inflation was 18.5% by the end March 2009.

In 2008/09, the Government planned to collect Tshs 4,728.6 billion in domestic revenue. However, due to the global financial and economic crisis, revenue collection by the end of June 2009 is expected to fall short of this target by 10 percent. Total domestic revenue collected to end of March 2009 was Tshs 3,199.1 billion. For 2009/10 domestic revenue collection has been projected at Tshs 5,096 billion equivalent to 16.4% of GDP.

Challenges ahead

Despite achievements in economic growth and revenue collection some challenges remain. These include:

- The effects of the current financial crisis have impacted agriculture, investment, infrastructure and food security leading to a Tshs 1.7 trillion stimulus package. This may entail a reduction in resources available as funds are set aside to cushion the effects of the crisis. In addition to the stimulus package, the government is looking into providing exemptions from various fees and levies. As a result this will reduce the amount of government revenue collected. The impact of this on donor dependency in the future is yet to be determined.
- The present infrastructure challenges leading to a lack of power availability to meet the demands of the economy, which, even at a reduced growth rate, are unlikely to be met by the available generation capacity. This is an issue that will require urgent intervention by Government.
- The execution of the budget faces risks if prices of foodstuffs and overall headline inflation continue to rise.

Budget Objectives 2009/10

The 2008/09 budget will continue to implement national plans as stipulated in the CCM Election Manifesto, National Development Vision 2025 and MKUKUTA. Unlike other years, this year's budget is being implemented during a time of economic and financial crisis. Therefore, in order to mitigate the effects of the crisis on the economy, the budget will focus on improving and supporting the agriculture sector.

The 2009/10 Budget Framework

The 2009/10 budget sets out the following targets:

- GDP growth rate of 5% in 2009;
- Control inflation at below 10% by end of June 2010;
- Contain the supply of M2 based on GDP, inflation and foreign reserves levels;
- To increase domestic revenue from 15.9% (estimated) of GDP in 2008/09 to 16.4% of GDP in 2009/10;
- To base the rate of foreign exchange on the movements in the Inter-Bank Foreign Exchange Market (IFEM);
- To remove institutional barriers in the financial sector particularly with regards to availability of loans to the private sector.

Revenue

The budget policy measures on revenue are focused on domestic revenue collection. For 2009/10 domestic revenue collection has been projected at Tshs 5,096 billion representing an increase of 7% on the 2008/09 target. The specific details of the revenue enhancing measures are set out in our highlights of tax changes.

In total, the budget revenues will be as follows:

	Tshs bn
Domestic Revenue	5,096
Grants and Loans	3,181
Domestic loans	1,082
LGA collections	138
Privatisation Proceeds	15
Total Revenue	9,513

Lowering donor dependence was a key theme in the 2008/09 budget. It was envisaged that recurrent expenditure will be fully funded by domestic revenue. However, due to the economic crisis, the revenue target was not achieved. As a result, alternative financing sources were explored including borrowing from the domestic financial markets. A total of Tshs 559.6 billion worth of bonds were sold in the domestic market.

Donor dependency is expected to grow for the upcoming year due to the economic crisis with an increase in budgeted revenue from grants and loans to comprise of 45% of the total annual budget of 2009/10.

Expenditure

The Government is proposing to spend Tshs 9,513.7 billion in 2010/11 as follows:

	Tshs bn
Recurrent	6,688
Development	2,825
Total Expenditure	9,513

Government expenditure in 2008/09 will focus on:

- Mitigating the impacts of the global economic crisis on the economy;
- Improving productivity in the agriculture and livestock sectors;
- Increasing population with access to clean and safe water;
- Improving water irrigation;
- Improving health and education services;
- Improving infrastructure;
- Developing industries;

- Research and development;
- Continuing decentralisation by devolution;
- Preparations for general elections in 2010.

The expenditure budget has been allocated in the following manner for key areas:

- 18.3% on the education sector;
- 7% on the agriculture sector;
- 11.5% on infrastructure;
- 10.1% on the health sector;
- 3.7% on the water sector;
- 3% on energy and minerals sector.

Global economic crisis

Broadly, the strategy adopted by the Government to address the effects of the crisis includes daily surveillance and supervision of banks conducted by the Bank of Tanzania to detect problems in the banking system and implement prompt remedial actions. Other measures include mobilisation of domestic resources; improving productivity in the agriculture sector to increase food supply and therefore decreased food inflation; and promoting tourism (especially domestic).

Credit and Money Supply

For the year ending December 2008, broad money supply grew at a rate of 29.7% compared to 27% in December 2007. The growth rate of extended broad money supply (M3) was 24% in December 2008 compared to 21.4% in December 2007. In March 2009, M2 growth rate was at 14.4% compared to 25.4 % in March 2008. This slowdown in the expansion of monetary aggregates is mainly attributed to slower growth of banks' credit to the private sector and net foreign assets of the banking system. During March 2009, the growth rate of credit was 35.9% compared to 40.2% in the previous year.

The interest rate on government securities declined from 11.4% in December 2007 to 10.99% in December 2008. The lending interest rates offered by commercial banks increased to 16.05% in December 2008 from 15.15% in December 2007.

Balance of Trade

The performance of the external sector was disappointing due to a continued increase in the current account deficit, from US$ 2,041.6 million in 2007 to US$ 2,333.6 million in 2008 representing an increase of 14.3%. The increased deficit was primarily driven by increases in the value of imports of goods and services compared to the value of exports.

The value of merchandise imports increased from US$ 4,860.9 million in 2007 to US$6,439.9 million in 2008 following an increase in importation of manufacturing, communication, transport and construction equipment in line with the growth of economic activities in the communication, transport and manufacturing sectors.

In addition, there was considerable increase (15%) in service receipts in 2008 mainly driven by tourism, transportation and other services. Travel (tourism) and gold receipts continued to dominate the export sector accounting for 27 percent and 18 percent, respectively[1].

Despite the deficit, foreign reserves increased by 3.9 % to US$ 2,869.7 million in 2008, from US$ 2,761. million in 2007. The reserves position in December 2008 was enough to cover 5 months of imports of goods and services.

As at 31 December 2008, the national debt had increased by 7% from US$5,891.1 million in December 2007 to US$ 6,329 million. This is equivalent to 32.6% of total GDP compared to 31.8% in 2007.

[1] Bank of Tanzania, Monthly Economic Review, April 2009

Sector policies and programmes to support budget initiatives

Agriculture, Livestock, Forestry and Hunting

Economic activities in the above areas grew by 4.6% in 2008 compared to 4% in the previous year, boosted by growth in crops; favourable weather conditions in 2007/08; improvement in irrigation and rural road infrastructure; and the fertiliser subsidy scheme.

However, there are general concerns about the slow growth rate of the agriculture sector and the impending drought condition. This will significantly affect the extent to which poverty reduction and food security targets can be met.

The Government proposes a number of measures for 2009/10 to increase productivity and growth in the agricultural sector. These include improvement in irrigation infrastructure and rural roads; implementation of the Agriculture Sector Development Programme (which includes increased use of fertiliser and improved seeds, and the development of crop markets); and containing the adverse effects of the global economic crisis on the sector. Other areas include increasing the quality of products; improving access to credit; increasing availability of farm inputs and reduction of unsustainable forest harvesting.

Fishing

Fishing activities grew by 5% in 2007 compared to 4.5% the previous year. This was attributed to increased control over illegal fishing in Exclusive Economic Zones. However, overall contribution of fishing to total GDP decreased to 1.2% in 2008 compared to 1.3% in 2007

Industry and construction

Mining and quarrying

Mining activities continued a downward trend. In 2008, the sector registered a significant fall in growth from 10.7% in 2007 to an all time low of 2.5% in 2008. Furthermore, the prices of major metals (with the exception of gold) have continued to decline. There have also been cases of postponement of major investment projects for, e.g. a US$3.5 billion aluminium smelting project in Mtwara. This situation is mainly attributed to the global financial crisis. The Government will continue to undertake a number of reforms including a reform of the tax structure.

Manufacturing

The manufacturing sector grew by 9.9% in 2008 compared to 8.7% in 2007. The increase was attributed to sustainability in industrial production particularly for food and dairy products; industrial chemicals; printing; and an overall increase in manufactured exports. Going forward the areas that will receive priority will include enhancement of local manufacturing capacity; value addition; and decrease of export of raw materials.

Construction

In 2008, the construction sector grew at a rate of 10.5% compared to 9.5% in 2007. This was driven by the construction of roads and bridges, residential and non-residential buildings and improvement in water infrastructure.

Recognising the importance of infrastructure for economic growth, the Government has continued to place considerable focus on construction in the upcoming year. As part of this commitment the Government has allocated 11.5% of the 2009/2010 expenditure budget to infrastructure.

Services

Communications

The communication sector grew by 20.5% in 2008 compared to 20.1% in 2007, outpacing all other economic activities. This was due to an overall increase in subscription rates particularly with respect to mobile phones.

Transport

Transport services grew by 6.9% compared to 6.5% the previous year. The increased growth rate was attributed to increase in the volume of road transport cargo and international air passengers. Increased priority will be placed on improving transport infrastructure in addition to creating incentives to attract private sector investment.

Electricity and gas

In 2008, the total contribution by the energy and gas sector to GDP reduced significantly to 5.4% in 2008 compared with 10.9% in 2007. This was attributed to a decline in electricity and gas generation; and the expiration of key contracts such as Dowans, APR and Aggreko.

The medium term strategies include increasing power generation particularly with regards to distribution and increased access in rural areas. In addition, the Government will intensify efforts to establish national oil reserves facilities and expansion of gas production facilities at Songo Songo and Mnazi Bay.

Education

The growth rate in the education sector was 6.9% in 2008 compared to 5.5% in 2007. This increase was mainly a result of the continued implementation of primary and secondary education development programmes, and increased recruitment of teachers.

In the 2009/100 budget education is allocated more funds than any other sector (18.3%) reflecting the Government's understanding that education is the key to economic development.

Health

Health services grew at 9.0% in 2008 compared to 8.8% in 2007. The growth was based on the implementation of vaccination, malaria, tuberculosis, and HIV/AIDS programmes.

In 2009/10 the Government's strategic focus on the health sector will include continued implementation of various public and primary health programmes; strengthening mother and child health services (MCH); and continuing to implement of national HIV/AIDS programmes.

Cross-cutting issues

Aside from the sectoral activities, the Government also plans to undertake significant steps to address several cross-cutting issues that impact on the economy. These include:

- Raising awareness of the 2006 National Population policy (particularly in light of the current 2.9% population growth rate);
- Continuing support of the employment bureau established in 2009 as part of the National Policy for Employment and its Strategy;
- Intensifying democracy by creating linkages between Employment Act CAP 343 and Local Government Act CAP 292. In addition, the Government will intensify efforts to improve the quality of the voter's register;
- Publishing the results of the National Governance and Corruption Survey by the end of June 2009;
- Improving the efficiency of the judiciary sector;
- Implementing the Second Strategy for Preventing HIV/AIDS Infections in 2008 – 2012;
- Developing programmes for empowering women economically, and strengthening gender focal points at all levels;
- Continuing to implement the National Environment Conservation Policy and its strategies.

Conclusion

The budget for 2009/10 will be executed in a period where the global economic crisis has started to take root in developing countries, specifically in Tanzania. The Government is considering several steps to mitigate some of the risks

posed by the above challenges including:

- An economic bailout plan;
- Mobilisation of domestic resources and providing guarantees for loans in the agriculture and SME sectors;
- Enhanced focus on the agriculture sector in general particularly with regards to improved irrigation infrastructure; input supply; market linkages and access to credit;
- Instituting measures to increase the country's attraction to investment and reducing the cost of doing business, for example via infrastructure improvements in key sectors such as power and transportation;
- Increasing overall productivity and competitiveness of the economy.

Overall, the Government is moving in the right direction by investing in areas that will pave the way to sustainable development. However, the success depends on our capacity to implement various initiatives in driving these policies at implementation level. In addition, the increase in dependency on grants and loans as demonstrated in the current budget may further exacerbate our inability to adequately maintain the effects of the global crisis.

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Tax Changes

Highlights based on the Finance Minister's speech

25% income tax rate for companies listed on DSE with at least 30% of shares publicly issued

VAT rate reduced to 18%

Fuel taxes exemption/VAT special relief for mining companies abolished

Lease of residential houses now subject to VAT

Inflationary adjustment to excise duty on alcohol, beer and cigarettes

Income Tax

Surprisingly there is only one change to the Income Tax Act. This is the proposal to reduce the corporate tax rate for companies listed on the Dar es Salaam Stock Exchange (DSE) from 30% to 25%. To qualify, at least 30% of the company's shares must be issued to the public. This change was actually introduced in 2006 but limited to the first three years following listing and applicable to companies having at least 35% shares issued to the public.

This is intended to encourage companies to list on the DSE and broaden their public ownership. However, it is not clear whether this change will apply to newly listed companies only or will also cover the existing companies whose shares are already floated on the DSE. In addition, it is not clear whether the intention is for the new rate of 25% to apply for the first three years as it is at the moment or to apply in perpetuity.

Value Added Tax

Change of rate to 18%

Finally we will see the VAT rate being reduced. The VAT rate has been reduced from 20% to 18%. The reason given for this reduction is to minimise the impact of the global economic crisis on the local economy. Though a lower rate would have been preferred (say 15%), the 18% rate is at least in line with one other EAC country (Uganda). In any case there was considerable pressure on the Minister to reduce the VAT rate as Tanzania had the highest rate in the region and one of the highest in Africa (only Cameroon's was higher!).

The Minister did not elaborate on transitional provisions to achieve a smooth move to the 18% rate. Experience from other jurisdictions shows that there will be a need for detailed transitional provisions (on tax points, credit notes, treatment of continuous supplies of services, deposits, etc) to go hand in hand with the change in rate thereby ensuring that disputes do not arise with the TRA. We therefore hope that such transitional provisions are included in the final legislation.

In a real sense the prices of all VATable goods and services should go down by just under 2% so in theory people should pay less. In the UK, a recent 2.5% VAT rate reduction boosted retail turnover by £2.1bn in the first three

months according to Alistair Darling. However it is unlikely that prices will go down in the short term for several reasons.
Firstly, the change in rate will result in a not insignificant administrative burden for retail businesses having to change their price labels and computer systems, and this will entail some additional cost.

Secondly, the change will have a relatively small impact on prices and many businesses may simply not bother to change their prices. For example on an item currently selling for Tshs 1,200, the VAT rate reduction will theoretically result in the price being reduced to Tshs 1,180 i.e. a change of only Tshs 20.

Thirdly, many businesses are not VAT registered, even when perhaps they should be. So if they are not charging VAT at all then the rate change becomes academic. At the same time however, a lower rate may encourage more businesses to comply and become registered.

Finally, on excisable goods, there is an increase in excise duty so some of the VAT savings will be offset by an increase in excise duty.

Other general changes

Another change is the proposal to start charging VAT on mobile phone services on the face value of the vouchers at source and not on the discounted value at which the vouchers are sold to wholesalers. This proposal is in line with the treatment in Kenya which came in 2006. It remains to be seen whether a similar approach will be taken by the TRA. The key reason is to ensure that there is no VAT leakage on the value added by super dealers.

New exemptions

From an economic efficiency perspective, a moderate VAT rate with a broad consumption base and few exemptions is always preferred to a high rate with many exemptions. Unfortunately we seem to be doing a mixture of the two i.e. we have decreased the VAT rate but keep on increasing the number of exemptions.

The following exemptions have been introduced:

- Heat insulated milk cooling tanks and aluminium jerry cans used for storage and collection of milk in the dairy industry. The aim is to promote their use for hygienic collection of milk thus improving the quality of milk. This also is in line with the import duty exemption and the treatment across EAC countries.
- Farm services of land preparation, cultivation, planting and harvesting. The aim is to reduce production costs in agriculture.
- Stevedoring services for imported cargo in relation to local vessels where VAT has been applied to the stevedoring on initial disembarkment. The stated aim is to encourage importers to use Tanga and Mtwara ports in substitution for Dar es Salaam, but the practical application is a little unclear.

Removal of exemptions

The following exemptions have been abolished:

- Exemption for air charter services (though it is not clear whether this will extend to tourist charters).

- Exemption for processed locally grown tea and coffee. This is a surprise change as it was only introduced in 2004 and 2006 respectively. Although the suppliers will now be able to claim the VAT on their inputs, the prices of these products are nevertheless likely to go up significantly.

- Exemption on electronic cash registers.

- Exemption on leased buildings and serviced apartments (except for lease of residential buildings by the National Housing Corporation and Registrar of Buildings)

  Although the Minister has stated that most residential houses will not be captured as the landlords will not be VAT registered, it only takes someone to lease two residential houses at US$ 1,500 per month each to trigger the need for VAT registration (based on the registration threshold of Tshs 40 million).

  Potentially a number of practical problems might arise:

  - There may be a need to register many new taxable persons before the end of June. This will increase TRA's administration costs, and presumably compliance costs also as it is likely that there will be a degree of evasion in this area.

  - More importantly, the change could easily result in increased rent costs for many people, even where their rent is relatively modest. The key determinant will be whether the landlord is above the VAT threshold, rather than the value of the individual tenant's rent.

  - From a practical perspective, Tanzania currently is the most expensive country in the East African region in terms of leased residential property and this change would appear to only make the situation worse.

It is notable that we have been unable to identify any other country in the world that imposes VAT on residential accommodation.

New special relief

The special relief granted to Tanzania Defence Forces duty free shops has been extended to include all Armed Forces. This will now include police and prison forces.

Removal/Amendment of special relief

The minister has proposed the abolishment or restriction of existing VAT special relief as follows:

- Limiting the special relief provided to water and sewerage authorities to only cover goods and services used for water and sewerage infrastructure development (currently this applies to all goods and services used in the performance of the authority's statutory functions)

- Limiting the special relief given to mining companies to prospecting and exploration activities only. Although this

has no impact on the Government's VAT revenue, the main effect will be to increase the size of VAT refund claims. Given the lengthy delays already experienced in receiving refunds from the TRA, the delays are only likely to get worse.

Bearing in mind that most mining projects rely significantly on bank lending, any delay in receipt of funds will effectively result in extra interest costs. Notwithstanding the law on this matter, TRA are not in the habit of paying interest on late refunds.

The following special reliefs have been abolished:

- Supply of inputs, raw and packaging materials for manufacture of human medicines. This will have an effective operational date of 1 January 2010 and will put pharmaceutical manufactures in a VAT refund position as their products are zero-rated.
- On charitable community-based; or other non-profit driven organisations or institutions and religious organisations. This is likely to impact negatively on these organisations as they are normally not registered for VAT and therefore will not be able to claim the VAT charged on their inputs.
- On deemed capital goods. In the past, goods imported by investors registered under the Tanzania Investment Act for a specific investment project could be deemed as capital goods and therefore entitled to VAT special relief.

Removal of Excise Duty and Road and Fuel Toll (Fuel Levy) Exemptions to Mining companies

The excise duty and road and fuel toll exemptions granted to mining companies have been abolished. For road and fuel toll, the removal will only affect companies entering into a Mining Development Agreement (MDA) with effect from 1 July 2009. The intention however is to also apply the abolition to companies with existing MDAs by means of MDA renegotiation. It is understood that this move is consistent with the recommendations of the Bomani Committee and so may not come as a great surprise to those in the sector. However we have some misgivings about the impact on Tanzania's ability to attract new investment in this sector.

Excise Duty

Mobile phone airtime

The excise duty on mobile phone services will now be charged at the point of sale of scratch cards (vouchers) at their face value unlike currently where it is charged at the point where the actual use of air time occurs.

While this change will strengthen the Government's cashflow position, it is also likely to cause a lot of practical problems and confusion to the mobile phone operators. With the advancement of technology, mobile phone operators now provide many services in addition to airtime (such as data, internet services and money transfers). Many of these services require the use of a common scratch card. The legislation only imposes excise duty on "mobile phone air time" and this raises serious questions such as how the mobile company

is meant to allocate the scratch card value between airtime and other non-excisable services.

Beverages

Excise duty on beverages has been increased in line with average inflation (7.5%).

Goods	Old Rate Tshs Per ltr	New Rate Tshs per ltr
Carbonated soft drinks	54.00	58.00
Clear beer (unmalted barley)	194.00	209.00
Malt Beer	329.00	354.00
Wine with more than 25% imported grapes	1,053.00	1,132.00
Spirits	1,561.00	1,678.00

Cigarettes

Similar to beverages, the rates for cigarettes have also been increased by 7.5%.

Goods	Old Rate Tshs	New Rate Tshs
Cigarettes without filter, containing more than 75% domestic tobacco	5,348 per mil	5,749 per mil
Cigarettes with filter, containing more than 75% domestic tobacco	12,618 per mil	13,564 per mil
Other cigarettes not mentioned above	22,915 per mil	24,633 per mil
Cut rag/filler	11,573 per kg	12,441 per kg

Excise duty on cigars remains at 30%.

Customs Duty

The list below summarises products which will now attract 0% import duty.

- Heat insulated milk cooling tanks for dairy industry
- Industrial spare parts
- Four wheel drive vehicles specially designed and built for tourist purposes
- Equipment and inputs (excluding motor vehicles) imported by a licensed company for direct and exclusive use in oil, gas or geothermal exploration and development
- Raw materials used in the manufacture of sanitary towels and tampons
- Heavy trucks of more than 20 tons under HS code 8704.23.90
- Synthetic yarn
- Pharmaceuticals
- Crude palm oil
- Asbestos fibers of HS codes 6812.8.00 and 8812.99.00 used in manufacture of brake linings and pads
- Television cameras, digital cameras and video camera recorders of HS code 8525.80.00

Other amendments of import duty rates

The Minister has proposed changes to the import duty rates on the following products.

Goods	Old Rate %	New Rate %
Worn clothing	45% or 30 US cents/kg	35% or 20 US cents/kg
Yoghurt and other butter milk of HS codes 0403.10.00 and 0403.90.00	25	60
Light trucks of at least 5 tons under HS code 8704.22.90	25	10

- Import duty remission has been granted on raw materials for use by paper and paperboard mills.
- Tanzania to continue to apply CET rate of 10% instead of 35% applied by other partner states in EAC on wheat grain of HS codes 1001.90.20 and 1001.90.90

Local Government Finance Act

The cap for charging produce cess has been reduced from 5% to 3%.

This change will be welcomed by farmers but will only be implemented in the 2010/2011 fiscal year to enable local governments to look for alternative sources of revenue.

Cancellation of Government Notice tax exemptions

The Minister announced plans to revoke 405 existing Government Notices providing specific tax exemptions to various companies and organisations. Although not explicitly stated, this may only apply to GN's issued prior to 2006. Where a revoked GN is still required, the beneficiary will be required to apply for a new GN in accordance with current laws and procedures. We anticipate that this may not be an easy exercise in practice.

East African Highlights

A synopsis of the salient features in the budget speeches delivered by the Finance Ministers of Kenya, Tanzania, Uganda and Rwanda

East African economies at a glance

Kenya records a decline in economic growth from 7% to 1.7% p.a.

Kenya Constituency Development Funds allocated more money

Tanzania records a 7.4% economic growth rate in 2008

Kenya

The economy experienced a downturn in 2008, growing by 1.7% compared to 7% in 2007. The reduced growth was due to the adverse effects of the events that followed the December 2007 general elections, sharp increase in the international prices of oil and fertiliser and the drought conditions following failed short-rains.

The expected growth for 2009 is only 3% due to the effects of the global recession.

The theme of the 2009/2010 budget is "**Overcoming today's challenges for a better Kenya tomorrow"** and aims at providing economic stimulus. It also provides for more devolution of expenditure compared to prior years, with more funds being channelled through the Constituency Development Fund (CDF). This is aimed at achieving greater equity and increasing the efficiency of spending.

The budget is expansionary, with increased expenditure in infrastructure and social projects. There will be no increase in taxes and the Government expects to finance the shortfall through savings from rationalisation of government expenditure and increased domestic borrowing.

Infrastructure is the key priority area with an allocation of KShs 140 billion, but there are doubts about its absorption.

Tanzania

Agriculture is a key focus area for the 2009/2010 budget with a motto of **"Agriculture First"**. Amongst a number of the measures planned are the allocation of more resources, including agro-inputs and farm implements, and the establishment of an Agricultural Bank.

The economy grew by 7.4% in the calendar year 2008 compared with 7.1% in 2007. However, in view of the current global economic and financial crisis, the Minister projects a reduced growth of 5% for the calendar year 2009. This in line with

Uganda projects a decline in economic growth in 2009/10 to 6% from 7% in the previous year

Rwanda records an impressive 11% economic growth rate in 2008

an IMF projection of a growth of between 5% and 6%.

Uganda

Uganda Government continued to pursue its macro-economic objectives and achieved an economic growth rate of 7% per annum, ensuring a competitive exchange rate and maintaining adequate foreign exchange reserves.

The effects of the global financial crisis are expected to continue in FY 2009/2010 and the growth projection is estimated to be 6%.

Rwanda

This was the first Government budget that conforms to the East Africa Community (EAC) budget calendar.

The economy grew by 11.2% mainly due to good performance in agriculture, growth in the industry sector with improvement in electricity supply and growth in the financial services, transport and logistics sectors.

The current global economic environment is expected to reduce demand for exports such as tea and coffee and reduced income and revenues from tourism.

Key highlights from the Kenya, Uganda, Tanzania and Rwanda economies

Key indicators of the performance of the East African economies are set out below. Where applicable, prior year comparatives have been included in brackets.

	Kenya	**Uganda**	**Tanzania**	**Rwanda**
Real GDP growth	1.7% (7%)	7.0% (8.9%)	7.4% (7.1%)	11.2% (*na)
Inflation				
λ Underlying	9.8% (5.7%)	12.6% (8.6%)	*na	*na
λ Overall	26.07% (9.8%)	13.5% (11.2%)	10.3% (7%)	*na
91 day TB rates	7.3% (6.87%)	7.4% (8.2%)	10.99% (11.4%)	*na
	KShs	*UShs*	*TShs*	*RwF*
Exchange rate to the dollar (Local currency = US$1)	79 (66)	2,216 (1,679)	1,196 (1,244)	577 (589)
Budgeted spend (billions)	865.6 (759.8)	*na (6,143)	9,513 (7,216)	823 (657)
Recurring	606.7 (563.6)	*na (3,372)	6,688 (4,726)	475 (395)
Development	258.9 (196.2)	*na (2,771)	2,825 (2,489)	348 (262)

*Not available

Import duty rates in EAC removed on certain goods

Kenya removes duty on inputs for use by paper manufactures

Tanzania to apply 10% duty on imported wheat

Uganda extends duty exemption on hotel construction

Rwanda introduces three tariff bands for import duty

Customs and Excise

East African Community

There are Common External Tariffs that are applied to goods imported into the EAC. The following are some of the proposals made in respect of these tariffs that are common to all the EAC countries:

- Exemption of import duty on all industrial spare parts to be managed through the duty remission scheme;
- exemption of import duty on all four wheel drive vehicles specially designed for tourist purposes;
- import duty on television cameras, digital cameras and video camera recorders removed;
- Import duty exemption on equipment used in oil, gas or geothermal exploration and development; and
- exemption of import duty on heat insulated milk tanks.

However, there were some changes unique to each of the East Africa Community countries as follows:

Kenya

Import duty on wheat increased from 10% (or US$ 50 per tonne) to 25%.

Import duty on raw materials for manufacture of paper packaging and sanitary towels removed.

Import duty on all synthetic yarns, acrylic yarn, polyester yarn and high ferocity yarn reduced from 10% to 0% in the cotton industry.

Goods, including materials supplies, equipment and motor vehicles for official use in the provision of relief services by the Kenya Committee of Red Cross exempted from duty.

Tanzania

Changes specific to Tanzania to conform to the EAC Customs Management Act and Common External Tariff and as agreed by the EAC Ministers for Finance, include:

- Tanzania to remove the 10% import duty on pharmaceuticals and start applying the CET rate of 0% and
- dispensation to Tanzania to apply a 10% duty rate on imported wheat grain instead of the 35% CET rate.

Uganda

Proposal to extend the exemption of import duty on construction materials for hotels, health and educational institutions for another one year.

Reduction of import duty from 25% to 10% for trucks of a carrying capacity of over five tons, for one year.

Reduction of import duties on trucks of 20 tons or more have been reduced from 20% to 0%.

Rwanda

Excise duty on airtime increased from 3% to 5% as initially agreed with the players in the sector to progressively adjust upwards the rate rather than a one-off shift in the tax rate.

The Government of Rwanda committed to start implementing the EAC Common External Tariff with effect from 1 July 2009. This implies that the customs tariff band will change from four tariff bands to three tariff bands with the highest tariff rate of 25% from 30% for finished products, 10% from 15% for intermediate goods and 0% from 5% raw materials. The 0% for capital equipment will no longer be applicable.

The following tax policy measures have been agreed at the EAC level and have been proposed to in the 2009/2010 budget:

- Remission of Common External Tariff (CET) on wheat grain at 0% for one year;
- CET rate for asbestos fibres reduced from 25% to 0%;
- import duty for yarn reduced from 10% to 0%;
- Rwanda to stay application of CET of 75% on rice and apply a duty rate of 30% for a period of two years;
- import duty reduced from 25% to 10% for trucks of carrying capacity of five tonnes and above for one year;
- import duty reduced from 25% to 0% on trucks of carrying capacity of over 20 tonnes for one year; and
- CET for kerosene stove to be reduced from 25% to 10%

  Exportation of scrap aluminium, steel, copper wires and cables banned.

Generous capital allowances introduced in Kenya

Tax losses in Kenya will now be carried forward for five years only

Excise duty on water reduced from 10% to 5% while on carbonated soft drinks and juices the rate reduced from 10% to 7%.

Mobile phones now zero rated for VAT in Kenya

Direct and indirect taxes

Kenya

Corporate tax

100% investment deduction on capital expenditure incurred by a film producer on purchase of filming equipment.

Wear and tear allowance on telecommunication equipment increased from 12.5% to 20%.

Tax deduction of 5% on computer software.

150% investment allowance on substantial investment in satellite towns around Nairobi, Mombasa and Kisumu.

Tax losses claimable, but not to exceed a five year period, unless approval is provided by the Commissioner.

With the landing of the undersea cables in Kenya, the Minister has proposed that the cost incurred in acquiring the right to use fibre optic cable be offset against taxable income over 20 years.

Personal tax

Tax exempt limit for pension increased from KShs 15,000 to KShs 25,000 per month.

Quarterly filing of PAYE returns in addition to the one filed in February each year.

Excise duty

Excise duty on water reduced from 10% to 5%, while on carbonated soft drinks and juices the rate reduced from 10% to 7%.

Excise duty on spirits changed from KShs 7 per 1% of alcohol to KShs 120 or 65% whichever is higher.

Excise duty on wines changed from KShs 7 per 1% of alcohol to KShs 70 or 50%, whichever is higher.

VAT

The following have been zero rated for VAT purposes:

- Taxable goods and services offered to film producers;
- power generators and generating sets; and
- refrigerated trucks and parts for agricultural, horticultural and forestry machinery.

The following have been exempted from VAT:

- Mobile phone sets and
- financial services, regardless of supplier.

Given the problem faced by traders, VAT withholding agents are now required to issue a VAT withholding certificate to their supplier at the time of making payment.

Claim period for relief of tax paid on goods in stock for newly registered taxpayers for VAT purposes extended from 30 days to six months.

Exporters who qualify for zero rated supplies to get supplies zero rated.

Tanzania

Corporate taxes

Reduction in threshold to qualify for reduced 25% corporate tax rate for companies listed on the Dar es Salaam Stock Exchange – in particular, criterion for qualification is shares issued to the public for at least 30% of share capital (instead of previous 35%).

Personal taxes

No change to individual tax thresholds.

Excise duty

Excise duty rates on non petroleum products have been increased by 7.5%, which was considered to be the average inflation rate for the period.

Abolition of excise duty exemption granted to the mining companies.

VAT

Reduction of the VAT rate from 20% to 18%.

VAT special relief given to mining sector now limited to cover only prospecting and exploration activities.

Removal of the VAT exemption for leased residential buildings (except for leases by NHC and the Registrar of Buildings) and serviced apartments. In addition, VAT exemption on processed tea and tobacco has been removed.

Uganda

Direct taxes

Exemption for all agro processing investments.

Amendment of the Income Tax Act to cater for Petroleum Transactions.

Excise duty

In order to promote growing and malting of barley in Uganda, the Minister has proposed to reduce excise duty on beer produced from barley grown and malted in Uganda from 60% to 40%.

VAT

To ease the challenges associated with counterpart funding, donor funded projects in agriculture, education and health sectors have been exempt from VAT and all VAT arrears relating to these projects are to be written off.

The Minister also proposes to extend the VAT exemption on construction materials for hotels and health and educational institutions for another year.

All lease transactions relating to items that are VAT exempt will also be VAT exempt. Prior to this, the VAT exemption only applied to the outright sale of assets and not to the lease of the same assets.

VAT of 5% applied on sale of houses has been abolished and house sales will be exempted from VAT.

Concept of branchless banking introduced in Kenya

Cost of listing on NSE reduced

Ownership rules for insurance companies amended in Kenya

405 Government licences in Tanzania revoked

Miscellaneous

Kenya

Banking

Proposed amendment to the Kenya Post Office Savings Bank Act to allow Postbank to transact in foreign exchange business in accordance with the CBK rules and regulations.

Branchless banking proposed, where banks will now be able to operate through agencies with wide distribution networks.

Capital markets

Minimum share capital for stock brokers and investment banks to be increased from KShs 5 million and KShs 30 million to KShs 50 million and KShs 250 million respectively.

Institutions under the Capital Markets Authority required to secure professional indemnity insurance.

Withholding tax on interest on bonds maturing within 10 years or more reduced from 15% to 10%.

Listing fee reduced from 0.3% to 0.15% for new public offers of equity.

Stock brokers and investment bankers now required to publish half year financial statements.

Agents restricted to one stock broker.

Insurance

Shareholding by a single person in an insurance company restricted to 25%.

Any person owning more than 20% of the shares in an insurance company restricted from day to day management of the company.

Tax on life business now based on the sum of the recommended surplus to be transferred arising from an actuarial valuation less any previous actuarial deficits. It also now excludes the 30% 'excess' management expenses that was previously chargeable.

Other

Sugar development levy on industrial sugar removed under the duty remission scheme.

Ban on exportation of scrap aluminum, steel and copper wires and cables.

Amendment of the penal code proposed to outlaw the operations of pyramid schemes including non-genuine multi-level marketing operations.

Minimum funding for defined benefit schemes increased from 80% to 100% of the value of accrued liabilities.

New investments by pension schemes that receive statutory contributions to be put in Government securities and infrastructure bonds issued by public institutions.

Tanzania

Abolition of the fuel levy exemption for mining companies entering into Mining Development Agreements from 1 July 2009. Government initiating contract negotiations with existing mining companies to remove the specific provisions granting this exemption in existing Mining Development Agreements.

Cap on "cess" (local Government taxes on agriculture) to reduce to 3% from current 5%, but not until 2010/2011.

Revocation of 405 Government notices which grant tax exemptions.

Reduction of visa fees for all categories of visitors to US$50.

Uganda

Total ban on plastic bags as a means for conveyance of goods and liquids is imposed to protect the environment. Six months will be given to the general public to find alternative means of packaging.

Environmental levy on other plastics of 120%.

Imposition of a ban on importation of old computers, freezers and refrigerators. A three month period allowed to enable goods in transit and in bonded warehouses to be cleared.