



The International Growth Centre

Evidence and Lessons from other Countries : An International Perspective

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IGC Zambia focuses on domestic resource mobilisation, public sector

Justification for the re-introduction of Sales Tax



Zambia is losing K9.6 billion annually in VAT refunds to exporters and manufacturers

With VAT there are a lot of fraudulent claims and double claims.



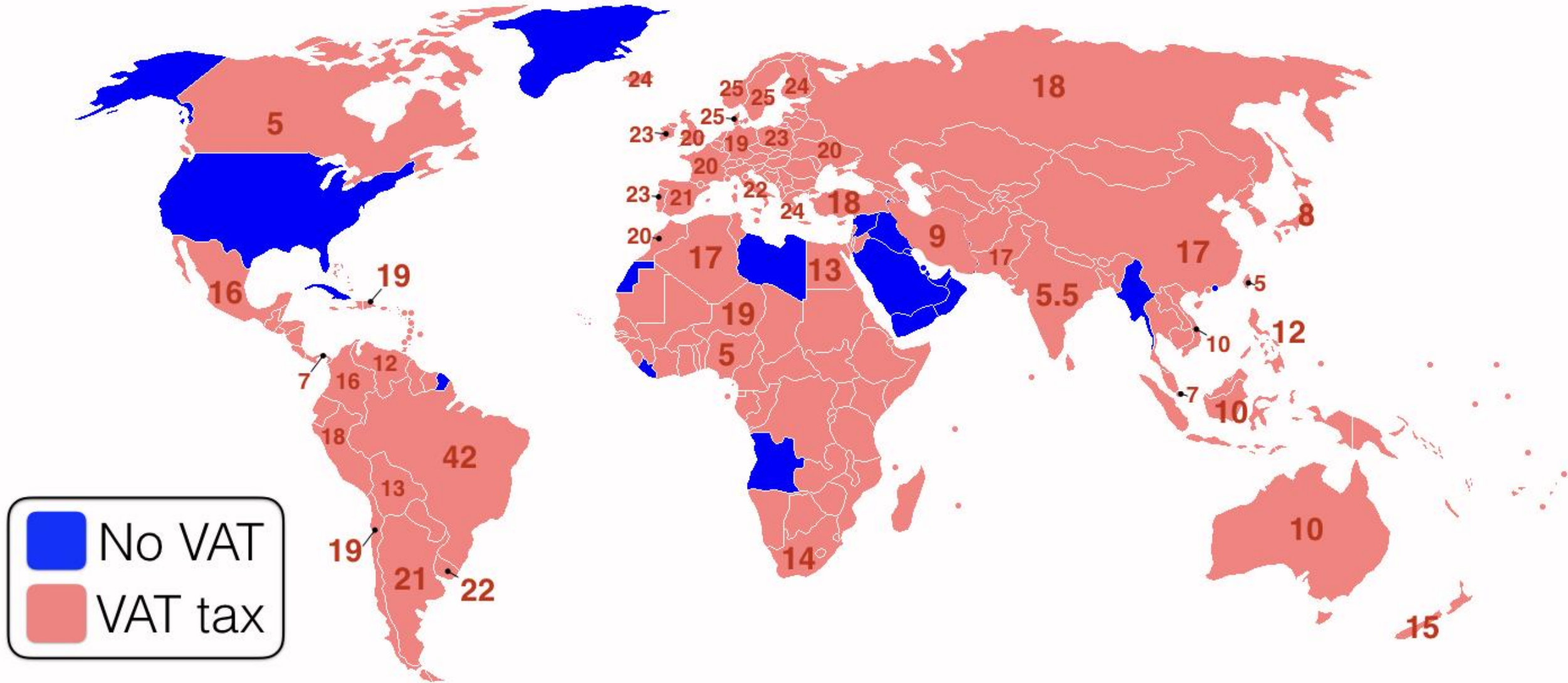
Sales tax will enhance domestic revenue mobilization and minimise revenue leakages.



Will this new tax deliver on this?



VAT around the World



Sales Tax around the world



Small Island states



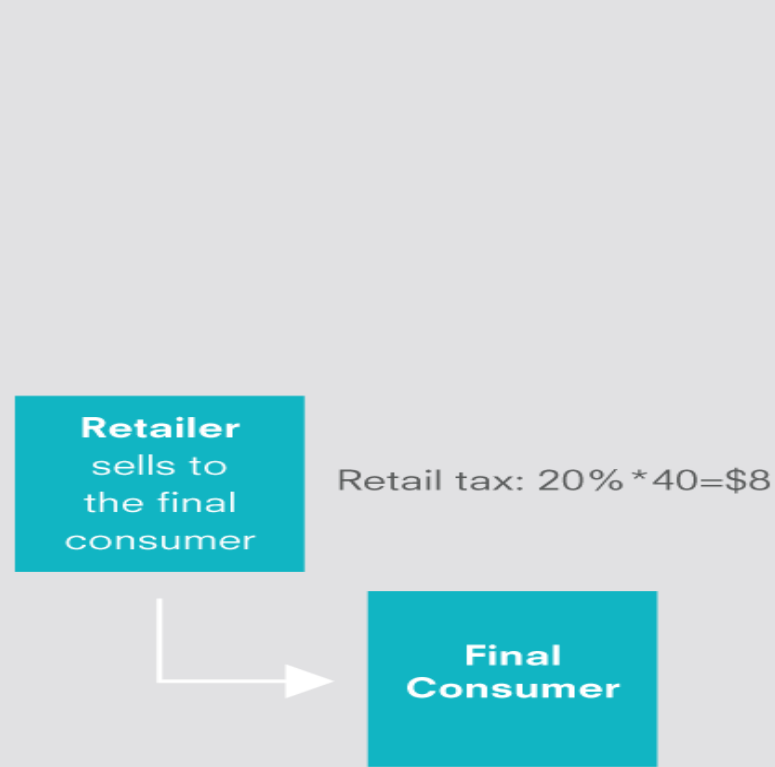
Federalist
Large
Advanced economies



Oil Rich Gulf
States

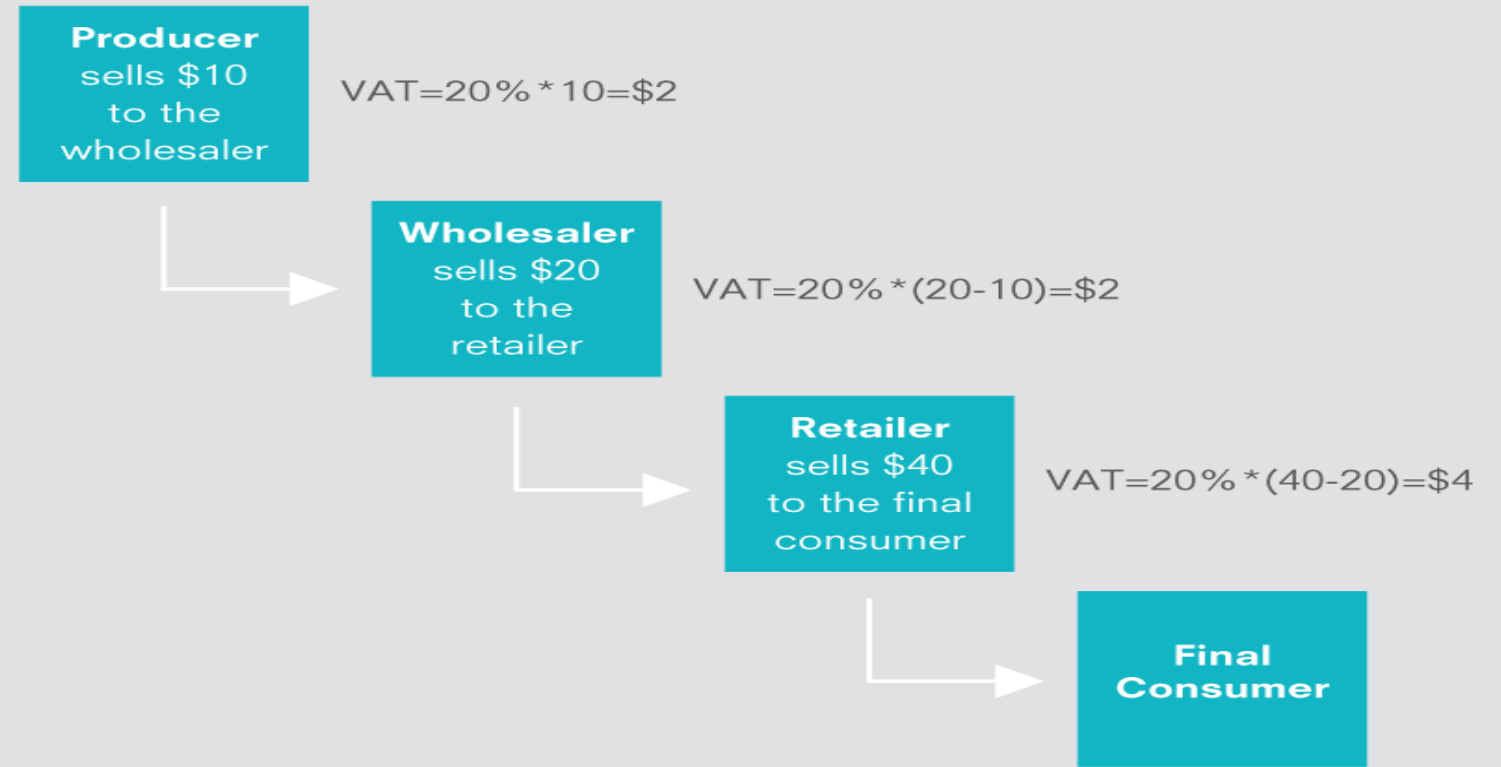
FIGURE 1: RETAIL SALES TAX VS VALUE ADDED TAX

Retail Sales Tax



Total Sales tax $20\% * 40 = \$8$

Value Added Tax



Total VAT $20\% * 10 + 20\% * (10) + 20\% * (20) = \underline{20\% * 40 = \$8}$

The figure illustrates a typical VAT system for a stylised supply chain and a tax rate of 20%. Although a retail sales tax and a VAT are applied differently, they could be equivalent taxes with perfect compliance and no exemptions.

Will Sales Tax enhance revenue mobilisation

Higher Revenue Mobilisation

- VAT has a self enforcing property that leads to higher revenue by creating incentives for B2B transactions.
- Revenue can be mobilised at each point in the chain while with sales tax mobilization is only at the end of the chain.
- Compliance spill over effect.

Lower Tax Evasion

- With VAT the asymmetry between the reporting incentives of suppliers and clients limits room for collusive evasion.
- VAT gives the ZRA the ability to crosscheck the values reported by a firm with records from suppliers and clients upon audit. With Sales tax you can't.

Both systems encounter a last mile problem

- If receipts are not issued to final consumer then revenue will not be collected.
- With VAT only the final payment will be lost with sales tax that is the only point revenue is collected.

Economy wide effects of VAT/Sales tax

VAT has Higher
Production
Efficiency

- VAT does not distort a firm's decisions towards imported or domestically produced goods. (In relation to an import duty)
- Sales tax distorts a firm's decisions towards shorter supply chains due to non deductibility of input tax. –**Keen, M (2016) Taxation and Development Again – IMF working paper**

Sales tax leads
to price
cascading

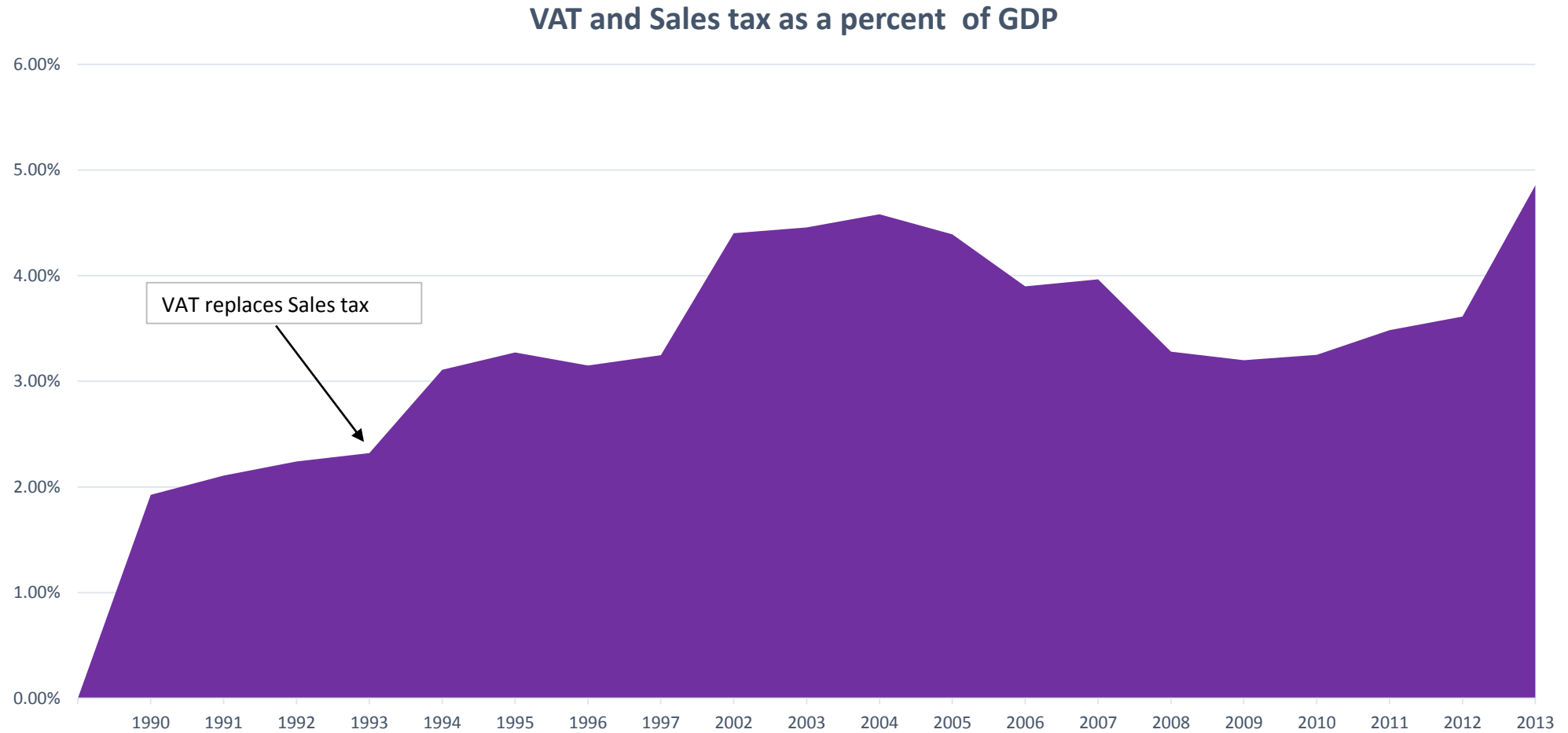
- Due to the non-deductibility of input tax with a sales tax it means that the tax will be built into the price of the product at each stage of the value chain leading to price cascading.

What is the deal with VAT refunds in the Zambia system?



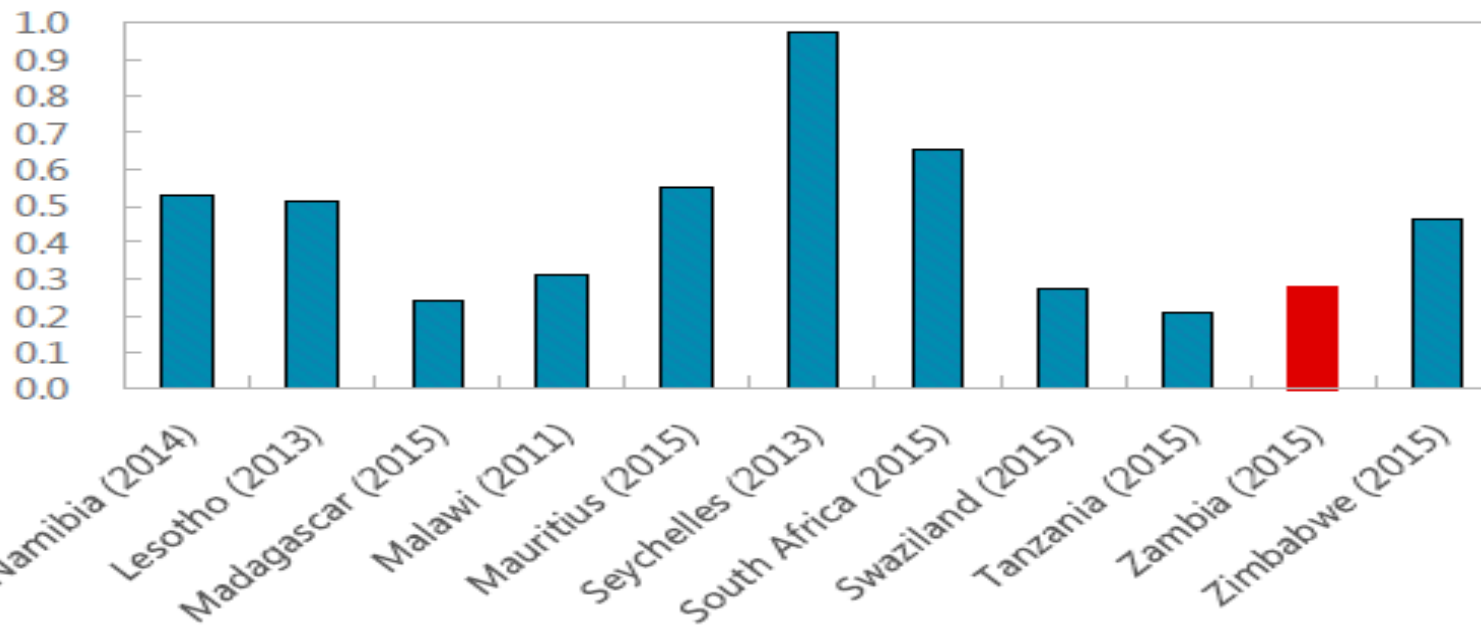
- In Zambia Exports are zero rated for VAT purposes which results in large refunds for export based tax payers such as the mines.

Has VAT underperformed in Zambia?



Has VAT underperformed in Zambia?

Text Figure 3. VAT C-Efficiency SADC Comparators, Latest Year of Actual Data Available



Sources: IMF Fiscal Affairs Department.

Conclusion and Recommendations

- VAT is not perfect and there is vast scope for reform but it is the better system for both revenue mobilization and lowering evasion.
- Technology used in conjunction with research can play a key role in improving the efficiency of VAT.

Thank you!