THE NAMIBIAN TAX CONSORTIUM

REPORT ON TAXATION

IN NAMIBIA

DECEMBER 2002

REPORT OF THE NAMIBIAN TAX CONSORTIUM ON THE TAX STRUCTURE OF NAMBIA

TO THE HONOURABLE MINISTER OF FINANCE

MAY IT PLEASE YOU MR MINISTER:

WE HAVE THE HONOUR TO SUBMIT HEREWITH THE REPORT OF THE CONSORTIUM.

SIGNED AT WINDHOEK, THIS 13th DAY OF DECEMBER 2002

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Summary of Main Recommendations

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1. Source-Based Taxation to be Retained	N/A	12
2. Wealth Tax in the Form of Estate Duty	2005/06	14
3. Introduction of Donations Tax	2004/05	14
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Introduction

The Government of Namibia contracted the Namtax Consortium to conduct a Tax Review in November 2001. The project has been funded by the Swedish International Development Authority (SIDA) and partly by the Government of Namibia. The Consortium is a joint venture between consultants at the University of Namibia and Tax Consulting Services Namibia (Pty) Ltd, a private sector company. Two Swedish experts are also part of the Consortium.

The Consortium wishes to thank the Minister of Finance, the management and staff of Inland Revenue and Customs and Excise for the opportunity to participate in the process of reviewing the tax system.

Terms of Reference

Following the independence of Namibia in 1990, the country's tax system has not undergone a comprehensive revision. We were accordingly asked to review all tax legislation which encompassed the following bodies of legislation:

- Income Tax Act
- Value Added Tax Act
- Petroleum Taxation Act
- Transfer Duty Act
- Stamp Duty Act
- Customs and Excise Duty Act

We were also asked more recently to comment on the new Land Tax as well as the Export Processing Zones or EPZ's.

Our specific terms of reference included:

- Reviewing and assessing the current tax system
- Making the necessary international and regional comparisons
- Addressing the issue of the redistribution of income
- Determining structural changes needed
- Addressing the perceived high rate of tax evasion and / or avoidance
- Reviewing the effectiveness and efficiency of tax administration
- Recommending relevant, practical and feasible options for implementation

Characteristics of the Current Tax System

The main characteristics of the Namibian tax system could be summarised as follows:

- Inherited from South Africa at independence:
  - An income tax levied almost exclusively on labour
  - A source (and deemed source) based income tax
  - A substantial body of decided (mostly S.A.) tax cases
  - A heavy reliance on the Southern African Customs Union (SACU) pool
  - The inability of Namibia to autonomously adjust excise taxes
- One of the best indirect taxes in the form of Value Added Tax (VAT), which was successfully introduced in 2000.
- A vulnerability to commodity prices for mining company revenue (especially diamond mining).

Tax Revenue

Tax revenue expressed as a percentage of GDP has increased from less than 25% of GDP in 1990/91 to 30,5% as an average for the last three years (see Annexure "A"). Of concern however, is the Ministry of Finance's projected decline in tax revenue over the

ensuing years. *Annexure "B"* illustrates the historic tax mix in Namibia, which without much interpretation, reveals the vulnerability to potentially declining SACU revenue, declining revenue from non-mining companies and a potential decrease in tax revenue from mining companies, due to potentially softer commodity prices.

Namibia's tax-to-GDP ratio is within internationally and regionally acceptable limits at around 30%. *Annexure "C"* provides comparative tax-to-GDP ratios in member countries of the Organisation for Economic Co-operation and Development (OECD) and two trading partners in the Southern African Development Community (SADC). Internationally, ratios have been declining in recent years after three decades of increases.

Namibia's "tax mix" for 2001/02 is graphically illustrated in *Annexure "D*", and the data represented below in Table 1 for ease of reference:

Table 1

Namibia: Tax Mix 2001/02

Customs & Excise	33%
VAT	25%
Individuals	23%
Diamond Mining	9%
Non-mining Companies	5%
Mining Companies	2%
NRST	1%
Transfer Duty	1%
Stamp Duty	1%

Customs and Excise duty contributes a large portion of total tax revenues in Namibia. The country's share in the regional pool is however subject to the revenue sharing formulae laid down in the Southern African Customs Union Agreement, which has recently been renegotiated. Whilst Article 26 provides some discretion to Namibia by allowing protection for local infant industries, the SACU system by nature does not enable Namibia to set duties in accordance with its own revenue requirements. Under the

new SACU Agreement, Namibia will have a say in shaping certain policies (e.g. Motor Industries Development Programme, Duty credits and rebates), and as regards the fuel levy already exercises full fiscal jurisdiction. Excise duties are principally determined by South Africa. The scope for the Consortium to therefore recommend improvements in Customs and Excise is therefore directed at Customs administration, where we believe significant improvements can be achieved.

VAT was successfully introduced in 2000 and is functioning well. The amendments in mid 2002 have left no need for any further recommendations from the Consortium.

The individual income tax, which constitutes 23% of revenue, represents an area we believe can be simplified and improved, so that efficiency gains can be utilised to rectify the declining yield from non-mining companies, due largely to inadequate field auditing.

Appendix 1 provides background information, which includes a general macro-economic overview of Namibia as well as highlighting post independence developments in the tax system.

Tax Policy Design

In Appendix 2 we explain some of the guiding principles scholars have recommended when deciding on suitable tax policy. These will not be repeated here. However, as a minimum, we recommend that tax policy changes should:

- Yield significant revenue
- Have a low cost of administration and compliance
- Be simple to understand
- Be equitable
- Support defined political policy objectives (e.g. re-distribution)

Tax Bases

As was illustrated above, Namibia raises revenue in three main ways; through Customs and Excise, VAT and Income Tax. Our Terms of Reference require us to consider whether we should retain, extend or reduce these various forms of taxation in Namibia and we have already indicated the limitation in being able to do so in the case of first, the lack of need for change in the second, and our chosen focus on the tax on individuals in the third, so as to render an overall improvement in the application of the income tax. However, we are also required to consider whether new taxes should be introduced to complement or replace existing ones. We mentioned that Namibia inherited an income tax system that represented a tax almost exclusively on labour income. In this regard, our Terms of Reference require us to consider the re-distributive effects of the system, which have as a backdrop the inequities of the past, evidenced by huge income disparity.

Taxes can be imposed on *income*, *consumption* (VAT and Excise Duties) or on *wealth*. All the objectives of a tax system cannot be satisfied simultaneously and comprehensively by any one tax. The question therefore arises as to whether new taxes are desirable in the first place and secondly, what is practical and achievable. Thirdly, should tax be levied on a world-wide basis or only on Namibian sourced income?

World-Wide (Residence) or Source Basis

Namibia's tax system is currently source-based with various deeming provisions. For example, income earned from work performed in Namibia is taxable in Namibia, regardless of where or by whom payment is made, and interest income received by ordinary residents of Namibia, regardless of where that interest is earned is taxable in Namibia – to cite but two examples. In practice, no country has a pure source or residence system. For all intents and purposes the same result can be achieved by

deeming certain categories of income to be sourced in Namibia, as would be accomplished by having a residence system and then having to exclude certain income.

Changing to a residence system places the taxing country in an internationally competitive arena and requires the taxing country to enforce the tax. Reporting requirements on controlled foreign entities and trying to account for the tax liability of residents via foreign entities, are examples of but two administrative challenges IRD would face. Furthermore, we do not believe that there is a sufficient threat to the Namibian tax base due to the relaxation of exchange controls, which might result in Namibian sourced income leaving the tax net. However, extending the tax base to that of a residence system may have the result that taxpayers vote with their feet – a consideration that has kept many smaller countries (there are about eighty countries on a source-based system) from switching to a residence system. A residence system befits a substantial country confident of being able to apply it.

Having reflected on the experiences of other countries in the region and the simplicity and competitive attractiveness of the source-based system, we recommend that Namibia remain with a source-based system for now. Appendix 3 contains a more detailed argument in support of the recommendation.

Capital Taxes

Income disparities and the appropriate tax treatment of persons with different taxable capacities, call into question the actual and perceived redistributive effects of the tax system.

We have accordingly examined the merits of recommending the introduction of a Capital Gains Tax (CGT), as well as a capital transfer tax on wealth. CGT which is more akin to a tax on income, and a capital transfer tax are not mutually exclusive and do therefore not preclude one another from a policy perspective.

Having examined the revenue yield in various other countries from CGT, over the past twenty years, notwithstanding strong equity markets over the period, the prospect of this complex tax yielding any worthwhile benefit to Namibia in the medium term is doubtful. The Consortium places the most optimistic estimate of revenue to be in the region of N$20 m to N$50 m per annum. This is less than that generated from Stamp Duty. We believe that Namibia should review this in the future, but the introduction of CGT at present will merely serve as a diversionary initiative to IRD, with little benefit, given the more pressing reforms we believe should be introduced.

We however recommend that consideration be given to the introduction of a tax on wealth transfer in the form of an estate duty and a donations tax at a rate of 20% - 25%. The appeal of a wealth tax that is imposed on estates lies with the ability to tax and distribute a percentage of wealth that has accumulated in relatively few hands over many years. A suitably determined abatement in the region of N$1,5m to N$2m per estate would mean that the taxing points were far fewer than they would be if the tax were to be imposed on individual inheritance. Furthermore, the Master's Office's current involvement with the winding up of these estates implies that no more than two staff should be required in IRD to administer an estate duty. Donations tax should not be viewed as a revenue generating tax, but rather as a legislative instrument designed to discourage donations from being made for the purpose of minimizing estate duty.

We have been unable to obtain the necessary information from the Master's Office so as to assess the potential yield that Estate Duty could generate. Further efforts should be made by IRD to try and obtain this information. We recommend that Estate Duty be introduced in 2005/06 and that Donations Tax be imposed as soon as possible, in order to pre-empt fortuitous tax planning by individuals. The basic structure as to how Estate Duty would be computed is set out in Appendix 3.

Deeming Certain Capital Gains as Income

The Income Tax Act specifically excludes "receipts or accruals of a capital nature" in its definition of gross income. There is no definition in the Act of what a "capital nature"

means and this therefore encourages taxpayers to convert or disguise taxable income as tax free capital gains. This is one of the motivating factors used when promoting a CGT.

Changes to the income tax system can be made in order to mitigate the uncertainty in the treatment of the distinction between capital and revenue. This will limit the temptation to engage in conversion transactions or simple non-disclosure.

In this regard, we propose not a capital gains tax per se, but rather a means of dissipating the grey area that exists in trying to distinguish between the capital and income. It is recommended that realised gains from the sale of financial instruments and fixed property (other than a primary residence or business premises, but including farms) be taxed in the hands of all taxpayers, based upon the holding period of the asset. We recommend that the period be twelve months for financial instruments and twenty-four months for fixed property. It is however recommended that retirement funds, life assurance funds and unit trusts be exempted from this provision. These funds are registered for the purposes of managing savings and should be accepted as not being engaged in a scheme for profit making on behalf of their clients.

The above would mean that, for example, the profit or loss on shares sold within a period of 12 months of acquisition, would be incorporated in the ordinary calculation of income tax liability for the taxpayer. We recommend that losses should be allowed, but that they be ring-fenced and only permitted as a set-off against a gain from this source of income. Losses that are not utilized in an applicable tax year should be allowed as a carryover to future years, limited say to a maximum period of seven years.

Dealers in shares or property would be treated in the ordinary course and would not be affected by the above recommendation.

Relief should be granted in certain circumstances, which should include:

a) Death, disability, insolvency or retrenchment

b) Group company transactions (to be defined)
c) Substitution or capitalisation share issues which result in no change in participation rights or payment either directly or indirectly from the taxpayer to the company

We recommend implementation with effect from the 2004/05 tax year.

Income Redistribution and Poverty Relief

Expectations as to the actual and perceived redistributive effects of the tax system have been mentioned above. It is recognised, however, that redistribution is often better achieved by other means, particularly through the expenditure side of the budget, albeit with its own limitations and difficulties. Furthermore, we have taken note of the extensive literature according to which taxes imposed on the rich often do not translate into benefits for the poor, and hence do not address the fundamental objective of creating greater equity.

The Consortium therefore proposes that the government give consideration to furthering a research proposal set out in Appendix 4 which recommends the payment of a small monthly grant to *every* Namibian 6 years old and older, funded by an increase in VAT.

The net effect of such an approach would be the same as paying a progressively higher anti-poverty grant to all Namibians whose monthly per person expenditure is lower than about N$1100, and to progressively tax those with a higher per person monthly expenditure. The automatic targeting achieved by this scheme overcomes all the inefficiencies of traditional poverty relief grants. About N$500 million would be re-distributed annually, targeted at the poorest. The reduction in the disparity of income between individuals brought about by the introduction of this proposal would result in Namibia's Gini coefficient improving from 0,68 to 0,61.

This proposal requires further field research on how best to deploy the technology in order to reach the widely distributed rural population. We believe that foreign donors could be secured to fund the capital expenditure needed for the delivery system. If successful, this will provide Namibia with a modern and secure means of delivering not only the grant to households, but also old age pensions. South Africa is currently giving serious consideration to a similar proposal. The detail regarding this proposal is set out in Appendix 4.

Tax Architecture – Income Tax

Namibia's income tax legislation can be described as a comprehensive income tax for individuals coupled with a company tax for incorporated entities. When considering reforms, we recommend that Namibia should strive to keep its tax system as simple as possible.

IRD made several proposals regarding simplification of the Namibian tax system. We have endorsed a proposal that could be regarded as a conceptual shift from a comprehensive income tax on individuals, to a *schedular* form of taxation for salaried employees, coupled with an expansion of *withholding taxes.* Both these methods of taxation have respectable ancestries and are utilised by developing and developed nations. The OECD member countries have extensively debated the introduction of standardised withholding taxes within their membership. We recommend that Namibia pursue these concepts in future modifications of its tax architecture, beginning with the schedularisation of employment income and a withholding tax on interest income earned by individuals.

Individuals – Income Tax

Tax Scale Design

Annexures "E" &"F" depict personal income tax rates in selected OECD and SADC countries. Namibia's maximum marginal rates are at an acceptable level, with scope regionally to lower rates when compared to countries like Botswana (25%), Angola (15%), Zambia (30%) and Tanzania (30%). There is also scope to provide relief in the lower brackets and to align the maximum marginal rate with the nominal corporate rate (35%). South Africa, for instance, has a scale that is more beneficial to lower income individuals. The current and recommended scales are shown below in Table 2.

Table 2

Tax Scale - Individuals

TAX RATES: 2002/2003			
-	20,000	-	-
20,000	40,000	-	18.0%
40,000	80,000	3,600	30.0%
80,000	200,000	15,600	35.0%
200,000		57,600	36.0%
RECOMMENDED TAX RATES: 2003/2004			
-	24,000	-	0.0%
24,000	40,000	-	17.5%
40,000	80,000	2,800	29.5%
80,000	200,000	14,600	34.5%
200,000		56,000	35.0%

Raising the tax threshold to N$ 24 000, coupled with rate adjustments, result in substantial reductions in tax paid. At N$30 000 p.a. the saving is 41.7%. At N$100 000 p.a. it is 4.9%. *Annexure "G"* illustrates the distribution and extent of the savings in taxes payable.

IRD have modeled the above adjustments and advise that they will not impact on budgeted revenues for 2003/2004. We recommend that the changes be given effect to in 2003/04.

Method of Taxation – Salaried Individuals

Salaried individuals render some 78% of tax returns issued for 2002 by IRD. This indicates where the bulk of staff time is allocated within IRD and also points to the area that can most likely produce an improvement in efficiency so that human resources can be directed towards improving the yield from company taxation.

A *final withholding tax* for salaried individuals is proposed, which is an enhancement of the existing PAYE system. It relieves the individual from having to render a return and it relieve IRD from issuing asessments. This schedular form of taxation on salary income has the following implications:

- Tax would be collected by the employer as with PAYE, but as a final tax.
- The period of assessment would be changed from 12 months to 1 month.
- Certain categories of income, such as director's fees, antedated salaries and lump-sum payments would be taxed on receipt as opposed to accrual.
- No deductions would be allowed against allowances for the private use of assets (e.g. car, phone, home offices). Expenses would instead have to be claimed from the employer by the employee. The employer would in turn claim them as a deduction for the company when computing the tax liability of the business.

This method of taxation should improve revenue yield and provide scope for further reduction in tax rates for individuals.

Individuals engaged in trade, farming or partnerships will be unaffected by this proposal to the extent that they earn non-salary income. We however recommend that directors of all Namibian companies earning salaries be required to pay tax in terms of the schedular proposal. At present only public company directors are subject to PAYE.

The recommendation to move to a schedular system, which is aimed at simplicity, does disturb horizontal equity in the tax system, but its consequent favouritism of

entrepreneurial income is not out of line with policy objectives and recognizes the additional risk that non-salaried individuals entertain.

The details of this proposal are contained in Appendix 5. If the proposal is accepted by government, we recommend that time be allowed for the drafting of legislation in 2003 and that proper consultation with the public be scheduled for 2004. The recommendation could then be introduced in the 2005/06 tax year.

Taxation of Passive Income – Withholding Taxes

Efforts to simplify the tax system by introducing, and in time expanding a schedular method of taxation, raises the question as to how to best deal with passive income earned by individuals, such as interest, dividends and rental income. Dividends are exempted from tax and we do not recommend a change to this policy. Rental income should continue to be dealt with in the ordinary course. However, the largest component of passive income earned by individuals is interest. IRD believe that many taxpayers are not disclosing interest income in their income tax returns and that large scale evasion through non-disclosure is taking place.

We recommend a withholding tax of 10% on interest paid by any financial institution to any individual. In most instances this tax will be final, but non-residents will usually be able to claim a credit in their country of residence for the tax withheld in Namibia. Moreover, resident individuals who are professionals or conducting a business in their own names and who render returns in which the gross interest is declared should be granted a credit when assessed. We further recommend that the N$500 p.a. interest exemption be abolished.

The withholding tax should be payable on the month-end following the lapse of 30 days. We estimate that this measure could raise some N$140 million in revenue in total. If approved, this should be announced in next year's Budget, effective 2004/05.

Nampost Savings Bank / Government Bonds

We support the continuation of the exemption that Government Bonds and the Nampost Savings Bank enjoy, noting that the Nampost funds are bulked and re-deposited into the banking system. Should severe portfolio shifts result over time due to the movement of wholesale funds to Nampost, then the matter should be revisited. The Nampost exemption will cause the fisc to forego N$1,9 million per annum based on current deposits, with a withholding tax rate of 10 %.

Deposit Taking Institutions

It is recommended that all deposit taking institutions be granted time to amend their systems so that they will be in a position to withhold the 10% tax, accounting for it on a per client basis. The timing of the introduction of this measure takes account hereof.

Trust Administrators

Administrators of will trusts and inter-vivos trusts should be required to collect and remit the tax on interest on behalf of the trust or where applicable, the beneficiary, to IRD on a final withholding basis. We recommend the recognition of "*special trusts*" for hardship cases, such as employee benefit trusts and trusts set up for the benefit of orphans and the disabled. (See Appendix 7).

Unit Trusts

Unit trusts are defined as companies for income tax purposes. Namibia has exempted unit trust income in the hands of residents from taxation since 1995, by deeming all income to be dividend income. We believe that this stimulatory measure should now be discontinued and unit trust management companies required to withhold a final tax on interest in the unit holder's account at a rate of 10%. Unit portfolios typically distribute income bi-annually and should be required to remit the proceeds to IRD on the month-end following the lapse of 30 days, as is recommended for all other institutions.

Non-Resident Shareholders Tax

NRST yielded N$ 105 million in revenue in 2001/02. We do not consider this withholding tax to be detrimental to investment in Namibia. Many countries provide a tax credit for NRST paid in other jurisdictions and it can therefore not be considered a final tax. We therefore recommend its continuation.

Companies and Close Corporations – Income Tax

We do not recommend any changes to the principle upon which companies are taxed. We would like to have been in a position to recommend a reduction in the nominal corporate rate of taxation, as we believe there is scope for a downward adjustment from a regional perspective, although the rate is not uncompetitive. Namibia's main trading partner, South Africa, imposes a 30% nominal rate, but Secondary Tax on Companies (STC) increases the tax on fully distributed profits to an effective 37,77%.

The EPZ exemptions and the 18% rate applicable to manufacturers preclude us from recommending any further reductions in the corporate rate at present, as we are concerned about declining corporate revenues. (see Appendix 6)

Tax Avoidance and Evasion

Our Terms of Reference require us to comment on and make recommendations regarding the perception that there is an undue loss of tax revenue in Namibia. These are perceptions and it is difficult to estimate the extent of lost revenue. However, we are of the opinion that some concern is warranted. The proposals to simplify the collection of income tax are directed at improving efficiencies so as to address the lack of enforcement, as we believe that taxes are to a large extent currently reliant on voluntary compliance. This is mentioned under income tax administration and discussed in greater length in Appendix 8. Similarly, our report on Customs administration points to

significant deficiencies in the application of the law, all of which could be contributing to evasion. Based upon other country estimates at our disposal, the extent of the "underground economy" in Namibia could be as high as 20-30% of GDP.

From a legislative perspective, we suggest that measures be introduced to limit transfer pricing by companies and limit the practice whereby international professional partnerships as a consequence of their multi-national make-up, dilute the Namibian income tax liability of local partners. The following recommendations are made:

- That "transfer pricing" legislation be introduced into the Income Tax Act. Furthermore in order to counter the charging of fees by foreign head offices and parent companies a 10% final withholding tax should be imposed on all foreign management fees.
- That "thin capitalisation" legislation be introduced to provide some means for IRD to counter the use of foreign loans to transfer revenues in the guise of interest payments.
- That Namibian partnership profits be ring-fenced for taxation in Namibia. Various solutions to this have been debated with IRD. IRD should after further investigation decide on the method most acceptable.

We recommend that transfer pricing and thin capitalisation legislation be introduced in 2003/04 and the legislation applicable to partnerships in 2005.

Export Processing Zones (EPZ's)

Although not part of our Terms of Reference, we were asked recently to comment on EPZ's as a policy instrument (see Appendix 10). In this regard, we express the view that EPZ's have been successful, but the cost in terms of the revenue foregone (including rates and taxes) needs to be monitored annually. There are also concerns that EPZ's conflict with World Trade Organisation (WTO) and Southern African Development Country (SADC) policy principles, being viewed as a harmful tax practice. International

literature is generally critical of this policy measure, unless the EPZ is situated in a liberal tax jurisdiction. We have already mentioned that this concession inhibits us from recommending further reductions in the corporate tax rate. EPZ's therefore disturb the horizontal equity and by implication impose a heavier burden on other tax payers.

Summary of Other Legislative Recommendations

We summarise hereunder the other proposals dealt with in our appendices:

1. The existing **retirement provisions** for individuals should be reviewed once the current proposals being considered in South Africa have been announced, which is likely to be within the next six months. This will enable a revision with more certainty.
2. **Long Term Life Assurers** – our consultations with the industry reveal that there are product limitations in Namibia compared to what is on offer in South Africa due to that country taxing assurers on a "Four Fund" principle. Namibia should review the need to revise this legislation in the medium term. We do not consider this to be urgent. (See Appendix 7 – Special Classes of Taxpayers)
3. **Mining and Petroleum** taxation – no changes recommended. (Appendix 7)
4. **Farming** – a minor recommendation that the deduction allowed for the erection of employee dwellings be raised from N$15 000 to N$50 000. (Appendix 7)
5. **Trusts** – legislative improvements are recommended, namely that trusts be defined as 'persons', that trusts be taxed at a flat rate – the maximum marginal tax rate, and that the concept of 'special trusts' be introduced in legislation so as to provide hardship relief and the taxing of the special trust as an ordinary person. (Appendix 7)

6. A "**section by section**" analysis of the Income Tax Act was conducted in association with representatives of the accounting profession and IRD. (Included in our compilation of Research Reports prepared by the Consortium). This provides IRD with a checklist of changes and deletions that can be implemented in order to update the Act. We recommend that they be prepared for implementation in 2005/06.
7. **Tax Tribunal** – we recommend the establishment of a tribunal to facilitate dispute resolution, as a speedy and simple means to resolve disputes before they are litigated in court. This could be announced in the 2003/04 Budget. (Appendix 9).
8. **Land Tax** – we recommend that this tax be treated as separate from other taxes and not be allowed as a credit against other tax liabilities. (Appendix 11)
9. **Stamp Duty Act** – we have reviewed the Act in conjunction with IRD and believe that simplification can be achieved by (1) decreasing the number of tariffs in order to decrease the number of denominations of stamps printed and stocked by IRD. (2) Decrease the various items included in the schedules applicable to Marketable Securities Tax. (3) Eliminate many of the exemptions in the Act. These amendments should be ready for introduction in 2005/06 if approved. (Appendix 12)
10. **Transfer Duty Act** – the Act can be simplified and relief provided to purchasers of lower value property. The different rates of tax in respect of Improved Land, Unimproved Land, and Agricultural Land financed by the Agricultural Bank, should be consolidated into one rate scale as follows:

Table 3: Proposed Transfer Duty Scale

Value of Unimproved / Improved Land	**Rates of Tax**
Does not exceed N$100 000	0
Exceeds N$100 000 but not N$200 000	0 + 1% of each N$1

Exceeds N$200 000 but not N$400 000	N$1000 + 5% of the amount over N$200 000
Exceeds N$400 000	N$11000 + 10% of the amount over N$400 000

The above amendments have been accepted by IRD as implementable with effect 2003/04. (Appendix 13)

Income Tax Administration

Findings

Inland Revenue can be described as an administration with high standards in the field of interpretation and administration of tax laws. The workflow has been computerised to a large degree and VAT has been implemented successfully. In addition to this, IRD have taken remarkable steps in the field of customer orientation based upon a Taxpayer Charter of a very high standard, even in an international context. However, there are a number of areas where IRD have been less successful. One is audit. The number of tax audits and the audit competence is very limited and there is no experience in the field of computerised audits. At the same time there is a lack of progressive Human Resources Management, partly due to the restrictions regarding the payment of competitive remuneration in order to attract and keep qualified personnel. In addition to this, there is insufficient use of modern operational management instruments, e.g. planning and follow-up, performance measurement and risk measurement.

Future Focus

In order to promote development towards the desired situation, considerable efforts must be made primarily in the areas of:

- Operational Management
- Tax Audits

- Human Resources Management (HRM).

There are other areas where there is a need for further improvement – e.g. operations and customer orientation – but these efforts appear to be rather limited compared to the need for improvement in the above mentioned areas.

The Challenges

IRD have developed high levels of competence at top management level in the field of interpretation and administration of tax laws. However, there is an apparent shortage of skill and experience with regard to modern management instruments, both operational (Planning and Follow-up, Decentralisation and Accountability, Performance Measurement etc) and non-operational (e.g. Human Resources Management). One challenge is to develop these modern instruments without losing or dramatically reducing the present competence described above.

At the same time, it will not be possible to develop new instruments unless the present relationship between IRD and the MoF is changed in a number of ways. First, there should be a written document making the roles of the two entities very clear. Second, the new instruments require decentralisation of power so that the IRD will be made accountable. This does not mean autonomy on the part of IRD but a considerable change in the present relationship between the two entities. This represents another challenge.

The present shortcomings in the field of tax audit can to some extent be explained by the absence of operational management instruments. However, a more obvious explanation is the lack of human resources management, primarily the inability to pay competitive remuneration in order to attract skilled employees. Therefore, a third challenge is to get the MoF to fund the necessary investments in both skilled expertise and equipment (primarily computers). Against this background it is evident that the majority of future auditors may need to be recruited from the present personnel within IRD. The proposal to

switch to a schedular system for salaried employees should free up assessors who can be trained for this purpose.

The effectiveness and the efficiency of an organisation cannot be achieved solely by improvements in management skills and through the acquisition of a few highly competent auditors. The operational result will primarily be dependent on the way employees are treated, i.e. trained, expected to participate in planning and follow-up, offered different careers and remunerated. The point is that a modern administration must rely on a number of HRM instruments, not only remuneration in order to be effective and efficient. The fourth challenge is to establish an HRM-policy that enables IRD to use and develop the entire capacity of present employees. Employees must feel that they actually represent the most valuable asset of the organisation and that top management is prepared to invest in their future, provided they are willing and capable of undergoing further training in order to meet new qualification demands.

Recommendations

We therefore recommend the establishment of an implementation project. Its manager should work in accordance with specific Terms of Reference from the Government and could be supported by a Steering Group consisting of representatives of the MoF and the taxpayer community. The project would comprise at least three sub-projects dealing with:

- Management
- Tax Audit
- Human Resources Management.

Proposals on how the project should be established are set out in the appendices. (Appendices 14, 15 & 16 are a general report on income tax administration, a proposal on an autonomous Revenue Authority and an implementation plan, which assumes that government may not wish to proceed with an autonomous Revenue Authority immediately.)

We recommend implementation in 2003/04.

Customs and Excise

Background

At the time of independence there was no Customs Administration in Namibia (other than in Walvis Bay). The new government therefore set itself the following objectives:

1. Establishing the infrastructure necessary for the collection of statistics on external trade.
2. The collection of indirect taxes and customs and excise duties on imports, production and consumption.
3. Ensuring proper control over import regimes (prohibitions and restrictions).
4. Automation of clearances of customs entries and trade data collection.

A Customs and Excise Administration has consequently been established with a clear Mission Statement, Guiding Philosophy and Corporate Goals. Primary customs laws have been consolidated into the Customs and Excise Act, No.20 of 1998. Functions have been regionalised with the official designation and servicing of 16 places of entry, 8 Customs and Excise Airports and 13 warehousing places.

Commercial entry clearances are done through the Automated System for Customs Data and Management (ASYCUDA). A human resources base of 440 positions has been established.

Namibia Customs is a member of the World Customs Organisation (WCO) and was elected as Chair for the WCO East and Southern African Region. It has participated in both SACU and the SADC Trade Protocol negotiations and implemented initiatives. It has also implemented trade and tariff preferences under the COTONOU (LOME IV) Agreement and gazetted regulations for the Namibia / Zimbabwe Trade Agreement, the African Growth and Opportunity Act (AGOA) and Export Processing Zones.

Domestically, a Public Awareness Campaign has been launched throughout all Regions, Customer Care Centres have been established and a Service Charter promoted. A Customs Reform and Modernisation Initiative was undertaken with participation of stakeholders and facilitators of the World Customs Organisation.

Approach

When deciding on where improvement in the directorate could most be affected, the Consortium decided that its approach should centre on administrative capacity and procedures. Improvements in administration would render the largest benefit to the fisc in monetary terms.

The Consortium therefore had two auditors experienced in the field of customs administration visit the following sites to perform a sample analysis:

- Windhoek Head Office
- Windhoek Regional Office
- Hosea Kutako International Airport
- Buitepos Border Post (Trans Kalahari)
- Walvis Bay Regional Office, including the harbour and airport.

Findings

Shortcomings were observed in the areas of risk management, qualified manpower, auditing and legal capacities, internal communication, decentralisation of decision making, IT system linkages required by some sections, equipment for cargo inspection and a lack of focus on specialised customs areas.

Challenges

Challenges facing the directorate include operationalising the new SACU Agreement, further implementation of the SADC Trade Protocol instruments, and competent participation in global trade negotiations. The migration to ASYCUDA ++ needs to be

dealt with in a seamless and least disruptive manner, so as not to add to the current shortcomings in on-line system usage identified in our report. Finally, the correction of the weaknesses identified in our findings needs to be urgently addressed.

Recommendations

The detailed findings are included in our Research Report. Appendix 17 provides a summary of the findings and recommendations. We recommend the commencement of an implementation project in 2003/04. We have recommended the establishment of such a project under "Income Tax Administration" and suggest that this initiative be established as a sub-project thereof.