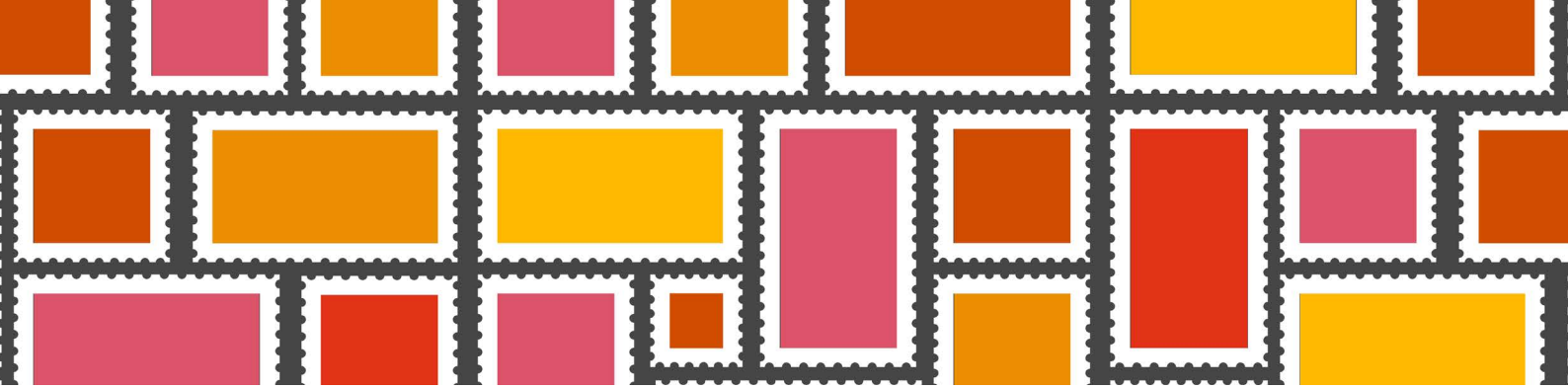




Tax Alert

Pre-Budget Tax Briefing 2: Taxes on Employment

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Get in touch

Rishit Shah

Partner/ Director

E: rishit.shah@pwc.com

 Let's connect on LinkedIn

Mirumbe Mseti

Partner/ Director

E: mirumbe.mseti@pwc.com

 Let's connect on LinkedIn

Aloys Byemerwa

Senior Manager

E: alloys.byemerwa@pwc.com

 Let's connect on LinkedIn

Dharmin Parmar

Manager

E: dharmin.parmar@pwc.com

 Let's connect on LinkedIn

In brief

- **Amendments to rationalise and simplify taxes on employment could:**
 - » Encourage compliance by the informal sector employers (and thereby broaden the tax base), and relieve costs for formal sector employers
 - » Enhance the country's regional competitiveness
- **Specific SDL (and WCF) proposals to consider:**
 - » Rate reduction to 3%, to be allocated two thirds (2%) to VETA, and one third (1%) to WCF (and remove separate WCF contribution)
 - » Exemption for businesses if leviable amount (i.e. total employee remuneration subject to SDL) does not exceed TZS 4 million in a particular month
 - » Filing requirement to be semi-annual (as with PAYE) instead of monthly
 - » Exemption for hospitality sector (until recovery)
- **Other proposals to consider (probably for future Budgets):**
 - » Indexation of PAYE thresholds, and rationalisation of tax rates (three rates instead of four)
 - » In the medium term, consider measures to align social security charges more closely with other countries in the region

Background

Payroll taxes in Tanzania are higher than payroll taxes in most countries including countries in the East African region (see table below). On the other hand, employment activity is predominantly informal¹, so the cost of employment taxes are effectively borne by a small minority.

The number of tax payments and filings related to employment taxes does adversely impact Tanzania's Paying Taxes ranking, being one of the indicators in the World Bank's Doing Business publication. In 2020² Tanzania's overall ranking was 141 (out of 190 countries), up from 144 in 2019; of the ten indicators, the Paying Taxes indicator was the second worst - ranked at 165 out of 190³. One of the contributory factors to the poor ranking is the number of payroll tax payments and filings in Tanzania as compared to other countries.

Currently, businesses are under significant economic pressure, and reviewing measures to cut down costs including reduction of employment costs (through either reducing salaries, retrenchment, etc). In addition to the above, companies in the hospitality sector have been highly impacted by the global pandemic (COVID-19).

As part of the pre-Budget stakeholder engagement process, in February 2021 we sent a pre-Budget submission with certain suggestions on potential tax issues for consideration. This newsletter summarises some of the employment tax issues, and potential changes, that we highlighted.

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Employment Taxes - Regional Comparison

		Tanzania	Kenya	Uganda	Rwanda
Taxes on Employer	Social security - employer contribution	10%	Nominal ⁴	10%	5%
	Skills and Development Levy	4%	N/A	N/A	N/A
	Workers Compensation Fund	1%	N/A	N/A	N/A
	Total taxes - Employer	15%	0%	10%	5%
Taxes on Employee	Income Tax - top marginal rate	30%	30%	40%	30%
	Social security - employee	10%	Nominal	5%	3%
	Total Taxes - Employee	40%	30%	45%	33%
	Total social security contribution	20%	Nominal	15%	8%

Income Tax (Pay As You Earn)

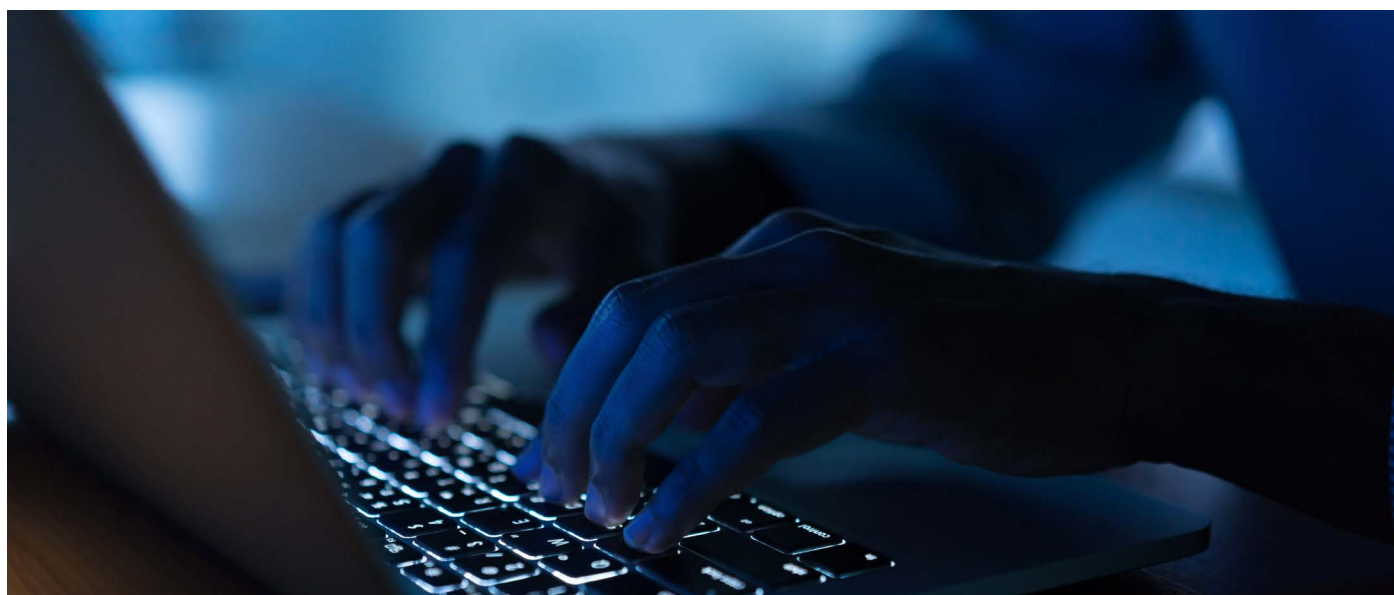
PAYE tax thresholds

If personal tax thresholds are to maintain their real value then these would be subject to an annual adjustment for inflation. However, the tendency has been for such adjustments to be infrequent as highlighted in the table below.

From	Jul 2000 to Jun 2002	Jul 2002 to Jun 2004	Jul 2004 to Jun 2005	Jul 2005 to Jun 2007	Jul 2007 to Jun 2008	Jul 2008 to Jun 2010	Jul 2010 to Jun 2012	Jul 2012 to Jun 2020	Jul 2020 to Date
	TZS	TZS	TZS	TZS	TZS	TZS	TZS	TZS	TZS
Lower Threshold (monthly)	45,000	50,000	60,000	80,000		100,000	135,000	170,000	270,000
Upper Threshold (monthly)	540,000					720,000			1,000,000

Set out below is a comparison - every five years - of the USD equivalent value of these thresholds. It does show that although these changes have been infrequent, the increase in the tax thresholds in July 2020 was quite significant.

	1 Jul 2000	1 Jul 2005	1 Jul 2010	1 Jul 2015	1 Jul 2020
FX rate - USD 1: TZS	799.54	1,127	1,379.62	1,974.31	2,297.53
	USD	USD	USD	USD	USD
Lower Threshold (monthly) - USD equivalent	56	71	98	86	118
Upper Threshold (monthly) - USD equivalent	675	479	522	365	435



Income up to the lower threshold is free of tax (or charged at a 0% rate). For income above this, there are four rates of tax with the highest three rates (20%, 25%, 30% remaining unchanged throughout the period) and the lowest rate (currently 9%⁵). Current tax bands are as follows:

	Bands of taxable income	Taxable income	Tax Rate	Tax on Band	Cumulative tax on income
	TZS	TZS	%	TZS	TZS
First	270,000	270,000	0	0	0
Next	250,000	520,000	9 ⁶	22,500	22,500
Next	240,000	760,000	20	48,000	70,500
Next	240,000	1,000,000	25	60,000	130,500
Over	1,000,000		30		

Consistent with the practice in recent years, it is understood from the President's speech on International Workers' Day that the lowest rate 9% will reduce to 8% from 1 July. Though this lower rate has gradually come down over the years, the practical impact of such a change is limited as the reduction just affects income in a particular band (the first band of income) - accordingly, the recent practice of a periodic 1% reduction in the lowest tax rate affects a band of income of TZS 250,000 and so at most results in a maximum tax reduction of TZS 2,500 per month.

Skills and Development Levy ("SDL")

Every employer with four or more employees is required to account for SDL, calculated as a percentage of "gross monthly emoluments payable by the employer".

SDL rate

In the 2012/2013 budget speech the Minister of Finance committed that the Government would carry out a review on the applicable rate of SDL so as to reduce the tax burden on employers and expand employment opportunities in the country. Consistent with this commitment the rate (previously 6%) reduced to 5% from 1 July 2013, 4.5% from 1 July 2016 and 4% from 1 July 2020. Whilst these reductions were a step in the right direction, more still needs to be done.

By contrast none of the other East African countries highlighted in the table above have an equivalent impost on employment costs. In addition, whilst a number of countries in the SADC region do have such levies, Tanzania's is the highest. A study published in 2020 by the International Labour Organisation titled "A Review of Skills Levy Systems in Countries of the Southern African Development Community"⁷ stated as follows: *"The majority of training levies in the selected SADC countries are based on payroll, with these levies ranging from 0.5 to 4.5 per cent, with the average being 1 per cent. In terms of levy rate, the outlier is the United Republic of Tanzania, with a 4.5 per cent payroll levy"¹⁶.*

SADC skills levy rates (per 2020 ILO study⁸):

Country	Botswana	Malawi	Mauritius ⁹	Namibia	South Africa	Tanzania	Zambia	Zimbabwe
Rate	0.05% - 0.2%	1%	1%-1.5%	1%	1%	4.5% (now 4.0% from 1 July 2020)	0.5%	1.0%
Base	Turnover	Payroll	Payroll	Payroll	Payroll	Payroll	Payroll	Payroll
Levy threshold	USD90,000 [1 million Botswana pula]	None	None	USD 66,000 [1 million Namibian dollars]	USD 33,000 [500,000 South African Rand]	Enterprises with four or more employees	USD 61,000 [800,000 Zambian Kwacha]	None

The ILO report includes the following statement amongst its recommendations: *"The United Republic of Tanzania should consider a levy rate review, ensuring involvement of employers' and workers' organizations centrally in the process. Most SADC training funds are financed via a payroll levy averaging about 1 %; this rate is in line with commonly agreed rates across various countries and regions of the world. However, the Tanzanian levy rate of 4.5 per cent is quite a lot higher than international experience."*¹⁰



Employers exempt from SDL

SDL exemptions¹¹ are currently limited to employers who are:

- Public Sector¹² / International Organisations¹³
- Public Benefit Organisations, in particular: Religious Institutions; Charitable Organisations; Registered Education Institutions
- Agricultural Employers in respect of employees directly and solely engaged in farming (and not in farm management, or in processing of farm products)

By way of illustration, in South Africa in addition to public sector and public benefit organisations, the list of exempt employers includes any employer whose total employee remuneration subject to SDL (leviable amount) over the next 12 month period will not exceed R500 000 (equivalent to roughly TZS 81 million). Though not expressly linked this threshold is half of the mandatory VAT registration threshold in South Africa (R 1 million). As highlighted in the table above several other SADC countries apply a threshold for application of the levy.

One possibility to consider for Tanzania could also be to include an exemption for businesses whose leviable amount (i.e. total employee remuneration subject to SDL) does not exceed a certain amount in a particular month. If 50% of the VAT registration threshold were chosen as a benchmark then this would imply a figure of TZS 50 million per annum - or, if to be applied to a monthly figure (probably more practical) then TZS 4 million per month.

Return filing

In 2015 a monthly filing requirement for SDL was introduced¹⁴. By contrast the requirement for filing PAYE returns is a semi-annual one. It would be better if the SDL filing requirement were aligned with the PAYE requirement - namely, semi-annually instead of monthly.

Workers Compensation Fund (“WCF”)

Since 1 July 2015, all Tanzanian employers have been required to submit a %age of employee wages to the Workers' Compensation Fund (WCF)¹⁵ as follows:

- 1%: private sector employers
- 0.5%: public sector employers

The base for WCF is the same as SDL and similarly is a cost to the employer (not a deduction from the employee). As with SDL, there is an obligation to file a return on a monthly basis. Whilst the objective of WCF is understood, namely providing employees with access to employment injury insurance, the concerns are that the introduction of this impost simply amplifies the challenges highlighted above in relation to SDL.

Summary of concerns

The multiplicity and level of employment taxes has the following major disadvantages:

- Increases the cost for employers in taking on (or keeping on) an employee
- Creates a competitive disadvantage as compared to regional neighbours
- Works against broadening the tax base by discouraging compliance
- Adversely impacts investment rankings such as the World Bank Doing Business ranking.

Way forward

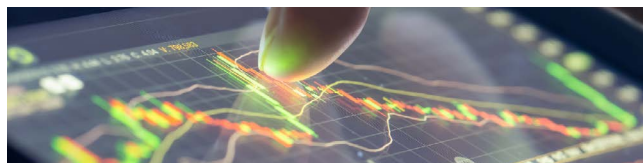
Changes to consider might include some or all of the following:

SDL and WCF

- **SDL**
 - » Reduce SDL rate to 3%, to be allocated two thirds (2%) to VETA, and one third (1%) to WCF.
 - » Exemption for businesses whose leviable amount (i.e. total employee remuneration subject to SDL) does not exceed TZS 4 million in a particular month.
 - » Exemption for companies in the hospitality sector, to continue until such time as the sector can be considered to have recovered from the impact of the pandemic.
 - » Align the filing requirement with the PAYE requirement - namely, semi-annually instead of monthly.
- **WCF:**
 - » Fund WCF through an appropriation of SDL funding (see above) and remove the WCF contribution.

Other:

- **PAYE**
 - » Consider simplification of the number of rates to three (say 10%, 20%, 30%; or even 5%, 15%, 30%) instead of the current four (9%, 20%, 25%, 30%), and if so then an appropriate adjustment of thresholds. Given the announcement of the new 8% rate expected to come into effect from July 2021, it is assumed any further rationalisation of rates (including the number of rates) will await future Budgets.
 - » Adjustment of thresholds to take account of inflation - this may not be practical for this Budget given the significant adjustment made in the 2020 budget, but something to consider in future years.
- **Social Security:**
 - » In the medium term, review the possibility for the rate of total social security contributions to be progressively reduced from the existing 20% to 15% over a time frame to be agreed, and consider the merits of setting a cap on contributions



Appendix

Footnotes

¹ ILO report, referred to in footnote 7 below (and in the narrative in this newsletter on skills and development levy) indicated informal employment in 2014 as 91% of total employment (Tanzania Integrated Labour Force Survey 2014 Analytical Report), significantly higher than other SADC countries (with the exception of Malawi).

² <http://documents1.worldbank.org/curated/en/171871575350897441/pdf/Doing-Business-2020-Comparing-Business-Regulation-in-190-Economies-Economy-Profile-of-Tanzania.pdf>

³ Worst ranked was "Trading across Borders" - 182/190

⁴ For many years the monthly NSSF contribution obligation by employers and employees in Kenya has been 5% of wages, with a standard maximum contribution of KES 200 (c.USD 2) each. A new NSSF Act provides for a higher rate of 6% of earnings, but still with a contribution cap (increased to between KES 360 and KES 1,080 per month); however, implementation of the new Act has been halted by a court case.⁵ Automatic application in cases exceeding USD48m following a change in law in September 2018

⁵ Rate was at 15% from 2007, then reduced to 14%, 13%, 12%, 11% and 9% in 2010, 2013, 2014, 2015 and 2020 respectively

⁶ On the International Workers' Day the President proposed to amend this rate to 8%. We understand that the intention is for this change to take effect from 1 July 2021 once legislated for under the Finance Act 2021

⁷ https://www.ilo.org/wcmsp5/groups/public/---ed_emp/---emp_ent/documents/publication/wcms_753306.pdf

⁸ Refer page 49 of the report

⁹ Mauritius - though rate is between 1% to 1.5%, amount received by fund is 0.5% to 1.0%

¹⁰ This commentary predated the 2020 Budget when the rate (as noted above) reduced to 4% (from 4.5%). Page 39 of the publication when considering the international position globally states: "In terms of the levy amount, 1–2 per cent appears to be a commonly agreed %age across countries and regions (UNESCO 2018a), a range that has remained unchanged for a decade (compare Johanson 2009)"

¹¹ See Section 20, The Vocational Education and Training Act

¹² Including Government departments, public institutions wholly financed by the Government, local government authorities

¹³ Including diplomatic missions, the United Nations and its organisations, international or other foreign institutions dealing with aid or technical assistance

¹⁴ <https://www.pwc.co.tz/assets/pdf/tax-alert-skills-and-development-levy-monthly-return.pdf>

¹⁵ <https://www.pwc.co.tz/assets/pdf/workers-compensation-fund.pdf>

¹⁶ This commentary predated the 2020 Budget when the rate (as noted above) reduced to 4% (from 4.5%).

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