



MINISTRY OF FINANCE, PLANNING AND ECONOMIC DEVELOPMENT

TAX POLICY DEPARTMENT

TAX EXPENDITURE REPORT FY, 2020/21

1.0 Introduction

This is a preliminary report on revenue loss due to tax expenditure in Uganda. The figures indicated in this report are bound to change following obtaining new information from final tax returns for FY 2020/21.

2.0 Definition of Tax Expenditures

Broadly, tax expenditures refer to “revenue losses attributable to provisions in the tax laws which allow special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability.” The justifications are mainly towards support for certain sectors or activities that are deemed to be of strategic importance in stimulating the level of economic activity or social welfare.

The exemptions/incentives constitute a cost to Government since revenue is foregone in the form of tax expenditure. Thus, tax expenditures are alternatives to direct spending programs that accomplish similar objectives. The current categorization of tax expenditures includes;

- i. Tax exemptions embedded in the tax laws;
- ii. Payments of taxes by Government on behalf of investors who are investing in areas deemed strategic by Government;
- iii. Payments of taxes on goods procured by organisations where Government is obliged by Agreement to grant exemption or take responsibility for taxes;
- iv. Religious, Cultural and Nongovernmental organisations whose activities are deemed essential to compliment Government programs.

3.0 Summary of Findings

Table 1 shows estimated revenue foregone on account of tax expenditures for the period FY 2016/17 to FY 2020/21.

Table 1: Revenue foregone for the period FY 2016/17 to FY 2020/21 (UGX billion)

Exemptions Category	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY2020/21
Total income tax Loss	391.85	453.79	1,009.84	851.21	2,358.67
VAT tax expenditures	815.15	1,323.55	1,434.34	1,855.49	2,195.34
Customs Tax Exemptions	960.022	912.456	1,716.37	2,065.15	3,168.51
Total Exemptions	2,167.02	2,689.80	4,160.55	4,771.85	7,722.52
GDP	108,518	120,485	132,096	139,711	148,278
Tax-GDP ratio	2.00%	2.23%	3.15%	3.42%	5.21%

Source: Authors’ calculations from data from URA data warehouse

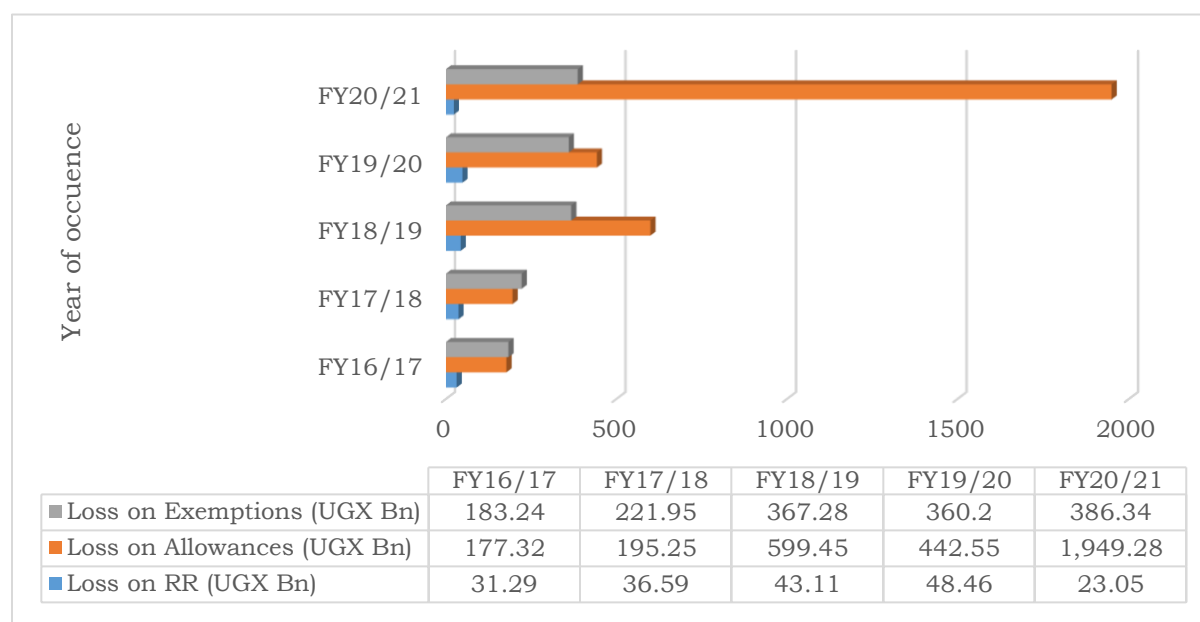
As seen in Table 1, revenue foregone on account of tax expenditures has increased from UGX 2,167.02 billion in FY 2016/17 to UGX 7,722.52 billion in FY 2020/21. As a percentage of GDP, tax expenditures increased from 2.0% to 5.2% over the same period.

4.0 Income taxes exemptions

Included in the tax exemptions calculation as deviations from the benchmark are; exempt income, various income tax holidays, additional allowances and deductions, and lower-than-benchmark withholding tax rates for special sectors. These are quantified, where possible, in the sections below.

The estimated revenue foregone on account of income tax related exemptions, allowable deductions and rate relief are shown in Figure 1.

Figure 1: Total income tax exemptions for the period FY2016/17-FY2019/20



Source: Author's calculations using data from URA data warehouse

Figure 1 indicates a dramatic increase revenue foregone arising from allowances and deductions that increased from UGX 442.55 billion in FY 2019/20 to UGX 1,949.28 billion in FY 2020/21, on account of UGX 3,772.92 billion mortgage interest declared by National Security Fund in FY 2020/21.

4.1 Income tax Exemptions

These comprise of among others; tax exemptions on employment income for specific groups of individuals, non-wage income of Members of Parliament, non-business capital gains, investment and/or rental income of several groups of

firms, and the most recent ten-year tax holidays for business and rental income to investors fulfilling specific criteria. They are either on individuals or corporations as provided in the analysis in Table 2.

Table 2: Revenue foregone from Income Tax Exemptions

EXEMPTIONS	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Employment income of armed forces	60.6	72.72	83.1	95.13	95.13
Incomes of collective investment schemes	0	0.2	0.22	0.75	2.19
Employment incomes of EADB employees	1.48	1.16	0.84	0.82	0.82
Business incomes of new investors in new plants and machinery for agro-processing	3.4	8.72	32.2	5.13	27.98
10-year tax holiday on business income tax for new investors manufacturing finished consumer and capital goods for export.	4.16	19.04	18.45	11.33	4.97
Employment income, other than salary, of a person employed as a Member of Parliament.	102.91	99.77	98.73	126.64	126.64
Income of Bujagali Hydro Power Project	0	0	108.4	100.04	90.74
Business and investment income tax for SACCOs	0.34	1.95	11.37	7.95	25.45
Lumpsum payments from employment income tax	3.84	4.01	4.46	3.44	0
Employment income of private retirement schemes	3.02	13.76	8.21	8.97	11.69
Dividends paid by a publicly traded company.	3.49	0.62	1.3	0	0.73
Total loss from exemptions	183.24	221.95	367.28	360.2	386.34

Source: Author's calculations using data from URA data warehouse.

Revenue foregone due to income tax exemptions increased by 7.3% from UGX 360.20 billion in FY 2019/20 to UGX 386.34 billion in FY 2020/21. The biggest contributors to this revenue foregone are exemptions related to; employment income tax for armed forces personnel, the income of Bujagali Hydro Power Project and employment income other than basic salary for MPs.

4.2 Allowances and Deductions

There include; deductions for interest incurred on mortgages, employing people with disabilities, charitable donations, and employee training exemptions and 'accelerated deducibility' on certain assets. Others include initial allowance on plant and machinery, mineral and petroleum exploration activities and industrial buildings. Table 3 below summarizes the estimated revenue foregone due to allowances and deductions as provided in the income tax law.

The drastic growth in a revenue foregone between FY 2017/18 and FY 2018/19 is attributed to the reinstatement of the provisions for initial allowances on plant and machinery and industrial buildings (outside a 50km radius from Kampala).

In addition, the drastic growth between FY 2019/20 and FY 2020/21 was on account of unusually high declaration of mortgage interests by the NSSF that individually declared interest of UGX 3,772.92 billion in FY 2020/21.

Table 3: Revenue foregone from Income Tax Allowances and Deductions

Allowances	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Interest incurred on mortgage used to acquire or construct premises for rent or leasing	133.71	155.15	337.44	152.74	1,352.79
Charitable donations	1.43	0.9	1.86	1.13	3.32
Accelerated deductibility of initial allowance in respect of plant and machinery.	N/A	N/A	96.09	139.07	328.95
Employee training expenditure	42.17	38.44	61.11	47.57	79.94
Accelerated deductibility of mineral and petroleum exploration expenditure	0.01	0.76	0	0	0.04
Accelerated deductibility of initial allowance in respect of industrial buildings.	N/A	N/A	102.95	102.03	184.23
Total loss from Allowances	177.32	195.25	599.45	442.55	1,949.28

Source: Author's calculations using data from URA data warehouse.

4.3 Rate Reliefs

These include; rate relief on dividends paid by a resident company listed on the stock exchange to a resident shareholder, rate relief on payments for assets by a resident person, rate relief on reinsurance premiums, service fees by mining companies, internet connectivity fees and telecommunication service fees, among others. The estimated revenue foregone due to reduced rates/rate relief reduced to UGX 23.05 billion in FY 2020/21 from UGX 48.46 billion in FY2019/20. This is on account of lower withholding tax rate on payment of service fees by mining and petroleum licensees from UGX 24.42 billion in FY 2019/20 to UGX 6.56 billion in FY 2020/21. The estimated revenue foregone is provided in Table 4.

Table 4: Annual revenue foregone from Income Tax Rate Reliefs

Rate Reliefs	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Lower withholding tax rate on dividends paid by a resident company listed on the stock exchange to a resident stockholder	3.96	0.98	1.56	1.34	1.12
Lower withholding tax rate on payment of reinsurance premiums by a resident insurance company	1.29	2.89	2.78	3.04	2.81
Lower withholding tax rate on payment of service fees by mining and petroleum licensees	11.08	18.748	15.047	24.42	6.56
Lower withholding tax rate on payment of fees for direct-to-home pay-services		0.01	1.28	0.18	0.03
Lower withholding tax rate on payment of fees for internet connectivity services to subscribers in Uganda	1.15	1.61	4.14	6.06	2.42
Lower withholding tax rate on payment of fees by a resident person for telecommunication services	11.11	7.71	10.78	6.65	3.36

Lower withholding tax rate on payment of transportation charges by a resident person to a non-resident	2.7	4.64	7.53	6.77	6.76
Total Income Tax loss (UGX Bn)	31.29	36.59	43.11	48.46	23.05

5.0 Value Added Tax (VAT) tax expenditures

The benchmark VAT rate in Uganda is **18%** of the value of the supply (good or service). There are supplies which are VAT exempt while others are zero-rated. For purposes of this section, the revenue foregone is estimated from zero-rated supplies, exempt supplies, VAT deferrals and deemed supplies.

In FY 2020/21, total tax revenue foregone due to VAT tax expenditures grew by 18.3% to UGX 2,195.34 billion from UGX 1,855.49 billion in FY 2019/20. As a percentage of GDP, the increased to 1.48% from 0.75% over the same period. Table 5 indicates revenue foregone due to VAT tax expenditures.

Table 5: Revenue Foregone due to VAT tax expenditures (UGX billion), FY2016/17 – FY2020/21

	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Exemptions	459.89	737.37	608.88	845.58	1,116.05
Allowances	41.85	153.17	384.69	690.76	776.51
Zero rated supplies	274.13	350.38	376.71	241.03	201.97
Deferrals	39.28	82.63	64.06	78.12	100.81
TOTAL revenue foregone	815.15	1,323.55	1,434.34	1,855.49	2,195.34
GDP at market prices	108,518	120,485	132,096	139,711	148,278
GDP ratio	0.75%	1.10%	1.09%	1.33%	1.48%

Source: Authors' calculations from URA data warehouse

5.1 Value Added Tax Exemptions from Exemptions

The value of revenue foregone due to VAT exemptions increased by 32.0% from UGX 845.58 billion FY 2019/20 to UGX 1,116.05 billion in FY 2020/21, mainly on account of growth in revenue foregone due to EACCMA exemptions. Details are provided in Table 6.

Note: various beneficiaries of VAT exempted supplies do not file VAT returns. Therefore, the revenue foregone due to VAT tax expenditures is potentially higher than what is indicated in Table 6.

Table 6: Revenue foregone from VAT xxemptions, FY 2016/17 – FY 2020/21

EXEMPTION	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Livestock, unprocessed foodstuffs and unprocessed agricultural products.	65.03	66.09	65.04	50.12	60.52
services, inputs, machinery, tools and implements suitable for use only in agriculture.	1.27	7.08	6.41	14.22	17.5
dental, medical, and veterinary goods	23.89	26.87	32.6	158.69	202.31
animal feeds and premises;	2.53	7.15	11.72	32.22	19.03
batteries and lanterns.	0.29	0.02	0.02	0.01	0.07
solar devices and equipment	12.37	14.9	19.44	9.46	9.25
lifejackets, lifesaving gear, headgear & speed governors	1.11	0.94	1.38	1.41	1.66
Supplies to contractors and Subcontractors in energy projects	23.79	25.8	36.95	34.87	31.2
Textile manufacturing operations, equipment and inputs.	0	0.06	14.97	21.02	31.95
production inputs for iron ore smelting, limestone mining and processing, processing of hides and skins	2.8	7.73	8.36	5.81	6.15
All goods categorized as "Exemptions" under the EACCMA	326.79	580.74	412.01	517.75	736.41
Total revenue foregone (UGX)	459.89	737.37	608.88	845.58	1,116.05

Source: Author's calculations using data from URA data warehouse.

5.2 Allowances

This section covers mainly Deemed VAT which comprises of three forms namely;

- i. Deemed VAT payment on supplies by a contractor to a licensee undermining or petroleum operations;
- ii. Deemed VAT on supplies to a contractor executing an aid-funded project; and
- iii. Deemed VAT on supplies by contractors executing aid-funded projects to a government ministry, department or agency.

Details are provided in Table 7.

Table 7: Revenue foregone from VAT Allowances (Deemed VAT)

Allowances	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Standard Rated Sales	41.81	141.42	382.39	684.5	764.03
Capital/Business Assets	0.04	11.75	2.3	6.26	12.48
Total Revenue foregone	41.85	153.17	384.69	690.76	776.51

Source: Authors' calculations using data from the URA data warehouse.

The revenue foregone due to VAT allowances arising from deemed VAT increased by 12.41% from UGX 690.76 billion in FY 2019/20 to UGX 776.51 billion in FY

2020/21, mainly on account of deemed VAT on supplies to contractors implementing Aid funded projects.

5.3 Zero-rated supplies tax expenditures

In FY 2020/21, total VAT revenue foregone due to zero-rated supplies declined by 16.2% to UGX 201.97 billion from UGX 241.03 billion in FY 2019/20, mainly on account of decline in VAT foregone on the supply of drugs and medicines which declined from UGX 157.36 billion to UGX 132.52 billion over the same period. Examples of other zero-rated supplies are; educational materials, agricultural inputs, cereals, handling services, etc.

5.4 Deferrals

The VAT Act provides for ‘*the deferment of VAT payments on the importation of capital equipment (capital and machinery)*’. Revenue foregone on account of this provision increased from UGX 39.28 billion in FY 2016/17 to UGX 100.81 billion in FY 2020/21.

6.0 Customs Duties

Uganda’s taxation of imports is governed by the East African Community Customs Management Act (EACCMA), which guides the operation of a harmonized trade policy across the EAC. The rates applicable to all imports are prescribed in the Common External Tariff (CET), which is an annex to the EACCMA. Tax expenditures under customs are in two categories; exemptions and duty remission and as a percentage of GDP, the ratio increased from 1.48% in FY 2019/20 to 2.14% in FY 2020/21. Details are provided in Table 8.

Table 8: Revenue foregone due to customs FY 2016/17 – FY 2020/21

Category	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Loss due to Customs Rate Reliefs	247.87	251.07	307.41	306.41	334.99
Loss due to Exemptions	712.152	661.386	1,408.96	1,758.74	2,833.52
Total Loss Under Trade Taxes (Ugx Bn.)	960.022	912.456	1,716.37	2,065.15	3,168.51
GDP at Current prices (UGX Bn)	108,518	120,485	132,096	139,711	148,278
Tax to GDP ratio	0.88%	0.76%	1.30%	1.48%	2.14%

Source: Authors’ calculations using data from URA systems

6.1 EACCMA exemptions

Revenue foregone due EACCMA exemptions increased from UGX 712.12 billion in FY 2016/17 to UGX 2,833.52 billion in FY 2020/21. Notably, revenue foregone due to ‘*Goods imported under Manufacture under bond (MUB)*’ increased from UGX 1,053.749 billion FY 2019/20 to UGX 2,299.440 billion in FY 2020/21. Details are provided in Table 9.

Table 9: Revenue foregone from import duty exemptions

Customs Exemptions	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Goods and Equipment for use in aid-funded projects	557.8	496.7	544.9	577.9	370.27
Gas cylinders	0.015	0.161	0.387	0.343	0.152
Preparations for cleaning dairy apparatus	0.3	0.494	0.486	0.314	0.333
Seeds for Sowing	4.717	3.807	3.216	4.251	4.696
Chemically defined compounds used as fertilizers	22.863	7.665	5.486	4.787	6.64
Diapers, Urine bags and hygienic bags	0.112	0.12	0.214	0.252	0.323
Diagnostic Reagents, Equipment & Blood collection tubes	32.486	74.217	34.962	45.455	66.996
Horticulture, Aquaculture, Agriculture / Floriculture Inputs	4.79	7.566	7.515	5.979	9.142
Packaging Material for Medicaments	0.864	0.817	0.551	0.512	0.417
Equipment for pharmaceutical manufacturers.	1.228	4.224	2.236	2.181	4.125
Specialized Solar equipment and accessories	1.464	0.353	1.703	23.506	1.24
Specially designed motor vehicles	0.083	0.025	0.147	0	0.352
Motor Vehicles for Transportation of Tourists	0	0	1.487	1.395	0.723
Security Equipment	0.026	0	0.048	0.048	0.057
Battery-operated vehicles	0	0	0.171	0.636	0.128
Refrigeration equipment	0.687	0.966	2.196	7.577	11.812
Hotel Equipment	73.399	19.396	7.856	25.019	45.526
Specialized motor vehicles and equipment.	4.744	16.735	14.222	4.557	10.451
Speed Governors	0.035	0.027	0.036	0.079	0.367
Goods imported under Manufacture under bond	6.459	27.303	779.691	1,053.75	2,299.44
Machinery, Spares and Inputs for Direct use in Oil, Gas and mineral exploration.	0.08	0.81	1.45	0.2	0.332
Total revenue foregone	712.152	661.386	1,408.96	1,758.74	2,833.52

Source: URA

6.2 Rate Reliefs

The goods considered here benefit from ‘Stays of Application’ and/or ‘Remission of duty’ which are renewed annually. Total revenue foregone on account of these increased by 9.3% from UGX 306.41 billion in FY 2019/20 to UGX 334.99 billion in FY 2020/21. The top five beneficiaries are; reduced duty rates for wheat grain; Motor Vehicles for transport of goods with gross vehicle weight exceeding 20 tons; Completely Knocked Down Kits (CKD) for Motor Cycles; Other orange juice, frozen or not frozen, Other, apple juice, Active yeasts, Petroleum jelly, Polyurethane resins – Other Unbleached Kraftliner in rolls or sheets and Other unbleached kraft paper and paperboard and odoriferous mixtures of a kind used as raw materials in the food or drink industries respectively. Details are provided in Table 10.

Table 108: Revenue foregone from Customs Rate Reliefs FY 2016/17 – FY20 20/21, UGX Billion

Customs Reduced rates	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
wheat grain.	111.395	145.43	142.626	116.278
Jacquard Material for Making Spring mattresses	0.191	0.286	0.35	0.65

Penstock pipes for use in Hydro Electric Power Projects.	0.206	0.298	0.533	0.65
Barley	0.002	0.003	0.022	0.001
Poly Vinyl Alcohol	0.023	0.063	0.065	0.051
Maternity (Mama) kit.	0.136	0.225	0.298	0.361
Other soap in other forms – Soap Noodles	0.204	0.297	0.364	0.345
Poly Cotton Material for making Mattresses.	1.579	1.51	2.074	1.399
Goods Vehicles with Gross Weight > 5 Tons but < 20 Tons.	10.517	10.148	9.134	11.726
Goods Vehicles with gross weight > 20 tons	11.487	19.526	23.455	51.035
Road tractors for semitrailers	5.17	5.65	6.57	11.51
Clothes-dryers	0.03	0.04	0.05	0.02
Bathrobes	0	0.14	0.06	0
Aerosol cans	0.08	0.15	0.04	0.06
Inputs for use in the manufacture of Energy Saving Stoves	7.09	8.5	10.06	12.44
Inputs for the manufacture Roofing tiles	0.02	0	0.01	0.08
Organic surface-active agents (Anionic) (LABSA)	1.1	1.29	0.78	0.84
Umbrella heads for roofing nails	0	0.41	0.46	0.6
Aluminum Barrier Laminates (ABL)	0.56	0.27	0.6	0.32
Hot melt adhesive, PE film, Plastic cask, Super Absorbent polymer, Nonwovens, Spandex, etc	10.26	9.77	11.42	12.57
Other non-wired glass	0.03	0.01	0.03	0
Stranded wire, ropes and cables	0	0.04	0.03	0.04
Other Paints and varnishes	0.06	0.76	0.27	0.17
Aluminum plates, sheets and strip, of a thickness exceeding 0.2 mm. Of aluminum alloy.	0	0	0.01	0
Steel Blanks for Spoons and forks	0.03	0.04	0.05	0.04
Inputs for the manufacture of furniture	0.04	0.25	0.44	0.44
CKD for flat iron, speakers, LED & CFL bulbs, DVD players, blenders and hot water kettles	0	0	0.34	0.2
Odoriferous mixtures of a kind used as raw materials in the food or drink industries	16.04	18.22	15.84	19.4
Completely Knocked Down Kits (CKD) for Motor Cycles	26.86	29.31	27.54	42.72
Other orange juice, frozen or not frozen; Other, apple juice; Active yeasts; Petroleum jelly; Polyurethane resins	26.62	30.96	30.41	30.41
Polyurethane resins; Unprinted;	0.01	0.03	0	0.01
Unbleached sack kraft paper in rolls or sheets; Paper and paperboard coated, impregnated or covered with plastics (excluding adhesives).	14.73	16.23	15.4	14.63
Raw materials and industrial inputs for manufacture of textile (garments):	3.31	3.21	5.61	4.17
Raw materials and industrial inputs for the manufacture of footwear (shoes):	1.36	1.29	1.34	1.62
Base Oil	1.95	3.07	0.14	0.2
Total revenue foregone	251.07	307.41	306.41	334.99
GDP (UGX Bn)	120,485	132,096	139,711	148,278
Revenue foregone as % of GDP)	0.21%	0.23%	0.22%	0.23%

Source: URA

7.0 Limitations of the report

Many beneficiaries of income tax and VAT exemptions do not file tax returns, hence data inadequacies. Therefore the estimated revenue foregone could potentially be higher than reported if all beneficiaries filed returns.