
EAC Excise Tax Harmonisation impact assessment study

TMEA
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1. Background and scope

Background of this study

The East African Community (EAC) is a regional organisation comprised of Kenya, Tanzania, Uganda, Burundi and Rwanda. The EAC aims primarily at widening and deepening the economic cooperation between the Partner States. Article 83(2)(e) of the 1999 Treaty establishing the EAC obliges the States to "harmonize their tax policies with a view to removing tax distortions in order to bring about a more efficient allocation of resources within the Community." For this purpose, a Customs Union was established in 2005. The Customs Union Protocol, which was subsequently agreed to put emphasis on, among others;

- the removal of internal taxes and non-tariff barriers on intra-EAC trade,
- the introduction of a common external trade policy through the common external tariff, and
- the introduction of a list of sensitive products that are to be provided additional protection.

The implementation of the common market protocol from 1 July 2010 is a strong commitment to deepen and widen EAC integration.

The article 32 of the Common Market protocol obliges the Partner States to undertake **progressive harmonization** of their tax policies and laws on domestic taxes with a view to **removing tax distortions** in order to facilitate the **free movement of goods, services, and capital and the promotion of investments within the Community**. (Emphasis our own)

The discriminatory tax systems in the Community hampers the enjoyment of the four freedoms (free movement of persons, free movement of workers, free movement of services and free movement of capital) granted by the Common Market. Tax neutrality is very critical for a good functioning common market to ensure that the tax systems of the States interfere as little as possible with free trade and competition.

The EAC Secretariat created the Technical Working Group on Excise Tax to draft common excise tax legislation. In its 3rd meeting in September 2010 in Arusha, the Working Group recommended that the secretariat conduct the excise tax harmonisation impact assessment study on revenue implications in the Partner States in order to facilitate discussions on the Schedules on the excise rates and the exemptions.

During the Regional Public Private Dialogue (PPD) on Harmonisation of Domestic Taxes in the EAC¹, held on 11th -12th November 2011, the following were recommended:

- That the EAC should work towards consolidating the gains of the Customs Union, in order to fully implement the Common Market Protocol.
- Tax Harmonization should be institutionalized under the Fiscal Affairs Committee of the EAC. Among others, the Committee should then develop a policy framework for tax harmonization that will serve as a reference point for tax reforms at national level and eventual convergence at the EAC level.
- On Excise Tax System Harmonization – The PPD recommended that the Excise Management Bill be finalized with the necessary essential input from the key private sectors whose goods and services are subject to excise. Priority should be given to definitions, administrative

¹ http://psfuganda.org/new/index.php?option=com_content&view=article&id=94:public-private-dialogue-on-harmonisation-of-domestic-taxes-in-the-eac-region&catid=21:news

procedures and processes. Additionally, a study on the impact of harmonization of excise duty structures should be conducted by the EAC Secretariat.

- On VAT Harmonization, there is need to build consensus in order to develop a legal framework on which a common procedures manual will be based.
- On Income tax procedures, there is need to identify areas that require harmonization, especially with regard to capital, services and enterprise; in order to develop a harmonized, but flexible income tax procedures code.
- A need was recognised to review further the merits and demerits of tax incentives, with a view to guiding tax incentives harmonization.
- The Double Taxation Agreement should be ratified and operationalized in the Partner States with immediate effect. The Model DTA with Third Party and the Code of Conduct on Harmful Tax Competition should both be expeditiously concluded and thereafter operationalized.

Based on this, the EABC requested support from TMEA to carry out a study on the revenue implication of excise tax harmonisation on the partner states. This is a follow up study on the Basic Assessment study² (Phase 1) whose highlights included the following:

- Excise tax harmonisation in the EAC will be determined by the Partner States' desired degree of regional integration. A harmonised system of excise will, improve the efficient working of the single market, reduce cross border formalities for movements of excisable goods, reduce the causes for cross border smuggling and reduce inter-state distortions from excise-induced differences in cost structures.
- Barriers to full harmonisation with common rates include, considerations around tax sovereignty, failure to agree on a common excise policy, fear of losing revenue, and likelihood of reluctance by the Partner States to agree on the gradual convergence of excise rates due to differences in per capita income.
- For full harmonisation to work, Partner States will be required to cede principles of tax sovereignty in relation to excise tax. This will require a regional holistic perspective rather than a nationalistic one, in order for the region to succeed.
- Considering Partner States are at different levels in respect of the existing excise regimes there is a need to engage in negotiations to agree on safeguards to Partner States that may be adversely impacted by excise revenue declines and reduced industry growth as a result of harmonization. A drastic overhaul of excise tax policy in the EAC Partner States will require securing trade-offs, political buy-in and agreeing on principles.
- Although EAC has its unique challenges in terms of illicit trade, wide disparities in rates and structures, and practices by revenue administrations, it should be possible to build the foundation of a harmonised excise tax system to secure long term growth in excise revenues and allow industry players to trade with a minimum of cross border issues.

In light of the foregoing PricewaterhouseCoopers Limited (PwC) was engaged to carry out the Phase II of the study. This phase of the study will assist in taking forward the recommendations of the Public Private Dialogue (PPD) on domestic tax harmonisation, which TMEA supported, in

² GIZ Report on Excise tax harmonisation in the EAC

addition to contributing to TMEA's overall objective of removing the barriers to trade and thus increasing intra-regional trade.

Scope of work

- Conduct an assessment of the revenue implications of the proposed methods of harmonisation of tax regimes, excise rates, tax base and exemption in the EAC.
- Conduct an analysis and propose a common list and rates of the excisable goods and services across the EAC.
- Assess the exemptions granted by EAC partners states excise tax laws and propose an appropriate exemption regime.
- Propose the most suitable way of harmonisation and propose the best options to guide policy makers.

2. Approach and methodology

We undertook the study through a combination of methodologies- collection of secondary data from publicly available sources, administering questionnaires, conducting oral interviews and reviewing the existing literature on previous studies carried out in the area of excise tax.

These were aimed at achieving the following:

- a) Understanding the specific areas of excise tax regime that will be affected by the proposed harmonisation.
- b) Establishing the various possible excise tax harmonisation scenarios and clearly documenting how these will affect the administration of excise tax.
- c) Discussing the likely impact of the harmonisation on the Partner States clearly identifying specific matters that need to be resolved.
- d) Establishing a link between stakeholder views and the results of data analysis on revenue impact
- e) Collecting stakeholder views on the proposed way forward.

Review of comparative case studies

In our review of the comparable case studies, we looked at the following economic blocs to give us an insight into their experiences and the lessons learnt in their harmonisation process.

- the European Union (EU);
- the Association of South East Asian Nations (ASEAN);
- the South African Customs Union (SACU);
- the Andean community; and,
- the Central African Economic and Monetary Community (CEMAC).

From our analysis, we were able to identify the community whose experiences are closest to the EAC and hence it's worth paying attention to the processes and lessons they went through in the harmonisation efforts.

Views from stakeholders

We administered a questionnaire to establish several facts regarding the prevailing understanding of excise duty, the prevailing economic conditions in the countries, the preferred harmonisation scenarios and likely challenges to harmonisation in the EAC. The questionnaires were administered in both the private sector and the public sector. We sought to understand any previous involvement the respondents might have had on the harmonisation process hence enabling us validate any responses given as well as categorise them. In categorising the responses separately into private sector and public sector responses, we took cognisance of the fact that these stakeholders at times have conflicting viewpoints which would then result in us getting conflicting responses on the various questions.

Revenue impact analysis

The data analysis was carried out to determine how the existing excise tax regimes will be affected as well as the qualitative and quantitative effect of the harmonisation process.

We obtained data in respect of the following key economic parameters from all the Partner States:

- Gross Domestic Product (GDP),

- the overall tax revenue from all tax heads
- the Excise tax collected and the contribution of all the excisable items to the total excise tax revenue

We analysed for each of the Partner State:

- the contribution of Tax to the overall GDP and the contribution of Excise tax to the overall tax revenue in the Partner States
- We carried out comparisons of percentages of revenue contribution of all the excisable items to the overall tax revenue.
- We have also provided comparison of excise revenue between all the partner states.

The Data analysis was carried out using Excel computer packages.

We analysed the data from the various countries to obtain comparatives on the following:

- the contribution of Tax to the overall GDP in the Partner States
- the contribution of Excise tax to the overall tax revenue in the Partner States
- percentages of revenue contribution of all the excisable items to the overall tax revenue.
- excise revenue between all the partner states.

The data used was collected from the revenue authorities of the five EAC partner states.

Limitations

In the study we faced the following limitations

- a) The quality of data available from certain countries was hard to ascertain because;
 - Certain countries could not separate excise duty collected on imports from excise duty on local purchases
 - In certain countries, the excise duty on beverages was not separated into the various categories.
 - There is no data available on the actual excise duty revenue forgone as a result of remission on local raw materials.
- b) Obtaining responses from the public sector/government departments especially in Kenya, Uganda and Tanzania was faced with a lot of resistance. The actual reason for this was not understood.
- c) The harmonisation scenarios on which the impact assessment was conducted were purely hypothetical based on the phase one report and they have not been discussed or validated in any other study available for public scrutiny.
- d) Despite the quality of data obtained, we have been able to propose a way forward based on both the analysis and the feedback obtained from stakeholders.

3. *Literature review*

What is tax harmonisation?

Article 32 Common Market protocol provides that *the Partner States undertake to progressively harmonize their tax policies and laws on domestic taxes with a view to removing tax distortions in order to facilitate the free movement of goods, services, and capital, and the promotion of investments within the Community.*

BNET Business Dictionary defines tax harmonisations as, the enactment of taxation laws in different jurisdiction such as neighbouring countries..... that are consistent with one another”. For some, tax harmonisation is stipulating a defined range of rates while for others it is concentrating on particular tax structures.

Countries within the region have different resources, different economic levels and different levels of political stability, education and social services. Indeed there exists a measure of inequality as depicted by the varied gross domestic product (GDP), GDP per Capita and purchasing power parity. The purpose of harmonising taxation structures and systems of EAC is to make Partner States compatible with the regional integration objective. The countries are gradually moving to a single market economy free from distortions caused by tax. It means viewing this region as one market and one economy. There is the need for harmonisation of taxes to facilitate;

- free movement of goods, services, and capital; and
- Promotion of investments within the Community.

There is also need to achieve a balance that would enhance the overall cohesion within the Community. Presently each country has different rules, methods and rates to determine tax liability. It would be easier for investors and tax administrators if there were similar rules in the region

Countries are sovereign nations and do have the authority to make policies independently. However, with the globalisation of trade and investment more and more countries are forming trading groups. Such alliances recognise the need to encourage trade and investments through the principle of “single market and economy”. For EAC the objective is to move from wide variation in tax policies to some degree of regional tax harmonisation through structures, definitions, rules and administrative procedures.

In relation to the European Union (EU), tax harmonisation is the process of creating common standards across the internal market. Harmonisation aims to:

- Create consistency of laws, regulations, standards and practices, so that the same rules will apply to businesses that operate in more than one Member State, and so that the businesses of one State do not obtain an economic advantage over those in another as a result of different rules; and
- Reduce compliance and regulatory burdens for businesses operating nationally or trans-nationally.

The EU seeks to achieve uniformity in laws of Member States in order to facilitate free trade and protect citizens. It seeks to co-ordinate different legal systems by eliminating major differences and creating minimum requirements or standards. Harmonisation is a process of ascertaining the admitted limits of international unification but does not necessarily amount to a vision of total uniformity.

In our view, tax harmonisation need not necessarily result in the same tax rates and laws. Tax harmonisation needs to be processes that will enable the EAC Partner States achieve the objective of eliminating tax distortions to facilitate the free movement of goods, services, and capital, and the promotion of investments within the Community.

From its conception, various authors on the subject have sought to crystallise the notion of ‘tax harmonisation’ into a definition which comprises all its facets. For instance, it has been suggested that harmonisation refers to “any situation where differences in taxation between the states (or provinces) are reduced either by co-operation among the states or by a federal government policy”. It is however acknowledged that a completely uniform tax system may “not be optimal or practical”. “Co-ordination” has been regarded by some as a kind of consultation process about organising tax systems in a similar manner. In essence, such an interpretation presents co-ordination as a low-level form of harmonisation.

Others have sought to define tax harmonisation in terms of its ends rather than on precise institutional arrangements and have proposed a more open definition.

Taking a wider view of tax harmonisation, one can adopt two approaches to the concept. The first, the “equalisation” approach, causes each country to converge with the others until it ends up with the same fiscal system. The second, the “differentials” or “fiscal diversity” approach, allows each country to use its tax system as a policy tool in achieving major economic aims.

‘Harmonisation of tax’ has also been held to refer to “the process of removing fiscal barriers and discrepancies between the tax systems of the various countries .Admittedly, efforts in the direction of tax harmonisation need not be confined to the boundaries of the EAC and may be extended to the rest of the globe. “Removing fiscal barriers” refers to the principle whereby imported goods and services within a free-trade area were not to be subject to any fiscal discrimination in comparison to domestically produced goods and services. In addition, the above definition refers to “removing...discrepancies between tax systems”, implying, rather than standardisation, the bringing of tax systems into harmony or agreement making up a consistent and orderly whole, without each part being identical and hence a more flexible approach.

Ultimately, the EAC tax harmonisation exercise can be generally defined as “the process of planning how to approximate the tax systems of the Partner States in order to better achieve the objectives of the Community.” The emphasis, rather than on standardization, is more on operating ‘in harmony’³.

Work done so far on excise tax harmonisation in EAC

The EAC secretariat has a technical working group on excise tax harmonisation. The Working Group was created by the EAC Secretariat to draft common excise tax legislation. In the intervening period, various workshops, technical meetings, studies and reports have been carried out to explore the best way forward in the harmonization process. The working groups held two meetings in the year 2010 in March and July. These meetings explored extensively the possibilities available for harmonisation and the various options to be explored, no concrete solutions were arrived at in as far as excise tax harmonisation is concerned.

In the year 2009, GTZ/EAC commissioned a report on excise tax harmonisation in the EAC. The study reviews the national tax systems within the EAC member countries, the macroeconomic using basic figures and the current stand of the inner-community integration analysed. It further discussed the value added tax laws, excise taxes and income taxes are discussed in detailed the report also contained the policy recommendations of the expert group and presented the results for the VAT, the excises and the corporate income tax (CIT). Additionally the requirements for tax procedures and administration as well as problems of transparency and information exchange were discussed in detail, Hans- Georg Petersen (Ed) (2010). These reports despite aiding in providing a detailed understand of the prevailing harmonisation position and providing focus areas for the harmonisation platform did not do much in advancing the harmonisation agenda.

³The Process of Corporate Tax Harmonisation in the EC©2001 [Dr Jean-Philippe Chetcuti](#)

In 2011, the regional Public Private Dialogue (PPD) on Harmonization of Domestic Taxes in the EAC region held in Dar es Salaam, from the 11th -12th November 2011 also strongly recommended that harmonisation is essential and needed to be speeded up. Subsequent to this, several other meetings have been held and discussions have been done regarding the process of harmonisation of excise duty in the EAC.

The East African Business Council (EABC) has an excise duty working group that is made up of entities involved in the manufacture of excisable goods and provision of excisable services. This working group has come together for various meetings most recently in January 2014. The aim of this working group is to provide input to the drivers of policy in an effort to ensure that their knowledge and insight into the challenges of excise duty in EAC is utilised.

In 2012, GIZ commissioned PwC to carry out a basic assessment study to review the status of the harmonisation process in the EAC. The study detailed the existence of huge divergence in the excise tax laws and regimes in the various countries of the EAC.

The report recommended the following areas of harmonisation:

i) Procedures and administration

As tax policy is developed and harmonised, the importance of good administration should not be overlooked. How a tax system is administered affects its yield, its incidence and its efficiency. The key areas pointed out as requiring harmonisation and procedures and administration were;

Definitions of excisable products,

Approval of persons and premises: This includes licensing of manufacturers, approval of premises and equipment, accounting for stock and movement of goods, operations of an excise warehouse, etc.

Tax point: have a clear understanding of when goods become liable to excise tax and when the excise tax must be paid.

Reimbursement and remission by Partner States,

Exemptions: For specified use or reason (diplomatic sales, duty free shops, armed forces, etc).

Procedures on movement of excisable goods within the EAC:

Use of technology to facilitate payment of excise tax and monitor movement of excisable goods in the EAC region.

ii) Classification rules and definitions

Though the EAC Partner States have mostly common excisable goods, these goods are defined and classified differently for excise duty purposes. It is vitally important that a product be treated the same for excise purposes in all Partner States.

iii) Remission schemes

While the remission schemes in the Partner States are all geared at promoting trade and making locally manufactured goods more competitive, harmonisation of remission schemes would ensure that the definitions are clear and it would also increase and simplify trade especially for regional investors as the schemes would be similar in procedures and administration.

iv) Excise duty rates

Owing to the different per capita income in the Partner States, it would be more feasible to start with setting maximum and minimum excise rates with the goal of facilitating a gradual convergence to single common rates. This would ensure that the Partner States are shielded from sudden changes that would affect their development plans

The study further proposed that to achieve effective harmonisation outcomes a phased approach that focuses on less contentious areas in the beginning and then continuously and in a subtle manner create impetus for further harmonisation.

The following harmonisation scenarios were proposed:

1. Harmonised procedures and structures; but country-specific rates

The harmonisation of the areas (i), (ii) and (iii) above i.e. procedures and administration; classification rules and definition; and remission schemes. This would also involve harmonisation of the structures of excise taxation with regard to the basis of levying excise duty i.e. specific, *ad valorem* or hybrid. This means that a product, say beer, would be subject to the same definition, classification and basis of levying excise duty in each of the Partner States.

The Partner States retaining their sovereignty in determination of the applicable excise duty rate to apply for each product.

2. Harmonised procedures and structures; but country-specific basis of levying excise duty

The harmonisation of the areas (i), (ii) and (iii) above i.e. procedures and administration; classification rules and definition; and remission schemes. This would also involve harmonisation of the structures of excise taxation with regard to the basis of levying excise duty i.e. specific, *ad valorem* or hybrid. This means that a product, say beer, would be subject to the same definition, classification and basis of levying excise duty in each of the Partner States.

The Partner States retaining their sovereignty in determination of the basis of levying excise duty (i.e. specific, *ad valorem* or hybrid) as well as the applicable excise duty rate for each product.

3. Complete Harmonisation

In this scenario, the Partner States would in addition to harmonisation of areas (i), (ii) and (iii) above also agree to the harmonisation of all the excise rates for all the excisable products.

This scenario should be considered as a continuation to Scenario 1 and/or Scenario 2 above in which different rates would be set as feasible in each of the Partner States with a view to a gradual convergence into a single rate per product.

It would be important at this stage to consider the different products that one Partner State imposes excise duty on, that the others do not e.g. cement in Uganda and powdered milk in Rwanda. This could be addressed by either having a transition period in which the Partner States would align the list of excisable goods or having a list of sensitive goods (as in the CET) and thereby letting such goods remain excisable in that Partner State.

Comparable Case Studies

The Association of South East Asian Nations (ASEAN)

This community was created in 1967 as a political group to strengthen the power and increase growth and development in member nations. The pioneer member nations were Indonesia, Malaysia, the Philippines, Singapore, and Thailand. The membership has since reached ten with Papua New Guinea and Timor-Leste (East Timor) given observer status. The main goals of ASEAN include improving the economies of member countries, as well as ensuring security and promotion of peace between the neighbouring nations. The unification of these primarily smaller nations helps them to protect themselves and each other from outside conflicts.

In 2003, the leaders of the ASEAN agreed to the formation of an ASEAN Economic Community (AEC) as part of its larger 'ASEAN Vision 2020' plan. A 'road map' for implementation was then laid out in 2007 in a document titled the 'ASEAN Economic Community Blueprint' in which the following 'characteristics' of the new regional economic integration were outlined as being:

- the creation of a single market and single production base
- a highly competitive economic region
- a region which is equitable in terms of economic development
- a region which is fully integrated into the global economy.

The formation of a single market and a single production base with the ASEAN region included the harmonisation of excise which is primarily a tax on the production (and/or import) of certain goods, although it can also be found being applied to some services⁴.

The members identified five commodities that were excisable across all the states

- Motor vehicles
- Beer
- Wine
- Distilled spirits
- Tobacco

Certain products were also identified as outliers that are taxed in certain countries as follows

- Non Alcoholic beverages
- Karaoke/Nightclub operations

The countries arrived at a short term agreement for the management of non-harmonised excise duties by opting to grant member states to retain or introduce national excise duties and systems of collection so that they can compensate for any losses arising from harmonisation efforts by tapping into additional sources of revenue.

One major impediment to harmonisation identified by these states is lack of transparency in "effective excise rates" particularly in taxation of fuels with most countries having a range subsidies and temporary cuts to protect their local markets. This problem can only be addressed by allowing the other countries sufficient leeway to determine what exact rates to charge while still governing it by providing for a floor and a ceiling.

The ASEAN community has the biggest similarity to the EAC in that there is no single dominant state, and there is not single state that is too far ahead of the others in terms of economic development and resource endowment.

The European Union (EU)

In 1993 the EU "harmonised" its excise rules through the establishment of an internal market. Following lengthy negotiations between the 15 Member States at that time, the Member States agreed to harmonise via "European Commission (EC) Directives" and four main excise Directives

⁴ World Customs Journal- Excise taxation of key commodities across South East Asia: a comparative analysis ahead of the ASEAN Economic Community in 2015 By *Rob Preece*

were introduced covering the three commodities subject to the harmonised rules: mineral oils, alcohol and alcohol beverages and tobacco products.

Generally in the EU market the categories of products subject to excise are:

- Energy products
- Electricity
- Alcohol and alcoholic beverages
- Manufactured tobacco.

The harmonisation process standardised the calculation of excise and provided a covered basis for allowing exemptions or reduced rates. Many areas of excise control remain discretionary, including accounting periods, the extent to which a tax warehouse system can apply and the value of financial guarantees or other security.

The directive however gives the members states the freedom to levy excise duty on services. As such, in levying excise duty on services, the identification of dutiable transaction is the major consideration. It has also clearly stipulated that where goods and services are supplied jointly the set of services that encompass a transaction should be identified separately.

The main points of note in the EU case are the fact that the specific directive has provided two key considerations that must be satisfied in the harmonisation process.

- Excise duty must not give rise to any formalities associated with crossing of borders
- The introduction of harmonized excise duties must not frustrate the aim of abolishing tax borders within the context of the internal market.

The EU has its main aim as the development of an internal market, where internal market is all the member states in the entire EU region. The harmonisation of excise duty is seen as a major step in the development of a borderless community that has a free flow of goods between Partner states.

Southern Africa Customs Union

The Southern Africa Customs Union (SACU) dates back to 1910, when South Africa, Basutoland, Swaziland and Bechuanaland signed up. Only Britain and South Africa were involved in the 1910 negotiations. This Agreement lasted until the British Protectorates received Independence in the mid 1960s. It was then renegotiated with the apartheid government, culminating in the 1969 Agreement.

The SACU states operate a single Excise law, procedures and tariff, that is, the South Africa Customs and Excise Act. The customs union can be said to have the longest experience in “harmonisation” of excise taxes, however, it should be noted that the nature of harmonisation is unique to SACU due to its history; that is, political and more importantly economic dominance by South Africa and economic dependency of Botswana, Lesotho, Namibia and Swaziland on South Africa.

Its stated objectives include:

To promote the integration of the Members into the global economy

To facilitate cross-border movement of goods between the Members

To establish effective, transparent and democratic institutions which will ensure equitable trade benefits to the Members

To facilitate the equitable sharing of revenue from customs, excise and additional duties

To promote fair competition, substantially increase investment and facilitate economic development

To facilitate the development of common policies and strategies

The defining characteristic of the SACU is the economic dominance of South Africa in contrast to the size of the other four members. The BLNS depend heavily on South Africa for a significant proportion of their trade, investment and in some cases (migrant) employment. The high level of dependence of

the smaller SACU member countries on South Africa is therefore reinforced by the revenue sharing arrangement. The 2002 SACU Agreement provides that excise revenues will be distributed on the basis of each country's share of total SACU GDP – a proxy for the value of excisable goods consumed. South Africa, as the largest economy in SACU, on average retains around 80% of total excise revenue collected.

Excisable products include:

- Petroleum products
- Alcoholic beverages
- Tobacco
- Ad-valorem products: Cosmetics, Vehicles, clocks, firearms, video equipment's and gaming machines.

The Andean Community

The Andean Community, consisting of four Member States – Bolivia, Colombia, Ecuador and Peru – harmonised its excise rules in 2005. The harmonisation process began in 1998, was ratified in July 2004 with implementation from 1 January 2005. The harmonisation of VAT and excise tax had been a priority for the Andean Community since 1998. The above timelines shows that harmonisation is not a quick fix. All sovereign nations must be satisfied that revenues can be maintained and businesses can operate in a secure fashion.

A report in to the key issues concerning harmonisation and its impact was finalised in 2002, four years after the decision had been made to explore the harmonisation process. Only after this phase did the Member State authorities begin negotiations in relation to the harmonisation process. Even after agreement, changes were implemented using transitional agreements. General principles in relation to the structure of excise were issued in a decision referred to as Decision 600 (Harmonization of excise type taxes) of July 12, 2004. Under Decision 600 the structure, common excise rules and procedures have been outlined for Member States to domesticate and implement as local excise legislation; however, Member States may set rates according to their cultural and policy needs using either an ad valorem system or specific system.

Therefore the harmonisation of excise in the Andean Community can be considered as partial harmonisation which requires further consideration. The model if adopted in EAC would lead to significant delays in the harmonisation process.

The Central African Economic and Monetary Community (CEMAC)

The Central African Economic and Monetary Community (CEMAC) is made up of six States: Gabon, Cameroon, the Central African Republic (CAR), Chad, the Republic of the Congo and Equatorial Guinea. With a total population of about 37 million, it covers a total surface of around 3 million km². Together with the larger Economic Community of Central African States (ECCAS) and the mainly inactive Economic Community of Great Lake Countries (CEPGL), CEMAC presents one of the Central African regional Communities established to promote cooperation and exchange among its members.

At their summit in Equatorial Guinea's capital Malabo in June 2002, the Heads of State defined four main priority fields for the Community:

- to develop capacities to maintain peace, security and stability, which are essential prerequisites for economic and social development;
- to develop physical, economic and monetary integration;
- to develop a culture of human integration; and

- to establish an autonomous financing mechanism for ECCAS.

In Summary

- The trading blocs studied harmonised the list of excisable commodities, the ASEAN community include motor vehicles, alcohol and tobacco. In the EU it was mainly; energy products, alcohol, tobacco and some selected services. In SACU it is; petroleum products, alcoholic beverages, tobacco, and a few luxury goods. This indicates that there is a lot of similarity in the excisable products across the three communities.
- The ASEAN community is still addressing rates differential while the EU settled on a rates system that provides for a floor and a ceiling with the countries allowed a leeway to choose the most appropriate and according to their preferences
- The EU and SACU have adopted common laws for excise that are applied across the states
- SACU has adopted a common border authority that collects excise tax which is later shared among the Partner States.

Comparison between EAC and other jurisdictions

In summary, certain products are excisable across all economic blocs while other are excisable only EAC

Product in EAC	Excisable in EU	Excisable in SACU	Excisable in ASEAN	Comments
Alcohol	Yes	Yes	Yes	Universally excisable
Tobacco	Yes	Yes	Yes	Universally excisable
Petroleum	Yes	Yes	Yes	Universally excisable
Soft Drinks	No	No	Yes	Excisable in EAC and ASEAN
Mineral Water	No	No	No	Only Excisable in EAC
Motor vehicles	No	No	No	Only Excisable in EAC
Plastics	No	No	No	Only Excisable in EAC
Sugar	No	No	No	Only Excisable in EAC
Cosmetics	No	Yes	No	Excisable in EAC and SACU
Cement	No	No	No	Only Excisable in EAC

From the table above, none of the jurisdictions reviewed imposes excise on the following items- mineral water, motor vehicle, plastics, cement and sugar. This is either because these products are considered essential (not luxury) or because there are other taxes or levies associated with externalities which may arise from the consumption of the products. The only plausible explanation as to why some EAC States impose excise duty on those products is purely for revenue generation purposes. Therefore any proposal to remove these items from the list of excisable product must address the revenue concerns of the affected States.

Comparison of number of countries whose products are excisable in EAC

Product in EAC	Number of countries product is excisable
Alcohol	5
Tobacco	5
Petroleum	4

Soft Drinks	5
Mineral Water	5
Motor vehicles	4
Plastics	2
Sugar	3
Cosmetics	2
Cement	1

As long as these outliers continue to exist, intra-EAC trade on those items are likely to be affected owing to the price differentials occasioned by the imposition of excise tax on those commodities i.e they will be more expensive in the country where excise duty is charged as opposed to country with no duty. This differential reduces in impact as the proportion of excise duty on the overall price reduces, it's however important to note that excise duty is not the only factor that contributes to price.

It is critical that any harmonisation efforts should not be driven solely by the need to have a common list of excisable products but rather the need to ensure that free movement of goods is not affected.

4. *Views from various stakeholders*

We administered questionnaires (attached as **appendix 1**) to obtain certain qualitative values from the excise tax payers in the EAC and get insights on their understanding of the regimes in the EAC. Our questions were aimed at identifying specific concerns and areas of interest for the tax payers as well as validating certain hypothetical scenarios. These questionnaires were administered by a combination of face to face interviews and email correspondence with the various respondents. The qualitative analysis stemming from the questionnaires is detailed below

Respondents to the questionnaires

Country	Organisation	Number of Questionnaires administered	Number of responses received
Burundi	Public Sector	10	6
	Private Sector	4	1
Kenya	Public Sector	12	2
	Private Sector	5	1
Rwanda	Public Sector	10	2
	Private Sector	5	2
Tanzania	Public Sector	12	2
	Private Sector	5	2
Uganda	Public Sector	12	2
	Private Sector	5	2
Total response		80	20

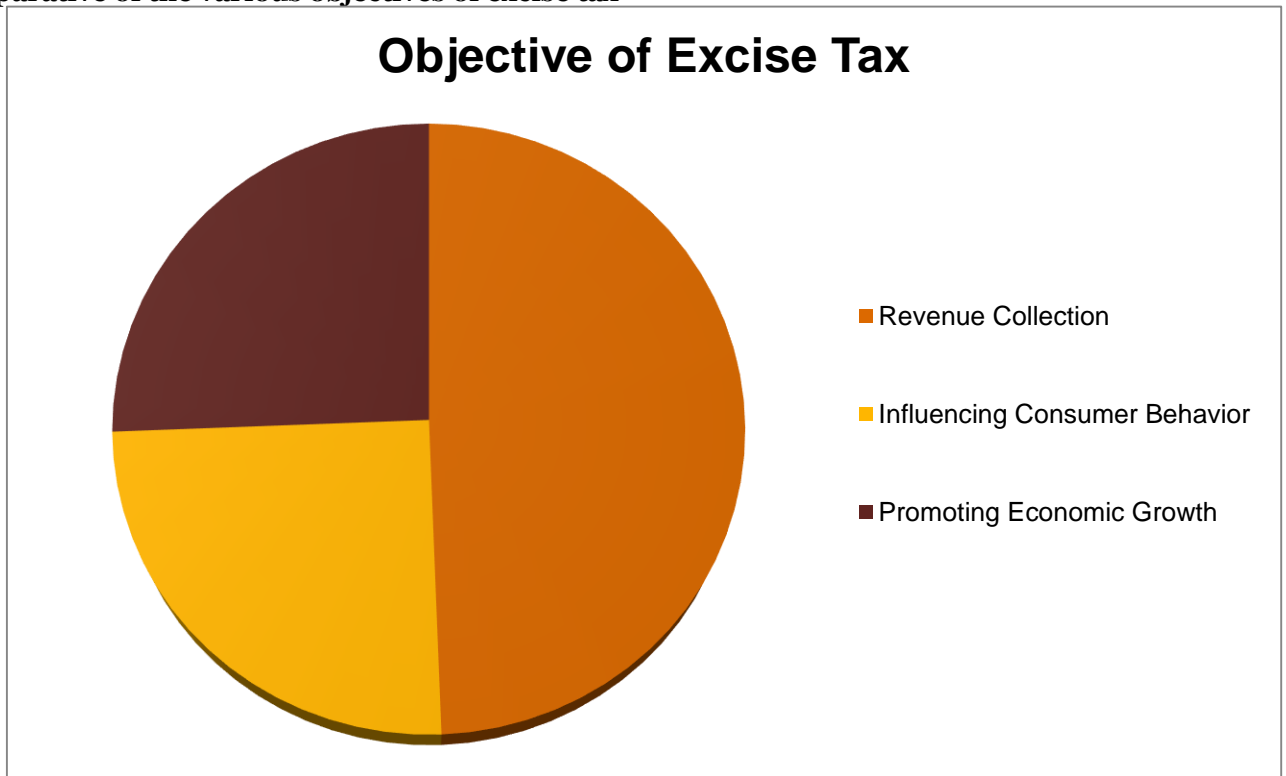
In our experience from the interactions with the stakeholders, the harmonisation process has not been a major topical issue on the public domain. It is therefore important to note that a good number of the respondents did not have comments on some of the questions while others viewed harmonisation to mean standardisation and uniformity.

We have attached the full list of individuals and a sample questionnaire as **Appendix 2** to this report for your perusal.

The main objective of excise Tax

	Public Sector			Private Sector		
	Objective of Excise Tax					
	Revenue Collection	Influencing consumer behavior	Promoting Econ Growth	Revenue Collection	Influencing consumer behavior	Promoting Econ Growth
Burundi	7	5	5	0	0	10
Kenya	10	6	7	10	1	1
Rwanda	10	5	1	10	6	7
Tanzania	8	4	3	10	5	1
Uganda	6	3	1	10	6	6
Total	41	23	17	40	18	25
Percentage	51	28	21	48	22	30

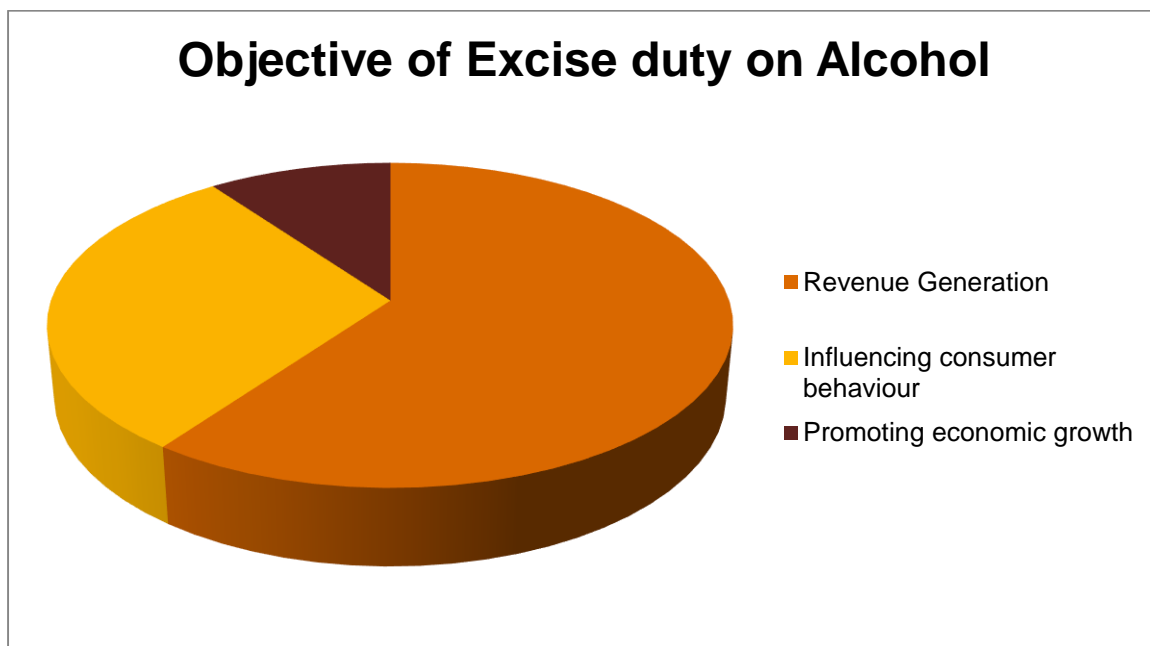
Comparative of the various objectives of excise tax



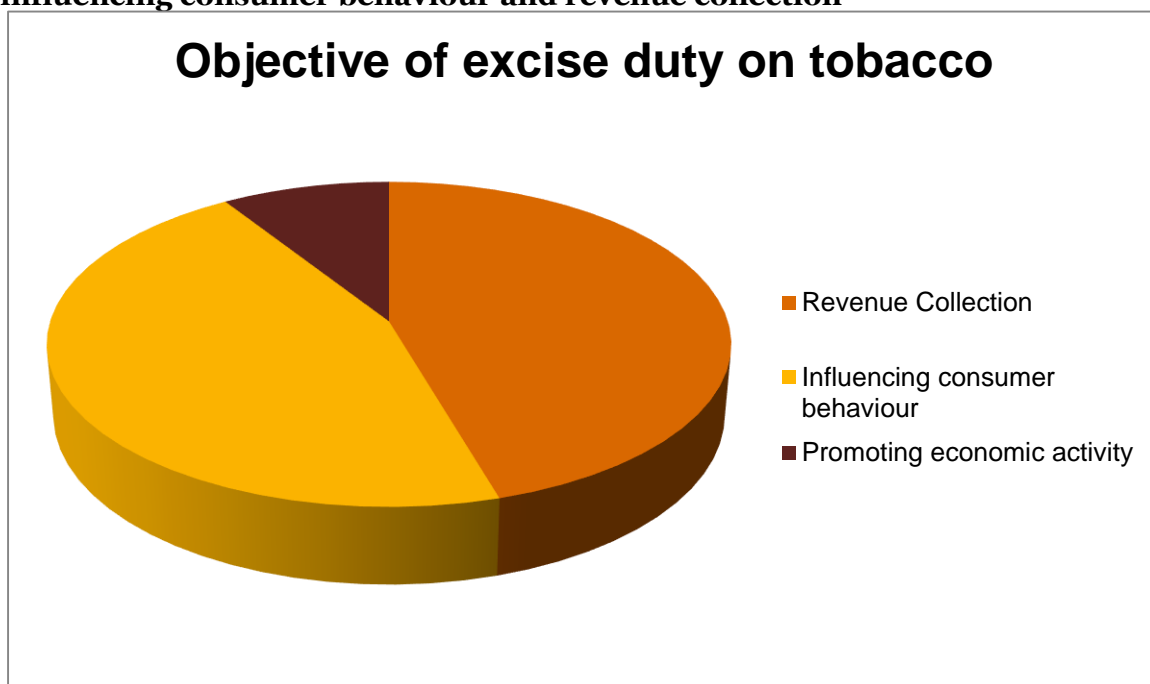
From the first question we can conclude that half of the respondents from both the private and public sector hold a popular opinion that excise duty is primarily used to collect revenues. This implies that the primary purpose of excise duty is to ensure that the governments meet their revenue targets. On the other hand, the remaining halves of the respondents were equally divided between influencing consumer behaviour and promoting economic growth as the objectives of excise tax.

In all the countries, the respondents both in the public and private sector were in agreement that the main product that is targeted by the authorities in meeting the revenue generation objectives is petroleum products followed by alcohol followed by tobacco.

1. Alcohol- The biggest objective of excise duty is revenue collection

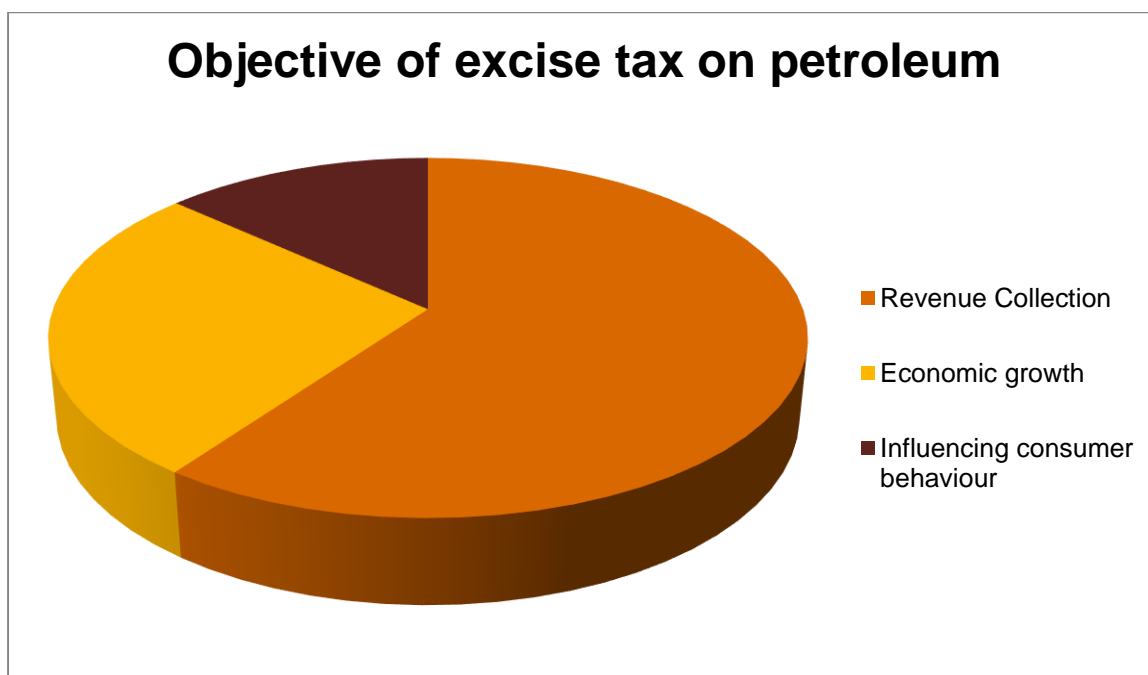


2. Tobacco- The main objective of excise duty on tobacco is shared between influencing consumer behaviour and revenue collection



From the above illustrations, it is therefore clear that the stakeholders across the Partner States are not clear on what exactly is the main objective of excise duty on these leading products across these states. It is therefore appropriate to infer that Partner States need to agree on a harmonised excise tax policy.

3. Petroleum products



On Average 59% of respondents felt that revenue collection is the sole motive of government policy on excise duty.

All policies and laws that are designed by the government are geared towards maximising revenue collections from the various excisable products. It is therefore important to note that 75% of respondents felt that influencing consumer behaviour is no longer a major purpose of excise tax. In some way this is viewed as an uncalled for deviation by the various Partner States.

That said, 25% of respondents felt that such historical objective of excise duty of influencing consumer behaviour should be retained. This is further enforced by the percentages of excise duty collected by the various partner states from the two main products tobacco and alcohol as shown below;

Table 2: Percentage average revenue collected from Alcohol and tobacco in the partner states

	Tobacco	Alcohol	Total %
Burundi	6.00	55.00	61.00
Kenya	22.04	50.50	72.54
Rwanda	8.51	60.27	68.78
Tanzania	15.81	38.61	54.42
Uganda	1.71	33.89	35.60
Total Average	10.81	47.654	58.47

From the table above, on average, the Entire region collects 58.47% of the excise duty from tobacco and alcohol. This affirms the assertions made by most respondents that excise tax is used to collect revenue as opposed to influencing consumer behaviour. This is a key area of interest in establishing the impact on government revenue. **It serves to ascertain the suggestion that most of the excise tax revenue is mainly sourced from two products**

Challenges with the current excise duty regime

According to the private sector respondents that we interviewed, the current excise duty regime faces many challenges amongst these challenges include:

- The existence of differentiated excise regimes with major differences in aspects such as rates and bases in the region, have caused artificial price differences in EAC. This has led to smuggling and black market trade hence causing a loss of revenue to the government.
- There are certain grey areas in the legislation such as excisable base for beers and interest charged on late payments among others.
- Tax remissions and exemptions in some states while they do not exist in other states leads to a distortion of cross market prices.
- The partner states place too much reliance on increasing Excise tax rates to increase tax collection as opposed to expanding the tax base hence causing resentment among the taxpayers.
- The lack of specific law on excise tax causes uncertainty for the business community in respect of the tax regime. The annual amendments to the excise law make the management of Government revenue very difficult.
- Excise tax is currently aimed at revenue collection as opposed to its original purpose which was to influence consumer behaviour.

The respondents therefore seem to all point at the lack of a harmonised structure where we could use either ad-valorem or specific structure is seen as the major failure in ensuring that taxation of excise duty in the region is better structured, organised and administered to ensure ease of doing business.

It is also important to note that a good number of the respondents do not have a clear idea of what harmonisation specifically entails.

How can excise tax harmonisation play a role in achieving the objectives set out under article 32 of EAC common market protocol

Most respondents that were interviewed in this study were of the idea that harmonization of excise duty in the EAC will play a major role in ensuring the achievement of the objectives of article 32 of the EAC common market protocol by ensuring;

- Increased competitiveness on EAC common market as investors will be subjected to similar tax conditions regardless of the country in which they have invested. This will allow smooth movement of products as well as capital flow.
- It will help create comfort and efficiency for regional companies. Though the rates need not be fully harmonised regional companies will comfortably move their goods across the Partner States without being concerned about the impact of excise duty.

- If not harmonised excise tax can be a source of illicit trade and when the difference is huge this has quite distorting effects.

Studies already carried out in various economies indicate that affordability of commodities is a major factor in increased illicit trade driven by excise duty. In the EU for example the Cooper and Witt⁵ study on the linkage between tax burden and illicit trade in excisable products discerned that the illicit trade in Tobacco specifically increased dramatically with the introduction of higher excise duty rates in the EU.

Preferred harmonisation scenario

In our interviews we sought to understand from the respondents which would be the preferred harmonisation scenario between;

- 1) Each EAC country to have its own excise tax structure, law and administrative procedures.
- 2) Create a model Excise Act from which all the member states will develop their own specific acts, rates, and customize to their own liking.
- 3) Develop an EAC Excise Management Act (EEMA) which will be used by all the Partner States with each Partner State having a schedule for its own structures rates and other specific regulations
- 4) Develop a EEMA that will be adopted in full by all the Partner States

The preferred harmonisation scenario per Partner State are as shown below:

Country	Commonly preferred scenario
Burundi	4
Kenya	4
Rwanda	3
Tanzania	2
Uganda	3

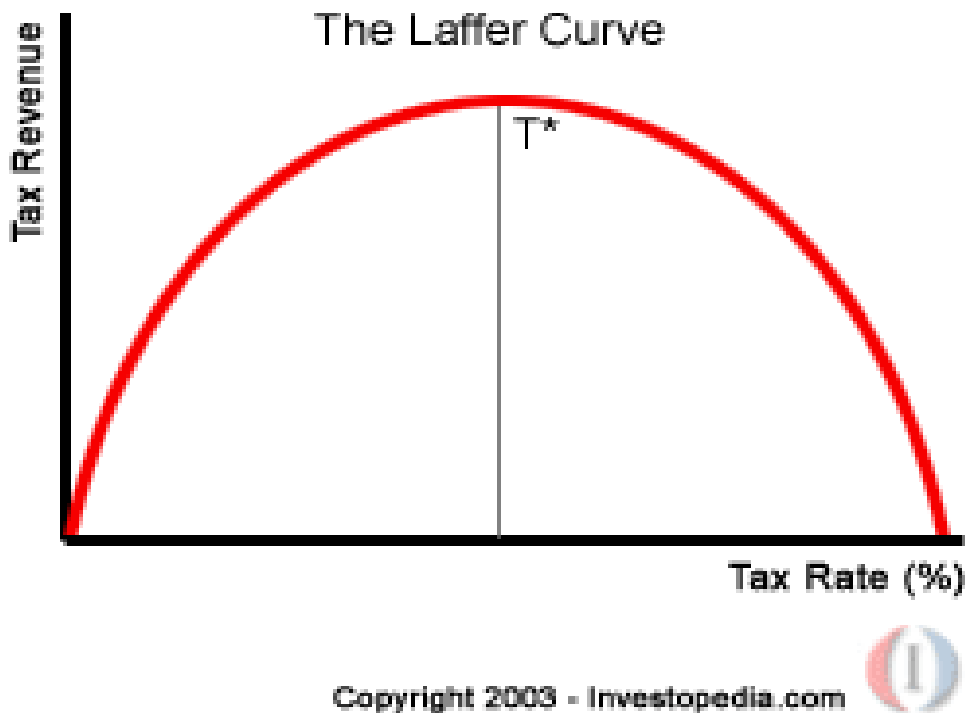
In a sense, the split of preferences among the Partner States is very clear with three different options being considered as viable alternatives. This further indicates the need for a clear policy position to guide any harmonisation efforts moving forward.

For most of the interviewed respondents, the major focus of harmonisation in the EAC should be to take care of price distortions in the EAC and curb illicit trade and smuggling of excisable commodities across the partner states in the EAC. These particular concerns have previously been faced in EU as part of the harmonisation process where certain countries retained excise duty on outlier products while the rest of the bloc had harmonised their products. Addressing this problem effectively would curb most of the current challenges of illicit trade and smuggling of excisable products. It is important to note that the higher the value of the particular product the higher the likelihood of it being smuggled when the excise duty regimes in neighbouring states is significant enough to occasion price distortions.

⁵ World Customs Journal -The linkage between tax burden and illicit trade of excisable products: the example of tobacco by Adrian Cooper and Daniel Witt

How do the rates of excise duty affect tax revenue-The Laffer Curve

Invented by Arthur Laffer, this curve shows the relationship between tax rates and tax revenue collected by governments.



While an increase in tax rates is meant to lead to an increase in tax revenue, the relationship has an inverted “U” behaviour. At a certain point “T” the increase in rates does not have a desired effect but instead leads to an inverse result and therefore a decline in revenue collection when the tax rate is at 100%, the tax revenue collection will be zero. The decline could be associated with two reasons.

- a) Alternative source of non-taxable products will be identified by consumers hence denying the government the revenue. These sources include smuggling of products into the territories
- b) Consumers will choose not to take the product at all.

The general principle of the curve can also be applicable in cases of remission, whereas remission is intended for certain purposes namely increase consumer uptake of products and promoting certain sectors.

Preferred excise structure

Most of the respondents interviewed preferred a specific excise structure; a significant other number preferred a hybrid structure while the minority preferred an ad valorem structure. The main reason why the majority preferred a specific structure is mainly because it is easier to apply and offers consistency. Other respondents also indicated that it is less likely to be subjected to manipulative manoeuvres by unscrupulous individuals seeking to outwit the system. As such the system would then have to be implemented across all the partner states to achieve the intended aim of ensuring free movement of goods among the Partner States. While this might not be a real necessity for the harmonisation process, it is important to note that it forms as part of the eventual outcome of harmonisation, it might be necessary for the Partner States to eventually agree on a common structure.

5. *Revenue impact analysis*

In carrying out the revenue impact analysis, we reviewed the tax revenue data from the various partner states and analysed it for comparative relationship. In our analysis we aimed at establishing the contribution of excise duty to the GDP as well as the percentage of excise duty to the total tax revenue in the Partner States.

The quality of data utilised in this analysis had limitations due to the fact that certain countries did not have separate data for excise duty on imports and excise duty on local goods/services. This data also relied heavily on the publications and communication received from the revenue authorities in the Partner States. Revenue authorities in these states should invest in technology applications to enable adequate tracking and review of data on excise tax in the regions

It is important to note that the quality of the data used for the analysis is low because certain countries could not provide a distinction between excise duty revenue collected from imports and that collected from local sources.

The combined averaged GDP for the EAC Partner States for the years 2010, 2011 and 2012 was USD 81,542,774,732 In terms of ranking, Kenya has the highest GDP followed by Tanzania, Uganda, Rwanda and Burundi in that order. In terms of GDP per capita Kenya comes first with the others following in a similar order.

Country	GDP (Average)
Burundi	2,233,333,333
Kenya	33,661,967,740
Rwanda	6,377,751,690
Tanzania	21,292,721,968
Uganda	17,977,000,000
Total	81,542,774,732

Total tax revenue as a percentage of GDP shows that the countries are also evenly matched in the tax collection and the role of tax revenue to the GDP.

Country	GDP (Average)	Total Tax revenue	Tax revenue as a percentage of GDP
Burundi	2,233,333,333	338,747,520	15%
Kenya	33,661,967,740	8,086,338,908	24%
Rwanda	6,377,751,690	865,568,896	14%
Tanzania	21,292,721,968	3,610,000,000	17%
Uganda	17,977,000,000	2,492,666,667	14%

All the partner states rely on tax revenue as a source of funding for their expenditure. From the above table it is evident that the partner states are at different stages of economic development.

In looking at the comparative GDP per capital of the various Partner States, it is clear that the difference is not very great hence the countries share quiet a number of similarities in the GDP Structure.

Country	GDP per Capita (USD)	Relative size (Using Uganda as a standard)
Burundi	265	0.49
Kenya	782	1.43
Rwanda	408	0.75
Tanzania	571	1.05
Uganda	545	1.00

Comparative percentages of Gross Tax Revenue in the 5 Partner States

The potential tax revenue for the EAC Partner States was USD 15,393,321,991 out of which Kenya accounts for the highest amount at 53% while Burundi has the lowest at 2%. This is in line with the percentages of GDP. Kenya's high revenue collection as a percentage of the EAC is an indicator of how much of the state expenditure is funded through tax collection.

Gross Tax Revenue in the countries indicates that the tax revenue is as expected in line with the size of the GDP.

Excise revenue as a % of total tax collected (2010-2012)

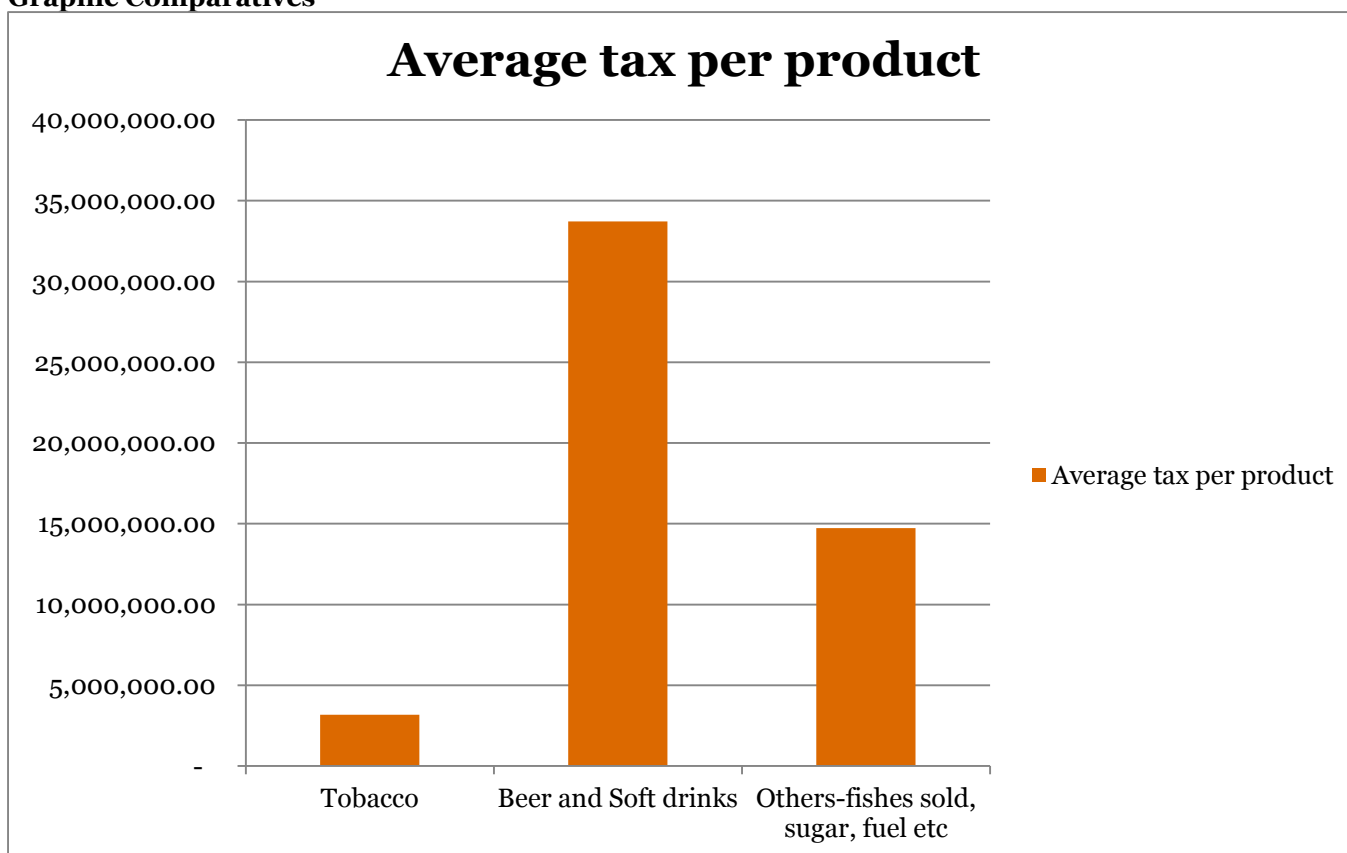
Country	Excise Revenue	Total tax	Excise revenue as a % of total rev
Burundi	51,629,478	338,747,520	15%
Kenya	408,965,769	8,086,338,908	5%
Rwanda	144,066,678	865,568,895	17%
Tanzania	275,000,000	3,610,000,000	8%
Uganda	185,033,333	2,492,666,666	7%
Total	1,064,695,259	15,393,321,990	

The quality of data utilised in this analysis had limitations due to the fact that certain countries did not have separate data for excise duty on imports and excise duty on local goods/services. This data also relied heavily on the publications and communication received from the revenue authorities in the Partner States. Revenue authorities in these states should invest in technology applications to enable adequate tracking and review of data on excise tax in the regions

Excise tax collected per product
1. Burundi

Excise Tax collected	Year 2010	Year 2011	Year 2012	Average tax per product	Percentage per product
Tobacco	3,196,963	3,408,125	2,912,128	3,172,405	6
Beer and Soft drinks	31,096,822	31,295,291	38,782,388	33,724,834	65
Others-fishes sold, sugar, fuel etc	14,125,162	18,058,065	12,013,491	14,732,239	29
Total	48,418,947	52,761,481	53,708,007	51,629,478	

Graphic Comparatives

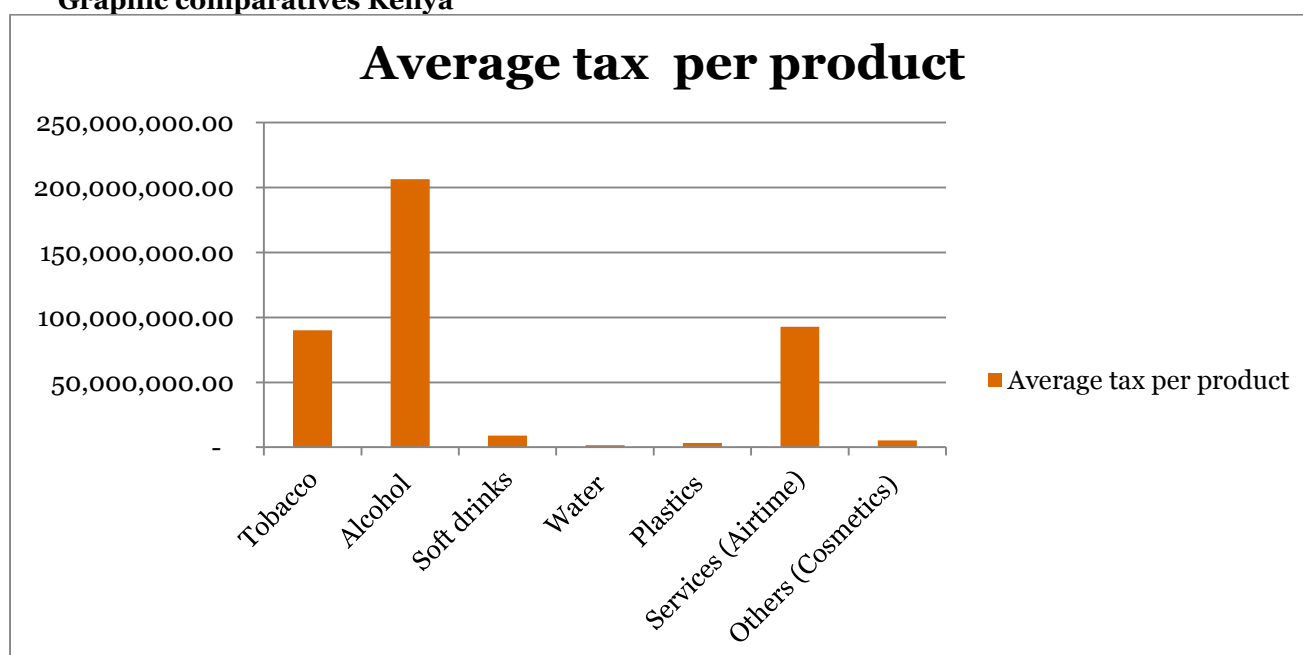


This there indicates that the bulk of excise duty is collected from beer alcohol and soft drinks. These are therefore the core products for excise duty purposes in Burundi.

2. Kenya (USD)

Excise Tax collected	Year 2010	Year 2011	Year 2012	Average tax per product	Percentage contribution
Tobacco	83,454,744	84,342,196	102,607,574	90,134,838	22.04%
Alcohol	194,676,290	210,881,225	214,071,660	206,543,058	50.50%
Soft drinks	7,997,634	8,460,911	10,632,414	9,030,320	2.21%
Water	903,373	1,808,515	1,985,041	1,565,643	0.38%
Plastics	2,253,537	2,761,107	5,153,663	3,389,436	0.83%
Services (Airtime)	97,953,875	86,262,928	94,500,918	92,905,907	22.72%
Others (Cosmetics)	3,299,677	2,693,162	10,196,865	5,396,568	1.32%
Total	390,539,130	397,210,044	439,148,135	408,965,769	

Graphic comparatives Kenya



The Kenyan comparatives indicate that Tobacco and Alcohol form the bulk of the excise tax collected in any given period. Excisable services specifically mobile phone airtime. Though the increase in consumer numbers for mobile phone services have increased over time, the excise tax collected from the same has reduced due to a reduction in the tariff rates. Plastics on the other hand have been a major source of debate regarding whether excise tax is the best way to regulate and control the industry. The data comparatives indicate that excise revenue collected from excise tax only forms 0.83% of the total excise tax collected hence its exclusion from the list of excisable products is not likely to have a significant impact on the excise revenue. The Kenyan 2012 Finance Act as read together with the Finance Bill 2013 introduced excise duty on fees, charges and commissions charged by financial institutions licensed by the Banking Act, the Insurance Act, the Central Bank of Kenya (CBK) Act, the Micro Financial Institutions Act or the

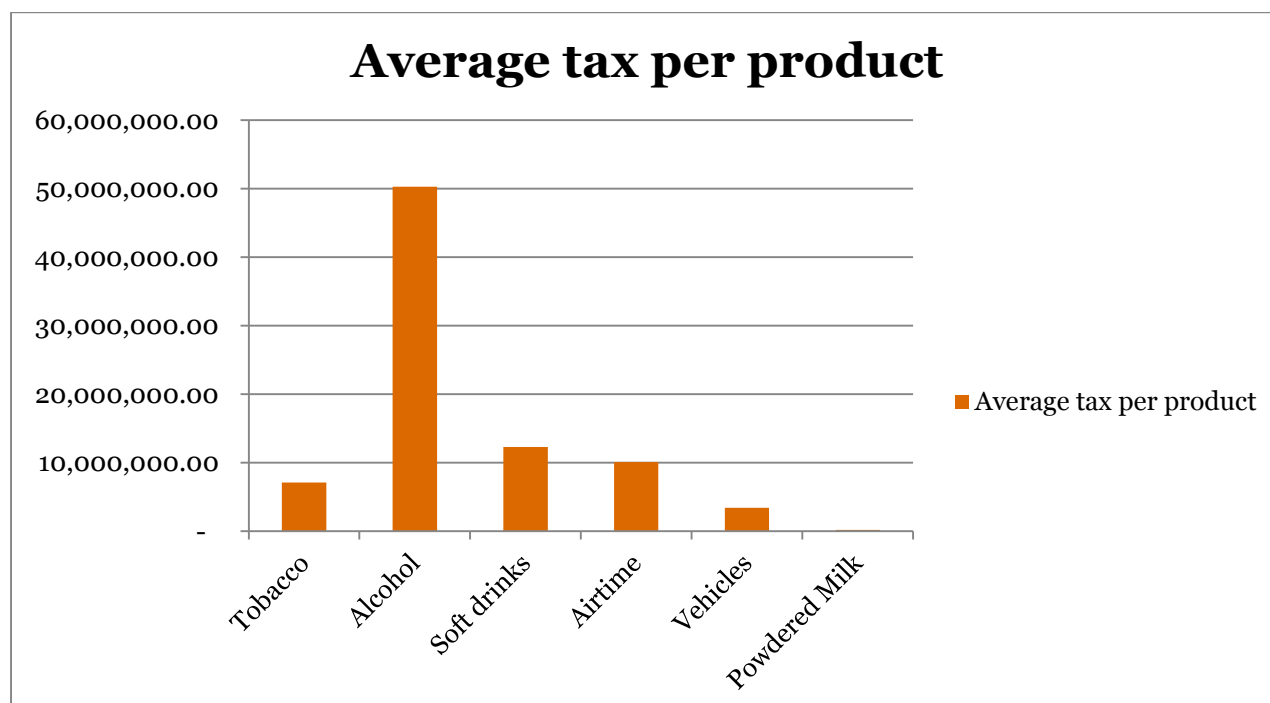
Sacco Societies Act. This introduction will increase the excise tax collected from services in coming years.

3. Rwanda

Excise Tax collected	Year 2010	Year 2011	Year 2012	Average tax per product	Percentage per product
Tobacco	6,679,011	6,985,184	7,630,363	7,098,186	8.51
Alcohol	40,670,370	51,327,373	58,849,802	50,282,515	60.27
Soft drinks	11,150,717	11,881,219	13,931,276	12,321,071	14.77
(Airtime)	6,655,207	10,701,289	12,955,972	10,104,156	12.11
Vehicles	2,493,396	3,356,812	4,456,061	3,435,423	4.12
(Powdered milk)	96,406	251,783	214,034	187,408	0.22
Total	67,745,107	84,503,660	98,037,508	83,428,759	

The excise duty revenue collected on soft drinks in Rwanda is extremely high at 15% compared to other partner states because Rwanda has the highest rate of excise duty on soft drinks

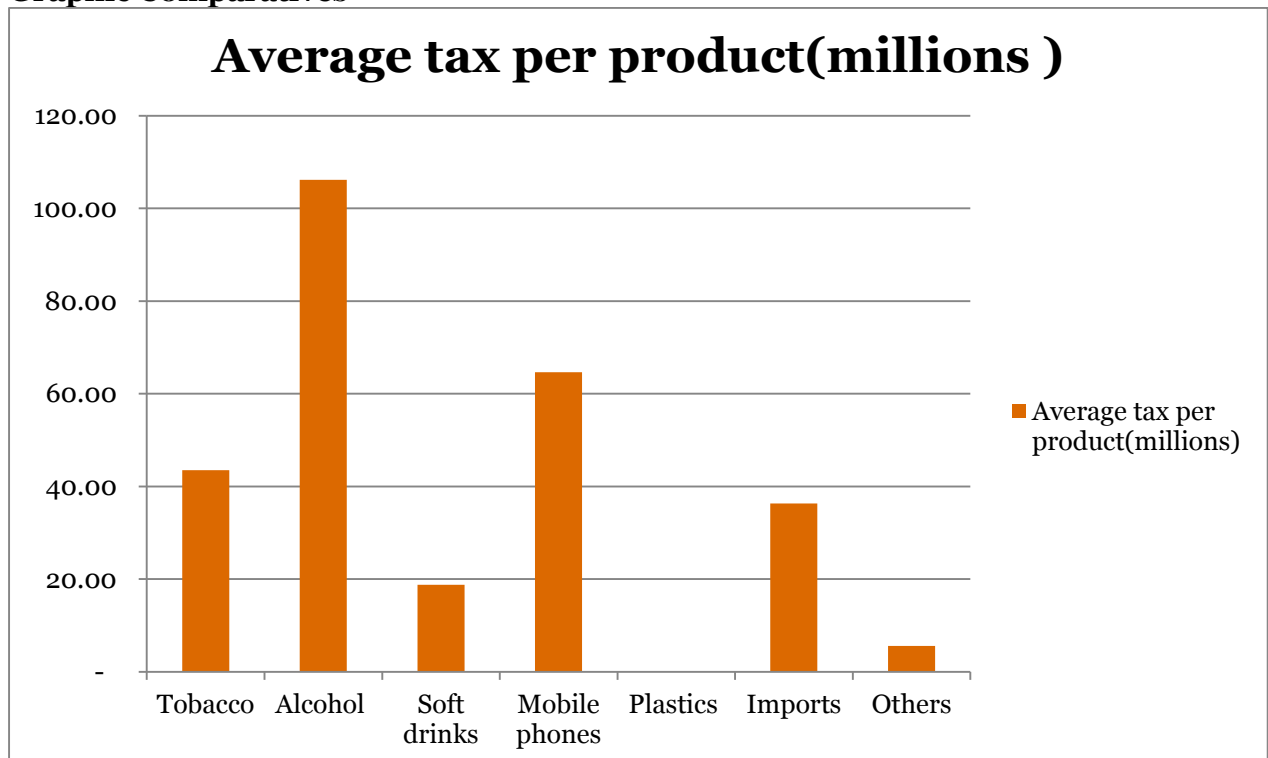
Graphic Comparatives



4. Tanzania

Excise Tax collected	Year 2010	Year 2011	Year 2012	Average tax per product(millions)	Percentage by Product
Tobacco	38,360,198	42,571,149	49,517,141	43,482,830	15.81
Alcohol	90,112,714	99,926,298	128,526,824	106,188,612	38.61
Soft drinks	16,843,874	17,807,210	21,631,186	18,760,756	6.82
Mobile phones	59,459,835	62,335,965	72,256,599	64,684,133	23.52
Plastics	39,585	10,732	7,569	19,295	0.01
Others	6,428,785	1,479,094	8,931,151	5,613,010	2.04
Total	211,244,991	224,130,448	280,870,470	275,055,112	

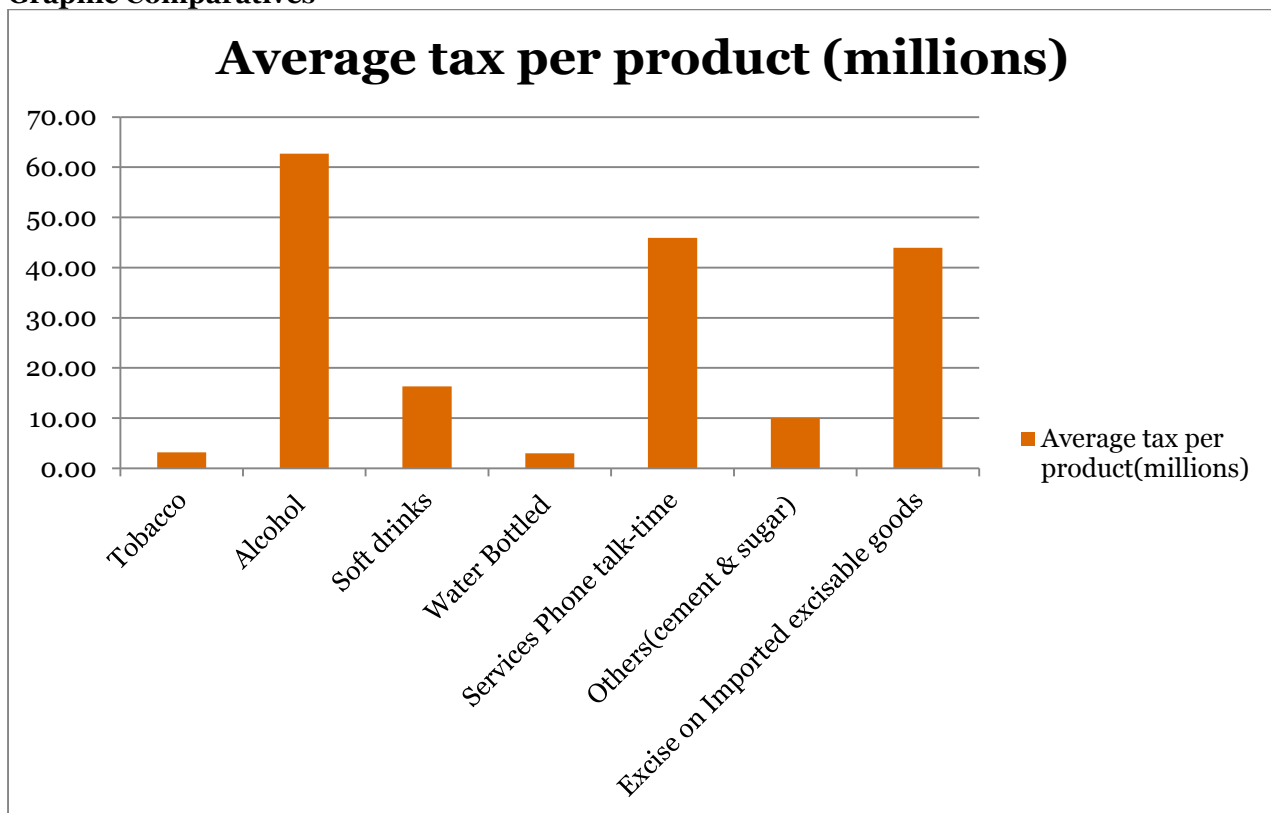
Graphic Comparatives



5. Uganda

Excise Tax collected	Year 2010	Year 2011	Year 2012	Average tax per product (millions)	Percentage by Product
Tobacco	3,700,000	2,800,000	3,000,000	3,166,667	1.71
Alcohol	53,800,000	58,800,000	75,500,000	62,700,000	33.89
Soft drinks	13,700,000	16,200,000	19,000,000	16,300,000	8.81
Water Bottled	2,100,000	3,500,000	3,400,000	3,000,000	1.62
Services Phone talk-time	49,000,000	43,300,000	45,400,000	45,900,000	24.81
Others(cement & sugar)	12,500,000	10,900,000	6,600,000	10,000,000	5.40
Excise on Imported excisable goods	39,200,000	40,100,000	52,600,000	43,966,667	23.76
Total	174,000,000	175,600,000	205,500,000	185,033,334	

Graphic Comparatives



The above analysis points out the following facts regarding excise duty collection in the EAC:

- a) The bulk of the excise duty is collected from certain products namely Alcohol, tobacco and motor vehicles with alcohol and tobacco contributing to an average of 58% of excise tax revenue in the EAC;
- b) Most Partner States have outlier products that contribute minimal volumes to excise duty revenue collected among the Partner States.
- c) While most Partner states have data on the volumes of excise duty collected, there is no adequate documentation of excise duty foregone from the remissions granted in the various Partner States.

6. *Proposal on a common list and “rate” of excisable products*

Common list of excisable products

Currently the EAC lacks a common list of excisable products and this is the cause of the variations in the excisable products from partner state to partner state. The partner states therefore need to define a common list of excisable goods that will then be adopted across the EAC.

It is important to note that such a list for excisable services is not necessary as the excise tax legislation does not affect or hamper free movement of services in the EAC.

Excisable products										
	Alcohol	Motor Vehicles	Tobacco	Petroleum products	Soft drinks	Plastics	Cosmetics	Sugar	Milk powder	Cement
Burundi	Y	Y	Y	Y	Y	-	Y			
Kenya	Y	Y	Y	Y	Y	Y	Y	Y		
Rwanda	Y	Y	Y	Y	Y	-	-	-	Y	
Tanzania	Y	Y	Y	Y	Y	-	-			
Uganda	Y	-	Y	Y	Y	Y	Y	Y		Y

As depicted by the table above, Kenya and Uganda have the largest list of excisable goods. This means that there is need to harmonise the list of the excisable products to not only ensure a common list for the EAC Partner states but also one that is in line with the international practice on excisable products.

By and large, the EAC Partner States impose excise tax on the same products, namely;

- alcoholic beverages,
- tobacco,
- motor vehicles,
- petroleum products,
- soft drinks, and
- bottled water

Despite the few outliers (such as plastics, cosmetics, sugar, cement, milk powder), it is quite evident that harmonizing products subject to excise within the EAC should not pose serious challenges. This can be achieved for example by dropping the outliers from the list.

A measure to cover any revenue losses arising from dropping some of the excisable items from the common list would be to have the products dropped from the list of excisable product subjected to another form of tax such as an increased rate of VAT or sales tax which will then cover the revenue loss. From review of the other jurisdictions (detailed under literature review), it is important to note that the trading blocs agreed on a list of excisable commodities as indicated in the table below;

Trading bloc	Excisable products
ASEAN	Motor vehicles, alcohol and tobacco
EU	Energy products, electricity, alcohol and manufactured tobacco
SACU	Petroleum products, alcoholic beverages, tobacco, and a few luxury goods

This indicates that there is a lot of similarity in the excisable products across the three trading

blocs.

To be in line with international practice, we recommend that EAC adopt the following list as the main excisable goods;

- Alcoholic beverages,
- Cigarettes,
- Motor vehicles, and
- Petroleum products.

This common list has been arrived at on the following basis;

- a) Our review of revenue analysis clearly shows that alcohol and tobacco contribute to 58% of total excise revenue, once you include the excise revenue from the other two products (motor vehicles and petroleum products), the excise revenue will not significantly be impacted by the exclusion of soft drinks and the outliers. The value and the excise component on the other products is low such that whether excise tax is charged on them or not it does not affect free movement of goods across the partner states.

	Tobacco	Alcohol	Total %
Burundi	6.00	55.00	61.00
Kenya	22.04	50.50	72.54
Rwanda	8.51	60.27	68.78
Tanzania	15.81	38.61	54.42
Uganda	1.71	33.89	35.60
Total Average	10.81	47.654	58.47

- b) Our review of comparable jurisdictions clearly shows that the four products listed above are excisable in all the comparable jurisdictions and that the outlier products were not excisable in most of these jurisdictions. It will be therefore in line with the prevailing international best practice.
- c) The majority of the stakeholders that we interviewed were of the view that the main role of excise duty is revenue collection with 51% of public sector respondents and 48% of private sector respondents holding this view (See section 4 above). With this clear assertion therefore, it is only necessary that excise duty is charged only on products which excise duty forms a major part of the price. These products are the ones listed above.

Average percentage Excise duty collected from outlier products					
Excise Tax collected	Burundi	Kenya	Rwanda	Tanzania	Uganda
Plastics	0	0.83	0	0.01	0
Others (Cosmetics)	0	1.32	0	2.04	0
Cement	0	0		0	2.8
Powdered milk	0	0	0.22	0	0
Total	0	2.15	0.22	2.05	2.8

This indicates that there is no significant revenue loss in any of the Partner States if excise duty on outlier products is not collected. This would also create a more level tax environment for the traders from all the Partner States.

The partner states should then discuss and determine whether soft drinks should be retained among the excisable goods. Such a determination will also be driven by the alternative measures that can be adopted to compensate for the revenue losses

To be able to achieve the above mentioned common list it is important that the products especially alcohol and tobacco, are defined and structured similarly across the partner states since these products are defined and classified differently for excise duty purposes across the partner states.

From our review, the excise duty structure for motor vehicles and petroleum closely aligned (nearly harmonised) across the EAC. It is therefore important for the partner states to focus on Alcohol and Tobacco in the harmonisation process; this is because besides the two contributing 58% of revenue they are the only two products where excise duty forms a major proportion of the price. For example no one would smuggle cement from Burundi to Uganda due to the differences in the excise duty regimes in the two countries.

Harmonised classification rules should be developed to complement the definitions that are currently in use. The rules should be based on well-defined criteria, such as the process by which they were manufactured, primary material used and content; or harmonised to match those of the EAC Common External Tariff (EAC CET). These rules should ensure consistency in classifying products across the Partner States.

A common list of excisable goods will eliminate market distortions. This will result in a shift from informal activities to formal trade activities and attract investment within the EAC.

It is our considered opinion therefore that while the excise duty regimes differ across the EAC, they do not have an impact on free movement of the other products namely soft drinks, water, sugar, powdered milk, plastics or cement as excise does not form a significant portion of the price.

Excise duty rates

EAC partner states are still charging excise duties on highly different tax bases. Since the partner states are at different economic stages, proposing common rates of excise tax will not be feasible. We therefore propose the setting a floor (minimum rate) and a ceiling (maximum rate) of excise duty within which all countries will then have to operate.

While the setting of excise duty rates at a floor and a ceiling is a possibility, the different structures adopted by the different partner states (specific, advalorem and hybrid) would make it difficult to set a common rate or a range of rates since the outcomes would be different. The valuation base would also be different with the various countries using a variety that includes ex-factory, retail selling price and warehouse price invariably.

In summary, the regimes are varied as shown below

Subject	Burundi	Kenya	Rwanda	Tanzania	Uganda
Structure	<ul style="list-style-type: none"> Alcohol-Specific and ad valorem Tobacco-Ad valorem Petroleum Products-N/A Others-Specific and ad valorem Airtime - <i>Ad valorem</i> 	<ul style="list-style-type: none"> Alcohol-Specific and ad valorem Tobacco-Specific and ad valorem Petroleum Products-Specific Others-Specific and ad valorem Airtime - Specific <i>Ad valorem</i> 	<ul style="list-style-type: none"> Alcohol-Ad valorem Tobacco-Ad valorem Petroleum Products-Specific Others Ad valorem Airtime - <i>Ad valorem</i> 	<ul style="list-style-type: none"> Alcohol-Specific Tobacco-Specific Petroleum Products-Specific Others-Specific and ad valorem Airtime - <i>Ad valorem</i> 	<ul style="list-style-type: none"> Alcohol-Ad valorem Tobacco-Specific and ad valorem Petroleum Products-Specific Others-Specific and ad valorem Airtime - <i>Ad valorem</i>
Valuation method	•	• Ex-factory and RSP	• Ex-factory	• Ex-factory	• Ex-factory and RSP

Valuation methods

Ad Valorem/Transaction value

The determination of value upon which ad valorem duty rates is applied is based on the transaction value of such goods. The transaction value is the price actually paid or payable, adjusted to include price paid for commissions except buying commission, containers and packaging, cost of assists, royalties, licence fee, ocean or air freight except transport incurred after importation, and insurance. Duties and taxes paid in the Partner States are excluded if they are part of the transaction value. Transaction value is the primary basis of valuation subject to the following conditions:

- There is evidence of sale for export;
- No restriction on the disposition or use of goods by the buyer;
- No part of the proceeds of any subsequent sale or use of the goods by the buyer will accrue directly or indirectly to the seller;
- The buyer and seller are not related, or where the buyer and seller are related, that the transaction value is acceptable for customs purposes.

A transaction value between related parties is acceptable if the circumstances of the sale of the imported goods indicates that the relationship did not influence the price actually paid or payable, or if the transaction value closely approximates the transaction value, deductive value or computed value of identical or similar merchandise, also known as “test values”.

Ad Quantum

In case of ad quantum, the duty is payable on the basis of certain unit e.g. weight, length, volume etc.

Retail Selling Price (RSP)

RSP means the maximum price which the excisable goods in packaged form maybe sold to the ultimate consumer and includes all taxes, freight,commission payable etc.

Significant differences in tax rates induce cross border shopping and smuggling activities; thus the only outcome often is tax evasion and criminal behaviour including corruption. This is because these differences provide leeway for products made in one country to be sold profitably in another country at a cheaper price despite the effect of transportation costs being factored in. A floor and ceiling type of rate system will address the disparity in cross border regimes in the rates.

As noted from the other trading blocs, agreeing on common rates is not achievable. The ASEAN trading bloc is still addressing rates differential while the EU settled on a rates system that provides for a floor and a ceiling with the countries allowed a leeway to choose the most appropriate and according to their preferences.

Please see **appendix 3** attached for the variances in valuation methods and excise structure.

7. Review of Remission schemes and proposal of an appropriate regime

Review of the existing remission schemes

Country	Remission	Exemption	Comments
Burundi	Exemption is granted on imported sugar for the industrial production of beer and soft drinks	None	None
Kenya	<p>Goods delivered by the manufacturer to the Navy, Armed and Air force institutes, Armed Forces canteen organisations, privileged bodies and persons;</p> <p>In the case of spirits they have been delivered from a distillery or distiller's warehouse for use in medical, scientific or educational purposes; or delivered for denaturing in a bonded warehouse.</p> <p>Petroleum oils refined in Kenya;</p> <p>Only beer made from locally sourced sorghum or millet is subject to remission</p>	<p>Goods entered under bond</p> <p>Goods imported for temporary use;</p>	Beer made from local raw materials are cheaper as compared to imports. This renders imports from other EAC States less competitive in the country because of the price differentials arising from the remission scheme. As a result this compromises the objective of free movement of goods across the Partner States
Rwanda	None	None	The exemption/remission schemes do not cover raw materials from EAC
Tanzania	<p>Remission (by way of reduced excise duty rates) on alcoholic beverages and fruit and vegetable juices made using local raw materials</p> <p>Remission or refund on spirits delivered for denaturing and spoilt beer.</p> <p>Remission on fuel imported by mining companies</p> <p>Remission on cigarettes made from 75% local tobacco.</p>	None	Products made from local raw materials are cheaper as compared to imports. This renders imports from other EAC States less competitive in the country because of the price differentials arising from the remission scheme. As a result this compromises the objective of free movement of goods across the Partner States
Uganda	<p>Remission (by way of reduced excise duty rates) on alcoholic beverages made using local raw materials.</p> <p>Spirits used in the manufacture of denatured spirits by a denaturer's at the denaturer's factory.</p> <p>Cigarettes made from local tobacco</p>	None	Products made from local raw materials especially alcohol made from local barley or wheat are cheaper compared to imports

Exemption Schemes

The Partner States have exemption regimes that cover a variety of areas, these include:

- Products entered for export,
- Products for privileged institutions and other diplomatic institutions, and
- Other products for specified use such as diplomatic duty free shops and good for certain targeted sectors such as oil exploration.

Though all countries have varied exemption schemes, the criteria for these exemptions is not clearly laid out or well agreed upon across the partner states. The main impact this has is on the attraction of investments and promotion of EAC as single investment destination. Other differences regarding the warehousing processes for goods meant for another Partner State as well as the declaration procedures for these goods need to be addressed

Best exemption scheme

It is our considered opinion therefore that:

- the Partner States need to establish an agreed criteria for granting excise duty exemption across the Partner States. This will guide the each Partner State as they seek to establish their own list of exempt items/institutions,
- the Partner States also need to agree common warehousing procedures, declaration and documentation requirements for products destined for another Partner State .

Remission Schemes

Although the remission schemes in the Partner States are all geared towards promoting domestic agricultural sector through the creation of ready market for the raw materials, the overall effect is that excisable products made from domestic raw materials are cheaper compared to imports and this in itself discourages the importation of these products into countries where such remission schemes exist. Furthermore, the distortions create smuggling where consumers would move across the borders to purchase the beverages in the country where prices are low and bring them into their own countries.

As the EAC economies are mainly agriculture based, the Partner States feel the need to support this important sector by providing for remissions or reduced excise rates on products made from local raw materials. Such initiatives are aimed at improving economic growth, industrialisation through value addition on agricultural products and the reduction of poverty amongst farmers. Among the Partner States, Uganda has the most comprehensive local raw materials regime with regard to its alcoholic beverages, followed by Tanzania. Kenya also has a remission scheme targeting certain alcoholic products brewed using local sorghum and millet.

A clear criteria and an agreed basis for the remission schemes between partner states would ensure that its effects are fairly spread in the EAC and hence ensure it does not create any price distortions in the trade among the Partner States. In addition the following need to be addressed:

- Refunds and remission by Partner States: On products released for consumption due to certain conditions, for example, spoilages, expired products and exports. The procedures to be followed are not similar among the Partner States.

Impact of varied remission schemes

	Kenya	Uganda
Excise rate for Malt beer	\$0.83 per litre	imported malt-60%, local malt- 40% and whose local raw material content, excluding water is at least 75% by weight of its constituents- 20%
	Kenya	Tanzania
Excise Tobacco	Cigarettes prepared from Tobacco and including any form of tip USD 14.29 per Mille or 35% of RSP	Cigarettes without filter containing more than 75% domestic tobacco at USD 5.29 per Mille. Other cigarettes at USD 22.66 per Mille

Alcohol			
	Retail price of beer in Kenya	Retail price of beer imported from Kenya to Uganda	Retail price of beer in Uganda using 75% local raw material
Assuming 1 litre of beer= \$2	2	2	2
Excise rates	0.83	1.2	0.4
Retail price of beer	2.83	3.2	2.4

Tobacco			
	Retail price of 1 Mille in Kenya	Retail price of a Mille imported from Kenya to Tanzania	Retail price of a Mille made in Tanzania using 75% local raw material.
Assuming 1 Mille is \$50	50	50	50
Excise rates	14.29	22.66	5.29
Retail price of cigarettes	64.29	72.66	55.29

Juices and soft drinks

The excise tax on fruit juices across these member states can be summarised as follows.

	Country	Excise Duty rate
1	Burundi	USD 21 per hectolitre which is equivalent to USD 0.21 per Litre
2	Kenya	7% of Ex-factory price
3	Rwanda	39% of Ex-factory price
4	Tanzania	a) Local raw materials USD 0.01 per Litre. b) Imported raw materials USD 0.05 per Litre
5	Uganda	13% of Ex-factory price

There is insignificant price distortion when soft beverages are exported from within the EAC partner states since the value of the products and the excise component is low. An example is as illustrated below.

Juices			
	Retail price of juice in Kenya	Retail price of juice imported from Kenya to Tanzania	Retail price of Juice in Tanzania using local raw material
Assuming 1 litre of juice= \$2	2	2	2
Excise rates	0.14	0.05	0.01
Retail price of Juice	2.14	2.05	2.01

The only challenge on their cross border movement will therefore be more of nontariff barriers and supply chain logistics as opposed to excise duty.

Proposal on appropriate remission regime

There are three ways to address the problem created by remission schemes;

1. The Partner States could agree to retain the status quo on these remission schemes. This will have a no impact on the excise duty revenue on the Partner States, the challenge with this is however the fact that the distortions will remain and hence the harmonisation process will not have made any step forward.
2. To define local raw materials as those from the entire EAC. This will mean that remission will be granted on any product that uses raw materials from any of the Partner States. Such a scheme will ensure that there are no price distortions on products when traded into the Partner States. This will in turn increase the ease of free movement of goods.
3. Eliminate the remission schemes entirely. This will ensure that there is no impact on prices of excisable goods when they are moved across the Partner States. This will also enhance free movement of goods. However as mentioned, the elimination of local raw material remission should be done in consultation with industry players as this poses the risk of losing consumers to illicit products such as unhygienic alcohol as the case witnessed in Kenya.

Having reviewed the various exemption regimes, economic blocs and the stakeholder concerns regarding the remission schemes, it is our considered opinion that **option 3** above is the most feasible due the following reasons:

- a) Under option 1 the challenges being currently experienced as a result of the distortions created by the remission schemes will continue to exist,
- b) The second option will be extremely difficult to implement as the benefits of the scheme will accrue to the partner state producing the raw materials and not to the partner state in which the excisable products will be consumed and taxed.

These two factors therefore indicate that only option 3 is feasible as a way forward on the exemption regimes.

It is important no note that the exemption schemes are dictated by other factors such as bilateral agreements and diplomatic relationships of the specific Partner States and hence it will be necessary to grant the partner states some level of autonomy in determining which exemptions to grant.

***8. Revenue implications
of the proposed
harmonisation
scenarios***

From the phase one report, there were three proposed harmonisation scenarios as detailed under chapter 3 of this report. In this section we seek to identify the various likely revenue implications of these proposed scenarios of harmonisation.

In the table below, we have summarised the various scenarios and the likely impact on revenue on a qualitative basis.

#	Proposed harmonisation scenario	Likely impact on revenue	Comments
1	<p>Harmonised procedures and structures; but country-specific rates This will involve the Partner States retaining their sovereignty in determination of the applicable excise duty rate to apply for each product.</p> <p>The relevant areas of harmonisation are (i) procedures and administration, (ii) classification rules and definitions and (iii) remission schemes as described below</p>	Depends on the Partner States and the decision taken regarding (iii) (see details below)	The major area of harmonisation with revenue impact will be (iii) on the remission schemes
2	<p>Harmonised procedures and structures; but country-specific basis of levying excise duty</p> <p>The Partner States retaining their sovereignty in determination of the basis of levying excise duty (i.e. specific, <i>ad valorem</i> or hybrid) as well as the applicable excise duty rate for each product.</p> <p>The relevant areas of harmonisation are (i) procedures and administration, (ii) classification rules and definitions and (iii) remission schemes as described below</p>	This is linked to scenario 1, the revenue impact is dependent on the Partner State	This has been addressed below
3	<p>Complete Harmonisation</p> <p>In this scenario, the Partner States would in addition to harmonisation of areas i) procedures and administration, (ii) classification rules and definitions and (iii) remission schemes also agree to the harmonisation of all the excise rates for all the excisable products.</p>	Depends on Partner State	This would be a culmination of scenario 1 & 2 above and hence all items of revenue implication would have been addressed under 1& 2.

Scenarios in detail

1. Harmonised procedures and structures; but country-specific rates

This scenario would involve harmonisation of the structures of excise taxation with regard to the basis of levying excise duty i.e. specific, *ad valorem* or hybrid. This means that a product, say beer, would be subject to the same definition, classification and basis of levying excise duty in

each of the Partner States. This scenario would involve the enactment of a single EAC Excise Management Act for use by all the Partner States (much like the EAC Customs Management Act). The only difference would be that this Act would have attached to it schedules specific to each country setting out the basis of levying excise duty and the applicable duty rates in that country.

2. Harmonised procedures and structures; but country-specific basis of levying excise duty

The Partner States retaining their sovereignty in determination of the basis of levying excise duty (i.e. specific, *ad valorem* or hybrid) as well as the applicable excise duty rate for each product. This scenario can further be negotiated to include a range of excise duty rates which the Partner States can impose on their products. This would involve setting of a minimum and maximum rates which the States can operate within. This would be a further step in the journey to full harmonisation.

3. Complete Harmonisation

This scenario should be considered as a continuation to Scenario 1 and/or Scenario 2 above in which different rates would be set as feasible in each of the Partner States with a view to a gradual convergence into a single rate per product.

It would be important at this stage to consider the different products that one Partner State imposes excise duty on, that the others do not e.g. cement in Uganda and powdered milk in Rwanda. This could be addressed by either having a transition period in which the Partner States would align the list of excisable goods or having a list of sensitive goods (as in the CET) and thereby letting such goods remain excisable in that Partner State.

In addressing the various harmonisation scenarios as proposed under the phase one report, we were informed by the various areas of harmonisation as proposed under the same report.

Areas of harmonisation

i) Procedures and administration

The key areas pointed out as requiring harmonisation and procedures and administration were;
Definitions of excisable products,

Approval of persons and premises: This includes licensing of manufacturers, approval of premises and equipment, accounting for stock and movement of goods, operations of an excise warehouse, etc.

Tax point: have a clear understanding of when goods become liable to excise tax and when the excise tax must be paid.

Reimbursement and remission by Partner States,

Exemptions: For specified use or reason (diplomatic sales, duty free shops, armed forces, etc).

Procedures on movement of excisable goods within the EAC:

Use of technology to facilitate payment of excise tax and monitor movement of excisable goods in the EAC region.

If harmonisation of the administrative procedure produces a scenario where excise duty is mainly collected from the four major products (alcohol, tobacco, motor vehicles and petroleum) as

identified in the previous section the estimated excise duty from these products in the various countries would be as detailed below.

Partner State	Current collection (Average)	Excise duty collected from the four products	Excise duty collected from the other products	Percentage
Burundi	-			
Kenya	431,390,884	427,061,530	4,329,354	1.00
Uganda	543,767,789	453,593,369	90,174,419	16.58
Tanzania	435,907,814	357,952,646	77,955,168	17.88
Rwanda	135,526,198	109,520,641	26,005,556	19.19

The compensation point for the foregone excise duty would be the possible revenue collected through other taxes such as Value Added Tax (VAT) and Income Tax. The numbers can however only be established through a detailed analysis done over a determined period during implementation.

ii) Classification rules and definitions

Though the EAC Partner States have mostly common excisable goods, these goods are defined and classified differently for excise duty purposes. It is vitally important that a product be treated the same for excise purposes in all Partner States.

iii) Remission schemes

While the remission schemes in the Partner States are all geared at promoting trade and making locally manufactured goods more competitive, harmonisation of remission schemes would ensure that the definitions are clear and it would also increase and simplify trade especially for regional investors as the schemes would be similar in procedures and administration

iv) Excise duty rates

Owing to the different per capita income in the Partner States, it would be more feasible to start with setting maximum and minimum excise rates with the goal of facilitating a gradual convergence to single common rates. This would ensure that the Partner States are shielded from sudden changes that would affect their development plans

How do the scenarios then link to revenue?

From our discussion in the preceding chapters it is clear that areas **i**, and **ii** do not have an impact on revenue collection. Areas **iii** and **iv** however have an impact on revenue collection. It is important to note that all the four areas proposed under the harmonisation scenarios have an equally significant role to play in the harmonisation process in achieving the various proposed harmonisation scenarios. We therefore dwell on areas **iii** and **iv** in our analysis as shown below. In looking at these areas we have made an effort to first determine whether the area of harmonisation will have an impact on revenue or whether it will have a neutral impact on revenue. The subsequent numerical simulation is then purely for purposes of simulating the likely impact as this is based on data whose quality is not verified.

Remission schemes

#	Possible Scenario	Likely impact on revenue	Comments
1	Retain status quo	This will have neutral revenue impact	Whilst there is a neutral excise revenue impact, it potentially results in distortions that hinder free movement of goods between partner states
2	Remission to be applied across the EAC	Adverse	This will mean that remission will be given on products from other partner states. Whilst this facilitates free movement of goods between partner states, the recipient partner state giving remission will have less excise revenue
3	Scrap the remission schemes	Favourable on excise; possible adverse economic impact	This will mean that the excise for local produced goods and those from other partner states will have equal excise duty treatment and thus facilitate free movement of goods. The partner states will need to determine if there is any adverse impact on their agriculture and manufacturing sectors and how this will be dealt with.

If excise duty remission is scrapped across the partner states

Country	Current collection (Average)	If no remission is granted**	Estimated increase in Excise collection	Percentage
Burundi	-	-	-	
Kenya	431,390,884	436,692,677	5,301,793	1.23
Uganda	543,767,789	574,735,711	30,967,923	5.70
Tanzania	435,907,814	509,796,566	73,888,752	16.95
Rwanda	135,526,198	135,526,198	-	-

The workings are based on the assumption that the elimination of remission will have a directly proportional impact on the excise duty collected. This ignores the likely impact on consumer behaviour (A detailed calculation is contained in Appendix 2 Attached)

The above calculations show the likely impact on revenue if the remissions are scrapped under a harmonised regime. On the other hand, it is important to note that the exemption schemes are dictated by other factors such as bilateral agreements and diplomatic relationships of the specific Partner States and hence it will be necessary to grant the partner states some level of autonomy in determining which exemptions to grant

***9. Most suitable way of
harmonisation and
best options***

Article 32 Common Market protocol provides that *the Partner States undertake to progressively harmonize their tax policies and laws on domestic taxes with a view to removing tax distortions in order to facilitate the free movement of goods, services, and capital, and the promotion of investments within the Community.*

We analyse below the objectives of Harmonisation and the hindrances based on the existing tax regimes across the Partner States;

Policy area/Objective	Hindrance
Free movement of goods and services	<ul style="list-style-type: none"> • Local raw materials remission schemes; • Significant variances in tax rates especially in tobacco, alcohol and soft drinks in Rwanda and Burundi; • Lack of clear definition of the principle being applied in imposition of excise duty on alcohol and tobacco.
Free movement of capital;	<ul style="list-style-type: none"> • Lack of clear definition of services; • Significant variances in tax rates
Attracting investment in EAC	<ul style="list-style-type: none"> • Administrative procedures; • Significant divergences in the applicable laws.

Harmonisation of excise duty in the region is a process that is long overdue and that is expected to bring with it a lot of benefits to the countries in the region, the manufacturers of excisable products as well as providing a better environment for the revenue authorities to collect revenue from excise duty.

Regarding remission granted on products from local raw materials, the country would lose the same average revenue as indicated above albeit with some compensation in the form of increased revenue from locally produced alcohol and tobacco products. This would be because excise duty lost on local raw material remission would be eliminated. Tanzania and Uganda have remission schemes for certain categories of alcoholic products made from local raw materials. As detailed under the analysis of remission schemes, such remissions make the goods produced using local raw materials have an edge over the imported products. It is important to note that this being an economic bloc, price distortions should not exist for goods imported from within the region.

To deal with the problem of varying excise rates, the partner states will have to set a floor and a ceiling to be used by all the EAC countries as a guide. The likely challenges to be encountered during this process include, some countries might keep their rates very close to the floor hence making them more attractive for excise duty and this could lead to price distortions. Certain producers of excisable products could choose to operate only in those countries with the lower rates.

The partner states could also choose to harmonise all the legal frameworks below in a gradual manner to lead to a fully harmonised excise tax regime. This will ensure that the legislation is tailored such that the regional distortions in prices of goods resulting from movement across the

states are eliminated. This option also envisages a long term situation where the excise duty law in the entire EAC region will be at a similar level with the EACCMA which provides for high levels of cohesion in the excise tax law across the states.

1. Ensure that there is a common principle and the related criteria for imposing excise duties on goods and services
2. Ensure that there is an agreed common treatment on goods manufactured using EAC local raw materials.

Most Suitable way of harmonisation

In assessing the advocacy areas we categorised the focus areas into four.

1. Exemption and remission schemes
2. Petroleum and Motor vehicles
3. Tobacco and alcohol products
4. Excise lite products (soft drinks, water, plastics, cement etc) where excise duty does not form a significant portion of the price

1. Exemption and remission schemes

Partner states should agree on common criteria for exemption of products and administrative procedures around products imported for export to other partner States or products intended for privileged institutions. This includes the warehousing and documentation procedures. While the individual Partner States will retain sovereignty over their own exemptions, the common criteria will serve as the overall guidance on the inclusion of items into this list. The remission schemes also need to be aligned to ensure that the free movement of good is not affected. We have detailed the review of remission schemes under **Section 7** of this report and therefore it is our opinion that the remission schemes need to be scrapped. **We have provided further details in the chart below.**

2. Motor vehicles and petroleum products

As mention under section 6 to this report the Partner States have a significantly aligned excise duty regime for motor vehicles and petroleum products. This level of harmonisation is highly beneficial; there is however steps that can be made to ensure that there is uniformity in criteria and documentation procedures across the EAC. Therefore as part of the next step forward the Partner States should agree on a common range of rates and criteria for the imposition of excise duty on these products.

3. Tobacco and Alcohol

Structure, rate and remission

- This will mainly be focused on the tobacco and alcohol products as discussed under chapter 6. Advocate for harmonised structure, valuation method and rates for alcohol and tobacco within the region.
- Focus on finding an agreeable remission scheme that does not hinder the free movement of goods.

Smuggling and illicit products

- Smuggling affects both the two focus sectors (alcohol and tobacco) by denying them revenue and eroding the market. It also denies government excise duty revenue.
- Illicit products besides having a similar effect as smuggling have the added disadvantage of lacking quality control hence affecting health of consumers.
- **This should be an item of focus for the stakeholders to protect the legitimate businesses**

Availability of products

- The best way to address the challenge of smuggling/illicit products is to advocate for an excise duty regime that ensures the products are affordable to the lower level consumer. This could be by a way of remission schemes targeting products intended for certain consumer categories. This will drive up the sales volumes and increase revenue collection.

The major factor behind the main focus being on alcohol and tobacco products is because excise duty forms a significant portion of the price and hence they are more prone to counterfeiting and smuggling. They also provide the bulk of excise duty revenue across the Partner States

4. Excise lite products

These are mainly the outlier products that include soft drinks, water, plastics, cosmetics, cement, and powdered milk among others. It is important to note that these products do not suffer from the challenges of smuggling and counterfeiting as is the case for alcohol and tobacco products. Secondly excise duty does not form a significant portion on these products. The advocacy area on these should therefore be mainly focused on:

- a) Establishing whether to retain excise duty on these products or whether to eliminate them from the list of excisable products (see section 6 of this report) and hence use alternative taxes to generate revenue
- b) If they are to be retained the Partner States should establish a clear set of guidelines on what makes a product be subject to excise duty.
- c) Focus on carrying out a good review of the regimes to ensure that the products standards as well as the duty rates are close to each other to enable ease of movement of capital across the Partner States. This is because the rates of duty are highly varied across the Partner States.
- d) Whether the Partner States choose to maintain certain outlier excise lite products in the category of excisable products or not, it will have no impact on free movement of goods

In addressing all the following areas of concern, there should be certain level of attention paid to the following areas.

- The bloc is predominantly made up of agriculture driven economies, the excise harmonisation process should therefore give due regard to the impact of agriculture on the economy. The states therefore need to determine how to grow the sector, either through remission schemes or through specific sector based incentives.
- Non-tariff barriers also play a major role in determining the ease of movement of goods across the Partner States; these include documentation requirements, ease of transportation, standardization as well as packaging requirements.
- Excise procedures such as documentation requirements as well as return filing and licensing procedures need to be addressed as well.

Other recommendations

To facilitate harmonisation process, we highlight below the other vital areas that stakeholders should focus on. This is based on outcome of our interviews with the various stakeholders in the Partner States.

- 1) Capacity building at EAC and in the Partner States for the development of legal instruments and tax administration. This will encompass ensuring that the people charged with driving the harmonisation agenda as well as developing the legal instruments within the specific Partner States have a clear understanding of the desired outcome of the harmonisation process. This will ensure that progress in the harmonization of the regimes is synchronized.
- 2) Deployment of technology tools to monitor cross border activities in goods and services- eventually once an EAC wide common electronic system is in place, businesses could be supplying good and services across the Partner States without the need to complete cross border customs formalities and the revenue authorities of the Partner States have an intra-state settlement process in place to transfer net collections (similar to the interbank settlement system).
- 3) Need to deal with non-tariff barriers - just a focus on harmonisation of tax policies and laws is not sufficient on its own to ensure free movement of goods, services and capital and for promotion of investments in the EAC. The Partner States should seek to eliminate other impediments to ensure the objective is achieved.
- 4) To have adequate stakeholder involvement in the harmonization process and hence ensure that all concerns raised by the various stakeholders are adequately addressed to avoid developing a poorly thought out harmonized regime.

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