



# DANQUAH INSTITUTE

*Media, Research & Policy Analysis Centre*

## PRESS STATEMENT

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### **VAT TO RISE AS GOVT SETS TO IMPLEMENT IMF CONDITIONALITIES**

The Danquah Institute (DI) has called on the Government of the Republic of Ghana to come clean and warn Ghanaians beforehand how much it intends to raise VAT and electricity prices in line with Government's policy to strengthen the fiscal state of the national economy.

With the end of September less than a week away, DI is also asking for the President Mills administration to let Ghanaians know how far it has gone in fulfilling the conditionalities set out in its June agreement with the World Bank, covering a \$300 million credit facility.

Against its clear manifesto promise that there would be no increases in taxes that directly affect the purchasing power of Ghanaians, Nana Attobrah Quarcoe, head of research at the DI, says, "by the understanding of the International Monetary Fund, at least, the rate of Value Added Tax (VAT) should go up or at least there should be a clear indication of that before the end of year." This will be in fulfilment with an agreement between the Ghana government and the two Bretton Wood institutions, he stresses.

VAT is currently at 15%, plus the 2.5% NHIL, which goes towards the National Health Insurance scheme. A 2 percentage points, the Danquah Institute predicts, is likely to be added to the VAT, making the total additional cost on VAT-rated goods and service to the consumer shooting up to 19.5%.

The Ghana government has entered into a new three-year arrangement with the International Monetary Fund under the Poverty Reduction and Growth Facility, which sets out the fiscal policy direction for the next two to three years.

The IMF Country Report on Ghana of August 2009, which outlines the details and "structural conditionalities" of this contract warns of hard days to come, the DI explains.

Not only does it talk of a possible increase in VAT, it makes mention of the Mills administration agreeing to slap VAT on many more items, by reducing the number of zero-rated VAT items. The IMF report states, "A number of zero-rated items (excluding exports) will be reviewed with the goal of eliminating the zero-rating."

Ghanaian households and businesses should also get ready for increases in electricity prices, Nana Attobrah says.

“While these extra charges may be seen as rational and necessary, the flip side is how that can negatively impact on attempts to revive economic activity and boost consumer confidence,” the researcher explains.

These price increases, he says, would be worsened by a squeeze on the public wage bill, which has seen no wage increase this year, flapping below the rate of inflation, a first in more than six years.

The Danquah Institute forecasts an end-of-year inflation rate of not less than 16.0%, against government’s revised forecast of 14.5%, a 2.5 percentage increase on its earlier forecast.

“With average yearly inflation not likely to fall below 19%,” Nana Attobrah argues, “this should mean that the trend in the last six or so years where public sector wage increases have more than matched inflation would be reversed.” Public sector wage increase this year has been ceiled at 17%.

The structural conditionalities which the NDC has signed on to place focus on strengthening fiscal institutions (tax policy, revenue administration) and addressing recurrent sources of spending pressure (particularly energy subsidies and the public sector wage bill).

According to the IMF document, Ghana’s tax system “is overwhelmed by special, often discretionary, exemptions that undermine confidence in the equity and effectiveness of the tax regime. Thresholds for VAT and business taxation are also too low, leading to wasteful use of scarce administrative resources on small taxpayers.”

The Ministry of Finance, Nana Attobrah notes, has pledged that “Steps taken in June 2009 to rein in exemptions will be intensified in the 2010 budget.”

He continues, quoting from the same document, “To simplify VAT administration, a review will also be conducted this year to reduce the number of zero-rated VAT items and convert domestic zero-rating to standard rate taxation. VAT thresholds and small business taxation will also be revisited.”

The Danquah Institute has, however, welcomed, as long overdue, steps being taken to form a single integrated domestic tax agency within the intended revenue authority, rather than maintaining separate agencies for income tax and VAT administrations. The authorities intend to launch a modernization strategy with these goals before the end of this year.

The Danquah Institute warns that the calculation by the World Bank that half a million more Ghanaians will fall below the poverty line of \$1.25 by next year may even be conservative. “This is because further fiscal measures will be needed to reduce the deficit to 6 percent of GDP in 2010 as projected. Again, an increase in utility tariffs will be needed to cover the rising costs of

power generation. And, the IMF is advising that steps to control public wage growth should be pursued, along with options for strengthened revenue mobilisation.”

**In May**, DI announced that “There is good news for Ghana. The International Monetary Fund and the World Bank in Washington, DC are prepared to give the Ghana government a ‘tentative allocation’ of funds totalling \$3.2 billion over the next three years. But, still to be made clear to Ghanaians are the conditions that the country has to meet before the funds will be made available.”

The press release said, the Danquah Institute, which welcomes the multi-billion dollar funding prospect, is however calling on government to “come clean and let Ghanaians know what the fine print says. We know bullets must be bitten. But what size and by who is what President Mills must tell us. The days when these things were done by stealth are far-spent,” says DI’s Executive Director, Asare “Gabby” Otchere-Darko.

“From what we are gathering,” Gabby said in May, “the Fund’s position to the Ghana government is that there should be no scope now for, what they call, countercyclical fiscal loosening. Indeed, the Fund is calling for ‘upfront fiscal restraint.’ Which means keep the lid on spending so tight as to keep fiscal deficit down, whether or not the spending is for essential infrastructural development or lifeline interventions.”

Again, he warned, “there are fears of utility bills, especially electricity, shooting up as subsidies for VRA and poor consumers are being discontinued or cut down. And, with worrying signs of a three-year virtual freeze on public sector wages and salaries,” the think tank, DI, is demanding “greater transparency” from the new government of social democrats on whatever conditionalities the Bretton Wood institutions are attaching to the funds they are currently dangling before the nation’s eyes.

This is the second time the Danquah Institute has made such a call for government to come clean on the scope of conditionalities. In March, even before any agreement was signed, the DI cautioned that there were hints that the Tema Oil Refinery was being prepared for privatisation, while it did not speak against the idea, the liberal think tank asked at the time for transparency. But, this warning was ignored.

On Thursday, July 2, Finance Minister Kwabena Duffour told Ghanaians, during an interview on Citi FM, that there were no conditionalities attached to the record \$535 million World Bank loan. Yet, there are six conditionalities contained in page vi of the World Bank programme document covering the \$300m Economic Governance and Poverty Reduction Credit, on which actions are to be taken before the end of this month.

The Danquah Institute welcomes some of the conditionalities, including the rationalisation, commercialisation and privatisation of half of subvented agencies, and the requirement that by September the Mills administration should have ready for submission to Parliament the Freedom of Information Bill.

“But, we need to know which 50 percent of all subvented agencies have been prepared for this future exercise of rationalisation, commercialisation and divestiture,” the researcher at DI, Nana Attobrah insists.