Debate No. 16 of 17.06.2006

ORAL ANSWER TO QUESTION

TAXATION POLICY (NEW) - INCOME TAX, NATIONAL RESIDENTIAL PROPERTY TAX

The Leader of the Opposition (Mr N. Bodha) (By Private Notice) asked the Deputy Prime Minister, Minister of Finance and Economic Development whether in regard to the new taxation policy, he will state in relation to -

(a) Income Tax for the financial year -

(i) 2005-2006, the number of individuals who were exempt therefrom and those liable to payment thereof and the amount collected, and

(ii) 2006-2007, the number of individuals who will be exempt therefrom and those liable to payment thereof and the forecast, if any, of revenue to be collected, and

(b) National Residential Property Tax announced in the Budget Speech for the financial year 2006-2007 -

(i) who will be subject to the new tax;

(ii) how it will be calculated, and

(iii) the forecast, if any, of revenue to be collected.

The Deputy Prime Minister, Minister of Finance & Economic Development (Mr R. Sithanen): Mr Speaker, Sir, Economics and budgets are about choices among a range of policy options. And let us admit some of the options are painful but necessary ones. A budget signals the economic orientation and the policy mix of the Government of the day. It attempts to achieve various objectives and it uses a policy mix, as we call it, to attain these objectives. The policy mix concerns its strategy on expenditures, on taxation and on other economic fundamentals like job creation, investment and the external balance. It is a well-known fact that different Government embrace different policy mix.

This Government has embraced a radically different policy mix from the previous one. The outgoing Government had pursued its own policy mix
comprising high expenditure, financed by high increases in VAT, high budget deficit and high debt. It is a choice of policy mix.

Obviously, Mr Speaker, Sir, each policy mix has economic consequences, both intended and unanticipated, and just like each medication has both curative ramifications and side effects. The entire nation knows what have been the economic consequences, intended or otherwise, of the policy mix of the previous Government. This policy mix has produced declining economic growth, high unemployment, falling private investment, plummeting foreign investment, declining savings, a very high budget deficit, an unsustainable level of public debt and a yawning deficit in the external balance. This is an indisputable fact as amply underscored by all official statistics and as robustly underlined by the articulate analysis of all experts, institutional and individual, international and local.

Mr Speaker, Sir, we have opted for a different policy mix. We have chosen a comprehensive reform package to consolidate public finances while simplifying and rationalising the tax system, making it progressive instead of regressive, and making it more transparent. At the same time we have given due consideration to the need to widen the circle of opportunities. The present tax system greatly discriminates against small and even medium-sized firms. Firms applying for investment incentives face hefty administrative costs and professional fees that require a large volume of business to support. The inequity and inefficiency of our tax system are aggravated by the numerous opportunities for evasion and avoidance. Many taxpayers in the highest income brackets end up paying far less as a proportion of their income than taxpayers in the lower and middle income bracket.

Our new tax policy brings about fundamental changes to restore fairness and to do away with exemptions, most of which have outlived their purposes and in some cases are even counterproductive. Some of the exemptions are not only perverting the tax regime, but distorting resource allocation and leading to suboptimal uses of economic resources. Such distortions lead to inefficiency in the economy that undermines our global competitiveness. And so, Mr Speaker, Sir, our tax reforms are not only about tax rates, tax administration, fairness and equity. It is also about the broader issue of economic efficiency and having a tax policy that is consistent with broader economic objectives and with the need to be globally competitive. It is about rewarding efforts, innovation and entrepreneurship while granting tax incentives and concessions sparingly in a transparent manner to encourage investment, especially foreign direct investment that will create jobs and more particularly jobs for the SMEs.
Moreover, Mr Speaker Sir, our new tax policy is set out in the broader context of fiscal consolidation. We have made tremendous efforts in this budget to contain expenditure – not only because there are wastages and inefficiencies to be eliminated and not only because we needed to get our spending priorities right and in line with the aspirations of the population, but also by containing expenditure, it will be easier, Mr Speaker, Sir, to reduce the tax burden of the population. I have said it in the Budget Speech every rupee of taxpayer money will have to be spent judiciously or will not be spent at all. Our expenditure policy and our tax reforms together have enabled us to maintain VAT at the same rate and not to broaden its base to include many food items such as fish, poultry, meat, fresh vegetables and services like electricity and water. These were the choices that we had to make. Raising tax, especially VAT is an easy way out. Mr Speaker, Sir, we have not chosen the easy route because of its adverse effects on both the economy and on consumers, especially those who find themselves at the bottom of the economic ladder.

With the new tax policy, Mauritius will join the league of nations with the lowest tax rate and most fairly spread tax burden in the world. This is a strong signal to investors to come and invest in our country to create wealth, to add value and to generate gainful employment opportunities. Having a single and low tax rate means that the marginal tax rate will also be low. And we are achieving this, Mr Speaker Sir, while at the same time improving the delivery of services and, more importantly, reducing the budget deficit from 5.5 % of GDP to 4 % of GDP.

I must also explain that the primary objective behind the National Residential Property tax is to ensure that there is progressivity in the system. We have set high income thresholds, in order to ensure that families in the lower income group either pay no tax or lower amount of income tax. But, at the same time, we must make sure that the system is progressive. The National Residential Property tax will ensure fairness.

The number of individuals liable to income tax in financial year 2005-06 is 72,000. With the new income tax measures announced in the Budget, it is estimated that 55% of them, that is, 40,000 will be below the new income exemption thresholds and will thus not pay any income tax. On the remaining 32,000 persons, 26,000 will pay less tax. The remaining 6,000 will pay more tax. They are found in the higher income groups and are those who have claimed high tax breaks.

As regards the revenue aspect, personal income tax is expected to yield Rs2.72 billion during the current financial year, that is, 2005-2006.
Had no policy measures been taken on personal income taxation, that amount would have increased to Rs3.125 billion, that is, by 15%. This is explained by –

(i) buoyancy;

(ii) growth in national income,

(iii) the fiscal drag phenomenon, as well as expected improvements in tax administration attributable to the coming into operation of MRA.

Mr Speaker, Sir, it is estimated that the new income taxation policy would cost Government a net amount of Rs600 m. next financial year, thus bringing the forecast of revenue under that item to Rs2.525 billion, as included in the Budget Estimates of the Budget that I presented on Friday last. This figure, Mr Speaker, Sir, takes also into account the effects of the enlargement of the tax-base, introduction of deduction at source collection methods, including on interest, and effects on tax administration efficiency from simplification of the system.

Regarding part (b) of the question, owners of residential property with annual income exceeding Rs215,000 will be subject to the National Property Tax. This tax will be raised on residential property, including bare residential land. The tax base will be the total surface area of residential land he/she owns together with campement sites leased from Government. If the residence is located on a large extent of agricultural land, the taxable area will be limited to 5,272 square metres. I am informed that this is the equivalent of 1.25 arpents. For flats and apartments, the floor area will be taken as the tax base.

The rate will be Rs10 per square metre of surface area of land for residential plots and Rs30 per square metre floor space for flats and apartments, from which, Mr Speaker, Sir, any amount of rates paid on those properties to local authorities will be deductible.

As regards part (b) (iii) of the question, I would like to point out that the National Property Tax will be applicable as from 01 July this year, but there won’t be any revenue for this year because the first payment of the tax will be in September 2007, that is, in about 15 months time, which would fall in the Budget 2007-2008. Thus, Mr Speaker, Sir, no revenue will be collected from this tax during the financial year 2006-2007. As for 2007-2008, it is forecast that a net amount - and what I mean by net, Mr Speaker, Sir, is the gross amount less that amount that would be deducted for those
who pay municipal rates - of Rs120 m. will be collected from this tax after deductions of the municipal taxes.

Mr Bodha: Mr Speaker, Sir, the Deputy Prime Minister took 20 minutes to explain the philosophy. I would like to…

(Interruptions)

Mr Speaker: Order!

Mr Bodha: Mr Speaker, Sir, the two questions are inter-woven, because in the paragraph relating to the National Residential Property Tax, that is the sentence where he says that it interweaves the four different thresholds. Mr Speaker, Sir, the taxation policy is just like the Budget, in fact. It does not cater at all for the reality of our Mauritian culture. The Deputy Prime Minister is saying that 40,000 people are going to be exempt, and this will bring only Rs200 m. less in the coffers of the State. How can he reconcile these two figures?

Mr Sithanen: Mr Speaker, Sir, it is very unfair. The hon. Leader of the Opposition comes with this question and does not even listen to the answer I have given. I have explained. Let me read again, Mr Speaker, Sir. This is what is unfair. Let me explain again.

“As regards the revenue aspect, personal income tax is expected to yield Rs2.72 m. during the financial year, that is, 2005-2006. Had no policy measures been taken on personal income taxation, that amount would have increased to Rs3.125 m. next year, that is, by 15%”.

And, this is because of -

(i) the buoyancy effect. Anybody who has been in this House for a long time knows that, every year, because of buoyancy, of tax enlargement, of tax base increases, this is so.

(ii) the enlargement of the base;

(iii) fiscal drag;

Let me explain what is fiscal drag. There are four bands, 10, 20, 25, 30. When your income increases, you move from one band to another band. This is why economists say that you are dragged into the fiscal net.
(iv) there will be better administration, because of the lower number of taxpayers;
(v) there is the MRA effect.

This is the whole purpose of the MRA, that is, to ensure an effective mobilisation of resources. I have said, Mr Speaker, Sir, that, if you take this into account, the net effect of these measures would cost Government a net amount of Rs600 m. next financial year. And, it is precisely, when you take this figure of Rs3.125 m. and deduct Rs600 m., you have the revenue estimate, that is contained in the Budget, of Rs2.525 m.

**Mr Bodha:** Mr Speaker, Sir, the Minister, himself, said that he has taken the painful option. Do you know who is going to pay for that painful option? Those very people who believed, on 01 May 2005…

**Mr Speaker:** Can I remind the hon. Leader of the Opposition that he has to put a question and must not make a speech. I have got a ruling of the House of Commons in front of me. He should just give some indication for the question to be understandable. That’s all. He cannot make a long speech.

**Mr Bodha:** I will go by your ruling, Mr Speaker, Sir. The thing is, Mr Speaker, Sir, that those who believed that with Rs25,000 a month they would have no tax, those who believed that they would have a tax holiday are, in fact, those who are going to be the most fleeced by this proposal.

**Mr Speaker:** Are they going to be the most fleeced? That is the question.

**Mr Sithanen:** Mr Speaker, Sir, the hon. Leader of the Opposition is dabling into counter productive populism. The hon. Prime Minister announced that all those who pay Rs25,000 per month would be excluded. Mr Speaker, Sir, let me explain to the hon. Leader of the Opposition that we have gone further than this mandate. First, every taxpayer who is married and who earns Rs25,000 will not pay a single cent of income tax, Mr Speaker, Sir.

*(Interruptions)*

The Leader of the Opposition does not want to listen! Second, Mr Speaker Sir, if both the husband and wife work, the principle of separate taxation will continue to apply. If you were here yesterday, I said that when hon. Gunnness raised that issue. They will be able to do that.
Mr Speaker, Sir, the hon. Prime Minister knows that very well. When we announced this policy we said that it is going to apply only to those who earn up to Rs25,000 and we say that those above Rs25,000 will have to pay the full tax later. And you know what happened? We worked hard in our Committee after 01 May to see how this can be implemented. I remember the hon. Prime Minister asked me: “Rama what will happen to those who earn Rs26,000? Do they have to pay tax on the whole Rs26,000 or they will pay only on Rs1,000?” And you know how much this costs? Mr Speaker, Sir, in this Budget we are telling them that those who earn Rs26,000, they won’t pay on the first Rs25,000. This is why I am saying that we have gone beyond our promise, Mr Speaker, Sir. And next, we know what is the average size of a family in Mauritius, Mr Speaker, Sir. You have the main income earner, his wife and two children. So, these are what we would call the typical Mauritian family with three dependents. They can earn up to Rs 32,670 and don’t pay a single cent on income tax.

Mr Speaker, Sir, 40,000 people will not pay income tax; 26,000 people will pay less income tax. Of course, I admit that 6000 people will have to pay more. So, each of you here can come with 20 cases where you are worse off. But, I can come with 40,000 cases to demonstrate clearly, unambiguously that the lower middle income group are the greatest beneficiaries of the taxation policy of this Government.

Mr Bodha: In fact, the middle class group is going to be the ones who are going to be fleeced. Mr Speaker, Sir, the Deputy Prime Minister and Minister of Finance is saying that they can have separate presentation on their income, but would they have had the same deductions? He said that the deductions that we have granted in the past are outdated. Does the Deputy Prime Minister consider the fact that people who have taken a loan to build their house for 10 years and who still have to pay the loan for the next ten years to be outdated?

Mr Sithanen: Mr Speaker, Sir, what is important as far as taxation is concerned, is what we call the effective rate of taxation; the paper rate of taxation is not important. As I indicated in my Budget, there were people who were earning Rs1 m., who, on paper, should pay 30%, but in effective rate of taxation was paying 2 or 3%. Let me enlighten the hon. Leader of the
Opposition. There are five variables that determine how much tax you pay.

(i) the threshold;
(ii) the exemptions, deductions and allowances;
(iii) the number of tax bands;
(iv) the speed with which you move from one tax band to the other, and
(v) the tax rate.

And look what we have done, Mr Speaker, Sir. I don’t know whether the hon. Leader of the Opposition realises that. One, we have raised considerably the threshold – Rs215,000, then it increases, depending on the number of dependants you have.

Secondly, we have reduced considerably the number of bands, from 4 to 2 and, eventually to one.

Third, many people have not understood that. I will ask each of my friends here to go and do the computation. In the existing system, Mr Speaker, Sir, you pay 20% on Rs25,000 - I don’t know how many people know that – which mean, what Economists called the speed with which you enter higher marginal rate. What we are suggesting, over and above a very high threshold, instead of paying 20% on the next Rs25,000 you will pay 15% on Rs500,000, Mr Speaker, Sir.

And fourth, the tax rate has come down. Now, on four out of the five criteria that determine what is the tax burden, I have given four to the people. We have also made sure that the next is not very penalising and, we have reduced the tax rate. If on top of that – and many people asked me, even my parents told me: it is very good what you have done, but you could have kept the interests deduction. Then, there would have been no reform, Mr Speaker, Sir. We cannot have le beurre et l’argent du beurre, et l’intérêt sur l’argent qui est mis en banque après avoir vendu le beurre.

**Mrs Hanoomanjee:** Can I ask the hon. Deputy Prime Minister and Minister of Finance whether he considers it fair that directors of big corporate bodies, who get huge dividends, would be exempted from the payment of income tax, while the middle-class will be fleeced? Does he consider this fair?
Mr Sithanen: Mr Speaker, Sir, the hon. lady was, I won’t say whether by design or accident, the Chairperson of MRA. So, she should know! Mr Speaker, Sir, there is an elementary principle of income tax, you don’t charge twice for the same income. Any lawyer knows that, Mr Speaker, Sir. Any fiscalist knows that. Just like if someone has committed an offence, you don’t charge him twice for the same offence.

The dividend is paid out of the profit of the company and the company has already paid taxes.

(Interruptions)

Mr Speaker, Sir, we have gone further. There are some companies that try to do what we call tax planning, which is a sophisticated term to avoid the tax. There are some companies, Mr Speaker, Sir, that don’t pay any tax, but they declare dividends. We have increased the alternative minimum tax from 5% to 7.5%, with a view to ensuring that at least we tax once the profit that they have not declared from an accounting point of view, Mr Speaker, Sir.

Mrs Jeewa-Daureeawoo: Est-ce que le ministre est d’accord qu’un propriétaire d’un vieux appartement à Camp Le Vieux va payer plus de taxe qu’un propriétaire d’un appartement à Floréal? Parce que le calcul va être fait sur la superficie et non le standard de l’appartement.

Mr Sithanen: Mr Speaker, Sir, this is an extremely fair question and I thank the hon. lady for asking me that question and giving me the chance to explain. Mr Speaker, Sir, we spent days and nights, the hon. Prime Minister, myself and our experts on what should be the best mechanism to levy the National Residential Property Tax. And that’s why many people are making confusion between this tax, and what demagogically they are calling a rural tax.

(Interruptions)

Why don’t you listen? This is the problem; there is neither a doctor, nor an economist on the other side. That’s the problem, Mr Speaker, Sir.

(Interruptions)

Mr Speaker: Order! Order, please! Time is running out!
(Interruptions)

Mr Sithanen: Mr Speaker, Sir, let me explain…

Mr Speaker: Order! Order!

Mr Sithanen: I am saying this, Mr Speaker, Sir, not to be unfair, because they are asking questions…

(Interruptions)

Mr Speaker: Order! Order, please! Let the hon. Deputy Prime Minister and Minister of Finance answer the question first.

Mr Sithanen: What I am saying is that there are different ways of levying this tax and true it is. But the hon. lady is forgetting two things. First, there is an income threshold. If the person who lives in Camp Le Vieux…

(Interruptions)

Obviously, Mr Speaker, Sir…

Mr Speaker: Order! Order!

Mr Sithanen: Mr Speaker, Sir, what we are saying is that…

(Interruptions)

Mr Speaker: Order! Order!

(Interruptions)

Mr Speaker: Order! Order! Hon. Bhgawan, Order! Order, please! Hon. Bhagwan be quiet, or I am going to suspend you for the rest of the sitting of this House.

(Interruptions)

I am sorry, hon. Bhagwan, I am warning you for the last time. If you have to walk out, you walk out.
(Interruptions)

Mr Speaker: Order! Order!

At this stage, Members of the Opposition left the Chamber.

Mr Sithanen: Mr Speaker, Sir, I am saying that first there is an income threshold. This question has been raised by many MPs, Mr Speaker, Sir. We have a problem. If we want to make a distinction on the basis of the location, there would have been a minimum of hundred such locations. Let me give a practical example. Let us take Floreal. You do not have expensive property everywhere in Floreal. So, you would have had to cut each piece of geography across the country, that would have been extremely cumbersome and it would have been extremely difficult to implement. What we have done for, Mr Speaker, Sir, is basically for a very simple transparent and low tax of Rs10 for land and Rs30 for flat.

Mr Speaker: Question time is over.

MOTION

SUSPENSION OF STANDING ORDER 10 (2)

The Prime Minister: Mr Speaker, Sir, I beg to move that all the business on today’s Order Paper be exempted from the provisions of paragraph (2) of Standing Order 10.

The Deputy Prime Minister, Minister of Public Infrastructure, Land Transport & Shipping (Dr. R. Beebeejaun) rose and seconded.

Question put and agreed to.