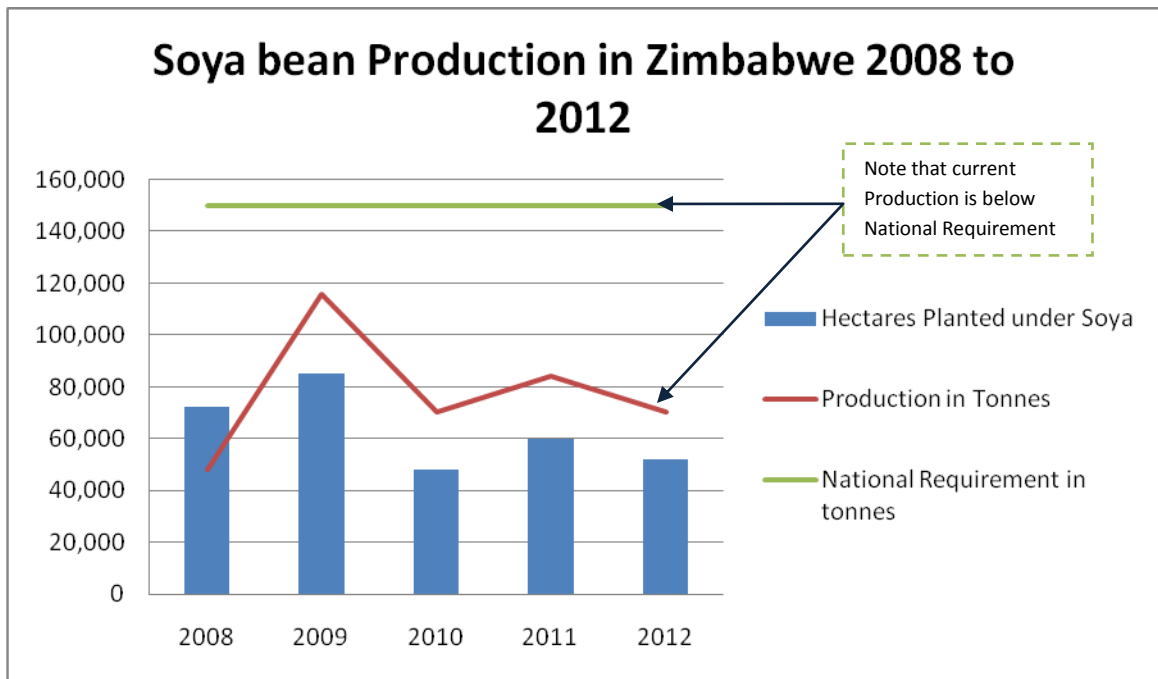


## Negative Implications of Value Added Tax on Soya Bean production in Zimbabwe

- Soya bean production in Zimbabwe is of strategic importance because:
  1. Soya beans are high in oil and protein and the crop significantly contributes to national food and nutrition security.
  2. Soya bean residues are a basic ingredient in the production of certain stock feeds which are, in turn, essential to the production of monogastric animals such as broilers and pigs which cannot digest cotton seed meal. They are also used in the production of farmed fish.
  3. Soya beans are a key raw material for downstream vegetable oil expressing industries, for example manufacturing cooking oil, margarine, soap, etc.
  4. Soya beans are leguminous and therefore fix nitrogen in the soil. When used in crop rotation programmes, they significantly contribute to increased soil fertility and reduced costs of production and indirectly increase yields of other food staples like maize and wheat.
- In Zimbabwe approximately 150 000 tonnes of Soya beans are required annually. The 2011/2012 production season yielded about 70,000 tonnes nationally off 51 000 hectares. The shortfall in supply is made up by imports as follows
  1. Soya cake from mainly Zambia South Africa and Malawi and
  2. Raw soya beans from Zambia and Malawi.

The Graph below illustrates local production trends since 2008.



- The following points should be noted when studying this graph:
  - The 2009 season is notable because it saw the largest area of land planted under soya beans in the history of Zimbabwe. The national average yield in that year was 1.3 MT/ha which is well below the yield potential of the varieties in use. Therefore national production of 115 000 tonnes still fell short of national demand.
  - In 2010 there was a dramatic decline in the area under production but a slight increase in the national average yield. In 2010, national production fell to 70 000 tonnes and the deficit was made up by imports totaling 90 000 MT soya bean equivalent mainly sourced from Zambia.
  - National Average yields per hectare are significantly lower than the yield potential of the soya bean varieties grown. Current National Average Yield is 1.3 tonnes per hectare.
- The key reasons for this under-production are mainly as follows:
  - Finance** - Inability of soya bean producers to access adequate finance for working capital.
  - Viability** - Relatively, high costs of production which makes profit on the crop marginal. The table below gives a model of current costs of production per hectare for both large and small scale farmers.

Table 1 - Soya bean Costs of Production

<b>Variable Costs of Production Per Hectare of Soya Beans USD</b>			
Labour	50		
Tillage, (equipment depreciation, R & M and Fuel)	80		
Aerial Spray	8		
Irrigation (water, Elec & R&M)	175		
Harvesting	90		
Interest on working capital finance @ 18%	167		
Insurance @ 0.65%	7		
Fertilizer (Compound L)	200		
Lime	30		
		<b>Colour Key</b>	
Fertilizer and Lime Transport in	12		Assumed exclusively Large and medium Scale Production Cost
Seed and Thiram (including Transport in)	150		Both Large Scale and Small Scale Farmer Production Cost
Herbicides	65		
Insecticides	10		
Fungicides	22		
Bags	9		
Transport Out to Market	25		
<b>Large Scale Production Cost</b>	<b>1,099</b>		<b>Expected Yield per hectare</b> 2.2 tonnes
<b>Small Scale Production Cost</b>	<b>523</b>		1.3 tonnes

It should be noted that these costs do not include the farmer's overheads for example: Rural District Council Levies, repairs to roads, fences, and farm worker houses, Environmental Management Agency Licenses, the cost of maintain fire guards, etc.

3. **Skills deficit** – In Zimbabwe, an experienced farmer on irrigated land can expect to achieve an average yield of at least 2.2 tonnes per hectare. The highest national average yield recorded since 1980 was 2.280 tonnes per ha in 1999. The highest yields by individual farmers recorded in Zimbabwe in the past have been between 3.5 and 4 tonnes per hectare. The current low average national yields are to a large extent due to a skills deficit amongst the majority of soya bean producers. Soya bean yields are extremely sensitive to agronomic practices (particularly: management of soil, timing of planting, spacing of rows, weeding, pest and disease management and timing of harvesting). A high standard of management of the crop is required in order to maximize yields per hectare.

4. **Regulatory Environment** - A regulatory and policy environment that does not support increased local soya bean production in the short, medium and long term. For example VAT on Soya beans.

- In Zimbabwe the vast majority of primary agricultural products are zero rated for VAT. The table below illustrates some basic common agricultural commodities that are zero rated for or exempt from VAT.

<u>Commodity</u>	<u>Rating for Value Added Tax (SI 273 of 2003. PART II of the FIRST SCHEDULE)</u>	<u>Exempt from Value Added Tax (SI 273 of 2003 PART I of the FIRST SCHEDULE)</u>	<u>Custom and Tariffs Handbook Codes</u>
<b>Vegetables</b>	0 %		<b>07.01 - 0714</b>
<b>Fruits</b>	0 %		<b>08.03 - 08.10</b>
<b>Maize</b>	0 %		<b>10.05</b>
<b>Wheat</b>	0 %		<b>10.01</b>
<b>Rice</b>	0 %		<b>10.06</b>
<b>Sugar beans</b>	0 %		<b>07.08</b>
<b>Sorghum</b>	0 %		<b>10.07</b>
<b>Tobacco sold on an Auction Floors in terms of the Tobacco Industry and Marketing Act [Chapter 18:20]</b>	N/A	YES	
<b>Barley</b>	Not listed therefore rated at 15 %		<b>10.03.0000</b>
<b>Soya beans</b>	Not listed therefore rated at 15 %		<b>12.01.0000</b>

- Currently, the Value Added Tax Act (particularly schedule 2) as read with the Customs and Tariffs handbook indicates that soya beans are rated at 15% (standard) for VAT.
- Therefore any soya bean producer who produces about 10 to 11 tonnes (valued at US \$ 5,000 turnover) of Soya beans exceeds the VAT registration threshold and must register and charge VAT for any soya beans sold.
- This is an apparent anomaly considering that basic products manufactured from soya beans are specifically zero rated as per the following table:

<b><u>Product made from soya beans</u></b>	
Cooking Oil (soya bean) 15.07	<b><u>0 % Rating for Value Added Tax (SI 273 of 2003. PART II of the Second SCHEDULE)</u></b>
Margarine 15.17.1000	
Animal feed	<b><u>0 % Rating for Value Added Tax (SI 273 of 2003. PART I of the Second SCHEDULE)</u></b>

- This has a negative implication on the Soya bean production and soya bean value chains in Zimbabwe, which are as follows:
  1. **A lack of incentive for farmers to grow soya beans.** Cost of Soya bean production is already very high, see Table 1 above. 15% VAT on the purchase price impacts even further on the already marginal profits, particularly when the problem of skills deficits resulting in low yields and expensive working capital costs are considered. VAT on soya beans will accentuate these problems. Local soya bean production will be unviable if ZIMRA aggressively pursues collection of VAT on soya bean sales. Farmers will choose to invest in and produce commodities that are already zero rated for VAT and thus soya production will decline even more. Table 2 below illustrates this point, together with the fact that even if registered soya bean producers were to claim back VAT paid on inputs it would not balance out the impact of the VAT on soya bean sales, because most inputs are already zero rated for VAT.
  2. **An increase in the local price of soya beans.** Currently, farmers rely on contract farming schemes to access inputs and in some cases working capital on credit. These Contract farming schemes in respect of soya bean production will become less attractive to the contract farming company because farmers will demand higher prices - possibly in excess of import parity - to ensure profitability. These companies will look at alternatives, for example, contracting producers of other commodities which are already zero rated for VAT, or simply importing their soya bean requirements thereby reducing the risks associated with contract farming e.g. side marketing, drought, lack of collateral security, etc.

<b>Table 2 Direct Costs of Production - Soyabeans</b>	<b>Cost Per hectare</b>	<b>Input Vat</b>
Labour	50	-
Fuel	30	-
Tractor R and M	50	7.50
Fertilizer Comp L	200	-
Lime	30	-
Fertilizer Transport	12	1.80
Seed, Thiram and Transport	150	-
Herbicides	65	-
Insecticides	10	-
Fungicides	22	-
Aerial Spray	8	1.13
Irrigation (water, Elec & R&M)	175	26.25
Harvesting	90	13.50
Bags	9	1.35
Transport to market	25	3.75
Interest on Finance (18%)	167	-
Insurance (0.65%)	7	-
	<b>1,099</b>	<b>55.28</b>
<b>Turnover and profit per hectare with VAT</b>		
Expected Average Yield per hectare (tonnes)	2.2	
Expected Average Price per tonne at time of harvest in 2013	550	
Therefore Total Income per hectare	1210	
Less 15% VAT	181.5	
<i>Sub total</i>	1028.5	
Therefore Gross Margin per hectare (i.e. Gross -direct costs - VAT + Input VAT)	(71)	
Plus recovered Input Vat	55.28	
<b>Total</b>	<b>(15.41)</b>	
<b>Turnover and profit per hectare without VAT</b>		
Expected Average Yield per hectare (tonnes)	2.2	
Expected Average Price per tonne at time of harvest in 2013	550	
Therefore Total Income per hectare	1210	
Gross Margin per hectare (i.e. less direct costs)	<b>111</b>	

3. **Unhealthy reliance on imports of soya as a raw material due to decreased local production.** Imposing VAT reduces domestic output because of higher production costs and worsens the current negative balance of payments position when imports occur to make up shortfalls to requirements. It is better to increase local production by making it more viable and attractive to local producers than to rely on imports. Buyers, traders and manufacturers already source much of their required soya beans from outside Zimbabwe. If local production was at more competitive levels and consequently increases to meet local demand, it would be unnecessary to rely on imports.
4. **Impacts on Agricultural Input manufactures and suppliers.** Reduced output of soya beans due to viability problems impacts negatively on fertilizer manufacturers and distributors, local seed companies and input suppliers because demand for inputs is decreased. This also adversely affects input prices as economies of scale in production are lower.
5. **Escalating world prices of soya beans.** An additional point to consider is that there is at present a world shortage of soya beans which has resulted in price escalations. It is imperative that Government support the competitive local production of soya beans rather than rely on costly imports.
6. **Impact of increased costs of soya beans as a raw material in stock feeds.** Continued reliance on imports for the manufacture of stock feeds means that costs of production of poultry, pigs and fish are subject to import parity price escalations.

## **Conclusion**

- **In conclusion Zimbabwe must ensure that local production of all primary agricultural commodities, including soya beans, is viable so that farmers are incentivized to grow all strategic crops. It is necessary that Government adopt policies to expand local soya bean production to levels that meet domestic demand for this commodity. The recommendations of Zimbabwean farmers are therefore as follows:**
1. **A Statutory Instrument specifically zero rating soya beans for VAT must be put in place at the earliest possible opportunity and well before the coming soya bean growing season.**
  2. **In the interim, ZIMRA should suspend the planned focused audits on soya bean farmers until such time as presentations have been made to Government and the aforementioned statutory instrument is in place.**