

REPUBLIC OF RWANDA



MEDIUM TERM REVENUE STRATEGY

2021 - 2024

MINISTRY OF FINANCE AND ECONOMIC PLANNING

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LIST OF ABBREVIATIONS

- ATAF – African Tax Administration Forum
- AV – ad valorem
- BNR - National Bank of Rwanda
- CIT - Corporate Income Tax
- CMA – Rwanda Capital Markets Authority
- COVID-19 - Coronavirus disease
- DRM - Domestic Resource Mobilization
- DP - Development Partner
- EAC - East African Community
- EBM - Electronic Billing Machines
- eFiling - Electronic Filing
- FCDO - Foreign, Commonwealth & Development Office
- FDI - Foreign Direct Investment
- FY - Fiscal Year
- GDP - Gross Domestic Product
- GIZ - Deutsche Gesellschaft für Internationale Zusammenarbeit
- GIZ MIP - Deutsche Gesellschaft für Internationale Zusammenarbeit Macroeconomic Investment Policies program
- GoR - Government of Rwanda
- ICT - Information and Communication Technology
- ICPAR – Institute of Certified Public Accountants Rwanda
- IMF - International Monetary Fund
- MBRP – Manufacture and Build to Recover Programme
- MINECOFIN - Ministry of Finance and Economic Planning
- MINICOM – Ministry of Trade and Industry
- MINIFRA – Ministry of Infrastructure
- NST - National Strategy for Transformation
- PAYE – Pay As You Earn
- PIT - Personal Income Tax
- PSF - Private Sector Federation
- RRA - Rwanda Revenue Authority
- RDB - Rwanda Development Board
- RFL – Rwanda Forensic Laboratory
- Rwf - Rwanda Franc
- SSA - Sub-Saharan Africa
- SDG – Sustainable Development Goals
- TaxDev – The Centre for Tax Analysis in Developing Countries
- TIN - Taxpayer Identification Number
- TPD – Tax Policy Directorate General in MINECOFIN
- OECD – Organisation for Economic Co-operation and Development
- VAT - Value Added Tax
- WHT – Withholding Tax

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EXECUTIVE SUMMARY

The MTRS sets out a package of reforms to align the tax system with Rwanda’s long-term social and economic objectives. Covering the period FY 2021/22 to FY 2023/24, the MTRS lays the foundation to achieve upper middle-income status by 2035 and high-income status by 2050. It proposes a set of tax policy, administrative, and legal reforms to promote human capital development, improve Rwanda’s global competitiveness, and develop a strong Revenue Administration.

By 2050, Rwanda will have a world-class tax system that is equitable and efficient, business-friendly with minimal exemptions, which encourages the repatriation of capital and facilitates broad and deep capital markets. A fundamental overhaul of the tax system is needed to achieve these ambitious goals. The MTRS marks the next step towards reforming the tax system and offers an opportunity to open dialogue between citizens and the government to achieve consensus on Rwanda’s future tax framework.

The strategy mobilizes domestic resources that will fund government investments to promote economic growth and a high quality of life for Rwandans. Tax revenues fund basic services that all citizens, especially the poorest sections of society, benefit from. The revenue goals of the MTRS finance the needs of the National Strategy for Transformation (NST1), which sets out the framework to transition from Vision 2020 towards Vision 2050. Considerable public investments are needed to achieve NST1. The overall budget requires financing to the level of Rwf 39,246 billion over (2017-2024), of which 56 percent will be funded through public resources while 41 percent will come from the private sector.

Achieving Vision 2050 requires an expansion of tax revenue from 15.8 percent of GDP in 2021 to 21.5 percent by 2035 and to 34 percent by 2050. Increasing tax revenues by 5.7 percent of GDP in the next fourteen years will be accomplished through a comprehensive strategy that reduces rates, broadens the domestic tax base, improves tax compliance, and curbs tax evasion. The MTRS proposes a tax framework that is competitive, encourages investment, and redistributes wealth.

The success of the MTRS hinges on obtaining consensus from Rwandans on the direction of tax policy and the importance of raising domestic revenues to reach Vision 2050. Meaningful engagement in the lead up to MTRS will be central to design successful policies that have the support of Rwandans.

The MTRS is being launched in an uncertain economic environment, as the impact of the COVID-19 pandemic continues to disrupt business. This MTRS aims to raise tax revenue by 1 percentage point of GDP in just 3 years, between July 2021 and June 2024, in order to:

- First, to increase resources available to invest in programmes that support the achievement of the SDG and NST1 goals.
- Second, as Rwanda’s public debt levels rise as a result of the pandemic’s impact on the economy and related necessary Government’s spending, the MTRS should be a key component of our fiscal consolidation strategy.
- Third, improve Rwanda’s capacity to collect taxes in order to strengthen institutions and build the country’s capability, enhancing self-sufficiency and reducing reliance on foreign aid.

The revenue increase will be delivered through 0.54 percent from administrative reforms and policy reforms will contribute 0.46 percentage points.

Table 1: Revenue Impact of the MTRS Reforms

MTRS Reform Proposal	Revenue Impact over MTRS Horizon (% of GDP)
Tax Policy Reforms	0.46
PIT Reforms	-0.4
CIT Reforms	0.8
VAT Reforms	-0.1
Excise Duty Reforms	0.15
Administrative Reforms	0.54
Shadow Economy & VAT rebate scheme	0.02
Compliance Improvement Strategies	0.46
Customs: valuation & classification	0.06

MTRS Interventions

Pillar 1: Human Development

The MTRS provides an opportunity to connect the tax system over the medium-term to the needs and objectives of human capital development articulated in Vision 2050.

1. Rwanda’s current PAYE schedule has an average effective tax rate that rises most steeply for the poorest individuals. The government will **increase progressivity in the PAYE rate structure and regularly update the thresholds based on inflation**. Restructuring the PAYE thresholds ensures those with the highest incomes make a greater contribution to fund public services.
2. To promote better health outcomes for Rwandan citizens and generate revenue that can be used to spend on health investments for example, the excise tax regime will be reassessed. **The government will consider an overall shift towards specific excise taxes that will be adjusted for inflation**. A specific excise tax on beer will be reviewed, alongside moving to a mix of specific and ad valorem taxes¹ for wine and spirits. The specific rate applied on cigarettes will also be reviewed and an excise on sugar content in beverages will be considered. The government will also conduct an assessment to **consider removing excise taxes levied on products that are beneficial to health when consumed and are produced domestically**, such as powdered milk and bottled water.

¹ Excise taxes that are ad valorem, are levied on the price of the product so fluctuate as the prices of commodities change, making them vulnerable to under-invoicing. Excise taxes that are specific are levied on units or weight of a product and are much easier to measure. Specific taxes are therefore more effective at reducing consumption.

Pillar 2: Competitiveness

The tax system must work effectively to attract investment and generate the revenues needed to push Rwanda to upper middle-income status by 2035.

1. The **Manufacture and Build to Recover Programme (MBRP)** supports economic recovery through temporary incentives for the manufacture and construction sectors. Strengthening these priority sectors are important to improve Rwanda's competitiveness in the long-term, building high quality infrastructure that is needed to attract global investments.

The following reforms complement each other and will be reviewed and implemented as a package.

2. **The government will review the CIT system during this MTRS period.** The review will consider options to move to a CIT system where **a lower tax rate is combined with a broader base, and incentives are not commonly used.** It will consider both the costs and benefits of tax incentives, as well as the competition and revenue implications of lower corporate rates.
3. **To encourage investment, the government will consider introducing immediate expensing of capital investments to replace depreciation.** This would mean that 100 percent of investment costs could be deducted from taxable income in the year that they are incurred, significantly reducing the upfront cost of investment. When reviewing this policy, potential limits will be considered to benefit SMEs.
4. **To encourage investment and risk taking, the government will consider allowing indefinite carry forward of losses.** The review of this policy will take into consideration limits to protect the tax system from abuse.
5. To ensure all companies pay their share of tax and to prevent tax evasion, **the government will consider implementation of a minimum alternative tax (MAT).** Such a tax would be based on turnover. Businesses pay either CIT or MAT liability, whichever is greater. If MAT is greater than CIT, the difference is a MAT credit which can be carried forward and offset against future tax liabilities. Extensive consultations involving taxpayers and businesses will contribute to the assessment and potential design of the MAT.
6. **In order to tackle Base Erosion and Profit Shifting, Rwanda will introduce policies to tax the digital economy.** As a first step, a VAT will be extended to include digital services and will be applied to goods and services sold online. The income tax law will also be updated to include corporate income from digital business operations. These laws will be applied to both Rwandan and non-resident entities operating in Rwanda.
7. The government will further address BEPS and support KIFC by cooperating with partner jurisdictions through Double Taxation Avoidance Agreements (DTAAs). Throughout the MTRS period, **the Government of Rwanda is committed to expand its DTAA network further with key partner countries.**

Pillar 3: Agricultural and Wealth Creation

The tax system will support the shift away from subsistence towards productive, professional farms.

1. To support development of the sector and provide relief to subsistence farmers, **the Government of Rwanda will maintain the VAT exemptions on existing agricultural and livestock products, and**

on agricultural inputs and materials. Inputs such as fertilizer, machinery are vital for the development of the sector, to advance productivity and add value.

Pillar 4: Urbanization and agglomeration

Rwanda's tax system will provide incentives to encourage private sector investment in affordable housing and to promote the development of low-emission cities.

1. **To support access to decent, affordable housing for all Rwandans, the Government of Rwanda proposes zero-rating VAT for the construction of new residential houses.** This will promote affordable housing for low-income households, widening access to housing.
2. Motor vehicle emissions contribute to air pollution which also has significant health effects. **The government will consider increasing excise taxes on the most polluting cars and banning the import of old vehicles.**
3. To incentivise better environmental motor purchases, **the government will exempt import and excise duties and zero-rated Value Added Tax for electric vehicles and equipment.**

Pillar 5: Accountable and Capable State Institutions

Good governance and effective institutions will determine Rwanda's socio-economic transformation to a high-income economy.

Strengthening Rwanda's Revenue Administration: The revenue administration measures in this MTRS build on RRA's strategic and reform plans to raise voluntary compliance through targeted strategies and modernize RRA's business operations by leveraging the use of technology and exploiting data science. The strategy will be broken into three areas:

1. Improving taxpayer services to support voluntary compliance in domestic tax and customs.
2. Enhancing taxpayer compliance through targeted initiatives.
3. Modernising RRA's business operations, capacity and productivity.

Strengthening Tax Policy Formulation: In order to expand the scope of tax policy advice delivery, the quantity and the capacity of TPD staff has to increase. Increasing the number of staff in the TPD and utilizing external resources in the short and medium-term:

1. To increase cooperation on policy design issues with RRA.
2. To seek advice from international agencies on selected issues to gain from international experience. As needed, this could be complemented by consultants provided through development partners such as GIZ, TaxDev, KOICA and FCDO.

Table 2: Overview of the MTRS Reforms

Policy Reforms	Administrative Reforms
<ol style="list-style-type: none"> 1. Increase progressivity of Personal Income Tax: <ol style="list-style-type: none"> a. Develop a new PAYE schedule b. Periodically align thresholds with inflation 2. Review Corporate Income Tax to support competitiveness: <ol style="list-style-type: none"> a. Reduce the CIT rate to enhance global competitiveness b. Phase out tax holidays and incentives in favor of more effective tools c. Introduce a turnover-based minimum alternative tax (MAT) d. Include income from digital services in the tax regime 3. Introduce VAT reforms, including: <ol style="list-style-type: none"> a. Incentives to increase the effectiveness of the EBM system b. Concessions to support affordable housing c. Zero-rating VAT for electric vehicles and equipment d. Introduction of a Digital Services VAT e. Temporary VAT exemptions under the MBRP. 4. Reform Excise and Environmental Taxes: <ol style="list-style-type: none"> a. Periodically align Excise rate with inflation b. Replace AV taxes on harmful goods with a specific tax c. Increase Excise tax on older vehicles to incentivize the upgrading of Rwanda’s fleet 	<ol style="list-style-type: none"> 1. Support voluntary compliance with improved taxpayer services: <ol style="list-style-type: none"> a. Digitize Tax Administration to offer a wider range of services and channels b. Use data science to develop effective and timely services and interventions c. Leverage stakeholder engagement in the design and delivery of taxpayer services 2. Enhance taxpayer compliance with well-resourced <i>Compliance Improvement Strategies</i> 3. Modernize RRA’s business operations, capacity, and productivity: <ol style="list-style-type: none"> a. Deploy a new business operating model b. Improve human resource management with targeted development. c. Strengthen RRA governance.

I. INTRODUCTION

Rwanda’s Medium-Term Revenue Strategy (MTRS) sets out the objectives for tax revenue over the period FY 2021/22 to FY 2023/24. This first MTRS marks the start of Vision 2050, Rwanda’s journey to achieve upper middle-income status in 2035 and high-income status in 2050. It proposes a set of holistic reforms to design a tax system that establishes consensus among all Rwandans while raising domestic revenue to finance the ambitions of Vision 2050. Covering tax law, policy and administration, its aims are to simplify the tax system, minimize the cost of compliance, and distribute the tax burden according to wealth.

1. Rationale for MTRS

Achieving Vision 2050 requires a well-designed and well-administered tax system that fairly distributes wealth and is adequate to meet the needs of a high-income country. The MTRS restructures the tax system through a package of reforms to be implemented together. It aligns the tax system with the objectives of Vision 2050 by promoting human capital development, improving Rwanda’s business competitiveness, facilitating agricultural wealth creation, and developing a strong Revenue Administration. The strategy mobilizes domestic resources that will fund government investments to promote economic growth and a high quality of life for all Rwandans.

Tax revenues fund basic services that all citizens, especially the poorest sections of society, benefit from. They are necessary for government investments in essential public services and to finance the transformation of the economy. Over the next three fiscal years, government investments will focus on improving the education system and developing human capital to improve labour productivity, supporting technological efforts to enhance efficiency gains in agriculture, and establishing high quality infrastructure. This not only improves the standard of living, but it strengthens the economic environment for more successful private sector initiatives.

In terms of tax productivity, huge advancements must be made in the next three decades to achieve high-income status by 2050. Rwanda’s tax-to-GDP ratio was 15.8 percent in FY 2019/20, compared to the OECD average for high income countries of 34 percent and a middle-income country average of 21.5 percent. In order to meet Rwanda’s ambitious health, education and infrastructure needs, drastic tax changes need to be made. Fundamental reform of the tax system is needed to close this gap and create a tax framework that adequately meets the needs of an advancing economy. By 2050, Rwanda aims to have a world-class tax system that is equitable and efficient, business-friendly with low tax rates and a broad base, which repatriates capital held overseas, encourages Rwandan citizens to invest domestically and facilitates broad and deep capital markets.

To achieve this, Vision 2050 sets a target for domestic revenue mobilisation of 21.5 percent of GDP by 2035. Increasing tax revenues by 5.7 percent of GDP in the next fourteen years will be reached through a comprehensive strategy that reduces rates, broadens the domestic tax base, improves tax compliance, and curbs tax evasion. Creating a competitive tax system that raises adequate revenues necessitates a holistic system, where the tax framework encourages capital inflow and discourages use of distortive tax exemptions. This MTRS is the first step towards reaching these goals and will be followed by additional MTRSs.

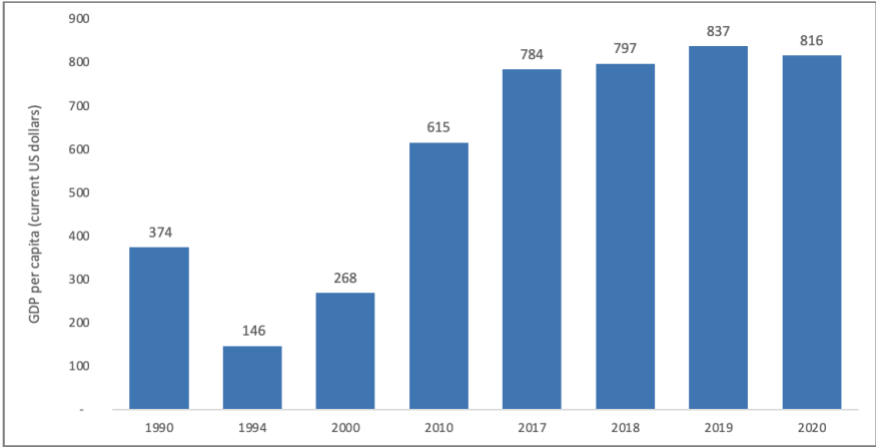
The National Strategy for Transformation (NST1), covering the period 2017 – 2024, sets out the framework for transition from Vision 2020 towards Vision 2050. NST1 provides the foundation to achieve Vision 2050. The revenue goals for this MTRS will cover the financing needs of NST1 which prioritises large-

scale government investments in education, job creation, human capital development, and good governance. The NST1 budget is Rwf 39 trillion over 2017-2024, with 56 percent financed by domestic resources. As for the period of the MTRS from FY 2021/22 to 2023/24, Rwf 22.2 trillion is required. Large public investments were the driving force behind impressive economic growth experienced in the first four years of NST1, with real GDP growth reaching 9.4 percent in 2019. The interventions outlined in this MTRS will facilitate the transition to private sector-led growth for the remainder of the period.

2. Economic Context

Rwanda’s development over the past two decades was mainly due to: rapid economic growth and macroeconomic stability promoting resilience to shocks; important poverty reduction; reduced inequality and increased access to services – health, education, finance. Rwanda registered rapid and important progress as GDP per capita tripled in less than two decades, from US\$268 in 2000 to US\$837 in 2019 and annual GDP growth averaged 7.8 percent throughout the period². The 1994 genocide against the Tutsi caused complete collapse of the Rwandan economy, destroying its socio-economic fabric. Through its economic development strategy, Vision 2020, Rwanda rapidly transformed the economy. More than 1 million Rwandans were lifted out of poverty with greater access to services such as health, education and finance. In 2020, the economy was hit by the COVID-19 shock with a GDP growth of -3.4 percent, but recovery is expected in the medium-term with growth expected to be more than 8 percent by 2023. In order to reach upper middle-income status by 2035, Rwanda’s GDP per capita must exceed US \$4,000.

Figure 1: GDP per Capita



Source: NISR, 2019

Economic Impact of COVID-19

The prolonged repercussions of the COVID-19 pandemic heavily impacted economic activity in Rwanda throughout 2020 and beyond. Swift government action contained the virus and prevented large loss of life; however, this was at the expense of economic activity. Rwanda went into full lockdown on March 21st until May

² NISR. 2020. *GDP National Accounts, 2020*

3rd 2020, after which lockdown measures were slowly lifted, but were put back in place from January 19th to February 9th 2021 in the city of Kigali. Following a surge in cases, a third lockdown was put in place from July 17th to July 31st 2021.

The lockdown measures themselves directly impacted production in the service and manufacturing sectors and caused disruptions to established supply-chains. The subsequent decrease in output further fueled the economic downturn as firms which were not directly affected by the lockdown faced reduced supply and demand from directly affected sectors. Furthermore, the simultaneous deterioration of the global economy also had a negative effect on the Rwandan economy through a reduction in export demand and tourism.

The economic impact of the lockdown on March 21st is reflected in April-June 2020. With a GDP growth of –12.4 percent, Rwanda had its first economic contraction since the beginning of comparable data collection in 2007. As the lockdown mainly targeted the industry and service sectors, it is not surprising that these sectors saw large contractions and were therefore the main drivers behind the unprecedented drop in GDP. Industrial sector output declined by 19 percent compared to the same quarter in 2019, contributing 3.5 percentage points to the overall economic contractions. As the largest sector, services accounted for more than 60 percent of the decline in economic activity, especially the hospitality and transport sectors, which saw growth rates of –62 and –41 percent respectively. Although the agricultural sector was not directly targeted by the lockdown measures, it was affected by unfavorable weather conditions and fluctuating international commodity prices. This is illustrated by the large decline in export crop production and the sector’s overall growth of –2 percent.

Tax revenue collections in FY 2019/20 were affected by measures to contain the COVID-19 pandemic. The total tax and fees collected by RRA amounted to Rwf 1,524 billion during FY 2019/20, a 7.4 percent increase from the previous period, compared to an annual average increase of 14 percent over the previous six years. Non-tax revenues, such as fees from national parks, also declined as tourism plummeted, widening Rwanda’s current account deficit. The pandemic has squeezed the Government of Rwanda’s fiscal space, with the fiscal deficit expected to be 9.2 percent of GDP in FY 2020/21, with public and publicly guaranteed debt at 71.3 percent of GDP at end-2020.

3. Government Tax Measures to Cope with COVID-19

In order to support businesses throughout the national lockdown, the Government of Rwanda, through the Rwanda Revenue Authority (RRA) and Ministry of Finance and Economic Planning, announced temporary administrative measures to alleviate the burden on taxpayers. These included:

- **Suspension of physical tax audits** for one month with an estimated revenue loss of Rwf 2bn.
- **Change to income tax quarterly prepayments** to reflect 2020 performance rather than total income tax paid in the previous year.
- **Extension to submit certified financial statements** for three months which allowed taxpayers to declare and pay taxes on profit using non-certified financial statements.
- **Extension of “Quitus Fiscal”³** application deadline for three months, giving taxpayers greater access to exemptions on 5% WHT on imports and 3% WHT on public tenders.
- **Softening enforcement measures** of tax arrears to provide relief for taxpayers experiencing financial hardship.
- **Waiving of penalties, fines and interest** on late payments for a period of three months.

³ Tax clearance certificate

- **Extension of payment deadlines.** CIT payments were extended for 15 days for large taxpayers and 30 days for small and medium taxpayers. The deadline for rental income and trading licenses were also extended.
- **PAYE waived** for six months for teachers of private schools and for employees of companies in the tourist sector.
- **VAT exemption** on masks and the import of essential medical equipment and expedited payment of **VAT refunds** owed to taxpayers.
- **Improved Customs operations** to facilitate faster release of goods, including introduction of an additional dry port and enforced use of online services in the Electronic Single Window.

4. Tax trends

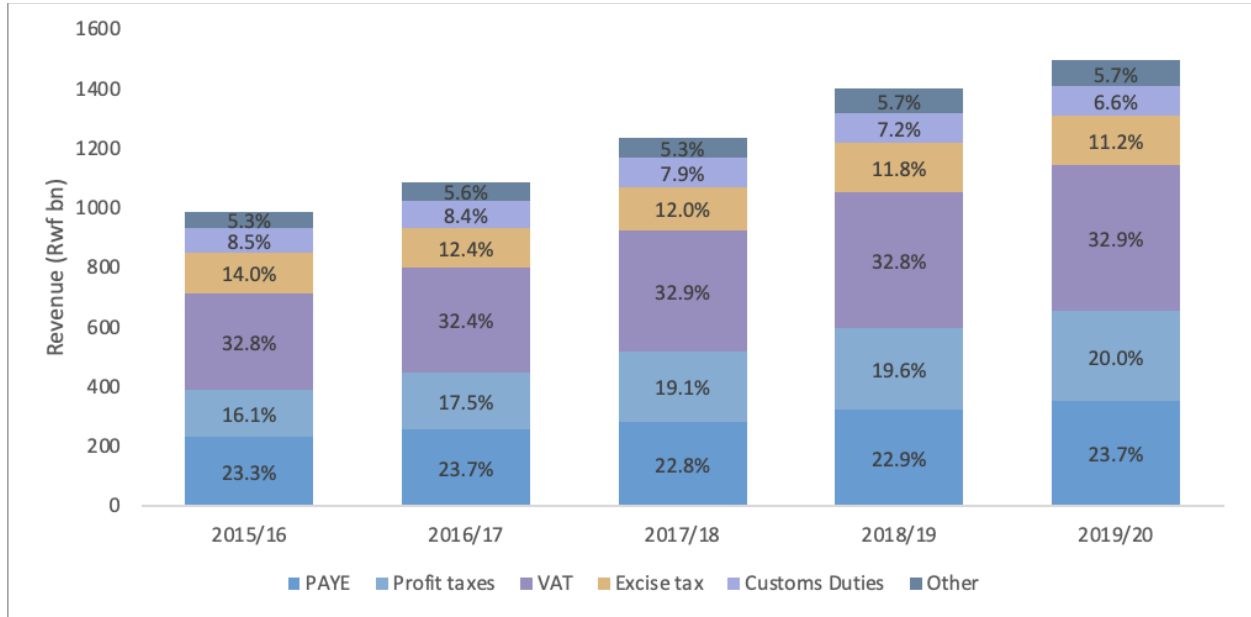
Rwanda’s impressive revenue collection since 1994 outperformed comparable countries, improving self-financing capabilities. Rwanda relied heavily on external support to restart the economy from 1994. Strong economic growth over the past two decades increased domestic tax revenue collection, slowly replacing grant funding and providing stability to government revenues. Since 1993, tax revenue collection has increased from about 8.8 percent of GDP to 15.8 percent in FY 2019/20. Rwanda now consistently outperforms other EAC countries, with the highest tax-to-GDP ratio in the EAC since 2016.

Three Investment Codes created in 2005, 2015 and 2021, established tax incentives to attract foreign investment to strategic industries. Tax incentives are used by the Government of Rwanda to encourage capital inflows and investment in the country. They have played an important role establishing Rwanda as a business-friendly country and developing strategic industries. However, the exemption regime erodes the corporate tax base, reducing the share of taxes paid by the private sector and distorts competition in the market. Tax revenues are needed so the government can make the investments needed to achieve the Vision 2050 ambitions. Thus, developing a competitive tax system that encourages capital inflow without eroding the corporate base and distorting competition, requires a move away from tax incentives toward a more efficient system where all entities make a fair contribution to the government purse.

VAT contributes the largest share to revenue collections, while international trade taxes are low compared to other Sub-Saharan countries. Deepening regional integration has reduced the share of customs duties in revenue collection since FY 2014/15, making Rwanda less reliant on international trade taxes than the Sub-Saharan average. A greater share of revenue collection is made up of PIT in Rwanda compared to other countries, with a Pay-As-You-Earn (PAYE) revenue ratio double that of Sub-Saharan peers of 22.9 percent in FY 2018/19. The IMF estimates that Rwanda’s VAT gap, the difference between potential revenues and the revenues collected, is 10 percent of GDP, with compliance gap making up 3.7 percent in FY 2018/19 and policy gap making up around 6 percent in 2018/19.

Rwanda’s tax system performs well for a low-income country but has experienced setbacks from COVID-19. The effectiveness of tax collection in Rwanda improved between 2000 and 2019. A tax system is buoyant if revenues increase more than proportionately to increases in GDP. Rwanda’s tax buoyancy increased from 1.24 between 2000 and 2008 to 1.41 between 2010 and 2019. However, tax buoyancy fell in 2020 as a result of the pandemic and is likely to recover to 1.11 between 2021 and 2025.

Figure 2: Tax revenue type as % of total tax revenue FY 17/18 - 19/20



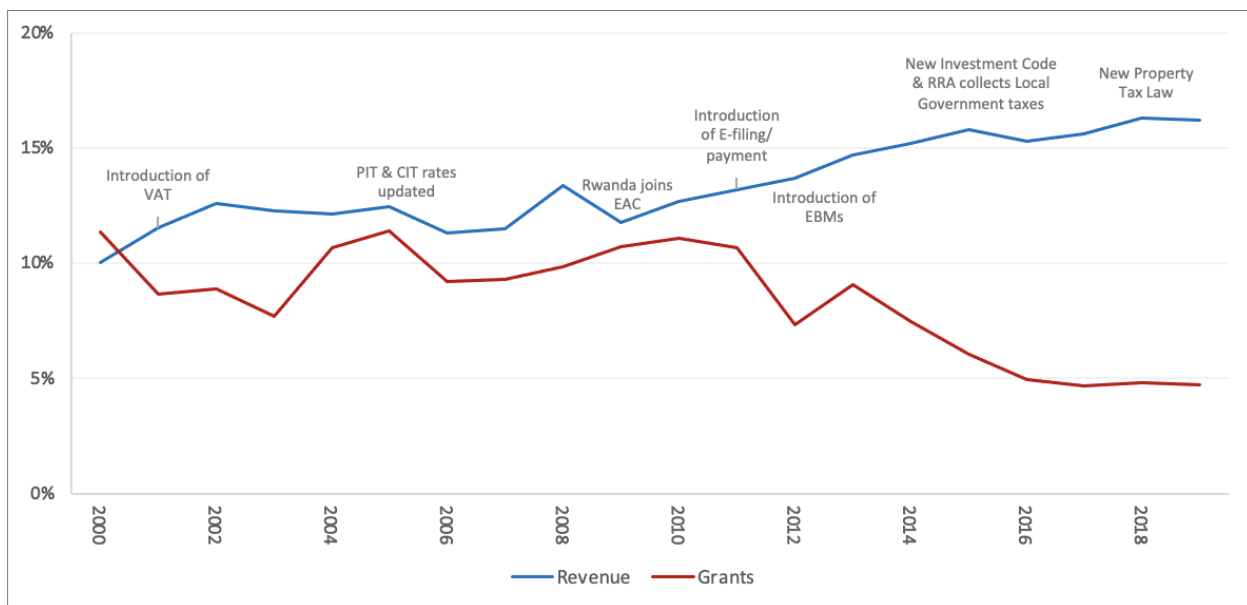
Source: RRA

Historical Tax reforms

Rwanda’s tax reforms can be separated into three major stages: restoration of the tax base; introduction of tax incentives to strengthen production for domestic and foreign investors; and enhancing efficiency in tax administration. In 1997, RRA was established to collect domestic revenue and better manage the scarce resources of the recovering Rwandan economy. RRA has continually strengthened its performance through parallel institutional and legal framework reforms. Initial reforms aimed to widen the tax base, with the introduction of VAT in 2001, reduction of CIT to 30 percent in 2005 and accession to EAC in 2009. Improved use of technology in RRA have reduced the cost of doing business, with the E-Tax portal introduced in 2011 and the Electronic Billing Machine (EBM) in 2012.

Key improvements within tax administration in recent years include taxpayer outreach, increasing the number of registered taxpayers, providing better services, enhanced use of IT, and better risk management. Streamlining and modernizing RRA have contributed to an improved business-enabling environment. Rwanda ranks 38th on the World Bank’s Ease of Doing Business report of 190 countries and scores 64.6 on the ease of paying taxes compared to the regional average of 54.7.

Figure 3: Rwanda’s Grants and Tax Revenues as percent of GDP



Source: MINECOFIN

II. APPROACH TO THE MTRS

1. Objectives

Rwanda's strong economic growth has been interrupted by the COVID-19 induced recession. Increased pressure on government resources and a cautious business environment have verified the need for robust reforms. Within this context, the MTRS has four main objectives:

1. **Support economic recovery:** have in place tax policies and administrative measures that support economic growth in the short-term.
2. **Simplification:** simplify the system to reduce the cost of tax administration and minimize the cost of compliance.
3. **Efficiency:** increase the tax base so that rates can be low, reducing the average tax burden.
4. **Equity:** ensure tax policies are fair and combat inequality - those who can pay more do pay more.

With these objectives in mind, the MTRS has a target of increasing the tax-to-GDP ratio from 15.8 percent in FY 2019/20 to 16.8 percent in FY 2023/24. This is an ambitious target given the ongoing COVID-19 pandemic and the uncertainty surrounding economic recovery.

Figure 4: Medium Term Revenue Projections for FY19/20-23/24 (Rwf bn)

	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Revenue	2,065.03	2,203.09	2,524.92	2,686.88	3,080.89	3,533.48	4,021.61	4,554.85
Taxes	1,378.80	1,475.61	1,593.60	1,760.10	2,066.33	2,405.53	2,744.12	3,179.14
Taxes on income, profits, and capital gains	588.80	641.48	677.89	740.07	842.52	965.59	1,098.73	1,255.93
Taxes on property	0.4	4.64	21.70	27.69	30.81	36.79	39.41	43.82
Taxes on goods and services	677.70	712.21	768.91	847.57	1,021.87	1,172.15	1,326.89	1,492.77
Taxes on international trade and transactions	111.90	117.28	125.09	144.77	171.14	231.00	279.09	386.62

Source: MINECOFIN

2. Scope of the MTRS

MTRS-1 is launched in an uncertain economic context as the protracted effects of COVID-19 continue to cause upheaval. The pandemic creates a dilemma for tax policy during this MTRS between raising revenues to meet NST1 and avoiding tax increases on adversely affected households and businesses that could weaken the economic recovery. The MTRS balances the need for revenue to finance pressing health and social needs with the need to support businesses and individuals so they can recover from the economic impact of the pandemic. To achieve this, tax policy reform measures are sequenced towards the end of the period, with a focus on further studies to lay the foundations for subsequent MTRSs. It focuses on improving efficiency in revenue administration, closing loopholes for tax evasion and enhancing taxpayer compliance.

3. Inclusiveness of the MTRS process

The MTRS should reflect consensus among all Rwandan citizens on the way forward for the tax policy framework. Opening dialogue between taxpayers and policymakers is central to the success of this MTRS. Understanding taxpayer’s concerns on the impact of proposed policies on incomes, profit margins, turnover, and ease of compliance will ensure that the government takes into consideration the full impact of proposals. Engaging with taxpayers in the policy design process offers an opportunity for stakeholders to raise issues and suggest solutions to be integrated into policies. Continuing this engagement after policies have been implemented will ensure the tax system is consistently improved. Opening a dialogue with taxpayers will also enhance understanding of the system and awareness of tax policy changes. The stakeholder engagement methods used in the MTRS are outlined in Annex 1.

III. MTRS INTERVENTIONS

The policy reform package restructures the tax framework around the MTRS objectives to address economic issues within the Vision 2050 pillars and weaknesses within the tax system that undermine revenue productivity. The interventions must be implemented together as a package in order to be financially viable.

Pillar 1: Human Development

Developing Rwanda’s human capital – the knowledge, skills, and health of the population – is a core component to achieve the long-term economic growth set out in Vision 2050. A healthy, educated workforce is more productive, better equipped to earn more and reinvest, creates a more inclusive society, and ends extreme poverty. The MTRS provides an opportunity to connect the tax system over the medium-term to the needs and objectives of human capital development articulated in Vision 2050. It is also an opportunity to open a meaningful dialogue between government, the private sector, and citizens about how this can best be achieved.

Rwanda’s population will increase by more than 50 percent between 2020 and 2035, whilst the share of the working age population will increase from 61 percent to 65 percent in 2050⁴. Government investments in high quality health care must expand to meet the needs of a growing, ageing population to ensure every Rwandan has access to the health care they need. Rwanda’s youth are the country’s future: ensuring they get into formal employment not only develops human capital but will strengthen government revenues for sustained economic growth. High quality education is needed to prepare Rwanda’s youth for the jobs of the future, so they are equipped with the skills to compete in the global economy.

Providing these fundamental services requires large scale government investments which rely on tax revenue. In FY 202/21, the Government of Rwanda spent 40 percent of its budget on development, with 15 percent of total expenditures on education compared to an OECD average of 11 percent in 2017. The difference not only shows the government’s prioritisation and commitment to investing in education, but it demonstrates the need to expand total revenues to reduce this share. Developing a tax system that generates the revenues to finance these investments and enables Rwanda to be self-sufficient requires the support of every Rwandan citizen. Higher voluntary compliance reduces the cost of tax collection so that more can be spent on investments in the future.

As income from grants recedes and Rwanda becomes self-sufficient, achieving the national objectives in Vision 2050 requires a reliant and robust tax system that can generate the revenues needed. Between 1990 and 2019, Rwanda’s life expectancy at birth increased by 35.6 years, the expected years of schooling increased by 5.5 years and gross national income increased by 130.9 percent⁵. These improved Rwanda’s Human Development Index (HDI) rating from 0.25 to 0.54 over the same period. Despite the impressive performance, Rwanda is currently ranked 160 out of 189 countries, placing it in the low human development category. Increasing the stock of government resources through greater tax revenues ensures investments can be made to develop Rwanda’s human capital and improve living standards.

The introduction of tax rate bands to income tax in 2005 improved progressivity in Rwanda’s tax system, ensuring wealthier individuals made a greater contribution to fund public services. The share of

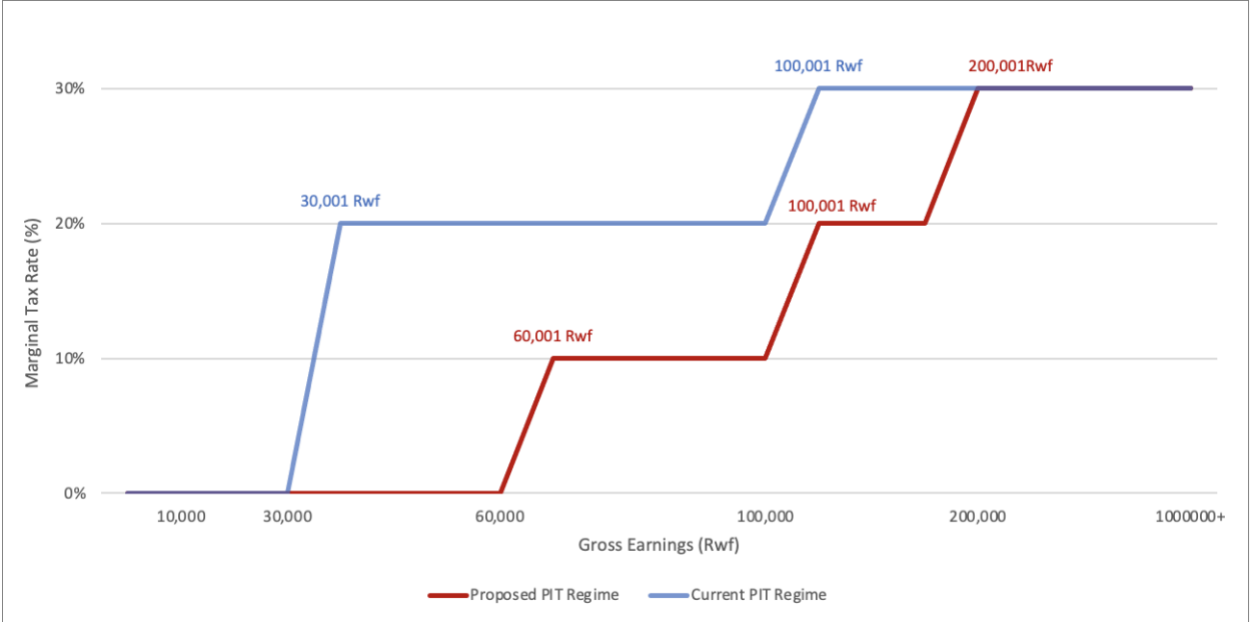
⁴ MINECOFIN. 2020. Vision 2050

⁵ UNDP. 2020. Human Development Report 2020. Available: http://hdr.undp.org/sites/all/themes/hdr_theme/country-notes/RWA.pdf

progressive, direct taxes, those that are imposed on income and profits, increased from 27.7 percent in 1994 to 35.8 percent in FY 2017/18, contributing to a reduction in income inequality. Progressive taxation can ensure that those who are most able to pay make a larger contribution, and taxes can be reduced on the poorest, so they have more income available to invest in their own futures. Although Rwanda’s Gini index declined from 0.52 in 2006 to 0.43 in 2017, it is still one of the highest in East Africa. Restructuring Rwanda’s tax system to adequately redistribute income and combat inequality is central to Vision 2050 and a core ambition of this MTRS.

The PAYE structure currently contains 21 percent of Rwanda’s labour force. Revenues from PAYE constitute 90 percent of the PIT regime and are an important contributor to government revenues. As Rwanda moves towards the Vision 2050 goals and achieves upper-middle income and high-income status, an increasing share of the labour force will be formalised and brought into the PIT structure. Rwanda’s current PAYE schedule has an average effective tax rate that rises most steeply for the poorest individuals and levels-off for the highest earners (Figure 6). Therefore, the government will **increase progressivity in the PIT rate structure and periodically align the thresholds to inflation** to improve fairness in the system. The new proposed rate structure is detailed in Figure 5 below.

Figure 5: PAYE Proposals



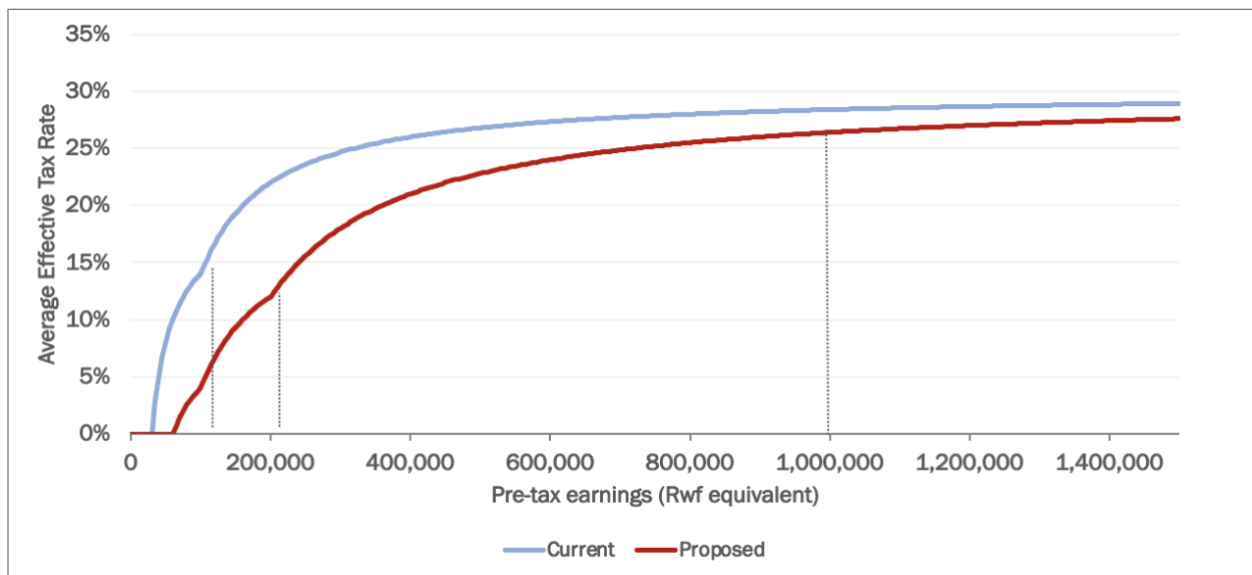
Source: MINECOFIN

The new PIT rate schedule will have three tax brackets, with the entry point reduced from 20 percent to 10 percent and the exemption threshold increased from Rwf 30,000 to Rwf 60,000. The low exemption threshold in the current regime uses significant administrative resources for marginal gains. Raising the exemption threshold means those on lower incomes will reduce the administrative capacity at the lower end of the income distribution. Implementing an additional tax bracket before reaching the top marginal rate aligns tax liability more closely to income level.

All 466,000 taxpayers in the PIT regime will see their tax bills reduce or stay the same as a result of this policy change. The number of taxpayers who are ‘tax-free’, paying 0 percent tax on income, will increase from 90,000 to 169,500 - alleviating the tax burden of 79,500 individuals. A total of 107,500 taxpayers will see their marginal tax rate fall from 20 to 10 percent, and 67,000 will see it fall from 30 to 20 percent. The largest portion of taxpayers, 122,000, earn above Rwf 200,000 and will also have reduced tax liability as a result of the marginal rates on their lower income⁶.

The PAYE tax brackets have not been revised since 2005, resulting in significant bracket creep. If tax schedules stay the same while inflation increases nominal income, the result is a reduction in real income as a larger proportion of salaries are paid in taxes. To avoid the recurrence of bracket creep in the future, thresholds will be periodically updated when revisions in the law allow, every 3 to 5 years. Updates will be more frequent if there are periods of abnormal inflationary pressures.

Figure 6: AETRs in the current and proposed PAYE regimes



Source: MINECOFIN

Indirect taxes ensure that prices reflect negative externalities and improve choices at an individual level which has a large impact on human development at a national scale. Excise taxes are an indirect tax applied on harmful goods to internalise negative external costs. Rwanda’s excise revenues, which equalled 1.77 percent of GDP in 2019/20, are below the average for African and other low-income developing countries, whose revenues from excises equalled 2.4 and 2.2 percent of GDP, respectively. Furthermore, Rwanda’s total excise revenues have decreased over time, from 1.93 percent of GDP in FY 2013/14. The majority of Rwanda’s excise revenues are from alcoholic beverages and petroleum products which constitute 76 percent of total excises, while collections on cigarettes and vehicles are low compared to other countries.

⁶ Figures correct as of December 2020.

Excise taxes can be levied as specific or ad valorem (AV). AV taxes are levied on price, whereas specific taxes are levied on the quantity sold. AV taxes fluctuate depending on the price of a commodity and are vulnerable to under-invoicing, whereas specific taxes levied on units or weight can be easily observed and measured. Specific taxes are therefore more effective at reducing consumption.

To promote better health outcomes for Rwandan citizens and generate revenue that can be spent on health investments, the excise tax regime will be reassessed. An overall shift towards specific excise taxes ensures better treatment of the excise regime. A **specific excise tax will be introduced on beer**. A **mix of specific and AV excise taxes will be applied to wine and spirits** and the **specific rate applied on cigarettes will be revised**. The MTRS **will consider excises levied on sugar content in beverages**. As a result of the shift towards specific taxes, **excise rates will be periodically adjusted for inflation** when there are revisions in the law to prevent erosion of the excise base in the future.

Removing excise taxes from products that are beneficial to the population will also be under consideration. **Excises currently levied on powdered milk and bottled water will be reviewed and possibly removed** as these products provide external benefits to society and are produced domestically.

Pillar 2: Competitiveness

Competitiveness enhances economic productivity, a key driver of growth and higher prosperity. Improving the institutions, policies and factors that determine productivity is a central theme of Vision 2050. Large scale investments in innovation, research and quality infrastructure will support the transition to a knowledge-based economy with high productivity gains.

To support the growth of high-quality infrastructure, boost economic recovery, and enhance competitiveness, the Government of Rwanda will **offer temporary tax incentives under the Manufacture and Build to Recover Programme (MBRP)**, adopted by Cabinet in December 2020. The benefits aim to support manufacturing and increase the production of construction materials, agro-processing, as well as hygiene and sanitation products. To stimulate private sector investment in the manufacturing and construction sectors, VAT exemptions are applied on locally produced raw materials and machinery, as well as imported construction materials not produced in EAC, to reduce the cost of construction. In the manufacturing sector, companies that create permanent jobs are eligible for reduced PAYE rates in 2021 and CIT tax credits are available for companies who demonstrate significant revenue or export performance. Other custom-related facilities will be required at EAC level. The programme will be in place for two years.

Attracting Long-Term Investments

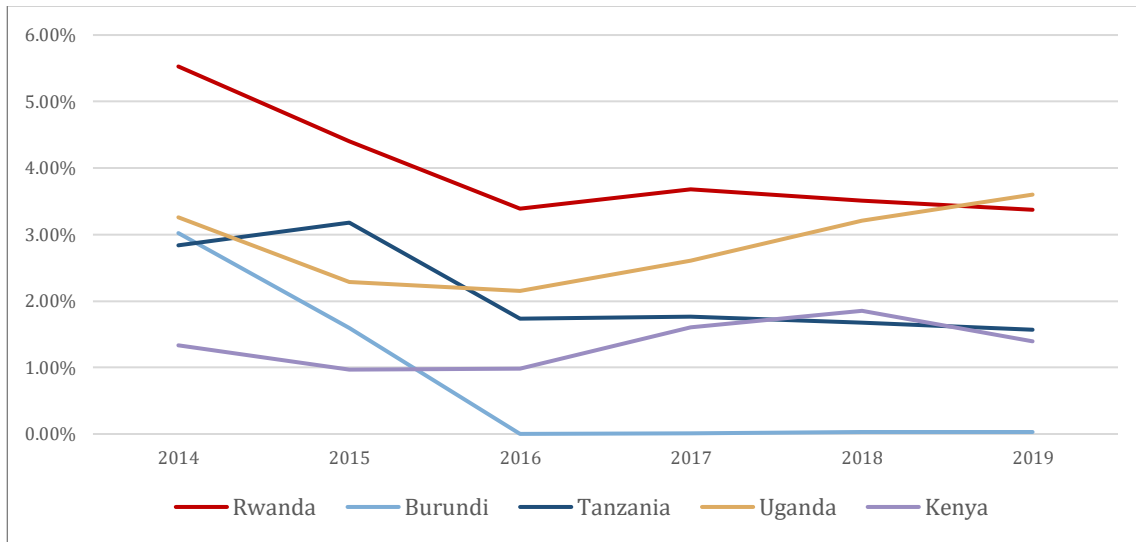
Rwanda must attract and sustain high private investment induced by domestic savings and capital inflows, alongside high public investment and improved human capital through education. Targeted government investments alongside private investments are key to establishing a globally competitive economy. The tax system is an important lever for both of these: tax revenues support government investments in health, education and infrastructure and the tax system can help attract foreign investment, ensure that the proceeds of FDI are reinvested in Rwanda, and support increased domestic savings and investment.

Private investment, funded by savings and foreign capital, will need to increase from around 15.7 percent of GDP in 2019 to about 21.4 percent of GDP by 2035. Rwanda's strong governance, stable political environment, and ease of doing business have helped attract FDI, with net inflows averaging over 3 percent of GDP over the past 10 years – the highest in the East African Community (Figure 7).

The competitiveness of the tax system is a factor affecting investment decisions, but evidence suggests it is less important than some other country characteristics, such as political stability and security, the legal and regulatory environment, the size of the domestic market, macroeconomic stability and a favourable exchange rate, the available talent and skill of labour, and good physical infrastructure⁷.

⁷ World Bank Global Investment Competitiveness Report 2017-18

Figure 7. FDI net inflows (% of GDP) 2014-19



Source: World Bank World Development Indicators & National Bank of Rwanda FPC 2020

Rwanda’s Investment Code plays an important role attracting foreign investors into the country and has developed priority sectors within the economy. To attract strategic investors who can bring technology, skills and knowledge that will have a substantive scale impact, recent initiatives have fast-tracked the issuance of tax incentives through issuing Cabinet approval. The government has the intention to launch the Kigali International Financial Center (KIFC), which will promote Rwanda as a competitive business and financial centre. Incentives to launch the industry are directed to holding companies, headquarters, fund management, and wealth management offices, with exemptions on capital gains tax, low CIT rates of either 15 or 3 percent, and no Withholding tax liabilities.

Tax incentives are commonly used throughout Africa to attract new foreign direct investment by creating a competitive edge through reduced tax burdens. They may partly explain the higher statutory rates found in the region; after accounting for tax incentives the effective CIT rate in Rwanda is estimated at 19 percent.

While tax incentives are viewed as necessary to offset other high non-tax costs, they have drawbacks and can often be counterproductive. Tax incentives distort competition between firms that are able to benefit from incentives and those firms that do not benefit and therefore pay a higher effective rate. They are difficult to police as exports leak into local markets, firms engage in transfer pricing, and reopen under new identities to keep time-limited benefits alive. Tax incentives also encourage rent-seeking behaviour as companies lobby to attain better deals. Furthermore, it has a limited impact on encouraging start-ups and innovation as most new firms make losses in their early years so they can’t use tax exemptions.

International evidence suggests that tax incentives are ineffective at increasing investment. The Investment Climate Advisory’s survey⁸ on investor motivation in Rwanda indicates that tax incentives applied in the past

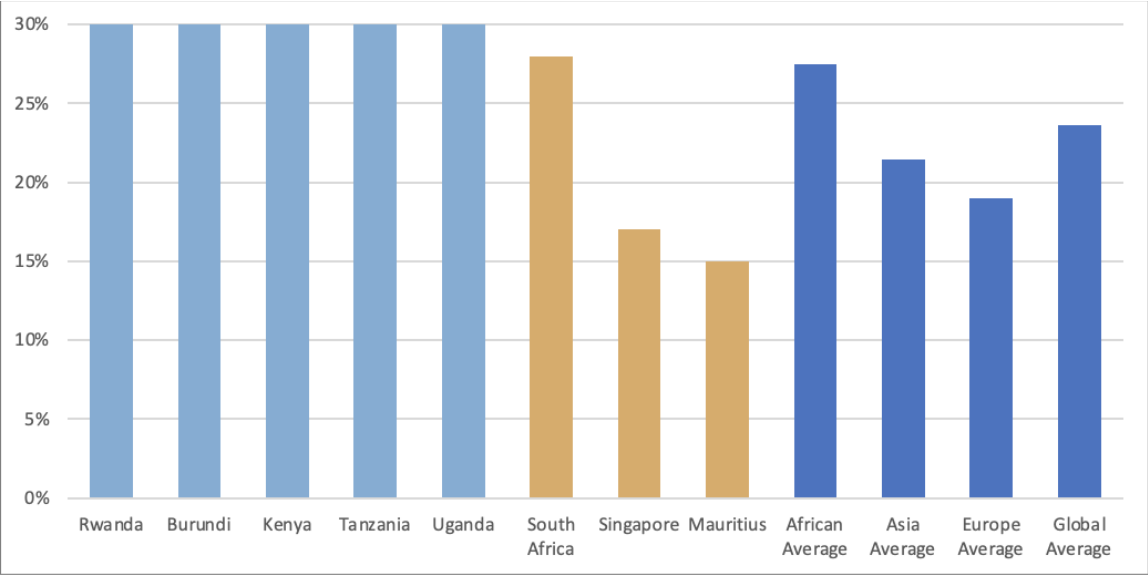
⁸ Sebastian, J. 2014. “Tax and Non-Tax Incentives and Investments: Evidence and Policy Implications”. *Investment Climate Advisory Services*. The World Bank Group

have been redundant. The redundancy ratio, the proportion of investors who would have invested in Rwanda even if the tax incentive were not provided, was 98 in 2011, compared to 61 in Kenya, 77 in Burundi, 91 in Tanzania and 93 in Uganda.

To achieve the goals set out in Vision 2050, the tax system must work effectively to attract investment and generate revenues needed to push Rwanda to upper middle-income status by 2035. Establishing a globally competitive tax system requires a comprehensive analysis of investment incentives to ensure benefits outweigh the costs: where incremental investments more than compensate for the loss of revenue.

Rwanda’s CIT rate of 30 percent is in line with other EAC members, although above the average across Africa as a whole. It is also around 7 percentage points higher than the global average, and 11 percentage points higher than in Europe, the region with the lowest rates (Figure 8).

Figure 8. Statutory corporate income tax rates, 2021



Source: KPMG

The government will therefore review the CIT system during this MTRS period. The review will consider options to move to a system of CIT, where **a lower tax rate is combined with a broader base, and incentives are not commonly used.** It will consider both the costs and benefits of tax incentives, as well as the competition and revenue implications of lower corporate rates. The new CIT regime will allow all firms to benefit from a low rate and attract investment while enhancing compliance by reducing the incentive for tax evasion. This will establish a fair CIT system that distributes the tax burden evenly across all firms, eliminating the erosive damage of incentives.

Where analysis shows that tax incentives do not generate enough investment to compensate for the loss of revenue, the incentive will be grandfathered. This means the Government of Rwanda will announce a date in the future when the tax incentive will no longer be granted, but those companies who have existing agreements with the government keep their incentive until the end of the agreed time period. Replacing the incentive regime

with more efficient means of encouraging investment creates a tax system that better supports local investment, mobilising existing wealth so it is recycled in the economy. This will be important as Rwanda's wealth increases, and it progresses to high income status.

The tax system can encourage businesses to invest. The current system enables firms to deduct the costs of investment over the life of the asset through depreciation, with different rates for different types of assets. For example, assets with a long lifespan such as buildings are deducted at a lower depreciation rate of 5 percent each year, while assets with shorter lifespans such as computers and accessories are granted tax depreciation at 50 percent. This can increase the amount of time needed for the investment to be recovered and for the firm to generate profits. It also requires firms to calculate depreciation for multiple assets, often at different rates and using different methodologies.

To encourage investment the government will consider introducing immediate expensing of capital investments to replace depreciation. This would mean that 100 percent of investment costs could be deducted from taxable income, significantly reducing the upfront cost of investment. When reviewing this policy, potential limits will be considered to benefit SMEs whilst ensuring large multinational companies continue to pay tax. This helps to support domestic investment and level the playing field as larger companies tend to benefit more from the current tax incentive system.

Full-expensing allows companies to reduce marginal effective tax rates. Replacing tax holidays and rate discounts in the Investment Code with full-expensing provides the same tax-free position when the project is growing, but ensures a project pays taxes when it is profitable. This improves fairness in the tax system and eliminates the base eroding effects of tax holidays. As the government is sharing the investment risk it sends a pro-business message. It reduces the administrative costs to businesses of calculating depreciation rates, promoting domestic and international investments.

Firms that invest can generate losses in the short-term before the investment leads to greater revenues and profits. The tax system allows firms to carry forward losses to reduce taxable income in subsequent years, up to a limit of five years. As the move to immediate expensing of capital will result in the tax system recognising larger losses up-front for investing firms, the limit of five years could result in more firms seeing their losses expire and having to pay more tax. This could discourage investment and risk taking. **Therefore, the government will consider allowing indefinite carry forward of losses.** The review of this policy will take into consideration limits to protect the tax system from abuse. This could include limiting the amount of losses deducted each year to a fixed share of the total losses carried forward, with unused losses carried forward indefinitely.

Fair contributions

Alongside greater private investment, meeting the aspirations of Vision 2050 will require public investment to increase from 10.4 percent of GDP in 2019 to 11 percent of GDP in 2035. This will be made possible by steady increases in the revenue-to-GDP ratio, mostly coming from taxes. CIT is an important element of the tax system, contributing 7.7 percent to total tax revenues in FY 19/20. However, the contributions of corporate taxes have fallen as a share of GDP: the productivity rate declined from 0.05 in FY 2004/05 to 0.044 in FY 2017/18. This is below comparator countries at the same level of development where productivity is 0.10; and it is far lower than the rate needed to achieve the ambitions of Vision 2050. Closing loopholes in the tax system to prevent the tax base from being eroded from practices such as tax evasion is key to laying the foundations of future economic growth. This MTRS provides the framework to open a dialogue between the government, the private sector, and citizens about how best to raise revenues in the corporate sector.

The practice of international tax avoidance is well documented, with corporate tax systems particularly prone to so-called “Base Erosion and Profit Shifting (BEPS)”. Countries around the world, both developed and developing, are in a constant game of cat-and-mouse with multinational enterprises that exploit legal loopholes in tax systems to shift profits to low- or zero-tax jurisdictions. International efforts to reform corporation taxes have made much ground in recent years through organisations such as the OECD and ATAF, with the notable progress coming from the US government which proposed a global minimum tax in April 2021. Although these international efforts are important for small countries like Rwanda, the proportion of taxes that will be assigned to small economies is likely to be marginal.

To address erosion of the tax base by the largest multinational companies, **the government will review whether a minimum alternative tax (MAT) could be used as a backstop against BEPS** ensuring all companies contribute fairly to tax revenues. Such a tax would be based on turnover and the government will assess different options in design of the MAT. Businesses pay either CIT or MAT liability, whichever is greater. If MAT is greater than CIT, the difference is a MAT Credit which can be carried forward and offset against future tax liabilities. The MAT prevents volatility in the tax system and smoothes business tax payments. As turnover is harder to misreport than profit, and MAT credits are claimed when companies are making profit, the MAT would be an important tool to prevent tax evasion and avoidance.

Extensive consultations involving taxpayers and businesses before implementation will determine the design of the MAT. A number of considerations will be discussed with taxpayers as the MAT increases complexity in the system. Recognizing how the MAT and CIT rate will affect business planning and profit margins across sectors will be crucial to design a corporate income regime that is both business-friendly and generates sufficient government revenues. The MAT will be designed for the Rwandan context and will consider specificities of different businesses.

In addition, the Government of Rwanda will continue to develop relationships with partner jurisdictions to further combat BEPS. Double Taxation Avoidance Agreements (DTAA) are mainly used to i) facilitate and encourage inbound investment and transfers of skills and technology, ii) facilitate outbound investment by residents of the other country and iii) to reduce cross-border tax avoidance and evasion through exchange of information and mutual assistance on tax matters. Rwanda has DTAAAs with ten countries that are currently enforced, with an additional four other DTAAAs pending imminent ratification. **For the above reasons and to support the KIFC initiative, the Government of Rwanda is committed to expand its DTAA network further with key partner countries over the MTRS period.**

Fair Contributions in a Digitized World

The use of digital platforms to access goods and services has rapidly expanded in Rwanda and is expected to continue to increase in the coming years as average incomes rise. Access to goods and services through digital means has expanded rapidly and the lockdowns in response to the COVID-19 pandemic in 2020 accelerated a shift in consumer preferences for the digital marketplace. The increasing uptake of e-commerce will continue as Rwanda progresses towards upper-middle income country and high-income country status.

Whilst the digital economy offers huge business opportunities for the private sector, it presents challenges for the tax administration. Taxation of the digital economy is complex as individuals may earn income in a separate tax jurisdiction to the one they physically reside and new forms of digital income fall outside the ambit of current tax laws. Although there are attempts to build multilateral approaches to digital taxation, implementing a domestic framework to tax the digital economy will shore up lost revenues in the short term. Capturing digital services in the tax net not only expands the tax base but ensures fair treatment of all Rwandans.

In order to tackle this Rwanda will introduce taxes on the digital economy, including a VAT on digital services. Goods and services sold online by a Rwandan or foreign resident to a recipient who resides in Rwanda will be taxable. Non-resident entities supplying digital services in Rwanda will have their VAT withheld by financial institutions, whereas residents will remit VAT through the existing framework. **The Government of Rwanda will also tax corporate income from digital business operations.** Non-resident companies with representation in Rwanda will also be liable to this digital income tax.

Enhancing Compliance

Rwanda collects 50.7 percent of feasible VAT revenues. This is below Uganda, Ethiopia, and South Africa, ranking 55 out of 70 countries for VAT effort. The large compliance gap in VAT of 3.7 percent of GDP⁹ is a major cause of this low efficiency. EBM's enhance formalisation and enable the tax administration to understand what is happening in the economy. To improve their uptake, **the Government of Rwanda will introduce a 10 percent VAT rebate to customers when they receive an EBM receipt.** The purpose of the rebate is to increase VAT compliance by increasing business-to-consumer receipt issuance through a relatively small financial incentive for the consumer. The rebate is a percentage of VAT on the sale to the consumer. VAT rebate would be paid following receipt by the tax authority of a VAT return giving rise to an excess credit. RRA will strive to have the refunds given within a reasonable timeframe of a refund claim being made.

⁹ Thackray, M., D'Agosto, E., and Yost, R. 2021. *Rwanda: Revenue Administration Gap Analysis Program – The Value-Added Tax Gap*. IMF: Washington, DC

Pillar 3: Agricultural and Wealth Creation

Agriculture plays a crucial role in the Rwandan economy, constituting 26 percent of GDP with 39 percent of the employed population working in the sector¹⁰, it was responsible for reducing poverty by two thirds in the Vision 2020 era¹¹. Vision 2050 envisages an agricultural sector that is high-tech with professional farmers utilising modern farming techniques such as greenhouses and urban farming. To achieve this, agriculture must be linked to urbanization and trade, enhancing productivity and increasing value-added per worker eight-fold by 2035 to reach upper middle-income status. Public expenditure will support this shift by targeting innovative financing and risk-sharing facilities, supporting research and investing in infrastructure that will add value.

The tax system will play an important role supporting the sector to make the transformational shift away from subsistence towards highly-productive, professional farms. Endorsing the emergence of new agricultural businesses models and lowering the costs of doing business by providing an efficient, simple tax system with low compliance costs, will facilitate this shift.

According to the Rwanda Food and Agricultural Organization, the agricultural sector contributes 1 percent to total tax revenues despite its prominence to the national economy. The sector is dominated by subsistence farmers who lie below the standard income tax threshold, resulting in low tax revenues from the PIT and CIT regimes.

To support development of the sector and provide relief to subsistence farmers, the Government of Rwanda will maintain the VAT exemptions on existing agricultural and livestock products, and on agricultural inputs and materials. Inputs such as fertilizer and machinery are vital for the development of the sector, to advance productivity and add value. Removing the requirement to pay VAT reduces the cost of these goods, therefore stimulating investment in this strategic area. Exempting VAT on unprocessed foodstuffs such as rice, sweet potatoes, maize and wheat, which are all staple foods for the Rwandan diet, benefits all Rwandans and ensures food is cheap and accessible to all.

¹⁰ NISR. 2021. Labour Force Survey: Annual Report 2020.

¹¹ MINECOFIN, 2020. Vision 2050.

Pillar 4: Urbanization and Agglomeration

As Rwanda develops the number of towns and cities will increase. Vision 2050 seeks to harness the opportunities presented by this change to improve the quality of life for Rwandans, including achieving universal access to quality services and amenities, including water, sanitation, housing, transport, energy, and broadband. While this will require an increase in tax revenues to fund government investments in these basic services, it will also depend on targeted incentives to encourage private sector investment. Rwanda's tax system offers an opportunity to provide relief to businesses looking to invest in these strategic areas. Furthermore, digitization of taxes are important to expand the use of smart technologies throughout the country.

To support access to decent, affordable housing for all Rwandans, the Government of Rwanda proposes zero-rating VAT for the construction of new residential houses. The new investment law grants preferential corporate income tax rate of 0 percent to real estate agencies whose investment capital is equal to or greater than USD 10 million. This will promote affordable housing for low-income people and encourage them to invest in housing. The policy increases incentives for real estate developers to invest in affordable housing programmes in Kigali city, where population density will increase.

Environmental Interventions

Sustainable and green urbanization will transform the quality of lives and promote health benefits for Rwandans. This is one of the key areas for development in Vision 2050, and the tax system can be better aligned to promote choices that improve air quality in the country. Motor vehicle emissions contribute to air pollution which also has significant neurological, respiratory, and reproductive health effects. Increasing urbanization in Rwanda will increase the importance of clean air for better health outcomes. **The government will consider increasing excise taxes on the most polluting cars** to internalize the cost of environmental damage and negative health effects. **The government will also consider banning the import of old vehicles** to further improve the air quality in Rwanda.

To incentivise better environmental motor purchases, the government will exempt import and excise duties and zero-rated Value Added Tax for electric vehicles and equipment. Electric vehicle imports were previously subject to 25 percent import duty, 18 percent VAT, and 5 to 15 percent excise duty, depending on the size of the engine. The withholding tax of 5 percent for electric vehicles and equipment will also be exempted, with other custom-related facilities requested at EAC level. Together with the increase in excise duties for older cars, these interventions will encourage more environmentally friendly car purchases and support the transition to a green economy.

Pillar 5: Accountable and Capable State Institutions

Good governance and effective institutions will determine Rwanda’s socio-economic transformation to a high-income economy. Rwanda’s tax institutions will leverage ICT and enhance staff capabilities to improve service delivery, reduce the cost of revenue collection, and build transparency and accountability. Developing capacity in tax policy formulation will also ensure that Rwanda’s tax system is responsive to changes in the economic environment.

Interventions

1. Strengthening Rwanda’s Revenue Administration

Over the course of the next 3 years, RRA will implement strategic initiatives that improve voluntary compliance. The success of tax policy reforms depends on the operational and administrative efficiency of RRA. Since inception, RRA has been successful in improving tax collections from Rwf 62.8 billion in 1998 to Rwf 1,516.3 billion in FY 2019/20. RRA seeks to expand revenue collection in the future by enhancing automation and improving efficiency of processes. The RRA Strategic Plan 2019-24 maps out key priorities needed to meet domestic financing needs. The revenue administration measures in this MTRS build on RRA’s strategic and reform plans to raise voluntary compliance through targeted strategies and modernize RRA’s business operations by leveraging the use of technology and exploiting data science. The strategy will be broken into three areas:

1) Improving taxpayer services to support voluntary compliance

RRA will improve the delivery of services through digital transformation that will broaden the tax base, enhance transparency, reduce the compliance burden, and improve administrative efficiency. Modern data science tools will be used to close compliance gaps by identifying and reintegrating taxpayers outside the tax system. While electronic platforms for tax registration, payment, filing, and dispute resolution will make procedures clear and transparent for taxpayers. Advanced analytics will also be used to identify taxpayers who underreport and will be a key driver of value by building up extensive data holdings.

Stakeholder consultations will be strengthened to improve services and develop user-based design techniques. This will help the RRA to identify usability problems, collect qualitative and quantitative data, and identify opportunities to improve products and services. User testing will ensure problems are identified early so that services are tailored to taxpayers. Furthermore, RRA will monitor taxpayer satisfaction and perceptions by conducting regular surveys. Engaging with citizens in the ways outlined will help to improve the taxpayer experience and build trust and confidence in the tax system, which will foster and support voluntary compliance.

2) Enhancing taxpayer compliance through targeted initiatives

RRA will target opportunities in key risk areas to improve voluntary compliance. Data science will be used to identify taxpayers with similar risk characteristics so that personalized communications and timely interventions can be developed. A series of Compliance Improvement Strategies will target high risk areas and implement graduated treatments based on risk level and prior behaviours to maximise voluntary compliance cost-effectively. These are outlined below:

- **Promoting Electronic Billing Machines (EBMs) and Improving VAT Compliance:** A multifaceted compliance strategy will improve support for small businesses and encourage community engagement

to reduce the illegal informal economy and encourage EBM usage. RRA will establish support centres for small businesses and engage citizens through an education campaign on the importance of obtaining receipts and offer incentives that encourage consumers to ask for receipts.

- **Aggressive Tax Planning by Individuals:** There is evidence that wealthy individuals have access to sophisticated advice and use offshore tax havens to avoid paying tax¹². RRA will provide support and supervision for wealthy citizens to manage their complex tax affairs so that the community has confidence all taxpayers are effectively managed by the RRA. This strategy will include awareness campaigns, require valid TIN for professional registration, and link tax compliance to re-licensing. RRA will also continue to participate in the international taxation arena on exchange of information, including implementation of the Convention on Mutual Administrative Assistance in Tax Matters in order to combat sophisticated tax planning.
- **Manufacturing Sector:** Improving compliance in the manufacturing sector will focus on increasing formality among smaller firms and tackling international base erosion and profit shifting with larger, foreign-owned firms. RRA will conduct educational campaigns, consult stakeholders, build data and analytics capabilities to strengthen detection of informality and will maximise Global Forum membership to address issues with larger firms.
- **Customs Compliance Improvement:** RRA will implement initiatives to improve tariff classification capabilities and advance the Valuation Unit. The customs unit will engage stakeholders to encourage voluntary compliance and review the sanctions policy. Risk management improvements for clearance, post customs audits, and IT responses will be implemented to develop the capability and effectiveness of the risk function.

3) **Modernising RRA's business operations, capacity, and productivity**

A new business operating model will strengthen RRA's organizational capacity to support implementation of these ambitious reforms. Improving IT infrastructure, building data analytics capacity, enhancing staff skills, and hiring more staff with a range of skills are crucial to expand performance and achieve the MTRS. Developing RRA's governance will be critical for effective coordination, oversight, collaboration, and implementation of the MTRS.

Building the technical skills to manage complex issues is a priority area for capacity enhancement in RRA. Focus areas will include: international taxation; implementation of new transfer pricing rules and standards of exchange; audit capabilities; advanced data analytics including data management and data science; economic analysis with a focus on revenue forecasting and tax expenditure analysis.

2. **Strengthening Tax Policy Formulation**

The newly created Tax Policy Directorate General (TPD) in MINECOFIN is responsible for a wide variety of tasks that includes advice on tax policy, identification of resources for tax revenue mobilization, impact of tax policy on economic agents, budget revenue forecasts, revenue performance monitoring and review of trade tax policies. Each one of these areas are highly significant and requires both staff and skills resources. However,

¹² Institute of Development Studies. 2020. *Working Paper 109: Tax Compliance of Wealthy individuals in Rwanda*. Jalia Kangave, Kieran Byrne and John Karangwa.

so far TPD has tried to fulfill these functions with a limited number of professionals, inevitably constraining delivery of tax policy advice. TPD is responsible for— i) all final revenue forecasts and collection estimates of policy changes for the national budget; ii) the TPD’s output would be integrated with the ministry’s development of the macro-economic assumptions; iii) the development and application of tax simulation models; (iv) analysis of revenue performance and trends (jointly with the revenue administration authorities); (v) identification and quantification of revenue, economic and distributional impacts of tax proposals; and (vi) public explanations of variances between budget revenue forecasts and actual outcome.

In order to expand the scope of tax policy advice delivery, the quantity and the capacity of TPD staff has to increase. Increasing the number of staff in the TPD and utilizing external resources in the short and medium-term:

- To increase cooperation on policy design issues with RRA.
- To seek advice from international agencies on selected issues to gain from international experience. As needed, this could be complemented by consultants provided through development partners such as GIZ, TaxDev, KOICA and FCDO.

IV. MONITORING AND EVALUATION

Monitoring and evaluation will form an integral part of the MTRS, providing a framework to track progress towards expected results and assess the impact of implementation throughout the three-year period. An MTRS Committee with stakeholders from across government, the private sector, and civil society will oversee evaluation of the MTRS implementation, while internal working groups within RRA and MINECOFIN will lead the monitoring of day-to-day implementation.

As the measures included in this MTRS require further studies and stakeholder engagement, the framework with which to measure the success must be flexible. Once policies are implemented, analysis of the revenue targets and the distributional impact of policies will be continually reassessed.

Evaluation, led by the MTRS Committee, will use reports produced by the RRA and MINECOFIN monitoring teams to ensure accountability and promote improvements in the implementation of the MTRS. This committee will meet regularly to ensure tax policies are being implemented according to timelines.

V. CONCLUSION

Rwanda must increase its revenue mobilization efforts to finance Vision 2050 and achieve its economic growth ambitions. The MTRS improves the likelihood of tax reform success because it takes a holistic and consensus-based approach to the reforms. Documenting this ambitious yet realistic plan over the next three years lays the foundation for long-term reform of the tax system while ensuring the government is accountable for achieving the 1 percentage tax-to-GDP growth. A careful combination of tax policy and tax administration changes over the next 3 years will achieve this target: administrative reforms will contribute an estimated 0.54 percent of GDP and policy reforms an estimated 0.46 percent of GDP. However, the overall success of these outcomes will depend on post-pandemic economic recovery.

The MTRS launches a nationwide conversation between the government and citizens to build consensus on the tax system. It is guided by principles of efficiency, equity, simplicity, and revenue growth, not solely focused on increased revenue generation. This first MTRS represents the Government of Rwanda's commitment to tax reform, and opens a dialogue with wider society on what the tax system should look like. For this reason, future MTRS will be more ambitious as the government and civil society will have established experience to build upon.

Restructuring of the tax system along the lines of this MTRS will be representative of extensive consultations with government and non-government stakeholders. This MTRS sets the high-level direction of tax policy changes over the next three years, but the details of policies will be determined through comprehensive stakeholder engagements at all stages of each policy development process. The common ambition to achieve Vision 2050 will be the uniting force behind this MTRS.

ANNEX 1: STAKEHOLDER ENGAGEMENT METHODS

Stakeholder engagement is a crucial element of inclusive policy making and will play a central role in the MTRS. Meaningful consultation requires involving stakeholders early in the policy design process, encouraging feedback and engagement during policy development, and continues following implementation of the policy. Such engagement must be free from manipulation and capture by organised interest groups. Furthermore, regulators must be held accountable through effective feedback mechanisms that ensure comments are handled appropriately and where necessary included in final policy proposals. Creating tax policy with a user-centred design improves understanding and acceptance of tax law and encourages active engagement and evaluation of policies.

The Organisation for Economic Coordination and Development (OECD) outlines best practice for methods of stakeholder engagement in policy making¹³:

- **Informal consultations** can be used at all stages of a policy design process to collect information from interested parties. These can be used ad hoc and include methods such as phone calls, letters, and emails. As they are less cumbersome, less formal and more flexible, policymakers can gain a range of views at speed, however, they are limited in transparency and accountability
- **Circulation of regulatory proposals** is also relatively inexpensive and can induce affected parties to provide information to policymakers. Circulation can be systematic, structured, routine, and predictable to gather a range of views. However, less organised groups are in weaker position than those who are well prepared to engage.
- **Public notice and comment** can be an open and inclusive way to engage with the public and is particularly important for lower-level laws when it is necessary to get technical information spread widely.

The MTRS will engage with stakeholders using the following methods:

- **Public meetings/townhalls** will be used to present proposed tax changes to a large group of people and communities. This method will be used when laws are in the final stages as it is more likely to be informative rather than consultative.
- **Workshops** will be used to outline proposed tax changes to affected stakeholders, gather opinions and views through participatory exercises to brainstorm issues and develop solutions. This will be the main method of consulting with stakeholders when developing policy reforms.
- **WebEx meetings** are low cost and beneficial when public gatherings are not allowed due to COVID-19 restrictions. Furthermore, they make it possible to target multiple geographies simultaneously. However, this method excludes those without access to internet, who are likely to be the most marginalised in public policy making. This method will only be used when severe restrictions are in place.

MTRS Stakeholder Engagement

Several consultations were conducted throughout the development of this MTRS and are outlined in the table below. Despite the challenges presented by COVID-19, these meetings took place in-person where necessary. Three separate workshops were conducted at the MINICOFIN Head Office for maximum engagement with private sector representatives. Invitees were divided into three sessions and grouped according to interests:

- Session one: representatives from the Civil Society Organisation, and the Rwanda Bar Association.

¹³ OECD. 2017. Best Practice Principles on Stakeholder Engagement in Regulatory Policy

- Session two: representatives from the Private Sector Federation Civil Chambers, Chamber of Commerce, Rwanda Bankers Association
- Session three: representatives from the Institute of Certified Public Accountants of Rwanda, PwC and Ernst & Young

The draft MTRS was shared with these stakeholders ahead of the meeting. Attendees at the workshops were presented with the draft policy proposals and asked to comment on behalf of those they were representing. Meetings were informative as the MTRS team explained the logic behind proposals, and consultative as attendees submitted their reactions. The content of this MTRS sets out the big picture of tax policy changes over the next three years, and the purpose of the stakeholder engagement was to obtain consensus on the overall objective and orientation of tax reforms.

MTRS Dissemination

Following Cabinet approval of this MTRS, numerous in-depth studies will be conducted to establish the details of each reform. Dissemination will aim to gather more feedback from larger groups with in-depth discussions. The dissemination process will ensure buy-in from the population and ensure issues are addressed when implementing the MTRS and designing the tax policy reforms.

Table 3: MTRS Stakeholder Engagement and Dissemination

Date	Stakeholders	Objective	Consultation method
Pre-Engagement: Government consultation on MTRS Policy Direction			
May	Rwanda Development Board	Obtain feedback on policy proposals	WebEx meeting with government stakeholders to discuss the proposals and receive comments.
	Ministry of Commerce and Industry		
	Ministry of Infrastructure		
	Central Bank of Rwanda		
Phase 1: Tax Policy Design consultation			
June	Rwanda Bankers' Association	Present proposals of tax changes; gather feedback on issues stakeholders raise; identify solutions	In-person Workshops with 15 representatives: tax policy proposals presented and discussed with attendees. Issues raised and solutions discussed.
	Private Sector Federation		
	PSF Civil Chambers		
	Small Businesses		
	Institute of Certified Public Accountants of Rwanda, PwC		
	Bar Association		
	Civil society organisations		
Phase 2: Approval			
August		Submit proposals to Cabinet	
August		Discuss proposals with Parliament & Commission	
Phase 3: Dissemination			
September	News, radio, tv journalists	Brief journalists on proposed policies	Media communication
September	All affected taxpayers	Educate public on new tax policies; continue to gather views on MTRS implementation	Communication & dissemination strategy
Phase 3: Ex-Post Consultation			
Throughout MTRS1	Representatives of taxpayers from public and private sectors	Gather informal comments on impact of new policies: successes/challenges, feed these comments into policy reviews; maintain channels for continual feedback. Consult on policy proposals for MTRS 2	WebEx/informal communication