November 8, 1999

Ghana's Trade Policies: Tariff Rate Structure and Revenues

1. Introduction

Ghana has a relatively simple tariff structure, comprising three major rate categories:

- a low rate of 0 percent (with some items recently raised to 5 percent) reserved primarily for primary products, capital goods, and some basic consumer goods,
- a moderate rate of 10 percent applied primarily to raw materials and intermediate inputs, as well as some consumer goods, and
- a higher rate of 25 percent, mainly on final consumer goods.

In addition

- there are a number of programs under which imports can be exempted from import duties[1] and
- manufacturers can apply for permission to import raw materials and intermediate inputs at concessionary duty rates.

This preliminary review of the tariff system addresses two issues — rationalization of the tariff structure and the revenue productivity of the import tariff system.

The economic effects of the current tariff structure are more perverse than is widely believed. More comprehensive reforms than those currently being discussed are called for. While revenue concerns are important, the unintended incentive effects of the tariff structure cannot be ignored.

Additional revenues could be obtained by tightening exemptions, adjusting the tariff rate structure, and administrative reform. We estimate that removal of exemptions that have no economic justification would yield about 31 to 38 billion cedis of additional revenues, about 7.8 to 9.5 percent of total tariff revenues, or 1.1 to 1.3 percent of total tax revenues. Raising the tariff on zero-rated goods to 5 percent would yield a maximum of 62.5 billion cedis of additional revenue, while lowering the 25 percent rate to 20 percent should cost no more 39 billion cedis.

The greatest potential for revenue improvement, as well as significantly enhanced trade facilitation is most likely to be found in administrative reform of customs and related procedures. While it is not possible to estimate the likely magnitudes, international experience suggests that revenue increases of 20 percent (on a base which includes import-related excises and VAT as well as import duties), and reductions in trading costs of a similar magnitude are well within the realm of possibility.

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[1] Duty exemption programs are dealt with in much more detail in a related report, Roshan Bajracharya and Frank Flatters *Ghana's Trade Policies: Exemptions from Import Duty*.

Immediate attention to likely problems arising from the termination of the PSI system, and simultaneous introduction of GATT valuation is also required in order to avoid some major revenue and other customs administration problems next year.

2. Rationalization of the Tariff Structure

General Effects of Tariffs

Import tariffs distort the allocation of resources, providing artificial incentives that direct resources away from their most productive uses. As a result, import tariffs reduce incomes and the sustainability of long term development.

Among the direct allocative effects of tariffs are that

- they harm exports by
  - raising the cost of imported and importable raw materials,
  - increasing the attractiveness of selling in the local market, and
  - artificially raising the foreign currency value of the domestic currency;
- they draw investments from sectors with low (or negative) levels of protection to those with higher levels of protection, thus lowering the overall productivity of investment in the economy;
- they reduce transparency and have effects that are difficult to predict, since they raise both the cost of imported inputs and the local price of protected outputs.

In addition, import tariffs

- create unintended subsidies to smuggling, and
- encourage rent-seeking by domestic producers and other special interests who see manipulation of government policies as an easier and more direct way to increase profits than engaging in productive economic activities.

These harmful effects of tariffs are greater

- the higher is the average level of tariff rates,
- the greater is the dispersion of rates,
- the greater are the differences in rates for similar products,
- the more the government attempts to use tariffs to achieve social purposes, and
- the more discretion there is in setting rates on a case-by-case basis.

Unintended Effects of Import Tariffs in Ghana

Ghana's tariff rate structure is relatively simple, and the rates are not exceptionally high. Nevertheless the system is surprisingly complex, and many of its effects are much different than what might have been intended. The following are relevant features of the tariff structure.

- Many primary products are taxed at rates of 10 and even 25 percent, thus raising their domestic cost to potential downstream processing industries.
- Final consumer goods are taxed at quite different rates — 0 percent for bicycles, 10 percent for TVs and 25 percent for VCRs, for instance. This reflects, in part, a desire to incorporate some progressivity into the import tariff system.
- There is a significant and growing use of "tailor made" tariffs which provide for zero rates on a wide range of industrial raw materials, contrary to the general "rule" of taxing these goods at 10 percent. These exceptional rates are found especially in chapters 82 (tools and machinery), 84 (boilers, machinery, mechanical appliances, and parts thereof), and 85 (electrical machinery and equipment, sound and television equipment, and parts thereof) of the Tariff Book.[2] Most of the special items in these chapters are zero rated for customs duty. These rates are not specific to any particular end uses or end users; they apply to all imports of these goods. In addition, there is growing use of tariff rates which are specific to particular end-users and/or end-uses. These latter rates, and the conditions attached to them, are found in chapter 98 of the Tariff Book. These rates are available only when the goods are imported "by manufacturers approved by the Commissioner" (Chapter 98A) or "by enterprises under the Ghana Investment Promotion Centre Act, 1994 (Act 478)" (Chapter 98B). For many of the Chapter 98 items, the Tariff Book specifies particular end uses for these products (e.g. "polyethylene for the manufacture of mosquito nets", "materials for mosquito coils", "raw materials for manufacturers of pipes and tubes of plastic",and "steel wire for hexagonal wire netting"). The rates are all either 0 or 10 percent.
- Manufacturers facing high import tariffs (25 percent) on important raw materials are permitted to apply for concessionary rates (10 percent) to give them access to these goods at lower cost. Application for concessionary rates must be made on a consignment-by-consignment basis, and can be processed only after the goods arrive in Ghana.

Some of the surprising and unintended effects of Ghana's tariff system can be illustrated with cases based on interviews with Ghanaian business persons and government officials. The limited time available for this study permitted neither a systematic sampling of Ghanaian industries nor an economy-wide effective protection study. Nevertheless, meetings were held with and data collected from a wide variety of businesses and government officials. The resulting examples, based on data from Ghanaian businesses and on actual Ghanaian import and export policies, provide an accurate reflection of some of the most important issues arising from the structure of the tariff system.

[2] For more details, see Ghana Investment Promotion Centre *Investment Incentives in Ghana As Provided Under the GIPC Act, 1994* (amended version, July 1998).

Case 1

Excessive Protection from Tailor Made Tariffs

Discussions with senior officials suggest a view among at least some policy makers that special tariff provisions are necessary to encourage the development of local industries. The protective effects of such tailor made tariffs are surprisingly large — much more than necessary to encourage industries that have any potential to be internationally competitive.

Consider the case of a simple kitchen utensil worth $1 in world markets and made in Ghana of imported aluminum worth $0.70 at world prices. At world prices, local value added in the manufacture of the utensil is $0.30.

Under Ghana's "standard" tariff regime (imports of final goods taxed at 25 percent and raw materials at 10 percent), the kitchen utensil would be subject to a 25 percent import tariff, and the imported aluminum would be taxed at 10 percent. As a result of these tariffs, the domestic cost of the imported aluminum raw material would rise from $0.70 to $0.77, and the local market price of the finished utensil would rise to $1.25. Under the "standard" tariff regime, therefore, a domestic producer would have a local processing margin of $0.48 ($1.25 - $0.77) rather than $0.30 under free trade. Thus the "standard" tariffs provide effective protection of 60 percent (the percentage difference between $0.48 and $0.30). This allows them to have costs which are 60 percent higher than foreign competitors — a very generous margin indeed.

Suppose now that, in order to provide additional assistance to utensil manufacturers, the statutory rate on aluminum sheet is reduced to zero. This lowers the cost of the imported raw material to $0.70, and raises the processing margin to $0.55 ($1.25 - $0.70). The effective protection provided by this tariff structure is 83 percent (the percentage difference between $0.55 and $0.30). Such a high level of protection, through tailor made provisions on input taxes, is certainly unnecessary.

Case 4, below, provides further illustrations of the difficulties with tailor made protection.

Case 2
Concessionary Rates

Cardboard cartons are required for the packaging of fresh fruit exports from Ghana. They are also used to package a wide range of other products which are sold in the domestic market and/or exported.

Two of the principal raw materials in making such cartons are heavy gauge kraft paper and starch. Both of these materials are imported, and are subject to import tariffs at a rate of 25 percent. These two imported materials account for at least 70 percent of the cost of a finished carton. Thus, import tariffs raise the cost of locally produced packing materials by at least 17.5 percent.

Carton manufacturers can apply for a concessionary rate of 10 percent on their imported raw materials. With this concessionary rate, the cost-raising effect of import tariffs is reduced, in principle, to 7 percent. However, the concessionary rate must be applied for on a consignment-by-consignment basis. Only the manufacturer (not a trader) is eligible for this rate, and the application may be submitted only when the goods arrive in port. The normal addition to port clearance time to complete these procedures is about a week. This results in additional working capital needs, and increased storage and demurrage costs, seriously reducing the cost-savings made possible by the concessionary rate.

Restriction of concessionary rate privileges to manufacturers prevents the emergence of traders who might be able to reap economies of scale, and provide particularly valuable services to small and new producers, and in meeting specialized and emergency needs of larger producers.

The only conceivable reason for this concessionary rate system is to ensure that goods with dual use — as manufacturing raw materials and as final goods — do not escape the higher rate intended for final goods. Neither heavy gauge kraft paper nor starch have significant use as final products. The statutory rate on such products should be reduced to 10 percent.

For raw materials that do have significant dual uses, the first best solution would be to lower the rates on final products, and second best would be to introduce a registration program for manufacturers and traders that reduces the costs of the concessionary rate procedures.[3]

[3] See Vincent Castonguay *Review of CEPS Activities with Respect to Controls, Processing Procedures and Trade Facilitation Regimes* (Sigma One Corporation), September 1999 for detailed recommendations in this regard.

Case 3
Indirect Exports

Locally made goods which are not exported directly, but which are used in the manufacture or packaging of domestically produced exports are known as indirect exports. Locally made packing materials are an example of such a product.

In the appropriate regulatory environment, the development of direct exporting activities soon promotes the development of indirect exporters — sometimes referred to as supporting industries. It is a serious mistake, however, to try to force exporters to use the products of local supporting industries. This only raises the costs of exporting industries, thus lowering their competitiveness and discouraging export investments. Ghana, quite sensibly, has procedures in place to provide exporters easy access to imported packing materials.

It is interesting, however, to look at the regulatory barriers to the development of domestic packaging industries. Cardboard cartons provide a good illustration. A pineapple exporter operating in a free zone or bonded facility is permitted to import cartons duty-free. The typical cost of a heavy duty imported carton is about $1. This is the price a local carton producer must be able to match in order to compete.

Imported materials (kraft paper and starch) make up about $0.70 of the cost of a carton, at world prices. If a local producer pays the full 25 percent tariff on these materials, the cost becomes $0.875, leaving only $0.125 as a processing margin, compared with $0.30 for a foreign producer. In other words, the local producer faces *negative* effective protection of 58.8 percent. If the local producer gets the concessionary rate of 10 percent on these materials and there are no additional costs associated with the procedure, the processing margin is increased to $0.23, and the effective protection he now faces is "only" minus 23.3 percent.

If the local producer is able to get a duty drawback on materials used in cartons sold to exporters, the cost penalty of the import duties is reduced. The extent of this reduction depends on the rate of import duty, the interest rate and the time taken to obtain the drawback. If the annual rate of interest is 30 percent, the rate of duty 10 percent, and the drawback takes 6 months to process (from time of import to the time of the refund), then the additional cost of each $0.70 of imported raw materials is $0.01. The local carton manufacturer still faces negative effective protection at a rate of 3.3 percent. If it takes a year to process the drawback claim, not uncommon in Ghana recently, this cost is doubled, and effective protection is minus 6.7 percent.

If the local carton producer gets permission to produce in a bonded manufacturing facility, and products sold to pineapple exporters are treated as exports, then import duties on raw materials can be fully avoided, and the company can compete on a level playing field against imported cartons — i.e. he would face an effective rate of protection of 0 percent on cartons produced as indirect exports.

The regulatory environment is clearly very important in fostering the development of indirect exports or supporting industries. Since export-oriented investors are conscious of the importance of supporting industries, these factors are important in their decisions as well.

Case 4

One Firm's Output is Another's Input — Which Makes it Difficult to Protect Everyone

Ghana has tried to use import tariffs to protect local producers. Some senior officials feel that ministers should have more flexibility to respond to emerging "needs" for protection. The garments and textile industry illustrates some of the difficulties encountered by this strategy.

Garments, a basic good for all Ghanaians, are subject to an import tariff of 25 percent. This might seem to be more than adequate to assist local producers. However, the magnitude of this tariff, together with the size of the local market, serve as a magnet to smugglers. Two of the most important forms of smuggling are transit shipments and imports of "used" clothing.

Transit shipments are a very well-known means of enrichment of dishonest traders who work in collusion with unscrupulous customs officials. Ten containers are entered into Ghana for transhipment to a neighboring country. As goods in transit they are exempted from import duty. The goods are accompanied by customs officials while in transit to the neighboring country, and are documented as being cleared out of Ghana. In reality, only one of the containers (at most) actually leaves Ghana, and the remainder are sold in the local market. This is good for local consumers, for the traders, and for the customs officials involved. It severely reduces government revenue and the protection provided to local garment producers by the 25 percent tariff.

"Used" clothing is extremely difficult to value for customs purposes, and is usually substantially undervalued. Furthermore, large amounts of used clothing are smuggled and/or brought in under "charitable" exemptions. This also diminishes the protective (and revenue) effects of the garment tariffs.

The textile, yarn and cotton industries are also important sources of income and employment in Ghana.

In light of the importance of textiles to the local economy, the government recently increased the import duty on textile imports from 10 percent to 25 percent. At the same time, certain textile imports from neighboring countries are allowed in duty-free as part of Ghana's ECOWAS commitments.

Yarn is subject to an import duty of 10 percent. Raw cotton is an export product for Ghana. However, its quality is of a relatively low grade (due to prevalence of impurities and to short fibre length), and so spinning industries must blend longer fibre imported cotton when making yarn. Imported cotton is also taxed at 10 percent.

This tariff structure for the different segments of the garments and textile industry are meant to protect local producers. But the net effect of this complex structure of protection is actually quite difficult to determine.

Garments: If the 25 percent tariff on garments succeeded in raising domestic prices 25 percent above world prices, and if the price of cloth, the main input, were also raised by 25 percent as a result of that tariff, garments would benefit from substantial effective protection of about 25 percent. However, with the prevalence of smuggling and of undervalued imports of used clothing, the tariff is unlikely to raise the prices of garments by much more than 10 percent. This would make the effective protection for garments negative, and probably in the order of -35 percent.[4]

[4] This assumes importable raw materials to account for 75 percent of the cost of garments, at world prices.

The main lesson here is that heavy protection of textiles is very harmful to garment producers. Of course, if a garment producer could get a concessionary rate of 10 percent on textile imports, his effective protection would return to about 10 percent. If concessionary rates were widely available, then it would be simpler and more efficient to lower the statutory rate on cloth to 10 percent — where it as until recently.

Textiles: With an effective tariff of 25 percent on cloth and 10 percent on fibre, textile producers get a very high level of effective protection — 60 percent if yarn accounts for 75 percent of the cost of cloth. If the high tariff on cloth is made partially ineffective by ECOWAS imports, by concessionary rates to most producers, or by smuggling, effective protection will be diminished. If the net effect of all these factors is to raise the cost of cloth by only 10 percent rather than 25 percent, yarn production receives effective protection of 10 percent.

Spinning: Yarn is subject to a 10 percent import tariff. Imported cotton, which is needed for blending with local cotton, is also taxed at 10 percent. In addition, each import shipment requires approval before it can be cleared into the country. While we have heard no stories of difficulties in obtaining permission, this process certainly raises the cost of importing. The net impact on the effective protection for yarn producers depends on the extent to which local cotton prices are raised by protection and by the proportions of local and imported cotton used in the spinning process. However, effective protection for yarn producers is almost certainly positive, but much less than 10 percent.

Cotton: Ghana exports cotton. Most of the imported inputs used in cotton production (fertilizers and chemicals) are duty-free. The net effect of these measures is to provide zero effective protection to cotton exports — cotton producers play on a level field in world markets. The 10 percent tariff on imported cotton provides some protection for domestic market sales, but we have no evidence on how much. All we can say is that cotton gets some effective protection for local market sales.

The general conclusion is that, despite some earnest efforts to protect all segments of the textile and garments industry, the government has been more successful at subsidizing smuggling and has quite possibly provided negative effective protection to the most labor intensive sector — garments — of this industry. This was certainly not the government's intention in developing the current tariff structure.

A much simpler and more uniform tariff structure, starting with a maximum rate of no more than 10 percent, would provide more uniform protection, reduce smuggling, contribute to government revenues, and quite likely reduce the local price of clothing.

Case 5
Using Tariffs for Income Redistribution

It is tempting to use import tariffs to achieve redistributive goals. By taxing imports of luxury goods at relatively high rates and exempting or zero-rating imports of basic goods, it seems possible to use import tariffs to achieve progressivity in the tax system. Ghana does this to some extent already. Bicycles, a basic good, face a zero rate of import duty; television sets are taxed at 10 percent, and VCRs at 25 percent. (On the other hand, footwear and garments are taxed at 25 percent, a high rate for such basic goods.)

Using import tariffs for this purpose ignores two important features of protection:

- tariffs also distort investment decisions, thus diminishing the efficiency with which a country uses its capital resources and reducing the long run rate of development, and
- tariffs also affect the demand for labor and other primary inputs, hence influencing the distribution of income at its source.

Placing high tariffs on luxury goods, for which demand is relatively small in a poor country like Ghana, provides an artificial incentive to invest in industries producing such goods. Providing low or negative protection to basic goods such as bicycles, on the other hand, prevents the development of labor intensive industries whose products have relatively high demand in Ghana.

Bicycles currently face a zero rate of import duty. They are also zero rated for VAT purposes, which means that local bicycle producers would not be able to get any tax credit on their inputs, thus putting them at a disadvantage relative to imports of VAT-exempt bicycles. As might be expected in these circumstances, despite its relatively low skilled labor intensity, this industry has not developed in Ghana, and no domestically produced or assembled are available in the market. The Tariff Book has recently been amended to add an item to chapter 98 which zero rates (for import duty purposes) parts and components used in the production or assembly of bicycles (by manufacturers approved by the Commissioner of Customs). At best this will make the tariff system neutral with respect to bicycle production.

Meanwhile, high tariffs on “luxury” goods encourage smuggling or (worse) the establishment of inefficient industries assembling goods with little demand in the local market.

Penalizing low-skill labor intensive industries and subsiding higher tech, more capital intensive industries reduces the demand for the poorest workers in Ghana, and hinders the development of industries in which Ghana might be expected to have a strong comparative advantage. This does not serve the redistributive purpose for which such measures were designed. And it reduces Ghana’s long term development potential.

The answer is not, of course, to give high protection to basic goods either. Difficulties with this approach can be seen in the garment industry example discussed earlier. The lesson is that the tariff regime should be made as neutral as possible — through low and uniform rates.

Case 6
Using Tariffs for Other Social Purposes

Under tariff item F.54 of the Third Schedule of the Customs and Excise Act, imported printed materials are exempt from import duties and sales taxes. While this has an admirable social purpose — to encourage literacy — it has some perverse implications.

Since Ghanaian publishers must pay import duties on imported paper, printing ink and other publishing materials, they are at a competitive disadvantage against imports. They face negative effective protection in the domestic market. In tenders for government textbooks, for instance, printers in Hong Kong have a cost advantage by virtue of duty free access to all these raw materials. A cost of this pro-literacy policy is to tax the establishment of domestic printers and publishers of Ghanaian reading materials.

Under this same provision, imports of used newspapers and magazines face zero duty and VAT, while clean paper is taxable (generally 10 percent). As a result, street foods are wrapped in old newspapers rather than clean paper, posing a hygiene issue for consumers of these foods.

Case 7
The Protective Effects of Some Proposed Tariff Reforms

Two relatively simple and straightforward tariff structure reforms are now under discussion. The first is to replace the zero rate facing many imports with a rate of 5 percent. The second is to lower all 25 percent rates to 20 percent. Some persons fear that these changes would reduce effective protection for many producers to unacceptably low levels.

To examine this contention, consider once again the illustrative kitchen utensil maker producing a product worth $1 in the world market and using imported raw materials worth $0.70 at world prices.

As shown earlier, current tariffs of 10 percent on raw material inputs and 25 percent on its output provide this manufacturer effective protection of 60 percent. With a zero rate on imported raw materials, effective protection would be 83 percent.

Suppose the tariff rate on the finished product were lowered to 20 percent and the tariff on raw materials was set at 5 percent, as suggested under one set of tariff reform proposals. The maximum price he could charge in the local market would be $1.20, and the domestic processing margin would be $0.43 ($1.20 minus the imported raw material cost of $0.77). This would give effective protection of 43 percent, a very high level of protection, and far in excess of the nominal tariff on the firm's final product.

However, there are still several reasons that producers might fear these tariff changes, especially the elimination of the zero rate category.

- In the absence of an effective and fast-disbursing duty drawback program, or adequate exemption programs for bonded warehouse or free zone production, eliminating the zero rate could be a serious hindrance to the competitiveness of those producing for export, as direct exporters, or as indirect exporters supplying inputs to direct exporters.
- Wide and arbitrary use of exemptions could nullify the effects of the tariff changes for some producers, putting them at unfair disadvantage against exempt imports, or giving them an unfair advantage in access to taxable raw materials.

Neither of these concerns necessarily provides a case against the suggested reforms. The first is an argument for effective programs for exporters, and the second emphasizes the importance of applying the new policies consistently across all producers and industries.

3. Import Tariffs and Government Revenue

According to the 1999 Budget, import duties were expected to raise about 400 billion cedis of government revenue in 1998. This was equivalent to 14 percent of total tax revenue.[5] In light of fiscal difficulties arising from falling commodity prices and previously committed outlays in respect of cocoa purchases, there is pressure to find additional revenue sources for the immediate future.

Without belittling the urgency of these revenue needs, it is important to ensure that measures to meet with immediate concerns are broadly consistent with structural changes needed to promote Ghana's long term development. In this context, it is useful to note that, with the relatively low percentage of import tariffs in total revenues, even a 30 percent increase in tariff revenues would increase total tax revenues by only 4.2 percent. Since major increases in tariff rates would have serious costs in terms of incentive effects and compliance, it would be prudent to look to other revenue sources in addition to tariffs.

Broadly speaking, there are three possible sources of new revenues from import tariffs:

- tightening of the exemption regimes,
- changes in tariff rates, and
- improvements in customs administration.

Exemption Regimes

According to preliminary estimates, about 1.87 trillion cedis out of Ghana's 1998 imports of 7.11 trillion cedis were exempt from import duties. (See Table 1.) The effective tax rate on non-exempt imports was approximately 5.6 percent. If the same effective rate could be obtained on all exempt imports, this would yield additional revenues of about 105 billion cedis.

However, this is an unrealistic expectation, for to do this would require eliminating a number of exemptions that are justified on economic grounds (e.g. for exporters) or are necessary as a condition of international agreements. A related report provides a detailed review of Ghana's import duty exemption regimes, and makes recommendations for removal or replacement of a number these exemptions.[6]

Among the proposed changes that might be expected to have a significant and predictable revenue effect would be elimination of the exemptions for the Volta River Authority, GIPC, and personal effects for home use. Imports in these three categories amounted to about 600 billion cedis, for 8.5 percent of total imports, in 1998. The effects of removing other exemptions, such as those for

[5] Revenue figures are from Table A.3 of the 1999 Budget.

[6] Roshan Bachracharya and Frank Flatters *Ghana's Trade Policies: Exemptions from Import Duty* October, 1999.

churches, charities, advertising matter and fishing floats are more difficult to estimate because of the way in which such exemptions are recorded by customs, with most of them apparently lumped under "Ministry of Finance exemptions." The total reported amount of "Ministry of Finance exemptions" in 1998 was 370 billion cedis, or 5.2 percent of total imports.

Other important exemptions (in terms of trade values), such as those for the grants and aid, ECOWAS imports, VALCO, the Minerals Commission, and diplomats should not be thought of as significant sources of additional revenue. Such exemptions are required as part of international agreements, are justified on economic grounds and/or would have to be replaced by measures of a more or less equivalent revenue impact elsewhere if removed.

Assuming that one-half of the imports under the Ministry of Finance heading would lose their exemptions under our recommendations, we could conclude that the recommended exemptions changes would subject an additional 785 billion cedis of imports to import duties (based on 1998 trade values). At an effective import duty rate identical to that applying to all dutiable imports in 1998 (5.6 percent), this would yield additional customs revenues of 38 billion cedis.

If personal effects for home use remained subject to duty exemption, the revenue gain would fall to 31 billion cedis.

These estimates do not include the possible effects of administrative reforms in monitoring and control of exempt imports, especially those entered on temporary exemption into bonded warehouses and free zones, and for re-export to other countries. We have no data on which to base estimates of such revenue gains, but we suspect that, based on "common knowledge" relayed to us by traders and other business persons, these revenue gains would be large relative to the estimated gains from changes in the lists of exempt imports.

Tariff Structure Reform

Two rate structure reforms are currently under discussion, i.e. raising the bottom rate from 0 to 5 percent and lowering the top rate from 25 to 20 percent. The latter is non-controversial from an economic perspective, while the former, which represents an increase in average rates (not good) and narrowing of the rate dispersion (good) is more uncertain.

The main reason for raising at least some goods from a 0 to a 5 percent rate is for revenue generation. An IMF/World Bank study conducted last year, based on 1997 data, suggested that applying such a measure to all consumer good imports would have only a very small impact on government revenues, raising import duty collections by only one percent. Broadening the increase to cover a wider range of goods would have a larger impact.

TABLE 1: EXEMPT AND DUTIABLE IMPORTS, 1998[7]

	Million Cedis	% Share
Dutiable		
Zero rated	1,247,954	17.6
Non-zero rated	3,991,323	56.2
Exempt*	1,867,199	26.3
Total Imports	7,106,477	100.0

*Note: This does not include goods entered under temporary exemption to bonded warehouses, free zones, or for transhipment. In the absence of data on goods cleared after such entries, we have assumed that 15 percent of goods entered under temporary exemption were exempted on clearance into the local market after temporary entry.[8]

According to estimates based on 1998 trade data made available for this study, 1.25 trillion cedis of imports entered Ghana at zero rates in 1998. If all of these imports were taxed at a rate of 5 percent, and if there were no negative response of imports to such an increase, this would yield 62.5 million cedis of revenues — an increase of 15.5 percent in total tariff revenues or 2.2 percent in total tax revenues. This is an upper bound on the expected revenue gains from elimination of the 0 percent rate category. The actual number will depend (negatively) on the proportion of goods

[7] Data in this table were calculated from ASYCUDA data provided by MOTI, in which all transactions were classified according to Ghana's customs processing code (CPC). Total imports can be counted either when goods enter the geographic area of the country (including bonded warehouses and free zones), or when they enter the customs territory of the country, after being cleared from bonded warehouses and free zones. For duty estimation purposes, the latter would be definitely preferred. However, due to serious gaps in data on clearances from free zones, it was necessary to count imports at the time of entry into the geographic area of the country. Exempt imports were defined for purposes of this table as all goods entered under standard exemption provisions, but not those given temporary exemption by virtue of being in a zone or warehouse, except for a presumed proportion (15%) that were assumed to be ultimately cleared into the customs area on an exempt basis. Non-zero-rated imports were defined as all "imports" that had HS codes with positive duty rates, and zero-rated imports were the residual.

[8] Table 1 of the related paper Roshan Bajracharya and Frank Flatters *Ghana's Trade Policies: Exemptions from Import Duty* provides a list of exempt imports including those entered under temporary exemption to bonded warehouses and free zones. For import duty collection purposes these latter goods are only temporarily exempt, and are ultimately dutiable when they enter the domestic market. For that reason we would include as "exempt" imports for purposes of the current table only those goods which are cleared from warehouses and zones on an exempt basis. Unfortunately, as explained in the other paper (and in the previous footnote), data were available on only a small portion of goods cleared from zones and warehouses into the domestic market. In the absence of the necessary information, we have simply assumed that 15 percent of goods entered into warehouses and free zones are ultimately cleared into the domestic market on an exempt basis.

which remain at a zero rate and on the elasticity of imports with respect to increases in the tariff.[9]

Barring a large response of (reported) imports to a lowering of the rate, changing the top duty rate from 25 to 20 percent will reduce tariff revenues. Last year's IMF/World Bank study estimated that this would have a negative impact in the order of 5 to 7 percent of total import duty revenues. According to estimates based on the 1998 trade data made available for this study, approximately 1.31 trillion cedis of 1998 imports were in HS categories with a statutory rate of 25 percent. However, as a result of the granting of concessionary rates, a sizeable portion of these goods were taxed at only 10 percent. The data did not permit a direct calculation of this proportion. However, the overall effective import tariff rate on imports of goods with a 25 percent statutory rate was estimated to be 19.04 percent. This suggests that about 60 percent of these goods were taxed at 25 percent and the remainder at 10 percent.[10]

Based on these calculations and assumptions, we estimate that 788.4 billion cedis of imports in 1998 were subject to and paid import duties at a rate of 25 percent. If this rate were lowered to 20 percent, and there imports were unchanged, revenues would fall by 5 percent of 788.4 billion cedis, or 39.4 billion cedis.

In addition to this reduction in the top duty rate, we would also recommend a thorough review of items in the top rate category in order to eliminate or at least seriously reduce the use of the concessionary rate system for manufacturers. This would be accomplished by moving all items which have a major use as an industrial raw material by Ghanaian producers (e.g. heavy duty kraft paper, starch, tire cord and other textiles) from the 25/20 percent category to a rate of 10 percent. While this might have a negative impact on revenues, it is likely to be small. More importantly, it would represent a major improvement and increase in certainty and transparency in the incentive regime.

Customs Administration

Ghana's customs administration procedures leave considerable room for improvement.[11] System administration problems are a source of considerable revenue loss and result in much higher than necessary costs of trade. Recent emergency measures to deal with what are perceived to be some

[9] The recent experience of increasing some zero rates to 5 percent provides a sobering view of likely elasticities. One of the major revenue-generating items was expected to be fish. Following imposition of the 5 percent duty, imported fish almost disappeared, with the result that almost no revenue was generated. The suspicion is that many of the fish that "disappeared" became "domestic" fish — i.e. caught by Ghanaian boats and/or in Ghanaian waters. Rules of origin for fresh and frozen fish are apparently very difficult to enforce.

[10] This is based on the fact that 0.6 (0.25) + 0.4 (0.10) = 0.19, the estimated effective tax rate for these imports.

[11] See Vincent Castonguay, *Review of CEPS Activities with Respect to Controls, Processing Procedures and Trade Facilitation Regimes* (Sigma One Corporation), September 1999 for detailed analysis of customs systems and procedures.

of the most serious problems have increased the costs of trade for honest and dishonest business persons alike, and are unlikely to have a significant impact on revenue collections.

Clearance of goods at Tema routinely takes 4 to 7 days, and even more for "special cases," such as imports under exemptions or into bonded warehouses. This compares with average clearing times of one day in some neighboring countries, and 15 minutes in Singapore. Significant improvements are possible, and they would have a large and beneficial impact on the high costs of doing business in Ghana.

To compound the current problems, Ghana's customs administration is facing two potentially enormous problems — termination of the PSI system and introduction of GATT valuation code, both scheduled to take effect on January 1, 2000.

These problems pose an emergency that could dwarf all other tariff revenue issues, and have a serious impact on VAT collections as well. However, this potential crisis can be turned into an opportunity to initiate serious reforms in customs administration which will greatly improve trade facilitation and revenue collections together. An outline of such a plan is provided elsewhere.[12]

The revenue implications of such reforms are, by their nature, almost impossible to estimate. That does not diminish their importance, especially in light of the fact that customs administration impinges on VAT and excise taxes as well as import tariffs. Experience in other countries has shown that customs administration reform can give an almost immediate boost, easily in the order of 20 percent, to customs related tax collections. Given the reported leakages in the systems for temporary exemptions for bonded warehouses, free zones and transhipment, the revenue gains for Ghana could be much higher. At the same time, total costs of importing can be expected to fall, almost immediately, by 20 percent as well. This will provide a big boost to all forms of economic activity in the country, but especially to non-traditional exports.

[12] See Vincent Castonguay, *ibid.*