AFRICAN TAX ADMINISTRATION FORUM

FORUM SUR L'ADMINISTRATION FISCALE AFRICAINE

Tax Incentives from Corporate Income Taxes in Africa

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Introduction

- Tax incentives are used globally and they have been used for decades
- Tax incentives are however particularly popular in Africa as a means of attracting Foreign Direct Investment.
- A 2017 study revealed that virtually every country in Africa had some form of tax incentives geared towards attracting FDI (KPMG 2017).
- A 2022 International Monetary Fund (IMF) paper described tax systems across Africa as ‘riddled with exemptions and incentives’. (Aslam, Delepierre, Gupta and Rawlings 2022: 2)

Nature of CIT related Tax Incentives

- CIT related Tax incentives in Africa typically take the form of tax holidays- a temporary exemption of a firm or investment from CIT
- A 2013 study of tax incentives in 30 SSA countries found that 60% of them are in the form of a tax holiday (James 2013: 11).
- Tax holidays usually have different thresholds for foreigners and locals and vary in duration from as little as one year to as long as 20 years
- Tax holidays are often preferred because they have the advantage of simplicity for both the investor and the tax authorities

Nature of CIT related Tax Incentives …..

- Tax holidays may be discretionary or non-discretionary.
  - Discretionary tax holidays typically involve an application seeking approval from a government official such as the Minister of Finance.
  - Non Discretionary tax holidays are laid out in the tax laws. However, they may be so broadly drafted as to require an approval process even when this is not explicitly provided for in the laws.
- The 2013 study of tax incentives in SSA found that 47% of them were discretionary (James 2013: 40).
- Very often the process of applying for and approving discretionary tax holidays is hidden from the public and this lack of transparency makes them prone to abuse.

Nature of CIT related Tax Incentives …..

- Discretionary tax holidays are common among African countries.
  - In Tanzania, the Minister of Finance may, by order published in the Gazette, exempt any income from tax to the extent specified in the order or vary any statutory exemption in the Income Tax Act (Section 10 of the Income Tax Act (Tanzania).
  - Tanzania also has tax holidays based on agreements approved by Cabinet on strategic projects or for a special strategic investment approved by the National Investment Steering Committee.
  - In Uganda, Tax incentives were historically controlled by the Executive. The Income Tax Decree of 1974 empowered the Minister of Finance to declare any class of income to be exempt. Ministerial discretion in granting tax exemptions continued into the early 1990s
  - This exemptions regime was criticised and thus abolished in 1997. However, along the way discretionary incentives re-emerged often taking the form of government paying taxes on behalf of the investors.

Nature of CIT related Tax Incentives …..

- Straight forward Non Discretionary tax incentives that does not require approval exit in some African countries. For instance,
  - In Malawi, Firms operating in the agro-processing sector and electricity generation, transmission, and distribution sector which meet requisite capital investment thresholds have a ten-year tax holiday (Eleventh Schedule of the Taxation Act Cap 41:01 (Malawi) and Taxation (Priority Industries) Regulations 2013 (Malawi).
  - In Sierra Leone, any business established after 1 January 2015 which makes the requisite capital investment and the minimum threshold of the number of employees is exempted (Section 24 of the Finance Act, 2015 (Sierra Leone).

Effectiveness of CIT related Tax Incentives

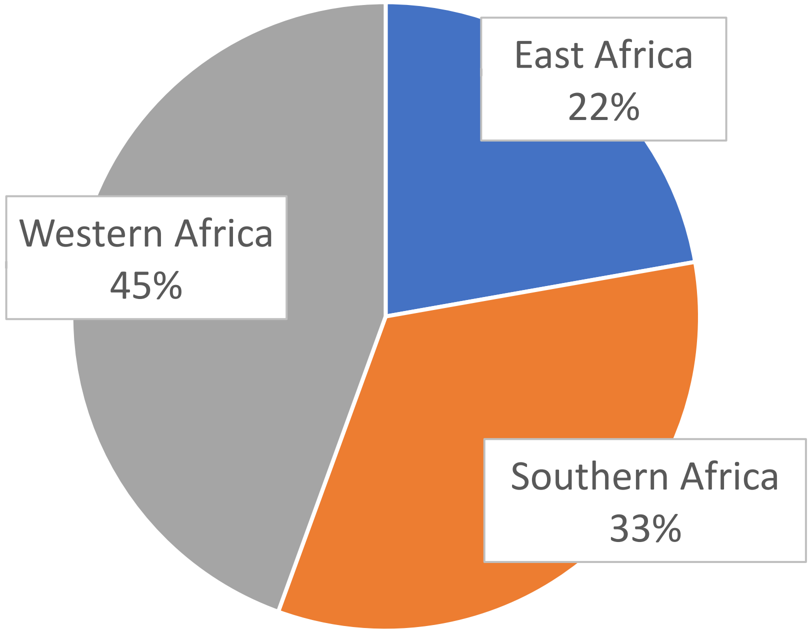
- A few studies have suggested that tax incentives can be effective in attracting FDI but only in countries with a better overall investment climate such as good infrastructure, reasonable transport costs, and a policy framework favouring investment (Jun 2017).
  - Tax incentives have reportedly been effective in countries like South Korea, Singapore, Malaysia, Ireland, Costa Rica, and Mauritius (Bolnik 2004; James 2013; World Bank 2009).
  - A 2013 study found that the boost in FDI from lowering effective tax rates is eight times stronger in countries with good investment climates (James 2013).
  - An examination of 25 empirical studies on the impact of CIT rates on the allocation of FDI, found that on average a 1% increase in a country's tax rate reduces FDI in that country by 3.3%.(de Mooij and Ederveen 2003),

Effectiveness of CIT related Tax Incentives

- In Africa, tax incentives are reported to be ineffective in attracting FDI
  - A 2010 study of 12 CFA Franc Zone countries over the period 1994–2006 found no robust positive relationship between tax holidays and investment (Parys and James 2010).
  - Another study examining the impact of CIT rates on FDI inflows to the gold and silver sectors of 16 African countries found ‘no statistically significant impact of mining CIT rates on the host country’s gold and silver FDI inflows’ (Seydou and Abdramane 2021).
- Therefore, Success in using tax incentives to spur rapid development appears to be the exception rather than the rule.

Preliminary Results from an ongoing ATAF study on Macro Fiscal Impact of tax expenditures in 33 African countries

Preliminary Results

Responses by region - survey	Total responses - survey
	• Total responses: **18** • Total expected: **33** • Response rate: **54.5%** • Countries that estimate/measure Tax Expenditures: **100% (of respondents)**

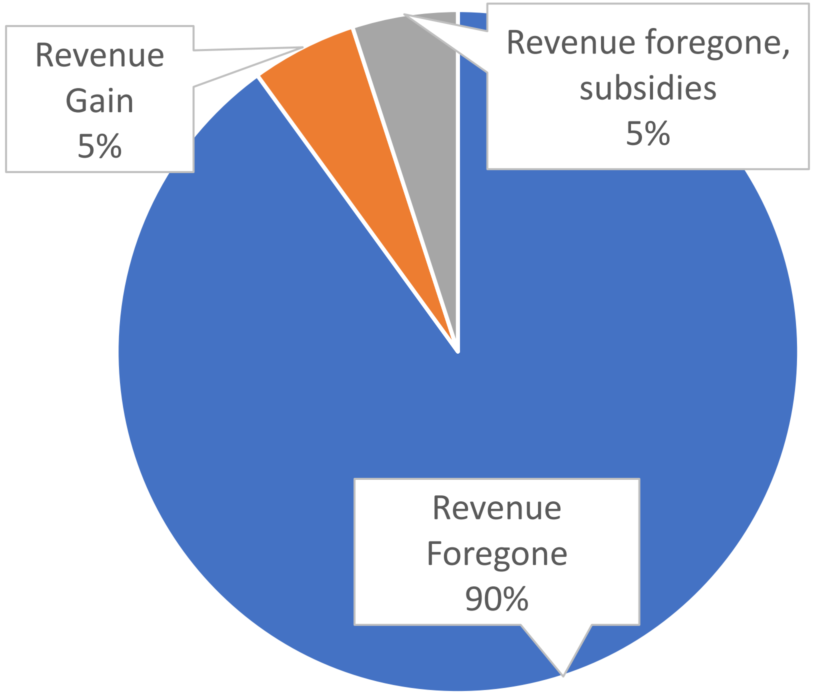
Preliminary Results

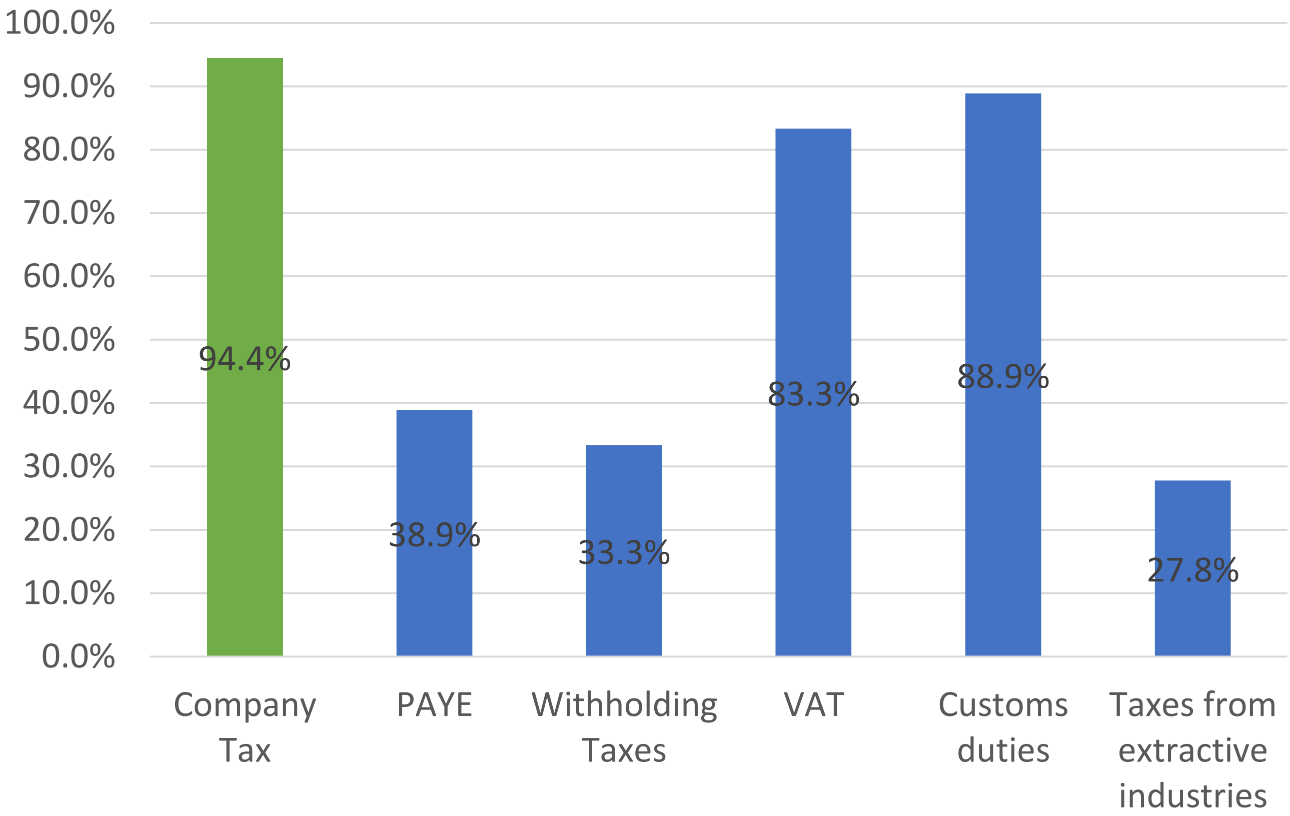
Survey respondents	Panel data respondents
Benin	Benin
Botswana	Botswana
Côte d'Ivoire	Burkina Faso
Eswatini	Cote d'Ivoire
Gambia	Eswatini
Kenya	Ghana
Madagascar	Kenya
Mauritania	Madagascar
Mauritius	Mauritius
Nigeria	Nigeria
Rwanda	Niger
Senegal	Rwanda
Sierra Leone	Seychelles
South Africa	Sierra Leone
South Sudan	South Africa
Uganda	Togo
Zambia	Zambia
18	**16***

Panel data (trend): 10
2020 TE data: 11

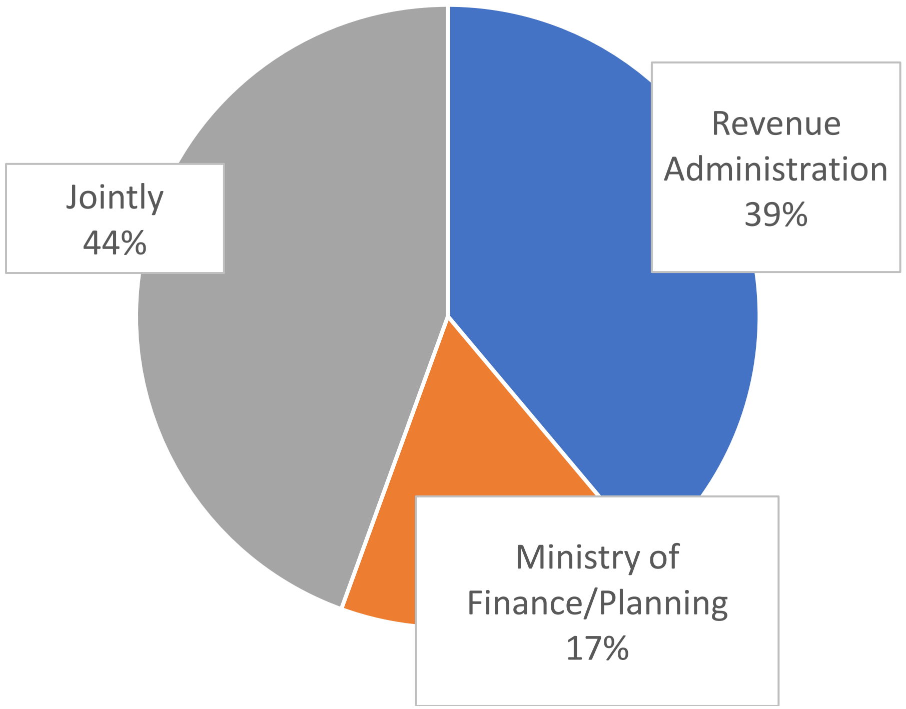
TE ESTIMATION METHOD AND TAX TYPES

Estimation method	Tax types for which TE Estimations are made

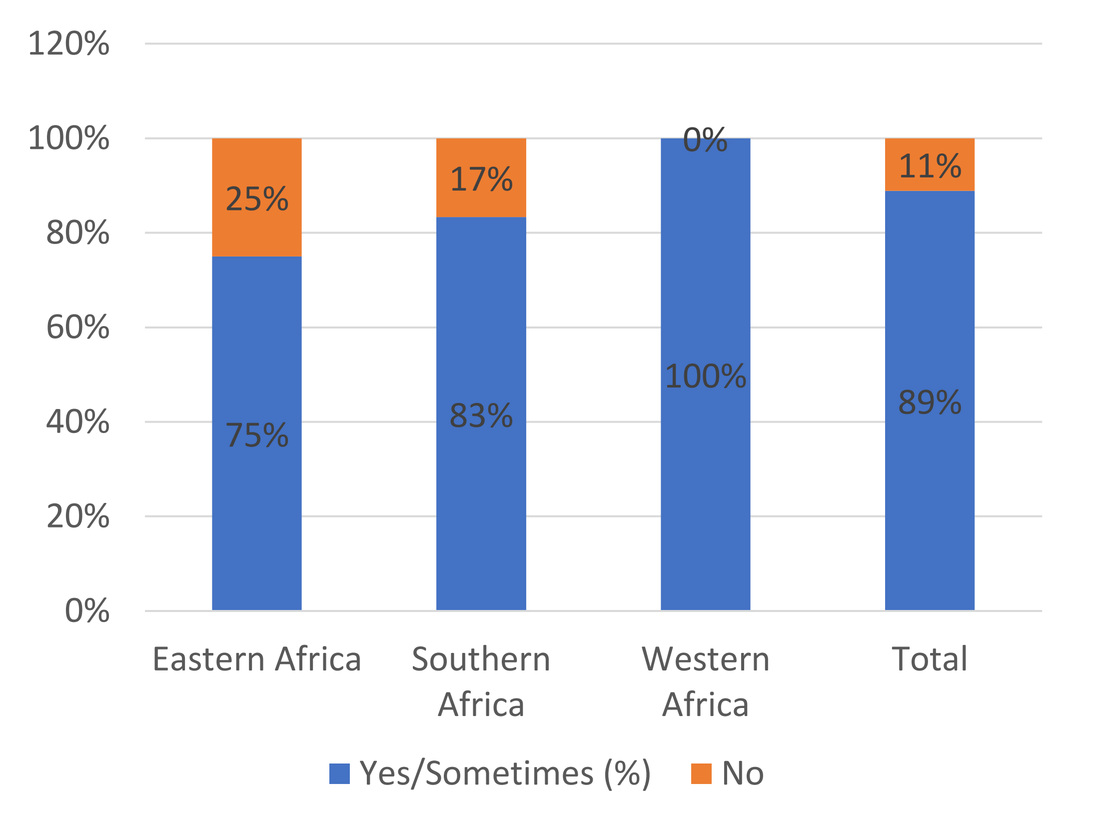
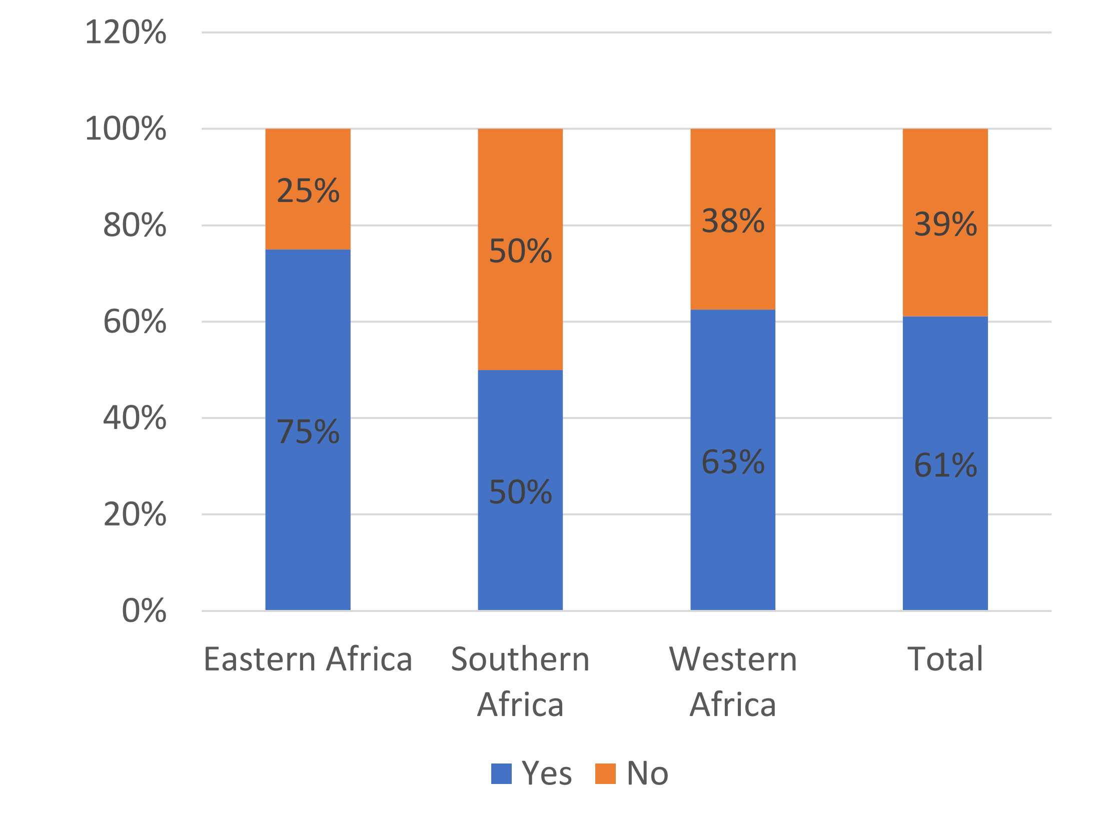




ESTIMATING AUTHORITIES

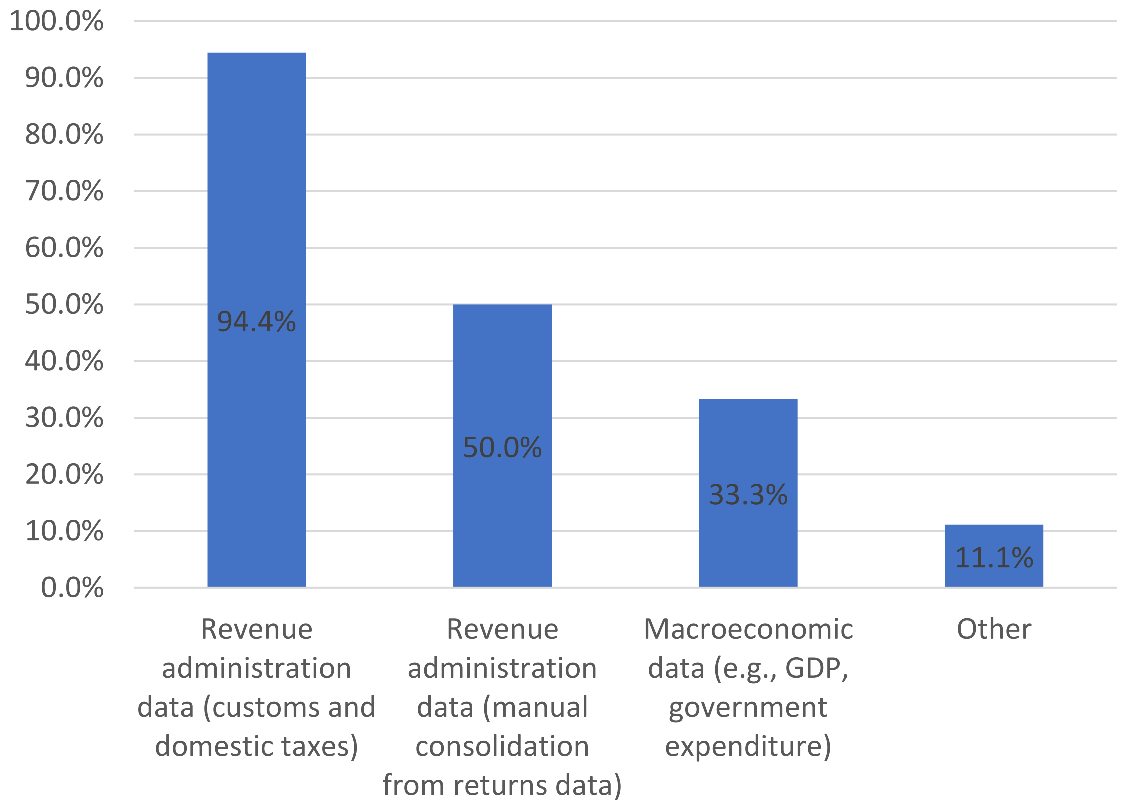
Estimating Authority	Frequency of estimations
	Frequency of estimation: **Annually: 94.4%** **Semi-annually: 5.6%**

TAX EXPENDITURES IN BUDGET

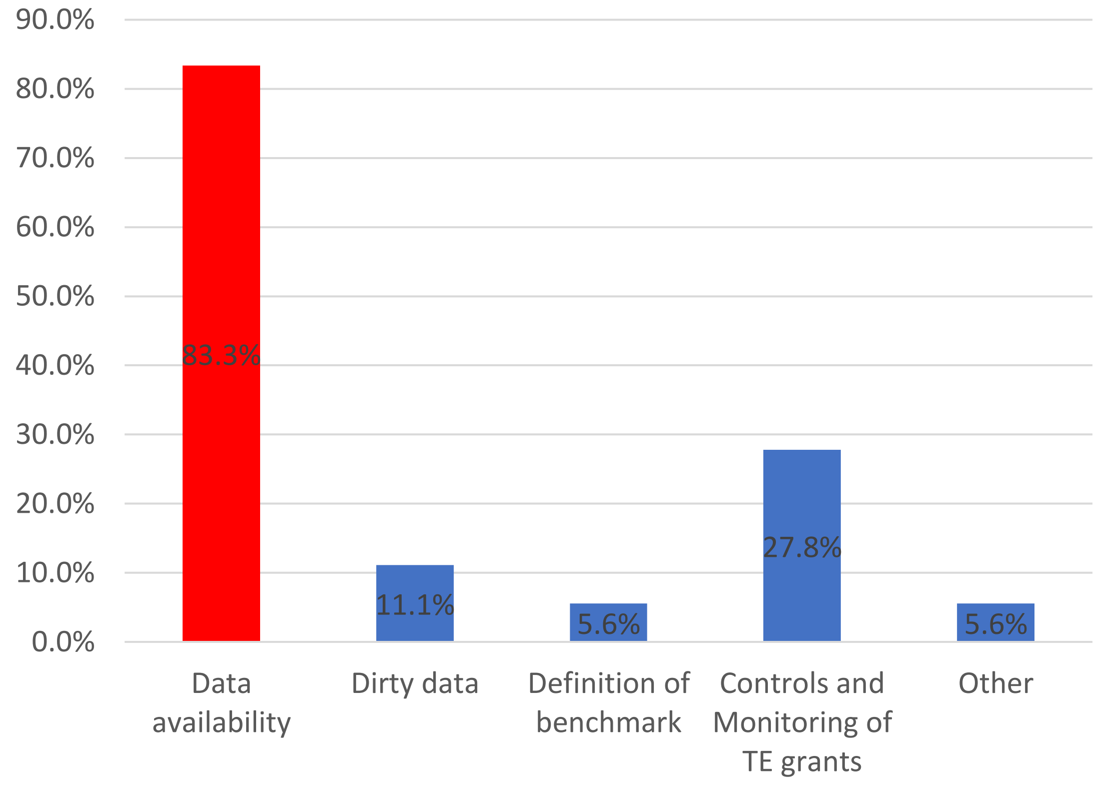
Consistency in measurement intervals	Publishing of TE in Budget
	

DATA SOURCES AND CHALLENGES

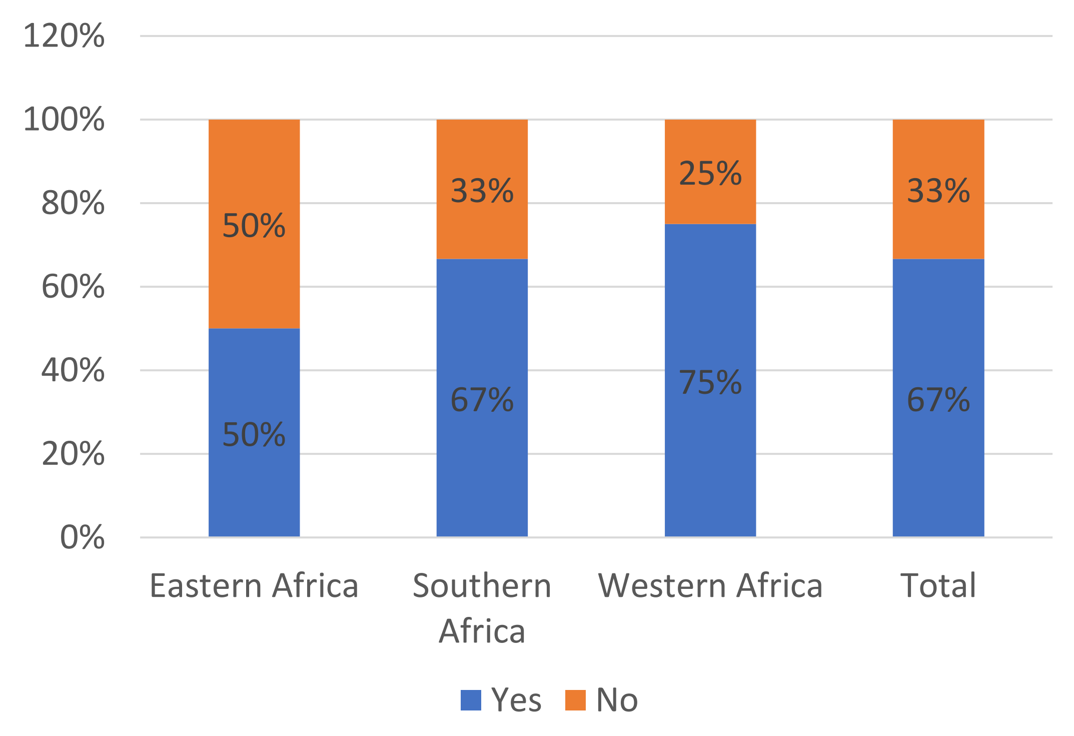
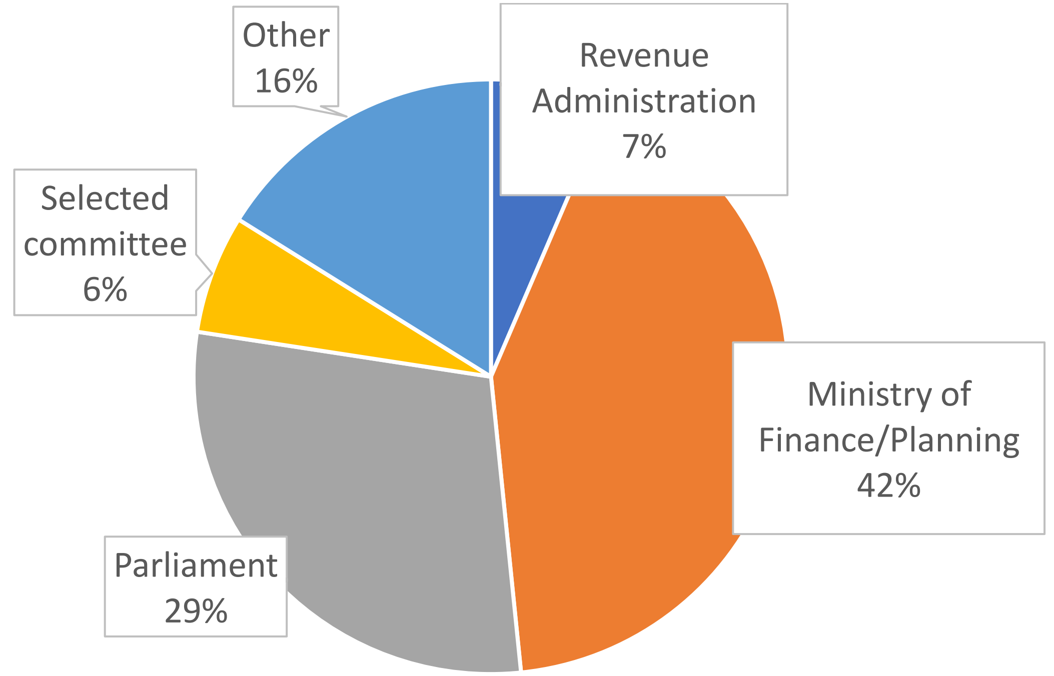
Data sources



Challenges

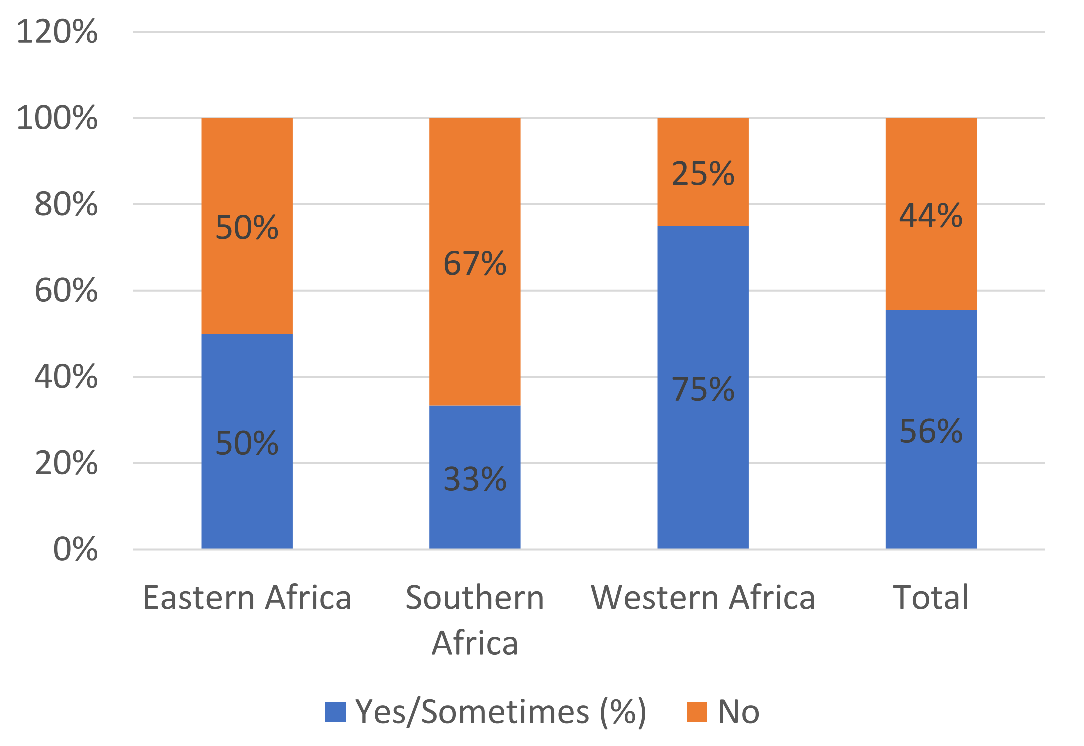


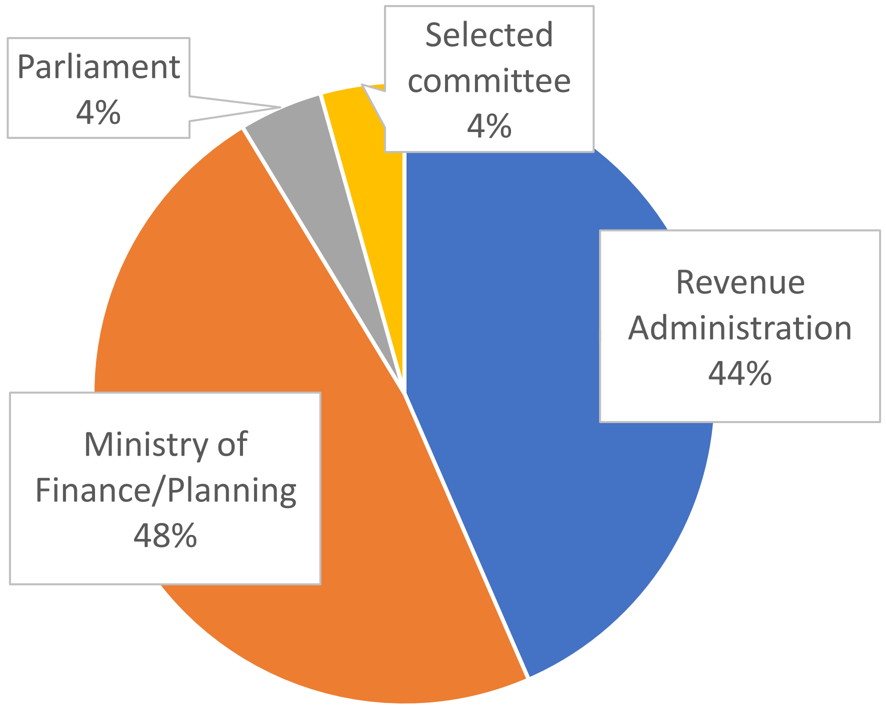
GRANTING OF TE BY LAW AND APPROVAL AUTHORITY

TE granted by law	By Approval authority
	

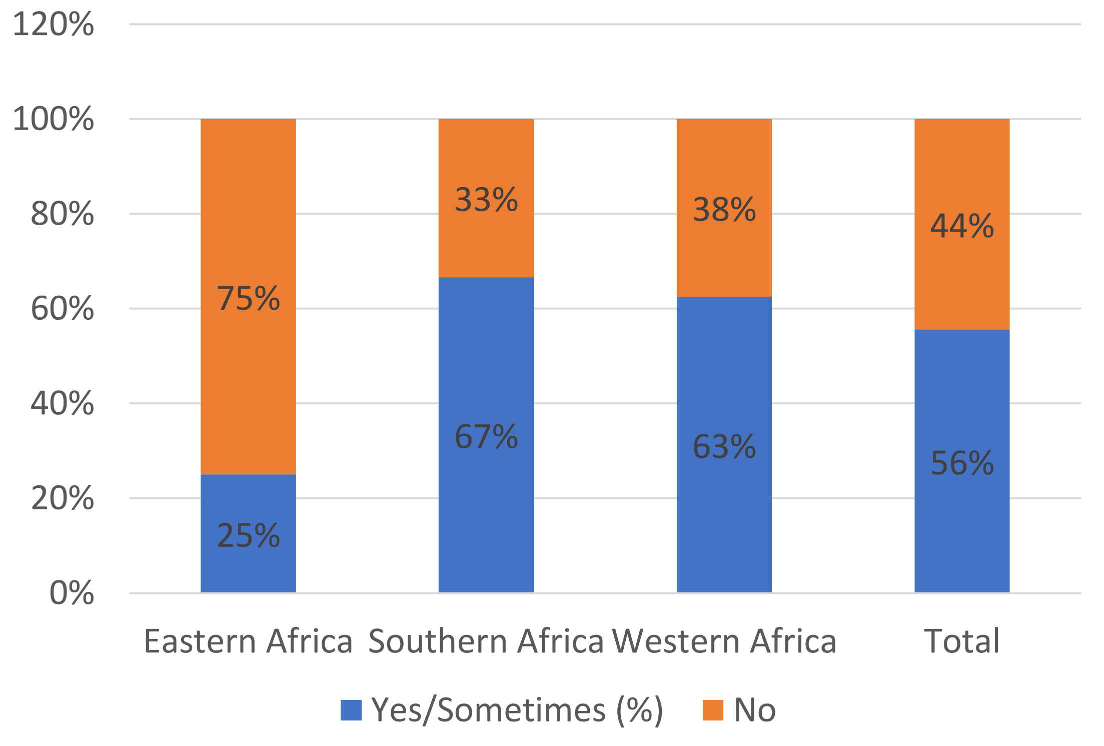
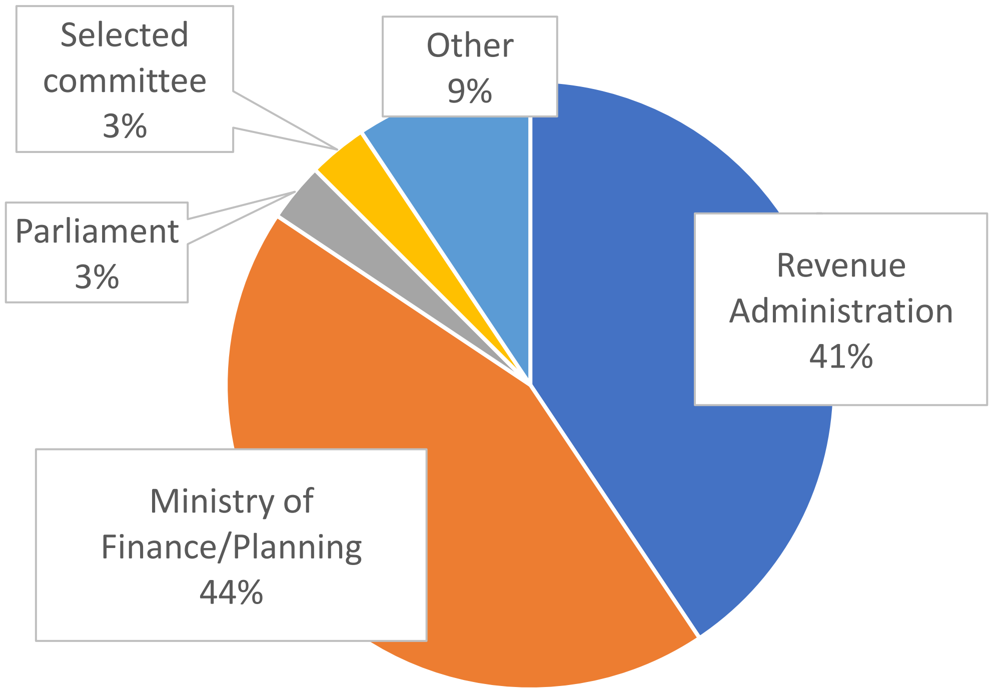
COST BENEFIT ANALYSIS DONE?

Cost-benefit analysis-Yes/No	Which authority perform C-B analysis

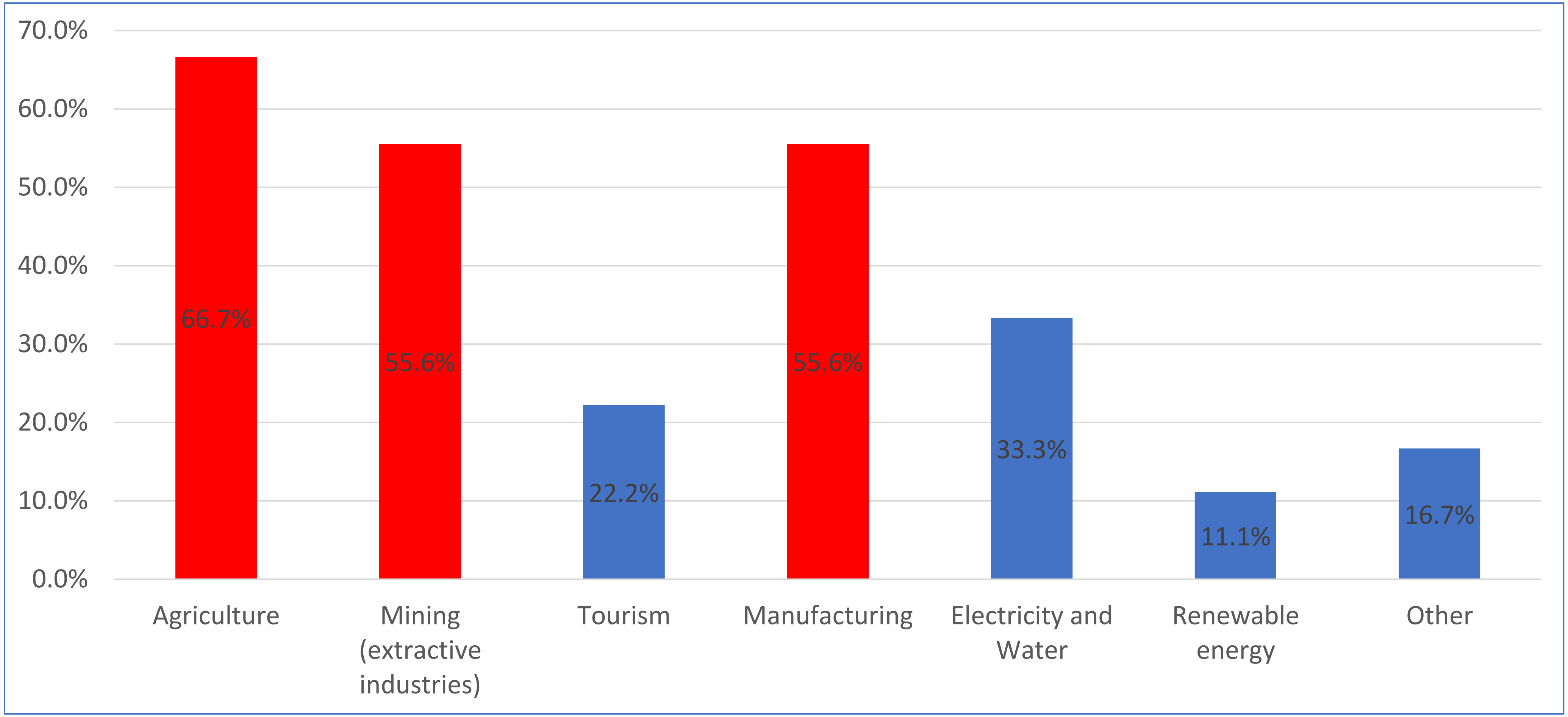




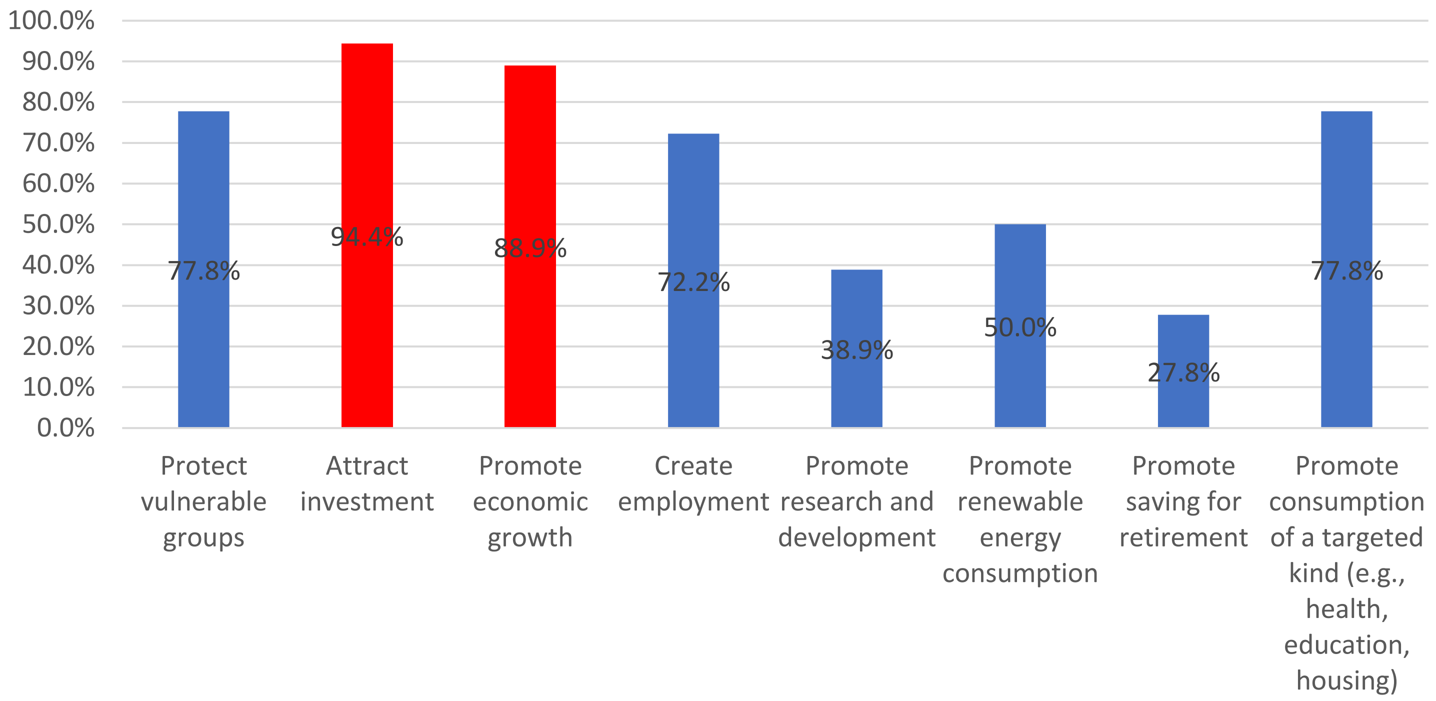
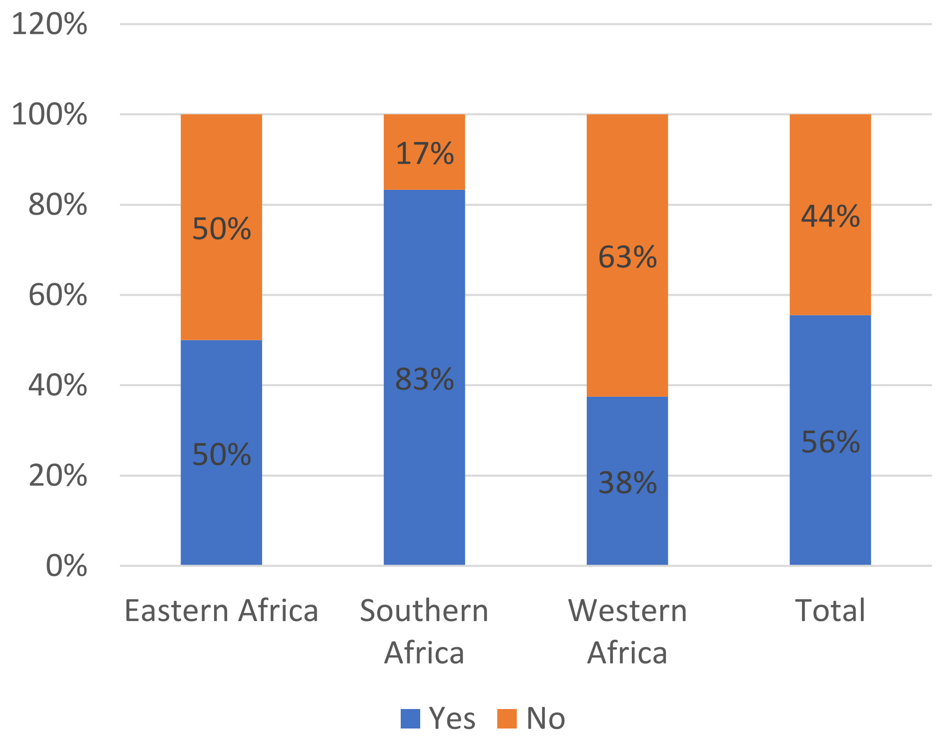
MONITORING OF TEs

TE monitoring - Yes/No	Which authority monitors
	

Sector specific TEs: Main beneficiaries



Sector specific TEs and reasons

Reasons for existence of TEs	Are TEs effective?
	

Preliminary Recomendations

05

Lastly, there should be vigilant monitoring by Parliament, civil society and the press

04

Lowering the statutory tax rate is the least distortionary form of investment incentive. A low standard rate applies uniformly to all profitable business activities without biasing the allocation of capital, the choice of production technology, or the form of financing

03

Tax holidays should be established through an appropriate, evidence-based tax expenditure governance framework to improve transparency.

02

If it is accepted that tax incentives must exist, they ought to be statutory non-discretionary tax incentives. All tax holidays should be granted transparently, through legislation.

01

The ideal approach is to eliminate tax holidays and focus on non-tax incentives for investors such as improved infrastructure


Thank you!