

The copyright of this thesis vests in the author. No quotation from it or information derived from it is to be published without full acknowledgement of the source. The thesis is to be used for private study or non-commercial research purposes only.

Published by the University of Cape Town (UCT) in terms of the non-exclusive license granted to UCT by the author.

**WHETHER TAX INCENTIVES
TO STIMULATE FOREIGN
DIRECT INVESTMENT FOR
MANUFACTURING IN THE
SADC REGION IS AN
INDICATOR OF HARMFUL
TAX COMPETITION**

SUBMITTED TO THE UNIVERSITY OF CAPE TOWN IN PARTIAL
FULFILMENT OF THE REQUIREMENTS FOR THE DEGREE

MASTER OF COMMERCE (TAXATION)

ADRIAAN JACOBUS VAN WIJK

STUDENT NUMBER: VWJADR002

SUBMITTED: FEBRUARY 2012

ACKNOWLEDGEMENTS

I dedicate this research study to my late father, Professor Attie van Wijk, and my mother, Corneel van Wijk, who taught me that the ability to read and write is the greatest gift I will ever receive. I am sincerely grateful for your strong words of encouragement, loyal support and steadfast guidance throughout my life.

My sincere gratitude is extended towards my supervisor, Professor Craig West, for his insightful comments and helpful technical suggestions. This research study benefited to a great extent from Professor West's expert guidance, and I thank him sincerely.

I am also grateful towards my employer, Swiss Re Life and Health Africa Ltd, for the study bursary enabling me to undertake this course.

Finally, I thank my Lord and Saviour, who blessed me with the invaluable ability to read and write. His boundless grace and unfathomable love for me is my source of strength and inspiration.

Adriaan van Wijk

Cape Town

February 2012

ABSTRACT

In 2002 the Southern African Development Community (SADC) issued the Memorandum of Understanding on Co-Operation in Taxation and Related Matters (MoU) to its fifteen member states. In terms of the MoU the member states agreed on steps to be taken to co-operate in taxation matters and to harmonise the tax regimes of the member states.

Many governments in the SADC region face pressure to amend their tax incentives in order to compete with tax relief offered elsewhere. At the same time member states have the responsibility to strengthen revenues in order to finance essential public goods and services. The challenge for member states is to develop and implement tax incentives in, amongst others, the manufacturing industry that will stimulate economic growth and contribute to the harmonisation of tax incentives in the SADC region without engaging in tax competition or acting prejudicially towards fellow member states.

The purpose of this study is to test whether or not the lowering of the corporate tax rates and/or the exemption from corporate taxes for manufacturing companies in the SADC region are indicative of member states endeavouring to achieve a common approach to the treatment and application of tax incentives and simultaneously avoid harmful tax competition.

The main research question was to determine whether a preferential corporate tax rate together with tax incentives specific to manufacturing companies could lead to a zero or low effective rate of tax and/or are restricted to particular taxpayers (usually non-residents) as required by the MoU.

The main conclusion of this research study indicated that three of the fifteen member states of the SADC, namely Lesotho, Malawi and Namibia, potentially engage in harmful tax competition in relation to its manufacturing industries as may be evidenced by a zero or low effective rate of tax only.

ABBREVIATIONS

Abbreviation	Meaning
AGOA	Africa Growth and Opportunity Act
DRC	Democratic Republic of Congo
EPZ	Export Processing Zone
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
MoU	Memorandum of Understanding on Co-Operation in Taxation and Related Matters issued by the SADC in 2002.
N\$	Namibian Dollar
OECD	Organisation for Economic Co-Operation and Development
OECD Report	The report published by the OECD in 1998, titled "Harmful Tax Competition: An Emerging Global Issue".
SADC	Southern African Development Community
SACU	Southern Africa Customs Union
UNCTAD	United Nations Centre for Trade and Development
USD	United States Dollar

TABLE OF CONTENTS

ACKNOWLEDGEMENTS	II
ABSTRACT.....	III
ABBREVIATIONS.....	IV
CHAPTER 1 INTRODUCTION.....	1
1.1 BACKGROUND.....	1
1.2 RATIONALE	2
1.3 RESEARCH QUESTION AND OBJECTIVES.....	4
1.4 RESEARCH METHODOLOGY	5
1.5 LIMITATIONS OF THE RESEARCH STUDY	6
1.6 CHAPTER LAYOUT	7
CHAPTER 2 FOREIGN DIRECT INVESTMENT.....	9
2.1 INTRODUCTION.....	9
2.2 THE DEFINITION, IMPORTANCE AND TRENDS OF FDI IN THE SADC REGION	9
2.2.1 Definition of FDI.....	9
2.2.2 Importance of FDI in the SADC region	10
2.2.3 Trends in FDI in the SADC region	10
2.3 FACTORS THAT INFLUENCE FDI.....	13
2.3.1 Policy and regulatory regimes.....	13
2.3.2 Macroeconomic stability	14
2.3.3 Market size and economic growth rates	14
2.3.4 Infrastructure	15
2.3.5 Skilled workforce	16
2.3.6 Corporate governance.....	17
2.3.7 Privatisation programmes.....	17
2.3.8 Taxation.....	18
2.4 TAX INCENTIVES	18
2.4.1 Definition of a tax incentive.....	18
2.4.2 Tax incentives that reduce the corporate income tax rate on profits derived from investment	19
2.4.2.1 Corporate income tax rate	19
2.4.2.2 Tax holidays	21
2.4.2.3 Carry forward of fiscal losses.....	22
2.4.3 Tax incentives that reduce the after-tax cost to business of purchasing new capital	23
2.4.3.1 Investment allowances	23
2.4.3.2 Investment tax credits.....	24
2.4.4 Tax incentives that reduce the after-tax cost of raising funds to finance the purchase of new capital.....	25
2.4.4.1 Exemption from or lowering of withholding taxes on passive income	25
2.5 CONCLUSION	26
CHAPTER 3 HARMFUL TAX COMPETITION	28
3.1 INTRODUCTION.....	28

3.2	DEFINITION OF TAX COMPETITION	29
3.3	THE OECD REPORT AND ITS PROGENY	30
3.4	THE SADC AND HARMFUL TAX COMPETITION	32
3.4.1	Zero or low effective rates of tax	33
3.4.2	Lack of transparency	34
3.4.3	Lack of effective exchange of information	35
3.4.4	Restricting tax incentives to particular taxpayers.....	36
3.4.5	Promotion of tax incentives as vehicles for tax minimization	37
3.4.6	Absence of substantial activity.....	37
3.5	ARTICLE 4(3)(b) OF THE MOU.....	38
3.6	BENEFITS OF TAX COMPETITION	38
3.7	PRACTICAL EXAMPLES OF TAX COMPETITION IN THE SADC.....	39
3.8	CONCLUSION	41
CHAPTER 4 TAX INCENTIVES FOR MANUFACTURING COMPANIES IN THE SADC REGION.....		43
4.1	INTRODUCTION.....	43
4.2	CORPORATE TAX RATES OF MANUFACTURING COMPANIES	43
4.3	TAX INCENTIVES OFFERED BY LESOTHO.....	46
4.3.1	Withholding tax rate on investment income.....	46
4.3.2	Preferential income tax rate.....	47
4.4	TAX INCENTIVES OFFERED BY NAMIBIA	47
4.4.1	Building cost allowance	48
4.4.2	Employee remuneration and training cost allowance.....	48
4.4.3	Export expenditure allowance	49
4.4.4	Export allowance	49
4.4.5	Transport allowance	50
4.4.6	Preferential income tax rate.....	50
4.5	TAX INCENTIVES OFFERED BY MALAWI.....	51
4.5.1	Building and machinery cost allowance.....	52
4.5.2	Pre-operating expenditure	53
4.5.3	Carry forward of losses	53
4.5.4	Training cost allowance.....	53
4.5.5	Export tax allowance	53
4.5.6	Preferential income tax rate.....	54
4.6	CONCLUSION	54
CHAPTER 5 APPLICATION OF ARTICLE 4(1) AND ARTICLE 4(2) OF THE MOU.....		55
5.1	INTRODUCTION.....	55
5.2	ARTICLE 4(1) OF THE MOU	55
5.2.1	Interpretation of article 4(1)	55
5.2.1.1	Common approach to the treatment and application of tax incentives	56
5.2.1.2	Tax incentives must be provided for only in tax legislation	56
5.2.2	Application of article 4(1)	57
5.2.2.1	Common approach to the treatment and application of tax incentives	57
5.2.2.2	Tax incentives must be provided for only in tax legislation	58
5.3	ARTICLE 4(3) OF THE MOU	59

5.3.1	Zero or low effective rates of tax	60
5.3.2	Restricting tax incentives to particular taxpayers.....	62
5.3.3	Other evidentiary factors	63
5.4	CONCLUSION	63
CHAPTER 6 CONCLUSION.....		65
BIBLIOGRAPHY		68

University of Cape Town

CHAPTER 1

INTRODUCTION

1.1 BACKGROUND

In 2002 the Southern African Development Community (SADC) issued the Memorandum of Understanding on Co-Operation in Taxation and Related Matters (MoU) to its fifteen member states. In terms of the MoU the member states agreed on steps to be taken to co-operate in taxation matters and to harmonise the tax regimes of the member states. Article 1 of the MoU defines a "tax incentive" as "a fiscal measure that is used to attract local or foreign investment capital to certain economic activities or particular areas in a country." Article 4(1) of the MoU stipulates that "[m]ember states will endeavour to achieve a common approach to the treatment and application of tax incentives and will, amongst other things, ensure that tax incentives are provided for only in tax legislation." Article 4(2) of the MoU provides a list of seven examples of tax incentives. Article 4(3) of the MoU states that "[m]ember states will, in the treatment and application of tax incentives, endeavour to avoid harmful tax competition as may be evidenced by [six factors]." These are: zero or low effective rates of tax; lack of transparency; lack of effective exchange of information; restricting tax incentives to particular taxpayers (usually non-residents); promotion of tax incentives as vehicles for tax minimisation; or, the absence of substantial activity in the jurisdiction to qualify for a tax incentive.

The sole objective of a tax system is to collect sufficient revenue necessary for delivering government policies and priorities in an efficient and equitable manner (Lesotho, 2009:4). In reaching that objective, governments also set out to achieve other sub-objectives, including the enablement of economic growth and development. Governments do realise that the tax rates should not distort incentives for investment in a country as it could potentially hamper economic growth and development. Consequently the tax system seeks to cause as little disruption as possible to potential business activity and the economic growth whilst at the same time meeting government's revenue requirements (Stretch *et al*, 2001:1; Bolnick, 2004:1-2).

Tax incentives sometimes "come in conflict with the principles of good taxation. The tax incentives should therefore be kept to the minimum as it over-complicates the tax system, making it more expensive to monitor the beneficiaries of such incentives and therefore increase the possibilities for tax evasion" (Lesotho, 2009:8).

It is assumed that tax incentives, such as those offered to the manufacturing industry, are introduced by governments to stimulate foreign direct investment (FDI) in a country (Biggs, 2007). Many governments in the SADC region face pressure to amend their tax incentives in order to compete with tax relief offered elsewhere (Bolnick, 2004:7). At the same time member states have the responsibility "to strengthen revenues in order to finance essential public goods and services" (Bolnick, 2004:7). The challenge for member states is to develop and implement tax incentives in the manufacturing industry that will stimulate economic growth and contribute to the harmonisation of tax incentives in the SADC region without engaging in tax competition or acting prejudicially towards fellow member states.

1.2 RATIONALE

The mission statement of the SADC is to promote sustainable and equitable economic growth and socio-economic development through efficient productive systems, deeper co-operation and integration, good governance, and durable peace and security, so that the region emerges as a competitive and effective player in international relations and the world economy. For decades member states of the SADC are continuously in a battle to find a balance between tax incentives that stimulate FDI and attract sufficient revenue in an effective manner that will attend to the member states' needs (Bolnick, 2004:1-1; Argent, 2008:1).

An overview of theoretical studies indicated that extensive research has been done on the factors that influence investors' decisions to invest in a foreign country (Walsh et al, 2010; Dabla-Norris et al, 2010). One of the factors that influence FDI is taxation (Mintz, 2004; Biggs, 2007). During a review of the empirical evidence, survey evidence and case studies on the importance of the role of taxation in influencing investors' decision to invest, Bolnick (2004:2-10 to 2-13) noted different conclusions for each type of study. Bolnick noted that empirical evidence suggested that if the user

cost of capital decreased by 10 percent as a result of a tax benefit, it is expected that investment would increase by 5 percent to 10 percent. Survey evidence, on the other hand, indicated that respondents place a low weight on tax factors in the overall decision process, even though tax variables can have a significant effect on the final decisions. Lastly, case studies indicated that tax incentives lure investors in Brazil and Mauritius, whereas non-tax incentives play a more important role in other countries such as Mexico and Pakistan.

Tax incentives include: reduced corporate income tax rates, loss carry forwards, tax holidays, investment tax credits, investment allowances, special exemptions from withholding taxes and additional deductions for qualifying expenses (Argent, 2008; Bolnick, 2004; Biggs, 2007). Empirical studies have been published determining the effect of tax incentives on investment decisions (Clark, 2000; Bolnick, 2004).

Research has also been conducted on tax competition, specifically the implications of taxation of investment on tax competition (Mintz, 2000; Stretch, 2001).

The websites of the SADC, local revenue authorities and investment promotion agencies as well those of the four major global accounting firms all provide information on the tax incentives offered by the fifteen member states of the SADC. These member states are: Angola, Botswana, Democratic Republic of Congo (DRC), Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, United Republic of Tanzania, Zambia and Zimbabwe.

Little research has been found to have been conducted on whether or not the tax incentives applied by member states of the SADC since 2002 towards manufacturing companies contributed to or detracted from the mission statement of the SADC. Following a review of corporate tax rates, and where applicable the tax incentives, available to manufacturing companies in the SADC region, it was noted that preferential income tax treatment is given to these companies by some member states. By critically analysing the corporate tax rates, and where applicable the tax incentives, applied by member states since 2002 to manufacturing companies, the proposed research study will test whether or not such preferential tax incentives are indicative of

harmful tax competition between member states in respect of the manufacturing industry.

1.3 RESEARCH QUESTION AND OBJECTIVES

The purpose of this study is to test whether the lowering of the corporate tax rates and/or the exemption from corporate taxes for manufacturing companies in the SADC region aligns with the aim of member states to achieve a common approach to the treatment and application of tax incentives and simultaneously avoid harmful tax competition or whether such tax incentives are indicative of the harmful tax competition that the member states are meant to avoid.

To achieve this purpose, the methodology requires the following five research objectives to be achieved, namely:

- critically analyse the factors that influence foreign investors' decision to invest in developing countries with specific emphasis on the role of taxation;
- critically analyse the definition of "harmful tax competition" and its role in determining tax policy of developing countries;
- critically analyse the corporate tax rates applied by the fifteen member states of the SADC since 2002 until present to manufacturing companies in order to identify those SADC member states that offer a preferential corporate tax rate to manufacturing companies;
- in the event that a preferential corporate tax rate does exist, determine whether that corporate tax rate together with tax incentives specific to manufacturing companies could lead to a zero or low effective rate of tax and/or are restricted to particular taxpayers (usually non-residents) as stipulated by article 4(3) of the MoU; and
- determine whether the corporate tax rates together with the tax incentives according to the paragraph above are provided for only in tax legislation (as opposed to other legislation) as is required by article 4(1) of the MoU.

1.4 RESEARCH METHODOLOGY

In the context of the purpose of the research study it is submitted that a doctrinal research methodology will be followed by conducting expository research in respect of the law that guides the development and application of tax incentives towards manufacturing companies by member states of the SADC. Doctrinal research asks what the law is on a particular issue. It is concerned with an analysis of the legal doctrine and how it has been developed and applied. Expository research is research conducted with the aim of explaining a specific subject matter or set of ideas in an organized manner. It requires a controlling idea (or thesis) that establishes and sustains the writer's focus. By conducting expository research the writer will aim to present and explain this particular development and application of tax incentives in a systematic manner.

The most recent academic literature available on factors that influence FDI in developing countries will be reviewed and summarised. In addition, the most recent academic literature available on harmful tax competition and its role in determining tax policy of developing countries will be reviewed and summarised. This information will aid the understanding of the development of tax incentives as a factor that influences FDI in developing countries. It will furthermore aid the understanding of the application of tax incentives to engage in harmful tax competition and the function it performs in determining tax policy. The information pertaining to tax incentives of the member states of the SADC to manufacturing companies would be collected and analysed in order to determine whether the corporate tax rates, and where applicable the tax incentives, applied by the member states of the SADC since 2002 to manufacturing companies indicate that the member states endeavour to achieve a common approach to the treatment and application of tax incentives and simultaneously avoid harmful tax competition or whether the tax incentives granted to manufacturing companies are indicative of harmful tax competition.

1.5 LIMITATIONS OF THE RESEARCH STUDY

In order to limit the research study the emphasis will firstly be on the corporate tax rates as a form of tax incentive applied by the above member states to manufacturing companies. In the event that a preferential corporate tax rate exists, further research will be conducted in order to determine if there are any other tax incentives specific to manufacturing companies. There are three reasons for this. Firstly, a review of the top fifteen developing countries indicated that low or no corporate tax rates played a role in attracting FDI to those countries (Mintz, 2004:6). Secondly, the need to have a basic tax structure in place is considered at least as important as having special incentives available (Bolnick, 2004:7-2). Thirdly, for purposes of determining whether a zero or low effective rate of tax exists (as stipulated by article 4(3)), the corporate tax rate and any tax incentives specific to manufacturing companies must be taken into account.

The research study only focuses on two of the six evidentiary factors of harmful tax competition as stipulated by article 4(3) of the MoU. These are: zero or low effective rates of tax and restricting tax incentives to particular taxpayers (usually non-residents). It is assumed that the remaining four factors are similar between all the member states of the SADC.

The most recent academic literature available on factors that influences FDI in developing countries indicates that non-tax factors (in contrast to tax factors) play a dominating role in influencing investment decisions and determining the viability of projects (Bolnick, 2004:3-1). For purposes of this research study it is assumed that these non-tax factors are constant across all member states of the SADC. The focus would thus only be on tax factors as the only (assumed) contrasting factors.

The decision to limit the research study to manufacturing companies was based on three grounds. Firstly, the standard pattern of development of modern economies is one where higher proportions of output originate from the most dynamic sectors of the economy, namely manufacturing and services. According to the SADC only South Africa and Mauritius have a sizeable manufacturing sector, contributing approximately 25 percent of the gross domestic product (GDP) of the SADC region. The SADC indicated that there are signs of positive growth in the manufacturing value added by

the other member states over the last years. It is thus expected that, in order to follow the development of modern economies, member states will progressively put more emphasis on unlocking the value in its manufacturing industries. Secondly, a review of the research conducted by Bolnick (2004:6-9) indicated an instance where certain member states specifically engaged in tax competition in respect of a manufacturing company. Thirdly, it is noted that the availability of labour in Africa incentivised Asian investors to set-up manufacturing companies in Lesotho, signalling the potential of other African countries as investment centres for manufacturing companies.

1.6 CHAPTER LAYOUT

A critical analysis of the factors that influence foreign investors' decision to invest in developing countries with specific emphasis on the role of taxation is examined in Chapter 2. The chapter firstly discusses the definition and importance of FDI and its trends in the SADC region. Thereafter the different factors that influence FDI in the SADC region are examined. Emphasis in this regard would be placed on the role of tax incentives, with specific focus on the advantages and disadvantages of tax incentives in effectively attracting FDI.

Chapter 3 critically analyses the definition of "harmful tax competition" and its role in determining tax policy of developing countries. The chapter commences with a discussion of the definition of tax competition. The report titled "Harmful Tax Competition: An Emerging Global Issue" ('the OECD Report) published by the Organisation for Economic Co-operation and Development (OECD) in 1998 and its progeny are then considered. Next, the different factors as listed in article 4(3) of the MoU are discussed with reference to the OECD Report. Finally, the benefits of tax competition and two recent examples of tax competition in the SADC region are discussed.

Chapter 4 provides a summary of the corporate tax rates offered by SADC member states to manufacturing companies. From the summary, it is determined which of the SADC countries' corporate tax rate for manufacturing companies could potentially result in a zero or low effective rate of tax. Should this be the case for any of the SADC countries, Chapter 4 will then critically analyse the investment tax incentives specific to

manufacturing companies in such countries with a view to determine whether those countries engage in harmful tax competition as contemplated by the MoU.

Chapter 5 commences with an examination of the interpretation of article 4(1), followed by the application thereof to the tax incentives. Thereafter two of the six evidentiary factors of article 4(3), namely zero or low effective rate of tax and restricting tax incentives to particular taxpayers, are applied to the tax incentives for manufacturing companies of those SADC countries identified in Chapter 4 as having tax incentives that potentially result in harmful tax competition.

The sixth and final chapter provides the synopsis of the research undertaken throughout the course of the research study as a whole. The research questions and objectives that were set for the research study will be revisited and the conclusions reached in the previous chapters of the research study will be applied to those research questions and research objectives.

University of Cape Town

CHAPTER 2

FOREIGN DIRECT INVESTMENT

2.1 INTRODUCTION

Economies across the globe regard FDI as a pivotal source to stimulate growth and raise productivity levels. The capability of governments to offer a tax system that attracts FDI is viewed as an essential component of "a national strategy to secure high standards of living" (Clark, 2000:1140). At the same time, however, the tax system performs a critical withholding function, taxing the domestic source income that was earned by the non-resident investors on its investments (Clark, 2000:1140). The desire to tax such income without discouraging foreign investors raises the question on the role of tax incentives to effectively attract FDI to the host country.

The chapter discusses the definition and importance of FDI and its trends in the SADC region. Thereafter the different factors that influence FDI in the SADC region are examined. Emphasis in this regard would be placed on the role of tax incentives, with specific focus on the advantages and disadvantages of tax incentives in effectively attracting FDI.

2.2 THE DEFINITION, IMPORTANCE AND TRENDS OF FDI IN THE SADC REGION

2.2.1 Definition of FDI

FDI refers to an investment made for the purpose of either acquiring a continuous investment in an existing enterprise or setting up a new enterprise, both in a country different to that of the investor's (Muradzikwa, 2002:2). An investment made for the purposes of acquiring a continuous investment, for example a merger and acquisition, is often referred to as a "brownfield investment" (UNCTAD, 2003:11; Mwilima, 2003:31). An investment made for the purposes of setting up a new enterprise is referred to as a "greenfield investment" and includes, for instance, the start-up of new companies (UNCTAD, 2003:11; Mwilima, 2003:31).

For the purposes of measuring FDI the World Bank defines FDI as "the net inflows of investment to acquire a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy other than that of the investor. It is the sum of equity capital, reinvestment of earnings, other long-term capital and short-term capital as shown in the balance of payments." The World Bank expresses FDI in United States Dollar (USD) or as a percentage of the GDP of a country.

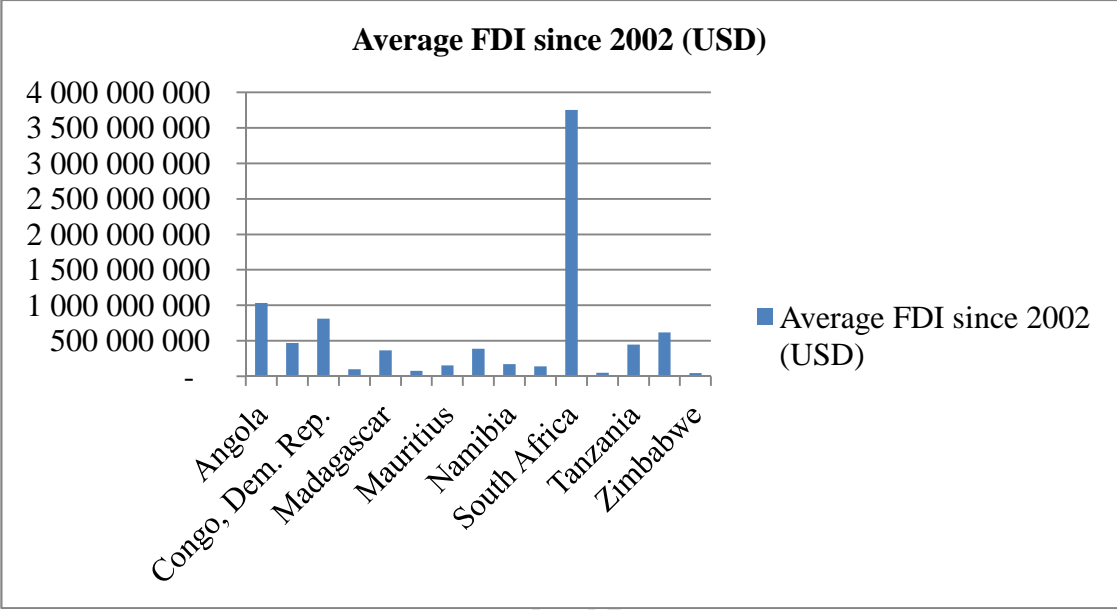
2.2.2 Importance of FDI in the SADC region

The SADC region has always been characterised by poor economic growth. The Economic Report on Africa by the United Nations Economic Commission for Africa suggested that FDI is the answer to solving Africa's economic struggles (Mwilima, 2003:32). It is thus not surprising that member states of the SADC are keenly in search of FDI to increase their economic growth and encourage their integration into the world economy (Mhlanga et al, 2009:1). Both the International Monetary Fund and the World Bank have noted that attracting large inflows of FDI would stimulate economic development in Africa (Mwilima, 2003:32).

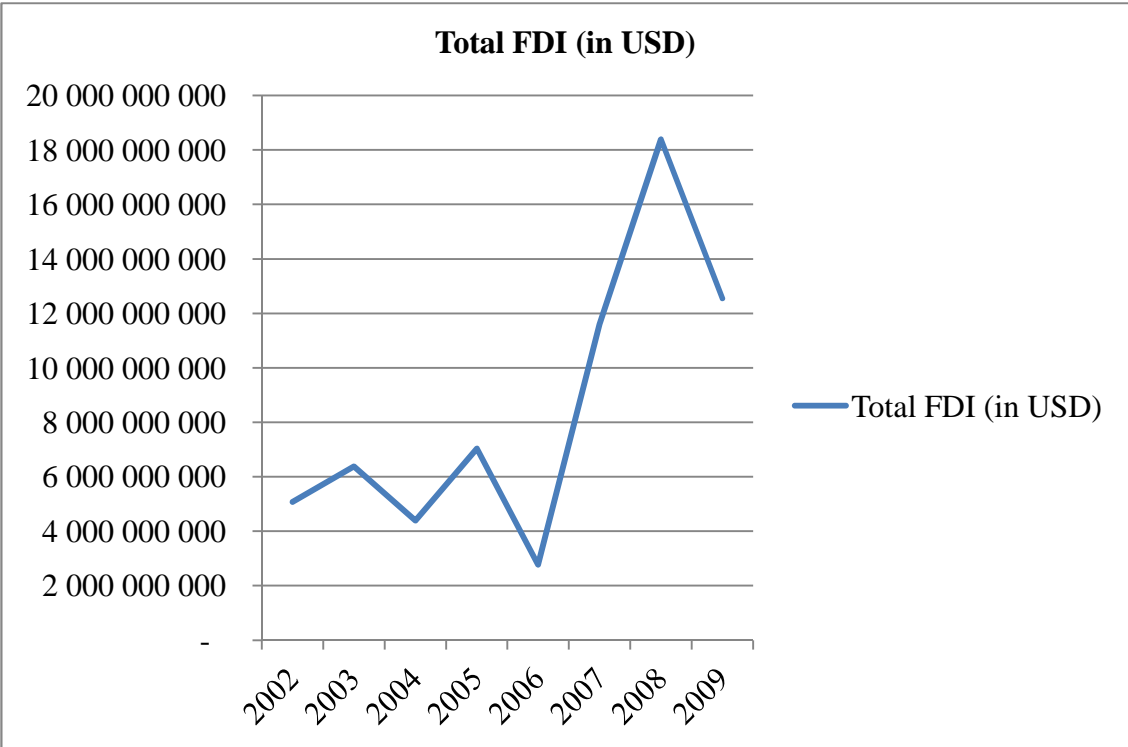
In general there are five reasons why governments of the member states of the SADC want to attract FDI (Mwilima, 2003:33; Mhlanga et al, 2009:1). Firstly, FDI is an important supply of capital formation when the capital base is low as investment inflow is a means to create a surplus in the capital account of the balance of payments (Mwilima, 2003:33). Secondly, since foreign investors, especially those from developed countries, would use technology from their home countries it is expected that there will be a transfer of technologies to the country invested in (Mwilima, 2003:33). Thirdly, FDI could create employment opportunities (Mwilima, 2003:33; Mhlanga et al, 2009:1). Fourthly, as result of FDI local employees would be equipped with new skills, such as managerial skills (Mwilima, 2003:33; Mhlanga et al, 2009:1). Finally, FDI could lead to increased competition in the export and entrepreneurship markets (Mwilima, 2003:33; Mhlanga et al, 2009:1).

2.2.3 Trends in FDI in the SADC region

From 2002 until 2009 the FDI inflows to the member states of the SADC accounted for 0.34 percent of the global FDI inflows (World Bank Data, 2011). The following figure



University of C



above.¹ South Africa remained the recipient of the largest part of the FDI in this period (World Bank Data, 2011).

The decrease in FDI since 2008 came as a result of the world economic crisis. This decrease was expected in light of the decrease of 54 percent in global FDI inflows in 2009 (UN News Centre, 2009). In addition, global cross border mergers and acquisitions decreased by 77 percent during the first quarter of that year (UN News Centre, 2009). In a press release by the UNCTAD it is noted that global FDI was expected to increase slowly in 2010 and gain momentum in 2011 (UNCTAD, 2009).

2.3 FACTORS THAT INFLUENCE FDI

Biggs (2007:6) notes that "tax exemption is like a dessert; it is good to have, but does not help very much if the meal is not there." Latest empirical work indicates that the influence of taxation on FDI locality decisions is significant and increasing (Clark, 2000:1140). FDI decisions are however also driven by factors other than taxation (Clark, 2000:1141; Biggs, 2007:6; Argent, 2008:4; Mwilima, 2003:38). These factors are discussed below.

2.3.1 Policy and regulatory regimes

Southern Africa continues to be characterised by practical issues concerning policy insecurity, or policy contradictions that have a propensity to affect the observations, integrity and the rate of fixed investment growth in the region (Muradzikwa, 2002:17). As a starting point the social and political stability of a country is one of the first considerations investors will pay attention to when considering investing in the SADC region. According to Clark (2000:1141) "political instability or the threat of political instability could be the single largest deterrent to FDI, since it renders all areas of public policy uncertain."

Countries that experience civil conflict and political turmoil are less attractive as FDI destinations (Mwilima, 2003:37). There are various examples to illustrate this. Angola, for example, experienced an increase in FDI in its petroleum industry only after the

¹ It is understood that, even though the Barclays Bank PLC and ABSA Bank Ltd merger was concluded in 2005, the actual investment inflows only started in 2006.

civil war ended in 2002 (Da Gama, 2005:34). Investment growth in South Africa during the apartheid era was negative (Rusiki, 2007:29). FDI in Zimbabwe decreased from USD 102.8 million in 2005 to USD 40 million in 2006 as a result of political instability (World Bank Data, 2011). Mwilima (2003:37) argues that there may be cases where foreign companies in developing countries may be involved in encouraging instability for commercial wealth.

2.3.2 Macroeconomic stability

Countries with sound economic policies that will add to macroeconomic stability will be likely candidates for attracting FDI (Mwilima 2007:37). According to Clark (2000:1140) "case studies tend to emphasize the importance of stability in the macroeconomic environment as a critical component of a successful framework to encourage FDI." Volatility in exchange rates and price levels add to the uncertainty and the apparent risk of FDI (Clark, 2000:1140). It has been noted that in order to attract FDI, countries in the SADC region are required to reform macroeconomic policies "to ensure stability and predictability of policy measures" (DPRU, 2000:10).

2.3.3 Market size and economic growth rates

The size of the market plays a key role in attracting FDI to a country (Mhlanga *et al*, 2009:20). Mhlanga *et al* (2009:6) noted that "market size as measured by per capita GDP is the most robust factor for explaining FDI inflows." In an interview conducted with 81 firms from the United Kingdom, Switzerland and Germany, 84 percent of the respondents noted that the size of the local market is a reason why they invest in the SADC region (Mwilima, 2003:38). This was the single largest determinant of all the factors listed by the interviewees of that study.

SADC has the second smallest population of all the regional integration agreements such as the European Union and the North American Free Trade Association (Muradzikwa, 2002:15). With fifteen members, the SADC is the second largest grouping but has the second smallest population next to Central Europe (Muradzikwa, 2002:14). The small market size in Southern Africa is further characterised by "high incidences of poverty (especially for women and children in under-developed rural areas), uneven distribution of income, wealth and opportunities" (Muradzikwa,

2002:14). The combination of these elements makes SADC an unattractive region in which to invest. It should be emphasised that low levels of investment "has generally led to low economic growth, and low economic growth itself has led to low levels of investment" (Muradzikwa, 2002:14).

2.3.4 Infrastructure

In a study conducted by Mhlanga *et al* (2009:20) to determine to what extent project-level FDI in the SADC region during the period 1994 to 2005 could be explained by a set of source country economic variables, it was noted that infrastructure development has a positive effect on FDI projects. Infrastructure development in the SADC region has been inhibited by fading levels of public investment on infrastructural projects (Muradzikwa, 2002:16). Increasing debt burdens, slow economic growth and increased pressure on SADC governments to lessen government expenditure continue to aggravate the backlog in infrastructure that the SADC faces (Muradzikwa, 2002:16).

Access to inputs and infrastructure are emphasised in case studies and empirical work to be a key consideration for foreign investors (Clark, 2000:1141). FDI would be discouraged if the inputs to production cannot be obtained at a competitive price and in a timely manner (Clark, 2000:1141). In the figure below different indicators of infrastructure are noted.

Figure 2.3 Infrastructure indicators in the SADC region

Country	Internet users per 100 people in 2009	Total railway lines in km in 2008 (*)	Roads paved as % of total roads in 2008 (*)
Angola	3.3	-	-
Botswana	6.2	888.00	-
Congo, Dem. Rep.	0.6	3,641.00	-
Lesotho	3.7	-	-
Madagascar	1.6	-	-

Malawi	4.7	-	-
Mauritius	22.7	-	98.00
Mozambique	2.7	3,116.00	21.00
Namibia	5.9	-	-
Seychelles	38.6	-	96.00
South Africa	9	22,051.00	-
Swaziland	7.6	300.00	-
Tanzania	1.5	-	7.00
Zambia	6.3	-	-
Zimbabwe	11.4	-	-
* An "-" indicates that no data was available for the country for that specific year.			

From the above it can be noted that countries in the SADC region (for which sufficient information is available) lack proper infrastructure. Without proper communication facilities an invariable delay in production of goods and/delivery of services takes place. The absence of railway lines and paved roads decreases the efficient transport of goods and delivery of services. For SADC economies, these infrastructure indicators are a reflection of the underdevelopment of vast areas of the African continent that has aggravated rural and urban poverty. This has rendered Africa an unappealing region to invest in, relative to other developing regions of the world (Muradzikwa 2002:16).

2.3.5 Skilled workforce

It is generally recognised that the answer to growth and redistribution is material increases in productive capacity investment (Muradzikwa, 2002:17). In an analysis of survey data from over eight-hundred firms the availability of skilled workers was noted as the single largest factor that inhibits investment growth in South Africa (Argent, 2008:4). The problem becomes more burdensome in that some countries lack proper

administration or have unsound government policies making it more difficult for potentially skilled workers to obtain work permits to a country (Muradzikwa 2002:17).

2.3.6 Corporate governance

It has become imperative that the rules and related administrative procedures in a country be transparent in order to limit any uncertainties in business planning (Clark, 2000:1141). Foreign capital could potentially flow elsewhere if commercial and other laws and regulations are irreconcilable with the operation of foreign owned companies (Clark, 2000:1141). In 2000, an investor opinion survey was published indicating that good corporate governance results in great rewards (Muradzikwa 2002:16). The survey involved two-hundred institutional investors which administers USD 3.5 trillion in funds (Muradzikwa 2002:16). Seventy-five percent of the investors noted that good corporate governance was as important as financial performance (Muradzikwa 2002:16). Furthermore, "a premium of good corporate governance in an organisation was assessed as high as twenty-seven percent" (Muradzikwa 2002:16).

Closely related to corporate governance is crime and corruption. Incidences of crime and corruption in African countries are often described in the media to the extent which it may potentially be accepted as the norm. The result is that Africa's image is portrayed as an unfavourable investment location (Mwilima, 2003:39). In a survey noted by Muradzikwa (2002:17), forty-five European and South African investors noted corruption as a crucial barrier to investment in South Africa.

2.3.7 Privatisation programmes

The implementation of effective privatisation programmes has promoted positive FDI trends in countries and has encouraged FDI to countries in the SADC region since 1993 (DPRU, 2000:3, 6). This has been especially significant in the mining industry, where previously state-owned enterprises were sold to foreign investors (DPRU, 2000:5). Other examples include the privatisation of entities within the telecommunications industry, for instance Telkom in South Africa.

Privatisation programmes have also certain procedural disadvantages. These include poor execution and supervision, a "lack of transparency and a high level of

politicisation" (DPRU, 2000:6). In the context of the success of privatisation programmes in the past, privatisation of state owned enterprises could be seen as a channel for FDI and it needs to be carefully regarded by SADC countries in its strive to reach higher levels of FDI growth (Muradzikwa, 2002:6).

2.3.8 Taxation

The transparency of the tax law and administrative uncertainty are often considered more important than the tax treatment of income and expenditure (Clark, 2000:1141-1142). Clark (2000:1142) also notes that "uncertainty over the tax consequences of FDI increases the perception of risk and thus discourages capital flows." This becomes all the more important if governments are eager to attract long-term, capital investments.

2.4 TAX INCENTIVES

Tax incentives (or fiscal incentives) form an integral part of many governments' investment promotion policies (Biggs, 2007:4). In developing countries reliance is often placed on indirect taxes such as exemptions from customs duties to serve as a tax incentive (Biggs, 2007:4). A greater reliance on other tax incentives could lead to increase FDI inflows, nurturing of domestic production and encouraging firms to increase supply of goods and services (Biggs, 2007:4).

Tax incentives can stimulate investment, specifically for projects that could be feasible in locations where non-tax factors are reasonably similar (Bolnick, 2004:3-1). Despite the constraints on the efficiency of tax incentives in attracting FDI, "a conceptually legitimate purpose for granting them in developing countries is to rectify some forms of market failure, most notably those involving externalities²" (Tanzi et al, 2000:25). But Tanzi et al (2005:25) notes that the most compelling reason for granting tax incentives by developing nations is to address regional development needs. It is thus important for tax incentives to positively influence the investment climate as it can lead to an increase in the investment effect.

2.4.1 Definition of a tax incentive

² The term "externalities" refers to an effect of a purchase or decision by a set of parties on others who did not have a choice and whose interests were not taken into account. An example of this would be pollution.

Incentives can be defined as "policies used to attract internationally mobile investors" (Mwilima, 2003:34). Tax incentives, as a form of incentive, are defined as "special tax provision[s] granted to a qualifying investment project (however determined) that represents a statutorily favourable deviation from a corresponding provision applicable to investment projects in general" (Argent, 2008:5).

The Business Dictionary (2011) defines a tax incentive as "the deduction, exclusion, or exemption from a tax liability, offered as an enticement to engage in a specified activity (such as investment in capital goods) for a certain period." The MoU issued by the SADC defines tax incentives as "fiscal measures that are used to attract local or foreign investment capital to certain economic activities or particular areas in a country."

The definition of tax incentives according to the Business Dictionary and the MoU is couched in purposive terms. For the purposes of this dissertation, both definitions require tax incentives to be utilised specifically to attract FDI. The definitions further narrow the extent of tax incentives by limiting tax incentives to certain economic activities or geographical areas in a country for a certain period. It is concluded, for the purposes of this dissertation, that a tax incentive can be identified on the basis that it has a distinct purpose in encouraging FDI to specific economic activities or geographical areas for a certain period.

Clark (2004:1143) divides tax incentives into three distinct categories: namely, "tax incentives that reduce the corporate income tax rate on profits derived from investment, tax incentives that reduce the after-tax cost to business of purchasing new capital and tax incentives that reduce the after-tax cost of raising funds to finance the purchase of new capital." In the discussion that follows this distinction will be used as a basis to distinguish between the different types of tax incentives.

2.4.2 Tax incentives that reduce the corporate income tax rate on profits derived from investment

2.4.2.1 *Corporate income tax rate*

The lowering of the overall corporate income tax rate on qualifying income remains the most favourable and innovative tax incentive used by developing and developed

countries alike (Mintz, 2004:11; Clark, 2004:1146). The corporate income tax rate has to be significantly below the global norm of 35 percent in order to be effective in attracting FDI (Biggs, 2007:8). The corporate income tax rate reduction can either be applicable to all domestic and foreign source income or to income earned by non-residents alone or a combination of these (Clark, 2004:1146). For instance, should a country have the need to attract FDI to its manufacturing sector, it could decide to reduce the corporate income tax rate for companies within the manufacturing sector, or a subsector thereof.

The main disadvantage of a lower corporate tax rate lies in the difficult definitional, administrative and compliance issues where the low corporate income tax rate is targeted at a specific income activity (Clark, 2004:1146). Legislative provisions and administrative regulations must be carefully drafted, ensuring that the income activities to which the lower corporate income tax rate applies are specifically defined and clear.

A further disadvantage of a lower corporate income tax rate is that it is often used as the first port-of-call for countries as a measure to attract FDI. The result of such application is a "race-to-the-bottom", during which developing countries make tax concessions which they cannot afford to give (Biggs, 2007:8).

The advantages of lowering the corporate income tax rate are as significant. Evidence suggests that a lower corporate income tax rate encourages FDI to a country (Biggs, 2007:8; Clark, 2004:1146). It furthermore "discourage[s] financial structures and repatriation behaviour aimed at eroding the host country tax revenue base" (Clark, 2004:1146). A lower corporate income tax rate could also potentially lead to an increase in entrepreneurial activities and reduce the incentives for income tax evasion (Biggs, 2007:8).

Finally, it should be noted that the corporate decision to invest in a particular country is often based on the effective income tax rate, rather than the corporate income tax rate (Biggs, 2007:10). The effective income tax rate is calculated by dividing the total amount of tax paid by the total income (Biggs, 2007:10). The effective income tax rate is thus the encompassing rate at which income tax is paid after taking into account progressive tax bands, offsets, discounts and reductions (Biggs, 2007:10). The

corporate income tax rate and the effective income tax rate can be different as a result of the means of funding, either by share capital or loan finance. It is thus submitted that countries should carefully consider the impact that a reduction in the corporate income tax rate will have on the effective income tax rate of investing firms, as well as on the total tax revenue before implementing such lower corporate income tax rate.

2.4.2.2 Tax holidays

A very common tax incentive used among developing nations to attract FDI is a tax holiday (Argent, 2008:7; Clark, 2004:1142; Biggs, 2007:11; Mintz, 2004:6; Tanzi et al, 2005:25). A tax holiday is a blunt form of tax incentive whereby a taxpayer is exempt from the corporate income tax rate for a specific period (Argent, 2008:6; Biggs, 2007:11). It is usually offered to new firms in a specific region and/or a specific industry (Clark, 2004:1145).

Argent (2008:7) notes that a reason why tax holidays are so common among developing nations is that it does not require an expense of public funds, especially where public funds are scarce. It further relieves the revenue authorities from the costs and time spent monitoring and administering taxpayers on whom the tax holidays are applied (Argent, 2008:7; Clark, 2004:1145; Tanzi et al, 2005:25). This makes tax holidays particularly attractive to countries which are implementing a corporate tax system.

Since tax holidays are awarded to new companies it may reward start-up companies which are often faced with cash-flow problems in the first year of existence (see Biggs, 2007:9). In the event that a tax holiday is offered to companies in a specific industry it could result in the transfer of skills and knowledge to domestic firms or employees (Clark, 2004:1145).

Despite the popularity of tax holidays its disadvantages are significant. Since tax holidays often only extend to new firms it creates a competitive advantage to new companies to the detriment of companies that are already established in the market (Mintz, 2004:10). Governments are then faced with the pressure of developing other tax incentives in order for non-tax holiday companies to compete with tax holiday companies (Mintz, 2004:10).

Secondly, it is often difficult to distinguish new firms from existing firms in order to determine whether a tax holiday should be applied (Mintz, 2004:10). This creates a further opportunity for tax evasion: existing companies can re-enter the market as so-called "new companies" and thereby enjoy the preferential treatment of a tax holiday (Mintz, 2004:10).

Thirdly, the revenue cost of tax holidays can be significant (Mintz, 2004:10). For instance, companies could shift income from non-tax holiday companies to tax holiday companies within the same group of companies. In such a way potential taxable income would be sheltered from taxation (Mintz, 2004:10; Argent, 2008:7). In the context of this disadvantage to governments, Argent (2008:7) further emphasises that it would be very difficult to even determine the tax revenue of tax holiday companies that is foregone because those companies are removed from the tax base.

To conclude, the distinguishing advantage of tax holidays is that it relieves the revenue authorities from the administrative and monitoring burden. Tax holidays do have a number of disadvantages. The most significant of these is the loss to the source country in tax revenue foregone. Tax holidays are generally least attractive to firms in sectors requiring long-term capital commitments. Despite its disadvantages, tax holidays remain a very popular form of tax incentive among developing nations.

2.4.2.3 *Carry forward of fiscal losses*

The carry forward of fiscal losses is a tax incentive by which the fiscal (or tax) losses of a firm are allowed to be carried forward to the following year, effectively reducing the taxable income (if any) of that firm for that following year. The reason for this is the "recognition of the fact that the tax year is an artificial construct" (Clark, 2004:1177). Following an economic recession it can thus be expected that the pool of fiscal losses would be relatively large (Clark, 2004:1177). The period for which fiscal losses may be carried forward is not always infinite, and could be limited to, for example, five years.

The advantage of this type of tax incentive is that it provides relief to start-up business. As noted above, start-up businesses often find it difficult to make a profit (and taxable income) in its first few years of existence. The carry forward of fiscal losses provides

these firms with the opportunity to save taxes in the first years during which they generate future taxable income.

The singular disadvantage of this type of tax incentive is the loss of tax revenue foregone. Further to that, taxpayers often use the carry forward of fiscal losses against income derived from another trade in a different country. For that reason legislative provisions in this regard often limit or "ring-fence" the set-off of fiscal losses to specific areas of income. The absence of such limitations for any industry would be a tax incentive.

2.4.3 Tax incentives that reduce the after-tax cost to business of purchasing new capital

2.4.3.1 *Investment allowances*

Investment allowances are "special or enhanced deductions against taxable income" (Clark, 2004:1146). An example of this is the accelerated depreciation allowance. For accounting purposes assets are depreciated over the useful economic life of the asset. These assets include fixed property, plant and equipment but it excludes, for instance, land. In order to encourage FDI host countries often allow assets to be written off over a shorter period for income tax purposes than for accounting purposes. The result is an increase in the allowance for the write-off of capital assets against taxable income, effectively reducing taxable income. A further example is an allowance for research and development expenditure. For example, source countries would often allow more than 100 percent of research and development expenditure to be deducted for income tax purposes in order to encourage firms to undertake research and development activities within the source country.

Biggs (2007:12) indicates four advantages of tax incentives. Firstly, they provide incentives for long-term capital investment as they allow more rapid recoupment of cash flow. Secondly, they are less costly than tax holidays since they are based on investment flows rather than corporate profits. Thirdly, they are embedded in tax legislation and do not require separate tax laws. Lastly, they are less exposed to transfer pricing manipulation.

A further advantage of an accelerated depreciation allowance is that it increases the present value of the claims against taxable income by moving them forward, closer to the time when the investment was made, without reducing the initial cost of the capital (Clark, 2004:1147). The greatest advantage for the taxpayer would be in the event that the cost of the asset can be written off in full in the first year during which it was acquired.

The disadvantage of this type of incentive is that it is dependent on the inflation rate of the host country (Biggs, 2007:12). For example, a "high inflation rate can quickly erode the value of the annual depreciation allowances, resulting in a relatively high effective income tax rate on capital" (Biggs, 2007:12). This is particularly significant to countries in the SADC region which are characterised by high levels of inflation, such as Zimbabwe.

In addition to being dependent upon the inflation rate, the investment allowance is also dependent upon the corporate income tax rate of the host country (Clark, 2004:1146). For instance, the higher (or lower) the corporate income tax rate is, the higher (or lower) the value of the allowances would be to the taxpaying firm (Clark, 2004:1146).

Accelerated depreciation allowance rates vary across categories of capital assets. This could lead to an increase in the administrative burden for revenue authorities (Biggs, 2007:13). It further provides opportunity for tax avoidance and prolonged settlement procedures (Biggs, 2007:13).

To conclude, investment allowances are a popular form of tax incentive as it signals host countries' commitment to long-term investment and growth. It provides for a faster recovery of investment costs, making it one of the most cost-effective tax incentives available.

2.4.3.2 *Investment tax credits*

Investment tax credits are tax incentives whereby allowances are provided against the tax liability, instead of against the taxable income. According to Clark (2004:1147) "investment tax credits may be flat or incremental." A flat investment tax credit is "earned as a fixed percentage of investment expenditure in a year of qualifying

(targeted) capital" (Clark, 2004:1147). An incremental tax credit, on the other hand, is "earned as a fixed percentage of qualifying investment expenditure in a year in excess of some base, which is typically a moving average base" (Clark, 2004:1147). The driving force behind incremental investment tax credits is to encourage expenditure that would not have been incurred in the absence of the tax relief (Clark, 2004:1147). The distinguishing feature between investment allowances and investment tax credits is that the latter reduces the income tax liability and is therefore not subject to the corporate income tax rate or the inflation rate of a country.

The present value of the flow of tax payments on income from short-term assets is smaller than those from long-term assets (Clark, 2004:1148). As a result thereof investment tax credits would have the most stimulative effect if it is directed towards short-term assets. Similarly, if short-term assets are replaced frequently the investment tax credit would be earned more often as well (Clark, 2004:1148).

2.4.4 Tax incentives that reduce the after-tax cost of raising funds to finance the purchase of new capital

2.4.4.1 *Exemption from or lowering of withholding taxes on passive income*

Income from FDI is taxed on the basis of the residence principle, namely that the taxation of the income occurs in the country of which the recipient of the income is a resident. As an exception to this principle, taxes are sometimes withheld on passive income, namely dividends, interest and royalties, in the country where the income was generated.

Greig (1993:29) notes that there are three reasons why countries implement a system of withholding tax. Firstly, a withholding tax system offers to a taxing authority a relatively efficient means of collecting tax revenue. The reason for this is that courts of one jurisdiction are often reluctant to enforce the tax legislation of another jurisdiction. Secondly, the question on the source of income is eliminated since a withholding tax system simplifies the determination of the liability of withholding tax. Thirdly, a withholding tax system is more attuned to double tax treaties because the "quantification of the withholding tax liability is that much simpler than quantification under other systems" (Greig, 1993:29).

Withholding tax is in many instances a final tax. This means that the recipient of the passive income is not obliged to declare the passive income as part of its taxable income since income tax was already levied on the passive income. As a corollary, in some instances the recipient is not entitled to claim a deduction for expenditure incurred in generating the income on which the tax was withheld (Greig, 1993:28).

In order to encourage FDI, developing countries sometimes provide relief from withholding taxes on passive income attributable to foreign investors (Clark, 2004:1142). This relief is in the form of exemption from withholding taxes or a lowering of the withholding tax rate on passive income.

Little research has been conducted on the advantages and disadvantages of the exemption from withholding taxes or a lowering of the withholding tax rate on passive income. It is submitted that an advantage to the investing firm is a decrease in its income tax liability, especially in countries with high withholding tax rates.

It is further submitted that the disadvantages of this form of tax incentive is three-fold. Firstly, it results in a loss to the source country in terms of taxes foregone. Secondly, it places an administrative burden on revenue authorities to monitor to which taxpaying firms this tax incentive must be applied. Finally, this type of tax incentive provides a window of opportunity for firms to engage in tax evasion strategies.

2.5 CONCLUSION

FDI is a much needed source of economic growth and development for countries in the SADC region. South Africa and Angola are the two SADC member states with the highest average FDI inflows since 2002. Cross-border mergers and acquisitions in the extraction and related service industries of Africa remained a significant source of FDI during this period, but new inbound mergers and acquisitions deals were also concluded in the banking industry.

Non-tax factors play a dominating role in influencing investment decisions and determining the viability of projects. Of these factors the policy and regulatory regime of the host country remains the most important. Empirical evidence suggests that the sensitivity of FDI to tax incentives is increasing over time. The most common tax

incentive that is introduced by governments to attract FDI is the lowering of the corporate income tax rate.

University of Cape Town

CHAPTER 3

HARMFUL TAX COMPETITION

3.1 INTRODUCTION

In 1999 the South African Department of Finance was elected to chair a SADC working group on improving tax co-operation between the fifteen member states of the SADC. Its encompassing objectives were to provide an attractive environment for FDI, promote employment opportunities and encourage stability and growth throughout the region (Stretch et al, 2000). In meeting those objectives the group had to work towards three goals, one being the reduction of harmful tax competition (Stretch et al, 2000).

Following the implementation of the working group the MoU was published by the SADC in 2002. Article 1 of the MoU defines "harmful tax competition" as "... a situation where the tax systems of a jurisdiction are designed in such a way that they erode the tax bases of other jurisdictions and attract investments or savings originating elsewhere, facilitating the avoidance of taxes in other jurisdictions." Article 4(3)(a) of the MoU lists six factors which are evidence of harmful tax competition.³ Article 4(3)(b) stipulates that member states of the SADC will endeavour to avoid "introducing tax legislation that prejudices another Member State's economic policies, activities, or the regional mobility of goods, services, capital or labour."

The MoU does not elaborate further on the evidential factors listed in article 4(3)(a). These factors are similar to some of the factors listed by the OECD in 1998 in its report titled "Harmful Tax Competition: An Emerging Global Issue" (OECD Report) as evidence of the existence of tax havens and/or harmful preferential tax regimes. The OECD Report recognized two problem areas facing international income taxation of geographically mobile activities, namely tax havens and harmful preferential tax regimes (Avi-Yonah, 2008:1; OECD, 1998:3). The OECD Report also defined the factors to be used in identifying harmful tax practices and proceed to make recommendations to counteract such practices (OECD, 1998:3).

³ These six factors are: zero or low effective rates of tax; lack of transparency; lack of effective exchange of information; restricting tax incentives to particular taxpayers (usually non-residents); promotion of tax incentives as vehicles for tax minimisation; or, the absence of substantial activity in the jurisdiction to qualify for a tax incentive.

This chapter discusses the definition of "tax competition". This is followed by an examination of the OECD Report and its progeny. The different factors as listed in article 4(3)(a) of the MoU is discussed with reference to the OECD Report. The reason for this discussion and examination is the absence of a broad definition and explanation of the concept of "tax competition" and the evidential factors thereof in the MoU. It is accordingly submitted that a study of the definition of "tax competition" in section 1 of the MoU and the factors listed in section 4(3)(a) of the MoU should be done with reference to the OECD Report in order to gain a better understanding of the definition and how the factors contribute to tax competition. Finally, the benefits of tax competition and two recent examples of tax competition in the SADC region are analysed.

3.2 DEFINITION OF TAX COMPETITION

In basic terms, tax competition refers to "countries using incentives in their tax systems to compete with each other in order to attract economic activity into their country and thereby increasing their tax revenue" (Holmes, 2007:381). Tax competition also refers to a process whereby countries interdependently set tax rates and tax bases (Rohác, 2010:5). Tax competition becomes "harmful" when "capital and resources are diverted away from their most efficient pre-tax allocation to countries that offer preferential tax regimes" (Holmes, 2007:381). In doing so the economies of other countries are harmed while the economies of countries that engage in tax competition are protected from similar harmful effects (Legwaila, 2010:137).

Tax competition has become an increasingly familiar sight over the last two decades as a result of "the deregulation and globalization of business" (Holmes, 2007:381). The development of technology has furthermore added to the mobility of capital, making it much easier for investors to transfer capital to low tax jurisdictions than before. As discussed in the previous chapter, countries use tax incentives (and their tax regimes) to lure foreign investors and attract FDI. This is not wrong *per se*, because in doing so "countries are exercising their right to fiscal sovereignty" (Legwaila, 2010:117).

There are broadly five arguments against tax competition. The first, as noted above, is that tax competition between countries diverts capital and resources away from their

most efficient pre-tax location. Tax revenue is dispersed between jurisdictions to the benefit of those countries that offer preferential tax regimes (Holmes, 2007:381). Tax competition thus "distorts the allocation of mobile factors of production across countries" and investment, employment and taxable income will move towards low-tax jurisdictions (Rohác, 2010:1; Bolnick, 2004:6-4).

Since tax revenue is primarily used to finance the expenditure of public goods and services the second argument is that tax competition can reduce tax revenue and endanger the economic stability of public income and expenditure (Rohác, 2010:1). The fiscal regime in a low-tax jurisdiction can encourage a country with a higher tax jurisdiction to reduce its own tax rates (against its will) to prevent the loss of tax revenue, resulting in a suboptimal supply of public services (Bolnick, 2004:6-5; Legwaila, 2010:118).

Thirdly, as a result of the loss of tax revenue, tax competition may require countries to tax other revenue sources more heavily, increase other taxes such as customs duties or increase the tax rate on less mobile activities such as labour (Legwaila, 2010:118).

Fourthly, developing countries, such as the member states of the SADC, often depend more on corporate tax revenues than developed countries. Empirical data indicates that tax competition amongst developed countries erode the tax base of developing countries and jeopardizes the opportunity for developing countries to enjoy the benefits of higher tax revenues (Keen et al, 2004:1324). SADC member states are thus vulnerable to aggressive tax relief offered by other countries outside of the SADC region that compete for investments (Bolnick, 2004:6-10).

The final argument is that tax preferences given to countries "often encourage tax avoidance and undermine the integrity and fairness of taxing international transactions" (Holmes, 2007:381-382).

3.3 THE OECD REPORT AND ITS PROGENY

In the context of the arguments against tax competition and with the increasing number of instances of tax competition worldwide the OECD has embarked upon initiatives that aim to prevent harmful tax competition. In 1988 the OECD published its first

report on international tax avoidance and evasion, titled "OECD Committee on Fiscal Affairs, Issues in International Taxation No. 1: International Tax Avoidance and Evasion – Four Related Studies". This report was the first inter-governmental pronouncement on the exploitation of tax treaties (Holmes, 2007:382). Following that report other international bodies than the OECD, for example the European Union, unified in the battle against tax competition and placed considerable emphasis on the denunciation of cross-jurisdictional tax avoidance (Holmes, 2007:382).

Since 1996 the OECD has been at the forefront to define "harmful tax practices" and to develop defensive measures to mitigate the adverse effects. Its focus of attention has been on tax havens that serve as centres for income to escape tax that would be levied in other jurisdictions. "In 1998 the OECD examined harmful tax competition in relation to finance and other service activities, which are highly geographically mobile", and published the OECD Report (OECD, 1998).

The OECD Report was intended to develop a better understanding of how tax havens and harmful preferential tax regimes, collectively referred to as harmful tax competition, affect the location of financial and other service activities, diminish the tax bases of other countries, alter trade and investment patterns and demoralize the fairness, neutrality and broad social acceptance of tax systems generally (OECD, 1998:8). The OECD Report distinguishes between "tax havens" and "harmful preferential tax regimes".

The OECD Report isolates four key factors as defining characteristics of a "tax haven". These are jurisdictions with (a) no or nominal income taxes, and one or more of a (b) lack of effective exchange of information, (c) lack of transparency and (d) lack of substantial activities by taxpayers (OECD, 1998:22).

Although the OECD Report is primarily concerned with tax havens, it also identifies four key factors of "harmful preferential tax regimes". These key factors are the first three from the list above along with "ring-fencing" of tax preferences. The last key factor is included with the effect that the tax relief is not available to resident taxpayers. In the light of this the key factor of "no substantial activity" is absent "because it is pertinent to tax havens but not to tax competition for real projects" (Bolnick, 2004:6-2).

Finally, the OECD Report also lists eight characteristics (as opposed to key factors) of a "harmful preferential tax regime". The OECD Report states that all of them should be taken into account when determining whether a preferential tax regime exists. These are: artificial definition of the tax base; failure to adhere to international transfer pricing principles; foreign source income exempt from residence country tax; negotiable tax rate or tax base; existence of secrecy provisions; access to a wide network of tax treaties lacking anti-abuse provisions; regimes which are promoted as tax minimisation vehicles; and the regime encourages purely tax-driven operations or arrangements.

Following the OECD Report the OECD published a list of thirty-five offshore jurisdictions that it planned to include in a "list of uncooperative tax havens, unless the countries made written commitments to exchange information in international criminal tax matters by December 2003 and in international civil tax matters by December 2005" (Avi-Yonah, 2008:3-4). Two of these offshore jurisdictions identified were Mauritius and the Seychelles, both being member states of the SADC (Avi-Yonah, 2008:3; Bolnick, 2004:6-2).

Since 2002 the list of thirty-five offshore jurisdictions decreased to only three countries (Avi-Yonah, 2008:5). Mauritius gave written consent to the OECD in early 2002, and the Seychelles subsequently also signed a letter of cooperation (Avi-Yonah, 2008:4; Bolnick, 2004:6-2).

3.4 THE SADC AND HARMFUL TAX COMPETITION

The MoU uses the term "harmful tax competition" instead of "harmful tax practices". Bolnick (2004:6-2) is of the view that the reason for the use of that terminology is the SADC's apprehension for the rivalry for substantive activities. Article 1 of the MoU defines "harmful tax competition" as "... a situation where the tax systems of a jurisdiction are designed in such a way that they erode the tax bases of other jurisdictions and attract investments or savings originating elsewhere, facilitating the avoidance of taxes in other jurisdictions." Article 4(3)(a) of the MoU lists a number of instances which are evidence of harmful tax competition. These are zero or low effective rates of tax, lack of transparency, lack of effective exchange of information, restricting tax incentives to particular taxpayers (usually non-residents), promotion of

tax incentives as vehicles for tax minimisation or the absence of substantial activity in the jurisdiction to qualify for a tax incentive. Article 4(3)(b) stipulates that member states of the SADC will endeavour to avoid "introducing tax legislation that prejudices another Member State's economic policies, activities, or the regional mobility of goods, services, capital or labour."

The instances which are evidence of harmful tax competition listed in article 4(3)(a) of the MoU includes all the five key factors for tax havens and harmful preferential tax regimes as identified by the OECD Report.⁴ It also includes one of the eight characteristics of a harmful preferential tax regime, namely the promotion of tax incentives as a vehicle for tax minimisation. Of the remaining seven characteristics of harmful preferential tax regimes per the OECD Report, three may be inappropriate for SADC. These are the failure to adhere to international transfer pricing principles, foreign source income exempt from residence country tax and access to a wide network of tax treaties lacking anti-abuse provisions. A possible reason for this is the "administrative constraints" of and lack of international tax treaties with SADC member states (Bolnick, 2004:6-3). It is submitted that the remaining four criteria, namely negotiable tax rate or tax base, existence of secrecy provisions, artificial definition of the tax base and the regime encourages purely tax-driven operations or arrangements, are as appropriate to the SADC region as elsewhere (Bolnick, 2004:6-3).

3.4.1 Zero or low effective rates of tax

A zero or low effective tax rate on the relevant income "is a necessary starting point for an examination of whether a preferential tax regime is harmful" (OECD, 1998:26). Of all five key factors listed in article 4(3)(a) this factor is the most important. The absence of income taxes is rare, since income tax accounts for the majority of a country's revenue. It is submitted that countries would rather exempt certain classes of taxpayers or certain activities from income tax than implementing a zero or low effective tax rate across all classes of taxpayers or activities.

As will be discussed in the following chapter, the effective income tax rate is the encompassing rate at which income tax is paid after taking into account progressive tax

⁴ These are jurisdictions with: no or nominal income taxes; a lack of effective exchange of information; a lack of transparency; a lack of substantial activities by taxpayers; and "ring-fencing" of tax preferences.

bands, offsets, discounts and reductions. The corporate income tax rate can further be reduced by deductions, exemptions and allowances (Legwaila, 2010:131). It can also be reduced by tax incentives on specific projects when a country applies those incentives with the purpose of attracting foreign investors (Legwaila, 2010:131). The OECD Report goes even further and notes that a zero or low effective tax rate may arise because of "the way in which a country defines the tax base to which the rate is applied" (OECD, 1998:26).

While tax competition is focused on zero or low effective rates of tax, it does not *per se* mean that a country does not generate its revenue by means of increasing other taxes, such as value-added tax, customs and excise duties (Legwaila, 2010:131-132). This aspect is often disregarded when an analysis of harmful tax competition is performed (Legwaila, 2010:131-132).

3.4.2 Lack of transparency

A lack of transparency arises from the manner in which a country's legal system is administered, especially if the tax regime is administered in a careless and secretive way that opens a window of opportunity for taxpayers to not comply with tax laws. A lack of transparency includes "the favourable application of laws and regulations, negotiable tax provisions, and the failure to make widely available administrative practices" (OECD, 1998:27). It is important to note that the lack of transparency extends towards a country's legal system, and not purely its tax system (Legwaila, 2010:133). The OECD Report states the following in respect of the lack of transparency (OECD, 1998:28):

"To be deemed transparent in terms of administrative practices, a tax regime's administration should normally satisfy both of the following conditions: First, it must set forth clearly the conditions of applicability to taxpayers in such a manner that those conditions may be invoked against the authorities; second, details of the regime, including any applications thereof in the case of a particular taxpayer, must be available to the tax authorities of other countries concerned. Regimes which do not meet these criteria are likely to increase harmful tax competition since non-transparent regimes give their beneficiaries latitude for negotiating with the tax authorities and may result in inequality of treatment of taxpayers in similar circumstances."

The following two factors are evident of a lack of transparency (OECD, 1998:28-29):

1. Advance tax rulings. When advance tax rulings are issued to a particular sector without disclosure of the conditions and without being generally applicable it could be indicative of a lack of transparency (Legwaila, 2010:134). Advance tax rulings can be a lawful and necessary practice of administrative authority when it is consistent with and does not negate or abolish statutory laws (OECD, 1998:29).
2. Special administrative practices that are contrary to the fundamental procedures underlying tax laws. This is evident in cases where the tax rate and the tax base is preset, but the administrative practices and enforcement thereof does not comply with the law or do not stipulate the conditions of the applicability (OECD, 1998:29). This could lead to various consequences, for instance, "encouraging corruption and discriminatory treatment" and making it more troublesome for other countries to enforce their tax laws (OECD, 1998:29).

Legwaila (2010:134) is of the view that the most negative effect of the lack of transparency is that if the country of residence does not have sufficient knowledge of the tax that is levied on its residents' income in other countries, it cannot take the necessary measures to correct the damage that was caused. This could be further extended to the case where the country of residence may grant double tax relief on income which otherwise should have been taxable (Legwaila, 2010:134).

3.4.3 Lack of effective exchange of information

Countries exchange information about their residents for various reasons, the most common example being the prevention of criminal activities. With the rise of the mobility of capital, and taxpayers moving capital across borders with the motivation of enjoying less tax in lower tax jurisdictions, the exchange of information has become a very important tool for countries to access information on persons' economic activities in other countries in order to assess their tax liability. As a result of the interaction between economics, banking and accounting, the information to be exchanged is not necessarily limited to tax information (Legwaila, 2010:134). As such the information could include bank and other accounts statements as well.

Holmes (2007:391) states that one of the key anti-avoidance provisions in double tax agreements is the capability of local tax authorities of each contracting state to exchange information about taxpayers between one another. Such provisions will allow the tax authority in Country A to collect information about its resident taxpayers' activities in Country B. On the other hand, the tax authorities in Country B would be allowed to gather information from Country B about residents of Country A that carries out activities or invest in Country B.

Often a country is prevented from exchanging information on taxpayers because of secrecy laws which prevent the tax authorities from gathering information on taxpayers that benefit from a preferential tax regime (OECD, 1998:29). An example of this is certain transactions such as the calculation of a selling price or relations between an enterprise and its business customers that are regarded as a business secret by the tax authorities. Other constraints are "bank secrecy rules, the absence of an annual general audit requirement for companies, no requirement for a public register of shareholders and the use of shares and financial instruments issued in bearer form" (Legwaila, 2010:135). For example, in a majority of South African double tax agreements a clause is inserted to compel a contracting state to exchange information that is appropriate to the carrying out of the requirements of the double tax agreement or the provisions of domestic laws concerning taxes of every kind imposed on behalf of the other contracting state (Oguttu, 2010:195).

Against this background, "the ability or willingness of a country to provide information to another country is a key factor" in determining whether the tax regime operated by a country has the effect of being harmful (OECD, 1998:29).

3.4.4 Restricting tax incentives to particular taxpayers

The "ring-fencing" of a regime from the domestic economy in favour of non-resident taxpayers is often a clear indication that a country is engaged in harmful tax competition. Taxpayers that are incorporated into the regime enjoy the benefit of the infrastructure of the country providing the preferential tax regime, without necessarily incurring the cost of the infrastructure (OECD, 1998:26). The OECD Report states that ring-fencing may take two forms, namely (a) "investors who benefit from the tax

regime are explicitly or implicitly denied access to domestic markets" and (b) "regimes that restrict the benefits to non-resident taxpayers" (OECD, 1998:28). The latter is included in article 4(3)(a) of the MoU.

The effect of ring-fencing is that taxpayers are relieved from the burden of paying taxes (usually at a relatively high rate) in the country of residence (Legwaila, 2010:125). This is further driven by the practice of tax professionals to research the countries with the lowest effective rate of tax and marketing their findings.

3.4.5 Promotion of tax incentives as vehicles for tax minimization

Although the promotion of tax incentives as vehicles for tax minimization is not a key factor to identify whether a harmful preferential tax regimes exists, the OECD Report states that it is one of several factors that can assist in identifying such regimes (OECD, 1998:33).

Some of the most successful preferential tax regimes are those that are widely endorsed by, or are endorsed with the consent of, the offering country (OECD, 1998:33). While marketing is not a requirement for determining whether or not a regime is harmful, the existence of marketing material promoting a regime as a tax minimisation vehicle may be an indication of whether a jurisdiction is seen and used principally as "a means of engaging in international tax avoidance and evasion" (OECD, 1998:33-34). Marketing material may also be a valuable source of information for tax and regulatory authorities (OECD, 1998:34).

It is submitted that countries themselves would not necessarily engage in such a form of advertising as it would create the opportunity for those countries to be criticised as tax havens. However, as noted above, the practice of tax professionals to research low tax jurisdictions may provide tax havens with all the publicity they need.

3.4.6 Absence of substantial activity

In general, capital will move across borders to economic activities with a clear purpose: to generate income and eventually a profit. The absence of a substantial activity in a country would often be an indication that the country could be attempting to attract

investment or transactions that are solely tax driven, instead of profit driven (OECD, 1998:23). It may further indicate that a country "does not (and cannot) provide a legal or commercial environment or offer any economic advantages that would attract substantive business activities in the absence of tax minimising opportunities it provides" (OECD, 1998:24).

The OECD Report rightly suggests that it may be difficult to determine when and whether an activity is substantial (OECD, 1998:24). For example, financial and management services may in certain situations involve substantial activities. It is submitted that to determine whether a country lacks substantial activity would involve an interpretation of the economic background and circumstances of the country.

3.5 ARTICLE 4(3)(b) OF THE MOU

Article 4(3)(b) of the MoU stipulates that member states of the SADC will endeavour to avoid "introducing tax legislation that prejudices another Member State's economic policies, activities, or the regional mobility of goods, services, capital or labour." It is clear that article 4(3)(b) refers to the harmful effects of tax competition, specifically the first argument against tax competition as discussed above.

The word "prejudices" is defined as *inter alia* "the detriment or injury caused to a person by the preconceived, unfavourable conviction of another or others" (The Free Dictionary By Farlex, 2012). In the context of this definition, it could be argued that if an investor chooses Country A over Country B based on better tax incentives offered by Country A, and Country B suffers to a significant detriment as a result thereof, then Country B is prejudiced.

3.6 BENEFITS OF TAX COMPETITION

There is increasing concern that the development of competitive bidding between SADC countries for FDI may persuade them to offer allowances on "regulation, taxes, environmental protection and labour standards that are unnecessary" (Zampini, 2008:1). Despite the negative perception that is often attached to tax competition by governments, there are also benefits that arise from it. Milton Friedman (as cited by Legwaila (2010:117)) stated the following in respect of tax competition:

"Competition among national governments in the public services they provide and in the taxes they impose is every bit as productive as competition among individuals or enterprises in the goods or services they offer for sale and the prices at which they offer them. Both lead to variety and innovation: to improvement in the quality of goods and services and a reduction in their cost. A government cartel is not less damaging than a private cartel."

The literature on the benefits of tax competition indicates that research in this study field is mostly focused on the economic impact of tax competition, rather than the tax impact. It is recognised that competitive forces is as beneficial in matters relating to establishments, public affairs and taxation than to the manufacture of private goods (Rohác, 2010:16).

There are three areas where tax competition affects the economy: it can have an impact on markets, on business and on governments (Teather, 2005:25–33; Rohác, 2010:1-16). The impact of tax competition on markets is mostly evident on the ability of companies to expand and pay out dividends. A higher corporate tax rate would result in less profits being retained, leading to less capital available for investment in expansion and business growth. In addition, if investment income is taxed at a high rate, then companies may be required to increase dividend payments in order to attract investment. The decrease in profits and increase in dividend payouts may put a strain on a company's retained earnings.

Secondly, tax havens give investors the opportunity to allow their capital to move easily between countries. Not only have investors a greater choice of where to direct their investments, but developing nations can more easily attract foreign capital which is often needed as a result of the short supply of local capital.

Finally, tax competition makes it more difficult for governments to simply raise revenue by increasing the corporate tax rate. As a result thereof governments increase their efficiency in delivering public goods and services and make better use of the limited resources available. Downward pressure on tax revenues from tax competition is thus a means of disciplining governments that spend inefficiently (Keen et al, 2004:1324).

3.7 PRACTICAL EXAMPLES OF TAX COMPETITION IN THE SADC

In order to illustrate the effect of tax competition on countries within the SADC region, two practical examples are discussed below.

Exhibit 1: The Case of Ramatex (Bolnick, 2004:6-9; Zapini, 2008:6)

Ramatex, a Malaysian based textile manufacturing company, was seeking to build a production facility in Southern Africa to benefit from the Africa Growth and Opportunity Act (AGOA). The AGOA was approved by the United States Congress and came into effect on 18 May 2000 as Title 1 of The Trade and Development Act of 2000. The AGOA offers tangible incentives for African countries to continue their efforts to open their economies and build free markets. Ramatex offered an investment of N\$1 billion, and sought investment incentives in South Africa, Madagascar and Botswana before finally deciding upon Namibia.

The Namibian Ministry of Trade claimed to have lured Ramatex by offering even greater concessions than those offered to other export processing zone (EPZ) companies. It offered an incentive package which included subsidised water and electricity, a 99-year tax exemption on land use as well as N\$60 million to prepare the site including the setting up of electricity, water and sewage infrastructure. This was justified on the grounds that the company would create between 3 000 and 5 000 jobs during the first two years and another 2 000 jobs in the following two years. Production started in mid-2002 and by April 2003, 3 000 jobs were created and in 2005, another 2 000 more people were employed.

The investment by Ramatex came at a greater cost than the Namibian authorities expected. As a result of the location of the production facility in Namibia, Ramatex closed down another production facility in South Africa, resulting in the loss of 2 500 South African jobs. The subsidised supply of water and electricity resulted in significant cost for the citizens of Windhoek, having to deal with sporadic water shortages. In 2005 mostly all of the 2 000 workers employed were migrant workers from Asia. In 2008 the Ramatex factory closed down its operations.

Exhibit 2: Tax Reform in Tanzania (Bolnick, 2004:6-6 to 6-7)

In 1991 the Presidential Commission in Tanzania introduced a decrease in its tax rates and duty tariffs to improve revenue performance. Despite the loss of revenue as a result of this tax reform, the government argued in its 1992/1993 budget that the loss would be far outweighed by the "improved compliance and tax administration, the elimination of certain exemptions and higher taxes on petroleum products." Unfortunately the budget overlooked some of the revenue enhancement measures that the Presidential Commission introduced as part of the tax reform.

In the light of the decrease in Tanzanian tax rates and duty tariffs, business leaders in Zambia, one of Tanzania's neighbouring countries and fellow member state of the SADC, requested its Minister of Finance to follow Tanzania's example. The Minister of Finance declined their request on the basis that Zambia could not introduce the tax cuts without jeopardizing its macroeconomic stability.

The decision of Zambia's Minister of Finance proved to be sound. The tax reform introduced in Tanzania led to a fiscal crisis in 1993, as Tanzania's revenue decreased by 21 percent in that year. The decrease was mostly attributed to falling revenue from indirect taxes, but interestingly zero-rated import provisions that were introduced also created new opportunities for tax evasion.

3.8 CONCLUSION

Tax competition is increasing as a result of the mobility of capital and the ease by which it can move across borders as a result of technological advances. Governments can use tax incentives (sometimes to their own detriment) in order to attract FDI from its most effective pre-tax location.

The rise of tax competition has necessitated various inter-governmental organisations such as the OECD and the SADC to address the issue. The OECD published the OECD Report in 1998 which is a detailed and elaborative report dealing with *inter alia* the characteristics of tax havens and preferential tax regimes as instances of harmful tax competition within the OECD member states. The SADC published the MoU by listing six factors that are evident of harmful tax competition. The MoU does not elaborate on these factors, but the factors are similar to those listed in the OECD Report. It is thus

submitted that the meaning of those evidential factors should be interpreted with reference to the OECD Report.

Despite the negative publicity surrounding tax competition there are also benefits that stem from it. Most importantly, tax competition encourages governments to allocate resources to the delivery of public goods and services in the most efficient way.

University of Cape Town

CHAPTER 4

TAX INCENTIVES FOR MANUFACTURING COMPANIES IN THE SADC REGION

4.1 INTRODUCTION

The purpose of this chapter is firstly to summarise the corporate tax rates offered by SADC member states to manufacturing companies. The corporate tax rate for manufacturing companies which are lower than the corporate income tax rate for other companies in the specific country is then analysed to establish if it could potentially result in a zero or low effective rate of tax. Finally, the tax incentives specific to manufacturing companies for those countries with zero or low effective rates are examined in detail with a view to establish whether or not those countries engage in harmful tax competition as contemplated by the MoU.

4.2 CORPORATE TAX RATES OF MANUFACTURING COMPANIES

The OECD Report (see Chapter 3) states that the "necessary starting point" to examine whether a preferential tax regime exists is to determine whether or not taxpayers are subject to a low or zero effective tax rate (OECD, 1998:26). In terms of article 4(3) of the MoU a low or zero effective tax rate is one of the evidential factors to be taken into consideration when determining whether SADC member states are engaging in harmful tax competition. The effective income tax rate is the encompassing rate at which income tax is paid after reducing the marginal corporate tax rate with progressive tax bands, offsets, discounts and reductions. The corporate income tax rate can further "be reduced by exemptions, deductions and allowances" (Legwaila, 2010:131). It can also be reduced by tax incentives on particular projects when a country applies those incentives with the purpose of attracting foreign investors (Legwaila, 2010:131). The OECD Report states that a zero or low effective tax rate may arise because of "the way in which a country defines the tax base to which the rate is applied" (OECD, 1998:26).

In order to determine whether the preferential income tax treatment is evidence of harmful tax competition it must be considered whether these (lower) corporate income tax rates give rise to a low or zero effective rate of tax. The OECD Report does not

define what a "low" effective rate of tax is. The OECD Report does however state that a zero or low effective tax rate may occur because the marginal rate itself is very low (OECD, 1998:26).

On the basis of the above understanding of effective tax rates, the corporate income tax rates for manufacturing companies in the SADC member states since 2002 were collated and evaluated in order to identify corporate income tax rates for manufacturing companies that could lead to instances of low or zero effective rates of tax. The results are illustrated in Figure 4.1 below.

Figure 4.1: Marginal corporate income tax rates for manufacturing companies

Country	Manufacturing companies	Other (a)
	%	%
Angola	35	35
Botswana	15	25
DRC	40	40
Lesotho		
- <i>Export to SACU members</i>	10	25
- <i>Export outside of SACU</i>	-	25
Madagascar	23	23
Malawi		
- <i>Manufacture products for export processing zone</i>	(b)	30
Mauritius	15	15
Mozambique	32	32
Namibia		
- <i>Export to SACU members</i>	18	34
- <i>Export outside of SACU</i>	-	34
Seychelles	40	40
South Africa	28	28
Swaziland	30	30
Tanzania	30	30
Zambia	35	35
Zimbabwe		
- <i>Export more than 50 percent of products</i>	20	25
<i>Notes:</i>		

- (a) The corporate income tax rates indicated in "Other" are the corporate income tax rates for companies other than specifically designated, such as farming or mining companies.
- (b) According to the Malawi Revenue Authority the manufacturing companies that currently qualify for this corporate income tax rate are Nyika Farms, Victoria Investments, Thyolo Nut Company, Crossbow Clothing, Win Win Garments, Kawalazi Estate, Sable Farming, Exclusive Garments (Mulli Group), Vizara Plantation, Vizara Eco Timbers, Zikomo Flowers, Giant Clothing, Crown Fashions and CTM Blankets.

From the above it is observed that the marginal corporate income tax rates for manufacturing companies in Botswana, Lesotho, Malawi, Namibia and Zimbabwe is specifically set at a lower rate than the corporate income tax rates for other companies in those countries. It is submitted that the marginal corporate income tax rates can be reduced with progressive tax bands, offsets, discounts and reductions, resulting in preferential income tax treatment towards manufacturing companies in Botswana, Lesotho, Namibia, Malawi and Zimbabwe.

As stated above, the OECD Report does not define what a "low" effective rate of tax is. The OECD Report does however states that a zero or low effective tax rate may occur because the marginal rate itself is very low (OECD, 1998:26). It is submitted that, for purposes of this research study further research be conducted in respect of Lesotho, Namibia and Malawi only. The reasons for this limitation are: firstly, the difference in the corporate income tax rate for manufacturing companies and other companies is 10 percent and 5 percent only for Botswana and Zimbabwe respectively; and secondly, Lesotho, Namibia and Malawi are the three SADC member states with the lowest marginal corporate tax rate for manufacturing companies and includes a corporate income tax rate of zero percent in certain circumstances.

The corporate tax rate for manufacturing companies in Lesotho and Namibia for the profits derived from the export of manufactured goods outside of the Southern Africa Customs Union (SACU) region, namely Botswana, Lesotho, Namibia, South Africa and Swaziland is nil percent. Similarly, the corporate income tax rate for manufacturing companies in Malawi that manufactures products for the EPZ is nil percent. In Malawi the EPZ is "any area approved by the Malawian Minister of Industry and Trade for the purpose of manufacturing of export products with the object of promoting economic growth by attracting foreign investments" (Malawi Revenue Authority, 2011). In Malawi, the EPZ scheme is governed by the Export Processing Zone Act of Parliament No. 11 of 1995 and regulated by the Export Processing Zone Regulations under Section 21 of the same Act (Malawi Revenue Authority, 2011). As seen in note (b) to Figure 4.1 above there are currently eight companies that qualify for this specific corporate income tax rate.

Since the corporate income tax rate for some manufacturing companies in Lesotho, Malawi and Namibia is nil percent, it will necessarily lead to zero or low effective rate of tax for those companies. This must be considered in the light of the tax incentives offered by these countries to manufacturing companies.

4.3 TAX INCENTIVES OFFERED BY LESOTHO

Section 3(1) of the Income Tax Order defines the word "manufacturing" as the "substantial transformation of tangible movable property", but does not include "construction, installation, assembly, transportation, power generation, or the provision of public utility services." The Government of Lesotho extends preferential treatment in respect of dividends and royalties with regards to manufacturing companies as well as the preferential income tax rate.

4.3.1 Withholding tax rate on investment income

Section 107(1) of the Income Tax Act 9 of 1993 (the Income Tax Act, 1993) stipulates that withholding tax is payable at the standard tax rate (currently 25 percent) on any "Lesotho-source dividend, interest, royalty, natural resource payment, or management charge paid to a non-resident." Section 107(2) of the Income Tax Act, 1993, determines that a dividend distributed by manufacturing companies from income which is from a

Lesotho-source and derived from manufacturing is not subject to a withholding tax rate. Similarly, section 107(3) of the Income Tax Act, 1993, stipulates that the rate of withholding tax payable on a Lesotho-source royalty paid in respect of technology used in the production of manufacturing income is only 15 percent as opposed to 25 percent.⁵

4.3.2 Preferential income tax rate

As noted in Figure 4.1 above, the income tax rate for companies other than manufacturers in Lesotho is 25 percent. The income tax rate for taxable income derived from manufactured goods exported outside of the SACU region is nil percent (Lesotho National Development Corporation). The income tax rate for taxable income derived from manufactured goods exported to SACU members is 10 percent (Lesotho National Development Corporation). Both rates are below the standard income tax rates on other companies, being 25 percent.

4.4 TAX INCENTIVES OFFERED BY NAMIBIA

Section 1 of the Income Tax Amendment Act, 2002, defines the phrase "manufacturing activity" as:

"(a) the physical or chemical transformation of materials or components into new products -

(i) whether manually or by mechanical or other process;

(ii) whether in a factory, at a private dwelling or any other place; or

(iii) whether for purposes of sale in the wholesale or in the retail trade; or

(b) the assembly of the component parts of manufactured products, but excluding -

(i) assembly on the site of prefabricated integral parts into bridges, water tanks, storage or warehouse facilities, railroad and elevated rights-of-way, lifts and escalators, plumbing,

⁵ In terms of the Explanatory Memorandum to the Income Tax (Amendment Bill), 1994, the reason for the withholding tax of 15 percent is to ensure that the withholding tax on royalties is the same as the effective tax rate for interest and management expenses (at the time). The latter expenses are deducted by the manufacturing company and thus subject to a corporate income tax rate (and effective rate) of 15 percent (which it was at the time of the amendment) (Explanatory Memorandum to the Income Tax (Amendment) Bill, 1994:570).

sprinklers, central heating, ventilating and air conditioning, lighting and electrical wiring, systems of building and all kinds of structures; and

(ii) assembly and installation of machinery and equipment rendered as a service incidental to the sale of goods by a person primarily engaged in the wholesale or retail trade;"

Section 3(1) of the Income Tax Amendment Act, 2002, stipulates that "[a] company which conducts or intends to conduct a manufacturing activity and which requires to be recognised as a registered manufacturer in respect of that manufacturing activity for the purposes of that Act, may apply for registration..." The Namibian income tax law contains tax incentives specifically directed towards registered manufacturers, including (but not limited to) a building cost allowance, employee remuneration and training cost allowance, an export allowance and an additional deduction for expenditure incurred in a foreign export country as well as for expenditure incurred in respect of land based transport.

4.4.1 Building cost allowance

A building allowance is deductible in respect of the costs incurred for the construction of a building used for the purposes of trade (PwC, 2011). Taxpayers (including registered manufactures) are entitled to an allowance of 20 percent of the cost of construction in the year in which the building enters service (PwC, 2011). Thereafter taxpayers other than registered manufacturers are entitled to a deduction of 4 percent per year for the following twenty years (PwC, 2011). The deduction available to registered manufacturers is 8 percent for the following ten years following the year the building entered service (PwC, 2011).

4.4.2 Employee remuneration and training cost allowance

In general, Namibian taxpayers are entitled to deduct for income tax purposes expenditure incurred in respect of the remuneration and training of employees (PwC, 2011). Registered manufacturers may deduct an additional 25 percent of the remuneration and training cost of employees that are directly engaged in the manufacturing process (PwC, 2011).

4.4.3 Export expenditure allowance

Export expenditure is deductible for income tax purposes (PwC, 2011). Registered manufacturers are entitled to an additional 25 percent of costs incurred in an export country for the purposes of exporting Namibian manufactured goods to such country (PwC, 2011). These costs are limited to expenditure incurred in respect of:

- (a) research on the marketing of goods in a foreign country;
- (b) advertising and soliciting of orders in a foreign country, including attendance of approved foreign trade exhibitions and outward trade missions, economy air fare, local travel and accommodation and exhibition costs;
- (c) provision of samples or technical information to prospective customers in a foreign country;
- (d) bringing prospective buyers from a foreign country to Namibia, including economy air fares and accommodation;
- (e) preparation or submission of tenders or quotations in respect of goods to be exported to a foreign country;
- (f) expenditure incurred to finalise contractual agreements; and
- (g) the appointment of agents in foreign countries (Ministry of Trade and Industry Republic of Namibia, 2011).⁶

4.4.4 Export allowance

Taxable income derived from the export of manufacture goods, other than fish and meat products, regardless of having been produced in Namibia or not, shall be reduced by an allowance equal to 80 percent of that taxable income (Ministry of Trade and Industry Republic of Namibia, 2011). Gross profit derived from the export of manufactured goods as a percentage of total gross profit should be used to determine the percentage of taxable income that is used to calculate the export allowance (PwC, 2011).

⁶ The additional deduction increased to 50 percent if the current export turnover exceeds the basic export turnover by more than 10 percent, but less than 25 percent. The additional deduction increased to 75 percent if the current export turnover exceeds the basic export turnover by 25 percent or more (Ministry of Trade and Industry Republic of Namibia, 2011).

For example, the total gross profit of a manufacturing company in a tax year is N\$750 million. The gross profit of that manufacturing company from the export of manufactured goods is N\$250 million, 33 percent of the total gross profit (N\$250 million / N\$750 million). The total taxable income of that manufacturing company for that tax year is N\$300 million. The taxable income derived from the export of manufacture of goods (excluding fish and meat products) is recalculated as N\$100 million (33 percent x N\$300 million). That recalculated taxable income is then reduced by 80 percent to N\$20 million. The latter amount is the taxable income derived from the export of manufactured goods (excluding fish and meat products) on which income tax will be calculated.

4.4.5 Transport allowance

In general, costs incurred in respect of the transport of goods by road or by rail are deductible for income tax purposes (PwC, 2011). Registered manufacturers are entitled to an additional allowance of 25 percent of land based transport costs in respect of material and components used in the manufacturing process or equipment imported for direct use in the manufacturing process (PwC, 2011).

4.4.6 Preferential income tax rate

The EPZ commenced in 1996 through the passing of the Export Processing Zones Act, 1994 (Incentives for Investors, 2011). The EPZ regime attracted 65 local and international companies engaged in various activities, such as the manufacture of car parts and soft toys as well as re-export activities (Incentives for Investors, 2011). These 65 companies have been granted EPZ status certificates (Incentives for Investors, 2011).

Section 3 of the Export Processing Zones Act, 1995, stipulates that "the objects and purposes of EPZ's are to attract, promote or increase the manufacture of export goods, to create or increase industrial employment, to create or expand export earnings, to create or expand industrial investment, including foreign investment and to encourage technology transfer and the development of management and labour skills in Namibia."

In order to qualify as an EPZ company the following three requirements must be met (PwC, 2011):

- a) Goods must be exported to countries other than countries in the SACU region;
- b) Industrial employment must be created or increased; and
- c) Namibia's export earnings must increase as a result of manufactured goods exported.

Manufacturing companies in Namibia can be divided into three categories for purposes of determining their corporate income tax rates. Firstly, as noted in Figure 4.1 above, the marginal corporate income tax rate for companies other than registered manufacturers in Namibia is 34 percent. Secondly, the income tax rate for registered manufacturers is 18 percent in respect of the taxable income for the manufacturing activity for which they are registered (PwC, 2011). This preferential income tax rate is applicable for a period of ten years from registration as a manufacturer (PwC, 2011). Thirdly, section 7(2) of the Export Processing Zones Act, 1995, states that an EPZ company shall not be liable to tax under the Income Tax Act, 1981.

4.5 TAX INCENTIVES OFFERED BY MALAWI

The Government of Malawi introduced the Investment Promotion Act in 1991. The purpose of this Act is (among others) to establish the Malawi Investment Promotion Agency. The Malawi Investment Promotion Agency is the body corporate responsible for investment promotion, investor assistance and advice to the Government of Malawi on investment matters. Section 8(2) to the Investment Promotion Act, 1991, stipulates that the Malawi Investment Promotion Agency will give priority to investment in *inter alia* manufacturing.

The Schedule to the Investment Promotion Act, 1991, states that:

"To further enhance Malawi's investment climate and international competitiveness, the Government is committed to continue the process of reducing rates of taxes and duties. This is to be achieved through the ongoing tax and trade reform programmes."

To encourage export-oriented investments, the Government of Malawi offers "incentives competitive to those found in other countries" (Investment Promotion Act, 1991:14). These incentives include (Investment Promotion Act, 1991:14):

- (a) *"An income tax allowance based on export sales of non-traditional products (i.e. products other than tobacco, tea, sugar and coffee); and*
- (b) *Rebates of import duties, surtaxes, and local taxes on most inputs used in production of export products."*

In addition to the above the Investment Promotion Act, 1991, states that the Government of Malawi is taking into account the establishment of other incentives, "including export financing and guarantee schemes, further developing a manufacturing-in-bond programme, creating export processing zones, and introducing measures to eliminate the payment of duties at the time of importation" (Investment Promotion Act, 1991:14).

4.5.1 Building and machinery cost allowance

Companies in Malawi are afforded an initial allowance of 20 percent of the cost of new and unused plant, machinery and equipment (PwC, 2011). Thereafter the cost of the assets less the initial allowance is written off over 10 or 5 years depending on the nature of the asset (PwC, 2011).

Manufacturing companies are not allowed to claim an initial allowance but are allowed an investment allowance. The investment allowance affords the manufacturing company the opportunity to deduct 100 percent of the cost of new and unused plant, machinery and equipment (PwC, 2011). The investment allowance for used plant, machinery and equipment for manufacturing companies is 20 percent (PwC, 2011). As a result of the investment allowance the cost of new and unused plant, machinery and equipment for manufacturing companies are not depreciated thereafter (PwC, 2011). Similarly to other companies, the cost of used plant, machinery and equipment less the investment allowance is written off over 10 or 5 years depending on the nature of the asset (PwC, 2011).

4.5.2 Pre-operating expenditure

Unlike any other company, a manufacturing company may claim as a deduction any expenditure incurred in the course of establishing the business, provided that the following are correct (PwC, 2011):

- a) The expenditure was incurred not more than 18 months before commencing the business; and
- b) The expenditure would have been allowed as a deduction if it had been incurred after commencing the business.

4.5.3 Carry forward of losses

Companies in Malawi are allowed to carry income tax losses forward for a maximum period of 6 years (PwC, 2011). Manufacturing companies are allowed to carry income tax losses forward for an infinite period (PwC, 2011).

4.5.4 Training cost allowance

Manufacturing companies that export traditional products (tobacco, tea, sugar and coffee) and non-traditional products are allowed an additional training cost allowance. This is an additional 50 percent allowance for of the costs incurred by the taxpayer during the year of assessment in the training of an employee who is a Malawian and intended to enable him/her to attain a qualification at the degree, diploma or certificate level (Investment Promotion Act, 1991:16).

4.5.5 Export tax allowance

The Government of Malawi distinguishes between manufacturing companies and business entities that manufacture under bond. The phrase "manufacture under bond" is not defined in the Investment Promotion Act, 1991. Section 2 of the Export Processing Zone Act, 1995, defines a "bonded factory" as "a factory situated in an EPZ." According to the East African Customs Union "manufacture under bond" refers to "an incentive extended to manufacturers to import plant, machinery, equipment and raw materials tax free, for exclusive use in the manufacture of goods for export" (East

African Customs Union, 2011). The Schedule to Investment Promotion Act, 1991, stipulates that companies manufacturing under bond are not subject to duties on imports of capital equipment used primarily in the manufacture of export products (Investment Promotion Act, 1991:17). A similar incentive is given to companies situated in EPZ's (Investment Promotion Act, 1991:17). On this basis it is submitted that the phrase "manufacture under bond" refers to manufacturing companies in Malawi that are situated in EPZ's.

Companies that manufacture under bond are allowed to deduct an additional 25 percent of the taxable income derived from the export of non-traditional products (PwC, 2011). Such companies are also allowed to deduct a transport tax allowance of 25 percent of the international transport costs to export non-traditional products.

4.5.6 Preferential income tax rate

Companies in Malawi can apply at the Ministry of Industry and Trade to be granted EPZ status. During the application process specific consideration is given to job creation, technology transfer, export diversification, use of local raw materials, warehousing capability and the proof of export markets. In the event that a company receives an EPZ status, then its income is not subject to income tax.

4.6 CONCLUSION

A review of the corporate tax rates available to manufacturing companies indicated that Botswana, Lesotho, Malawi, Namibia and Zimbabwe offers special corporate tax rates for manufacturing companies, subject to certain conditions, such as manufacturing products for an EPZ. The special corporate tax rate for Botswana and Zimbabwe was however not low enough to be considered as giving rise to a "low or zero effective rate of tax" as contemplated by article 4(3) of the MoU. An analysis of the tax incentives of Lesotho, Namibia and Malawi indicated that those countries offer various tax incentives to (both resident and non-resident) manufacturing companies in order to stimulate FDI.

CHAPTER 5

APPLICATION OF ARTICLE 4(1) AND ARTICLE 4(3) OF THE MOU

5.1 INTRODUCTION

This chapter applies the requirements of article 4(1) and two of the six evidentiary factors of article 4(3), namely zero or low effective rate of tax and restricting tax incentives to particular taxpayers, to the tax incentives as discussed in Chapter 4. The purpose of this chapter is to determine whether there is an indication that the Governments of Lesotho, Namibia and Malawi engage in harmful tax competition in respect of the manufacturing industry in the context of the above mentioned evidentiary factors and on the assumption that the other four factors are similar between the member states of the SADC. This chapter focuses on Lesotho, Namibia and Malawi because these three countries had the lowest nominal corporate tax rate for manufacturing companies of the SADC member states.

The chapter discusses the interpretation of article 4(1), followed by the application thereof to the tax incentives. Thereafter two of the six evidentiary factors of article 4(3) are applied to the tax incentives for manufacturing companies in Lesotho, Malawi and Namibia.

5.2 ARTICLE 4(1) OF THE MOU

5.2.1 Interpretation of article 4(1)

Article 4(1) stipulates that:

"Member States will endeavour to achieve a common approach to the treatment and application of tax incentives and will, amongst other things, ensure that tax incentives are provided for only in tax legislation." (Emphasis added.)

The MoU does not elaborate how member states will be able to achieve a common approach to the treatment and application of tax incentives, nor does it provide a definition of the words "treatment" and "application". For purposes of this discussion article 4(1) is divided into two parts. The first part relates to the common approach that

must be followed by member states in the treatment and application of tax incentives. The second part relates to the requirement that member states must ensure that tax incentives are provided for only in tax legislation.

5.2.1.1 *Common approach to the treatment and application of tax incentives*

The Concise Oxford Dictionary (1999) defines the word "treatment" as "the process or manner of treating something in a certain way". The word "application" is defined as "the action of putting something into operation" or "practical use or relevance" (The Concise Oxford Dictionary, 1999).

In order to interpret article 4(1) it is submitted that the ordinary, grammatical meaning of the words in article 4(1) should be used, especially for the words "treatment" and "application". As discussed in Chapter 2, tax incentives can stimulate investment, in particular for projects that could be feasible in locations where non-tax factors are reasonably similar (Bolnick, 2004:3-1). This is specifically relevant to developing countries, as tax incentives in those countries are principally intended to attract FDI (Easson et al, 2002:16). If the literal interpretive approach is adhered to, then article 4(1) could be interpreted as meaning that the common approach of member states must be to "treat" and "put" tax incentives "into operation" for the purpose of stimulating FDI in the respective countries.

5.2.1.2 *Tax incentives must be provided for only in tax legislation*

It is uncertain what the drafters of article 4(1) intended when they used the words "amongst other things". The fact that the words "ensure that tax incentives are provided for only in tax legislation" thereafter are specifically inserted emphasises the importance attached thereto by the drafters.

The words "tax legislation" are drafted in wide terms and are not defined in the MoU. In Chapter 3 it was noted that as a result of the loss of tax revenue, tax competition may require countries to tax other revenue sources more heavily, increase other taxes such as customs duties or increase the tax rate on less mobile activities such as labour. It is submitted that, in accordance with its wide ambit, the drafters presumably intended to undertake a holistic view and to include all taxes administered by the revenue

authorities. It is also submitted that the words "tax legislation" include the provisions of each member state's income tax legislation, legal precedent and/or current practice of the local revenue authorities.

5.2.2 Application of article 4(1)

5.2.2.1 *Common approach to the treatment and application of tax incentives*

According to the Tax Policy of the Government of Lesotho the tax system must focus on "growth facilitation" in foreign investment (Lesotho, 2009:8). As a result thereof the Tax Policy notes that Lesotho should utilize the tax system as an instrument to achieve a competitive advantage for FDI (Lesotho, 2009:8). Furthermore, the Tax Policy states that "tax incentives are meant to nurture specific sectors that are regarded as key or strategic" (Lesotho, 2009:8).

The Ministry of Trade and Industry of Namibia states that "[i]t has also made considerable effort to put competitive tax and non-tax incentives in place in order to attract foreign investment to the Export Processing Zones and to encourage both foreigners and locals to invest in the manufacturing sector." (Emphasis added.) (Ministry of Trade and Industry Namibia, 2011).

On the website of the Ministry of Trade and Industry of Namibia the following reason is furnished for the exemption from corporate tax for manufacturing companies exporting products outside of the SACU region (Ministry of Trade and Industry of Namibia, 2011):

"As a far-reaching incentive for manufacturers, the Namibian Government adopted a policy for the establishment of an Export Processing Zone (EPZ) regime to serve as a tax haven for export-oriented manufacturing enterprises in the country, in exchange for technology transfer, capital inflow, skills development and job creation." (Emphasis added.)

In respect of the tax incentives available to registered manufacturers the Ministry of Trade and Industry of Namibia states that (Ministry of Trade and Industry of Namibia, 2011):

"The Government of the Republic of Namibia is committed to stimulate economic growth and employment and to establish Namibia as a gateway location in the Southern African region. Incentives are largely concentrated on stimulating manufacturing in Namibia and promoting exports into the region and to the rest of the world. Incentive regimes in place are designed to give Namibia-based entrepreneurs who invest in manufacturing and re-export trade a competitive edge."

In Malawi, the Malawi Investment Promotion Agency was established as an organisation in 1991 by the Investment Promotion Act, 1991. Section 6 of the Investment Promotion Act, 1991, signals the Government of Malawi's commitment to investment in Malawi. Section 8 of the Investment Promotion Act, 1991, stipulates that the general objective of the Malawi Investment Promotion Agency is "to promote, attract, encourage, facilitate and support local and foreign investment in Malawi..."

The aim of the Government of Malawi on investment incentives is to encourage development that will increase GDP, be of benefit to the country's foreign exchange reserves and develop employment opportunities (Magalasi, 2009:25). The majority of investment incentives come directly and indirectly through the tax system (Magalasi, 2009:25).

The Schedule to the Investment Promotion Act, 1991, notes that "...Malawi offers an array of incentives, which often give new businesses an effective tax holiday for the first several years of operation." On the website of the Malawi Investment Promotion Agency it is stated that "Malawi offers a wide range of tax incentives with the aim of encouraging development, enhancing output, earning or saving foreign exchange, and expanding employment opportunities."

5.2.2.2 Tax incentives must be provided for only in tax legislation

The exemption and partial relief from withholding tax for dividends and royalties respectively in Lesotho is drafted in section 107 of the Income Tax Order. The exemption and partial relief from corporate tax for the taxable income derived from the export of products outside and to the SACU region respectively could not be found in the five Income Tax Acts or the four Income Tax Regulations listed on the website of the Lesotho Revenue Authority. This exemption and partial relief could only be found on the website of the SADC.

The allowances available to registered manufacturers in Namibia in respect of a building cost allowance, employee remuneration and training cost allowance, export allowance and an additional deduction for expenditure incurred in a foreign export country as well as for expenditure incurred in respect of land based transport are drafted in the Income Tax Act, 2002. The exemption from corporate tax to registered manufactures in the EPZ could not be found in the income tax legislation of Namibia. Section 7(2) of the Export Processing Zones Act, 1994, states that an EPZ company shall not be liable to tax under the Income Tax Act, 1981.

The Revenue Authority of Malawi did not list any Income Tax Acts on its website, but the website does state that tax incentives are found in the Taxation Act. This was also noted by Magalasi (2009:25) The building allowance and machinery cost allowance, the pre-operating expenditure, the carry forward of losses, the training cost allowance and the export tax allowance as discussed in Chapter 4 were extracted from the Schedule to the Investment Promotion Act (as administered by the Government of Malawi), 1991, but not from the income tax legislation.

Section 5 of the Investment Promotion Act, 1991, establishes the Malawi Investment Promotion Agency. Section 6(e) of the Investment Promotion Act, 1991, states that the Malawi Investment Promotion Agency shall have the power "to do all such things as the Agency considers being... conducive to the fulfilment of the purposes of the [Investment Promotion] Act..." It could be argued that the Investment Promotion Act, 1991, is fiscal legislation to the extent that the Malawi Investment Promotion Agency is a fiscal department of the Government of Malawi and has the authority to administer the Investment Promotion Act, 1991.

5.3 ARTICLE 4(3) OF THE MOU

Article 4(3)(a) of the MoU lists six factors which are evidence of harmful tax competition. These are zero or low effective rates of tax, lack of transparency, lack of effective exchange of information, restricting tax incentives to particular taxpayers (usually non-residents), promotion of tax incentives as vehicles for tax minimisation or the absence of substantial activity in the jurisdiction to qualify for a tax incentive. This research study is specifically concerned with two of the six factors, namely zero or low

effective rates of tax and restricting tax incentives to particular taxpayers (usually non-residents).

5.3.1 Zero or low effective rates of tax

The taxable income derived by manufacturing companies in Namibia and Lesotho from the export of goods to outside the SACU region is not subject to income tax. Similarly, the taxable income derived by the eight manufacturing companies in Malawi that qualify for EPZ status is also not subject to income tax. This exemption from corporate income tax results in a zero effective rate of tax. Article 4(2) of the MoU stipulates that "tax incentives may include tax privileged EPZ's or enterprise zones." The question that arises is whether the drafters of article 4(2) intended that the tax privileges offered by EPZ's or enterprise zones should include the total exemption from corporate income tax.

In simple terms, an EPZ is a "trade policy instrument [that is] used to promote" the export of non-traditional products (Madani, 1999:11). According to the World Bank, an EPZ offers a firm "free trade conditions and a liberal regulatory environment" (Madani, 1999:11). Usually these zones are set up in underdeveloped parts of the host country and "organized around major seaports, international airports and national frontiers" (Wikipedia, 2012). Kusago et al (1998:5) defines an EPZ as "a clearly delineated industrial estate which constitutes a free trade enclave in the customs and trade regime of a country, and where foreign manufacturing firms producing mainly for export, benefit from a certain number of fiscal and financial incentives." The Business Dictionary defines an EPZ as a:

"Type of free trade zone, set up generally in developing countries by their governments to promote industrial and commercial exports. In addition to providing the benefits of a free trade zone, these zones offer other incentives such as exemptions from certain taxes and business regulations. Also called development economic zone or special economic zone." (Emphasis added.)

Firstly, since the purpose of an EPZ is to promote the export of products and provide a free trade environment, it is expected that the relief from taxes would rather be found in the exemption from indirect taxes such as customs and excise duties that often results

in additional costs to products. It is submitted that the relief from corporate income tax is not as closely associated with "free trade" because it does not have such a direct impact on trade prices as indirect taxes have. It is concluded that a "tax privileged EPZ or enterprise zone" as noted in article 4(2) refers to the tax privileges offered in the form of exemption from customs and excise duties, sales tax and value-added tax.

Secondly, the SACU is a customs union (as opposed to an EPZ) with the primary goal to promote economic development through regional coordination of trade. Its mission statement is *inter alia* to develop common policies and strategies for areas such as trade facilitation, effective customs controls and competition.

Thirdly, according to the Lesotho National Development Corporation the country does not have any conventional EPZ's. In Namibia, for example, the EPZ is not limited to a geographical area and registered manufacturers are allowed to establish their businesses anywhere in the country (Incentives for Investors, 2011). This is contrary to one definition of an EPZ above (see Wikipedia (2012); Kusago et al (1998:5)) which specifically states that an EPZ is a clearly delineated industrial estate which constitutes a free trade enclave in the customs and trade regime of a country.

On the basis of the three arguments above it is submitted that the allowance of a nil corporate tax rate available to certain manufacturers in Lesotho, Namibia and Malawi does not fall within the tax privileged EPZ's or enterprise zones as contemplated by article 4(2). It is therefore submitted that this allowance is evidence of harmful tax competition.

Of all the SADC member states (including Lesotho and Malawi), the allowances available to registered manufacturers in Namibia are the most extensive. In the light of the lower corporate income rate of 18 percent, coupled with the export allowance, there is a possibility that registered manufacturers in Namibia could be subject to a low effective rate of tax.

For example, the gross profit derived by a registered manufacturer in Namibia from the export of goods (excluding fish and meat products) is 70 percent of the total gross profit. If that registered manufacturer has a total taxable income of N\$1 000, then the taxable income derived from the export of manufactured goods is N\$700 (N\$1 000 x

70 percent) for purposes of calculating the export allowance. The export allowance is calculated as N\$560 (N\$700 x 80 percent) and the total taxable income would be reduced by N\$560 to N\$440 (N\$1 000 less N\$560), resulting in an income tax liability of N\$82.80 (N\$460 x 18 percent). If that registered manufacturer had a net profit before tax of N\$1 300, its effective income tax rate would be 6.4 percent (N\$82.80 / N\$1 300). An effective tax rate of 6.4 percent is much lower than the 18 percent tax rate available to registered manufacturers in Namibia and the corporate tax rate of 34 percent for other taxpayers.

This low(er) effective rate of tax is an indicator that the Government of Namibia is engaging in harmful tax competition in respect of its manufacturing industry. Since the lower corporate tax rate of 18 percent is only applicable to registered manufacturers for the first ten years of operation, it could be argued that it is similar to a tax holiday. Article 4(2) states that tax incentives may include tax holidays. If so, then it would not, of itself, be evidence of harmful tax competition as contemplated by article 4(3).

A review of the tax incentives available to manufacturers in Lesotho and Malawi as summarised in Chapter 4 indicated that those incentives would not in the normal course of business lead to a zero or low effective rate of tax.

5.3.2 Restricting tax incentives to particular taxpayers

By its very nature, the tax incentives as discussed in Chapter 4 are restricted to a particular taxpayer, namely manufacturing companies. Article 4(3) does not specify who those particular taxpayers are, but stipulates that it is "usually non-residents". In the absence of any limitation on whom the particular taxpayers are, it could be argued that the tax incentives for manufacturers in Lesotho, Namibia and Malawi fall within the ambit of article 4(3).

It is unlikely that the above argument will prevail. Tax incentives are often used by SADC member states as a means to stimulate economic growth in a specific area, such as mining or farming. This is emphasised in the Tax Policy of the Government of Lesotho which states that "tax incentives are used to nurture specific sectors that are regarded as key or strategic" (Lesotho, 2009:8). In some instances tax incentives are used to compensate for a lack of infrastructure. For that purpose tax legislation of

SADC member states includes various tax incentives restricted to taxpayers in particular industries. It would be impractical and unreasonable to consider that as evidence of harmful tax competition.

It is submitted that the use of the words "usually non-residents" in article 4(3) indicate that the drafters of article 4(3) were specifically referring to the restriction of tax incentives to investments of non-resident taxpayers. Easson et al (2002:16) notes that there are two arguments in favour of extending tax incentives to resident taxpayers as well. Firstly, prejudice towards resident taxpayers "distorts competition." It may limit the growth of local businesses or prevent the expansion of a domestic sector. Secondly, restricting tax incentives exclusively to non-resident taxpayers is in some instances unproductive because it provides the opportunity for resident taxpayers to engage in "round-tripping" and conceal local investment as coming from foreign sources.

5.3.3 Other evidentiary factors

The research study was limited to a discussion and application of two of the six evidentiary factors listed in article 4(3), namely zero or low effective rates of tax and restricting tax incentives to particular taxpayers, usually non-residents. There is an opportunity to conduct further research on the question whether the SADC member states engage in harmful tax competition as may be evidenced by a lack of transparency, lack of effective exchange of information, promotion of tax incentives as vehicles for tax minimisation or the absence of substantial activity in the jurisdiction to qualify for a tax incentive.

5.4 CONCLUSION

In respect of article 4(1) it is concluded that the common approach of the Governments of Lesotho, Namibia and Malawi to the treatment and application of tax incentives to manufacturing companies is to stimulate economic growth and FDI in the manufacturing industry. It was noted that in the case of Malawi tax incentives are not always provided for in tax legislation only but it is also provided for in the Schedule to the Investment Promotion Act (as administered by the Government of Malawi), 1991. In the case of Namibia it was noted that the exemption from corporate income tax for registered manufacturers exporting outside of the SACU region is stipulated in section

7(2) of the Export Processing Zones Act, 1994. This exemption could not be found in the income tax legislation of Namibia.

In this chapter the provisions of article 4(3) are applied to the tax incentives as discussed in Chapter 4. The taxable income for manufacturing companies in Namibia and Lesotho from the export of goods outside the SACU region is not subject to tax. Similarly, the taxable income for eight manufacturing companies in Malawi that qualified for EPZ status is also not subject to income tax. It is concluded that this results in a zero effective rate of tax. Furthermore, the extensive tax incentives available to registered manufacturers in Namibia, specifically the export allowance, could potentially result in a low effective rate of tax. As such, it is concluded that there is an indication that the Governments of Lesotho, Namibia and Malawi are engaging in harmful tax competition to the extent that a zero or low effective rate of tax is evidence thereof. This conclusion is based on the assumption that all other evidentiary factors listed by article 4(3) of the MoU are similar between these states.

It is further concluded that even though the tax incentives are restricted to particular taxpayers, namely manufacturing companies, it does not fall within the ambit of the restriction as contemplated by article 4(3).

Finally, there is an opportunity to conduct further research on the question whether the SADC member states engage in harmful tax competition as may be evidenced by the remaining factors of lack of transparency, lack of effective exchange of information, promotion of tax incentives as vehicles for tax minimisation or the absence of substantial activity in the jurisdiction to qualify for a tax incentive.

CHAPTER 6

CONCLUSION

The conclusions reached in the earlier chapters are summarised in this chapter. The conclusions will be contextualised in relation to the original research objectives set.

The first research objective set was to critically analyse the factors that influence foreign investors' decision to invest in developing countries with specific emphasis on the role of taxation. It is noted that non-tax factors play a dominating role in influencing investment decisions and determining the viability of projects.⁷ Of these factors the policy and regulatory regime of the host country remains the most important. Empirical evidence suggests that the sensitivity of FDI to tax incentives is increasing over time. The most common tax incentive that is introduced by governments to attract FDI is the lowering of the corporate income tax rate.

The second research objective required a critical analysis of the definition of "harmful tax competition" and its role in determining tax policy of developing countries. It was concluded that tax competition is becoming a familiar trend because of the mobility of capital and the ease by which it can move across borders as a result of technological advances. Governments could use investment tax incentives (sometimes to their own detriment) in order to attract FDI from its most effective pre-tax location.

The rise of tax competition necessitated various inter-governmental organisations such as the OECD and the SADC to address the issue. The OECD published the OECD Report in 1998 which is a detailed and elaborative report dealing with *inter alia* the characteristics of tax havens and preferential tax regimes as instances of harmful tax competition within the OECD member states. The SADC published the MoU by listing six factors that are evidence of harmful tax competition. The MoU does not elaborate on these factors, but the factors are similar to some of the factors listed in the OECD Report. It is thus submitted that the meaning of those evidential factors should be interpreted with reference to the OECD Report.

⁷ For purposes of this research study it was assumed that non-tax factors are constant across all member states of the SADC. The focus of the research study was on tax factors only.

Despite the negative publicity surrounding tax competition there are also benefits that stem from it. Most importantly, tax competition encourages governments to allocate resources to the delivery of public goods and services in the most efficient way.

The third research objective set required critical analysis of the corporate tax rates applied by the fifteen member states of the SADC since 2002 until present to manufacturing companies in order to identify SADC member states that offer a preferential corporate tax rate to manufacturing companies. A review of the corporate tax rates available to manufacturing companies indicated that Botswana, Lesotho, Malawi, Namibia and Zimbabwe offers special corporate tax rates for manufacturing companies, subject to certain conditions, such as manufacturing products for an EPZ. The special corporate tax rate for Botswana and Zimbabwe is however not low enough to be considered as giving rise to a "low or zero effective rate of tax" as contemplated by article 4(3) of the MoU. An analysis of the tax incentives of Lesotho, Namibia and Malawi indicated that those countries offer various tax incentives to manufacturing companies in order to stimulate FDI.

The fourth research objective was to critically determine whether the corporate tax rate together with tax incentives specific to manufacturing companies could lead to a zero or low effective rate of tax and/or are restricted to particular taxpayers (usually non-residents) as stipulated by article 4(3) of the MoU. In Chapter 4 an analysis of the investment tax incentives of Lesotho, Namibia and Malawi indicated that those countries offer various investment tax incentives specific to manufacturing companies in order to stimulate FDI.

Chapter 5 provided the application of the provisions of article 4(3) to the investment tax incentives as discussed as part of the fourth research objective. It is concluded that the taxable income for manufacturing companies in Namibia and Lesotho from the export of goods outside the SACU region is not subject to tax. Similarly, the taxable income for eight manufacturing companies in Malawi that qualified for EPZ status is also not subject to income tax. This results in a zero effective rate of tax. Furthermore, the extensive tax incentives available to registered manufacturers in Namibia, specifically the export allowance, could potentially result in a low effective rate of tax. As such, it is concluded that there is an indication that the Governments of Lesotho,

Namibia and Malawi are engaging in harmful tax competition to the extent that a zero or low effective rate of tax is evidence thereof. This conclusion is based on the assumption that all other evidentiary factors listed by article 4(3) of the MoU are similar between these states.

It was further concluded that even though the investment tax incentives are restricted to particular taxpayers, namely manufacturing companies, it does not fall within the ambit of the restriction as contemplated by article 4(3).

The fifth and final research objective was to critically determine whether the corporate tax rates together with the tax incentives as analysed as part of the fourth research objective are provided for only in tax legislation as is required by article 4(1) of the MoU. In respect of article 4(1) it is concluded that the common approach of the Governments of Lesotho, Namibia and Malawi to the treatment and application of tax incentives to manufacturing companies is to stimulate economic growth and FDI in the manufacturing industry. It is noted that in the case of Malawi tax incentives are not always provided for in tax legislation only but it is also provided for in the Schedule to the Investment Promotion Act (as administered by the Government of Malawi), 1991. In the case of Namibia it is noted that the exemption from corporate income tax for registered manufacturers exporting outside of the SACU region is stipulated in the Foreign Investment Act, 1990, but could not be identified in the income tax legislation.

Finally, this research study indicated that three of the fifteen member states of the SADC potentially engage in harmful tax competition in relation to its manufacturing industries as may be evidenced by a zero or low effective rate of tax only. This research study presents the platform for research to be conducted on the question whether those (or any other) SADC member states engage in harmful tax competition as may be evidenced by combining this research with research on the remaining factors of lack of transparency, lack of effective exchange of information, promotion of tax incentives as vehicles for tax minimisation or the absence of substantial activity in the jurisdiction to qualify for a tax incentive.

BIBLIOGRAPHY

Dictionaries/Encyclopaedia

The Business Dictionary, 2011. [Online]. Available:
<http://www.businessdictionary.com/definition/tax-incentive.html> [22 June 2011]

The Business Dictionary. 2011. [Online]. Available:
<http://www.businessdictionary.com/definition/export-processing-zone-EPZ.html> [12 September 2011]

The Concise Oxford Dictionary. 10th ed. 1999. United States: Oxford University Press Inc.

The Free Dictionary by Farlex. 2012. [Online]. Available:
<http://www.thefreedictionary.com/prejudice> [21 January 2012]

WIKIPEDIA. 2011. *The Free Encyclopedia*. [Online]. Available:
http://en.wikipedia.org/wiki/Free_trade_zone [21 January 2012]

Legislation

EXPLANATORY MEMORANDUM TO THE INCOME TAX (AMENDMENT) BILL. 1994. [Online]. Available:
[http://www.lra.org.ls/Downloadable_Docs/Legislation/Tax_Revenue_Acts/IncomeTax/Exp_memorandum/Explanatory%20Memorandum%20to%20the%20Income%20Tax%20\(Amendment\)%20Bill,%20Government%20Notice%20No%2035%20of%201994.pdf](http://www.lra.org.ls/Downloadable_Docs/Legislation/Tax_Revenue_Acts/IncomeTax/Exp_memorandum/Explanatory%20Memorandum%20to%20the%20Income%20Tax%20(Amendment)%20Bill,%20Government%20Notice%20No%2035%20of%201994.pdf) [23 January 2012]

EXPORT PROCESSING ZONES ACT, 1995. *Export Processing Zones, Act 11 of 1995*. [Online]. Available: http://www.malawi-invest.net/docs/investment_guide/investment_policy&legislation/export_processing_zones_act.pdf [6 September 2011]

FOREIGN INVESTMENT ACT, 1990. *Foreign Investment Act, No 27 of 1990*. [Online]. Available: http://www.mti.gov.na/publications/investment_act.pdf [13 September 2011]

INCOME TAX AMENDMENT ACT, 2002. *Income Tax Amendment Act No 7 of 2002*. [Online]. Available:
http://www.commonlii.org/na/legis/num_act/itaa2002196.pdf [11 September 2011]

INCOME TAX ACT, 1993. *Income Tax Act No 9 of 1993*. [Online]. Available:
www.lra.org.ls/Legal.php [30 August 2011]

INVESTMENT PROMOTION ACT, 1991. *The Investment Promotion Act, 1991*. [Online]. Available: <http://www.malawi-invest.net/docs/Downloads/Investment%20Promotion%20Act%20of%201991.pdf> [5 September 2011]

Media articles

MFULA, C. 2010. FDI at record high due to mining, manufacturing booms. *Reuters*. 18 August. [Online]. Available: <http://www.reuters.com/article/2010/08/18/zambia-investment-idUSLDE67H0EF20100818> [13 June 2011]

UN News Centre. 2009. *Foreign direct investment plummeted in early 2009, UN trade arm reports*. 24 June 2009. *UN News Centre*. 24 June. [Online]. Available: <http://www.un.org/apps/news/story.asp?NewsID=31251&Cr=foreign+direct+investment&Cr1=> [7 June 2011]

Books:

HOLMES, K. 2007. *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Taxation*. Amsterdam: IBFD Publications BV

Websites:

ARGENT, J. 2008. *Tax Incentives for Investment in South Africa*. [Online]. Available: http://www.budgetspeechcompetition.co.za/download_files/winners_and_finalists/2008_winning/jonathan_argent.pdf [28 February 2011]

AVI-YONAH, R.S. 2008. *The OECD Harmful Tax Competition Report: A Tenth Anniversary Retrospective*. [Online]. Available: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1194942 [24 June 2011]

BIGGS, P. 2007. *Tax Incentives to Attract FDI*. [Online]. Available: www.ictregulationtoolkit.org/en/Document.3450.pdf [27 May 2011]

BOLNICK, B. 2004. *Effectiveness and Economic Impact of Tax Incentives in the SADC Region*. [Online]. Available: http://www.nathaninc.com/sites/default/files/Effectiveness_and_Economic_Impact_of_Tax_Incentives_in_the_SADC_Region_0.pdf [26 May 2011]

CLARK, W.S. 2000. *Tax Incentives for Foreign Direct Investment: Empirical Evidence on Effects and Alternative Policy Options*. [Online]. Available: http://www.ctf.ca/ctfweb/Documents/PDF/2000ctj/2000ctj4_clark.pdf [27 May 2011]

DA GAMA, A.N.P. 2005. *FDI in Angola: Constraints Encountered by Investors in the Angolan Territory*. [Online]. Available: http://etd.uwc.ac.za/usrfiles/modules/etd/docs/etd_init_4115_1174562136.pdf [13 June 2011]

DABLA-NORRIS, E.; HONDA, J.; LAHRECHE, A.; VERDIER, G. 2010. *FDI Flows to Low-Income Countries: Global Drivers and Growth Implications*. [Online]. Available: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1620251## [4 February 2012]

DEVELOPMENT OF POLICY RESEARCH UNIT UNIVERSITY OF CAPE TOWN ("DPRU"). 2000. *What are the major trends and determinants of foreign direct investment in SADC countries?* [Online]. Available: http://www.commerce.uct.ac.za/Research_Units/DPRU/PBriefsPDF/PDFs/P2.PDF [1 June 2011]

EASSON, Z AND ZOLT, M.N. 2002. *Tax Incentives*. [Online]. Available: <http://siteresources.worldbank.org/INTTPA/Resources/EassonZoltPaper.pdf> [12 September 2011]

EAST AFRICAN CUSTOMS UNION, 2011. *Customs Procedures*. [Online]. Available: http://www.eac.int/customs/index.php?option=com_content&view=article&id=48&Itemid=95 [6 September 2011]

- GREIG, J.A. 1993. *Aspects of interest withholding tax*. [Online]. Available: <http://epublications.bond.edu.au/cgi/viewcontent.cgi?article=1032&context=rlij&sei-redir=1#search=%22aspects%20interest%20withholding%20tax%22> [25 June 2011]
- INCENTIVES FOR INVESTORS, 2011. *The Online Guide to Namibia*. [Online]. Available: <http://www.namibweb.com/tin.htm> [12 September 2011]
- KEEN, M. & SIMONE, A. 2004. *Is Tax Competition Harming Developing Countries More Than Developed?*. [Online]. Available: http://www.taxjustice.net/cms/upload/pdf/Keen_TNI_copyright_tax_competition_developing.pdf [24 June 2011]
- KUSAGO, T AND TZANNATOS, Z. 1998. *Export Processing Zones: In Need of an Update*. [Online]. Available: <http://siteresources.worldbank.org/SOCIALPROTECTION/Resources/SP-Discussion-papers/Labor-Market-DP/9802.pdf> [13 September 2011]
- LEGWAILA, T. 2010. *The Suitability of the South African Corporate Tax Regime for the Use of South African Resident Intermediary Holding Companies*. [Online]. Available: <http://upetd.up.ac.za/thesis/available/etd-05222010-170510/unrestricted/00front.pdf> [24 June 2011]
- LESOTHO NATIONAL DEVELOPMENT CORPORATION, 2011. *Incentives*. [Online]. Available: <http://www.lndc.org.ls/Incentives.htm> [12 September 2011]
- LESOTHO. Department of Finance and Development Planning. 2009. *Tax Policy of the Government of Lesotho*. [Online]. Available: http://www.finance.gov.ls/data/National_Tax_Policyv2_2.pdf [2 April 2011]
- MADANI, D. 1999. *A Review of the Role and Impact of Export Processing Zones*. [Online]. Available: <http://siteresources.worldbank.org/INTRANETTRADE/Resources/MadaniEPZ.pdf> [13 September 2011]
- MAGALASI, C. 2009. *Unmasking the Malawi Taxation System*. [Online]. Available: <http://somo.nl/dossiers-en/economic-reform/tax-justice/tj/documents/unmasking-the-malawi-taxation-system> [16 September 2011]
- MALAWI INVESTMENT PROMOTION AGENCY, 2011. *Investment Opportunities in Malawi*. [Online]. Available: http://www.malawi-invest.net/inves_opp.html [12 August 2011]
- MALAWI REVENUE AUTHORITY, 2011. *Malawi Revenue Authority website*. [Online]. Available: http://www.mra.mw/it_companies.php [12 August 2011]
- MHLANGA, N; BLALOCK, G and CHRISTY, R. 2009. *Understanding Foreign Direct Investment in the Southern African Development Community: An Analysis Based on Project-Level Data*. [Online]. Available: [http://ageconsearch.umn.edu/bitstream/51632/2/FDI%20in%20SADC%20IAAE%20Contributed%20Paper\(693\)-IAAE09.pdf](http://ageconsearch.umn.edu/bitstream/51632/2/FDI%20in%20SADC%20IAAE%20Contributed%20Paper(693)-IAAE09.pdf) [1 June 2011]
- MINISTRY OF TRADE AND INDUSTRY OF NAMIBIA, 2011. *Incentives*. [Online]. Available: <http://www.mti.gov.na/subpage.php?linkNo=22> [16 September 2011]
- MINISTRY OF TRADE AND INDUSTRY REPUBLIC OF NAMIBIA, 2011. *Ministry of Trade and Industry Republic of Namibia website*. [Online]. Available: <http://www.mti.gov.na/subpage.php?linkNo=80> [24 August 2011]

MINTZ, J. M. 2004. *The Changing Structure of Tax Policies for Foreign Direct Investment in Developing Countries*. [Online]. Available: http://aysps.gsu.edu/isp/files/ISP_CONFERENCE_TAX_REFORM_MINTZ_PAPER.pdf [25 June 2011]

MURADZIKWA, S. 2002. *Foreign Investment in SADC*. [Online]. Available: <http://allafrica.com/download/resource/main/main/idatcs/00010104:f68f647cb249e50b52f1f7016d0a6498.pdf> [1 June 2011]

MWILIMA, N. 2003. *Foreign Direct Investment in Africa*. [Online]. Available: http://www.sarpn.org.za/documents/d0000883/P994-African_Social_Observatory_PilotProject_FDI.pdf [28 February 2011]

OGUTTU, A.W. 2010. *A Critique on the OECD Campaign Against Tax Havens: Has It Been Successful? A South African Perspective*. [Online]. Available: http://search.sabinet.co.za/WebZ/Authorize?sessionid=0&bad=ejour/ejour_badsearch.html&portal=ejournal&next=images/ejour/ju_slr/ju_slr_v21_n1_a10.pdf [23 July 2011]

ORGANISATION FOR ECONOMIC COOPERATION AND DEVELOPMENT ("OECD"). 1998. *Harmful Tax Competition: An Emerging Global Issue*. [Online]. Available: <http://www.oecd.org/dataoecd/33/0/1904176.pdf> [22 June 2011]

PwC. 2011. *Worldwide Tax Summaries*. [Online]. Available: <http://taxsummaries.pwc.com/uk/taxsummaries/wwts.nsf/ID/PPAA-85RDKF> [4 August 2011]

ROHÁČ, D. 2010. *Tax competition: A curse or a blessing?* [Online]. Available: <http://www.taxcompetition.org/articles/tax-competition-blessing> [22 June 2011]

RUSIKI, T.G. 2007. *Trends and determinants of inward foreign direct investment to South Africa*. [Online]. Available: <http://eprints.ru.ac.za/1124/1/Rusike-MCom-2008.pdf> [13 June 2011]

STRETCH, R & SILKE, J. 2000. *SARS and SADC Tax Co-ordination*. [Online]. Available: [http://za-zatlxn001:8090/nxt/gateway.dll?f=templates\\$fn=default.htm\\$vid=mylnb:10.1048/enu](http://za-zatlxn001:8090/nxt/gateway.dll?f=templates$fn=default.htm$vid=mylnb:10.1048/enu) [21 June 2011]

TANZI, V. AND HOWELL, H.Z. 2000. *Tax Policy for Emerging Markets: Developing Countries*. [Online]. Available: <http://www.imf.org/external/pubs/ft/wp/2000/wp0035.pdf> [21 June 2011]

TEATHER, R. 2005. *The Benefits of Tax Competition*. [Online]. Available: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=878438 [22 June 2011]

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT. 2003. [Online]. Available: *Investment Policy Review Lesotho*. http://www.unctad.org/en/docs/iteipc20034_en.pdf [3 March 2011]

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT (UNCTAD). 2007. *Foreign Direct Investment Reached New Record in 2007*. [Online]. Available: <http://www.unctad.org/templates/webflyer.asp?docid=9439&intItemID=1528&lang=1> [7 June 2011]

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT ("UNCTAD"). 2009. *Slow recovery in FDI expected in 2010; more substantial rebound due in 2011, UNCTAD survey reveals*. [Online]. Available: <http://www.unctad.org/templates/Webflyer.asp?docID=11802&intItemID=1528&lang=1> [7 June 2011]

WALSH, J.P. AND JIANGYAN, Y. 2010. *Determinants of Foreign Direct Investment: A Sectoral and Institutional Approach*. [Online]. Available: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1662260 [6 February 2012]

WORLD BANK DATA, 2011. *Data Indicators*. [Online]. Available: <http://data.worldbank.org> [22 March 2011]

WORLD BANK GROUP MULTILATERAL INVESTMENT GUARANTEE AGENCY. 2007. *Snapshot Africa – Lesotho Benchmarking FDI Competitiveness*. [Online] Available: http://www.fdi.net/documents/WorldBank/databases/snapshot_africa/docs/snapshot_africa_lesotho.pdf [9 March 2011]

ZAMPINI, D. 2008. *Developing a Balanced Framework for Foreign Direct Investment in the SADC: A Decent Work Perspective*. [Online]. Available: http://www.tralac.org/cause_data/images/1694/MRI2008Chapter5Zampini.pdf [22 July 2011]

University of Cape Town