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MASTERS IN TAX LAW

A CRITICAL ANALYSIS OF THE TANZANIA INCOME TAX ACT, 2004 ON RESOLVING INTERNATIONAL DISPUTES RELATING TO TAXATION.

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STATEMENT

Research dissertation presented for the approval of Senate in fulfilment of part of the requirements for the Masters in Tax Law in approved courses and a minor dissertation. The other part of the requirement for this qualification was the completion of a programme of courses.

I hereby declare that I have read and understood the regulations governing the submission of Masters in Tax Law dissertations, including those relating to length and plagiarism, as contained in the rules of this University, and that this dissertation conforms to those regulations.

Signed by candidate

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MSSSAL002

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CHAPTER ONE

INTRODUCTION

1.1 Background to the Problem

Over the last eight years, the Tanzanian business climate has improved and its economic growth over the period of 2000 to 2007 range is an average of 7 per cent.[1] The economic growth is the result of 1990s economic globalization and economic liberalisation programme pledge by the Tanzanian government through its economic policy during those times. As a result, Tanzania is among the African countries with the fastest growing economies in the world thus a target for foreign investments.[2]

The economic liberalisation of early 1990s[3] and economic integrations with other countries on trade, has made it possible for Tanzania to receive foreign investments from other countries and at the same time the income wealth from individuals and business entities have flowed out of Tanzania to other countries.[4]

Due to these economic developments and cross-border transactions, the Tanzanian tax system like any other state is forced to design an 'effective international tax system that considers a range of income flows and wealth that will ensure an individual or company do not bypass its tax system in way that the country will not allow.'[5] In most cases, this is where the challenge comes.

As a result of many of these cross-border transactions, the matter of how and when a country is entitled to collect its revenue once a tax liability is confirmed becomes a matter of delicacy that may even lead

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[1] NE Mkono & OA Tetteh-Kujorjie 'Tanzania' in T Sanders (ed) *The Inward Investment and International Taxation Review* 3ed (2003) 578.
[2] Ibid.
[3] Ibid.
[4] A Lymer & J Hasseldine *The International Taxation System* (2002) 5.
[5] Lymer & Hassedline op cit (n4) 12.

to international tax disputes due to the lack of their operational arrangements.

Many of these cross-border transactions involve multinational firms and companies which requires these companies to locate operations in Tanzania.[6] The collection of the tax revenue arising from the profits generated by these transactions has become a serious challenge to the Tanzanian tax administration.[7] The challenges arises when tax may be imposed on these multinationals in other jurisdictions, for example, their state of residence. The result is international double taxation and tax disputes.

With the rise of international double taxation and tax disputes, harmonisation to remove tension between countries is required.[8] Therefore, many sovereign states including Tanzania have developed mechanisms of controlling the situation by making sure that international double taxation is either prevented or eliminated through the use of domestic tax laws, treaties and other international instruments.[9]

1.2 Statement of the Problem.

The research paper is focused on one area of international tax dispute which is international double taxation. The problem to be examined is how the Tanzanian Income Tax Act no. 11 of 2004[10] (hereinafter referred to the Income Tax Act) as a domestic tax law resolves international double taxation issues alongside methods offered under the double taxation agreements that Tanzania has concluded.

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[6] JR Hines *International Taxation and Multination Activity* (2001) 1.

[7] Ibid.

[8] C Read 'The Evolution of International Taxation' in C Read & GN Gregoriou (eds) *International Taxation Handbook: Policy, Practice, Standards & Regulation* 1ed (2007) 5.

[9] Ibid.

[10] The Income Tax Act 11 of 2004.

1.3 Aim and Objective of the Research

The study intends to make an inquiry on whether the Income Tax Act as a domestic tax law is capable of resolving international double taxation by looking at the methods that it uses. It also aim at ascertaining if the Income Tax Act or the double taxation agreement is effective on alleviating international double taxation.

1.4 Scope and Methodology of the Research

The research is based on a critical analysis of the Income Tax Act and how it resolves the issue of international double taxation. The focus point will be on the types of relief it offers.

The approach will be analytical and comparative, one that will start by discussing the concept of international taxation and international double taxation followed by the legal framework of the Tanzanian tax system, the analysis of the relevant provisions of the Income Tax Act and methods used to resolve international double taxation in relation to different international double taxation treaties that Tanzania has entered with other sovereign states. In addition, the position of the law where no tax treaty has been entered into with the state of residence of a taxpayer will be considered.

1.5 Research outline

In achieving the aim of this research, the paper will consist of five chapters.

Chapter one focuses mainly on the introduction, which gives an overview of what the research is about. The chapter addresses issues of background, statement of the problem, methodology and objectives of the study.

Chapter two discusses international taxation and international double taxation. The chapter further explains different ways that international double taxation arises and how it is prevented.

Chapter three focuses on the analysis of methods used by the Income Tax Act on resolving international double taxation. The chapter will start by looking at the historical background of Tanzanian legal framework on its tax system, structure and administration.

Chapter four analyses methods of relief used under double taxation agreements concluded by Tanzania.

Chapter five is the conclusion. This chapter briefly analyses the findings of the research. In addition, recommendations will be provided on way the forward.

CHAPTER TWO

INTERNATIONAL TAXATION AND INTERNATIONAL DOUBLE TAXATION

2.1 Introduction

The growth of cross-border transactions and investments has led to countries to develop a highly national tax systems to cater for their existence because countries have no restrictions to implement taxes on their jurisdictions. The same implies to international tax law to impose restrictions to national fiscal laws on how revenue is collected on cross- border activities. For that reason, the issue of international taxation is of more concern and needs more understanding on how tax revenue is imposed and allocated among prospective countries.

This chapter explains the concept of international taxation in a general perspective and how international tax disputes arise and are resolved.

2.2 International Taxation

Due to interconnected nature of the global economy, the main question under international taxation is the extent to which a country has the right to tax a foreign individual or company. This poses a challenge in taxation when considering how to tax foreign individuals or corporations, given the fact that there are no definite international rules to govern the flexibility of a sovereign nation's usage of its tax code within its jurisdiction.

International taxation is defined by Michael Kobetsky[11] as taxation of cross-border transactions or activities that deals with taxation of both residents (individuals and companies) deriving foreign income and non-residents deriving income that has a source within a country.[12]

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[11] M Kobetsky *International Taxation of Permanent Establishment: Principles and Policy* (2011).

[12] Kobetsky op cit (n11) 11 to13.

Moreover, according to him, at international level, the principle of taxation can only be on the basis of residence and source principle.[13] In that regard, the principle requires a resident taxpayer to have a nexus with a particular country that will tax him on his world-wide income while taxation of income derived from a source country will be considered to a non-residents who has a nexus with the country that provided the said of income within its jurisdiction.

Miller and Oats[14] consider international taxation to be international tax laws with both international rules of customary law and international agreements.[15] Because of the consistency of these international norms, the law (international tax law) tends to cover the right of a states to impose taxes on foreign incomes and at the same time providing for a dispute settlement mechanism through tax treaties for clearance of the right to tax between respective states where the right to tax is not clear[16] or where there is jurisdictional conflict.

In that case, international taxation comprises of rules that determines how taxpayers trading in cross-broader will pay tax by examining when and how tax will be paid once liability is confirmed.[17]

2.3 International Tax Disputes

There is no a direct definition of the term or concept 'international tax disputes' but in all circumstances, international tax disputes are the result of tax jurisdiction conflicts which is the central principle of international taxation as it gives states taxing rights.

Under international taxation, the right of jurisdiction of states to tax is an important criteria that is based on the principle of territoriality[18]

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[13] Ibid.

[14] A Miller & L Oats *Principles of International Taxation* 3ed (2012).
[15] Miller & Oats Op cit (n14) 22.
[16] Ibid.
[17] Lymer & Hasseldine op cit (n4) 2.
[18] J Monsenego *Taxation of Foreign Business Income within the European Internal Market* (2012) 45 to 46.

and world-wide taxation[19] which are source and residence. Though it is utmost important, there are no rules under international tax law that stipulates limitations on how a national tax jurisdiction cannot go beyond in collecting taxes at the same time empowering a nation to enjoy its sovereignty in imposing taxes.[20] The lack of these limitations lead conflicts between national jurisdictions.

'Where there are mismatches between national tax laws, the jurisdiction conflicts can be exacerbated...'[21] because of the principle of territoriality[22] and worldwide taxation,[23] which gives two or more sovereign states with concurrent jurisdiction under international tax law to have legal rights to impose tax[24] on the same taxable event.[25] That is to say, tax is imposed on the same taxable activity by the source country and residence country.[26]

Under the source country, the country's right to impose tax or taxes is exercised on the taxpayer's taxable activities that are exercised within the country or on the property producing the taxable income if the same is situated within the country.[27] On the other hand, under the residence country, tax is imposed on the taxpayer (individual or companies) who is a resident deriving taxable income or is the owner of the property that generates taxable income that have its residence or domicile within his residence country.[28]

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[19] L Olivier & M Honiball *International Tax: A South African Perspective 5ed (2011) 2 to 3.*
[20] A Nizamiev *The Main Characteristics of State's Jurisdiction to Tax in International Dimension* LLM (Georgia) (2003) 40.
[21] United Nations Conference on Trade and Development: Taxation, UNCTAD Series on Issues in International Investment Agreement, United Nations, New York and Geneva, 2000, available at *http://www.unctad.org/en/docs/iteiit16_en.pdf*, accessed on 1 April 2014.
[22] Monsenego op cit (n18) 45 to 46.
[23] Olivier op cit (n119) 2 to 3.
[24] Nizamiev op cit (n20) 41.
[25] United Nations Conference on Trade and Development: Taxation, UNCTAD Series on Issues in International Investment Agreement op cit (n21) 11 to 20.
[26] United Nations Conference on Trade and Development: Taxation, UNCTAD Series on Issues in International Investment Agreement op cit (n21) 20.
[27] Ibid.
[28] Ibid.

It is self-evident that, elimination of tax jurisdiction conflicts is done through national tax law or tax treaties[29] concluded by states; such as bilateral treaties (involving two states) and sometimes multilateral treaties (involving more than two states).[30] Although most treaties have provided guidelines on the way forward in solving double taxation, conflicts still exists and states are becoming more concerned on arising issue of erosion of tax base. It has becomes a new issue in international tax law because of the continuance applications of the principles of jurisdiction to tax (source and residence principles)[31] while the question of who should bear the burden of relief remain with no answer.[32] Based on the above discussion, the dispute to be discussed for the purpose of this research paper is international double taxation.

2.4 International Double Taxation in General

Where there is an engagement of taxpayer in cross-border transactions, there is a likelihood of his income to be taxed more than once in different tax jurisdiction. In that situation, where income is taxed twice, international double taxation is said to have occurred.

In a plain English, double taxation is a situation where the same income and the same person is taxed more than once and at international level, double taxation or sometimes referd to international double taxation is defined to mean a situation where two or more sovereign states asserts to tax the same income generated by a taxpayer in cross-border transaction.

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[29] United Nations Conference on Trade and Development: Taxation, UNCTAD Series on Issues in International Investment Agreement op cit (n21) 17.
[30] Ibid.
[31] FDAM Luoga *A Sourcebook of Income Tax Law in Tanzania* (2000) 163.
[32] Ibid.

Lymer and Hasseldine, have define international double taxation to be a situation where tax base is taxed more than once as a result of applying both residency and source principles of taxation.[33]

Page 21 of the UNCTD[34] define international double taxation to be a situation where two or more sovereign states with concurrent tax jurisdiction to exercise their taxing rights to the same income of a taxpayer by the base of either source or residence principles without giving regards to any sort of relief to the other state.

It can therefore be said, international double taxation is result of conflicts of tax jurisdiction which are based on the principle of source and residence jurisdiction.[35] Authors of international tax law such as Mogens Rasmussen[36] and many more have given different demonstrations on how international double taxation occurs.

Basing on his theory, the occurrence of international double taxation is categorized into two categories; juridical international double taxation and economic international double taxation.[37]

Koker[38] and Holmes[39] have both defined juridical international double taxation to be taxation of income of the same taxpayer more than once by two or more sovereign states having the same right to tax while, economic international double taxation arises where different taxpayers are being taxed by more states on the same income.[40]

In most occasions when it comes to international double taxation disputes, juridical international double taxation carries a lot of

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[33] Lymer & Hasseldine op cit (n4) 7.

[34] United Nations Conference on Trade and Development: Taxation, UNCTAD Series on Issues in International Investment Agreement op cit (n21) 58.

[35] Ibid.

[36] M Rasmussen *International Double Taxation* (2011).

[37] Rasmussen op cit (n35) 1 to 2.

[38] AD Koker *Silke on International Tax* 12.6 (online book).

[39] K Holmes *International Tax Policy & Double Tax Treaties: An Introduction to Principles and Application* (2007) 22.

[40] Koker op cit (n37) 12.6

magnitude on the issue. The reason as to why it's of great magnitude is because of how it raises conflicts over tax jurisdiction and "...Its harmful effects on the exchange of goods and services and movements of capital, technology and persons..."[41] Under juridical double taxation, international double taxation can arise in the following ways; through source conflicts, dual residence conflicts and residence- source conflicts.[42]

2.4.1 Source Conflicts

Source conflicts are the results of two or more states assert to have equal jurisdiction to tax over a transaction.[43] It happens that, the two states in accordance with their tax systems and national tax laws, have the rights to tax the income generated by a taxpayer from a source within either of the states.[44]

Under this situation, the right to impose tax or taxes on taxpayers who are both resident and non-residents[45] becomes a matter of entitlement as each states claim to have the said entitled right.[46] And because of this right, taxpayers are left in a position of suffering double taxation on their income.

2.4.1 Dual Residence Conflicts

Dual residence conflicts also referred to residence-residence conflict is one among the factor that causes international double taxation under the juridical double taxation. It occurs where there more than two sovereign states under their national tax laws claim that a taxpayer in issue is a resident of their country.[47]

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[41] Holmes op cit (n38) 22

[42] Ibid.

[43] Luoga op cit (n31) 164.
[44] Holmes op cit (n38) 23.
[45] Olivier & Honiball op cit (n19) 52.

[46] Holmes op cit (n38) 22.
[47] L Riccardi *Chinese Tax Law & International Treaties* (2013) 75.

The dual residence conflicts normally occur to individual taxpayers and companies.[48] It might happen that the same taxpayer has equal connection between two countries. For example, a situation where a taxpayer is a company, dual residence arises where the company is incorporated in Tanzania and considered to be a Tanzanian taxpayer at the same time being manage and controlled (place of effective management) in South Africa.[49] And as for the case of individual taxpayers, dual residence arises where an individual taxpayer domicile in one country but also during his year of income spends time working in another country.[50]

Under the two situations, the taxpayer has established a link between the two countries and as a result of that link, each country claims to have a right of imposing tax[51] on the taxpayer's generated income on the basis of world-wide income tax as the principle of residency suggests.

2.4.3 Residence-Source Conflict

Residence-source conflict is a situation where a taxpayer is being taxed twice by two or more countries on different occasion but on the same income he generated. That is, one country assert to tax his income by being a resident of the country[52] while the other country asserts to have the right to tax the same income by claiming it was generated from the source of the said country.[53]

From the above aspects, international double taxation will arise if both countries decides to tax the taxpayer's income under the basis of source and residence.[54]

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[48] Luoga op cit (n31) 164.
[49] Holmes op cit (n38) 23.
[50] Luoga op cit (n31) 164.
[51] Holmes op cit (n38) 25.
[52] Riccardi op cit (n47) 76.
[53] Ibid.
[54] Luoga op cit (n31) 165.

Although the above discussed factors are the main cause of juridical double taxation, there also are other factors that may result to international double taxation. They include, the setting of how a country can determine the concept of arm's length is to be interpreted on cross-border transactions[55] or in other occasion how income is being defined and determined by other countries.[56]

The aforesaid facts makes international double taxation unacceptable because it impedes cross-border trade with countries tax jurisdictions as it violates a natural balance of accounts and could serve as a disincentive to pay taxes for otherwise law abiding taxpayers. For that reason, countries have taken different measures to relieve international double taxation.

In general, regardless of whose tax jurisdiction, measures to relieve international double taxation are done through countries domestic tax laws, treaties and other international instruments. As for the treaties, countries may choose to enter into them to prevent the rise of it.

2.5 Eliminating International Double Taxation

International double taxation is a global phenomenon that countries desires to resolve on both domestic and international levels. On international level, the desire of avoiding and eliminating international double taxation can be traced back in 1920s when the United Nation and the League of Nations came into being after the end of World War One[57] with the aim of having free trade among countries.

The promotion of free trade on international level suggested by the United Nations Committee and the League of Nationals led to the formation of both Organisation for Economic Co-operation and

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[55] Riccardi op cit (n47) 76.
[56] Ibid.
[57] F Pötgens *Income from International Private Employment* (2006) 15 to 21.

Development (OECD) and the United Nations (UN) Tax Models as Models to be followed by countries as guidelines in avoiding and eliminating international double taxation.[58]

According to the two Models, two methods of eliminating international double taxation are provided; tax credit and tax exemption as reliefs to a taxpayer's income that might suffer double taxation as a result of cross-border transactions. The two methods will be discussed in general in this chapter.

However, there are several ways of eliminating international double taxation but the most common method preferred are through the use of treaties and domestic tax law[59]. Reliefs provided under domestic tax law are unilateral reliefs that will be further discussed in chapter three in relation to Tanzanian Income Tax Act.

Depending on the choice of the contracting states, treaties for eliminating international double taxation can be concluded either in bilateral or multilateral; though the bilateral treaties are the most preferable one, but in general all treaties aim in yielding the same results.

Whatever methods chosen to eliminate international double taxation, the aim is to provide reliefs to a taxpayer suffering or being a victim of international double taxation and the country's tax system in general. The methods used by these treaties to provide reliefs are within the guideline of either the OECD Model or the UN Model, they include; tax exemption, tax credit and tax deduction though not provided under the Models but countries use it anyway.[60] Each relief serves a purpose to a taxpayer and it is applicable in different situation depending on what caused the double tax.

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[58] Luoga op cit (n31) 172.

[59] Olivier & Honiball op cit (n19) 6.

[60] Luoga op cit (n31) 166 to170.

2.5.1 Tax Exemption Relief

Both OECD Model and UN Tax Models[61] requires tax exemption to be offered by taxpayer's resident country on income derived or capital owned from foreign sources.

Therefore, tax exemption relief is given to taxpayers by their resident countries as a method of eliminating source-residence conflict[62] as well as dual residence conflict. Under this relief, international double taxation is eliminated by giving jurisdictional taxing rights to the country of source.[63] That is, tax is imposed on local income only[64] by exempting income accrued from foreign sources.[65] And since tax is imposed on territorial basis by taxpayer's country of resident,[66] the country has an option of either granting a full or limited tax exemption.

By offering full tax exemption, the resident country of the taxpayer excludes all of its foreign source income[67] and upon making its tax liability, the rate applicable will be the usual domestic tax rate.[68] In doing so, the resident country will be said to have offered its resident taxpayer a full tax exemption that separates its domestic income from foreign source income.[69] But it should be noted that, full tax exemption is different from exemption with progression.

Exemption with progression is only used a method of determining tax rate to a taxpayer by his resident country.[70] The resident country

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[61] Article 23A (1) of the OECD Model Tax Convention on Income and Capital of 2010 and The United Nations Model Double Taxation Convention between Developed and Developing Countries of 2011.

[62] Holmes op cit (n38) 25.

[63] BJ Arnold & MJ McIntyre *International Tax Primer* 2ed (2002) 3.

[64] Holmes op cit (n38) 25.

[65] Olivier & Honiball op cit (n19) 6.

[66] Arnold & McIntyre op cit (n63) 33.

[67] Holmes op cit (n38) 25.

[68] Ibid.

[69] Ibid.

[70] Arnold & McIntyre op cit (n63) 34.

uses the exempted foreign source income to determine the rate of tax to be imposed to taxpayer's none exempted taxable incomes[71] with the aim of finding the average tax rate which would have been used if foreign source income were to be taxed in the resident country[72] and also used as a way of imposing high rates on its domestic income while making sure there is no distortion of tax exemption relief.[73]

Apart from exemption with progression being complex to tax authority as it requires them to get information from foreign source countries on the amount of income their resident taxpayers accrue,[74] the exemption method is easy to administer especially for developing countries and is effective in eliminating international double taxation.[75]

2.5.2 Tax Credit

Tax credit is another method required under both OECD Model and UN Tax Models to be provided for to the taxpayer. Under their Articles 23B (1), they require taxpayer's resident country to allow a deduction from taxpayer's local income; an amount equal to the income paid in the foreign state.

Where there is residence-source conflict over the same income generated by the same taxpayer, the two states are allowed to impose taxes on such income however, tax credit relief will be given to the taxpayer by its resident country.[76] Under this relief, the taxpayer's country of residence will impose tax on all foreign income but at the same time allows deduction to be made on its local income accrued worldwide.[77]

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[71] Ibid.

[72] Ibid.

[73] Holmes op cit (n38) 27.

[74] Arnold & McIntyre op cit (n63) 34.

[75] Holmes op cit (n38) 28.

[76] Arnold & McIntyre op cit (n62) 30.

[77] Holmes op cit (n38) 28.

It can either be given in full or limited (ordinary credit). Full tax credit reduces the whole amount of tax paid by resident taxpayer by deducting the tax paid to foreign source by its resident country[78] while ordinary tax credit (limited tax credit) uses tax rate deduction an amount that shall not exceed the income tax rate that is due on income that is taxed in the source country.[79] That is to say, tax credit as a relief of alleviating international double taxation will depend on the tax rate of the two countries in conflict.[80]

2.5.3 Tax Deduction

Under this method, the taxpayer's country of residence taxes both domestic source income and foreign source income but at the same time allows the resident taxpayer to claim for deduction of its foreign income[81] as it is considered to be business cost[82] or current expenses on earning foreign income.[83]

Tax deduction as a method of eliminating international double taxation is mostly used in countries with low tax rates on their world-wide taxes on their resident taxpayers.[84] The method has proved to be less effective on eliminating international double taxation especially the residence-source conflict.[85]

2.6 Conclusion

As seen above, the chapter has address the concept of international taxation and how different international transactions or activities can result into disputes and the same being resolved.

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[78] Holmes op cit (n38) 28.

[79] Rasmussen op cit (n35) 5.

[80] Ibid.

[81] Holmes op cit (n38) 34.

[82] Luoga op cit (n31) 168.

[83] Arnold & McIntyre op cit (n62) 30.

[84] Ibid.

[85] Holmes op cit (n38) 34 to 35.

The reliefs offered under international taxation as methods of relieving international double taxation are the results of the OECD Tax Model and UN Tax Model. Both Models requires only two reliefs to be offered when there is international double taxation; tax exemption and tax credit because they are the most desired methods than tax deduction method although countries uses it as one among the reliefs under its domestic law.

The rationale shown by these two Tax Models on the said methods is that, the two methods completely relieve international double taxation; for example, if full exemption or credit is provided, international double taxation is completely relieved or where the tax rates allowed are limited on both exemption or credit.

CHAPTER THREE

INTERNATIONAL DOUBLE TAXATION UNDER THE INCOME TAX ACT.

3.1 Introduction

Many authors of international tax suggests the increase of cross-border transactions has made international double taxation to be one of the central problem in international taxation[86] that sovereign states are facing including Tanzania. For this reason, Tanzania under its Income Tax Act and the whole tax system has managed to implement unilateral reliefs as a method of resolving the international double taxation.

This chapter is intended to look on the analysis of unilateral reliefs offered by the Income Tax Act as a method of relieving international double taxation. It will start by looking at the historical background of the Tanzanian tax system and further understanding on how disputes are settled between the taxpayers and tax officials; in order to make a link on how taxes are payable after reliefs are offered.

3.2 Historical Background of the Tanzanian Tax System

Tanzanian tax system is designed in three taxing distribution categories[87] which includes tax unit that signifies who is to be taxed, what is to be taxed as a tax base and the tax structures on how and why taxpayers are to be taxed.[88] This kind of a system is the result of

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[86] Lymer and Hasseldine op cit (n4) 50.

[87] Luoga op cit (n31) 10.

[88] Luoga op cit (n31) 10 to 21.

both direct and indirect taxes[89] imposed by the government serve as a major source of Tanzanian revenue among other sources.[90]

The system was introduced in early 1920s by the British colony after the fall of the German rule in 1919 at the end of World War One.[91] It was in 1940 where the British introduced income tax under the Colonial Income Tax Ordinance that tax was, for the first, levied on import and excise duties, because no income taxes were imposed due to the low income of Tanzanian citizen.[92]

After the independence of 1961, Tanzania for the first time introduced its own Income Tax Act of 1973.[93] This Act repealed and replaced the Income Tax Act of 1971 used by it when it was still a member of East African Community.[94] But due to economic and liberalisation programmes introduced by the government in early 1990s,[95] it became difficult to the use the Income Tax Act, 1973 because it was not effective. As a results, the new and the current Income Tax Act was enacted. This latter Act has been subject to revisions from time to time.

3.3 The Legal Framework

In Tanzania, income is levied under the Income Act, an Act enacted 'to make provision for the charge, assessment and collection of Income Tax for the ascertainment of the income to be charged and for matters incidental thereto'.[96] The Act is the main authority when it

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[89] P Kasser 'Presentation by the Commissioner for Large Tax Payers of the Tanzanian Revenue Authority' *Tanzania Investment Forum*, 30 October 2006, available at *http://www. invest-in.tanzania.ru/downloads/TAXATION%20IN%20TANZANIA.pdf*, accessed on 10 April 2014.

[90] *http://www.mof.go.tz/index.php?option=com_content&view=article&id=37:revenue-a-taxation_policy&itemid=53*, accessed on 10 April 2014.

[91] Luoga op cit (n31) 3.

[92] Ibid.

[93] Luoga op cit (n31) 5.

[94] Ibid.

[95] Mkono & Tettech-Kujorjie op cit (n1) 578.

[96] The preamble of the Income Tax Act 11 of 2004.

comes to income tax matters and it is applicable to both Tanzania mainland and Tanzania Zanzibar.[97]

According to the Income Act, income tax is levied on both individuals and companies[98] where tax is charged on taxable income accrued worldwide to all residents and on income derived by non- residents from a source within Tanzania.[99] As for corporations to become Tanzanian residents, such corporations must be incorporated under the Tanzania's Companies Act Chapter 212 of 2002 or by any time during the year of income, their management and control of their affairs were exercised in the country.[100]

Therefore, total income of a resident taxpayer is levied from on world-wide (sources) income while income tax is levied on non-residents on income derived strictly from sources within Tanzania.

3.4 Income Tax Base its Calculations and Payments

The Constitution of United Republic of Tanzania, 1977 (amended time to time) hereinafter referred to as the Constitution of Tanzania, stipulates that, no person is required to pay any amount of tax other than that stated by the law itself.[101] In this case, income tax under the Income Act is levied on individual gains or profits accrued from employment,[102] business[103] or investment (income tax bases)[104] on both residents and non-residents.

Under the provision of section 5 of the Income Tax Act, out of these income tax bases, a calculation shall be done on the total sum of income of a person's chargeable income from the year of income less allowable reductions.[105] These calculations process are done by the

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[97] Section 2 of the Income Tax Act 11 of 2004.
[98] Section 3 of the Income Tax Act 11 of 2004.
[99] Section 6(1)(a) and (b) of the Income Tax Act 11 of 2004.
[100] Section 66(4 (b) Income Tax Act 11 0f 2004.
[101] Article 138(1) of the Constitution of United Republic of Tanzania, 1977 (amended time to time).
[102] Section 7 of the Income Tax Act 11 of 2004.
[103] Section 8 of the Income Tax Act 11 0f 2004.
[104] Section 9 of the Income Tax Act 11 of 2004.
[105] Section 5 of the Income Tax Act 11 of 2004.

taxpayer themselves under the requirement of the Income Tax Act which provides for three methods that payments of income tax can be done. The methods includes income tax payable by withholding, income tax payable by instalment and income tax payable on assessment.[106]

3.4.1 Income Tax Payable by Withholding

Withholding taxes are covered under the provisions of sections 81 82 and 83 of the Income Tax Act. The section 81 covers withholding tax from employment. The section provides for an obligation to a resident employer to withhold income tax of its employees. According to the section, withholding of income tax is done on the natural person who accrues income from employment and its collection is through PAYE (pay as you earn) in a specified tax rate provided for under paragraph 4(1) of the First Schedule to the Income Tax Act.

At the same time income is withheld from investment as per section 82 of the Act by a person[107] if the said income is from investment paid by resident person in terms of dividend, interest, natural resource payment, rent or royalty with the source within Tanzania[108] and it is not withheld under the provision of section 81 of the same Act.

Lastly, income tax is withheld by a resident person from payments of service fees to a resident person in respect of mining business, service fees to a non-resident person or an insurance premium with a source in Tanzania to a non-resident person.[109]

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[106] Section 78(1)(a) of the Income Tax Act 11 of 2004.
[107] Section 3 of the Income Tax Act 11 of 2004, person means an individual or entity.
[108] Section 82(1)(a) and (b) of the Income Tax Act 11 of 2004.
[109] Section 83(1)(a) and (b) of the Income Tax Act 11 of 2004.

In all categories, income tax will be deducted at the time of making payments by persons making such (withholding) payments whether to a resident or non-resident taxpayer.[110]

3.4.2 Income Tax Payable by Instalments

A taxpayer who derives or is expect to derive chargeable income from investment or business or, from employment (where its employer is not under the obligation to withhold income tax in case of employment as per section 81 of the Income Tax Act) shall pay income tax by instalments.[111]

Payment by instalments can be done quarterly in case a person's year of income is twelve month period or at each end of three months period at the beginning of the year of income and a final instalment on the last day of the year.[112]

3.4.3 Income Tax Payable on Assessment

Just like in any other jurisdiction, tax assessment is on the upper mind of the people who are being assessed. The provision of section 94 of the Income Tax Act gives powers to the taxpayer to make a self-assessment by filling a return of income not later than three months after the end of each year of income,[113] to estimate the amount of income tax payable for the said year of income.

Although the Income Tax Act has given the right and powers to the taxpayer, the same is given to the Commissioner for Domestic Revenue. Based on his best judgment rule, he can examine the return and make any necessary adjustments to the taxable income.[114] The adjustment will be made where the taxpayer has failed to file a return of income or has the intention of evading or even

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[110] K Ongwamuhana *Tax Compliance in Tanzania: analysis of Law & Policy affecting Voluntary Tax Payer Compliance* (2011) 132.

[111] Section 88(1)(a) and (b) Income Tax Act 11 of 2004.
[112] Section 88(2)(a) and (b) Income Tax Act 11 of 2004.
[113] Section 92 Income Tax Act 11 of 2004.
[114] Section 96 Income Tax Act 11 of 2004.

delaying paying tax[115] or where he feels there is a reason of fraud made by the taxpayer.[116]

Where it is believed by the commissioner under all reasonable cause that a person is about to leave country, the provision of section 95 of the Income Tax Act, gives the commissioner power make a jeopardy assessment.

At all times whether it is an adjusted assessment or jeopardy assessment, a written notice of assessment must be issued by the commissioner to the taxpayer.[117] The said notice shall state the reasons as to why the Commissioner for Domestic Revenue has made the assessment, the date, time and the manner by which tax payable on assessment is made and the manner of which the taxpayer can object the assessment.[118]

3.5 Methods used to Eliminate International Double Taxation

As stated early, most countries in the world including Tanzania imposes tax on their residence on world-wide basis while taxing its non- residence on gains or profits derived within its source[119] in respect of withholding taxes.

This type of taxing system might result in international double taxation where there is a cross-border transaction made by its residence outside its taxing jurisdiction or by non-residence within its taxing jurisdiction; and the outcome of international double taxation may lead to an increase of tax burden to the taxpayer[120] in turn

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[115] Section 96(3) (a) of the Income Tax Act 11 of 2004.
[116] Section 96(3) (b) of the Income Tax Act 11 of 2004.
[117] Section 97 of the Income Tax Act 11 of 2004.
[118] Ibid.
[119] V Daurer & R Krever 'Choosing between the UN and OECD Tax Policy Models: An African Case Study' at 7, available at *http://www.cadmus.eui.eu/bitstream/handle/1814/24517/RSCAS_2012_60rev.pdf?sequence=3*, accessed on 8 August 2014.

[120] DN Mahangila & MM Nchimbi *Income Tax in Tanzania* 1ed (2013) 143.

tempt the taxpayer to either evade or avoid tax liability,[121] thus loss of government revenue.

In order to avoid revenue loss while encouraging tax payments from taxpayers, the government under the ministry of finance together with TRA through the Income Tax Act, have adopted the use of unilateral reliefs as a mechanism of eliminating the problem. Although the reliefs are generally applicable under the Income Tax Act, for the purpose of this study, emphasis is done on withholding taxes.

In Tanzania, withheld taxes are amount of taxes retained on specific payments and are included in when calculating chargeable income from employment income and investment income and they include; dividend, interest, natural resource payment, rent or royalty, payment in respect of services fee and contract payments and payment in respect to supply of goods to the government and its institutions,[122] (dividends, interests and royalties are the focus of the study).

Paragraph 4 of the First schedule of the Income Tax Act provides for standard tax rate for withholding taxes on dividend income to be five per cent if paid by a corporation listed on the Dar es Salaam Stock Exchange or ten per cent if paid by any other corporation on both resident and non-resident taxpayers. Interest paid to a resident or non-resident is ten per cent while royalties is taxed at 15 per cent for both resident and non-residents.

In general, the Income Tax Act provides three types of unilateral tax reliefs to a taxpayer as methods of eliminating international double taxation and they include, tax exemption, tax deduction and tax credit or foreign tax relief.

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[121] Ibid.

[122] Sections 81, 82, 83 and 83A of the Income Tax Act 11 of 2004.

3.5.1 Tax Exemption

Tax exemption is one among the reliefs that the Income Tax Act offers as a method of avoiding or eliminating international double taxation. The relief is provided for under section 10 and Second Schedule of the Income Tax Act and it is offered on both residence and non-residence taxpayers.[123]

According to the two provisions, in alleviating international double taxation, Section 10 empowers the Minister of Finance on his discretionary powers to grant tax exemption whether in full or limited 'on any income or class of incomes accrued in or derived from Tanzania'[124] including any income from activities that where partly carried on within or partly outside Tanzania.[125] The Second Schedule of the Act provides for statutory tax exemptions on classes of income. However, the Income Tax Act does not provided for any tax exemption on dividend income on either resident or non-resident taxpayer but on interests earned by non-residents taxpayers on deposits in banks registered by the Bank of Tanzania are exempted from taxes.[126]

3.5.2 Tax Deduction

Tax deduction is another relief offered under the income Tax Act as a method of eliminating double taxation. The relief covered under the provision of sections 11 being the general provision to sections 19 of the Income Tax Act. The relief is offered on both business and investment income to Tanzanian residents[127] whose income tax is imposed on world-wide basis and considered to be the cost of

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[123] Section 10 of the Income Tax Act 11 of 2004. Cf Second Schedule.

[124] Section 10(1) (a) of the Income Tax Act 11 of 2004.

[125] Ibid.

[126] Paragraph 1(n) of the Second Schedule of the Income Tax Act 11 of 2004.

[127] Arnold & McIntyre (n63) 30.

carrying on the business or investment,[128] for example, where dividend is paid to a non-resident shareholder by a resident corporation, the corporation paid the said dividend will be entitled to a proportionate deduction of withholding tax credit withheld.[129]

3.5.3 Tax Credit or Foreign Tax Relief

The relief is covered under the provision of section 77 of the Income Tax Act. According to the provision, Tanzanian resident persons have a right to claim for tax credit of any foreign income paid in respect of the person's taxable foreign income.

Upon claiming the credit, the foreign tax shall be calculated separately for each year of income and shall not exceed the average rate of Tanzania income tax of the person for a year of income applied to the person's taxable foreign income on which the foreign income tax was paid.[130]

Furthermore, the average rate of Tanzanian income tax is determined by dividing the amount of the total tax payable over the taxable income. All foreign tax credit are calculated on world-wide basis rather than on the basis of quarantining income from separate country on a country by country basis.[131]

3.6 Tax Disputes Settlement Regime

Tax disputes are inevitable between taxpayers and tax authorities. The Income Tax Act and other tax laws in Tanzania recognise the right of a taxpayer to challenge tax decisions. All matters regarding tax disputes in relation to objection against tax assessment, denial of double taxation reliefs (from either the Income Tax Act itself or Tax Treaties) by any tax official etc, are governed by the Tanzania

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[128] Luoga op cit (n31) 168.

[129] Section 36 of the Finance Act 6 of 2014.

[130] Section 77(2) of the Income Tax Act 11 of 2014.

[131] Ibid.

Revenue Authority (hereinafter referred as TRA), the Tax Revenue Appeals Board (hereinafter referred to as the Board) and the Tax Revenue Appeals Tribunal (hereinafter referred to as the Tribunal) as administrators of all tax laws which creates tax disputes settlement regime (hereinafter referred as the Regime) which has vest all powers dealing with tax matters to the Commissioner General, TRA and the Board.[132]

The right to challenge a tax decision is given by an express provision of the law. This right is covered under the Constitution of Tanzania under Article13 (6) which stipulates the basic rights and duties of a person being determined; that is, a person is entitled to a fair hearing and has a right to appeal against any decision made upon him.

The Tax Revenue Appeals Act[133] (hereinafter referred to TRAA) under its provision of sections twelve, fourteen, sixteen and twenty five has made it possible for a taxpayer to appeal against any decision made against him by the Commissioner for Domestic Revenue. At the same time, the provision of section 6 of the Tanzania Revenue Authority Act[134] (hereinafter referred to as TRA Act) also provides a right to a taxpayer to challenge any tax decision.

3.6.1 Application of the TRAA

TRAA is applicable to Tanzania mainland and Tanzania Zanzibar[135] with original jurisdiction to hear and determine all tax disputes arising from all tax laws administered by the TRA.[136] Theoretically, the term 'all tax disputes arising from all tax laws administered by the TRA' purport to include Tax Treaties as well.

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[132] Kasser op cit (n89) 3.
[133] Tax Revenue Appeals Act 15 of 2000.
[134] Tanzania Revenue Authority Act 11 of 1995.
[135] Section 2 Tax Revenue Appeals Act 15 of 2000.
[136] Section 7 Tax Revenue Appeals Act 15 of 2000.

3.6.2 General Conditions and Procedural Requirements for Appeals

An appeal is not an inherent right to the taxpayer but rather a right that must be given by express enactment provision of a law and not by any means be implied.[137] For that case, its conditions and procedures are to be followed in order to acquire the right that a taxpayer seek to obtain.

Where there is any denial of any right in relation to international double taxation reliefs or where there is an object raised by a taxpayer regarding tax assessment made against him, the taxpayer has a right to appeal to the Board. While appealing to the Board, the taxpayer must raise an objection giving reasons thereto. In raising the objection, a written notice shall be issued disputing the assessment[138] whilst objecting, the taxpayer shall pending the final determination of the objection pay the amount of tax which is not in dispute or one third of the assessed tax whichever amount is greater.[139]

Within the period of thirty days[140] the taxpayer (appellant) must give a written notice of his intention to the Commissioner General contesting against his decision on a disputed matter by way of appeal to the Board. At the same time, within period of forty days. The same notice shall be filled to the Board.[141]

After all conditions and requirements have been fulfilled, the Board shall proceed to determine the matter. For the purpose of hearing and determining an appeal, the Board shall consist of a chairman who is appointed by the minister of finance, two vice chairmen and four members.[142] The decision of the Board is subject to an appeal. Any

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[137] SR Myneni *Law of Taxation* (2001) 256.
[138] Section12 of the Tax Revenue Appeals Act 15 0f 2000.
[139] Section 12(3) and Section 13 of the Tax Revenue Appeals Act 15 of 2000.
[140] Section 12(1) and (2) of the Tax Revenue Appeals Act 15 of 2000.
[141] Section 16(3) of the Tax Revenue Appeals Act 15 of 2000.
[142] Section 4 of the Tax Revenue Appeals Act 15 of 2000.

party who is not satisfied with the decision of the Board may appeal to the Tax Appeal Tribunal (hereinafter referred to the Tribunal).

The Tribunal shall consist of a chairman who is appointed by the Present of United Republic of Tanzania, two vice-chairmen and other four members appointed by the minister of finance. At the same time, any party if aggrieved with the decision of the Tribunal can apply to the High Court of Tanzania then to the Tanzanian Court of Appeal for the final determination of the matter.[143]

3.7 Conclusion

In this chapter, the main focus was on domestic reliefs that are offered under the Income Tax Act as methods of eliminating international double taxation. The starting point was the Tanzanian tax system that gave out a clear indication how the system works once reliefs are provided. That is to say, once reliefs are offered the matter does not only end there but other procedures are to be followed.

Reliefs offered under the Income Tax Act are unilateral the reliefs with an aim of not only avoid and eliminate international double taxation but also to keep a balanced relationship between taxpayers and the government. For example, tax exemptions are offered with an intention of encouraging investment by both residents and non-resident taxpayers while tax credit, directly reduces taxpayer tax liabilities by allowing deductions to be made on foreign income. As for tax deduction, though it is seen to be biased on foreign investment and that is not neutral in allocation of resources between countries, it encourages domestic investment at the same time making sure resident with world-wide income are equally treated under the Income Tax Act. This is why, where there is a denial of any relief, a taxpayer has a right of challenging the decision of the Commissioner General.

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[143] Section 25 of the Tax Revenue Appeals Act 15 of 2000.

CHAPTER FOUR

TANZANIAN DOUBLE TAXATION TREATIES.

4.1 Introduction

Under international law lies tax treaties[144] with the main aim of avoiding international double taxation and prevention of fiscal evasion with respect to taxes on income and capital gains that may arise from juridical international double taxation.[145] Although their mode of existence is different and separate from that of countries domestic tax laws, their implementation are done by the local tax legislators.[146]

The objective of this chapter is to consider and analyse international double taxation treaties entered into by Tanzania and the methods of relief they offer in eliminating international double taxation.

4.2 Double Taxation Treaties

Historically, international double taxation treaties existed before the outbreak of the First World War[147] with the aim of 'allocating tax rights on international transactions to a taxpayer's country of residence'.[148] Other than that, their aim was to resolve the problem of juridical international double taxation[149] with the first treaty signed with Belgium and France in 1843.[150]

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[144] G Maisto *Tax Treaties and Domestic Law* (2006) 3.

[145] OECD Commentaries of the Articles of the Model Tax Convention 306.

[146] Maisto op cit (n142) 3.

[147] Holmes op cit (n38) 56.

[148] Ibid.

[149] Ibid.

[150] Olivier & Haniball op cit (n19) 7.

International double taxation treaties are sometimes referred to as international tax agreement,[151] double tax agreement[152] or double tax treaties[153] but for the purpose of this study there hereinafter referred to as tax treaties.

In their plain definition, tax treaties are simply 'tax agreement between two countries that outline a series of articles which clarifies the tax rules between the countries on specific subjects'[154] or 'an agreement between two or more countries for the avoidance of double taxation'.[155]

As stated on chapter two, tax treaties can either be bilateral or multilateral. Whether bilateral or multilateral tax treaties, one must understand and interpret them in their whole context by looking at their objective and purpose in a plain meaning[156] to establish their significant role of reducing and eliminating international double taxation.[157]

As mentioned above, the primary purpose of a tax treaty is to minimise and eliminate the effect of international double taxation on the side of the taxpayer in order to facilitate the exchange of goods and services, movement of capital, technology and skilled personnel.[158]

However, tax treaties are also used in preventing fiscal evasion on income taxes through the method of exchanging information between

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[151] Section 128(1) of the Income Tax Act 11 of 2004.

[152] Olivier & Haniball op cit (n19) 7.

[153] Holmes op cit (n38) 53.

[154] Lymer & Hasseldine op cit (n4) 127.

[155] Holmes op cit (n38) 54.

[156] FA Engelen *Interpretation of Tax Treaties under International Law* (2004) 128.

[157] Holmes op cit (n38) 53.

[158] Mahangila & Nchimbi op cit (n130) 144.

contracting countries.[159] As the principle of good taxing system suggested by Adam Smith in "The Wealth of Nation", equity and even tax neutrality are to be present in one's tax system, therefore, even if tax treaties since the rationale of the states concluding them is not only on avoiding international double taxation and preventing fiscal evasion but also to have a good economic relationships with foreign countries through their taxpayers by facilitating international trade and commerce in cross- border investments[160] and making sure that there is a good tax system that can accommodate both domestic and foreign businesses.

Nevertheless, before reaching to an agreeable tax treaty, an understanding of the nature of a tax treaty is of a great importance. Every tax treaty before its conclusion must have a starting point or base of its existence; meaning, the kind of a tax model a contracting country is willing to follow and incorporate its rules and procedures in its tax treaty depending on the negotiation with the other contracting country.

The most popular and followed tax models are, the United Nations Model Convention between Developed and Developing Countries (hereinafter referred to as the UN Model) and the Organisation for Economic Co-operation and Development's Model Convention on Income and Capital (hereinafter referred to as OECD Model). Though both models addresses and put emphasis on the same issues in regards to avoiding international double taxation of international income flow and prevention of fiscal evasion with respect to taxes on income and capital gains, they have different expectations.

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[159] Article 26 of the OECD Model Tax Convention on Income and Capital and Article 26 of the UN Model Double Taxation Convention between Developed and Developing Countries.

[160] Lymer & Hasseldine op cit (n4) 124.

Their difference is on the application of the concept of neutrality that is 'based on allocation of capital'.[161] The concept is divided into two, capital export neutrality and capital import neutrality.[162] Capital export neutrality, operates under the residence tax base principle were it application of standard tax rate to its investment firm with no regards to where they are located[163] while capital import neutrality is based on the principle of territoriality or source, it requires firms invested on different given location with different nationalities be taxed the same.[164]

Therefore, the OECD Model, is based on capital export neutrality were it shifts the taxing right to capital exporting countries[165] by giving the residence country a choice of either using tax credit method or exemption method as methods of eliminating international double taxation[166] while giving the source country a limitation on both of its right to tax at income that have its source and to tax at a lower rate where its right is retained.[167] Whereas, the UN Model on the other hand is based on the concept of capital import neutrality that tries to keep a balance between the country of source and residence by giving more priority to the country of source[168] hence being a model that encourages capital importation.[169]

4.3 Tanzanian Tax Treaties

As stated on chapter one of the study, the increase of business and investment opportunities in Tanzania has led to its growing economy

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[161] JG Gravelle *Reforms of U.S International Taxation: Alternatives* (2010) 4.

[162] Gravelle op cit (n159) 5.

[163] Ibid.

[164] Ibid.

[165] Daurer & Krever op cit (n129) 7.

[166] Luoga op cit (n31) 172.

[167] Ibid.

[168] Luoga op cit (n31) 173.

[169] Daurer & Krever op cit (n129) 7.

for its sustainable wealth creation. And as of recent, the economic growth has increased from seven per cent to nearly 19 per cent from the year of 2007/2008 to 2014/2015.[170] Despite all the achievements made by the government still the economy sector is facing with fundamental problems one being the challenge of broadening the tax base with the aim of increasing its domestic financial capacity. Therefore, considering the nature of its tax policy, which is among other things, to promote economic growth and encouraging foreign investments while protecting its domestic market in general,[171] the government is committed by making sure that cross-border investments and any business activities that may lead to international double taxation, does not affect the growth of its economy hence concluding tax treaties.

Moreover, basing on the level of its economic growth and tax policy arrangements, another reason of why Tanzania has tax treaties despite of other reasons, is to eliminate and avoid international double taxation together with making sure that there is a high level of preventing fiscal evasion on income taxes. By these reasons per se, Tanzania has signed different tax treaties. Accordingly, it has nine bilateral tax treaties with the following countries; Zambia in 1968,[172] Canada in 1995,[173] Denmark in 1976,[174] Italy in 1973,[175] Finland in

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[170] Budget Speech by the Minister for Finance Hon. Saada Mkuya Salum (MP) Introducing to the National Assembly, the Estimates of Government Revenue and Expenditure for Fiscal year of 2014 to 2015, available at *http://www.mof.go.tz/mofdocs/msemaji/EnglishBudgetSpeechMOF2014.pdf.*, accessed on 26 July 2014.

[171] Ongwamuhana op cit (n110) 157 to 158.

[172] For Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect of Taxes on Income.

[173] For Avoidance of Double Taxation and Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital.

[174] For Avoidance of Double Taxation and Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital.

[175] For Avoidance of Double Taxation and Prevention of Fiscal Evasion with Respect to Taxes on Income.

1976,[176] India in 2011,[177] Norway in 1976,[178] Sweden in 1976[179] and South Africa in 2005.[180] It has also concluded one multilateral treaty of East African Community (hereinafter referred to as EAC Treaty) in 2000[181] with five countries of East Africa namely, Tanzania itself, Kenya, Uganda, Burundi and Rwanda. And just like any other international instrument, Tanzanian tax treaties have more or less the same legal structure into comparison with other countries; that is, they start with the scope of application and end with termination clause.

4.4 Reliefs under Tax Treaties

Under the Income Tax Act, the above stated tax treaties are referred to as international agreement with the meaning of 'a treaty or other agreement with foreign government that has entered into force in the United Republic providing for:

a. relief of international double taxation and prevention of fiscal evasion or

b. reciprocal administrative assistance in the enforcement of tax liabilities'.[182]

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[176] For Avoidance of Double Taxation and Prevention of Fiscal Evasion with Respect to taxes on Income and Capital.

[177] For Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect of Taxes on Income.

[178] For Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect of Taxes on Income and Capital.

[179] For Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect of Taxes on Income and Capital.

[180] For Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect of Taxes on Income.

[181] For Development of Policies and Programmes the will aim at Widening and Deepening Co-operation among the Partner States in Political, Economic, Social and Cultural Fields, Research and Technology, Defense, Security and Legal and Judicial affairs for their mutual benefit.

[182] Section 128(6) of the Income Tax Act 11 of 2004.

The nature of the tax treaties concluded lies on two model of tax conventions; the OECD Model and the UN Model but more on the UN Model because it gives more weight on the source principle than the OECD Model; thus compromising between the source principle and the residence principle.[183] However, out of ten tax treaties concluded, nine of (expect the EAC multilateral tax treaty) them where made under the guideline of the OECD Model.

When it comes to their interpretation, their legal status is provided for under the provision of section 128(1) of the Income Tax Act that states, the terms of any tax treaty concluded by Tanzania prevail over the provisions of the Income Tax Act to an extent where there is an inconsistency between the terms of the tax treaty and of the Income Tax Act.

However, the terms of these tax treaties shall not apply to the provision of subsection 4 read together with subsection 5 of section 128 that provides for conditions which must be met by an entity desiring for tax exemption as relief of an international double taxation. Therefore, the limitation is on granting tax exemption relief to an entity which is not a resident of the other contracting state which is a party to a tax treaty and the beneficial owners of the income or payment are not residents of the same state.

As seen under the provision of section 128 (6) of the Income Tax Act, the underlying aim of tax treaties is to avoid international double taxation specifically juridical international double taxation on both active incomes and passive incomes. [184]Therefore, in general, depending with the tax treaty negotiations, the relief offered under

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[183] Luoga op cit (n31) 173.

[184] Committee of experts on international cooperation in tax matters seventh session: Revision on the manual for the negotiation of bilateral tax treaties, Geneva, 24 to 28 October 2011, 17 to 18, available at *http://www.un.org/esa/ffd/tax/seventhsession/CRP11_introduction_2011.pdfI*, accessed on 12 August 2014.

tax treaties as methods of eliminating international double taxation; are tax credit, tax exemption or, and tax deduction (as explained on chapter two) but the most effective one is tax credit with the reason that its application extends to foreign income on withholding taxes and also because 'none of the tax treaties entered reduces the tax rate of withholding taxes to non-residents below its domestic tax rate',[185]unlike tax exemption.[186]

As discussed on chapter three regarding withholding taxes, the below table explains how reliefs given under the Income Tax Act and the ones under tax treaty operates:

Nature of payment	Tanzania withholding tax rates on both residents and non-residents	South Africa-Tanzania Income Tax Treaty (2005) Not exceeding	India-Tanzania Income Tax Treaty (2011) Not exceeding	Italy- Tanzania Income Tax Act (1979) Not exceeding
Dividend	10 per cent	10 per cent	5 to10 per cent	10 per cent
Interest	10 per cent	10 per cent	10 per cent	10 per cent
Royalties	15 per cent	10 per cent	10 per cent	10 per cent

Moreover, the tax credit assures non manipulation of tax credit rates by the source country for its own advantage of making higher rates on credit towards the foreign tax payers whose countries offers tax credit; and if it does, it will be said to have breached the non-discrimination provision under the tax treaty.[187]

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[185] Mkono & Tetteh-Kujorjie op cit (n1) 584.

[186] Ibid.

[187] Ibid.

Furthermore, the reliefs under the tax treaties are offered on the priority of allocating taxing powers, in other words, by looking at the source and resident principle underlined in international taxation while determining which state will have the primary tax pay and which will have the secondary tax pay. By having this allocating powers, normally the state with primary tax pay is usually the country of resident of the taxpayer and the state with the secondary tax pay is the country of nationality of the tax payer or the country where income was derived.

Nevertheless, because of the primary and secondary tax pay on tax credit, tax exemption and tax reduction reliefs, the focus is on the agreeing rate of tax which is normally lower than the one offered by the Income Tax Act as show on the above table.

4.5 Position of Law Where no Tax Treaty

Taxpayers who are not under the scope of any tax treaty in a sense that there are not covered by it and who are likely to be affected by international double taxation, their fate lies on domestic tax rules. The provision of section 67 of the Income Tax Act, allows relief for taxpayers even where there is no formal double taxation relief agreement

If the said taxpayer is a Tanzanian resident and has engaged in cross-border transaction with a state that has no tax relationship with Tanzania, then the Income Tax Act will provide him or her the foreign tax relief in order to avoid or eliminate international double taxation. However, the burden of proof lies upon him to show that there is a likelihood of his income to be taxed twice.[188]

4.6 Conclusion

The chapter has attempted to show the nature of tax treaties that Tanzania have in an attempt of eliminating international double

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[188] Mahangila & Nchimbi op cit (n129) 144.

taxation. It has also shown the different types of reliefs offered by parties to the treaty and their proposed method of arriving to the aimed achievement. And basing on both OECD and UN Models of tax, the chapter has shown the difference between the two models though in a slightest way when it comes to allocating tax right powers. Lastly, under the tax treaties when it comes to relief of either tax credit, tax exemption or tax reduction, the offering base is on the source country that has limited taxing right as compared to the resident country.

CHAPTER FIVE

THE GENERAL CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

The study was aimed at analysing the Tanzanian Income Tax Act, 2004 on the aspect of how it resolves international tax disputes with special focus on international double taxation. The aim was to see how the Income Tax Act provides solutions on how international double taxation can be avoided or eliminated where the same income is purported to be taxed by two or more states as a result of cross-borders activities of the taxpayer. And in the course of doing so, the focused issues were the methods used by both the Income Tax Act and tax treaties that Tanzania have concluded with other states on avoiding or eliminating international double taxation. The outcome of the analysis is as follows:

The general analysis of the study has shown that, in an attempt to resolve by avoiding and, or eliminating international double taxation, Tanzania uses both unilateral and bilateral relief. That is, relief provided under the Income Tax Act and those under the Tax Treaties. Although the reliefs are equally the same, the method used in offering them is totally different from each other with different aims.

As stated above, the Income Tax Act offers unilateral tax relief that includes, tax exemption, tax deduction and tax credit (foreign tax relief) on as a method of avoiding or eliminating international double taxation on Tanzanian taxpayers resident and non-residents deriving income that has a source within Tanzania with an aim of having a balance between its domestic and foreign economy.

Though it has been said in general that unilateral methods of relief are less productive in combatting the issue of international double taxation than those offered by tax treaties because they only benefit the domestic economy as they are taken on one side only, they seem to be more realistic and reasonable for a country like Tanzania that is

still on the process of developing its economy. The unilateral relief do not only try to eliminate international double taxation but also protecting the country's domestic revenue by reducing tax liability on businessmen and investors while protecting the foreign income that has been taxed.

On the other hand, the study has shown that, Tanzanian tax treaties are divided into two categories, that is, bilateral tax treaties concluded with nine countries and one multination tax treaty that consists of five East African countries. When tax treaties are used as an alternative tool of avoiding or eliminating international double taxation, depending on the tax treaty, they offer bilateral relief such as tax credit, tax deduction and even tax exemption (tax exemption is offered as a relief if it's online with the requirement of the Income Tax Act.)

The methods used by these tax treaties on the above mentioned reliefs in relieving international double taxation, is to give one contracting state an exclusive taxing right. That is, allowing one state to impose tax on income which is on dispute and it is usually the taxpayers' country of residence. For example, where income is derived from Tanzania by a Danish resident, under normal circumstances tax will be imposed by both states claiming to have the right. For the case of Tanzania, it will impose tax on the ground that income is attributable with factors within its territory while Denmark will claim the same income on the ground that tax is imposed on world-wide basis on its resident taxpayers, but because there is a double taxation agreement between the two countries, income will then be charged by Denmark. If Tanzania has been given the right to tax the income, it must use lower tax rate than the one that it would normally use. Therefore, the method of relief offered under tax treaties are based on the principle of residence than source with the aim of limiting taxing rights of the country where income is said to be

derived while leaving more room and taxing powers to taxpayer's country of residence.

In analysing the Income Tax Act on whether it is capable of resolving international double taxation or being effective on alleviating international double taxation in comparison with the tax treaties, it is in the researchers' opinion that, the Income Tax Act is indeed capable and its solutions are better in resolving international double taxation as compared to tax treaties. This goes with reason that, tax treaties have been designed to override provisions of many income tax Acts including the Income Tax Act for the benefit of one party basing on the following reasons:

Firstly, Tanzania is a developing country and engages its economic relationship with countries (Denmark, South Africa, Canada, Sweden, Italy, Finland et cetera) that are more developed. Looking at the system and the nature of its economy, Tanzania tends to attract foreign investment to secure an increase of its international economic recognitions with the aim of expanding both of its domestic and foreign economy but ends up falling on influence of strong developed countries that in turn uses the methods of eliminating international double taxation under tax treaties to their own advantages; as seen in the case of *Tullow Tanzania BV v Commissioner General*[189] were it was stated by Hon.P.M. Kente, the Chairman of the Board that,

> 'Tanzania is facing the might of powerful economic interest that have the full backing of their equally formidable government...and we deliberately and unnecessarily setting up a David and Goliath contest of which we are not sure of victory... It is in these challenging circumstances that our law need to be interpreted so as to safeguard the interest of the nation and avoid leaving our nation at the mercy of the strong nation...'[190]

Secondly, the intended aim of tax treaties is to eliminate international double taxation and prevent fiscal evasion of income taxes in order to strengthen the ability of states on imposing fairs taxes on cross-border transactions but that intention has been manipulated and

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[189] Income Tax Appeal Case No. 1 of 2011 (unreported) 7 to 8.

[190] Ibid.

changed into an abuse of the strong economic countries over the Income Tax Act by making sure that all taxes are eliminated on their side. That is, they take an advantage of their status by making sure that the global economy keeps more pressure on domestic tax laws for their own benefit, thus they override the Income Tax Act.

From the above facts of the study, the researcher would like to comment on the following recommendations;

1. The Income Tax Act should remove the provision of section 128 that gives tax treaties more prevailing powers than its own provisions and introduce a provision that will prevent the inappropriate benefits of tax treaties. In that way, the abuse shown by these treaties will be minimal when it comes to eliminating international double taxation
2. There should be a balance between the Income Tax Act and the tax treaties on tax rate so that the two laws could work together in resolving the problem of international double taxation.
3. Tanzania should change it tax policy that has kept more focus on attracting foreign investors and try to encourage its taxpayers to invest more in the domestic economy than depending more on foreign investors that normally leads to an outbreak of international double taxation.

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