CORPORATE TAX EVASION AND AVOIDANCE IN UGANDA

SEATINI

Strengthening Africa in World Trade

actionaid

April 2017

CORPORATE TAX EVASION AND AVOIDANCE IN UGANDA

April 2017

Table of Contents

List of Figures

List of Tables

Acknowledgements

This research was jointly produced by SEATINI Uganda and ActionAid Uganda.We appreciate the following for contributing to the production of this research; Mr. Daniel Lukwago, Mr. Jeff Mbanga, Mr. Rodney Golooba,Mr. George Bogere, Grace Namugambe, Nelly Busingye, Regina Navuga.

List of Acronyms

AAIU	Action Aid Uganda
BEPS	Base Erosion and Profit Shifting
BIT	Bilateral Investment Treaty
BoU	Bank of Uganda
CIT	Corporate Income Tax
DTA	Double Taxation Agreement
DTT	Double Taxation Treaty
EAC	East African Community
FDIs	Foreign Direct Investments
FIA	Financial Intelligence Authority
FYs	Fiscal Years
GDP	Gross Domestic Product
GFI	Global Financial Integrity
GIZ	Deutsche Gesellschaft fur InternationaleZusammenarbeit
ICT	Information and Communications Technology
IFFs	Illicit Financial Flows
IGC	International Growth Center
IMF	International Monetary Fund
ITA	Income Tax Act
MNCs	Multi-National Corporations
MoFPED	Ministry of Finance, Planning and Economic Development
OECD	Organisation for Economic Cooperation and Development
PAYE	Pay As You Earn
PIT	Personal Income Tax
PSAs	Production Sharing Agreements
SEATINI	Southern and Eastern Africa Trade, Information and Negotiations Institute
TREP	Taxpayer Registration Expansion Project
TTR	Total Tax Revenue
UGX	Uganda Shillings
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNECA	United Nations Economic Commission for Africa
URA	Uganda Revenue Authority
URSB	Uganda Registration Services Bureau
VAT	Value Added Tax

Executive Summary

Tax evasion and tax avoidance or dodging by individuals and companies is a great concern in many developing countries including Uganda. Newspapers and other media too occasionally convey reports of gross tax evasion and avoidance. Conservative estimates by GFI based on illicit flows puts the loss of CIT at about US$ US$ 1,077million annually. This means that MNCs in Uganda are deliberately or otherwise engaging in tax dodging. While the Government of Uganda has made some efforts such as enacting a number of amendments to its tax laws aimed at closing the loopholes used by MNCs and individuals to evade or dodge taxes, the tax regime is still susceptible to tax planning, especially by MNCs. This study was carried out to investigate tax evasion and tax avoidance or dodging by companies and individuals in Uganda. The study was carried out mainly through literature review of secondary data and analytical studies from various sources. The key findings of the study are summarized below:

Schemes used to evade and avoid paying taxes

The commonly used instruments by individuals and corporations to minimize or circumvent their tax liability include: Trade Misinvoicing - involves deliberately misreporting the value of a commercial transaction on an invoice submitted to customs; Treaty Shopping – where company uses a subsidiary located in a jurisdiction with a low tax rate, and has special benefits for its residents, for the purpose of reducing its tax bill in another country where income is derived; Round tripping – a domestic company re-registers in the jurisdiction of treaty partners, presenting themselves as if they are external investors; Transfer Pricing Manipulation - happens whenever two companies that are part of the same multinational group trade with each other; Base Erosion and Profit Shifting- strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations; Thin capitalization - a strategy in which a company frontloads debt from low tax jurisdictions into markets where tax rates are high; Exploitation of capacity deficiencies within tax authorities; deliberate choice of location for certain (intangible) assets; among others.

Reforms aimed at elimination tax evasion and avoidance in Uganda

Over the last decade Uganda has developed reforms geared at eliminating tax evasion and avoidance, through amendment of the Income Tax ActSome of the amendments to minimise tax avoidance include: Article 88 to deal with international agreements (i.e. DTAs); article 89, to deal with thin capitalisation; and article 90 and 91 to deal with anti-avoidance. Other reforms include: Computerization of tax processes; Strengthening the capacity of URA; implementing the Taxpayer Registration Expansion Project (TREP); and strong penalties for tax evasion under the Tax Procedure Code Act 2014.

Corporate Income Tax Performance

Corporate Income Tax (CIT) is collected from companies, based on their net income. Corporate Income Tax (CIT) grew by 74 percent from UGX 419.6 billion in FY 2010/11 to UGX 732.2 in FY 2015/16. However, CIT revenues have remained below 10 percent of total tax revenue (TTR) over the past decade. For instance, in FY 2015/16 CIT contributed just 7 percent of total tax revenue while PAYE and VAT contributed 16 percent each. URA attributes the poor performance of CIT to the slowdown in the economy and low profitability especially for the telecom industry. However, some analysts disagree with URA's claim, noting that the main factor behind the drastic fluctuation in

CIT is not the gradual shift in the profitability of companies but rather aggressive tax planning structures of MNCs; some companies might be using more sophisticated means to reduce their tax bills, regardless of the profits they make.

The CIT regime in Uganda faces challenges of incomplete and inconsistent rules applicable to different types of income; non-transparent provision of tax incentives and exemptions; Illicit Financial Flows through overpricing, transfer pricing, tax evasion, money laundering, corruption and false declarations among others; exploitation of Double Taxation Treaties (DTTs) by MNCs; inadequacy implementation of punitive sanctions on tax dodging and avoidance.

We therefore, provide the following recommendation:

- MoFPED should fast track the review of the existing DTTs, particularly those with so-called conduit jurisdictions, often used by MNCs in their tax avoidance schemes.
- Government should ensure transparency and accountability in the provision of tax exemptions as part of minimizing cases of tax avoidance.
- Parliament should amend all laws, which facilitate tax evasion and avoidance.
- Government should subject all tax exemptions including those in DTTs and PSAs to parliamentary approval.
- The BoU and Financial Intelligence Authority should enhance greater collaboration on tracking financial transfers for purposes of detecting tax evasion and money laundering.
- URA should ask for clearer information on taxes from multinationals. There should be an addition of two new columns on the tax form- one for offshore income on which the MNC is deferring taxes and another to capture the company's reserves for "uncertain tax positions.
- URA should continuously build the capacity of its staff to detect and investigate tax dodging by MNCs particularly in the newly emerging businesses with peculiar structures including intangibles in the mining and services sector.

Section 1: Introduction

Tax evasion and tax avoidance are so closely intertwined. Tax evasion is to do with illegal practices for purposes of escaping taxation. This includes all endeavors by individuals and corporate bodies to conceal taxable income or profits. The GIZ (2010) in its definition of tax evasion includes misrepresentation of sources and amounts of income as well as overstating deductions and exemptions. Tax evasion is often linked to illegal activities and therefore the incomes sources are usually disguised or concealed. This makes detection and measurement of tax evasion difficult. The proxy for tax evasion by the Global Financial Integrity (GFI) includes financial flows due to illegal and illicit activities. Other definitions of the tax evasion associate the term with the informal sector.

Tax avoidance or dodging on the other hand occurs within the law. In this case individuals or firms exploit loopholes in the taxation laws for purposes of reducing their tax liability. The most prominent form of tax avoidance is through tax planning where financial undertakings are done in such a way that the tax liabilities are minimized. Thus tax avoidance is legal but goes against the primary objective of the tax system. This contradiction in many instances arises out of competing and at times contradicting objectives and policies of governments. For instance a government may allow deductibles in the computation of taxable income, which companies may exploit by inflating such deductibles especially through transfer pricing in their books of accounts. This was the case with MTN where allowable deductions such as money paid for management services are allowed by the law but in using that allowance the company decided to use a percentage of turnover as the management fee paid for work similar to that done by local staff.

While tax evasion and tax avoidance are differentiated in the literature, in reality the two are so closely related, distinction between the two is far less clear in practice (ibid). Understanding the link and the premise upon which they can be dealt with as distinct is critical. In this study we try to examine the dimensions and modes they usually take as well as the underlying factors.

1.1 Background

Tax evasion and tax avoidance or dodging by individuals and companies is a great concern in many developing countries including Uganda. There is anecdotal evidence that Uganda is losing significant tax revenue due to tax evasion and avoidance. A revenue administration gap analysis by the IMF (2014) found that while the Value Added Tax (VAT) tax base had grown significantly as depicted by the increase in compliance gap from just under 5% in 2003/4 to over 6% in 2012/13, the compliance gap as a percentage of potential VAT had remained constant at 60% over the same period. The study also notes that compliance level in Uganda remains below that of countries at similar level of development. Another study by the IGC (2015) found that 87% of seller firms declared amounts lower than those declared by the buyer. The study estimated the tax compliance gap of about 747 billion.

Newspapers and other media too occasionally convey reports of gross tax evasion and avoidance. In October 2015, a joint investigation by the Observer and Finance Uncovered a global investigative journalism network unearthed how between 2003 and 2009, MTN Uganda had shifted three per cent of its revenue every year to MTN International in Mauritius under the disguise of 'management services' even when the company itself [MTN] confirmed that the Mauritian company employs no staff at all . The Panama leaks (2016) also revealed how billions of dollars had been hidden by wealthy figures and Uganda was no exception. The leaks also showed how Heritage decided a month to the execution of its Sale and Purchase Agreement with Tullow to move its domicile from

Bahamas to Mauritius with a view of avoiding to paying Capital Gains Tax. While it informed Ugandan courts that the move was for "better time zones" in England in its case with Tullow, Heritage admitted that the purpose was to avoid paying capital gains tax. .Uganda earned up to $ 434 million in capital gains tax after protracted court battles locally and internationally.

While the Government of Uganda has made some efforts in streamlining the Corporate Income Tax (CIT) regime, CIT is susceptible to tax planning, especially among MNCs that have the resources to hire experienced tax managers. MNCs have attained some power to indirectly influence tax policy to favor their operations against the mutual benefit and revenue generation objectives of the government.

Uganda like many developing countries is beset by budget deficits due to low revenue mobilization. This has led to many other problems as the country borrows both domestically and internationally to finance the budget deficit. The IMF (2015) projects Uganda's deficit to average 5.5 percent in the long run and public and publically guaranteed external debt is expected to remain below 36 percent of GDP in the medium term. While the debt levels are deemed to be sustainable at current levels, debt is eroding the funds available for social services. Over the last two financial years, the allocation to debt repayment has been estimated at over 10% of the national budget over the last two financial years. This is the equivalent of the allocation to the health sector. In the FY 2017/18 budget, out of the 29 trillion budget, 2.6 trillion has been allocated to interest payment. Moreover tax revenue as a percentage of GDP remains at less than 14%. Compared to other EAC countries, Uganda's Tax to GDP ratio is one of the lowest; stood at 11.7 per cent, Kenya's was 20.0 per cent, Rwanda's 14.7 per cent and Tanzania's 21.0 per cent in 2013/14 (EAC Secretariat, 2015).Part of the causes of poor tax revenue performance is tax evasion and avoidance by individuals and companies.

It is against this background that Southern and Eastern Africa Trade, Information and Negotiations Institute (SEATINI-Uganda) and Action Aid Uganda (AAIU) carried out this study to investigate tax evasion and avoidance or dodging by individuals and companies in Uganda.

The study specifically aimed at:

a. Identifying the loopholes and gaps in Uganda's tax systems, laws that facilitate MNCs and business personnel to evade and avoid paying their fair share of tax in Uganda.

b. To examine the trends on how much corporate tax has generated from FY 2013/14- 2015/16 vis-à-vis other taxes – such as PAYE and VAT- and the opportunities and challenges corporate income tax regime faces.

c. To provide policy and practice recommendations to curb tax evasion dodging and evasion.

1.2 Methodology and Scope

The study mainly involved literature review of secondary data and analytical studies from various sources such as government, international agencies (WB, IMF, and OECD), Financial and statistical data on tax, newspapers and general studies on taxation. We examined the tax gap or lack of information and evaluated the extent to which the legal framework is responsible for tax evasion and avoidance.

The study scope was limited to the Corporate Income Tax (CIT), the Value Added Tax and Personal Income Tax (PIT) tax regime and laws in Uganda. Data used in the study covered mainly FYs 2013/14 to 2015/16.

1.3 Limitation of the study

The study was constrained by lack of information on tax evasion and avoidance by companies. Related practices are highly guarded by firms and taxable incomes hidden or disguised as something else. Information by the URA on performance of MNCs in relation to tax is scanty and is inadequate in most cases. URA maintains that it is bound by the confidentiality clauses it has signed with companies. Even government institutions such as the Office of Auditor General find it hard to carry out audits of taxes paid by individual taxpayers and companies. Furthermore, the sensitivity of tax evasion and avoidance makes many actors and would be respondents cagy on providing reliable and credible information. The study therefore largely depended on review of secondary data and literature.

Section 2: Tax Evasion and Tax Avoidance

2.1 National and International dimensions of tax evasion and avoidance

Tax evasion and avoidance has both national and international dimensions. The national dimension relates to situations where individuals or firms undertake practices to evade or minimize taxes within their country of residence without any involvement of individuals or firms outside the country. The GIZ (ibid) defines the national dimension of tax evasion and avoidance to include incomes and revenues generated in the domestic informal economy, income not reported by a legal or natural person and other means of 'getting around' solely domestic tax liabilities.

The international dimension relates to all instances of tax evasion and avoidance, which take place due to international trade, movement of labor across borders and foreign direct investment. Uganda's tax exemptions are usually underpinned by a discourse on attracting investments. GIZ (ibid) describes the international dimension of tax evasion and avoidance to include multi-national corporations (MNCs) tax-driven shifting of profits, tax evasion and avoidance against the background of investment incentives and special enterprise zones, as well as various kinds of VAT and tariff fraud accompanying international trade in goods and services.

2.2 Schemes used by MNCs and business personnel to evade and avoid paying taxes in Uganda

The commonly used instruments by individuals and corporations to minimize or circumvent their tax liability are summarised in Table 1. The table shows the different modes of evading tax obligations that violate national tax laws. These include misreporting and non-declaration of personal income or corporate profits to circumvent direct income taxation or tax obligations resulting from sale of goods and services. It is important to note that the modes of tax evasion are not mutually exclusive but may also result as a consequence of one another (GIZ, 2010).

Table 1: Possible modes of tax evasion and avoidance in developing countries

Tax Evasion: Intentional falsification of tax relevant information	Tax Avoidance: Exploiting the legal scope for discretion of the tax system running counter to the purpose of the tax law
▪ Non declaration of assets in offshore financial accounts ▪ Trade mispricing ▪ VAT fraud: – Missing trader fraud/carousel fraud – Miss classification of goods – Smuggling of goods ▪ Bribing tax officials ▪ Abuse of tax incentives by falsely claiming eligibility	▪ Profit shifting: – Pricing intercompany tangible goods transactions/barter trade – Increase in intercompany debt – Location of central services and intangible assets ▪ Bargaining for tax incentives

Source: GIZ (2010)

Holding offshore financial accounts to conceal taxable income from tax authorities in the country of residence allows tax evaders to benefit from low or zero taxes abroad, exploiting bank secrecy and poor financial regulation abroad. The resulting tax revenue loss for developing countries is substantial: According to estimates reported by GFI, developing countries lost close to US$ 785 billion in illicit financial outflows between 2004 and 2013 (GFI, 2016). Applying a 30 percent rate brings the tax revenue loss to about US$ 236 billion over the same period. Specific modes of tax evasion and dodging are described below.

Trade Misinvoicing

Trade misinvoicingisdefined by Global Financial Integrity as a method for moving money illicitly across borders, which involves deliberately misreporting the value of a commercial transaction on an invoice submitted to customs. In other words trade misinvoicing is a form of trade-based money laundering. The GFI report (2014) identifies four basic categories of trade misinvoicing: import under-invoicing, import over-invoicing, export under-invoicing, and export over-invoicing. Most trade misinvoicing is done with the knowledge and approval of the seller and the buyer in the transaction. The two parties, if they are not part of the same company, will agree to the misinvoicing and how they will settle the transaction outside legal confines, often through a deposit into another bank account.

Trade misinvoicing is common with transactions related to shared services. For example, at group level, a MNC can contract one consulting firm to offer services to the entire group. Usually, the firm that has been contracted will ask for a block figure for the services to the entire group. However, the MNC can decide to collude with the hired firm and direct it to split the bill, so that the fees are spread across the group. With this, the MNC can ask the hired company to increase its bill in those subsidiaries where the tax is high, and reduce the amount where the tax rates are low. For instance, the MNC can pay a higher figure to a consultancy firm for its services to a subsidiary in a country like Uganda, which supports the reduction in taxable income, but pay a lower amount to the same consultancy firm for its services in a country like Mauritius.

It's hard for most tax authorities in developing countries like Uganda to discover trade misinvoicing. One of the ways of finding out misinvoicing is to share information with other countries. However, confidentiality clauses remain a barrier in unearthing these price disparities. To address this challenge, URA opted not to consider method one under the World Trade Organisation rules for determining customs value of goods being imported into the country especially used motor vehicles and instead opted for method three where it uses indicative value. The major challenge facing the indicative approach is that at times the value attached is far higher than the actual which has led to taxpayers seeking ways to avoid paying tax all together or contest the value.

Treaty Shopping

Treaty shopping is an aggressive tax planning structure that allows a company to use a subsidiary located in a jurisdiction with a low tax rate, and has special benefits for its residents, for the purpose of reducing its tax bill in another country where income is derived. The purposes of treaty shopping are usually on two levels: for a MNC to take advantage of the double taxation treaty, or, in the event that a double taxation treaty does not exist, limit the amount of information that can be divulged. For example, a number of MNCs have gone treaty shopping in low-tax jurisdictions such as Mauritius and the Netherlands because these two have signed DTTs with Uganda.

Uganda has been described as vulnerable to treaty shopping particularly through the Netherlands, Mauritius and Bermuda route. The Private Sector Investment Survey of 2014 by Bank of Uganda noted that the top ten sources of FDI to Uganda during 2013 in terms of stocks were Netherlands, Australia, UK, Mauritius, Kenya, Switzerland, India, Belgium, United States of America, and Bermuda. Hearson and Kangave (2016), show that about 95% of FDI in Uganda from the Netherlands originates from elsewhere.

Box 1: Treaty Shopping; the Case of Zain

In September 2014 an Appeals Court in Uganda ruled in favor of the Uganda Revenue Authority (URA) in the Zain case. Shares in a Netherlands company (Zain Africa BV) that owned 100% of a Ugandan telecommunications provider were transferred between two Netherlands companies (from Zain BV to Bharti A BV) and it was argued that even if taxation was allowed under domestic law, under the Netherlands – Uganda tax treaty Uganda had no taxing right preserved (there was no equivalent to the UN or OECD Article 13(4)). Uganda's tax authorities successfully applied Section 88(5) of Uganda's Income Tax Act to preserve its taxing right. This provides that: "Where an international agreement provides that income derived from sources in Uganda is exempt from Ugandan tax or is subject to a reduction in the rate of Ugandan tax, the benefit of that exemption or reduction is not available to any person who, for the purposes of the agreement, is a resident of the other contracting state where 50 percent or more of the underlying ownership of that person is held by an individual or individuals who are not residents of that other Contracting State for the purposes of the agreement."

The Court ruling overturned an earlier High Court decision that Uganda had no jurisdiction to tax. It does not finally dispose of the case but the matter was sent back to the URA to consider whether and if so what amount of gain was sourced in Uganda and taxable.

Source: Daniel K. Kalinaki (2014). The East African, (13 September 2014)

Uganda tried to address the challenge of treaty shopping under Section 88(5) of the Income Tax Act. however, there is still a challenge of underlying ownership which although is a more plausible yardstick, it creates problems due to administrative weaknesses. For example, Zain BV which owned 100% shares in Zain Africa BV decided to sell shares to Barti as a way of avoiding tax on sell of immovable property being its telecommunications infrastructure. Under the old rules, all URA needed to do was find out if the underlying ownership of Zain BV was from Netherlands in which case it would enjoy treaty benefits if any. Since the underlying ownership of Zain BV is from Netherlands, the company would enjoy treaty benefits.

Round tripping

Under this, domestic companies re-register in the jurisdiction of treaty partners, presenting themselves as if they are external investors. The companies can benefit from advantageous treaty terms, e.g. exclusion of source taxation on capital gains from the alienation of shares. This is particularly appealing if the other country has a low tax regime. For example, Ugandan companies can register and then send their profits to Mauritius to take advantage of personal tax of 22.5% as compared to Uganda's 30%, or corporate tax of 15% as compared to 30%, respectively. Round tripping also allows domestic companies to take advantage of incentives their country of origin only offers to foreign investors (SEATINI& Action Aid, 2014).

Transfer Pricing Manipulation

Transfer pricing happens whenever two companies that are part of the same multinational group trade with each other: when a Ugandan-based subsidiary of MTN, for example, buys something from a Rwanda-based subsidiary of MTN. Transfer pricing is not, in itself, illegal or necessarily abusive. What is illegal or abusive is transfer mispricing, also known as transfer pricing manipulation or abusive transfer pricing.

In most cases, two subsidiaries of a MNC trade with each other especially through management services, sometimes referred to as business process outsourcing. Management services are services that a company imports into the country, usually from its subsidiary, to support its local operations. Some of the examples of these services include: marketing, human resource training, corporate advisory services.

Management Fees

The challenges tax authorities such as URA face in assessing management services are that there is no standard market price for management services; and it's hard to prove whether a multinational's claim that management services were offered out of another jurisdiction is true. In addition, it's hard to prove whether management services should be priced using the "arms-length principle ". The arm's length price is usually considered to be acceptable for tax purposes when two unrelated companies trade with each. However, when two related companies trade with each other, they may wish to artificially distort the price at which the trade is recorded, to minimise the overall tax bill.

The URA through its investigations discovered that some imported management services, on which MNCs claim tax deductions were not needed just as it has argued. This was evidenced in its case against MTN Uganda (see Box 2).

Box 2: URA's demand for information on MTN Management Fees

In December 2011, URA issued MTN with a "notice of assessment". Its tax investigations department had audited the MTN's Ugandan operation, and issued a $69 million tax bill. This was for a number of tax issues between 2003 and 2009, but a large portion was to do with a dispute over management fees, most of which had been paid to Mauritius.

URA complained that MTN Uganda had not provided sufficient and reliable evidence of the services provided and the related costs of providing those specific services to MTN Group. URA had previously asked for evidence of specific work performed by MTN Group for MTN Uganda for each of the tax years 2003 and 2009. However, the Authority had been provided with very little information relating to 2009 and the latter years. The authority noted that the information provided by MTN Uganda was very far from justifying a payment of three per cent MTN Uganda's turnover as management fees.

This was complicated by the fact that many MNCs (such as MTN) undertake key management decisions, even those that are tax-related, at the group level. In his presentation in 2012, Hugo Vollebregt, then a partner in PWC Netherlands, noted that "Authorization levels at MTN Uganda are restricted: even the CEO of MTN Uganda has no authority to spend on marketing outside the approved budget and business plan."

In their response, through PWC their tax representatives, MTN noted that "MTN Uganda does not have in its possession any trial balances for MTN Mauritius or any other trial balances of any MTN group company that is resident outside Uganda. These documents are MTN Mauritius/MTN group's internal documents".

The decision to run MTN Uganda out of the South Africa office presents the parent company the opportunity to structure the transactions in a manner that limits the tax bill from a source country such as Uganda. This whole modus operandi left URA with some tough questions to answer: Did the parent company that procured the goods or services need them? Were the goods or services delivered? Were the goods paid for? Were there cheaper options from the local market, which could have made their importation unnecessary?

Getting to the bottom of these basic questions is extremely difficult because companies are reluctant to offer information, especially if it is from another tax jurisdiction.

Other forms of Transfer pricing manipulation including profit shifting, deliberate location of intangible assets and thin capitalization are described below.

Base Erosion and Profit Shifting

Base erosion and profit shifting (BEPS) refers to tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations. Some MNCs set up a subsidiary in a "conduit country" only to avoid being taxed in the country of operation. Instead, by using such conduit country, profits end up in developed countries, with minimal taxes paid in the countries where production happens there by eroding the tax base of source countries. Uganda is in most cases the source country for international and FDIs; meaning that this is where profits are generated.

In February 2013, the Organisation for Economic Cooperation and Development (OECD) published its report on Base Erosion and Profit Shifting (BEPS). The report revealed that the current international tax system has not kept pace with developments in the business environment providing Multi-National Corporations (MNCs) with plenty of opportunities to exploit legal loopholes and enjoy double non-taxation of income. The report further notes that taxation is at the core of countries sovereignty, but the interaction of domestic tax rules with international tax rules in some cases leads to gaps and frictions.

The deliberate choice of location for certain (intangible) assets

Intangible assets, are those assets that one cannot touch and whose fair value is hard to determine. Some of these intangible assets include brands, patents, goodwill, software, and bandwidth. Over 80 percent of the taxes collected in Uganda is from MNCs like MTN, Nile Breweries, Sab Miller, Uganda Breweries, BAT, and Century bottling among, however all of them pay for the use of worldwide brands such as coca cola. For instance,of the total $106 million that Airtel paid for Warid telecom Uganda in 2013, at least $43.6 million was valued as goodwill. An OECD report of 2016, notes the difficult of dealing with intangible assets, which multinationals use for amortization: "A number of complex policy questions remain to be fully resolved, including reforms on how companies report their investments in intangibles, as well as issues relating to the tax treatment of intangibles, which can promote or discourage investment in R&D, affect how intangibles are used, and affect how they are traded."

Most tax authorities including URA find it hard to clearly value an intangible asset that a MNC can claim a tax deduction, making it vulnerable to tax avoidance. The challenge is that Uganda does not have an instrument that shows the transfer of some intangible assets such as goodwill, leaving the URA with nothing to base on to assess taxes. Companies could also take advantage of lowering their taxable income by recording an impairment charge on goodwill, where the goodwill's carrying value on the financial statement exceeds its fair value.

In Uganda, it becomes harder for URA to tax goodwill, which companies usually use to claim a tax deduction, because goodwill does not require a transfer instrument. This can mean there is nothing to base on for purposes of tax.

Thin Capitalisation

Thin capitalization means a strategy in which a company frontloads debt from low tax jurisdictions into markets where tax rates are high. A MNC can do this by channeling money, sometimes at a higher interest rate than the market rate, into its subsidiary as part of increasing costs. By so doing, a company operating in Uganda can book the loans it is paying back as part of the costs, thereby limiting the amount of tax it should pay. However, this debt overload can be interpreted as a company's strategy to partake some of the profits out of the local company.
URA recognized the issue of thin capitalization as a tax avoidance scheme; section 89 (1) of the income tax act tries to address this challenge.It limits a thinly-capitalized company other than a financial institution from deducting interest payments in excess of the debt-to-equity ratio which is 1.5:1.

Complex structures and insufficient information

Most MNCs operate complex structures and do not provide sufficient information to tax authorities to do proper audits of their financial operations. For instance, the disclosure clauses in the Production Sharing Agreements (PSAs) in the extractive sector which are negotiated outside the tax system is a case in point. This makes it hard for tax authorities (i.e. URA) to access sufficient information when it is assessing tax on related-party transactions. Accessing information becomes more difficult in situations where the MNCs domiciles in a jurisdiction that has a double taxation treaty with Uganda; since the double taxation agreement takes precedence over Uganda's Income Tax Act. A good example is the URA's demand for information that would have helped make t a fairer assessment on MTN Uganda's management fees. Under such a system of secrecy, therefore, undertaking tax avoidance schemes becomes somewhat easier.

Exploitation of capacity deficiencies within tax authorities

Some MNCs also take advantage of capacity deficiencies within URA to detect, investigate and prosecute tax evasion and dodging. This is particularly so in relation to nascent lines of business including mobile money services, mineral extraction and intangibles.

Box 3: Capacity of URA to investigate mobile money taxes questioned

Kampala, Uganda: Lines have been drawn. MTN has moved to court amidst threats by URA to seize her money in banks, all in order to recover more than UGX 326 billion in 'unpaid' taxes. The tax alleged to be outstanding spans over a period of four years beginning 2011. URA claims that between the period under consideration MTN was declaring less earnings from mobile money and Airtime sales. And that as a result of the supposed under declarations, URA asserts, the telecom firm ended up 'dodging' payment of a total of UGX 326,996,917,906 to the national coffers.

While the tax body insisted that MTN had dodged paying the taxes in question, the telecom firm asserts how the assessment is unfounded, double taxation and grounded on lack of knowledge on part of the tax collector as far as taxation of the business of mobile money and airtime is concerned. MTN lodged the lawsuit at the commercial division of the high court on December 7th 2016 through the Kampala Associated Advocates. And to its relief, the Court's Deputy Registrar issued an interim order blocking the enforcement of URA's demand notice.

Mwambe K S (2016). The Investigator, (9, December 2016)

Corruption

Developing countries that suffer from inefficiencies in the administration and enforcement of taxes are exposed to bribing activities by companies (GIZ, 2010). Studies have shown that at least half of the revenue that should be collected can be lost by government treasuries through corruption (SEATINI Uganda, TJNA & Oxfam Novib, 2012). Opportunities for corruption among tax officials arise in the context of corrupt networks, wage differentials, corrupt management, and in the context of poor internal detection and punishment mechanisms. Officials' corrupt actions often take one of two forms: they are either abusive, whereby officers extort from honest taxpayers; or are collusive, in which case they engage with the corrupt behavior of tax avoiders (Bridi. A, 2010). Although URA tried to counter corruption through computerized tax processes which reduced the contact between taxpayers and tax officials, the vice is still rampant in Uganda.

Section 3: Review of Uganda's Tax System

Examining the adequacy or gaps in the tax laws requires an understanding of the underlying factors or enablers. The GIZ (2010) categorizes the reasons into two. First category includes factors that negatively affect taxpayers' compliance including low tax morale and high cost of compliance. Second category contains reasons for the low ability of tax administration to enforce tax liabilities primarily due to insufficiencies in the administration and collection of taxes as well as weak capacity in auditing and monitoring tax payments, which limit the possibility to detect and prosecute violators.

3.1 Tax Laws

The current laws governing Uganda's tax system include: the Constitution of the Republic of Uganda, 1995; The Local Government Act 1997 as amended (Cap 243); the Income Tax Act (ITA), 1997 (Cap 340); the Value Added Tax Act (VAT), 1996 (Cap.349); the Public Finance Management Act, 2015 [Cap 149]; the East African Excise Management Act, 2004 (Cap 28); the Stamps Duty Act, 1915 [Cap 342]; the Traffic and Road Safety Act, 1998 (Cap 361); the Gaming and Pool Betting (Control and Taxation) Act, 1968 (Cap 292); The East African Community Customs Management Act, 2004; URA Act,1991 (Cap 1996); Investment Code Act, 1991 (Cap 92); Free Zones Act 2014; and Tax Procedures Code Act, 2014.

Tax Procedures Code Act, 2014

The Tax Procedures Code Act is aimed at harmonizing and consolidating all tax procedures in Uganda. The objectives of the Act are to: adopt uniform procedures for the registration, assessment and collection of all domestic taxes; promote efficiency in domestic tax administration by harmonizing, consolidating and regulating tax procedures in a single law; and streamline and simplify the administration and collection of taxes (URA, 2016).

Income Tax Act, 1997 (Cap 340)

Since evasion and avoidance is most abundant with direct taxes, we briefly talk about the Income Tax Act, 1997 (Cap 340). The Income Tax Act (ITA) commenced in 1997 with the aim of consolidating and amending the law relating to income tax and for other connected purposes. The main objective of this action was levying tax on a residence basis, ensuring simplicity and promoting a flat tax rate scale. The government has often amended the Income Tax Act as one of the strategies of widening and deepening the tax base, and further close the loopholes that often facilitate tax avoidance and evasion. Some of the amendments include: In 2016, Section 88(5) the limitation of treaty benefits clause in Double Taxation agreements, the ratio for Thin Capitalization rules was changed to ensure the ratio of debt to equity within related companies is controlled; Section 38 and 75 in relation to losses carried forward in relation to mergers targeted the Airtel Warid Takeover; and; section 89 amended the definition of petroleum taxation.

Although the current legal framework is comprehensive, there are challenges in effective implementation of some of the provisions of these laws, partly due to weaknesses within the mandated government institutions. Some of the weaknesses are discussed in the subsequent sections of this report.

3.2 Institutions

The institutions responsible for taxation in Uganda include: a) the Ministry of Finance, Planning and Economic Development (MoFPED) which is responsible for the formulation of policies aimed at generating domestic revenue and promoting investment, consumption and savings; b) the Parliament of Uganda is mandated by the Constitution of Uganda (article 152) to authorize the imposition of any taxes. The Parliament works through committees (budget; national economy; and finance, planning and economic development) to scrutinize, analyze and consult on tax matters; c) Uganda Revenue Authority (URA), which is responsible for the assessment and collection of specified tax revenues. The URA identifies, informs and assesses taxpayers; d) the Uganda Financial Intelligence Authority (FIA) is mandated with tackling illicit financial flows (IFFs) in Uganda.

The performance assessment of URA done by IMF in 2015 identified some of the weaknesses that can facilitate tax evasion and avoidance:

- Low level of certainty as to the accuracy of the taxpayer registration database.
- Weak initiatives to detect businesses, which fail to register and fall short of good international practice.
- Mechanisms to identify, assess, and prioritize risks are not well structured and limited evidence of comparative evaluation and measurement of risks.
- Process of compliance risk mitigation does not adequately address all risks. There is no structured approach to evaluate and prioritize these risks.
- On-time return filing rates are low while information on timely payment of taxes is not monitored.

According to Namugumya D.S (2016), URA is yet to start employing external industrial experts to provide assistance with cross border audits. Input from specialists for example trade sector advisors, experts for brand value and corporate finance specialists would help the tax officers get a better understanding of the business environment of MNEs. The experts could also help with the valuation of intangible assets, which is a challenge for most tax administrations.

There are political constraints related to the power relations around taxation. The top leadership of URA has become powerful and has the bargaining power to resist reform and to get away with extracting revenues for private gain. The on-going oil handshake saga is a manifestation of this power. Furthermore, it is difficult to levy taxes especially if they affect the relatively wealthier people who have more political influence. This was the case for Members for Parliament who exempted themselves from paying tax.

For Uganda to reduce tax evasion and avoidance, the responsible institutions have to be strong. However, limited funding and staffing hinders these institutions from effectively implementing their mandates. It is also important to note that the political clout that MNCs enjoy sometimes makes it difficult for institutions to undertake their mandate. Some of these MNCs have hired well-connected officials, such as Chairpersons on their board of directors, who help them during lobbying on matters of taxation.

The limited collaboration among institutions, especially when it comes to sharing information, weakens the capacity of institutions to curb tax avoidance. A clear example of this can be seen from the Auditor General's complaint over the URA's reluctance to release information because it is bound by confidentiality clauses.

3.3 Reforms aimed at elimination tax evasion and avoidance in Uganda

Over the last decade Uganda has developed reforms geared at eliminating tax evasion and avoidance, among them include:

- Amendment of tax laws
  - The Income Tax Act Cap 340 is annually amended to increase tax revenue by widening and deepening the tax base. Some amendments were made in 2016 include:
    - **Carry forward losses in relation to mergers and acquisition.** Section 38 and section 75 were harmonized; section 75 provides that underlying ownership of companies should not change by 50% or more otherwise special conditions apply.
    - **Double Taxation Agreements (DTA).** Clarification of conditions under which businesses may benefit from reduced tax rates under S.88(5). Changes that were made are; Public Limited Companies are excluded from the restrictions. Any other company with substantial operations in the DTA country can also benefit from favorable treaty rates if they are the beneficial owners.
    - **Petroleum Sector:** Aligned provisions of the Income Tax Act to the Petroleum Act and PSAs.

  - In 2014, GoU enacted a Tax Procedures Code Actto guide and harmonise the administrative procedures of the current tax laws hence easing the compliance process for taxpayers.
  - VAT Act (amendment 2016). Such as: a) Business Process Outsourcing; the person providing the service will claim VAT credit on services imported. In this case URA will issue a Practice Note to define Business Process Outsourcing. b) Midstream Petroleum Operations; provision for VAT registration will enable companies to claim VAT refunds in the midstream petroleum operations. c) Re-classification of items under standard rated and exempt.

- **Combating international tax evasion and avoidance schemes**

To deal with treaty shopping, Article 88(5) of the clause in the Income Tax Act was amended to include a clause on anti-avoidance aimed at denying treaty benefits to a treaty party if the "underlying ownership" of that party was less than 50 percent of shareholdersresident in a country that was signatory to the treaty. However, in 2016, the clause was amended again probably to appease investors. The new amendment sought to bring about more moderation in determining whether to deny or allow the benefits by bringing in aspects of beneficial ownership under which legal ownership and economic ownership are considered. It made it impossible to just deny treaty benefits just because of the 50% underlying ownership aspect but called for a more complicated way of determining beneficial ownership for treaty benefits to be considered. In a complex structure of the multinationals, authorities such as the URA might find it hard to know the identity of beneficial ownership.

In 2011, GoU introduced transfer-pricing rules to ensure that transactions within related entities are priced fairly and reflect an arms-length fee.

URA charges a non-claimable 18% VAT on the importation of IT and BPO services into Uganda. While the 18% VAT charge limits the multinational's use of BPOs as tax avoidance conduits, other East African countries allow companies reclaim the tax. There are complaints from an association of business process outsourcing that the 18% tax charge portrays Uganda as an uncompetitive environment for companies to do business.

As a measure of limiting thin capitalization, under article 89 of the ITA, government placed the debt to equity ratio that a foreign-controlled company, other than a financial institution must hold in excess of 1.5:1. This was meant to reduce the revenue leakages due to tax planning by foreign companies.

In addition, Article 90 and 91 of the ITA handles the tax avoidance issues.Section 90 authorizes the Commissioner to distribute, apportion or allocate income, deductions or credits between or among related taxpayers to clearly reflect income.

Section 91 allows the commissioner to re-characterize a transaction or an element of a transaction that was entered into as part of a tax avoidance scheme.

- **Double Taxation Treaties (DTTs):** DTTs are intended to eliminate taxpayers being taxed twice for cross-border flows of goods and services. However, DTAs are open to abuse especially if the design is not well structured. Consequently, the Government of Uganda suspended negotiations on new tax treaties until there are clearer guidelines on how the country should benefit from such agreements. Government currently has a policy to guide negotiation of double taxation treaties.

- **Computerization of tax processes:** The URA has a fully functional web portal (www.ura.go.ug) that facilitates taxpayer registration and the acquisition of Tax Identification Numbers (TIN). The URA e-tax system facilitates the filing of returns for domestic tax. It allows taxpayers to register payments and file tax returns online. For international trade taxes, the authority uses a customs data system called ASYCUDA WORLD. Recent trade facilitation improvements include the introduction of an electronic cargo tracking system to track the movement of goods through East Africa. The computerized tax processes improved both administration and reduced the contact between taxpayers and tax officials in order to counter corruption.

- **Strengthening the capacity of URA.**

- In March 2016, URA set up a specialized unit, the International Taxation Unit (ITU) based in the Large Taxpayers' Office, which, among others, handles the transfer pricing issues. The ITU has built capacity in investigating transfer pricing with facilitation from the African Tax Forum, World Bank and the International Monetary Fund. The ITU is being expanded following a phased approach over a period of three years and will ultimately have about 25 staff by the year 2019/2020. The unit will also commence issuing Advanced Pricing Agreements in the year 2018/2109.

- URA also entered into partnerships with tax authorities and organisations like the African Tax Administration Forum and the Kenya Revenue Authority, as it beefs up its international and related party audit capacity.

- **Taxpayer Registration Expansion Project (TREP).** URA in collaboration with Uganda Registration Services Bureau (URSB), the Kampala Capital City Authority (KCCA) and local governments rolled out the Taxpayer Registration Expansion Project (TREP) and is earmarked to expand URA's tax register by 103,570 value clients (clients who submit returns and pay income tax) and generate revenue worth UGX 12.9 billion (URA, 2014).

- **Penalties for tax evasion.** The Tax Procedure Code Act 2014, provides for various penalties for default in furnishing tax returns, failing to maintain proper records, making false or misleading statements and understating provisional tax estimates. For example, the penalty for failing to furnish tax returns is 2 percent of the tax payable under return or 10 current point per month, whichever is higher. For failure to keep proper records, the penalty is double the amount of tax payable for the period to which the failure relates. These penalties should be able to deter tax evasion, the challenge is effective implementation.

Section 4. Corporate Income Tax in Uganda

4.1 Uganda's CIT structure

Corporate Income Tax (CIT) is collected from companies, based on their net income. Companies resident in Uganda are taxable on their worldwide income and gains, while non-residents are taxed on income sourced in Uganda. The income tax rate applicable to the chargeable income of companies is 30 percent, with the exception of: mining companies; non-resident air transport, shipping, and some telecommunication services; and resident companies with a turnover below UGX 150m. A rate of 1.5 percent of turnover is used to determine income tax payable by a resident company with turnover between UGX 50m and UGX 150m. However, on application to the Commissioner General of URA, a resident company with a turnover of less than UGX 150m may be taxed at 30 percent. This category excludes professionals, public entertainment services, public utility services, or construction services (PWC, 2016).

Table 2: Uganda's CIT structure

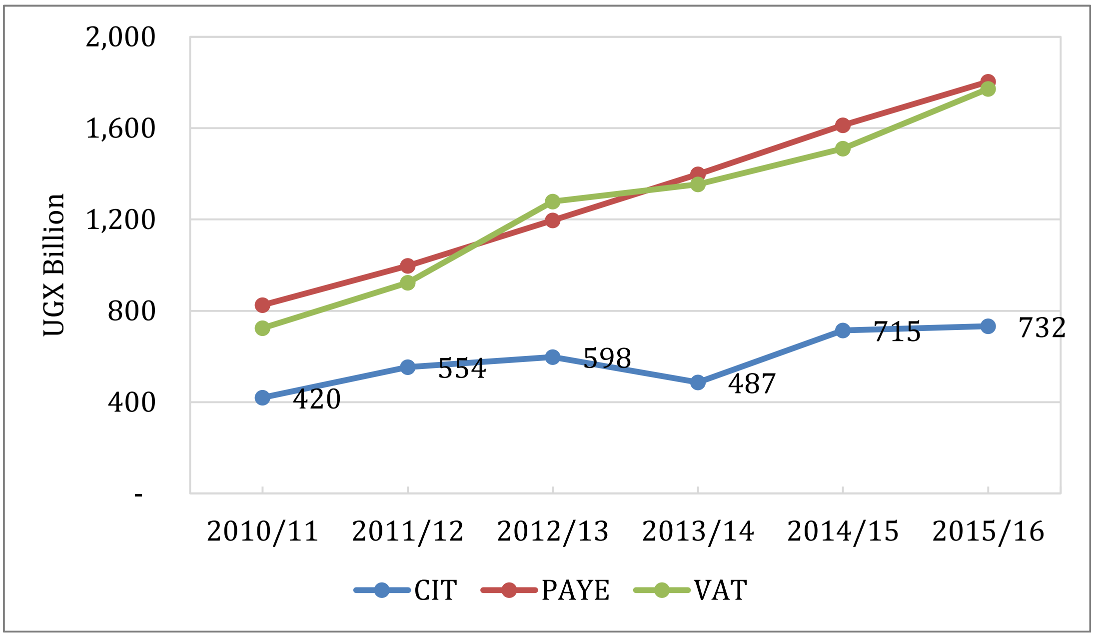
Tax rate	Exemptions	Remarks
30 percent for resident companies	Dividends received by a resident company from another resident company, of which it owns more than 25 percent of shares.	A company may adopt a tax year different from the normal July–June FY with the consent of the commissioner
2 percent for non-resident shipping and aerospace companies.	2 percent of income tax payable can be deducted for companies with at least 5 percent of full-time employees are persons with disabilities.	A provisional return must be filed within six months of the start of the company's accounting year.
25–45 percent for mining companies1		The estimated tax for the year is payable in two installments before the end of the first six-month period and before the company's year-end. A final return and balance payment is due within six months at the financial year.

Source: PWC (2016)

4.2 Corporate Income Tax Performance

Uganda has seen a significant increase in tTtal Tax Revenue (TTR) in the recent past. Net collections by URA (excluding Govt. taxes and Tax refunds) have grown from UGX 5.1 trillion in 2010/11 to UGX 11.23 trillion in 2015/16. Corporate Income Tax (CIT) grew by 74 percent from UGX 419.6 billion in FY 2010/11 to UGX 732.2 in FY 2015/16. This increment is far below that of PAYE and VAT which grew by 118 and 145 percent respectively as shown in figure 1. CIT.

Figure 1: Trends in CIT, PAYE & VAT Revenues (FY 2010/11- 2015/16)



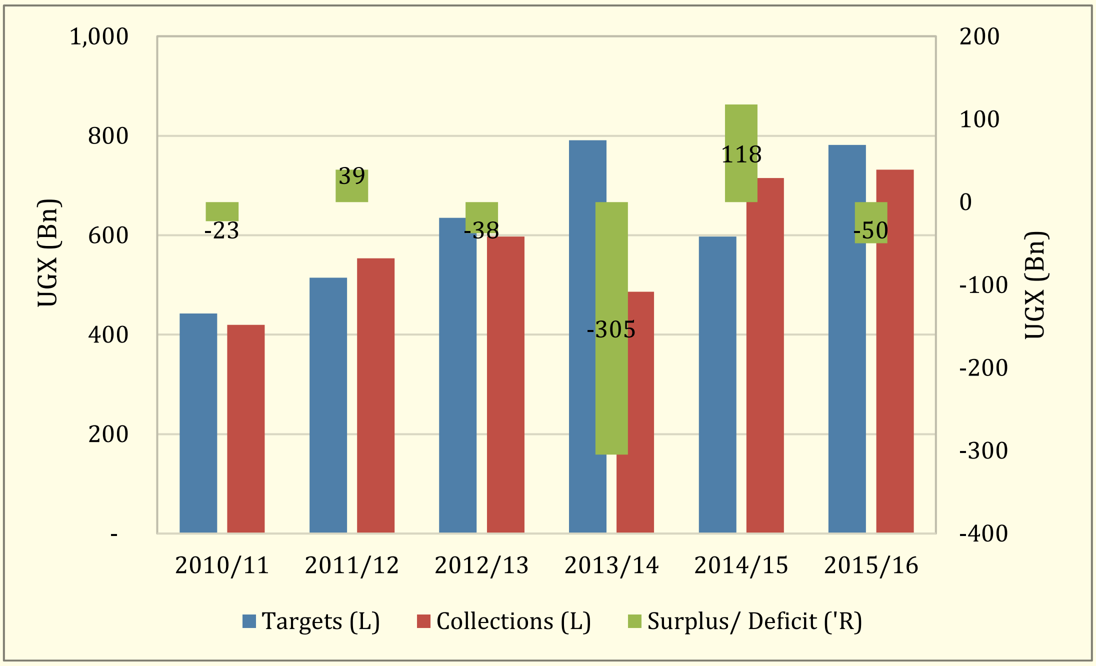
Source: Author's calculations based on URA Statistics

Corporation taxes in developing countries tend to be fairly inefficient. Provisions that make sense in more developed economies tend to narrow the CIT tax base without providing any noticeable incentive. For example, multiple rates differentiated along sectoral lines, exemptions for certain sectors, and the allowable depreciation of physical assets for tax purposes tend to narrow the tax base (Kiyaga L, 2007). In addition, carry-forward loss provisions in ITA Section 38 for companies that farm out, merge or simply close businesses also affect CIT collections in Uganda. URA revenue performance reports reveal that corporate tax collections posted an average annual deficit of UGX 43 billion between 2010/11 and 2015/16 as shown in figure 2.

URA attributes the poor performance of CIT to the slowdown in the economy and low profitability especially for the telecom industry. However, some analysts disagree with URA's claim, noting that the main factor behind the drastic fluctuation in CIT is not gradualshift in the profitability of companies but rather aggressive tax planning structures of MNCs.

For instance, some companies might be using more sophisticated means to reduce their tax bills, regardless of the profits they make. For example, when you examine MTN Group's financial statement for the year 2015. The MTN group noted that MTN Uganda, the biggest telecom firm in Uganda (which accounts for a market share of 51.1%) reported a 2% increase in revenue compared to 2014 and a slight 4.7 percentage point drop in Earnings Before Interest, Tax, Depreciation and Amortization (EBITDA) over the same period. Although there are many factors to consider before tax is deducted, both figures on MTN Uganda are far lower than the average drop in corporate income tax paid over the same period, which is 23%. There was a far bigger drop in the average corporate income tax paid than the fall in earnings some telecom companies reported.

Figure 2: Trends in CIT performance (FY 2010/11- 2015/16)



Source: Author's calculations based on URA Statistics

While there is no information on the compliance rates for CIT in Uganda, there are indications that tax compliance is generally low. For instance, a 2014 report by the IMF showed that the VAT compliance gap – the difference between potential VAT revenues under the current legislation and actual VAT revenues - could amount to 60%, or 6% of GDP. Another study by the International Growth Center (IGC) in 2015 found that 87% of the seller-firms in the sample declared amounts lower than those declared by the buyer. The study estimated non-declared sales of about UGX 4,148 billion. Applying a standard rate of 18% yields an estimated VAT compliance gap of UGX 747 billion. The IGC observed that most of the miss reporting by firms constituted tax evasion.

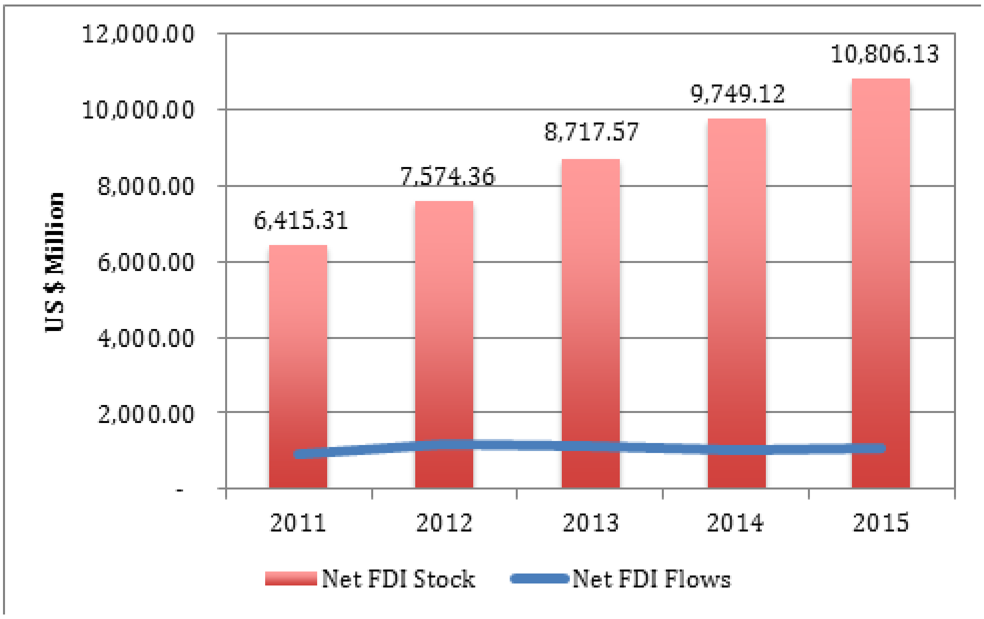
4.3 Challenges facing the corporate income tax regime in Uganda

The corporate income tax regime in Uganda faces two basic challenges namely incomplete and inconsistent rules applicable to different types of income, which can be attributed to poor policy design, poor tax administration or both. Other related challenges include:

Tax incentives and exemptions

One of the major reasons for tax incentives and exemptions is the desire to attract investment. Uganda's fiscal incentive package for foreign investors provides generous capital recovery terms, particularly for medium and long-term investors whose projects entail significant plant and machinery costs and involve significant training (US Department of State, 2014). However there are indications that the gain from investment due to tax incentives less than compensates for lost income. Data from UNCTAD shows that while inward FDI in Uganda has been on the increase reaching US$ 10.8billion in 2015, there has been no significant change in the level of Net FDI flows as shown in figure 3. This means that the increase in inward FDI stock has been matched by a similar increase in outward FDI. This appears to weaken the argument of providing tax incentives with the aim of attracting investment.

Figure 3: Inward FDI stock and Net FDI flows



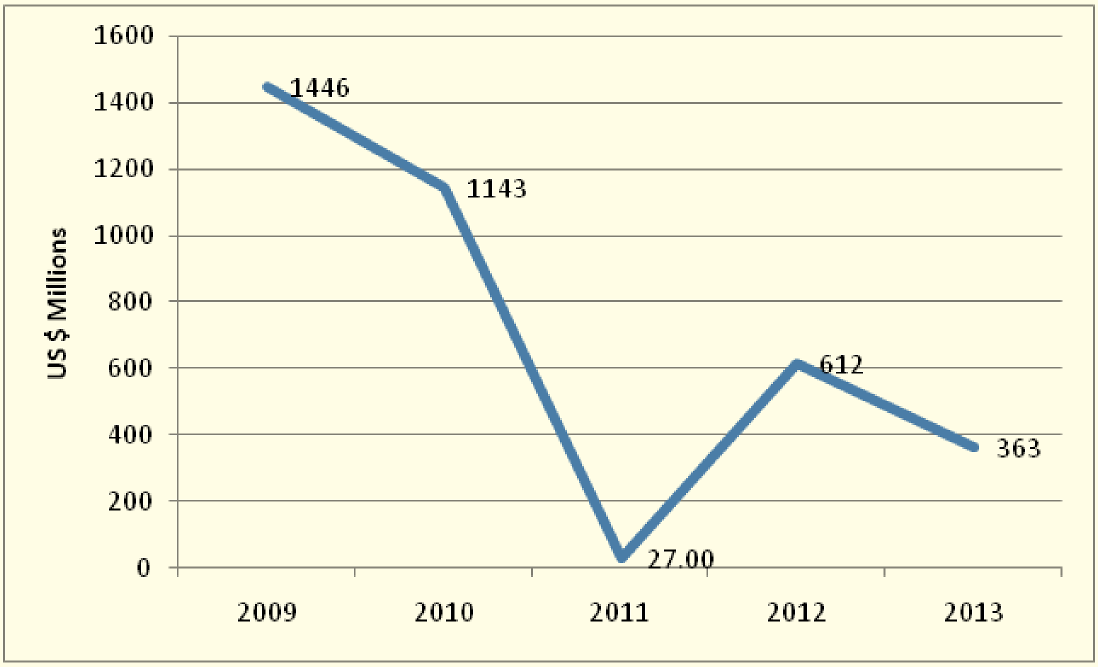
Source: Authors calculations based on UNCTAD data 2016

The biggest challenge is that currently Uganda does not have a clear policy about how tax incentives and exemptions are awarded to investors(SEATINI, 2013). The Minister of Finance has the power to grant tax and non-tax incentives, as well as waive the tax due depending on the reasons and evidence provided by the URA Commissioner-General. Although Uganda's Constitution (Article 152(2)) obliges the Minister of Finance to provide information on how much tax the government directly paid on behalf of some taxpayers. However, parliament cannot legally reverse the minister's decisions; therefore, the proper and equitable use of these broad discretionary powers is open to abuse (SEATINI, TJNA & Oxfam, 2016). Theinconsistent application of waivers and exemptions based on favoritism and intense lobbying by some MNCs. Most MNCs possess high bargaining power towards government officials. Tax incentives for foreign investments not only enable foreign firms to avoid taxation but in turn give rise to illegal tax evasion activities of domestic companies e.g. by re-labelling domestic investments as FDI (round-tripping) or selling businesses to subsidiaries disguised as new investors as a means to become eligible for tax holidays that are exclusively granted to new investors (double dipping) (GIZ, 2010).

Illicit Financial Flows

Illicit financial flows (IFFs) are money illegally earned, transferred or used, by means including: undocumented commercial transactions or purely criminal activities such as overpricing, transfer pricing, tax evasion, money laundering, corruption and false declarations. While data from the Global Financial Integrity (GFI) shows that IFFs from Uganda are on a downward trend since 2009 as shown in Figure 4, the amounts involved remain substantial. It is estimated that about US $ 3,591 million left Uganda in IFFs between 2009 and 2013. Applying a 30 percent tax rate brings the loss in CIT to US$ 1,077 million over this period. This could be on a higher side; considering not all the money lost to IFFs may necessarily affect CIT collections.

Figure 4: Illicit Financial Flows from Uganda 2009 -2013



Source: GFI at www.gfintegrity .org accessed on March 16, 2016

Uganda is among the countries that adopted the Mbeki High-level report on IFFs in Africa titled 'Track it. Stop it. Get it.' at the 24th African Union Summit in Addis Ababa in January 2015. According to the United Nations Economic Commission for Africa, one of its recommendations was to establish or strengthen the independent institutions and agencies of government responsible for preventing IFFs. The Uganda Financial Intelligence Authority (FIA) is the institution mandated with tackling IFFs in Uganda (Republic of Uganda, 2013). However, inadequate funding has hindered the performance of the FIA; the authority was allocated only UGX 7.45 billion in FY 2016/17.

Double Taxation Treaties (DTTs)

Double Taxation Treaties (DTTs) are meant to regulate taxation in multiple jurisdictions to avoid duplicate taxation. In general, DTAs tend to among others: define which taxes are covered and who is a resident and eligible for benefits; and reduce the amounts of tax withheld from interest, dividends, and royalties paid by a resident of one country to residents of the other country. Uganda is a signatory to ten DTTs . However, DTTs are prone to exploitation in low tax jurisdictions. MNCs re-route investments through such locations, avoid paying taxes due in the countries where they invest. Uganda signed a DTT with Mauritius, which is regarded as one of the most harmful DTAs in Africa (Ochola J, 2014). According to Ochola, the DTTs that Mauritius has signed confer a number of benefits to companies that are resident in the country. Among the benefits is the exemption from Capital Gains Tax (CGT). This means that companies investing through Mauritius completely avoid paying CGT and are able to keep huge profits from monies due as tax.

Uganda negotiated DTAs based on the OECD model which favours resident countries as opposed to source states. For instance, URA faced a legal hurdle when Zain Africa International BV and Heritage Oil argued that the tax on the sale of their Ugandan units was a subject for the jurisdictions in which they had been incorporated – Zain for Netherlands and Heritage for Mauritius. Heritage re-domiciled in Mauritius to take advantage of the DTA with Uganda and ZAIN cleverly usedthe existing DTA between Netherlands and Uganda to avoid crafting the sale as a sale of immovable property situated in Uganda which would be taxable in Uganda to employing a share sale which is taxable in the residence state and not Uganda.

Conversion and Transfer Policies

Uganda keeps open capital accounts, and Ugandan laws impose no restrictions on capital transfers in and out of Uganda. MNCs can obtain foreign exchange and make transfers at commercial banks without approval from the Bank of Uganda in order to repatriate profits and dividends, and make payments for imports and services. Somehow this facilitates tax evasion and avoidance.

Inadequate capacity to detect and prosecute tax evasion

The difference between tax dodging and avoidance is not as clear as it should be to invoke punitive sanctions. Muscagni and others (2014) argue that typically transfer pricing and other practices aimed at tax avoidance are not illegal and they therefore cannot be strictly labelled as tax evasion. Instead they are the result of increased globalisation in production processes, international competition amongst countries to attract capitals, and the aggressive exploitation of grey areas in tax laws. In many instances tax related cases involving MNCs in Uganda are decided out of court and their litigation a protracted spectacle.

Section 5. Conclusions and Recommendations

5.1 Conclusion

Tax evasion and tax avoidance or dodging by MNCs and individuals is a great concern in many developing countries including Uganda. Conservative estimates by GFI based on illicit flows puts the loss of CIT at about US$ US$ 1,077million. This means that MNCs in Uganda are deliberately or otherwise engaging in tax dodging. This is largely through mispricing, misinvoicing, transfer pricing and in some cases engaging in outright corruption tendencies. While Uganda has enacted a number of amendments to its tax laws aimed at closing the loopholes used by MNCs and individuals to evade or dodge taxes, there are still challenges with non-transparent provision of tax incentives and exemptions; abating illicit financial flows; exploitation of DTTs by MNCs; and inadequate capacity to detect and prosecute tax evasion. In addition, the ever-changing business landscape presentsnew challenges to the Uganda's tax regime.

Against this, we recommend the following:

5.2 Recommendations

5.2.1. Ministry of Finance Planning and Economic Development

a. Should fast track thereview of the existing DTTs, particularly those with so-called conduit jurisdictions, often used by MNCs in their tax avoidance schemes.
b. Should enter into a memorandum of understanding with some of the countries it does not have a double taxation treaty with in order to access information about multinational entities
c. Should amend policies to allow more access to information of companies of public interest. At the moment, institutions such as the URA, which are bound by confidentiality clauses, do not release enough information to offices such as the Auditor General's, making it harder for a tax audit trail.
d. Promote transparency and accountability in the provision of tax exemptions as part of minimizing cases of tax avoidance.
e. Spearhead a comprehensive review of the legal framework in Uganda including other laws, regulations to identify contradictions and their implications for generation of tax revenue.
f. Ensure greater collaboration between BoU and Financial Intelligence Authority on tracking financial transfers for purposes of detecting tax evasion and money laundering.
g. Introduce foreign exchange control measures where all transfers above a certain amount are approved by BoU upon ascertaining that all taxes due are paid. This measure also has the benefit of controlling the capital flight.
h. Should ensure that the fiscal regime is transparent and provides guidelines for PSAs. There should be a combination of royalty and a tax targeted explicitly on rents, in addition to the corporate income tax applied on all businesses.

5.2.2. Uganda Revenue Authority

a. Should ask for clearer information on taxes from multinationals. There should be an addition of two new columns on the tax form- one for offshore income on which the MNC is deferring taxes and another to capture the company's reserves for "uncertain tax positions.

b. Build capacity of its staff to detect and investigate tax dodging by MNCs particularly in the newly emerging businesses with peculiar structures including intangibles in the mining and services sector. This can be done through placements, internships in countries where practices are more advanced.
c. Allocate more resources both financial and human for tax audits of MNCs. This will enable the authority to investigate potential cases of tax dodging and evasion.
d. Increase sharing of information with other revenue authorities around the world. This will enable the authority to get more information on tactics like thin capitalization and transfer price manipulations used by MNCs.

5.2.3. Parliament

a. Should amend all laws, which facilitate tax evasion and avoidance.
b. Should subject all tax exemptions including those in DTTs and PSAs to parliamentary approval. This will rid the country of problems related to arbitrariness of tax exemptions witnessed in the past.
c. Should demand for periodic reports on tax exemptions to ensure that they serve their purpose and where necessary revisions made. This report should indicate the beneficiary companies, the amount of tax revenue foregone and progress on achievement of objectives for the exemptions.

References

AfDB (2010). Domestic Resource Mobilization for Poverty Reduction in East Africa: Uganda Case Study

Bank of Uganda (2014), Private Sector Investment Survey Report.

Bridi.A (2010).Corruption in tax administration.U4 Expert Answer. Transparency International

EAC Secretariat (2015), East African Community Facts and Figures 2015.http://www.eac.int/statistics/index.php?option=com_docman&Itemid=153

GFI at www.gfintegrity .org accessed on March 16, 2016

Hearson and Kangave (2016).A Review of Uganda's Tax Treaties and Recommendations for Action.

IGC (2015). Fiscal Capacity and Tax Revenues in Uganda

International Monetary Fund (2012). 'Fiscal Regimes for Extractive Industries: Design and Implementation' Prepared by the Fiscal Affairs Department.

IMF (2014). Uganda- Revenue Administration Gap Analysis Program- The VAT Gap

IMF (2015). Tax Administration Diagnostic Assessment Tool: Performance Assessment Report- Uganda

IMF (2015).Fifth Review Under the Policy Support Instrument and Request for Waiver of an Assessment Criterion and Modification of Assessment Criteria—Debt Sustainability Analysis

Kaggwa M. (2013). FDI in Uganda and its Implications for the Economic, Social and Cultural Rights of Ugandans.

Kalinaki D.K (2014). Court gives URA nod to seek taxes on sale of Zain assets in Uganda. The East African, 13 September 2014 http://www.theeastafrican.co.ke/news/URA-taxes-on-sale-of-Zain-assets-in-Uganda/2558-2451578-hsf0gfz/index.html

GFI (2014). Hiding in Plain Sight

Kiyaga L (2007). Tax Policy Challenges Facing Developing Countries: A Case Study of Uganda. Queen's University Kingston

Mwambe K.S (2016). Money Blues: MTN Uganda Faces Shs326B Tax Evasion Scandal as URA Talks Tough. The Investigator (9, December 2016).

Namugumya D.S (2016). Transfer pricing of intangible assets: The case of Uganda. African Tax Research Network and the African Tax Administration Forum

Ochola J (2014). Double Taxation Agreement: implications for Social service delivery. Econews Africa. Naivasha 27th June 2014

PWC (2016). Uganda Corporate – Taxes on corporate income. http://taxsummaries.pwc.com/uk/taxsummaries/wwts.nsf/ID/Uganda-Corporate-Taxes-on-corporate-income

Republic of Uganda (2014). Tax Procedure Code Act 2014

Republic of Uganda. (2013). Anti-Money Laundering Act 2013

SEATINI (2013). Tax Incentives and Exemptions in Uganda: Implications on Domestic Revenue Generation

SEATINI and Action Aid. (2014). Double Taxation Treaties in Uganda: Impact and Policy Implications. http://www.seatiniuganda.org/publications/research/72-double-taxation-treaties-in-uganda-1/file.html

SEATINI Uganda, TJNA & Oxfam Novib (2012). Taxation State-Building and Governance

SEATINI, TJNA & Oxfam (2016). Fair Tax Monitor: Uganda

UNCTAD (2016). Inward and Outward Foreign Direct Investment Flows and Stock. https://knoema.com/UNCTADFDI2016/inward-and-outward-foreign-direct-investment-flows-and-stock?location=1002150-uganda

UNECA (n.d). Advocacy in Global Processes: Towards Implementing the Recommendations of the AU/ECA High Level Panel on Illicit Financial Flows (IFF) from Africa. http://www.regionalcommissions.org/iffbkg.pdf

URA (2014). Tax Register Expansion Project (TREP) to tap into the informal sector: https://www.ura.go.ug/download/CGMS/TREP_FINAL.pdf

URA (2015). Performance - Statistics (collections 1991-2016) https://www.ura.go.ug/topmenu/topmenuMain.jsp?viewPageNo=5#

URA (2016). Tax Policy Changes FY 2016/2017

GIZ (2010).Addressing tax evasion and tax avoidance in developing countries.

SEATINI Uganda
Plot 806, Block 213, Bukoto - Kisaasi Road
P.O BOX 3138, Kampala
Tel: +256 414 540 856
Email: seatini@infocom.co.ug
Website: www.seatiniuganda.org