A LEGAL ANALYSIS OF TAX INCENTIVES IN ENCOURAGING FOREIGN DIRECT INVESTMENTS IN THE OIL AND GAS SECTOR OF UGANDA: A CASE STUDY OF TAX HOLIDAYS

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A DISSERTATION SUBMITTED TO THE FACULTY OF LAW IN PARTIAL FULFULMENT OF THE REQUIREMENT FOR THE AWARD OF MASTER OF LAWS IN OIL AND GAS LAW AT THE INSTITUTE OF PETROLEUM STUDIES KAMPALA IN AFFLIATION TO UCU.

MAY, 2023

DECLARATION

I, *Muhindo Kithula Harriet*, declare that this dissertation is my work and it has not beensubmitted before to any other institution of higher learning for the fulfillment of any academic award.

Signed: ....

Date: ....

APPROVAL

I, certify that this dissertation entitled ―*A Legal Analysis of Tax Incentives in encouraging Foreign Direct Investments in the Oil and Gas Sector of Uganda: A Case Study of Tax Holidays*‖ was done under my guidance and satisfies the partial fulfillment of the requirements for the award of the Master of Laws Degree (LL.M) in Oil and Gas.

Signature…………………………………………………….

Mr. UMARWOTH Robert

University Supervisor

Date ………/………/……………………...

DEDICATION

This study is dedicated to my husband, Edgar Kizza and sons Nigel Mumbere, Nathaniel Louis Bwambale, and Anselm Masereka Kyomuhendo for loving and supporting me through my study.

Mwasingya Kutsibu

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First my heartfelt gratitude goes to God the Almighty who has seen me through this journey in my studies. I will forever glorify his name.

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Finally, I acknowledge with a deep sense of reverence, my gratitude towards my family and friends who have supported me morally as well as economically.

Thanking you very much.

MUHINDO KITHULA HARRIET

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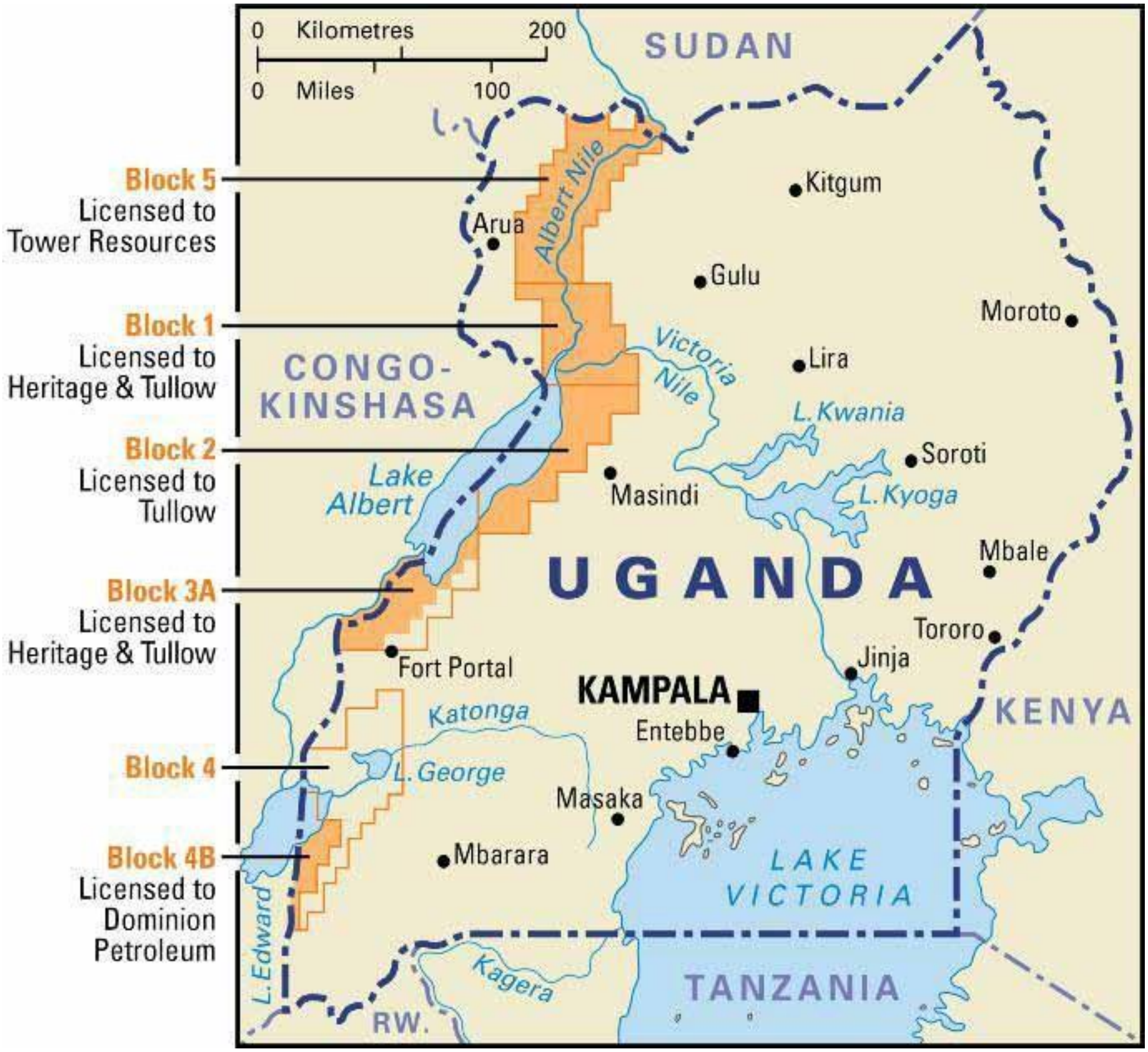

Source: - Petroleum Exploration Production Department, August, 2009

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- National Content Policy for the Petroleum Subsector in Uganda: Ministry of Energy and Mineral Development (February 2017).
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- Petroleum Authority of Uganda (August 2018): Current Status of the Oil and Gas Sector in Uganda.
- Production Sharing Agreement (PSA) for Petroleum Exploration Development and Production in the Republic of Uganda.
- Taxation Handbook: A Guide to Taxation in Uganda. © Uganda Revenue Authority 2015.
- The National Content Study in the Oil and Gas Sector in Uganda, September 2011.
- The Petroleum Authority of Uganda; Implementation of the national Content Policy: Progress and Challenges (September 2018).
- Uganda Vision 2040.

LIST OF KEY ACRONYMS

CIT	Corporate Investment Tax
COMESA	Common Market for Eastern and Southern Africa
FDI	Foreign Direct Investment
ITA	Income Tax Act
LNG	Liquefied Natural Gas
PAU	Petroleum Authority of Uganda
PEPD	Petroleum Exploration and Production Department
PSA	Production sharing Agreement
PSCs	Production-Sharing Contracts
PURA	Petroleum Upstream Regulatory Authority
TAT	Tax Appeals Tribunal
TIA	Tanzania Investment Act
UBOS	Uganda Bureau of Statistics
UDEAC	Central African Customs and Economic Union
UIA	Uganda Investment Authority
UNCTAD	United Nations Conference on Trade and Development
UNOC	Uganda National Oil Company
URA	Uganda Revenue Authority
VAT	Value Added Tax
WHT	Withholding Tax

ABSTRACT

This study focused on performing a legal analysis on the role of tax holiday as an incentive for encouraging Foreign Direct Investments in the Oil and Gas Sector of Uganda. The study was guided by two major specific objectives which were to analyze the effectiveness of the laws relating to tax holidays in encouraging FDI and to explore the corresponding flaws associated to offering tax holidays in the Uganda ‘s oil and gas sector. The overall study adopted a qualitative doctrinal legal research approach in carrying out the study. The researcher chose a case study research design to guide the investigation process of the legal phenomenon under study used a systematic literature review method as the methodology for collecting data. The study disclosed that the law provides for tax credit under the income tax Act, that imposes heavy tax value added tax under Value Added Tax Act 1996 (VAT), imposes duty tax under the Exercise Management Act (1970) to be paid by the licensee investors. The study further revealed that tax holidays generally place a significant burden on tax administration and on taxpayers at large. It is recommended that other mechanisms like enhanced transparency and overall improvement of investment climate should be used to attract FDI in oil and gas industry.

Key Words: Tax holidays, Foreign Direct Investment, Oil and gas Industry

CHAPTER ONE

GENERAL INTRODUCTION

1.1 Introduction

It is worth noting from the on-set beginning that experiences from other oil producing countries like United States of America, Norway among others have showed that the entire process of oil and gas production require a very versatile capital investment. However, most host governments especially those in developing countries with huge endowment of various mineral deposits such as South Sudan, Democratic Republic of Congo (DRC) among others lack the capital muscles to exploit the minerals, this is where the involvement of foreign direct investment (FDI) becomes necessary.

In regards to the above, it is important to note that FDI companies are attracted by favorable investment environment[1]; these among other things includes the existence of fair and attractive legislative and policy tax system. In association to the aforementioned, some scholars have argued that tax policies have the overriding capability of influencing the desire of foreign direct investors since higher tax burden invariably means lower investment returns, thereby reducing willingness of investors to commit their investment funds.[2]Further, it has been severally noted that a country‘s tax regime in one way or the other plays a very vital role in determining a positive or negative investments[3].

The focus of this thesis is to examine how Uganda tax policy can play a lead role in attracting the much needed capital from foreign direct investors in order to be able to finance its huge oil and gas capital industry. Therefore, this introductory chapter encompasses among other things; the background information of the study, the problem statement, the research objectives, the research questions, scope of the study, the justification of the study, and the conceptual framework.

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[1]Morisset, J., & Pirnia, N. (2000). How tax policy and incentives affect foreign direct investment: a review.
[2]Gordon R.H. and Hines J.R. (2002): International Taxation and Multinational Activity in the Organization for Economic Corporation and Development policy frame Work Paper Series 8854at www.OECD.org.ECO.Public-Finance. Accessed 1st April 2021.
[3]Lim, E. G. (2001). Determinants of, and the relation between, foreign direct investment and growth a summary of the recent literature

1.2 Background to the Study

For the purpose of achieving a comprehensive introduction and analysis to this study, the researcher opted to adopt a four model aspect of writing the background to the study which will be sub-divided into thematic areas as following; a historical, theoretical, conceptual and contextual perspectives as seen below.

1.2.1 Historical Background

The history of oil and gas discovery in Uganda has its history that dates back to the late 19th century when local communities discovered oil; see pages in areas along the Albertine region. The discoveries were subsequently documented by Emin Pasha in 1877 and later by British colonial administrator and explorer in the name of Fredrick Lugard in 1890.[4]However, in the later years around the 20th century, there was an irregular exploration that took place but was heavily hindered by geopolitical events.[5]But later on in the early 1920‘s, there was an aggressive and significant oil exploration which led to a substantial amounts of hydrocarbons traced in the Albertine Graben.[6] This discovery was later to be followed by the first ever drilling of wells that took place later in 1938. Additional, exploration was carried in the 1940‘s and 1950‘s and several shallow wells were bored mainly for strategic purposes.[7]

It should be recalled that, oil and gas undertakings were profoundly interrupted by major political turmoil that withered the country for considerably several years not until the 1980‘s when aeromagnetic data across the entire Graben region was obtained. Interesting, the continuous aeromagnetic surveys that were carried out during the period between1983 and 1992 produced a magnificent hint to suggest that perhaps Uganda had the prospects of further oil reserves.[8]After a long spell of exploration, the existence of commercially viable quantities of oil

[4]Low, D. A. (2009). *Fabrication of empire: The British and the Uganda kingdoms, 1890-1902*. Cambridge University Press.
[5]Bassam Farrouh (2015): Hard bargaining and complex politics in East Africa, the Oxford Institute for Emerging studies, October, 2015.
[6]Kasimbazi. E. (2016): Legal and Environment Dimension of oil exploration in Uganda.
[7] Ibid.
[8]Sebastian Wolf & Vishal Aditya Potluri (2018): Uganda‘s oil, how much, when and how it will be governed, WIDER Working Paper 2018-179 December 2018, united Nations University Institute for Development Economic Research.

in the Albertine Graben most especially in the Western Uganda was announced by the Government of the republic of Uganda in 2006.[9]

Interestingly, by end of financial year 2014/2015, Uganda had already announced the existence of twenty-one (21) oil and gas field discoveries with an estimated volume of about 6.5 billion barrels of oil which can be equated to 1.4 billion barrels of recoverable oil and gas.[10] But overall, Uganda's gas reserves have been projected to be 672 billion Cubic feet of gas with 499 billion barrels of non-associated gas and 173 associated gas.[11]Despite of the discoveries, oil and gas explorers suggest that there is still a considerable potential of discovering more petroleum given that less than 40 per cent of the total area in Albertine Graben with the potential for petroleum production has been explored.[12]As a valuable natural resource, the government became expectant that oil production shall increase in government revenue and general promotion of sustainable development in Uganda.[13] This expectation of national benefits by the citizens from oil production sparked reactions in governance of oil wealth to avoid the experiences of other countries where discovery and exploitation of oil has attracted woes rather than wealth.[14]

In connection to oil and gas tax policy which is the second variable of study, literature review suggest that the history of oil and gas taxation is quiet not very clear, but the traceable pieces of information designates that oil taxation dates way back to the periods of 1916 in the UnitedStates of America (USA). In the early days of oil and gas taxes in the USA, the taxation policy was based on the Federal energy tax policy.[15]Ultimately, the whole notion of tax policy in the oil and gas industry of the USA transformed during the 1970's largely due to the desire to widen revenue base for the nation. Evidence through the literatures suggest that the desire to implementthe new energy tax policy during the period of the 1970's encompassed the introduction of

[9] Veit, P., Excell C. & Zomer, A (2011): Avoiding the Resource Curse: Spotlight on Oil in Uganda. WRI Working Paper. World Resources Institute, Washington DC. Available online at http://www.wri.org/project/equity-poverty-environment; International Alert (May 2011): Oil and Gas laws in Uganda: A Legislator's Guide. Oil Discussion Paper No.1.
[10]Council, a. (2017). Downstream oil theft.
[11] International Alert (May 2011): Oil and Gas laws in Uganda: A Legislator's Guide. Oil Discussion Paper No.1.
[12] Ministry of Energy & Mineral Development (MEMD) (2017): Ministerial Policy Statements, Government of Uganda, Kampala www.energyandminerals.go.ug;
[13] Veit, P., et al (2011): Avoiding the Resource Curse: Spotlight on Oil in Uganda. WRI Working Paper. World Resources Institute, Washington DC. Available online at http://www.wri.org/project/equity-poverty-environment.
[14] Kizza J, Bategeka L, & Ssewanyana S (2011); Righting Resource- Curse Wrongs in Uganda: The Case of Oil Discovery and the Management of Popular Expectations, Economic Policy Research Centre, Kampala.
[15] Salvatore Lazzari (2008): _Energy Tax Policy: History and Current issues' (2008) CRS report for Congress.

numerous tax subsidies which included; special tax credits, tax deductions, tax exclusions which subsequently informed most of the contemporary oil and gas tax policies for different liquid fuels.[16]

In regards to the historical perspective above, this study will seek to analyze how the current Ugandan tax incentives is likely to encourage the investments of capitals form foreign multinational companies in to the oil and gas industry of Uganda.

1.2.2 Contextual Background

This study will be confined within the context of legislative tax policy but with a key focus of how the tax regime can be used to attract foreign direct investments in the oil and gas industry of Uganda. The petroleum authority of Uganda declared the country as a petroleum province with an estimated in-place volume of petroleum resources of 6 billion barrels of oil equivalent with 1.4 billion barrels recoverable and over 500 billion cubic feet of gas.[17]To this effect, Uganda has promulgate various legislations in regards to the management of oil and gas; the national oil and gas policy approved in 2008 with an overall objective to provide regulation for the Country‘s emerging oil and gas sector. Several other sets of legislative regulations on health, safety and environment have been formulated; for instance, the national content policy, local content policy, the public finance Act 2015, which carters for among other things the management of revenues ensuing from petroleum activities.[18]

In the oil and gas industry, taxation is one of the vital elements that strongly relate with the possibilities of interesting or discouraging investors, as such the concept of tax cuts and incentives have been widely debated in the oil and gas sector. This probably explains why Uganda‘s tax regime has been carefully designed to offer a series of tax incentives to investors inthe oil sector of the economy.   Tax incentives that are offered to investors in legislation of oil and gas sector of Uganda include among others: tax deductions, tax holidays, tax credits, state participation, tax waivers and many others. This study shall focus on one of the tax incentives under the Ugandan laws mainly on the use of tax holidays to attract foreign investments.

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[16]Aquila, G., et al (2017). An overview of incentive policies for the expansion of renewable energy generation in electricity power systems and the Brazilian experience. *Renewable and Sustainable Energy Reviews*, *70*, 1090-1098.
[17]Petroleum Authority of Uganda (August 2018): Current Status of the Oil and Gas Sector in Uganda.
[18]The Petroleum (Exploration, Development and Production) Act 2013, and Transmission and Midstream Storage) Act 2013.

In Uganda just like other economies the overall objectives its fiscal regime is to permit the government to maximize its revenue and at the same time cater for the interests of the investors by offering investors various forms of incentives as a way of encouraging them to invest in the oil and gas sector and other sectors of the economy. In regards to the contextual setting of this research, the foundational basis upon which this study is built is the fact that despite the immense effort by the Uganda government to encourage foreign company investments (FCIs) through offering tax incentives in the oil and gas sector, the sector remains less developed, the study therefore seeks to explore why the use of incentives in the oil and sector has hardly had an impact in encouraging more investments in Uganda‘s oil and gas sector.

1.2.3 Theoretical Background

There are several theories that have been propounded with a view to explain the relationship between tax policies and foreign direct investments. However, most of the theories are economically oriented, for instance the capital arbitrage theory of international capital movement and the theory of international capital markets.[19]The researcher has found it very challenging to identify a single theory whose content can fit in the different types of foreign direct investment or the investment made by a particular multinational corporation or country in any region.[20]In regards to the drive towards privatization and globalization, a lot of reliance has been placed in foreign direct investors (FDI) as a source of capital especially concerning huge projects like in the oil and gas industry as a stimulant for economic growth in developing countries.[21]

The relationship between legal systems and FDI is an historical one that traces its roots during the 1990‘s, whereby foreign investors were largely enticed by the existence of enabling legal systems whose tax policies are predictable and efficient. This is what created the **‘***ideal paradigm*
_theory whose construction targeted the attraction of FDIs through the existence of a functioning

[19] Yelpaala, K. (1985): In search of effective policies for foreign direct investment: Alternatives to tax incentive policies. Northwestern Journal of International Law & Business, 7(2), 208-266; Jorgenson, D. (1963). Capital theory and investment behavior. American Economic Review, 53, 247-259; Ranis, G., & Fei, J.C.H. (1961) A theory of economic development. American Economic Review, 51, 533-565.
[20] Nayak, Dinkar and Rahul N. Choudhury (2014): A selective review of foreign direct investment theories. Asia-Pacific Research and Training Network on Trade (ART Net), Bangkok Working Paper Series No. 143, March 2014, Bangkok, United nations Economic and Social Commission for Asia and the Pacific (ESCAP).
[21] Perry, Amanda (2000): An Ideal Legal System for Attracting Foreign Direct Investment? Some Theory and Reality. American University International Law Review 15, No. 6 (2000): 1627-1657.

legal system. The theory propounds that the stability of a legal system can easily be predicted when the laws are stable, accessible, and clear.[22]

The proponents of the *ideal paradigm* theory expounded that an inefficient legal system generally increases transaction costs by failing to provide cheap mechanisms for enforcing legal rights and obligations.[23]Low transaction costs are ensured where the host country‘s laws are of good quality and its courts and bureaucracies are provided with adequate infrastructure with skillful and properly enumerated staffs.[24]It must be borne in mind that having a legal system that fails to provide credible information regarding the status of legal rights and obligations ofinvestors must be reformed in order to create greater certainty for foreign investors, otherwise the FDI wouldn‘t consider investing their huge capitals in such unfair environment.

The role of efficient legal system in promoting the influx of FDI was further reiterated by the United Nations Conference on Trade and Development (UNCTAD),[25]that the role of tax incentives in promoting the interests of FDI has been studied by scholars for years with no clear conclusions as to its advantages and disadvantages established. However, it was submitted that tax incentives are usually preferred and introduced by many developing countries with the aim of achieving international competitiveness to attract FDI.[26]But generally low corporate taxes increase FDI flows by attracting new investors, retaining existing investors and encouraging reinvestments of returns accrued by existing enterprises.[27]

In conclusion, the adoption and application of the *ideal paradigm* theory as a tool for attracting FDI is plausible, however its application possess some practical challenges as its proponents assumes a literally perfect operating legal systems were the law making process is democratic and all other implementation stages are perfect which is a very impossible thing in most developing countries with Uganda inclusive.

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[22] David Flint et al., (1996): Constitutional and Legislative Safeguards forFDI:*A Comparative Review Utilizing Australia and China, in* Economic Development,Foreign Investment and the Law 104 (Robert Pritchard, ed. 1996).
[23] R.H. Coase (1988): The Firm, the Market and the Law 114-19 (1988).
[24] World Bank Report (1997): The Role of the State in a Changing World 7- 8, 99-100.
[25] UNCTAD. (2000). Tax incentives and foreign direct investment: A global survey. ASIT Advisory Studies No. 16
[26] OECD. (2001): *Corporate tax incentives for foreign direct investment*. Paris, France: OECD publications service.
[27]Onyeiwu, S., & Shrestha, H. (2005): T*ax incentives and foreign direct investment in the MENA region*. Cairo, Egypt: 12th Annual conference of the Economic Research Forum.

1.2.4 Conceptual Background

This study investigates tax incentives, specifically tax holidays as a tool for attracting FDI in the oil and gas industry of Uganda. Tax incentives are measures that provide a favorable taxtreatment to companies involved in huge capital investment ventures like the oil and gas industry. Tax holidays are policies in which huge capital investors are exempted from meeting a classified type of taxes for a given period of time, contingent upon criteria such as being aforeign investor investing in certain industries and activities that are considered particularly important for economic growth. Apart from tax holidays, other tax incentives include tax stability agreements, accelerated depreciation, tax credits, investment allowance and loss relief.

Tax holidays can be defined as a reduction of a given amount and type of tax for a period of time, and most developing countries offer incentives in the form of a tax holiday to companies to attract direct foreign investment.[28]Reports suggest that45% of developing countries imposes tax holiday at the rate of 85% to promote investments or are directed toward incentive instruments such as corporate tax deduction.[29]In theory, there is no doubt that tax incentive policies can theoretically lead to a significant positive growth and development only if they are actually working as conceptualized and intended with further positive impact in attracting investment by lowering cost of capital. Conversely, tax holidays pose large risks of skewed incentives, harmful abuses as well as risks to public finances if not ideologically implemented.

Be that as discussed above, this study shall consider examining the concept of tax incentives in the form of tax holidays which is highly conceptualized as an essential for attracting FDIs. Further, the researcher will attempt to answer the key research questions including: how have taxholidays encouraged foreign direct investments in the oil and gas sector in Uganda and what are the shortcomings of offering tax holidays as an incentive in the oil and gas sector in Uganda?

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[28]Lim, D. (1983). Fiscal incentives and direct foreign investment in less developed countries. *The Journal of Development Studies*, *19*(2), 207-212.
[29]Tax Guide (2018). *Worldwide Corporate Tax Guide*. EY's Tax Services; World Development Report. (2004). *A Better Investment Climate for Everyone*. The World Bank and Oxford University Press.

1.3 Problem Statement

In 2008 Uganda was rated as one of the lowest in hierarchy among the countries that encourage foreign direct investments (FDIs) especially in the oil and gas sector.[30]In regards to aforementioned, Uganda's foreign direct investment (FDI) inflows registered in 2014 was noted as only US$ 1,059 million trailing behind Tanzania with US$ 2,142 million in the EAC Region.[31]The above suggests that Uganda lagged behind in attracting FDI among the founding members of the East African Community and only contributed 25% of FDI inflows in the EAC. Ordinarily, the use of tax incentives is often one of the key attributes used to attract FDI in most developing countries to boost their industries like the oil and gas industry. .

The idea of tax incentives is to attract FDIs, to this Slusarczyk[32]stated that the ability of an economy to attract FDI is an important measure of the country's investment which in other words demonstrates her internationalization. The ability to attract FDI is an important determinant of economic growth, according to Uganda's oil revenue management policy, the working fiscal regime for the petroleum sector is based on a production sharing agreement (PSA).[33] Under which oil companies are contracted by government and are rewarded an agreed share in the production.

Despite of the comprehensive various tax incentives provided under the laws of Uganda, it remains very unclear how the adoption and practice of tax holiday will play any significant role in attracting foreign direct investors in the oil and gas industry of Uganda. As such this study shall explore how best Uganda can use tax incentives to encourage FDI in the oil and gas industry.

1.4 Purpose of the Study

The purpose of this study is to investigate and produce empirical knowledge on the relationship between how tax incentives can attract FDI in the oil and gas industry in Uganda.

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[30]World Investment Organization and the World Bank (2008) report.
[31] Uganda Investment Authority (2014): Annual Investment Abstract- Financial Year 2014/2015, East African Community (EAC) FDI Inflow Trends p. 19.
[32]Slusarczyk, B. (2019): _Tax incentives as a main factor to attract foreign direct investments in Poland' https://www.researchgate.net/publication/325362243> accessed 27September 29, 2019.
[33] See Production Sharing Agreement (PSA) for Petroleum Exploration Development and Production in the Republic of Uganda by and between the Government of the Republic of Uganda and Tullow Uganda Limited: In respect of the Kanywataba Prospect Area February, 2012.

1.5 Objectives of the Study

1.5.1 General Objective

The study seeks to examine the legal and regulatory framework relating to tax holidays as a basis for encouraging foreign company investments in the oil and gas sector in Uganda.

1.5.2 Specific Objectives

1. To analyze the effectiveness of the laws relating to tax holidays in encouraging FDI into the oil and gas sector in Uganda.
2. To explore the corresponding flaws associated to offering tax holidays in the Uganda‘s oil and gas sector.

1.6 Research Questions

1. How have tax holidays encouraged foreign direct investments in the oil and gas sector in Uganda?
2. What are the shortcomings of offering tax holidays as an incentive in the oil and gas sector in Uganda?

1.7 Significance of the Study

To the policy makers, the study findings will be shared with other institutions especially those that are involved in encouraging more investments in the oil and gas sector, for example Uganda Investment Authority (UIA).

To the Researchers, this study should help the researchers to be able to articulate pertinent problems that are hindering the foreign company investments despite the availability of tax incentives to the investors in Uganda‘s oil and gas industry.

To the students, this study is of significance in that it can be used by students who would want to learn more about the issue of promoting sustainable financing in Uganda‘s petroleum industry through fiscal tax policies that attract long-term investment in the oil and gas industry.

Finally, the study is also significant to the researcher for the award of the Master of Laws (LL. M) (Oil and Gas) of Uganda Christian University.

1.8 Justification of the Study

A general reading of Article 244[34] is to the effect that Parliament shall make laws for among other things, for regulating the exploitation of minerals and sharing of royalties arising from mineral exploitation. In relation to the above, the Constitutional objective XI notes that the roleof the State shall give the highest priority to the enactment of legislation establishing measures that protect and enhance the right of the people to equal opportunities in development. In regards to the above, the parliament of the republic of Uganda has passed various enabling laws for regulating the business of oil and gas activities in Uganda.

In essence, the formulation of those laws took into account the possibilities of enticing FDIs through offering favorable tax incentives for investors into capital projects like in the oil and gas industry. Sources acknowledges that Uganda has endeavoured to put up better fiscal petroleum regimes[35] as a way of encouraging FDIs through up scaling investments incentives in thecountry. The adoption of such policy directives is to the effect that capitalizing on FDIs one of the principle objectives of the government of Uganda.[36]

In spite of the encouraging legislative and policy framework for encouraging investors to Uganda, reports suggest that Uganda has remained less attractive to foreign investments despite measures and efforts taken by the government to encourage more foreign investments in the country in the oil and gas sector.[37] The justification of this study is to establish how the tax incentives under the laws can be better utilized to realize there intended objectives of attracting FDI in the oil and gas industry of Uganda.

1.9 Scope of the Study

1.9.1 Content scope

This study shall focus on analyzing the effectiveness of the enabling legislations relating to tax incentives especially tax holidays with the view of boosting foreign direct investments into the oil and gas sector in Uganda. Some of the tax incentives include tax holidays, tax credits, tax

[34]The 1995 Constitution of the Republic of Uganda (as amended)
[35]Rwengabo, S. (2017): *Efficiency, Sustainability, and Exit Strategy in the Oil and Gas Sector: Lessons from Ecuador for Uganda,* ACODE Policy Research Paper Series No. 81, 2017, Kampala: ACODE.
[36]Uganda Investment Authority (UIA) Report of 2018.
[37]Uganda Investment Authority (UIA) Report of 2018.

deductions, tax allowances, exemptions, exclusions among others. However, the researcher will specifically focus on exploring the corresponding flaws associated to offering tax holidays in the Uganda‘s oil and gas sector.

1.9.2 Geographical scope

This study was carried out in Uganda which is located in the East Africa region, it is bordered by Kenya in the East, Tanzania in the south, Democratic Republic of Congo (DRC) in the west, South Sudan in the North and Rwanda in the south western part (See List of Charts). Uganda is endowed with several minerals including the oil and gas fields which are located in western part of Uganda and bordering the DRC. Uganda has a population of about 45 million people according to UBOS report.[38]

1.9.3 Time scope

The study shall cover a time scope stretching to 10 years starting from the time the oil and gastax laws and policies were passed in 2009 up to 2019. The researcher chose this time frame because it is during this period that oil and gas legislative and policy framework intending to attract FDI was formulated.

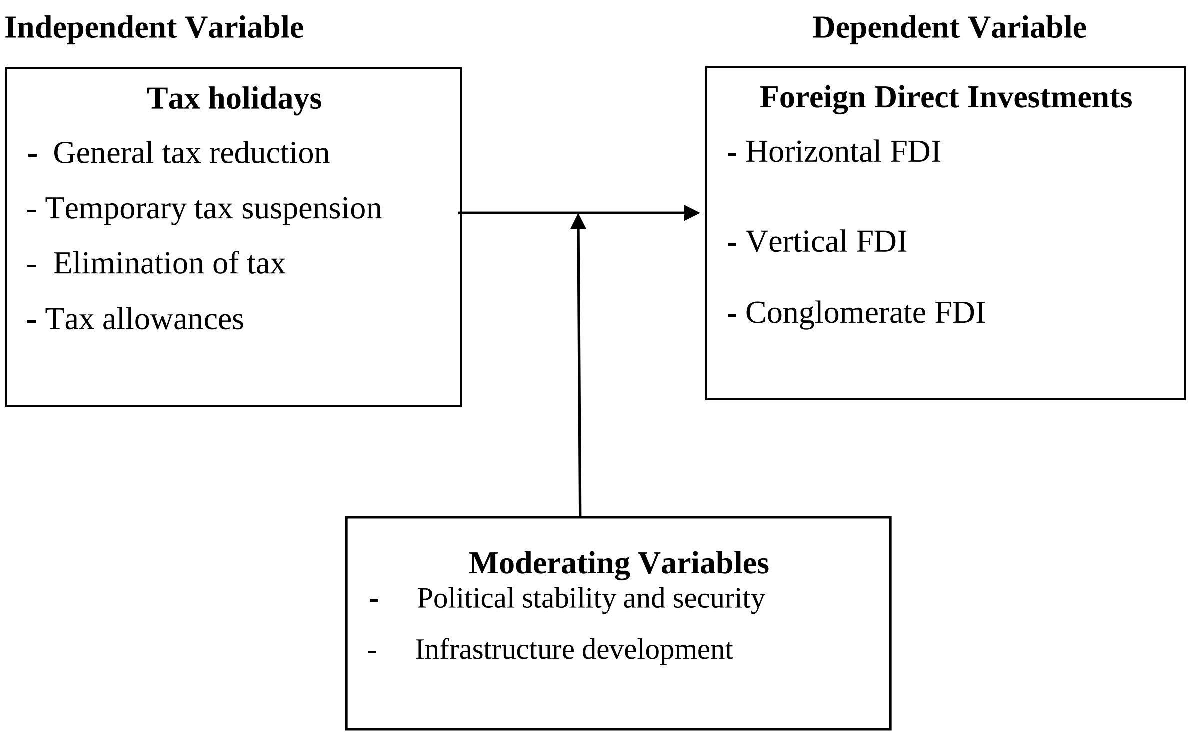
1.10 Conceptual Framework of the Study

In the conceptual framework below, the researcher draws a conceived relationship between the independent variable and the dependent variable. The researcher envisages that the provision of tax holidays in the form of general tax reduction, temporary tax suspension, elimination of tax, tax allowances to entice and attract foreign direct investors to invest their huge capital either using the horizontal, vertical or the conglomerate methods in to the oil and gas industry in Uganda. Other than the afore mentioned independent variable, the researcher predicts that the presence of political stability and existence of well-established infrastructure plays a huge role inattracting FDI in the petroleum industry other than the tax holidays incentives.

The researcher used the conceptual framework because it aims at mapping out the variables of interest with their vital attributes, but also describes the relationships between the two variables (Independent and Dependent variables) in the study.

[38] UBOS (2018): Estimates in its statistics report.

Title: The Conceptual Framework Demonstrating the Relationship between Fiscal Tax Incentives and Foreign Direct Investments in the Oil and Gas Sector of Uganda.



Source: Constructed by the researcher Muhindo K. H: 2021.

1.11 Chaptalization

Chapter one comprises the general introduction to the research.

Chapter two deals with the literature review in line with the objectives.

Chapter three gives the research methodology.

Chapter four presents the legal aspects of the tax holidays in encouraging FDI

Chapter five presents a comparative analysis with the jurisdictions of Kenya

Chapter six presents the summary of research findings, conclusion and recommendations

CHAPTER TWO

LITERATURE REVIEW ON NON-LEGAL ASPECT

2.1 Introduction

In this chapter, the researcher shall focus on scholarly literatures about tax incentives; tax holidays and their relationship with encouraging foreign direct investments. The literature reviewshall be guided by the research objectives in this study, which among other things are associated with the effectiveness of the laws relating to tax holidays in encouraging FDIs and the shortcomings of offering tax holidays as an incentive in the oil and gas sector.

2.2 Legislations directives on tax holidays in encouraging FDIs

Tax holidays are a common form of legislative tax incentives used by developing countries and countries with economies in transition to attract FDI. Under a tax holiday, qualifying firms are exempted from paying corporate income tax for a given specified period of time. It is important to note that in some context the legislative provisions may exempt investment firms from other tax liabilities as well. The philosophy behind tax holidays is that it eliminates tax responsibilities on net revenues from a given investment projects over the holiday period, which some scholars believe encourages foreign direct investment[39]. Once an investment firm is accorded tax holidays, that doesn‘t in totality exempt the firm from meeting other forms of tax responsibility.

In most contemporary economies, it is very common especially for developing countries to offer foreign investors substantial fiscal incentives including tax holidays in order to encourage FDI and eventually stimulate local economic growth[40]. Other than the tax holiday incentives, other fiscal incentives among other things includes other forms of generous tax treatment of new investment disbursements, provision of good roads, worker training, and other public inputs at a considerately below market prices which also plays a role in encouraging FDI.

[39] Chan, K. H., & Lan Mo, P. L. (2000). Tax holidays and tax noncompliance: An empirical study of corporate tax audits in China's developing economy. *The Accounting Review*, *75*(4), 469-484.

[40] United Nations Conference on Trade and Development (UNCTAD). (2000): Tax incentives and foreign direct investment – a global survey. ASIT Advisory Studies No. 16. New York and Geneva: United Nations.

A careful examination of the tax holiday provisions indicates that it is a common phenomenon to find that developing countries grant tax incentives to investments mostly related to exploration and extraction of mineral reserves among others. For instance, in the 1970s and early 1980s, countries like Indonesia offered foreign investors tax holidays that were similar to those granted by many other countries at the time.[41]

As one of the most popular way of hooking foreign investors to invest in capital projects like explorations and extractions of minerals, tax holidays remains one of the traditional and popular form of incentives that was used by 74% of all transition countries and by 87% of the Central and Eastern Europe and the Baltic countries.[42]This is also very consistent with the contemporary global forms and nature of incentives used to incite huge foreign capital investors; these incentives take the form of reduced corporate income tax and tax holidays.[43]In light of the various positive effects of tax holiday as a determinant factor for encouraging FDI, somescholars have reasoned that in one way or the other it increases investment which subsequently led to several other positive externalities like job creation.[44]In agreement to the above, other scholars[45] have stated that investment incentives may provide higher revenues from the possible increase in investment from other countries, and social benefits that include jobs and positive externalities.

Across most African countries engaged in the production of oil and gas businesses have given tax holidays or some sort of incentives to foreign investors who invested in the mineral subsector, preferably in the oil and gas industry. For instance, in Cameroon, an investment allowance equivalent to 50 per cent of the cost of utilities and transportation is granted to an enterprise established in a non-urban area.[46]In Côte d‘Ivoire, the Investment Code provides an 8- year tax holiday when the investment site is located outside the region of the economic capital,

[41]Fahmi, M. R. (2012). Analyzing the relationship between tax holiday and foreign direct investment in Indonesia. *Asia Pacific Studies Ritsumeikanasia Pacific University Japan*.
[42]Fergus Cass (2007): Attracting FDI to transition countries: The use of incentives and promotion agencies. Transnational Corporations, Vol. 16, No. 2 (August 2007)
[43] UNCTAD (2000): *Tax Incentives and Foreign Direct Investment: A Global Survey*, New York and Geneva: United Nations.
[44]Madiès, T. and J. Dethier. (2010): Fiscal competition in developing countries: A survey of the theoretical and empirical literature. Policy Research Working Paper 5311. Washington, D.C.: World Bank.
[45]Sebastian, J. (2009): *Tax and non-tax incentives and investments: Evidence and policy implications.* Washington, D.C.: Foreign Investment Advisory Service (FIAS), the World Bank Group.
[46]Onjala, J. (2016). Chinese Direct Investments in Africa: Motivations and Environmental Implications. *Georgetown Journal of International Affairs*, 91-102.

Abidjan.[47] Tax incentives are granted under the Mining Code and the Petroleum Code for enterprises involved in mining and petroleum activities. In Egypt, a basic five-year tax holiday is awarded for priority sectors in the Old Valley, including oil sector support services.[48] There is a 10-year tax holiday for projects in new industrial zones and projects in the New Valley are entitled to a tax holiday of 20 years, and in Nigeria, accelerated capital allowances are granted onthe basis of the cost of qualified capital expenditure to investors that establish operations in rural areas where facilities such as electricity, tarred roads, telephones and water supply are not available.[49]Furthermore in Nigeria, the legislation provided for a company engaged in marketing and distribution of natural gas for commercial purposes or engaged in laying transmission and distribution pipe lines is granted varying types of incentives including a three-year renewable tax-free period and accelerated capital allowances at 90 per cent rate.[50]

In light of the foregoing, summarily it is noticeable that in one way or the other, African countries have used their legislative avenues to grant foreign huge capital investors tax incentives in order to be able to attract exploitation of their minerals including oil and gas.

2.3 The role of tax holidays in encouraging investors

The philosophy that tax holidays encourage FDI has been adopted and applied by literally every oil and gas producing countries. For instance in the Middle East and North Africa (MENA) countries have heavily used tax various tax deductions models better foreign direct investment performances.[51] All MENA countries direct or otherwise indirectly have offered investment incentives with the view to boost employment, encourage the development of the private sectors and improve their competitive position in today‘s global economy. While most international studies[52] have shown that general economic and framework conditions, rather than incentives,

[47]Møller, V., & Roberts, B. (2017). New beginnings in an ancient region: Well-being in Sub-Saharan Africa. In *The pursuit of human well-being* (pp. 161-215). Springer, Cham.
[48]Mossallam, M. (2021). Egypt‘s foreign direct investment regime: Evolution and limitations. *Routledge Handbook on Contemporary Egypt*, 212-226.
[49]Olaleye, M. O., Riro, G. K., & Memba, F. S. (2016). Effect of reduced company income tax incentives on foreign direct investment in listed Nigerian manufacturing companies.
[50]Donwa, P. A., Mgbame, C. O., & Ekpulu, G. A. (2015). Economic Growth: Oil and Gas Contributions. *Sci-Afric Research Journal of Accounting and Monetary Policy*, *1*(2), 102-108.
[51]Clark, C.; Cebreiro, A. and Böhmer, A. (June, 2007): *Tax Incentives for Investment – A Global Perspective:* experiences in MENA and non-MENA countries. MENA- OECD Investment Programme at www.oecd.org./mena/investment accessed 29th April, 2020.
[52] See for example Dunning (1993), Globerman and Shapiro (1999), and Shapiro and Globerman (2001).

are far more important in determining the size and quality of investment inflows, incentives can compensate for market failures, are seen as easy to implement, and often seen as effective policy tools for achieving economic and social objectives.

Despite the popularity and widespread use of tax holidays incentives in the MENA region, overall there is no tangible evidence produced especially with the aid of a careful systematic reviews of the effectiveness of the various incentives offered by hosting countries. However, thismay be because in most countries there is no dependable data on the actual various investments made whether directly or otherwise to the benefits of the host economy and the cost of the incentives in terms of direct spending or revenue lost.

It is important to point out that every country uses different types of incentives other than tax holidays to influence the decisions of foreign direct investment; some of these incentives include reduced corporate tax rates[53], as well as other incentives like market preferences and monopoly rights. A general reading from a global perspective a reduction in the base rate of corporate income tax and tax holidays is the most widely used form of fiscal incentive. Egypt, Jordan, Lebanon, Morocco and Tunisia use tax deductions and tax holiday with the view to attract FDI.

As opposed to the philosophy of using tax holidays, surprisingly some countries like Bahrain and United Arab Emirates attract FDI to exploit rich natural resources like oil and gas by relying very less on special preferences like tax holidays and special financing regimes, and instead have high corporate income tax rates and withholding taxes earned from oil production and exploitation.[54] In this regard, tax incentives are generally not sufficient as a basis to attract major flows of investment. Mauritius, Costa Rica, Ireland and Malaysia[55] are some of the prime examples of successful countries attracting investment that offer many advantages to investors other than tax breaks; such as stable economic and political conditions, a well-educated labor force, good infrastructure, open trade for exporters, dependable rule of law, and effective investment promotion systems.[56]

[53]Abdioğlu, N., Biniş, M., & Arslan, M. (2016). The effect of corporate tax rate on foreign direct investment: A panel study for OECD countries. *Ege Academic Review*, *16*(4), 599-610.

[54] Bahrain, 46 per cent of net profits on income of oil companies; United Arab Emirates does not have corporate taxes at federal level. At emirate level oil producing companies and branches of foreign banks are required to pay tax rates between 0 and 55 per cent.

[55] SADC Region Technical report 2007.

[56]Bellak, C, M Leibrecht, and J P Damijan (2009): ―Infrastructure Endowment and Corporate Income Taxes as Determinants of Foreign Direct Investment in Central and Eastern European Countries.‖ *The World Economy* 32

In some countries like Indonesia, tax holidays and selected tax incentives programs were terminated in favor of a more attractive general tax regimes, this otherwise reinforced the theory that special tax incentives are also very effective in attracting foreign direct investors to invest in an economy to aid its economic development.[57] Further evidence from Morocco, shows that the macroeconomic evaluation of the efficacy of the overall tax incentives showed a positive effect on private investment for the first year of application of incentives, a positive but decelerated effect during the second year and negative effect after the third year.[58]

In Egypt, a new type of tax was introduced[59] with the main objective of streamlining the old tax system with the view of improving and removing tax obstacles to investors. That new law pulled down the maximum corporate income tax rate from 40 per cent to 20 per cent and abolished the totality of the income tax exemptions.[60]The new law also integrated the corporate tax rates across industries and simplified tax procedures. The visible overall impact of such tax reform and introduction of the tax incentives reportedly improved on FDI performance which suggested that FDI flows almost double in absolute value compared the year before 2005.[61]

In light of the above and in 2002 the Foreign Investment Advisory Service (FIAS) of the World Bank conducted a study on the promotion of private investment in Tunisia. In particular, the study analyzed the role of the fiscal system, including the fiscal and financial incentives, on the private investment trends. It was found out that in the period between 1996 and 2001, private investment in Tunisia on average increased by 10 per cent, which was higher than in other countries in the region, and placed Tunisia at the same level with countries as Ireland. The upward surge was attributed to the county‘s adoption and use of tax incentives.

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(2): 267–90; see: James, S, (2009): ―Tax and Non-Tax Incentives and Investments: Evidence and Policy Implications.‖ *Foreign Investment Advisory Service*, World Bank, Washington, DC.

[57]Zee, H. H., Stotsky, J. G., & Ley, E. (2002). Tax incentives for business investment: a primer for policy makers in developing countries. *World development*, *30*(9), 1497-1516.

[58]Clark, C.; Cebreiro, A. and Böhmer, A. (June, 2007): *Tax Incentives for Investment – A Global Perspective:* experiences in MENA and non-MENA countries. MENA- OECD Investment Programme at www.oecd.org./mena/investment accessed 29th April, 2020.

[59]Income tax law (Law No. 91 of 2005) came into force in Egypt on 10 June 2005

[60]The new law stipulates that companies and firms established under the old Investment Guarantee and Incentives Law but which have not commenced operation or production until the effective date of the new law (10 July 2005), are required to start operation or production within three years from the effective date of the new law.

[61]Clark, C.; Cebreiro, A. and Böhmer, A. (June, 2007): *Tax Incentives for Investment – A Global Perspective:* experiences in MENA and non-MENA countries. MENA- OECD Investment Programme at www.oecd.org./mena/investment accessed 29th April, 2020.

In conclusion, the effectiveness of tax incentives in attracting FDI depends on the tax incentives and public goods provision in the host nation.[62]Typically, FDI location favors nations with the highest public goods provision and lowest tax burden.

2.4 The Shortcomings of offering tax holidays as an incentive in the oil and gas sector

This section focuses on examining some of the negative effects of using tax incentives, specifically tax holidays as a tool for attracting and retaining FDI in an economy desirous of investing in capital projects like in the oil and gas industry. There are several studies that are in agreement with the use of tax incentives as a mean of attracting FDI, for example the impact of tax holiday incentive for investment in Ethiopia was found to be significant, however the study concluded that despite of such tax holiday incentives, it never played a big deal in motivating investors largely due to the fact that the time frame of the tax holiday is too short for investors.[63]

It is important to note that tax holidays place a significant burden on tax administration and on taxpayers in general.

Other studies reveal that fiscal incentives may also have negative impacts. Madiès & Dethier[64] noted that there are several arguments against tax incentives. One is that such regime is costly to administer and could very easily decrease fiscal revenue. Another is that it is prone to corruption and rent-seeking. Such illicit behaviors are particularly observed in developing countries that have strict budgetary constraints. Also, intense competition and bidding war may lead to countries favoring foreign firms over the welfare of local firms. Lastly, tax incentives could create economic distortions as firms try to move as many transactions as possible to the sector with the lowest taxation or build new firms just before existing tax preferences expire.

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[62]Tiebout. (1956): A pure theory of local expenditures. *Journal of Political Economy*, 64, 416-424; and Onyeiwu, S., & Shrestha, H. (2005):and non-MENA countries. MENA- OECD Investment Programme at www.oecd.org./mena/investment accessed 29th April, 2020.

[63]Saporna, D. G. D. G. C. The Impact of Tax Holiday on Investment in Ethiopia: The Case of LTO Branch.

[64]Madiès, T. and J. Dethier (2010): Fiscal competition in developing countries: A survey of the theoretical and empirical literature. Policy Research Working Paper 5311. Washington, D.C.: World Bank.

According to Sebastian,[65] potential costs of investment incentive policies are revenue losses from investments that would have been made even without the incentives, and other indirectcosts such as economic distortions and administrative costs. In developing countries, the effects of fiscal incentives on FDI location vary. Study by de Mooij & Ederveen[66] revealed that a 1 percentage-point increase in a tax measure in a certain location leads to a 3.3% reduction in foreign investment. This finding together with similar others affirms and presupposes that unfavorable tax environment discourages foreign direct investors to invest their huge capitals ina given economy.

The study of Bénassy-Quéré et al,[67] included data on FDI flows from 1984-2000 for 11 OECD countries; the findings revealed that tax differentials play an important role in influencing the understanding and judgment decisions of foreign direct investors. The impact however was concluded not be proportional because low tax rates were found out not to necessarily translate in to higher FDI, while high taxes obviously tended to decrease new FDI inflows.[68] Tax incentives impose significant costs on the countries using them, though these costs are notalways easily visible. In order to appreciate the associated costs of offering general tax incentivesand specifically offering tax holidays to investors, such costs are as classified in four categories below;

Forgone revenues: the losses in tax revenue from tax incentives mainly come from three known sources; firstly, the forgone revenue that otherwise would have been collected from the activities undertaken; secondly, the forgone revenue from projects that would have been undertaken even if the investor did not receive any tax incentives; and thirdly, lost revenue from investors and activities that improperly claim incentives (taxpayers abuse) or shift income from related taxable firms to those firms qualifying for favorable tax treatments (tax planning).

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[65]Sebastian, J. (2009): *Tax and non-tax incentives and investments: Evidence and policy implications.* Washington, D.C.: Foreign Investment Advisory Service (FIAS), The World Bank Group.
[66]De Mooij, R. (2008): Corporate tax elasticities - a reader‘s guide to empirical findings. Oxford University Centre for Business Taxation Working Paper 08/22. Oxford: Oxford University Centre for Business Taxation.
[67]Bénassy-Quéré, A., L. Fontagné, and A. Lahrèche-Révil. (2006): Tax competition and foreign direct investment. CEPII, Working Paper No 2003 – 17. Paris: Centre d'EtudesProspectives et d'Informations Internationales.
[68]Clark, C(June, 2007): *Tax Incentives for Investment – A Global Perspective:* experiences in MENA and non- MENA countries. MENA- OECD Investment Programme at www.oecd.org./mena/investment accessed 29th April, 2020.

Fiscal losses resulting from the non-collection of taxes that would otherwise be due also referred to as tax expenditure. Such expenditure can be very significant, especially in developing countries. The World Bank technical assistance estimated that tax expenditures from incentives to be as high as 5.9 percent in Cambodia, 5.2 percent in Ghana, and 3.9 percent Dominican Republic of their independent various GDP.[69]The report further observed that such expenditure through forgone revenue often does not undergo the same scrutiny and public control as regular government spending, and in many developing countries tax expenditure is not even systematically measured or published.

Enforcement and compliance costs: these costs increase with the complexity of the tax system and the system of fiscal incentives in terms of qualifying and reporting requirements. In addition,there are noticeable problems of perception of lack of fairness when targeted incentives are used,which invariably reduces the commitments to compliance and, therefore, increases enforcement efforts and costs. Administrative costs for both firms and the government due to cumbersome procedures for granting and monitoring incentives. *Retaliation* against new or more generous incentives by competing investment locations.[70]

Lack of transparency: when the rationale for granting tax incentives is based more on discretionary and subjective qualification requirements, instead of automatic and objective requirements, they can originate rent-seeking behavior and facilitate officials‘ abuse on the granting process. In particular, for developing and emerging economies, it is important to move away from discretionary incentives towards greater reliance on *rules-based* means of attracting FDI - national and international rules that maintain or strengthen environmental and laborstandards and create stability, predictability and transparency for policy makers and investors alike. *Rent-seeking* by firms engaging in non-productive behavior to obtain an incentive, or outright corruption where decision makers are bribed to grant incentives.[71] Such costs are often amplified by a lack of transparency in the design and administration of incentives. *Tax planning*

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[69] Ibid

[70]Klemm, A and S Van Parys. (2012): –Empirical Evidence on the Effects of Tax Incentives.‖ *International Tax and Public Finance* 19 (3): 393–423; see OECD (Organization for Economic Co-operation and Development). 1998. –Harmful Tax Competition: An Emerging Global Issue.‖ *OECD*, Paris.

[71]James, S, (2009):―Tax and Non-Tax Incentives and Investments: Evidence and Policy Implications.‖ *Foreign Investment Advisory Service*, World Bank, Washington, DC.

and evasion by the private sector, for example, through shifting of profits from non-exempted to exempted affiliates in the same firm by manipulating internal transfer prices.[72]

Evidence on the benefits of incentives for FDI attraction is not very clear but has attracted mixed up opinions, but for developing for developing countries this is particularly limited. While high corporate tax rates clearly have a negative effect on FDI entry,[73] evidence on the impact of tax incentives is much more mixed. Several studies find them to be of limited effectiveness at the aggregate level.[74] But the research base for a targeted approach to incentives in developing countries remains small as most existing studies focus on OECD countries and often do not allow sector- or investor-type-specific conclusions on the effectiveness of incentives.

2.5 Extraneous factors influencing foreign direct investments

The increasing level of competition for foreign direct investment (FDI) overtime triggered many countries to offer fiscal incentives which include tax holidays, import duty exemptions, investment allowances, and tax reductions and accelerated depreciation among others.[75]All of which were intended to attract investments from FDI, however other than those legislative incentives mentioned above, there are some other extraneous factors that contribute towards influencing the investment decisions of FDI in a given economy and those factors are identified below.

2.5.1 Transparency as a tool for encouraging FDIs

Transparency is one of the major issues that investors treasures when dealing with potential clients from where there anticipate putting in their huge capitals. The higher in risk and uncertainty stem from the presence of bribery and corruption, unstable economic policies, weak and poorly enforced property rights, and inefficient government institutions, all these touches on the key issue of trust from transparency. The issue of transparency in business investment

[72]Heckemeyer, J and M Overesch. (2013): –Multinationals' Profit Response to Tax Differentials: Effect Size and Shifting Channels.‖ *ZEW Discussion Paper 13-045*,.
[73]Bénassy-Quéré, –How Does FDI React to Corporate Taxation?‖ *International Tax and Public Finance* 12 (5): 583
[74]Allen, N et al (2001): –Using Tax Incentives to Compete for Foreign Investment: Are They Worth the Costs?‖ *Foreign Investment Advisory Service Occasional Paper 15*, World Bank, Washington, DC.
[75]Morisset, J. and N. Pirnia. (2000): How tax policy and incentives affect foreign direct investment: A review. Policy Research Working Paper 2509. Washington, D.C.: World Bank.

decisions is one of the novelist issues in economics and finance among businessmen and policy makers.

Transparency consists of making relevant laws and regulations publicly available, notifying concerned parties when laws change and ensuring uniform administration and application.[76] It also involves offering concerned parties the opportunity to comment on new laws and regulations, communicating the policy objectives of proposed changes, allowing time for public review and providing a means to communicate with relevant authorities.

The aspects of non-transparency relate to the level of bureaucratic inefficiency within the government and poor enforcement of the rule of law. These two factors can pose severe barriers to business. If the quality of government service is unpredictable, companies‘ exposure to additional risks is increased.

2.5.2 Investment Climate in encouraging FDIs

In the context of heavy capital project like in the oil and gas, the investment climate plays a vital role in influencing the decision of foreign direct investors, and the investment climate consists of array of issues ranging from political stability, availability of infrastructures and the practice of the rule of law in a given economy.

By all ordinary standards, no investor would dream of pouring in huge capitals in a politically unstable economy. This therefore infers that political instability is a harmful factor that hinders the flow of FDI a country and the growth of an economy as it is based on economic theories and real-life experiences.[77]In fact, political instability has diverse consequences on all economic indicators in terms of growth and development, apparently it is considered by economists as a serious disease harmful to economic performance.[78]

In relation to political stability, prevailing government infrastructures in form of good andefficient roads networks, fair cost electricity, and a well-established institutional modeling for

[76]Bauhr, Monika, and Marcia Grimes. "What is government transparency." *QoG Working Paper Series* 2012, no. 16 (2012): 16.
[77] Abdul Malik Nazeer & Mansur Masih (2017): Impact of political instability on foreign direct investment and Economic Growth: Evidence from Malaysia. INCEIF, Malaysia. MPRA Paper No. 79418.
[78]Carmignani, F. (2003). Political instability, uncertainty, and economics. Journal of Economic Surveys 17(1), 1-54; Lothian J.R.

offering good governance and the rule of law as far as managing investment climate is concerned. In relation to the aforementioned, study findings suggested that exporters fromforeign firms are more constrained in their activity by physical infrastructure hurdles and the lackof skilled workers compared to firms supplying the domestic market.[79]Furthermore, other research found that a high economic risk has a negative and significant effect on FDI flows into Africa generally; the study finding further observed that an increase in the infrastructure of a country has a positive and significant effect on the number and frequencies of FDI inflows.[80]

In developing countries, an essential requirement for attracting FDI and subsequently economic growth and sustainable development is the provision of efficient, reliable and affordable infrastructure services, such as power, transport and telecommunications.[81]The availability of efficient infrastructure services is an important determinant of the pace of market development and output growth, and, in addition, access to affordable infrastructure services for consumption purposes serves to improve household welfare, particularly among the poor. The availability of infrastructure promotes FDI because it reduces operational costs. Recent studies also assert that the availability of public goods plays a crucial role in determining the structure of cost and productivity of firms in the private sector.[82]

The qualities of the physical infrastructure (such as air transport, railway transport, the road network and ease of communication) of the host country have a positive relationship with FDI inflow.[83] Infrastructure improves the business investment environment for FDI by subsidizing the cost associated with total investment by foreign investors and thus raising the rate of return from the investment. Another key factor that encourages FDI to invest in a given economy is the strength and nature of governance in place. To this effect an empirical study findings revealed that of the six components of good governance, political stability and absence of violence,

[79]Kinda, T. (2010). Investment climate and FDI in developing countries: firm-level evidence. *World development*, *38*(4), 498-513.
[80]Kariuki, C. (2015). The determinants of foreign direct investment in the African Union. *Journal of Economics, Business and Management*, *3*(3), 346-351.

[81] Colin Kirkpatrick, David Parker and Yin-Fang Zhang (n.d.): Foreign direct investment in infrastructure in developing countries: does regulation make a difference? And Moran, T. (1999). *Foreign Direct Investment and Development* (Washington, D.C.: Institute for International Economics).
[82] Bénassy-Quéré A. et al (2007). Tax and Public Input Competition, Economic Policy, 22: 385–430.
[83] Manpreet Kaur; Apalak Khatua and Surendra S. Yadav (2016): Infrastructure Development and FDI Inflow to Developing Economies: Evidence from India. Article *in* Thunderbird International Business Review · February 2016

government effectiveness, rule of law, and control of corruption are the key determinants of FDI inflows.[84]

2.6 Conclusion

It must be emphasized that from the discussions through literature reviews above, several nations all over the world offer some sort of tax incentives in one form or the other with the view that the incentives will attract foreign investors to invest in their respective economies. The underlining principle behind tax incentives is that they are given at the expense of foregoing potential tax revenue that an economy would otherwise benefit from. However, it must be emphasized that despite the benefits of tax holidays as an incentive, it generally ranks low among the significant influences that fascinate foreign direct investors as other factors like political and economic stability in the alternative play a vital role in enticing foreign direct investors.

Despite of the fact that tax holidays are the commonest form of tax incentives used by most developing countries to attract FDI, there are a number of shortcomings of offering tax holidays as an incentive in the oil and gas sector that could potentially affect the performance of the economy especially the amount of revenue to be collected.

[84]Mengistu, A. A., & Adhikary, B. K. (2011). Does good governance matter for FDI inflows? Evidence from Asian economies. *Asia Pacific business review, 17*(3), 281-299.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

In any research undertaking, the methodology plays an important role in determining the authenticity of the study findings.[85] As such in this chapter, the researcher presents the research methodology that was used during in carrying out this study. This among other things captured, the research design, data collection methods, ethical issues, method of data analysis among others.

3.2 Research Approach

The study adopted a qualitative doctrinal legal research is a type of research approach in which a systematic review of legal propositions regarding a particular legal phenomenon is critically done to analyses the relationship between rules, and explains areas of difficulty and, predicts future developments.[86]A qualitative doctrinal legal research is considered a suitable research design for this study because this study is based on law and legal propositions like principles of law, theories statutes, cases and rules concerning taxation policy in promoting sustainable financing in the Oil and Gas Sector in Uganda.

3.3 Research Study Design

In this study, the researcher chose a case study design to guide the investigation process of the legal phenomenon under study. A case study is a research approach that is used to generate an in-depth, multi-faceted understanding of a complex issue in its real-life context.[87] It is an established research design that is used extensively in a wide variety of disciplines including law,this is largely due to the fact that enables the legal researcher to take one or a series of legal propositions as a point of focus of the research; thus how tax holidays can reliably attract foreign direct investors in capital project like in the oil and gas industry in Uganda.

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[85]Gawas, V. M. (2017). Doctrinal legal research method a guiding principle in reforming the law and legal system towards the research development.
[86]Budianto, A. (2020). Legal Research Methodology Reposition in Research on Social Science. *International Journal of Criminology and Sociology*, *9*, 1339-1346.
[87]Argyrou, A. (2017). Making the case for case studies in empirical legal research. *Utrecht Law Review*, *13*(3), 95-113.

3.4 Research Data Collection Method

The researcher adopted a systematic literature review method as the methodology for collecting data. A systematic literature review focuses on identifying, selecting and disapprovingly evaluating existing published research materials in order to answer a well formulated question.[88] In this study, both legal and non-legal literatures were used to ensure that the study finding is comprehensively informed. This method of data collection was adopted because of the qualitative legal nature of the study that presupposes evaluation of existing legal documents including but not limited to the laws, policies, and theories.

3.5 Sources of data

In this study, the researcher used various source of data ranging from legal instruments, to policy documents and journal articles published in reputable journals as described below.

3.5.1 Primary

In legal research, primary legal sources comprise of the tangible laws in that are in the form of the Constitutions, decided court cases, Acts of parliament or statutes, and administrative rulesand regulations.[89] In this study while discussing the legal aspects, the researcher used mostly the laws of Uganda and other related countries.

3.5.2 Secondary

For the purposes of ensuring a comprehensive study finding, the research also used a lot of secondary sources of materials to inform the study on tax holidays and incitement of FDI in the oil and gas industry of Uganda. In essence, the secondary sources encamp assess the materials that discusses, elucidates, assesses, and critique the law.[90]Apparently, they discuss the law, but rather are not the law in themselves. Some of the secondary source materials include; law journals, law dictionaries, encyclopedias, and treatises among others are a great place to start your legal research

[88]Snyder, H. (2019). Literature review as a research methodology: An overview and guidelines. *Journal of business research*, *104*, 333-339.
[89]Gawas, V. M. (2017). Doctrinal legal research method a guiding principle in reforming the law and legal system towards the research development.
[90]Budianto, A. (2020). Legal Research Methodology Reposition in Research on Social Science. *International Journal of Criminology and Sociology, 9*, 1339-1346.

3.6 Data analysis method

In the context of formal research undertaking, data analysis is well-defined to mean the processes through which carefully collected data is cleaned and transformed in such a way that only suitable information is processed to make meaning by answering the research questions. For the purpose of accuracy, the researcher adopted a thematic analysis technique to analyze the collected data. Thematic analysis is a qualitative data analysis method that involves reading through a data set for instance, transcripts from in depth interviews and thereafter identifying patterns in meaning across the data.[91] The above technique was very instrumental in identifying common themes in the data collected through systematic literature reviews especially data that are relevant to answer the research questions.

3.7 Ethical considerations

One of the fundamental elements that affirms or discredits research study findings is how the ethical perspectives were utilized.[92] By and large, ethics plays a key role in confirming the authenticity of study findings, for the above mentioned importance of ethics in research, the researcher undertook to follow all the ethical principles are applicable to the study including working with the appointed university supervisor, completing proposal and having it signed by the supervisor, working comments from the proposal defense, and importantly all works used in the study were properly acknowledged and cited.

3.8 Challenges faced

The pursuit of this study did not go without challenges, others were personal but affected the completion of the study on time but others are very integral to the quest of the study. First of all, it has not been easy accessing scholarly information especially from reputable journals as some articles asked for some money to be paid, however, the guidance of the supervisor was very instrumental in helping me out of this predicament, as I was in some context advised to use information appearing only from the abstracts.

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[91]Riger, S. T. E. P. H. A. N. I. E., & Sigurvinsdottir, R. A. N. N. V. E. I. G. (2016). Thematic analysis. *Handbook of methodological approaches to community-based research: Qualitative, quantitative, and mixed methods*, 33-41.
[92]McKenna, L., & Gray, R. (2018). The importance of ethics in research publications. *Collegian*, *25*(2), 147-148.

It wasn‘t an easy thing to appreciate the research methodology entirely, like research design, study approach and performing data analysis using established and tested methods like the thematic analysis model, however I had to read more with genuine support of the supervisor, I managed to succeed in producing this dissertation report.

3.9 Implementation strategy

The research output shall be first disseminated during thesis defense forum, thereafter the researcher hopes to share the study findings inform of legal opinion and writing a policy brief to the relevant authorities especial the concerned line ministries, the researcher hopes to write a complete journal manuscript for journal publication, and finally a copy of the thesis will be shared with the University for Library Usage.

CHAPTER FOUR

LEGAL ASPECTS OF TAX HOLIDAYS AND FOREIGN DIRECT INVESTMENT IN THE OIL AND GAS SECTOR OF UGANDA

4.1 Introduction

In all national jurisdictions were natural minerals resource is exploited, the exercise of tax systems is tripartite in nature, this involve the establishment of tax policy, tax laws and tax administration unit and this is the very tax system that Uganda has adopted. This chapter of the research focused entirely on identifying and analyzing the legal framework of tax incentives, especially tax holidays that are awarded to capital investors in the oil and gas industry and establish the role of the tax holidays in enhancing sustainable financing in Uganda‘s oil and gas sector.

4.2 Legal Framework

In Uganda, the legal regime on tax holidays in the oil and gas sector has its roots traceable right from the Constitution,[93] under the Article 244 of the constitution, it is stated that all minerals and petroleum in, on or under, any land or waters in Uganda are vested in the government on the behalf of the people of Uganda. This explains why in managing Uganda‘s petroleum resources, there are several vital legally binding instruments which include; the national oil and gas policy 2008, the petroleum (exploration, Development and production) Act 2013, the petroleum (Refining, Conversion, Transmission and midstream storage) Act 2013, oil and gas revenue management policy of 2012, the Income Tax (Amendment) Act, 2019 among others.

The 1995 Constitution of the Republic of Uganda (As amended)

It is of utmost importance to note that the Constitution is the ground norm of Uganda, thus forms the basis upon which all other laws stems including tax holidays legal and policy provisions. Article 152, (1) of the Constitution observes that‗. . . *no tax shall be imposed except under the authority of an Act of Parliament'*. In other words, this Article empowers the Parliament as the only institution to make such laws on all matters concerning tax and taxation policy in Uganda.

[93]the 1995 Constitution of the Republic of Uganda (as amended)

In the same vein, Article 244 of the Constitution provides for the ownership and control of minerals and petroleum in Uganda as a country by vesting that responsibility in the hands of the government of the Republic of Uganda. The Article in part thus state;

> *Parliament shall make laws for regulating the exploitation of minerals, sharing of royalties arising from mineral exploitation, conditions for payment of indemnities arisingout of exploitation of minerals and the conditions regarding the restoration of derelict lands.*
>
> *Clause (2) of the same Article acknowledges that minerals and mineral ores shall be exploited taking into account the interests of the individual land owners, local governments and the central Government.*

Although the Constitution doesn‘t directly provide for tax incentive as a means for enticing foreign direct investors, it vividly gives powers to the parliament to make such laws that are subject to regulating the exploration and exploitation of minerals and petroleum, the management of accruing revenues, payment of indemnities, and the conditions for the restorationof derelict lands.

Income Tax Act[94]

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. Section 4 of the Act imposes income tax, under subsections (3) which states that:

> *Where a taxpayer is allowed more than one tax credit for a year of income, the credits shall be applied in the following order— (a) the foreign tax credit allowed under section 81; then (b) the tax credit allowed under section 128; then (c) the tax credit allowed under section 111(8).*[95]

A general reading of the identified provision of this Act, presupposes that it has some serious negative consequences as far as inciting the inflow of FDI into huge capital investments is concerned. This adverse consequence was ably observed in the case of *Kinyara Sugar Works ltd*

[94] Income Tax Act 1997 (Cap 340) as amended
[95] Income Tax Act 1997 (Cap 340): Section 4, Sub-sections (1) - (3).

vs. Commissioner General, URA. Kinyara Sugar Works Ltd[96] is a limited liability Company incorporated in Uganda and filed this suit against the Commissioner General, Uganda Revenue Authority for a declaration that it is entitled to tax exemption incentives under section 21 (z) of the Income Tax Act as amended by the Income Tax (Amendment) (No. 2) Act 19 of 2008 for income derived by it from its new plant and machinery procured to enhance its sugar cane processing capacity from 2200 tons of cane sugar per day to 3500 tons of cane sugar perday.[97] This type of tax policy and administration scares aware potential investors in the oil and gas industry of Uganda.

Value Added Tax Act [98]1996 (Cap 349) (as amended July 2005)

Another law promulgated by the parliament of Uganda on taxation is the Value Added Tax Act 1996 (VAT) which was introduced in Uganda 1996 and amended in July 2005 but is still applicable today as a valid legal instrument in Uganda. Important to emphasize is the fact thatthe VAT replaced the sales tax and Commercial Transaction Levy (CTL). In specific context, section 5 of the VAT Act 1996 provides for persons liable to pay tax as, thus

> *(a) In the case of a taxable supply, it is to be paid for by the taxable person making the supply; and (b) in the case of an import of goods, it is to be paid for by the importer; and (c) in case of an import of services, is to be paid by the recipient of the imported services.*[99]

In regards to the legislative provision above, the obvious implication is that a foreign investor has to shoulder the heavy and various tax burdens under such legal provision. This obviously doesn‘t encourage serious investors from investing their capitals be it financial or in services.

Excise Management Act 1970 (Cap 335) as amended in 2003

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[96] Kinyara Sugar Ltd v Commissioner General Uganda Revenue Authority (HCCS 73 of 2011) [2012] UGCommC 114

[97]Kinyara Sugar Ltd vs. Commissioner General Uganda Revenue Authority (H.C.C.S NO 73 OF 2011) [2012] UGCOMMC 114 (31 August 2012). See also AAR Health Services (U) Limited vs. Uganda Revenue Authority (CIVIL SUIT No. 270 OF 2011) [2016] UGCOMMC 201 (27 October 2016).

[98] Value Added Tax Act 1996 (Cap 349)

[99] Ibid,Person Liable to pay tax, Section 5.

The main objective of this Act of parliament, the exercise management Act (1970) is to provide oversight regulatory roles of the excise duties. For the avoidance of doubt, the excise duties are levied on various goods inclusive of fuel among other items, regardless whether they are reproduced in or imported into Uganda. Section 39 of the Excise Management Act 1970 specifies that:

> *Subject to the provisions of the excise laws, duty shall be paid by a licensee on excisable goods manufactured by him at the rates and in the circumstances specified in the appropriate partner State legislation* [100]

A general reading of the provision insinuate that the investors must pay more tax on goods produced or imported on top of other taxes already levied on the same goods and services. In the long run, this negatively affects the supply chain of petroleum products in the country and subsequently the inflow of FDI to invest in the oil and gas industry of Uganda.

Local Government Act (Cap 243)[101]

The local government Act is one of the legislation that provides of tax regime that in one way or the other influences the decision of investors who intends to invest in the local area were the mineral is located. Section 80 of the Act allows local government to levy, charge and collect fees and taxes, including among other things, Local Service Tax (LST), land-based charges like premium, building plan approval fees, land fees, Ground rent; Business licenses, user charges and permits; royalties from electricity generation, mineral mining and exploration and protected areas. It is important to emphasize that these fees and dues and taxes can‘t be avoided by investors especially were they are physically engaged in establishing working plants. As such in totality, these levies and charges influence investment decisions into the country and consequently the inflow of FDI in the country.

In addition, Section 77 (1) empowers LGs to formulate, approve and execute their budgets and plans and to collect revenue and spend it.[102] The investors will invest in a locality under the

[100] Excise Management Act 1970 Cap 335 as amended 2003: Section 39.
[101]The Local Government Act 1997 Cap 243 (as amended)
[102]Republic of Uganda. (1997). The Local Governments Act (CAP 243), as amended.

management of the local governments and these budgets and plans become influential in investment decisions.

Mining Act 2003 (Cap 148)

This is one of the laws whose provisions related to tax directly applies to minerals in which category the oil and gas applies. It is an Act that replaced the Mining Act, Cap. 148, with a new legislation on mining and mineral development which conforms, and otherwise gives effect, to the relevant provisions of the Constitution; to vest the ownership and control of all minerals in Uganda in the Government; to provide for the acquisition of mineral rights; and to provide for other related matters. Section 98[103]on royalties:

> *. . . all minerals obtained or mined in the course of prospecting, exploration, mining or mineral beneficiation operations shall be subject to the payment of royalties on the gross value of the minerals based on the prevailing market price of the minerals at such rates as shall be prescribed. (2) Royalty shall be shared by the Government, Local Governments and owners or lawful occupiers of land subject to mineral rights in the manner specified in the Second Schedule to this Act.*

In summary, the provision of this Act determines the mode and nature of distribution of royalties derived from extraction and production of minerals in this case oil and gas. But what theprovision means is that any investor, who comes across such heavy tax burden, may be subsequently influenced to look somewhere else to invest their capitals since it‘s obvious that thereturn on investment will be ridiculed.

Investment Code Act [104]

This is an Act that replaced the Investment Code Act 1991, with an overriding objective to make it conform to the Constitution and provide for the registration of investors and investment licenses. In summary, the Act establishes a code to make provision in the law relating to local and foreign investments in Uganda by providing for more favorable conditions for investment, toestablish the Uganda Investment Authority and to provide for other related matters. Section 12 gives the Qualification for incentives as:

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[103] The Mining Act, 2003 Chapter 148, laws of Uganda

[104]Investment Code Act 2019 Cap 92 (as amended 29th March 2019)

An investor who, in addition to the qualifications for incentives set out in any other law, meets the following qualifications for incentives and commences operations after the commencement of this Act, qualifies for incentives.

Under the above legal provision, some of the condition set forth includes among other things meeting the minimum investment capital for the investment, exports a minimum of eightypercent of the goods produced, provides for substitution of thirty percent of the value of importedproducts, seventy percent of the raw materials used are sourced locally, and directly employs a minimum of sixty percent of citizens, and introduces advanced.

Generally noticing, the requirement of labeled under the law above appears to be immense on the side of the investors though they serve meaningful purpose to the host country and its local populations. This means that investors will have to make the hard decisions whether to invest in such an environment or to bypass it.

4.3 Institutional Framework

Under this section, the researcher will focus on identifying and examining the institutional framework responsible for the implementation of investment incentives in the capacity of tax holidays whose purpose is intended to attract FDI in Uganda‘s oil and gas industry.

The Uganda Revenue Authority (URA)

The Uganda Revenue Authority is a corporate government legal entity established by the Act of parliament.[105] In essence the URA is the central body for the assessment and collection of specified revenue, administration and enforcement of laws relating to such revenue in Uganda.

The URA serves as a central body for the assessment and collection of specified tax revenues as it identifies, informs and assesses taxpayers. The URA is headed by a Commissioner General who is appointed by the Minister of Finance, Planning and Economic Development. Although the URA is a quasi-autonomous institution, for budgetary purposes, it is regarded as a department under Ministry of Finance, Planning and Economic Development (MFPED) and is

[105]The Uganda Revenue Authority Chapter 196, laws of Uganda

subject to the same financial rules and disciplines as other departments.[106]Also make a direct role it plays in charging and collecting revenue from the FDIs.

Uganda Investment Authority (UIA)

The Uganda Investment Authority (UIA) is a semi-autonomous investment promotion and facilitation organization in Uganda and is owned by the government of Uganda. The UIA was created by the Ugandan Parliament in 1991 under the Investment Code 1991 (revised in 2019). UIA is a statutory agency mandated to initiate and support measures that enhance investment in Uganda and advise Government on appropriate policies conducive for investment promotion and growth. The mission of the UIA is to promote and facilitate investment projects, and advocate for a competitive business environment.[107]

In Financial Year (FY) 2016/17 Uganda registered a 9.8 percent growth in the amount of licensed investments from US$ 1.522 billion in 2015/16 to US $ 1.67 billion in 2016/17. Thiswas some growth compared to the previous FY, from US $ 1,059 million in 2014/15 to US $ 1,522 million in 2015/16.[108] China contributed the highest amount of FDI licensed investmentsin Uganda that accounted for 31.9 percent of all the FDI licensed investments in 2016/17 and India was in the second position with US $ 162.8 million which accounted for 15.5 percent of all the licensed investments in 2016/17.[109]

Petroleum Authority of Uganda (PAU)

This authority was put in place to regulate the different players in the oil and gas sub-sector. The specific roles of this regulatory body among other things include monitoring and regulating petroleum operations including reserve estimation and measurement of the produced oil and gas, proposing and implementing regulations and monitoring expenditure on licenses among others.

Uganda National Oil Company (UNOC)

In addition to the various policy and regulation framework, the government of Uganda set up an entity to handle its commercial interests in the oil and gas sub sector. For instance, State

[106] SEATINI, TJNA & Oxfam. (2016). Fair Tax Monitor: Uganda.
[107]Profile of Uganda Investment Authority". Comesaria.org. Retrieved 29 May 2019.
[108] Uganda Investment Authority (2017): Annual Investment Abstract, FY 2016/2017.
[109]World Investment Reports for 2015-2017, by UNCTAD.

participation in the licenses and marketing the country‘s share of oil and gas production received in kind. However, the specific roles of UNOC among other things include managing the business aspects of State participation, developing in depth expertise in the oil and gas industry and most importantly optimizing value to its shareholders among others.

Ministry of Finance, Planning and Economic Development (MFPED)

The Ministry of Finance, Planning and Economic Development (MFPED) is responsible for the formulation of policies aimed at generating domestic revenue and promoting capital investments, consumption and savings. However, policy formulation is limited to a few technocrats, to the exclusion of other stakeholders, such as civil society and taxpayers themselves. Broad tax policy objectives are contained in annual budget speeches; which area is fleshed out in legislation.

The Parliament of Uganda

The role of parliament in the oil and gas sector is basically enacting legislations for the management of oil and gas revenues and to monitoring performance in the petroleum sector through policy statements and annual budgets. The Parliament of the Republic of Uganda is mandated by the Constitution of the Republic of Uganda under Article 244 to impose taxes. In addition, is responsible for making laws on capital investments and approving external borrowing. The Parliament works through committees to scrutinize analyze and consult on tax matters.

4.4 Conclusion

It is of paramount importance to reckon on the facts presented above that the tax system in Uganda is comprised of the tax policy and tax legislation. Uganda as a nation has various legal and regulatory legal instruments that govern the formation and implementation of various incentives including tax holidays whose ambition is to attract foreign direct investors. What remains to be established is whether those tax incentives under the law can, and has interested investors into the oil and gas industry of Uganda.

CHAPTER FIVE

A COMPARATIVE LEGAL ANALYSISOF TAX HOLIDAYS WITH KENYA

5.1 Introduction

The purpose of this chapter is to examine the nature of tax holidays for encouraging FDIs and provide a comparative analysis with some selected East African neighboring countries of Kenya and Tanzania. Kenya and Tanzania were chosen from among the many oil and gas producing countries, based on their historically active levels of East African Community and similar stage in oil and gas activity, relative maturity, and accessibility of their governance instruments.

5.2A Comparative Legal Analysis of tax Holidays with Kenya

Sustainable management of the oil and gas sector is one of the greatest yet elusive ideals facing most petroleum rich countries. History of oil and gas producing countries globally suggests that many oil-rich economies have plundered their opportunities and wasted valuable time by spending oil revenues unproductively in what has been named resource curse.[110] By and large, Kenya and Tanzania have been recorded to have made commendable strides since 2007 and 2010 respectively in petroleum-wealth exploitation and management. It is therefore, imperative upon Uganda to learn from such earlier entrants in the sector, thus this comparative analysis section to draw lessons from the East African neighbors of Kenya and Tanzania for Uganda‘s nascent oil and gas sector.

5.2.1 The Legal Regime on Investment and Tax Incentives in Kenya

The major legislation for regulating and promoting FDI in Kenya is the Income Promotion Act

(IPA) 2004.[111]Under the IPA, the Kenyan Investment Authorities (KIA) was established as the lead institution in the promotion and facilitation of investment in Kenya. The KIA is also responsible for advocating for a conducive investment climate, providing accurate information, and offering quality services, such as, obtaining all the necessary licenses for investors, and implementing new investment projects. Furthermore, the KIA plays a vital role in helping in the grant of incentives to investors and advises the government on measures to increase the ease of

[110]Norad (2012): Facing the Resource Curse: Norway‘s Oil for Development Program. Report 6/2012. Norad Evaluation Department.

[111] See *IPA, supra* note 20; *Kenya Vision 2030, supra* note 218.

doing business and attracting FDI.[112]In addition to the above, as the main government body responsible for facilitating investment, the KIA aims is to reduce the bureaucratic delays in the licensing of investors, and in the grant of tax incentives and exemptions from the relevant authorities.[113]In contrast, Uganda has Uganda Investment Authority that performs a much similar roles and duty as that of its Kenyan counterpart.

In regards to the tax incentives that Kenya offers to investors, the country still offers various kinds of tax incentives in many sectors of the economy. The tax system is comprised of countlesssets of legislation that grants tax reductions to investors.[114]The major tax incentive under the various legislations includes tax holidays, ID allowances, customs duty exemptions, and concessionary CIT rates for some sectors. Most of the incentives are contained in the ITA and are of general application across sectors, but the operation of the tax incentives is spontaneous as provided for under the laws of Kenya, except in a few specific cases where administrative intervention is required. Comparatively, Uganda offers tax holidays for capital investors as discussed under the legal aspects of this research, however previous research on this subject matter in Uganda disclosed that tax holidays effectively reduce effective average tax rates (EATR) and favor high-profit short-lived (less than 5 years) investment projects raising doubts about their overall rationale.[115]

The current corporate income tax (CIT) rates for firms located within the export processing zones (EPZ) is at 30 per cent for resident corporations and 37.5 per cent for permanent establishments, reduced CIT rates apply in specific sectors including the capital markets and mineral sectors. Further, all licensed EPZ projects are eligible to the following incentives among other many incentives: firstly, a 10-year corporate income tax holiday and a 25% tax rate for a further 10 years thereafter, in regards to the tax incentives above, a study concluded that increase in corporate income incentive led to an increase in the ROA, number of jobs and length of stay of the EPZ firms in Kenya.[116]Secondly, a 10-year withholding tax holiday on disbursements and other remittances to non-resident parties; a study to that effect concluded that export promotion incentive had the most significant effect on foreign direct investment followed by industrial

[112] See Kenya Investment Authority (KenInvest), ―Who We Are‖ (16 June 2019)
[113] See *Kenya Vision 2030, supra* note 218 at 1.
[114] See *ITA Kenya, supra* note 20; *IPA, supra* note 20; *EPZA, supra* note 20; *SEZA, supra* note 20.
[115]Lakuma, P. C. (2019). Attracting Investments Using Tax Incentives in Uganda: The Effective Tax Rates.
[116]Kuria, J., Omboi, B., & Achoki, G. (2017). Effect of corporate income tax incentive on the performance of EPZ firms in Kenya.

building allowance and investment deduction allowance.[117]Thirdly, a perpetual exemption from VAT and customs import duty on raw materials, machinery, office equipment, certain petroleum fuel, construction resources.

However, to encourage investment in physical capital like industrial buildings, machinery and equipment plants, IDs are allowed under the ITA in many sectors including natural minerals, and the accelerated deductions are allowed for plant, property and equipment in export processing zone (EPZs) and overall mining industry.[118]It has been severally argued that tax incentives play aminor role in making investment decisions as governments uses them as a means to an end.[119]Conversely, following the establishment of EAC in 1999, Kenya, Tanzania and Uganda created a custom union with a common external tariff in 2005 whose aim was to create a larger regional market that will enable firms to set operation in any of the East Africa nations.

In regards to the aforementioned, in unique conditions, the EAC countries made attempts to increase the tax incentives in order to attract FDI with the view that such increment willinvariably escalate jobs and exports. The more prominent incentives offered to the foreign firms operating in Export Processing Zone include; tax holiday where a firm is exempted from the corporate income tax for up to10years, exemption from import duty on machinery, raw materials and input meant for export production.[120]In reference to the above, research study that explored the relationship between the application of tax holiday and capital deductions as a tool for attracting and retaining Foreign Direct Investments in Export Processing Zones (EPZs), subsequently disclosed that the use of tax holiday in one way or the other immensely influences the attraction and retention of Foreign Direct Investments.[121]

There are various tax incentives available in Kenya including initial 10-year tax holiday for companies operating in the Export processing Zone and subsequent reduction of corporate tax rate to 20% for the next ten years, tax loss carry forward for the next four years from the year of

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[117]Mutisya, A. N., Muturi, W., & Kemboi, I. (2019). Effect of tax incentives on foreign direct investment In Kenya. *International Journal of Business Management & Finance*, *3*(2), 51-64.

[118] See Wikipedia, ―Tourism in Kenya‖ (16 June 2019), online: *Wikipedia* <en.wikipedia.org> [perma.cc/wiki/Tourism in_ Kenya].

[119] UNCTAD (2005). *Investment policy review, Kenya*. New York: United Nations

[120]Action aid, (2012): Tax, privatisation and the right to education: Influencing education financing and tax policy to transform children‘s lives.

[121] Thuita G.W. (2017): An Investigation of the Effect of Tax Incentives on the FDIs: A Case of Export processing zones (EPZs) in Athi River Kenya. Journal of Accounting, Finance and Auditing Studies 3/1 (2017) 17-36.

income the tax loss was first incurred, investment deduction of 150% for investment of more than Kshs.200million outside the cities of Mombasa, Kisumu and Nairobi.[122]

In contrast to the above deliberated benefit of tax incentives used as a means of attracting greater levels of Foreign Direct Investment (FDI) into the country. Evidence from some sources points to the fact that such tax incentives are also contributing to very large revenue losses and to some extend are very unnecessary for attracting FDI.[123]Government estimates were that Kenya has lost over KShs 100 billion (US$ 1.1 billion) a year from all tax incentives and exemptions.[124] Of these, trade-related tax incentives were at least KShs 12 billion (US$ 133 million) in 2007/08 andmay have been as high as US$ 566.9 million. Thus, the country is being deprived of badly- needed resources to reduce poverty and improve the general welfare of the population. Kenya‘s provision of tax incentives is part of the tax competition among the members of the East African Community.

Although Kenya was leading as a destination of FDI to the East Africa Community in the 1970 and 1980, the relative level of inflows was 7.5% of GDP in 2003 compared to 25.3% for Africa and 31.5% for developing countries.[125] Despite the numerous tax incentives, the Kenyan EPZs have not achieved much in terms of job creation and inflows whereby in 2010 Kenya was lagging behind with only US$ 133 compared with Tanzania and Uganda which had massive inflows of US$700 and US$848 respectively.[126]Conversely in a comparative context, studies have revealed that tax holidays don‘t necessarily attract FDI as its relationship didn‘t reveal any statistically significant influence on FDI inflow. Be that as it may, the study found that instead investment allowances had a positive statistically significance influence on and FDI inflow in East African Countries.[127]

[122] (Kenya Income Tax ACT, CAP 470 and 517 Laws of Kenya).
[123]Tax competition in East Africa: A race to the bottom? Tax incentives and revenue losses in Kenya. Tax Justice Network-Africa. PO Box 25112, Nairobi 00100, Kenya, May 2012.
[124]Mahoro, J. C. G. (2015). A Comparative Study on Advantages of Tax Incentives and Exemptions Under Rwandan and Kenyan Legal Regimes. *Available at SSRN 3125310*.
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5.3 Conclusion

In relation to the comparative analysis above, it was found out that in the traditional East African countries of Uganda, Kenya and Tanzania; all those members States practiced some sort of incentives provisions in form of tax holidays, tax deductions, tax credits among others. However, the viability of those mechanisms of tax incentives to attract FDI attracted a mix reaction inform of various research studies presented above.

CHAPTER SIX

SUMMARY OF FINDING, RECOMMENDATION AND CONCLUSION

6.1 Introduction

In this last chapter of the study, the researcher presents the summary of crucial study findings; for the purpose of clarity, the results presented are guided by the various research objectives and research questions created and asked in chapter one of this research. In a coherent manner, the summary of findings will be in a logical manner with commensurate recommendations based on the findings, and finally make a general conclusion regarding the purpose of the study.

6.2 Summary of research findings

In the pursuit of this research, there were several findings in relation to the research question that was asked in chapter one, but for the sake of this chapter the researcher will focus on presenting some of the vital and key results. Importantly, the presentation of the summary of findings are guided by the research objectives created in chapter one and will be presented in their logical order as seen below;

6.2.1 Effectiveness of the law on tax holidays in encouraging FDI in oil and gas in Uganda.

In reference to the first objective which was to analyze the effectiveness of the laws relating to tax holidays in encouraging FDI into the oil and gas sector of Uganda, the study findings disclosed that in Uganda there are various provisions of the law relating to tax holidays for capital investments as outlined below;

The Constitution under Article 152(1) observes that no tax shall be imposed except under the authority of an Act of Parliament, and Article 244 of the same Constitution provides for the ownership and control of minerals and petroleum in Uganda as a country by vesting that responsibility in the hands of the government of the republic of Uganda. Although the Constitution doesn‘t directly provide for tax incentive, it gave powers to the parliament to make such laws for regulating the exploration and exploitation of minerals and petroleum, the management of accruing revenues, payment of indemnities among other things.

The study also disclosed that Section 4 of the income tax Act provides for tax credits that are applicable to a tax payer especially in a situation where a tax payer is allowed more than one tax credit in a year. It is well established from the various literatures accessed and presented under chapter two to this study that tax credit as a form of tax holidays plays a big role in enticing FDI

Further, under section 5 of the Value Added Tax Act 1996 (VAT) which imposed tax on all taxable person on all goods and services to be imported to Uganda has a similar spirit of the law with section 39 of the Exercise Management Act (1970) which also imposes duty to be paid by a licensee on excisable goods manufactured by him at the rates and in the circumstances specified in the appropriate partner State legislation. The understanding of such legal provision is that it scares away potential investors as the amount to be paid in tax accumulates in such payments.

In regards to the above, the study revealed under section 80 of the local government Act that the local government has the liberty to levy, charge and collect fees and taxes like premium, land fees, royalties from electricity generation, mineral mining and exploration and protected areas, in connection to the above, section 98 of the Mining Act, Cap. 148, provides that all minerals mined shall be subject to the payment of royalties on the gross value of the minerals and royalty shall be shared by the Government, Local Governments and owners or lawful occupiers of land subject to mineral rights in the manner specified in the Second Schedule to this Act.

In block summary, the legal regime about general legislative tax incentives appears more deterrent to attract FDI especially in the undertaking of capital projects like oil and gas. But also in respect to tax holiday specifically, the overall provision of the law seems to have very little significance as far as attracting FDI into the oil and gas sector of Uganda is concerned. This is largely due to the fact that other forms and types of taxes levied to the investors over shadows the benefits intended under the tax holiday periods.

6.2.2 The corresponding flaws associated to offering tax holidays

In regards to the second research objective which was to explore the corresponding flaws associated to offering tax holidays in the Uganda‘s oil and gas sector, the study findings disclosed a number of significance consequences that arises from offering tax holidays. These negative experiences were empirically draw from experiences of other countries that also offered tax holidays in their oil and gas sector with the view to attract FDI.

In respect to the second objective above the study disclosed that under tax holiday, qualifying firms are exempted from paying corporate income tax for a given specified period of time. For instance, looking at experiences of other countries, in Cameroon, an investment allowanceequivalent to 50 per cent of the cost of utilities and transportation is granted to an investor established in a non-urban area. In Côte d‘Ivoire, the Investment Code provides an 8-year tax holiday when the investment site is located outside the region of the economic capital, Abidjan. In Egypt, a basic five-year tax holiday is awarded for priority sectors in the Old Valley, includingoil sector support services, and in Nigeria, accelerated capital allowances are granted on the basisof the cost of qualified capital expenditure to investors that establish operations in rural areas where facilities such as electricity, tarred roads, telephones and water supply are not available.

In regards to the above, the study further noted that tax holidays generally place a significant burden on tax administration and on taxpayers at large. Findings illustrated that tax holiday regime is in fact very pricy to administer and it effortlessly decrease overall fiscal revenue. The study also observed that tax incentives creates financial falsifications as companies try to move as many transactions as possible to the sector with the lowest taxation, and the potential costs of investment incentive policies are obvious revenue losses from investments that would have been made even without the incentives, and other such related indirect costs such as economicdistortions and administrative costs.

In relation to the above study findings, the researcher concludes that legislating tax holidays as one of the incentives to attract FDI should be carefully levied and administered, and in extreme situations the researcher recommends that tax holidays should be discouraged as a tool for enticing FDI in the oil and gas sector. Instead the researcher agrees with the notion that other fiscal options which the study found were very instrumental in attracting FDI like firstly the enhancement of transparency as a tool for encouraging FDIs which consists of making relevant laws and regulations publicly available, notifying concerned parties when laws change and ensuring uniform administration and application, secondly improving on the overall investment climate like improving and sustaining political stability, ensuring availability of good and functional infrastructures and the practice of the rule of law in a given economy.

6.3 Study recommendations

In light of the research findings presented in a summary form above, therefore, the researcher makes the following recommendations as possible action line for policy makers to deal with issues associated with tax holidays as a ground for attracting FDI into the Ugandan oil and gas industry.

The cabinet and the parliament of Uganda should consider amending the law related to tax holidays in such a way that its provision clarifies and except FDI in the oil and gas industry frompaying other related taxes that otherwise covers up for the lost revenue in tax holiday period

The researcher recommends that the Uganda revenue authority should administer the incentive of tax holidays with due care such that potential investors in the oil and gas industry of Uganda do not suffer the wrath of other hidden tax and costs.

The researcher further recommends that the government continues investing in other sectors that jointly creates an enabling investment climate for FDI. Such investment climates encompass political stability, availability of good and functional infrastructures and the practice of the rule of law in a given economy.

6.4 Area for future research

The researcher recommends that a study must be undertaken in the following areas;

- Perform an empirical study examining the cost of administering tax holidays as a tool for attracting FDI in the oil and gas sector in Uganda
- A study establishing the viability of offering other types of incentives as a substitute for tax incentives on the oil and gas industry in Uganda
- A research in to the practices and experiences of tax incentives administrator in the oil and gas industry in Uganda

- A research into the opinions and attitude of FDI in the oil and gas industry of Uganda about the tax incentives they are offered.

6.5 General conclusion

Overall, the researcher accomplished the study proposed objective of analyzing the law and implication of the flaws related to implementing tax holidays as an incentive intended to attract FDI in Uganda‘s oil and gas industry. The research findings evidently established that the intention of using tax holidays as an incentive for attracting FDI in the oil and gas industry of Uganda is very disastrous, however the researcher recommended an optional measure that can beadopted to entice FDI to invest in the oil and gas industry of Uganda.

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