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Glossary

KPMG KPMG Advisory Limited

EABC East African Business Council

TMEA TradeMark East Africa

EAC East African Community

EAC Partner States Burundi, Democratic Republic of Congo (DRC), Rwanda, Tanzania,

Kenya, Uganda, and South Sudan

PPD Public-Private Sector Dialogue

NTBs Non-Tarif Barries

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Executive Summary

This report summarises the findings of the study commissioned by EABC Secretariat through TMEA Regional PPD Programme, to identify existing discriminative taxes in the EAC Partner States and their impact on intra-EAC trade and investment and to recommend advocacy roadmap for the harmonisation of excise duties in the region. These research findings are intended to develop a policy brief to support EABC to advocate for harmonisation of excise duties and elimination of discriminative taxes on domestic tax regimes in the EAC region.

The research comprises feedback from key stakeholders across the region, such as Revenue Authorities, respective Ministries responsible for tax policy formulation, EAC secretariat for fiscal and monetary policy, the Ministry responsible for EAC integration, and taxpayers from several sectors (including telecommunication sector, drinking water and carbonated drinks manufacturers, beer and spirits manufacturers, cigarette manufacturers, and banking and financial institutions).

In this study, both primary and secondary data were used. Primary data involved the use of questionnaires and secondary data were derived from publications and publicly available records. Interviewing method (face-to-face) was employed as a sequential data collection method to capture additional information that was not covered by the open-ended questions in the questionnaires.

This draft report elaborates diverse views by different stakeholders in relation to the impact of discriminative taxes and harmonisation of excise duties among EAC Partner States. For example, whilst some stakeholders opine that the un-harmonised or varied and discriminatory excise duties levied against the movement of like or similar goods and services across the region is one of the trade barriers that need to be eliminated, others do not believe that excise duty is a barrier to intra-EAC trade and investment. The latter attributes the low volume of intra-EAC trade and investment to other factors such as fiscal policy stability and the political ban on trade or other commercial activities from one member state to the other (among others).

On excise duty, most taxpayers who responded to the questionnaires indicated that the excise duty rates across the region are generally on the high side (which has a ripple effect on the cost of doing business). Without admitting this fact, policy makers and enforcers in the EAC Partner States believe that if the excise duty rates were to be lowered, there would be (i) implications for the health of the citizens, which would mean increased cost of medical treatments and (ii) loss of government revenue. The study has also revealed the common criteria for imposing excise duty and proposes several approaches for reducing disparities in excise duty rates.

Despite the diverse reasoning by different stakeholders on discriminative taxes and excise duties in the EAC Partner States, there is a wide recognition (among such stakeholders) that elimination or harmonisation of tax policies in the region can play an important role in removing tax distortions in order to bring about a more efficient allocation of resources within the Community.

Whilst the study reveals that the advantages of harmonisation of excise duties in the region are well known by most stakeholders, including policy makers, it also reveals that there has been a number of challenges that hinder the execution, including perceived fear of loss of revenue, lack of political willingness to support the cause, and bureaucratic decision making.

On the other hand, respondents believe that harmonisation of Excise Duty comes with some disadvantages given that different Partner States are at different macro and microeconomic levels as well as industrial development levels.

This report sets out a list of existing discriminative taxes (income tax, VAT and Excise duty), which is attached as **Annex A**. In addition, the report sets out the impact of discriminative taxes and varied or un-harmonised excise duties on intra-EAC trade and investment. In addition, the report sets out an inventory list of excise duties for excisable products and services, which is attached as **Annex B**.

Lastly, this report recommends several options and modalities for the elimination of identified discriminative taxes and harmonisation of excise duties among EAC Partner States. These includes the following:

- Being conscious of the fact that excise duty is commonly a sin tax, the study recommends continuing adopting the hybrid structure of excise duty rates (i.e., both ad valorem and flat rates). This study also recommends removing excise duty on all, non-harmful goods, and services such telecommunication products/ services as well as financial services and introduce environmental taxes such as carbon tax to account for the revenue leakage.
- Inclusion of the private sector in the harmonization of domestic taxes; and



1. Background and Context

EABC has a mandate of promoting the interests of the EAC business community and enhance trade and competitiveness by participating actively and positively in influencing legal and regulatory formulation to improve the business environment. Currently, EABC is implementing the TMEA¹ project titled Public-Private Sector Dialogue (PPD) for Trade and Investment in Eastern Africa.

This regional project targets to mainstream advocacy throughout TMEA's project clusters, which includes customs and tax, and Non-Tariff Barriers (NTBs).

1.1. Rationale and objective of the assignment

One of the EABC-TMEA project outcomes is to improve the adoption and harmonization of customs and domestic tax-related policies and principles among the Partner States with a view of reducing tariffs, taxes, levies, exemption regimes and increasing import/export tax incentives. In line with this outcome, it is noted that through the Treaty for the establishment of the EAC the Partner States undertook to harmonize their tax policies with a view to removing tax distortions in order to bring about a more efficient allocation of resources within the Community. Subsequently, harmonisation of the taxes and non-application of discriminative taxes are emphasized in the three stages of the EAC integration which are Customs Union, Common Market and Monetary Union.

With a non-discriminatory tax regime there is a commitment that in the course of the establishment of the Customs Union, the EAC Partner States shall among other things eliminate internal tariffs and other charges of equivalent effect. The EAC Treaty through Article 75(4) commits the Partner States not to impose any new duties and taxes or increase existing ones in respect of products traded within the Community.

Additionally, Article 15 on National Treatment of the Protocol on the Establishment of the EAC Customs Union bar EAC Partner States from using discriminately administrative measures or internal taxes on imported products from the EAC Partner States against similar domestic products. Specifically, Article 15(1) of the Protocol states that the Partner States shall not (a) enact legislation or apply administrative measures which directly or indirectly discriminate against the same or like products of the Partner; or (b) impose on each other's products any internal taxation of such a nature as to afford indirect protection to other products. Furthermore, the Protocol through article 15(2) reinforces non-discrimination on internal tax by stating that "No Partner States shall impose, directly or indirectly, on the products of the other Partner States any internal taxation of any kind in excess of that imposed, directly or indirectly, on similar domestic products". Article 15(3) on National Treatment of the Protocol ends by stating that where products are exported to the territory of any Partner State, any repayment of internal taxation shall not exceed the internal taxation imposed on them, whether directly or indirectly.

With regards to the harmonisation of excise duties/taxes as part of domestic taxes legal justification is mainly derived from Article 83(2)(e) of the Treaty for Establishment of EAC, which obliges the Partner States to "harmonize their tax policies with a view to removing tax distortions in order to bring about a more efficient allocation of resources within the

Uganda, and The Democratic Republic of Congo (DRC).

¹ TradeMark East Africa (TMEA) is a multi-donor funded, not for profit organization which was established in the year 2010 with the aim of promoting regional trade and prosperity In East Africa. TMEA combines a regional approach with national-level interventions and works closely with East Africa institutions (e.g., EAC EAC Secretariat, Corridors Authorities), national governments, and private sector and civil society organisations. TMEA has its headquarters in Nairobi - Kenya with branches in Burundi, Rwanda, South Sudan, Tanzania,

Community". The Article is reinforced by Article 32 on the harmonisation of tax policies and laws of the Common Market Protocol that states "the Partner States undertake to progressively harmonize their tax policies and laws on domestic taxes with a view to removing tax distortions in order to facilitate the free movement of goods, services, and capital, and the promotion of investments within the Community". In addition, Article 8 of the East African Monetary Union Protocol provides for harmonisation and coordination of fiscal policies and avoidance of harmful tax competition. Tax neutrality is very critical for the good functioning of both the Customs Union and Common Market.

The Protocol on the Establishment of the EAC clearly defines excise duty as a non-discriminative duty imposed by Partner State on locally produced or similar imported goods. This definition reinforces the need for EAC Partner States to harmonize excise duties as part of domestic or internal taxes in the EAC region to avoid trade disputes due to the existence of un-harmonised and discriminatory excise duties against like or similar products.

Furthermore, the EAC Policy for Harmonisation of Domestic Taxes which was adopted in 2018 by the Council has stated that the varied tax systems in the Community may hamper the enjoyment of the freedom granted by the Treaty, the Common Market Protocol, and the Monetary Union Protocol hence the need for harmonisation of domestic taxes. The policy framework provides the scope of the harmonisation of excise duty which includes the determination of dutiable goods and services, excise duty rates and determination of rules on local content.

While customs duties have been mainly eliminated in intra EAC trade, especially for the EAC originating goods, un-harmonised excise duties levied on the movement of goods and services across the region continue to restrict trade, create an unlevel playing field and prevent the full realization of benefits availed by of the EAC integration process (Treaty, Customs Union, Common Market and Monetary Union). Most of the excise duties in the EAC Partner States have discriminatory effects and cause distortions in cross-border transactions and investment decisions. In addition, the un-harmonised domestic taxes are sometimes sources of trade disputes, thus a call for harmonization of domestic taxes.

Despite all the above-mentioned provisions, un-harmonised excise duties and discriminatory taxes are still a major concern for the business community in the EAC. Although the EAC Partner States started to implement the Customs Union in 2005 and the transition period ended in 2010, some Partner States still impose discriminatory taxes in respect of products traded within the Community. In addition, the process of the actual harmonisation of domestic taxes including excise duties has been very slow.

In view of the above, EABC Secretariat through TMEA Regional PPD Programme commissioned this study on discriminative taxes and excise duties in the EAC Partner States.

This study will develop an inventory of all discriminative taxes, the impact of discriminative taxes on intra-EAC trade & investment, analyse the existing excise duties in the EAC Partner States, their impact on intra-EAC trade and suggest clear recommendations & advocacy roadmap for the elimination or harmonisation of discriminative taxes and excise duties.

1.2. Scope of work

The Study as depicted in this report entails undertaking the following:

- Developing a comprehensive list of existing discriminative taxes on goods and services in the EAC Partner States;
- Developing an inventory list of excise duties for excisable products and services and their respective rates in the EAC Partner States;

- Establishing the impact of discriminative taxes and un-harmonised excise duties on intra-EAC trade and investment;
- Analysing the existing excise duties in the EAC Partner States with a view to identifying their differences and similarities;
- Analysing existing rules on local content on excise duty regime in the EAC Partner States;
- Determining and recommending appropriate options and modalities for the elimination of identified discriminative taxes and harmonisation of excise duties in the EAC:
- Proposing common criteria for imposing excise duty on goods and services (including determination of the compulsory list of dutiable goods and services);
- Proposing common criteria for determining the optimal duty rates in the Partner States and common criteria for reducing disparities in duty rates; and
- Developing EABC Policy brief, which the EABC will use to advocate for harmonisation of excise duties and elimination of discriminative taxes on domestic tax regimes in the EAC region.

2. Literature Review

2.1. Introduction

Article 32 of the Common Market protocol provides that the Partner States undertake to progressively harmonize their tax policies and laws on domestic taxes with a view to removing tax distortions in order to facilitate the free movement of goods, services, and capital, and the promotion of investments within the Community.

The International Risk Management Institute defines tax harmonization as a euphemistic term for tax increases, promoted by governments in high-tax jurisdictions, to encourage other jurisdictions to follow their taxing policies, so eliminating "tax havens" for internationally mobile businesses." The best example is the European Union where all countries must have a value added tax of at least 15%. Countries in the European Union have been spearheading harmonisation of taxes to try and make it easier for their citizens, companies, and business to carry out transactions of their goods and services with no restrictions or barriers that are caused by different tax rates in different jurisdictions.

As much as the idea of a harmonized tax system is very attractive, it is somewhat limited by the fact that different countries are at different levels of economic, industrial, and political revolution. This can be evidenced in a study carried out by Fabio Wasserfallen on Political and Economic Integration in the EU: The Case of Failed Tax Harmonization³. The findings showed that the motion to harmonize taxes was predominantly resisted by heads of state of low tax countries. Moreover, the researcher determined that the introduction of central and eastern Europe countries greatly reduced the chances of achieving a uniform tax policy. Hence, it can be concluded that most countries are finding it difficult to come to a compromise with other countries presenting a unique scenario of willingness to unite but at the same time taking care of their own interests.

According to research carried out by the Paul Conconi on the desirability of Partial Tax Harmonization with respect to capital taxes, they looked at scenarios of no tax harmonization (all countries set taxes unilaterally), global tax harmonization (all countries coordinate their capital taxes) and partial harmonization (only a subset of countries coordinates their capital taxes). The researcher concluded that where capital has been made mobile, partial tax harmonization benefits all countries compared to global and no harmonization at all. From this research, it can be concluded that when tax harmonization is implemented within different trading blocs, it is more beneficial compared to all countries trying to achieve a harmonized rate of taxes.

Most recently, the African Union has been spearheading a project called the African Continental Free Trade Area (AfCFTA), whose main agenda is to liberalize import duties (tariff) through Tariff concession. This is being done with a view to making it easier for businesses such that, regardless of where their branches are located, they can avoid the paradox of one branch being more profitable than another due to the preferential taxes and tariffs in different countries.

³ https://wcfia.harvard.edu/files/wcfia/files/fwasserfallen_political_and_economic_integration.pdf

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 $[\]frac{\text{https://www.irmi.com/term/insurance-definitions/tax-harmonization\#:} \sim :text=Tax\%20 Harmonization\%20 \\ \frac{\%E2\%80\%94\%20a\%20 euphemistic\%20 term, havens\%22\%20 for\%20 internationally\%20 mobile\%20 businesses.}$

Bringing it closer home, the EAC recently submitted its tariff concessions, which shows its willingness to achieve harmony with other countries and trading blocs within the African region.

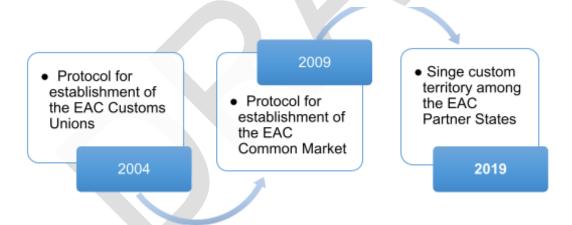
Various studies and efforts have been made in the past concerning the discriminative tax treatments among the EAC Partner States, which has brought us steps closer to harmonisation of the tax regimes. In the various studies, different grounds are given for and against excise duty harmonisation.

According to Cesifo working paper (issue 8442,July 202), excise duties were stated as the most viable option and tax instrument to augment government revenues. The reasoning behind this is that they are collectable and enforceable at low administrative and compliance costs and can be designed to promote economic efficiency and to enhance the progressivity of the tax system. In the paper, Sijbren Cnossen, stated that "Excise duties also tend to meet with a higher degree of public acceptance than most other taxes. Unlike broad-based income and consumption taxes, increases in excise duties need not delay economic recovery".

According to the ActionAid, International Briefing published in October 2018, the major disadvantage of excise taxes is that they may be highly regressive i.e., "Excise taxes on fuel may increase the price of this essential item (and other items too, because of increased transport costs) beyond the reach of poor people, if there are no exemptions".

2.2. Harmonization of taxes in EAC

The EAC has had key milestones since its establishment and among many of those, the table below summarises a few in relation to harmonisation of excise duties in the region:



The need for tax harmonisation is highlighted under various articles of the Treaty for Establishment of EAC, including the following:

- Under Article 75(6) of the EAC Treaty, EAC Partner States are committed to refrain from enacting legislations or applying administrative measures that directly or indirectly discriminate against the same or like products of other Partner States; and
- Article 83(2)(e) of the Treaty for Establishment of EAC obliges the Partner States to "harmonize their tax policies with a view to removing tax distortions in order to bring about a more efficient allocation of resources within the Community".

2.3. EABC Baseline Survey Report by Dr Margaret K. Chemengich

On 26 September 2019, Dr Margaret K. Chemengich submitted a report to EABC, being a baseline survey on customs and domestic tax proposals adopted by EAC Partner States.

This report demonstrated that on domestic taxes EAC Partner States impose discriminatory internal taxes (domestic taxes), levies and other charges on goods transfer to their country. Whilst the report highlighted that there was near convergence on corporate tax rate and VAT rates, it also noted wider disparities on Excise Taxes and taxes on income.

Subsequently, EABC held a consultative Meeting on 30 and 31 October 2019 to harmonize Policy Proposals on Customs and Domestic Taxes⁴. The proposals were submitted to EAC Secretariat.

2.4. EAC Excise Tax Harmonisation impact assessment report by PwC

In November 2014, PwC issued a report on the EAC excise duty harmonisation impact assessment, which covered the then existing policy frameworks and exemption regimes, methods of valuation for excisable goods, and the legal instruments to be used in harmonisation. The report highlighted several challenges associated with the current varied/un-harmonised excise duty regime. Specifically, the report highlighted the following:

- The existence of differentiated excise regimes with major differences in aspects such as rates and bases in the region, have caused artificial price differences in EAC.
 This has led to smuggling and black-market trade hence causing a loss of revenue to the government.
 - Tax remissions and exemptions in some states while they do not exist in other states leads to a distortion of cross market prices.
- The Partner States place too much reliance on increasing Excise tax rates to increase tax collection as opposed to expanding the tax base hence causing resentment among the taxpayers.
- Excise tax is currently aimed at revenue collection as opposed to its original purpose which was to influence consumer behaviour.

PwC's report also summarised three different types of excise structure, which are (i) specific excise structure; (ii) a hybrid structure; and (iii) an ad valorem structure. According to PwC, most respondents interviewed preferred the specific excise structure for the reasons that it is easier to apply and offers consistency, and also less likely to be subjected to manipulative manoeuvres by unscrupulous individuals seeking to outwit the system.

2.5. EAC Domestic Tax Harmonisation Policy approved by the EAC (2019)

In May 2019, the EAC Council of Ministers approved EAC Domestic Tax Harmonisation Policy, with the overall objective of creating a clear regional approach to the harmonisation of excise duties, value added tax (VAT) and income tax so that the Partner States are clear on their roles and responsibilities. This would ensure that the process of harmonisation is efficient, cost effective and consistent.

Prior to the formulation of the Domestic Tax Harmonization Policy, a series of studies were commissioned by the EAC secretariat to provide insights into the tax landscapes in the Partner States and identify three main areas of action: Excise Duties, Value Added Tax (VAT) and income taxes.

According to the EAC Domestic Tax Harmonisation Policy, harmonising Excise duties, VAT, and income taxes in the EAC region will result into the below benefits:

- Eliminating distortions that could undermine the implementation of the EAC Common Market Protocol and the EAC Monetary Union Protocol;
- Facilitating cross-border trade and investment to promote sustainable growth and a fair distribution of available resources in the region;

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⁴ https://eabc-online.com/matrix-of-issues/

- Avoiding harmful tax competition that may artificially render one Partner State more attractive than the others and erode the tax bases;
- Enhancing tax compliance and enforcement; and
- Ensuring predictable and simple tax system and to promote the region as a single investment destination.

Partner States agreed on (i) a gradual approach to tax harmonisation in the EAC and (ii) a sufficiently flexible approach leaving Partner States some flexibility to, for example, set rates (sometimes subject to a minimum). The table below summarises the key policy highlighted in the EAC Domestic Tax Harmonisation Policy.

Taxes	Policy
	 Adopt a destination principle of taxation; Adopt common rules for determining dutiable goods and services; Select common excise duty instruments: ad valorem, specific, or a combination thereof (which could include a mix between ad valorem and a specific); Introduce EAC-wide minimum1 excise rates by type of good and services with regular adjustments and periodic realignment to consider inflation and exchange rate movements;
Excise Duty	 Introduce common tax rules for exports and movement of excisable goods and services between Partner States; Adopt principles for determining the framework for tax incentives for excise duties.
	 Adopt a destination principle of taxation; Adopt common rules for determining, mandatory exemptions and a limited list of optional exemptions;
	 Adopt common rules for determining place of supply, time of supply/ tax point, and taxable values; Adopt a single positive standard rate in each Partner State subject to an EAC-wide minimum;
	 Adopt a zero-rating approach for all exports; Adopt a limited zero rating/ for specific domestic supplies; Adopt limited VAT reliefs for specific persons and organisations;
VAT	 Adopt common rules for implementing the tax credit method; Adopt principles for determining the framework for tax incentives under VAT; Adopt common procedures regarding registration rules; Adopt common minimum thresholds for VAT mandatory registration
	 Adopt common principle of taxation (worldwide or territorial), based on a comprehensive regional study; Allocate the taxing rights on all types of incomes in line with the agreed source and/or residence rules;
Income	 Adopt common rules for determining the tax base; Introduce a minimum income tax rates for each category, to prevent rate competition; Adopt principles for determining the framework for income tax incentives to
Tax	prevent harmful tax competition.

2.6. The EAC Agreement on Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income.

Double taxation remains a major hurdle for cross-border investment flows because investment income sourced in one country is taxed in both the country of source and the country of residence of the taxpayer. The EAC Agreement on the Avoidance of Double Taxation was signed in November 2010, but some of the EAC Partner States have been reluctant in ratifying the same due to fears of loss of revenue and tax evasion.

The agreement set the foundation for taxation of different income from business, investment and employments as follows;

- Profits of an enterprise are only taxable in the country of residence and so are profits from permanent establishments. However, while determining profits of a permanent establishment, amounts charged by the permanent establishment to the head office of the enterprise or any of its offices by way of royalties or fees are not accounted save for banking enterprises. This was intended to limit tax competition among the Partner States while the decision to invest in any of the states would be based on other factors such as the return on capital employed, residual income, gross domestic product and so on⁵.
- Dividends paid by a company which is a resident of a Contracting State to a resident of any of the other Contracting States may be taxed in that other State. However, when such dividends are taxed in the state in which the company paying the dividends is resident, the rate is capped at 5% of the gross amount of the dividends provided that the recipient of the dividends is the beneficial owner of the same.
- Interest arising in a Contracting State and paid to a resident of any of the other Contracting States may be taxed in that other Contracting State. When such interest is taxed in the state in which the company paying the interest is resident, the rate is fixed at 10% of the gross amount of the interest paid. However, interest derived and beneficially owned by the government, political subdivision or local authority of an East African state or institution, body/board which is wholly owned by the aforesaid is exempt from tax.
- Royalties arising in a Contracting State and paid to a resident of any of the other Contracting States may be taxed in that other Contracting State. However, such royalties may also be taxed in the Contracting State in which they arise, and according to the law of that State, but if the beneficial owner is a resident of the other Contracting State, the tax so charged shall be fixed at 10% of the gross amount of the royalties.
- Management or professional fees arising in a Contracting State which are derived by a resident of any of the other Contracting States may be taxed in that other Contracting State. However, such management or professional fees may also be taxed in the Contracting State in which they arise, and according to the law of that State; but where the beneficial owner of such management or professional fees is a resident of the other Contracting State, the tax so charged shall be fixed at 10% of the gross amount of the management or professional fees.
- Pensions, annuities, and social security payments arising in an East African Community state and paid in consideration of past employment to a resident of any other state within the East African Community is taxable only in the state which the payment arises. In circumstances where the payment is made by a resident of any of the other East African Community state or a permanent establishment situated therein, it may be taxed in any of the other states save for national/state contributions which are only taxable in the state which they are made. The EAC DTA seeks to maintain the status quo regarding distributions
- The Contracting States agree to lend each other assistance and support with a view to the collection, in accordance with their respective laws or administrative practice,

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https://www.iflr1000.com/NewsAndAnalysis/the-eac-double-taxation-treaty-explained/Index/1664

of the taxes to which the Agreement apply and of any administrative penalties, interests and costs pertaining to the said taxes.

Generally, the EAC Double Tax Treaty is a key tool for elimination of double taxation and prevent double non-taxation, tax evasion or aggressive tax planning/avoidance. Double Tax Agreements promotes cross-border investment through minimization of tax obstacles among the treaty countries and prevention of cross-border tax avoidance. Therefore, the EAC Double Tax Treaty is an important instrument towards harmonisation of taxes across the region.

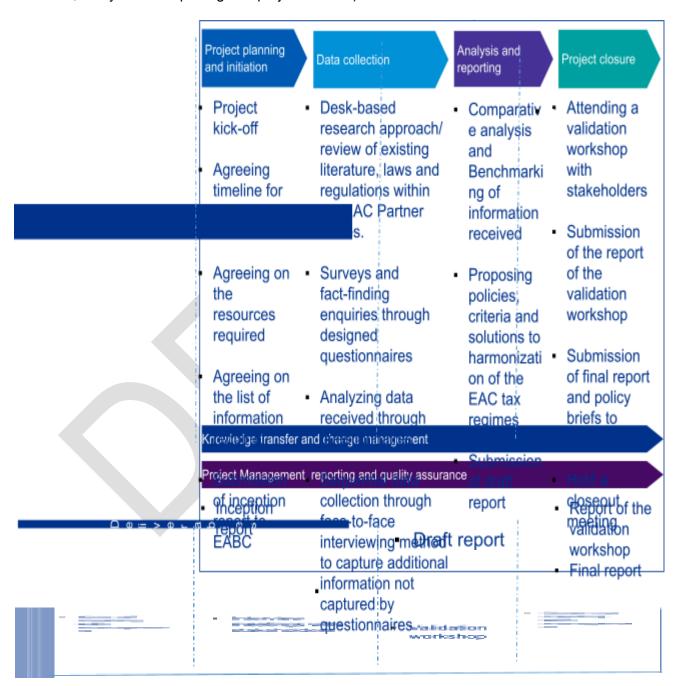


3. Our approach and methodology

3.1. Project approach

KPMG adopted a customized and tailored approach designed to deliver value. During the study, attention was paid to analysing the current discriminative taxes within the EAC with particular attention to Excise Duty with the view of identifying possible alternatives on how they can be harmonized.

We have executed the project through four major phases i.e. (project planning, data collection, analysis and reporting and project closure) as illustrated below:



3.2. Focus areas

In our approach and methodology, we looked and reviewed on the following taxes:

1



Excise duty and electronic tax stamps (ETS) Excise Duty is charged on specific local or manufactured goods and services at varying rates by all EAC Partner States. These rates also vary for similar products among the Partner States.

We identified similarities and variations in excise duties and their impact on trade and

3



Employment taxes (Income Tax??)

- mpសment taxes affects regional
- The inty of also explanate options on a down the duting sets of doing business since employers are also affected.
- Employment taxes greatly differ from country to country including in the EAC Partner States.
- This study also consists of a report

2



Value Added Tax (VAT)

- VAT is a consumption tax charged on supplies of goods and services. The disparities that exist in terms of rates and its implementation among the EAC Partner States is a business concern and was worth studying.
- The study therefore highlighted these disparities and discriminative
- 4



Digital Services Tax (DST)

- pasotiises thewexist in its owing repersonenon and organishes to the trade of the testiment. pursuit of widening their tax base.
 - This study also covered newfound interest in DST and how it can be best implemented to impact trade and investment positively among the EAC Partner States.

4. Results, analysis, and recommendations

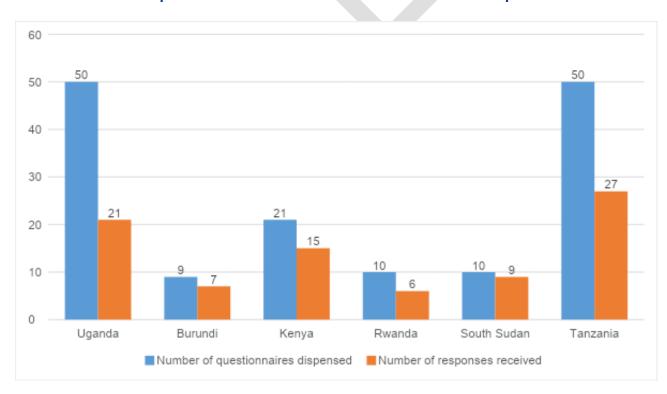
We present below the key findings and analyses of the information collected from various respondents. Our analysis is directed at establishing an inventory list of discriminative taxes (domestic taxes) and excise duties in EAC region and recommending on the elimination of discriminative taxes and proposals on harmonisation of excise duty regime for the EAC.

The data were collected through questionnaires, (which were circulated to the intended respondents by email. Our questions were focused on gathering both informed and thoughtful insights on discriminative taxes and Excise duty in general. The questionnaires were supported with both interviews, and documentary reviews.

4.1. Actual number respondents

The study targeted a sample size that was dependent on the importance of the stakeholders in determining the impact of the discriminative taxes as well as their opinion on the harmonization of Excise Duties. Below is the summary of the actual number of respondents as compared to the total intended number of respondents, indicating that a significant number of respondents are yet to respond to the questionnaires:

4.1.1. Actual number of respondents versus the total intended number of respondents

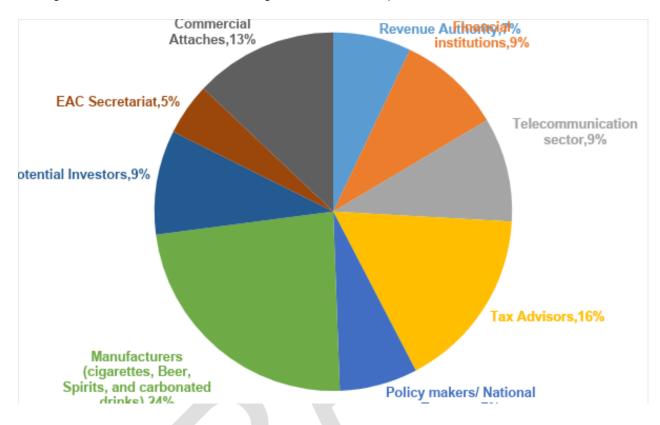


As noted from the above, a total 150 questionnaires were distributed to the respondents, but only 85 (about 57%) have actually been responded to. The poor response rate was triggered by the fact that data collection requests from key respondents such as Government Ministries became bureaucratic and hectic, which demanded more follow up time than anticipated. The other respondents, specifically taxpayers, were rather uninterested and declined the requests for data and information. The disinterest was further expressed with views that the harmonization process of the EAC taxes do not require studies (since there are already enough studies in place) but rather it is largely dependent on other crucial issues like political will – this fact is discussed further under Paragraph 4.3.3 below.

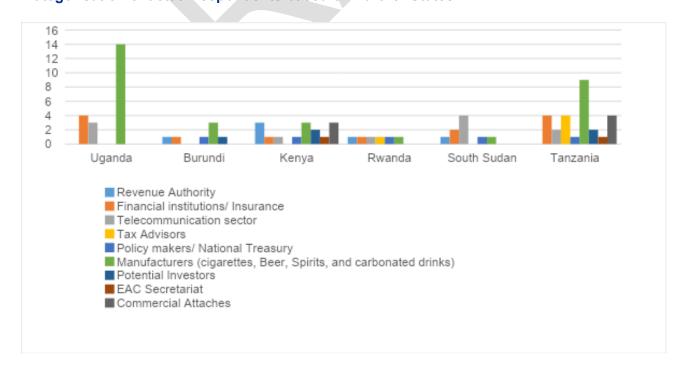
4.2. Categorization of the respondents

4.2.1. Categorisation of actual respondents by percentage

The figures below summarise the categories of actual respondents:



4.2.2. Categorisation of actual respondents based on Partner States



4.3. Stakeholders' views and our analysis of the research findings

In presentation of the research findings, we have analysed the responses based on the different sectors that participated in the survey as summarised under paragraph 4.2 above:

4.3.1. Disparity of domestic taxes

Respondents have highlighted a number of discriminative taxes such as VAT, excise duties and income taxes, which are not harmonized within the EAC countries, and they agree that they have heard investors/ other taxpayers complaining about these discriminative taxes in the region. However, the Respondent from the Burundian Ministry of Finance, Budget and Economic Planning stated that investors have never complained about discriminative taxes.

In addition, majority of the respondents acknowledge that the cost of compliance for manufacturers/ importers of excisable goods is high (except the Burundian Revenue Authority and Agence Burundaise de Developpement, both of whom believe that the cost of compliance for the manufacturers and importers of Excisable goods is Medium). For example, Excise Duty on locally produced goods is calculated and filed 3 times a month in Rwanda.

Another example is the introduction of electronic/digital tax stamps on excisable goods in the region. This is generally reported by manufacturers to have increased the cost of production and encouraging capital flight and inefficiency as it is monopolized by one supplier.

The list of discriminative taxes identified by respondents is attached as **Annex A**. In summary, respondents believe that for the free movement of goods, services, and capital, and the promotion of investments within the EAC to be realized fully, there is a need for harmonisation of the discriminative taxes. It is worth noting that despite free movement of goods within EAC Partner states, the only taxes that are exempt are the ones charged on imports into the Partner states. All other local taxes are levied when goods are being transferred within the EAC Partner states.

Below is the analysis of the domestic taxes that have been identified as discriminative:

(i) Income Tax

Across the region, income tax is based on both source rule and residence status of the taxpayer. Generally, residents are taxed based on worldwide income and non-residents are taxed only to the extent of income sourced from the respective EAC Partner State.

Whilst resident corporations are subjected to 30% income tax (applicable on chargeable profits), resident individuals are generally taxed on progressive rates (with a maximum of 30% for the higher band for all EAC Partner States except South Sudan where the highest band is 20%). However, in Rwanda the Lump Sum regime is available to taxpayers with an annual turnover between FRW 12,000,001 and FRW 20,000,000. The taxpayer must pay a specific 'Lump Sum' tax due equal to 3% of their annual turnover.

Principles of income tax

On the other hand, taxation of partnerships is based on the percentage of their stake/shares in the firm. This ensures that all equity partners share the company profits fairly and are taxed based on their on the share of profits allocated to them. There are no specific rules for taxation of partnerships in

	South Sudan. Partnerships in South Sudan are taxed under business profit
	tax and are considered business organizations.
	Currently, income tax is applicable on chargeable profits (the difference between chargeable income and deductible expenses). Chargeable income
	and deductible expenditure are generally recognised on an accrual basis
	according to generally accepted accounting principles.
	according to generally accepted accounting principles.
	However, the deductibility of expenses for income tax purposes varies from
	one country to the other. The main areas of disparity include restrictions on
	the advance deduction of expenditure, special rules for interest expenditure
	(thin capitalisation rules), depreciation allowances, and Transfer Pricing
	rules. Other disparities arise from filing and payment requirements, whereby
	dates for payments and filing are generally not aligned – which increases
	the cost of compliance.
	The tay have is always dependent on the accommissifuation within a
	The tax base is always dependent on the economic situation within a country. Factors such as inflation, and natural calamities are some factors
	that may cause a tax base to either increase or decrease. This is because
	such events reduce the productivity, financial and economic wellness of
	companies and thus affecting the cashflow within the region. For example, in
	Kenya, the tax rate for companies was reduced to 25% during the
	COVID-19 pandemic. This was to cushion companies since most were not
	able to work and were facing huge losses due to the pandemic.
	Therefore, the EAC partner states should investigate the common factors
	such as industrial revolution, economic stability (inflation) etc to come up
	with a common tax base within the region.
Rules on	Currently, all Partner States within the EAC region employ an income tax
determination of	rate of 30%. Therefore, the EAC could consider maintaining a rate of
tax base	between 25%-30%.
	Income derived by individuals, whether from business or employment, is
	subjected to income tax at progressive rates. However, employment Income
Individual Income	is paid in the form of PAYE, and is remitted by an employer to the Revenue
Taxes	Authority on behalf of the employee.
	In the respective EAC Partner States, WHT is levied at varying rates
	depending on the nature of payment and residence status of the payee. In
	some specific cases, resident WHT is regarded as a final withholding payment and in many cases the WHT suffered is creditable against the final
	income tax. Non-Resident WHT is a final tax.
	modific tax. Non Rootont Will to a martax.
	The withholding tax rates on similar services vary widely among EAC
	Partner States. For example, withholding tax on technical services, rent and
	supplies of goods and services to the governments is at 20% in South
	Sudan while the rate ranges from 5% to 15% in other countries depending
Withholding Taxes	on resident status of the payee.
	All countries across the region have transfer pricing rules, which requires
	that transactions between related parties be at arm's length. For the
	purposes of Transfer Pricing, a Permanent Establishment of a foreign entity
International	is regarded as a distinct legal entity separate from its Head Office.
Taxation and	For the case of Kenya, the following expenses are treated as non-deductible
Transfer Pricing	expenses in determining the taxable income of the PE;

- Interest, royalties or management or professional fees paid by the PE to the non-resident person; and
- Foreign exchange loss or gain with respect to net assets or liabilities established between the PE in Kenya and the non-resident person.

In Tanzania, the above expenses are deductible subject to Transfer Pricing requirements. However, transactions between Head office and the domestic PE are generally not recognised.

(ii) VAT

	VAT is charged based on the source and destination principle, which means that a product is charged VAT based on the source when it comes to importation of goods and services. While the destination principle refers to when VAT is charged at the end process of selling the goods and services to the consumer.
	However, for countries such as Tanzania, the destination principle entails inclusion of the "use or enjoyment clause", which intended to ensure taxation takes place where services are ultimately consumed. This is reported by respondents as a grey area especially when services are performed in Tanzania but delivered to persons outside Tanzania.
VAT Principle to be used	In South Sudan, there is no VAT regime. The Country has sales tax. It is a consumption tax charged on the production of goods in South Sudan, the import of goods into South Sudan and specified services such as hotel, bar, and restaurant services. The Finance Act 2022/23 also introduced sales tax on telecommunications and commissions. The rate of sales tax is 18%.
Determination of	The common VAT rate among the EAC partner states is between
taxation rates	16%-18%. Respondents believe that a tax rate of 16% is more reasonable. VAT on imported services is accounted for on a Reverse- charge
VAT treatment of cross border/ imported services.	mechanism, meaning that it is recognised as both input and output VAT. In South Sudan, imported services do not attract sales tax.
	In all countries, refund claims are made by way of formal application. In some countries the refund application is made online and in other countries the refund application is made in writing after the taxpayer has carried out a VAT refund audit by an independent licensed Certified Public Accountant. In Rwanda, the refund process is to some extent automated. If during a particular prescribed taxation period, the input tax exceeds the output tax, the Commissioner General of Rwanda Revenue Authority is required to refund the supplier the due amount to which the supplier stands in credit by reason of the excess, on receipt of the relevant tax return document within thirty (30) days; • After one day from the expiry of the prescribed period for tax declaration.
Procedures for refund	 After receipt of proof of the last outstanding tax declaration. There is no VAT regime in South Sudan.
Rules for differentiated sectors	In countries like Kenya, there are products that have different VAT rates based on their sector. For example, petroleum products have a different rate of 8%, different from the standard rate of 16% charged on other goods and services. This is done in order to encourage transportation and industrialization in the country.

In the recent past, taxpayers in Tanzania have been submitting similar proposals during pre-budget consultation window. However, the above is yet to be adopted in Tanzania.

(iii) Electronic tax stamps (ETS)

From the analysis of the questionnaires, most respondents alluded that the cost of compliance in the manufacturing sector is high and thus a hindrance to the cost of doing business in the EAC.

Different respondents from the manufacturing sector (except South Sudan, which do not have ETS) have reported that the cost of ETS is on the higher side. For example, ETS has been introduced on carbonated soft drinks in Tanzania since August 2019 at US\$ 3.60 per 1000 stamps. Subsequently in January 22 this has been fixed as TZS 8,082.62 per 1000 stamps. As a result, businesses have been incurring significant additional cost to manufacture, resulting in loss of margins and difficult to support its working capital requirements.

Since ETS has made the control system around Excise Duty revenue more robust, we would opine that this would probably be the right time to reduce either Excise Duty or ETS cost and make businesses viable financially. We also recommend that each country should have different colours of the excisable stamps for the different categories of excisable products to ensure correct capture of trade statistics and to ensure that counterfeits from the partner states are easily identifiable.

As part of the efforts to harmonize the tax in the Partner States, it is imperative that the effects of the varying prices of the electronic stamps be considered as they contribute to higher prices for products. We would recommend that the respective Governments considers competitive tendering for the stamp suppliers, and should one be selected to operate within the region, prices should be benchmarked between the Partner States.

(iv) Excise Duty

In East Africa, Excise duty is generally imposed on the following items:

- excisable goods manufactured in the Partner State a by a licensed manufacturer;
- excisable services supplied in the Partner State by a licensed person; or
- excisable goods imported into the Partner States.

Unlike other EAC countries, South Sudan imports most of the items that are excisable. These imports include; cigarettes, buses, motor cycles, motor vehicles, soft drinks (except water), beers and wines. Considering that South Sudan is a young economy, the tax base for excise duty is not as broad as other EAC Partner States. However, the country is finding ways to avoid over dependency on the oil resources in the country by widening the tax base. According to the National Revenue Authority, out of the total revenue contribution, domestic tax contributes 82%, customs contribute 18%. The biggest contributor of the domestic tax is the business profit tax followed by Personal Income Tax and then excise duty. For some of the respondents we interviewed like MTN South Sudan, it was highlighted that excise duty is the biggest tax expense they have.

The respondents expressed knowledge on applicability of excise duty on excisable products and services as well as the applicable rates in their respective countries. When asked about the rate of Excise Duty, all of the respondents in the Partner States (except Burundi) agreed that the rates are on a higher side. Respondents (taxpayers) in Burundi said that the rates are medium compared to other EAC Partner States.

There is also a general alignment among all respondents that Excise Duty is charged on a large number of goods and services that are not deemed "luxurious" such as financial services, telecommunication products and services, imported pasta, imported potatoes, imported onions, and imported phones (among others). Excise Duty for good or items that are luxuries is not disputed (although the rates may need to be revisited) - but when Excise Duty is applied to items like bank transactions, it defeats the financial inclusion agenda.

Furthermore, it was noted that the rates are high primarily because, each year, through changes in the Finance Act, there is the inclusion of more goods and services, which increases the number of excisable products in the respective countries. This means that the cost of doing business continues to increase, which has a ripple effect on the cost of goods as the increase in excise duty means the burden will be passed down to consumers as well.

Generally, respondents agree that the high rate of Excise Duty can be a barrier for investors investing or intending to invest in the EAC Partner States. However, few respondents (policy makers) believes that if the rates were not as high as they are, there would be implications for the health of the citizens and the cost of health would increase. Despite this argument, they are aligned that excise duty should be progressively reduced on non-harmful goods such as financial transactions. This is expected to improve the cost of doing business in the region.

On the other hand, some of the respondents especially from SEZs do not believe that excise duty is a barrier to their investment given the preferential rates given to them. However, for NGOs, they do believe that excise duty is a barrier, especially due to the rigorous and punitive legislation involved. This informed their response to the cost of compliance which they said is quite high in Kenya and Tanzania.

4.3.2. Harmonisation of Excise Duties

When asked if it is possible to harmonize the Excise Duty rates among EAC Partner States, majority of the respondents said that harmonization would be possible. Essentially, many respondents across all countries of the EAC expressed immense positivity in relation to the harmonization of excise duty rates in the region.

However, l'Office Burundais des Recettes (OBR), which is the Burundian Revenue Authority believe that it may not be possible to harmonize the Excise Duty rates among the EAC Partner States unless there are further studies on Excise Duty harmonization.

The respondents that agree that it is important and possible to harmonize the Excise Duty rates among the EAC Partner States, have stated that harmonisation would come with some advantages as outlined below:

- Decrease in market prices with stabilization (i.e., the products will be affordable). For example, a respondent from cosmetics and perfume industry indicated that Products from Dubai and Other Markets like China are obtained at a low cost and have a better competitive advantage in the market and so the harmonisation will address the problem of the influx of such products on the market.
- Excise Duty will not be a heavy tax burden to taxpayers
- The number of taxpayers will increase due to the willingness of the taxpayers to pay (compliance will improve as smuggling is likely to be minimised).
- Ease the cost of doing business
- Predictability of the EAC tax regime, which is important for businesses to ensure proper tax planning
- Enhance EAC integration toward monetary and political union
- Lower cost of living for citizens in the Partner States

- Attract Foreign Direct Investments into the region
- Level playing field for investors in all countries hence healthy competition
- It will curb round-tripping of products since the main contributor to the round-tripping of goods within the EAC is the excise duty disparity
- Harmonization of excise duty rates will also ensure equity and fairness across the countries as well as ease of application.
- Increase in revenue from excisable goods as harmonization is likely to reduce the number of goods that are disguised as exports to avoid payment of the appropriate taxes
- Ease of trading especially for the landlocked countries like Burundi and Rwanda

Whilst highlighting the advantages, some respondents have also cautioned that the harmonisation may not necessarily be advantageous only – it may be associated with some level of disadvantages due to different economic levels, which may result in leakage of revenue for some countries. Below are the disadvantages mentioned by respondents:

- Overreliance on excise taxes for revenue generation (it is easy to tax consumption, a low-lying fruit), lack of creativity or innovation in tax collection
- High cost of living due to high cost of goods and services
- Depressed savings due to more money spent on consumption
- Competing national interests including fiscal needs, varying developmental levels, debt levels, local production capacities for excisable products, and regulations on health (among others), which if not properly addressed, will disenfranchise other Partner States

Given the research findings, it can be deduced that elimination of discriminative taxes and harmonization of excise duty among the EAC partner states may not be an easy feat. This is because different partner states are at different levels of economic and industrialization revolution, and some of the countries may be dependent on the taxes that they impose on the goods. However, given the fact that most respondents believe that harmonization is possible and necessary, it is imperative that the EAC partner states finds solutions to help in minimizing if not eliminate discriminative taxes as well as harmonize excise duty.

One of the ways we recommend is to reduce the cost of compliance for the various taxes mentioned as discriminatory. Some of the repercussion such as penalties and interests are punitive to taxpayers and therefore disincentivise the local manufacturers as well as discourage foreign investment into the country.

Another option would be to start harmonizing the excise duty rate for products gradually among all partner states. Given that the different partner states are at different levels of economic stabilization and industrial revolution, this will ensure that as much as it may take time, the overall objective will still be achieved, and all countries will be growing at the same pace towards achieving the overall goal of harmonization of excise duty rates among the partner states. The end result would help come up with a common act of law such as EACCMA, but now for excise duty.

4.3.3. Impact of discriminative taxes and un-harmonised excise duties on intra-EAC trade and investment

The impact of discriminative taxes is evident among the EAC Partner States through price distortions caused by the different taxes imposed on different products. The differing tax systems hamper the enjoyment of free movement of goods, services, capital, and workers and thus adversely affects the EAC-intra trade. By way of an example and as indicated in **Annex A**, VAT in Uganda, Tanzania, and Rwanda is 18% while in Kenya VAT is charged at

16%. This causes a difference in prices of the commodities between Kenya and Uganda, making one country preferential to trade than the others.

Overall, the intra-EAC trade takes a hit as one country may end up benefitting more than another, which bars the agenda of having a common trading bloc within the EAC. Furthermore, the EAC Agreement on Avoidance of Double Taxation has only been ratified by three countries i.e., Kenya, Uganda, and Rwanda, which means that businesses and investments are facing double taxation on income earned in both countries.

Secondly, illicit trade, which occurs through the smuggling of excisable goods, presence of counterfeit products and tax stamps, or through diversion of export products into the local market, may thrive.

Furthermore, unharmonized excise duties and discriminative taxes cause unfair competition thereby stifling sufficient production of goods. Unharmonized duties and discriminative taxes are harmful to local producers and discourage industrialization. Also, discriminative and unharmonized taxes cause price distortions which limits the enjoyment of free movement of goods, services, and capital.

Lastly, arbitrary changes in unharmonized duties and discriminative taxes discourage a stable inflow of Foreign Direct investment

4.3.4. Legal and Economic Justification

Legally, the EAC partner states have gone great lengths to help harmonize the various tax rates within the region. This includes the formulation of documents such as the EAC Policy on Harmonization of Domestic Taxes as well as the EAC Agreement on Avoidance of Double Taxation., which shows that the Partner States are willing to have a harmonized tax system, even though this has been faced by various challenges economically.

The EAC Agreement on Avoidance of Double Taxation has only been ratified by Uganda, Kenya, and Rwanda. The delay in the harmonization of domestic taxes is primarily because of the perceived loss of revenue and fear by the individual Partner States, of losing sovereignty on tax matters.

Pre-budgetary tax reform proposals have been made by various stakeholders among the different EAC partner states for the fiscal year 2023-24, with Tanzanian taxpayers looking to a reduced excise duty rate on electronic communication services from 17% to 10% as well as increase the VAT registration threshold to TZS 300m (approximately USD 128,000). On the other hand, from 1 January 2023, Kenya increased its capital gains tax from 5% to a whopping 15% while also exempting from VAT plant and machinery imported by manufacturers or investors in the manufacture of pharmaceutical products. In Uganda, there are proposals for expansion of VAT exemption regime to include assistive devices for persons with disabilities, supply of airport user services charged by the CAA and the supply of oxygen for medical use as well as new investment of \$5 million to any hospital with capacity to provide specialized medical care. In Rwanda currently, there is a review of Pay As You Earn (PAYE) bands and VAT on digital supply is to be introduced but with a transitional period.

This goes to show the disparity in the harmonization of different taxes, especially excise duty, given that different items are classified differently among the Excise Duty acts in different Partner States. The EAC should solidify Policy on Harmonization of Domestic Taxes as well as the EAC Agreement on Avoidance of Double Taxation.

4.3.5. What is holding the harmonisation efforts?

Elimination and harmonization of discriminative taxes is not a short but rather a long-term agenda. This study reveals that the efforts to harmonize domestic taxes began about 12 years ago. The efforts were steered by Tax Policy and Tax Administration sub committees in East Africa Community (EAC) soon after the successfully implementation of harmonization of customs taxes.

The approach aimed at developing a regional legal tax instruments with the following objectives:

- Ensure free trade of goods and services within EAC Partner States;
- Harmonise procedures and tax regime to improve compliance; and
- Remove tax competition (rest to the bottom) among EAC Partner States.

In an effort to harmonize domestic taxes, EAC Tax Policy and Tax Administration subcommittee developed and came with draft legal instruments in 2010 for both Excise Duty and VAT referred as EAC Excise Tax Act and EAC VAT Tax Act respectively. The same were brought to the respective ministers of finance for approval, however such efforts were not successful as the ministers were reluctant in approving and instead directed EAC Tax Policy and Tax Administration subcommittee to develop the tax policy that would guide the harmonization before rushing to the harmonization itself.

The subcommittee went back and drafted the tax policy for harmonization of domestic taxes, which was subsequently adopted by the council in May 2019. The main aim of the policy is to guide the process of harmonization of domestic taxes among EAC member states.

The policy highlights, among other things, that harmonization should be a gradual approach meaning starting with a single domestic tax at a time and view its progress before implementing harmonization of another domestic tax. The Partner State, therefore, agreed to first progress on excise harmonisation, followed by VAT and finally income tax harmonisation.

In light of the above background, we posed as an interview question to various respondents, as to what is holding the harmonisation of taxes including excise duties in EAC Partner States. Several respondents opined that acceptance of harmonization of domestic taxes would remove the power of individual Partner States to individually manage its domestic tax structure. This is, again, attributed to the difference in economic status and revenue needs. Therefore, the delay in the harmonization of domestic taxes is primarily because of the perceived loss of revenue and fear of losing sovereignty on tax matters by the respective Partner States.

The efforts on harmonization of excise duty are ongoing and the subcommittee stacked on the harmonization of tax rates (deciding on the minimum rate for taxing). The reason being that each Partner State uses different methods for taxing commodities. Other countries use Ad valorem and others use specific rates which hinder the point at which the minimum rate can be set. However, the subcommittee got assistance from IMF expertise to make the conversion and align the rates. These efforts were expected to resume on 5 December 2022, when the subcommittee meeting of member countries was scheduled to agree on the minimum taxing rate for each commodity. KPMG will follow up on the outcome of this meeting and update the report accordingly.

We also came across a presentation by EABC during 2022/23 Post Budget Consultations and Sensitization EAC Common External Tariff – a meeting that was held in Dar es salaam in July 2022. The presentation slides highlights (among other things) that there is generally no political will to move forward with the harmonisation of the domestic tax agenda because

of fear of losing sovereignty on tax matters. The slides states further that some of the EAC Partner States are fearing that the harmonisation of domestic taxes will erode their policy space of using domestic taxes as policy instruments

The above view of the EABC is mirrored by the EAC Secretariat respondent, who opines that for harmonization of domestic taxes to be successful it requires political will.

4.3.6. Recommendations

Despite the anticipated disadvantages, stakeholders within the region believe that, through the harmonization of excise duty and elimination of discriminative taxes, the region will achieve a greater increase in the volume of intra – EAC trade as well as strengthen the economic, political, and social ties that are already existing among the EAC Partner States.

Based on the above, stakeholders recommend the following:

(i) Criteria for imposing excise duty

Taxes, levies, and fees are usually the methods governments all over the world to generate revenue. Just like other taxes, Excise duty is imposed for the following reasons:

- To raise revenue:
- To deter consumption of certain harmful goods;
- To deter importation of goods from outside the continent considering the MFN rule;
 and
- As an anti-damping measure.

Historically, excise duty used to be a sin tax levied on goods that had negative externalities. However, stakeholders believe that EAC Governments have departed from this initial purpose and are now levying excise duties on non-harmful goods such as financial services, food, and clothing. Clearly, it appears that Excise duty is now driven by revenue collection targets.

As the continent has opened up, intra-Africa trade is now a reality. In line with this, EAC Partner States should open up for Intra-EAC trade and investment. Thus, there is a need to revisit the purpose and limit the applicability of Excise duty to harmful goods manufactured or imported into the region. Stakeholders recommends the following measures:

- Avoid imposing Excise duty on basic goods such as food and clothing
- Consumption of goods and services should not be taxed by way of excise duty but rather should be taxed by way of VAT
- Luxurious or non-basic goods should have an ad-valorem excise duty rates, which is widely the current practice across the region.

(ii) Duty Base of Manufactured and imported products

Currently, excisable goods and services are levied at a hybrid of ad valorem duty rates and specific/ flat rates. South Sudan's excise duty is based on ad valorem only. The table below summarises the common goods excisable in the region:

Tax Base	Tax rates
Beer-Malted	Specific
Beer- Unmalted	Specific
Wine	Specific
Spirit, Liquor etc	Specific

Cigarettes	Specific
Carbonated drinks	Specific
Juices	Specific
Bottled Water	Specific
Motor vehicle	Hybrid
Cellular Phone	Ad valorem
Fuel Products	Specific
Cosmetics	Ad valorem
Internet services	Ad valorem
Financial Services	Ad valorem
Airtime	Ad valorem

Revenue Authorities across the region expressed concerns over chances of tax evasion under the ad valorem rates since unfaithful taxpayers are always looking for strategies to lower their tax burden. However, other respondents recommend the ad valorem duty rates because under this structure excise duty would be determined by volume – meaning it is not discriminative in the sense that low-priced goods do not suffer.

We note from a similar study conducted by PwC in 2014 (refer to <u>paragraph 2.4</u> above) that most respondents interviewed preferred the specific excise structure for the reasons that it is easier to apply and offers consistency, and also less likely to be subjected to manipulative manoeuvres by unscrupulous individuals seeking to outwit the system.

Given the above different reasoning by different stakeholders, we would recommend continuing with the current hybrid structure (i.e., both ad valorem and flat excise rates).

(iii) Excise duty rates

It is worth noting that since the EAC operates as one economic trading zone, there are a number of multinational companies that have presence in more than one country. Therefore, the Excise duty rates should be harmonised in order to avoid smuggling and aggressive tax planning.

The rate for Excise Duty for varying commodities should be limited to a certain maximum rate (say 15%). The majority of the respondents agreed that if the government is to remove/reduce Excise Duty on both imports and locally manufactured goods and services, there will be substitutes for this tax. The suggested one is tax that can be levied on companies polluting the environment (Carbon Tax).

However, the Burundian respondents expressed that they are not aware of a substitute for Excise Duty if the government of Burundi removes or reduces it. In our view, given that the rates in Burundi are perceived medium, we do not see this view of the Burundian respondents as a threat to the harmonisation.

Another substitute could be the formalisation of the informal sector. The local sector is largely informal and means of formalizing should be brought into consideration as a means for additional tax revenue that may be lost due to harmonisation of excise duty in the EAC Partner States. In essence, the informal sector challenges the formal sector with competitions (with either substandard products or cheap products since they do not pay taxes).

(iv) Reducing disparities in excise duty

A move to smooth harmonization should include legislating uniform laws governing excise duty within the EAC region and to have one harmonized excise duty rate for similar excisable goods/ services. This co-ordinated approach will help to ensure that the exemptions and rebates are uniformly applied in the region.

An alternative would be for every Partner State to have their own legal instrument, which would give flexibility and authority to each Partner State to control its affairs. This is also highlighted in the EAC Domestic Tax Harmonisation Policy that was approved by the EAC Council of Ministers in May 2019. However, should this approach be adopted, then there must be a central point (say Council of Ministers) that will be giving directives with regards to the minimum and maximum tax rates but the authority of deciding the tax rate should remain in the hands of the specific Partner State. Such Also, the council directives will have to set the mandatory goods and services to be subjected to excise duty, leaving room for the specific Partner States to add other goods/ services.

In trying to harmonize, the aspect of landlocked countries like Uganda, Burundi and Rwanda should be considered, as the inland costs like transport and handling and transport increase the cost of goods.

Most respondents from Uganda were of the view that harmonization can be achieved by reducing the existing excise duties due to their costly impacts, that in turn discourage foreign direct investment. A more feasible and viable option would be to adopt a common external tariff for excise duty. The common tariff would provide durability in trade, traders would be able to make plans with the confidence that the tariff is constant. The policies affecting excise duty on imports would no longer be changed arbitrarily and this will ensure the attraction of more foreign direct investments.

The EAC Partner States should actively involve the private sector in the harmonization process. More importantly, topics around elimination of discriminative taxes should not be discussed on a bilateral basis – but rather as an EAC economic bloc agenda.

(v) Local content policy on products manufactured using products from the EAC region

Local content (LC) from an EAC perspective is the value contributed to the national economy through the production and sourcing of national goods and services. This is the wealth local Partner State companies create in transforming raw materials sourced from other countries to final outputs for export. At a local country level, this policy endeavours to promote the supply of domestically produced goods and the employment of the local workforce.

EAC countries need to institute local content rules to encourage Intra-EAC trade and investments. Below are some of the examples of the recently introduced local content incentives to benefit local manufacturers in Kenya:

The Kenyan VAT Act was amended by the Finance Act 2022 to exempt from VAT inputs and raw materials used in the manufacture of passenger vehicles and locally manufactured passenger motor vehicles. Based on this provision, locally manufactured means a motor vehicle for the transportation of passengers which is manufactured in Kenya and whose total value comprises at least 30% of parts designed and manufactured in Kenya by an original equipment manufacturer operating in Kenya.

This change is intended to encourage investment in the automotive sector and is highly likely to spur manufacturing of passenger motor vehicles in Kenya.

The Kenyan excise duty Act was amended by the Finance Act 2022 to exempt from excise duty Locally manufactured passenger cars. This may see a reduction in the cost of locally manufactured passenger vehicles. However, this is linked to a condition that at least 30% of the parts are to be designed and manufactured in Kenya by an original equipment manufacturer operating in Kenya.

In 2018, Tanzania introduced local content requirements in the extractive sector⁶ with the objective (among others) of promoting the maximization of value-addition and job creation through the use of local expertise, goods and services, businesses and financing in the mining/oil and gas industry value chain and their retention in Tanzania.

In the case of Uganda, the Parliament passed the National Local Content Bill, 2019, (National Local Content Act) into law and as at December 2022 it awaits the President's assent. The Act seeks to address and remedy the shortcomings and defects with all existing policy, legislation and guidelines touching on the subject of local content in Uganda and include, the Public Procurement and Disposal of Public Assets Act, 2003, (PPDA), the Petroleum (Exploration, Development and Production) Act, 2013, the Petroleum (Exploration, Development and Production) (National Content) Regulations, 2016, the Guidelines on Reservation Schemes to Promote Local Content, 2018 and the 'Buy Uganda Build Uganda' (BUBU) Policy. Each of these laws, regulations, guidelines, and policies presented shortcomings to holistically addressing the overall question of national local content, hence the need for legislation to align them.

The overall object of the Uganda National Local Content Act therefore is to impose local content obligations on ALL persons using public resources or carrying on an activity under a license in Uganda.

In Rwanda, beer produced with locally sourced inputs is charged at 30% compared to Other beers imported, which are at 60%. This is to encourage local manufacturing of beer amongst the residents and boosting the economy. Similarly, wine produced with locally sourced inputs is charged at 30% compared to other wines imported which are charged at a rate of 70%, to encourage local manufacturing of wine amongst the residents and boosting the economy.

Generally, various measures including legislation and strategic documents have been formulated on local content across the region. Encouraging local content will improve value addition and economies of scale for businesses, services, items, and specialists (human capital). Together, these factors would result in increased output, enhanced skill development, greater job possibilities, and improved information transfer.

According to the European Centre for Development Policy Management (ECDPM - 2016), both developed and developing nations utilize local content policies to encourage the use of local inputs and support home companies. Additionally, any economy that wants to thrive economically must consider or give high priority to fostering local content, which is a proliferation that helps to support industrial development.

Promoting local content and a robust manufacturing sector has many advantages, including greater competitiveness, job generation, increased exports, and savings. This is therefore something that can still be deliberated upon and analysed in order to ensure that locally

The local content policy in oil and gas results from the Tanzania Petroleum (Local Content) Regulations which were issued in May 2017.

⁶ The local content Regulations in mining follow the amendments of the Mining Act, 2010 through the Written Laws (Misc. Amendments) Act, Act No. 7 of 2017.

manufactured goods are promoted using incentives that will increase the production and sale of these manufactured goods.

4.3.7. Conclusion

In the financial year 2020/21, the Ugandan Revenue Authority (URA), Tanzanian Revenue Authority (TRA) and Rwanda Revenue Authority (RRA) all showed an increase in excise duty collections with excise duty contributing to 12.17% to Uganda's total revenue collection, 11.88% to Rwanda's total revenue collection as well as 39% to Tanzania's total revenue collection, the highest in the region. More recently, in the financial year 2021/22, the Kenyan Revenue Authority collected KSH 66.529 billion in taxes attributable to excise duty collection, an increase of 6.2% from the previous financial year. This shows the importance of excise duty in the region.

Although stakeholders across the region do not dispute the imposition of excise duties, they believe that un-harmonised or varied and discriminatory excise duty levied against the movement of like or similar goods and services across the region needs to be harmonised. The harmonization of the Excise duties among the EAC partner states is a welcome move because, in general, it will increase investment as well as improve the welfare of the citizens of the different partner states.

However, the harmonisation may also come with some disadvantages given that different member states are at different macro and microeconomic levels as well as industrial levels. Nonetheless, from the responses received from different stakeholders within the region, we believe that, through the harmonization of excise duty and elimination of discriminative taxes as highlighted by taxpayers in different industries, the region shall achieve a greater increase in the volume of trade as well as strengthen the economic, political, and social ties that are already existing among the EAC Partner States.

5. Annexes

Annex A: List of Discriminative taxes (domestic taxes) and excise duties in EAC region

Annex B: Copies of the completed questionnaires



Bibliography

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