# How Uganda is surrendering trillions in tax agreements to multinational firms

We unearth how Double Taxation Agreements (DTAs) — first used in 1919 to prevent taxing the same income twice — are increasingly aiding multinational companies and some wealthy individuals (investors) to evade paying their fair share of taxes. As a result, multinational companies that have earned their income here, rarely pay their taxes, thanks to the DTAs, **Ismail Musa Ladu** writes.

The country is in danger of blindly signing away her taxing rights at the expense of attracting Foreign Direct Investment (FDI) whose impact according to economic analysts is yet to properly propel the economy to the heights previously anticipated.

With Double Taxation Agreements (DTA) also referred to as Double Taxation Treaties (DTT) that Uganda has since entered with about a dozen countries over the years, there is fear among tax experts and practitioners, including the country's tax prefect regarding this legally binding agreements on revenue compliance and mobilisation.

According to tax professionals, the tax rights that the government has signed with several countries, some of which are a well-known tax haven jurisdictions, hasn't helped tax collectors efforts to enforce compliance across board but only enriches multinational companies and wealthy individuals to get away with "murder."

As FDI grows according to Uganda Investment Authority records, tax contributions from such investments have been shrinking. This is pegged on the escalating number of DTAs signed by the government which in turn either reduces or takes away the country's rights to tax revenue earned here by the multinationals and high net worth individuals.

While researching on the status of DTA in Uganda, Ms Mwajumah Mubiru Nakku, found out that a growing number of companies are investing in Uganda through DTA partner states with a sole aim of paying as little taxes as possible or nothing at all if opportunity avails itself.

The biggest benefits accrued from DTAs, according to Ms Nakku's research were in most cases reaped by multi-national companies who cannot wait to take advantage of the reduced tax rates in the agreement and low or zero taxation in home countries.

The tax expert also notes that DTA partner states such as Netherlands and Mauritius – both well-known tax haven jurisdictions – account for a growing number of major investments in Uganda. But Uganda should be concerned about it, because it has grave implications on domestic resource mobilisation.

Unfortunately, Ms Nakku says: "Government appears unprepared or unwilling to take appropriate steps to address this problem."

Crude oil containers in Bullisa district. A study by Oxfam Uganda reveals that a growing number of companies are taking advantage of Uganda's DTA with the Netherlands to invest in Uganda's oil sector. PHOTO BYERONIE KAMUKAMA

## CORPORATE TAX EVASION

A study by SEATINI–Uganda and Action Aid on DTA and corporate tax evasion and avoidance in Uganda indicates that it is no longer uncommon to find capital exporting countries pressurising Low Developing Countries (LDCs) in exchange for FDI, for a favourable tax dispensation which will give the investors reasonable income and the capital exporting countries the right to tax their profits.

The same study further noted that developing countries such as Uganda tend to compete for this FDI from the capital exporting countries, making generous offers of tax incentives. This according to Ms Nakku means developing countries such as Uganda forfeit potential tax revenue. Yet studies including one done by the World Bank revealed that tax incentives are not necessarily what attracts FDI.

"A country does not need tax incentives to invest in another country as there are so many factors which can influence its decision to do so, for example, the location of the country, availability of cheap labour and raw materials, amongst others," SEATINI–Uganda and Action Aid International report reads in part.


### Exploiting DTAs

Strategic investments, according to Uganda Revenue Authority (URA) and Uganda Investment Authority (UIA) researchers, originate from The Netherlands, a northwestern European country, known for its flat landscape of canals, tulip fields, windmills and cycling routes.

Some of the main investments in the mobile communications sector originate from countries which have a treaty with Uganda, but they have been structured via third countries with more favourable treaties.

For example, Bharti Airtel has its headquarters in India but has structured its investments to Uganda via Netherlands. The Uganda-Netherlands treaty makes Uganda a potential treaty shopping route in the field of capital gains tax as it prevents the country from taxing the sale of shares in a Ugandan company by a Netherlands company. This creates a window for a foreign investor to avoid paying capital gains tax on the sale of immovable property in Uganda by structuring the purchase through a vehicle in the Netherlands.

**Shs314b**

REVENUE (CAPITAL GAINS TAX) THAT IS AT STAKE DUE TO THE DOUBLE TAXATION AGREEMENT BETWEEN UGANDA AND NETHERLANDS INVOLVING URA AND ZAIN TELECOM



Oil sample of Uganda's crude oil. China National Offshore Oil Corporation owns their Ugandan petroleum rights through the British Virgin Islands, a tax haven. PHOTO BY ERONIE KAMUKAMA

The DTA between Uganda-Netherlands, is responsible for the capital gains tax dispute involving URA and Zain Telecom, with over $85 million (about Shs314 billion) worth of revenue at stake.

### The case

The matter between URA's Commissioner General versus Zain International BV is currently under arbitration. According to Court documents, Zain International BV disposed of its 100 per cent shareholding in Zain Africa BV to Bharti Airtel International. Both companies are resident in the Netherlands. Zain Africa BV, the subject of the disposal, had 100 per cent shareholding in Celtel Uganda Holdings BV which owned 99.99 per cent of Celtel Uganda Limited.

Celtel Uganda Ltd's shares in Uganda were not transferred and its property, movable or immovable, was not disposed of. The transfer of the shares in Zain Africa BV took place in the Netherlands.

The Commissioner General, Uganda Revenue Authority (URA), raised an assessment of Capital Gain Tax (CGT) against Zain International BV on the resultant gain realised from the disposal of shares.

Zain International BV objected to the assessment and stated that the transaction was only concerned with the transfer of shares of Zain Africa BV in the Netherlands, and that no shares in Celtel Uganda Ltd were disposed of.

The URA later made an objection decision stating that the transaction under consideration is one of gain arising from the disposal of an interest in immovable property located in Uganda.

The Zain case was unfortunately not decided on its merits but on procedural issues, which saw the assessment raised by the URA being set aside for procedural impropriety, although the court maintained that URA had the jurisdiction to raise a proper tax assessment against Zain international BV. Fresh assessment regarding the same was raised by the URA.

This matter is now under arbitration where it has taken years awaiting conclusion.

The Zain case is a reflection of that Uganda could be losing a lot of revenue through transactions, or indirect transfers of capital assets since it does not have any provision regarding the taxation of property in rich countries.

### Treaty shopping

Here is another example of treaty shopping—taking advantage of DTA, involving Uganda and Heritage Oil and Gas Company Limited.

In 2010, HOGL sold its 50 per cent stake in Uganda's oil fields to Tullow Uganda Limited for $1.5 Billion (about Shs5.5 trillion). Accordingly, Uganda, through Uganda Revenue Authority (URA) imposed a capital gains tax on the transaction amounting to $404 million (about 1.4 trillion). This resulted into four years tax dispute in Uganda's Tax Appeals Tribunal and a commercial court in London before Uganda won the battle.

The panama papers report that HOGL had learnt about the eminent CGT liability before it was actually imposed. So it opted to re-domicile from Bahamas to Mauritius to dodge the tax liability in Uganda and partake of the benefit from the Mauritius-Uganda DTA, according to one of the leaked emails.

The move by HOGL to re-domicile was an attempt to avoid paying taxes in Uganda. This shows how Uganda can potentially lose out and not benefit from its DTAs due to aggressive tax planning, tax avoidance and treaty shopping amongst others means.

There is another case that could pave way for more than a trillion shillings loss in revenue once the oil tap begins to flow.

Earlier last year, Oxfam Uganda undertook a study that revealed that Uganda may lose revenue of up to $400 million (Shs1.5 trillion) in a single oil well (Block EA1) in the Albertine, thanks to the DTA with Netherlands.

The study revealed that a growing number of companies are taking advantage of Uganda's DTA with the Netherlands to invest in Uganda's oil sector. This includes companies such as Tullow and TOTAL, which initially invested in Uganda through other countries, but are reported to be re-domiciling the investments in Uganda through Netherlands and (or) Mauritius. This trend is also being embraced by local investors who are reportedly registering their companies through these countries to invest in Uganda.

### Oil rights

To cash in on DTA by paying very little taxes or nothing at all, it has emerged that the ownerships of some of the leading multinational companies investing in key and strategic sectors of the economy hasn't only gotten a little complicated but are also linked to a tax haven jurisdiction.

For example, the OXFAM report discloses that one of the three upstream partners heavily involved in exploitation of the country's oil resource has its parent company in a tax treaty country.

According to the report, both TOTAL and Tullow own their petroleum rights in Uganda through subsidiaries based in the Netherlands.

Before selling its stake, Tullow Oil Plc was a tax resident of the United Kingdom. In Uganda, it owned the rights to its assets here through Tullow Overseas Holdings B.V. The report further found out that TOTAL SA owns its rights through TOTAL E&P Uganda B.V. (Netherlands).

China National Offshore Oil Corporation (CNOOC), the new oil upstream partner owns their Ugandan petroleum rights through the British Virgin Islands, a notable tax haven.

The two—Total E&P Uganda is partnering with CNOOC Uganda Limited, an overseas branch of CNOOC Limited in the development of Uganda's oil resources in the Lake Albert region.

CNOOC became a major player in the year 2012 when Tullow Oil farmed-down an agreement with oil two oil companies—Total E&P Uganda and CNOOC Uganda Limited in which they each acquired interest in the Lake Albert Exploration Areas 1, 1A-Lyec, 2 and 3-Kingfisher before Tullow completely gave way. Together, the partners will soon move into the Development phase of the oil resources.

## TAX HAVENS

### Double Taxation Treaties

The report titled: *Securing a Fair Share of Uganda's Oil Revenues*, noted that Uganda currently has Double Taxation Treaties in place with 10 countries:

1. Belgium
2. Denmark
3. India
4. Italy
5. Mauritius
6. The Netherlands
7. Norway
8. South Africa
9. The UK
10. Zambia

Uganda has negotiated DTAs with United Arab Emirates and China but they are yet to be enforced.

**Shs1.5t**

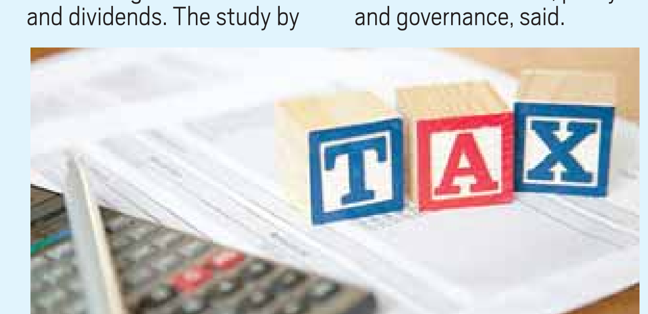
AMOUNT OF MONEY UGANDA COULD LOSE IN AN OIL WELL IN THE ALBERTINE REGGION DUE TO THE DOUBLE TAXATION AGREEMENT WITH NETHERLANDS

### Most attractive tax haven

Netherlands remains a highly attractive location for multinationals to establish subsidiaries.

Having concluded tax treaties with more than 90 countries, routing money through a subsidiary in The Netherlands allows companies to minimise withholding taxes on interest and dividends. The study by OXFAM also revealed that, both TOTAL and Tullow own their petroleum rights in Uganda through subsidiaries based in the Netherlands.

"The Netherlands remains a highly attractive location for multinationals to establish subsidiaries," Mr Gerald Byarugaba, a specialist in extractive resources, policy and governance, said.




### Permanent Establishment

Basing on research conducted by several stakeholders, including URA, Uganda will not get the full benefits arising out her DTAs with Mauritius and the Netherlands. Therefore, a revision of these treaties is needed regarding the Articles on capital gains and the Permanent Establishment Articles.

A permanent establishment (PE) is a fixed place of business which generally gives rise to income or value-added tax liability in a particular jurisdiction.

**10**

NUMBER OF COUNTRIES WHICH UGANDA HAS DOUBLE TAXATION AGREEMENTS WITH


**Multinationals who operate in more than one country therefore plan their taxes in such a way that they pay where the tax rates is low.** ILLUSTRATION BY IVAN SSENYONJO

# How to deal with tax leakages in Double Taxation Agreements

In the second and final part of this article, we look at possible ways to reduce if not eliminate the deep damage caused by the Double Taxation Agreement (DTA) which multinationals companies and several wealthy individuals in the country use to avoid and evade paying their fair share of taxes, **Ismail Musa Ladu** explains.

Uganda Revenue Authority (URA), the country's tax prefect, has raised a red flag over the abuse of the Double Taxation Agreement (DTA) after it has become obvious that the real benefits of the treaty are thoroughly being abused by multi-national companies and some wealthy individuals who shouldn't be having difficulties paying their fair share of taxes.

Unlike previously, the tax collector (URA) now has no second thoughts regarding the damaging effects of DTAs, considering its ability to accentuate a growing risk of revenue losses to the country.

Uganda has DTAs with nearly a dozen countries, including Netherlands, a tax haven jurisdiction. Soon, China and United Arab Emirates (UAE) – who all accounts for a growing number of major investments in Uganda, will join the list.

Already, through the legally binding agreements, multinationals and wealthy individuals are taking undue advantage of the low tax rates provided for in the DTAs to avoid and evade paying their due taxes, all at the expense of domestic revenue generation efforts which URA has, for years, been trying to widen.

"DTA is a tax leakage point; and this concerns us a lot," URA Commissioner General, Ms Doris Akol said last week in a sideline interview.

**Shs1.9b**

TAX ASSESSMENT AMOUNT ACCORDING TO URA FOR TARGET WELL CONTROL UGANDA LIMITED IN RELATION TO CORPORATE INCOME TAX, WITHHOLDING TAX (WHT), PAY AS YOU EARN (PAYE) AND VALUE ADDED TAX (VAT)

She continued: "This is because it (DTA) creates an avenue for people to take away income earned here and have it recognised as income earned in jurisdictions with low tax rates."

### PROFIT SHIFTING

Then there is profit shifting. Here, what should technically be a profit that the corporation has made is characterised as another form of income that attract no taxes or pays very little revenue if at all. According to Ms Akol, this 'immoral' method is increasingly rearing its ugly head.

She said: "Recently, profits that should pay corporation tax are being characterised as intellectual property (IP). And this is because in many of the DTAs, intellectual property is paid to jurisdictions that own it (IP) and in many cases, its tax rate is low."

All these, according to tax experts does not happen by default but by design, particularly after combing through the DTAs looking for any advantage to exploit to the fullest.

In case of a dispute, according to Ms Ruth Namirembe, a tax and legal expert, DTAs supersede the Income Tax Act, making it almost impossible for the likes of tax prefects to win back any tax rights given away by the treaty to another country.

The recent ruling of the High Court of Uganda on what constitutes a permanent establishment among other issues, further exemplifies the effects of DTA to a country's rights to collect taxes earned within its jurisdiction.

In this matter, URA carried out a comprehensive tax audit on Target Well Control Uganda Limited (Target Well Uganda) and assessed tax of Shs1.9 billion in relation to Corporate Income Tax, Withholding Tax (WHT), Pay As You Earn (PAYE) and Value Added Tax (VAT).

The tax collectors demanded Withholding Tax (WHT) on lease payments by Target Well Uganda to Target Well Control (UK) Limited in respect of leased directional drilling equipment. URA also disallowed input VAT arising from supplies made by Neptune Petroleum (U) Ltd (Neptune) to Target Well Uganda.

Target Well Uganda objected to the assessments on grounds that lease payments are not subject to WHT under the Uganda-UK Double Taxation Agreement (DTA). Despite URA objection, the High Court ruled in favour of Target Well Uganda, thanks to the DTA. URA is believed to have appealed this decision because of its impact on domestic revenue mobilisation.



### WAY FORWARD

There is a mixed reaction regarding government's view and understanding of DTAs. On one hand, the government seemed concerned about its effects and on the other, it looks unbothered by the state of affairs.

In an interview with the acting director economic affairs at the Ministry of Finance, Planning and Economic Development, Mr Moses Kaggwa, it emerged that the government fully understands the extent of the damage that the DTAs have on the country's ability to internally generate revenue, explaining why the government took the decision to suspend DTAs in 2014.

But he is also cognisant of government's policy to attract FDI into the country using all sorts of sweeteners and baits, with DTA, despite being a revenue leakage tool, being one of the hooks used to achieve that end of the bargain, even as studies indicate that this kind of initiative does not hold water; for tax and related issue come down the pecking order of a serious investor looking to invest in a country.

In an interview with an economist and a tax expert at the Ministry of Finance, Planning and Economic Development, Mr Gerald Namoma, it was clear that government is not about to ditch DTAs but try to reform them with reflection of the country's current and future aspirations.

"There is no we way can discuss DTAs in isolation of the international context because if you do so you will be an island," Mr Namoma said.

He continued: "Others will sign them (DTA) and you could lose out. The important thing is to have control over them and that is what we are trying to do."

According to Mr Namoma, DTA relevance far supersedes FDI claims, stressing that it is needed to help to relieve tax constraints that could arise between two countries.

He disclosed that government is currently renegotiating with some tax havens over DTAs such as The Netherlands.

Eventually, all DTAs will be reviewed and renegotiated as the Cabinet, according to Mr Namoma has already been put on alert by the minister of finance.

"We are doing this because we are aware about the revenue losses caused by DTA," he said.

### TRANSFER PRICING

For Uganda, according to Ms Akol, DTAs are being used to perpetuate transfer pricing, resulting into revenue losses that the country should have otherwise collected.

Through transfer pricing, a multinational corporation can "transfer the prices" of income and expenses to a low-tax jurisdiction to reduce taxation or get away with it should opportunity arise.

As if that is not bad enough, multinational companies have also taken to treaty shopping to further abuse DTAs. Under this, the corporation does business here but chooses to register the entity in a jurisdiction that has DTAs with Uganda to take advantage of the treaty and not pay its due share of taxes yet the income of the business is being earned in the country, making it taxable here, according to Ms Akol.

### ABOUT DOUBLE TAXATION AGREEMENT

A Double Taxation Agreement is all about who has taxing rights. The purpose is to ensure that taxes are not paid in two jurisdictions. Multinationals who operate in more than one country therefore plan their taxes in such a way that they pay where the tax rates are low.


**Government is trying to reform DTAs to reflect the country's current and future aspirations.** ILLUSTRATION BY IVAN SSENYONJO

## SOLVING DTA ISSUES

### Anti-abusive clause needed


As for Mr Gerald Byarugaba, a specialist in Extractive Resources, Policy and Governance at Oxfam, Parliament must play an active role during DTA negotiations and have the last word on it by endorsing it before enforcement. Currently, DTA is almost exclusively a Cabinet affair and a few government ministries, namely Ministry of Finance and Ministry of Foreign Affairs.

He also suggested that an anti-abusive clause is provided in the DTA, saying that will go a long way in plugging tax leakages emanating from the treaty, further stressing that no matter the circumstances, DTA shouldn't take away tax liabilities. This, he said, should be in addition to denying third parties any opportunities to cash in on DTA.

### Mutual benefits needed

For the Commissioner Customs, Dicksons Collins Kateshumbwa, government shouldn't shy away from tackling this matter which has since become a global concern. To benefit from DTA, Mr Kateshumbwa said the benefits between the countries involved must be mutual.

"There is always a danger if you have a DTAs with a country that perhaps you don't have any trade or economic relations with or very minimal for that matter. With that, you will be giving away perhaps a lot than the benefits you accrue," said Mr Katehsumbwa in an interview last week. Already in an effort to deal with the challenges emanating from DTAs, whose actual objective is to avoid paying taxes in two different jurisdictions, the tax prefect has set up International Tax Division that specifically manages multinationals companies.


### Aggressive tax planning

To reduce the abuse of DTAs, Ms Akol said: "We are beefing up our capacity with help from international tax organisations to enable us recognize all these aggressive tax schemes which are increasingly being frowned upon at international level.

"Aggressive tax planning now being identified as tax evasion is frowned upon. There are moves to create sanctions for it. Listed companies and their regulatory agencies also frown upon aggressive tax planning and we think this is a good gesture," Ms Akol said at the sidelines of URA E-Hub closure last week.

Automatic exchange of information to profile multinationals and understand whether they use DTAs to avoid paying taxes in both countries is becoming a practice among revenue authorities.

She also disclosed that URA has always advocated for renegotiations of DTAs especially, "Where we see a lot of investment being reported as if doing business with Uganda and yet that may not be entirely the case."

Importantly, DTAs shouldn't be viewed as investment attraction instrument but rather bilateral investment treaties, according to Ms Akol. These will be more appropriate because there will be no requirement to lose tax revenues.