This part of the report conducts a brief analysis on another missed opportunity to increase the tax base in ECOWAS: tax incentives. Tax incentives can induce massive losses of government revenues, and can create tax competition. The analysis below demonstrates that tax incentives are not necessarily a primary motivational factor for foreign investment, and yet pose a risk to regional economic integration.

**Despite their high cost, tax incentives are not necessarily a main factor for attracting FDI.** A study by Stefan Van Parys and Sebastian James concluded that tax changes in the CFA Franc zone did not have significant impact on flows of FDI or fixed capital formation. The study shows that other aspects such as increasing investor confidence by broadening legal guarantees and simplifying the tax system were, however, successful in drawing more foreign investments. Furthermore, a comparison among ECOWAS countries and between ECOWAS and other countries shows that a higher corporate tax rate does not necessarily mean less FDI, as illustrated by comparing Côte d’Ivoire and Nigeria, or India, in figure 12.
Other studies conducted in Africa have come to similar conclusions, including a study authored by the Global Tax Simplification Team of the World Bank Group. Surveys of investors in four countries in the East African Community in 2013 showed that more than 90 percent of respondents would still have made investments even without incentives. The experience of Uganda and Tanzania (see Box 3) confirms that the creation or elimination of tax incentives has little direct impact on FDI.

**BOX 3: CASE STUDY: UGANDA AND TANZANIA**

The experience of Uganda and Tanzania has shown that tax incentives are not decisive factors in attracting FDI.

**Uganda:**
In 1997, the Ugandan government decided to eliminate tax relief, leaving Uganda with taxes that are generally higher than the rest of East Africa. The following graph shows that despite higher taxes and no incentive measures, Uganda continued to attract FDI, and did so at a higher rate than the other East African Community countries, which maintained their tax incentives.

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146 WBG, Effectiveness of Tax Incentives in Attracting Investment; Evidence and Policy Implications. N/A.
147 WBG 2013.
Figure 13: Trends in FDI in East African countries

Million US dollars

Source: Tax Justice Network-Africa & ActionAid International, Tax competition in East Africa: A race to the bottom, April 2012

Source: Tax Justice Network-Africa & ActionAid International, Tax competition in East Africa: A race to the bottom, April 2012

Tanzania:
The Government of the Republic of Tanzania introduced Export Processing Zones (EPZ) in 2002. These zones offer “attractive” tax incentives: businesses are exempted from corporate tax and all other taxes for the first ten years. They are also exempted from tariffs on imports of raw materials and equipment. Mining companies are exempted from capital gains tax and tariffs on imported fuel. They pay reduced rates on stamp duties and value-added tax (VAT).

However, the graph that follows shows that, despite the incentives introduced in 2002, there has been no increase in FDI aside from a temporary increase in 2005.

Figure: FDI in Tanzania between 1995 and 2002 (percent GDP)

Further, tax incentives create competition between ECOWAS countries, leading to a net loss at the regional level. A recent International Monetary Fund (IMF) study on 173 countries\textsuperscript{148} showed that tax incentives in a given country can, to a large extent, have negative spillovers on policies implemented in other countries. A one-point reduction in the corporate tax (CT) rate in all 173 countries causes a 3.7 percent reduction in the corporate tax base in a given country over the short term.\textsuperscript{149} Over the long term, the study found that, for a typical country that maintains its corporate tax rate, a one percentage point reduction, collectively, in the CT rate in the rest of the other countries leads to a reduction of approximately 6.5 percent of the CT base in a typical country. The study also observed that in such cases, the typical country, rather than maintaining its CT rate, reduces it by an average of 0.5 point. This increases its tax base by 4 percent, leaving a net loss of 2.5 percent of the tax base (the difference between the exogenous effects – the 6.5 percent reduction of CT base – and the result of the internal adjustments – the 4 percent increase on CT base).

In West Africa, all WAEMU countries enacted their investment codes between 1989 and 2000 granting differing tax incentives (see table 7).

<table>
<thead>
<tr>
<th>Country</th>
<th>Date</th>
<th>Excluded activities</th>
<th>Tax incentives provided in Operation phase</th>
<th>Length of holiday during operation phase (years)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Togo</td>
<td>31 October 1989</td>
<td>Retail</td>
<td>Exemption from tariff and minimum tax; employer payroll tax rate reduced to 2 per cent</td>
<td>Not specified</td>
</tr>
<tr>
<td></td>
<td>3 August 1995</td>
<td>Construction and public works, retail, transportation, financial services.</td>
<td>Exemption from CIT and employer payroll tax; reduction of later to 50 percent and to 25 percent after holiday period ends; exemption from “contribution foncière”</td>
<td>5 to 8 years: depends on activities</td>
</tr>
<tr>
<td>Niger</td>
<td>12 July 2001</td>
<td>Retail, mining, and petroleum</td>
<td>Exemption from tariff (if no local substitute) and VAT</td>
<td>5 years</td>
</tr>
<tr>
<td>Senegal</td>
<td>6 February 2004</td>
<td>Retail</td>
<td>Investment allowance of 50 percent; exemption from employer payroll tax</td>
<td>Up to 8 years: depends on invested amount and whether firm is new or established</td>
</tr>
<tr>
<td>Mali</td>
<td>19 August 2005</td>
<td>Retail, mining, and petroleum</td>
<td>Exemption from tariff (if no local substitute) and VAT</td>
<td>5 to 8 years: depends on amount invested</td>
</tr>
</tbody>
</table>

\textsuperscript{148} IMF, Spillovers in international corporate taxation, 2014. This study was conducted for the period 1980-2013; the sample included all ECOWAS countries (Source: IMF, Spillovers in international corporate taxation, 2014)

\textsuperscript{149} Ibid.
The same trend applies also to the non-WAEMU countries in ECOWAS. For instance, CIT in the mining sector was reduced from as high as 45 percent in 1986 to 25 percent in 2011. At the same time initial capital allowances increased (from 25 percent in 1986 to 80 percent in 2011), as well as exemptions and other expatriate employee tax incentives all in line with the attempt to attract investment. Several other tax incentives in the agriculture and manufacturing sectors have all conspired to create a tax competitive environment by reducing the effective tax rate.

More can be done to harmonize tax incentive policies in the region. ECOWAS and WAEMU have made attempts at harmonizing tax policies. These initiatives include the adoption of a Common External Tariff (CET) within ECOWAS, which implies that all goods entering into the customs territory of any ECOWAS country will be assessed at the same rate of customs duty (0 percent, 5 percent, 10 percent, 20 percent, and 35 percent). The CET is expected to be effective in 2015 within the ECOWAS region. WAEMU has also issued directives that specify the tax rates that countries can apply. However, a recent review of harmonization efforts at the

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**TAX INCENTIVES IN WEST AFRICA**

<table>
<thead>
<tr>
<th>Country</th>
<th>Date</th>
<th>Excluded activities</th>
<th>Tax incentives provided in</th>
<th>Tax incentives provided in Operation phase</th>
<th>Length of holiday during operation phase (years)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Benin</td>
<td>31 December 2009</td>
<td>Retail, reconditioning activities and polluting activities</td>
<td>Exemption from registration fees, tariff, and VAT</td>
<td>Exemption from CIT, patente, and exit tax</td>
<td>5 to 9 years: depends on amount invested and location</td>
</tr>
<tr>
<td>Guinea-Bissau</td>
<td>31 December 2009</td>
<td>Mining, petroleum, forestry</td>
<td>Tariff (Guinea Bissau does not have a VAT)</td>
<td>Exemption from CIT and employer payroll tax; annual reduction of CIT to 90 per cent, 80 percent, 60 per cent, 40 per cent, and 20 per cent thereafter</td>
<td>2 years</td>
</tr>
<tr>
<td>Burkina Faso</td>
<td>29 January 2010</td>
<td>Retail, mining, banking, telecoms (except activities for which a government agreement was signed with the investor)</td>
<td>Tariff reduced to 5 percent, exemption from VAT</td>
<td>Longer loss carry forward period; exemption from employer payroll taxes, patente; investment tax credit; and holiday period extended by 3 years for investment in rural areas</td>
<td>5 to 7 years: depends on amount invested</td>
</tr>
</tbody>
</table>

Source: Mario Mansour and Grégoire Rota-Graziosi; WAEMU, Tax Coordination, Tax Competition, and Revenue Mobilization in the WAEMU, 2013 – based on Investment Codes (enacted between 1989 and 2010).

151 Ibid.
152 ECOWAS, 2014; Gret-Iram, Etude prospective sur les mesures de protection nécessaires pour le développement du secteur agricole en Afrique de l’Ouest (illustration sur quelques filières stratégiques).
WAEMU level has shown that policies other than tax legislation, such as investment codes, may be used by the states as a means to circumvent regional guidelines. This situation derives from the fact that free zone laws at the national level, often part of investment codes, may contain important preferential regimes. For example, Senegal provides income tax holidays for up to 50 years in its 2007 free zone law.

Further, special tax exemptions are sometimes authorized by the very guidelines or regulations that are aimed at harmonizing national tax policies. Indeed, Article 37 of regulation no. 08, on the adoption of rules to avoid double taxation within WAEMU and rules governing assistance in tax matters, stipulates in paragraph 5 that “the provisions of the present Regulation must not form an obstacle to the implementation of more favorable tax treatments provided under the national legislation of the individual member states to promote investment.” This may explain why the overall impact of harmonizing tax incentives has been very limited, as countries can grant tax exemptions outside the tax laws even while following regional directives on applicable tax rates.

Given the net effects of tax incentives on the economy of West Africa, we see a clear need to work toward harmonizing and rationalizing tax incentive policies in the ECOWAS region.

153 Mario Mansour and Grégoire Rota-Graziosi; WAEMU, Tax Coordination, Tax Competition, and Revenue Mobilization in the West African Economic and Monetary Union, 2013.