ENHANCING COMPETITIVE TAX INCENTIVES FOR A SUSTAINABLE INVESTMENTS ATTRACTION IN RWANDA

By HABIMANA Pie
Pg 102000694

A Thesis submitted to the Faculty of Law of the National University of Rwanda in Partial Fulfilment of the Requirements for the Award of the Degree of Master of Laws (LL.M) in Business Law

Under Supervision of Dr. NTEZILYAYO Faustin

October 2011
Declaration

“I, Habimana Pie, hereby declare that this Thesis, entitled Enhancing Competitive Tax Incentives for a Sustainable Investments Attraction in Rwanda is my original work and that, to the best of my knowledge and belief, it has not been submitted and/or presented before for any Degree or any other academic award in any University or Institution of Higher Learning, and that all the sources I have used or quoted have been genuinely indicated and acknowledged as complete references to appraise their author’s intellectual contribution to the world’s science basket”.

________________________________________
Name and Signature of the Candidate

________________________________________
Date
Approval

“I, Dr Ntezilyayo Faustin, confirm that the work reported in this Thesis Enhancing Competitive Tax Incentives for a Sustainable Investments Attraction in Rwanda was carried out by the candidate under my supervision”.

________________________________________
Name and Signature of the Supervisor

________________________________________
Date
Dedicated

To

The Almighty, my parents, and my country—Rwanda.
Acknowledgment

Every time, I feel very thankful to my parents who sent me at school when I was at my early age. At that time, I was not aware of what was happening and innocently followed their instructions. Without their good education, I would not have reached this stage that I am feeling extremely proud of.

I am very grateful to the supervisor of this Thesis, Dr Ntezilyayo Faustin, a true scholar, who provided invaluable guidance throughout the research process, whose instructions have made this Thesis as it is now, and inspired me too much to go up and higher in the field of business tax law. Continuing thanks also go to Dr Emmanuel Ugirashebuja, Dean of the Faculty of Law at National University of Rwanda, a true gentleman, whose advices always shape my ways of acting and living.

I would also like to thank the management of the National University of Rwanda, for having facilitated me to afford my Master’s studies during an entire period of one year. I am indebted to my classmates, whose ambiance and friendship climate have been always an adding strength during a long journey of LL.M studies. My thanks are also due to any person, who in one way another has contributed to the success of my Master’s studies.

Dears, from my deep feelings, I am saying thanks to you all.

HABIMANA Pie
<table>
<thead>
<tr>
<th>Abbreviation</th>
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<tr>
<td>%</td>
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<tr>
<td>AJEP</td>
<td>African Journal of Economic Policy</td>
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<td>art.</td>
<td>article</td>
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<tr>
<td>CEO</td>
<td>Chief Executive Officer</td>
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<tr>
<td>COMESA</td>
<td>Common Market for Eastern and Southern Africa</td>
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<td>DRC</td>
<td>Democratic Republic of Congo</td>
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<td>DTAA</td>
<td>Double Tax Avoidance Agreement</td>
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<td>EAC</td>
<td>East African Community</td>
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<td>ed.</td>
<td>edition</td>
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<tr>
<td>EPZs</td>
<td>Export Processing Zone (s)</td>
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<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
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<td>FIAS</td>
<td>Foreign Investment Advisory Service</td>
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<td>FTZs</td>
<td>Free Trade Zone (s)</td>
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<td>GDP</td>
<td>Gross Domestic Product</td>
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<tr>
<td>GoR</td>
<td>Government of Rwanda</td>
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<tr>
<td>GTZ</td>
<td>Gesellschaft für Technische Zusammenarbeit</td>
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<tr>
<td>IBRD</td>
<td>International Bank for Reconstruction and Development</td>
</tr>
<tr>
<td>ibid.</td>
<td><em>ibidem</em> (the same author, the same book, the same page)</td>
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<tr>
<td>id.</td>
<td><em>idem</em> (the same author, the same book, different page)</td>
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<tr>
<td>ICER</td>
<td>International Centre for Economic Research</td>
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<td>ICRIER</td>
<td>Indian Council for Research on International Economic Relations</td>
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<tr>
<td>ICT</td>
<td>Information Communication and Technology</td>
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<tr>
<td>IFC</td>
<td>International Finance Corporation</td>
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<td>ILO</td>
<td>International Labour Organization</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<tr>
<td>IPAR</td>
<td>Institute of Policy Analysis and Research</td>
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<tr>
<td>ITD</td>
<td>International Trade Department (of the World Bank)</td>
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<tr>
<td>JORIND</td>
<td>Journal of Research in National Development</td>
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<tr>
<td>KFTZ</td>
<td>Kigali Free Trade Zone</td>
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<tr>
<td>KPMG</td>
<td>Klynveld, Peat, Marwick, Goerdeler</td>
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<tr>
<td>KSEZ</td>
<td>Kigali Special Economic Zone</td>
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<tr>
<td>LaRRI</td>
<td>Labour Resource and Research Institute</td>
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LL.M : Latin Legum Magister (Master of Laws)
M&E : Machinery and Equipment
MAGERWA : Magasins Généraux du Rwanda
MIGA : Multinational Investment Guarantee Agency
MINICOM : Ministry of Commerce, Industry, Investment promotion, Tourism and Cooperatives
MNC : Multinational Corporations
MNEs : Multi-National Enterprises
NUR : National University of Rwanda
OECD : Organisation for Economic Cooperation and Development
O.G. : Official Gazette
op. cit. : opera citato
p. : page
parag. : paragraph
Pg : Postgraduate
pp. : from page to page
PPP : Private-Public-Partnership
PREMN : Poverty Reduction and Economic Management Network (of the World Bank)
PUF : Presses Universitaires de France
RADIC : Revue Africaine de Droit International et Comparé
R&D : Research and development
RDB : Rwanda Development Board
RRA : Rwanda Revenue Authority
SEZs : Special Economic Zone (s)
SEZAR : Special Economic Zones regulatory Authority of Rwanda
SMEs : Small and Medium Enterprises
SWOT : Strengths, Weaknesses, Opportunities and Threats
TA : Tax Agreement
TIN : Taxpayer Identification Number
TJN : Tax Justice Network
UAE : United Arab Emirates
UN : United Nations
UNCTAD : United Nations Conference on Trade and Development
UNCTC : United Nations Centre on Transnational Corporations
<table>
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<tr>
<td>UNESCAP</td>
<td>United Nations Economic and Social Commission for Asia and the Pacific</td>
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<tr>
<td>UNIDO</td>
<td>United Nations Industrial Development Organization</td>
</tr>
<tr>
<td>UNR</td>
<td>Université Nationale du Rwanda</td>
</tr>
<tr>
<td>USA</td>
<td>United States of America</td>
</tr>
<tr>
<td>USD</td>
<td>United States Dollar</td>
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<tr>
<td>VAT</td>
<td>Value Added Tax</td>
</tr>
<tr>
<td>VCLT</td>
<td>Vienna Convention on the Law of Treaties</td>
</tr>
<tr>
<td>vol.</td>
<td>volume</td>
</tr>
<tr>
<td>WAEMU</td>
<td>West African Economic and Monetary Union</td>
</tr>
<tr>
<td>WB</td>
<td>World Bank</td>
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<tr>
<td>WEPZA</td>
<td>World Export Processing Zones Association</td>
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<tr>
<td>WTO</td>
<td>World Trade Organization</td>
</tr>
<tr>
<td>www</td>
<td>world wide web</td>
</tr>
<tr>
<td>ZFIE</td>
<td>Zones Franches Industrielles d’Exportation</td>
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Executive summary

Different countries struggle to increase their economic growth and development through different strategies depending on countries’ situations. Worldwide, one of the factors leading to economic growth and development is the attraction of foreign direct investments. Among different factors that attract FDI, tax system stands as one of the major determinants of FDI. As far as Rwanda is concerned, the policymakers have been changing tax laws, especially in 1997, when Rwanda Revenue Authority was created, and in 2005, the year in which major tax laws have been adopted, others modified and complemented. In the focus of attracting investment, Rwanda tax laws offer a number of tax incentives, targeting at making Rwanda’s tax system business friendly.

In front of these, some reports and analysts see these incentives as abusive and qualified Rwanda as tax generous state, which in consequence lead to the lost of a large amount of government revenues. The same reports and analysts also see these incentives as playing a little role as far as investments attraction is concerned. On the other side, there is an opposing perception of some business doers who consider Rwanda’ tax system as constituting one of the major factors that hampers a prosperous development of their businesses.

This Thesis analyses the existing tax incentives that are presently offered under Rwandan tax laws. It also investigates whether Rwanda needs to use tax incentives to attract investments. In front of these, it resulted from the conducted research that Rwanda offers a large number of tax incentives. Unfortunately, it was revealed that such offered incentives are unable to attract investments basically because they do not directly target investment as their purpose. Thus, this Thesis found the creation of Special Economic Zones as one of the effective strategies that can be used to attract more investments in Rwanda. In this regard, this Thesis appreciates the efforts of the Government of Rwanda to establish the special economic zones starting with Kigali Special Economic Zone and call upon the government’s injection of more efforts.
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PRELIMINARY CHAPTER: INTRODUCTION TO THE STUDY

This preliminary chapter deals with the introductory remarks on the research into question and highlights the methodology used to come up with the results of research. The combination of the two gives the reader the general idea on the work done as well as the expectations on the content of the following chapters.

0.1. Introductory remarks

This Thesis constitutes an academic research entitled “Enhancing Competitive Tax Incentives for a Sustainable Investments Attraction in Rwanda”. To undertake a study on tax incentives in a developing country is not an easy task considering that taxes affect and are affected by a wide range of political, economic, cultural, institutional and historical factors as well as revenue flows, income distributions and economic performance. The first part of this preliminary chapter focuses on the background of the study, states the problem and the questions of the research, highlights the theoretical framework, the literature review, explains the objectives of the study, its rationale and significance, formulates the hypotheses and then the scope and the chapters breakdown. And, the second part deals with the used methodology to effectively conduct the research and come with the results herein presented.

0.1.1. Background of the study

Investment, considered in its ordinary meaning as an action or process of investing, is one of the major factors that contribute to the economic development. Investment is defined as an act of putting money into financial schemes, shares or property with the expectation of achieving a profit or devoting one’s time, energy or capital to an undertaking with the expectation of a worthwhile result or more generally buying a product whose usefulness would repay the cost.

Within the line of increasing Rwanda’s economic growth and development, the Government of Rwanda has set up different developmental programs crosscutting different socio-economic sectors like the promotion of investments, both national and foreign investments, promotion of some economic areas like tourism and ICT, development of mega projects like electricity projects, just to mention a few. All these projects cannot be run successfully without FDI

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intervention. Since investors are mainly profit oriented, they choose to invest their capitals in countries where there are enough opportunities to get profits and in which countries, probabilities to get their money back is highly expected. It is in this respect that the Rwandan Government has for example made all efforts to put in place a conducive investment regime, known as National Investment Code as well as other laws thereto related, to attract FDI bearing in mind the package of benefits this one brings and the positive impacts it generates on a country’s economy.3

Worldwide, there exist a number of investment determinants but some are considered to be more crucial than others. Such are for example the situation of the market in general, the labour market, the general security, the good governance, the taxation system or tax legal regime as well as the general justice system, plus other investment facilities, among others. Thus, considering the importance of investments in promoting a country’s development, and recalling the efforts of the GoR to attract both national and foreign investments, it has been logical to us to think of some factors or opportunities that may attract investments, particularly foreign direct investments as well as some other factors that may stand as impediments to investments.

This was the main reason of conducting a research on how taxation system can better be dealt with in order to attract investments, both national and foreign, but particularly FDIs. Taking into consideration the role that investors attach to taxation, different methods can be used to attract investments in Rwanda through taxation deals. A typical example that can be mentioned is the conception of modernised free zones like SEZs (Special Economic Zones)4.

Remembering that these constitute special enclaves, outside a nation’s normal customs barriers, and inside which the firms, mostly foreign, enjoy favoured treatment with respect to imports of intermediate goods, taxation and infrastructure5, a successful creation and management of SEZs in Rwanda, added to other existing potentials, can attract more foreign direct investments.

4 The concept “Special Economic Zones” covers a broad range of specific zone types including but not limited to the Export Processing Zones (EPZ), Free Trade Zones (FTZ), Free Zones (FZ), Industrial Parks or Industrial Estates (IE), Free Ports, Urban Enterprise Zones, etc.
Importance should be attached to the fact that today, the promotion of tax incentives is seen as a strategic determining factor to ensure a country’s economic development and growth and constitutes a major factor of investments. For example, Israeli has created EPZs in which any private enterprise engaged in manufacturing, research and development, or overseas services, including an off-shore financial institution, is eligible to become a zone business, and then benefit different variety of tax reductions and exemptions.\(^6\) Again, the promotion of free zones, in which companies (usually foreign although not absolute) enjoy tax holidays and exemptions from import duties and taxes and other benefits, is one way through which many developing country governments have sought to reap benefits from the global economy.\(^7\)

On this point of dealing with taxes to cope with globalised economy, A. Klemm argues that tax incentives are granted for a wide variety of reasons, but tax competition is a particularly important force behind many of them.\(^8\) The same author affirms that one of the forces shaping tax policy in many countries is the need to maintain a competitive tax system in an increasingly globalised economy\(^9\) with a target to attract mobile capital.\(^10\) Hence, the main concern in this study was to explore how Rwanda can better use tax incentives in order to attract more investments in Rwanda, focusing mainly on the creation and development of Special Economic Zones. Thus, our thesis is entitled “Enhancing competitive tax incentives for a sustainable investments attraction in Rwanda”.

Today, Rwanda relies on a number of potentials like the general security, good governance, the geographical position, etc. to attract investments. Competitive tax incentives, once added to other factors, would increase the revenue and the economic growth of Rwanda. For example, the Rwanda Revenue Authority increased revenues from 9% in 1998 to 14.7% in 2005 thanks to a combination of political will, earmarked technical donor support and the mainstreaming of tax politics and policies within the public domain.\(^11\) Such data shows to what extent is it important to deal with tax parameters in order to increase a country’s economic growth and development.

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\(^7\) P. Glick & F. Roubaud, *op. cit.*, p. 723.


\(^9\) *Idem*, p. 6.

\(^10\) *Idem*, p. 8.

0.1.2. Problem statement
Various studies, although not many, pointed out different analyses with regard to Rwandan tax legal regime. Different authors have generally explored the tax incentives in one way or another, worldwide.\(^{12}\) Other studies have focused on different ways taxation can be used to improve economic growth like descriptive studies of SEZs success or failure stories in different countries worldwide. However, the research gap in this regard concerns the particular features of Rwanda’s legal potentialities to deal with tax incentives as a method to attract investments in Rwanda. As a new contribution, Rwanda’s potentialities as far as investment attraction through tax incentives is concerned have been carefully and systematically researched on. Moreover, this Thesis constitutes the first academic paper on Special Economic Zones, recently introduced in Rwanda.

0.1.3. Research questions
In analysing the trends of enhancing competitive tax incentives as a method of attracting investments, mostly foreign direct investments, in Rwanda, our research focus was guided by the following questions:

1. What tax incentives are presently offered to investors under Rwandan tax laws?
2. Why and to what extent Rwanda needs to use tax incentives to attract investments, i.e. what are the justifications for Rwanda to use tax incentives as a method of attracting investments?
3. What appropriate tax incentives can be used in Rwanda to sustainably attract foreign direct investments?

0.1.4. Theoretical framework
One of the forces shaping tax policies in many countries is the need to maintain a competitive tax system in an increasingly globalised economy, through which, countries attempt to attract capital or taxable profits.\(^{13}\) In this regard, R. Haywood affirms that the one and only policy that can be designed specifically to offer this for a portion of a country is Special Economic Zones (SEZs).\(^{14}\) In the same sense, J. Mutti confirms that free zones have been a successful development tool in many countries since their modern inception in 1950s.\(^{15}\) This author argues, “All of the Asian tigers and newly industrialised countries have used SEZs to their

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\(^{12}\) With regard to this, A. Klemm (op. cit., p. 22) correctly affirms that there is very little work specifically addressing tax incentives for general investment, particularly in developing countries.

\(^{13}\) A. Klemm, op. cit., p. 6.

advantage. So have Mexico, Central America, and a number of Caribbean states. Egypt, the UAE and Jordan have thriving zone programs, and Turkey has been one of the most innovative and successful [special economic] zone countries. Trade growth in Kenya, Mauritius, and Madagascar has also been driven by zones [...] and WEPZA research shows that [special economic] zone policies are most effective in lower middle income countries.\textsuperscript{16}

In this study, attention was paid to FDI tax incentives but more particularly to SEZ as an important tool to create a dynamic investment oriented to exports and kick-start to development. Alliance was done to U. Halim who sees SEZ policy as an opportunistic alliance between the neoliberal agenda of less state intervention and policies of state-led development aimed at maximising profits from the open market regime\textsuperscript{17} as well as to the World Bank Group according to which SEZs have been a powerful instrument for economic growth and structural transformation in the sense that SEZs played a critical role in facilitating the industrial development and upgrading the tiger economies,\textsuperscript{18} and so on.\textsuperscript{19} Our view is that Rwanda, following the example of other small countries like Mauritius and Singapore, can develop SEZs and increase its economic growth and sustainable development. This Thesis even sees SEZs development in Rwanda as one of the most effective ways to foster rapid development.

\textbf{0.1.5. Literature review}

According to J. Olabisi, investors often emphasize the relative importance of tax system in investment decision if compared with other considerations such as political and economic stability, availability of social infrastructure, security of life and property and the general cost

\begin{footnotesize}
\begin{itemize}
\item\textsuperscript{15} J. Mutti, “Economic Processing Zones: Removing Trade and Tax Obstacles to Growth”, Grinell College, WEPZA 25\textsuperscript{th} Birthday Conference, Istanbul, Turkey, 21\textsuperscript{st} October 2003, in \textit{Journal of the Flagstaff Institute}, vol. 28, n° 1, June 2004, p. 23.
\item\textsuperscript{17} U. Halim, “Special Economic Zones: Untold Agonies – Experiences from Asian countries”, India, PAN AP, 2008, p. 6.
\item\textsuperscript{19} A number of authors have developed in one way another, the contributing role of SEZs (per se or through its different aspects) to countries’ economic growth and development. For instance, C. Baissac (\textit{idem}, pp. 64-65) sees EPZ as a pioneer in the attraction of FDI, D. N. Abdulai argues that EPZs accelerate the process of industrialisation of developing countries and constitute a fast pioneer in the attraction of export oriented FDI and exports promotion (D. N. Abdulai, “Attracting Foreign Direct Investment for Growth and Development in Sub-Saharan Africa: Policy Options and Strategic Alternatives”, \textit{Africa Development}, vol. 32, n° 2, 2007, p. 6 available at \url{http://www.ajol.info/index.php/ad/article/view/57170/45558}, accessed on 01\textsuperscript{st} June 2011).
\end{itemize}
\end{footnotesize}
of doing business and so on\textsuperscript{20} and taxation has been used to encourage savings, investment and re-distribution of income.\textsuperscript{21} W. S. Clark argues that the ability to offer a tax system that attracts foreign capital is viewed as a critical component of a national strategy to secure high standards of living, since Multinational Enterprises (MNEs) generate higher than average profits, invest significantly in research and development (R&D), and offer well-paying employment opportunities.\textsuperscript{22}

From a comparative study, different tax centred elements have played a key role in one way or another in a number of success stories particularly in Africa and elsewhere worldwide. For instance, since the mid-1960s, many developing countries have tried to stimulate exports of non-traditional manufactures through establishment of EPZs\textsuperscript{23}, which has led to economic performance of many countries like Indonesia, Republic of Korea, Malaysia and the Philippines in Asia\textsuperscript{24} and Mauritius in Africa. In Mauritius, foreign Chinese firms have been prominent in export processing zone (EPZ) manufacturing and might be seen to have brought in, the main technological impulse from which, the Mauritian economy has benefited since 1984.\textsuperscript{25}

Again, most governments regard SEZs as a suitable strategy to find a niche in the global economy and the World Bank considers the introduction of SEZs as a signal of a country’s departure from import substitution towards an export-oriented economy.\textsuperscript{26} In his studies, J. Olabisi found and concluded that tax incentives had a positive impact on investment decision; and tax incentive coupled with political stability stimulate the economic growth.\textsuperscript{27} Hence, different options can be used depending on which tax incentive is needed for a given category of investment. For example, service investors can better be granted tax holidays whereas EPZ and/or SEZ systems better fit for industrial investments.

\textsuperscript{20} J. Olabisi, \textit{op. cit.}, p. 114.

\textsuperscript{21} \textit{Ibidem}.


\textsuperscript{23} P. G. Warr, \textit{op. cit.}, p. 65.

\textsuperscript{24} \textit{Idem}, p. 66.


\textsuperscript{27} J. Olabisi, \textit{op. cit.}, p. 118.
More specifically, D. A. De Rosa and V. O. Roningen investigated the economic implications of a proposal that Rwanda establish itself as an economy wide free trade zone, following in the footsteps of some better known small, populous countries that have established themselves as free trade zones such as Hong Kong and Singapore in the Far East, and Dubai and Mauritius in the Near East and Africa. The two scholars concluded that the Rwanda FTZ proposal should be viewed as not only attainable but also appropriate to overcome the country’s present international stigma and attract the private sector capital and technical know-how from abroad, necessary to promote Rwanda and integrate its human, agricultural, and other resources more productively into the new global economy and the regional economy of Eastern and Central Africa.

0.1.6. Research objectives
The study was undertaken aiming towards achieving the following objectives:
1. To examine what pro-investment tax incentives can be found under Rwandan tax law;
2. To explore different reasons that justify why and to what extent Rwanda needs to use tax incentives as a method to attract investments;
3. To formulate which appropriate tax incentives can better be used in Rwanda to sustainably attract more investments.

0.1.7. Rationale and significance of the study
This study mainly targeted at providing an insight into Rwanda’s tax legal regime and assessing how far it can be used to attract investments. It is then of great importance to Rwandans since it discusses issues regarding tax incentives, one of the factors that can promote Rwanda’s economic growth and development. This study is also helpful to policy makers and planners since it provides basic data and principles as well as an academic analysis with regard to the area under study.

Scholars interested in researching in this area may also find this study useful for consultation since it is among the first of its kind, if not the first. This study is again beneficial to other researchers by providing necessary knowledge and information to be used as a basis for further research of the same direction.

29 *Idem*, p. 25.
0.1.8. Hypotheses
Rwanda doesn’t have enough natural resources to economically develop itself. However, Rwanda is in strategic geographic position to attract investments and has a number of opportunities from the legal system in general as well as other socio-economic factors. Tax incentives should be added and dealt with systematically, in order to attract investments instead of standing as an obstacle to investments. Hence, different methods of tax incentives can be used like the maximum exploitation and promotion of SEZs. Understandably, Rwanda can get more advantages than disadvantages in setting up such zones.

0.1.9. Scope and chapters breakdown
The factors that affect investment attraction are so many and fall mainly within legal, economic, social and politico-administrative fields. This study only covers the legal perspective of investment attraction through tax incentives deals and is centred on Rwanda. Hence, the main concerned fields of law are the tax law and the investment law. In time, the concern is from 1997, the year of creation of RRA and the starting point of many tax reforms in Rwanda up to now.

This study is subdivided into four chapters. After the preliminary chapter made of the general introduction and the methodology, the first chapter describes the present status of tax incentives and investments in Rwanda. The second chapter analyses the need to increase the competitiveness of tax incentives in Rwanda and the third chapter talks about the modalities of undertaking a new area of tax incentives, which is the creation and development of special economic zones. The fourth and the last chapter draws the conclusions of the study, highlight the recommendations and suggest some areas for future research.

0.2. Methodology
At a large extent, this research was mainly desk research i.e. library and internet based research but complements from field research was also of great importance. This study undoubtedly draws on both primary sources, i.e. first-hand materials, reflections and statements like statutes, cases, official reports and the results of empirical surveys; as well as the secondary sources, i.e. second-hand accounts and comments on primary sources. From this perspective, international and national literatures relevant to the study into question were analyzed and included international legal instruments, national laws and policies, textbooks, 

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journal articles, internet sources as well as other publications. Hereunder, the research design, instruments and sampling for interviews are fully detailed.

0.2.1. Research design
According to G. Rugg & M. Petre, research design is about finding things out systematically, map making as opposed to treasure hunting and, if one plans his/her research design properly, then whatever he/she finds should be a useful contribution to knowledge.31 Thus, our research was mainly exploratory and was literature-based research cross-calibrated by field studies. Hence, during our research, field studies provide important needed data for an advanced and appropriate research standard. Since SEZs are at the introductory stage in Rwanda, we conducted a field visit to analyze how far Rwanda is at now and it provided us the practical image of SEZs development in Rwanda.

0.2.2. Instruments
According to the nature of this study, various instruments were used to get needed data. In order to appropriately collect needed data, methods such as library research, internet searches and interviews with key informants were used. Thus, at first instance, reading books, published and unpublished documents, legal texts, both national and international, reports, and policy papers related to the study; either from library or from the internet, was obviously crucial. We therefore carefully scrutinized and analyzed the documents, which were consulted, synthesized and resorted to comparison methods. To add quality to the provided information, interview guide questions were asked and answers were carefully recorded. Still for interview, the selection of respondents was judgmental, i.e. we purposively used our own judgment about who to interview but the target was always people who are involved in taxation and investment in one way another.

0.2.3. Limitations
Considering the largeness of this study, the main obstacles to this study were related to time and to financial means. The time constraints have for sure limited the collection and analysis of all data, considering that this is an academic research with deadlines. The financial means have also constituted an obstacle to surveys and field studies. For instance, we would have liked to conduct field visits to some regional countries advanced in this matter like Mauritius and Kenya; unfortunately, we have not managed to find sufficient funds for this exercise. The

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two obstacles have also, at some extent, hampered the redaction and editing processes of the final work.

CHAPTER ONE. STATE OF PLAY OF TAX INCENTIVES AND INVESTMENTS IN RWANDA

Like any other tax legal system, the Rwanda tax regime offers a variety of tax incentives to investors. This chapter discusses different tax incentives offered under Rwandan tax laws as well as other aspects of tax that promote investments. It also presents how investment climate is in Rwanda, by analysing how Rwanda competes internationally to attract investors through a legal and institutional framework pertaining to investment.

I.1. Tax incentives

Tax incentives are common around the world and are constantly evolving and few public finance laws are passed without reference to special rules regarding a specific activity or circumstance. In principle, a tax incentive package must be tailored to the particular tax environment and should be designed to provide attractive returns on invested capital and provide a predictable tax environment for the investor. Hereunder, the concept of tax incentive is clarified before presenting different tax incentives that are offered under Rwandan tax laws.

I.1.1. Concept of tax incentives

In terms of art. 2 of the law n° 26/2005 of 17/12/2005 relating to investment and export promotion and facilitation, commonly referred to as National Investment Code, incentive is referred to as any fiscal and non-fiscal inducement given to an investor to support and encourage investment in any sector of the Rwandan economy. In the sense of this law, an incentive can be tax related or not. Since the present concern is tax incentive, reference is made to the Black’s Law Dictionary, which defines tax incentive as a governmental enticement, through a tax benefit, to engage in a particular activity. In this regard, tax incentive refers to a generic term for all the measures adopted by the government to

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33 R. Haywood, op. cit., p. 20.
deliberately manipulate the tax system to the advantage of a potential taxpayer.\textsuperscript{35} Tax incentive is also considered as any measurable economic advantage afforded to specific enterprises or categories of enterprises by (or at the direction of) a government in order to encourage them to behave in a certain manner,\textsuperscript{36} which in some instance may be a tool for attracting investment.\textsuperscript{37}

Tax incentives are also defined as all measures that provide for a more favourable tax treatment of certain activities or sectors compared to what is granted to general industry.\textsuperscript{38} In other words, tax incentive refers to a deliberate reduction in or total elimination of tax liability granted by the government in order to encourage a particular economic unit to act in some desirable ways, which may be to invest more, produce more, employ more, export more, sell more, consume less, import less and pollute less.\textsuperscript{39} In our view, this last definition is more complete than the previous ones because it contains the main idea of tax incentive, which is the removal, in total or in partial, of the tax burden, with a target to incite or stimulate people to act in desirable ways, taking into consideration different functions\textsuperscript{40} of taxes.

I.1.2. Existing tax incentives into Rwandan tax laws

In principal, incentives should be designed to create a transparent and open international standard business environment where the investor will be able to compete with other firms engaged in global trade.\textsuperscript{41} Considering this, Rwanda tax laws offer a variety of tax incentives, including but not limited to profit tax discounts, investment allowances, research and development incentives, as well as other tax incentives offered in one way or another to investors who qualify.

\begin{thebibliography}{99}
\bibitem{36} UN, \textit{Incentives and Foreign Direct Investment}, UNCTAD, Division on Transnational Corporations and Investment, New York, 1996, p. 3.
\bibitem{37} \textit{Ibidem}.
\bibitem{38} A. Klemm, \textit{op. cit.}, p. 3.
\bibitem{40} At this point, it is worthy to mention that taxes have different functions, mainly financial, economic and social. In the views of C. Duanjie, taxes were historically introduced to satisfy government’s need for revenue and taxes constitute a major source of revenue for government (financial function). The same scholar continue arguing that while other motives for taxation emerged as economies became more complex, such as the protection of local industries and industrial promotion (economic function), environmental protection and income redistribution (social function), the primary purpose of taxation is still that of collecting revenue to finance government services. For more details, see C. Duanjie, “Reformulating the Tax Incentive Program in Jordan: Analysis and Recommendations”, ITP Paper 0412, University of Toronto, Joseph L. Rotman School of Management, International Tax Program, p. 5. See also E. Kambanda, \textit{Effects of Taxation System on Business Community in Rwanda: A Survey of Selected Units}, Memoir, Butare, NUR, Faculty of Economics and Management, 2003, p. 21. (not published).
\bibitem{41} R. Haywood, \textit{op. cit.}, p. 14.
\end{thebibliography}
I.1.2.1. Profit tax discount

Under Rwandan tax law, profit tax discount occurs in two categories, namely the case of employment of a large number of Rwandans as well as the case of exports that bring in Rwanda a given amount of incomes. According to art.41 of Income Tax Act, an investor is entitled to a profit tax discount on different rates depending on how much he/she employs Rwandan citizens. Thus, four bands exist to this regard: a profit tax discount of 2% is granted to an investor who employs between 100 and 200 Rwandans, 5% to an investor who employs between 201 and 400 Rwandans, 6% to an investor who employs between 401 and 900 Rwandans, and 7% to an investor who employs more than 900 Rwandans. However, we find this incentive not much attractive for investors since it imposes heavy conditions, which cannot be fulfilled by small businesses. For instance, no single business in Butare town can afford at least the first band, i.e. the band of 2% for an investor who employs between 100 and 200 Rwandans.

Another category of profit tax discount is granted to an investor taxpayer who exports commodities or services that bring to the country a large amount of incomes. In fact, if the exported commodities or services bring to the country between 3,000,000 USD and 5,000,000 USD, the taxpayer is entitled to a tax discount of 3% whereas if the exported commodities or services bring to the country more than 5,000,000 USD the tax discount becomes 5%. Still like for profit tax discount on the ground of employing Rwandans, such exports cannot also be afforded by small corporations and find it not much attractive too.

I.1.2.2. Investment allowances and investment tax credits

Investment allowances and investment tax credits constitute another channel through which investment incentives may be adjusted. Both investment allowances and investment tax

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42 Art. 41 para. 5 of the law n° 16/2005 of 18/08/2005 on direct taxes on income in O.G. n° 1 of 01/01/2006 as modified and completed by the law n° 73/2008 of 31/12/2008 in O.G. n° 19 of 11/05/2009, and again modified and completed by the law n° 24/2010 of 28/05/2010 in O.G. n° special of 28/05/2010, hereinafter referred to as Income Tax Law. However, apart from the number, there exist two other conditions to benefit discount on profit tax. The first condition is to maintain the employees for a period of at least six months during a tax period whereas the second condition is about the remuneration of considered employees that must be paid an amount that is not taxed at 0%.

43 Butare town is situated in the southern province, 135 km away from Kigali city. It used to be considered as the second largest town after the capital city Kigali. Although there are no official recent statistics on Rwanda’s cities’ largeness, Butare town is still considered among the first largest towns of Rwanda, and from the past up to now is regarded as intellectual and cultural purse of Rwanda (X. “Rwanda-Major cities”, available at http://www.rwandatourism.com/test/page.php?uri=major_cities, accessed on 14th August 2011).

44 Art. 42 of the Income tax law.
credits are earned as a fixed percentage of qualifying investment expenditures.\textsuperscript{45} However, although the two may seem to be closer one each other, W. S. Clark differentiates them as follow: “investment allowance is deducted against the tax base, its value to the investing firm depends, among other things, on the value of the corporate income tax rate applicable to the tax base; the higher (lower) the tax rate, the higher (lower) the amount of tax relief on a given amount of investment allowance claimed. In contrast, variations in the corporate tax rate do not affect the value of investment tax credits”.\textsuperscript{46} Thus, unlike a tax credit, the value of investment allowance varies across firms unless if there is a single tax rate, and the value is affected by changes to the tax rate, with a tax cut reducing it.\textsuperscript{47}

Further, investment tax credit refers to a reduction of a certain fraction of an investment from the tax liability.\textsuperscript{48} Thus, investment tax credit is a reduction of tax, not income, by some percentage of the investment, for instance a 10\% investment tax credit for investing in 100,000 USD machine would reduce tax by 10,000 USD.\textsuperscript{49} And, rules of investment tax credit differ regarding excess credits (credits in excess of tax liability) and include the possibility that they may be lost, carried forward or refunded.\textsuperscript{50} In some instances, investment tax credits are offered, not so much as tax incentive, but just to simplify tax administration.\textsuperscript{51}

To encourage investments, the Rwandan tax regime offers investment allowances. From the above distinction from investment tax credit, investment allowance refers to a deduction of a certain fraction of an investment from taxable profits (in addition to depreciation).\textsuperscript{52} According to W. D. Popkin, an asset is depreciable for the tax purposes if (1) it is used for business or income production; and (2) has a determinable useful life (that is, it will eventually lose its usefulness), and then, the depreciation deduction allocates the deduction of


\textsuperscript{46} Ibidem.

\textsuperscript{47} A. Klemm, \textit{op. cit.}, p. 4.

\textsuperscript{48} Ibidem. In the same sense, W. S. Clark, \textit{op. cit.}, p. 1147 distinguishes flat investment tax credit from incremental investment tax credit. According to this author, a flat investment tax credit is earned as a fixed percentage of investment expenditures incurred in a year on qualifying (targeted) capital, while, an incremental investment tax credit, in contrast, is earned as a fixed percentage of qualifying investment expenditures in a year in excess of some base, which is typically a moving-average base (for example, the average investment expenditure by the taxpayer over the previous three years).


\textsuperscript{50} A. Klemm, \textit{op. cit.}, p. 4.

\textsuperscript{51} W. D. Popkin, \textit{op. cit.}, p. 262.

\textsuperscript{52} A. Klemm, \textit{op. cit.}, p. 4.
an asset’s basis over its useful life, in accordance with some formula.\textsuperscript{53} The same author affirms that depreciable assets can be tangible (buildings, machines), or intangible (covenants not to compete), as long as they have a determinable useful life.\textsuperscript{54}

Under an investment allowance, firms are provided with faster or more generous write-offs for qualifying capital costs.\textsuperscript{55} W. S. Clark distinguishes two types of investment allowances:\textsuperscript{56}

1. Investment allowance with accelerated depreciation through which firms are allowed to write off capital costs over a shorter time period than that dictated by the capital’s useful economic life, which generally is accounting basis for depreciating capital costs. While this treatment does not alter the total amount of capital cost to be depreciated, it increases the present value of the claims by shifting them forward, closer to the time of the investment;

2. Investment allowance with an enhanced deduction through which firms are allowed to claim total deductions for the costs of qualifying capital that exceed the (market) price at which it is acquired. Depending on the rate at which these (inflated) costs can be depreciated, this may generate a stream of deductions that exceed, in present value, the corresponding acquisition costs.

Under the Rwandan law no 16/2005 of 18/08/2005 on direct taxes on income\textsuperscript{57}, an investment allowance of 40\% of the invested amount in new or used assets maybe depreciated, excluding motor vehicles that carry less than 8 persons, except those exclusively used in a tourist business is deductible for a registered investor in the first tax period of purchase and/or of use of such an asset if the conditions provided for by the law are fulfilled.\textsuperscript{58} The investment allowance becomes 50\% instead of 40\% if the registered business is located outside Kigali or falls within the priority sectors determined by the Investment Code of Rwanda.\textsuperscript{59}

\textsuperscript{53} W. D. Popkin, \textit{op. cit.}, p. 243.
\textsuperscript{54} \textit{Ibidem}. On this point, the author clarifies the subject matter of depreciation and says that the term “amortization” is usually used for intangible property instead of depreciation. Still in the same line of ideas, depreciation is not limited to property that physically wastes away. Depreciation is a financial concept dealing with investments, not a physics dealing with atoms and molecules. If property is expected to become obsolete in 10 years, it has a 10 year life, even though it physically exists after 10 years.
\textsuperscript{55} W. S. Clark, \textit{op. cit.}, p. 1147.
\textsuperscript{56} \textit{Ibidem}.
\textsuperscript{57} Income tax law as modified and completed up to date.
\textsuperscript{58} Art. 26 of the Income tax law. Such conditions are cumulative and are as follows:
   1. The amount of business assets invested is equal to 30,000,000 Rwandan francs, and
   2. The business assets are held at the establishment for at least three (3) tax periods after the tax period in which the investment allowance was taken into consideration.
\textsuperscript{59} Art. 26 parag. 2 of the Income tax law. In terms of art. 29 of the law no 26/2005 of 17/12/2005 relating to investment and export promotion and facilitation, commonly referred to as national investment code, the priority sectors are information communication and technology; tourism; energy; agriculture and agro-based industries, fishing and forestry; industry; re-export trade; mining; research; infrastructure, especially investments in water
It is worth mentioning that if the business asset that is granted an investment allowance is disposed before the end of the period of three tax periods after the tax period in which the investment allowance was taken into consideration, the reduction of income tax caused by the investment allowance, increased by an interest and penalties applicable to taxpayers who do not pay tax on time, starting from when that investment allowance was granted to the time of disposal, must be paid back to the Tax Administration unless such an asset is removed due to natural calamities or other involuntary conversion. At this point, the Rwandan legislator should have simply excluded the removal of an asset due to force majeure, just to simplify the language, one of the characteristics of a good tax system.

I.1.2.3. Research and development tax incentives

Training incentives or research and development (R&D) incentives, whose intent is to provide the investor with more skilled and thus more productive labour, are often thought of as attractive investment promotion tools and, can take several forms, from providing training programs to tax relief or salary subsidy for on-the-job training. A growing literature has explored the specific effect of R&D tax incentives and found that they have a significant effect.

In most worldwide tax systems, expenses incurred for Research and Development are deductible incomes from taxation. Under Rwandan tax law, this is provided for by article 27 of the Income tax law, according to which all training and research expenses incurred and declared as agreed by a taxpayer and which promote activities during a tax period are considered as deductible from taxable profits. However, expenses on training, research and on promotion of activities as applied in article 27 of the Income tax law do not concern the purchase of land, houses, buildings and other immovable properties including refining, rehabilitation and reconstruction as well as exploration expenses and other assets.

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60 Art. 26 parag. 3 of the Income tax law.
63 However, the application of article 27 is subject to article 21. This article imposes four conditions for a taxable profit to be deducted as expense. It must be incurred for the direct purpose of, and in the normal course of business; it must correspond to a real expense and can be substantial with proper documents; it must lead to a decrease in the net assets of the business; and it must be used for activities related to the tax period in which they it is incurred.
From a wide point of view, expenses incurred for staff training are included within R&D expenses, and hence deductible from taxation. At this point, the Rwandan law remains silent on the extent of training which could be deducted from taxation or not. In front of this ambiguity, one may consider that any training, regardless of the duration or the award is considered as training cost, then deductible from taxable profits.

I.1.2.4. Incentives offered in the VAT code and in national investment code

The Value Added Tax (VAT) was introduced for first time in Rwanda in 2001 as a tax on consumer expenditure collected on business transactions (supply of goods and services) and imports, replacing what was called ICHA (Impôt sur le Chiffre d’Affaires, which was calculated on the turnover). It is governed by a series of acts, ranging from laws to Commissioner General’s rules passing through Ministerial Orders. As far as tax incentives are concerned, the VAT code exempts some goods and services from VAT payment and tax at zero rate exports and supplies to privileged persons. The Rwandan tax law also considers bad debt relief in benefit of a registered supplier taxpayer who cannot recover already paid VAT.

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64 Art. 27 parag. 2 of the Income tax law.
66 The list of exempted goods and services from VAT payment is given out by art. 86 of the law n° 06/2001 of 20/01/2001 on the code of Value Added Tax as modified and completed by the law n° 23/2002 of 10/07/2002 and again modified and complemented by the law n° 25/2010 of 28/05/2010. According to this article, such exempted goods and services are water supply services; goods and services for health purposes; educational materials and services; books, newspapers, journals and other electronic equipments used as educational materials, transport services; lending, lease and sale; financial and insurance services; precious metal; funeral services; energy supplies; trade union subscriptions; leasing of exempted goods; agricultural and livestock products except for those processed; agricultural inputs and equipments; some goods and services imported by persons with investment certificate; listed equipments of information, communication and technology; mobile handsets and the subscriber identification module.
67 Art. 87 of the VAT code.
68 According to article 67 of the Ministerial Order n° 001 of 13/01/2003 providing for value added tax rules and taxation procedure, where a registered supplier has supplied goods or services for a consideration in money, and has paid the full tax on the supply to the Commissioner General, but has not within 18 months alter the supply received payment, in whole or in part, from the person to whom the goods are supplied, the registered supplier may seek a refund of that portion of the tax paid for which he has not received payment. However, this is possible to the condition that the debtor has been declared insolvent under the terms of the law governing insolvency as well as the law on companies. Currently, matters relating to commercial insolvency are governed by the law n° 12/2009 of 26/05/2009 relating to commercial recovery and settling of issues arising from insolvency, in O.G. n° special of 26/05/2009, whereas companies are governed by the law n° 07/2009 of 27/04/2009 relating to companies, in O.G. n° 17 bis of 27/04/2009, as modified and complemented by the law n° 14/2010 of 07/05/2010, in O.G. n° special of 14/05/2010.
Apart from the VAT code, the law no 26/2005 of 17/12/2005 relating to investment and export promotion and facilitation, commonly referred to as National Investment Code, also provides a number of tax incentives. First and foremost, it is important to mention that this law excludes any form of discrimination between foreign investors and Rwandans investors.69 In terms of art. 17 of this code, goods and services imported according to the certificate of registration of an investment project are exempted from payment of VAT that is levied on such goods and services. And, upon request by the RDB, depending on the nature of projects and the importance they have to the nation, their location or the capital invested, the Cabinet may put in place additional incentives and facilities to investors.70 This means that apart from the general incentives that are granted to any investor who qualifies, a given investor may be granted additional incentives, which are particular to him/her and not granted to other investors.

I.1.3. Some other pro-investment tax related aspects

The Rwandan tax system contains a number of some aspects that favour investments. For instance, companies that carry out micro finance activities approved by competent authorities71, pay corporate income tax at the rate of 0% for a period of five years from the time of the approval of the activity, which time period may be renewed.72 The Rwandan tax law also grants foreign tax credits73 and provides for loss carried forward. In this regard, if the determination of business profit results in a loss in a tax period, the loss may be deducted from the business profit in the next five tax periods, earlier losses being deducted before later losses.74 However, foreign sourced losses can neither reduce domestic sourced business profits nor reduce future domestic sourced business profits.75 Under Rwandan tax laws, it is also

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69 In terms of art. 7 of the National Investment Code, foreign investors may invest and have shares in investment projects in Rwanda and shall be treated in the same way as Rwandan investors in matters related to incentives and facilities.

70 Art. 19 of the national investment code.

71 In Rwanda, the power to approve activities of a micro finance fall within the competence of the Central Bank of Rwanda. This is provided for by art. 6.3 of the law no 55/2007 of 30/11/2007 governing the Central Bank of Rwanda as well as the art. 9 and 50 of the law no 40/2008 of 26/08/2008 establishing the organisation of micro finance activities, in O.G. no 13 of 30/03/2009.

72 Art. 42 parag. 3 of the Income tax law.

73 Foreign Tax Credit is provided for by art. 6 of the Income tax law. In terms of this article, if during a tax period, a resident in Rwanda generates income derived from taxable activities performed abroad, the income tax payable by that resident in respect of that income is reduced by the amount of foreign tax payable on such income. However, the reduction of the income tax paid abroad cannot exceed the tax payable in Rwanda on income from abroad. As a matter of evidence, the amount of foreign tax payable shall be substantiated by appropriate evidence such as tax declaration, a withholding tax certificate or any other similar acceptable document.

74 Art. 29 parag. 1 of the Income tax law.

75 Art. 29 parag. 2 of the Income tax law.
possible to pay taxes in instalments and there is also possibility to benefit from waive of tax liability.\textsuperscript{76}

Another pro-investment tax related aspect under Rwandan law concerns the import duties. In terms of Annex I to the national investment code, an investor who imports machinery and raw materials is exempted from import duties; exemption from duties on one personal car, on personal properties and on household properties of a foreign investor or an expatriate who works for a registered investment enterprise; exemption from payment of import and excise duties for a registered investor who imports specialised vehicles, etc.

Still on the issue of import duties, in 1994, import tariff rates in Rwanda were nearly 40\% on average, with tariff peaks as high as 100\% or more, whereas today, they stand at only 11.3\% on average, with tariff peaks no higher than 25\%.\textsuperscript{77} Still on the issue of customs, from time to time, efforts have been put in place to reduce the red tape in view of reducing time taken to clear consignment in customs at the same time to minimize risk as shown by the following table on the gradual reduction of release time over past four years based on mean time from lodging a declaration to exit of goods from customs control.\textsuperscript{78}

\begin{table}[h]
\centering
\begin{tabular}{|c|c|}
\hline
\textbf{Year} & \textbf{Time release} \\
\hline
2007 & 3 days, 11 hours and 16 minutes \\
\hline
2008 & 2 days, 19 hours and 32 minutes \\
\hline
2009 & 1 day, 5 hours and 49 minutes \\
\hline
2010 & 1 day, 2 hours and 3 minutes \\
\hline
\end{tabular}
\caption{Release time of goods from Customs (2007-2010)}
\label{tab:customs}
\end{table}

\textsuperscript{76} According to article 23 of the Commissioner General Rules n° 002/2007 of 15/06/2007 implementing the law n° 25/2005 of 04/12/2005 on tax procedures as modified and completed by the Commissioner General Rules n° 008/2009 of 12/12/2009 a taxpayer may request to pay the tax due in instalments during a period which may not exceed 12 months. However, this is subject to conditions namely to provide a proof of payment of an amount worth at least 25\% of the tax due, regularly pay taxes and duties correctly, not have been implicated in use of forged documents on taxes and duties, provide a guarantee acceptable to the tax administration (even though the Commissioner General may allow a taxpayer to pay in instalments without necessarily executing a guarantee based on circumstantial evidence of hardship or a proved compliance record of the taxpayer). Also, according to art. 69 of the law n° 25/2005 of 04/12/2005 on tax procedures as modified and completed by the law n° 74/2008 of 31/12/2008, in \textit{O.G.} n° 19 of 11/05/2009, it is possible for a taxpayer to apply for a waiver of tax liability, interest on late payments and administrative fines in case of substantial hardships indicating no ability to clear the tax liability. However, to apply for this waiver requires a long process as follows: the waiver is applied for in the note sent to the Commissioner General. If the tax administration finds that the request of the taxpayer is founded, it makes a report to the Minister. The report is then transmitted to the Cabinet in order to make a decision. Again, addition to this long procedure, a waiver of tax liability is granted in a situation where the Competent Court has declared the taxpayer insolvent (art. 5 of the Ministerial Order n° 002/07 of 09/05/2007 governing the implementation of the law n° 25/2005 of 04/12/2005 on tax procedures).

\textsuperscript{77} D. A. De Rosa & V. O. Roningen, \textit{op. cit.}, p. 1.

Among other pro-investment tax related features that can be mentioned are also\(^79\) extended working hours at border posts\(^80\), online services\(^81\), automatic online issuance of TIN when a company is registering at the Office of the Registrar General\(^82\) as well as increased tax service delivery.\(^83\)

I.2. Insight into Rwanda’s investment climate

According to Easter African Community (EAC) Model Investment Code, investment is defined as the contribution of local or foreign capital by an investor including the creation or acquisition of business assets by or for a business enterprise.\(^84\) The Rwandan law doesn’t define what investment is but rather defines investment activity as any new activity, any new business assets whether operations of the expansion, restructuring or rehabilitation of an existing investment enterprise.\(^85\) Worldwide, stimulating inward investment as a growth and development strategy, is pursued both in developed and in developing countries,\(^86\) and Rwanda, like other countries, is involved in fiercely competitive rivalry to attract foreign investors.

\(^79\) Idem, pp. 18-20.
\(^80\) In March 2010, a joint Uganda/Rwanda 24 hours one-stop border pint and simplified trade regime was launched at Gatuna border, and this facility benefits the private sector by accelerating business transactions and providing quality and quick services. The same is La Corniche border with DRC at Gisenyi-Goma.
\(^81\) RRA has now introduced online downloadable tax declaration forms. Furthermore, RRA has also developed the online tax calculators for VAT, personal and corporate income taxes. This facility gives taxpayers an option to print the online filled forms and effectively use them while filing tax declaration forms without using manual calculators, which is prone to errors. Still on the technological improvement, the RRA has introduced ASY-SCAN, a customs system that involves electronic submission of necessary supporting documents. This system is implemented in three offices namely SDV ICD, Kanombe and Gikondo. With this system, clearing agents and other stakeholders can scan documents and interact online with customs officers without leaving their offices.
\(^82\) The registration of companies in Rwanda is currently done according to the law n° 07/2009 of 27/04/2009 relating to companies, in O.G. n° 17 bis of 27/04/2009, as modified and complemented by the law n° 14/2010 of 07/05/2010, in O.G. n° special of 14/05/2010. The application for registration is filled to the Registrar General according to article 13 and the following articles of this law.
\(^83\) Some of RRA services are decentralised and this Authority has offices in many areas like in RDB offices for instance and deals with banks like ECOBANK, BK, COGEBANQUE, which banks collect taxes on behalf of RRA, thus simplifying the tax payment.
\(^84\) East African Community Secretariat, Draft Roadmap Towards Effective Promotion of Investments in EAC, Arusha, Tanzania, February 2008, p. 2; East African Community Secretariat, The East African Community Model Investment Code, Arusha, Tanzania, 2006. According to this Code, Investment include expansion, restructuring, improvement or rehabilitation of a business enterprise; movable and immovable property as well as any other rights in respect of every kind of asset; rights derived from shares, bonds and other kinds of interests in companies and joint ventures; title to money, goodwill and other assets and to any performance having an economic value; rights in the field of intellectual property, technical process and know-how; rights granted under public law including rights to protect, explore, extract and win natural resources.
\(^85\) Art. 2. 9° of the national investment code.
I.2.1. Rwanda in international investment attraction competition

It has been said that investment climate in a country is the collective set of incentives that establish the rules of the game to which economic actors must adhere.\textsuperscript{87} Set by a wide variety of sources, including government policies, cultures of public administration, institutional, social, and physical infrastructure, the investment climate determines the level and certainty of returns expected by investors on every investment made by them.\textsuperscript{88} D. S. Olawuyi\textsuperscript{89} summarizes all those elements and affirms that the general investment climate of a country can be broken down into three main areas namely the macroeconomic and trade policy\textsuperscript{90}, microeconomic framework\textsuperscript{91} and enabling infrastructure.\textsuperscript{92}

To attract investments, a wide range of aspects has to be taken into consideration and improved accordingly. In fact, everything a country does or is can be seen by an investor as either an incentive or a disincentive. In views of R. Haywood, an investor first seeks a predictable environment, then a productive environment, and finally low cost environment.\textsuperscript{93} Thus, a climate that helps to create a predictable, productive, low cost environment attracts investment while actions that interfere with creating such an environment discourage investors.\textsuperscript{94}

As far as investment is concerned, Rwanda is quite active in the regional integration schemes in Africa. Rwanda partakes in a number of global and regional integration organisations and

\textsuperscript{88} \textit{Ibidem}.
\textsuperscript{89} \textit{Ibidem}.
\textsuperscript{90} Macroeconomic and trade policy covers the capacity of domestic institutions to reduce the costs of international trade and finance, and to ensure a consistently safe atmosphere for investments, (e.g. fiscal, monetary, trade, and exchange rate policy, administration of customs ad ports, security of lives and property, strength of rule of law, and political stability). Hence, developing countries bedevilled by war, political instability, dictatorship, the absence of the rule of law, and heavy taxation burdens score very low on this point since they are considered as unsafe and risky for investments.
\textsuperscript{91} Microeconomic framework focuses on the existence of trade friendly regulations, predictable government policies and the availability of efficient enforcing agencies devoid of unnecessary bureaucracy and unwholesome administrative bottlenecks. Thus, a country with flexible and less cumbersome rules on market entry and exit, macro-economic stability, comprehensive legal frameworks on contractual relations, proven enforcement capabilities, availability of pools of skilled workers and other sources of human capital, will be perceived as an attractive location for investments.
\textsuperscript{92} Enabling infrastructure: this covers the availability of key public infrastructure necessary for production activities and investments e.g. electricity, land, efficient security service systems, skilled employees, efficient transportation systems and the availability of basic infrastructural facilities. Since these basic infrastructures are pre-requisites for doing business in a country, developing countries that cannot guarantee them are often considered as unattractive investments locations.
\textsuperscript{93} R. Haywood, \textit{op. cit.}, p. 15.
\textsuperscript{94} \textit{Ibidem}. 
agreements and is eligible for a number of trade and investment initiatives, including but not limited to East African Community, African Union, New Partnership for Africa’s Development, the Community Investment Code of the Economic Community of the Great Lakes Countries, the Common Market for Eastern and Southern Africa, the African Trade Insurance Agency (ATI), etc. In the views of Rwanda Development Board (RDB), Rwanda’s membership in such regional and global organisations and treaties constitutes and serves a great interest to potential investors. Actually, this is true in the sense that the membership in different organisations leads to a number of agreements, which may in one way or another favour investors.

I.2.2. Legal framework of investments in Rwanda

According to the Ministry of Trade and Industry, the Rwandan Government has made all efforts to put in place a conducive investment regime in order to attract foreign direct investment bearing in mind the package of benefits it brings and the positive impacts it generates on the economy of Rwanda. It is in this regard that the National Investment Code has been adopted in 1998 and later on amended in 2005 through the law n° 26/2005 of 17/12/2005 relating to investment and export promotion and facilitation. This National Investment Code enhances the competitiveness of Rwanda as an investment hub that leads to quality production in goods and services.

In addition to this National Investment Code of 2005, other pro-investment laws have been adopted like the law n° 31/2009 of 26/10/2009 on the protection of intellectual property; the law n° 18/2010 of 12/05/2010 relating to electronic messages, electronic signatures and electronic transactions; the law n° 07/2009 of 27/04/2009 relating to companies, as modified and complemented by the law n° 14/2010 of 07/05/2010; the law n° 12/2009 of 26/05/2009 relating to commercial recovery and settling of issues arising from insolvency, etc.

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96 MINICOM, op. cit., p. 7.
97 Ibidem.
98 In O.G. n° 50 bis of 14/12/2009.
99 In O.G. n° 20 of 17/05/2010.
100 In O.G. n° 17 bis of 27/04/2009.
101 In O.G. n° special of 14/05/2010.
102 In O.G. n° special of 26/05/2009.
103 There is a long list of laws recently enacted to boost investment and business in Rwanda. In addition to the above mentioned laws, one can also mention the law on mortgages of 2009 as modified and completed in 2010, the law on security interests movable property of 2009 as modified and completed in 2010, the law governing

Even though the GoR has put in place consistent efforts conducive to investments, which is interesting, the remaining effort in our view would be to deal with tax incentives to complement all efforts undertaken in order to have a full investment attraction and retention complete. In an interview with one investor operating in Kigali, one of the most mentioned impediment to investors in Rwanda was the tax system. In fact, according to this investor, most aspects of doing business in Rwanda are highly attractive but the problem is that some investors may prefer to suspend their activities once established due to unfavourable tax regime, and consequently withdraw their business from Rwanda. However, other two interviewees have been of different views. Unfortunately, they have not clearly defined their arguments, they only insisted on the importance of taxes to a country’s life.

I.2.3. Investments’ institutional framework in Rwanda

The government of Rwanda has amalgamated all its different agencies, which used to deal with investment promotion such as Rwanda Investment and Export Promotion Agency (RIEPA), Rwanda Office for Tourism and Protection of National Parks (ORTPN), etc. into one institution called Rwanda Development Board (RDB). RDB has been established in 2008
by the organic law nº 53/2008 of 02/09/2008. The RDB’s vision is to transform Rwanda into a dynamic global hub for business, investment, and innovation. Its mission is to fast track economic development in Rwanda by enabling private sector growth. RDB has three cross cutting departments namely investment promotion and implementation department, assets and business management department, and the department of human capital and institutional development. RDB operates through five economic clusters namely agriculture, services, tourism & conservation, ICT, and trade & manufacturing. RDB provides different services to boost investment in Rwanda like offering investment certificates and aftercare services, and it has scored much result since its creation.

Although the government of Rwanda has made all those efforts to attract more investors, the tax regime still constitute an un-enthusiastic area which need reforms, through which the government can set up more favourable tax regime to investors. The following chapter discusses to what extent Rwanda needs to increase its tax incentives competitiveness in order to attract more investors.

Summary of the first chapter

Different tax incentives are presently offered under Rwandan tax laws like the profit tax discount, the research and development write off, the possibility of benefiting foreign tax...

\[\text{footnote}110\text{ That is the organic law nº 53/2008 of 02/09/2008 establishing Rwanda Development Board (RDB) and determining its responsibilities, organisation and functioning, in O.G. nº special of 05/09/2008.}

\[\text{footnote}111\text{ Source: http://www.rdb.rw/about-rdb/organization-structure.html, accessed on 04\textsuperscript{th} August 2011.}

\[\text{footnote}112\text{ Investment certificate is a document granted to an investor who fulfils the conditions and entitles him/her to a variety of incentives. Once a business among eligible priority sectors is registered and has a capital investment equal to or more than 250,000 USD for foreign promoters and equal to or more than 100,000 USD for local and COMESA citizens, an investor may apply and register for an investment that entitles access to both fiscal and non-fiscal incentives. However, even though this is a good initiative, the amount of investment required to benefit investment certificate is too high and we would suggest the RDB to reduce it. Again, the law imposes conditions to the holder of a certificate of registration. In terms of art. 9 of the national investment code, such conditions are to keep proper financial and accounting records of the investment enterprise, to make a declaration of the profits of the investment enterprise as required by the tax laws and to transmit a copy to the RDB, to maintain a sample of commodities and data relating to operations of the investment enterprise for a period of 5 years, to permit the employees of the RDB, in the execution of their duties, access to the premises and records of the investment enterprise, to produce a detailed annual activity report indicating the status of the investment enterprise and to submit a copy to the RDB within 3 months after the end of the calendar year, to respond to any questions and to provide information on the operations of the investment enterprise in a period of 5 days of such request, provided that RDB uses this information in confidence.}

\[\text{footnote}113\text{ The aftercare services refer to assistance rendered to investors to ensure that business projects are implemented free of avoidable impediments are offered. This means that for any bottlenecks that may arise, an officer is assigned to follow up and fix the problem, especially if the problem arises between the investor and the government.}

\[\text{footnote}114\text{ For instance in 2010, 105 investment projects were registered with expectation to generate 381,000,000 USD of which FDI is estimated at 173,000,000 USD while local investments are estimated at 208,000,000 USD. 6,207 companies were also registered including the reputable global hospitality brand of Marriott, Radisson and Hilton.}
credits and investments allowances, etc. The VAT law and the national investment code also offer a number of tax incentives to investors who fulfil the laid down conditions. Apart from these direct tax incentives, the Rwanda tax system contains a number of some aspects that play a positive role to attract investors in one way another like the tax administration and governance. All these, added to other investment attraction factors, contribute to the promotion of business in Rwanda. However, the present situation reveals that there is still a need for Rwanda to exploit more the tax system in order to increase the investment flow in Rwanda.

CHAPTER II. ANALYSING THE NEED TO INCREASE THE COMPETITIVENESS OF TAX INCENTIVES IN RWANDA

Tax incentives are a vital component of many governments’ investment promotion strategies and they can play an important role in attracting investment, nurturing domestic production and encouraging firms to expand their supplies.\textsuperscript{115} Tax incentives can also help diversify the economy and move from the heavy reliance on customs and commodity taxes often found in developing countries to greater reliance on the formal economy, including a diversified tax base.\textsuperscript{116}

Offering tax incentives to attract FDI has become a global phenomenon and part of economic globalization in the 1990s, spreading throughout Europe, Asia, and even Africa.\textsuperscript{117} Today, many of the emerging economies and rapid developing countries are those countries that set up tax incentives in the recent past years, i.e. during 1980s-2000s. For example, Korea wrote its foreign investment law in 1998 expanding the scope of tax incentives to foreign investors; Slovakia reduced its corporate tax by 20\% in the 2000 budget; Singapore offers various preferential tax treatments such as concessionary tax rates and tax exemptions to attract foreign banks; Germany allows companies belonging to the same multinational corporation (MNC) to be taxed on a consolidated basis; China has also actively engaged in the competition for FDI by offering tax incentives; and Taiwan, Iran and Nepal all have offered


\textsuperscript{116} Ibidem.

tax incentives to attract FDI in chemical, oil industries, or public utilities. Some other countries like Mauritius, Botswana and Malaysia, have also created free zones and their economies have increased to some extent.

It is widely known that taxation is essential for sustainable development. In fact, taxation supports the basic function of a sustainable state and sets the context for economic growth. To this effect, countries resort to tax competition as effective way to attract investors, whose overall benefit is to stimulate economic growth and sustain the national development. In this regard, Rwanda has set up different tax incentives as presented in the previous chapter. The IPAR Report of June 2011 presented Rwanda as the most generous of the EAC countries in providing tax incentives for FDI and domestic investment. Unfortunately, some analysts find this as having negative impact. Even though, from the above mentioned examples of current world’s good economies, which used tax incentives to attract investments, Rwanda should follow the same line to set up competitive tax incentives regime in order to attract FDI and thus strengthen its economic development.

This chapter presents pro-arguments to the need and use of tax incentives to attract investments in Rwanda. It starts from the relationship between tax incentives, investments and economic growth, then justifies the use of tax incentives and their fitness to Rwanda, and ends with highlight of some principles and drivers in the choice of tax incentives.

II.1. Exploring the nexus between tax incentives, investments and economic growth

There exists a very close relationship between tax, investments and economic growth. In fact, a country’s legislation in general and a country’s tax system in particular, constitute one of

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118 Ibidem.
120 For instance, the IPAR Report of June 2011 criticises that Rwanda is foregoing about a quarter of its potential revenue each year in tax incentives from businesses alone, and 14% of its potential budget. S. Musana also argues that there are factors other than incentives that attract investors to Rwanda such as security, zero tolerance for corruption, transparency, economic environment, technology, etc. For more details, see S. Musana, “The Impact of Tax Incentives – The Rwandan experience: Key Findings, Highlights of Successes and Challenges, and Recommendations”, in M. Mukuna, *Report on the Regional Policy Round Table: Harmful Tax Competition in East Africa: A Race to the Bottom?*, TJN – Africa, July 2011, p. 9.
121 For instance, talking to the New Times about the expected introduction of the law on gaming and betting taxes, P. Brazoua, the CEO of RGC (Rwanda Gaming Corporation) said that the lack of regulatory laws has significantly slowed down the progress of the industry since its introduction in 2004 and added that he is optimistic that the profitability of the industry in the short run, as well as its professional management, will become more beneficial to the economy once the regulatory and taxation law are effective. He also revealed that RGC has contacted foreign investors who agreed to inject US$ 20 million in the business but once the laws are in
the major investment determinants for any country worldwide. In the same vein, the legal regime in general as well as tax legislation in particular influence much a country’s economy and contribute much to its economic development.


However, the use of tax incentives to attract investors and lead to economic growth constitutes a complex idea considering the way of doing business in the today’s world. In this regard, J. Li and D. Sandler affirm that international trade and investments are no longer the playground of a select group of large multinational corporations and wealthy individuals, considering that in today’s global economy, many SMEs engage in cross-border business, and international investment is now available even to small investors.\footnote{J. Li and D. Sandler, “The Relationship between Domestic Anti-Avoidance Legislation and Tax Treaties”, Canadian Tax Journal, vol. 45, n° 5, 1997, p. 894, available at http://www.ctf.ca/ctfweb/Documents/PDF/1997ctj/1997CTJ5_Li.pdf, accessed on 22nd August 2011.} At this point, one cannot forget that a traditional rationale for investment incentives is to encourage capital investment, and the designers of tax incentives around the world have believed that they can induce investors to place, laws becoming like a pre-condition. For more details, see I. R. Mugisha, “Government to Introduce Gaming Tax and Law”, The New Times, n° 2455, Kigali, Tuesday, 14th June 2011, p. 14.
follow directions favoured by the government, which in turn are assumed to ensure wider benefits for the overall economy.\(^{127}\)

In addition, investors often emphasize the relative importance of the tax system in investment decision if compared with other considerations such as political and economic stability, availability of social infrastructure, security of life and property and the general cost of doing business and so on.\(^{128}\) This is the reason why in most cases the governments use taxes [through tax policies] to stimulate their economies.\(^{129}\) For instance, in DRC, the mining sector has been reformed to attract more investors through offering different advantages in customs and taxation.\(^{130}\) In some cases, tax incentives may also be seen as a counterweight to the investments disincentives inherent in the general tax system.\(^{131}\)

According to C. Duanjie, capital investments grow once investors take advantage of new incentives as they become available across the economy, and the collection of company income tax can be expected to grow steadily.\(^{132}\) This is because tax incentives induce firms to invest more in an economy and a tax system can hold an effect on the finance of the firms by affecting investor decisions.

Albeit, some authors argue that taxes can only have impact on investment and economic growth if other investment determinants are also developed. In their studies, J. Morisset and N. Pirmia have found that taxes can have a significant impact on foreign investments flow if other factors like political and economic stability, infrastructure and transport costs are the same.\(^{133}\) This means that taxes alone cannot have a significant impact even if they play an

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\(^{127}\) C. Duanjie, *op. cit.*, p. 5.
\(^{130}\) A. K. Sumaili, “Legal Protection of Foreign Investors by the New Mining Code of the DRC: Case of the Mining Centre of Kamituga”, *African Law Study Library*, vol. 3, Nairobi, p. 33. According to this author, DRC, despite its richness in natural resources, the mining sector has risked to total collapse and been regarded as of less value to national life simply due to unhealthy political climate and judicial laws that were neither investors friendly nor offering incentives. However, with a fervent need to attract and retain investors in the country, the DRC Government has undertaken a series of reforms. As a matter of example, the mining sector has been reformed to attract more investors through offering different advantages in customs and taxation, like exportation of samples destined for analysis and industrial trials exempted from any customs duty whatsoever, or any other form of taxation whatsoever, household effects belonging to mining expatriate personnel imported tax free, temporarily duty free importation for a period of up to 18 months, etc.
\(^{132}\) C. Duanjie, *op. cit.*, p. 4.
important role in investment attraction and economic growth. Consequently, if other factors are already favourably set, the use of tax incentives can play an effective role in attracting investments.

II.2. Justifications of tax incentives to Rwanda

Worldwide, in the view of increasing productivity growth as well as recognising the importance of innovation in all aspects of business to enable productivity gains and increased market shares, policy makers continually review their tax rules to ensure that they are internationally competitive.\textsuperscript{134} W. S. Clark affirms that the ability to offer a tax system that attracts foreign capital is viewed as a critical component of a national strategy to secure high standards of living, giving an example of multinational enterprises (MNEs) that generate higher than average profits, invest significantly in research and development and offer well-paying employment opportunities.\textsuperscript{135}

Today, the world is becoming more globalised and resources are becoming more internationally mobile. Consequently, the issue of tax competition\textsuperscript{136} has taken a centre stage of debates surrounding national tax systems.\textsuperscript{137} Thus, Rwanda would not stay out of the competition but should rather stand up to revise its tax system, so that it becomes more competitive than it is today. There exist a number of reasons that justify why Rwanda can use tax incentives to attract investors. Methodologically, these reasons are hereunder divided into the reasons pertaining to natural and geographic position of Rwanda in the region on one hand and socio-economic reasons on the other hand.

II.2.1. Natural and geographic position reasons

Rwanda is a landlocked country situated in the East African region, bordering with Burundi in the southern, Tanzania in east, Uganda in north and DRC in west. The majority of Rwanda’s trade goods pass through Kenya ports and to a little extent through Tanzania ports. Among the six countries\textsuperscript{138} of its region, Rwanda is the smallest and landlocked with a long distance to ports. This geographical position constitutes a big challenge to Rwanda in matter of business,

\textsuperscript{134} W. S. Clark, \textit{op. cit.}, p. 1140.
\textsuperscript{135} \textit{Ibidem}.
\textsuperscript{136} According to literature surveys by Wilson (1999) and Fuest, Huber and Mintz (2005), cited by A. Klemm, \textit{op. cit.}, p. 7, tax competition refers to a process in which countries attempt to attract capital or taxable profits, by reducing taxes on capital.
\textsuperscript{138} Reference is made to Rwanda, four neighbouring countries plus Kenya.
international trade and economic development. This has been also affirmed by S. Musana, according to who, Rwanda’s geographical position constitutes one of the main challenges in the area of taxation in particular and on country’s development in general. In the region, Rwanda also has less natural potentials compared to its neighbours. For instance, DRC in the west is worldwide known for its natural resources. Tanzania in east is also wealthy in free land, the same for Uganda in north. Kenya on its side gets much benefit of coasting the Indian Ocean, and most of the goods coming in or getting out the East African region pass through its ports.

In fact, Rwanda doesn’t have many natural resources, which can compete regionally as its comparative advantage. The comparative advantage is a theory developed by Adam Smith and extended by David Ricardo according to which, the thrust of comparative advantage in political economy is that a country that exploits its comparative advantage enhances the likelihood that it will benefit from participating in the global economy.

Today, Rwanda has managed to put in place different initiatives, which favours investment and it’s time to adjust existing tax incentives as well as to add the modern ones. The World Bank (WB) and International Finance Corporation (IFC) Report of 2011 on doing business reports examples of such initiatives and improvements, like dealing with construction permits made easier, enhanced access to credit by allowing borrowers the right to inspect their own credit report and mandating that loans of all sizes be reported to the Credit Reference Bureau, the reduced number of trade documents required as well as enhanced joint border management procedures with neighbours, leading to an improvement in the trade logistics environment.

All those artificial improvements are intended to overcome the weakness in natural resources, and there is a need to put in place modern tax incentives for the sake of an effective improved investment attraction. At this point, it should be noted for instance, that in marketing the Kigali Free Trade Zone, the government of Rwanda emphasizes that this comes as a way to

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139 S. Musana, “The Impact of Tax Incentives – The Rwandan experience: Key Findings, Highlights of Successes and Challenges, and Recommendations”, in M. Mukuna, Report on the Regional Policy Round Table: Harmful Tax Competition in East Africa: A Race to the Bottom?, TJN – Africa, July 2011, p. 8. Other cited challenges are the poverty level (this author mentions that 57% of the population falls under the poverty line), few skilled workers and the preference of investors to locate in urban rather than rural areas.


141 World Bank & International Finance Corporation, Doing Business 2011, Washington, 2011, p. 141. Among other improvements recorded by the WB & IFC include but are not limited to implementation of 22 business regulation reforms and strengthened investor protections. For details, see at p. 6.
have access to a large market accessible from the location that is not easily served by other trade routes in the region.142

II.2.2. Socio-economic reasons

Rwanda needs to set up modern tax incentives to attract investments and change the face of its economic sectors. The country is currently facing underemployment in the rural economy where land tenure is becoming too fragmented for efficient agricultural production and innovation.143 Rwanda is also facing limited opportunities for employment in urban areas where there has been slow development of labour-intensive manufacturing activities.144 With sufficient FDI and greater education of the labour force145, a modernised tax regime in Rwanda might also add to the country’s existing potentials for higher economic welfare and growth by taking advantage of the country’s strategic position at the geographic and linguistic crossroads between Anglophone East Africa and Francophone Central Africa, to serve as a regional entrepot centre for not only merchandise trade but also trade in services, including tourism and information and communications technology (ICT) related services.146

Modern tax incentives may also help Rwanda to adapt itself in a global competitive world, to globalization and capitalist economic competition, especially in terms of manufacturing trends. Stressing the current global character of manufacturing, P. Dicken notes that “Competitive bidding via overseas promotional agencies and investment incentives has become endemic throughout the world … The important point about such international (and inter-regional) competition is that for certain types of investment it is truly global in extent. For the cost-oriented transnational investments … countries and localities in Europe and North America may well be in direct competition with locations in Asia and Latin America”147. And, J. Peck considers the increased competition between states for foreign investments as an aspect only of the reinforcement of the competition between localities at all levels (international, regional, national and local), which is the ultimate spatial consequence of the victory of neo-liberalism.148

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142 P. Abbott (dir), op. cit., p. 13.
144 Ibidem.
147 P. Dicken, op. cit., p. 98.
Still on socio-economic side, up to now, Rwanda’s exports are highly concentrated on traditional agricultural commodities, chiefly coffee, tea, pyrethrum, and hides and skins.¹⁴⁹ In contrast, Rwanda’s imports span a wide variety of products, especially manufactures, reflecting the paucity of manufacturing activity in Rwanda outside of the coffee, tea, beverages and tobacco industries.¹⁵⁰ Also notably, the country’s total import bill exceeds its aggregate export earnings by a wide margin, sustained by generous foreign aid inflows.¹⁵¹ At this level, D. A. De Rosa & V. O. Roningen affirms that, if Rwanda’s future imports are to stay at their current level, Rwanda must look increasingly to financing its import bill through either greater export earnings or greater inflows of FDI.¹⁵² In our view, one of the most leading ways to achieve this is to attract investments through systematic tax incentives, more exactly the creation of special economic zones.

By the same token, it is argued that FDI location decisions are influenced by the characteristics of host countries, such as endowment of natural resources and labour, level of economic development, macroeconomic and political conditions as well as tax incentives policy.¹⁵³ In this way, countries that lack appropriate economic conditions such as natural resources, infrastructures, and modern technology often offer generous incentives to compensate those weaknesses.¹⁵⁴ Talking to a journalist of Radio Salus at the time of presenting the Africa Competitiveness Report 2011 at Kigali, P. Ondiege, the Chief Research Economist in the Development Research Department of the African Development Bank, stressed that investors attach more importance to taxes, reason why Rwanda needs to put in place a tax regime, which is more favourable to investors to attract them.¹⁵⁵ However, even though L. Rugwabiza, an officer in the Ministry of trade and industry, agrees that investors attach more importance to taxes, he said that the tax regime in Rwanda is favourable to investors and fits to attract them.¹⁵⁶

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¹⁵⁰ Ibidem.
¹⁵¹ Ibidem.
¹⁵² Ibidem.
¹⁵³ Q. Li, op. cit., p. 63.
¹⁵⁴ Ibidem, pp. 63-64.
¹⁵⁵ P. Ondiege, Chief Research Economist, Development Research Department, African Development Bank, during an interview with B. Nzabagerageza, Radio Salus journalist, news, on 10th August 2011 at 20h17.
¹⁵⁶ L. Rugwabiza, MINICOM, in an interview with B. Nzabagerageza, Radio Salus journalist, news, on 10th August 2011 at 20h17.
In our view, the tax regime in Rwanda does not much favour investors since it doesn’t really offer many incentives to them. In this regard, we refer to the survey conducted jointly by the World Economic Forum, World Bank and African Development Bank, whose results stressed tax regime as one of the most impediments to investments in Rwanda. During this survey, from a list of 15 factors, respondents were asked to select the five most problematic for doing business in Rwanda and to rank them between 1 (most problematic) and 5 (last problematic). As a result, tax regulations came at the second place and scored 15.1% and tax rates came at the third place with 13.9%. These results show to what extent tax regime in Rwanda constitutes a huge impediment to investment. Thus, bearing in mind that significant factors that influence business location are public services, such as infrastructure and education, and the overall tax system, as affirmed by J. M. Mintz, a retouch of Rwanda’s tax legal system through a sound tax incentives offer, may welcome more investors than it does now.

II.3. Fitness of tax incentives to Rwanda: SWOT analysis

In today’s globalized world, a country’s trade performance and export sophistication and diversification are critical indicators of its competitiveness and are drivers of economic performance. For competitiveness, to properly work out, a country, especially developing country must attract as many as possible investors, both from national to multinational corporations. And it has been emphasized that the cost of inputs (labour, capital, materials, and energy), the quality of physical infrastructure, and the tax system are critical in determining a country’s competitiveness in the global export markets for simple manufacturers.

Presently, Rwanda has a number of potentials that already attract investors. An important element to bear in mind is that a sustainable investments attraction is a result of combined factors, including a good taxation system. For instance, in Ireland, this country’s economic miracle has long been admired by many developing countries and this miracle is attributable to a combination of factors in addition to the country’s efficient tax system, such as its access

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157 World Economic Forum, World Bank and African Development Bank, *The Africa Competitiveness Report 2011*, Geneva, 2011, p. 176. Other mentioned problematic are the access to financing as the first with 24.9%, inadequate supply of infrastructure as the fourth with 10.9%, inadequately educated workforce as fifth with 9.6%, poor work ethic in national labour force as the sixth with 7.2%, inefficient government bureaucracy as the seventh with 4.7%, policy instability as the eighth with 4.5%, inflation as ninth with 3.6%, foreign currency regulations as tenth with 2.1%, poor public health as eleventh with 2.1%, corruption as twelfth with 0.6%, crime and theft as thirteenth with 0.4%, restrictive labour regulations as fourteenth with 0.2% and the government instability/coups came last and scored 0.0%.


to the large European market, investments in education, and its ability as an English speaking
country to attract foreign investment. Among all those elements, the tax system has been shown to constitute an overall positive component of the Irish success story.

Rwanda policy makers, like other African policy makers, might perceive the effects of basing the economy on the export of manufactured goods as fundamentally different from basing it on the export of raw materials. The historical justification for such a belief might of course be the experiences of Western countries that grew rich by exporting manufactured goods and more lately, the experience of the Asian tigers that inspired many developing countries to repeat their success at export-oriented industrialization. The better way to proceed to this economy is to increase the number and the volume of FDI, which can mainly be done through tax incentives.

To better assess the fitness of tax incentives to Rwanda, one may regard this using the SWOT system, i.e. highlighting the strengths and the weaknesses (which are internal factors), and the opportunities and the threats (which are external factors).

II.3.1. Strengths and weaknesses

On one side, Rwanda has a number of positive factors that can be relied on to attract investors through modern tax incentives. According to A. Aggarwal, tax incentive zones’ performance in attracting investment and promoting export competitiveness relies on a number of sets of determinants including but not limited to the location, quality of infrastructure facilities, quality of governance and incentive package. With regard to these five determinants, Rwanda is in good position to have highly performing tax incentive zones, capable to attract

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160 Idem, p. xiii.
161 C. Duanjie, op.cit., p. 27.
162 Ibidem.
164 A. Aggarwal, Performance of Export Processing Zones: A Comparative Analysis of India, Sri Lanka and Bangladesh, New Delhi, ICRIER, 2005, p. 58. In this regard, the same author explains the five sets of determinants as follows: region specific location factors as the developments of the region in which zone is located and industrial culture in the region; strategic specific location factors with regard to proximity of the zone to ports and airports, and proximity to a bigger city; country specific location factors with regard to development of the country, labour cost, availability of raw materials and policy regime; quality of infrastructure including physical infrastructure within the zone like water, electricity, warehousing, transport, telecommunication, police station, fire station and banks, physical infrastructure external to the zone like transport facilities for the zones, roads leading to the zones and port facilities, social infrastructure like residential complexes, schools, hospitals and recreation facilities; quality of governance as to a streamlined, prompt and efficient bureaucracy and custom controls in all stages of the creation and running of an EPZ crucial to its performance plus a clear and transparent legal and regulatory structure and an unfettered and stable policy framework to ensure the success of the zones;
investors. At this point, one can mention efforts of the GoR to ensure the rule of law, improvement of both soft and physical business infrastructures, fast track approvals for all administrative procedures, the institutional support provided by the Rwanda Development Board, plus the cumulative impact of the right macro-economic environment and the micro business environment that already exist in Rwanda, as well as other elements that reduce the cost of doing business in Rwanda.

In addition to these, there exist a number of other internal factors that once combined with tax incentives may attract more investors. Examples of such strengths include but are not limited to the good governance system, the low rate of corruption and zero tolerance to corruption policy, as well as the high level of strengthened tight security that is found in Rwanda, compared to its neighbouring countries.\textsuperscript{165} The political stability is also another strength that Rwanda may rely on to attract investments. Talking about non-tax determinants of FDI, W. S. Clark affirms that case studies tend to emphasize the importance of political stability and stability in the macroeconomic environment as critical components of a successful framework to encourage FDI.\textsuperscript{166} One can also mention good infrastructure with regard to the reliability of communication systems, water, electricity and financial services offered to the business community, including the recent creation of a stock exchange market, secured and clean environment, as well as relative good medical services and education, etc. All those elements once combined with tax incentives may constitute a solid base on which investors attraction in Rwanda can be relied on.

On the other side, there exist also some internal factors, which can be considered as weaknesses to the use of tax incentives to attract investors in Rwanda. This is because although the tax incentives constitute a key element towards a country’s economic development, this may not properly happen if not supported by some other natural, political zone specific characteristics like the size, the concentration of economic activities as well as the capital intensity of the zone.

\textsuperscript{165} Interview with Azhar Iqbar, the Managing Director of Chatha Motors, Kigali, on 02\textsuperscript{nd} August 2011.

\textsuperscript{166} W. S. Clark, \textit{op. cit.}, p. 1141. According to this author, political instability or the threat of political instability can be the single largest deterrent to FDI, since it renders all areas of public policy uncertain, as in the macroeconomic context, instability in exchange rates and price levels also increases uncertainty and the perceived risk of FDI, tending to discourage investment flows. Other important factors mentioned by this author are the legal and regulatory framework (FDI can be inhibited if commercial and other laws and regulations are incompatible with the operation of foreign-owned companies. Important areas include the protection of intellectual property rights, the ability to repatriate profits, and a free market for currency exchange. It is important that rules and related administrative procedures be transparent to minimize uncertainties in business planning), access to inputs and infrastructure, the size of the market (FDI are encouraged by the existence of a
and socio-economic features. For instance, according to the World Bank, the success of the Export Processing Zones (EPZ) program in Mauritius is attributable to Mauritius’ most valuable economic resources: its literate labour force, as educational levels were much higher than in other developing countries and the availability of semi-skilled cheap workers, which attracted both foreign and domestic investments into the EPZ program.\textsuperscript{167} Thus, the use of tax incentives to attract investment in Rwanda can be weakened by the insufficiency of natural resources to compensate revenues from exempted taxes as well as the low percentage of skilled labour and technicians.

II.3.2. Opportunities and threats

On one side, Rwanda has many opportunities that are helpful to investment attraction through tax incentives. Some of the Rwanda’s main opportunities to better attract foreign investors once tax incentives are strengthened are the membership into various regional integrations like EAC and COMESA, as well as the good partnership and cooperation that Rwanda has established with foreign countries, both on political and trade matters. These constitute an important advantage, considering the benefits that a regional integration brings to its members.\textsuperscript{168}

On the other side, some other external factors may also constitute a threat to the use of tax incentives as a mean to attract investors in Rwanda. One of the major threats can be the reliance of a large party of the budget to foreign donors and lenders.\textsuperscript{169} In fact, Rwanda, like many other developing countries, relies much on western countries and international organisations like the World Bank, IMF and WTO. These institutions may then refrain and challenge Rwanda from using tax incentives as properly fits.\textsuperscript{170} For instance, the exemption large potential market where consumer demand for certain goods has been largely unfilled to date) as well as transparency of the tax law and administrative certainty.


\textsuperscript{168} For example, cross-border movements from one country to another within the EAC have increased since the creation of this Community, the existing project to create one tourist visa in EAC members, the harmonization of education and communication policies, etc. All those socio-economic and political aspects of regional integration have an impact on investments attraction, once combined with tax incentives.

\textsuperscript{169} Taking an example of 2011/12 budget, the total domestic revenue collections have been projected at 529.4 billion Rwf, equivalent to 49.8\% contribution to total expenditure, which means that the remaining 50.2\% is expected to come from grants and lending. For more details, see KPMG, “Budget Brief Rwanda 2011”, available at www.kpmg.com/eastafrica, accessed on 24\textsuperscript{th} August 2011.

from import duties on goods in SEZs may constitute a prohibited export subsidy within the meaning of art. 3.1(a) of the Uruguay Round Agreement on Subsidies and Countervailing Measures.

Grossomodo, in the context of balancing the role of tax incentives with regard to investment attraction, A. Aggarwal asked the sampled firms how important it is to offer fiscal incentives for attracting investment and the result of his survey showed that, contrary to the expectations, fiscal incentives are considered very important in determining the attractiveness of the zones. Thus, with regard to the above SWOT analysis of the fitness of tax incentives to Rwanda, Rwanda will be right to use systematic tax incentives and then extend it as a comparative advantage in international trade. In other words, Rwanda should set up competitive tax incentives and exploit them as its comparative advantage in the region. However, the choice of tax incentives to be set must well be carefully studied bearing in mind that a bad choice of tax incentives lead to failures, and consequently, disadvantages become higher than advantages. Thus, attention should be paid to some principles, and adjusted according to the realities of the country.

II.4. Principles for choosing and running tax incentives

The issue of choosing which tax incentive is appropriate for a given situation is very crucial. This is because tax incentives do not always bring advantages to the country’s economy and development. In some cases, tax incentives may have negative effects and in some countries, they have failed in one way another. Although empirical research on tax incentives shows that they sometimes work in attracting FDI but remains unclear whether they are beneficial overall, a brief overview of the empirical literature suggests that incentives work only if certain pre-conditions are met, and provided the correct design is chosen. However, it should be absolutely erroneous to affirm that all tax incentives lead to negative effects for a given country.

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that free zones can likely and easily breach the WTO rules especially the provisions of Agreement on Subsidies and Countervailing Measures (SCM) of WTO.

171 90% of the respondents in India and Sri Lanka and 100% in Bangladesh regarded tax benefits much more important than subsidies or grants and 63% of the respondents found subsidies also very important in attracting investment in the zones. For more details, see A. Aggarwal, op. cit., p. 28 and 69.

Conclusively, taxation experts argue that tax incentives need to be purposively well designed, implemented and monitored.\footnote{Easson and Zolt, 2010, cited in P. Abbott (dir), *op. cit.*, p. 10.} Thus, the most relevant and skilled task consists in choosing which tax incentive to adopt, in other words which tax incentive among others fits for a given situation considering its particularities. Hence, the choice of tax incentive must be principled if the policy maker wants to avoid errors and mistakes, which may lead the country to unexpected results. Some of the guiding principles while choosing tax incentive are common for the good general tax policy while others are more particular to tax incentives.

**II.4.1. Principle of transparency**

One of the guiding principles for choosing tax incentive common for good general tax policy is the transparency. This principle is important because investors need to be able to understand incentive schemes if they are to base their investment decisions on them and reduces the scope for corruption.\footnote{Idem, pp. 12-13.} To be deemed transparent, a tax regime’s administration must satisfy some conditions. For instance, (a) the tax administration must clearly set forth the conditions of applicability to taxpayers, and (b) details of the regime including any application thereof in the case of a particular taxpayer, must be available.\footnote{EAC, *Development of an EAC Model Agreement for the Avoidance of Double Taxation and an EAC Code of Conduct against Harmful Tax Competition*, Final Report, 2010, p. 13.}

The principle of transparency goes together with the principle of accountability. In the views of D. Brunori, the costs and benefits of fiscal decisions, especially those that afford special treatment to particular taxpayers, should be understood by the electorate as well as tax administrators; and if a tax policy is used to promote specific behaviour (such as economic development) it is essential that the policy be evaluated in terms of whether it meets its intended goal.\footnote{D. Brunori, *op. cit.*, p. 53.} Accountability of government to citizens is also essential in the sense that taxation encourages citizens to make claims on governments and hold them accountable for public expenditure.\footnote{D. Brautigam, “Taxation and Governance in Africa: Take a Second Look” in *American Enterprise for Public Policy Research*, 2008, n° 1, W. Prichard, *Taxation and State Building: Towards a Governance Focused Tax Reform Agenda*, Institute of Development Studies Working Paper n° 341, Sussex, University of Sussex, 2010 and H. Peterson (ed), *Tax Systems and Tax Harmonization in the East African Community: Report for GTZ and the General Secretariat of the EAC on Tax Harmonisation and Regional Integration*, Potsdam, University of Potsdam, cited in P. Abbott (dir), *op. cit.*, p. 39.} Briefly, with this principle of accountability, a tax policy in a democratic society should be arrived at openly and transparently.
For the sake of transparency and accountability, importance must also be attached to the legality of tax incentives. In Rwanda, strict observance must be given to art. 81 of the Constitution of the Republic of Rwanda according to which no taxation can be imposed, modified or suppressed except by law and no exemption from or reduction of tax may be granted unless authorised by law.\textsuperscript{178} In the same sense, article 79 of the same Constitution also reads that every year the Chamber of deputies has to adopt the finance law, i.e. the budget, and before the final adoption of the budget, the President of the Chamber of Deputies seeks the opinion of the Senate.

**II.4.2. Principle of predictability**

Another principle that may guide the choice of tax incentives is the predictability. In fact, investors need to be able to rely on a certain stability of tax incentives granted, before engaging in a major investment and one can understand how a project requiring repeat investment over the years would be discouraged by frequent tax changes, even if incentives granted on previous investment were grandfathered.\textsuperscript{179} This principle of predictability stands as a complement to the principle of certainty. Certainty requires that the number and types of tax changes be kept to a minimum and taxpayers should not be subject to frequent changes in rates or bases.\textsuperscript{180}

The predictability and/or stability are considered as the most powerful set of incentives, since once an investor is assured that the environment will not change to adversely affect him, he may easily be convinced to invest in that environment\textsuperscript{181}. This is because frequent changes interfere with economic choices as well as long-term financial planning.

**II.4.3. Other principles**

Apart from the above mentioned principles, another related principle is that tax incentives should be automatic rather than discretionary. A. Klemm argues: “in the hypothetical case of an impartial, incorruptible, predictable and omniscient public service, discretionary incentives would be preferable, as these would ensure that limited resources are focused on investments that would not have taken place otherwise and which entail the highest possible social return. However, in more realistic settings, continues the same author, there are strong reasons for

\textsuperscript{178} Art. 81 of the Constitution of the Republic of Rwanda of 04\textsuperscript{th} June 2003 as amended to date, in \textit{O.G.} n° special of 04\textsuperscript{th} June 2003.

\textsuperscript{179} A. Klemm, \textit{op. cit.}, p. 12.

\textsuperscript{180} D. Brunori, \textit{op. cit.}, p. 53.

\textsuperscript{181} R. Haywood, \textit{op. cit.}, p. 17.
automatic incentives, based on clearly defined criteria, reflecting both the risk of corruption and the difficulty governments have in picking winners”. To these principles, one may add that provisions providing for tax incentives should also be robust to tax evasion; otherwise, if they open new routes for evasion, then their costs will increase enormously. In the same line, the provisions providing for tax incentives should be robust not only to avoid tax evasion, but also tax avoidance, considering that this leads almost to the similar economic and financial effects with the first.

II.5. Drivers of tax incentives in Rwanda: the present and future perspectives

The present driver of tax incentives in Rwanda mainly lies in the promotion of investment with a perspective of economic growth and development. In fact, the taxation policy in Rwanda is presently focused on widening the tax base to increase fiscal revenues especially focusing on registering the informal sector, simplifying tax procedures and encouraging both FDI and domestic investments. In this regard, tax incentives constitute a part of a basket of measures to attract investments, with a target of encouraging private sector growth and development of a knowledge-based economy.

Different studies showed that tax incentives apparently do have some role to play and if appropriately utilised, they can make a difference, especially in countries having good political economy with transparency and less corruption, as is the case of Rwanda. Unfortunately, a number of international agencies have recommended that the GoR review the existing tax incentives and/or simply eliminate them, qualifying such incentives as harmful to the Rwandan economy in general and highly distorting the government revenues and investments in particular. Reports on the tax regime in Rwanda have also recommended that the policy of granting tax incentives be reviewed and have clearly developed a need to determine which tax incentives are harmful and which are effective and necessary.

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183 P. Abbott (dir), op. cit., p. 17.
184 S. Musana, op. cit., p. 8.
185 For instance, the IMF Report of 2007 argued that Rwanda would do better in tax revenue generation if it did not have in place the tax incentives and exemptions introduced in 2005 and found them to be counterproductive or ineffective because they distort the investment climate, and what Rwanda fails to tax may be taxed in the investors domicile; UNCTAD in 2006 recommended a review of the policy arguing that the government needed to develop a clear vision as to how fiscal incentives could achieve the national development goal, and that the tax incentives be made to all investors irrespective of size of investment as Rwanda was more likely to attract SMES; the FIAS also in 2006 recommended the GoR to review and eliminate as many fiscal incentives as possible and ensure that any that remains is not overly generous. For more details, see P. Abbott (dir), op. cit., p. 20-21.
186 P. Abbott (dir), op. cit., p. 10. As mentioned by this author, such reports are for instance the African Development Bank Group, Domestic Resource Mobilisation for Poverty Reduction in East Africa: Rwanda Case Study, Regional Department East Africa, 2010 and H. Petersen (ed.) et al., Tax Systems and Tax Harmonisation
Even though some authors recognise that Rwanda’s existing complex system of tax incentives has contributed to a significant increase in private sector investment, which resulted in the creation of new jobs, increase in exports especially into areas prioritised by the government\textsuperscript{187}, we don’t find the existing system effective enough especially if one takes into consideration critics from different analysts like the loss of some revenues by the Government as well as the continuing dependence on foreign grants and aids.

Pursuant to that, there is a need to reform the existing tax incentives system and adopt the new modern ones oriented to effective investments attraction and export promotion. At this point, we strongly support the idea of the 2010 Development Driven Trade Policy Framework prepared by the UNCTAD and the Ministry of Trade and Industry according to which tax reductions/exemptions in terms of tariffs should promote the inflow of industrial inputs and that consideration should be given to more strategically located export processing zones with more effective incentives provided.\textsuperscript{188} It is in this regard that we appreciate the efforts of the GoR for adopting a new law regulating special economic zones in Rwanda.\textsuperscript{189} The following chapter deals with special economic zones recently introduced in Rwanda, as a new undertake of the GoR to boost the nation’s economic growth and development.

**Summary of the second chapter**

There is a close relationship between tax incentives, investments and economic growth, in the sense that tax incentives influence investments flow and these lead to economic growth. Taking into account the natural and geographic position of Rwanda, as well as other socio-economic aspects pertaining to Rwanda, there is much need for Rwanda to strategically use tax system to attract more investments in Rwanda. The balance between advantages and disadvantages that Rwanda may get in using modernised tax incentives also shows that advantages are higher than disadvantages. However, the major concern in using tax incentives to attract investment is the choice of appropriate tax incentive. In this regard, a number of principles matters a lot like the principle of predictability, the principle of transparency and accountability and so on.

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\textsuperscript{187} P. Abbott (dir), *op. cit.*

\textsuperscript{188} Idem, p. 16.

\textsuperscript{189} That is the law no 05/2011 of 21/03/2011 regulating special economic zones in Rwanda, in O. G. no special of 30 March 2011, hereinafter referred to as SEZ law.
CHAPTER III. UNDERTAKING A NEW AREA OF TAX INCENTIVES IN RWANDA: SPECIAL ECONOMIC ZONES (SEZs)

Tax incentives are granted for a wide variety of reasons and they are seen as a central element of the Government’s policy of providing a competitive environment for economic growth and poverty reduction. This thesis deals with tax incentives that promote economic growth and development and let aside such tax incentives that are used for other motives like social goals. With this consideration, one of the major purposes of tax incentives is to promote targeted economic activities and stand as a potential tool to develop the national economy of a given country. In this vein, creations of export-oriented zones have been promoted by international agencies such as the World Bank and UNIDO, and according to the World Bank, the establishment of economic zones is the easiest system to arrange for economies at an early stage of economic development with limited administrative capacity and can be an appropriate way to attract investments. This chapter describes Special Economic Zones (SEZs), newly established in Rwanda, as a modernized form of tax incentives appropriate to attract more investments in Rwanda and boost Rwanda’s development and economic growth.

III.1. Basic concept and functioning of Special Economic Zones in Rwanda

The creation of special economic zones in Rwanda constitutes one of the major new undertakings of the GoR. It is worthy to bear in mind that Rwanda is not the first country to

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establish SEZs on African continent as well as on other continents. Many African countries have created free zones in their respective territories in one model or another.

III.1.1. SEZs designation and description

The terms special economic zones, export processing zones, free trade zones, free zones, duty free zones, manufacturing zones, free export zones, have been widely used interchangeably to cover situations in which tariffs and other customs duties are suspended for consumption only, production only, or both production and consumption.\textsuperscript{192} Still in this sense, some use these terms as synonyms.\textsuperscript{193} However, some others make distinctions between these terms\textsuperscript{194} whereas others adopt the term “special economic zone” as a general expression that covers all the above mentioned components.\textsuperscript{195} According to D. Kamanzi, studies showed that there exist 23 terms referring to free zones\textsuperscript{196} and UNIDO has grouped them into five (5) rubrics basing on their main targets as follows:

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<thead>
<tr>
<th>Group I: Trade</th>
<th>Group II: Exports</th>
<th>Group III: Processing</th>
<th>Group IV: Economic activity</th>
<th>Group V: General</th>
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<tr>
<td>Customs zone</td>
<td>Duty-free export processing zone</td>
<td>Export processing free zone</td>
<td>Investment promotion zone</td>
<td>Free zone</td>
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<td>Customs free zone</td>
<td>Export free zone</td>
<td>Export processing zone</td>
<td>Joint enterprise zone</td>
<td>Free port</td>
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<td>Free trade zone</td>
<td>Export processing free zone</td>
<td>Free export processing zone</td>
<td>Technology zone</td>
<td>Maquiladora</td>
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<td>Tax free trade zone</td>
<td>Export processing zone</td>
<td>Free production zone</td>
<td>Special economic zone</td>
<td>Tax free zone</td>
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<td>Free export processing regime</td>
<td>Industrial processing zone</td>
<td>Zone of joint entrepreneurship</td>
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<td>Export processing regime</td>
<td>Industrial free zone</td>
<td>International service zone</td>
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This Thesis uses the term “Special Economic Zone” not in an absolute isolated way but rather in partial interchangeable sense with the above mentioned terms. Thus, we refer to S. Nishitateno, according to who, SEZs are interested in developing practically all items of

\textsuperscript{191} S. Endresen & LaRRI, \textit{op. cit.}, p. 25.
\textsuperscript{192} D. A. DeRosa & V. O. Roningen, \textit{op. cit.}, p. 1 at footnote 2.
\textsuperscript{193} M-C. Almeida, \textit{op. cit.}, p. 1.
\textsuperscript{196} UNCTC, \textit{The Challenge of Free Economic Zones in Central and Eastern Europe}, 1991, cited in D. Kamanzi, “De quel type de zone franche le Rwanda a-t-il besoin?”, \textit{Law Review}, National University of Rwanda, Faculty of Law, April 1999, n° 003, p. 60. Among the 23 terms, this author argues that the most known are Free ports, Free trade, Foreign Trade zones, Export processing zones, Export processing regime, Special economic zones and Free zones. For more details, see D. Kamanzi, \textit{Les aspects juridiques de l’instauration au Rwanda d’un régime de ZFIE}, Mémoire, Butare, UNR, Faculté de Droit, 1998, pp. 18-23.
industry, agriculture, livestock breeding, fish breeding and poultry farming, tourism, housing and construction, research and manufacture involving high technology and techniques and other trades of common interest to investors. We also consider C. Baissac according to who, SEZs include commercial free zones, free trade zones and free zones, EPZs, free enterprises or single factory/unit free zones & free ports. Afterwards, we consider that the main target of creating special economic zones is to economically develop Rwanda basing on its potential areas of investment as developed by RDB. This Thesis also stresses the argument of D. Kamanzi, who proposes SEZs as a form of free zones that better fits for Rwanda, and through which Rwanda can overcome some of its economic challenges like import substitution and export-based development.

With regard to the above mentioned variety of terminologies, different definitions of SEZs have been coined. S. Nishitateno defines SEZ as an area where enterprises are treated more preferentially than in other areas in relation to such matters as the tax rate and the scope of operations in order to attract foreign capital and advanced technology for modernisation. SEZs are also described as specifically designated geographical areas where economic and commercial policies are more liberal than in the rest of the country, with an aim of attracting more foreign investment. According to C. Baissac, despite the many variations in names and forms, reference made to the nomenclature of SEZs, these can be broadly defined as “demarcated geographic areas contained within a country’s national boundaries where the rules of business are different from those that prevail in the national territory, such differential

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199 According to RDB, priority investment sectors are infrastructure, agriculture, energy, tourism, ICT, real estate & construction, financial services, and mining. For more details, see RDB, *Investing in Rwanda - An Overview*, 2011, p. 11.

200 D. Kamanzi, “De quel type de zone franche le Rwanda a-t-il besoin?”, *op. cit.*, p. 60 and p. 64.


203 C. Baissac, explains the SEZ nomenclature as follows: Special refers to the differential regulatory regime that distinguishes the zone from the prevalent domestic economy; Economic refers to the broadest type of activities now allowed in zones, without prejudice regarding their nature and focus; Zone refers to the physically or legally bounded economic space contained in the domestic country. For more details, see C. Baissac, “Brief History of
rules principally dealing with investment conditions, international trade and customs, taxation, and the regulatory environment, whereby the zone is given a business environment that is intended to be more liberal from a policy perspective and more effective from an administrative perspective than that of the national territory.”

In front of these parsimonious definitions, we find SEZs as regulatory demarcated geographical business areas within a normal country’s borders, specifically designed to attract FDI in order to boost the country’s development and economic growth, through preferential treatment in terms of taxation and investment conditions.

II.1.2. Functioning of Special Economic Zones

A well developed and designed SEZ brings a variety of benefits to the establishing country like creation of new employment opportunities, attraction of FDI, stimulation of economic growth, transfer of new technologies, promotion of foreign exchange earnings, promotion of economic engines, etc. All these to successfully happen, some of the requirements consist in a well designed administration as well as a focused soft and hard infrastructure.

Presently, it is worldwide considered that SEZs have some importance with regard to economic development in the sense that: (1) SEZs have been the most potent and most successful vehicle for transporting FDI into developing countries and emerging market economies and (2) FDI rather than trade has become the most important vehicle for bringing goods and services to foreign markets and for integrating national production systems.

Thus, a successful SEZ requires a strategic and a well thought set up. Hence, the creation and management of SEZs in Rwanda requires the Government to guarantee a number of major concessions to investors in terms of investment mechanisms as well as guarantees and incentives. In this regard, the GoR must produce some efforts to lessen bureaucracy and make the initial phase of the investment period less cumbersome for SEZs investors. The

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SEZs and Overview of Policy Debates” in T. Farole (dir), Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience, Washington, IBRD, 2011, p. 27.

204 C. Baissac, op. cit., p. 23. This author also mentions that definitions of SEZs vary across countries and institutions, and evolve continuously as new types of zones are developed and older types disappear or are adapted, and suggests that any attempt at a comprehensive definition of SEZs must be sufficiently broad to encompass the bewildering array of past, present, and future zones, and yet sufficiently precise to exclude those that do not display the essential structural features that make a zone a zone.

Government must also subsidize sites for production, buildings and infrastructure such as roads, transportation, telecommunications as well as other facilities.\textsuperscript{206} Thus, even though SEZs development activities may be done by any person (developer), not necessarily and not preferably the Government, the GoR to successfully establish and run SEZs must, before granting incentives to SEZs users, first grant such incentives to SEZs developers and operators.

On the other side, even though SEZs investors benefit a wide range of incentives and advantages,\textsuperscript{207} some conditions are also imposed to companies operating in such areas in order to properly serve the role expected from them. It is in this sense that art. 28 of the SEZ law imposes licensed users to perform activities indicated in the license granted to them, commence activities within the timeline determined in the zone licensing regulation, and so on. Even though this law doesn’t impose the percentage of the goods that must be exported, art. 2.7 and more specifically art. 25 of the National Investment Code obligate SEZs investors to export at least 80\% of their productions. Globally, compared to some other African countries\textsuperscript{208} that impose heavy conditions to Zones investors, Rwanda is flexible with regard to conditions imposed on SEZs investors and this flexibility may stand as a comparative advantage to Rwanda’s special economic zones.

\textbf{III.2. Establishment and development of Special Economic Zones in Rwanda}

Globally, Special Economic Zones have existed a long time ago in the past but the initiative to establish them in Rwanda occurred in the end of the last 20\textsuperscript{th} century. For the moment, the development activities of SEZs in Rwanda have started with infrastructure development as well as institutional and regulatory framework drawings.

\textsuperscript{206} In terms of art. 2.15 of the SEZ law, an establishment and development of a zone or a part of a zone may be done by an individual or a legal entity, which holds a licence to that effect.

\textsuperscript{207} In most cases, investors in SEZs are exempted from customs duties on imports such as civil construction machinery and materials as well as on raw materials used for export goods, given generous tax exemptions especially during the period of recovery of investment expenditure, which period can last during a specified time period of years, and so on. For instance in Namibia, EPZ incentives include but are not limited to corporate tax holiday, exemption from import duties on imported intermediate and capital goods, exemption from sales tax, stamp and transfer duties on goods and services required for EPZ activities, reduction in foreign exchange controls, guarantee of free repatriation of capital and profits, permission for EPZ investors to hold foreign currency accounts locally, access to streamlined regulatory service (one stop shop), refund of up to 75\% of costs of pre-approved training of Namibian citizens. More details can be found in O. Ayoade, “Why Export Processing Zones?”, \textit{Namibian Business Journal}, 1997, vol. 7, n° 3, p. 14, available at http://www.larri.com.na/files/EPZ%20.pdf, accessed on 01\textsuperscript{st} August 2011.

\textsuperscript{208} For instance in Namibia, EPZs investors are required to export at least 85\% of their productions and no strikes or lock-outs are allowed in EPZs. For more details, see O. Ayoade, \textit{op. cit.}, p. 14.
III.2.1. Historical background of Special Economic Zones in Rwanda

From a global point of view, some scholars reveal that SEZs are not a new phenomenon at all in the world trading scene and argue that the existence of such systems could be dated back even to Roman times.\footnote{Kreida, 1975, pp. 43-44, cited in K. Y. Wong & D. K. Y. Chu, Geografiska Annaler. Series B, Human Geography, vol. 66, no 1, 1984, p. 1, available at http://www.jstor.org/pss/490524?query=zones%3Band%3BSpecial%3BECU%3BZones%3Band%3BSpecial%3BEconomic%3BZones%3Band%3Bgenerators%3D6ace%3D6f%3D6wc%3Don%2Bsearch%3Dyes, accessed on 06\textsuperscript{th} October 2011. See also C. Baissac, “Brief History of SEZs and Overview of Policy Debates” in T. Farole (dir), Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience, Washington, IBRD, 2011, p. 231.} For instance, apart from the Island of Delos in the Cyclades considered by many as the first approximation of a free zone in the sense that it provided free-trade-like conditions, between the 13\textsuperscript{th} and 17\textsuperscript{th} centuries, the Hanseatic League (an organisation of cities along the Baltic Sea) ran a series of monopoly trades along sea and land routes; and similarly, across Europe, cities were granted royal privileges and charters giving them monopolies in certain trades or freedom from certain prohibitions, taxes, duties, or excises.\footnote{K. Y. Wong & D. K. Y. Chu, op. cit., p. 31-32.} K. Y. Wong & D. K. Y. Chu affirm that from the 18\textsuperscript{th} century onwards, these commercial free trade zones have been established on the world’s major trade routes with the functions of trans-shipment, storage and the re-export of goods without customs formalities.\footnote{C. Baissac, op. cit., p. 1.} According to the World Bank estimates of 2007, there were more than 3,000 projects taking place in SEZs in 120 countries worldwide.\footnote{X., “Special Economic Zones as a Model for Economic Development of Backward Country”, available at http://www.globalrp.org/special-economic-zones-as-a-model-for-economic-development-of-backward-country.html, accessed on 07\textsuperscript{th} October 2011.}

In Rwanda, an idea of creating free zones in Rwanda started in the end of 1980 years when a delegation of the Ministry of Finance and Economy attended a meeting of the development of private sector in Africa and profited the opportunity to visit Mauritius free zones.\footnote{Ministère des Finances et de l’Économie, Réunion sous-régionale de haut niveau sur le développement du secteur privé en Afrique, Ile Maurice, du 20 au 22 Juillet 1988, Rapport de mission, p. 51.} From that meeting, Rwanda wanted to establish many free zones in Kigali capital city as well as in provincial cities like Butare and Gisenyi.\footnote{J. C. Klotchkoff, “Enquête, Zone franche: un franc succès”, Jeune Afrique Économie, n° 272 du 05 au 18 octobre 1998, p. 33.} Unfortunately, these initiatives have not survived the chaos of 1990 war, which ended in 1994 with Genocide against the Tutsi. The idea revived some years later, but run at a slow pace, and it is this year, 2011, that a law to that effect has been adopted. The adoption of the law regulating SEZs has been followed by the rapid
activities of SEZ development at Kigali. Before, the Zone was termed Kigali Free Trade Zone but thereafter it became Kigali Special Economic Zone.

However, even before the adoption of this specific law on SEZ, different other laws have tackled special economic zones in Rwanda in one way another, especially with the tax law reform of 2005. For instance, art. 86.15g of the VAT law exempts from VAT goods and services meant for free economic zone imported by persons with investment certificate. In the same sense, art. 41 parag. 3 of the Income Tax Law mentions that a registered entity that operates in a Free Trade Zone that fulfils the requirements stipulated in the Rwandan law on investment promotion is entitled to (1) pay corporate income tax at the rate of zero per cent, (2) exemption from withholding tax mentioned in art. 51 of the same law and (3) tax free repatriation of profit. On regional level, part XIV of the East African Community Customs Management Act of 2004 as amended up to 08th December 2008, to which Rwanda is part since 2007, deals with export processing zones and free ports in the Community.

Up to now, the first planned special economic zone is the Kigali Special Economic Zone (KSEZ), which is intended to provide a trade, logistics and service hub to serve the northern great lakes region including Rwanda itself, Burundi, western Uganda, western Tanzania and eastern DRC; and it will be open to distribution and manufacturing companies including those engaged in professional, financial and technical service in targeted industrial sectors like agro-

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215 That’s at Nyandungu, in the Sector of Ndera, Gasabo district, Kigali City. However, even before this law came into force, some development activities have already started and one may wonder on which legal basis the activities development was based on.

216 In an interview with the press, A. Ruzibuka, the Chairman of the taskforce that is tasked to implement the KSEZ project, said that the term “Kigali Free Trade Zone” would not be a good deal for Rwanda because it has a threshold requirement and therefore after different consultations with stakeholders and visiting other economic zones in the region, the GoR decided to change “Kigali Free Trade Zone” into “Kigali Special Economic Zone”, which will be more competitive with flexibility to accommodate different activities like ICT Park, trading facilities, free port and export processing zone. For more details, see G. Majyambere, “KFTZ named Kigali Special Economic Zone”, In2EastAfrica, Thursday October 07th 2010, available at http://in2eastafrica.net/kftz-named-kigali-special-economic-zone/, accessed on 09th October 2011. This is also reflected by art. 3 of the SEZs law stating the rationale for the establishment of Zones including increase of developed land, increasing infrastructure and increasing participation of private sector in development activities, promote a high-quality business, etc.

217 That is a withholding tax of 15% levied on the payments (made by resident individuals or resident entities including tax-exempt entities) like dividends except inter-company dividends, interests; royalties; service fees including management and technical service fees; performance payments made to an artist, a musician or a sportsperson irrespective of whether paid directly or through an entity that is not resident in Rwanda; lottery and other gambling proceeds and goods supplied by companies or physical persons not registered in tax administration.
processing, ICT/shared services, cold storage/horticulture, textiles/clothes, petroleum storage, dry goods warehousing, high value trading and crafts.\textsuperscript{218}

Conclusively, one may argue that the establishment of SEZs in Rwanda took a very long time. Even though this might be true, one cannot find it as a negative point considering that the successful establishment and run of SEZs requires much attention and scrutinised processes. In the views of FIAS\textsuperscript{219}, SEZs development experience suggest that the failure or success of a zone is highly linked to its policy and incentive framework as well as the way in which it is located, developed and managed.\textsuperscript{220} Even though it is still too early to predict anything about the success or failure of SEZs in Rwanda, the progress of KSEZ is up to now to an appreciable stage and has already produced remarkable results. For instance, up to now, the KSEZ has so far attracted over 28 investors, with 90\% of the first phase covering 100 hectares, already booked,\textsuperscript{221} which figures constitute a stone of much successful expectations.

According to the piecemeal information available on the infrastructure development of KSEZ\textsuperscript{222}, the basic infrastructure like ground-levelling, installation of water system, electricity, road network, fibre optic cables, etc. are now completed and some of the buildings are almost also completed. On 26\textsuperscript{th} September 2011, in an interview with The New Times, A. Ruzibuka, the Chairman of the Taskforce charged with KSEZ implementation revealed that 90\% of infrastructure development have completed and projected that by November 2011 the first phase will be complete.\textsuperscript{223}

\textsuperscript{218} P. Abbott, \textit{op. cit.}, p. 25. This Author also mentions that, during an interview with an Officer from RDB, in May 2011, it was revealed that at that time, KSEZ was proving difficulties to attract investors due the high cost of land.

\textsuperscript{219} FIAS is the multi-donor investment climate advisory service managed by IFC, MIGA and the World Bank (IBRD). It is an integrator of services to improve the business-enabling environment of member countries and in particular, FIAS advises governments of developing and transition countries on regulatory simplification, investment policy and promotion, and industry-specific investment climate issues.


\textsuperscript{221} \textit{Ibidem}. The Chairman also revealed that an investor who books a space at KSEZ pays 30\% of the total amount of the plot he/she purchases, and it is only allowed to purchase a minimum size of 5,000 square metres and the maximum size depends on the kind of business an investor wants to set up, i.e. an investor who want a large land needs to explain why he/she needs such much land. This is because they don’t want to end up with few investors but rather a vibrant area with a large number of activities, whereby investors will be sourcing raw materials to each other so that a synergy can be operational.

\textsuperscript{222} Such information are mainly based on the observation that we did during our field visit effected on 02\textsuperscript{nd} August 2011 on the site where KSEZ is being developed as well as to the informal interviews we had with constructors on the site.

\textsuperscript{223} X., “Rwanda: Investors Rush for Space at Kigali Special Economic Zone”, AllAfrica Global Media, 26\textsuperscript{th} September 2011, available at \url{http://allafrica.com/stories/201109261853.html}, accessed on 09\textsuperscript{th} October 2011.
III.2.2. Infrastructure development of Special Economic Zones in Rwanda

The success of special economic zones is critically linked to the way in which they are located, developed and managed. The law on SEZs doesn’t say anything about the location of a SEZ. It only mentions some of the criteria that are taken into consideration to establish a Zone.\textsuperscript{224} Still on the location of SEZ, the law allows any person to make recommendation for the establishment of a Zone but also stresses that the establishment of a Zone must be done in accordance with the master plan, otherwise, the intervention of a Prime Minister’s Order shall be required.\textsuperscript{225}

Contrary to some SEZs that have been implemented using fully public institutional structures (government operator and developer) or fully private institutional structures (private operators and developers), the development and management of special economic zones in Rwanda are done on private-public-partnership (PPP) basis.\textsuperscript{226} For instance, art. 17 of the SEZs law states that any person may be authorised to develop or operate a Zone if he/she is licensed under the law. In our view, we find this SEZs PPP development and management a very good initiative considering the benefits that PPP offers to the development and economic growth of the developing countries.\textsuperscript{227}

In light of the SEZs law, the development of a zone is subject to three stakeholders namely the developer, the operator and the user. The developer is an individual or a legal entity that holds a licence for establishing and developing a zone or a part of a zone.\textsuperscript{228} The operator is an individual or a legal entity that is licensed to operate a zone in accordance with the SEZ law and the terms of the Zone Operator agreement with SEZAR, whereas the term “User” refers to

\textsuperscript{224} In terms of art. 4 of the SEZ law, some of the main criteria for establishing a Zone include the following: to provide a conducive environment for the promotion of agro-industry, financial, tourist and recreational activities, green energy technology industry, residential buildings or any other type of economic development centre; to identify land dedicated to the above-mentioned activities; to develop such land by developing infrastructures and improving existing ones; and to provide investors with satisfactory, fast and effective services.

\textsuperscript{225} Art. 7 of the SEZ law.

\textsuperscript{226} The KSEZ project is a public-private partnership with the GoR as the major contributor of resources. In this project, the GoR owns 45% while the other partners have 55%. Apart from the GoR, other partners are the Rwanda Development Bank, the Rwanda Social Security Board (RSSB), insurance firm-SONARWA, Prime Holdings, MAGERWA and Bond Trading. For more details, see X., “Rwanda: Investors Rush for Space at Kigali Special Economic Zone”, AllAfrica Global Media, 26\textsuperscript{th} September 2011, available at http://allafrica.com/stories/201109261853.html, accessed on 09\textsuperscript{th} October 2011.

\textsuperscript{227} According to European Commission-Directorate General-Regional Policy, Guidelines for Successful Public-Private Partnerships, January 2003, at p. 6, PPPs present a number of recognised advantages for the public sector to exploit including the ability to raise additional finance in an environment of budgetary restrictions, make the best use of private sector operational efficiencies to reduce cost and increase quality to the public and the ability to speed up infrastructure development.

\textsuperscript{228} Art. 3.15 of the SEZ law.
an individual or a legal entity that is licensed to carry out activities in part or the entire Zone in accordance with SEZ law and the terms of an agreement with a Zone Operator and the SEZAR.\textsuperscript{229} Either all these stakeholders can be a public person or a private person since the law has not set any limitation.

**III.2.3. Incentives and facilities available to Special Economic Zones investors**

Under the law on SEZs, different incentives are granted to SEZs investors, mainly with regard to the rights over the land\textsuperscript{230}, customs exemptions\textsuperscript{231}, facilitation in obtaining visa and operating license as well as enjoyment of facilitating One Stop Centre.\textsuperscript{232} Investors in SEZs also enjoy a wide range of tax incentives as developed in the first chapter of this Thesis.\textsuperscript{233} Other preferential benefits in SEZs also include right to mortgage the land in SEZ,\textsuperscript{234} right to transfer the user license to another party subject to the approval of the SEZAR\textsuperscript{235} as well as a wide flexibility in labour management.\textsuperscript{236}

Worldwide, other major tax incentives that are offered to SEZs investors include but are not limited to tax holidays and tax amnesties. Tax holidays constitute a common form of tax incentive used primarily by developing countries to attract FDI.\textsuperscript{237} Under a tax holiday, qualifying newly established firms are not required to pay corporate income tax for a specified time period, in order to encourage investment\textsuperscript{238}, which time period varies depending on different elements taken into consideration.\textsuperscript{239} Thus, tax holidays refer to temporary

\textsuperscript{229} Art. 3.16 & 17 of the SEZ law.
\textsuperscript{230} In terms of art. 14, 15 and 24 of the SEZ law, a Zone developer and operator shall be entitled to leasehold right over the land in a Zone and a Zone operator may be entitled to lease or sub-lease all or any part of the land in a Zone on behalf of a Zone developer and this land may also be mortgaged. A zone developer or operator shall also be entitled to dispose the land of the area within the limits of the establishment decision, freely set prices for land and fees for service delivery in the area depending on invested capital and expected profits.
\textsuperscript{231} As provided for by art. 33 of the SEZ law, imported goods shall enter free trade zone areas free from customs duties, and may remain in storage in free trade zone areas for an amount of time as specified in the Zone regulations.
\textsuperscript{232} According to art. 32 of the SEZ law, every Zone shall have a One Stop Centre for the purpose of facilitating the operations of the developer, operator and user of the Zone.
\textsuperscript{233} SEZs investors enjoy the general tax incentives granted to all investors as well as specific tax incentives granted specifically to SEZs investors only.
\textsuperscript{234} Art. 15 of the SEZ law.
\textsuperscript{235} Art. 29 of the SEZ law. However, the transfer is subject to the approval by SEZAR.
\textsuperscript{236} Art. 37 of the SEZ law.
\textsuperscript{237} W. S. Clark, \textit{op. cit.}, p. 1144.
\textsuperscript{238} \textit{Idem}, p. 1145-1146.
\textsuperscript{239} For instance in Egypt, the length of the tax holiday varies according to the number of employees, the location of the investment, and the type of business. For example, the five year tax holiday is available for all industrial and commercial projects that hire 50 or more employees and maintain proper accounting books, whereas projects located in new industrial zones, new urban communities, and remote areas are exempt from tax for 10 years from the beginning of their activities. Egypt also allows a three year exemption from stamp duty and provides an unconditional initial investment allowance of 25% for investment in machinery and equipment. For more details, see C. Duanjie, \textit{op. cit.}, p. 23.
exemption of a new firm or investment from certain specified taxes, like corporate income tax. Tax holiday may be full or partial. Full tax holidays provide full exemptions whereas partial tax holidays offer reduced obligations and both may have beneficial impact depending on other factors.

The Rwandan law on SEZ remains silent about tax holidays as a form of tax incentives to be granted to investors in special economic zones. However, an investor in SEZ may benefit from tax holiday basing on art. 41 parag. 3 of the Income Tax Law according to which a registered entity that operates in a Free Trade Zone that fulfils the requirements stipulated in the Rwandan law on investment promotion is entitled to pay corporate income tax at the rate of zero per cent. Considering that, investors may manipulate loopholes in laws and avoid taxes using tax holidays, we strongly support this silence of the SEZ law and don’t appreciate exoneration of SEZs investors up to 0% of corporate tax. Instead, it is advisable for the Government to use accelerated depreciation allowance instead of tax holidays. In fact, accelerated depreciation allowance does not change total deductions, but only brings them forward in time. This means that in case of an initially unprofitable investment, there may be no benefit and then no taxes deducted, but taxes will still be taken in later years of profitability.

Apart from tax holidays, tax amnesties constitute another category of tax incentive that is widely granted to SEZs investors. Tax amnesties typically allow individuals or firms to pay

240 A. Klemm, op. cit., p. 4.
241 For instance, Ireland used its business tax system to encourage businesses to locate there, thus creating the opportunities for its skilled labour to work in Ireland rather than move to other countries, by reducing its corporate income tax rates to 10% (partial tax holiday) for manufacturing and international financial services. As result, Ireland has been ranked the first country with cumulative increase in real GDP per capita of 25 OECD countries between 1988 and 1998. However, apart from reforming its tax system by offering tax holidays and cutting down corporate tax rates, other factors have played an important role like joining the European Union, heavily investing in education, etc. More details can be found in J. M. Mintz, op. cit., p. 8.
242 Even though tax holidays are viewed as a simple tax incentive with a relatively low compliance burden, which makes this form of incentive attractive, tax holidays, if not well managed by the state, risk to be subjected to the manipulation of investors, which in some cases lead to tax avoidance. For instance, tax holidays are particularly attractive to short-term, footloose and rapidly profitable investment, as the benefits accrue only during the limited period of the tax holiday and these are unlikely to match the authorities’ priorities. Again, there is a threat that investors may exit and/or close their businesses after the holiday.
243 A. Klemm, op. cit., p. 15. This author provides an example of Ireland. In Ireland, the accelerated depreciation allowance may take the form of an initial allowance of free depreciation at any time for any firm entitled to the aforementioned low income tax rate of 10%. The initial allowance must be claimed up to the full amount available or not at all, which may be most suitable for profitable companies that use the proceeds to upgrade or increase their capital capacity, and the free depreciation may be claimed as any amount between zero and the maximum amount available up to the unclaimed capital cost. This is particularly suited to start-up companies, which can use up all the tax depreciation allowance before paying any income taxes once they become profitable,
previously unpaid taxes without being subject to some or all of the financial and criminal penalties that the discovery of tax evasion normally brings\textsuperscript{244}. Many countries worldwide have adopted tax amnesty in one form or another,\textsuperscript{245} and sometimes the repetition of amnesty took place at an interval as short as every two years.\textsuperscript{246}

Tax amnesties do not only waive criminal and civil penalties but also offer tax evaders the opportunity to satisfy their fiscal obligations,\textsuperscript{247} and in practice, a widely used form of tax reduction is the waiving of interest charges,\textsuperscript{248} whereas in other cases, the amnesty implies the reduction of the nominal tax rate.\textsuperscript{249}

Even if tax amnesty may have negative impact\textsuperscript{250}, tax amnesty constitutes a recommendable tax incentive that, with extreme attention, may be offered to SEZs investors because it might have more advantages than disadvantages. For instance, the voluntary tax compliance may increase after an amnesty.\textsuperscript{251} This is because, in principle, citizens are willing to pay taxes and this type of incentive has the effect of being a tax holiday for start-up firms and encourages long-term capital expansion, but prevents conventional tax holiday owners from escaping tax liability after they become profitable.

\textsuperscript{244} J. Alm, \textit{op. cit.}, p. 1.

\textsuperscript{245} As affirmed by J. Alm, \textit{op. cit.}, p. 1, in the 1998s, nearly forty states in the USA have enacted some form of tax amnesty, sometimes more than once and many other countries have also used one or more amnesties. These countries include those in all parts of the world: in Europe there are Belgium, France, Ireland, Italy and Switzerland; in Latin America there are Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, Honduras, Mexico, Panama, Peru and Uruguay; in Asia there are India, Malaysia, Pakistan and Sri Lanka; and in the Pacific there are Australia, Indonesia, New Zealand and the Philippines.

\textsuperscript{246} H. Sharan, \textit{Essays on Value Added and Tax Amnesty Programs}, West Virginia University, 2005.


\textsuperscript{250} For instance, honest taxpayers may view the amnesty as an unfair tax break for tax cheaters and reduce their voluntary compliance in response; some individuals may pay taxes largely out of a feeling of guilt and if the amnesty lessens guilt as a motivating factor, post amnesty compliance suffers; the mere announcement of the amnesty may also make taxpayers aware of the widespread presence of noncompliance, something that was previously unknown to them; the announcement of the amnesty may also make taxpayers aware of the ease of tax evasion, that is, taxpayers may have felt that tax evasion would be quickly detected and punished, but the amnesty sends a signal that the tax authority is unable to enforce the tax laws; and also the individuals may expect another amnesty to be given in the future, and again decide to pay less taxes voluntarily in anticipation that this evasion will be forgiven at some point in the future. As recommended by this author, individuals or firms are more likely to participate if a tax amnesty is accompanied by a significant change in the tax system and citizens must believe that the amnesty is a one-time opportunity, which means that the government must have credibility. For details, see J. Alm, \textit{op. cit.}, p. 3.

\textsuperscript{251} According to J. Alm, \textit{op. cit.}, p. 3, tax amnesty may increase voluntary compliance in the sense that in some cases, if not in most cases, individuals may wish to correct their previous illegal actions but be afraid of the prosecution and penalties that normally accompany the discovery of tax evasion. But, by giving them the opportunity to correct their previous tax evasion and to enter or re-enter the system, a tax amnesty will increase voluntary compliance since tax authority now has a record of their activities. Compliance will also increase if the
because either they feel morally obliged to comply or they wish to avoid expected sanctions, and if the Government enforces sanctions, it receives revenues but also bears administrative costs\textsuperscript{252}, which would be avoided.

Tax amnesties may also be used to cover tax arrears whose recovery may be difficult and/or sometimes impossible using the traditional systems. For instance, the RRA Annual Activity Report for 2009/2010 mentions that total tax arrears recovered during 2009/2010 amounted to Rwf 13.8 billion and contributed to 3.6\% to the total tax collections, figures, which is interesting.\textsuperscript{253} However, the same report mentions that despite efforts made in recovering tax arrears, there still exists a large amount of tax arrears not yet recovered, in the range of Rwf 64.9 billion as at June 30, 2010, which amount is quite higher than the recovered amount; and this report details that 35\% of the total tax arrears were categorized under potential recoverable cases, 53\% under difficult cases, while 12\% were under irrecoverable cases.\textsuperscript{254} Thus, if the GoR could use tax amnesty, it would recover a large amount of arrears especially those categorized as difficult and more for such categorized as irrecoverable.

Hence, the Rwanda Revenue Authority (RRA) would rather use tax amnesty instead of deciding that: “there is need to give priority to larger and more recent cases of tax arrears to avoid aging of these and write-off the old ones”.\textsuperscript{255} In fact, this technique looks not effective since some of tax arrears shall never be recovered, like those categorized as unrecoverable as well as a part of those categorized as difficult recoverable.

Above all, an important element to bear in mind is that the first factor to SEZs success is not tax incentives. Experience shows that the use of generous incentives packages to offset other disadvantages (such as poor location and facilities) is ineffective in terms of over-all zone performance, due in large part to the increasing commonality of zone investment incentives in recent years.\textsuperscript{256} Also, the negative impact of restrictive policies and practices embedded in many zone programs has been proven even greater than that of uncompetitive incentives schemes and examples include restrictive treatment of real assets, inappropriate application of

\footnotesize{amnesty is followed by greater enforcement efforts and by stronger civil and criminal penalties as well as a more extensive taxpayer services and better education on taxpayer responsibilities, both of which make taxpayers more willing to pay their taxes.}

\textsuperscript{252} C. Marchese & A. Cassone, \textit{op. cit.}, p. 3.
\textsuperscript{253} RRA, \textit{op. cit.}, p. 14.
\textsuperscript{255} \textit{Ibidem}.
\textsuperscript{256} FIAS, \textit{op. cit.}, p. 49.
extraterritoriality principles, performances, prevention of private sector development of zones, weak administrative bodies, trade exclusions on zone merchandise, etc. 257

III.2.4. Monitoring and enforcing Special Economic Zones operations

The management of special economic zones in Rwanda is done by a regulatory organ referred to as “SEZAR” 258, responsible for coordinating activities, designing and providing direction of strategies as well as ensuring the operation and supervision of a Zone. The responsibilities of SEZAR are detailed out in art. 12 of the SEZ law 259 and it is vested with the sole power to issue licence for development, operation and use of a Zone. 260 Still on this point of license, the application for a license to develop and operate a Zone is also addressed to and granted by the SEZAR, 261 which may also suspend or revoke a zone developer or operator license by virtue of laws and agreement between both parties 262 as well as a user license. 263 Subject to the provisions of the Penal Code, SEZAR has the power to impose administrative sanctions against any Zone developer, operator and user who violates regulations governing a Zone and the agreement they signed. 264 In fact, SEZAR is the overall authority of daily management of special economic zones in Rwanda.

Up to now, SEZAR is housed in RDB and one may wonder if it will continue to be like a department or a unit of RDB or if it will form an independent organ. At this point, we don’t find it to be a good idea to continue hosting SEZAR in RDB, basing on the views of FIAS, according to which, a government, to successfully run SEZs, must ensure sufficient autonomy of the zone authority particularly over staffing, budget, spending and policymaking as well as

257 Ibidem. Other obstacles to SEZs successes relate to physical design, development and management practices like poor site locations, entailing heavy capital expenditures, uncompetitive policies such as reliance on tax holidays, rigid performance requirements, poor labour policies and practices as well as poor zone development practices like inappropriately designed or over-designed facilities, inadequate maintenance and promotion practices, cumbersome procedures and controls, inadequate administrative structures or too many bodies involved in zone administration as well as weak coordination between private developers and governments in infrastructure provision. 258 In terms of art. 2.14 of the SEZ law, SEZAR means Special Economic Zones Regulatory Authority of Rwanda. 259 Such responsibilities of SEZAR are: to collaborate with relevant Government authorities to enable Zones to fulfill their responsibilities as provided by their governing laws; to ensure that Zones comply with laws, develop them and facilitate their smooth operation; to ensure that systems for the provision of administrative services to prospective developer, operator or user are available in a Zone; to receive and follow up applications filed by developers, operators and users of a Zone; to keep operational records of each Zone; to issue the certificate of origin for all goods that are shipped from a Zone; and to advise Government on matters relating to the establishment of Zones. 260 Art. 16 of the SEZ law. 261 Art. 19 of the SEZ law. 262 Art. 25 parag. 1 of the SEZ law. 263 Art. 31 of the SEZ law. 264 Art. 40 of the SEZ law.
ensure an adequate authority by constituting an independent board comprised of key
government ministers and private sector representatives who may constitute the majority of
the board membership to ensure flexibility, results-orientation and customer care focus.  
Thus, for a better effectiveness of SEZAR, this might be a totally independent and
autonomous organ, financially and administratively. To this effect, SEZAR might be a
separate entity, different from RDB. However, with regard to the mission of RDB, there might
be a sound working relationship between the two, for instance at reporting level.

III.3. Regulatory framework of Rwanda Special Economic Zones

SEZs in Rwanda are governed by a wide range of legal texts forming a system composed of
one specific law plus other general laws and regulations. Despite the existence of such legal
arsenal, the creation, development and management of SEZs are closely linked to a number of
legal issues, that requires, to some extent, a retouch of existing country’s legal system in order
to cope with SEZs.

III.3.1. Legal frame for the Rwanda Special Economic Zones scheme in Rwanda

The starting point of SEZs in Rwanda is the provisions in the law n° 26/2005 of 17/12/2005
relating to investment and export promotion and facilitation. This law talks about free
economic zones in articles 22 to 26. In terms of art. 25 of this law, an investor operating in a
free economic zone shall be entitled to a right of importing machinery, equipments and raw
materials (for the industry) and other goods free of duty, and an investment enterprise to
operate in free economic zones must export at least 80% of its production.

Six (6) years later, a specific law on free zones was adopted, that is the law n° 05/2011 of
21/03/2011 regulating special economic zones. This law doesn’t define what special economic
zone is. In front of this silence, we refer to art. 2.7 of the law n° 26/2005 of 17/12/2005
relating to investment and export promotion and facilitation, which defines Free Economic
Zone as an area designated by the competent authority where goods and services are imported
free of duties. The same article recognizes three (3) types of free economic zones namely
Export commodity processing zone (EPZ), Free trade zone (FTZ) and Single enterprise
considered as export processing zone (SEEPZ).

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265 FIAS, op. cit., pp. 56-57.
266 Point 6 of the Annex I to the law n° 26/2005 of 17/12/2005 relating to investment and export promotion and facilitation.
267 In terms of art. 2.7 parag. 2, EPZ means a clearly geographically demarcated industrial zone where imported
or locally produced machinery, equipment, goods and services are imported free of duty and utilized in producing
Surprisingly, the recently adopted law on free zones talks about special economic zones and doesn’t refer to any of the above mentioned specific models. In front of this silence, we consider the term SEZs as encompassing a wide variety of related concepts as above explained, explaining the multiplicity of names and forms as a result of several factors, including (1) the need to differentiate among types of zones that display very real differences in form and function; (2) differences in economic terminology among countries; (3) zone promoters’ desires to differentiate their products from those of the competitors; and (4) the consequences of multiple translations.

It is worth mentioning that a combined reading of the two laws leads to the consideration that the target in Rwanda is not the creation of EPZs as such, i.e. considered in its individualised meaning, nor free trade zones or any other individualised free zone model but rather the legislator and policy makers target special economic zones as a form of free zone that will widely touch on different priority sectors of Rwandan economy.

Another point on the law n° 05/2011 of 21/03/2011 regulating special economic zones in Rwanda, is that this law is too short on specifics and consequently contains ambiguities on some points. As a matter of getting out of these, it envisages the adoption of implementing orders and regulations, which up to now have not yet been adopted. This situation creates a number of legal problems and some of which are not yet fully answered up to now, while others are likely to occur.

### III.3.2. Some legal issues that may arise with Rwanda Special Economic Zones

Setting up SEZs raises a number of legal issues, ranging mainly from employment and labour rights to environment and international regulations. Employment in most free zones exhibits new goods with at least 80% of those goods exported and 20% sold locally after paying the necessary duties and taxes.

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268 Art. 2.7 parag. 3 defines FTZ as a geographically demarcated area into which goods and services are imported free of duties and taxes with at least 80% of those goods and services sold for re-export while 20% are sold locally after paying all the necessary duties and taxes.

269 SEEPZ is defined by art. 2.7 parag. 4 as an industry because of its nature or production factors located outside a geographically demarcated zone, where imported and locally produced machinery, equipment, goods and services are imported free of duties and utilized in producing new goods of which 80% of those goods and services are exported while 20% are sold locally after paying all the necessary duties and taxes.

270 See chapter III, section one, paragraph one.

some basic patterns such as the predominance of semi-skilled young and women workers.\textsuperscript{272} In addition, even though the SEZs have a number of benefits as far as employment is concerned, most of them are also marked by very long working hours and high turnover, which may work to prevent it from being a source of long-term employment and economic advancement.\textsuperscript{273} With regard to these probable violations of labour rights in SEZs, art. 37 of the law on SEZs provides that labour and management relations in each zone shall be governed by the existing labour laws of Rwanda. However, in consideration of the purposes for which a Zone was created, an Order of the Minister in charge of labour shall determine labour conditions in that Zone.\textsuperscript{274}

Apart from employment and labour rights issues, setting up SEZs may face in some instances the pressure from outside and in some instance needs tough discussions and negotiations. This is because many of the international development agencies discourage its use.\textsuperscript{275} Again, SEZs, like any other free zones, are subject to a number of international rules, mainly the Kyoto Convention and WTO agreements. Starting with the Kyoto Convention, its Annex F\textsuperscript{1} concerns customs and came into force in 1979. The Annex D 2 also deals with free zones and views them as outside of normal customs control and gives voluntary and suggestive guidelines to customs authorities as far as free zones are concerned.\textsuperscript{277} The Revised Kyoto Convention also mentions that free zones should be treated as outside the domestic customs territory, but should be eligible for national certificates of origin and participate in trade and market access agreements.\textsuperscript{278}

\textsuperscript{273} Ibidem.
\textsuperscript{274} Art. 37 parag. 2 of the SEZ law. However, with regard to the provisions of this second paragraph, one may wonder if the Minister in charge of labour can issue an order, which is contrary to labour laws.
\textsuperscript{275} R. Haywood, “Using Trade Preferences to Promote EPZ Development”, Speech at World Free Zone Convention, Cairo, Egypt, 27\textsuperscript{th} April 2004, in \textit{Journal of the Flagstaff Institute}, vol. 28, n° 1, June 2004, p. 7, critics say that it is benefiting only multinational corporations and not the people.
\textsuperscript{276} Rwanda became party by the Presidential Order n° 57/01 of 20/08/2009 ratifying the revised Kyoto Convention on the simplification and harmonisation of customs procedures signed on 26/06/1999, in O.G. n° 42 of 19/10/2009.
\textsuperscript{277} The Standard 2 of Chapter II of the specific Annex D of the Revised Kyoto Convention states that National legislation shall specify the requirements relating to the establishment of free zones, the kinds of goods admissible to such zones and the nature of operations, etc.
\textsuperscript{278} In the views of FIAS, this constitutes one of the key elements of a best-practice policy framework. For more details, see FIAS, \textit{Special Economic Zones: Performances, Lessons Learned and Implications for Zone Development}, Washington, April 2008, p. 52.
Further, the Kyoto Convention legitimizes and agrees that no duty be charged on the SEZs products that enter the domestic customs territory, but only for that portion of the product that was created in the SEZ, whereas the foreign sourced components of the products have to be charged at the entrance to the local market.

As far as WTO agreements are concerned, they do not directly target the free zones. However, the membership of the WTO entails adherence to the Agreement on Subsidies and Countervailing Measures (SCM Agreement)\textsuperscript{279} and this has some regulatory and policy issues on the free zones. As an instance, export based incentives are prohibited for most countries and incentives based on domestic content are prohibited to all countries.\textsuperscript{280}

Still on the same point, although SEZs do not appear in the WTO agreements, some of their provisions affect the zone incentive regime.\textsuperscript{281} In fact, even if the SCM Agreement doesn’t affect services-oriented export subsidies, which fall outside the scope of it, many manufacturing-oriented export subsidies fall foul of the prohibition on specific subsidies covered by that agreement.\textsuperscript{282} Still on the same point, SCM Agreement poses a number of potential compliance problems for SEZs due to a variety of incentives offered to investors therein. In terms of SCM Agreement, prohibited subsidies are those conditional on export, or the use of national rather than imported inputs, and, actionable subsidies, by contrast, may give rise to consultations if they injure another WTO member’s domestic industry, nullify tariff concessions, or seriously prejudice another WTO member’s interests.\textsuperscript{283}

As mentioned by the FIAS team:

> “The general consensus is that SEZ regimes are consistent with the WTO so long as benefits are not contingent on export performance, use of local content, or maintenance of a foreign exchange balance; or primarily benefit a specific firm, industrial, or other interest. Zone regimes that have specific incentives linked to export performance –


\textsuperscript{280}R. Haywood, \textit{op. cit.}, p. 22.

\textsuperscript{281}FIAS, \textit{op. cit.}, p. 54.

\textsuperscript{282}This results from a combined reading of art. 1 of the SCM Agreement according to which a subsidy is defined as a financial contribution by a government or any public body within the territory of a WTO member that confers a benefit on the recipient; art. 2 which adds that subsidies must be specific to an enterprise, an industry or a region to become “actionable” within the required procedures under the agreement, while art. 3 prohibits two types of subsidy outright: those attaching to the export of goods or to the substitution of imports. For more details, see P. Muchlinski, \textit{op. cit.}, p. 21.
such as minimum export requirements, subsidised rent or utilities, or a lower tax on export income – are not compatible with WTO mandates and need to be altered. In addition, some analysts conclude that the broad exemptions of import duties and charges granted to SEZ enterprises may constitute a prohibited export subsidy since firms operating under other regimes are permitted duty-free importation of only those inputs used in the production of goods”.

Apart from FIAS Team, the World Bank also agrees that SEZ regimes are consistent with the WTO so long as benefits are not contingent on export performance, use of local content, or maintenance of a foreign exchange balance; or primarily benefit a specific firm, industry, or other interest and zone regimes that have specific incentives linked to export performance – such as minimum export requirements, subsidised rent or utilities, or a lower tax on export income – are not compatible with WTO mandates and need to be altered.

Briefly, the SEZs are not prohibited as such with regard to international economic rules. However, some of the patterns of SEZs are likely to fall within the prohibited subsidies under international economic rules and this situation requires the governments to set up the zones but with specific attention to avoid those prohibited incentives. Up to now, no aspect of KSEZ can be considered as incompatible with international law, mainly with the WTO rules and no official claim has be lodged up to now against KSEZ.

III.3.3. Harmonizing the legal system to cope with Special Economic Zones

In order to cope with SEZs, Rwanda needs to reform some of its laws, either by enacting new laws or by adapting the existing ones. Internally, up to now, the first procedure has been done with adoption of the law n° 05/2011 of 21/03/2011 regulating special economic zones in Rwanda. This law envisages the adoption of implementing ministerial orders like a Prime Minister’s Order establishing a zone in an area which is not covered by a master plan, a Prime Minister’s Order establishing a zone whether on private state land, private Kigali city land, private district land and individual’s or legal entity’s land, a Prime Minister’s Order

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283 FIAS, op. cit., p. 54. However, these subsidies are permitted under the WTO, and are actionable only in that the affected parties have legal recourse under the WTO dispute resolution mechanism.
284 Ibidem.
285 P. Muchlinski, op. cit., p. 22.
286 In O. G. n° special of 30 march 2011.
287 Art. 7 in fine of the SEZs law.
288 Art. 9 of the SEZs law.
determining powers, organisation and functioning of SEZAR,\textsuperscript{289} an Order of the Minister in Charge of trade and industry determining an amount of non-refundable Developer License application fee,\textsuperscript{290} and an Order of the Minister in charge of Labour determining labour conditions in Zones.\textsuperscript{291}

Internationally, the establishment of SEZs in Rwanda risk to be hampered by a relative small number of international tax agreements\textsuperscript{292} that Rwanda entertain with other states. At this point, it is quite surprising and not appreciable to hear that Rwanda has only three (3) double taxation avoidance agreements.\textsuperscript{293} In fact, once SEZs are fully established and fully operating, Rwanda will need to conclude more double taxation avoidance agreements (DTAAs) to facilitate foreign SEZs investors enjoy freedom from double taxation. This is because tax agreements constitute one of the basic fundamental corner stone to attract investments especially FDI. As affirmed by A. Barak, tax treaties are designed to facilitate economic relations between countries by attempting to solve the problems created by double taxation.\textsuperscript{294} Clearly and understandably, an investor would prefer to invest in a state that has a tax treaty rather than in a state that doesn’t. In this regard, Rwanda should adopt many tax treaties as possible with foreign states especially those whose citizens are more interested to invest in Rwanda’s SEZs.

\textsuperscript{289} Art. 13 of the SEZs.
\textsuperscript{290} Art. 20 in fine of the SEZs law.
\textsuperscript{291} Art. 37 of the SEZs law.
\textsuperscript{292} A tax agreement refers to an agreement or a treaty between two or more states (see H. Ayadi, \textit{Droit fiscal international}, Tunis, CPU, 2001, p. 91 for details) and a distinction is made between pure tax agreements from tax clauses inserted in an international agreement (P. Marchessou, \textit{L’interprétation des textes fiscaux}, Paris, Economica, 1980, p. 13 for details).
\textsuperscript{293} Up to now, Rwanda has concluded only three double taxation avoidance agreements namely the Convention signed in Kigali, Rwanda, on 16\textsuperscript{th} April 2007, between the Republic of Rwanda and the Kingdom of Belgium for the avoidance of double taxation and the prevention of tax fraud and fiscal evasion with respect to taxes on income and capital, ratified by the presidential order n° 57/01 of 04/10/2010, in \textit{O.G.} n° 41 of 11/10/2010; the DTAAs signed with Mauritius in 2001 and came into force in 2003; and the Agreement on the avoidance of double taxation and embezzlement of taxes with respect to taxes on income between Rwanda and South Africa, signed on 05/12/2002, ratified by the Presidential Order n° 36/2009 of 14/07/2009, in \textit{O.G.} n° 35 of 31/08/2009. In this matter, some countries have reached an appreciable stage and have concluded a significant number of tax treaties. For instance, Canada has over 80 tax treaties (as mentioned in M. N. Kandev, “Tax Treaty Interpretation: Determining Domestic Meaning under Article 3 (2) of the OECD Model”, \textit{Canadian Tax Journal}, vol. 55, n° 1, 2007, p. 33, available at http://www.ctf.ca/ctfweb/Documents/PDF/2007ctj/2007ctj1-kandev.pdf, accessed on 11\textsuperscript{th} September 2011), whereas Morocco has 48 double taxation avoidance agreements and 24 projects to this effect (for details, see Annex 6 of R. Ouiazzane, \textit{Tanger, quel regime de zone franche?}, memoire de Master, Universite Paris Dauphine, 2008, available at http://memoireonline.com/07/10/3720/Tanger-quel-regime-de-zone-franche-.html, accessed on 15\textsuperscript{th} June 2011).
Still on the point of DTAAs, another point that needs much attention is about the implementation and interpretation of such DTAAs. As far as the implementation is concerned, art. 190 of the Constitution of the Republic of Rwanda of 04th June 2003 as amended to date, reads that upon their publication in the Official Gazette, international treaties and agreements which have been conclusively adopted in accordance with the provisions of law become more binding than organic laws and ordinary laws except in the case of non compliance by one of parties. Though, in Rwanda, like in other most countries, a treaty doesn’t become part of domestic law until it is enacted, i.e. ratified, which ratification incorporate it into domestic system and publicise it to that effect.

As a matter of interpretation, there exists a large debate on the prevalence of treaty provisions and the provisions of domestic law. J. Li and D. Sandler argue that although the basic principle governing the relationship between treaty provisions and domestic law is that the provisions of the treaty prevail in the event of any inconsistency between the treaty provisions and domestic taxation provisions, there is a competing principle of domestic law according to which parliament is supreme, and consequently, parliament can enact legislation that overrides previous legislation, including a tax treaty incorporated into domestic law.

This is because most of the states, if not all, attach a great importance to the principle of state sovereignty and logically international tax agreement cannot go beyond the state sovereignty. According to J. P. Jarnevic, the tax person must be realistic: “the state sovereignty shall always be a must; no state can abandon its important sections of its sovereignty in tax field. And, it shall be an absolute illusion to think of a universal tax system, many international tax systems have to coexist, logical situation because the taxation reflects the socio, economic and political structures”. In the same sense, the growing tendency in

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295 For instance in Canada, a treaty does not become part of domestic law until it is enacted, like any other statute. For more details, check J. Li and D. Sandler, op. cit., p. 895.
296 Ibidem.
297 The principle of state sovereignty is provided for by article 2.1 of the UN Charter. According to this principle, the UN and its Members, in pursuit of the purposes stated in art. 1 of the same Charter, shall act in accordance with a set of principles, and the first point reads that the UN is based on the principle of the sovereign equality of all its members.
298 Own translation. The original French version of J. P. Jarnevic, op. cit., pp. 2-3 is as follow: “Le fiscaliste se doit-être réaliste: la souveraineté étatique sera toujours incontournable; aucun État n’est dispose a abandonner des pans importants de sa souveraineté dans le domaine fiscal. Il serait absolument illusoire d’attendre un «ordre fiscal universel» plusieurs «ordres fiscaux internationaux» doivent coexister; situation logique dans la mesure où la fiscalité est un reflet de structures sociales, économiques et politiques”.

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some jurisdictions, notably the USA, is to resort to treaty overrides in order to protect the domestic tax base.\(^{299}\)

In France, the subsidiarity of tax agreements has been reaffirmed by the *Conseil d’État Français* in the judgment *Societe Kingroup* of 04\(^{th}\) April 1997\(^{300}\) as well as in the judgment n° 232276 of 28\(^{th}\) June 2002 according to which, if a bilateral agreement concluded to avoid double taxation, basing on the Constitution, can eliminate a given point of domestic tax law, it cannot itself directly serve as a legal provision for a decision regarding taxation; and it is up to the tax judge to first check in the domestic tax law and see if the contested taxation has been validly established, and if yes on which basis.\(^{301}\) In the same sense, the customs of international tax law admits a taxpayer to request that a tax agreement not be considered simply because or to the sole motive that it aggravates its situation.\(^{302}\) The same considerations constitute also an utmost importance as far as the interpretation of tax agreements\(^{303}\) is concerned.

Thus, for a successful run of SEZs in Rwanda, Rwanda needs to conclude more DTAAAs and at this point we call upon attention of the GoR as far as the implementation and interpretation of

\(^{299}\) J. Li and D. Sandler, *op. cit.*, p. 895.


\(^{303}\) In *The Queen v. Crown Forest Industries Limited et al.*, 95 DTC 5389, at 5393 (SCC), cited in M. N. Kandev, *op. cit.*, p. 35, Justice J. Iacobucci affirmed that “in interpreting a treaty, the paramount goal is to find the meaning of the words in question. This process involves looking to the language used and the intentions of the parties”. From this extinguished judge, not only the language of the treaty must be taken into consideration but also the intentions of the parties, i.e. what the parties wanted to conclude an agreement into question. This way of interpreting a tax treaty has been emphasised by the Canadian courts according to which “contrary to an ordinary taxing statute a tax treaty must be given a liberal interpretation with a view of implementing the true intentions of the parties. A literal or legalistic interpretation must be avoided when the basic object of the treaty might be defeated or frustrated insofar as the particular item under consideration is concerned” (*Gladden Estate v. The Queen*, 85 DTC 5188, at 5191 (FCTD), cited in M. N. Kandev, *op. cit.*, p. 36). Still in Canada, in *Stubart Investments Limited v. The Queen*, the Supreme Court of Canada accepted the “modern approach” to statutory interpretation as formulated by Driedger: “Today there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament” (see E. A. Driedger, *The Construction of Statutes*, 2\(^{nd}\) ed., Toronto, Butterworths, 1983, p. 87, cited in J. Li and D. Sandler, *op. cit.*, p. 917). However, the Supreme Court of Canada has indicated that the object and purpose of a statutory provision is relevant only if there is doubt or ambiguity as to the meaning of the provision; if there is no doubt or ambiguity – that is, the provision of the Act has a plain meaning – the plain meaning prevails (see J. Li and D. Sandler, *op. cit.*, p. 917 for details). Especially in tax treaties, the intention of the parties is so relevant and much emphasized. In the Saunders judgment, justice Fodham affirmed, “where a tax convention is involved, however, the situation is different and a liberal interpretation is usual, in the interest of the comity of nations. Tax conventions are negotiated primarily to remedy a subject’s tax position by the avoidance of double taxation rather than to make it burdensome. Accordingly, it is undesirable to look beyond the four corners of the convention when seeking the ascertain meaning of a particular phrase or word therein” (for more details, see M. Duval, “Interprétation des conventions fiscales”, *Canadian Tax Journal*, vol. 39, n° 5, 1991, p. 1229, available at [http://www.ctf.ca/ctfweb/documents/pdf](http://www.ctf.ca/ctfweb/documents/pdf), accessed on 31st July 2011).
such agreements are concerned. To this regard, importance should be attached to the
awareness of the principle of sovereignty and the Government must make sure that while
concluding tax treaties, these will not overcome national rules except in cases required to do
so by the national interests. Rwanda might also be in good preparation to deal with some
international agencies that may perceive SEZs as violating international rules.

Summary of the third chapter
Basing on the current situation of Rwanda, Special Economic Zones constitute a
recommended strategy for the Government of Rwanda to increase investments flow. It is in
this regard that after a long period of initiating such zones in Rwanda, this Thesis appraises
the efforts of the Government and appreciates the stage that these zones are up to now.
However, some critics are also remarkable, especially with regard to the legal framework of
SEZs in Rwanda. Mainly, these critics result from the fact that the developmental activities of
such zones are progressing very well but the legal framework moves at a slow pace. To
illustrate this, for instance, up to now, the only legal step done has been the adoption of the
law governing SEZs in Rwanda but no single implementing order and/or regulation is yet
adopted. Though, much needs to be done especially on the legal side of the special economic
zones in Rwanda.

CHAPTER IV. GENERAL CONCLUSION, RECOMMENDATIONS AND AREAS
FOR FUTURE RESEARCH
This chapter focuses on the conclusions of the discussed matters, presentation of related
recommendations and suggest some areas relating to the discussed topic that need further
research.

IV.1. Concluding remarks
The primary purpose of any tax system is to raise revenue to cover the costs of public
expenditures and it is in this regard that the tax system is merely a means (collection) to an
end (funding outlays determined through the political process).\textsuperscript{304} Though, a tax system must not only provide for current spending, but also be capable of meeting the future revenue needs of the state.\textsuperscript{305} It is in this regard that tax policy makers always devise tax systems that are much better than the already existing ones.

Bearing in mind the importance that the business community attach to taxes, the conception a good tax system constitutes one of the major tasks of the government. This is because the tax system must satisfy two extreme sides, i.e. the business community on one hand and the government on the other hand. All in all, the better approach is to have continuing process of revising tax regulations. It is in this regard that the GoR, bearing in mind the national economic strategies, has operated reforms in terms of fiscal issues, starting with the creation of Rwanda Revenue Authority in 1998 and modifying a majority of tax laws in 2005.

Despite such tax laws reform, the business community is still claiming that Rwanda tax system still constitutes an obstacle to a rapid development of some businesses in Rwanda. Apart from the informal perception of the business community, some reports have also pointed out some aspects of Rwanda tax system as constraints to business development, and more precisely to investment attraction. Rather, mainly due to some natural factors, Rwanda needs much FDI to sustainably develop itself.

This Thesis studied how Rwanda can use tax incentive in order to attract investments. The starting point has been a short description of the present tax incentives, i.e. tax incentives that presently exist under Rwandan tax laws. To this purpose, the concept of tax incentives has been explored and different existing tax incentives have been described. This Thesis also had an insight into Rwanda’s investment climate at present situation. A smooth overview of Rwandan tax laws led to a conclusion that up to now, Rwanda has a large number of tax incentives that are generally granted to businesses and some tax incentives that are only granted to some investors.

Bearing this in mind, this Thesis discussed in the second chapter whether Rwanda has more need to use tax incentives to attract investments or not. To this end, a correlation between tax incentives, investments and economic growth was first done. A smooth analysis of natural and

\textsuperscript{304} D. Brunori, \textit{op. cit.}, p. 52.  
\textsuperscript{305} \textit{Ibidem}. 
geographical situation of Rwanda as well as some other socio-economic reasons pertaining to Rwanda, revealed that Rwanda doesn’t have much comparative advantages in the region and concluded that Rwanda needs much to use tax incentives to attract investments, taking it as one of the possible effective solutions. Comparing the strengths and opportunities to weaknesses and threats of using tax incentives to attract investments in Rwanda, it was found that using tax incentives as a strategy to attract investments in Rwanda can bring advantages that are higher than disadvantages. With this, the major task that may arise is the choice of tax incentives that can be used, which choice, if principled cannot cause any problem.

This led to the third chapter. In this chapter, reference made to some perceptions according to which, Rwanda offers generous tax incentives, which may be true or not\footnote{This was not the subject of our research and we maintain a neutral position in front of such arguments.}, special economic zone was discussed as a type of tax incentive that better fit to attract more investments in Rwanda. Along chapter three, the present situation of SEZs in Rwanda was discussed and through an analytical comparison, some features of the SEZs in Rwanda mainly the legal issues pertaining to such zones were also discussed. Conclusory, as far as the establishment process of KSEZ is concerned, much need to be yet done and its potentials have not yet been completely brought into play. However, basing on what has been done up to now, even though the road is not easy, there is much expectations on the success of KSEZ and one can expect that once fully operating, KSEZ will immensely contribute to the sustainable development and economic growth of the country.

All in all, it should be noted that adopting any simple tax reform or change constitute a big ambitious undertaking, which encompasses far more than this Thesis can suggest; and one must bear in mind the affirmation of two tax experts according to which “It is critical to ensure that changes in tax policy are compatible with administrative capacity”\footnote{M. R. Bird & M. Casanegra de Jantscher, \textit{Improving Tax Administration in Developing Countries}, International Monetary Fund, 1992, p. 1.}. As an instance, a country, like Rwanda, to establish SEZs need to undertake careful cost-benefit analyses to determine the real profitability of such programs, including both direct costs like infrastructure and subsidized services and indirect costs in the form of foregone government revenue and national income as a result of tax exemptions, unfettered profit repatriation and so on.
IV.2. Recommendations

Basing on what discussed along this Thesis and considering its support to the creation of SEZs in Rwanda to sustainably attract FDI in Rwanda, it’s time to highlight some rational recommendations to the GoR, especially the tax policy makers in Rwanda.

In his study on reformulating tax incentives in Jordan, C. Duanjie remarked that “to achieve the efficiency, simplicity, and fairness in taxation and to follow international best practices, Jordan’s cumbersome and inefficient investment incentives program should be replaced by a simpler and more efficient program that is directly linked to capital investment”. Rwanda should adopt the same approach and grant tax incentives that are directly linked to capital investments, instead of having a large chain of tax incentives but that do not really attract investments but rather consequently constitute a base of qualifying Rwanda as one of the generous tax incentives country, which in turn lead to an unnecessary loss of government revenues as consequence.

More specifically, the GoR should strengthen the SEZs in Rwanda and mainly attention should be taken to the purpose of SEZs in Rwanda. To this regard, the GoR must choose some priority sectors that can be developed through SEZs and once done take another set of priority sectors and so on. In our view, present priority sectors may be developed through SEZs in the following order of preference: ICT, financial services, infrastructure, industry, energy, tourism, agriculture, real estate and construction, and so on.

In addition to the strengthening of SEZs, other supplementing technical aspects should also be taken into consideration to have a full efficient investment attraction. For instance, a successful run of SEZs goes together with a high need of a large number of cheap and well skilled labour forces. To this regard, the education system should be strengthened and mainly target the category of people who can greatly serve in SEZs depending on which activities are mainly targeted in SEZs.

Again, the GoR while introducing the SEZs as competitive tax incentives, capable and ready to compete with tax incentives offered by other states especially those states in the region, the attention should be taken to the limitations of such incentives. This must also be taken as a serious concern because the fact of enhancing more and more (or maximizing) competitive tax
incentives may lead the country to the situation of tax havens, situation that is internationally condemned. Such limitations will also help the GoR to be in conformity with international regulations especially with the WTO rules.

IV.3. Areas for future research

Notwithstanding the significant research done along this Thesis and the subsequent discussions pertaining to it, it would extremely be erroneous to consider that it exhaustively answered all questions thereto related. It would also be seriously erroneous to try research on all questions pertaining to the research topic. Consequently, there are a number of critical questions that are unanswered as well as some other issues that are not yet analysed in details. It is in this regard that further research undertakings are irrefutably needed.

For instance, it would be very important to study the aspects and limitations to tax competition, which can likely lead to tax havens, especially in the context of regional integration. It would also be very important to study the possibility of expanding investment or business opportunities through tax deals especially for the developing countries. In the same sense, considering that, in most cases, the direct person who benefits the tax incentives is the big business corporations, there is a need to study the nexus between tax incentives and the socio-economic improvements especially in developing countries. It would also be very important to study the compatibility between SEZs rules and WTO rules.

A research on implications of tax deals on economic growth and sustainable development in developing countries would also be of great importance. Other topics like the extent of impact assessment of tax competition on FDI, implications of globalisation on tax competition, the role of tax competition on international investment-promotion competition, a study on the regulation of international tax competition, etc. would also be more than welcome.

REFERENCES

i. Legal texts

   a. National legal texts


3. Law n° 05/2011 of 21/03/2011 regulating special economic zones in Rwanda, in O. G. n° special of 30 March 2011.


12. Law n° 16/2005 of 18/08/2005 on direct taxes on income (in O.G. n° 1 of 01/01/2006) as modified and completed by the law n° 73/2008 of 31/12/2008 (in O.G. n° 19 of 11/05/2009), and again modified and completed by the law n° 24/2010 of 28/05/2010 in O.G. n° special of 28/05/2010.


b. Bilateral and multilateral agreements
1. Convention signed in Kigali, Rwanda, on 16th April 2007, between the Republic of Rwanda and the Kingdom of Belgium for the avoidance of double taxation and the prevention of tax fraud and fiscal evasion with respect to taxes on income and capital, ratified by the presidential order n° 57/01 of 04/10/2010, in O.G. n° 41 of 11/10/2010.

ii. Books


### iii. Journal articles

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iv. Reports, Papers and Policies


v. Memoirs


3. **Interviews**
   1. Interview with Azhar Iqbar, the Managing Director of Chatha Motors, Kigali, on 02\textsuperscript{nd} August 2011.
   2. Interview with G. M., a public servant working with a government entity, who conditioned us to keep his names anonymous, on 02\textsuperscript{nd} August 2011.
   3. Interview with R. R., a public servant working with a government entity, who conditioned us to keep his names anonymous, on 02\textsuperscript{nd} August 2011.

4. **Electronic sources**


5. **Other sources**


Thesis summary

Different countries struggle to increase their economic growth and development through different strategies depending on countries’ situations. Worldwide, one of the factors leading to economic growth and development is the attraction of foreign direct investments (FDI). Among different factors that attract FDI, tax system stands as one of the major determinants of FDI. As far as Rwanda is concerned, the policymakers have been changing tax laws, especially in 1997, when Rwanda Revenue Authority was created, and in 2005, the year in which major tax laws have been adopted, others modified and complemented. In the focus of attracting investment, Rwanda tax laws offer a number of tax incentives, targeting at making Rwanda’s tax system business friendly.

In front of these, some reports and analysts see and consider these incentives as abusive and qualified Rwanda as tax generous State, which in consequence lead to the loss of a large amount of government revenues. The same reports and analysts also see and consider these incentives as playing a little role as far as investments attraction is concerned. On the other side, there is an opposing perception of some business doers who consider Rwanda’s tax system as constituting one of the major factors that hampers a prosperous development of their businesses.

In my Thesis, entitled “Enhancing Competitive Tax Incentives for a Sustainable Investments Attraction in Rwanda”, I analysed the existing tax incentives i.e. those which are presently offered under Rwandan tax laws, focusing on their advantages and disadvantages. I also investigated whether Rwanda needs to use tax incentives to attract investments and here the point was to assess the needs and necessity of Rwanda to use tax incentives in order to attract investments through a SWOT analysis. In front of these, it resulted from the conducted research that Rwanda offers a large number of tax incentives. Unfortunately, it was revealed that such offered incentives are unable to attract investments basically because they do not directly target investment as their purpose. Thus, in my Thesis I found the creation of Special Economic Zones as one of the effective strategies that can be used to attract more investments in Rwanda. It is in this regard that I appreciated, in my Thesis, the efforts of the Government of Rwanda to establish the special economic zones starting with Kigali Special Economic Zone and call upon the government’s injection of more efforts.
Briefly, my Thesis focuses on the need and necessity of using tax incentives to attract investments in Rwanda and concluded showing which appropriate tax incentives may be used to effectively achieve this target.