TRANSFER PRICING
“FAIRNESS IN TAXING MULTINATIONALS AND EXTRACTIVE INDUSTRIES”

Tanzanian Perspective

Presented by:

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Large Taxpayers Department
Tanzania Revenue Authority (TRA)
Coverage

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2.0 MNE’s form of business-illustrated
3.0 Transfer Pricing in Tanzania-analyzed
4.0 Special attention-Extractives
5.0 Taxation initiative for Extractives
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   6.2 Effective administration of TP
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1.0 Introduction

- Transfer Pricing is increasingly rampant following increased existence of large Multinational Enterprises (MNEs) in the global economy.
- It is estimated that more than 30% (source: UN TP manual) of all business transactions worldwide are between related parties. International transactions are therefore no longer governed entirely by market forces, but highly driven by the common interests of the entities of a group.
- One thing is crystal clear: MNEs will always seek for higher profitability (business perspective), reducing their tax liabilities through various legal and illegal schemes.
- This is where Transfer Pricing (TP) becomes a corner story.
Among the efforts towards counteracting abusive TP which results into profit shifting is that several countries have managed or are trying to craft some rules.

In Tanzania section 33 of ITA 2004 is relevant.

The provision uphold the Arm’s Length Principle (ALP)

However, having sec. 33 is one thing, integral systems for TP detection and effective administration of such complex international taxation issue is another side of the coin.

This presentation aims at giving you a picture from Tanzania perspective.
2.0 MNE’s forms of business-illustrated

Coy A in Netherland Manufacturer

Transaction may be in form of:
- Royalty
- Management fee
- Procurement charges
- Interest
- Products, etc.

Coy A1 in Tanzania Sales company

Coy A2 Mauritius Management Company
3.0 Transfer Pricing in Tanzania-analyzed

- Like several other African countries, Tanzania is currently striving to aggressively confront the transfer mis-pricing of intra group transactions.
- Mining sector is prominent in its complex global interposed organizational set up and inter-company’s services due to its worldwide business chain.
- Manufacturing, Agriculture and Telecommunications sectors are also popular in intra-group services i.e. Management services, Procurement services and Royalty.
- The extent to which TP problem is depriving govt. revenue from each sector is yet to be known due to, inter-alia, the dynamics of the sectors, complexity of tax planning schemes, skills gap, uneffective EoI, research level etc.
3.1 TP in Tanzania-Status of extractive industry

- Extractive industry has been a dominant sector economically for the last decade
- The emerging Oil and Gas Sector in Tanzania is envisaged to reign extractive industry at number 1 for the coming decades
- These economic changes are expected to pose greater TP problems and challenges to Tanzania
- Tanzania and its TRA: We are positioning ourselves for a greater transparency and fairness through effective legal and administrative framework in the extractive sector and other sectors of the economy
- One may ask, “How!?” - I will come to this later…
- You may first have a glance below on how Mining FDI inflows are dominant sector as pictured in our economy
3.2 Leading sectors and FDI inflow per source country

### Leading Sectors:
- Mining
- Manufacturing
- Communication
- Wholesale & Retail
- Agriculture
- Finance

### TABLE 11: Flow of FDI by Source Country in Tanzania (USD Million), 1999-2008

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- The extent to which Tax haven and low tax jurisdictions features in FDI inflow to Tanzania is a great concern to TRA and government as a whole
- Mauritius (low or no tax) is the third in terms of FDI inflow to Tanzania!
- UK, Canada and Norway are leading in extractive industry in Tanzania
- TRA currently intensively engaged in TP study and audits with special attention to Mining and Telecom after capacity building and ITU incept.
- Intra-group service transactions e.g Technical and Mgmt fees, marketing, royalties etc. are dealt with in Mining, Telecom, Financial, manuf. etc
### 3.3 How low tax/shelters features in Tz FDI

**TABLE 11: Flow of FDI by Source Country in Tanzania (USD Million), 1999-2008**

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<td>11</td>
<td>Singapore</td>
<td>0.01</td>
<td>0.05</td>
<td>0.03</td>
<td>0</td>
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<td>1.31</td>
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<td>Switzerland</td>
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<td>15</td>
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<td>0.84</td>
<td>0.01</td>
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<td>16</td>
<td>Sweden</td>
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<tr>
<td>17</td>
<td>Bermuda</td>
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<td>61.79</td>
<td>-1.33</td>
<td>0.08</td>
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<td>10.81</td>
<td>5.83</td>
<td>4.92</td>
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<td>Luxembourg</td>
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<td>8.52</td>
<td>7.18</td>
<td>0.18</td>
<td>0.9</td>
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</table>

- May not be interested in numbers rather on Tanzania FDI inflow and its business pattern.
- This is how FDI business is flowing to Tanzania.
- One may ask, “do some of these countries have interest in investing into Africa - Tanzania?”
- TP specialist will definitely tell you, *"Tax Planning Scheme"* of MNEs is taking advantage of low or no tax system in those countries for its shifted profits.
- With emerging oil and gas sector we think this phenomenon may increase at a higher degree.

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TANZANIA REVENUE AUTHORITY
### 3.4 Percentage contribution of leading FDI sectors to GDP

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<tbody>
<tr>
<td><strong>Mining</strong></td>
<td>1.8</td>
<td>2.1</td>
<td>2.4</td>
<td>2.6</td>
<td>2.9</td>
<td>3.2</td>
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<td>3.4</td>
<td>3.3</td>
<td>3.3</td>
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<td><strong>Manufacturing</strong></td>
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<td>8.3</td>
<td>8.1</td>
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<td><strong>Finance</strong></td>
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<td>1.7</td>
<td>1.7</td>
<td>1.6</td>
<td>1.7</td>
<td>1.7</td>
<td>1.6</td>
<td>1.6</td>
<td>1.7</td>
<td>1.8</td>
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<tr>
<td><strong>Agriculture</strong></td>
<td>29</td>
<td>28.6</td>
<td>28.7</td>
<td>29.5</td>
<td>27.6</td>
<td>26.2</td>
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<td>25.7</td>
<td>24.6</td>
<td>24.1</td>
<td>23.7</td>
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<tr>
<td><strong>Construction</strong></td>
<td>5.2</td>
<td>6.8</td>
<td>8</td>
<td>7.9</td>
<td>7.8</td>
<td>7.8</td>
<td>7.8</td>
<td>7.7</td>
<td>7.9</td>
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<td>8</td>
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<tr>
<td><strong>Communications</strong></td>
<td>1.2</td>
<td>1.2</td>
<td>1.3</td>
<td>1.5</td>
<td>1.7</td>
<td>2.1</td>
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<td>2.5</td>
<td>2.1</td>
<td>2.1</td>
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Agriculture is the leading sector followed by Manufacturing.

Construction takes third position followed by Mining and Communication.

Finance follows after the above sectors.
3.5 TP in Tanzania-Current initiatives

- TRA is currently working very closely with various stakeholders to study, identify, administer and assess TP magnitude, effect and trend for improved & effective measures.

- It is carrying out researches and closely following up reports by various institutions, researchers, NGOs, Civil Society Groups etc. to enhance better administration of TP schemes.

- To mention a few reports:
  - **The One Billion Dollar Question Report 2012**: “How Can Tanzania Stop Losing So Much Tax Revenue”
  - ActionAid 2012 report: **“Calling Time”** Why SAB Miller should stop dodging taxes in Africa”
  - Associated British Foods: **Sweet for Nothing”**
  - **Koffi Annan-BBC News**-10th May, 2013: Africa losses twice as much revenue through tax loopholes by and largely by TP as it gets from donors”
4.0 Special attention-Extractives

- Extractive industry is booming in Tanzania and therefore we are setting tax agenda at a front seat.
- Legal and administrative strengthening of mining sector through review of fiscal and stabilization clauses in our Mining Development Agreement (MDA) and Production Sharing Agreement (PSA) in oil and gas sector are among the measures taken.
- Extractive Industry Revenue Forecasting Models: A revenue deterministic model: Modeling capacity building project involving key government institutions TRA being key and member and coordinator.
- Study for inception of new Oil and Gas Regime
5.0 Taxation initiative for Extractives

- ITU and special Teams formed by TRA for audits of Extractives-Mining, Oil & Gas.
- Audits conducted revealed existence of TP in the mining sector.
- Areas prone to TP includes mineral pricing, intra-group services.
- Other risk areas revealed by teams includes hedging arrangements.
- Substantial tax adjustments and assessments made for income and tax losses.
- Most of assessments subjected to appellant mechanisms by MNEs.
Extractive Sector Revenue Contribution Trend (Source: TRA)

### Collected taxes

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<td>160,881</td>
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<td>2011/12</td>
<td>393,247</td>
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</table>
6.0 TP Challenges

- The most critical challenge in TP relates to the determination of the arm’s length price to ascertain appropriate taxable profit.
- Tanzania has adopted some ALP as per OECD/UN guidelines to provide some guidance although currently they elicit more questions than answers in our local practice.
- TP is more challenging due to:
  - Infancy TP legal framework and;
  - Effective administration of TP.
6.1 Challenges-Infancy of TP legal framework

- TP require a robust legal framework which as well, require a coordinated efforts of policy makers, legislature, Competent Authority, tax practitioners and public at large.

- Section 33 of ITA need to be backed-up by regulations and TP guidelines (TRA has played its part by close involvement in already drafted TP Guidelines and Regulations/Rules).

- FDIs accompanied by tax incentives may be prone to tax base erosion if not properly researched and regulated. Costs of tax incentives should be well studied and analyzed.

- Some of the DTAs have been outlived by recent amendment in the main Model Tax Conventions and Regional Cooperation Model. 10 DTAs concluded and ratified...
6.2 Challenges-Effective administration of TP

- Lack uniform and consistent regional (EAC; SADC) approach to counter and prevent tax avoidance and evasion of MNC’s tax planning techniques. However ATAF is trying
- Inherent skill gaps to effective administer TP
- Lack of working tools i.e. TP database for practical application of the arm’s length price.
- Lack of legal force to compel disclosure of financial information for comparability purpose.
- Un-effective EoI among various jurisdictions eg. ATAF agreement on EoI not yet effective and some members not endorsed.
7.0 Remedial measures

- We can not sit down and cry, “confidence is a plant of slow growth” and that is how we move.
- TRA and government have given an increased and special focus on tax matters of MNEs and TP in particular.
- Establishment of International Taxation Unit (ITU) in TRA-with specialist TP team which is currently dedicating time and attention to TP audits and issues.
- Acquisition of databases for benchmarking (already set budget for and procurement is in progress).
- Inception of specific TP rules and guidelines (draft regulations are awaiting for approval by Minister)—very soon we will have them in place.
Remedial measures – Cont’d

- Intensive capacity building through trainings and practical skills acquisition on TP. Extended appreciations to assistance from Norad through NTA; US Treasury through OTA; UK’s HMRC/DFID, DANIDA and JICA among others.
- Enhanced cooperation in Africa eg. ATAF, SADC, EAC in Multilateral EoI
- Signing of new treaties (DTAs and TIEAs) to ease information exchange.
- Efforts to join other global multilateral forums eg. CIAT, OECD’s Global Forum on EoI and Transparency.
8.0 Conclusions

- Most developing countries including Tanzania are increasingly faced by common TP challenges.
- Un-effective legal and administrative framework; lack of skilled human capacity and cooperation among jurisdictions are predominant.
- A call is therefore made for these countries to enhance their efforts for effective TP frameworks and increased jurisdictional and regional cooperation on tax matters.
- This will enable confrontation of the challenges in the administration of TP and tax base erosion.
- Optimal achievements in these grave concerns may results from coordinated and joint efforts and willingness of policy makers and legislators, Revenue Authorities, researchers, taxpayers, tax practitioners and public at large.
THANK YOU FOR LISTENING
&
WELCOME TO TANZANIA