

**Competition to attract foreign direct investment through tax
incentives as a threat for the realisation of socio-economic
rights in Africa**

**Submitted in partial fulfilment of the requirements of the degree LLM
(Human Rights and Democratisation in Africa)**

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Declaration

I, **Samuel Tilahun Tessema**, hereby declare that this dissertation is an original work and has never been presented to any other institution. I also declare that all secondary information used has been duly acknowledged in this dissertation.

Signed.....

Date...3...November 2008.....

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Signature.....

Date.....3...November 2008.....

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List of abbreviations

AU – African Union

CRBM – Campagna per la riforma della Banca Mondiale

EURODAD – European network on debt & development

FDI – Foreign direct investment

GDP – Gross domestic product

IMF – International Monetary Fund

LDCs – Least developed countries

MNCs – Multinational Companies/ corporations

OAU – Organisation of African Unity

TJN-A – Tax Justice Network for Africa

UNCTAD – United Nations Conference on Trade and Development

VAT – Value added tax

WB – World Bank

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Chapter One

1. Introduction

1.1. Background of the study

The Economic Report on Africa by the United Nations Economic Commission for Africa advocates that foreign direct investment (FDI) is the key to solving Africa's economic problems.¹ Bodies such as the International Monetary Fund (IMF) and the World Bank (WB) have suggested that attracting large inflows of FDI would result in economic development.² Because of this and the perceived benefits that FDI is believed to bring to a host country, African countries have taken various initiatives to attract FDI.³ These initiatives include a general improvement in the investment environments like improvement of infrastructure, liberalisation of the economy and granting of various incentives one of which is tax incentives.⁴

Regarding tax incentives, which is the concern of this research, a United Nations study shows that in 1994 at least 103 countries offered tax incentives for FDI: another study revealed that in 1997, 41 new incentives were introduced.⁵ Today tax incentives are widely perceived to act as 'signals', indicating a country's receptiveness to FDI. In view of their prevalence, it is possible that their absence may even be read as a negative signal.⁶ This has led African states into a fierce tax competition in order to attract more FDI into their territory through tax incentives, the result being a huge loss of national revenue which could have been used for infrastructural development and for better delivery of public services to citizens.

¹ N Mwilima 'Foreign direct investment in Africa' in African Social Observatory Pilot Project *Foreign direct investment* (2003) 32.

² As above.

³ Increased pool of capital and revenue, employment opportunity, introduction of new skills and transfer of technology are some of the most commonly mentioned benefits that FDI is presumed to bring to a host country.

⁴ HP Ngowi 'Tax incentives for foreign direct investment (FDI): Types and who should/should not qualify in Tanzania' (2000) 1 *Tanzanet Journal* 19.

⁵ United Nations Conference on Trade and Development (UNCTAD) *World investment report 1998* 55.

⁶ A Easson *Tax incentives for foreign direct investment* (2004) 72.

Meanwhile, almost all African states are members to most international and regional human rights instruments that protect socio-economic rights. For instance, at present 48 out of the total of 53 African countries are members to the International Covenant on Economic, Social and Cultural Rights (CESCR) and all have adopted the Universal Declaration of Human Rights.⁷ All the 53 member states of the African Union are also parties to the African Charter on Human and Peoples' Rights.⁸ These three human rights instruments set the standards for the protection of socio-economic rights both at the international and regional levels. With a view to show their commitment and devotion for the protection of socio-economic rights, African states have further gone to the extent of including some of the socio-economic rights recognised by the international and regional human rights documents into their national constitutions and legislations.⁹

All in all African states have willingly committed themselves for the respect, protection and fulfilment of all socio-economic rights at the international, regional and national levels. Accordingly, African states have bound themselves, in some cases, to immediately address human rights issues and in others to take steps to the maximum of its available resources, with a view to achieving progressively the full realisation of the rights.¹⁰ Here the phrase 'available resources' is very crucial as resources include the revenue of a country. One major source of revenue for states is tax and any decision made by states on tax policy affect the revenue of the state and ultimately impact upon the realisation of socio-economic rights. Tax incentives, as part of tax policies of a state, therefore should be issue of concern when one talks about the realisation of socio-economic rights in a country. Tax incentives obviously result in reduction of government revenue consequently reducing the capital available for public services and infrastructural construction which in effect means less

⁷ F Viljoen *International human rights law in Africa* (2007) 122.

⁸ <http://www.africa-union.org> (accessed 4 September 2008).

⁹ The norms of customary international human rights law are by and large incorporated in the constitutions of African states. See C Heyns (ed) 2 *Human rights law in Africa* (2004). See also Viljoen (n 7 above) 573.

¹⁰ UN Committee on Economic, Social and Cultural Rights General Comment No 3 'The nature of state parties' obligations' 14/12/90 para 2.

revenue available for the realisation of socio-economic rights. And when the tax incentives become more generous as a result of competition to attract FDI, as it is the case in most African countries, the capital available for the protection and fulfilment of those rights also decreases to that extent.

The concern raised in this research is therefore that interstate competition is healthy up to a point but it can also reach a pitch at which the costs of competition outweigh the benefits. Not only measures taken by each state undermine the economies of the others, but states are also finding themselves caught in a 'race to the bottom' in which competitive pressures compel them each to adopt measures contrary to their citizens' interests.¹¹

It is this unchecked desperate measure by African states to attract FDI that inspired this research. This research tries to show how this unhealthy interstate competition is leading to the granting of extremely generous tax incentives which in turn affects the socio-economic conditions of African countries. It is the mission of this research to find out in what ways exactly the granting of tax incentives threatens the realisation of socio-economic rights in Africa. The research is therefore intended to expose the potential danger tax incentives pose on the respect, protection and fulfilment of socio-economic rights in African countries.

1.2. Statement of the research problem

The main problem in the deployment of tax incentives as means of attracting FDI lies in the fact that, it is driven by political reasons, not economic ones. In a political atmosphere dominated by concerns about economic vitality and jobs, elected officials face intense pressure to engage in the incentive competition. This is especially true for African countries which are under continuous internal and external political pressure because of their fragile economies and extremely high

¹¹ PD Enrich 'Saving the states from themselves: Commerce clause constraints on state tax incentives for business' (1996) 110 *Harvard Law Review* 377.

unemployment rate. Under such conditions therefore the absence of empirical evidence for the economic efficacy of tax incentives does little to quell the political enthusiasm.¹² This briefly summarises the whole politics behind tax incentives. There is not much economic benefit that African states get through tax incentives instead they lose lots of revenue.

Then what is the impact of this negligent, if not deliberate, acts of African countries on the socio-economic rights of their citizens? Are tax incentive schemes in compliance with the obligations to respect, protect and fulfil of African countries as assumed under the different international and regional human rights instruments? How do they affect the socio-economic rights of African people and how can these acts of governments be challenged using the relevant human rights instruments ratified by African countries? are the questions that this research tries to seek answer to.

1.3. Focus and objective of the study

The main objective of the study is to show how the use of tax incentives as means of attracting FDI is threatening the realisation of socio-economic rights in Africa. Particular attention is given to the discussion on how the granting of generous tax incentives can affect the proper and adequate provision of public services and infrastructures by highly reducing government revenue. The research does not intend to analyse the impact of loss of revenue through tax incentives on each and every socio-economic right. Rather the focus is on its general impact on obligations of African states to respect, protect and fulfil socio-economic rights as derived from the major international, regional and national human rights instruments.

Since tax incentives are mostly given to FDI, the research focuses only on tax incentives given to FDI, not to portfolio investments. Emphasis is also given to socio-economic rights as compared to civil and political rights because of the

¹² Easson (n 6 above) 87.

directly felt impact that tax incentives have on the realisation of socio-economic rights.

1.4. Significance of the study

The study is significant as it helps to put the ‘seemingly healthy’ and increasingly growing trend of giving untargeted and excessively generous tax incentives to the human rights test. It helps to evaluate the efficacy of tax incentives and the potential threat they pose on the realisation of socio-economic rights in Africa. In short, it can enable governments and policy makers in Africa to have a general picture of the ‘unnoticed’ negative spill over effects that tax incentives have on the welfare and wellbeing of the society and the state, so that concerned organs including the state can take appropriate measures to rectify the situation. It also helps states to reconsider and reformulate their fiscal policies in line with their international human rights obligations.

Furthermore, it gives new dimension to the struggle for the justiciability of socio-economic rights by exposing some of the reasons why African governments find themselves ‘out of cash’ to realise most socio-economic rights. Since it is also a new area of research, it helps to stimulate other human rights scholars to research and reflect their views on the topic.

1.5. Research methodology and limitations

The research is mainly a library and desktop based research. It involves an analytical exploration of primary and secondary sources. Different treaties, books, reports, data, websites and internet sources are used as an input in the research. Because of time constraints the research mostly relies on secondary sources than primary sources.

The research limits itself to the macro-study and analysis of the impact of tax incentives on Africa as a whole and does not look into individual cases

because of lack of resources and time.¹³ However, examples from different African countries are used to illustrate and substantiate the different points made in the research work.

1.6. Literature review

Most scholarly writings in the area of tax incentives and FDI are written by economists and tax lawyers who by and large write about the economic aspect of the issue. The writer has not come across with a single publication which tries to approach the topic from human rights perspective.

But scholars like Alex Easson¹⁴ have tried to touch upon the issue, though from a different angle. Easson in his book entitled 'Tax incentives for foreign direct investment' asserts the position taken by most international organisations like International Monetary Fund (IMF) by saying that states are advised to avoid introducing tax incentives as means of attracting FDI. In doing so he shows how tax incentives affect the revenue of a country and the distortive effect that they have on business decisions. But Easson's main objective is to suggest better ways of utilising tax incentives so as to make the host state beneficiary; and never approaches the matter from human rights perspective. So, at least in this respect this research is original.

A relatively closer approach to the topic the writer raises in this research is followed by Peter Enrich in his article published in Harvard Law Review in which he argues that American states are engaged in interstate competition by providing tax incentives for businesses to locate in-state.¹⁵ He argues that these state location incentives harm the states and their citizens. But Enrich concludes by proposing ways of using the American Commerce Clause to stop what he calls

¹³ Case study on this topic requires looking into tax incentive schemes of a country, analyzing it and estimating its cost and then studying it against the government's budget. Much of this task demands expertise in economics (which the writer does not have) and access to government's budget breakdown (needs relatively longer period) to come up with something tangible. However, what the writer does is draw its conclusions based on available information, data and facts which clearly substantiate the hypothesis of the research.

¹⁴ Easson (n 6 above).

¹⁵ Enrich (n 11 above).

‘second Civil War’ between states. So, he approaches the matter as a purely business issue and domestic affair. But it cannot be denied that the approach taken by Enrich has helped the writer, to some extent, to shape the research the way it is now.

One issue, however, remains the same; the research approaches the issue of tax incentives from a completely different and genuinely new perspective which is human rights.

1.7. Overview of chapters

By considering the word limits and with a view to lay a clear structure this work is divided into five chapters.

Chapter one: presents the background of the study and the justification. It points to the focus, objectives, methodology and limitations of the work.

Chapter two: explains the role of tax incentives in attracting FDI in Africa. In the process the chapter also defines tax incentives and explains the commonly used types of tax incentives by states.

Chapter three: discusses the socio-economic rights obligations that African states have assumed at international, regional and national levels. This chapter clearly lays down the obligations assumed by and conducts expected from African states under the CESC, Universal Declaration, African Charter and their respective national constitutions.

Chapter four: goes on to expose the development or human rights protection dilemma that most African countries find themselves in as a result of tax incentives. The impending and actual danger that tax incentives are causing and are likely to cause for the realisation of socio-economic rights in Africa is assessed.

Chapter five: concludes and gives recommendations based on the findings of the research work.

Chapter Two

2. Tax incentives and their effect on FDI inflow to Africa

2.1. Introduction

Over the past two decades, most governments have been actively promoting their countries as investment locations to attract scarce private capital and associated technology and managerial skills in order to help achieve their development goals. They have increasingly adopted measures to facilitate the entry of FDI. Examples of such measures include liberalizing the laws and regulations for the admission and establishment of foreign investment projects; providing guarantees for repatriation of investment and profits; and establishing mechanisms for the settlement of investment disputes. Tax incentives are also part of these promotional efforts.¹⁶

Tax incentives have become a global phenomenon as more and more governments try to attract multinational companies and enhance the associated technology spillovers. Although hardly new, this trend appears to have strengthened since the early 1990s.¹⁷ Consequently, using the tax system to influence economic behavior by granting tax incentives for particular activities has developed several literatures following the lead of Professor Stanley Surrey.¹⁸ Now there is abundant literature especially on the question of whether tax incentives are decisive in influencing the location of FDI, which is also one issue that is addressed in this work. But before engaging upon such topic it is important to have a common understanding as to what tax incentives are and their types.

2.2. Defining tax incentives

While trying to find an answer as to what tax incentives are, one may come across with correlated terms like investment incentive, fiscal incentive or financial (monetary)

¹⁶ United Nations Conference on Trade and Development *Tax incentives and foreign direct investment: A global survey* (2000) 11.

¹⁷ J Morisset 'Tax incentives: Using tax incentives to attract foreign direct investment' *View point The World Bank Group* January 2003 1.

¹⁸ D Holland & RJ Vann 'Income tax incentives for investment' in V Thuronyi *Tax law design and drafting* (1998) 1.

incentives. So, it is more than appropriate at this point to be able to clearly situate the place and distinctive characters of tax incentives amidst the others.

Investment incentives can take a variety of forms but are usually classified as either financial incentives or fiscal incentives.¹⁹ Financial incentives usually take the form of grants or loans on preferential terms to assist in the acquisition of capital assets. Alternatively, the host government may agree to bear part of the costs involved in establishing the operation, for example, providing infrastructure, or training workers.²⁰ The tendency is for developed countries to use financial incentives in preference to fiscal incentives: by contrast, developing countries are more inclined to offer tax incentives, often because the funds simply are not available to make an up-front cash grant or loan.²¹

Thus, while investment incentives is a broad concept including financial and fiscal incentives, tax incentives is relatively narrow as it is just one type of fiscal incentives. Tax incentives, as it can be understood from the term itself, operates through the tax system and confer benefits in the form of reductions in the tax that would otherwise be payable. Looking at the definition of tax incentives may give us a clearer picture.

Alex Easson and Eric Zolt define tax incentives as²²

...those special exclusions, exemptions, or deductions that provide special credits, preferential tax rates or deferral of tax liability. Tax incentives can take the form of tax holidays for a limited duration, current deductibility for certain types of expenditures, or reduced import tariffs or customs duties.

In explaining the reality surrounding their definition, Easson and Zolt concede to the fact that sometimes it could be hard to make the distinction between special and general provisions. This is to mean though at times it is easy to identify tax

¹⁹ According to Easson there are also measures of a non-financial nature that are sometimes listed as investment incentives in promotional literature issued by foreign investment agencies and which often have impact on investment decisions. These are sometimes referred to as 'rule-based' incentives (as opposed to monetary incentives), and include such measures as the relaxation – for qualifying investors – of the normal residence permit or work permit rules, of restrictions on capital transfers, or even of minimum pay and worker protection legislation. Easson (n 6 above) 1-2.

²⁰ Easson (n 6 above) 2.

²¹ As above.

²² A Easson & EM Zolt 'Tax incentives' (2002) 3.

incentives, in other times it can be difficult to distinguish between provisions that are deemed to be part of the general tax structure and those that provide special treatment. This distinction they say will become even more important as countries may be limited in their ability to adopt targeted tax incentives.²³

With a view to avoid the abovementioned problem Zee, Stotsky and Ley define tax incentives in a more comprehensive way by making a clear distinction between tax incentives provisions and generally applicable tax provisions as follows:²⁴

A tax incentive can be defined either in statutory or effective terms. In statutory terms, it would be a special tax provision granted to qualified investment projects(however determined) that represents a statutorily favorable deviation from a corresponding provision applicable to investment projects in general (i.e. projects that receive no special tax provision). An implication of this definition is that any tax provision that is applicable to all investment projects does not constitute a tax incentive. In effective terms, a tax incentive would be a special tax provision granted to qualified investment projects that has the effect of lowering the effective tax burden that would be borne by investors in the absence of the special tax provision.

Therefore, it is important to make a distinction between provisions that are specific and those that are part of the general system. This is sometimes difficult and may even not be possible. A tax could be structured in such a way that there is no benchmark from which departures are made. For example, a country might be divided into a number of zones, in each of which a different tax rate is imposed. In other cases, the benchmark may actually be the exception rather than the rule.²⁵

From the above two definitions we can see that not all statutory tax incentives are necessarily effective in reducing an investor's tax burden and the common feature of both statutory and effective tax incentives is that they are special, not general. Thus, for example, a generous depreciation system offered to all investors is not an

²³ As above.

²⁴ HH Zee et al 'Tax incentives for business investment: A primer for policy makers in developing countries' (2002) 14.

²⁵ Easson (n 6 above) 3. See also A Easson ' State aid and the Primarolo List' (2001) 5 *EC Tax Journal* 109; C Pinto ' EC Sate aid rules and tax incentives' (1999) 39 *European Taxation* 295; W Schon 'Taxation and state aid law in the European Union' (1999) 36 *Common Market Law Review* 911.

incentive in the sense used here, even though it might benefit some type of investors more than others. In this work, ‘incentive’ will be used in the statutory sense, regardless of whether it is effective in practice.

2.3. Types of tax incentives

Tax incentives are of different types. They can be given in the form of reduced corporate income tax, exemption from payment of tax for a limited or unlimited period of time or accelerated depreciation on capital assets. Or states may also decide to reduce sales tax, value added tax (VAT), import tax or customs duties. Whatever form they may take or in whatever name they are called, they fall under a general category of tax incentives as long as they are provided with the intention to reduce the tax burden of investors and of course as discussed before they should be special. Under this section those incentives that can be considered tax incentives according to our definition are discussed.

3.3.1. Reduced corporate income tax rates

Governments may set exemptions from, or reduce rates of corporate income or profits tax in order to attract FDI into specific sectors or regions.²⁶ Complete exemption is usually reserved for enterprises operating in the offshore sector or located in export processing zones. For example, Mauritius exempts companies located in the export processing zone and in the ‘freeport’, and also exempts most types of offshore businesses.²⁷ Reduced corporate income tax rates are widely used as an incentive applicable to certain types of promoted activity or to the income therefrom. In Ghana for instance the standard rate of 32.5 percent is reduced to 25 percent for hotels and to 8 percent for income from non-traditional exports.²⁸

²⁶ UNCTAD (n 16 above) 19.

²⁷ Easson (n 6 above) 133.

²⁸ As above.

3.3.2. Tax holidays

Tax holidays are a common form of tax incentives used by developing countries and countries in transition to attract FDI. They are also perhaps the most abused and certainly the most frequently criticized form of tax incentives. Under tax holidays qualifying 'newly-established firms' are exempt from paying corporate income tax for a specified time period.²⁹ The provisions may exempt firms from other tax liabilities as well. Tax holidays eliminate tax on net revenues from investment projects over the holiday period.³⁰ Tax holidays can vary from as little as one year to as long as 20 years.³¹ More than two-third of African countries provide tax incentives for FDI.³²

3.3.3. Investment allowances

Investment allowances are deductions from taxable income based on some percentage of new investment. They tend to lower the effective price of acquiring capital. It is given as a specified percentage of qualifying investment expenditures. Investment allowances may apply to all forms of capital investment or they may be restricted to specific categories, such as machineries or technologically advanced equipments, or to capital investment in certain activities, such as research and development.³³ The allowance is usually expressed as a percentage of the qualifying investment. In Kenya, for example, a full 100 per cent allowance is given for qualifying investment. In South Africa the allowance varies from 50 to 100 percent.³⁴

3.3.4. Investment tax credits

An investment allowance reduces taxable income, whereas an investment tax credit is set against the tax payable: thus, for example, if the relevant corporate income tax rate

²⁹ Usually tax holidays provide an exemption for or reduction in the corporate income tax rate or provide for a period of complete exemption followed by a further period during which the rate is reduced-usually by 50 percent.

³⁰ UNCTAD (n 16 above) 19.

³¹ Easson & Zolt (n 22 above) 19.

³² S Gupta & S Tareq 'Mobilising revenue' *Finance and development* September 2008 46.

³³ UNCTAD (n 16 above) 20.

³⁴ Easson (n 6 above) 143.

is 40 per cent, an investment allowance of 50 per cent of the amount invested equates to an investment credit of 20 per cent of that amount.³⁵

In some countries, investment tax credits may only be claimed in the year they are earned. Typically, however, unused credits may be carried forward for a limited number of years to offset future tax liabilities. As in the case of investment allowance, they are meaningful to firms only if they can be carried forward or backward. Another option is to make unused credits refundable – that is allow their value to be claimed in cash in the year earned.³⁶

3.3.5. Reinvestment allowances

Some countries provide incentives for the reinvestment of profits. This can be done in two ways. First, the tax liability of the enterprise itself can be reduced by allowing a deduction for the amount reinvested (or a proportion thereof) from the profits otherwise taxable. Second, the shareholder, or parent company, can be given a refund of the tax paid by the local enterprise up to a stated proportion of the amount reinvested (whether in the original enterprise that made the profit or in some other qualifying enterprise).³⁷

3.3.6. Deductions for qualifying expenses

It provides for favorable rules for the deduction of certain types of expenditures incurred. Some countries allow more than full deduction for tax purposes of qualifying expenses. For example, they may allow double deduction of training expenses, research and development, or export marketing expenses.³⁸ This type of incentive may be considered together with measures to encourage investors to retain funds for longer periods.

³⁵ Easson (n 6 above) 144.

³⁶ UNCTAD (n 16 above) 21.

³⁷ Easson (n 6 above) 146.

³⁸ UNCTAD (n 16 above) 22.

3.3.7. Accelerated depreciation

The term ‘accelerated depreciation’ generally refers to any depreciation scheme that provides for writing off the cost of an asset, for tax purposes, at a rate faster than the true economic depreciation. Many countries use some type of ‘declining balance’ method of depreciation or other type of accelerated depreciation as part of their benchmark tax system.³⁹ For those countries, however, that do not generally provide accelerated depreciation, a tax incentive can provide for deducting the cost of acquisition more quickly than would be allowed under the normal ‘benchmark’ depreciation schedules.⁴⁰ It is in this latter sense that the term is used here, since what we are considering are tax incentives – that is, tax provisions that are more advantageous than the normal benchmark tax system. Whether a country has a normal depreciation regime that is generous and thus encourages investment, is another question: the issue here is whether it provides a special (more favorable) depreciation regime that is available to some, but not all, investors or investments.

3.3.8. Reduced withholding taxes

It is not uncommon for countries to provide reduced or zero rates of withholding tax as an incentive for FDI, either generally or to promote particular objectives such as the transfer of technology.⁴¹ Exemption from withholding tax is sometimes given in the case of interest on loans made at preferential rates or in the case of royalties or technical assistance fees paid in respect of technology transfers. It is also quite common for dividends paid out of exempt profits – for example, profits earned during a tax holiday period – to be exempt from withholding tax.⁴²

The other types of tax incentives that are used by states to attract FDI are preferential treatment of long term capital gains, zero or reduced tariffs, employment based deductions, tax credits for value additions and tax reductions or credits for

³⁹ Easson & Zolt (n 22 above) 22.

⁴⁰ As above.

⁴¹ As above.

⁴² As above.

foreign hard currency earnings.⁴³ But they are not discussed here because they are not commonly employed by most African countries as means of attracting FDI.

At this juncture one may ask how effective tax incentives are in attracting FDI. The next section tries to address this issue.

3.4. Effect of tax incentives on FDI inflow to Africa

As a result of aggressive competition among states to attract FDI, tax incentives have now become a global phenomenon.⁴⁴ In 1996 it was reported that some 103 countries offered tax incentives for FDI. This number has surely increased since then as each year around 30 – 40 new incentives are introduced.⁴⁵ However, despite its increasing popularity, expert opinion and the advice offered by international bodies to the governments of developing nations firmly opposes the use of tax incentives as means of attracting FDI.

The role of incentives in promoting FDI has been the subject of many studies. There have been some spectacular successes as well as notable failures in their roles as facilitators of FDI. The literatures and studies conducted also suggest the same. Supporters of tax incentives argue that under certain conditions, tax incentives increase investment, create jobs and other socio-economic benefits.⁴⁶ And opponents believe that tax incentives may not be the first-best mechanism for attracting FDI and the costs of incentives to attract FDI outweigh the benefits. They believe that incentives may exacerbate problems like governance and corruption and it would be better to improve the local infrastructure and stabilize the macro-economy.⁴⁷

⁴³ See UNCTAD (n 16 above) 19-22. Easson and Zolt also list a number of other tax incentives in addition to the ones discussed but except the difference in names they refer to the same thing.

⁴⁴ J Morisset & N Pirnia 'How tax policy and incentives affect foreign direct investment: A review' (2001) 1.

⁴⁵ United Nations Conference on Trade and Development *Incentives and foreign direct investment* (1996) 5.

⁴⁶ E Cleeve 'How effective are fiscal incentives to attract FDI to sub-Saharan Africa' (2006) 7. See also M Blomstrom & H Kokko 'The economics of foreign direct investment incentives' NBER Working Paper, No 9489 2003 and B Bora 'Investment Distortions and the International Policy Architecture' World Trade Organisation Working Paper Geneva 2002.

⁴⁷ As above. See also R Halvorsen, 'Fiscal incentives for investment in Thailand' in A Shah (ed) *Fiscal incentives for investment and innovation* (1995); C Osman 'Policy competition for foreign direct investment: A study of competition among governments to attract FDI' OECD 2000; J Wilson 'The tax treatment of imperfectly mobile firms: Rent seeking, rent protection, and rent destruction' in R Feenstra et al (eds) *The political economy of Trade policy: Papers in Honour of Jagdish Bhagwati* (1996) & LT Wells 'Using tax

Many least developed countries including African countries have provided investment incentives to entice MNCs to locate in their economies but have achieved little success in generating the expected investment flows. This experience over a number of years suggests that fiscal incentives have not been effective in countering factors that work against locating in the sub-Saharan region, such as poor physical and institutional infrastructures and economic stability.⁴⁸ Therefore, as factors intended to attract FDI, incentives are of secondary importance.

As the global survey conducted by UNCTAD indicates tax incentives are only secondary to more fundamental determinants, such as market size, access to raw materials and availability of skilled labor. The survey shows that investors generally tend to adopt a two-stage process when evaluating countries as investment locations. In the first stage, they screen countries based on their fundamental determinants. Only those countries that pass these criteria go to the next stage of evaluation where tax rates, grants and other incentives may become important. Thus, it is generally recognised that investment incentives have only moderate importance in attracting FDI.⁴⁹

As mentioned earlier most tax incentives are based on tax holidays and other instruments designed to reduce the effective rate of corporate tax. But such tax incentives increase investment flows only if projects are sensitive to differential taxation and it is very difficult in practice to correctly select such projects.⁵⁰ Furthermore, in many cases, it is the most profitable investments that are most likely to receive incentives even though these projects could have been undertaken in the absence of incentives.⁵¹

For many least developed countries (LDCs), particularly African countries, the bulk of FDI originates from the United Kingdom, United States, Germany and France;

incentives to compete for foreign investment: Are they worth the cost?' Foreign Investment Advisory Service Washing World Bank 2001.

⁴⁸ Cleeve (n 46 above) 8.

⁴⁹ UNCTAD (n 16 above) 11.

⁵⁰ Cleeve (n 46 above) 9.

⁵¹ As above.

countries that provide their firms investing abroad with foreign tax credits.⁵² Therefore, a lower tax rate in African countries will be directly offset by a higher rate in the investing country.⁵³ As a result, fiscal incentives lose their attractiveness for foreign firms to increase investments since lower African taxes may be offset one-to-one in these countries. Tax incentives of this type do not increase investment. In fact this type of incentive only results in the transfer of revenue from Africa to the richer home countries.⁵⁴

It can be inferred from the foregoing discussion that the significance of tax incentives on FDI location depends on:⁵⁵

- (i) 'The source of FDI; if the investment is from advanced economies like the USA, UK, France and Germany, where home firms are offered foreign tax credit, such incentives will have very little effect on the firms' location decision. Most investments in Africa come from these countries, so it is very unlikely for African countries to attract FDI using tax incentives.
- (ii) The type of project; short-term, footloose investments, such as banking, insurance, internet, and others benefit most from fiscal incentives, especially tax holidays. Most investments in Africa are long-term, such as mining and agricultural projects. Therefore, providing tax incentives in such cases does not make any difference as the companies are going to invest whether the incentive is there or not.
- (iii) The motivation for the investment; if investment is natural resource or market seeking, fiscal incentives could only be a relatively minor determinant of FDI inflows. Most investments in Africa are on natural resources.'

⁵² For Sub-Saharan Africa in the period 1996-2000, 78% of all FDI inflows to Africa comes from these four countries, with the USA alone accounting for 37% of the total.

⁵³ V Tanzi & H Zee 'Tax policy for emerging markets: Developing Countries' IMF Working Paper (2000) 35.

⁵⁴ KL Fletcher 'Tax Incentives in Cambodia, Lao PDR, and Vietnam' International Monetary Fund (2002) 5.

⁵⁵ Cleeve (n 46 above) 11.

Therefore, as an investor who was interviewed on the issue of incentives and FDI put it ‘tax exemption is like a dessert, good to have, but it does not help very much if the meal is not there’.⁵⁶ This briefly summarizes the answer to the question raised at the beginning of this section. In general the effect of tax incentives on FDI is rather limited, at least compared to other factors such as political stability, the costs and availability of labor and basic infrastructure. The importance of these other factors suggests that tax policy is a poor instrument to compensate for various negative factors in the investment climate of a country.

3.5. Conclusion

Many African countries have offered investment incentives for business to locate in underdeveloped, more costly and otherwise unattractive regions with little success in generating sustainable investment flows to those areas.⁵⁷ This experience strongly suggests that the fiscal investment incentives popular in developing countries have not been effective in making up for fundamental weaknesses in the investment climate.

Fiscal incentives could be a significant determinant of FDI inflows to Africa, if investment is efficiency seeking or strategic asset seeking, but only a few African countries possess locational factors that would attract these types of FDI like South Africa and Mauritius.⁵⁸ Because of this tax incentives are not helping African states to attract FDI and hence are not recommendable except in some carefully studied sectors and investments. As the IMF and WB recommended, it is better for African countries to focus on the improvement of their infrastructure and other services to attract FDI than providing tax incentives.

⁵⁶ Morisset & Pirnia (n 44 above) 5.

⁵⁷ Morisset & Pirnia (n 44 above) 7-8.

⁵⁸ Cleeve (n 46 above) 11.

Chapter 3

3. The protection of socio-economic rights in Africa

3.1. Introduction

Under this chapter an attempt is made to find out the human rights commitments assumed by African states with specific reference to provisions in treaties ratified by African states which have direct relevance to the issue of tax incentives. For this purpose, emphasis is given to socio-economic rights because of the direct impact tax incentives have on the realisation of these rights. Having this objective in mind first the socio-economic rights related obligations of African states under different international and regional human rights treaties are discussed. In the next part further investigation is made into the national constitutions of African states to show how far most African states have gone to comply with the human rights treaties that they have ratified.

Most treaties – international or regional – ratified by African countries and their constitutions recognize and protect a wide variety of rights: from civil and political rights to socio-economic rights and sometimes developmental rights; from individual to collective rights.⁵⁹ Socio-economic rights as one group of rights recognized in both international and regional treaties and domestic constitutions and legislations are discussed in the coming section.

3.2. The socio-economic rights obligations of African states

Although their justiciability both at international and national levels is still a highly debatable issue, socio-economic rights have managed to get considerable recognition since the Cold War.⁶⁰ There is no universally agreed upon list of rights that belong to such category of rights but there seems to be a common understanding among

⁵⁹ See Universal Declaration of Human Rights (Universal Declaration) of 1948; International Covenant on Civil and Political Rights (CCPR) of 1966; International Covenant on Economic, Social and Cultural Rights (CESCR) of 1966; African Charter on Human and Peoples' Rights (African Charter) of 1981. To have a general idea as to the human rights content of African countries' constitutions see C Heyns & W Kanguongo 'Current developments: Constitutional human rights law in Africa' (2006) 22 *South African Journal of Human Rights* 673.

⁶⁰ I Currie & J de Waal *The Bill of Rights handbook* (2005) 567-568.

scholars that the rights that are included under the Universal Declaration of Human Rights and as they were later elaborated and supplemented by the International Covenant on Economic, Social and Cultural Rights (CESCR) provide a complete list of socio-economic rights. The rights under the two documents relate to the conditions that are necessary to meet basic human needs such as food, shelter, education, health care and gainful employment.⁶¹ They include the rights to education, adequate housing, food, water, the highest attainable standard of health, the right to work and rights at work, as well as the cultural rights of minorities and indigenous peoples. Together they set the standards for the protection of socio-economic rights at the global level.

3.2.1. At global level

There are a number of international human rights instruments ratified by most African countries which protect socio-economic rights.⁶² But the major international documents from which the socio-economic rights obligations of African states at the global level emanate from are the Universal Declaration and CESCR. In the coming sections a brief discussion on the extent and nature of protection of socio-economic rights under these two documents is made.

c. Universal Declaration of Human Rights

The Universal Declaration is the first international document which came with a full catalogue of human rights: civil and political rights as well as economic, social and cultural rights.⁶³ The economic, social and cultural rights provided from article 22 to

⁶¹ Amnesty International USA 'Economic, social and cultural rights' <http://www.amnestyusa.org/economic-social-cultural-rights/page.do?id=1011006&n1=3&n2=29> (accessed 5 September 2008)

⁶² These instruments include: the Convention on the Rights of the Child (CRC) of 1989, the Convention on the Elimination of All Forms of Discrimination against Women (CEDAW) of 1979, the International Convention on the Elimination of All Forms of Racial Discrimination (CERD) of 1965 and the International Convention on the Protection of the Rights of All Migrant Workers and Members of their Families (CPMWF) of 1990. C Mbanzira 'A path to realizing economic, social and cultural rights in Africa: A critique of the New Partnership for Africa's Development' (2004) 4 *African Human Rights Law Journal* 34.

⁶³ However, it should be noted that the American Declaration of the Rights and Duties of Man, which was approved a few months before the Universal Declaration had took in economic, social and cultural rights. JO Oraa 'Universal Declaration of Human Rights' in FG Isa & K de Feyter (eds) *International protection of human rights: Achievements and challenges* (2006)100.

27 of the Universal Declaration include the right to standard of living adequate for the health and well-being of oneself and one's family, including food, clothing, housing and medical care and other necessary social services.⁶⁴ They also include the right to social security.⁶⁵

All the other provisions of the Universal Declaration on economic, social and cultural rights elaborate the abovementioned rights except article 23 and 24. Article 23 talks about the right to work which includes not only a favorable working environment and protection against unemployment but also equal pay for equal work.⁶⁶ Similarly, article 24 addresses the issue of reasonable limitation of working hours and leave with pay as part of the right to rest and leisure. The other socio-economic right protected under the Universal Declaration is the right to education. It is clearly provided that at least primary education should be for free. At this juncture one may ask, how the state is supposed to protect these rights and what the nature of its obligation is, if any.

The state is expected to organize its national resources and work for the realization of the rights. And whenever the resources that a state has domestically are not enough for the realization of the rights, the next option would be to resort to international cooperation and assistance.⁶⁷ The state is expected to make an effort to fulfil the socio-economic rights of its population. So, in providing the basic infrastructures like schools, hospitals, roads or other public services which are indispensable for the realization of the rights as incorporated under the Universal Declaration, the state should first look into its resources and make the best effort possible to utilize the same to the maximum possible in order to properly discharge its obligations.⁶⁸

⁶⁴ Universal Declaration art 22 & art 25.

⁶⁵ The right to social security as provided under the Declaration includes security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond ones control. Universal Declaration art 25(1).

⁶⁶ Universal Declaration art 23.

⁶⁷ Universal Declaration art 22.

⁶⁸ Oraa (n 63 above) 103.

Here the question that we have to answer is whether African states are parties to the Universal Declaration? and if they are, what is the nature of their obligation under such document? or to what extent are they abide by the instrument?

Even though by the time the Universal Declaration was adopted, most African states were still under colonial rule and hence were not part of the adoption process, now all are parties to the Universal Declaration.⁶⁹ This means the Universal Declaration is applicable to all of them. But again the nature of their obligation under the Universal Declaration is another issue.

The legal nature of the Universal Declaration is a complex issue, which has provoked, and continues to provoke, a certain amount of controversy among the international community. By only considering that the Universal Declaration is not a treaty, one may conclude that it is not *per se* a legally binding document for those states which are parties to it⁷⁰ and thus African states are not bound by it. However, despite the character the Universal Declaration had when it was approved, it can be safely concluded that in the decades following 1948 the document has undergone a significant transformation as regards its legal value. It is now an instrument which creates legal obligations for member states of the UN.⁷¹ It is also argued that the Universal Declaration has attained the status of customary international law.⁷² But again it is said that not all but only some of the provisions of Universal Declaration have reached that status and those are the civil and political rights, not the socio-economic ones.⁷³

In some cases, however, economic, social and cultural rights are better supported in the international community than some of the civil and political rights.⁷⁴ Moreover, making such a distinction between civil and political rights on the one hand

⁶⁹ <http://www.un.org/events/humanrights/udhr60/declaration.shtml> (accessed 1 September 2008).

⁷⁰ Oraa (n 63 above) 117. The Universal Declaration was adopted by the General Assembly of the United Nations as a resolution, and, therefore, in accordance with the UN Charter art 13, it is a recommendation with no legal force.

⁷¹ Oraa (n 63 above) 119.

⁷² J Dugard *International law: A South African perspective* (2005) 315.

⁷³ As above.

⁷⁴ Some of the economic, social and cultural rights that are soon expected to attain the status of customary international law are the right to free choice of employment, the right to form and join trade unions, and the right to free and accessible primary education.

and economic, social and cultural rights on the other would contradict the current trend on human rights, which insists that human rights are ‘universal, indivisible and interdependent and interrelated. The international community must treat human rights globally in a fair and equal manner, on the same footing, and with same emphasis’⁷⁵.

On top of that it should be remembered that as it was declared by the Proclamation of Teheran in 1968:⁷⁶

The Universal Declaration of Human Rights states a common understanding of the peoples of the world concerning the inalienable and inviolable rights of all members of the human family and constitutes an obligation for the members of the international community.

So, every member of the UN is bound to respect and protect the provisions of the Universal Declaration. It is a contract between governments and their people and therefore the people have the right to demand for their rights under the Universal Declaration to be respected.⁷⁷ Based on this, African people can also demand for their rights guaranteed under the Universal Declaration whenever the need arises and the government is also duty bound to respond to that.

d. International Covenant on Economic, Social and Cultural Rights

‘The CESCR is one of the two human rights treaties that converted the lofty ideals elaborated in the Universal Declaration into binding state obligations.’⁷⁸ In its attempt to realize social justice, the document covers a wide scope of rights from the right to work, to form trade unions, social security, to achievement of adequate standard of living, health, education...⁷⁹ The Covenant as well sets minimum and concrete duties and obligations as regards economic, social, and cultural rights, which the state and the international community have the duty to respect.

⁷⁵ Vienna Declaration and Program of Action adopted on 25 June 1993 para 5.

⁷⁶ Dugard (n 72 above) 315. The Proclamation of Teheran of 1968 was adopted by 84 states.

⁷⁷ <http://www.un.org/events/humanrights/udhr60/declaration.shtml> (accessed 1 September 2008).

⁷⁸ Viljoen (n 7 above) 120.

⁷⁹ See CESCR.

Some of the state obligations are those that can be justifiably and immediately put into effect.⁸⁰ Others are to be progressively realized in the sense that states are expected to take targeted and concrete steps towards their full realization. State parties in taking such measures are obliged to act to the maximum of their available resources.⁸¹ As a treaty these obligations set under the Covenant are undoubtedly binding on member states.

Currently, forty-eight African countries are member states to CESCR⁸² and are therefore bound to implement the provisions of the Covenant immediately or progressively depending on the nature of the obligation. To this effect they should be able to use their available resources as effectively and efficiently as possible. They must at least meet the minimum core obligations expected from them and should make an effort to use all resources that are at their disposal in an effort to satisfy, as a matter of priority, those minimum obligations.⁸³ Although nine African countries have made reservations and interpretive declarations while ratifying the Covenant, none of those reservations or interpretive declarations qualify the nature of obligation provided under the Covenant.⁸⁴ Therefore, it is possible to say that African states are willing to immediately or progressively realize their obligations under the Covenant to the ‘maximum of their available resources’.

Cumulatively, therefore, the Universal Declaration and CESCR put African states under a binding legal obligation to meet the economic, social and cultural needs of their society by making maximum use of their resources. The two instruments also entitle African people to claim their rights from their respective governments whenever they are denied of their basic needs, infrastructures or social services.

⁸⁰ General Comment No 3 para 5.

⁸¹ General Comment No 3 para 1.

⁸² Viljoen (n 7 above) 122. See also <http://www2.ohchr.org/english/bodies/ratification/3.htm> (accessed 15 May 2008).

⁸³ General Comment No 3 para 1.

⁸⁴ Viljoen (n 7 above) 122-123.

3.2.2. At regional level

The African regional human rights system has been developed under the auspices of the Organization of Africa Unity (OAU), which was transformed in 2001 into the African Union (AU).⁸⁵ Unlike under the new AU, with its promising commitment to the promotion and protection of human rights, the question of human rights did not feature prominently on the agenda of the OAU following its creation 1963.⁸⁶ While article 2(1)(e) of the OAU Charter declared as one of the OAU's goals that member states should 'promote international cooperation, having due regard to the charter of the United Nations and the Universal Declaration', it took almost two decades before the assembly of Heads of State and Governments was prepared to adopt the African Charter on Human and Peoples' Rights (African Charter) in 1981 and came into force in 1986.⁸⁷

The African Charter is now the principal human rights instrument for the protection of human rights on the African continent. The African Charter recognizes a wide variety of human rights norms. It recognizes political and civil rights to socio-economic rights, individual and collective rights. The Charter is also unique for including duties together with rights. It is therefore under this Charter that the socio-economic rights of the African people are mainly protected at the regional level.

The African Charter guarantees the enjoyment of some major socio-economic rights.⁸⁸ What is more is that the Charter does not make any distinction between the two generations of rights and makes both groups of rights equally justiciable. By doing so it does not only strive to change the dire poverty and exploitation by the elites but it also acknowledges that accountability through the law forms part of the solution.⁸⁹

⁸⁵ C Heyns & M Killander 'The African regional human rights system' in FG Isa & K de Feyter (eds) *International protection of human rights: Achievements and challenges* (2006) 510-511.

⁸⁶ GJ Naldi 'Future trends in human rights in Africa; The increased role of the OAU?' in M Evans & R Murray (eds) *The African Charter on Human and Peoples' Rights: The system in practice 1986-2000* (2002) 1.

⁸⁷ M du Plessis 'The African Union' in Dugard (n 72 above) 557.

⁸⁸ The right to work under equitable and satisfactory conditions(article 15); the right to receive equal pay for equal work (article 15); the right to enjoy the best attainable state of physical and mental health including medical care for the sick (article 16); the right to education(article 17); the right to freely take part in the cultural life of one's community (article 17); and the right of women, children, the aged and the disabled to special measures of protection in keeping with their physical or moral needs (article 18).

⁸⁹ Viljoen (n 7 above) 237.

One frequently mentioned gap on the African Charter with regard to socio-economic rights is it includes only a few socio-economic rights as compared to the Universal Declaration and CDESCR. Some of the major socio-economic rights not provided in the Charter are the right to food, water, social security and housing. However, the African Commission on Human and Peoples' Rights (African Commission) has managed to fill this gap in its jurisprudence to ensure that these unwritten socio-economic rights are protected through the means of other socio-economic rights that are codified in the Charter.⁹⁰

In general, the African Charter together with the precedents set by the African Commission afford a better protection for the socio-economic rights of the African people regionally. Moreover, the fact that the African Charter puts civil and political rights on equal footing with socio-economic rights makes their justiciability easier. What is more is that all 53 members of the AU are parties to the African Charter and thus all of them have the obligation to respect, protect and fulfill the socio-economic rights of the people residing within their territories. And of course the people also have the respective right to demand the respect, protection or fulfillment of their rights whenever the state fails to meet its obligations under the Charter.

The obligations of African states and the rights of their people with regards to socio-economic rights is further strengthened by other regional human rights instruments. These additional regional human rights instruments that concretize the respective obligations and rights of states and its citizens are the Protocol on the Rights of Women⁹¹ and African Children's Charter⁹².

⁹⁰ For example, the Commission has found that the starvation of prisoners violated art 16's guarantee of the right to enjoy the best attainable state of physical and mental health, and it has decided that forcibly evicting persons from their homes amounted to a violation the right to property guaranteed in art 14. Depriving persons of basic services such as drinking water, electricity and basic medicine has also been characterized by the Commission as a violation of art 16. Du Plessis (n 87 above) 560.

⁹¹ Protocol to the African Charter on Human and Peoples' Rights on the Rights of Women adopted on 11 July 2003 and entered into force on 25 November 2005 arts 12, 13, 14, 15, 16, 17 & 18.

⁹² African Charter on the Rights and Welfare of the Child adopted on 11 July 1990 and came into force on 29 November 1999 arts 1, 11, 12, 13, 14 & 15.

3.2.3. At national level

We have now reached a stage where all the 53 African countries have written constitutions and all of them in one way or another recognize the concept of human rights in their constitutions. In fact except the Constitutions of Cameroon and Comoros, which give recognition to human rights only in their Preambles, all the other African constitutions recognize human rights in their bills of rights and in some cases also in directive principles of state policy and similar sections.⁹³ In addition to the bill of rights, a number of African constitutions have as well provisions which make international human rights treaties ratified by the state to be part and parcel of the law of the land. This in effect makes the states' obligation stronger as at least in principle they can be enforced before domestic courts.

What is interesting is that the bills of rights accommodate both civil and political rights and economic, social and cultural rights. Of course it cannot be denied that the civil and political rights are more popular than the socio-economic ones.⁹⁴ But still numerous African constitutions provide for at least some justiciable socio-economic rights. According to Viljoen 'geographically, the reach of justiciable socio-economic rights in Africa is already quite wide'.⁹⁵

Coming to the specific socio-economic rights protected under the constitutions, researches show that the right to work⁹⁶, education⁹⁷ and protection of the family⁹⁸ are

⁹³ Heyns & Kanguongo (n 59 above) 677.

⁹⁴ Heyns & Kanguongo (n 59 above) 683.

⁹⁵ Simply looking at Algeria (an arabophone country with an Islam-based legal tradition), Benin and Burkina Faso (francophone countries belonging to the civil law family), Cape Verde and Mozambique (lusophone countries also part of the civil law family), and South Africa (an anglophone common law country) which all include numerous socio-economic rights in their constitutions, enable us to buy the assertion. Viljoen (n 7 above) 573.

⁹⁶ The right to work as the most protected socio-economic right is found in the constitutions of 46 African countries. As the right is a broad right, the aspects of the right protected also differ in the different constitutions. Heyns & Kanguongo (n 59 above) 698.

⁹⁷ The right to education as the second most recognized constitutional socio-economic right is found in the constitutions of 45 African countries. In most of the constitutions the state is responsible for providing education which often includes free basic primary education and in some situations the states obligation extends to providing progressively free education. Heyns & Kanguongo (n 59 above) 700.

⁹⁸ The right to the protection of the family which includes the right to marriage, children's right and that of the youth is recognised totally in 42 African constitutions. Heyns & Kanguongo (n 59 above) 703-704.

the rights that are widely recognized. A right to culture which is also another type of socio-economic right is included in 41 constitutions.⁹⁹

The right to health although it is not provided in an elaborated and clear manner as we find it under CESC, we still find it in the constitutions of 39 African countries in different formulations.¹⁰⁰ The other group of socio-economic rights that are protected under African constitutions are the right to social security which is found in 29 constitutions and the right to an adequate standard of living in 14 constitutions.¹⁰¹

Domestic legislations on socio-economic rights are also found in some African countries making those rights more justiciable and facilitate their realization. As legislations tend to be more clearly and precisely formulated than constitutional standards, they overcome the argument that vagueness implies non-justiciability. They are also more accessible sources of remedy.¹⁰² Some examples of legislated socio-economic rights are found in South Africa, Djibouti, Burundi, Namibia and Benin.¹⁰³

3.3. Conclusion

African states have committed themselves under international as well as regional level to protect the socio-economic rights of their people by signing and ratifying international documents. Under CESC and African Charter they have an undisputable legal duty to protect the socio-economic interest of their people. The socially and legally binding contract – the constitution – that they have entered with their people is another source of their obligation. The legally binding nature of their constitutional obligations is further strengthened by the fact that in most African countries the constitution is the supreme law of the land.¹⁰⁴ Therefore, there is no way that African states can avoid responsibility for their failure to comply with their international and national obligations for the protection of socio-economic rights.

⁹⁹ Heyns & Kanguongo (n 59 above) 704-705.

¹⁰⁰ As above.

¹⁰¹ Heyns & Kanguongo (n 59 above) 708-709 & 710-711.

¹⁰² Viljoen (n 7 above) 571.

¹⁰³ Viljoen (n 7 above) 571-572.

¹⁰⁴ Heyns & Kanguongo (n 59 above) 677.

Though the implementation is always the biggest challenge, being able to precisely identify and assert the nature and extent of their obligation is the first important step for successful implementation.

It does not take that much research to know that the realization of all rights especially socio-economic rights have financial implications. This is to mean when a state sets out to fulfil its obligations, the first thing it needs among other things is resources. The source could be internal or external. Whatever the source of the revenue, any act or policy of the state that affects the revenue of the country affects the way public services are provided. It has a serious impact on the construction of infrastructures and provision of public services. This will have a direct impact on the socio-economic rights of its people and of course affect the other rights of its people. Any policy of a government on taxes, as major sources of state revenue, will either increase or decrease government revenue. This is where the issue of tax incentives comes into the picture. Tax incentives as part of government fiscal policy reduce tax revenues which means reduced state revenue and which in turn means less capital for financing public services and the construction of infrastructures.

So, the point is state obligation to realize socio-economic rights starts with the way states design their fiscal policies. Taxes in general and tax incentives in particular are part of the fiscal policies of governments' and hence any policy regarding those matters should always take into consideration the interest of its people and the human rights obligations of the state. The next chapter tries to show the potential impact of tax incentives on the realisation of socio-economic rights vis-à-vis the human rights obligations of African states.

Chapter four

4. Competition through tax incentives as a threat for the realisation of socio-economic rights in Africa

4.1. Introduction

For many African countries, attracting FDI has become the industrial policy of choice, with tax incentives being used as an instrument of competition.¹⁰⁵ Consequently, tax incentives in Africa are now used more widely than in the 1980s. Low-income countries in the region use such incentives more extensively than do middle-income countries – yet FDI in sub-Saharan Africa, other than in the resource sector, has increased very little over the past two decades.¹⁰⁶

Therefore, there is now a need for African governments to reassess the value of tax incentives, especially following the UNCTAD (2005) report on 'Economic Development in Africa', which shows that profit remittances in many sub-Saharan African countries have in recent years significantly exceeded total FDI inflows. Apart from remittances, tax incentives come with an immediate opportunity cost in lost government revenue¹⁰⁷ and they are also believed to have other social costs in the form of corruption and administrative costs.¹⁰⁸

It is mainly the huge loss of government revenue and other spill over costs of tax incentives that under this work is argued to have posed potential threat to the realisation of socio-economic rights in Africa.

¹⁰⁵ Mwilima (n 1 above) 4. Although competition among states to attract investment may be essentially healthy, the use of tax incentives as an instrument of such competition is perceived by many commentators detrimental. As Enrich remarks, in the context of incentives competition within the United States, 'from the states' collective vantage point, the net effect of the incentive competition is, in fact, far worse than zero-sum. For, although the states can expect to achieve no overall gain in business activity or jobs, they do incur a very substantial loss of tax revenues'. Enrich (n 11 above) 400.

¹⁰⁶ Gupta & Tareq (n 32 above) 46-47. Since 1970, FDI inflows into Africa has increased only modestly, from an annual average of almost \$1.9 billion in 1983 –1987 to \$3.1 billion in 1988 –1992 and \$6.0 billion in 1993 –1997. While inflows to developing countries as a group almost quadrupled, from less than \$20 billion in 1981–1985 to an average of \$75 billion in the years 1991– 1995, inflows into Africa only two folded during that period. As a result, Africa's share in total inflows to developing countries dropped significantly: from more than 11 per cent in 1976 –1980 to 9 per cent in 1981–1985, 5 per cent in 1991 – 1995 and to 4 per cent in 1996-1997. United Nations Conference on Trade and Development *Foreign direct investment in Africa: Performance and Potential* (1999) 2.

¹⁰⁷ Cleeve (n 46 above) 10.

¹⁰⁸ Easson (n 6 above) 77.

4.2. Loss of revenue through tax incentives – a threat for the realisation of socio-economic rights in Africa

In recent decades, there has been increasing competition among African governments to attract FDI by offering a wide range of tax incentives.¹⁰⁹ However, despite their efforts they have achieved very little in enticing foreign MNCs. What is worse is that African states are losing a large amount of government revenue. For instance, as the UNCTAD study shows gold exports in Ghana for the period 1990-2003 rose threefold to about \$893.6 million, of which Ghana earned only about 5% in revenue. In Tanzania, between 1997 and 2002, gold export earning stood at around \$890 million, with only about 10% going to government revenue in the form of taxes and royalties.¹¹⁰ In Tunisia, relatively successful in attracting FDI, the fiscal costs associated with the incentive regime amounted to almost 20 percent of the total percent of private investment in 2001.¹¹¹ This is the result of excessively generous and untargeted tax incentives which undermines tax revenues and the effectiveness of domestic tax systems.¹¹²

What does then the loss of tax revenue has to do with the realization of socio-economic rights?

We hear every day that there is no money for development projects, for building schools and dispensaries. Yet people hear billions of shillings lost in tax revenue...How do we explain this to people who we tell there is no money for basic services?¹¹³

The above quote briefly elucidates how loss of tax revenue undermines the realisation of socio-economic rights by depleting state revenue necessary for the realisation of socio-economic rights.

¹⁰⁹ A Mosioma 'The role of tax incentives in encouraging harmful tax competition in the East African flower industry' (2007) 1.

¹¹⁰ Cleeve (n 46 above) 10.

¹¹¹ Morisette (n 17 above) 3.

¹¹² Easson (n 6 above) 103.

¹¹³ John Cheyo Chairman, Parliamentary Public Accounts Committee Tanzania quoted in M Curtis & T Lissu 'A golden opportunity?' (2008) 17.

It is difficult to conceive of any state action designed to create and facilitate an economic, social and political environment conducive to the enjoyment, exercise and realization of economic, social and cultural rights that can be undertaken without funds from the national coffer. The state cannot comply with its obligations unless it uses part of its resources to do so.¹¹⁴ This points to the very serious need for African states to effectively and prudently allocate their financial resources, tax revenue being the major one,¹¹⁵ in order to comply with their obligations to respect, protect and fulfil socio-economic rights.¹¹⁶

Under this chapter, it is argued that the loss of revenue through tax incentives leads to the violation of the three-level 'typology' of state obligations: the obligation to respect, protect and fulfil.

4.2.1. Loss of revenue as a violation of the obligation to respect

The obligation to respect requires the state to refrain from taking any action that would negate economic, social and cultural rights.¹¹⁷ In an endeavour to meet this obligation African states are expected to refrain from taking any action that obstructs the full enjoyment of socio-economic rights by the people. In this regard any measure by the states which is of retrogressive nature requires the most careful consideration and needs to be fully justified in the context of full use of maximum available resources by the states.¹¹⁸

A 'deliberate retrogressive measure' means any measure that implies a step back in the level of protection of socio-economic rights, which is the consequence of an

¹¹⁴ MSI Diokno 'A rights based approach to budget analysis' (1999) 7.

¹¹⁵ Tax revenues are the primary and traditional sources of states' revenue. Especially in Africa tax account for almost all of governments' revenue and thus forms the biggest part of domestic resources. Although in most African countries because of the dominance of the informal sector and the inefficiency of the tax system, the tax - to - GDP ratio is low as compared to the developed world, it with no doubt forms the lion's share of the domestic revenue. United Nations Conference on Trade and Development *Economic development in Africa: Reclaiming policy space* (2007) 16. See also Diokno (n 114 above) 25.

¹¹⁶ As above.

¹¹⁷ V Dankwa et al 'Commentary to the Maastricht guidelines on violations of Economic, social and cultural rights' (1998) 20 *Human Rights Quarterly* 705 713. See also Dionko (n 114 above) 6.

¹¹⁸ General Comment No 3 para 9.

intentional decision by the state.¹¹⁹ This may occur, for example, when a state adopts any legislation or policy with a direct or collateral negative effect on the enjoyment of socio-economic rights by individuals.¹²⁰ The case of tax incentives represents a deliberate retrogressive measure by states. In the first place, when African states design tax policies and change them into laws to grant tax incentives they are fully aware of the nature and consequences of such policies and laws. This is because the standard advice given by international financial institutions like World Bank and IMF woos African states to avoid using tax incentives as means of attracting FDI. The advice clearly indicates the inefficiency of tax incentives and the related loss of national revenue and the consequent deterioration of the welfare of their people that may occur as a result of their policies.¹²¹ This standard advice is also shared and advocated by several eminent experts from both developing and developed countries.¹²² Their practical experience in failing to attract FDI through tax incentives, as discussed under chapter two, and the loss of revenue they incur are other evidences showing that the states have continued to follow the policies deliberately – with full knowledge of their consequences.

The immediate consequence of this deliberate act of states to use tax incentives to attract FDI is loss of state revenue which ultimately has to be paid for by reduction in the services provided by the host government.¹²³ It means the government reduces its expenditure on education, health or infrastructure which are indispensable for the realisation and enjoyment of socio-economic rights.¹²⁴ This cut in public expenditure is a violation of economic, social and cultural rights.¹²⁵

¹¹⁹ University for Peace 'Substantive human rights: The right to adequate standard of living' in Human Rights Education Project CD-ROM (2004).

¹²⁰ As above.

¹²¹ Easson (n 6 above) 63.

¹²² See Ngowi (n 4 above), Easson (n 6 above) and Enrich (n 11 above).

¹²³ Easson (n 6 above) 76-77.

¹²⁴ Looking into which specific public sectors are affected by the loss of revenue may show one of the following facts. In some cases all the public sectors could be affected: that is education, health, housing, food and others. In other cases the effect of the budget reduction may be felt in some of the sectors. In still other instances only one sector could be affected. Whichever the case, the loss of revenue impacts on the realization of at least one and at most all socio-economic rights. Of course there is a fourth probability that all the sectors may not be affected which is very rare as several literatures show that sectors involved in social/public services are the major, if not the primary, sectors where the effect of lack of budget is felt. As above.

¹²⁵ The Maastricht Guidelines on Violations of Economic, Social and Cultural Rights (Maastricht Guidelines) 22 – 26 January 1997 Guideline 14. See also General Comment No 3 para 9.

The only excuse states have for taking such deliberate retrogressive measures is by proving that the policies have been introduced after the most careful consideration of all alternatives and that they are fully justified. However, African states' acts in using tax incentives as means of attracting FDI are neither carefully considered nor fully justified. They are not carefully considered because African states are following the policies on tax incentives irrespective of the fact that they have been proved to be notoriously ineffective and cause loss of revenue to the state.¹²⁶ This is without forgetting that African states have also been openly advised to abandon their policies on tax incentives.¹²⁷ Therefore, it is not possible to say that African states are taking retrogressive measures with most careful consideration of all alternatives as they have a clear and better alternative to abandon the policies on tax incentives.

Their acts are neither fully justified by reference to the totality of other socio-economic rights and in the context of the full use of the states' maximum available resources. For one thing, there is no right based justification for the use of tax incentives. For another, the justifications are not either economic reasons, they are purely political. Evidences show that tax incentives are given not because of their perceived importance in attracting FDI but rather because of political reasons.¹²⁸ The ever increasing competition from other countries and pressure from MNCs for better tax treatment are the other reasons why African countries take the risk to use tax incentives irrespective of expert opinion and advice by international organizations.¹²⁹ They are not as well justified in the context of the full use of states' maximum available resources for the simple reason that they cause loss of revenue to the state without bringing any considerable income in return. The money lost through tax incentives is money lost for no justifiable reason, not from economic perspective not from human rights angle. All the above factors prove that the acts of African states in granting tax incentives are not fully considered and justified. Instead African states

¹²⁶ Easson (n 6 above) 77.

¹²⁷ As recommended by IMF and WB.

¹²⁸ In a political atmosphere dominated by concerns about economic vitality and jobs, elected officials face intense pressure to engage in the incentive competition. This is especially true for African countries which are under continuous internal and external political pressure because of their fragile economies and extremely high number of unemployment rate. Under such conditions the absence of empirical evidence for the economic efficacy of tax incentives does little to quell the political enthusiasm. Enrich (n 11 above) 392 – 396.

¹²⁹ Easson (n 6 above) 85.

are deliberately pursuing their political and economic greed at the expense of human rights protection.

Therefore, African states by taking deliberate retrogressive measures they are violating their obligation to respect the socio-economic rights of their people. Their policies on tax incentives are policies that cause reduction in public expenditure, which is a violation of economic, social and cultural rights.¹³⁰

African states are further obliged to address issues of human rights 'as a matter of priority' in allocating and utilizing their limited resources.¹³¹ When states intentionally forego tax revenues for political reasons and as a result their actions risk the protection of human rights, it becomes obvious that they are not treating human rights issues as a matter of priority as they are expected to. When they have the choice and capacity to abandon the harmful tax incentives packages, they instead choose to follow and even worse promote an economic policy from which neither the people nor the state benefit. In such a way, they reduce their expenditure on basic social services and infrastructures which inevitably affects the socio-economic rights of the people. The fiscal policy that they are following is therefore in contradiction with their duty to refrain from taking any action that would negate the realization of socio-economic rights.

It is also in direct contradiction with their commitments to take deliberate, concrete and targeted steps towards the realization of socio-economic rights.¹³² African states have the obligation to move as expeditiously and effectively as possible towards the creation of conducive environment for the realisation of socio-economic rights.¹³³ Thus, they are required to continuously take steps forward in order to achieve the full realisation of the rights recognised in the instruments. From what we saw, the states by engaging in a harmful tax competition they are rather taking backward steps without any justifications. The economic greed and the competition to attract FDI ultimately, as Enrich would say, is compelling them to take measures that are

¹³⁰ Maastricht Guidelines 11 provides that a state is in violation of economic, social and cultural rights when it deliberately pursues a policy which contravenes its obligations under the CESC.

¹³¹ General Comment No 3 para 10.

¹³² General Comment No 3 para 2.

¹³³ As above.

contrary to the interests of their citizens'. By taking such measures African states are not only jeopardizing the interests and rights of their people but they are actually violating their obligations to respect the socio-economic rights of their people by failing to take deliberate, concrete and targeted steps towards the realization of the rights.

In this respect, Tanzania provides us with the perfect example revealing how loss of revenue through tax incentives affects the socio-economic rights of people. Tanzania is one of the fastest-emerging gold producers in Africa. It is thought to have the continent's largest gold reserves after South Africa.¹³⁴ It accounts for more than 90 per cent of the country's mineral exports. In 2007 gold exports were worth more than £500 million.¹³⁵ The country in general its 39 million citizens in particular, however, have gained few benefits from this huge natural coffer as the country is losing millions of shillings through tax incentives.

As the Tanzanian weekly newspaper - Sunday Citizen - reports the country lost a total of \$1.1 billion through tax incentives and poor documentation of gold production data. This, the news letter estimates, amounts to about 10 per cent of the country's GDP, which by the end of 2007 was valued at \$ 12 billion.¹³⁶

This sum is enough to build 1 000km of tarmac roads as well as funding 30 000 university students for ten years at the cost of US \$2 000 per student per academic year.¹³⁷ The people of Tanzania who are the ultimate owners of the resources let alone benefiting from their resources they are suffering as the result of the government's policies. Had those tax incentives policies were not in place, they could have benefitted from the revenue that would have been collected from those companies. That is what the report tries to show by roughly estimating to what extent the people of Tanzania would have benefited from the developmental projects that could have been financed using the revenue that was forgone through tax incentives. For the above reasons we can say that the government of Tanzania has failed to refrain from taking measures that negate the enjoyment of socio-economic rights. The fiscal policy of the government towards tax incentives violates its obligation to respect.

¹³⁴ A Christian Aid report 'Death and taxes: The true toll of tax dodging' May 2008 11.

¹³⁵ As above.

¹³⁶ 'Gold plunder exposed' *Sunday Citizen* 17 October 2008.

¹³⁷ As above.

The tax incentives are excessively generous and untargeted which take no notice of the human rights obligations assumed by the Government.¹³⁸ The policies on tax incentives are neither economically efficient and effective nor considerate of the human rights obligations of the Government.¹³⁹

4.2.2. Loss of revenue as a violation of the obligation to protect

The state is obliged to protect right-holders against other subjects by legislation and provision of effective remedies.¹⁴⁰ The obligation to protect includes the state's responsibility to ensure that private entities or individuals, including MNCs over which they exercise jurisdiction, do not deprive individuals of their economic, social and cultural rights.¹⁴¹

It is conceded that tax incentives schemes provide companies with ample opportunity to avoid and evade taxes.¹⁴² In Africa especially, where there is financial constraint, there are few or no mechanisms to ensure that firms do not use incentives to facilitate tax avoidance and evasion.¹⁴³ Accordingly, companies use this gap in the

¹³⁸ For example, the mining sector and export processing zones, have a 0% tax rate on the following; custom duty on capital goods, sales tax on capital goods and withholding tax on interest. The agricultural sector, air aviation, commercial building, commercial development and micro- finance banks, export oriented projects, geographical special development areas, human resources development, manufacturing, natural resources, rehabilitation and expansion, tourism and tour operations, transport and radio and television broadcasting enjoy a 0% tax rate on sales tax on capital goods and withholding tax on interest. All the sectors mentioned above enjoy a 100% capital allowance deduction in the years of income. Ngowi (n 4 above) 25.

¹³⁹ Tanzania is member state to CESCPR since 11 September 1976 and African Charter since 18 February 1984.

¹⁴⁰ *Social and Economic Rights Action Centre (SERAC) and Another v Nigeria* (2001) AHRLR 60 (ACHPR 2001) para 46.

¹⁴¹ Maastricht Guidelines 18.

¹⁴² Many scholars agree that tax incentives are prone to corruption and abuse. For instance, Garcia-Mila and Mcguire argue that tax incentives reflect the ability of the firm to bribe or coerce the leaders of the government. They give instances where companies bribed politicians to get generous tax incentives. Morisset also contends that tax incentives create frequent opportunities for illicit behaviour by companies and tax administrators. He further goes on to say that these issues of illicit behaviour become crucial in developing countries, which face more budgetary constraints and corruption than do industrial countries. Even the UNCTAD study shows that tax incentives regimes are susceptible to corruption. See Easson (n 6 above) 77 and also Morisset & Pirnia (n 44 above) 3; T Garcia – Milla & TJ Mcguire 'Tax incentives and the city' (2002) 26; Morisset (n 17 above) 3 & UNCTAD (n 16 above) 17.

¹⁴³ E Gugi & GR Zordow 'International tax competition and tax incentives in developing countries' (2002) 2.

tax incentive schemes to transfer large amounts of money using transfer pricing and other illicit conducts.¹⁴⁴

Tax evasion, tax avoidance and other forms of corruption are estimated to reduce tax revenues in some African countries by as much as 50 per cent, dramatically reducing funds available for public spending.¹⁴⁵ Research by the Ghanaian Ministry of Justice has revealed that 12 sampled companies owed nearly Cide 12 billion in unpaid taxes between them. Grossing up the results to include all companies suggests that government revenues from corporate profits could be boosted by approximately 50 per cent by tackling organised tax avoidance in Ghana.¹⁴⁶

Tax Justice Network for Africa (TJN-A) also reports that one third of Sudan's potential tax yield is lost to tax evasion. Tackling this problem, the report suggests, would go a long way towards overcoming the government's budget deficit estimated at \$ 429 million in 2005.¹⁴⁷ In the same report TJN-A indicates that in South Africa up to R30 billion (45% of government revenue) of due taxes remain uncollected largely due to evasion by rich individuals and avoidance by companies.¹⁴⁸

Under investigation by the Nigerian Economic and Financial Crime Commission, the US oil services company Halliburton admitted that its officials had paid bribes amounting to \$2.4 million to tax officials in return for favorable tax treatment worth more than \$14 million.¹⁴⁹

Charterhouse Bank was closed by the Central Bank of Kenya in 2006 after it was revealed that Charterhouse had deliberately flouted know-your-client rules and assisted its client, Nakumatt (a supermarket chain), to evade tax and launder money. The loss of revenues to the Kenyan government is estimated at US\$240 million.¹⁵⁰

¹⁴⁴ As above.

¹⁴⁵ Tax Justice Network for Africa (TJN-A) 'Looting Africa: Some facts and figures' 3 <http://www.liberationafrique.org/IMG/pdf/TJN4Africa.pdf> (accessed 2 October 2008).

¹⁴⁶ 'Who pays taxes in Ghana' *Daily Graphic* 5 December 2006.

¹⁴⁷ TJN-A (n 145 above) 2.

¹⁴⁸ As above.

¹⁴⁹ OM Bakre 'The spoils of oil: How multinationals and their professional advisors drain Nigeria of much needed resources' 2 *Tax Justice Focus* 1 4-5.

¹⁵⁰ T Mogusu 'Charterhouse distances itself from money-laundering claim' *The Standard* (Kenya) 24 June 2006.

This shows that MNCs operating in Africa are denying African states a huge amount of revenue mainly using the gaps created by tax incentive administration.¹⁵¹ As a result, African states are losing revenues that could have been used for improving the socio-economic situation of their population. The lost revenue could have been used for financing different developmental projects and public services that help to build and establish infrastructures and institutions through which the socio-economic rights of the people can be at least minimally guaranteed.¹⁵² The loss is attributable to the failure of African states to establish the necessary legal and institutional mechanisms for controlling the illicit behavior by companies that are caused as a result of the gaps that tax incentives create.¹⁵³ Hence they have failed to protect their citizens from the illicit acts of the MNCs which are plundering their resources and money.

African states are therefore responsible for lack of due diligence in controlling the behavior of the MNCs, which is a violation of the obligation to protect socio-economic rights.¹⁵⁴

4.2.3. Loss of revenue leading to the violation of the obligation to fulfil

The obligation to fulfil relates closely to the duty of states to devote the maximum of available resources towards the progressive realisation of economic, social and cultural rights.¹⁵⁵ It requires the state to take appropriate legislative, administrative, budgetary, judicial and other measures towards the full realization of economic, social and cultural rights.¹⁵⁶ It is more of a positive expectation on the part of state to move its machinery towards the actual realisation of the rights.¹⁵⁷

¹⁵¹ A EURODAD, CRBM, WEED and Bretton Woods Project report 'Addressing development's black hole: Regulating capital flight' May 2008 11-12.

¹⁵² TJN-A (n 145 above) 3.

¹⁵³ In the *SERAC v Nigeria* the African Commission stated that the obligation to protect generally entails the creation and maintenance of an atmosphere or framework by an effective interplay of laws and regulations so that individuals will be able to freely realise their rights and freedoms. *SERAC* (n 140 above) para 46.

¹⁵⁴ Maastricht Guidelines 18. Art 20(5) of the African Charter also imposes a duty on African states to eliminate all forms of exploitation by MNCs so as to enable their people to fully benefit from the advantages derived from their national resources.

¹⁵⁵ *Dankwa et al* (n 117 above) 714.

¹⁵⁶ *Dionko* (n 114 above) 6.

¹⁵⁷ *SERAC* (n 140 above) para 47.

Needless to say states have only limited resources. In fact it is because of this very reason that resource constraints are the most common justifications raised for limiting the fulfillment of socio-economic rights.¹⁵⁸ Even the human rights instruments to which African states are parties to take cognizance of this fact. The CESCER, for instance, provides that states are required to act within the available resources that they have.¹⁵⁹ Similarly the Universal Declaration recognises that everyone has the right to enjoy socio-economic rights 'in accordance with the organization and resources of each state'.¹⁶⁰ In the African Charter, even though there is no explicit provision which qualifies the enjoyment of the rights, the jurisprudence of the African Commission shows that it is possible to read in those limitations using the international human rights instruments ratified by African states.¹⁶¹

However, this is not to mean that states are free to dismiss every case on socio-economic rights based on resource constraints. Resource constraint is a recognised limitation but it is not an absolute limitation. Under the CESCER, for instance, states are expected to make the best use of their available resources. The approach by CESCER is also adopted by the African Commission and hence can be used for the African Charter too. Under the Universal Declaration African states are required to make national efforts within the resources that they have to ensure the realization of socio-economic rights.¹⁶² Thus, the limitation is not absolute as states are required to make efforts to utilise their available resources to the maximum possible for the realisation of socio-economic rights.

Therefore, African states, as parties to those human rights instruments, have the duty to make sure that their financial resources are well managed to enable the enjoyment of socio-economic rights by the vast majority of the population.¹⁶³ One way of checking if states are using their available resources to the maximum possible, is by looking into the national budget of the countries. The state's national budget indicates exactly how much financial resources are available for state use. It also indicates the

¹⁵⁸ *Eldridge v British Columbia* (1997) 151 DLR (4th) 577.

¹⁵⁹ CESCER art 2(1) & General Comment 3 No paras 9 & 10.

¹⁶⁰ Universal Declaration art 22.

¹⁶¹ *Purohit and Others v The Gambia* (2003) AHRLR 96 (ACHPR 2000) para 84.

¹⁶² Universal Declaration art 22.

¹⁶³ Diokno (n 114 above) 12.

various state programs and actions which are to be funded by the national budget.¹⁶⁴ By looking closely at each expenditure item under each ministry, department or state office, one may identify programs and projects that may appear to obstruct the realization and enjoyment of socio-economic rights.¹⁶⁵

Tax incentives can be identified as governmental programs and projects that obstruct the realization of socio-economic rights. As argued before tax incentives besides their inability to meet their purposes – that is attracting FDI – they also entail loss of state revenue and have administrative costs for their granting, implementation and follow-up.¹⁶⁶ They are part of state programs that demand state resources.¹⁶⁷ When states allocate budgets for programs and policies like tax incentives that obstruct the realization of socio-economic rights by reducing government expenditure on public services, then they cannot be said to have well managed their resources for the realization of socio-economic rights. Actually they are mismanaging their resources. Moreover, by looking at the general expenditures¹⁶⁸ and costs of tax incentives in contrast to other badly needed services like social services, one can tell African states are not making the necessary efforts to effectively utilize or to make maximum use of their available resources for the fulfillment of socio-economic rights.¹⁶⁹ This implies their failure to utilize their available resources to the maximum for the full realization of socio-economic rights which is again a clear case of violation of socio-economic rights.¹⁷⁰

As it was pointed out at the beginning of this section, the obligation to fulfill relates to the devotion of maximum of available resources for the progressive realization of socio-economic rights. Therefore, the fact that tax incentives result in the

¹⁶⁴ Diokno (n 114 above) 8.

¹⁶⁵ As above. See also Limburg Principles on the Implementation of the International Covenant on Economic, Social and Cultural Rights 1986; see also General Comments 1 to 12 adopted by the UN Committee on Economic, Social and Cultural Rights & Maastricht Guidelines.

¹⁶⁶ UNCTAD (n 16 above) 23.

¹⁶⁷ The administration of tax incentives could be carried out by different government departments depending on the type of incentive and governmental structure. Whichever governmental organ is undertaking the task of administration it needs its own budget for administration in addition to the tax incentive scheme by itself being one major expenditure. As above.

¹⁶⁸ Professor Stanley Surrey is the one who for the first time noted the equivalence of tax incentives to direct expenditure programs and coined the term 'tax expenditures' to refer to them. Holland & Vann (n 18 above) 1.

¹⁶⁹ Diokno (n 114 above) 9.

¹⁷⁰ Maastricht Guidelines 15.

failure of African states to utilize their available resources to the maximum means they are in violation of their obligation to fulfill.

African states are wasting government revenue for a cause that serves neither the interest of the people nor that of the government while their people are living in dire poverty. This by no means can be justified by limitation of resources argument and is a violation of the obligation to fulfil.

Again Tanzania provides us with another example on this issue. A report titled 'A golden opportunity?' reveals that Tanzania has lost out at least US \$400 million over the past seven years from low royalties and lost taxes from mining companies.¹⁷¹ The amount would have provided a 'huge boost to tackling poverty in Tanzania'. The report says the government's budget for 2007-08 envisaged spending US \$48 per person on development expenditure such as education, health, infrastructure and water. The lost revenue could have paid for more than 8.3 million people to receive such services.¹⁷² The amount, the report adds, was equivalent to more than 1.5 times Tanzania's entire health budget for 2007. It could have funded the building of more than 66 000 secondary-school classrooms.¹⁷³

This loss is taking place in a country where currently about 31 per cent of the total population survives on one meal a day because of grinding poverty. Therefore, by no standard the Government can justify its acts on the grounds of limitation of resources while it is losing millions of dollars for tax incentives schemes that is benefiting neither the people nor the economy.

The living conditions of the people of Geita, Tanzania, is an ideal example to demonstrate how African countries can be held responsible for failing to meet their obligation to fulfil by losing revenue to tax incentives. The Geita gold mine is one of Africa's biggest open-cast mines. In 2006 AngloGold Ashanti (AGA), the Company owning the Geita gold mine, produced 308 000 ounces of gold.¹⁷⁴ It has been widely reported in the Tanzanian media that it will only start paying corporation tax in 2011,

¹⁷¹ Curtis & Lissu (n 113 above) 26.

¹⁷² As above.

¹⁷³ As above.

¹⁷⁴ A Christian Aid report (n 134 above) 13.

11 years after starting operations.¹⁷⁵ Yet its own annual reports show the company has made operating profits of \$93m from Geita between 2002 and mid-2007. The Government of Tanzania is forgoing the huge income that could have been gained by taxing the Company while the people of Geita are living in a dire situation.

Geita's roads are in a lamentable state and water has to be fetched from wells as the main water-pipe goes direct from Lake Victoria to the mine camp, with no outlets for the local residents. Geita District Hospital was built in 1956 and has not seen much upgrading since. It is busy, with about 250 outpatients a day and some 160 inpatients. Many of the wards have two patients to a bed. The busiest place is the HIV clinic, with an average of 150 patients a day.¹⁷⁶

While the people are living in such a situation the government is forgoing millions of dollars which could have been used for the betterment of the lives of its subjects. This is not effective use of resources and cannot be justified on the grounds of resource constraints as it is the government itself which is responsible for the 'lack' of resources. It cannot raise its own fault as a defence for failing to fulfil its obligations. Therefore, as it is illustrated by the case of Tanzania, African states should not be allowed to raise the defence of resource constraints for their failure to fulfil socio-economic rights, when they are losing revenue through tax incentives.

Denying people basic social services is a violation of the 'minimum core obligation' requirement. It is a well established precedent that a state 'in which any significant number of individuals are deprived of essential foodstuffs, of essential primary health care, of basic shelter and housing, or of the most basic forms of education is, prima facie, failing to discharge its obligations under the Covenant'.¹⁷⁷

For Tanzania or any other African state to be able to justify its failures to meet the minimum core obligations to lack of available resources, it should show that 'every effort has been made to use all resources that are at its disposition in an effort to

¹⁷⁵ As above.

¹⁷⁶ As above.

¹⁷⁷ General Comment No 3 para 10.

satisfy, as a matter of priority, those minimum obligations'.¹⁷⁸ When they are losing a substantial amount of revenue, which they could and should have secured, as a result of inefficient and untargeted policies while their people are living in dehumanizing poverty, then it will be a clear failure to fulfil socio-economic rights. Following this line of argument, therefore, the fiscal policies on tax incentives followed by most African countries, if not all, are not in conformity with their international human rights commitments.

4.3. Conclusion

When a government decides to pay for lost revenue through tax incentives by reducing expenditure on education, health or infrastructure, the result is the country becomes less attractive to other potential investors.¹⁷⁹ Or if it decides to increase taxes on wages and consumption to compensate for the lost revenue because of the incentives, labor and living costs are likely to rise, again with a possible detrimental effect on other investments, especially domestic investments.¹⁸⁰

Eventually, therefore, African states will neither benefit economically nor will they be able to comply with their human rights obligations by sticking to their policies and practices of granting tax incentives to attract FDI. In fact they may find themselves in a situation where they are no more attractive to FDI because of the deteriorated infrastructure and public services. As a result, they will also be jurisdictions where serious socio-economic rights violations occur, probably more than what they are experiencing now. Thus, following the current trend of competition through tax incentives gets African states nowhere close to where they are aspiring to reach economically and most importantly it becomes a setback in the realisation of socio-economic rights.

¹⁷⁸ As above.

¹⁷⁹ Easson (n 6 above) 76 – 77.

¹⁸⁰ As above.

Chapter Five

5. Conclusions and recommendations

5.1. Conclusion

There is an increasingly growing trend among African countries of using tax incentives as means of attracting FDI. It is fuelled by the strong desire and need to development. However, the employment of tax incentives as means of attracting FDI let alone bringing development, it is eroding the limited revenue base that African states have. African states loss a substantial amount of revenue every year through tax incentives without gaining any considerable income in return. This loss of revenue caused by tax incentives is not a mere economic policy failure, but it is also a failure and a danger to human rights protection in general and to the protection of socio-economic rights in particular.

Loss of revenue through tax incentives fails socio-economic rights protection in basically three respects. Firstly, as part of a state's fiscal policy tax incentives have the effect of distorting the enjoyment of socio-economic rights by reducing expenditure on basic social services and infrastructures which directly have an impact on the realization of socio-economic rights. This contradicts states' obligation to refrain from taking measures, including policies that disrupt the progressive realization of socio-economic rights. Secondly, when there is shortage of funds to finance projects and programs that are indispensable for the enjoyment of socio-economic rights, then obviously the state would not be in a position to meet its obligation to fulfil. There would not be enough hospitals, schools, roads or other basic social services for the people to exercise their socio-economic rights. The loss of revenue caused by tax incentives prevents states from fulfilling socio-economic rights to the fullest extent possible. Thirdly, tax incentives besides themselves being unnecessary government expenditures and having costs, they also create an opportunity for MNCs to cause further loss of revenue by avoiding and evading taxes. The inherent problems in the administration of tax incentives are making African states to loss incalculable amount of revenue every year. This is mostly attributable to African government's failure to fill the gap created by their own policies and that failure is denying the mass the benefit

that they are entitled to. In this way African states are failing to protect their people against the acts of MNCs in disregard of their obligation to protect. Therefore, tax incentives especially the loss of revenue caused by tax incentives is posing a major threat to the realization of socio-economic rights in Africa.

The research has made the link between tax incentives and the realization of socio-economic rights by showing that tax incentives lead to loss of revenue and revenue as major component of state resources is the most important tool in the realization of socio-economic rights. Based on studies and reports, the research vividly depicts that the loss of revenue through tax incentives has an impact on socio-economic rights mainly by reducing government expenditure on social services. The related costs of tax incentives are also other factors considered that elicit the state's and people's resources and deny the people better life and living conditions which actually means denial of socio-economic rights. The examples taken from some African countries make it a point that the whole research is not based on mere theoretical speculations but on practical experiences and existing problems in Africa. Taking into account the horrible socio-economic condition of most African countries and the limited resources that they have, a conclusion is made that following fiscal policies that exacerbate the existing situation amounts to a violation of the obligations of African states to progressively realize socio-economic rights as assumed under different international and regional human rights instruments.

5.2. Recommendations

It is very crucial to note that in this research the position is not that African states should avoid using tax incentives of all kind in all situations. Rather the proposition is that African states as a rule should not use tax incentives to attract FDI.¹⁸¹

Most importantly African states in whatever they do should be guided by and give priority to their human rights obligations. Policy makers and governments should make sure that the policies they design, the laws they enact and the decisions they

¹⁸¹ As we have seen under chapter two most MNCs look at the market size, the resource, infrastructures or cost of labor when they want to invest in a country. The tax system or tax incentives are only of secondary consideration.

take are in conformity with their human rights commitments. Tax incentives as part of government's fiscal policies should also be subject to the human rights scrutiny.¹⁸²

It is shown that tax incentives have the effect of reducing expenditures of governments on projects that would help to improve the socio-economic conditions of people. That means they will drag back the state from progressively realizing its socio-economic obligations. Therefore, it is high time for African governments to reassess their tax incentives schemes in light of their human rights obligations. In doing so, they should, to the extent possible, avoid using tax incentives to attract FDI as they are ineffective and lead to loss of revenue. The granting of tax incentives when they are not of any importance would be nothing but a loss and would endanger socio-economic rights protection.¹⁸³ But if it is found absolutely necessary to use tax incentives to attract FDI, it should be targeted and well designed¹⁸⁴ with a view to ensure that there will not be any negative spill over effects on the realization or on the budget for the realization of socio-economic rights. The economic or developmental efficiency of tax incentives should always be considered together with its neutral effect or positive contribution for the realization of socio-economic rights. As their obligations entail, they should make sure that there will not be any loss of revenue of any kind because of tax incentives that will retard the realization of socio-economic rights.

¹⁸² One way of doing that could be by involving human rights experts as stakeholders in the discussions related to laws and policies on tax incentives.

¹⁸³ If tax incentives do not attract additional investments they represent nothing but a revenue loss to the government.

¹⁸⁴ (a) Investments that would have come to the country in any event (in absence of tax incentives for example) should not qualify for tax incentives. In this case it is the investors that are disparate not the government. (b) Investments in natural resource extraction or other rent-generating activities do not need to be attracted by tax incentives. (c) Investments that are aiming at selling in the domestic market need not qualify for tax incentives. If the investors have to locate within for the aim of supplying the market there, tax incentives for them would be a direct loss of revenue. (d) Foot-loose short-term investments too should not qualify for tax incentives generally, and tax holidays in particular. Such investments include the quick-profit business such as in the trade sector, restaurants and construction. These investments are very dynamic. If affected by any disturbance of any kind, they may leave to another destination (country). (e) Another type of investment that should not qualify for tax incentives are low cost assembly plants that are highly mobile. They are likely to move to new jurisdiction to take the advantage of tax holidays there where these expire on the former location. (f) Fictive FDI should not qualify for tax incentives. These are FDI created to carry on what is in fact a domestically owned business. (g) Some special purpose incentives should not be given to some investments. For example incentives to employment creation, regional development or special activities like transfer of technology for that matter that would have occurred in any event should not be granted. Generally, the investments that cannot compensate the cost of the tax incentives should not qualify. See Ngowi (n 4 above).

In addition, African states should also be aware of the illicit conduct of MNCs that poses another danger for the realization of socio-economic rights by causing substantial loss of revenue. This needs the immediate response of African states. They should fill every hole that tax incentives administration create either by eliminating tax incentives or by putting in place legal and institutional mechanisms to fight the illicit acts of MNCs. Then they will be in a better position to protect the socio-economic rights of their people from prejudicial acts of MNCs.

As part of their international obligation to co-operate and assist one another to promote economic, social and cultural rights, African states should reach on tax harmonization agreements amongst each other and with the rest of the international community to avoid harmful tax competition through tax incentives. The tax harmonization agreements, besides the promotion of economic cooperation and development, should have as a matter of priority the promotion of all human rights with particular emphasis on the avoidance of any state conduct (related to taxation) that retards or halts the progressive realization of socio-economic rights.¹⁸⁵

In order to be able to supervise the progress states are making in the implementation of the above recommendations, African states should be required to present periodic reports to the African Commission, on the steps they are taking towards the gradual elimination of tax incentives and competition as part of measures taken to progressively realize socio-economic rights (as rights recognized under the Charter).¹⁸⁶ They should also be required to submit the same kind of report to the Committee on Economic, Social and Cultural Rights.¹⁸⁷

Furthermore, African states should not be allowed to raise resource constraint as a defense for their failure to meet their human rights obligations when it is proved that they are losing revenue as a result of untargeted tax incentives and through costs

¹⁸⁵ CЕССR art 2(1), Universal Declaration art 22 & Limburg Principles paras 29 – 34 all advocate for international cooperation and assistance among states for the protection and progressive realization of socio-economic rights. The African Charter also talks about international cooperation in its Preamble.

¹⁸⁶ According to art 62 of the African Charter, African states are required to submit periodic reports every two years on the legislative and other measures they taking with a view to giving effect to the rights and freedoms guaranteed in the Charter.

¹⁸⁷ Under arts 16 & 17 of CЕССR states are required to submit reports on the measures which they have adopted and the progress made in achieving the observance of the rights recognized in the Covenant.

related to the administration of tax incentive packages. The organ before which the case is presented, whether the African Commission or African Court or domestic courts, should look into expert opinion and reports on the amount of tax revenue lost through tax incentives while considering the resource constraint defense that may be raised by African states.

Bringing legal actions, at the regional and domestic level, against African states based on the different international, regional and national human rights instruments is also possible when they fail to meet their obligations as shown under chapter four. If the state has provisions in its constitution or domestic legislations that protect socio-economic rights, then using such provisions for cases before domestic courts is advisable since it increases their justiciability and enforceability. Whenever there are gaps in the provisions, they should be supplemented by the provisions of African Charter, CESCRC and Universal Declaration. For cases before the African Commission or African Court, the complainant should use the African Charter together with CESCRC and Universal Declaration using article 60 of the Charter and article 7 of the Protocol Establishing the African Court as the case may be.

In this way it is possible to facilitate the progressive realization of socio-economic rights and make sure that African people will not be denied of their socio-economic rights because of ingenuine resource constraint defences by states. Fighting the sources of all problems to the justiciability and realisation of socio-economic rights in Africa is what is generally proposed in this research by taking tax incentives as an example.

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