



UNIVERSITEIT VAN PRETORIA
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**EXAMINATION OF THE EFFECTIVENESS OF REGULATION OF
FOREIGN DIRECT INVESTMENT IN TANZANIA**

**THESIS SUBMITTED IN PARTIAL FULFILMENT OF THE
REQUIREMENTS FOR THE DEGREE OF MASTER'S OF LAW IN
INTERNATIONAL TRADE AND INVESTMENT LAW IN AFRICA**

**INTERNATIONAL DEVELOPMENT LAW UNIT, CENTRE FOR HUMAN
RIGHTS, FACULTY OF LAW, UNIVERSITY OF PRETORIA**

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DECLARATION

I declare that this Mini-Dissertation which is hereby submitted for the award of Master's of Law degree (LLM) in International Trade and Investment Law in Africa at International Development Law Unit, Centre for Human Rights, Faculty of Law, University of Pretoria, is my original work and it has not been previously submitted for the award of a degree at this or any other tertiary institution. Other works cited or referred to are accordingly acknowledged.

Lilian Melkizedeki Kimaro

DEDICATION

This piece of work is for my family, especially my loving husband, Dr. Melkizedeki Stephen Kimaro who always encourages and supports me tirelessly. To my precious children, Gilbert and Eileen thank you for understanding and encouraging me throughout my master's programme.

ACKNOWLEDGMENT

I owe special gratitude to my family for providing me with the support and the encouragement throughout my studies. A deep appreciation to the Australian Aid for the sponsorship.

I would like to thank the following people who in whatever measures, provided me valuable assistance in the production of this work;

Prof. Daniel Bradlow, Director of the LLM (International Trade and Investment Law) who ensured that we had international renowned resource persons to conduct the program. Mr. Olufemi Soyaju for his close supervision and guidance in the writing of this thesis; my sincere thanks are also due to Ms. Susan Karungi for her tutorial and technical guidance which build the base for this thesis. My sincere thanks is extended to Mrs. Emily Laubscher for her wholeheartedly support. She was a friend and a mother to me.

Prof. Chris Maina Peter, Lecturer at School of Law, University of Dar es Salaam and a member of the International Law Commission, for his encouragement and being gracious with time so as to provide helpful insights and relevant materials. I acknowledge Prof. Kenneth Mwenda's advice in this area of research.

I wish to extend my heartfelt gratitude and thanks to the Centre for Human Rights, University of Pretoria for giving me an opportunity to pursue this master's programme. I am grateful to all the members of the teaching staff for impacting us with knowledge, insightful and practical experience. A series of targeted modules offered by them enabled us to acquire significant knowledge from the course. I would like to give my sincere thanks to my employer, Ministry of Foreign Affairs and International Cooperation of Tanzania for allowing me to attend this programme.

I would also like to thank Ms. Mercy Kitonga of the Ministry of Foreign Affairs and International Cooperation of Tanzania, who assisted me in editing this work. Lastly, I appreciate

the support from Ms. Glory Bildard and Mr. Patrick Chove of Tanzania Investment Centre for providing me with valuable materials.

Thank you and May God bless you all.

ACRONYMS & ABBREVIATIONS

ACU	After Care Unity
AJIL	American Journal of International Law
AU	African Union
BGT	Biwater Gauff (Tanzania)
BITs	Bilateral Investment Treaties
BRELA	Business Registration and Licensing Agency
CGI	Corporate Guide International Ltd.
CRDB	Cooperatives Rural and Development Bank
CSR	Corporate Social Responsibility
DAHACO	Dar es Salaam Airports Handling Company Ltd.
DRC	Democratic Republic of Congo
DTTs	Double Taxation Treaties
DTAs	Avoidance of Double Taxation Treaties
EAC	East African Community
EEZ	Exclusive Economic Zone
EIA	Environmental Impact Assessment
EPZs	Export Processing Zones
ETW	Entrepreneurship Training Workshop
EU	European Union
FDI	Foreign Direct Investment
FREZA	Free Economic Zones Authority
FTAs	Free Trade Agreements
GATT	General Agreement on Tariffs and Trade

GDP	Gross Domestic Product
GFCF	Gross Fixed Capital Formation
ICC	International Chamber of Commerce
ICSID	International Centre for the Settlement of Investment Disputes
IEDC	International Economic Development Council
IAs	International Investment Agreements
ILO	International Labour Organisation
IMF	International Monetary Fund
IPC	Investment Promotion Centre
ITO	International Trade Organisation
JTI	Japan Tobacco International
MAI	Multilateral Agreement on Investment
MAP	Millennium Partnership for the African Recovery Programme
MFN	Most Favoured Nation Treatment
MNEs	Multilateral Enterprises
NAFTA	North American Free Trade Agreement
NBC	National Bank of Commerce
NEMC	National Environmental Management Council
NEPAD	New Partnership for Africa's Development
NGOs	Non-Governmental Organisations
OAU	Organisation of African Unity
OECD	Organisation for Economic Cooperation and Development
OSHA	Office of Safety and Health Administration
PESA	Private Enterprise Support Activities

PVV	Physical Verification Visits
R & D	Research and Development
RTAs	Regional Trade Agreements
Republic	United Republic of Tanzania
SA	States of America
SMEs	Small and Medium Enterprises
TANESCO	Tanzania Electric Supply Company Ltd.
TANROADS	Tanzania National Roads Agency
TANU	Tanganyika African National Union
TAZARA	Tanzania Zambia Railway Authority
TBL	Tanzania Breweries Limited
TCC	Tanzania Cigarette Company
THA	Tanzania Harbours Authority
TIC	Tanzania Investment Centre
TIN	Tax Identification Number
TNCs	Transnational Corporations
TRA	Tanzania Revenue Authority
Tsh.	Tanzanian shilling
UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
UNCTC	United Nations Commission on Transnational Corporations
UNGA	United Nations General Assembly
UNIDO	United Nations Industrial Development Organisation

USA	United State of America
USAID	United States Agency for International Development
VAT	Value Added Tax
VQF	Vocational Qualifications Framework
WTO	World Trade Organisation
WWF	World Wide Fund for Nature
ZIPA	Zanzibar Investment Promotion Authority

DIRECTORY OF CASES

Biwater Gauff (Tanzania) Ltd v. United Republic of Tanzania

Dowans Holdings SA (Costa Rica) and Dowans Tanzania Limited v. Tanzania Electric Supply Company Limited (Tanzania)

Edward Mlaki and Another v. The Regional Police Commander Kilimanjaro Region and Another

Genin v Estonia

John Mwombeki Byombalirwa v. The Regional Commissioner, Kagera and Another

Khimji Gangji Sisodya v. Republic

Noble Ventures v Romania

Salini Costruttori SpA and Italstrade SpA v. Kingdom of Morocco

USA (LF Neer) v United Mexican States

LIST OF TREATIES & INSTRUMENTS

African Charter on Human and Peoples' Rights, 1982

Agreement between the Government of the United Republic of Tanzania and the Government of the Kingdom of Denmark Concerning the Promotion and Reciprocal Protection of Investments

Agreement between the Government of the United Republic of Tanzania and the Government of the United Kingdom of Great Britain and Northern Ireland for the Promotion and Protection of Investments, 1994

Agreement between the Government of the United Republic of Tanzania and the Government of the Republic of Finland on the Promotion and Protection of Investments

Agreement between the Government of the United Republic of Tanzania and the Government of the Italian Republic on the Promotion and Protection of Investments

Agreement between the Government of the United Republic of Tanzania and the Government of the Kingdom of Sweden on the Promotion and Reciprocal Protection of Investments

Agreement on Encouragement and Reciprocal Protection of Investments between the United Republic of Tanzania and the Kingdom of the Netherlands

Constitution of the United Republic of Tanzania, 1977

Convention Establishing the Multilateral Investment Guarantee Agency of 1985, entered into force on 12 April 1988

Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958, which entered into force on 7th June 1959

Convention on the Settlement of Investment Disputes between States and Nationals of other States of 1965, entered into force on 14 October 1966

Industrial Shares (Acquisition) Act, 1967

Insurance (Vesting Interests and Regulation) Act, 1967

National Bank of Commerce (Establishment and Vesting of Assets and Liabilities) Act 1 of 1967

National Agricultural Products Board (Vesting of Interests) Act, 1967

Paris Convention for the Protection of Industrial Property of 1883 (Revised at Brussels in 1900, Washington in 1911, The Hague in 1925, London in 1934, Lisbon in 1958 and Stockholm in 1967, and as amended in 1979), signed in 1994

State Trading Corporation (Establishment and Vesting of Interests) Act, 1967

Treaty between the United Republic of Tanzania and the Federal Republic of Germany concerning the Encouragement and Reciprocal Protection of Investments, 1967

Tanzania Export Processing Zones Act, 2002

Tanganyika Foreign Investment (Protection) Act, 1963

Tanzania Investment Act, 1997

Tanzania Investment Regulations, 2002

Tanzania Land Act, 1999

Tanzania National Investment (Promotion and Protection) Act, 1990

Tanzania Village Land Act, 1999

Zanzibar Investment Promotion and Protection Act, 2004

TABLE OF CONTENTS

DECLARATION	i
DEDICATION	ii
ACKNOWLEDGMENT.....	iii
ACRONYMS & ABBREVIATIONS.....	v
DIRECTORY OF CASES	ix
LIST OF TREATIES & INSTRUMENTS	x
TABLE OF CONTENTS.....	xii
CHAPTER ONE	1
INTRODUCTION	1
1.1 Background to the research.....	1
1.2 Problem Statement	5
1.3 Research Questions	6
1.4 Objective and Significance of the Study.....	6
1.5 Definition of concepts	7
1.6 Literature Review	8
1.7 Research Methodology.....	11
1.8 Outline of Chapters	11
1.9 Scope and delineation.....	12
CHAPTER TWO	14
CONCEPTUAL AND THEORETICAL FRAMEWORK FOR REGULATION OF FOREIGN DIRECT INVESTMENT.....	14
2.1 Introduction	14
2.2 Foreign Direct Investment and Economic Development	15

2.3 Principles Underlying Foreign Direct Investment	16
2.3.1 Fair and equitable treatment principle	16
2.3.2 Full protection and security principle	17
2.3.3 Most-Favoured-Nation principle	17
2.3.4 National Treatment principle	18
2.3.5 Protection against expropriation principle	18
2.4 Economic Theories of Foreign Direct Investment	23
2.4.1 The classical theory	23
2.4.2 The dependency theory	24
2.4.3 Tanzania and economic theories of foreign direct investment	24
2.5 Regulation of Foreign Direct Investment	25
2.5.1 International Initiatives in Regulating Foreign Direct Investment	26
2.5.2 Challenges in Establishing Multilateral Accord over the Regulation of Foreign Direct Investment	28
2.5.3 Foreign Direct Investment at Regional Level	29
2.6 Conclusion	31
CHAPTER THREE	33
AN OVERVIEW OF LEGAL, REGULATORY AND INSTITUTIONAL FRAMEWORK FOR FOREIGN DIRECT INVESTMENT IN TANZANIA	33
3.1 Introduction	33
3.2 Tanzania Legal Characteristics	33
3.3 Tanzania Investment Promotion Policy	34
3.4 Foreign direct investment inflow in Tanzania	35
3.5 Substantive laws and regulatory frameworks related to foreign direct investment in Tanzania	36

3.5.1 Major laws and regulation affecting foreign investment.....	36
3.5.2 Legal framework of investment at independence.....	37
3.5.3 Some Changes and Tanzania Investment (Promotion and Protection) Act, 1990.....	38
3.5.4 The current law related to foreign investment in Tanzania.....	39
3.6 Incentives and Tax Policy and its Effect to Foreign Direct Investment.....	41
3.6.1 Incentives and Guarantees Offered by Tanzania Investment Centre.....	41
3.6.2 Tax Policy.....	42
3.6.3 Avoidance of double taxation treaties.....	45
3.7 Institutional framework for foreign investment in Tanzania.....	45
3.7.1 Tanzania Investment Centre.....	46
3.7.2 Practicality of Tanzania Investment Centre as a ‘One Stop Centre’.....	46
3.7.3 Performance of the Centre.....	48
3.7.4 Limited Institutional Capacity in Monitoring Investments or After Care Services.....	49
3.7.5 Administration of tax incentives.....	50
3.8 The Impact of Chinese Investments in Tanzania.....	51
3.8.1 Chinese Presence in Tanzania.....	51
3.8.2 Chinese investments in Tanzania.....	52
3.8.3 The Impact of the Chinese.....	52
3.9 Conclusion.....	54
CHAPTER FOUR.....	55
REGULATORY AND INSTITUTIONAL REFORM FOR FOREIGN INVESTMENT AND ITS IMPACT TO TANZANIA ECONOMY.....	55
4.1 Introduction.....	55
4.2 The challenges of investment treaties in regulating foreign investment to foster economic development.....	55

4.2.1 Tanzania Investment Act.....	55
4.2.2 Bilateral Investment Treaties and developmental goals.....	56
4.3 Institutional weaknesses.....	57
4.3.1 Tanzania Investment Centre Structure.....	57
4.4 Tax Incentives.....	58
4.4.1 Corporate Tax Reduction.....	59
4.5 Introduction of E-platform to Registration and Licensing Agencies.....	60
4.6 Foreign Direct Investment and its Impact to Economic Development in Tanzania.....	60
4.6.1 Examples of Foreign Direct Investments’ Impact on Tanzania.....	61
4.6.2 Analysis of Foreign Direct Investment in Various Sectors in Tanzania.....	65
4.6.3 Other Challenges and Way forward.....	71
4.7 Conclusion.....	74
CHAPTER FIVE.....	75
FINAL CONCLUSION.....	75
5.1 Summary of findings.....	75
5.2 Conclusion.....	76
5.3 Recommendations.....	76
Bibliography.....	79

CHAPTER ONE

INTRODUCTION

1.1 Background to the research

International foreign investment law has witnessed a rapid growth in the past few decades. The number of bilateral and regional investment treaties concluded between states has grown. True to history, this growth has never been smooth, admittedly, ‘such controversy resulted from the law on the subject being the focus of conflict between several forces released at the conclusion of the Second World War’.¹

International law relating to foreign investment covers two types of investments, foreign direct investment (FDI) and portfolio investment. FDI is distinguished from portfolio investment because portfolio investment does not entail control by government. Moreover, in portfolio investment the investor takes upon himself the risks involved in investments.² FDI investors who take both ownership and control positions in the domestic firms, are in effect the managers of the firms under their control; whereas foreign portfolio investment investors, who gain ownership without control of domestic firms, must delegate decisions to managers, but limit their freedom to make decisions because the manager’s agenda may not always a direct fit, in-line with and consistent with that of the owners. With this, manager vs. owners’ dynamic, portfolio investment projects are considered to be managed less efficiently than direct investment projects. Direct investors are more informed than portfolio investors regarding changes in the prospects of their projects. This, enables them to manage their projects more efficiently generating an advantage, with an added value in the capital markets, to direct investments relative to portfolio investments.³

In the early 1960s, Africa witnessed emergency of new independent states. New phenomenon was seen in the context of managing economies in a bid to strengthen the countries’ economy, states started to compete for foreign investment. Creating enabling environment to attract FDI,

¹ Sornarajah, M (2004) *The International Law on Foreign Investment*

² Sornarajah (n 1 above) 7

³ Itay, G & Razin, ‘Foreign Direct Investment vs. Foreign Portfolio Investment’ National Bureau of Economic Research Working Paper 11047, <http://www.nber.org/papers/w11047.pdf> (accessed 17 November 2011)

the process involved creation and review of respective laws. This is in line with the thinking that foreign investment could be beneficial to the host economy if the foreign investment is harnessed to the economic development of the host economy.⁴ Then, developing countries began to enact in legislation that was designed to screen foreign investment having regard to the effect it would have on the domestic economy. This is thought to be in continuous process; hence the interest of this study is to examine the effectiveness of the legal and regulation of FDI in Tanzania and its reflection to economic development.

Due to time constraint this thesis will focus on foreign direct investment in Africa. The definition of FDI has raised lot controversy for more than a decade. Different authors have tried to define it. Sornarajah⁵ defines foreign investment as the transfer of tangible or intangible assets from one country into another for use in the recipient country to generate wealth under the total or partial control of the owner of the assets. He further clarifies that this transfer can include movement of physical property such as equipment or the physical property that is brought or constructed such as plantations or manufacturing plants as constituting foreign direct investment.⁶

Sebastian Manciaux, in his article *the Notion of Investment: New Controversies*⁷ discusses how different awards and decisions have been reached at International Centre for Settlement of Investment Dispute (ICSID) on the matter. He discusses the criteria set in *Salini* case⁸ when investment was defined to include substantial commitment, duration of performance, regularity of profit and return, assumption of risks, and significance for the host state's development.

Another definition, most widely used is by the International Monetary Fund (IMF) and United Nations Conference on Trade and Development (UNCTAD). The IMF defines the concept as the category of international investment that reflects the objective of a resident entity in one economy obtaining a lasting interest in an enterprise resident in another economy. The lasting interest implies the existence of a long term relationship between the direct investor and the

⁴ United Nations Committee on Transnational Corporations 1970s

⁵ Sornarajah (2004) 7

⁶ As above

⁷ Manciaux, S 'The Notion of Investment: New Controversies' (2008) 9 *The Journal of World Investment & Trade*

6

⁸ *Salini Costruttori SpA & Italstrade SpA v. Kingdom of Morocco*, ICSID Case ARB/00/4

enterprise and a significant degree of influence and the presence of the investor on the management of the enterprise. Direct investment comprises of the initial transactions and all subsequent transactions between investors and among affiliated enterprises, both incorporated and unincorporated.⁹

The OECD, in its guidelines¹⁰ also adheres to this definition with a slightly different twist; defining FDI as a lasting interest by a resident entity in one economy in an entity located in a host economy, presuming the existence of a long-term relationship between the direct investor and the local entity and a significant degree of influence on the management of the local entity. The entity in the home country can be referred to as the direct investor and the one in the host country as the direct investment recipient. OECD highlights that absolute control by the foreign direct investor is not required and that it should be considered enough that the investor's transaction enables him to participate in or influence, the management of the direct investment entity, and sets the prerequisite for control to be ownership of at least 10 percent.¹¹

This thesis will adapt the definition of FDI influenced by the *Salini* case

which explored FDI from a legal, political and economic point of view, in effect encompassing the core controversies of defining FDIs.

Tanzania with its strategic geographical location, political stability, enormous natural resources, and world renowned tourist attractions to include Ngorongoro Crater, Mount Kilimanjaro, Serengeti, Lake Manyara and the spice island of Zanzibar is a FDI heaven. The country is an emerging economy with almost limitless growth potential. Investment opportunities existing in Tanzania are categorised in terms of lead and priority sectors, where a number of them remain untapped. These include agriculture, mining, tourism, manufacturing, banking and insurance services, education and health, and natural resources.¹² According to the 2011 World Bank report¹³ Tanzania is classified as a low income economy with \$ 500 Gross National Income per

⁹ International Monetary Fund, Balance of Payment Manual, Fifth edition, Washington D.C. (1993) 86

¹⁰ Organisation for Economic Cooperation and Development, *Detailed Benchmark Definition of Foreign Direct Investment*, Third edition, Paris (1996) 7

¹¹ Organisation for Economic Cooperation and Development, Directorate for Financial and Enterprise Affairs. Glossary of Foreign Direct Investment terms and definitions <http://www.oecd.org/dataoecd/56/1/2487495.pdf>

¹² <http://www.tic.co.tz> (accessed 10/8/2011)

¹³ World Bank Report on World Development Indicators, April 2011, Washington D.C. <http://data.worldbank.org> (accessed 26 November 2011)

capita. The country has a population size of 44 million and its Gross Domestic Product (GDP) growth was recorded to be 6.0 percent in 2009 and 7.0 percent in 2010.

Peter and Mwakaje¹⁴ have documented the history of FDI in Tanzania since its independence. Noting that the growth of FDI in Tanzania has been characterised by upheavals, Peter and Mwakaje further note that the country started well with the enactment of the Foreign Investment (Protection) Act in 1963 which aimed at attracting investors.¹⁵ The Act was fortified by bilateral investment treaties between the newly independent State and some developed countries such as the United States of America, Switzerland, Federal and the Republic of Germany. The adoption of the Arusha Declaration that marked a localisation of all major means of production, placing them exclusively under the custodianship of the government effectively nullified any pre existing FDI aspirations and bilateral treaties that were in existence hitherto.¹⁶ The drastic change in the policy that was the proclamation of the Arusha Declaration was further supported by Legislation that was enacted to that effect and culminated in the mass nationalisations of various investments in the country.¹⁷ Which are banks, retail and wholesale trades, agricultural products marketing, insurance business and industrial shares in various private companies.

The trend however did not last. In the present global economy, Tanzania has re embraced liberalisation of its economy manifested in the removal of all obstacles that previously hampered the inflow of free private investment. Free market economy has re-emerged and expanded, acting as a, stimulus for the reflow FDI back into the country. This change went hand in hand with measures that boosted investor attraction – back into the country both at policy level¹⁸ as well as by the enactment of a legal basis for investment promotion and protection through the National Investment (Promotion and Protection) Act of 1990.¹⁹ The measures that were taken marked a new era in Tanzania one that was smarter with regards to investment. Currently, the country has no single legal framework for the regulation of foreign investment; rather Tanzania Investment Act²⁰ is used as the law to govern investments in the country. The new initiative also led to the

¹⁴ Peter, CP & Mwakaje, SJ (2004) *Investments in Tanzania: Some Comments – Some Issues*

¹⁵ Act 40 of 1963, Foreign Investments (Protection) Act <http://www.parliament.go.tz/Polis/PAMS/Docs/40-1963.pdf>

¹⁶ This was passed on 29 January 1967

¹⁷ Nationalisation Act, 1967

¹⁸ The objective of the policy was to create a conducive environment for attracting and promoting investors

¹⁹ The Act was to create a friendly environment for investors as a move towards opening up the economy

²⁰ Act 26 of 1997

establishment of Investment Promotion Centre (IPC), which later changed to Tanzania Investment Centre (TIC).

The Tanzania Investment Centre established as ‘one stop’ centre for attracting and managing investments has since its inception played a key role in boosting investment in the country. According to TIC report to date, China alone has registered more than 280 projects in Tanzania.²¹ The monetary value of these projects had by the end of 2010 exceeded US\$ 200 million.²² However, all is not roses, several challenges remain, mostly relating to the regulation of investments including whether the current legal framework governing investment in Tanzania contributes positively towards attracting investments that boost the economy or detracts from the country as a prime investment destination.

1.2 Problem Statement

From Tanzania Investment Centre reports it is fact that Tanzania has received considerable FDI. The decade long analysis has shown TIC had registered over 4,084 investments between 1997 and 2007, of which 25.04 percent were foreign. Total FDI into Tanzania between 1995 and 2004 totaled US\$ 2476.4 million compared to less than US\$ 2 million between 1986 and 1991.²³ Despite this massive investment, actual translation into actual economic development has been miniscule, disappointing and almost non-existent. Some international authors like Sornarajah, Brownlie and Subedi in analysis peg such shortfall to insufficient regulations. In various international organisations reports this has been the centre of discussion. The World Bank report²⁴ argued that though legal and regulatory frameworks for FDI are not the primary drivers of investment decision, they can tip an investment decision in favour of a particular economy. Strong, stable legal and regulatory frameworks help create transparent environments conducive for investment. UNCTAD in its expert meeting discussed the right for the host state to regulate

²¹ ‘Tanzania Investment Report 2004 Foreign Private Investment in Tanzania’ <http://www.tic.co.tz>

²² Rutaiwa, JL ‘Empirical Analysis of China-Africa Economic and Trade Cooperation for Good or Bad: A Case of Tanzania’ (2011) 1 *International Journal of Academic Research in Business and Social Sciences* 3 www.hrmars.com/journals (accessed 12 January 2012)

²³ Report on the Study of Growth and Impact of Investment in Tanzania (2008)

²⁴ Investing Across Borders: Indicators of Foreign Direct Investment Regulation in 87 economies 2010 report <http://iab.worldbank.org/~media/FPDKM/IAB/Documents/IAB-report.pdf>

FDI in order to manage negative externalities caused by the investment.²⁵ In Tanzania Maina, Rugumamu, Kabelwa, Moshi and others on different occasions have written about the relationship between foreign direct investments regulations and economic performance.

This study shall therefore seek to explore the correlation between the effectiveness of FDI regulation and the resulting host country's economic development, with Tanzania as a case study for analysis.

1.3 Research Questions

The researcher is of the view that there is a deficit in the regulation of FDI's in Tanzania which explains the failure in achieving policy objectives for economic development.

The following questions will guide the researcher in answering this vital issue:

- 1) What is state of legal and regulatory framework for FDI in Tanzania?
- 2) Why the critical imperative for review of legal and regulatory framework for FDI in Tanzania?

1.4 Objective and Significance of the Study

The objective of this dissertation is to examine the efficacy of legal, regulatory and institutional frameworks in host/recipients country's in regulating FDI for envisaged economic development.

The study is relevant to academics and researchers as they will build on what has being written and provide new insights and knowledge. It is also important to policy makers as it will contribute to the current knowledge base on the correlation between investment regulatory frameworks and actual realisation of objectives as well as offer tools for improving the competitiveness of investment regulation in Tanzania and other countries with like conditions, for purposes of fostering economic development.

²⁵ 'The Development Dimension of FDI: Policy and Rule-Making Perspectives' proceedings of the Expert meeting held in Geneva from 6 to 8 November 2002 New York: United Nations (2003)
http://unctad.org/en/docs/iteiia20034_en.pdf

The study will also contribute to ongoing debate that, investments by developed and emerging economies to Africa are driven by hunger for raw materials and not for altruistic intentions of boosting the continent's economic development. And that foreign investment may adversely affect the country's economy by crowding out domestic investment and lowering domestic savings in effect adversely affecting the host country's development trajectory.

1.5 Definition of concepts

As propounded by various authors like Thomas, Seers, Sasha Lennon, and international bodies like UNDP, IMF and WB, there are many differences in terms of what constitutes development. Thomas argues development as a concept is inherently highly complex, ambiguous and contested both theoretically and politically.²⁶ Sasha Lennon, SGS notes that broadly economic development is typically measured not just in terms of jobs and income but also improvements in human development, education, health and environmental sustainability.

According to Seers the purpose of development is to reduce poverty, inequality and unemployment. For him if all these have become less severe, then beyond doubt this has been a period of development for the country concerned.²⁷ Scott Templeton proposes that there is no single, widely accepted definition of economic development, but there is considerable agreement that the main goal of economic development is improving the economic wellbeing of a community.

Recent United Nations documents emphasise 'human development,' measured by life expectancy, adult literacy, access to all three levels of education, as well as people's average income, which is a necessary condition of their freedom of choice, in effect, broadening the notion of development to incorporate individuals' well-being, from their health status to their economic and political freedom. The *Human Development Report 1996*, put it best when it propounds that 'human development is the end—economic growth a means.'²⁸

²⁶ Thomas, A (2004) 'The Study of Development' Paper prepared for DSA Annual Conference, 6 November

²⁷ Seers, D 'The Meaning of Development, with a Postscript' 1979

²⁸ http://www.worldbank.org/depweb/english/beyond/beyondco/beg_01.pdf (accessed 19 November 2011)

The International Economic Development Council (IEDC)²⁹, proposes that economic development can be described in terms of objectives such as the creation of jobs and wealth, and the improvement of quality of life. To the IEDC, economic development is a process that influences growth and restructuring of an economy to enhance the economic wellbeing of a community, through job creation, job retention, tax base enhancements and quality of life.

As there seems to be no common definition for economic development, no single strategy, policy, program or formula for achieving successful economic development; and communities differ in their geographic and political strengths and weaknesses, each community therefore, will have a unique set of challenges for economic development. For purposes of this study, development shall be taken to encompass progress in country's economy, manifested in improvement in living standards of the people and creation of more employment to the local people.

1.6 Literature Review

Foreign investment has always been considered a crucial catalyst for economic growth for all countries around the world. Various authors and publications of international bodies have discussed the issue whether the flow of capital in the country have any impact to country's development. There is ongoing debate whether regulation of FDI should be restrictive or not. For those who are against the idea of restrictiveness argue that investors are always hesitant to invest in countries with too much restriction hence low level of capital inflow. On the other hand, those who support the idea are of the view that if regulation of FDI is not existent, the purpose of economic growth will be defeated. The researcher seeks to find the answer by drawing from multiple sources of information. Focus will be on effectiveness of the regulatory regime governing FDI in Tanzania and protection of domestic interests.

Sornarajah³⁰ argues the issue of the right to regulate FDI will remain a stumbling block. He add even the Doha Declaration mandates that the investment should reflect in a balanced manner the interests of home and host countries, and take due account of the development policies and

²⁹ <http://www.iedconline.org/hotlinks/whtecodev.html>

³⁰ Sornarajah (2004) 313

objectives of host governments as well as their right to regulate investment for the public interest. The researcher seeks to reflect on Sornarajah's contribution in this study.

Leon Trakman 2010³¹ discusses that in theory, the liberalisation of FDI should benefit both foreign investors and help domestic economies share in the wealth derived from foreign investment. He critically discusses that the evolving right of investors to participate in FDI within a liberalised international regime and the sovereignty of states to protect domestic interests from the exigencies of FDI is an ongoing concern. In his view, he sees the need for international investment law to address conflicts arising out of this tension between state sovereignty and the liberalisation of investment in a manner that is principled, transparent and evenhanded.

Some of the international publications report that foreign investment plays an important role in complementing developmental processes at the national level by enhancing export competitiveness, creating employment opportunities and providing opportunities to local labour to develop new skills.³² Ranjan, on the other hand,³³ argues that foreign investment may adversely affect the country's economy by lowering domestic savings and investment by reducing competition and crowding out domestic investment.

Another contribution as discussed by Irandoust 2010³⁴ FDI is one of the major sources that contribute to economic growth through capital accumulation, technology transfer and knowledge spillovers. The World Bank report of 2006 shows that FDI accounts for more than 60 percent of private capital flows to the developing world. This expansion of FDI has encourage policymakers in developing countries to attract more foreign capital by reducing barriers to FDI and offering tax incentives and subsidies believing that FDI promote economic growth.

³¹ Foreign Direct Investment: Hazard or Opportunity?

³² United Nations Conference on Trade and Development, 1999 www.unctad.org

³³ Ranjan, P 'International Investment Agreements and Regulatory Discretion: Case study of India' (2008) *The Journal of World Investment & Trade*

³⁴ Irandoust, M 'A Survey of Recent Developments in the Literature of FDI – Led Growth Hypothesis' (2010) *The Journal of World Investment & Trade*

On the other hand, Lall and Narula 2004³⁵ raised an issue that most developing countries have removed restrictions on FDI inflows, but this has allowed foreign investors to exploit existing capabilities more freely. Thus this research sees a need to look on regulation of FDI with much focus to Tanzania. The role of FDI in economic development remains valid hence the interest of researcher to draw attention on the importance of effectively regulating FDI to achieve this important long term goal.

There are views from economic studies which suggest that, as developing countries are concerned, FDI can promote growth; much will depend on the state in issue, the nature of FDI, the manner of its use and the regulations imposed on it.

Busse and Groizard³⁶ explore the linkage between income growth rates and FDI inflows, and argue that countries need a sound business environment in the form of good government regulations to be able to benefit from FDI. The researcher agrees with the authors and wants to explore further how this can be done.

Schrijver in his book³⁷ discusses how the Havana conference reached an agreement on treatment of foreign investment. He pointed out that the Agreement provided for certain rights of host states to regulate foreign investment. In promoting and protecting foreign investment host states have rights to regulate for the benefit of their societies.

Andrew Guzman, 1998³⁸ contribute also to this debate and pointed that the regulatory regime governing FDI needs to be stable and sensitive to sociocultural and economic change.

The efforts to attract capital inflow do not end at country level. The East African Community (EAC) has taken economic reforms initiatives to strengthen investors' confidence to attract

³⁵ Lall, S & Narula, R 'Foreign Direct Investment and its Role in Economic Development: Do we Need a New Agenda?' (2004) *The European Journal of Development Research*

³⁶ Busse, M & Groizard, JL 'Foreign Direct Investment' <http://econ.worldbank.org/external/default/main?print=Y&pagePK=64> (accessed 19 November 2011)

³⁷ Schrijver, N (1997) *Sovereignty over Natural Resources: Balancing Rights and Duties*

³⁸ Guzman, AT 'Why LDCs sign treaties that hurt them: Explaining the popularity of BITs' (1998) http://works.bepress.com/andrew_guzman/15

capital inflow; this is recognised as the engine of economic growth - An EAC Model Investment Code.³⁹

1.7 Research Methodology

This will be explorative research, mostly qualitative which will constitute a desk and library based research. It will rely on both published and unpublished material. Internet sources will also be widely referred to. The research will analyse both primary and secondary sources to draw meaningful conclusions. Primary sources shall contain international and domestic treaties, conventions and statutes. The collection of secondary data will involve the preexisting information from books, articles, journals and reports from relevant stakeholders including Ministry of Foreign Affairs, Tanzania Investment Centre, Ministry of Trade and Industry, Ministry of Finance & Planning and Prime Ministers' Office of the United Republic of Tanzania.

1.8 Outline of Chapters

Regarding the organisation, the thesis consists of five chapters arranged in a coherent manner. An introductory chapter presenting an overview of the thesis topic, a definition of the research problem, methodology for data collection and analysis, guiding research questions, objective and significance of the study, literature review and scope of the research.

Chapter two shall focus on the regulation of foreign direct investment, highlighting existing international initiatives for regulating foreign direct investment and principles underlying FDI and conduct an examination of challenges in establishing multilateral accord over the regulation of FDI. The chapter will also focus briefly on the African take on legal frameworks for FDI before providing an overview of FDI at regional level focusing on the EAC Model Investment Code and efforts by EAC to create enabling environment for foreign investment to thrive. Tanzania is a member of the EAC and a case study for the region.

³⁹ 2002 Code is not a binding legal instrument but rather a model whose features the Partner States may incorporate into their national laws

Chapter three shall present challenges in regulating FDI. The laws governing investment in Tanzania will be critically examined in the interest of discerning whether they are addressing issues of economic growth and development. The institutional framework of the prime Tanzanian investment agency will be looked at under the chapter in order to see if the structure is realistic and empowered to monitor foreign investors. Some cases from local and international bodies such as *Biwater Gauff (Tanzania) Ltd v. United Republic of Tanzania*, *Dowans v. TANESCO*, *Edward Mlaki and Another v. The Regional Police Commander Kilimanjaro Region and Another* and others will also be looked at to be able to have a wider view on the treatment of foreign investment.

Chapter four critically discusses the imperative for reforms of the legal and regulatory framework for FDI in Tanzania. Under the chapter, other challenges will be discussed in detail by looking on practical examples to see why the need for legal and regulatory reforms.

Chapter five which covers the conclusion and recommendations will summarise the findings and draw conclusion that are recommended for implementation.

1.9 Scope and delineation

This thesis will limit the use of the word development. As explained in the definition of concepts, development is wide and a complex issue, with many different and sometimes contentious definitions. It has always been ‘open ended’ in that there can be as many dimensions to it. The study will limit development to improvement on country’s economy and improvement in living standards of people.

It is worth noting that this dissertation covers Tanzania Mainland only. Due to time constraint Zanzibar has been left out. The United Republic of Tanzania has a unique legal arrangement when it comes to implementation of international agreements including trade and investment. United Republic of Tanzania comprises of two governments, that of Tanzania Mainland and Zanzibar both enjoying powers on domestic implementation. There are some issues which are characterised as Union Matters⁴⁰ and others which are non-union matters. Investments fall under

⁴⁰ Schedule one to the Constitution of the United Republic of Tanzania of 1977 lists the Union Matters

non-union matters where each part of the Union deals with investments separately. In Zanzibar investment matters are governed by the Zanzibar Investment Promotion and Protection Act,⁴¹ and the body entrusted with dealing with investments is the Zanzibar Investment Promotion Authority (ZIPA).

⁴¹ Act 11 of 2004

CHAPTER TWO

CONCEPTUAL AND THEORETICAL FRAMEWORK FOR REGULATION OF FOREIGN DIRECT INVESTMENT

2.1 Introduction

This chapter explains the regulation of foreign direct investment. It seeks to explain the relationship between FDI, economic development and regulation process. The chapter will review principles underlying FDI and economic theories of FDI. It shall examine international efforts level to regulate investment and look at standards of treatment of foreign investment in customary international law with the aim of assessing the nature and scope of the core principles of foreign investment law.

Thorough examination of challenges in establishing multilateral accord over the regulation of FDI will be conducted. An overview of FDI at regional level will be conducted focusing on the EAC Model Investment Code and efforts by EAC on creation of enabling environment for foreign investment to thrive.

The world has witnessed remarkable growth in FDI flows, spurred by strategies on investment by transnational corporations (TNCs) and liberalisation of national FDI policies. Numerous bilateral investment treaties and number of regional and interregional agreements have been concluded. It is believed that FDI offers benefits to host economies in terms of capital inflows, technology transfer, shared managerial skills and knowledge, improved access to export markets and so on. However, there are no guarantees that the opening up of a host country to foreign investment result in FDI inflows. Even when the adage proves true, development and other envisaged results differ considerably, depending on the circumstances. There are suggestions that governments need to consider what role they want inward FDI to play in their economies development process and design their FDI policies accordingly.⁴²

⁴² 'The development dimension of FDI: policies to enhance the role of FDI in the national and international context-policy issues to consider' (2002)

Following the rapid inflow of FDI the right to control foreign investment became topical in many countries. Up until the 1980s most countries made extensive use of restrictions on foreign investment. Since the 1980s there has been a complete reversal where countries start providing an open and predictable investment regime in their domestic reform agenda portraying an open handed welcome to foreign investment.

Under the chapter, a number of books, articles and international instruments will be summarised in order to bring wider understanding of regulation of FDI.

2.2 Foreign Direct Investment and Economic Development

The development dimension of FDI has been particularly relevant since the 2001 WTO Ministerial Meeting in Doha in relation to the development implications of, and prospects for, closer multilateral cooperation on long-term cross-border investment, particularly FDI.

Attraction of FDI is becoming increasingly important especially for developing countries. However this is often based on the implicit assumption that greater inflows of FDI will bring certain benefits to the country's economy.⁴³ Many states, particularly the least developed states, have liberalised their foreign investment laws and made a large number of investment treaties without witnessing the expected flows of foreign investment.⁴⁴ It has been discussed that despite the assumption that flow of foreign investment lead to economic development, the treaties are neither specifically designed to foster economic development nor do they contain any meaningful provisions as to the promotion of such economic development aspirations.

Various authors are of the view that the impact of FDI will largely depend on the conditions of the host economy, for example the level of domestic investment/savings, the mode of entry and the sector involved, as well as a country's ability to regulate foreign investment.⁴⁵ It is believed, FDI, where it generates and expands businesses, can help stimulate employment, raise wages and replace declining market sectors. However the benefits may only be felt by a small portion of the

⁴³ 'Foreign Direct Investment: A Lead Driver for Sustainable Development?' Towards Earth Summit 2002 Economic Briefing Series No. 1

⁴⁴ Sornarajah (2004) 262

⁴⁵ World Investment Report 1999

population, for example where employment and training is given to more educated, typically wealthy elites or there is an urban emphasis, wage differentials between income groups will be exacerbated.⁴⁶

2.3 Principles Underlying Foreign Direct Investment

The guiding legal foundation for modern foreign investment law is customary international law, protection to aliens, including foreign investors, the notion of diplomatic protection, international human rights law and the international law of state responsibility. The underlying idea is to ensure there is no discrimination in the conduct of international business. Basically there are five main principles of foreign investment law namely, Most Favoured Nation (MFN) principle, the national treatment principle, fair and equitable treatment principle, full protection and security principle and protection of foreign investment against expropriation.

These principles are employed to secure a certain level of treatment for foreign investors in host countries with different objectives. Looking on Most Favoured Nation principle, its purpose is to grant foreign investors from a country the same favourable treatment that is accorded to foreign investors from third countries operating in the host country. The object of the national treatment principle is to grant treatment comparable to that accorded to domestic investors operating in the host country itself. While the fair and equitable treatment brings in the elements of fairness and equity drawn from international law especially the principle of minimum standards and practice, as well as domestic law principles concerning the overall treatment of foreign investment in a host country.

2.3.1 Fair and equitable treatment principle

The concept of fair and equitable treatment is a major and important principle of foreign investment law. When states began to conclude BITs as the principal vehicle to regulate and promote foreign investment, this principle was incorporated as a key provision. The principle provides a basic level of protection to foreign investors and is based on the elements of fairness

⁴⁶ OECD a. (1999) Foreign Direct Investment and the Environment: An Overview of Literature

and equity. Violation of this principle by the host state concerned is the most common allegation made by foreign investors before international investment tribunals.⁴⁷

One of the early cases to deal with the notion of ‘denial of justice’ as an example of an unfair treatment was the *Neer* case.⁴⁸ This case was the beginning for governmental treatment of foreign investors as to amount to an unfair treatment under international law. It was held, in this case that the treatment of aliens, in order to constitute an international delinquency,

should amount to an outrage, bad faith, willful neglect of duty, or to an insufficiency of governmental action so far short of international standards, that every reasonable and impartial man would recognise its insufficiency.

In another case of *Genin v Estonia*,⁴⁹ the arbitration tribunal stated that a violation of the fair and equitable principle could be established by acts showing willful neglect of duty, an insufficiency of action falling far below international standards, or even subjective bad faith.

2.3.2 Full protection and security principle

The entitlement of foreign investors to full protection and security is another principle found in many BITs and Free Trade Agreements (FTAs). It was argued, in *Noble Ventures v Romania*,⁵⁰ that Romania was required to provide Noble Ventures with ‘full protection and security’, which required Romania to enforce its own laws and to provide police protection to protect the investment of foreign investors located in Romania.⁵¹

2.3.3 Most-Favoured-Nation principle

MFN treatment is one of the oldest and most important principles of both foreign investment law and the law of international trade. Although traditionally the MFN principle has been linked to trade agreements, it has come to play an important role in investment protection. The reason why foreign investors seek protection under the MFN principle is to avoid any discrimination against them which would put them at a competitive disadvantage compared to other investors from

⁴⁷ Subedi, SP (2008) *International Investment Law: Reconciling Policy and Principle*

⁴⁸ *USA (LF Neer) v United Mexican States* (1927) 21 American Journal of International Law 555- 556

⁴⁹ *Genin v Estonia*, ICSID Case No ARB/99/2, Award of 25 June 2001

⁵⁰ *Noble Ventures v Romania*, ICSID Case No ARB/01/11 of 12 October 2005, 12

⁵¹ Subedi (2008) 67

third countries. The underlying idea behind this principle is to ensure equality of competitive opportunities between investors from different foreign countries.⁵²

UNCTAD has discussed this principle and provide the definition. In its report MFN treatment in the context of foreign investment means that ‘a host country treats investors from one foreign country no less favourably than investors from any other foreign country’.⁵³

2.3.4 National Treatment principle

As discussed by Subedi the objective of the national treatment principle is to address discrimination on the basis of nationality of ownership of an investment. In order to ascertain what discrimination is it is necessary to compare the treatment of the foreign investor to the treatment accorded to a domestic investor in similar circumstances. The principle of national treatment under foreign investment law has a slightly different meaning from the meaning accorded to this principle in international trade law.⁵⁴ The national treatment, as defined in UNCTAD report means a host country extends to foreign investors treatment that is at least as favourable as the treatment that it accords to national investors in like circumstances.

2.3.5 Protection against expropriation principle

Protection of foreign investment against expropriation is a centuries old principle of foreign investment law. As a rule of thumb, foreign owned property may not be expropriated or subjected to a measure tantamount to expropriation unless the following four conditions are met. First an expropriation must be for a public purpose. Second expropriation should be non-discriminatory. Third it is taken in accordance with applicable laws and due process. Fourth full compensation is paid.⁵⁵

What constitute expropriation and discrimination, what is a public purpose and what is meant by full compensation has been the matter of controversy and most scholars have made their own

⁵² As above 68

⁵³ UNCTAD, Most-Favoured-Nation Treatment, UNCTAD Series on Issues in International Investment Agreements: New York and Geneva, United Nations (1999) 1

⁵⁴ Subedi (2008) 71

⁵⁵ As above 74

contribution to this debate. According to Higgins, the ‘public purpose’ principle signifies ‘a means of differentiating takings for purely private gain on the part of the ruler from those for reasons related to the economic preferences of the country concerned’.⁵⁶

Taking without due process of law would entail a taking in contravention of the principle of equality before the law, fair hearing and other principles of natural justice generally recognised by the world’s principal legal systems. Similarly, a discriminatory taking would entail unlawful discrimination between domestic and foreign investors engaged in like business and in like circumstances as well as between foreigners of different nationalities.

Based on jurisprudence and the literature on the subject matter there are four types of expropriation that constitute proper expropriation.

Direct Expropriation

Direct Expropriation constitutes the actual taking of property by the host government by direct means, including the loss of all, or almost all, useful control of property. This is the most obvious form of outright expropriation and its definition is less controversial. Tanzania Mainland, the focus of this study, followed the promulgation of Arusha Declaration in 1967; conducted direct expropriation where mass nationalisations of various investments in the country occurred. The government enacted laws through which various enterprises were taken over by the state. A Nationalisation Act, 1967 that was enacted for that purpose gave the government permission to expropriate property in the public interest.⁵⁷ A number of enterprises were affected following the enactment of other different laws. These include, banks through the National Bank of Commerce (Establishment and Vesting of Assets and Liabilities) Act,⁵⁸ retail and wholesale trade through the State Trading Corporation (Establishment and Vesting of Interests) Act,⁵⁹ agricultural products marketing through the National Agricultural Products Board (Vesting of Interests) Act,⁶⁰ insurance business where a monopoly was created vide the Insurance (Vesting Interests

⁵⁶ Higgins, R ‘The Taking of Property by the State’ (1982-III) 176, *Recueil des Cours* 259, 371

⁵⁷ Peter, CM *Foreign Investments in Tanzania: the Mainland and Zanzibar* (1994)

⁵⁸ Act 1 of 1967

⁵⁹ Act 2 of 1967

⁶⁰ Act 3 of 1967

and Regulation) Act,⁶¹ and industrial shares in various private companies vide Industrial Shares (Acquisition) Act.⁶² This expropriation was proper and legal since its aim was for public purposes and was taken through the above mentioned laws and the most important, the government paid compensation for the nationalised property.

Indirect Expropriation

Another type of expropriation is indirect expropriation which involves taking governmental, whether administrative or legislative, measure that does not directly take property but has the same impact by depriving the owner of the substantial benefits of the property.⁶³ This has also happened in Tanzania where the matter was taken to the International Centre for Settlement of Investment Disputes (ICSID) for arbitration.⁶⁴ *Biwater* case arose out of a dispute between a British project company (the Claimant), held jointly by a British and a German company, and the Republic of Tanzania (Respondent) over a concession to operate the water and sewerage services of Tanzania's big commercial city, Dar es Salaam. After concluding that Claimant failed to meet its contractual obligations, which forced Tanzania to cancel the contract and regained possession of assets previously leased to Claimant. Claimant brought an action before ICSID under the United Kingdom (UK)-Tanzania BIT, claiming that Tanzania breached its obligation to afford Claimant fair and equitable treatment, to provide full protection and security, not to take unreasonable and discriminatory measures, and to guarantee the unrestricted transfer of funds.

The issue before the Tribunal was whether Tanzania's conduct amounted to indirect expropriation. According to *Biwater* the Republic's conduct amounted to the expropriation of BGT's investment in two respects. First, the repudiation of the Lease Contract and more precisely, the means by which the government sought to implement the termination and second, the occupation of City Water's facilities, usurpation of management control and deportation of City Water's senior managers.⁶⁵ The Claimant supported her argument by referring to article 5(1)

⁶¹ Act 4 of 1967

⁶² Act 5 of 1967

⁶³ Subedi (2008) 76

⁶⁴ *Biwater Gauff (Tanzania) Limited v United Republic of Tanzania* ICSID Case No. ARB/05/22

⁶⁵ As above award 393 408

of BIT between Tanzania and UK.⁶⁶ Under the article, it is expressly stated that investments of nationals or companies of either contracting Party shall not be:

‘nationalised, expropriated or subjected to measures having effect equivalent to nationalisation or expropriation ... in the territory of the other Contracting Party except for a public purpose related to the internal needs of that Party on a nondiscriminatory basis and against prompt, adequate and effective compensation....’

By inclusion of the words “*measures having effect equivalent to ... expropriation*”, BGT observes that article 5 encompasses both direct expropriation, in the sense of formal governmental takings, and *de facto* or indirect expropriations, which are the product of measures short of an actual taking of title, but which nonetheless result in the effective loss of management, use or control, or a significant depreciation of the value, of the assets of a foreign investor.⁶⁷ The Claimant emphasised that the Republic has failed to comply with the requirements of Article 5 by not acted for a legitimate ‘public purpose related to the internal needs of the Republic’; and that has failed to act ‘on a non-discriminatory basis’; and it has failed to pay BGT ‘prompt, adequate and effective compensation’.⁶⁸ Hence, the Republic is in breach of Article 5, thus invoking its international responsibility and, in principle, entitling BGT to seek full *restitutio in integrum* or its monetary equivalent.⁶⁹

In response the Republic argued that BGT’s expropriation claim fails for a number of reasons. First BGT did not have anything that could have been expropriated, even in principle. Second BGT’s own decisions and actions defeat its expropriation claim and third, BGT has failed to prove that any alleged expropriatory act caused compensable harm.⁷⁰ The Republic supported her argument by saying, expropriation occurs when ‘the owner was deprived of fundamental rights of ownership and it appears that this deprivation is not merely ephemeral’. She cited *Pope&Talbot* case, where a NAFTA tribunal required that ‘measures affecting property interests’ had to be of certain ‘magnitude or severity’ to qualify as indirect expropriation. In the *TECMED* case, another authority that was referred to, an ICSID tribunal held that in accordance with

⁶⁶ Signed on 7 January 1994 and entered into force on 2 August 1996

⁶⁷ *Biwater* award 395

⁶⁸ *Biwater*, award 397

⁶⁹ As above, award 398

⁷⁰ As above, award 419

international law, the investment could be considered as having been indirectly expropriated if the deprivation of the foreign investor's property was 'not temporary'.⁷¹

After hearing the arguments from both parties, the tribunal found Tanzania had committed an indirect expropriation of BGT's investment through a series of actions that transcended the behaviour expected of a party to the project contracts and entered the realm of exercise of sovereign authority that violated Tanzania's treaty obligations. Specifically, instead of following the contractually prescribed course for termination of the projects contracts, the Tanzanian government openly repudiated the lease contract with City Water causing public furor, called the performance bond, cancelled the VAT waiver, and deported City Water's expatriate staff. In the Tribunal's view, the cumulative effect of these acts amounted to an unlawful expropriation of BGT's rights in the lease contract and in the project because BGT's rights, although due to expire a short time thereafter under the contracts' Notice of Termination, were still technically valid.

Creeping Expropriation

Creeping expropriation, which is the third type of expropriation is also a form of indirect expropriation. It involves the use of a series of governmental measures to reduce the economic value of the investment. What is involved here is the cumulative impact of the measures rather than individual measures which on their own may not amount to expropriation.⁷²

Regulatory Expropriation

This form of expropriation has been regarded as another form of indirect expropriation. Under this type a measure taken by the host government for regulatory purposes has an impact on the economic value of the asset owned by the foreign investor sufficient to be deemed an expropriation.⁷³ For a measure to constitute regulatory taking that amount to expropriation requiring compensation, and the measure should be a discriminatory one.

⁷¹ As above, award 438

⁷² Subedi (2008) 76

⁷³ Subedi (2008) 77

2.4 Economic Theories of Foreign Direct Investment

There are two conflicting economic theories on foreign investment. One maintains that foreign investment is wholly beneficial to the host state while the other maintains that unless a state turns away from dependence on foreign investment it cannot achieve development.⁷⁴

2.4.1 The classical theory

The classical economic theory takes the position that foreign investment is wholly beneficial to the host economy basing this assumption on spillover benefits the most important being that foreign capital brought into the host state ensures presence of domestic capital for use in other public benefit activities. Arguably, technology brought by foreign investor leads to the diffusion of technology within the host economy; foreign investment creates new employment; the labour that is so employed will acquire new skills associated with the technology introduced; management skills will also be transferred to local personnel; infrastructure facilities built will be to the general benefit of the economy and that upgrade facilities and infrastructure such as transport, health or education for the benefit of foreign investor will also benefit society as a whole. Following all these benefits of foreign investment flows, foreign investment must be protected by international law. Such protection will facilitate the flow of foreign investment and lead to the economic development of less developed countries.

Sornarajah argues that despite the edicts of classical theory, there is no evidence yet that its tenets are based on accurate evidence. Though initial capital inflows may take place through foreign investment, there is evidence that outflows by way of repatriation of profits are greater.⁷⁵ He keeps on arguing that some studies indicate that capital outflows associated with foreign investment may be twice as much as the initial inflows. He argues further that aspects presumed to be advantageous such as new technology may be untrue largely because, technology pegged to investment is not current technology, rather that which outlived its usefulness in the State of Origin but was inaccessible, and therefore seems new to the developing state.

⁷⁴ As above 51

⁷⁵ Subedi (2008) 51

He argues further that the claim that management skills are transferred may also be unreal as higher positions requiring training and confidence are rarely within the reach of local personnel. The claim that infrastructure facilities are built may also be contested as health and educational facilities that are created are only accessible to the elite within the host state who could afford such facilities.⁷⁶

2.4.2 The dependency theory

The dependency theory as opposed to the classical theory has the view that foreign investment will not bring about meaningful economic development. The fact that most investment is made by multinational corporations which have their headquarters in the developed states and operate through subsidiaries in developing states, have interests of its parent company and its shareholders in the home country. As a result multinational corporations come to serve the interests of the developed states in which they have their headquarters. The home states become the central economies of the world, and the states of the developing world become peripheral economies serving the interests of the home states. Development becomes impossible in the peripheral economies unless they can break out of the situation in which they are tied to the central economies through foreign investment.⁷⁷ Sornarajah argues that the resources which flow into the state as a result of foreign investment are seen as benefiting only the elite classes in the developing state, who readily form alliances with foreign capital.

According to dependency theory, foreign investment is bad as it keeps developing countries in a state of permanent dependence on the central economies of developed states and does not promote development. Unless a developing state break out of the dependence situation, economic development becomes impossible in the state.⁷⁸

2.4.3 Tanzania and economic theories of foreign direct investment

Looking at both theories, one can postulate that Tanzania's laws and institutions are oriented within classical theory. This is visible via the way the role of foreign investment activities in the

⁷⁶ Sornarajah (2004) 53-54

⁷⁷ As above, 57

⁷⁸ As above, 58

development process of the country came to prominence and dominance. This is evidenced through the efforts made by Tanzania to create enabling environment for investment by making changes in the national and institutional infrastructure. The trend begun with the formulation of a National Investment Policy in 1990 aimed at creating a positive environment that could attract foreign investment, that would cut through the bureaucracy of interacting with multiple government entities for an investor. In the interest of enhancing the legal framework for arbitration of investment disputes, Tanzania joined the International Centre for Settlement of Investment Disputes (ICSID) and the Multilateral Investment Guarantee Agency (MIGA), as another means of ensuring that the environment to investments in the country was conducive and provided confidence to potential foreign investors.

2.5 Regulation of Foreign Direct Investment

The regulation of FDI is a controversial issue. The bone of contention not challenging the need to regulate, but rather the entity that should regulate. FDI is a considerable investment. However, the end result is not guaranteed, the development is not always an end all. Expectations pegged to FDI and its achievement can have negative connotation for national sovereignty and interests.⁷⁹ It is believed that FDI is an important source of capital for growth in developing countries. The researcher is of the view due to a rapid and massive growth in foreign investment, and an expansion of economic activities gave rise to the need to regulate foreign investment. The question remains who should regulate. According to various literature regulation of international investment can be in different forms, market regulation; national regulation; international regulation through bilateral investment agreements, multilateral, plurilateral or contractual regulation; and lastly regulation can be regional regulation in trade agreements.

Some scholars have argued that countries need a sound business environment in the form of good government regulations to be able to benefit from FDI. Others have suggested that well designed regulatory systems are the only way to ensure an economy can protect itself from the consequences of poorly implemented FDI.⁸⁰ The regulation of the activities of FDI in a host

⁷⁹ Leal-Arcas, R (2011) *International Trade and Investment Law: Multilateral, Regional and Bilateral Governance*

⁸⁰ Kirkpatrick, C et al 'Foreign Direct Investment in Infrastructure in Developing Countries: Does Regulation Make a Difference?' (2006) 15(1) *Transnational Corporations* 143

country is seen at three different levels, the national level where national laws and the implementation of government investment policy inform the process, the regional level which considers treaty obligations involving the Member states who are party to it and the practice of customary international law in the region and the international level which calls for the application of rules of conventional and customary international law.

2.5.1 International Initiatives in Regulating Foreign Direct Investment

Attempts to regulate foreign investment at international level have been made since the inception of the United Nations (UN). Efforts were made under the auspices of the UN, the Bretton Woods Institutions and other economic organisations such as the Organisation of Economic Change and Development (OECD) to regulate investment.⁸¹ Several attempts have been made to come up with a comprehensive code on foreign investment. Due to the existence of conflicting approaches to the issue foreign investment protection and the existence of contending systems relating to the treatment of foreign investment; there is no multilateral agreement on foreign investment.

The first attempt to address the issues of contention with regards to foreign investment was made under the Havana Charter (1948).⁸² The Havana Charter which was to launch the International Trade Organisation (ITO) to replace the temporary GATT arrangement addressed both international direct investment activities under articles 11 and 12 and competition policies under chapter V. Had it been ratified, the ITO thus would have had some competence over both government policies and actions affecting global corporations and the conduct of corporations themselves. Articles 11 and 12 though were not sufficient to provide for strong governance of host nation policies and practices. Under chapter V, the ITO would have had some powers to regulate restrictive business practices of global corporations and have much more authority to regulate the activities of international firms than to regulate government actions affecting these firms.⁸³

⁸¹ Subedi (2008) 19

⁸² Somarajah (2004) 269

⁸³ 'Postwar Efforts at Rule Making' http://www.piie.com/publications/chapters_preview/54/5iie1117.pdf (accessed 10 February 2012)

Another attempt was made in 1959 by major capital exporting countries to adopt an international instrument on foreign investment known as the Abs-Shawcross Draft Convention on Investment Abroad to protect the interests of foreign investors. However, this Draft Convention receives strong opposition from the capital importing countries and was not adopted. Although most of its provisions found their way once again into the 1967 Draft Convention on the Protection of Foreign Property proposed by the OECD, this too was not adopted and remained as a draft.⁸⁴

Another attempt to draft a code of conduct on multinational corporations by now defunct United Nations Commission on Transnational Corporations (UNCTC) failed due to its non-acceptance by the developed states. These instruments contained rules that were favouring the interests of the developing states.⁸⁵ In essence, a movement was geared at creating a New International Economic Order giving greater control over foreign investment to developing states. The codes were resisted by the developed states, which put forward their own version of the code. At the end these efforts did not succeed.

In 1992 there were other efforts to draft instruments on Guidelines on Foreign Investment. This was proposed by a study group of the World Bank and the Multilateral Agreement in Investment (MAI) attempted by OECD. Though these were non-binding it did not succeed due to the fact that in 1990s, there was movement for the liberalisation of the regime for investments. The developing countries turned away from the attempt to create New International Economic Order and were courting foreign investors by granting them high standards of protection through their domestic laws and investment treaties.⁸⁶

With the beginning of the 21st century, new attempts were made to regulate foreign investment. After the failure of the World Bank, IMF, OECD and UNCTC to formulate a balance and comprehensive set of standards on foreign investment, efforts were made by the European Union (EU), with the support of the US, at the Doha Ministerial Conference in November 2001 to put the issue of regulation of foreign investment on the world trade agenda.⁸⁷

⁸⁴ Subedi (2008) 21

⁸⁵ Somarajah (2004) 270

⁸⁶ As above 271

⁸⁷ Subedi (2008) 46 47

2.5.2 Challenges in Establishing Multilateral Accord over the Regulation of Foreign Direct Investment

If states had agreed on the norms that constitute the international law of foreign investment, there could have been a multilateral agreement on foreign investment with substantive rules which apply in the area. As mentioned earlier, there is no such multilateral agreement due to the conflicting approaches to the problem of foreign investment protection and the existence of contending systems relating to the treatment of foreign investment. Several attempts that were made failed due to different interests. There is debate on investment instruments on the extent to grant liberalisation, treatment and protection to foreign investments on the basis of external standards contained in treaties, and to ensure regulatory control to protect the host state's interests at the same time. Clash of interests between developing and developed countries on the subject matter surfaced during the Doha Round of multilateral trade negotiations.

The main difference between these two groups of states centred around the purpose of an international treaty on foreign investment. While developed countries wished to achieve through the treaty the free mobility of capital by minimising the authority of governments with regard to the imposition of conditions and regulations on foreign investors, developing countries wished to protect the autonomy of their respective governments over both investment policy and the right to regulate the activities of foreign investors.⁸⁸ The Doha Ministerial Meeting stressed for development issues to be approached in a balanced manner and the right of regulation in the interests of developing states in achieving their economic objectives to achieve importance.

In the 1980s much of the developing world went through a period of economic difficulty due to the failures of their generally socialist-economic policies and began to reverse their traditional attitude towards foreign investment, which was now seen as a solution to their economic problems. By the mid-1980s the developing countries were competing with each other to attract foreign investment and offering unprecedented incentives to foreign investment.⁸⁹ In the face of such competition for foreign investment, the disintegration of Third World solidarity, the chaos

⁸⁸ A Report (2002) of the Working Group on the Relationship between Trade and Investment to the General Council of the WTO, WT/WGTI/6 of 9 December 2002

⁸⁹ Subedi (2008) 28

in the communist world that followed the collapse of Communism in Europe and the fall of the Berlin Wall, there was no longer the appetite within the UN to push ahead with the adoption of an international instrument to regulate or control the activities of foreign investors. By the late 1980s the pendulum had begun to swing in the opposite direction, rendering the idea of regulation of foreign investment in favour of host countries redundant.⁹⁰ After the collapse of the Soviet Union, most developing countries came to embrace the idea that foreign investment was a necessity for economic development, and good incentives, including legal protection, had to be offered to attract such investment. In 1990s foreign investment law was adjusted or modified to suit the need of Trans National Corporations.

2.5.3 Foreign Direct Investment at Regional Level

In the absence of a global treaty on foreign investment, both BITs and regional treaties have sought to fill the vacuum and lead the way. Regional integration agreements are among the most powerful means to attract FDI. These agreements have dramatically increased since the mid-1980s, the most significant being North American Free Trade Agreement (NAFTA), Mercosur, Association of South East Asian Nations and the European Union, with a single market since 1985. These regional agreements promote FDI as they facilitate more investment among the member countries but they also promote FDI from outside the region or agreements. Regional agreements attract MNEs for a number of reasons. They create larger markets; they imply a greater degree of market deregulation within member states, which attract MNEs from outside.⁹¹ The African Union, East African Community and SADC which Tanzania is a member is also one of those regional groupings.

African context on legal framework for foreign direct investment

African countries have made considerable efforts over the past decade to improve their investment climate. Many countries have liberalised their investment regulations and offered incentives to foreign investors. It is believed after these initiatives the economic performance of the region had substantially improved from the mid-1990s.

⁹⁰ As above

⁹¹ Bartels, FL 'FDI Policy Instruments: Advantages and Disadvantages' UNIDO Working Paper 1/2009 http://www.unido.org/fileadmin/user_media/Publications/RSF_DPR/WP012009_Ebook.pdf (accessed 18 March 2012)

In its efforts the region has gone as far as adopting a program with the purpose of eliminating poverty in Africa and develops economies of the continent. The New Partnership for Africa's Development (NEPAD) is an instrument with the provision of legal certainty to foreign investors adopted for this purpose. Among the initiatives taken is to guarantee a sound and conducive environment for the development of private sector activities and the promotion of foreign investment and trade.⁹²

Despite offering a number of attractions to foreign investors, other sources declared that FDI has increased only modestly, as the image of Africa among many foreign investors still tends to be one of a continent associated mainly with political turmoil, economic instability, diseases and natural disasters. However, although these problems persist in some African countries and although they are a serious impediment to the development of these countries, little attempt is often made to differentiate between the individual situations of more than 50 countries of the continent. As a result, it is believed that many African countries are not even listed for consideration by transnational corporations when it comes to locational decision for FDI.⁹³

Foreign Direct Investment in East African Community

EAC is the regional intergovernmental organisation of the Republics of Burundi, Kenya, Rwanda, Uganda and United Republic of Tanzania. FDI as a means of economic growth has been welcomed by most of these nations. Considerable liberalisation of the prevalent investment regulations has been undertaken to facilitate the smooth flow of FDI into these economies. East Africa does not have foreign investment legislation which is binding on the partner states. The applicable law is just a model that the partner states may adopt.⁹⁴ The foreign investment laws that are generally applied in East Africa are those of the partner states. Some partner states have also ratified international instruments in relation to foreign investment.

East Africa is a region overflowing with potential foreign investments with the aim of harnessing this potential to cause economic growth and development in the region. The partner states of the

⁹² Established in 2001 at OAU 37th Session, AHG/Decl. 1 (XXXVII) <http://www.africa-union.org/root/AU/Documents/Decisions/hog/11HoGAssembly2001.pdf> (accessed 24 January 2012)

⁹³ <http://www.unctad.org/en/docs/poiteiitm15.pdf> (accessed 23 February 2012)

⁹⁴ Investment Code, 2006, <http://www.eac.int/invest/index>. (accessed 22 February 2012)

EAC have agreed to cooperate in the areas of investment and industrial development,⁹⁵ with the aim of rationalise investments and harmonise incentives with a view to promote the Community as a single investment area.

2.6 Conclusion

In concluding therefore, one can say there is a relationship between FDI and economic development. There is a belief that FDI generates positive effects for host countries. From classical point of view, FDI has shown its ability to contribute significantly to increase capital, boost human capital and speeds up technological transfer. FDI can also play an important role in modernising a national economy and promote economic development. Developing countries are trying to liberalise their economies in order to attract FDI but, attracting FDI is not enough for economic development, the host country need to have policies in place in order to reap the benefits of FDI. It needs to put rules and regulations in place that will ensure economic development for the country. A sound regulatory framework and efficient supporting institutions to enforce the relevant laws and regulations are imperative for FDI to enter and succeed.

The UN, OECD and other international institutions had played a major role in trying to come up with standard rules on foreign investment. Despite all these efforts to regulate investment, none of them have this item on their active agenda, leaving the matter to customary international law and BITs or Free Trade Agreements. Their contributions though, may not have led to a successful conclusion of a global comprehensive treaty on this subject, but they have helped in the development of the main principles of law governing treatment of foreign investment under international law. Most of the fundamental principles of foreign investment law make foreign investors to be entitled to the protection of such principles even in the absence of a BIT between a host and home state.

It is worth noting that these principles of international foreign investment law are worth reading because the underlying idea behind them is to ensure there is no discrimination in the conduct of international business.

⁹⁵ The Treaty for the Establishment of the East African Community, 1999 Chapter 12 arts 79 & 80

Lastly, it has been noted that the existence of an international minimum standard for the treatment of foreign investment has been frequently challenged in the past. This has been the object of tension between developed and developing countries, with several countries challenging the existence of a customary international law of minimum standard. The Minimum Standard of Treatment ensures investments of investors, fair and equitable treatment and full protection and security in accordance with the principles of customary international law. For that matter is binding upon a State and provides a minimum guarantee to foreign investors, even where the State follows a policy that is in principle opposed to foreign investment.

CHAPTER THREE

AN OVERVIEW OF LEGAL, REGULATORY AND INSTITUTIONAL FRAMEWORK FOR FOREIGN DIRECT INVESTMENT IN TANZANIA

3.1 Introduction

Chapter three gives brief introduction to Tanzania, the centre of this study; where the focus is on legal characteristics. The chapter critically examines the laws governing investment in Tanzania. The aim is to see if the laws are sufficient to address issues of economic development and point out the problems. Review of laws related to foreign investment since independence will be reviewed and some amendments occurred will be looked at as well. Details of challenges in regulating FDI are presented under the chapter. Regulatory and institutional framework for regulating foreign investment will be conducted. This is to see whether the agency entrusted with dealing with investment matters is competent in regulating and monitoring investment activities to foster development.

Specific research questions have been formulated to answer the vital issues. Following the research objective two questions are formulated to guide the study in answering the vital factual legal issues. The first and main question, central to this study is:

What is the state of legal and regulatory framework for FDI in Tanzania?

The aim of this question is to verify whether there is deficit in regulating FDI.

Other question formulated to answer all relevant concepts of this study, and help formulate the answer to the main question will be discussed under chapter four:

Why the need for review of FDI legal and regulatory framework in Tanzania?

3.2 Tanzania Legal Characteristics

Tanzania is a country in East Africa and lies between one and eleven degrees south of the Equator. Dodoma is the capital and Dar es Salaam, is the largest and commercial city. Tanzania covers the surface area of 947,000 square kilometres. It shares borders with eight countries. Its

northern border is shared with Kenya and Uganda, the southern one with Zambia, Malawi and Mozambique. Democratic Republic of Congo (DRC), Rwanda and Burundi are on the west. The Indian Ocean lies in the eastern part where it embraces the beautiful island of Zanzibar. Another beautiful island, Mafia, is located down-south the coast line.⁹⁶

Tanzania had its own legal system based on customs and practice before Second World War. After World War II, Tanzania the then Tanganyika was declared a Trust Territory of the United Nations, with Britain's role to ensure its progress towards self-government and eventual independence. Having become under British protectorate, Tanzania has adopted a legal system based primarily on English common law. In terms of the hierarchy of legal, administrative and regulatory instruments, the first source of law in Tanzania is the Constitution.⁹⁷ Constitution is the supreme law of the land and provides for a bill of rights. In Tanzanian Constitution there are also provisions for 'claw back' so the rights under the bill of rights are not absolute, but subject to legal regulation.

The second tier of the hierarchy is the statutes or acts of Parliament, which are published in the Government Gazette. The third source is the case law, comprising cases from the High Court and Court of Appeal, which create precedents that bind lower courts. The fourth source is received laws, which includes common, doctrine of equity and statutes applicable in England law before 1920. And the fifth source of law is customary and Islamic law. Finally, international treaties and conventions are a source of domestic law as long as they have been ratified by Parliament.⁹⁸

3.3 Tanzania Investment Promotion Policy

Following the liberalisation of the economy and efforts to create an enabling environment for investment, Tanzania established a clear policy of openness to both foreign investment and trade. Efforts have also been made to improve public private sector dialogue on investment issues, as part of the efforts to facilitate the role that private investments can play in the development of the country.

⁹⁶ <http://www.tanzania.go.tz/> (accessed 2 December 2011)

⁹⁷ The Constitution of the United Republic of Tanzania, 1977 as amended from time to time

⁹⁸ <http://www.tanzania.go.tz/> (accessed 2 December 2011)

The national investment promotion policy of 1990 was reviewed in 1996 taking into account the new policy developments in the country during the 1990-96 periods. The revised policy included greater emphasis on promoting domestic capacities and encouragement of domestic entrepreneurship, export development, facilitation of new technology and enhancement of transparency in the legal framework and deregulation of investment processes. It further made improvements in providing more competitive incentives with a view to directing investments towards areas that are most crucial for Tanzania's economic development.⁹⁹

3.4 Foreign direct investment inflow in Tanzania

Tanzania is regarded as one of the countries with the highest growth potential in Africa with enormous potential as an investment destination. It is one of the most promising emerging markets in the region, offering a unique combination of developed economic infrastructure and a vibrant emerging market economy.¹⁰⁰ Tanzania investment guideline indicates that between 2004 and 2007 Tanzania GDP grew at an average annual rate of 7.3 percent making it one of the fastest growing economies in Africa.

Tanzania is one of the Africa's best performing countries in terms of GDP growth and attracting FDI. When Tanzania Investment Centre, the government primary agency in dealing with investment started full operation investment inflows have increased abruptly from about 178 projects worth US\$ 0.87 billion per year recorded in the year 2000 to 871 project worth US\$ 6.68 billion per year in 2008.¹⁰¹ This reflects both the available investment opportunities as well as the positive restructuring of the investment regime that has taken place. Another important factor is its remarkable set of natural resources, long term stable democracy and strong macroeconomic performance.

Another important factor worthy noting, when the 1997 Act was enacted shortly after the launching of the New Investment Policy of Tanzania in 1996, the Act provides the basic investment framework for Tanzania, with new and modern legislations reflecting the world

⁹⁹ Tanzania Investment Promotion Policy, 1996 <http://www.tzonline.org/pdf/nationalinvestmentpromotionpolicy.pdf>

¹⁰⁰ Tanzania Investment Guide 2008 and Beyond, <http://www.tic.co.tz/ticwebsite.nsf/FILE/TICGuideline.pdf>
(accessed 20 February 2012)

¹⁰¹ <http://www.tic.co.tz>

economic conditions in general and Tanzania's conditions in particular. As a result of these commendable government efforts FDI inflows in the country rose from US\$ 12 million in 1992 to US\$ 260.2 million in 2004 after reaching a peak of US\$ 516.7 million in 1999.

This inflow supposed to make a great contribution to the overall economic development of Tanzania. It was expected for the foreign invested enterprises to contribute to tax revenues, bring in capital, technology import, create employment opportunities, impart skills and other benefits. But the FDI has so far not give that positive impact as what people were look forward to see.

3.5 Substantive laws and regulatory frameworks related to foreign direct investment in Tanzania

The laws and regulations in Tanzania have been put in place to provide a legal framework conducive to the functioning of a market economy. They include laws dealing with capital markets, mining investments, banking and financial institutions, land ownership, taxation, foreign exchange, petroleum exploration and development, and export-processing zones. A number of practical regulations liberalising conduct of business and reducing red tape have been introduced.

3.5.1 Major laws and regulation affecting foreign investment

In Tanzania major laws and regulation affecting foreign investment is in five groups. These include investment; trade, taxation, finance and audit; labour, immigration and citizenship; environment, forestry, construction and land; and trademarks.

Investment

Under investment category there are Tanzania Investment Act, Export Processing Zones Act, 2002, the Capital Markets and Securities Act of 1994, and the Mining Act of 1998 as repealed in 2010.

Trade, taxation, finance and audit

Under this group there are Business Licensing Act of 1972, Banking and Financial Institutions Act of 1991, Customs Tariff (Amendment) Act of 1976, Income Tax Act of 2004, and Value Added Tax Act of 1997.

Labour, immigration and citizenship

There are two legislations that affect foreign investment in this category namely, Trade Union Act of 1998 and Immigration Act of 1995.

Environment, forestry, construction and land

Land Act of 1999 and Village Land Act of 1999 provides for the management and administration of land.

Trademarks

Lastly, there is Trade and Service Marks Act of 1986, Patents Act of 1987 and Copyright and Neighbouring Rights Act of 1999.

3.5.2 Legal framework of investment at independence

Tanzania Mainland the then Tanganyika attained its independence on 9 December 1961 from British. Following independence, the state in Tanganyika took an active role in developing the economy. Armed with a World Bank report on Tanganyika's development potential, the state sought out foreign investors willing to establish import substituting industries in the country. Foreign Investment (Protection) Act was enacted in 1963 to give protection to certain approved foreign investments in order to attract investors in the country.¹⁰² Before independence during the colonial period, all economic policies were geared to intensify colonial exploitation and to safeguard colonial interests at the expense of indigenous communities. This went hand in hand with the enactment of some laws that were obstacles to foreign investors and create environment favourable to them.

Tanganyika Foreign Investment (Protection) Act, 1963

The enactment of this legislation provided statutory guarantees to foreign investors which would encourage them to invest in the country. In addition, the government entered into bilateral

¹⁰² Act 40 of 1963

agreements with foreign governments on encouragement and promotion and protection of investments. The exercise of enactment of this investment legislation succeeded in attracting foreign investors in the country where investors from developed countries came and invest in the country. These include the United State of America, Switzerland, Federal Republic of Germany and German Democratic Republic. Despite its purpose and achievement things were not smooth. In the process of liberalisation of the economy it was felt that the Foreign Investment Protection Act of 1963 has been overtaken by the development that has been taking place both internally and externally. It was vivid that even after the passage of this Act; Tanganyika could not attract foreign investors in manufacturing sector.¹⁰³

Moreover, soon after independence, the TANU government adopted a World Bank development model which was the result of studies conducted during the last decade of the colonial era. The model required further integration of rural dwellers into the world capitalist market through the intensification of export cash crops; cotton, tobacco, sisal, groundnuts, tea, coffee, pyrethrum, sugar and cashew nuts.

Also in 1966 the country found itself in serious socio-economic and political crisis, which was fuelled by conflicts with Britain, the Federal Republic of Germany and the USA that upset the flow of foreign industrial investments and foreign aid to finance agricultural, industrial and other development projects. Therefore new tactics and new directions were imperative.

Furthermore, the approach used by the TANU government after independence stemmed from the fact that TANU and its allies wanted to get rid of colonialists contributed to the failure. Thereafter it was total confusion and disappointment to both leaders and the led alike. It is against this background that the Arusha Declaration was proclaimed in 1967. As was discussed in chapter two, the Nyerere's ideology on socialism through the Arusha Declaration, legislation was enacted and then mass nationalisations of various investments in the country occurred.

3.5.3 Some Changes and Tanzania Investment (Promotion and Protection) Act, 1990

¹⁰³ Peter (1994)

The purpose of the National Investment (Promotion and Protection) Act of 1990 was to stimulate local and foreign investment by establishing rules governing investment in Tanzania enterprises, particularly foreign capital. The Act applies throughout industry except petroleum and minerals. While the Act replaced the Foreign Investment (Protection) Act of 1963, it incorporated with necessary amendments, a number of other statutes including the Companies (Regulation of Dividends and Surpluses and Miscellaneous Provisions) Act, 1972.

It is important to be noted that, another purpose for the 1990 Act was to avoid the gross economic errors and mismanagement that have blemished so many parastatal enterprises financed from abroad by means of a monitoring mechanism with statutory powers of control. This was through establishment of machinery for the stimulation of investment in Tanzanian industry and offers tax incentives for investment in new enterprises and the expansion or rehabilitation of existing enterprises. It also lay down rules to ensure that new investment, particularly from overseas, does not lead to abuses and is directed towards enterprises of greatest importance to the Tanzanian economy without creating new burdens only capable of satisfaction in foreign exchange.¹⁰⁴

3.5.4 The current law related to foreign investment in Tanzania

Tanzanian government like most other governments has been actively promoting its country as investment destination. It has increasingly adopted measures to facilitate the entry of FDI. Examples of such measures include liberalising 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. The country provides the best incentives to investors like tax incentives as part of these promotional efforts. In improving the overall legal framework for investment activities in the country, Tanzania amended the National Investment (Promotion and Protection) Act of 1990 and came up with Tanzania Investment Act of 1997.

Tanzania Investment Act, 1997

¹⁰⁴ Tanzania's New Investment Code <http://www.tzaffairs.org/1990/09/tanzania's-new-investment-code/> (accessed 27 March 2012)

The investments in Tanzania are now governed by the Tanzania Investment Act.¹⁰⁵ This Act has to be read together with the Financial Laws (Miscellaneous Amendments) Act.¹⁰⁶ The main purpose of enacting the 1997 investment act is to guide investment activities as well as to provide for more favourable conditions for investors. This Act does not apply to mining and oil exploration sectors. These sectors are governed under the Mining Act, 1998¹⁰⁷ and the Petroleum (Exploration and Production) Act, 1980 respectively.

Unlike the National Investment (Promotion and Protection) Act of 1990, the 1997 Act of has no clear schedule on investment areas. The 1990 Act had a very clear schedule specifically showing investment areas. Under the schedule Controlled areas were set for large investment which required for private/public partnership. As pointed out by Maina and Mwakaje, investments envisaged here were like iron and steel production; machine tools manufacture; chemical fertilizer and pesticides production; and airlines. Reserved areas were of strategic importance and were exclusively reserved for public investment. Importantly, there were investment areas purposely for local investments. Unfortunately, this is not the case with the 1997 Investment Act. The whole country is up for snatch for both local and foreign investors. There is no reservation of certain areas of the economy exclusively for nationals.¹⁰⁸ These included retail and wholesale trade; product brokerage; business representation for foreign companies; public relations business; operation of taxis, barber shops, hairdressing and beauty salons, butcheries just to mention few.

This loophole led to complain among the local petty traders. The question that need to be answered can we real classify them as investors who bring in capital for country's economic development; or just competitors who came to suffocate and create unfair competition to the local community who are not able to compete since they do not have enough capital.

¹⁰⁵ Act 26 of 1997

¹⁰⁶ Act 27 of 1997

¹⁰⁷ Tanzania's Parliament passed the new Mining Act (Act 14 of 2010). The Act was re-enacted with substantial amendments the provisions that regulate the law relating to prospecting for mining

¹⁰⁸ Maina & Mwakaje (2004) 19

As also pointed out by Maina and Mwakaje, among the weaknesses in the 1997 Act is its silence on joint venture provision.¹⁰⁹ Liberation of the economy was hailed as a policy that will open avenues through which the local and foreign capital would walk together to prosperity. The real logic for giving preference to or requiring joint ventures is to try to capture more of the benefits that foreign investors have to offer. In particular, technology transfer, access to external markets, and more robust backward linkages to the domestic economy than would take place without preferences/requirements for joint ventures. On the other hand, local partners can be particularly valuable in providing location-specific knowledge regarding host-country markets, local tastes, local business practices, local labour practices, local suppliers, and local business-government relations.¹¹⁰

3.6 Incentives and Tax Policy and its Effect to Foreign Direct Investment

Host countries do always expect to maximise the long-term economic benefits for foreign corporate presence. However, there are various costs associated with FDI as well. Among the costs include those related to countries competing for FDI; market failures in the investment process and the possible divergences between foreign companies and national interests. For example, promotion of FDI has been very expensive as developing countries often make major concessions in terms of special incentives to foreign investors in order to compete for foreign investment with other countries. These incentives include among others lower income taxes or income tax holidays, import duty exemptions, and subsidies for investment. In Tanzania, incentive packages were introduced during the economic liberalisation era.

3.6.1 Incentives and Guarantees Offered by Tanzania Investment Centre

The TIC offers financial incentives and guarantees to those who pass its tests for the Certificate of Incentives. For example tax reductions in the areas of import duty and VAT; Duty drawbacks on imported inputs; reduced corporate taxes through capital exemption, favorable asset depreciations, and lower withholding taxes; automatic ability to hire up to five expatriate employees without government review (two leading industries, mineral and petroleum, actually

¹⁰⁹ As above, 27

¹¹⁰ 'FDI and Joint-Ventures Requirements' http://www.piie.com/publications/chapters_preview/53/7ie258x.pdf (accessed 14 May 2012)

get more generous incentives and are not restricted to the ceiling of five expatriate employees, for instance); practically unrestricted repatriation of funds; greater protection by the government against non-commercial risks; more assistance from government; Fast-track renewals for licenses, residence and work permits, and so on through TIC assistance; and guarantee against expropriation and nationalisation, unless government fairly and expeditiously compensates for nationalisation (Tanzania is a signatory of several international treaties on this matter).

3.6.2 Tax Policy

The Government of Tanzania has implemented tax administration reforms to improve efficiency as well as rationalise the tax structure. The tax base and rate structure of the Tanzanian tax system has been rationalised and streamlined with a view to instituting a fair, simple, equitable, efficient and investor friendly tax regime. A number of taxes have been abolished, the regulatory framework has been harmonised, an incentive regime has been put in place and the rates have been gradually reduced.¹¹¹

Tanzania has offered a tax incentive regime conducive to investment provided for in the various tax statutes, like the Income Tax Act,¹¹² Value Added Tax Act¹¹³ and the East African Customs Management Act, 2004. Also the Tanzania Investment Act, Mining and Petroleum Acts are also used to facilitate the granting of tax incentives. The incentives cut across a broad spectrum of investment goods including non-taxation of imports of capital goods and raw materials, deferment of VAT on capital goods and capital allowances on investment goods for income tax purposes. Also in place are exonerations and exemptions of goods and services specifically for investment purposes.

In offering economy wide tax incentives, special attention is directed to the lead and priority sectors. For all these sectors, except petroleum and gas sector, acquisition of all capital goods and parts are zero rated for import duty purposes and VAT thereon deferred. Research expenses for agriculture are allowable for income tax purposes, while capital acquisitions are 100 percent

¹¹¹ http://invest-in.tanzania.ru/taxation_in_tanzania.htm (accessed 2 May 2012)

¹¹² Act 11 of 2004

¹¹³ Act 24 of 1997

expensed. To attract productive investment in the petroleum and gas sector petroleum legislation was enacted. Equipment and materials used in exploration are tax-exempt.

Investors in priority sectors enjoy zero import duty rates for importation of capital goods and deferment of VAT. There is also a set of exemptions granted on those investing in export processing through the Free Economic Zones Authority (FREZA) and Export Processing Zones (EPZ).

Among the tax incentives introduced by Tanzanian government has raised a lot of complaint to local community like tax holidays. Under a tax holiday, qualifying newly established firms are exempt from paying corporate income tax for a specified time period for example five years. The provisions may exempt firms from other tax liabilities as well. There is elimination of tax on net revenues from investment projects over the holiday period.

Investment experts, particularly from investment promotion agencies, view incentives as an important policy variable in their strategies to attract FDI for economic development. The government has offered unreasonably large incentives to entice foreign companies in the country. But, it has been recognised that investment incentives have only moderate importance in attracting FDI.¹¹⁴ Furthermore, this has a negative impact on fiscal revenues and creates significant possibilities for suspicious behaviours from tax administrations and companies. Unlike advanced economies, which have tended to broaden tax bases and cut tax rates while maintaining revenues, developing economies like Tanzania have cut rates, introduced special regimes and lost revenues.¹¹⁵

Although granting investment incentives may promote long term growth, but it goes against another major goal of the government of Tanzania of raising tax revenue. As incentives often cause losses of tax revenues (for example, duty exemptions), Tanzanian government through Tanzania Revenue Authority (TRA), bears the burden of such incentives. TRA and TIC have

¹¹⁴ See UNCTAD-DTCI. Incentives and Foreign Direct Investment, Geneva and New York: United Nations Publications, E.96.II.A.6, 1996; OECD

¹¹⁵ 'A Partial Race to the Bottom: Corporate Tax Developments in Emerging and Developing Economies' IMF Working Paper WP/12/28 <http://www.imf.org/external/pubs/ft/wp/2012/wp1228.pdf> (accessed 30 April 2012)

been at the centre of this conflict between long term economic growth (advocated by TIC) and short term tax gains (the driving force at TRA). TRA finds claims regarding future economic benefits hard to accept if they involve incentives that prevent it from meeting its collection targets. Even though the 1997 Act amended financial laws enforced by TRA in order to reduce conflicts between the two institutions, TIC and TRA still face conflicts of interpretation. Draws from literature reviewed this study finds that Tanzanian government is facing challenge in implementing its policy of decreasing tax benefits for registered investors as by implication, is increasingly reluctant to sacrifice tax revenues in the name of long term growth.

These tax incentives like tax holidays to large foreign companies have also brought about public outcry against the policy. This is partly associated with FDI's failure to contribute to country's economic growth efforts caused by poor management of FDI and weak regulatory mechanisms. Incentives given to FDIs are generous, wide open ended and the government is deemed not to have put in place strategic regulatory laws, rules and procedures to control and monitor operations of FDIs in terms of what they are doing and what they are not allowed to do. As a result, it entails significantly higher revenue cost for the government and abuse by some foreign companies. It simply result in the transfer of tax revenues from the host country treasury to the home country treasury. Companies use this loophole by shifting profits or real activity elsewhere in such an extreme fashion as to escape paying tax once the grace period is over.

A good example is when majority of the hotels that were listed for rehabilitation or were not functioning well and were ones situated in the National parks, rather than those that were in business and conference centers or operating casinos. Beyond the heavy investments, the government, in a bid to create an enabling environment, has been giving tax exemptions to investors. Over the years, investors whose investments were approved by the TIC have been enjoying a tax holiday of five years as part of the incentives. For this matter, many enterprises have changed hands before the elapse of the five years to allow another investor to enjoy the same. For example, the Sheraton hotel became the Royal Palm in 2001, just before the five years had expired; and by 2004, it was sold to another investor, the Swiss based Movenpick; and now is no longer under the Swiss investor but under Serena hotels.

3.6.3 Avoidance of double taxation treaties

To increase inward FDI, policy makers increasingly resort to the ratification of double taxation treaties (DTTs).¹¹⁶ This can have costs of negotiating and ratifying the contract and giving up some fiscal sovereignty. There could also be a loss in tax revenues for at least one of the signing parties. This is particularly important from the point of view of developing countries as most treaties favour residence-based over source based taxation.

Tanzania so far has signed Double Taxation Treaties (DTAs) with various countries include Canada, Denmark, Finland, India, Italy, United Kingdom, Norway, Sweden and Zambia. Tanzania is also in the process of negotiating treaties with several countries including Belgium, Burundi, Iran, Lebanon, Malaysia, Mauritius, Pakistan and Rwanda.¹¹⁷ This study has discovered that DTAs offer a gain to the investor with no impact on net additional investment. Moreover, it may have the unintended effect of encouraging investors to repatriate profits rather than to reinvest them in the host country where they would further promote economic development. Another unintended effect of these methods is what is known as ‘treaty shopping’ by investors. They could avoid, seemingly legally, higher taxes in a country where they want to invest, by funneling their investment through another country with which the targeted country has a tax treaty with favourable provisions.¹¹⁸

3.7 Institutional framework for foreign investment in Tanzania

Some countries have statutory structure specifically governing the regulation of investment. India for example has central regulatory authority responsible for the regulation of investment in the country. In other countries, different regulators become involved to the extent that entities subject to their jurisdiction end up providing investment advisory services.

¹¹⁶ ‘The Impact of Double Taxation Treaties on Foreign Direct Investment: Evidence from Large Dyadic Panel Data’ http://personal.lse.ac.uk/barthel/docs/DTT_FDI.pdf (accessed 4 May 2012)

¹¹⁷ <http://www.tanzania.go.tz/commerce.html> (accessed 4 May 2012)

¹¹⁸ ‘Tax Incentives and Foreign Direct Investment’ a Global Survey. UNCTAD/ITE/IPC/Misc.3 ASIT Advisory Studies No. 16, http://unctad.org/en/docs/iteipcmisc3_en.pdf (accessed 29 April 2012) 29

The pro investment attitude by government of Tanzania is clearly demonstrated by the innovative investment legislation, the increasing number of FDI in the country and economic and structural reforms that have led to substantial progress in establishing a functioning market economy. In Tanzania, institutional support for priority investment projects is readily available from the agency entrusted with dealing with investment matters, Tanzania Investment Centre (TIC) and other government institutions.

3.7.1 Tanzania Investment Centre

The main purpose of establishing TIC is to have an effective and efficient investment agency responsible to promote, coordinate, encourage and facilitate investment in Tanzania and to advise the government on investment related matters.¹¹⁹ Section 15 shows the overall missions of the Centre is to promote and facilitate investment for national economic growth by enhancing an environment conducive for business and entrepreneurship growth.

TIC is the focal point for all investors and first point of call for potential investors. In order to strengthen and expedite facilitation services, six different senior officers from government institutions have been permanently stationed at TIC to serve investors under one roof and the general direction of the TIC Executive Director. Presently these officers include those from Ministry of Lands and Human Settlements (access to land);¹²⁰ Tanzania Revenue Authority (national government taxation); Immigration Department (Class A and Class B work permits); Ministry of Labour (Class B work permits), Ministry of Industry and Trade (national business licenses); and Business Registration & Licensing Agency (registration of companies, business name registration, 'industrial' licenses, trade and service marks, patents and copyrights).

3.7.2 Practicality of Tanzania Investment Centre as a 'One Stop Centre'

Theoretically 'one stop centre' is right and good but practically it is not possible. The crucial and important question is whether TIC is real a 'one stop shop'. The above mentioned government institutions are placed under one roof to enforce core regulations affecting most investors.

¹¹⁹ Section 4 of the Act

¹²⁰ Followed the new responsibilities given to TIC by the Land Act of 1999, the Centre now is supposed to help the Ministry of Land to build a Land Bank, where the occupation of land by investors is tagged

Although they are under one roof, they have to work with their home institutions in the background and deliver various authorisations to the investor at the TIC.

The Tanzania Investment Act of 1997 states that government agencies must reply to TIC requests within 14 days. If not, TIC can assume its request is tacitly answered in the affirmative. In practice, however, if the request is for a document such as a license or certificate, the investor simply has to wait for the document, because TIC cannot issue it in lieu of the issuing agency. If the investor submits all the required evidence, however, then the next step is up to TIC. It then takes TIC seven days to issue the Certificate of Incentives.¹²¹ When the investor lets TIC handle all facilitation matters, it typically takes one month for TIC to make its final decision. Immigration requirements alone can take from seven to 14 days.¹²²

Licensing Agencies

Sectoral licenses (‘major licenses’) are normally delivered in specialised ministries; mining and fishing for example, these ministries have not yet assigned staff to TIC. However, TIC can send its staff to help settle matters in those ministries on behalf of investors. Where complexities occur, the investor must accompany TIC facilitators in specific government institutions to elaborate on information contained in the application. Otherwise, the facilitators can handle processes in the background without the investor’s presence. Also the investor cannot have all the services required under TIC, he has to go physically to other government institutions. A good example is the National Environmental Management Council (NEMC).

Services Offered by the Centre

It is also evident that the Centre’s services are not fully available to all investors. In the process of investing in Tanzania though not clearly stated anywhere yet, the first step for the cautious investor should be to contact NEMC. NEMC will assess whether an Environmental Impact Assessment (EIA) study must be done for the project or no more EIA investigation is necessary. This would be determined by information provided for by the investor in preliminary assessment

¹²¹ See Business Guide, 40

¹²² Tanzania Investor Roadmap: Primers on Regulations 3rd Edition, prepared for USAID/Tanzania under Contract No. PCE-I-817-99-00002-00 by Development Alternatives, Inc. (DAI) Private Enterprise Support Activities (PESA) Project Dar es Salaam, 23 January 2004

form. If an EIA is needed, the investor will contact one of many specialised local consulting firms to do the assessment. There are no explicit rules prohibiting foreign experts to conduct the EIA, but NEMC encourages the use or participation of a local firm.¹²³ If EIA is not needed, or if the cost and conclusions of the EIA still warrant investing in Tanzania, the owners would then go through the core formalities.

First, they will register the company at the Business Registration and Licensing Agency (BRELA). This process involves a name search to verify that the proposed name is not used by another business. Then they will obtain a tax identification number (TIN) from the Tanzania Revenue Authority (TRA). At TRA, the business will also get a VAT registration number, especially if the start of operations is imminent.

The third step is to obtain a general business license from the Ministry of Trade's Internal Trade Section. Otherwise, the general business license will be issued by the local government with jurisdiction over the location of the business. Tanzania has an Office of Safety and Health Administration (OSHA), where its mandate was enlarged in 2003 to cover any workplace, a new mandate that will likely become controversial. Finally, new investors with annual exports above US\$ 100,000 who will export at least 70 percent of their production can apply for Export Processing Zone (EPZ) operator status. EPZs come with attractive incentives described in a 2002 law that became operational in early 2003.¹²⁴

For the above challenge it is difficult for TIC to work effectively as a 'one stop' centre, this study has suggested some solution which is provided for under chapter four. Introduction of electronic system (E-platform) has been suggested and discussed in detailed in the said chapter.

3.7.3 Performance of the Centre

Tanzania Investment Centre record of promoting, attracting and retaining investors in the country since its inception is undisputed. The question is whether the level of investment attained is beneficial to the country's economic development. Despite all the successes the current level

¹²³ Tanzania Investor Roadmap: Primers on Regulations 3rd Edition (2004)

¹²⁴ Act 11 of 2002 'Tanzania Export Processing Zones Act'

of investment is not yet adequate for realising Tanzania's Development Vision 2025 goal of reducing poverty and promoting sustainable development through GDP growth of over 8 percent.¹²⁵ This study have find out there are still some weaknesses in regulating and monitoring foreign investors that need to be addressed for the country to benefit more from foreign investment. If the country is to achieve its development goals, there are some suggestions for the recent investment to GDP ratio to be increased to at least 25 percent to achieve a growth rate of its intended goal of 8 percent. This can be achieved by making further economic and legal improvement for example in regulation and institutional effectiveness.

3.7.4 Limited Institutional Capacity in Monitoring Investments or After Care Services

Apart from promoting investment, Tanzania Investment Centre is also offering investor friendly post investment services (After Care Services) and monitoring. This will provide feedback on fulfilling investment goals and aspirations. Monitoring would provide opportunity for closer cooperation between TIC and investors in resolving problems and fostering greater impact of investments. Monitoring can be done by following the post statutory measures as provided for under part VI of the Investment Regulations,¹²⁶ where a holder of an investment certificate is required to inform TIC in writing of the date of commencement of investment. TIC is expected to verify the commencement of operations. The investor has to notify TIC in writing if a holder of investment certificate ceases to operate. A holder of investment certificate is also required to inform TIC when: a person other than the person to whom the certificate was issued has succeeded to the investment; the name or description of the business or enterprise is changed or there is an enlargement of or substantial variation in the investment. Tanzania Investment Centre is expected to verify those information and if satisfied amend the certificate.

Track down investors

Statutorily this is okay, but practically this is not the case. The burden of making FDI work for the development of Tanzania lies within the realm of the government. The pertinent question what monitoring and enforcements mechanisms are in place to ensure FDI is regulated well? In

¹²⁵ Report on the Study of Growth and Impact of Investment in Tanzania <http://www.tic.co.tz/TICGrowth-Impact.pdf> (accessed 3 May 2012)

¹²⁶ Investment Regulations of 2002

Tanzania follow up of businesses like firms' benefiting from the incentives is neglected. The capacity to monitor is particularly weak. There are not enough resources to track down investors. It is a well-known fact that without effective monitoring, governments cannot ascertain the magnitude of actual investment inflows as this information is vital to governments as it provides input to enable them to direct and control foreign investment, to formulate investment policies and strategies, and to target foreign investment projects by industry, characteristic and home country for promotion. This lack of monitoring capability has also led to a situation in which foreign investors in a host country because of weak monitoring systems, promise anything government demand in order to obtain investment licenses and incentives and then configure the investment project in whatever manner best suits their interests.

Economic development goal

All registered investors are required to submit a 'progress report' to TIC within six months of being registered. Renewal of incentives beyond this point requires a petition that leads to examination of the project. Tanzania Investment Centre's challenge of limited staff, does not give it the capacity to effectively monitor post application to ascertain whether the government's vision of fostering long-term economic growth through investment has been attained and the registered investment has brought in any economic impact to the country. When looking on part VI of the 2002 regulations there is no mention of tracking achievement of economic development goals.

3.7.5 Administration of tax incentives

While tax incentives are enunciated in the tax law, their administration is carried out by different government agencies. For example, tax deductions or allowances on employee training may be administered by the labour department, duty exemptions by the customs department and income and profit tax exemptions by the revenue department. Such diversity of agencies dealing with tax incentives tends to increase the inconvenience of doing business. It is generally recognised that investors prefer to deal with one government agency and that they like to be able to determine from the start the total package of incentives available.

3.8 The Impact of Chinese Investments in Tanzania

3.8.1 Chinese Presence in Tanzania

This study learnt there are eight different objectives behind China's presence in Africa including Tanzania. These include assurance of the supply of raw materials for China, create a market for Chinese products and services, obtain land for agricultural purposes, channel migration of Chinese people to Africa, gain diplomatic support from African countries, present an alternative to the Western development model, provide an alternative to Western development cooperation and emphasise China's status as a superpower.¹²⁷

China is already present and quite active in Tanzania since its independence in 1961. At that time the Chinese leaders supported movements for independence and anti-colonial activities. In the post-colonial era Chairman Mao Zedong supported socialist regimes in particular. The construction of the Tanzania Zambia Railway Authority (TAZARA) railway line took place in the 1960s. It runs from the Zambian copper mines capital, Kapirimposhi to the Tanzanian commercial city and main port, Dar es Salaam. It was built by the Chinese because no other donor was willing to provide support to the socialist government of Tanzania.

The presence of China can also be seen in different ways. The number of Chinese people living and working in Tanzania has increased. The goods and services rendered, for example from Tanzania, China imports mainly ores, wooden logs and cotton, while it exports garments, batteries and other consumer goods to the country. China is an important source of aid, soft loans and cheap products for Tanzania. There are development assistance help to build the necessary infrastructure although the quality may be low and operation and maintenance are not always organised. China has a commitment to invest in Tanzania. A Chinese mission visited Tanzania in August 2006 made some promises to invest and this was welcomed well by the then Tanzanian vice president who pledged government support to investors trying to achieve the goals of the government. The number of Chinese projects registered for investment since then has increased to 250.

¹²⁷ Dijk, MP (ed) *The New Presence of China in Africa* (2009) 11 12

3.8.2 Chinese investments in Tanzania

Historically the main source countries of FDI funding to Africa are the United States, the United Kingdom and France. China has dramatically increased its presence in the continent in the past decade and became the 5th largest country of origin of foreign investment on the continent in 2009; its growing impact on trade, aid and investment in Africa has attracted increasing academic, media, and government attention.¹²⁸ It is within this context that this study examines the activities of Chinese investors in Tanzania in order to gain a better understanding of the specific consequences of Chinese FDI for economic development in the country.

China is the third world's largest economy and one of Tanzania's top five investors engages in mining, agriculture, manufacturing, tourism, energy, and, health and education sectors among others. Tanzania Investment Centre records indicate that in 2007 alone, China invested US\$ 3 billion in ten African economies, of which US\$ 111 million was invested in Tanzania. However, there are claims that Chinese investments in Tanzania and in Africa generally are driven by its hunger for raw materials and energy. This is due to Chinese investors' conduct after registering with TIC and obtains the Certificate of Compliance.

3.8.3 The Impact of the Chinese

How will the development of Tanzania be affected by the rapid growth of China's exports and investments? China takes over markets in African countries particularly Tanzania more easily than it manages to break into European or American markets. Will Tanzania be able to compete with China in sectors like the production of shoes or textile? Different authors have argued that African industries are usually not 'competing with', but in the best cases 'complementary to' Chinese industrial exports and investments in the country concerned. Countries like Tanzania find it difficult to compete in an international or global context, while their markets are flooded with cheap Chinese products. There are textiles and garments from China exported to Tanzania competing with the local tailors. Informal local tailors no longer compete with modern textile and garment industries in Tanzania. They have to produce at lower prices than Chinese textile

¹²⁸ 'Assessing China's Role in Foreign Direct Investment in Southern Africa' March 2011 <http://www.ccs.org.za/wp-content/uploads/2011/03/Final-report-CCS-March-2011-CCS.pdf> (accessed 29 February 2012)

and garment industries and have to come up with more attractive products than the second hand clothing from Europe, which is available almost everywhere nowadays.¹²⁹ The researcher agrees with Dijk for Tanzania to have a plastic recycling plant. Scrap metal has already become valuable in Tanzania for exports, and the hope is that people will recover plastics in the future for local processing. Surprisingly, currently most of the plastic bottles are compressed and exported to China, where the material is reused.

There is a strong perception among the Tanzanian community that Chinese activities in Tanzania are slanted towards trade rather than investment. Many Chinese economic actors obtain investment licenses but continue to import Chinese goods into Tanzania rather than making actual investments. Some believe that this could be a strategy to test the market before establishing manufacturing operations.¹³⁰

The researcher is of the view all this is due to deficits in regulating foreign investments in the country. This is a challenge to the government that needs urgent attention. Another pertinent question which needs to be looked at is whether Chinese are genuine investors for country's economic development. There is record of Chinese investors having colluded with some unscrupulous local business people to defraud the country of revenues through smuggling of forestry products worth US\$ 58 million annually between 2004 and 2005. Cases of cheap and fake products manufactured in China, which create unfair competition with locally manufactured products is also widespread. All these led to the survey conducted by Dar es Salaam regional authorities which established that most Chinese entrepreneurs were engaged in business other than what their Tanzania Investment Centre certificates show. A number of Chinese investors rub shoulders with locals in strategic business places like Kariakoo, Sinza and Manzese, selling shoes, sandals, and cheap clothes. But most of these goods are said to be produced locally in backyards.

¹²⁹ Dijk (2009) 14

¹³⁰ 'Pattern of Chinese Investments, Aid and Trade in Tanzania' October 2009

3.9 Conclusion

When Tanzania Investment Act of 1997 came in place and establishment of ‘one stop’ investment agency, there was high expectation for change and impact to the country economy. Neither the Investment Act of 1997 nor the Investment Centre has managed to demonstrate on empirical evidence the achievements of what were anticipated. Theoretical review of the Centre’s performance has revealed inadequacy on attracting foreign investors. On the other hand the Act’s adequacy has been questioned hence the need for its examination as it is done in systematically in this qualitative study and concluded in chapter five.

The study has find some silent features in the investment act. The law is silent on joint venture as this is expected to open avenue through which local and foreign investors would join their capital together to prosperity. In the law investors receives rights but they have no duties. There are certain duties which ought to have been clearly spelt out in the act like training of locals and gradual localisation of the foreign enterprise.

CHAPTER FOUR

REGULATORY AND INSTITUTIONAL REFORM FOR FOREIGN INVESTMENT AND ITS IMPACT TO TANZANIA ECONOMY

4.1 Introduction

Chapter four discusses the importance of foreign direct investment regulation on economic development, the case of Tanzania. The discussion will be grounded on the assessment of the strengths and weaknesses of existing legal framework, with an objective of determining whether there is a need for imminent regulatory reform.

The following question was formulated to answer the relevant concepts of this study:

Why the need for review of FDI legal and regulatory framework in Tanzania?

4.2 The challenges of investment treaties in regulating foreign investment to foster economic development

4.2.1 Tanzania Investment Act

As pointed out in literature reviewed in chapter three, there are some challenges in the 1997 Act that need some amendments. The literature reveals silent features in the Act on Joint Ventures, poses a challenge in attainment economic goals. The Act lacks clear direction on this contemporary mode of conducting business, currently favoured by investors. It is the opinion of the researcher that joint venture clause need to be accommodated in the Act to open avenues for local and foreign investors to join hands for more success.

The act has given foreign investors various rights but it is silent on duties on the part of investors. The act fails short of incorporating Corporate Social Responsibility (CSR) clause. This is an area which needs amendment. This will enable foreign investors to have certain duties and responsibility to the local community. This need to be made compliance for foreign invested enterprises in Tanzania. CSR would encourage foreign companies to play a role in engaging with stakeholders and contribute to the economic, social and environmental development in Tanzania.

This researcher agrees with Baker that CSR is the continuing commitment by business to behave ethically and contribute to economic development. He argues one should look at CSR in terms of its relevance to economic development.¹³¹ Given the importance of the regulation of foreign investment as well as a link between legislation and CSR, the researcher is of the opinion incorporation of CSR in the investment legislation is the best approach. This will allow companies to conduct themselves responsibly and abide to it since they will be legally bound. On economic point of view, large companies will help to deliver or improve different sectors and thereby expand economic opportunity. Sectors like extractive industries, financial services, tourism, food and beverage and many more will benefit from this.¹³²

4.2.2 Bilateral Investment Treaties and developmental goals

Investment is considered to be a vital input for economic development. But it has being observed that BITs display sensitivity to development policy and are based on outdated and ‘defective mold’.¹³³ Discussions among scholars in an academic workshop have generate views that these treaties offer extensive legal protections for foreign investors, but fail to safeguard the rights of government to act for important policy interests, without fear of breaching the treaty’s vague commitments. It is worried this limit the ‘policy space’ of developing countries with respect to regulating the economy. It was also viewed which this study concur with, many developing countries faced serious capacity problems when it came to negotiating investment agreements, and to analyse the practical legal and policy consequences of negotiating such agreements. As pointed out there is need for investment agreements to be balanced, and to factor in a development dimension.

¹³¹ Baker, J ‘Corporate Social Responsibility and Economic Development’
<http://www.oecd.org/dataoecd/24/35/2423198.pdf> (accessed 16 May 2012)

¹³² A report on the Role of Private Sector in Expanding Economic Opportunity through Collaborative Action , October 2007 http://www.hks.harvard.edu/m-cbg/CSRI/publications/report_29_HarvardEODialogueSummary20071018.pdf (accessed 16 May 2012)

¹³³ A report on Bilateral Investment Treaties: Implications for Sustainable Development and Options for Regulation http://www.fes-globalization.org/publications/ConferenceReports/FESCRBerlin_Peterson.pdf (accessed 17 May 2012)

From the discussions, this study reviewed BITs between Tanzania and various countries.¹³⁴ It discovered developmental goals are missing in those BITs. Drawing from those discussions, re-think of Tanzania's investment treaty model is warranted.

4.3 Institutional weaknesses

4.3.1 Tanzania Investment Centre Structure

The current structure of Tanzania Investment Centre bears no clear unit or department which is responsible for regulation of foreign investment with clearly outlined mandate. Looking on the current structure the study examines possibility of two different respective solutions:

Strengthen the After Care Unit

TIC has After Care Unit (ACU). This is one of the units under the Department of Investment Facilitation. This unit is expected to do monitoring but it has no power to do so under the current Act. In performing its duties the Unit is faced with many other challenges like lack of human resource; lack of funds; poor roads in some regions where projects are located; and government bureaucracy in different areas.

Attraction of FDI goes hand in hand with the analysis of costs and benefits of these investments, which requires monitoring and evaluation. The government needs to further strengthen the after care services. TIC needs to have an effective mechanism for tracking foreign investments and make regular post approval follow up of investors. An effective mechanism will help in tracking foreign investment and determine its effect to the community. There is need for legislation to give the ACU more power for it to be able to conduct proper assessment. The assessment will help to assess the beneficial impact foreign investors bring to the country. Due to its challenge of lack of resources, the study sees the need for more staff and more budget allocation to the Unit.

Upgrade the After Care Unit to departmental level

This study is of the opinion there is a need to change the status of After Care unit to a fully fledged department. The way the current structure is designed the departments function as

¹³⁴ Denmark, Finland, Germany, Italy, Korea, the Netherlands, South Africa, Sweden, Switzerland and UK

independent, coherent administrative structure, while the units are designed to provide a supportive role to the departments and their functions in the Centre. The ACU has the primary functions of conducting ordinary project visit to all registered projects for the purpose of advising on future plans including re-investment, localisation of skills, technology transfers, and others; conducting physical verification visits (PVV) to verify specific aspects before decisions are made in relation to granting new certificates or any other approval; and monitoring progress of registered projects just to mention few. These duties while all are vital do not in fact care the full extent of requirements of the Centre and allow the ACU to play its rightful role.

With due consideration that countries need effective regulatory mechanism to be able to benefit from FDI, effective regulation is a foregone conclusion. The After Care unit has to be a fully fledged department in order to effectively exercise the monitoring role. Currently the ACU is limited in scope and consequently unable to fulfill the many necessary functions. Paradoxically, in comparison with the bulk of the activities the Unit is understaffed and unable to adequately follow-up, monitor and analyse on the many matters that come to their attention. A number of staff needs to be scaled up take into account on the importance of including different fields like lawyers, economists, analysts and others.

4.4 Tax Incentives

As discussed in chapter three, there are many types of tax incentives offered to foreign investors in Tanzania. As a result this has caused problems to the country's revenue earnings. Among the problems existing is the way is used to shelter income from taxation through transfer pricing and the transfer of operations from existing firms to new ones that qualify for the incentives. Investment allowances pose problems as well as it is difficult to define the eligible expenditures and to choose the rate of allowance for credit. There is a need for tax law amendments for the country not to lose revenue as it is of now.

The legal instruments granting tax incentives should be drafted carefully so that they achieve policy objectives with a minimum leakage of tax revenue. They should be expressed as precisely as possible so as to avoid the need for frequent corrections or changes. It is believed that frequent

changes could contribute to the perception that the tax system is complex and difficult to comply with.¹³⁵ In Tanzania this can be evidenced on the investment inflows declined in 2009 by about 41 percent from what was achieved in 2008. The major causes of the decline were mainly due to some changes which were abruptly introduced in the investment incentive regime in the second half of 2009.¹³⁶ So Tanzania needs to look at tax laws and improve them along those lines.

The government of Tanzania can as well refrain from huge tax exemptions for foreign investors. There is evidence that the government of Botswana refrained from offering tax exemptions to foreign investors but managed to attract more foreign investment in part because of following prudent economic management principles that also assured investors that their property rights would be protected. That is achieving stable legal framework, a strong macroeconomic policy and favourable investment climate is more fundamental to attracting FDI than just offering tax exemptions. The following are some suggestions on how this can possibly be done.

4.4.1 Corporate Tax Reduction

The government of Tanzania may improve on tax laws by abolishing tax holidays and reduced corporate income tax rate. The government may set a lower corporate income tax rate as an exception to specific sectors or regions. Hong Kong (China), Indonesia, Ireland, the Lao People's Democratic Republic, Cambodia and Estonia are a few countries that use this type of incentive. This may be targeted at the income of foreign investors who meet specified criteria, or it may be applied for attracting additional FDI. Malaysia for example did this in the mid-1980s when investment inflows were below expectations.¹³⁷

This may be targeted at investment in regions that are disadvantaged due to their remoteness from major urban centres. Operating in a remote area may entail higher costs and place the location at a competitive disadvantage relative to other possible sites. Moreover, firms may find

¹³⁵ 'Tax Incentives and Foreign Direct Investment, a Global Survey' http://unctad.org/en/docs/iteipcmisc3_en.pdf (accessed 29 April 2012) 3

¹³⁶ Interview of the Executive Director of Tanzania Investment Centre conducted by Corporate Guides International Ltd. Tanzania in 2010, <http://www.corporate-tanzania.com/assets/pdf/2010/interview/ctz-2010-interview-naiko.pdf> (accessed 2 May 2012)

¹³⁷ (n 135 above) 19

it difficult to encourage skilled labour to relocate and work in remote areas that do not offer the services and conveniences available in other centres. Workers may demand higher wages to compensate for this, which again implies higher costs for prospective investors. Tax incentives may be provided in such cases to compensate investors for these additional business costs.

4.5 Introduction of E-platform to Registration and Licensing Agencies

There are still time delays in giving licenses or registering companies. Existing business licensing process and registration needs to be further simplified and streamlined in order to reduce the cost of doing business. So this study is of the view there is need for an introduction of Electronic System (E-platform) for more efficiency and effectiveness. This can be done by legislating the deadline for these processes and give the TIC, as ‘one stop centre’ mandate to make a follow up on the deadline. Once government procedures have been streamlined and redesigned as part of regulatory reforms, use of computerised databases and registries can lead to further improvements in regulatory performance.¹³⁸

4.6 Foreign Direct Investment and its Impact to Economic Development in Tanzania

In evaluating the impact of FDI on the economy, different criteria have been involved so as to examine the costs and benefits of investment. Criteria such as employment and tax revenue generation, emphasis is on the overall objective of promoting investment to improve productivity and competitiveness of the Tanzania economy.¹³⁹ Impressive impact has been apparent in certain areas and weak in others.

Although there is modest employment opportunities, still impact on adding value, technology transfer and environment on conservation is relatively weak. Despite significant inflow of FDI, the manufacturing sector is still struggling to improve productivity. FDI in agriculture sector has managed to bring about significant transformation both in terms of the performance of the

¹³⁸ (n 125 above) 29

¹³⁹ As above

particular commodity/sub sector such as floriculture and in economic impact of the neighbouring community.¹⁴⁰

4.6.1 Examples of Foreign Direct Investments' Impact on Tanzania

Capital

In Tanzania FDI has significantly contributed to capital formation despite the fact the large share of capital formation is held by the domestic investment. Using the official statistics, between 1999 and 2004, FDI averaged about 5 percent of GDP.¹⁴¹

Employment Generation

In Tanzania foreign investment demands the use of many expatriate managers and professionals, whose skills are domestically available, this could be regarded as holding back local skills development. In Tanzania there are a lot of people with all the skills and expertise required for various projects. Unfortunately the tendency has shown that foreign companies most of the times like to import their own people on the ground that there are no people with such skills in the country.

The researcher is of the view that for the country to benefit more and create more jobs for unemployed population, it is important for legislations to introduce a 'National Qualification Framework' within the labour laws. Globally, a qualification framework aims to organise information for coordination perspectives. By setting up a framework, it helps people to make logical decisions and coordinate them from a large perspective. A Qualifications Framework is the structure into which accredited qualifications are placed. This allows learners, training providers and employers to gain information about the broad equivalence of qualifications. For example, a Vocational Qualifications Framework (VQF) helps to create parity of esteem between vocational and academic qualifications.

¹⁴⁰ (n 138 above) 14

¹⁴¹ Kabelwa GC 'Potential Impacts of FDI on Economic Development in Tanzania' (2006) <http://www.tzonline.org/pdf/potentialimpactsofFDIoneconomicdevelopmentintanzania6.pdf> (accessed 24 January 2012) 12

Labour law legislation should provide reform. It should be reformed to accommodate this framework and provide relevant data base to Tanzania Investment Centre.

Technology, Knowledge and Skills Transfer

As Kabelwa discusses,¹⁴² there are four channels through which technology transferred by FDI can be diffused in the host country. These include: FDI establishing linkages with domestic enterprises-as suppliers (backward linkage) or users (forward linkage), skills transfer through training, learning-by-doing, learning-by-interacting, and job mobility, demonstration effects as local firms copy or adapt new technologies, market channels and management techniques introduced by foreign investors. This can take place in activities that involve processing or manufacturing and it can also be diffused in services and strategic technology partnership between a foreign investor and a domestic partner in areas such as R&D; and know-how, design and technical specifications and R&D capability.

For example, with backward linkage the Tanzania Breweries (TBL)¹⁴³ initiated a comprehensive programme of local sourcing. TBL identified a number of inputs to the production of beer that could be sourced locally from the primary inputs (barley) to other intermediate inputs in the packaging process. It is approximated that TBL's sources about 30 percent of its barley requirement from domestic sources. For this purpose it has set up a malting plant in Moshi¹⁴⁴ to systemise the purchase of barley from over 500 farmers in the region. In 2000, approximately US\$ 2.4 million were paid to farmers for the crop, representing the single largest source of direct income for farmers in the region. TBL also planned to meet the entire barley requirement from local sources (increasing from 6,000 to 26,000 tones) through further investment in research and development of the crop to improve yields and deepening of the present linkages with the farming community.

¹⁴² Kabelwa (2006)

¹⁴³ In November 1993, South African Breweries acquired 46% of Tanzania Breweries Ltd. (TBL) for US\$ 21 million. As part of its achievements, in September 1998, TBL became the Dar es Salaam Stock Exchange's second company to acquire a listing and South African Breweries had its share increased to 50.5%. Since the joint venture agreement with Tanzanian Government, the company has increased its interest in Tanzania Distilleries Ltd to 100% and its interest in Darbrew Ltd, a sorghum beer producer to 60%

¹⁴⁴ A district in Kilimanjaro region

Other important backward linkages established by TBL are the sourcing of locally manufactured glass beer bottles. Another supplier in Tanzania for TBL is Carnaud Metal Box, manufacturer of metal crown corks. This supplier is also a long established foreign affiliate and was the first supplier to enter into a technical collaboration with TBL. In addition, TBL sources plastic crates and shrink-to-fit packaging from Simba Plastics and is currently sourcing some of its bottle label requirements from Tanzania Printers, a local printing company (labels). TBL has also established strong backward links with Showerlux Ltd, manufacturer of industrial chemicals. Around 36 percent of TBL's inputs are sourced locally and plans are to increase this percentage to 50.

Skills and management

Tanzania Cigarette Company (TCC)¹⁴⁵ gives a good example of the importance to human resource training and development. For TCC, the human capital component was vital in the achieving various forms of upgrading and benefiting from the forms of technology transfer from the parent company. Locals are employed in key management positions (such as technical, administrative and sales and marketing positions) as a result of the extensive capabilities and host country experience they possess.

TCC has now put in place extensive internal and external training programs. It is one of the main employers in Tanzania, and seeks and retains the best young graduates in Tanzania, providing them with career advancement opportunities as well as external training and secondments to other plants around the world. Other training programs have been aimed at broadening managers' international exposure within the parent network and the training centre in St. Petersburg, Russia. For example, a system of secondments of TCC personnel to sister affiliates has picked momentum in recent years and a number of local personnel from middle management upwards have already benefited. These training programs are emphasised for the development of senior management in supervisory and technical staff.¹⁴⁶

Competition

¹⁴⁵ A Tanzania based company engaged in the manufacture, marketing and sale of cigarette and tobacco products. The Company exports to DRC, Mozambique, Malawi, Zambia and Comoros

¹⁴⁶ Kabelwa (2006)

The entry of South African firms provides a vivid example of the benefits from competition. Competition from South African companies has resulted into the improvement of product quality, the availability of additional products in the market, and expansion of the product market. TBL for example, has managed to introduce new brands in the market. Three beers (Kilimanjaro Premium Lager, Castle Lager and Ndovu Lager), have proved successful in the market. The new brands have done remarkably well to grow the beer market and replace imported beers.¹⁴⁷

Revenue generation

The table below shows the contribution of 10 privatised industries (to foreign investors) in tax revenue in Tanzania between 2001 and 2003. According to the Table the privatised companies contributed about 6.7, 9.1 and 9.2 percent of total tax revenue in 2001, 2002 and 2003 respectively.

Contribution of the Privatised Firms to the Tax Revenue in Tanzania

Name of Company	Year of Privatisation	Year Tax	Contribution (Tsh Million)	% of Total Tax Revenue
TBL	1993	2001	30,052.1	3.2
		2002	45,065.5	4.3
		2003	58,665.8	4.8
TCC	1995	2001	11,445.8	1.2
		2002	15,781.3	1.5
		2003	24,443.2	2.0
CARNAUDMETALBOX	2000	2001	412.6	0.0
		2002	815.8	0.1
		2003	1,210.8	0.1
TZ PORTLAND CEMENT	1997	2001	3,445.1	0.4
		2002	4,083.2	0.4

¹⁴⁷ Kabelwa, G 'South African FDI into East African: the case of Tanzania' (2002)

		2003	6,217.1	0.5
DAR BREW LTD	1997	2001	347.0	0.0
		2002	5,537.2	0.5
		2003	293.2	0.0
THA	2000	2001	5,681.6	0.6
		2002	7,670.1	0.7
		2003	7,415.8	0.6
DAHACO	2000	2001	893.6	0.1
		2002	2,023.2	0.2
		2003	1,060.1	0.1
NBC (1997) LTD	1997	2001	4,217.3	0.5
		2002	5,797.4	0.6
		2003	6,506.4	0.5
TANZANIA DISTILLERIES		2001	4,163.5	0.4
		2002	5,781.5	0.6
		2003	3,198.8	0.3
CRDB	1997	2001	1,498.8	0.2
		2002	2,201.6	0.2
		2003	3,215.5	0.3

Source: Adopted from Ulanga (2005)

4.6.2 Analysis of Foreign Direct Investment in Various Sectors in Tanzania

Tourism

Tanzania's tourist sector is still a leading sector in the Tanzanian economy. Tanzania is the only country in the world to allocate more than 25 percent of its total area to wildlife parks and game reserves. It has 14 national parks, 17 game reserves, 50 game controlled areas, a conservation area, two marine parks and two marine reserves.¹⁴⁸ According to the Ministry of Natural Resources and Tourism, the sector in 2000 to 2003 accounted for roughly 14 to 16 percent of GDP and the Tourism Policy of September 1999 calls for a GDP contribution of 25 to 30 percent by 2010. To meet the 2010 goal, the industry had to grow at a rate of 15 percent per year, assuming that GDP grows at a 6 percent average.

In Tanzania tourism is claimed to be a sector with significant linkages to other sectors such as agriculture, fishing, retailing and arts and crafts; and that it has economic spin offs into other sectors such as communication, education, energy, construction and the general development of the infrastructure thereby benefiting the economy as a whole. This make tourism become one of the options to diversify the economy and supplement a declining agricultural sector; create jobs in both rural and urban areas; and offer entrepreneurial opportunities for small and medium enterprises as well as community cooperatives.

So in promoting it, the country expects to earn foreign exchange hence increase of tax revenues. It is expected in the process could lead to enhanced living standards, economic well-being, social and cultural development.¹⁴⁹ With this ambivalent stance on the role of tourism in development, Tanzania came out with a comprehensive tourism policy which more or less accorded with the new changes in 1991.

There has been an increase in the number of investments in tourism through buying of existing facilities, leasing and direct investments. But, there are cast doubts about the claims made by the government officials, policy makers, politicians and even some academicians who have researched on the sector, on its contribution to the economy and development in general. Given all of the above, the pertinent issue still remains what Tanzania actually benefits from tourism.

¹⁴⁸ Tanzania Investment Guide 2008 and Beyond, <http://www.tic.co.tz/ticwebsite.nsf/FILE/TICGuideline.pdf> (accessed 20 February 2012)

¹⁴⁹ Chambua, G 'Tourism and Development in Tanzania: Myths and Realities' <http://www.iipt.org/africa2007/PDFs/GeofreyChambua.pdf> (accessed 4 May 2012)

The government claims that besides foreign exchange earnings, the sector generates money in the form of taxes, creates employment and stimulates growth in other sectors such as agriculture and construction. As critically examined by Chambua in his article,¹⁵⁰ these claims shows that although these claims are based on certain facts, he argued the reality is different. He said, and the researcher agrees with that what is not concealed behind these claims is the fact that the sector is premised on the destruction of other sectors such as agriculture, livestock keeping, fishing and other rural and coastal and marine based resources by encroaching on resources that are indispensable for the survival and prosperity of the rural dwellers. Moreover, the exploitative and dehumanising working conditions of those employed in the sector are not considered at all. It is claimed that among the benefits accrued directly to people are employment opportunities. Official figures show that the sector employed about 157,000 workers by 2001. What is not pointed out is the fact that working conditions in tourism are notoriously exploitative and humiliating, given the low wages in the sector as it is difficult to have viable unions in the face of dominance of seasonal, unskilled and casual labour and outsourcing of some functions.

Too often tourism only creates a few permanent paid jobs, and even these are very lowly paying. Wage levels are determined by the grade of the restaurant or hotel, whereby workers in five star hotels command higher wages. Tourism is by nature a seasonal industry and all hotels, hunting companies, travel and tour agents employ casual or part time staff at certain times of the year to perform some core services. Employment of casuals is particularly common in out sourced services (laundry, cleaning, security and others). Out sourcing often means lower wages, loss of benefits and retrenchments. This, combined together with the high levels of unemployment in the country, and the policies of retrenchment has in most cases led to lower levels of trade union membership and an erosion of worker power. This allows employers to pay no overtime, sick benefits or pensions.¹⁵¹

George Chambua keeps on arguing that tourism has a leakage factor in that substantial amounts of money earned from the sector leaves the countries of destination to pay for the imports consumed by the sector or in terms of repatriation. The country is not only losing money in terms

¹⁵⁰ (n 149 above)

¹⁵¹ (n 149 above) 19 20

of foreign exchange and leakages, but also the amounts of money it has been compelled to use from taxes and loans for privatisation of facilities, sustenance of incentives for investors and creation of infrastructure to service tourism.

Manufacturing sector

The largest sector for FDI is believed to be the manufacturing sector. Tanzania is an economy increasingly oriented towards manufacturing and export. In 2007, the sector grew by 8.7 percent compared to 8.6 percent in 2006, while the contribution of the sector to real GDP grew by 7.8 percent in 2007. The increase in growth was mainly attributable to increased production in sectors such as cement, beverages, corrugated iron sheets, iron and steel products, cigarette, plastic and textile products; where much of the FDI went to food and beverages.¹⁵²

Mining sector

The mining sector continues to play an important and growing part in the Tanzanian economy. Mining is the fastest growing sector in Tanzania in terms of its share of exports. The value of mineral exports increased from US\$14 million in 1996 to US\$711 million in 2005. Mining is believed to be the second largest sector for FDI with about 28 percent of total FDI stock by 2001 and the largest single sub-sector in terms of FDI has been the gold mining industry.

The growth in mining sector has being contributed by Tanzania's ability to attract mineral explorations and investment. This ability has been highly dependent on the country's abundance of mineral resources. The county has extensive mineral resources, the major ones being gold, diamond, base metals such as nickel, cobalt and copper. Tanzania also has gemstones such as ruby, sapphire and tanzanite; industrial minerals such as soda ash, kaolin and phosphate and iron ore and coal. Tanzania is the world's only source of tanzanite, a precious stone found in the open mines around Arusha region.

The growth in mining sector was also boosted with 1990s revised, investor friendly investment and mining code which was introduced in 1998, which was well received by international

¹⁵² Tanzania Investment Guide (2008) 22

investors. There has been a dramatic growth in the mining sector since that time and made Tanzania to be the continent's third largest gold producer after South Africa and Ghana. Reports from the Ministry of Energy and Minerals show that mining sector contribution to GDP was around 1 percent in 1998. In 2000s this figure rise and accounted for 2.5 to 2.8 percent of GDP. According to the Development Vision 2025, the sector is predicted to account for 10 percent of GDP in 2025.

Agricultural sector

In agricultural sector several reforms have been undertaken including granting the private sector permission to compete in the processing and marketing of cash crops; land laws have been revised to allow for long term leases of up to 99 years for foreign companies. Tanzania's agriculture and agribusiness have a number of competitive advantages, making the country a viable investment destination. The comparative advantages include, among others, biodiversity, competitive input costs, infrastructure such as deep water ports, international airports, a network of roads and railways, and a fast growing sophisticated financial sector.¹⁵³

The share of agriculture is 25.8 percent of the total GDP. Crops account for almost 34.6 percent and livestock almost 6.0 percent. However, the share of agriculture has been declining since the 1990s as a result of considerable growth in other sectors such as mining and manufacturing. In Tanzania major cash crops include coffee, cotton, tea, tobacco and cashew nuts as well as horticultural and floricultural products while main food crops include maize, rice, pulses and wheat.¹⁵⁴

Although agriculture is the backbone of the Tanzania's economy, the sector contributes only about 6.7 percent of the total FDI stock. This is a challenge for the government to attract foreign investors who may have competitive advantage in the sector. The researcher agrees with Kabelwa who said Tanzania can attract foreign investors in areas like cattle breeding, fruit production and canning, fruit juice production, flower production, cattle and game ranches and

¹⁵³ (n 152 above) 10 11

¹⁵⁴ As above, 5

timber production. Attraction of FDI in the agro processing industries can also be a key in the development of the agriculture sector.¹⁵⁵

So far the government has made commendable efforts to pursue macroeconomic policies that will motivate investment in agriculture by small and large scale commercial farmers through creation of enabling environment and provision of proactive support to private operators, farmers' organisations and other stakeholders and by ensuring a strong regulatory mechanism. There have been substantial improvements in road infrastructure through TANROADS whereby roads connecting major regional centres and to neighbouring countries have been improved to tarmac level. Also TIC in collaboration with the Ministry of Lands, Housing and Human Settlements Developments has been mandated to establish land bank for investors. In this regard, 4.0 million acres of land have been identified and modalities for ownership are underway. The Land Act has also been amended to allow land to be used as capital for investment.¹⁵⁶

Fisheries

Since 1998, the fishing industry has seen some changes, most notably increased access to foreign investment. Foreign investors can operate through joint venture operations with Tanzanian companies, and are strongly encouraged to do so. In addition, the division has become more customer service oriented with better service, quicker turnaround times, more transparency, and overall improved support. In 1999 to 2004 the fishing industry reported to have contributed to 1.6 to 3.1 percent of GDP.

The government of Tanzania though is concerned about over fishing, so is taking a cautious stance on the fishing industry. It is trying to promote underutilised areas, such as EEZ fishing and aquaculture, and some changes have been made that encourage investment. They see these as areas with immense potential for foreign investment. Despite the division's efforts, two of the areas with the largest potential, EEZ and aquaculture, seem to be growing slowly. As discussed in Tanzania Investor Roadmap: Primers on Regulations report of 2004, if the government wants

¹⁵⁵ Kabelwa (2006)

¹⁵⁶ Act 2 of 2004 'The Land (Amendment) Act'

to exploit these areas further, it should continue its advertising campaign and closely examine the reasons for weakness in these areas.

4.6.3 Other Challenges and Way forward

Challenges of utilities in the country

Concerning utilities, one major complaint by all investors is the cost of electricity, a cost that includes not only the tariffs but also the damages to equipment caused by TANESCO's operation. Apart from the cost of electricity the power is also not stable and enough for operations. Water is not cited for its cost, but rather for its unstable supply, if not its unavailability. Telecommunication is perceived as expensive; however, the business community deems it less of an issue today than before.

Complaints on tax burden in Tanzania

As observed in the Tanzania Investor Roadmap of 2004 which the researcher tend to agree partly, is that most fundamental problem with business regulations in Tanzania is the pretext to extract revenue from the private sector. A multitude of charges with concomitant procedures and paperwork transfer money from the private sector to the public sector that is from the more productive to the less productive sector. While the tax collector finds these punctures attractive, they weaken the private sector. They cut its working capital and drag it through time consuming procedures that ultimately have no real economic meaning. This contributes to repel investors away from Tanzania.

The researcher does not agree on foreign investors' perspective as foreign investors enjoy a number of tax incentives while this is not the case with local investors. The researcher is of the view that the government need to change its strategy and not depend only on foreign investment for its development goals and discourage the local investors. There must be a balance between the two. So incentives should be provided to local investors as well to encourage them. Without incentives to local investors, it is hard to envisage prospects for significant growth.

The researcher agrees with the fact that the cost of running the government is still too high for the private economy to support. So the government of Tanzania has to embrace a higher dimension of reform: intelligent taxation that does not push the brakes where acceleration is needed, and vice versa.

Another issue is the restriction of Export Processing Zone (EPZ) status to new export businesses only. The policy cannot be found in the EPZ law or regulations, but it is currently practiced. Agro-processors, agro-processing are natural economic avenue for Tanzania. New EPZ agro-processors would displace existing ones due to their cheaper operational costs. The policy can potentially destroy existing agro-processing businesses and the local experience that these agro-processors have accumulated over time. As all these issues increase costs directly or indirectly, it follows that the international competitiveness of Tanzania is at stake if reforms do not continue to rationalise its economy. This is due to the spread of wireless and the reduction of its cost in the last 5 years, in addition to a similar phenomenon for the Internet. A new issue is the restriction of EPZ status to new export businesses

Corruption and ambitious plans

Corruption is one of obstacles pose challenges to country's development. Corruption practices by political leaders are wide spread in Tanzania. This has led to inefficiencies in the public service.¹⁵⁷ The circumstances under which various government institutions entered into agreements with foreign companies pose a lot of questions and doubt. The arbitration case that involved Richmond Development Company (Richmond) and Dowans Holdings SA (Costa Rica)/Dowans Tanzania Limited (Dowans) is one of the examples of cases that ignored experts' opinions because of corruption.

In 2006 Tanzania faced a serious crisis in electricity supply and as an emergency measure Richmond was awarded a contract to supply generators to provide 100 megawatts at a cost of Tsh. 172 billion equivalent to US\$ 150 million. The generators failed to arrive on time, they did not work as required and the pipeline was never built. However, the government had to keep the

¹⁵⁷ Corruption-the latest, Business and the Economy, Issue 99 <http://www.tzaffairs.org/category/business-the-economy/> (accessed 18 May 2012)

contract and keep paying a non-existing company US\$ 137,000 a day without power being generated. And now Tanzanians are faced with the problem of repaying the debt, with the government increasing the electricity bill by 40 percent.

Richmond and Dowans instituted a case against TANESCO to the International Chamber of Commerce (ICC) for arbitration,¹⁵⁸ claiming US\$ 169 and 149 million respectively. The two claimants had gone to ICC after TANESCO moved to High Court to restrain the power producers from disposing its turbines. Dowans wanted to sale the turbines after the government terminates power production and purchase agreements between TANESCO and the firm on grounds of underperformance.

Dowans came into Tanzania in 2007 after taking over the contract of Richmond which had failed to deliver after signing an agreement with the government to produce emergency power. On 23 June 2006 TANESCO entered into the Emergency Power Supply Agreement with Richmond which assigned its contractual rights to Dowans Holdings SA. Thereafter, Dowans Holdings SA assigned its duties to its subsidiary company, Dowans Tanzania Limited. It is alleged that after the review of the agreement and irregularities in the contract, TANESCO wrote to Dowans on 30 June 2008 stating a decommissioning of the plants because the contract was void and hence contract termination by the government. This is what makes the companies to file their claims to the ICC.

Looking on section 31 of the Tanzania Public Procurement Act¹⁵⁹ it explicitly states that no public body shall award any contract unless the award has been approved by appropriate tender board. Under the Act, the Richmond/Dowans contract is the product of an illegal tendering system because it was not awarded by TANESCO's own tender board. This was the basis for TANESCO's ultimate decision to terminate the contract assigned to Dowans Tanzania Limited by Richmond. The ICC ruling made on 15 November 2010 held TANESCO responsible for the

¹⁵⁸ *Dowans Holdings SA (Costa Rica) and Dowans Tanzania Limited v. Tanzania Electric Supply Company Limited (Tanzania)*, International Chamber of Commerce – International Court of Arbitration, Case No. 15947/VRO, 2009

¹⁵⁹ Act 21 of 2004

breach of the agreement and ordered it to pay the claimants US\$ US\$ 65.8 million for breach of a contract.

4.7 Conclusion

Despite the impact that foreign investment that has been brought to Tanzanian economy, the impact is still not vigorous given the means through which that impact occurs and the structural constraint that are characteristic of the economy. There are still some weaknesses and challenges that need improvement. There are weak sectoral linkages in the economy and limited structure of investment distribution. The impact on the local community is rather temporary and voluntary depending on the discretion of large investors. It is then imperative for the Act to be amended to include the clause which will address the mentioned challenges.

CHAPTER FIVE

FINAL CONCLUSION

This chapter combines the findings of the entire dissertation and draws some final conclusions. Recommendations are also given under the chapter.

5.1 Summary of findings

Generally, chapter two is on conceptual and theoretical framework for regulation of FDI; where principles underlying FDI and economic theories of FDI were reviewed. Relationship between FDI, economic development and regulation was explained. The research find out there is a link between FDI and economic development and classical theory is of the view FDI can play an important role to promote economic development. However this study has learnt a host country need to have sound regulatory framework, efficient supporting institutions to enforce the laws and regulations in order to reap the benefits of FDI. The dependency theory which is opposed to the classical theory has the view that unless a developing state break out of the dependence situation, foreign investment will not bring meaningful economic development.

Under the chapter efforts made at international level to regulate investment were examined. Although the efforts to have comprehensive treaty over the regulation of foreign investment did not succeed, their contributions have helped in the development of the main principles of law governing treatment of foreign investment under international law.

In chapter three overview of legal, regulatory and institutional framework for FDI in Tanzania was conducted. The study learnt that the act governing investment and investment agency have not managed to demonstrate on empirical evidence the achievements of what were anticipated. Theoretical review of the Centres performance has revealed inadequacy in regulating FDI. On the other hand, the Act is also not adequate as there are silent features that pose challenges in regulating FDI effectively.

In chapter four discussions has been grounded on the assessment of the strengths and weaknesses of existing legal framework, to see the need for critical imperative for review of legal and regulatory framework for FDI. Silent features in the 1997 Act on joint ventures, duties to investors and developmental goals pose challenges that need amendment.

5.2 Conclusion

From the literature reviewed, this study has learnt that as attraction of FDI emerged as important policy, regulation of the same has also emerged as an important part. Regulatory reforms have become an important policy area where it requires the establishment of appropriate legal and institutional frameworks. The absence of regulatory controls over the sudden inflow of foreign investment brings economic misunderstanding within the state.

The host country needs to have policies in place in order to reap the benefits of FDI. Despite the success of Tanzania in attracting foreign investment there are still some weaknesses in terms of its structure in regulating investment. The country faces challenges in creating an improved business environment this including regulatory uncertainty. The general public is of the view that the government had not adequately assessed foreign investment to ensure they were in the countries interest.

5.3 Recommendations

To conclude, the major findings of this thesis relate to effectiveness in regulating FDI, legal framework, regulations and institutional structure pose challenges that need to be addressed. Therefore this study's main recommendations are directed towards developing a sound regulatory framework which should be efficient and supporting institutions that enforce the relevant laws and regulations.

Drawing from the findings on the silent features in 1997 investment Act, joint venture clause need to be accommodated in the Act. This will open opportunities for local and foreign investors to join hands for more prosperity. It is also recommended for Corporate Social Responsibility

clause to be incorporated in the Act. Its inclusion to the Act will enable foreign investors to have certain duties as well.

It is recommended for Tanzanian regulatory oversight to be strengthened. Tanzania Investment Act of 1997 being the primary act in governing investments in Tanzania need review especially, its structure in order to bring a clear understanding of who is responsible for regulating. There is need for legislation to give the organ responsible for monitoring foreign investment more power to be able to play its rightful role of monitoring investment effectively and conduct proper assessment. An effective mechanism will help in tracking foreign investment.

Due to the nature of bilateral investment treaties, the suggestion is for the introduction of a new BIT model which contains development purposes. As said by Boulle and Klaaren which the researcher agrees, it is suggested for the model to be drafted with a particular focus in balancing between development of Tanzania and the protection of foreign investor rights.¹⁶⁰ Various ways can be used include its inclusion in the preamble.

It is recommended for legal instruments granting tax incentives to be reexamined to be sure they achieve policy objectives with a minimum leakage of tax revenue. The government of Tanzania can as well refrain from huge tax exemptions for foreign investors. Improvement on tax laws by abolishing tax holidays and reduced corporate income tax rate is highly recommended. Lower corporate income tax rate may be set as an exception to the general tax regime in order to attract FDI into specific sectors or regions. Tax incentives may be targeted at investment in regions that are disadvantaged due to their remoteness from major urban centres.

Introduction of Electronic System (E-platform) is recommended by this study for more efficiency and effectiveness in licensing and registration procedures. Deadline for these processes can be legislated and TIC as ‘one stop centre’ given mandate to make a follow up on those deadlines.

¹⁶⁰ Boulle, L & Klaaren, J ‘Developing countries, BITs and ICSID Arbitration: Views from Africa’ (2009)

Rutaihwa recommended for rules and regulations to be observed when granting investment permit to Chinese. The researcher agrees with him as it has being observed some of Chinese may come as investors but ending up engaging themselves in petty business that can be done by local traders.

It is recommended for Tanzania to have a plastic recycling plant as suggested by Dijk.

Drawing from UNCTAD report¹⁶¹ the study recommends for Tanzania to promote investment in promising sectors. As a strategy to benefit more from FDI, it is recommended for the country to request for IPR of UNCTAD assistance to conduct analysis of the sector/s with high potential. This will assist Tanzania to further exploit its comparative advantage.

¹⁶¹ UNCTAD report on Investment Policy Review Programme: a Framework for Attracting and Benefiting from Foreign Direct Investment (2008) www.unctad.org/ipr (accessed 17 November 2011)

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