Tax integration within the East African Community:
A partial model for regional integration in Africa

This article tries to demonstrate until far the East African Community may be seen as a model of regional integration in Africa. From an optimal treaty to a deficient practice, the EAC experience reveals the role of taxation in a project of regional integration.

1. Introduction

When thinking about "regional integration", the first template that comes to mind is generally the European Union (EU). The EU has, in the last six decades, provided an example form which lessons on integration, harmonization and regional culture. However, the EAC forms a good case study as a regional integration for a number of reasons. First, the EAC can trace its origin to around the same time that the EU began the process of integration. Given that the EAC is yet to meet the same success as the EU in terms of a deep level of integration that encompasses a unique currency, we think the difference between these two regional organizations may shed some light on regional integration in Africa on a broader basis. Subsequently, the question arises what is missing within the EAC Law for further integration and harmonization of policies. In the author's opinion, the answer to the question teaches about the kind of impediments regional integrations are experiencing in Africa.

Therefore, also for historical reasons, the question arises as to whether it is still possible to discuss whether regional integration is still effective and if it can go further between EAC members' states. The answer to this question may, in the author's view, help to understand of the impediments regional integrations in Africa must overcome.

The East African Community traces its origins to the construction of the railway between Kenya and Uganda as from 1897 until 1901. The railway was the starting point of a series of institutions which were essential to its integration: a Customs Collection Centre in 1900, an East African Currency Board in 1905, a Postal Union in 1905, a Court of Appeal for Eastern Africa 1909, a Customs Union in 1919, an East African Income Tax Board in 1940, the Joint Economic Council in 1940. During those years while European Countries were still involved in strong wars Uganda, Kenya and Tanzania signed a treaty for an East African Cooperation in 1967 establishing the East Africa High Commission, the East African Common Services Organization and the East Africa Community.

---

1 Anapaula Trindade Marinho, IBFD Research Associate within the AMELA Team - Knowledge Centre, PhD candidate on International Tax Law Université Paris 1 Panthéon Sorbonne and Master II in Tax Law by the same University; and Catherine Ngina Mutava, IBFD Research Associate within the AMELA Team – Knowledge Centre, LLM in Tax Law by NYU.

2 The said "European Community" was founded by the Treaty of Rome, which has officially established the European Economic Community (TEEC). This international agreement founded itself the European Economic Community (EEC) on 1 January 1958. It was signed on 25 March 1957 by Belgium, France, Italy, Luxembourg, the Netherlands and West Germany. Since then, an important progression happened in terms of Partner States - the number has increased to 28 countries today - and in terms of statute thanks to the enactment of the Treaty on the functioning of the European Union in force as from 1 December 2009.
Unfortunately, the glorious years ceased temporarily when in 1977 the treaty for East African Co-operation was officially dissolved due to lack of 3 essential ingredients: strong political will, strong participation of the private sector and civil society in the co-operation activities and continued disproportionate sharing of benefits among Partner States.

Despite the fall out, the member states resumed negotiations between 1977 and 1999 culminating in the signing of the EAC Treaty on 30 November 1999. A parallel can be drawn with the EU which was, around the same period, getting stronger by consolidating its commitments. The EAC treaty was amended in 2007 to allow Rwanda and Burundi to join the EAC. Other than the extension of the membership, no amendments to the original treaty itself were made.

Nevertheless, here is the second reason for why the EAC is a perfect case study for regional integration in Africa, the treaty signed in 1999 is particularly refined comparable to the Treaty of Rome. The EAC treaty establishes for a strong community with strong institutions that are appropriate for the adoption and for the enforcement of its rules, as well as for the protection of the EAC residents' rights.

The authors will seek to demonstrate the refinement of EAC treaty as well as its appropriateness as a model for regional integration in Africa (see section 2). The authors will subsequently look at how the current domestic law of each of the EAC Partners States breaches the provisions of the treaty with respect to taxation and tax policy in general (see section 3). The aim is to demonstrate the role of taxation within a project of regional economic integration. In the author's opinion, despite of an almost perfect treaty, an economic regional integration is impossible without tax integration.

In this sense, the EAC treaty is, from the author's opinion, the most refined and appropriate treaty to use when analysing regional integration in Africa. A review of the failure by the EAC to apply its provisions with respect to taxation for example, must be taken into consideration in order to determine how the domestic identify how the missing keystone comes from the domestic level.

2. The EAC Treaty, a model for regional integration in Africa

If the EU is compared to the EAC, the EAC Treaty is by far better drafted. Indeed, the EAC treaty contains number of explicit provisions which had to be clarified by either the European Court of Justice through its case law or the European Commission itself through recommendations. As we will demonstrate now, the EAC Treaty can be seen as a model in terms of relevant and explicit provisions required for regional integration purposes and, more precisely, for tax integration purposes.

2.1. Exhaustive guiding principles

First of all, the EAC Treaty provides a wide scope for the community. The treaty aims to establish a Customs Union, a Common Market and a Monetary Union. Article 7 of the EAC Treaty, establishes

---

3 Treaty for the establishment of the East African Community, as amended on 14th December 2006, and 20th August 2007., preamble, pages 1 and 2

4 During this period, we can mention the signature and the entry into force of the Schengen Treaty in 1985, the adoption and the entry into force of the Single European Act in 1986-1987, the adoption and the entry into force of the Maastricht Treaty in 1992 and 1993, the signature of the Treaty of Amsterdam on 2 October 1997. This last treaty meant a greater emphasis on citizenship and the rights of individuals, an attempt to achieve more democracy in the shape of increased powers for the European Parliament, a new title on employment, a Community area of freedom, security and justice, the beginnings of a common foreign and security policy (CFSP) and the reform of the institutions in the run-up to enlargement.

5 Burundi and Rwanda joined the EAC on 6 July 2009.
an export oriented economy with free movement of goods, persons, labour, services, capital, information and technology, as well as the protection of human and people rights thanks to the “African Charter on Human and People’s rights”. As regards taxation, the Charter allows for the development of tax human rights identical to those ruled by the European Court of Human Rights’ case law. The EAC treaty provides five principles which frame the interaction between the national and the community level. These principles, asserted by article 7 of the EAC Treaty, are the principle of subsidiarity, the principle of variable geometry, the equitable distribution of benefits, the principle of complementarity and the principle of asymmetry.

Most of these principles have were not provided for explicitly in the EU Treaty and were, as a result, the subject of trials in in the European Court of Justice for decades, as still remains a current issue in terms of general policy for the European Commission and the European Parliament. These principles are the core of a regional integration given that they coordinate both the national and the community actions on each sector. The inclusion of these principles in the treaty which establishes the regional community illustrates a previous agreement from each Partner State to cede its powers to the Community.

The principle of subsidiarity, which has been the subject of discussions within the EU, for a long time is explicitly provided for in the EAC Treaty. The EAC Treaty provides for the achievement of subsidiarity "with emphasis on multi-level participation and the involvement of a wide range of stakeholders in the process of integration". At this stage, it is important to mention that the treaty does not expressly state to what extent partner states cede their powers to the Community nor to which sectors subsidiarity will apply. It may therefore be necessary to explicitly provide in the Treaty the level of subsidiarity envisaged as well as the sectors that will be under the control and direction of the Community institutions in order to avoid conflicts, disharmony and resistances between and from the Partner States. This is the reason for why the Treaty of Lisbon includes a definition of the principle of subsidiarity and provides also several tools to check its right application.

6 For few examples: taxpayers may claim based on the European Convention of human rights against sanctions ordered by administrative bodies (CEDH, 21/02/1984, Öztürk c/ RFA; CEDH, 24/02/1994, Bendemoun c/ France); prerogative of jurisdictions to review or not tax sanctions ordered by tax authorities (CEDH, 23/09/1998, Malige c/ France); taxpayers must dispose of previous remedies against tax raid (CEDH, 21/02/2008, Ravon c/ France).


8 When discussing about the Constitution for Europe in 2004, the main issues where focused on the emergence of a sovereign organization that would prevail over the national sovereignty formally only, without changing on deep the functioning of the community but resulting on a paralysis because of the symbol itself. Among an important literature, Eric L’Heolguic’h (2005), “Le Traité établissant une Constitution pour l’Europe : une étape dans la dynamique constitutionnelle européenne”, Les Cahiers européens de Sciences Po, n° 04, Paris: Centre d'études européennes at Sciences Po.. Leading on a broader basis with the existence of distinguished competences between members states and the European Union, D. Berlin, Droit fiscal communautaire, PUF, 1988, p.23.

9 Article 7 of the EAC Treaty

10 Article 5 of the Treaty of Lisbon. Before the Treaty of Lisbon, the Protocol n° 2 to the Treaty of Rome, included by the Treaty of Amsterdam, provided a definition and a detailed explanation on the principle of subsidiarity. The article 5 of the Treaty post Maastricht is much clearer than the EAC article, providing that: "La
The inclusion of the principles of variable geometry, complementarity and asymmetry in the EAC Treaty also deserves some reflection. The EAC Treaty innovates by listing each of them, where the Treaty of Maastricht and the Treaty of Lisbon mention, after the principle of subsidiarity, the principles of attribution and of proportionality. However, the innovation is partly an advantage given that the definition lacks of precision for all of them. First of all, the principle of complementarity is defined in Article 1 of the Treaty as “the principle which defines the extent to which economic variables support each other in economic activity. Further description would be important since the principle of subsidiarity is very often explained through a “complementary” relationship between two instances, i.e., the local and the central authorities, who are willing to share part of its prerogatives. The question arises which are these “economic variables” and what is the meaning of "support" within the context of the Treaty. As regards the principle of variable geometry, the EAC Treaty mentions that it "allows for progression in co-operation among groups within the Community for wider integration schemes in various fields and at different speeds". This last principle is also unique when comparing to the Treaty of Rome and to the Treaty of Lisbon, which both focus on the principles of subsidiarity, attribution and proportionality. Does this principle relate to a stand-still clause which would apply for certain provisions, and, at the same time, does this principle lead with the time for each Partner State to apply EAC law when just enacted? Similar remarks may be addressed regarding the principle of asymmetry; how shall derogations to the logic of symmetry be understood? What is the difference comparing to the principle of variable geometry? Once more, a proper definition lacks when the aim is to reach the optimal level of precision for facilitating the aim of integrating.

Finally, the EAC Treaty provides expressly for an equitable distribution of benefits and "measures to address economic imbalances that may arise" from the operation of the Community. Even though the Treaty might go further, this provision introduces the need to avoid and correct imbalances among as one of the main goals of the Community must address.

2.2. Principle of precedence within the context of a strong Court of Justice

The EAC Treaty proves its superior draftsmanship as it addresses the principle of precedence explicitly in comparison to the EU which has been forced to rely on the European Court of Justice to interpret and consolidate the principle. Articles 8 and 16 provides that "in pursuance of the provisions of paragraph 4 of this Article, the Partner States undertake to make the necessary legal instruments to confer precedence of Community organs, institutions and laws over similar national ones". This explicit provision, combined with those of article 16 under which states that "subject to the provisions of this Treaty, the regulations, directives and decisions of the Council taken or given in pursuance of the provisions of this Treaty shall be binding on the Partner States, on all organs and institutions of the Community other than the Summit, the Court and the Assembly within their jurisdictions, and on those to whom they may under this treaty be addressed". The first statement to be addressed concerns the eventual conflict which arises when some Partner States follow a dualist approach with respect to international law, whereas some other Partner States follow a monalist approach.

Comunauté agit dans les limites des compétences qui lui sont conférées et des objectifs qui lui sont assignés par le présent traité. Dans les domaines qui ne relèvent pas de sa compétence exclusive, la Communauté n’intervient, conformément au principe de subsidiarité, que si et dans la mesure où les objectifs de l’action envisagée ne peuvent pas être réalisés de manière suffisante par les États membres et peuvent donc, en raison des dimensions ou des effets de l’action envisagée, être mieux réalisés au niveau communautaire. L’action de la Communauté n’excède pas ce qui est nécessaire pour atteindre les objectifs du présent traité. ».

11 Article 5 of the Treaty of Lisbon of 2009.

12 Going deep through the protocols and annexes, no further precisions are given a part the definition provided in the under article 1 of the EAC Treaty.
question whether the Law enacted by the Community institutions shall prevail over the national Law of each Member State is expressly avoided contrary to the European side. While the European Institutions were already established and enacting rules, each member state had to solve the principle of precedence within its national jurisdiction and, until recently, pending queries still remain on how to combine preliminary constitutional ruling mechanisms by national courts with the European preliminary ruling mechanism.

The EAC Treaty provides for a strong and accessible Court of Justice contrary to some impediments regarding the European Court of Justice. From articles 28 to 36 of the EAC Treaty, to the East African Court of Justice is vested with a combination of jurisdiction and accessibility which is rare within regional integrations in general. The East African Court of Justice is granted a competence on first instance and as an appellate division. It has jurisdiction over the interpretation and the application of the treaty, as well as it has jurisdiction over Partner States who fails to fulfil an obligation under the treaty. National courts may apply for a preliminary ruling on matters touching on the Treaty and residents of Partner States may approach the court on the legality of any act, regulation, directive, decision or action of a State or of an institution of the Community. By providing for residents to refer to the court any decision or action of a State or of an institution, the Treaty allows proceedings against circulars or instructions issued by the tax authorities, for example. At the national level, this option is not always provided by the law. Further, the ‘Treaty explicitly provides the decisions of the court have precedence over the decisions of national courts on similar matters (article 33). Within the EU context, this was not explicitly provided for resulting in some of the dualist countries questioning the effect of the European Union Court of Justice’ decision in domestic law. Finally, the Court is competent for providing advisory opinions under the request of the Summit, the Council or a Partner State (article 36). Therefore, any question regarding regional policies may be referred to the court for checking whether it would breach one of the four pillars, for example (article 36). Under the same article, a Partner State shall take without any delay the measures required by the Court.

2.3. Consensus or relative majority rule

In addition to explicit guiding action principles and an accessible Court of Justice, policy making is also facilitated under the EAC Treaty provisions. This feature is probably the most important as a strong court and admirable guiding action principles will be of no effect when the policy making process may be blocked at the level of the regional organization. Unlike the EU’s, the Summit, the Council and the East African legislative assembly do not need unanimous or majority rule. The Summit and the Council’s decisions are subject to the consensus rule, while the legislative assembly enacts legislation under the relative majority rule (article 58). Both the consensus and the relative majority rule tend to facilitate the adoption of measures and regulations in general, which would never been adopted under the absolute majority principle if we look at other regional organizations experience.

14 Only the European Commission or member states may refer to the European Court of Justice.
15 With regards to direct taxation, the unanimity is required by EU law.
Having identified the advantages of the EAC Treaty, the question arises why the regional integration within the EAC is not as efficient as it should be giving the sophisticated institutional arsenal implemented by the treaty. In the author's opinion, a regional integration depends also on regional tax integration. As far as integration with respect to taxation does not become true, integration as a whole process remains unreachable.

2.4. A relevant tax arsenal

The EAC Treaty can be deemed to be a model including taxation. Within the context of a community which embodies the establishment of a customs union, a common market and a monetary union, a lack of a certain level of harmonization of the national tax systems involved and a lack of harmonized tax policy could compromise integration as a whole.

Contrary to the treaty establishing the European Union\(^\text{16}\), the EAC treaty is in theory a model with respect to tax policy and makes provision for tax harmonization with different provisions. In the establishment of a Customs Union, Article 75 provides for the elimination of internal tariffs and other charges of equivalent effect as well as for the establishment of a common external tariff. The EU also prohibits of any kind of disguised tax behind extra charges or higher costs for foreign products as an example. Under the same article 75, "partner States shall not impose any new duties and taxes or increase existing ones in respect of products traded within the Community and shall transmit to the Secretariat all information on any tariffs for study by the relevant institutions of the Community". The Partners States are therefore subject to a “stand still” clause explicitly defined in the treaty and a first essential step when aiming to harmonize national tax policies and systems. The Partners States are also obliged to refrain from enacting legislation or applying measures which directly or indirectly discriminate. The link to be made here is between these provisions and article 76 which establishes the basis of the common market: free movement of labour, goods, services, capital and the right of establishment. This provision tends to avoid any kind of discriminatory tax rule that would act as a barrier against moving to or trading with one of the Partner States, for example exit taxes. Similarly, different tax treatment of dividends or e.g. a permanent establishment of a foreign subsidiary if residents were taxed at a lower rate or exempt from tax is not allowed for. Even though nothing more was said regarding tax harmonization and integration, one could use the European Court of Justice's case law to build up a harmonized tax system between the Partner States thanks to the observance of these freedoms. Their interpretation and implications may go very far if Courts and nationals, apply the treaty orthodoxy.

With respect to co-operation in investment and industrial development, articles 79 and 80 of the EAC Treaty provide for the harmonization and the rationalization of investment incentives including relating to taxation of industries. The avoidance of double taxation is also explicitly stated. Here we have two “hot” tax issues. The first is the use of tax incentives by emerging economies. After decades of implementing tax incentives, the emerging economies had to face its inefficiency comparing to the high cost that they represent. The question is also how to reconcile tax incentives with the need of tax receipts for public finances, and the arms' length policy with respect to the Partners States. If a parallel with the European Union Law is to be made, the harmonization and the rationalization of the tax incentives reflect the State Aid provisions. A rational must be respected nowadays and a strong procedure applies whenever a country detects a tax incentive by one of its Partners which would not have been subject to previous approval by the European Commission.

---

\(^{16} \) Only indirect taxation is covered by the aim of harmonizing contrary to direct taxation, for example.
The second important tax issue concerns the avoidance of double taxation. The original EU Treaty did not explicitly take into consideration the avoidance of double taxation, leaving to each Partner State its own network of double tax conventions to solve any claim. A few years ago, the question became of huge importance: should the community adopt a general multilateral convention for the avoidance of double or multiple taxation within Partner States? Which rule shall a Partner State make to prevail where a conflict between a European directive, regulation, or article of the treaty is in conflict with a double tax convention provision? These questions arose because the European Treaty was silent on this.

The fact that the EAC treaty, has a provision that explicitly deals with the avoidance of double taxation does not, in practice, solve a double taxation situation but helps to use the principle of such avoidance as a directive that each Partner State shall develop the required normative tools. When the aim is to reach the optimal level of prescriptions tending to integration, in the author’s opinion the EAC should enact a model of double tax convention for its Partners States and further regulate the double taxation which may occur between these States. The best example is given at the level of the African continent, with the West African Economic and Monetary Union model of double tax convention. Further, under the provisions of article 82, with respect to a monetary and financial co-operation, the EAC Treaty calls for fiscal co-operation, harmonised macro-economic policies within taxation, adjustment of fiscal policies to ensure monetary stability, harmonization of tax policies to remove tax distortions (article 83) and harmonization of taxation of capital market transactions. Unlike the EU, the scope of the tax harmonization and co-operation is not restricted to indirect taxation. This broader approach allows a more extensive tax harmonization and integration between the different tax systems which are involved since all fields of taxation seems potentially concerned. Finally, in addition to the Treaty provides for a Customs Management Act was enacted and still in force.

Despite of a huge arsenal with respect to taxation provided by the EAC Treaty, in practice we face inefficient provisions. In the author’s opinion, it’s possible to see a link between the lack of further integration within the EAC Partner States and the lack of tax harmonization and cooperation.

3. The lack of tax integration in practice, an obstacle to regional integration

One of the main objects of the EAC as enshrined in the treaty establishing it is to ensure equitable economic development within the region. In a bid to ensure that this and the other objects of the treaty are attained and to ensure a protection of the rights granted to each of the member states, the treaty provides that the member states are to harmonize their tax policies with a view of removing tax distortions. The end aim of this being to ensure a more efficient allocation of resources within the community. This second half of the paper discusses tax harmonization as envisaged in the Treaty and Procols, its success and challenges currently faced.

The EAC common market and customs union aim at applying the principle of asymmetry while at the same time eliminating internal tariffs. The gist being that each country will be

---

17 A regulation was enacted by the member states. The provisions go far until the establishment of an ad-hoc jurisdiction in charge of the interpretation of any treaty seeking for the avoidance of double taxation and tax evasion: REGLEMENT N° 08/2008/CM/UEMOA.
18 Article 5(3) EAC Treaty.
19 Article 83(2)(c) EAC Treaty.
allowed to maintain their tax system as well as their tax rates but they hope to merely harmonize the systems. This deals with harmonizing the tax bases and adopting similar tax principles while at the same time engaging in information sharing between the tax authorities of the member states.

3.1. **Transactional taxes and free movement of goods**

In a bid to remove distortions created by tax differences, the EAC member states adopted the East African Community Customs and Management Act (EACCMA). The Act, which was adopted by the member states in 2005 provides for uniform application of customs treatment of movement of goods into and within the community. EACCMA proves for a common external tariff applicable on all goods imported into the region.

The implementation of EACCMA has been one of the successes of regional integration in the EAC. The success can be credited to a number of reasons. The precedence afforded to EACCMA and the institutions set up under it and the Treaty is one of the main reasons. In the implementation of the Act, the member states gave precedence, as required under Treaty, to the laws and institutions of the EAC over their own domestic laws. This prevents an overlap or conflict between the domestic laws of each member states.

The success can further be credited to the adoption of a common policy on customs within the region. Although each country maintains its own customs authority, a Directorate of Customs is established under EACCMA is charged with the responsibility of formulating and co-ordinating the customs and trade policies with the region. The A Directorate is established under EACCMA to come up with a policy on customs for the region. The result has been a co-ordinated development of customs policy within the region offering certainty to investors as well as going a long way in securing the freedom of movement of goods within the EAC. The success in removing the internal tariffs and establishing a common external tariff is reduced by the different customs procedures put in place for goods in intra-community trade. Despite the fact that the treaty provides that for free movement, the movement is greatly hampered by the fact that the goods are still required to go through the same customs procedures as other goods imported from outside the community. The long administrative procedures put in place by each member states effectively remove the benefits presented by EACCMA as they occasion delays to traders seeking to export goods to other members within the community. The delays in effect create the very distortionary effect that the Treaty aimed at curing when it envisaged the creation of a market as they make goods imported from a member state less competitive than those manufactured in that state.

The success receive further draw backs from the the lack of co-ordination and harmonization in the tax policies of the member states in other areas of tax thereby threatening the rights granted under the treaty with regard to free movement of goods, services, capital and people.

---

20 Article 8(4) EAC Treaty.
21 Section 3 and 4 EACCMA.
22 Section 3 and 4 EACCMA.
In the area of excise, for example, a lack of co-ordination in the policy governing application and levying of excise duty hamper results in member states adopting different ways of levying the tax as well as different rates. In particular Uganda and Rwanda and Burundi levying the tax at ad valorem rate while Kenya and Tanzania opt to apply specific rates in relation to certain goods. The different rate and different ways in which the tax is levied subtract from the right conferred on freedom of goods as well as capital. The different rates distort the market giving a distinct advantage to manufacturers based in countries where the excise duty is lower. The result is that the products from manufacturers from lower tax jurisdictions are more competitive in terms of pricing due to the excise duty differences. This may impact the location of industries within the EAC and in effect draw away from one of the key objects of the Treaty of attaining equitable economic development within the EAC. Similarly, the lack of coordination means that goods coming in from another member state must be subjected to excise duty and therefore subject to long waits at the border points as the goods are verified and customs duty imposed. This occasions delays and detracts from the freedom of movement of goods as envisaged in the treaty.

VAT is another area where the taxation remains largely unharmonized resulting there have been efforts to bring about compatibility within the areas of VAT and customs. The fundamental issues with regard to the tax base and sourcing need to be harmonized. In order for integration to work effectively it will be necessary to ensure that the goods within the community are either exempted from tax or taxed at a standard rate.

As it stands, each of the EAC member states applies the destination based model of levying VAT. The destination based model requires that VAT is levied on goods and services where they are consumed. Therefore if, for example, a Rwanda based trader exports goods to Uganda, the goods would ordinarily be treated as an export and therefore would be subject to zero-rating. However, the goods would be subject to VAT at the point of importation in Uganda. Whereas this might work normally where integration is not intended, when it comes to integration, it creates a loophole for tax avoidance as the goods can be smuggled through the borders denying both Rwanda and Uganda the VAT due. To avoid smuggling, policing of the borders becomes necessary and this adds to the administrative burden on each member state and also increases the amount of time that goods from other member states take to arrive. This acts as an impediment to the free movement of goods within the region.

The EAC could borrow lessons from either the EU or the Andean Community approach with different implications and considerations. The EU has adopted a two pronged VAT system approach to cater for movement of goods within and without the community. Those being sold to any member within the community are sourced according to an origin based model whereas those leaving the community are taxed according to a destination based model. The origin based model requires that VAT is levied by the country of origin and as such exports within the community are not treated as exports for purposes of VAT.

This system is essential for the EU as the application of the destination based model within the community would lead to goods being sold within the community being zero rated and therefore causing a shift of the tax base where the importing country gets the tax on the goods being sold through application of reverse charge VAT. If such a model were adopted, then if a Tanzanian trader, for example, sells goods to a person in Uganda, then the goods will be subject to VAT in Tanzania and no additional VAT will be levied in Uganda and there will be no need police borders to ensure that VAT is levied.
The EU mixed type of sourcing however requires a high level of coordination within the member states as the importer in this case is allowed to claim a notional input credit for the import. For such a system to work, the compliance levels need to be high and the level of coordination among the tax authorities in the member states is required is also high. Furthermore, a common database for taxpayers within the region may be required. It also requires the existence of an enforcement institution with the legal force to resolve conflict and ensure compliance. This role is effectively played by the European Court of Justice. Tax compliance levels in the EAC are very low and the problem is further compounded by the large shadow economy within the region. The EAC region on the other hand faces institutional constraints therefore making this method unsuitable for the region at this level of integration.

The Andean Community on the other hand maintains a destination based model for all sales whether within or without the community and so far has been successful. Although it requires border patrols and a higher level of tax administration than the EU model, it is more suitable for the EAC currently since the region does not have the institutional capacity to enforce the EU model which requires a higher level of integration to be successful.

However the formulation of a standard list for the goods that are exempt and those which are not is imperative if the standardization of VAT is to work. This is the one area where the member states must be willing to accept standardization otherwise it is likely to lead to discrimination among the member states with certain goods being exempt or zero rated in one country while remaining taxable in the next. The provision of long lists for the different items is also likely to cause increased complexities in administration thereby increasing the opportunities for VAT fraud. Therefore in this one area of tax, the member states will be required to have uniformity. This has worked well the Andean Community which maintains a common list for exempt and zero rated goods and services.

3.2. Harmonizing tax incentives

To achieve equitable development of the region and to promote the EAC as a single investment area, the Treaty provides that there should be a harmonization of investment incentives. As it stands, this is one of the areas that remains completely unco-ordinated with each country making efforts through different incentives to attract investment to its jurisdiction at the expense of the region as a whole. With the removal of tariff obstacles in intra-regional trade, the place of establishment is increasingly being determined by the different incentives offered by the member states. Each of the member states, except Uganda, for example, provides for export processing zone that are generally exempt from tax for periods of certain period. In this regard, Kenya offers a 10 year tax holiday for companies in the export processing zone with the companies enjoying a reduced tax rate of 25% for the next 10 years. Supplies made to the companies are also zero-rated. Similarly, Burundi...

---

23 Statistics indicate the size of the problem in the area with the Kenya’s shadow economy being the lowest while constituting 34.8% of the economy and Tanzania 58.2%, GTZ, Tax Systems and Tax Harmonization in the East African Community available at http://www.eacgermany.org/index.php/eac-gtz-programme/tax-harmonisation/55-tax-harmonisation (last visited on 30 August 2013).
24 Article 80(f) EAC Treaty
26 Paragraph 3 of the Fifth Schedule to the VAT Act, Cap 476 of the Laws of Kenya.
offers a 10 year tax holiday for companies in a free trade zone area\textsuperscript{27}. In Tanzania, companies operating within an EPZ area are entitled to a 10 year tax holiday. Rwanda also offers a tax holiday for holding companies as well as for countries operating within a free trade zone. The incentives are not just limited to tax holidays but also extend to general investment deductions that range from 50\% to 150\% being offered by the different member states.

The competition to offer the best tax incentives is in violation of the requirement to rationalize tax incentives with a bid to promoting the EAC as a single investment area\textsuperscript{28}. Due to the lack of co-ordination in the area, the incentives are offered with respect to different industries. The result is likely to be a shift in capital with manufacturers in that industry preferring to set up in Kenya or any other region that provides them with the tax holidays or tax incentives.

The flight of capital derogates from the goal of developing the region equitable and results in unequal distribution of capital resources and development of industries within the region. This was one of the key reasons for the dissolution of the EAC in 1977 and should be addressed. In this regard, the EAC should borrow from the EU on control of State Aid. Where an EU member state is regarded as having offered state aid to certain industries which results in those industries or persons having a distinct advantage over similar persons in other member states, then the state aid is deemed to not have existed and the person will be required to pay back taxes that would have been due on his income had the state aid not been offered to him. Such an approach equals the field for all persons engaging in a particular industry with none having a distinct advantage over the others as a result of the tax incentives offered by their country of establishment.

3.3. Harmonizing income tax bases

Taxation of income and capital gains among the member states also remains largely uncoordinated and unharmonized. Each member state has a different tax base. The tax base is defined in the IBFD glossary to mean "the nature of the thing that is taxed, i.e. the taxable object (such as income or capital). The term is also used in a narrower sense to refer to the amount or composition of the taxable object, e.g. what items are included in or excluded from the computation (such as deductions or losses) or the net amount that is computed taking into account these items".

The vast differences in the tax base in each of the member states play a role in determining investment location especially now that traders has free access to all the EAC market with the removal of barriers within the EAC. Investors will, among other factors, be influenced by the amount of tax they will be required to pay on their income and this will be determined by the tax base and the tax rates.

\textsuperscript{27} article 39, Book II of the General Tax Code of Burundi

\textsuperscript{28} Article 80(f) EAC Treaty.
The different tax base of the member states provide for planning opportunities for investors depending on their line of business. In respect to income tax for example, Kenya does not tax capital gains while the other member states levy a tax on capital gains made in their jurisdictions. The effect of this is that it makes Kenya more attractive as an investment destination where the gains sought are capital gains. This detracts from the intended objective of attaining balanced economic development within the region.

Similarly, Rwanda excludes from its tax base, agricultural income below a certain limit. The effect is to make agricultural goods from Rwanda to have a marked advantage over those from other member states and removes from the benefits that should accrue to member states as a result of the integration process. A Ugandan trader would thus, for example be at a distinct disadvantage in trying to sell his produce in Rwanda since he would be required to take the tax he will pay into consideration in determining the pricing of his produce.

In the author’s opinion, the adoption of a code of conduct for investment incentives and company income taxation might go a long in aiding the harmonization of income tax as recommended by the IMF, and as experienced by the European Union. That code might go a long way in reducing the distortions caused by the different tax bases and incentives offered by the member states. Finally, we hope have reached to demonstrate how without tax integration no economic regional integration as a whole is possible.