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## **Investor Rights vis à vis State's Right to Regulate – the Case of Uganda**

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# INVESTOR RIGHTS vis a vis STATE'S RIGHT TO REGULATE

## THE CASE OF UGANDA

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# Presentation Outline

- Background & Overview of Investment in Uganda
- Definitions: Right vs. privilege/ incentive, investor, state
- Sources of Rights - Who gives the rights? is it the state or investor? are they inherent/absolute or qualified? How are the rights identified? (legal framework)
- State Regulation -how are the rights enforced? Is regulation a mechanism for controlling rights abuse?
- Challenges and Recommendations
- Conclusion

## Background and Overview

- Growth rate (01/02) - 6.0%; Projected (02/03) - 4.9%
- Foreign Direct Investment (FDI) inflow/GDP - 3.6%.  
*(This is just about average for sub-Saharan Africa)*
- Average FDI inflows (97-00) - US\$ 171.0M.  
*(This figure has tripled compared to US\$ 45.0M in 1990-1995)*
- Uganda Govt. recognizes the importance of private capital in generating economic growth and alleviating poverty. Slow down in economic growth in has heightened the importance and urgency of seeking increased private investment, including inflows of foreign direct investment (FDI) to help stimulate further economic growth.

## Investment Overview - continued

- Since 1996, Uganda, with assistance from various donors and multilateral agencies, has undertaken a range of initiatives aimed at improving the investment and business climate.
- Institutional Reform – Uganda Investment Authority (UIA), Uganda Revenue Authority (URA).
- Decentralization – each district is now preparing an investment profile that shows its potential for investment

## Investment Overview-continued

- Commercial Justice Reform Program - established Uganda Law Reform Commission (LRC) and a commercial division of the high court. LRC has drafted 60 new laws and amendments (even though only 15 have been passed)
- Tax Appeals Tribunal – gives the public an informal and quick review of tax decisions
- District Land Tribunal – listens to land cases. Still new.
- The Inspectorate of Government (IGG) Act– Dec 2002: provides for the powers and procedures required by IGG to fight corruption

## Investment Overview - continued

- Improving facilitation of domestic and foreign investors (UIA has concluded a memoranda of understanding with various government agencies encouraging them to inter alia adopt client charters.
- And many others.....

# Definitions

**Right:**-an abstract idea of that which is due to a person or governmental body by law or tradition or nature

**Absolute right**-incapable of being repudiated or transferred to another ;not subject to forfeiture

**Qualified right**-limited or restricted; not absolute  
contingent on something else

**Privilege:**- a special advantage or immunity or benefit not enjoyed by all

**Incentive** :-a positive motivational influence

# Definitions-cont'd

A foreign investor :

- A person who is not a citizen of Uganda
- A company in which more than 50% of the shares are held by a person who is not a citizen of Uganda
- A partnership in which the majority of partners are not citizens of Uganda.

State:-the group of people comprising the government of a sovereign state

## Sources of Rights-Legal Framework

- The Uganda Constitution (1995)
- The Investment Code –1991 (amended 1997)
- The Income Tax Act – 1997 (amended 1998)
- Commercial Justice Reform/Law Reform Commission (1992)
- Commercial Court (Practice) Directions (1996, 2002)
- Tax Appeals Tribunal (1997)
- Arbitration and Conciliation Act (2000)

## Sources of rights -Legal framework - continued

- The Exchange Control Act – 1964 (amendment in process)
- The Land Act – 1998
- District Land Tribunals - new
- Insurance Statute – provides framework for insurance sector and established the Insurance commission, the regulatory body for the sector.
- Capital Markets Authority,
- The WTO Rules - Principle of National Treatment?
- Other International Instruments

## Investor rights in Uganda Constitution

- Article 20 & 21 – Fundamental rights and freedoms of the individual are inherent and not granted by the state. The rights and freedoms of the individual and groups shall be respected, upheld and promoted by all organs and agencies of government and by all persons:-
- All persons are equal before and under the law in all spheres of political, economic, social and cultural life and in every other respect and shall enjoy equal protection of the law.

# Uganda constitution-cont.d

- A person shall not be discriminated against on the ground of sex, race, colour, ethnic origin, tribe, birth, creed or religion, or social or economic standing, political opinion or disability.
- Nothing in this article shall prevent Parliament from enacting laws that are necessary for implementing policies and programmes aimed at redressing social, economic, or educational or other imbalance in society.....
- **Note:- The above rights talk about equality of all before the law but do not necessarily address investors.**

# Investor rights in the Investment Code (1991)

## PRIORITY AREAS

- An investor may engage in any type of business or enterprise (unless otherwise specified-e.g crop protection)

## PROCESSING OF APPLICATION

- UIA will investigate and prepare a report in respect to an application for an investment license within 30 days
- UIA shall within 14 days after the report make decision to approve or disapprove application
- UIA shall inform the applicant of its decision within 7 days

## Investor rights-Investment code (cont.d)

- In case of refusal to grant a license, UIA shall refer application and report to the Minister with reasons for denial and **provide a copy to the applicant**
- If applicant is not notified of UIA's decision **within 90 days**, he/she **may lodge complaint** to the Minister who shall **within 30 days** investigate complaint and inform complainant of the results of the investigation

## Investor rights – Investment code (cont'd)

### EXTENSION OF VALIDITY/REVOCAION OF LICENSE

- If a holder of an investment license is unable to begin operating, he may, **giving reasons, apply to the authority for the extension of the period of validity of the license.**
- Where an investor is in breach of any provision of the investment code or terms and conditions of his license, the authority **shall give written notice to the investor requiring him to show cause within a reasonable time why the license should not be revoked.**

## Investor rights – Investment code (cont'd)

### CREDIT

- A foreign investor may obtain credit from domestic financial institutions up to the limit established by Bank of Uganda

### PROTECTION OF FOREIGN INVESTMENTS

- A business enterprise of an investor, or an interest, or right over property forming part of that enterprise **shall not be compulsorily taken possession of or acquired** (subject to provisions in the constitution)

## Investor rights – Investment code (cont'd)

- If a licensed business of an investor is compulsorily taken possession of or acquired, compensation in respect of the fair market value of the enterprise shall be paid within a period not exceeding 12 months from the date of possession or acquisition
- Compensation shall be freely transferable out of Uganda and shall not be subject to exchange control restrictions.

## Investor rights – Investment code (cont'd)

### EXTERNALISATION OF FUNDS

An investor is entitled to externalize funds for a) Repayment of foreign loans or interest on the loans b) Payment of dividends to shareholders

- Payment of emoluments
- Externalization of profits or proceeds on disposal of assets

## Investor rights – Income Tax Act (1997)

### BACKGROUND

- In 1997, tax incentives were repealed from the Investment code and replaced with tax allowances as stipulated in the Income Tax Act (1997) and the Amended Finance Act (1998).
- Tax allowances are assessed and administered by the Uganda Revenue Authority.
- In addition to the above, the investor shall be entitled to a drawback of duties and sales tax payable on imported inputs used in producing goods for export.

## Investor rights – Income Tax Act 97 (cont'd)

- A foreign investor and his expatriate staff **shall be exempt from payment of import duty and sales tax on 1 motor vehicle, personal and household effects within the first 12 months.**

CAPITAL ALLOWANCE- initial allowance on plant and machinery, industrial buildings (including extensions) and Hotels

DEPRECIATION-Computers and data handling equip,Earth moving equipment , Plant and machinery,Vessels, industry and hotel buildings

# Income tax act-cont.d

OTHER DEDUCTIONS ALLOWED- All expenses and losses incurred in the production of income during the tax year, Any loss incurred on the disposal of assets, 20% of expenditures and losses incurred in the production of rental income

## Investor rights – WTO rules?

- Since Uganda is a member of the WTO, If investor is from a country that is also a WTO member, he may be protected by the “non discrimination/national treatment” principle. Therefore, foreign investors may invest and engage in any business activity which local investors of the partner state may undertake. (except as maybe otherwise provided by the law) WTO principles of “Transparency” and “predictability” could also apply.
- WTO TRIMS-Bound by the TRIMS agreement. No notifications made to TRIMS so far

## What do other International Treaties say about investor rights?

- EAC – Model Investment code in progress
- COMESA –
- AU/NEPAD
- ACP-EU
- African Charter on Human and People's rights
- UN Convention on Economic, Social and Political rights

## How are the rights enforced? -State regulation

- The Uganda Investment Authority (UIA) was established by the Investment code (1991) to promote, facilitate and supervise investment in Uganda.
- Other important functions are to assist potential investors in identifying and establishing investment opportunities
  - To receive and review applications for investment, issue licenses and certificates of incentives; To secure other required licenses, secondary approvals and permits for investors and their staff
  - To supervise implementation of the Inv. code, deal with complaints and do all other acts necessary or conducive to the performance of the functions of the authority.

## State regulation – cont'd

- License is the most common and effective tool used by UIA to regulate investors. It is issued in lieu of investment application/proposal meeting certain standards prescribed by government
- Company must be registered with office of the Registrar General
- Government sets minimum thresholds for portfolio investment
- Government retains right to change the amounts from time to time

## State regulation – cont'd

- An environmental impact assessment (EIA) is carried out for any investments deemed to have potential impacts on the environment.
- URA keeps records of all imports and verifies exports
- UIA keeps a register of all certificates of approval to externalize funds.
- In case investor receives domestic credit, government appoints agent to verify due application for the credit as stated in the license

## State Regulation – cont'd

- Implementation process is monitored to ensure it is going on as stated in proposal. If there are any variations, government must be notified.
- Investment is routinely evaluated for (a) job creation (b) revenue generation to government (c) social contributions (d) impact on economy (e) how government policy may be affecting the project etc.
- Disputes between government and an investor will be settled through negotiations for an amicable settlement, or may be submitted to arbitration in accordance with the methods mutually agreed upon by both parties. If the parties do not agree to mode of arbitration, the aggrieved party may appeal to the Commercial court.

## Challenges for Regulators

Regulation is carried out by state bodies which depend entirely on limited government funds which are insufficient. This also means there is insufficient manpower and technology to achieve all parts of their mandate and recommended changes

- UIA is a “one-stop-center” charged with conducting and coordinating all matters relating to investment. However, they do not have all the expertise required for e.g tax assessments, EIA etc. Furthermore, It is not easy to find and recruit staff with all the required skills

## Challenges for Regulators – (cont'd)

- Regulators have to balance the all important role of attracting investment and maintaining good relationships with existing investors whose opinion and word of mouth matters immensely to future investors, with ensuring their investments are viable and the investors are not fraudulent.
- The mandate and associated powers of UIA often overlap with other sectors – Many related initiatives are currently being undertaken by other government bodies including Ministry of Trade, URA, National Environment Management Authority, Registrar General's Office etc.

## Challenges for Regulators (cont'd)

- Lack of data – Even though a wealth of information about potential investors is available on the internet, it is not always in user friendly form and may require substantial staff time to effectively process. Therefore state is not always able to verify that information provided by investor is correct.
- - Absence of a risk-based system of inspections. Customs officials physically inspect 100% of all import consignments. URA personnel have difficulty applying the GATT valuation system because it relies on the validity of importer invoices which constitute a high incidence of fraud and non compliance by importers.

# Challenges for regulators-cont

- Substandard Environmental impact assessments which make it hard for the reviewing authority (NEMA) to render a correct decision.

## Challenges for Investors

### REGISTRATION ISSUES

- Duplicative, overly complex, and laborious process for establishing a business (failure of one-stop center)
- Access to land – only 20% of available land is registered, title registration system is poorly administered, poor security of files, complexity of four different tenure systems, etc

# Challenges for Investors – cont'd

## TAX ISSUES:

- Income tax statute transfers the burden of proof to the tax payer and yet there are no clear guidelines in the form of rulings, and practice notices.
- There are contradictory interpretations of the tax law in different URA departments
- Procedures of The Tax Appeals Tribunal are perceived to be unduly legalistic and time consuming.

# Challenges for Investors – cont'd

## CUSTOMS ISSUES

- Lack of consistency and transparency in application of valuation comparators.
- Customs appeal process is vague
- Duty drawback system is inefficient and cumbersome. Regulations require physical presence of customs official for packaging and loading of goods that qualify for duty drawback. Payments for duty drawback should be made within 7 days but they actually take months due to delays in internal customs procedures for verifying and approving payments

## Challenges for Investors – cont'd

### LEGAL ISSUES

- Lack of consistency between existing laws/regulations and procedures- parts of government accelerate changes in procedures (e.g. stop gap measures to reduce negative impact of legislation) before they are reflected in laws and regulations. Even though is an understandable response to a problem that may need to be fixed quickly, it compromises the transparency and consistency of procedures and provides opportunity for subjectivity and inconsistency. (Stop-gap measures can be changed summarily or may be subject to the discretionary authority of officials). It can also result in confusion and uncertainty on the part of investors since the practice differs from the prescription of the law.

## Recommendations

### REGISTRATION

- Investment registration and establishment procedures need to be simplified and streamlined –
  - UIA should computerize the registration process and assign a single identification number for all administrative transactions including registration and taxation; Consolidate existing forms into single business registration form
  - Introduce system of interagency information sharing subject to strict confidentiality guidelines (sign non-disclosure agreements)

## Recommendations - continued

### LEGAL FRAMEWORK

- Review the rules on deductibility of expenses for tax purposes and simplify and de-formalize the Tax Appeal Tribunal.
- Constitutional restrictions that prohibit or limit the participation of foreign investors in both crop and animal production should be relaxed. While these restrictions have the advantage of keeping agricultural production in the control of the indigenous people, it is likely to pose a serious constraint to the modernization of agriculture in the long term.

# Recommendations-cont'd

- Revise current Investment code - possibly replace UIA's regulatory role of screening and approvals with promotional assistance and facilitation
- The Law Reform Commission's work program needs to include laws relating to taxation management and administration e.g. The Customs Management Act, the Value Added Tax statute. Banking, Foreign Exchange and anti-money laundering laws need to be updated to keep up with international developments in those areas.
- More resources should be allocated to the process of enacting legislation in order to make it faster

# Recommendations – cont'd

## CUSTOMS

- Introduce principle of selectivity as the basis of all import/export inspection procedures.
- Design new procedures, regulations for the collection of data to facilitate risk-based inspections, as well as computerization of procedures and management systems
- Data needs to be compiled on the volume of transactions, reasons for rejection, penalties imposed and appeals. This information needs to be analyzed for trends in order to make recommendations for improvement. It should also be disseminated to various stakeholders.

## Recommendations – cont'd

### DATA AND ADMINISTRATIVE ISSUES

- UIA should consult/coordinate with overlapping sectors/ministries to clarify roles, and declare competencies
- UIA needs to partner with specialized information providers and statistical agencies in order to gather information from the internet better tailored to their needs

## Recommendations - continued

- External partners need to be brought on board to provide direct funding or undertake tasks beyond UIA's resources
- Partner with other organizations to train and supply knowledge lacking in UIA – for example specialized chambers of commerce, local companies etc
- Register foreign and local investments for planning and facilitative purposes. This would help UIA determine who needs support, planned capital investment, planned employment of local personnel etc. UIA will be able to better advise government and will strengthen its monitoring function based on concrete data.

# Conclusion

- Is state regulation enough or does Uganda need an international investment agreement?
- The view from Uganda is that there is no need for an international agreement on investment. Current regulation in place is working even though substantial improvements are needed. (see recommendations).
- There is also a school of thought that advocates for abolishing the national investment code. They argue that the national treatment principle implies that domestic and foreign investors be treated equally under the law. Any benefits or incentives may be established under other laws. E.g fiscal incentives should be placed in the tax code.

# Conclusion – cont.

- An opposing view states that existing and prospective investors need legal protection, and since our neighboring countries like Kenya and Tanzania have investment codes, If Uganda were to abolish the code, it may discourage investors.

Are investor rights absolute or qualified?

- Per the definitions of absolute and qualified rights – This paper's view is that the rights in the Uganda constitution are absolute, (only in as far as equality before the law is concerned, otherwise they are are qualified.
- The WTO legal mechanism is only binding if the investor is a member

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