Country Competitiveness: Reform or Stagnate!

'*Taxspectives*' by Afolabi Elebiju I Originally published in *ThisDay Lawyer, 2nd March, 2010, p.vii*

Introduction

Two recent events gave rise to this week's title. One, the approval of the National Tax Policy (NTP) by the Federal Executive Council - a news items that could easily have passed unnoticed in the din of advocacy/intrigues over the President's extended absence. Second was the fortuitous reunion with my May 2007 Graduate Paper, "*Promoting Country Competitiveness Through Sectoral Reforms: Case Study of Nigerian Mobile Telecommunications Sector, 1996-2007.*" I felt a rush of emotions: the continuing relevance of issues discussed - and many failed predictions of incremental enhancement of our competitiveness through consolidation of various sectoral reforms by the (then) incoming administration.

In my view, the NTP which focuses on non-oil taxation seems to strike the right chord; not surprisingly, given the sheer intellectual rigour and effort that went into it, a project that started in 2002. However, some of the fiscal provisions of the Petroleum Industry Bill (PIB) – currently before the National Assembly, and which seeks to transform the Nigerian oil sector – are underpinned by policy objectives that seem antithetical to the NTP, and could potentially hamstring our standing to compete for investments in the sector. Preparatory to subsequent review of the NTP/PIB, this week I share snippets from the Competitiveness Paper.

> *FDI is such a critical economic reality that the issue is not whether Nigeria needs it, but how to effectively compete for more than her fair share of global capital.*

Reform or Stagnate!

As part of the Introduction, I wrote: "*... the administration's policy reforms [is] exemplified by the National Policy on Telecommunications ..., which sought to bring transparency, structure and order to the sector based on its recognition that it is a veritable tool for national development and for attracting FDI into Nigeria....*

The essential hypothesis of this paper is that sectoral reforms have boosted Nigeria's country competitiveness in the global telecoms industry - the transformation of Nigeria's telecoms sector since 1999/2000 is a model of how an enabling sector environment could attract local and foreign investment and increase the country's competitiveness for foreign capital. Furthermore, I argue that the telecoms liberalisation model can be replicated with necessary amendments in other infrastructural sectors like power, water, transport... to attract FDI and record multiplier effects on the economy....

Underscoring my thesis is the fact that despite full liberalisation of the Nigerian investment environment since 1995, and the availability of tax incentives prior to 1995, there was minimal or nil foreign investment in telecoms, and the country's teledensity was ridiculously low. And Nigeria has always had a huge

market because of its population…

I will also highlight current status of other sectoral reforms … their potential impact on improving country competitiveness, and the imperative of speeding up reforms… by the new administration, upon assumption of office on May 29 2007. …

At the moment, the power sector shows that sectoral reform requires more than legislative enactment and institutional set-up of a regulator pursuant to the new regulatory regime….the President-elect's reported intention to declare a state of emergency in the power sector on assumption of office signals a step in the right direction….”

At page 112: “*Nigeria's potentials largely informed Goldman Sachs' prediction in a recent study, How Solid Are the BRICS? that Nigeria will be the 20th largest economy by 2025 and the 12th largest global economy [ahead] of countries like Italy and Canada by 2050… However, as Goldman Sachs noted … 'there is a major distinction between the BRICS potential and reality. The key to turning one into the other… relies largely on the BRICs finding and keeping in place the conditions for growth... As we showed, miracle conditions are not necessary, but a basic set of powerful conditions is crucial.'”*

How Useful Are Tax Incentives?

At pages 115 and 116, the Paper postulated, “*A note of caution has been sounded for example, that undue emphasis on tax incentives only as an investment promotion strategy may not be worthwhile. 'The use of tax incentives is widespread even though the available empirical evidence on the cost effectiveness of such incentives in stimulating investment is highly inconclusive.' The high divestment rate from Nigeria during the mid to late 1990s bears evidence of this hypothesis. During that period, the introduction or expansion of many incentives did not counteract the 'pariah country status' of Nigeria as a country under … military rule. Thus Nigeria attracted substantial foreign investment only in the oil and gas sector from already existing, rather than new, entrants.”*

Indeed, footnote 341 (at p.116), noted: “*As with every topical issue, there are pro and con arguments. Proponents … argue that there is some signaling involved in a country's grant of incentives – it markets itself positively as the [preferred] destination for FDIs, simultaneously boosting the confidence level of local investors. Reduction of effective tax rates on profits … translates into more profitable investments, and may facilitate the re-investments of domestic earnings therefrom. Furthermore, corporate tax cuts could help the growth of capital markets…*

On the other hand, 'the investment climate …demands a plethora of enabling factors in order to impress investors as the ideal destination for their capital. The most important of these are political stability, a lucrative market, enabling infrastructure, an investor friendly legal and judicial system, an accountable and transparent political administration, and skilled and trained labor.' Kalungi,… citing an Ugandan survey where only 1 out of 12 investors ranked tax incentives as the most important factor in attracting investments…

A tax incentive is redundant if investments would still be made without it and such investments are not 'footloose' … being easily relocable to another country…Citing other examples of 'inappropriate' incentives, he concludes by recommending a single tax incentive, e.g. a 20% low tax rate, instead of multifarous regime…

[Arguably,] great global demand for Nigerian gas, jostling for gas blocks/projects by competing investors, increased domestic gas utilisation … together with the requirement for elimination of gas flaring by 2008 cumulatively constitute a tax redundancy theory that informs the current effort to restrict gas incentives vide the proposed amendments to tax legislation…"

"In the Global Competitiveness Index rankings …, Nigeria fell from 83rd position in 2005 to 101 … in 2006, signaling that modest achievements are not enough, as other countries are also making efforts to improve their own competitiveness. The challenges have been well defined, documented and discussed. What is now required is focused and sustainable action that consolidates on modest gains achieved, of course with requisite participation of the private sector."

Improving Nigeria's FDI Flows

Pages 113-115: *"Why is FDI so important to Nigeria? 'First, it is now generally recognized that FDI has become a significant source of finance in developing countries. It has become a useful means of integrating into the global market place. But Africa has been let out of this process for many reasons.…' FDI is such a critical economic reality that the issue is not whether Nigeria needs it, but how to effectively compete for more than her fair share of global capital.*

FDI data from UNCTAD supports the view that democracy and reforms … have started to exert positive impact on Nigeria's competitiveness…Using data available as of October 2006, UNCTAD shows a 60% growth in Nigeria's FDI inflow between 2004 and 2006. It is highly unlikely that … [absent] reforms, Nigeria could have attained the position of being the 3rd African FDI destination in 2005… with inflow of US$3.4 billion, representing 70% of West African inflows."

LeLaw Disclaimer

Thank you for reading this article. Although we hope you find it informative, please note that same is not legal advice and must not be construed as such. However, if you have any enquiries, please contact the author, Afolabi Elebiju at a.elebiju@lelawlegal.com