

**THE REPUBLIC OF UGANDA**  
**THE HIGH COURT OF UGANDA**  
**COMMERCIAL DIVISION**  
**HCT - 00 - CC - CS - 303 – 2008**

**HAJJI MUSA NTALE ..... PLAINTIFF**

**VERSUS**

**UGANDA REVENUE AUTHORITY ..... DEFENDANT**

**BEFORE:     HON. JUSTICE GEOFFREY KIRYABWIRE**

**J u d g m e n t**

The plaintiff HAJJI MUSA NTALE filed this suit against the defendant, Uganda Revenue Authority for an order that the defendant refunds Ushs 50,160,000/= paid to it by Cairo International Bank Ltd and an order that the plaintiff is not indebted to the defendant for any income tax arrears for the period 1997-2007, in respect of premises known as Plot 24 Upper Naguru East Road.

The facts agreed by the parties for trial are that the Plaintiff during the year 1997 borrowed Shs. 175,000,000/= from Cairo International Bank Limited (hereinafter referred to as the Bank) for the purpose of completing a Block of eight flats at Naguru in Kampala.

The loan was advanced in the form of building materials and the money paid directly to the contractors by the Bank.

The Bank then entered into a tenancy agreement with the Plaintiff whereby the Bank would occupy the flats and the rent which would have been paid to the Plaintiff was to be withheld by the Bank for a period of ten years, that is up to 2007, and was so withheld.

The Defendant demanded tax arrears for that period from Cairo International Bank Ltd by way of third party agency notices and the Bank paid to the Defendant Shs. 50,160,000/= out of rent due to the Plaintiff for the period after 2007.

The Plaintiff contends that the money advanced as a loan to him by Cairo International Bank Ltd and withheld by the said Bank was money spent on producing the income and is fully deductible under section 22 of the Income Tax Act and prays that the Shs. 50,160,000/= received by the Defendant from the Bank to be refunded to him

The Defendant on the other hand contends that money withheld by the Bank was a taxable income and could not be deducted under section 22 of the Income Tax Act.

The plaintiff was represented by Mr. Kusiima while the defendant was represented by Mr. Ouma. The parties did not schedule the case, but simply filed written submissions. Both counsels agreed that the court should write a judgment based on their submissions.

**Issue:                Whether rental money withheld by a mortgagee bank in occupation of premises built using the loan as repayment thereof is deductible within the meaning of S. 22 of the Income Tax Act.**

Counsel for the plaintiff submitted that Section 5 of the Income Tax Act imposes rental tax on every individual who has rental income for the year of income. Counsel for the plaintiff however submitted that it is a principle of taxation that one who has not earned income can not be taxed and that the chargeable income of a person for a year of income is the gross income of the person for the year less the total deductions allowed. In this regard he referred Court to sections 15 and 16 of the Income Tax Act.

Counsel for the plaintiff submitted that there was no chargeable income for the plaintiff during the period years 1997 to 2007. This is because the rental income due to him was retained by the bank to complete the unfinished block of flats. Furthermore, that the expenditure spent by the bank on behalf of the plaintiff to put up the building for purposes of earning rental income was expenditure incurred in the production of that income and was therefore wholly deductible for purposes of ascertaining chargeable income within the meaning of Section 22 (1) (a) of the Income Tax Act.

Counsel for the plaintiff submitted that the defendant took the view that deductions on rental income were only limited to 20% of the income as expenditures and losses incurred in the production of such income under S. 22 (1) (c) of the Income Tax Act. Counsel for the plaintiff argued that this could not be the case because the intention of this provision cannot be to limit a rental income earner to 20% deductions thereby subjecting him to a loss of 80% of his expenditure on developing the property. Counsel submitted that he did not agree that subsection (c) above limits the plaintiff to a 20% deduction only.

In reply, Counsel for the defendant submitted that rental income is imposed only on individuals, and it has to be segregated from gross income; in this regard he referred court to Sections 5 (1), S. 5(3) and 22 (1) (c) of the Income Tax Act. Counsel for the defendant submitted that the plaintiff earned rental income during the period of 1997 to 2007, in the form of a repayment of the loan that had been disbursed by Cairo International Bank.

Counsel for the defendant further submitted that Section 15 of the Income Tax Act which provides for chargeable income when read together with Section 5(3) (a) of the same Act means that rental income and gross income are to be segregated when computing tax. It therefore followed that chargeable income only arises in the cases of gross income and not rental income. Counsel for the defendant referred to the definitions of the terms; rent, rental income and payment under the Income Tax Act and submitted that in view of those definitions, the plaintiff earned rental income between the years 1997 and 2007, albeit in the form of a repayment of a loan disbursed by Cairo International Bank and it is irrelevant that the bank instead of handing over the money to the plaintiff would channel it to itself.

Counsel for the defendant further submitted that Sections 22 (1) (a) and (c) of the Income Tax Act provide for different circumstances. In this regard Section 22 (1) (a) of the Act covers expenditures and losses of persons engaged in business as long as it is not that of letting property, while Section 21(1) (c) of the Act deals with rental income, and therefore, the deductions on rental income are restricted to 20%.

Counsel for the defendant submitted that in the construction of statutes, a strict and literal interpretation is preferred and therefore the Act should be interpreted the way it is and not as it ought to be. He referred to Rowlett J, in the case of CAPE SYNDICATE V INLAND REVENUE COMMISSIONER (1921) 1 KB 64 for this submission.

In rejoinder, Counsel for the plaintiff submitted that Section 22 (1) (c) is a blanket allowance for all rental income earners whether one has incurred expenditure or not in that year, and that it also takes care of rental income earners who having made the total deduction of expenditures still have a surplus. That all the expenditures must be first deducted to get net income which is then subject to 20% deduction. Counsel for the plaintiff further submitted that the reason why rental income is not included in the gross income is to avoid double taxation and therefore if only 20% is deducted from the rental income, then this would defeat the purpose of Section 2 of the Act.

I have carefully considered the submissions of both counsels for which I am grateful. Having taken into account the issue as framed by the parties and the submissions of both counsels, I find it necessary under order 15 rules (1) (5) to pose the following questions for consideration by the court under this issue to bring clarity;

- (i) Whether the money collected by Cairo International Bank from the plaintiff's property was to rental income under the Income Tax Act.
- (ii) Whether the money is subject to rental tax, and if so, what are the deductions allowed on the said money under the Income Tax Act?
- (iii) What are the remedies available to the parties?

I will now address those issues.

- (i) Whether the money collected by Cairo International Bank from the plaintiff's property was rental income under the Income Tax Act.**

The term rent is defined under S. 2 (ccc) of the Income Tax Act as follows;

*“rent” means any payment, including a premium or like amount, made as consideration for the use or occupation of, or the right to use or occupy, land or buildings”*

I have perused the tenancy agreement dated 12<sup>th</sup> March 1997 (Annexure F to the plaint), between the plaintiff and Cairo International bank by which the plaintiff agreed to let the property for a period of ten years for rent at a rate of Ushs. 3,800,000/= per month for the eight flats. Furthermore, in the tenancy agreement, it was agreed that the tenancy would be linked to the credit facility so that the rent received was credited to the plaintiff's loan account as a loan payment under Paragraph 4 of the rental agreement. There is no doubt that the parties to the rental agreement intended this agreement to be a rental agreement, and therefore, the proceeds from the letting of the property was rent, which was instead of being collected by the plaintiff as the landlord, credited on his loan account with the bank.

Section 2 (ddd) of the Income Tax Act defines the term rental income as follows;

*“rental income”, in relation to an individual for a year of income, means the total amount of rent derived by the individual for the year of income from the lease of immovable property in Uganda by the individual with the deduction of any expenditures and losses incurred by the individual in respect of the property”*

In this case the rental income was paid through the servicing of a loan with the bank which was also a tenant in the same premises.

The term payment is defined under the Income Tax Act. According to Section 2 (xx) of the Act,

*“payment...” includes any amount paid or payable in cash or kind, and any other means of conferring value or benefit on a person”*

The term payment under the Act is wide enough to include any means of conferring value or benefit on a person. The plaintiff was entitled to receive the rent payments from the property. However, by virtue of the rental agreement between him and the bank, the rent payments were credited on his loan account with the bank. The payment of rent to the bank to reduce the indebtedness of the plaintiff in my view constitutes a value or benefit to the plaintiff and would therefore amount to a payment within the meaning of the term “payment” under the Income Tax Act.

In light of these provisions, it follows and I accordingly so find that the amount paid as rent for the occupation of the property, although paid to the bank to reduce the indebtedness of the plaintiff to the bank, was a payment made to the plaintiff and therefore, amount to rental income.

**(ii) Whether the money is subject to rental tax, and if so, what are the deductions allowed on the said money under the Income Tax Act.**

Section 5 (1) of the Income Tax Act provides for rental tax, on rental income as follows;

***“Rental tax imposed.***

*(1) Subject to and in accordance with this Act, a tax shall be charged for each year of income and is imposed on every individual who has rental income for the year of income.”*

Furthermore, Section 5 (3) of the Act provides that,

*“The tax imposed under this section on an individual is separate from the tax imposed under section 4 and—*

*(a) the rental income of the individual shall not be included in the gross income of the individual for any year of income;*

- (b) *expenditures and losses incurred by the individual in the production of the rental income shall be allowed as a deduction under this Act for any year of income; and*
- (c) *the tax payable by a resident individual under this section shall not be reduced by any tax credits allowed to the individual under this Act”*

It follows from this section that rental income is treated separately from the gross income of an individual. To that extent Counsel for the defendant was correct in his submissions.

Furthermore, what amounts to chargeable income is defined in Section 15 of the Act as follows;

***“Chargeable income.***

*Subject to section 16, the chargeable income of a person for a year of income is the gross income of the person for the year less total deductions allowed under this Act for the year.”*

It therefore follows that chargeable income for tax purposes should be calculated less the total deductions allowed under the Act for that year.

Section 22 of the Act provides for the deductions that are allowed follows;

***“Expenses of deriving income.***

- (1) *Subject to this Act, for the purposes of ascertaining the chargeable income of a person for a year of income, there shall be allowed as a deduction—*
  - (a) *all expenditures and losses incurred by the person during the year of income to the extent to which the expenditures or losses were incurred in the production of income included in gross income;*
  - (b) *the amount of any loss as determined under Part VI, which deals with gains and losses on the disposal of assets, incurred by the person on the disposal of a business asset during the year of income, whether or not the asset was on revenue or capital account; and*
  - (c) *in the case of rental income, 20 percent of the rental income as expenditures and losses incurred by the individual in the production of such income.”*

I have already found that the Act provides separately for chargeable income subject to income tax and rental income subject to rental tax. It therefore follows that in respect of rental income the applicable provision of the Act is Section S. 21(1) (c) which specifically provides that the deduction allowed in case of rental income is 20 % of the rental income as expenditures and losses incurred by the individual in the production of such income.

It is trite law that where the language of a tax statute is plain and unambiguous, the words of the statute should be given should be given their ordinary and strict interpretation. This position of the law is stated in the cases of **CAPE BRANDY SYNDICATE V INLAND REVENUE COMMISSIONERS** [1921] 1 K.B. 64, 71 and **INLAND REVENUE COMMISSIONERS V PLUMMER** [1980] A.C. 896.

It therefore follows that the deduction allowed on the plaintiff's rental income is 20 % of the rental income as expenditures and losses incurred by the individual in the production of such income.

I find that the rental money withheld by Cairo International Bank as mortgagee bank in occupation of premises built using the loan as repayment is subject to rental tax under the Income Tax Act and the plaintiff is only entitled to deductions of 20% of the rental income as expenditures and losses incurred by the individual in the production of the rental income. I accordingly find that the assessment made by the defendant's rental income to have been correct and hence collection of it under a third party agency notice.

In the premises, the suit is dismissed with costs.

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Justice Geoffrey Kiryabwire  
**JUDGE**

Date: 10/07/12

10/07/12

9:35am

**Judgment read and signed in open court in the presence of;**

- Nakku Najjuma for Defendant

In court

- None of the parties
- Rose Emeru – Court Clerk

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**Geoffrey Kiryabwire**

**JUDGE**

**Date: 10/07/2012**