THE REPUBLIC OF UGANDA

IN THE HIGH COURT OF UGANDA AT KAMPALA

(COMMERCIAL DIVISION)

CIVIL APPEAL NO. 29 OF 2020

(Arising from TAT Application No. 3 of 2019)

NATIONAL SOCIAL SECURITY FUND :::::::::::::::::::::::::::::::: APPELLANT

VERSUS

UGANDA REVENUE AUTHORITY :::::::::::::::::::::::::::::::::: RESPONDENT

<u>BEFORE: HON. MR. JUSTICE BONIFACE WAMALA</u>

<u>RULING</u>

Introduction

This is an appeal from the decision of the Tax Appeals Tribunal (hereinafter called ***TAT***) delivered on the 27th day of March, 2020.

Background

The brief facts of the case are that sometime in 2001, the Appellant sought clarification from the Respondent about the tax treatment of the interest expense it incurs when paying benefits to members. By letter dated 23rd August 2001, the Respondent wrote to the Appellant confirming that interest paid to members' accounts by NSSF is accepted as an allowed deduction. On 20th November 2013, however, the Respondent wrote another letter communicating that interest paid /payable to members is not an allowed deduction since it fails to satisfy the conditions for deductibility under Section 25 of the Income Tax Act (hereinafter referred to as **ITA**).

The Respondent conducted an audit for the period 2005 to 2012 on the Applicant and issued an assessment of UGX 30,521,703,065 as principal tax and penal tax interest of UGX 12,196,875,941 to the Applicant, disallowing the said interest as an allowable deduction. The Appellant objected to the assessment on the ground that it was entitled to deduct the said interest under S. 25(1) of the ITA. The Respondent issued an objection decision maintaining its position that the Applicant was not entitled to make the said deduction.

The Appellant filed a suit in the High Court of Uganda (Commercial Division) vide Civil Suit No. 366 of 2014 challenging the objection decision. The parties amicably settled the other issues contained in the objection decision except the issue of interest paid to NSSF members being an allowable deduction and the legality of penal tax on the assessed sum hence the tax liability of UGX 42,196,249,077 which the Respondent insisted was payable by the Appellant. However due to the decision in Uganda Revenue Authority versus Rabbo Enterprises Ltd and Another, the matter was referred to the Tax Appeals Tribunal.

The Appellant filed an appeal before the Tax Appeals Tribunal (TAT) challenging the objection decision of the Respondent. The TAT delivered a ruling in favour of the Respondent to effect that the interest payable to the Appellant's members is not an allowable deduction and that the Appellant is liable to pay the principal tax and penal tax assessed. However, in the minority ruling, one of the Tribunal members held that the Appellant was not liable to pay the penal tax assessed.

The Appellant being dissatisfied with the decision of the TAT lodged this appeal on the following grounds:

1. The learned members of the Tribunal erred in law when they found that the Contributions made by the Applicant's members do not create a debt obligation within the meaning of Sections 25(1) and 2(s) of the Income Tax Act and therefore found that the interest was not a deductible expense.
2. The learned members of the Tribunal erred in law when they held that the said interest is not a payment of an expense of income of capital nature but a return on investment.

3. The learned members of the Tribunal erred in law when they held that the annual interest paid by the Appellant to its members was not incurred in the production of income included in the gross income.
4. The learned members of the Tribunal erred in law when they found that the Respondent's letter dated 23rd August, 2001 did not create a legitimate expectation for the Applicant.
5. The learned members of the Tribunal erred in law in finding that the Appellant was liable to penal tax.
6. The learned members of the Tribunal erred in law when they failed to properly evaluate the evidence on record and thereby came to an erroneous decision.

Representation and Hearing

At the hearing, the Appellant was represented by Mr. Kambona Oscar, Mr. Birungyi Cephas, Mr. Bruce Musinguzi and Mr. Martin Mbanza. The Respondent was represented by Ms. Mwajuma Nakku Mubiru, Mr. Ronald Baluku Masamba, Ms. Barbra Ajambo Nahone and Mr. Aliddeki Ssali Alex.

It was agreed that the matter proceeds by way of written submissions. Both Counsel made and filed their respective submissions. Counsel also appeared before me and made oral highlights of their submissions. I will consider the Counsel's submissions in the course of handling the respective grounds of appeal. I will however begin with a preliminary issue that was dwelt upon by both Counsel regarding the role of the High Court as an appellate court in matters arising from the decisions of the Tax Appeals Tribunal.

Role of the High Court as an Appellate Court in TAT Matters

Counsel for the Appellant in their submissions considered the matter as a first appeal from the TAT to the High Court and relied on the decision of ***Kifamunte Henry V Uganda, SCCA No. 10 of 1997*** regarding the duty of a first appellate Court to appraise the evidence on record and make its own inferences on all issues of law.

In reply, it was submitted for the Respondent that appeals from the Tribunal to the High Court are governed by the provisions of Section 27(2) of the Tax Appeals Tribunal Act which provides as follows:

> *An appeal to the High Court may be made **on questions of law only**, and the notice of appeal shall state the question or questions of law that will be raised on the appeal.*

Counsel for the Respondent submitted that in the case of ***Uganda Revenue Authority V. Tembo Steels Ltd, Civil Appeal No. 09 of 2006 (Arising out of TAT No. 22 Of 2005*), Justice Christopher Madrama Izama** held as follows;

> ***"In the case of section 27 of the Tax Appeals Tribunal Act, the analogy of a second appeal applies because it specifically provides that an appeal will be on questions of law only. It does not have to be a second appeal for this point to be made. The statute is clear and unambiguous that every appeal to the High Court may be made only on questions of law. It is clear that the intention of Legislature in the above instance is to leave questions of fact such as assessment to professionals and reserve to the courts only points of law for determination. With the above authorities as a guideline the question is whether the grounds in the notice of appeal disclose "questions of law" within the meaning and intent of section 27 of the Tax Appeals Tribunal's Act so as to confer jurisdiction on the High Court to determine the ground ... Where there is no question of law or controversy of law, section 27 of the Tax Appeals Tribunal does not give the High Court jurisdiction to entertain the ground of appeal or the appeal if no other point of law is raised."***

Counsel for the Respondent therefore submitted that in light of the above provision of the law and authority, the High Court is only mandated to entertain appeals from the Tribunal only on points of law, and not fact. Counsel submitted that the authorities relied on by the Appellant on the role of the first appellate Court are therefore not applicable in this case, since at this stage, the Court is not concerned with evaluation of evidence but rather with adjudicating only points of law.

Counsel for the Appellants made no rejoinder to this submission.

Looking at the provision of Section 27 (2) of the TAT Act, the word "may" is used. It states:

> *An appeal to the High Court <u>may</u> be made **<u>on questions of law only</u>**, and the notice of appeal shall state the question or questions of law that will be raised on the appeal. [Emphasis added]*

From my reading of the said provision, the word "may" is in reference to the choice of an aggrieved party to file an appeal or not. It does not refer to a choice as to whether to restrict the appeal to questions of law only or to include questions of fact or mixed law and facts. As such, once a party elects to file an appeal, they will do so by a notice of appeal, in which notice the party **"shall state the question or questions of law that will be raised on the appeal"**. This connotes that the requirement that the appeal from the TAT to the High Court be based on questions of law only is mandatory.

I am therefore in agreement with **Madrama J.** (as he then was) in ***Uganda Revenue Authority V. Tembo Steels Ltd (supra)*** that in the case of section 27 of the Tax Appeals Tribunal Act, the analogy of a second appeal applies because it specifically provides that an appeal will be on questions of law only; and that it does not have to be a second appeal for this point to be made. The true position of the law, therefore, is that when entertaining an appeal such as this one, the appeal has to be based on questions of law only and the High Court conducts the appeal as if it were a second appeal. As such, it calls for no re-evaluation or re-appraisal of evidence before the Court makes its findings. The Court's consideration is to be directed towards errors and misdirection on points of law only.

The reason for this appears to me to be clear. This is because the proceedings that take place in the Tribunal are always preceded by a decision of the Commissioner or the Respondent generally that gives rise to either an appeal to the TAT or an application for review. Such is usually either a taxation decision or an objection decision. In my view, the intention of the legislature was to treat the proceeding in the High Court as a second appeal; in light of the two earlier proceedings, one within the Respondent's mandate and the other in the TAT.

I will now proceed to consider the grounds of appeal on their merits.

Ground 1: That the learned members of the Tribunal erred in law when they found that the contributions made by the Applicant's members do not create a debt obligation within the meaning of Sections 25(1) and 2(s) of the Income Tax Act and therefore found that interest was not a deductible expense.

Appellant's Submissions

Counsel for the Appellant submitted that the Tribunal held that the contributions by the Appellant's members do not constitute a debt obligation within the meaning of Sections 25 (1) and 2 (s) of the Income Tax Act (hereinafter referred to as **ITA**). Counsel submitted that the Tribunal based its interpretation of S. 2(s) of the ITA on the **"ejusdem generis"** rule of statutory construction/interpretation to state that accounts payable and notes payable are things of the same general kind or class as current liabilities in a company's balance sheet. The Tribunal's interpretation of Section 25(1) of the ITA was that the term "debt obligation" is only applicable to debts payable by a company within a short period or namely, a company's **current liabilities.** The Tribunal further held that contributions made to NSSF are not current liabilities in the Applicant's balance sheet because they may not be payable within a short period.

Counsel submitted that the Tribunal also held that the relationship between NSSF and members is not that of a debtor/creditor. That NSSF owes a fiduciary duty to the members and beneficiaries and that the contributions of members do not create a debt obligation within the meaning of S. 25(1) and S. 2(s) of the ITA as what is involved is a trustee/member'/beneficiaries' relationship.

The Appellant's Counsel submitted that the Tribunal misdirected itself in its application of the rules of statutory interpretation since the rules follow hierarchy whereby the first option is to use the literal approach before using the purposive rule, the mischief rule and the ejusdem generis rule. Therefore, where words are not ambiguous, then their ordinary meaning is the primal meaning.

Counsel relied on the case of ***URA V Siraje Hassan Kajura & Others, SCCA No. 9 of 2015*** where it was held that;

> ***Where words or emphasis are clear and unambiguous, they must be construed in its natural and ordinary sense. Where the language of the Constitution/Statute sought to be interpreted is imprecise or ambiguous, a liberal generous or purposeful interpretation should be given to it.***

Counsel submitted that the Supreme Court in the above cited case relied on the case of ***Cape Brandy Syndicate V IRC [1921] 1 KB 64 at 71*** where it was held that;

> ***In a taxing Act <u>one has to look merely at what is clearly said.</u> There is no room for any intendment. There is no equity about tax. There is no presumption as to tax. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used.***

Counsel therefore submitted that it was therefore apparent that for the court to apply any other method of statutory interpretation, there has to be shown some form of ambiguity or unclearness, in the absence of which the words are to be given their direct meaning.

Counsel submitted that in the present case, the Tribunal was not right to invoke the *ejusdem generis* rule when interpreting Section 2 (s) of the ITA which defines a 'debt obligation'. Counsel submitted that Section 2 (s) is clear and unambiguous. There was no need to invoke the *ejusdem generis* rule because in defining debt obligation, the Section uses the words *'an obligation to make a repayment of money to another person'.* The aforementioned is the only condition that one needs to meet in order to qualify as a debt obligation. The Section then provides examples of debt obligations which include *"accounts payable and the obligations arising under promissory notes, bills of exchange and bonds'.* The undisputed facts are that the Appellant has an obligation to repay the contributions, with interest, to the members. Therefore, once it is clear that NSSF had an obligation to pay contributions with interest to its members, then it was entirely unnecessary for the Tribunal to attempt to use the *ejusdem generis* rule.

The Appellant's Counsel further submitted that in any case, the *ejusdem generis* rule is only applicable where general or ambiguous words follow a list of words considered to be of the same kind; not when a general word or term is followed by a set of words or terms. Counsel cited the <u>**Black's Law Dictionary (8th Edition, 2004 at page 1568**</u>) for the definition of the principle of *ejusdem generis* and the cases of ***The Registered Trustees of Kampala Institute V Departed Asians Property Custodian Board,***

SCCA No. 23 of 1993 and ***Radio Pacis Limited Vs the Commissioner General Uganda Revenue Authority, HCCS No. 8 of 2013***.

Counsel for the Appellant also submitted that the Tribunal misconstrued the definition of the term 'debt obligation' as per the ITA. Counsel submitted that the test for what constitutes a debt obligation is whether a person owes another any obligation to make a repayment of money as provided for under Section 2 (s) of the ITA. It was the Appellant's submission that the Appellant has an obligation to make a repayment to its members. Counsel relied on the provisions of the NSSF Act Cap 222, to wit; Sections 2, 19, 34, 35, to argue that since the monies in issue are members' savings, the Appellant owes its contributors an obligation to repay members' money and, in doing so, the Appellant has an obligation to pay with interest. Counsel submitted that the obligation to pay the benefits with interest is created by statute and is therefore mandatory.

Counsel therefore concluded that the Tribunal misdirected itself and erred in law by concluding that the term 'debt obligation' only applies to debts payable by a company within a short period or the company's current liabilities, thereby coming to a wrong conclusion that the contribution by the Appellant's members do not constitute a debt obligation within the meaning of Sections 25 (1) and 2 (s) of the ITA.

Respondent's Submissions

In reply, it was submitted by Counsel for the Respondent that the Respondent entirely agreed with the holding of the Tax Appeals Tribunal to the effect that the contributions by the Appellant's members do not constitute a debt obligation within the meaning of Section 25 (1) of the ITA. Counsel submitted that S. 25 (1) of the ITA establishes the conditions upon which interest is to be allowed as a deduction under the Income Tax Act, namely that; a debt obligation arises; the debt obligation is incurred by a person in the production of income; the income is included in gross income; and the deduction for interest is allowed only during the year of income.

Counsel submitted that it was the Respondent's submission that no debt obligation arises in the Appellant's case and accordingly, the Appellant cannot claim the expense relating to interest paid out to its members, to be used for its own tax benefit. Counsel submitted that the Appellant's claim that the members' contributions result into a debt obligation and the interest paid into member's accounts is an allowable deduction emanates from the erroneous interpretation by the Appellant that the expense incurred by the Appellant falls within the meaning of Section 25 of the Income Tax Act which is not the case.

Counsel submitted that according to Section 2 of the NSSF Act, the Appellant is mandated to **make payments** of benefits and other payments to its members; yet the obligation under Section 2 (s) of the ITA is to **make a repayment** of money. Counsel submitted that as used in the NSSF Act and the ITA, the words 'payments' and 'repayments' are two separate words. Counsel relied on the **Black's Law Dictionary, 11th Edition, Page 1363** for the definition of the word 'payment'; and the **Collins Concise English Dictionary, Seventh Edition, on page 1405** for the definition of the word 'repay'.

Counsel submitted that the interest paid to the members by NSSF is not a debt obligation in as far as it does not relate to a repayment. Indeed, the NSSF Act only provides for payments to be made by the Appellant to its members and NOT repayments. The interest paid by the Appellant to its members is an interest payment. The fact that it is not a repayment automatically disqualifies it from falling within the definition of a debt obligation under S. 2 of the ITA. The NSSF Act does not have and did not foresee the contributions paid out to the members as being a debt obligation. No wonder no such words were used by the draftsman.

Counsel submitted that the payments made by the Appellant includes contributions made by the employers, who are not beneficiaries of these contributions, but rather merely contributors to the fund. The Appellant owes no obligation to the employers (who contribute the highest percentage to the fund of 10% as opposed to the employees' 5% contribution). The Respondent questioned why there was no claim by the Appellant of a debt obligation or a debtor-creditor relationship with the employers as contributors. Counsel argued that the only plausible answer was because the Appellant was aware that it only has an obligation to pay out and not an obligation to make a repayment.

Counsel also submitted that Section 19 of the NSSF Act provides for the different types of benefits that can be accessed by the Appellant's members. According to Counsel, it follows that the contributions by members are simply monies kept on the member's account until an occurrence of some future event that the money may be paid out by the Appellant to its contributing member. This does not in any way favor the interpretation that the contributions are a debt obligation for which interest must be paid so as to qualify as an expense to be an allowable deduction under section 25 (1) of the ITA.

Counsel further submitted that Section 35 (1) provides for interest which is to be **calculated on the balance standing to the credit of the account of the member of the fund**. As such, the "**balance standing"** is the contribution that is made by the members which is on their account and as earlier submitted above, this contribution within the meaning of the NSSF Act is not a debt obligation within the meaning of Section 25(1) and S. 2(s) of the Income Tax Act.

Counsel relied on the **Black's Law Dictionary, 11th Edition, on page 506** to define the word a "debt" and submitted that for a debt obligation to exist between persons, there has to be a debtor-creditor relationship. Counsel submitted that since the Income Tax Act makes mention of interest payment in respect of a debt obligation, this implies the existence of a debtor – creditor relationship. Accordingly, the intention of the law was to provide for a deduction of the expense incurred as interest in instances where a tax payer is indebted to another and hence incurs interest in the course of repaying their debt which they are obliged to do so.

Counsel further submitted that the said provision does not apply to the Appellant who is not in a debtor – creditor relationship with her members but rather a trustee and fiduciary relationship since the members save with the Appellant and in turn receive "interest" in every year. The said "interest" is akin to a dividend or a profit earned by the members of the Applicant and does not relate to interest which arises as a result of a debt obligation. Counsel supported the decision of the Tribunal in its ruling and argued that had the relationship between the Appellant and its members created a debtor-creditor relationship, the Appellant would have included the same as a liability in its balance sheet which it did not do.

Counsel relied on the decision in **National Security Fund V Makerere University Guest House (Civil Suit No. 525 OF 2015) [2017] UGCOMMC 27 (6 September 2017)** to submit that the Appellant is a trustee who holds funds on behalf of her members, invests the said funds and announces a profit which is distributed to the members annually. Counsel submitted that this is a return of profit on members' investment and NOT interest expense as is the case between a debtor and a creditor. The trustees owe a fiduciary duty to the beneficiaries and in this case the **trust is created by and governed by the NSSF Act** as managed by a Board and employees who are charged with management of property of the members until when the **savings are transferred back to the beneficiary for whom the trust is created by Parliament**. They are required to pay the savings with interest and do not have a beneficial interest in the fund other than reasonable remuneration and lawful fees and charges.

Regarding the Appellant's submission on the rules of statutory interpretation, Counsel for the Respondent submitted that they entirely agree with the application of the rules of statutory interpretation made by the Tribunal in construing Sections 2(s) and 25(1) of the Income Tax Act. Counsel cited numerous authorities and argued that the *text* (literal meaning) cannot be applied in isolation of the *context (the background purpose- purposive approach).* Therefore, the advancement of the argument that the literal meaning can be applied strictly without the contextual approach has long been departed from by Courts in several Jurisdictions as shown in the authorities cited. (***W. T. Ramsay Ltd Vs. Inland Revenue Commissioners: HL 12 MAR 1981 [1981] 1 All ER 865; Republic Vs Commissioner Domestic Taxes & Sony Holdings Limited Misc. Civil Application No. 363 of 2018; Reserve Bank of India Vs. Peerless General Finance and Investment Co. Ltd & Others {1987} 1 SCC 424***; ***Commissioners of Inland Revenue V. Mcguckian [1997] UKHL 22; [1997] 1 WLR 99***; ***Nyamuchoncho & Anor V. Attorney General & Ors (Miscelleneous Cause No. 241 of 2017) [2018] UGHCCD 95***).

Counsel therefore submitted that it only follows then, that the use of the *ejusdem generis* rule by the learned members of the Tribunal was not in error but a matter of principle in applying the rules of statutory interpretation. It is the context that gives the provision of the statute color.

Counsel further submitted that employers and employees in designated employment are mandatorily required by the law to contribute savings to the Applicant and accordingly, a debt obligation does not arise since the same cannot be created under legal compulsion. Counsel relied on Section 7 of the NSSF Act to argue that the relationship between the Applicant and her members lacks **the element of voluntariness** which is part and parcel of **the debtor vs borrower relationship** which would ordinarily give rise to **repayment** of money to the debtor with interest, default of which attracts legal consequences.

Counsel concluded that in light of the above submissions and authorities, it was the Respondent's submission that the Honorable members of the Tribunal did not err in law when they correctly held that the contributions made by the Appellant's members do not create a debt obligation within the meaning of S. 25(1) and 2(s) of the ITA. Counsel prayed that the Court be pleased to uphold the decision of the Tax Appeals Tribunal, find no merit in this ground of Appeal and strike it out.

Appellants Submissions in Rejoinder

Counsel for the Appellant reiterated their earlier submissions and further stated that the arguments of the Respondent on the difference between the words 'payment' and 'repayment' notwithstanding, the Appellant submits that even using the business analogy to understand the transactions of social security, it is clear that the employer and employee make payments to the fund and at the appropriate time, the fund repays those contributions plus interest to the members. It was therefore the submission of the Appellant that even without going into semantics and interpretation of words, payment and repayment are part and parcel of the Appellant's business.

Counsel further submitted that even going by the dictionary meaning, repayment is payment. The appellant pays back the money contributed by the members with interest. There was therefore a debt obligation on the Appellant to pay the benefits to its members. Counsel relied on Sections 11, 19 and 34 of the NSSF Act for that submission.

Counsel submitted that the contributions made by the employers are made for the benefit of the employees (members) but were also an entitlement of the employee. The employer cannot opt out of this contribution and neither can the Appellant opt out from repaying the said contribution to the employees. Counsel submitted that the Respondent's understanding of the Appellant's business as merely keeping money on a member's account over simplifies the business of the Appellant which is regulated by an Act of Parliament. The obligations of the Appellant to make these payments to the employees are not only mandatory or statutory but are the justification for social security. If the Fund were not paying interest, the employees would merely be losing money because whatever would be paid would be eroded by inflation.

Counsel emphasized that contrary to the submission of the Respondent, employees whose benefits are due from the Fund, have a right to sue for them in case the Fund defaults. The members' right to sue arises from a debtor-creditor relationship which was created by statute as soon as the member made the contribution; in line with Section 2(2) of the NSSF Act.

The Appellant disagreed with the Respondent and the finding of the Tribunal that there is a trustee and fiduciary relationship between the employee and the Fund. The Appellant further submitted that the Appellant is neither a Trust created under the Trustees Act, nor does it operate under a Board of Trustees. Counsel submitted that it was noteworthy that the Respondent in its submissions did not address the arguments raised by the Appellant about the definitions of a Trust and a Retirement Fund in the Income Tax Act. The Respondent also did not address itself to the definitions of a fiduciary relationship. Counsel stated that the arguments of the Respondent that the decision in the case of **NSSF V Makerere University Guest House Civil Suit No.525 of 2015** binds this Court is erroneous and oblivious of the doctrines of precedent.

Counsel concluded that the argument by the Respondent that 'voluntariness' (sic) is a condition precedent to a debt obligation is an unfounded argument; and that the 'debtor-borrower relationship' is a term that is alien to the Income Tax Act and to common sense.

Resolution by the Court

The relevant provisions concerning a debt obligation for purpose of determining whether interest is allowed as a deductible expense are Sections 25 (1) and 2 (s) of the ITA.

Section 25 (1) of the ITA provides:

> *Subject to this Act, a person is allowed a deduction for interest incurred during the year of income in respect of a debt obligation to the extent that the debt obligation has been incurred by the person in the production of income included in gross income.*

Section 2 (s) of the ITA provides:

> *"debt obligation" means an obligation to make a repayment of money to another person, including accounts payable and the obligations arising under promissory notes, bills of exchange and bonds.*

The Tax Appeals Tribunal (TAT) considered the meaning of the terms used under Section 2 (s) of the ITA and came to the conclusion that the common thread is that there is a debt owed by one person to another creating an obligation to pay. The Tribunal then applied the *ejusdem generis* rule and found that arising from the items mentioned in Section 2 (s), accounts payables and notes payable which are things of the same general kind or class are current liabilities in a company's balance sheet.

Referring to the definition of current liabilities as "short-term debt", inter alia, the Tribunal found that it was apparent that the intention of the legislature was to restrict the meaning of the term "debt obligation" to debts payable by a company within a short period, that is, the company's current liabilities. The Tribunal concluded that, as such, for an item to be included among the things specifically mentioned under S. 2 (s), it must be a current liability in a company's balance sheet. The Tribunal concluded that the contributions made to NSSF are not current liabilities in the Applicant's (now Appellant) balance sheet because they may not be payable within a short period.

The Appellant challenged the application by the Tribunal of the *ejusdem generis* rule of statutory interpretation on two grounds. One was that where words of a statute were clear and unambiguous, the rules of statutory interpretation dictate that the literal rule is applied first before resorting to the purposive rule. Secondly, the *ejusdem generis* rule was not applicable to the provision that was subject of construction by the Tribunal. The Respondent, on their part, defended the approach taken by the Tribunal and submitted that the TAT correctly applied the *ejusdem generis* rule.

Traditionally, there are four main rules for statutory interpretation, namely, the literal rule, golden rule, the mischief rule and the *ejusdem generis* rule. Over time, the courts have developed an integrated approach that is known as the purposive approach. The purposive approach attempts to integrate any or a combination of the above four rules and does not conflict or compete for space with them. Basically, the purposive approach seeks to look for the intention of the legislature from the words used in a statute. Where the words are clear and unambiguous and the court is capable of assigning meaning and purpose to the said words, the court will look no further than the literal rule. However, where the language of the statute sought to be interpreted is imprecise or ambiguous, a liberal, generous or purposeful interpretation is applied by the court. **See: *URA V Siraje Hassan Kajura & Others, SCCA No. 9 of 2015.***

To my mind therefore, when applying the rules of statutory interpretation, the first point of call is the literal rule provided its application does not lead to absurdity. As between the literal rule and the *ejusdem generis* rule, the former is first in hierarchy. To that extent, I am in agreement with the Appellant's Counsel that without showing the inadequacy of the literal rule in regard to the language used in Section 2 (s), the Tribunal was not right in its application of the *ejusdem generis* rule.

Secondly, and more importantly, the *ejusdem generis* rule by definition is a canon of statutory construction that where general words or phrases follow a list of specifics, the general words or phrases will be interpreted to include only the items of the same type or scope of genus as those listed. **See:** The **Black's Law Dictionary (8th edition, 2004) at page 1568**; ***The Registered Trustees of Kampala Institute V Departed Asians Property Custodian Board SCCA No. 23/93***; and ***Radio Pacis Limited vs the Commissioner General Uganda Revenue Authority (HCCS 8 of 2013)***.

It is clear that for the rule to apply, a list of particular words is given by the provision and is followed by general words which must be interpreted as the same in scope and genus as the particular words. It is not the other way round; where general words are followed by a set of specific words or examples.

Section 2 (s) of the ITA which the Tribunal was interpreting defines a "debt obligation" as;

> *"an obligation to make a repayment of money to another person, including accounts payable and the obligations arising under promissory notes, bills of exchange and bonds".*

It is clear that the phrase "an obligation to make a repayment of money to another person" constitute the general words in that phrase. The phrase "including accounts payable and the obligations arising under promissory notes, bills of exchange and bonds" are the specific words and, indeed, examples of what is included in the general words. Such a provision does not call in the application of the *ejusdem generis* rule as clearly laid out above. The rule was therefore wrongly applied by the Tribunal which may have led the learned members of the Tribunal to arrive at a wrong conclusion as to the meaning of the term “debt obligation” under Section 2 (s) of the ITA.

It is my considered view that looking at the provision in Section 2 (s) of the ITA, the words used are clear and unambiguous. Use of the literal rule coupled with a purposive approach is capable of delivering appropriate meaning of the term debt obligation as used under the ITA and arriving at the clear intention of the legislature.

From reading of *Section 2 (s) of the ITA* and the submissions by the parties, the test for what constitutes a debt obligation is whether a person owes another any obligation to make a repayment of money. *Section 2 of the NSSF Act* provides:

> *“There is established a fund to be known as the National Social Security Fund, into which there shall be paid all contributions and all other payments made in accordance with this Act and out of which there shall be paid all benefits and other payments required by this Act.*”

A reading of Sections 19, 34 and 35 of the NSSF Act discloses that the benefits includes the amount of a member’s contribution plus interest paid annually to each member as they stand on account at the time repayment is due. It was submitted by Counsel for the Appellant that the obligation to pay both the benefits and interest is created by statute and is therefore mandatory. For the Respondent, it was submitted that the obligation created upon the Appellant by the NSSF Act is to make payments of benefits and not repayment; and that since those payments are not repayments, they do not amount to a debt obligation within the meaning of Section 2 (s) of the ITA. Counsel for the Respondent relied on the Dictionary meaning of the words “payment” and “repayment”.

With all due respect, I find this distinction quite elementary and not substantive in the least. I agree with the Appellant’s Counsel that it is a question of semantics. From the very definitions from the **Black's Law Dictionary (supra)** and the **Collins Concise English Dictionary (supra)** as cited by the Respondent's Counsel, it is clear that "payment" may include "a repayment". When a person performs an obligation by delivery of money (which is payment), the person may be doing so in repayment of money they received from the other and are refunding it. In that way, the payment is in fact a repayment or refund.

From the operations of the Appellant as provided for under the NSSF Act, it is clear to me that the employers and employees make payments to the Fund and at the appropriate time, the Fund repays those contributions plus interest to the members. I do not see how such a transaction does not amount to a repayment. I therefore reject this line of argument by the Respondent.

It was argued for the Respondent that the payments made by the Appellant includes contributions made by employers who are not beneficiaries and against whom the Appellant does not claim a debt obligation. The Respondent questioned how such would amount to a debt obligation as against the beneficiaries. However, according to the Appellant, the contributions made by the employers are made for the benefit of the employees (members) and are an entitlement of the employees. The employer cannot opt out of this contribution and neither can the Appellant opt out from repaying the said contribution with interest to the employees.

I find the above argument by the Appellant made out basing on the provisions of the NSSF Act and upon the understanding of how the Fund operates. Although the employers make contributions to the Fund, it is clear to all the relevant stakeholders in that regard that the money remitted to the Fund by the employer belongs to the employee, and for a specific purpose; being social security. The obligation to repay this money with interest is therefore towards the employee who is the beneficiary; and not the employer even when the latter is the one who actually remitted the contributions.

It was shown by the Appellant that the “balance standing” as used under Section 34 of the Act refers to money on the employee’s account and not on the NSSF account. As such, when the Appellant uses the said monies to invest, it is equivalent to borrowing the employee’s money upon which the Appellant has to pay interest at the end of the year. I agree with this representation of the nature of the business of the Appellant. Contrary to the argument of the Respondent, the arrangement does not have to include an express loan agreement so as to amount to a debt obligation. A debt obligation may arise by operation of the law or by business operations. That is the case with the Appellant. It is also the same obligation that arises out of the relationship between the tax payer and the Respondent. There is no express debtor-creditor relationship between a tax payer and the Respondent but by operation of the law, a tax payer has a debt obligation against the tax authority.

It was held by the Tribunal that the relationship between NSSF and members is not that of a debtor/creditor but a trustee and fiduciary relationship and that the contributions of members do not create a debt obligation within the meaning of S. 25(1) and S. 2(s) of the ITA and what is paid to the members is not interest but a profit or return on investment. The Appellant submits that it is neither a Trust created under the Trustees Act, nor does it operate under a Board of Trustees. The Appellant disputed the claim that the interest paid to its members was not interest but a profit or dividend; showing that there was a clear difference between a profit and a dividend and the two terms cannot relate to the same transaction.

I am in agreement with the Appellant. The NSSF Act is clear as to the operations of the Fund. What is paid is interest and the way it is arrived at is clearly set out under the Act. It was uncalled for in my view for the Tribunal to import into the Act the aspects of profit or dividend where the express provisions of the law say otherwise. There is also nothing in the Act that defines or represents the Appellant as a Trust. I am in agreement with the Appellant that the decision in ***NSSF V Makerere University Guest House (supra)*** was cited by the Respondent out of context.

The issue in the above case concerned ownership of property and whether the compulsory contribution towards the Fund amounted to deprivation of property in accordance with Article 26 of the Constitution. The categorization by the Learned Judge of the relationship between the Fund and its members as that of a trustee – beneficiary was not for purpose or upon the language of taxation. It was upon general principles according to the facts that were before the Court. The Court's finding did not take into account the words "dividend" and "interest" as used in the ITA. Such a finding cannot therefore be used as the basis for determining the technical difference between the terms for taxation purposes.

My finding therefore is that the words "interest" as used both in the ITA and the NSSF Act on the one part, and the term "debt obligation" as used in the ITA are clear and unambiguous. The intention of the legislature is also clear to me that the law intended to create a debt obligation as between the Fund and its members.

It was therefore an error on the part of the Tribunal in interpreting Section 2(s) and Section 25 of the ITA to conclude that the term "debt obligation" only applies to debts payable by a company within a short period or namely, to the company's current liabilities. That way the Tribunal wrongly concluded that on that basis, the contributions by the Appellant's members do not constitute a debt obligation within the meaning of the said provisions of the ITA, and were therefore not a deductible expense. I find that the Appellant has satisfied the Court that the contributions by the Appellant's members constitute a debt obligation as against the Appellant within the meaning of Sections 25 (1) and 2 (s) of the ITA. The first ground of appeal therefore succeeds.

Ground 2: The learned members of the Tribunal erred in law when they held that the said interest is not a payment of an expense of income of capital nature but a return on investment.

Appellant's Submissions

It was submitted by the Appellant that the question of whether the amount referred to as interest under S. 35 of the NSSF Act qualifies as interest for the purposes of S. 25 (1) and 2 (kk) of the ITA is again one of statutory interpretation. Counsel submitted that the ITA was enacted in 1997 while the NSSF Act came into force in 1985. Therefore, if the framers of the ITA had considered that interest in the NSSF Act did not fall within the definition of Section 2(s) of the ITA, they would have provided for that exception.

Counsel relied on the definition of interest under Section 2 (kk) of the ITA and submitted that the definition of "interest" is quite broad and not restricted to a single definition as the Tribunal treated it. Therefore, the expenses/interest in question could properly have fallen anywhere in Section 2 (kk) sub-section i, ii, or iii of the ITA. The Tribunal was therefore wrong to restrict its meaning to only that which arises between a lender and borrower. Counsel submitted that the Appellant has a debt obligation to its members and the interest that arises there from is the kind envisaged under the Income Tax Act.

The Appellant's Counsel submitted that the Tribunal's finding that an NSSF member does not have the right to make a demand for immediate repayment of his contribution and that NSSF is therefore not a borrower, was erroneous. Counsel submitted that the issue of immediate demand for repayment is not a condition for interest to be deductible under Sections 25 and 2(kk) of the ITA. The conditions are that the interest should be incurred as a result of a debt obligation. It matters not that the person whose money has to be repaid has the right to demand immediate payment or not. Counsel argued that if the ITA wanted only persons that can demand immediate payment, it would have clearly stated so. Counsel therefore submitted that the Tribunal erred in law in finding that the interest paid by the Appellant is not the one envisaged under Section 25 of the ITA.

Counsel further submitted that it was not in dispute that some form of payment is made by the Appellant to the members. The payment made was of interest because the payment is as a result of a debt obligation and therefore meets the criteria in Section 2(kk)(i). Counsel submitted that the payment could also fit under Section 2(kk)(ii) of the ITA which defines interest to include other payments functionally equivalent to interest, or Section 2 (kk)(iii) of the ITA that defines interest to include any commitment. Counsel therefore concluded that the Appellant has satisfied the test of whether the payment was of interest or not.

Counsel faulted the Tribunal for ruling that the interest in issue paid by the Applicant to its members is a return on investment; and that the members of NSSF are like shareholders who invest in a company's ventures with an intention of obtaining dividends. The Appellant's Counsel relied on the definition of a dividend under Section 2(w) of the ITA and submitted that in order for one to receive a dividend, they must be a shareholder in a company.

Counsel argued that under the Public Enterprise Reform and Divestiture Act, Cap 98, the only shareholder in the Appellant is the government of Uganda. Counsel stated that this was corroborated by the uncontroverted evidence of the Appellant's witness before the Tribunal who testified that NSSF is 100% owned by government. Counsel submitted that the members, therefore, do not constitute shareholders in the Appellant. Therefore, any payments to them cannot be regarded as a dividend or a return on investment. Counsel argued that as such, the conclusion by the Tribunal that interest paid by NSSF to its members amounts to dividends was unqualified and misdirected.

Respondent's Submissions

Counsel for the Respondent defended the finding and conclusion of the Tribunal to the effect that the amount referred to as interest under Section 35 of the NSSF Act does not qualify as interest for purposes of Section 25 (1) and S. 2(kk) of the ITA. Counsel cited the power of the Court to use the purposive approach of statutory interpretation which enables the court to look beyond the words of the particular statute. In that regard, Counsel invited the Court to look at the definition of "interest" as used in the *Kenya's National Social Security Act, No. 45 of 2013* since the NSSF Act of Uganda does not define the word "interest".

Counsel submitted that ***<u>interest on the contributions</u>*** as used under Section 34 (1) of the NSSF Act of Uganda is definitely synonymous with ***the investment income credited to the accounts of individual members*** as provided for in the Kenya's National Social Security Act, No. 45 of 2013, an Act made in 2013. Counsel made further reference to Section 35 of the NSSF Act and submitted that the Appellant is obliged to make payments to its members and the said payment is akin to a dividend or a return on investment. Accordingly, it cannot be said to cause a debt obligation within the meaning and context of the Income Tax Act since it is investment income which is credited onto the accounts of members at the specified rates.

Counsel argued that the above scenario is clearly distinguishable from an instance where a person borrows from the bank at a particular interest rate and is obliged to make monthly repayments of the money borrowed in accordance with the terms and conditions as agreed upon between the parties. Counsel concluded that the interest referred to under the NSSF Act constitutes a return on investment and thus the expense incurred in this regard is not deductible and therefore the holding by the learned members of the Tribunal was rightly grounded. Counsel prayed that the Court be pleased to answer this ground in negative and strike it out.

Appellant's Submissions in Rejoinder

It was submitted that Section 2 of the NSSF Act is about the scope of business of NSSF (the Appellant) and is not an attempt to define the word 'interest' or 'debt obligation'. The NSSF Act does not define interest but by specifying an interest rate and the base on which the rate is applied, it is obvious that what is paid is interest as is known in its ordinary meaning.

Counsel submitted that the Respondent's attempt to insert the definition of interest from a Kenyan legislation into the NSSF Act of Uganda was an attempt to erroneously use the purposive approach where the subject provisions of the Ugandan law are very clear and where the two systems are quite different. There is no ambiguity created by the definition of the word 'interest' under S. 2 (kk) of the Income Tax Act and the use of the same word under Section 35 of the NSSF Act and S. 25(1) of the Income Tax Act. The elements of the interest provided under S. 35 of the NSSF Act qualify it as interest for the purposes of S. 2 (kk) and S. 25(1) of the ITA. Counsel argued that there was no ambiguity and hence the literal rule must apply.

Resolution by the Court

As I pointed out in ground one above, the purposive approach of statutory interpretation is an integrated approach and does not conflict with the literal rule or indeed with any of the other rules. Under the purposive approach, if the words of a statute are plain, clear and promote the legislative intent, then no more that the clear and ordinary meaning of those words should be resorted to. As such, the purposive approach itself reinforces the literal rule, just as it does to the other rules of statutory interpretation. Therefore, the issue with the approach adopted by the Respondent is not so much that they invoked the purposive approach but that they did so contrary to the plain and clear words of the provisions in

Sections 2 (kk) and 25 (1) of the ITA on the one hand and Sections 34 (1) and 35 of the NSSF Act on the other.

Under *Section 2 (kk) of the Income Tax Act*, interest is defined to include;

(i) any payment, including a discount or premium, made under a debt obligation which is not a return of capital;

(ii) any swap or other payments functionally equivalent to interest;

(iii) any commitment, guarantee, or service fee paid in respect of a debt obligation or swap agreement; or

(iv) a distribution by a building society. [Emphasis added]

Section 34 (1) of the NSSF Act provides –

> *There shall be opened and maintained for each member of the fund an account in the fund to which shall be credit all standard, voluntary and supplementary contributions and interest on the contributions and from which there shall be paid any benefits and refunds to or in respect of the member and all prescribed fees chargeable for issuing evidence of membership and registration.*

Section 35 of the NSSF Act makes a range of provisions on interest, the rate and how the same is to be applied on a member's account.

In its ruling, the Tribunal held that the amount referred to as interest under S. 35 of the NSSF Act do not qualify as interest for purposes of Section 25 (1) and Section 2 (kk) of the ITA. The reasoning of the Tribunal was that the meaning of a debt obligation under Section 25(1) implies the existence of a lender-borrower relationship; and that the interest should be in respect to what a borrower pays a lender. The Tribunal found that the interest paid by the Appellant in this case is compensation for use of the members' contributions. That NSSF is not a borrower but rather an investor/trustee. The Tribunal found so because, according to them, interest paid under the NSSF Act has certain conditions to be met by the beneficiaries as laid out under S.19 of the NSSF Act; secondly, an NSSF member does not have the right to make an immediate demand for immediate repayment of his contribution; and thirdly, although interest paid under the NSSF Act is compensation, the intention of the legislature was that for such interest to be a deductible expense, it ought to have arisen as a debt obligation or a lender – borrower relationship.

Having found that a debt obligation exists as between the Appellant and its members, I find that the wording of Section 2 (kk) is plain and unambiguous. Interest is any payment made under a debt obligation which is not a return of capital; or any other payment that is functionally equivalent to interest; or any commitment paid in respect of a debt obligation.

The facts before us is that contributions are made on behalf of members of the Appellant which are put on the members' accounts. The Appellant manages these accounts and uses these monies to invest, make earnings and at the end of each year, give interest at a rate that is determined by the Minister but, in any case, not less than 2.5% per annum. According to the Appellant, the monies standing on the members' account is the member's money and the Fund borrows it to make the necessary investments to earn money which they pay as interest to the members in addition to defraying off other expenditures of the Fund. The Appellant reasons that if they did not do so, the members' money would keep on losing value owing to inflation and this would, as well, affect their gross income.

For the Respondent, it is argued that the interest that is paid to members is a return of capital or a return on investment, that is equivalent to a profit or a dividend that is paid after the Appellant has used the member's money. The Respondent reasoned that the Appellant is a trustee to the members/beneficiaries and owes the members a fiduciary duty to ensure that their money is well managed and grown through a return on investment.

I am in agreement with the Appellant that the claim by the Respondent that what is paid by the Appellant to the members is a profit or dividend is not borne out by the provisions of either the ITA or the NSSF Act. The members are not shareholders in the Appellant, whose 100% shareholding belongs to the Government. The Appellant's members cannot therefore be entitled to dividends, profit or return on investment or of capital over a business that does not belong to them. What is paid to the members clearly is interest for use of the member's money by the Appellant to make earnings.

In the circumstances therefore, I find that the payment made by the Appellant is capable of being described as "any payment made under a debt obligation which is not a return of capital"; or "any other payment that is functionally equivalent to interest"; or "any commitment paid in respect of a debt obligation". My finding therefore is that the payment made by the Appellant to its members is a payment of an expense of income, thus interest, in respect of a debt obligation not being a return of capital or a return on investment. The second ground of appeal therefore succeeds.

Ground 3: The learned members of the Tribunal erred in law when they held that the annual interest paid by the Appellant to its members was not incurred in the production of income included in the gross income.

Appellant's Submissions

Counsel for the Appellant submitted that Section 25 (1) of the ITA makes two tests for allowance of a deduction for interest, namely; the interest should be incurred during the year of income; and it should be incurred by the person in the production of income included in the gross income.

As to whether interest is incurred during the year of income, Counsel submitted that under Section 35 of the NSSF Act, it is mandatory for the Appellant to pay interest to the members. As such, the Appellant has a liability (incurred) towards its members for the contributions they make. It is not in dispute therefore that the interest is incurred, however the test of whether the interest is incurred during the year of income is one related to allocation. In this case since the expense is incurred continuously in all years, it was disingenuous for the Tribunal to agree with the argument of the Respondent that the interest rate is pronounced the following year. Counsel submitted that the Appellant in its submissions before the Tribunal extensively argued this position of the timing difference but the Tribunal ignored the same.

Counsel submitted that it is well established that tax returns are filed six months after an accounting period so the interest will in any case be in the period before filing the tax return. Besides it is normal practice to pay other expenses like bonuses and dividends in the following year after establishing the business performance. It is also well established that financial statements have always been made on historical basis. Financial Statements are different from budgets. One cannot argue that the payment belongs in the accounts of the year of payment.

The Appellant therefore submitted that in whichever year the interest is allocated to the employees' account is an accounting issue. It is not a question of law. The Appellant used the accrual method of accounting not cash, therefore the year cannot change the transaction.

Regarding the question whether the interest was incurred in the production of income included in the gross income, the Appellant made reference to Sections 30, 34 and 35 of the NSSF Act.

Counsel submitted that under *Section 34 of the Act*, the Appellant receives its revenue, being contributions from its members(employees). This is confirmed by *Section 28 (a)* which provides that the funds and resources of the fund shall consist of all sums from time to time received by or falling due to the fund in respect of contributions, income on investment, fees, fines, penalties and interest on dues. Under *Section 30 thereof*, the

Appellant invests the excess money available to it. The earnings by the Appellant are used to pay the interest to the members account, reserve account and defray other expenses of the Appellant.

Counsel further submitted that the statutory obligation to credit the member's account with interest is on a monthly basis from the time a member is registered with the fund. It is therefore clear that the interest deducted by the Appellant is part of the production process of the income that ultimately becomes the chargeable income of the Appellant.

Counsel further submitted that the test as to whether the interest was an expense incurred by the person in the production of income included in the gross income in the instant case was based on two aspects; one is whether the interest was an expense incurred by the NSSF; and two, whether the expense was incurred in the production of NSSF's income. Counsel submitted that in order to answer the two above questions, one requires to first understand the nature of NSSF's business and how the Fund earns its income.

It was the Appellant's submission that it receives contributions from employees as specified by statute, all the contributions received are invested through government bonds, treasury bills, other securities, equity investments in high profile companies and investment in properties such as land and rental property. The Appellant earns income from these investments which forms part of the gross income of the Applicant and is subject to tax. Counsel argued that if NSSF were not investing the funds, then it would merely be keeping the funds and the amounts paid to those qualified to receive them would actually be less than what they contributed and the whole exercise would be meaningless.

Counsel concluded that it was therefore disingenuous for the Tribunal to think that the payment of interest is not part and parcel of the Appellant's business. Counsel argued that if the Respondent's position is taken, then the Appellant will not have chargeable income. In any case, *Section 22 (2) of the ITA* defines what does <u>not</u> qualify as allowable deductions and the interest in question is not provided for. The Tribunal ought to have sought guidance from this provision but it did not, thereby coming to a wrong conclusion. Counsel therefore submitted that the Appellant's operations meet the tests under Section 25 (1) of the ITA as the interest paid to the contributors was incurred in the production of income and was therefore an allowable deduction.

Respondent's Submissions

It is the Respondent's submission that the annual interest paid by the Appellant to its members was not incurred in the production of income included in gross income. Counsel submitted that in line with Section 25 (1) of the ITA, it is the Respondent's position that the debt obligation (in this case the interest) should be incurred in order to produce income that is included in gross income in order for such an amount to be allowable as a deduction whilst determining the chargeable income of the tax payer. The provision envisages that interest will be incurred in the course of producing that income. Therefore, to the extent that interest will be incurred in the production of income but not of a character of a debt obligation incurred by that person in the year of income, included in gross income, such interest will not be allowable.

Counsel submitted that under Section 35 (2) and (7) of the NSSF Act, the interest rate is declared by the Minister after the end of the financial year and the rate is effective on the day that the declaration is made. The Respondent argued that this means that the obligation to pay interest arises after the year end; which is after derivation of such income. It would follow that in that scenario the interest rate is applied or declared by the Minister after the income has been derived and set aside for apportionment. Counsel relied on the case of ***AM Bisley & Co. Ltd Vs Cir (1985) TNZTC 5082*** to buttress their argument that since interest expense is determined after the year end, it does not constitute an existing obligation which arose in the course of that year and cannot be incurred as an expense for tax purposes.

Counsel further submitted that the interest paid into the members' account by the Applicant is simply an appropriation of income since it is not incurred in the course of producing this income but is determined after the income is derived. The Respondent therefore entirely agreed with the holding of the Tribunal to the effect that annual interest paid by the Appellant to its members was not incurred in the production of income included in gross income. The Respondent invited the Court to answer this ground in the negative.

Appellant's Submissions in Rejoinder

Counsel submitted that the submission by the Respondent that the interest is determined after derivation of such income is a wrong assertion. It was the Appellant's submission that it is only a timing difference issue and would mean that the said interest would only be deductible in the subsequent year. This would not have an effect on the Appellant claiming the interest, but it would only be an issue of when the Applicant can claim the interest.

Counsel invited the Court to take cognizance of the fact that although the interest rate is declared by the Minister at the end of the year, this interest has to be applied on the members' balances at the beginning of the year. Section 47 of the Income Tax Act specifically provides for when interest should be accounted for. Counsel submitted that the interest of the members should be taken into account when it accrues which is during the year of production of income when the interest is paid on the investments made with the contributions.

It was therefore the Appellant's argument that the interest is actually incurred and accrues during the year of income and is only declared at the end by the Minister. However, throughout the year, the management of the

Appellant incurs the interest through the various investments made with the members' contributions. The interest payable to the members is only decided upon at the end of the year. Therefore, the date of declaration is a timing issue, but it does not erase the fact that the interest was incurred during the year of income.

Counsel further argued that it was worth noting that since the interest is computed on a debt obligation, it means that at the start of the year the obligation is known. This further implies that during the year, various investments are undertaken to repay that obligation with interest. As a result, it can be concluded that the interest is incurred during the year of income; and therefore, the interest would have been incurred in a particular year and is deductible in the same year.

Counsel therefore concluded that the Tribunal erred in law when they held that the annual interest paid by the Appellant to its members was not incurred in the production of income included in the gross income. The Appellant prayed to Court to find that the Appellant's operations meet the tests under Section 25 (1) of the ITA; to the effect that the interest paid to the contributors was incurred in the production of income and is therefore an allowable deduction.

Resolution by the Court

The Tribunal while holding that the interest paid by the Applicant was not incurred in the production of income included in the gross income stated that the interest paid by the Applicant is not a payment of an expense of income of capital nature but a return of investment. The Tribunal reasoned that the members of NSSF are like shareholders who invest in a company's ventures with the intention of obtaining dividends. The Tribunal further reasoned that if interest is not taxable as provided for under S. 38 of the NSSF Act and is a return on investment, then it cannot be an expense incurred in the production of income included in the gross income.

The Tribunal relied on the case of ***Ralli Estates Ltd v Commissioner of Income Tax [1961] 1 E.A 48*** where Lord Denning stated thus:

> ***Their Lordships prefer to turn back to the words of the Act and ask whether the payments were expenses wholly or exclusively incurred in the production of income of the payer and this means that you must look at the purpose of the payments. Were they paid in order to acquire capital assets? Or for a capital purpose? If so, they are capital expenditure. But if for an income purpose they are revenue expenditure.***

It was stated by Counsel for the Appellant that the ***Ralli Estates case (Supra)*** relied upon by the Tribunal was distinguishable from the instant matter. Counsel argued that in the above case, Lord Denning was quoting Section 14 (1) of the East African Income Tax (Management) Act, 1952 which stated that;

"… for purposes of ascertaining the total income of any person there shall be deducted all outgoing and expenses wholly and exclusively incurred during the year of income by such person in the production of income".

Counsel pointed out that the matter in contention in the ***Ralli Estates case (Supra)*** was the treatment of expenses on purchase of land (capital expenditure) by the Applicant and unrelated to interest. The case was therefore distinguishable and not applicable to this matter.

Perusal of the ***Ralli Estates case (supra)*** discloses that it is true as stated by the Appellant that the court's consideration was as to whether the expense was for an income purpose or a capital purpose and concerned treatment of expenses on purchase of land (which is capital expenditure) by the Applicant and the court's finding was unrelated to interest. I am therefore in agreement with the Appellant's Counsel that the said case was distinguishable from the circumstances of the present matter.

The other basis of the Tribunal's finding was that if interest is not taxable and is a return on investment then it cannot be an expense incurred in the production of income included in the gross income. I have already found that the interest paid by the Appellant to its members is not a return on investment. As shown by the Appellant, the interest is an expense which, if not made, the Appellant would be acting in contravention with the provisions of the NSSF Act. I agree that savings are made in the Fund for social security and the only way the members' savings keep meaningful and growing is through the payment of interest. It is therefore true that payment of interest is part and parcel of the Appellant's business and would, on that ground, qualify to be an expense made in the production of income.

According to Section 25 (1) of the ITA, for interest to be allowed as a deduction, the interest should be incurred during the year of income; and it should be incurred by the person in the production of income included in the gross income. It is clear from a reading of Section 35 of the NSSF Act that although interest is declared at the end of the year, the obligation to pay interest on the part of the Appellant accrues at the beginning of the year. Similarly, to the members, the right to interest accrues at the beginning of the year. As submitted by the Appellant, the fact that the payment of interest is effected the following year is merely an accounting issue and not a legal issue. I agree that it changes neither the obligation to pay interest nor the accrual of the interest for the benefit of the Appellant's members. I am therefore satisfied upon the law and the facts before me that the interest paid to the Appellant's members is incurred during the year of income. Clearly, incurring and effecting payment are different aspects under the law.

Secondly, the nature of the Appellant's business is that it receives contributions for employees as specified under the Act. The Appellant invests the contributions in a number of ventures as was shown in evidence. The Appellant then earns income from these investments which earnings form part of the gross income of the Appellant and is subject to tax. As a consequence of use of the said contributions to make the said earnings, the Appellant incurs the obligation to pay interest to the owners of the money (the members). It is therefore clear that the interest deducted by the Appellant is part of the production process of the income that ultimately becomes the chargeable income of the Appellant. I do not find it disputable that the earnings made by the Appellant from using the said contributions for investment form part of the gross income of the Appellant. As such, the interest payable to the members is incurred in the production of income included in the gross income.

The Learned Members of the Tribunal therefore erred in their conclusion and finding that the annual interest paid by the Appellant to its members was not incurred during the year of income and in the production of income included in the gross income. The third ground of appeal also succeeds.

Ground 4: The learned members of the Tribunal erred in law when they found that the Respondent's letter dated 23rd August, 2001 did not create a legitimate expectation for the Applicant.

Appellant's Submissions

It was the Appellant's case before the Tribunal, as an alternative argument, that the Appellant was entitled to rely on the legitimate expectation created by the letter by the Respondent dated 23rd August 2001 which was to the effect that interest paid by the Appellant to its members was an allowable deduction. Counsel for the Appellant relied on a number of court decisions that elucidate the doctrine of legitimate expectation, namely; ***DMW (U) Ltd v Attorney General & Another UGHCCD Civil Suit No. 24 of 2019; Associate Professor Charles Niwagaba vs. Makerere University [2019]*** relying on the English case of ***Council of Civil Service Union vs. Minister for Civil Service [1984] ALL ER 935 at page 949***.

Counsel submitted that the communication in the said letter was the Respondent's position and the interest was treated as such until the Respondent's letter dated 20th November 2013 that altered that position. Counsel submitted that having acknowledged that the said letter created a legitimate expectation, the Tribunal should have vacated the whole assessment.

Counsel further submitted that the Tribunal had no basis for arriving at the conclusion that the doctrine of legitimate expectation could not be used to legalize an illegality. Counsel submitted that the letter in question was legally issued by the Respondent on 23rd August 2001. The objection decision issued by the Respondent on 14th April 2004 stated that the interest in question was not an allowable deduction, it did not state that the position or letter issued in 2001 was illegal.

The Appellant's Counsel also argued that the letter dated 23rd August 2001 amounted to a private ruling within the meaning of **Section 161 of the Income Tax Act** (now **Section 45** of the Tax Procedure Code Act). Counsel relied on the case of ***Gordon Sentiba & Others V Uganda Revenue Authority Misc Cause No. 35 of 2010*** for the submission that since there was full disclosure by the Appellant, and the letter communicating the Respondent's position was relied on by the Appellant with the Respondent's knowledge for over 9 years, the same amounted to a private ruling and was binding on the Commissioner.

Respondent's Submissions

It was the respondent's submission that the letter dated 23rd August, 2001 did not create a legitimate expectation for the Appellant and the Respondent strongly agreed with the Ruling of the Tribunal in this regard. Counsel relied on the decisions in ***Keroche Industries Limited V Kenya Revenue Authority & 5 Others {2007} e KLR***; ***Republic Vs. Kenya Revenue Authority Exparte Shake Distributors Limited {2012} e KLR***; and ***Justice Kalpana Rawal Vs Judicial Service Commission & 3***

Others {2016} E Klr, CA; for the meaning and parameters of the doctrine of legitimate expectation.

Counsel submitted that the doctrine is applicable where the representation made by the respondent is one which can be competently and lawfully made. In the instant appeal the Tribunal ruled that interest paid by the Appellant cannot be considered an allowable deduction under the auspices of Section 25(1) and S. 2 (s) of the ITA and therefore the doctrine cannot be used to legalize an illegality. Counsel further submitted that the doctrine does not apply where clear statutory words override any contrary expectations however founded. The words of the ITA under section 25(1) and S. 2(s) are very clear that the interest earned from investment of member's contributions by the Appellant is not the interest envisaged in Section 25(1) and S 2(s). Therefore, any contrary expectation cannot override a statutory provision.

Counsel for the Respondent also submitted that the claim by the Appellant that the letter of 23rd August 2001 was a private ruling was erroneous. Counsel submitted that the letter was an ordinary letter written from the Respondent to the Appellant. Counsel further submitted that this issue of the letter being a private ruling was never raised by the Appellant, neither in its objection notice to the Respondent nor in the Application before the Tax Appeals Tribunal.

Counsel further submitted that provisions for a private ruling are clearly stipulated under S. 45 of the Tax Procedure Code Act (TPCA). An Application for a private ruling must be in writing and clearly state the purpose for which a private ruling is sought, following which the Commissioner issues a private ruling which must meet the requirements under S. 45(7) of the TPCA. Counsel emphasized that the request for a private ruling must clearly state that it is being sought for; which was not done by the Appellant, but rather, what was written was a general letter.

Counsel concluded that the Tribunal was right when it concluded that the doctrine of legitimate expectation would not apply in the instant case.

Appellant's Submissions in Rejoinder

Counsel for the Appellant reiterated their earlier submissions and further submitted that the law in dispute is Section 25, which allows for deductions of interest incurred in respect of debt obligations. Counsel submitted that the authorities cited by the Respondent support the notion of a promise being made within the confines of the law. Counsel submitted that the law allows for deductions of interest where one has incurred a debt obligation. It is therefore legal for one to claim such deduction. The Appellant had already established that it incurs such interest and in 2001 wrote to the Respondent and claimed that such deductions were applicable to it in light of its operations and the law and the deductions were *accepted as an allowable deduction* as per the Respondent's letter. In arriving at this decision, the Respondent presumably reviewed the law and established that interest was an allowable deduction under Section 25 of the ITA. It was therefore within the confines of the law and within its power, as the above authorities hold, to determine that such interest was deductible and made this position known to the Appellant, which it relied on for 11 years until 2013. A legitimate expectation was therefore created.

Counsel prayed that the court finds that the learned members of the Tribunal erred in law when they found that the Respondent's letter dated 23rd August 2001 did not create a legitimate expectation for the Applicant that the interest paid to members' accounts was a deductible expense.

Resolution by the Court

The meaning and parameters of the doctrine of legitimate expectation has been laid down in a number of decided cases. In ***DMW (U) Ltd v Attorney General & Another (supra)***, it was held by the Court that;

> ***Legitimate expectations may be based on some statement or undertaking by or on behalf of public authority which has the***

duty of making the decision if the authority has through its officers acted in a way that would make it a part or inconsistent with good administration for a person to be denied an inquiry.

In ***Associate Professor Charles Niwagaba Vs. Makerere University (supra)*** relying on the English case of ***Council of Civil Service Union vs. Minister for Civil Service (supra)***, it was held that;

> ***Legitimate expectation derives from the need to secure certainty and predictability in administrative or quasi administrative decisions or actions. It seeks to enforce promise or representation given by or on behalf of an authority to an individual to the end that lawful bargains are not thwarted.***

In ***Republic Vs. Kenya Revenue Authority Exparte Shake Distributors Limited (supra)***, the court stated:

> ***It follows therefore that the cornerstone of legitimate expectation is a promise made to a party by a public body that it will act or not act in a certain manner. For the promise to hold, the same must be made within the confines of law. A public body cannot make a promise which goes against the express letter of the law. In the case before me there is no evidence of a written or verbal promise made to the Applicant that its goods would be allowed in Kenya once he obtained the necessary licenses. One may argue that the legitimate expectation was based on the understanding that goods from Uganda would be admitted into Kenya at a duty rate of 0%. However, that argument cannot hold when one considers the fact that the Respondent has a statutory duty to ensure that all the necessary taxes for goods entering Kenya have been paid. The Applicant's argument that its legitimate expectation was breached therefore fails.***

In ***Justice Kalpana Rawal Vs Judicial Service Commission & 3 Others (supra)***, the court held:

> ***Legitimate expectation is a doctrine well recognized and established in administrative law. In Commonwealth Commission of Kenya & 5 others, SC Petition Nos. 14,14A,14B & 14C of 2014, the supreme Court stated that legitimate expectation would arise when a body, by representation or by past practice has around an expectation that is <u>within its power to fulfill</u>. For an expectation to be legitimate, therefore, it must be founded upon a promise or practice by a public authority that is expected <u>to fulfil the expectation</u>. Other important aspects of the doctrine are:***
>
> ***(a) <u>The Law does not protect every expectation save only for the those which are legitimate</u> (South African Veterinary Council v. Szymanski 2003 ZASCA 11);***
>
> ***(b) <u>Clear statutory words override any contrary expectations however founded</u> (R.v.DPP ex parte Kebilele Wainanina Kigathi Mungai, HC J.R Misc. 356 of 2013;***
>
> ***(c) The representation must be one which the decision-<u>maker can competently and lawfully make without which reliance cannot be legitimate</u> (Hauptleisch v. Caledon Divisional Council (1963) (4) SA53);***
>
> ***(d) Legitimate expectation does not arise when it is made ultra the decision- maker's powers (Rowland v. Environment Agency (2003) EWCA Civ. 1885); and***
>
> ***(e) A public authority which has made a representation <u>which it has no power to make is not precluded from asserting the correct position which is within its power to make</u> (Republic v. Kenya Revenue Authority ex-parte Aberdare Freight Services Ltd (2004) KLR 530).***

The Tribunal held in its Ruling that much as the said letter created an expectation that interest paid by the Appellant was deductible, the

Respondent would not in the exercise of its statutory duty of collecting taxes be fettered by the said letter. The Tribunal held the view that in order for the Applicant to rely on the doctrine of legitimate expectation, the expectation had to be legal. That in the instant case, since the Tribunal had already held that the interest paid by the Applicant could not be considered an allowable deduction, the said letter of 23rd August 2001 was not helpful and could not be relied on by the Applicant. The Respondent strongly supported this finding of the Tribunal.

As seen from the facts before the Court and legal authorities, there is no dispute that the letter of 23rd August 2001 from the Respondent to the Applicant created an expectation on the part of the Appellant. The only dispute is whether the expectation was lawful and within the confines of the Respondent's statutory authority to make. The Respondent argues that the expectation was illegal and ultra vires the powers of the Respondent; which argument the Tribunal agreed with.

To establish the veracity of that argument, I need to examine the mandate and powers of the Respondent. The Respondent is created by the Uganda Revenue Authority Act, Cap 196 of the Laws of Uganda (**URA Act)**. The long title to the Act is: **"An Act to establish the Uganda Revenue Authority as a central body for the assessment and collection of specified revenue, to administer and enforce the laws relating to such revenue and to provide for related matters".**

Under *Section 3 (1) (a) of the URA Act*, one of the functions of the authority is to *"administer and give effect to the laws or the specified provisions of the laws set out in the first Schedule to this Act, and for this purpose to assess, collect and account for all revenues to which those laws apply".*

From the above provisions, the authority is the central body for the assessment and collection of specified revenue, to administer and enforce the laws relating to such revenue. Income Tax is one such revenue and the

ITA is one of the laws that the Authority is mandated to administer and enforce. The authority holds the function of administering and giving effect to the relevant laws and to assess, collect and account for all revenues to which the said laws apply.

In my considered view, in the course of execution of the said mandate and specific function, the Authority has the power and mandate to interpret the relevant laws. A particular interpretation assigned by the Authority to a particular provision of the law is a lawful construction of such a provision unless and until otherwise changed by them or by a higher authority. The Authority has the power and mandate to enforce and adhere to such an interpretation of the law in a bid to give effect to a relevant provision of the law. Such an interpretation does not have to be infallible. It may be a wrong construction of the law but as long as it is made through the right channels and in a proper exercise of jurisdiction, it is lawful and binding upon not only the people who receive and rely on it but also on the Authority itself.

It is therefore not a correct position of the law that if the Authority later on discovers that it was wrong in a previous interpretation of the law, and as a result changes its position, that the earlier position is deemed illegal and unreliable. I find that an absurd interpretation of the law. The Authority has the right and power to change its position on a particular interpretation. But when it does so, their new position takes effect from the time it is made and does not render the earlier position illegal or unreliable.

On the facts before me, the Respondent made the position and communicated it to the Appellant by letter dated 23rd August 2001. The letter indicates in its body that the Respondent had reached the position that the interest paid by the Appellant to its members was to be treated as an allowable deduction; and that they had reached such a position after reviewing a number of correspondences between the Appellant and the Respondent. The Respondent left this position unchanged until the year 2013. In my view, the change of position by letter dated 20th November, 2013 does not negate or render void the earlier position. The changed position cannot take effect retrospectively. It does so from the date it is made.

It is therefore not correct as argued by the Respondent and upheld by the Tribunal that because the Authority found that it was wrong in its earlier interpretation of the law, the earlier position was illegal and could not be relied upon. I am unable to agree with that reasoning and conclusion.

It was argued by the Respondent that relying on the letter of 23rd August 2001 would tantamount to the Respondent imposing a tax contrary to the provisions of the law and exercising a power it does not have. This argument is not valid. As shown above, the Respondent has power to administer and enforce tax laws and in doing so, to interpret specific provisions of the laws. The positions reached by the Respondent in 2001 and 2013 respectively was not a function of imposing a tax or taxes, it was a function of interpreting the ITA in order to give effect to its provisions; which is within the Respondent's power and mandate.

It is also clear that the reason the Respondent changed its position in 2013 was not because it was found to be illegal but because they came to a different conclusion upon construction of the same law. As such from the year 2001 to 2013, tax on the interest in issue could not be assessed in any other way other than in compliance with the position of the Authority.

It is therefore my conclusion that a legitimate expectation was created in favour of the Appellant upon which the Appellant was entitled to rely during the period of the assessment herein in issue. The legal authorities relied on by the Respondent present a correct position of the law but do not support the position of the Respondent. The Tribunal was therefore in error when it found that the legitimate expectation thereby created was illegal and could not be relied upon by the Appellant.

As such even if I had not reached the conclusion that the interest in issue was an allowable deduction, I would have come to the conclusion that the interest would not have been subject to tax for the period 2005 to 2013 when the position changed. The Appellant would have had no liability to pay the tax on the basis of the doctrine of legitimate expectation.

The further argument by the Appellant that the said letter amounted to a private ruling by the Commissioner is not supported by the provisions of Section 161 of the ITA and Section 45 of the Tax Procedure Code Act and I have found no need to belabor this point. The 4th ground of appeal also succeeds to the extent stated above.

Ground 5: The learned members of the Tribunal erred in law in finding that the Appellant was liable for penal tax.

Appellant's Submissions

Counsel for the Appellant relied on the provisions of Section 136 of the ITA and the decision in ***Kasampa Kalifani V URA HCCS No.579 of 2007*** to submit that a person was liable to pay a penal tax at the rate specified in the law if he/she fails to pay tax imposed under the statute on or before the due date. Counsel submitted that penal tax is payable when a tax payer fails to pay tax that is due. It must therefore be shown that the tax payer failed to pay a due tax. The Respondent did not adduce any evidence to prove any of the conditions set out in Section 136 of the ITA.

Counsel for the Appellant supported the dissenting decision of one of the members of the Tribunal who found that the Appellant was not liable to pay penal tax. Counsel faulted the majority members of the Tribunal for concluding that the Appellant was liable to pay penal tax for a period when the tax was never due.

Respondent's Submissions

For the Respondent, it was submitted that penal tax is a creature of statute and so is any tax imposed. A tax payer cannot escape tax by categorizing it different from tax; penal tax is tax and therefore cannot be severed from the principle amount of tax due. It is therefore our humble submission that the Tribunal rightly held that the Appellant was liable to penal tax.

Counsel submitted that under ***Article 17 of the Constitution of Uganda 1995 as amended***, *every citizen has a duty to pay taxes and to do so promptly.* Non-payment or delayed payment of taxes stalls and delays government business and further hampers service delivery. As such, the legislature in its wisdom found it worthy and proper that delayed payment of taxes should be penalized.

Counsel further submitted that even if the Respondent was inclined to waive the penalty, the law does NOT grant the Respondent power to waive penalty. On the contrary, the Respondent is mandated to abide by the law and implement the imposition of penalty and interest in accordance with the law. Counsel therefore concluded that the Honorable Tribunal Members rightly held that the Appellant was liable to penal tax. Counsel prayed that this ground should be answered in the negative.

In **rejoinder**, the Appellant reiterated their first above submissions.

Resolution by the Court

I agree with the position of the law cited by the Appellant that in order for a person to be subjected to payment of penal tax, the tax must be due and payable and the person fails to pay the same in time or at all. Section 136 of the ITA and the decision in ***Kasampa Kalifani V URA (supra)*** refers. For the person to be found to have failed to pay the tax in issue, it has to be shown that the person was aware or ought to have been aware of the tax obligation and they either willfully or negligently failed to make the payment. Where the tax is not due or there is no evidence that the tax payer knew or ought to have known that such tax obligation exists; or actually knew or believed that no such tax obligation exists, such a person cannot be subjected to penal tax if it is later found or decided that they are after all liable to pay a particular tax. Penal tax is to penalize default; and default is expected to be by willful or negligent conduct. In my view, the use of the word "fail" in Section 136 of the ITA connotes conduct on the part of the tax payer. It does not envisage penalty where either the tax was not due or the tax payer was not aware of the existence of the tax obligation or where they reasonably believed no such tax obligation actually existed.

In the present case, the Appellant showed that they reasonably believed no such tax obligation existed. They based their belief on a position communicated to them by letter dated 23rd August 2001. It cannot be said they failed to pay the tax. They reasonably believed no such tax obligation existed. Further, as found herein above, no tax was actually due and payable as against the Appellant.

In this regard, I am in agreement with the dissenting opinion of the member of the Tribunal that the Appellant was not liable to pay penal tax. The majority members of the tribunal therefore erred when they found that the Appellant was subject to payment of penal tax in the circumstances of the present case. The fifth ground of appeal also succeeds.

Ground 6: The learned members of the Tribunal erred in law when they failed to properly evaluate the evidence on record and thereby came to an erroneous decision.

In light of my finding herein above on the role of this Court in appeals arising out of decisions of the Tax Appeals Tribunal, this ground becomes inconsequential and unsustainable. A question as to "whether the Tribunal failed to properly evaluate evidence on record" is a question of fact. A question as to "whether the Tribunal had a duty to evaluate evidence" would be a question of law. But the latter is not the question. The former was the question that was raised by the Appellant. As found out above, an appeal such as this one must be based on questions of law only. This ground of appeal is therefore accordingly rejected and struck out.

Decision of the Court

In all therefore, the appeal has succeeded on grounds one to five. In substance therefore, the appeal wholly succeeds. I accordingly set aside the Ruling and Orders of the Tax Appeals Tribunal and substitute them with the decision that:

1. The interest paid by the Appellant to its members is declared a deductible expense for income tax purposes.
2. The Appellant is not liable to pay the principal tax assessed of UGX 30,521,703,065/=.
3. The Appellant is not liable to pay the penal tax or interest of UGX 12,196,879,941/=.
4. The Respondent pays costs of the proceedings in this Court and in the Tax Appeals Tribunal.

It is so ordered.

Signed, dated and delivered by email this 2nd day of November, 2020.

Boniface Wamala
JUDGE