THE REPUBLIC OF UGANDA

IN THE HIGH COURT OF UGANDA AT KAMPALA

[COMMERCIAL DIVISION]

ARISING FROM CIVIL APPEAL NO. 43 OF 2022

[ARISING FROM TAT APPLICATION NO. 39 OF 2021]

LUWALUWA INVESTMENT LIMITED] APPELLANT

VERSUS

UGANDA REVENUE AUTHORITY] RESPONDENT

Before: Hon. Justice Ocaya Thomas O.R

JUDGMENT

Background:

The background to this Appeal is quite interesting.

Simbamanyo Estates limited ("**Simbamanyo**") borrowed over Ten Million Dollars from Equity Bank Uganda Limited, a financial institution duly licensed and regulated by the Bank of Uganda. As part of the various securities pledged to secure the said loan, including but not limited to personal guarantees from the Directors of Simbamanyo, Debentures, Share pledges etc., Peter Kamya – a Director of Simbamanyo and the registered proprietor of five properties comprised in Kyadondo Block 243 Plots 1799 & 1800, 2794, 957 and 958, and Kyadondo Block 237 plot 95 all located at Mutungo, Luzira (otherwise known as "Afrique Suites") mortgaged the said properties to Equity Bank (the "Mortgagee") and pledged the said properties as further security for the mortgage.

Simbamanyo defaulted on its loan obligations which forced Equity Bank to foreclose on the mortgage and advertise Afrique Suites for sale by way of public auction to recover the outstanding loan amounts in accordance with the provisions of **the Mortgage Act 2009.**

In October 2020, after a public auction organised by CL Risk Management Services under the provisions of the Mortgage Act (and not under an order of the High Court of Uganda) on behalf of Equity Bank in its capacity as the Mortgagee, the Applicant acquired all the five properties comprising Afrique Suites from the Bank.

Equity Bank subsequently accounted for all income tax attributable to the sale of Afrique Suites and all its other banking activities for the year 2020 and filed its financial statements which were published to the public in accordance with the financial institutions law in Uganda. A copy of these financial statements may be accessed on Equity Bank's website.

On the 10th day of March, 2021, the Respondent wrote a letter to the Appellant vide URA/DT/1009796953 informing the Appellant that a review of its transactions was being conducted and requested the Appellant to furnish the Respondent with documents pertaining to the Appellant's purchase of seven properties worth **UGX 21,404,800,000 (Uganda Shillings Twenty-One Billion Four Hundred Four Million Eight Hundred Thousand)** from Equity Bank Ltd and two other clients.

On the 15th March, the Appellant responded to URA's letter sharing the required documents and explained further that **section 118B (2)** under which URA proposed to proceed did not apply to the Appellant particularly with respect to Afrique Suites which had been acquired from Equity Bank at a public auction. The letter also informed URA that the withholding tax in respect of the other two properties had been duly paid by the Appellant.

On 8th April 2021, URA issued an administrative assessment to the Appellant for withholding tax to the tune of **UGX 965,700,000 (Uganda Shillings Nine Hundred Sixty-Five Million, Seven Hundred Thousand only)** in disregard of the Appellant's letter of 15th March 2021 and the evidence of payment of WHT in respect of the other two properties which URA vide email dated 7th April 2021 had acknowledged receipt of.

On the same date, the Appellant wrote a letter responding to URA's email of 7th April 2020 explaining in detail why the 6% WHT did not apply to their acquisition of Afrique Suites. On the 12th day of April, 2021, the Appellant formally objected to the assessment. In addition, the Appellant wrote a letter to the Respondent explaining the grounds of the objection. Consequently, on the 11th day of May, 2021, the Respondent made its objection decision wherein it upheld the assessment.

On 14th May 2021, the Appellant filed an application for review of the Respondent's objection decision and subsequently paid 30% of the tax in dispute.

The Appellant being dissatisfied with the objection decisions and the Respondent's assessments in respect to WHT, made the Application for review of the same in the Tax Appeals Tribunal (TAT) on the following grounds;

(a) The Appellant had no obligation to withhold tax at 6% when it acquired Afrique Suites;

(b) **Section 118B (2)** of the **ITA** does not apply to foreclosure of mortgaged property by a Bank. In arriving at the assessment, URA treated the sale of Afrique Suites by Equity Bank as a sale of a business asset. The Bank did not sell a business asset owned by it. The properties which the Bank foreclosed do not qualify as business assets, the properties were merely sold to recover the principal and interest outstanding to the Bank;

(c) The sale by the Bank therefore took the form and character of the loan obligations which the Bank was trying to recover i.e., principal and interest;

(d) There is no withholding tax payable by a borrower when repaying the principal sum borrowed from a financial institution as this does not qualify as income received by a financial institution but a mere refund of the sums advanced by the Financial Institution;

(e) Under section **117 (2) (b)** of the **ITA**, interest income paid to financial institutions is exempt from withholding tax;

(f) Therefore, there was no obligation on the Applicant to withhold tax on the foreclosure of Afrique Suites by Equity Bank Limited.

On 23rd September 2022, the Tax Appeals Tribunal (TAT) by majority decision decided in favour of the Respondent and ordered that the assessment of **UGX 965,700,000 (Uganda Shillings Nine Hundred Sixty-Five Million, Seven Hundred Thousand only)** be upheld and that;

(a) The provisions of section 118B (2) of the Income Tax Act are clear and there is no reason why the literal and ordinary meanings should not apply to it.

(b) Section 118B (2) does not conflict with section 117(2) of the Income Tax Act.

(c) The Applicant is not exempted under section 119 (5) of the Income Tax Act.

(d) The Application is dismissed with costs.

The Appellant being dissatisfied with the decision of the Tribunal (TAT) lodged an Appeal in this Court on the following grounds;

(a) That the learned members of the Tribunal (TAT) erred in law when they held that Afrique Suites was a business asset within the meaning of

section 118B (2) of the Income Tax Act, in complete disregard of the mode of acquisition of the property through public auction and the character of the seller, Equity Bank, which sold as mortgagee under the auspices of the Mortgage Act;

(b) That the learned members of the Tribunal erred in law when they held that Section 118B (2) of the Income Tax Act was not ambiguous;

(c) That the learned members of the Tribunal erred in law when they held that Section 118 (B)(2) of the Income Tax Act did not conflict with Section 117 (2) (b) of the Income Tax Act;

(d) That the learned members of the Tribunal erred in law when they held that section 117 (2) (b) deals with exemption of withholding tax on interest which is business income whereas section 119 B (2) deals with withholding tax on purchase of a property which is property income.

(e) That the learned members of the Tribunal erred in law when they held that purchase price is not interest in complete disregard of section 18 (2) of the Income Tax Act which states that interest retains its character for the purpose of any section of the Income Tax Act referring to such income.

Representation and Submissions

The Appellant was represented by M/s Katende, Ssempebwa & Co. Advocates while the Respondent was represented by its Legal Services and Board Affairs Department.

Both Counsel made written submissions along with authorities in support of their respective cases in this appeal as directed by court which I have had the benefit of reading and for which I am grateful.

Grounds of Appeal

As noted above, the Appellant raised four grounds of appeal which are as below:

(a) That the learned members of the Tribunal erred in law when they held that Afrique Suites was a business asset within the meaning of section 118B (2) of the Income Tax Act, in complete disregard of the mode of acquisition of the property through public auction and the character of the seller, Equity Bank, which sold as mortgagee under the auspices of the Mortgage Act.

(b) That the learned members of the Tribunal erred in law when they held that Section 118B (2) of the Income Tax Act was not ambiguous

(c) That the learned members of the Tribunal erred in law when they held that Section 118 (B)(2) of the Income Tax Act did not conflict with Section 117 (2) (b) of the Income Tax Act

(d) That the learned members of the Tribunal erred in law when they held that section 117 (2) (b) deals with exemption of withholding tax on interest which is business income whereas section 119 B (2) deals with withholding tax on purchase of a property which is property income.

(e) That the learned members of the Tribunal erred in law when they held that purchase price is not interest in complete disregard of section 18 (2) of the Income Tax Act which states that interest retains its character for the purpose of any section of the Income Tax Act referring to such income.

Role of First Appellate Court

It is the duty of this court as a first appellate court to re-hear the case by subjecting the evidence presented to the trial court to a fresh and exhaustive scrutiny and re-appraisal before coming to its own conclusion (see **Father Nanensio Begumisa and three Others v. Eric Tiberaga SCCA 17of 2000\ [2004] KALR 236**).

In a case of conflicting evidence, the appeal court has to make due allowance for the fact that it has neither seen nor heard the witnesses, it must weigh the conflicting evidence and draw its own inference and conclusions (see **Tonny Kilama & Anor v Mrs. Grace Perepetua Otim HCCA 31/2019**).

In exercise of its appellate jurisdiction, this court may interfere with a finding of fact if the trial court is shown to have overlooked any material feature in the evidence of a witness or if the balance of probabilities as to the credibility of the witness is inclined against the opinion of the trial court. In particular, this court is not bound necessarily to follow the trial courts's findings of fact if it appears either that he or she has clearly failed on some point to take account of particular circumstances or probabilities materially to estimate the evidence or if the impression based on demeanor of a witness is inconsistent with the evidence in the case generally. It is not every slip of a lower court that will result in an appeal being allowed: it is only those mistakes that have been shown to have affected or influenced the decision appealed against that will result in the appeal being allowed.

Right of Appeal

The court observes that the right of appeal is a creature of statute and must be given expressly by statute (see **Hamam Singh Bhogal T/a Hamam Singh & Co. v. Jadva Karsan (1953) 20 EACA 17\ Baku Raphael v. Attorney General S. C Civil Appeal No. 1 of 2005 and Attorney General v. Shah (No. 4) [1971] EA 50**).

This Court has jurisdiction to hear and determine appeals from the decisions of the Tax Appeals Tribunal in accordance with the provisions of **Section 27** of the Tax Appeals Tribunal Act. Accordingly, this appeal is competently before this court. See Also **Roche Transport v URA HCCA 20/2021**

The Respondent raised preliminary points of law. Accordingly, I find it necessary to resolve those preliminary points before proceeding to the merits of the Appeal, if at all.

PART I: DETERMINATION OF PRELIMINARY POINTS OF LAW

In its submissions, the Respondent raised two preliminary points of law;

(a) Ground 1 of the grounds of appeal relates to matters of mixed law and fact contrary to Section 27(2) of the Tax Appeals Tribunal Act.

(b) Grounds 1 and 5 of the appellant's grounds of appeal are argumentative and offend the provisions of Order 43 Rules 1 and 2.

I will determine the preliminary objections in the order presented above.

Ground 1 Offends Section 27(2)

Section 27(2) of the Tax Appeals Tribunal Act ["TATA"] provides thus:

"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."

In **Uganda Revenue Authority v Tembo Steels Ltd, HCCA 09/2006** 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."
See also **National Social Security Fund v Uganda Revenue Authority HCCA 29/2020**

Ground One of the Appellant's appeal reads thus;
"That the learned members of the Tribunal erred in law when they held that Afrique Suites was a business asset within the meaning of section 118B (2) of the Income Tax Act, in complete disregard of the mode of acquisition of the property through public auction and the character of the seller, Equity Bank, which sold as mortgagee under the auspices of the Mortgage Act."

A question of law is about what the correct legal test (or legal interpretation) is while a question of fact is concerned with what actually took place. See **Elias Kasolo v Security Group Uganda Limited & Anor CACA 212/2020**
My reading of ground one is that the applicant is challenging both the interpretation of Section 118(B)(2) by the Tax Appeals Tribunal as well as its application to the facts of the present case. Accordingly, it would follow that applicant framed a ground of mixed law and fact.

What is the effect of this? In **NSSF v URA (Supra)**, the court held thus
"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."

It follows that a ground of mixed law and fact is not maintainable in appeals to this court from the tax appeals tribunal and such a ground, where framed in the memorandum of appeal, must be struck out. Accordingly, I uphold this preliminary objection by Counsel for the Respondent. However, in the view of completeness, I will render a decision on this ground, just in case my finding on this preliminary objection is overruled on appeal.

Grounds 1 and 5 are argumentative

Order 43 Rule 1(2) provides thus:

"The memorandum shall set forth, concisely and under distinct heads, the grounds of objection to the decree appealed from without any argument or narrative; and the grounds shall be numbered consecutively."

A ground of Appeal should clearly demonstrate the error in the judgment of court but should not be worded as to narrate or contain subjective assertions but a concise objective critique of the judgment of court.

Ground One reads thus:

That the learned members of the Tribunal erred in law when they held that Afrique Suites was a business asset within the meaning of section 118B (2) of the Income Tax Act, in complete disregard of the mode of acquisition of the property through public auction and the character of the seller, Equity Bank, which sold as mortgagee under the auspices of the Mortgage Act.

Ground Five reads thus:

That the learned members of the Tribunal erred in law when they held that purchase price is not interest in complete disregard of section 18 (2) of the Income Tax Act which states that interest retains its character for the purpose of any section of the Income Tax Act referring to such income.

In Ground 1, the Appellant asserts that the Tax Appeals Tribunal arrived at a wrong decision to wit where Afrique Suites was a business asset because the Tribunal disregarded the mode of acquisition of the property and the character of the seller.

In my view, this is not argumentative but instead a precise statement of what the Appellant views to be an error in the judgment of court.

Turning to Ground 5, the Appellant charges that the decision of the Tax Appeals Tribunal in holding that the purchase price of mortgaged property is not interest was in disregard of Section 18(5) of the Income Tax Act. Again, this is not argumentative but instead a precise statement of what the Appellant views to be an error in the judgment of court.

Accordingly, I find the Respondent's contentions on this head to be without merit.

PART II: DETERMINATION OF APPEAL

Both Counsel made submissions in respect of each of the grounds of appeal. It is trite law that submissions are not evidence and accordingly do not need to be reiterated in a judgment. However, owing to the fact that the present dispute raises important points of law of public importance, I will attempt to reproduce the submissions of Counsel in some detail on each of the grounds of appeal.

Ground One: That the learned members of the Tribunal erred in law when they held that Afrique Suites was a business asset within the meaning of section 118B (2) of the Income Tax Act, in complete disregard of the mode of acquisition of the property through public auction and the character of the seller, Equity Bank, which sold as mortgagee under the auspices of the Mortgage Act.

Appellant's Submissions

Counsel for the Appellant submitted that the finding by the Tax Appeals Tribunal ["Tribunal"] that Afrique Suites was owned and had value and was therefore an asset finding was erroneous to the extent that it was not an asset of Equity Bank who was the seller as Equity Bank did not "own" the property. According to Black's Law dictionary's definition of an asset, "ownership" is one of the two primary requirements for an item to qualify as an asset and in this case, Equity bank just did not own the property.

Counsel submitted that Afrique suites was not owned by Equity Bank and the Bank did not represent the property as its asset in its balance sheet as shown by the evidence of the Head of Credit for Equity Bank, Mr. Jimmy Mwangangi at paragraph 16 Applicant witness statement of Jimmy Mwangangi on Page 55 of the ROA where he stated that

"Afrique Suites was never owned by Equity Bank Uganda Limited nor were the properties comprised of Afrique suites ever registered in the names of Equity Bank Uganda Limited"

Counsel referred to The Mortgage Act 2009 as restricting the rights of a mortgagee over a security and incorporating the well settled principle of law that "once a mortgage, always a mortgage". Counsel cited Section 8 (1) of the Mortgage Act that states that;

"…a mortgage shall have effect as a security only and shall not operate as a transfer of any interest or right in the land from the mortgagor to the mortgagee…."

Counsel cited the Court of Appeal case of KIYAGA V SEGUJJA AND ANOTHER CIVIL APPEAL NO. 37 OF 2010, where it was held that

"from the principles espoused, if money is lent on the security of land, the lender will get security and nothing more. It is trite law that once a mortgage always a mortgage"

Therefore, Counsel contended, by virtue of the Mortgage Deed executed with the borrower and marked as Exhibit AE21 in the Joint Trial Bundle (page 166 ROA), Equity Bank only acquired security rights conferred under the Mortgage Act to a mortgagee in Afrique Suites and did not at any one point acquire any rights of ownership over the said Property

Further, Counsel argued that under Section 38 of the Financial Institutions Act 2004 ("FIA"), banks in Uganda are not allowed to own immovable property. Section 38 (1) FIA of the Act provides that;

"A financial institution shall not purchase or acquire any immovable property or any right in it except as may be reasonably necessary for the purpose of conducting its business or of housing or providing amenities for its staff, in which case the cost of the property, in aggregate, shall not exceed one hundred percent of the financial institution's core capital."

Accordingly, it was Counsel's view that Equity bank therefore could not legally own or use Afrique Suites in its business given the above restriction on the ownership of immovable property by financial institutions under the Financial Institutions Act.

Counsel charged that Equity Bank did not purchase or acquire the property in issue for purposes of conducting its business since Equity only had a mortgage on the property and a mortgage as already defined above does not operate as a transfer of interest in a property or a grant any rights of ownership to property. Therefore, a property mortgaged to a bank, is not property sold to a bank and does not become an asset of the bank in any shape or form. Afrique Suites was not an asset of Equity Bank, the seller of the property to the Applicant, and therefore it cannot be a business asset of the seller. Once it is not a business asset, Section 118 B (2) does not apply to this transaction.

Counsel submitted that the tribunal wrongly relied on the definition of an Asset from Black's Law Dictionary, 10th Edition in disregard to Section 8 of the Mortgage Act which defines a mortgage as a security only.

Counsel referenced the second definition of an asset Black's Law Dictionary, 10th Edition which reads as below:

"the entries on a balance sheet showing the items of property owned, including cash, inventory, equipment, real estate, accounts receivable, and goodwill"

Counsel submitted that Equity Bank did not represent the property as its asset in its balance sheet as shown by the evidence of the Head of Credit for Equity Bank, Mr. Jimmy Mwangangi at paragraph 16 of the Applicant witness statement of Jimmy Mwangangi on Page 55 of the ROA.

Counsel referenced under Section 2 of the Mortgage Act 2009 a Mortgage is defined as:-

"mortgage" includes any charge or lien over land or any estate or interest in land in Uganda for securing the payment of an existing or future or a contingent debt or other money or money's worth or the performance of an obligation and includes a second or subsequent mortgage, a third party mortgage and a sub mortgage;

Counsel relied on the above section to submit that a mortgage is not an account receivable or a loan or a debt owed to the bank but simply a charge over land for securing the payment of a contingent debt. Therefore, a mortgage is not an asset that can be listed in the books of accounts of the Mortgagee (Equity Bank) as an asset. According to Counsel, no financial institution when preparing its books of accounts lists the securities it holds for the loans it issues out – whether mortgages, personal guarantees, charges on fixed deposit accounts, share pledges, debentures etc.-as assets of the bank; the fact that a mortgage is never listed as one of the assets of Equity Bank in its books of accounts clearly shows that the mortgage of Afrique Suites is not an asset – business or otherwise- of Equity Bank, the Seller.

The mortgage was simply a charge or lien for the debt owed to Equity Bank by Simbamanyo.

Counsel then proceeded to reference the third definition of an asset according to Black's Law Dictionary, 10th Edition which reads thus:

"All the property of a person (esp. A bankrupt or deceased person) available for paying debts or for distribution"

Counsel cited Section 30 (1) of the Mortgage Act as detailing how the proceeds from the sale of mortgaged land should be utilized. The Section provides thus:

"The purchase money received by a mortgagee who has exercised his or her power of sale shall be applied in the following order of priority—

(a)in payment of any rates, rents, taxes, charges or other sums owing and required to be paid on the mortgaged land;

(b)in discharge of any prior mortgage or other encumbrance subject to which the sale was made;

(c)in payment of all costs and reasonable expenses properly incurred and incidental to the sale or any attempted sale;

(d)in discharge of the sum advanced under the mortgage or so much of it as remains outstanding, interest, costs and all other monies due under the mortgage, including any monies advanced to a receiver in respect of the mortgaged land under section 2;

(e)in payment of any subsequent mortgages in order of their priority; and

(f)the residue, if any, of the money 'received shall be paid to the person who, immediately before the sale, was entitled to discharge the mortgage."

Counsel cited the of the case of Hill v Smathers, 173 NC 642, 92 SE 607, 609; as authority for the proposition that the term assets as applied to banks was said to be broad enough to cover anything which is or may be: -

"available to pay creditors; but as usually understood, it refers to the tangible property of the corporation…"

Counsel submitted that, on the basis of the above authorities, the proceeds from the sale of the property were not available for paying the debts of Equity Bank or for distribution to its creditors or shareholders and therefore the said mortgages and the said properties could not be classified as assets of Equity bank. This is because the property was merely held by Equity Bank as a security to secure loan obligations of the borrower. Equity Bank did not have control over the property to the extent that the Bank could not sale the Property until the Borrower defaulted on its loan obligations and triggered the Bank's limited power of sale under the Mortgage Act 2009

Counsel submitted that Afrique Suites was not an asset of the bank because the property was not registered in the names of Equity Bank and was not available to Equity bank to pay its creditors and it was not the tangible property of the bank. The bank merely held the property as a security under the auspices of the Mortgage Act.

Counsel cited Section 2 (h) of the ITA which reads thus:
"an asset which is used or held ready for use in a business, and includes any asset held for sale in a business and any asset of a partnership or company."

Counsel submitted that Afrique Suites did not qualify as a "business asset" within the meaning of Section 2(h) of the ITA above at the time of Equity Bank's foreclosure and sale to the Appellant because the property does not meet any of the requirements prescribed under Section 2(h) of the ITA necessary to qualify a property as a business asset for purposes of income tax. Counsel contended that under Section 2(h) of the ITA, for a property to qualify as a business asset for purposes of withholding tax under Section 118B (2) of the ITA, it is important to prove the following;

(a) that the Property is an asset;
(b) that the asset is used in a business; or
(c) the asset is held ready for use in a business;

(d) includes an asset held ready for sale in a business;

(e) includes an asset that is owned by a partnership or company

Counsel submitted that Afrique Suites was not an asset of Equity Bank the seller (because of Counsel's submissions above) and neither was it an asset held ready for use by the Bank. Equity Bank could not use or hold ready for use Afrique Suites as an asset because the Bank did not own the property or have a right to own it and determine its final uses. It only held the property as security to secure the loan obligations of its borrower. Accordingly, the first two definitions (b) and (c) were not applicable.

As for definition (d), Counsel submitted Equity Bank Uganda Limited did not hold Afrique Suites as an asset ready for sale in its business. It only held it as a mortgage as a charge for the outstanding loan amounts owed to Equity Bank by Simbamanyo under the Mortgage Act. Counsel contended that If Equity bank was holding Afrique Suites, ready for sale this would mean that Equity Bank could at any time of its choosing, under any conditions sale the property and use the proceeds of the sale for any purpose it chooses.

Counsel stressed that Section 31 (f) of the Mortgage Act which states that any residue from the sale of the mortgaged property by a mortgagee may be paid to the person entitled to discharge the mortgage (borrower). He contended that this means that the Bank's interest over the property extends only up to repayment of principal and interest. Beyond this, the bank's interest in the property ceases and all excess money received at the sale is supposed to be paid to the borrower

Counsel charged that a mortgage is simply security for the repayment of a loan issued to the Applicant. Financial institutions utilize various securities to secure the loans they issue for instance, fixed deposit accounts, personal and corporate guarantees, contracts for proceeds from businesses, debentures, share pledges, mortgages etc; when a borrower defaults and the financial institution exercises its

recovery rights by recovering from a fixed deposit, a guarantee or any other contract the borrower does not withhold 6% of the value of the security recovered because as explained above, the bank is recovering its principal loan amount (which is not subject to any tax) plus interest (which interest is exempt from tax under Section 117 (2) b ITA).

According to Counsel, it follows therefore that when a bank sells property under a mortgage to recover outstanding loans, it is merely recovering its principal and interest and is exempt from any withholding tax. As stated herein, the bank, as a mortgagee, has a very limited interest in the property and can only use it to recover outstanding loans and not to sale it at will as it could any other asset that the bank owns.

Counsel criticised The Tribunal for disregarding the mode of acquisition of the property through public auction and the character of the seller, Equity Bank, which sold as mortgagee under the auspices of the Mortgage Act.

Counsel argued that Afrique Suites was not a business asset within the meaning of section 118B (2) of the Income Tax Act because of the unique manner in which the property was acquired by the Applicant. Afrique Suites was acquired by the Applicant at a public auction organized on behalf of Equity Bank by CL Risk Management services limited.

Counsel cited Section 26 of the Mortgage Act which provides for a Mortgagee's power of sale as follows

"(1) Where a mortgagor is in default of his or her obligations under a mortgage and remains in default at the expiry of the time provided for the rectification of that default in the notice served on him or her under section 19 (3), a mortgagee may exercise his or her power to sell the mortgaged land."

Counsel relied on the above section to submit that the sale of Afrique Suites was not an ordinary sale of property. It was the exercise of a limited power of sale by Equity Bank under the Mortgage Act to recover outstanding principal and interest from the Borrower as specified in Section 30 of the Mortgage Act

Counsel submitted that because the purpose of the sale by Equity Bank was to recover principal and interest, the character of Afrique Suites changed from its original state and could only be looked at as recovery of principal and interest for income tax purposes.

He cited Section 18 (2) of the Income Tax Act which provides that any amount included in business income retains its character as interest and charged that the error in the decision at first instance is partly a function of the fact that The Tribunal did not consider this provision of the law when making its decision.

Counsel submitted that Section 18(2) ITA above is to qualify the sale of a mortgaged property as recovery of interest. This is because according to the section, interest retains its character as interest income regardless of any other reference used under the Act. Therefore, Section 18(2) ITA would trump Section 118 B (2) ITA which seeks to qualify interest income as a business asset.

Counsel proceeded to submit that further proof of the sale retaining its character as interest is evident from the fact that there is a restriction on the use of the proceeds of a sale of mortgaged property under the law.

Respondent's Submissions

Counsel for the Respondent referenced Section 118(2)(b) which provides thus:

"A resident person who purchases a business or business asset shall withhold tax at a rate specified in Part VIII of the Third Schedule."

Counsel submitted that from the above provision, for one to be held liable to withhold tax under S. 118B (2), the following have to be considered;

1. The person purchasing is a resident person
2. There is a purchase
3. The purchase is for a business or a business asset.
4. The Purchaser must withhold tax.

Counsel submitted that it was not in dispute that the Appellant was a resident person within the meaning of Section 2(hh) and 10 of the Income Tax Act ["ITA"].

Counsel submitted that the second thing to consider is whether there was a purchase. Counsel submitted that Simbamanyo Estates Limited (Principal debtor/Mortgagor) and Peter Kamya (Mortgagor) took out a mortgage with Equity Bank Uganda Limited (Mortgagee) and pledged five properties registered in the mortgagor's names as security for the mortgage. The Mortgagors were the registered proprietors of Afrique Suites which is seated on the five plots of land. Equity Bank Uganda Limited subsequently registered the mortgage on all the five properties comprising Afrique Suites. The mortgagor defaulted on its loan obligations upon which, Equity Bank exercised its right of foreclosure on the mortgage to recover the outstanding loan amount.

Counsel referred to Witness Statement of AW1, Luwangula Ronald, paragraphs 3 - 6 on page 50-52 of the Record of Appeal and submitted that on 8th October 2020, the Appellant submitted its bid for the purchase of Afrique suites., the Appellant received a response to her bid to purchase the properties i,e, Afrique Suites and the five plots of land in which Equity Bank accepted the Appellant's bid to purchase the property. Resultantly, Counsel submitted, a sale Agreement for the purchase of the property was to be prepared by the Bank upon confirmation of payment. Counsel relied on Exhibit AE6, Page 129 of the Record of Appeal. Counsel submitted that subsequently, on 8th October 2020, the Appellant purchased

Afrique Suites (seated on five plots of land) from Equity Bank and paid UGX. **16,095,000,000. (Uganda Shillings Sixteen Billion, Ninety Five Million only)**

Counsel therefore contended that there was a sale within Section 118(B)(2) of the Income Tax Act.

Counsel submitted that having established that there was a purchase by a resident person, one needs to determine whether the property in question was a business or a business asset. Counsel relied on Section 2(h) of the Income Tax Act which states as follows;

"business asset" means an asset which is used or held ready for use in a business, and includes any asset held for sale in a business and any asset of a partnership or company;"

Counsel submitted that when construing the term business asset, it must be established that either;

a) That the property in question was an asset which was being used in a business, or
b) That the land in question was an asset held ready for use in a business, or
c) That the property in question was an asset held for sale in a business, or
d) That the property in question was an asset of a partnership or a company.

Counsel submitted that the use of the word "or" means that the property in question should fall in either or any of the above requirements but need not to satisfy all the requirements for it to qualify as a business asset.

As regards item (a) above, Counsel contended that the suit property was an asset. She contended that the ITA defines the term Business Asset but does not define the term 'asset.' Counsel cited the Crane Bank v URA (Hct-Oo-Cc-Ca-18) [Ugcommc 42] as authority for the proposition that where the Act does not define a word or

term, then the word or term must be given its ordinary literal meaning. The courts may have recourse to dictionaries, though with care.

Counsel relied on Black's Law Dictionary which defines an asset is defined as; an item that is owned and has value. She submitted that this definition has been cited with approval in the High Court case of Vivo Energy Uganda Limited Vs. URA Civil Appeal No. 1 Of 2019 and Shri Satvinder Singh Kalra Vs Commissioner of Wealth-Tax (2007 109 Itd 241 Pune).

Accordingly, the Respondent submitted that Afrique Suites was an asset. She contended that is regardless to who actually owned or controlled the interests of the said property as Section 118B(2) does not address itself to ownership. The dictionary meaning provided by Black's Law Dictionary sets out two requirements for an item to qualify as an asset namely that an item must be owned and have value.

Counsel argued that it is pertinent to note that the definition doesn't restrict the term 'asset' to any particular owner but rather gives a wide interpretation on ownership. According to Counsel, the term "ownership" synchronizes with the "to own" which is defined in Black's Law Dictionary at page 1200 as:

"The bundle of rights allowing one to use, manage and enjoy property, including the right to convey it to others, Ownership implies the right to possess a thing, regardless of any actual or constructive control."

Counsel then referred to the record and submitted that the suit property belonged to Peter Kamya; the Certificates in Title to the said properties being on record. To this end, Counsel submitted that the suit property had value and was eventually used as security for obtaining a loan; if the property had no value, it would not have been used as security for the mortgage.

Counsel argued that the second element classifying an item as an asset is that it must have value.

Counsel argued that legislature did not wish to restrict the withholding of taxes to only where the business asset belonged to the seller and that the legislature wanted to cover all purchases of business asset. Accordingly, she submitted that the decision of the tribunal was proper.

Counsel argued that the fact that the property was owned and had value means that the suit property was an asset regardless of who owned it at the time of the purchase. Having argued that the property was an asset, counsel turned to consider whether the property was an asset within the definition of Section 2(h) of the Income Tax Act. According to Counsel, for an asset to be determined as a business asset, it has to be used in a business or be held ready for use in a business.

Counsel contended that the suit property was used as a hotel as confirmed by Appellant's witness, Mr. Jimmy Mwangangi. Additionally, pictures of the property are attached to the witness statement of the Mr. Jimmy at Page 127 of the Record of Appeal. Counsel submitted that The property is described as "Simbamanyo House" situated on the land comprised in Leasehold Register Volume 2220 Folio 3 Plot 2 Lumumba Avenue and "Afrique Suites Hotel".

Counsel relied on the case of LIQUIDATORS OF PURSA (1954) 25 ITR 265 (SC), the words "used for the purposes of the business" were defined thus;
"used for the purpose of enabling the owner to carry on the business and earn profits in the business…The word "used" has been read in some of the pool cases in a wide sense so as to include a passive as well as active user."

Counsel submitted that the property in question was held for use in the business of a hotel and was therefore a business asset. Accordingly, the Tribunal was therefore right to hold that the same was a business asset. Counsel took note of the

argument by Counsel for the Appellant that the Mortgage Act restricts a mortgagee over security and that Equity bank only acquired secured rights thereof, the suite property could not have been owned by the bank and consequently, the property was not an asset to which Section 118B(2) could apply.

In response, Counsel submitted that Section 118B(2) does not make reference to the Mortgage Act and therefore it would be erroneous if, while interpreting the Income Tax Act, to refer to the Mortgage Act. Counsel submitted that it is a well-known principle of interpretation of taxation statutes that where a taxing statute is clear, words are given their ordinary meaning and these words cannot be qualified by definitions of other statutes.

Counsel relied on the decision of BANK OF ENGLAND VS VAGLIANO BROTHER (1891 AC 107), where it was held that;

"An Act is to be ascertained in the first instance from the natural meaning of its language and is not to be qualified by considerations deriving from the antecedent law… I think the proper course is in the first instance to examine the language of the statute and to ask what is its natural meaning, uninfluenced by any considerations derived from the previous state of the law, and not to start with inquiring how the law previously stood, and then, assuming that it was probably intended to leave it unaltered, to see if the words of the enactment will bear an interpretation in conformity with this view.'… 'If a statute, intended to embody in a code a particular branch of the law, is to be treated in this fashion, it appears to me that its utility will be almost entirely destroyed, and the very object with which it was enacted will be frustrated. The purpose of such a statute surely was that on any point specifically dealt with by it, the law should be ascertained by interpreting the language used instead of, as before, by roaming over a vast number of authorities in order to discover what the law was, extracting it by a minute critical examination of the prior decisions, dependent upon a knowledge of the exact effect even an obsolete proceeding such as a demurrer to evidence…It seems to me that, construing the statute by adding to it words which are neither

found therein nor for which authority could be found in the language of the statute itself, is to sin against one of the most familiar rules of construction, and I am wholly unable to adopt the view that, where a statute is expressly said to codify the law, you are at liberty to go outside the code so created, because before the existence of that code another law prevailed.'

As regards the non-recognition of the property on Equity Bank's balance sheet, Counsel submitted Section 118B(2) was not enacted to attract tax liability from purchasers where the seller was the actual owner of the property. According to Counsel, the legislature merely cast a wide net in order to capture taxes from whichever purchaser (regardless of who owned the asset) of a business or a business asset and hence the Tribunal was correct when it stated that a seller does not need to have an asset in its balance sheet in order to sell it and that restricting withholding tax to where business assets belong to a seller may have undesired effects.

Counsel submitted that nothing in Section 118B(2) calls upon the Respondent to inquire into the mode of acquisition of property before the tax is assessed; the section relates to a purchaser of property and does not restrict a purchase to any methods and it is immaterial that the purchase was done by way of public auction or private treaty or even Sale-Purchase Agreement. As long as there is a purchase, Counsel submitted, the purchaser is obliged to withhold taxes of 6% on the total purchase price.

Counsel referred to Black's Law Dictionary 10th Edition page 1429 as defining the word "PURCHASE" to include acquisition of an interest in property through a mortgage. It provides that;

i) The Act or an instance of buying.

ii) The Acquisition of an interest in real or personal property by sale, discount, negotiation, MORTGAGE, pledge, lien, issue, reissue, gift or any other voluntary transaction.

Counsel cited the case of RE FRONTIER CONSTRUCTION AND DEVELOPMENT LTD (1970) 14 CBR (NS) 291 AT 295, where it was held thus;

"…the word 'PURCHASE' …should be given the ordinary meaning and commercial and business like meaning of the word, vis, (acquisition by payment of money or an equivalent and refusing to apply it to the technicalities of real property law")

Counsel relied on the above authorities to submit that a purchase includes acquisition of property through a mortgage. Counsel referred to Section 30 (1) of the Mortgage Act as providing that 'PURCHASE' money has to be used in payment of any taxes due. The said section reads;

"The PURCHASE money received by a mortgagee who has exercised his or her power SHALL BE APPLIED IN THE FOLLOWING ORDER OF PRIORITY –

(a) 'In payment of any rates, rents, TAXES, charges or other sums owing and required to be paid on the mortgaged land'"

Counsel therefore contended that a sale under a mortgage could not be exempted from withholding yet the same Mortgage Act provides for the payment of tax out of the consideration for the purchase of the property.

Decision

I note that each of the above questions raises questions of statutory interpretation. It is important to being by considering the principles to application of tax statutes.

I am cognizant of the decision in **Cape Brandy Syndicate v IRC (1921) K.B 64** where it was held thus

"In a taxing Act, clear words are necessary in order to tax the subject in a taxing act, one has merely to look at what is clearly said. There is no room for an intendment. There is no equity about tax. There is no presumption as to a tax. Nothing is to be read in it, nothing is to be implied. One can only look fairly at the language used."

See also **Uganda Revenue Authority v Siraje Hassan Kajura SCCA 9/2015, Chestnut Uganda Limited v Uganda Revenue Authority TAT Application No. 94 of 2019.**

However, more recent precedents have underscored the use of other rules of statutory interpretation in interpreting tax statutes. In **URA v COWI A/S HCCA 34/2020** my learned brother Justice Mubiru opined extensively on the principles of statutory interpretation in respect of tax statutes. I am constrained to quote his judgment in some detail:

"It has for long been a well-established principle in the interpretation of tax legislation that the taxpayer may only be taxed by clear words (see Russell v. Scott [I948] A.C. 422 and Macpherson v. Hall (H.M. Inspector of Taxes) (1969-1973) 48 TC 210). In the event of ambiguity in tax legislation (where the provisions is so obscure that no meaning can be given to it), the taxpayer will be given the benefit of the ambiguity (see Fleming v. Associated Newspapers Ltd. (1970) 48 15 T.C. 382 at 390). Until relatively recently courts generally used this "strict and literal" approach to the interpretation of statutes, especially in fiscal matters, to overcome interpretational problems. It did not matter that such approach led to unfairness or even hardship.

However, in modern times, any exercise in interpretation and application of statutes cannot be undertaken on the assumption that it is an exercise without any object, that the Acts have no "spirit" or aim. For example the House of Lords, in Pepper (Inspector of Taxes) v. Hart [1993] 1 All ER 42, used the "purposive" approach to the interpretation of a fiscal statute and confirmed that it is permissible to use the Hansard Reports as an aid to statutory interpretation. Lord Denning led the way in Davis v. Johnson [1978] 1 All ER 841, when he used to the Hansard Parliamentary Debates Report (the "Hansard Reports"), the use of which was previously denied to the judiciary, as an aid to assist the court in finding the intention of Parliament and the purpose behind a provision. He rejected the notion

that judges should "grope about in the dark for the meaning of an Act without switching on the light."

The harmonious rule of legislative interpretation is adopted when there is a conflict between two or more statutes or between two provisions of the same statute. The rule requires that a legislative instrument must be construed on the prima facie basis that its provisions are intended to give effect to harmonious goals. The provisions of one statute should be interpreted in harmony with the tenor of other statutory provisions or the overall statutory purpose. Where conflict appears to arise from the language of particular provisions, the conflict must be alleviated, so far as possible, by adjusting the meaning of the competing provisions to achieve that result which will best give effect to the purpose and language of those provisions while maintaining the unity of all the statutory provisions. However, if this is not possible then it is settled law that where there is a conflict between two sections, and one cannot reconcile the two, one has to determine which the leading provision is and which the subordinate provision is, and which one must give way to the other.

In Metropolitan Life Limited v. Commissioner for the South African Revenue Services [2008] 4 All SA 558 (C), the court was of the view that when faced with apparently conflicting provisions in tax legislation, the interpreter must endeavour to arrive at an interpretation which gives effect to the purpose with which the Legislature enacted the relevant provisions. The purpose (which is usually clear or easily discernible) is used, in conjunction with the appropriate meaning of the language of the provision, as a guide in order to ascertain the legislator's intention and the scope of the provision. The court will then consider the extent to which the meaning that is given to the words achieves or defeats the apparent scope and purpose of the legislation.

Using both the purposive and harmonious rules of legislative interpretation, a court must read two allegedly conflicting statutes or instruments made

thereunder to give effect to each if it can do so while preserving their sense and purpose. The preferred interpretative approach is for both provisions to be interpreted purposively and holistically in order to be given a clear meaning whenever plausible, so that the provisions in the Regulations can be made to do work within the scheme of the Act. Only if provisions of two different statutes are irreconcilably conflicting, or if the later statute covers the whole subject of the earlier one and is clearly intended as a substitute, will courts apply the rule that the later of the two prevails."

See Also **Mangin v Inland Revenue Commissioner (1971) 1 ALL ER 179, URA v Patrick Nabiryo & Ors CACA 45/2013, Stanbic Bank Uganda Ltd & 7 Ors v Uganda Revenue Authority HCCA 170 of 2007**

The intention and context of a tax statute are helpful in its interpretation. In **INFORMER NO. TCI/002/07/05 – 06 v URA HCCS 579/2007**, court cited with approval the decision in **Engineering Industry Training Board v Samuel Talbot [1969] 1 ALL E.R. 480** when Lord Denning held thus:

> "But we no longer construe Acts of Parliament according to their literal meaning. We construe them according to their object and intent."

From the above, it is clear that the modern approach to interpretation is what is relied on to interpret tax laws, as opposed to the approach in Cape Brandy (above). Interpretation of tax laws is a holistic approach in which the court tries to ascertain the objective intention of the legislation while utilizing one or more than one of the canons of construction. It is when, applying these canons, that if a statute is vague, it should be interpreted in favour of the tax payer.

I must add however that, on top of the above, where the meaning of a statute cannot be discerned except through a more than reasonably simple process of inquiry, the same is vague and ought to be interpreted in favour of the tax payer.

Tax laws should be clear and easy to understand in order not to make it unduly burdensome for persons and entities to comply by having to go through an unduly complex process of ascertaining their meaning. This is what is called tax transparency. Law makers have a duty to ensure that tax laws are clear, transparent and accessible. See **OECD (2014), "Fundamental principles of taxation", in Addressing the Tax Challenges of the Digital Economy, OECD Publishing, Paris**, **Richard Murphy and Andrew Baker (2021), Making Tax Work: A Framework for Enhancing Tax Transparency. GIFT**.

Having reviewed the principles guiding interpretation of tax statutes, we will now interpret the impugned statutes guided by the principles above.

Section 118B(2) of the ITA, which is the section on which the bulk of this appeal rotates, provides thus:

"A resident person who purchases a business or business asset shall withhold at a rate specified in Part VIII of the Third Schedule."

From the above, three foundational things must be established:

(a) There is a purchase

(b) The purchaser is a resident person

(c) The purchase of a business or business asset.

Purchase

According to the **Black's Law Dictionary, 10th Edition, P.1354** defines a purchase this way

"1. The act or an instance of buying. 2. The acquisition of real property by one's own or another's act (as by will or gift) rather than by descent or inheritance."

A Purchaser is defined at **P. 1355** as

"One who obtains property for money or other valuable consideration; a buyer."

It is not in dispute that the Appellant bought the suit properties from Equity Bank in October 2020 and become the proprietor of the same by virtue of the sale. Accordingly, the first element has been satisfied.

Residence

The Appellant is a company. **Section 10** of the ITA defines a resident company thus:

"A company is a resident company for a year of income if it—
(a) is incorporated or formed under the laws of Uganda;
(b) has its management and control exercised in Uganda at any time during the year of
income; or
(c) undertakes the majority of its operations in Uganda during the year of income."

It is not in dispute that the Appellant is a resident of Uganda for tax purposes. What's more, the documents on record reveal that the Appellant falls in all of the above indicators for a tax resident company even if meeting one of the thresholds is sufficient.

Accordingly, the second element is also met.

Business Asset

Both Counsel attempted to define what a business asset is by defining what an asset was and then working their way to a business asset. In my view, the best starting point is the provision of law defining the word "business asset". **Section 2(h)** defines a business asset in this manner:

"business asset" means an asset which is used or held ready for use in a business, and includes any asset held for sale in a business and any asset of a partnership or company."

One must note that it is not the sale of any asset that triggers the application of **Section 118B(2)** of the ITA. Instead, it is the sale of a business asset that does so. From the reading of **Section 2(h)** above, an asset is a business asset if

(a) that the asset is used in a business; or

(b) the asset is held ready for use in a business;

The above definition also includes an asset held ready for sale in a business and an asset that is owned by a partnership or company.

What Is an Asset?

What is an asset is not defined by the ITA. As correctly submitted by Counsel for the respondent, when a word is not defined by the act, recourse can be had to a dictionary to define the word. This is because words used in legislation should ideally be given their ordinary meaning save in certain circumstances. See **Vivo Energy Uganda Limited v URA Civil Appeal No. 1 Of 2019**

The **Black's Law Dictionary, 10th Edition, Page 134** defines "asset" in this manner:

"1. An item that is owned and has value. 2. (pl.) The entries on a balance sheet showing the items

Of property owned, including cash, inventory, equipment, real estate, accounts receivable, and good will.3. (pl.) All the property of a person (esp. a bankrupt or deceased person) available for paying debts or for distribution."

An Item Owned and Has Value

It is not in dispute between the parties that the suit properties were owned by a one Eng. Peter Kamya whose company mortgaged it to Equity Bank Limited. It is also not in dispute that the suit properties were sold by that bank to the Appellant for value.

In my view, Counsel for the Respondent was correct in submitting that since the property was owned by Mr. Kamya at the time of transfer, had been used as security for a loan and sold for value, the same was owned and had value thereby classifying it as an asset.

Entry On Balance Sheet

Counsel for the Appellant criticized the TAT for holding that the suit properties were assets in light of evidence adduced by the Appellant that the properties were not reflected on its balance sheet. Counsel for the Respondent contended that this had no bearing because one needs to read only the provisions of the law to render an accurate interpretation.

Let's stop for a moment and consider the accounting treatment of mortgages from the perspective of a bank. Whereas accounting principles do not oust the provisions of the law, they are no doubt helpful in understanding and applying the law and recourse should be had to them except if they conflict with the provisions of the law. See **Mukwano Enterprises Ltd v Uganda Revenue Authority TAT Application No. 06 of 2018**.

When a bank extends a mortgage to a borrower, it essentially creates a loan agreement in which the borrower pledges the property as collateral for the loan. This loan agreement may be classified as a financial instrument or a non-financial asset, depending on the nature of the mortgage.

If the mortgage is classified as a financial instrument, then the accounting guidance for financial instruments, as set out in IAS 32 "Financial Instruments: Presentation" and IFRS 9 "Financial Instruments," would apply. Under IAS 32 and IFRS 9, the bank would recognize the mortgage loan as a financial asset and the borrower's obligation to pay the loan as a financial liability.

The bank would initially record the mortgage loan at fair value, which would be the present value of the expected future cash flows from the loan, discounted at the market rate of interest. The bank would also need to classify the financial asset and the financial liability as either amortized cost, fair value through profit or loss, or fair value through other comprehensive income, depending on the bank's business model and the contractual cash flow characteristics of the mortgage.

If the mortgage is classified as amortized cost, the bank would recognize interest income on the mortgage loan over the life of the loan, using the effective interest rate method. The bank would also recognize any impairment losses on the mortgage loan, which would reduce the carrying amount of the financial asset on the balance sheet.

If the mortgage is classified as fair value through profit or loss or fair value through other comprehensive income, the bank would recognize any changes in the fair value of the mortgage loan in either profit or loss or other comprehensive income, depending on the classification of the financial instrument.

If the mortgage is not classified as a financial instrument, then the accounting guidance for property, plant, and equipment, as set out in IAS 16 "Property, Plant and Equipment," would apply. Under IAS 16, the bank would recognize the mortgaged property as a non-financial asset and record it at cost or fair value, depending on the circumstances of the acquisition.

If the bank forecloses on the mortgaged property and takes possession of it, the bank would need to determine the fair value of the property and recognize it on the balance sheet as a non-financial asset. If the fair value of the property is less than the carrying amount of the mortgage loan, the bank would recognize an impairment loss on the mortgage loan, which would reduce the carrying amount of the financial asset on the balance sheet.

In both cases, the bank would need to disclose information about the mortgage and the mortgaged property in the notes to its financial statements. This information would include the carrying amounts of the financial and non-financial assets, any impairment losses recognized, and any other significant terms and conditions of the mortgage agreement.

Accordingly, it is not accurate to say that mortgaged property is not reflected on the books of the bank as an asset. What is for sure is that they are not financial assets. Only the facility (that is, the loan) is reflected on its balance sheet as an asset (a financial asset).

It would follow therefore that, at least after foreclosure, mortgaged property is an asset of the bank.

Property for Paying Debts or Distribution

Section 26 of the Mortgage Act which provides for a Mortgagee's power of sale as follows

"(1) Where a mortgagor is in default of his or her obligations under a mortgage and remains in default at the expiry of the time provided for the rectification of that default in the notice served on him or her under section 19 (3), a mortgagee may exercise his or her power to sell the mortgaged land."

Further, **Section 8 (1)** of the Mortgage Act that states that;

"…a mortgage shall have effect as a security only and shall not operate as a transfer of any interest or right in the land from the mortgagor to the mortgagee…."

See also **Francis Kiyaga v Josephine Ssegujja & Anor CACA 76 of 2011**

As correctly submitted by Counsel for the Appellant, a mortgage is security for the repayment of a debt. The property under a mortgage is pledged only as security for the repayment of the loan and the mortgagor is entitled to redeem the property given as security once the loan it secured is repaid. Once there is a default on the loan, the mortgagee is entitled to take advantage of all the statutory reliefs available to a mortgagee on a mortgagor's default.

It follows from the above that mortgaged property is not property of the bank available to pay its debts or for distribution and may not be liquidated to satisfy drawing requests of the bank's shareholders.

I agree with Counsel for the Appellant that applying the definition on this head, the mortgaged properties would not be assets of the bank.

So, again, what is an asset?

Reading Section 118B(2) above, there is no requirement that the asset must be the that of the entity selling. The property to be sold need only be an asset. This is because selling of property is not only done by the proprietors but may also be sold by third parties (such as agents, donees of powers of attorney, auctioneers among others).

Accordingly, reading Section 118B(2) it is sufficient if the thing meets at least one definition of an asset. Essentially, the section requires that the thing to be sold should be an asset of someone not necessarily the person selling the same.

From the above, the proprieties met two of the three definitions of an asset (owned and has value and recorded on the balance sheet). In my view therefore, the suit

properties (referred to as "Afrique Suites") are an asset within the meaning of Section 118B(2) and Section 2(h) of the ITA.

Is an Asset Automatically Business Asset?

Section 118B(2) does not cover the sale of all assets. It restricts itself to the sale of business assets. What constitutes a business asset is defined in Section 2(h). Essentially, a thing is a business asset if

(a) that the asset is used in a business; or

(b) the asset is held ready for use in a business;

Used in a business

The starting point is to note that the statute uses the word "a" as opposed to words that may have a narrowing effect such as "the". The effect of this in my view is that once it is demonstrated that the asset was used in any business, the same is a business asset notwithstanding that it was not used in the business of the bank.

Counsel for the Respondent cited the Indian Supreme Court case **of Liquidators Of Pursa Limited v Commissioner Of Income Tax 1954 SCR 767** where the court dealt with the phrase "used for the purposes of the business. The Court held thus:

"The words "used for the purposes of the business" obviously mean used for the purpose of enabling the owner to carry on the business and earn profits in the business."

In this case, Section 2(h) deals with use of the asset for the purposes of a business. In my view, this means that the asset sold should be used by a business carry on its operations and earn profits, whether or not profits are actually earned.

In **UMEME Limited & Anor v Uganda Revenue Authority TAT Application 40 of 2018**, Court defined "use" as to employ something for the accomplishment of a purpose. Accordingly, the asset must play some role to the business of the

taxpayer, even if that role is not one that contributes to the core part of the owner's business. See **Azar Nut Company v Commissioner Of Internal Revenue 931 F.2d 314 (5th Cir. 1991), Al Carter Co v Commissioner Of Internal Revenue 143 F.2d 296 (5th Cir. 1944)**

In considering whether a property is used in the business of a tax payer, consideration should be had, subject to the circumstances of each case, to the continuity and regularity of the use of the asset, as well as the taxpayer's operations and the role that asset plays therein. See **Southern Natural Gas Co. v. United States, 188 Ct.Cl. 302, 378-379, 412 F.2d 1222, 1268 (1969)**

It was not in dispute that the suit property constitutes property describes as Afrique Suites, a hotel business. It is this property that was mortgaged to the bank and consequently sold to the appellant. The property was being run as a hotel with the view of making profit. Accordingly, in my considered opinion, the same is an asset used in a business, in this case, the business of the mortgagee.

Counsel for the Appellant submitted that Afrique Suites is was not used in the business of the Appellant and therefore could not qualify as a business asset. In my view, the use of the expression "used in a business" did not require for the asset to be used in the business of the Appellant for it to become a business asset. The law simply requires that the asset be in any business for it qualify as a business asset.

In **UMEME Limited & Anor v Uganda Revenue Authority TAT Application (Supra)**, the court warned against applying extraneous conditions to the application of a statutory provision which are not captured within the provision of the law. I agree with these dicta and would like to add that it is not the role of the court to legislate. If a court inserts conditions to the application of a provision of law which do not exist in a text, it is legislating and therefore acting outside of the constitutional mandate conferred upon it by law.

I can find no basis in Section 2(h) for the contention that the asset must first be used in the business of the entity selling it for it to qualify as a business asset. If the law had wanted to impose this condition, the same would have been indicated in the text of the provision; the legislators who made the provision were not short or space to include it. The condition does not exist within the section and I will not forcefully insert it there.

It takes note of the decision **in Comfort Homes v Uganda Revenue Authority TAT Application 66 of 2010** where it was held that for an asset to qualify as a business asset, he transaction leading to its purchase must be a business transaction. With the greatest respect to the members of the Tax Appeals Tribunal, I can find no condition to that effect in the law. All the law requires is for a resident person to purchase a business asset. As to whether the transaction between them is a business transaction is immaterial on the reading of Section 118B(2).

It follows therefore that Afrique Suites is a business asset. My finding here means I do not have to consider whether Afrique Suites is a business asset by virtue of being held ready for use in a business but I will nonetheless pronounce myself on the same.

<u>Ready for use in a business</u>

An asset is held ready for use in a business if it is available to be put to use in the business. In **Niranjan Chandra v Commissioner Of Income Tax 1963 49 ITR 177 All**, the court considered whether idle assets were being "used for the purposes of the business". Court held thus:

"A truck which is put into motion for transporting goods on hire from time to time or periodically is as much used for the purposes of the business when stationery as a truck continuously in motion. In the words of Lord Summer in Birendra Kumar Ghosh v. Emperor, "They also serve who only stand and wait." Though a telephone is meant for receiving sound from a distance, it is said to be used by a person even though the person is not actually receiving any sound with its help. A burglar alarm

can be said to be in use at a given moment even though there is no burglar in the premises and the alarm is not ringing at the moment. An article which is meant for yielding a certain result and which yields the result not continuously but periodically as and when required, cannot be said to be not in use at a particular time simply because it is not yielding the result at that time. If it is capable of yielding the result and is available for producing the result, it is in use. It is only that article which is meant to go on yielding the result continuously that can be said to be not in use at a time when it is not yielding the result. A truck to be used for the purpose of the business of plying trucks and lorries on hire is not an article of this kind, not being meant to be used continuously without a break. Hiring is always for a certain time or for a certain distance and as soon as the time is over or the distance is covered the article hired must remain idle till it is to be hired again."

See also **Sanghavi Movers v Dy. CIT 2008 110 ITD 1**

Essentially therefore, the duo definition of an asset [as used or held ready to use] covers what are referred to as active assets in other jurisdictions. These are assets which the tax payer is employing or are available for the tax payer to employ in their operations. See **Commissioner of Taxation v Eichmann [2019] FCA 2155**

I have already found that Afrique Suites was a business asset belonging to its previous owner at the time of purchase by the appellant. If my decision on the first head of business classification is overturned (i.e that it is a business asset used by its owner at the time of purchase), I would like to pronounce myself on the second head of classification namely whether it was held ready for use.

From the evidence on record, it is clear that the buildings were developed and furnished to run a hotel known as Afrique Suites. At the very least, the properties now subject to litigation constitute business assets that were held ready for use as the same were developed and furnished to be utilized to operate a hotel, whether or not a hotel was being operated at the time of purchase.

Accordingly, I find that the Tax Appeals Tribunal correctly held that the suit properties were business assets within the meaning of Section 2(h) and 118B(2) of the Income Tax Act. Ground one of appeal fails.

Ground Two: That the learned members of the Tribunal erred in law when they held that Section 118B (2) of the Income Tax Act was not ambiguous
Ground Three: That the learned members of the Tribunal erred in law when they held that Section 118 (B)(2) of the Income Tax Act did not conflict with Section 117 (2) (b) of the Income Tax Act

Submissions of Counsel for The Appellant

Counsel for the Appellant criticised the tribunal for holding that Section 118B(2) of the Income Tax Act was not ambiguous. Counsel submitted that the Tribunal's interpretation is erroneous and would set a very dangerous precedent since such an interpretation causes automatic absurdities and would go against the context of the text and the law.

Counsel submitted that Section 118 B (2) ITA is ambiguous to the extent that it does not specify in whose hands the asset sold should qualify as a business asset in order for the obligation to withhold tax to be triggered.

Counsel argued that ITA merely states that "a resident person who purchases a business asset shall withhold tax..." Counsel argued that what may be a business asset in the hands of a seller may not be a business asset in the hands of the purchaser. For instance, in the transfer of a condominium property from a real estate developer to an individual acquiring the land for residential purposes. In the hands of the seller, the property is a business asset however in the hands of the buyer, the property is not a business asset.

Counsel submitted that the fact that property can and does change character for income tax purposes creates confusion in the interpretation of Section 118B (2)

ITA particularly with respect to, in whose hands (between the seller and purchaser) must the asset be held as a business asset in order to trigger the obligation to withhold tax. Counsel submitted that it was unclear whether the obligation to withhold is triggered if the seller does not hold the property as a business asset but the buyer intends to use it as a business asset in their business.

Counsel submitted that more confusion is caused where both the seller and buyer of the property do not hold it as business asset but the property is a business asset in the hands of some third party. Counsel gave the example of the present case; the properties were not a business asset to the seller, Equity Bank and also not a business asset to the buyer namely the applicant.

Counsel submitted that in the instant case, the owner of the property Peter Kamya was using the property as a hotel but the purchaser [namely the appellant] did not purchase the hotel business of Peter Kamya but simply the land and buildings and he has not used the property as a hotel at all. More importantly Equity bank which actually sold the property was not using the property as a hotel but as mortgaged property which was security for repayment of a loan. Therefore, the property could not have been a business asset in the hands of the seller or the buyer [the appellant].

Counsel relied on the case of UGANDA REVENUE AUTHORITY V UGANDA TAXI OPERATOR AND DRIVERS ASSOCIATION CIVIL APPEAL NO. 13 OF 2015 as authority for the proposition that if a legislation is ambiguous, the court should adopt the interpretation that favours the tax payer.

Counsel cited the case of Stanbic Bank (U) Limited & 7 Others V Uganda Revenue Authority HCCS 792 of 2006 & 170 of 2007 as authority for the proposition that before one is assessed for a tax liability, the law imposing the liability should be clear and unequivocal.

Counsel relied on the case of LAFARGE MIDWEST INC V CITY OF DETROIT, STATE OF MICHIGAN COURT OF APPEALS NO. 289292 where the court held that a provision of law is ambiguous only if it irreconcilably conflicts with another provision or when it is equally susceptible to more than one meaning.

Counsel submitted that since Section 118B (2) ITA does not does not specify in whose hands the asset sold should qualify as a business asset, the provision is susceptible to more than one meaning and therefore it is ambiguous and ought to be interpreted in favor of the tax payer/the Applicant. The provision falls short of the "clear and unequivocable" standard set by the courts

Counsel submitted that this court was under a duty to construe Section 118B(2) ITA in such a manner as not to achieve an unreasonable effect. Counsel cited the case of FARID MEGHANI VERSUS URA HCCA 6 OF 2021 PAGES 7 TO 8, as authority for the proposition that courts are required to construe statutes to avoid unreasonable results, and further to presume that the Legislature does not intend to enact useless or meaningless legislation.

Counsel contended that if the impugned section was interpreted strictly as was done by the tribunal, the following absurdity would be created:

(a) On the one hand, it would mean that lenders enforcing loan obligations through foreclosure of business assets particularly immovable property would be required to pay withholding tax at 6%. Given that foreclosure is just one form of loan recovery for banks, requiring payment of 6% on proceeds of a foreclosure sale would effectively charge 6% on all loan recoveries through foreclosure and maintain the exemption on other forms of loan recovery that do not involve the sale of property. This is particularly absurd because a lender who pursues foreclosure as a form of recovery has already incurred loss due to late / non-payment of the loan by the mortgagor

and now the imposition of a 6% withholding tax would unjustifiably impose a further burden on the lender. A lender who receives timely payments of principal and interest is not required to account for withholding tax on the interest payments however a lender who has already suffered nonpayment and endured the rigorous procedure to recover their loan is further punished by requiring a further deduction of 6% withholding tax? This cannot have been the intention of the legislature.

(b) Applying withholding tax on the disposal of foreclosed property has the net effect of charging withholding tax on interest income of financial institutions which interest is exempt under section 117 (2)(b) of the same Income Tax.

Counsel submitted that statutes must be read as a whole. He cited the case of FARID MEGHANI VERSUS URA HCCA 6 OF 2021 as authority for this proposition.

Counsel contended that charging withholding tax on financial institutions runs contrary to the very purpose of withholding taxes in general and the withholding tax under section 118B(2) specifically. He charged that withholding taxes are meant to collect taxes from a section of tax payers who may not regularly comply with their tax obligations and who the Government may not easily trace to enforce compliance.

Counsel submitted that tax law that compliant tax payers who regularly comply with their tax obligations are exempt from withholding tax in accordance with Section 119(5) (f) (ii) of the Income Tax Act.

Counsel critised the tax appeals tribunal for erroneously ruling that the Applicant/Appellant did not provide a list of entities that are exempt from WHT under section 119(5) ITA yet the same had been supplied and is contained at page 137 of the ROA Counsel submitted that in the said document, the Managing

Director of Equity Bank confirmed that Equity Bank was number 1228 on the list of exempt entities published by the Respondent in 2020.

Counsel contended that it is judicial notice that this list is published annually by the Respondent and can be accessed on the Respondent's website at any time. Equity Bank Uganda Limited and indeed many financial institutions in Uganda are routinely included on the list of exempt entities since its first publication and Equity Bank continues to be recognized by the Respondent as an exempt organization under section 119(5)(f)(ii).

We submit that the inclusion of Equity Bank and other financial institutions on the withholding exempt list shows that the Respondent trusts that the Bank will comply with its tax obligations under the Income Tax Act.

Counsel submitted it was perversely counterintuitive that the same legislature that declared a bank's income is exempt from withholding tax under section 117(2)(b) and also provided for a withholding exempt list of compliant tax payers under section 119(5)(f)(ii), (on which the Respondent habitually includes Equity Bank), could have intended that, the same banks pay withholding tax when they foreclose on properties to recover interest and principal.

Counsel prayed that this Honourable court finds that the provisions of section 118B (2) of the ITA are ambiguous to the extent that they are capable of more than one meaning and / or conflict with section 117(2)(b) of the Income Tax Act.

Submissions by Counsel for The Respondent

Counsel for the Respondent supported the decision of the Tax Appeals Tribunal. She submitted that for a provision of the law to be considered ambiguous, it must either be capable of more than one meaning or it must irreconcilably conflict with another provision of the law. Counsel cited the case of LAFARGE MIDWEST INC. VS CITY OF DETROIT, STATE OF MICHIGAN COURT OF APPEAL NO, 289292.

My Lord, we seek to argue first on the point that an act is ambiguous where it is capable of more than one meaning. The second element of ambiguity where a provision irreconcilably conflicts with another provision shall be argued under Grounds 3, 4 and 5 as it substantially relates to interest payments.

Counsel submitted that the act provides that a purchaser of a business asset shall withhold tax. The implication of the section is that only the purchasers of business assets and not sellers of the same.

Counsel submitted that the Tribunal was rightly guided by the literal rule of interpretation which is that the literal interpretation of a statute takes precedence unless it is ambiguous. Counsel cited the case of National Social Security Fund V Uganda Revenue Authority HCCA No. 29 Of 2020 as authority for this proposition. Counsel submitted that the section neither provides for any ambiguity nor does it provide for any absurdity and therefore there was no need for the Tribunal to delve into the nature of the sale where the Act did not mention anything about the seller.

Counsel contended that once the purchaser fell within the tenets of 118B(2), in that he purchased a business asset, whose definition is clearly laid out in the act, his mandate was to withhold the tax equivalent to 6% of the purchase price.

Counsel took note of the submission by the Appellant that Section 118B(2) is ambiguous because it does not specify in whose hands the asset should be for the obligation to withhold to arise. She submitted that the intention of parliament was to capture all forms of assets regardless of the person selling. Had parliament intended to specify the sellers from whom a purchase would trigger a withholding tax obligation, it would have stated so.

Counsel submitted that the fact that the section does not specify whose hands the asset should be does not make the section ambiguous as it does not leave the

section susceptible to more than one meaning and neither does it that make it conflict with any other provision of the Income Tax Act.

As to the analogy on the application of the impugned section say on a purchase of condominium property, Counsel submitted that the facts at hand only relate to a purchase of a business asset and not condominium property or to transfer of a hotel from a deceased person as the Appellant seems to suggest. According to Counsel, these arguments are therefore not only moot but also academic as a determination on them will not affect the substantive issues at hand. Counsel cited the case of Uganda Human Rights Network for Journalists v UCC HCMC No. 219 of 2013 as authority for this proposition.

Decision

As correctly submitted by both Counsel, a provision of law is vague if it irrevocably conflicts with another provision or if it is susceptible to more than one meaning. See **Black's Law Dictionary, 8th Edition, Pg. 88, Lafarge Midwest Inc. v City of Detroit. State of Michigan Court of Appeals No. 289292, Crane Bank v Uganda Revenue Authority HCT HCCA No 18 of 2010, Roche Transport Limited v Uganda Revenue Authority HCCA 20/2021**

Counsel for the Appellant submitted that **Section 118B(2)** was vague because

(a) It was susceptible to more than one meaning

(b) It conflicts with Section 117 (2)(b) of the ITA

Numerous Meanings

Counsel for the Appellant submitted that it was not clear in whose hands the asset sold should be a business asset in order for the obligation to withhold to be triggered.

I am unable to agree with Counsel for the appellant. The law requires a purchase of a business asset by a non-resident person. Once these ingredients are met, there is an obligation to withhold tax by the purchaser of the asset.

It does not matter that the asset is not a business asset in the hands of either the buyer or the seller; what is necessary is that the asset must be a business asset to someone; that is, it must constitute an asset used or held ready for use in the business of some entity.

The rationale for this, in my view, is that the section focuses not on the relevance of the asset to the contracting parties to the sale and purchase agreement, but the objective status of the asset as used or liable to be used in a business. For there to arise an obligation to withhold, it must be demonstrated that one person uses the asset in their business or holds the asset ready for use for the same purposes.

As correctly found by the Tax Appeals Tribunal, the effect of the appellant's reasoning would be that parties would use third parties with the view of evading tax. What is clear is that Section 118B(2) charges tax on the transaction of selling and buying a business asset, notwithstanding the fact that the asset is not a business asset of the transacting parties. It is the status of the asset as a business asset coupled with its purchase that creates the obligation to withhold, the obligation being on the purchaser of the asset.

I cannot find any contrary meanings of the law and I accordingly reject the submissions by Counsel for the Respondent that the impugned provision is capable of multiple conflicting interpretations. I cannot find any contrary interpretation to the interpretation rendered above and the submissions of Counsel for the Appellant on this head were neither correct nor convincing.

Conflict with Section 117 (2)(b) of the ITA

Section 117(1) and (2) of the ITA provides thus:

"(1) Subject to subsection (2), a resident person who pays interest to another resident person shall withhold tax on the gross amount of the payment at the rate prescribed in Part V of the Third Schedule to this Act.

(2) This Section does not apply to—

(a) interest paid by a natural person;

(b) interest, other than interest from government securities, paid to a financial institution;

(c) interest paid by a company to an associated company; or

(d) interest paid which is exempt from tax in the hands of the recipient."

Section 117(1) and (2) of the ITA exempts interest payments to financial institutions from tax. It is not in dispute that Equity Bank is a registered and duly licensed financial institution within of the Financial Institutions Act.

Counsel for the Appellant (to briefly state his argument) submitted that consideration from the sale of mortgaged property includes both the principal loan sum as well as interest. Counsel submitted that neither of the two classes of the money above are amenable to tax and therefore, contrary to the provisions of **Section 118B(2)**, the said sums are not amenable to tax.

I must note that withholding is a mode of collection of tax and not a head of tax in itself. Withholding allows the Respondent to collect tax from the entity purchasing a good or tax by remitting a portion of the consideration to the Respondent directly, rather than the same having to first be declared and remitted by the entity receiving the payment.

By way of first principles, **Section 118B(2)** (which provides for withholding) is a mode of collection of income tax. Where the transaction is not amenable to income tax, there can be no withholding since there is no tax to remit.

Income tax is imposed by **Section 4** of the Income Tax Act which provides thus:

"Subject to, and in accordance with this Act, a tax to be known as income tax shall be charged for each year of income, and is imposed on every person who has chargeable income."

What is chargeable income? **Section 15** of the Income Tax Act provides:

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

See also **URA v Siraje Hassan Kajura SCCA 9/2015**

This begs the question; what is income? **Black's Law Dictionary, 10th Edition P.831** defines income thus:

"The money or other form of payment that one receives, usu. periodically, from employment, business, investments, royalties, gifts, and the like. See EARNINGS. Cf. PROFIT."

In **LABRIE, F. E. (1953). The Meaning of Income in the Law of Income Tax. University of Toronto Press**. http://www.jstor.org/stable/10.3138/j.ctvcj2kz2 income is defined this way:

"Income means literally "incoming" or "what comes in" considered in relation to money or money's worth…… "income" [is] defined as "the gain derived from capital, from labour, or from both combined."

See Also **Stratton's Independence v. Howbert, 231 U.S. 399, 34 S.Ct. 136, 140, 58 L.Ed. 285, Doyle v. Mitchell Bros. Co., 247 U.S. 179, 38 S.Ct. 467, 62 L.Ed. 105, Eisner v. Macomber, 252 U.S. 189, 40 S.Ct. 189, 193, 64 L.Ed. 521, 9 A.L.R. 1570, North American Oil Consol. v. Burnet, 286 U.S. 417, 52 S.Ct. 613, 76 L.Ed. 1197, Bowers v. Kerbaugh-Empire Co., 271 U.S. 170, Conner v. US, 303 F.Supp. 1187**

The question then becomes, what is the character of consideration received from the sale of mortgaged property. This, as correctly held by the dissenting panelist in the tribunal, depends on what a mortgagee is entitled to in respect of consideration received from the sale of the mortgaged property.

Section 36 of the Mortgage Act provides thus:

"The purchase money received by a mortgagee who has exercised his or her power of sale shall be applied in the following order of priority

a) In payment of any rates, taxes, charges, or other sums owing and required to be paid on the mortgaged land,

b) In discharge of any prior mortgage or other encumbrance subject to which the sale was made,

c) In payment of all costs and reasonable expenses properly incurred and incidental to the sale or any attempted sale,

d) In discharge of the sum advanced under the mortgage or so much of it as remains outstanding, interest, costs, and all other monies due under the mortgage, including any monies advanced to a receiver in respect of the mortgaged land under section 2,

e) In payment of any subsequent mortgages in order of their priority: and

f) The residue, if any, of the money received shall be paid to the person who, immediately before the sale, was entitled to discharge the mortgage."

It follows that there are essentially two categories to which the consideration falls

(a) Principal loan amounts

(b) Interest, charges and penalties

(c) Surplus due to the mortgagor

Items (a), (c) do not constitute income to the bank. Neither does surplus due to the mortgagor since the same must be paid to the mortgagor.

The principal loan amount is not chargeable income and the same is not amenable to tax. See **Section 15 and 17 of the Income Tax Act**.

Only interest and payments under the mortgage (such as penalties, fees and charges) constitute chargeable income. However, **Section 117 (2) (b)** above exempts financial institutions from withholding tax in respect of interest paid to them with the exception of interest from government securities.

Section 2(kk) defines interest in the following manner

"(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;"

It follows from the above that other payments which might not be termed interest in the ordinary use of the word are also interest within the meaning of **Section 2(kk)**. These include arrangement fees, processing fees, fines and such related charges.

These payments are exempt from withholding tax courtesy of **Section 117 (2) (b)**. Yet, Section 118B(2) declares that the same are subject to withholding tax. There is therefore a conflict between **Section 117(2)(b)** and **Section 118B(2)**.

As already stated above, a provision of law is ambiguous if it contradicts another provision of law in such a way that the law imposes two contradictory provisions that cannot be reconciled. It is different where one provision of law contradicts another but one of the provisions is subject to the other. In those circumstances, even when there is a conflict, there is no ambiguity because it is clear as to which law takes precedence. Accordingly, a conflict causing ambiguity occurs when there is a conflict between two provisions of the law of the same hierarchy.

In the instant case, **Section 118B(2)** conflicts with **Section 117(2)(b)** and none is entitled to prevail over the other.

In those circumstances, the court must harmonise them by taking the interpretation that is most favorable to the tax payer. See **Uganda Revenue Authority V Uganda Taxi Operator and Drivers Association Civil Appeal No. 13 Of 2015**.

As held in **Stanbic Bank (U) Limited & 7 Others V Uganda Revenue Authority HCCS 792 of 2006 & 170 of 2007** before one is assessed for a tax liability, the law imposing the liability should be clear and unequivocal. This is to ensure that taxpayers know clearly, without the need for strenuous and complex reflection, the taxes applicable to them, the rates of tax and the circumstances under which those taxes apply.

Accordingly, this court takes the view that consideration from the disposal of mortgage property, in as far as it includes interest is exempt from withholding in accordance with **Section 117(2)(b)** of the Income Tax Act.

It also follows from the above that only the surplus of the consideration for the sale of mortgaged property is properly amenable to withholding tax within the meaning of Section 118B(2) if the other conditions therein are met.

In **Crane v. Commissioner, 331 U.S. 1 (1947)**, the US Supreme Court, considering a related matter found that a tax law does not attach at and tax something that is not income. In this case, the proceeds from the disposal of the mortgaged property only yielded the principal loaned sum and not the interest.

At pages 177-179 of the record, the Appellant led evidence that mortgagee lent USD 10 million to the mortgagor and was only able to recover USD 4.35 million by way of selling of the mortgaged properties to the appellant. This evidence was not challenged. From the above, clearly the entire amount of money paid by the

Appellant was received by the bank as a recovery of the principal loan sum. Accordingly, therefore, the same is exempt from tax and the Appellant had no obligation to withhold tax on the amount paid under the sale and purchase agreement with the bank.

Accordingly, the Appellant's appeal succeeds on grounds 2 and 3.

Ground Four: That the learned members of the Tribunal erred in law when they held that section 117 (2) (b) deals with exemption of withholding tax on interest which is business income whereas section 119 B (2) deals with withholding tax on purchase of a property which is property income.

Ground Five: That the learned members of the Tribunal erred in law when they held that purchase price is not interest in complete disregard of section 18 (2) of the Income Tax Act which states that interest retains its character for the purpose of any section of the Income Tax Act referring to such income.

Whereas Counsel for the Appellant handled grounds 3,4 and 5 together. I felt it was proper to handle grounds 2 and 3 together, and then 4 and 5 together.

Submissions of Counsel for The Appellant

Counsel submitted that the sale of mortgaged property by Equity Bank takes the form and character of the loan obligations the bank was trying to recover i.e., principal and interest. According to Counsel, since the repayment of principal is not taxable as income under the Ugandan tax laws, then focus should be placed on the taxation of the interest received by the Bank. Counsel submitted that Section 18(1) (f) of the Income Tax Act provides that business income includes interest derived by a person engaged in the business of banking or money lending.

Counsel submitted that the import of Section 18 (2) ITA above is to qualify the sale of a mortgaged property as recovery of interest. This is because according to the section, interest retains its character as interest income regardless of any other

reference used under the Act. Therefore, according to Counsel, Section 18(2) ITA would trump Section 118 B(2) ITA which seeks to qualify interest income as a business asset

Counsel submitted that Section 117 (2) (b) ITA of the Income Tax Act, interest income paid to financial institutions is exempt from withholding tax and therefore, the Respondent erred to claim WHT under section 118B (2) which does not apply to foreclosure of mortgaged securities by Banks. According to Counsel, the proper section that ought to apply to the sale of mortgaged property is section 117 (2) (b) which exempts interest income paid to a Bank from withholding tax.

Counsel submitted that there is a clear conflict between section 118B (2) and section 117 (2) (b) of the Income Tax Act. Counsel cited the case of Roger v United States 185 US 83 (1902) to support the argument that since Section 117(2)(b) dealt more specifically with interest payments to banks, the same should take precedence over Section 118B(2) which is of more general application.

Counsel took note of the finding of the tax appeals tribunal that the purchase price is not interest and therefore the same was amenable to withholding tax. Counsel relied on Section 18(1)(a) and (f) of the ITA to mean any income derived by a person in carrying on a business and includes both the amount of any gain derived by a person on the disposal of a business asset and interest derived by a person engaged in the business of banking or money lending.

Counsel submitted that Property income on the other hand is defined under section 20 of the ITA and specifically excludes any amount which would qualify as business income.

Counsel submitted that both interest derived from banking business as well as income from the sale of a business asset qualify as business income and that where a mortgage is foreclosed to recover principal and interest, the proceeds of the sale

of property retain their character as interest in accordance with section 18(2) of the ITA.

Counsel submitted that the learned members of the Tribunal erred in law when they held that Section 118B (2) of the Income Tax Act did not conflict with Section 117 (2) (b) of the Income Tax Act and the learned members of the Tribunal erred in law when they held that purchase price is not interest in complete disregard of section 18 (2) of the Income Tax Act which states that interest retains its character for the purpose of any section of the Income Tax Act referring to such income.

Submissions by Counsel for The Respondent

Counsel for the Respondent submitted that Court has been clear on how to strictly construe tax exemptions against the entity claiming them. According to Counsel, an entity seeking to rely on an exemption has to clearly point to the law exempting them.

The Appellant seeks to erroneously apply an exemption extended to financial institutions to itself. Section 117(2)(b) relates to interest paid by a resident to a none resident. Section 118B(2) relates to withholding tax on purchase of assets. The Appellant is neither a financial institution nor a money lender to whom the interest exemption under S. 117(2)(b) would apply.

Counsel cited the cases of Siraje Hassan Kajura v. URA (above) and Manilla North Tollways Corporation v Commissioner Of Internal Revenue C.T.A Eb No. 812 Of 2012.

Counsel submitted that Section 118B(2) could not be read into Section 117(2)(B) as the same relates to different tax heads albeit under a similar tax collection method of withholding tax. Section 118B(2) relates to withholding tax on property income i.e. purchase of an asset whereas Section 117 relates to withholding tax derived from payment of interest to resident persons.

Counsel submitted that had the legislature intended that the Section be limited by other provisions of the law, it would have clearly provided the words "subject to other provisions of this Act." According to Counsel, if the Parliament had wanted Section 117 to act as an exemption to the provisions of Section 118B(2), it would have stated so since Section 118B(2) is a latter enactment of 2019 to Section 117 which was enacted in 2006.

Counsel contended that Section 118B(2) is in regards to the purchasers of the Business Assets and not sellers. Counsel submitted that Appellant was the purchaser of the suit property and therefore purchaser paid was purchase price and the same cannot be regarded as a payment of interest.

Counsel submitted that the Appellant is neither a bank nor a financial institution and could not take benefit from this exemption. According to Counsel, Section 117(2)(b) provides applies only to a person paying interest and the Appellant was not one such person.

Counsel submitted Section 2(kk) which defines '*interest*' does not provide for payment of interest includes payment of purchase price accruing from a sale of mortgaged property. Counsel referenced the sale and purchase agreement at Page 132 of the record and submitted that the amount paid by the Appellant to the bank was clearly expressed as a "*purchase price*" and not a payment of interest.

Counsel submitted that Appellant was not a party to the loan agreement between Equity Bank and the borrower that led to the accrual of interest. According to Counsel, for payment of interest to be made, it has to be established that the payment relates to a debt obligation which is defined by Section 2(s) of the Income Tax Act 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".

Counsel submitted that under Section 18(1)(f), the payments made must be in respect to interest that has been derived in respect of a trade receivable. Counsel contended that that the amounts in question were not payments of interest as they were not derived in respect of a trade receivable.

Counsel further submitted that the second limb of Section 18(1)(f) is in respect to interest derived by a person in the business of banking or money lending. According to Counsel, the Appellant did not have any debt obligation to which he would have made an interest payment.

Counsel submitted that where payments made were '*purchase price*' and not '*interest*', Section 18 is inapplicable to the transaction.

Decision

The thrust of the dispute on these grounds related to the application of **Sections 18(1)(f) and (2)** of the Income Tax Act. **Section 18(1)(f)** reads:

"Business income means any income derived by a person in carrying on a business and includes the following amounts, whether of a revenue or capital nature—

(f) interest derived by a person in respect of trade receivables or by a person engaged in the business of banking or money lending."

Section 18(2) reads:

"An amount included in business income under subsection (1) (f) or (g) retains its character as interest or rent for the purposes of any Section of this Act referring to such income."

Essentially, **Section 18(2)** means that the fact that interest is collated with other incomes does not operate to change its nature or preclude it from special provisions applying to it in Section 18.

The submission by Counsel for the Appellant is that a sale of mortgaged property is essentially a recovery of principal and interest and therefore the sums received

are at all material times principal or interest and not anything else. Counsel for the Respondent took the opposite view, submitting that consideration for the sale of mortgaged property is simply that; consideration and therefore subject to tax.

In my view, the determination of these two grounds rests on one question; how is money from the purchase of mortgaged property classified? Is it consideration or is it interest and principal? The second question, which is closely related, is whether there is a gain once the property is sold.

Classification of Proceeds from The Sale of Mortgaged Property

Counsel for the Appellant contended that the proceeds from the sale of mortgaged property is capital and interest which are exempt from tax. He relied on Section 18(2) of the Income Tax Act. Counsel for the Respondent contended that the same was consideration amenable to tax.

In my view, the starting point is to consider the nature of a mortgage. Essentially, a mortgage is a charge on land subject to the right by the mortgagor, who receives money on the security of land, to redeem the land from the charge of the mortgage by repaying the loaned sums along with any other monies payable (such as interest, arrangement fees etc). See **Halsbury's Laws Of England, Vol 32, Para 391, Page 207**.

A mortgage is a lien on land as security for the repayment of money. See **Section 2 Mortgage Act, R.L Jain v Loy Kyomugisha HCCS 98/2013** At law, a lien is right to retain the property and in some case to sell it as a means of enforcing payment. See **Re London and Globe Finance Corporation (1902) 2 Ch 416, Branch Banking Law and Practice third edition 1993 Page 94, Brandao .v. Barnett (1846) 12 CL & FIN 789, RE Cosslett (Contractors) Ltd [1998] Ch 495, CA 508G, Cooperative Bank v Christopher Kisembo HCCS 398/2002, Proscovia Kiggundu v Administrator General HCMC 40/2020, Bukenya Henry v Remode Enterprises Limited CACA 40/2014**

The lien created by a mortgage is unique; it is not exactly the same as a possessory lien which is held over movable property. Instead, the mortgagor typically retains possession while the mortgagee obtains control.

In my view, a mortgage is essentially the act of placing a non-liquid security in exchange for liquidity. If there is a failure to return the liquid asset (money) with interest, the mortgagor takes over the mortgaged asset and either liquidates it or retains it. Typically, the mortgagor liquidates it to obtain a refund of their money and interest. From this background, the mortgage allows owners of non-liquid assets to obtain money without having to sell them (especially where they don't desire so or it might be hard to find value buyers).

Accordingly, when one obtains a mortgage, they "swap" one asset for another, subject to the right to return the "new asset" (money) with interest and recover the old asset (typically land). This is the reason why the mortgaged property is expressed as a contingent asset and the loan as an actual asset; the swap is not yet complete and the bank still "owns" the loaned sums. See Matex Commercial Supplies Ltd and Another vs. Euro Bank Ltd (in liquidation) [2008] 1 EA at page 216, Maithya vs. Housing Finance Company of Kenya and another [2003] 1 EA 133, HCMA No 614 of 2012 Kakooza Abdullah vs. Stanbic Bank (U) Ltd and HCMA No. 202 of 2012 David Luyiga and Messrs Stanbic Bank (U) Ltd.

In **Steel Rolling Mills & Ors v Standard Chartered Bank (U) Limited HCMA 829/2015** the court held thus

"Section 20 (c) of the Mortgage Act 2009 provides that where the Mortgagor is in default and does not comply with the notice served on him or her under section 19, the Mortgagor may lease the mortgaged land or where the mortgage is of a lease, sublease the land. Just like the power of sale of a Mortgagee, the power to manage the property mortgaged includes the power to lease the property. The essence of any security arrangement with a bank is that the bank would be able to apply the security towards realizing its monies."

It follows that the sale of mortgaged property is really the bank swapping its non-liquid asset for a liquid one namely money and a profit. In my view, the mortgaged property is merely another form of holding its capital and interest. This is the purpose of conferring the lien upon it by law.

Accordingly, I agree with Counsel for the Respondent that in disposing the same, the bank is obtaining a refund of capital and interest which are not amenable to withholding tax in accordance with the Income Tax Act.

Difference Between Section 117(2)(b) and Section 118B(2)

A reading of **Section 117(2)(b)** shows that it exempts interest payments from withholding tax. **Section 118B(2)** charges withholding tax on the purchase of mortgaged property which, as shown above, includes interest and capital in accordance with Section 18(2) of the Income Tax Act.

I find myself unable to agree with the learned members of the tribunal. Both Sections 118B(2) and Section 117(2)(b) deal with interest payments, albeit in different circumstances; the former with regard to the liquidation of a security to recover interest and the former on the direct payment of loan interest.

Both sections cannot be reconciled because **Section 117(2)(b)** imposes a blanket exemption from withholding tax on interest payments to financial institutions while **Section 118B(2)** imposes withholding tax on the same.

In my view, whereas the two provisions engage interest at different points of contact in the transaction cycle (direct payment vis a vis recovery) they impose contradictory rules over the same category of money, namely interest, that are incapable of reconciliation.

Accordingly therefore, I find that the Section 117(2)(b) and Section 118B(2) both have an application to interest payments to financial institutions and the Tax

Appeals Tribunal erred in holding that the same were unrelated and/or did not have a cross cutting effect.

On the whole, the Appellant succeeds on grounds four and five.

Conclusion

In Conclusion, the Appellant's appeal succeeds on Grounds 2-5 and is accordingly allowed with the following orders:

(a) The Appellant's Appeal is allowed and the majority decision of the Tax Appeals Tribunal be set aside;

(b) This Court hereby makes a declaration that foreclosure by a bank takes the form and character of the loan obligations the bank was trying to recover i.e., principal and interest;

(c) This Court hereby makes a declaration that there is no withholding tax payable by a borrower when repaying the principal sum borrowed from a financial institution as this does not qualify as income received by a financial institution but a mere refund of the sums advanced by the Financial Institution.

(d) This Court hereby makes a declaration that interest income is exempt from withholding tax under section 117 (2) (b) of the income tax act

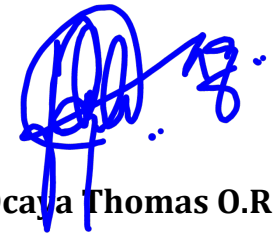
(e) This Court hereby makes a declaration that Section 118B(2) conflicts with Section 117(2)(b) in as far as it seeks to impose withholding tax on interest collected by way of sale of mortgaged property

(f) The Respondent is hereby ordered to refund to the Appellant the sum paid as 30% tax in accordance with Section 15 of the Tax Appeals Tribunal.

(g) That the Appeal having largely succeeded in part the Respondent is ordered to pay two thirds of the total cost in this Court and at the Tax Appeals Tribunal.

I so order.

Delivered electronically this 22nd day of May 2023 and uploaded on ECCMIS.



Ocaya Thomas O.R

Judge,

22nd May 2023