itTHE REPUBLIC OF UGANDA

IN THE TAX APPEALS TRIBUNAL OF UGANDA AT KAMPALA

TAT APPLICATION NO. 18 OF 2019

AFGRI UGANDA LIMITED ==========APPLICANT

VERSUS

UGANDA REVENUE AUTHORITY ==========RESPONDENT

BEFORE DR. ASA MUGENYI, DR. STEPHEN AKABWAY, MR. GEORGE MUGERWA

RULING

This is an application challenging a withholding tax assessment of Shs. 912,934,373.58 by the respondent on the applicant involving interpretation of what amounts to interest accrued or paid to a non-resident company.

The applicant is a company incorporated under the laws of Uganda. Afgri Agri Services Mauritius (hereinafter called Afgri Mauritius) is a major shareholder (99% shareholding) of the applicant. From 2014 to 2017, the holding company granted interest-bearing loans to the applicant, which were disclosed by the applicant in an Associated Party Disclosure Notice to the respondent. The respondent issued a withholding tax assessment on the applicant which was later revised to Shs. 912,934,373.58.

The following are the agreed issues:

1. Whether the applicant is liable to pay withholding tax on the interest?
2. What remedies are available to the parties?

The applicant was represented by Mr. Edward Balaba and Ms. Lucy Kemigisha while the respondent was represented by Ms. Diana Kagonyera Mulira.

The dispute between the parties revolves around the imposition of withholding tax on interest paid on inter group company loans by a non-resident parent company to a

subsidiary company. The rate of taxation is determined by the double taxation agreement between Mauritius and Uganda. The applicant contended it is not liable to pay withholding tax as it was exempt and no interest was paid to the holding company.

The applicant's witness, Sabiiti Ohionah Atulinda, its Senior Accountant, testified that the applicant was incorporated in Uganda and registered with the respondent for tax purposes. The applicant is a subsidiary of Afgri Agri Services Mauritius Limited which owns 99% of its shares. Afgri Agri Services Mauritius Limited was initially known as Afgri Investments (Uganda) Limited then it changed its name to Afgri Grain Management Mauritius Limited. The applicant is involved in managing and financing other subsidiary companies which buy and sell agricultural stock. The funds for buying the stock is obtained by the applicant who gets interest bearing loans from Afgri Mauritius. The witness testified she submitted the information in an Associated Party Disclosure form to the respondent which disclosed that the applicant received interest- bearing loans from Afgri Mauritius which was used for business operations of its subsidiaries. The respondent raised the issue of withholding tax and issued a withholding tax assessment. The applicant objected on the ground that the loans are exempt from withholding tax as the applicant has not yet paid interest. The applicant's audited statements from 2014 to 2017 show that interest is due and not yet paid to Afgri Mauritius. The witness testified that the interest has not yet been paid for the period 2014 to 2017. She also testified that the applicant and the other Afgri entities use an automated accounting system called Sage which reports interest under a pre-programmed code named 'interest paid'. She further testified that the applicant accounts for its income taxes on an accrual basis, which means the applicant reports income when it is receivable and reports expenditure when it is payable. Therefore for the years 2014 to 2017 the applicant claimed interest accrued on the loan but not yet paid as a deduction in the respective years of income. She stated that the applicant has been in a loss- making position since 2015 and therefore not been able to pay interest on its interest bearing loans. She testified that the respondent issued on 30th January 2019, 13th February 2019 and 29th March 2019 eleven third party agency notices on the applicant's accounts. The applicant's accounts were frozen. It could not receive funds from its financiers and clients. It was not able to make timely payments.

The respondent's witness, Mr. Frank Kasozi, working in its compliance division testified that that the applicant is a subsidiary of Afgri Mauritius investment Limited. The applicant is a holding company of several other companies in Uganda. On the 4th September 2017 the applicant submitted a Related Party Disclosure form declaring related party transactions for the period 2015 to 2017, interest income, amounts borrowed and loans from related parties. The respondent examined the transfer pricing records of the applicant and Afgri Mauritius Investment Limited which established that the former had been paying interest to the latter. The applicant did not declare any withholding tax on interest. The applicant's tax returns and financial statements when examined revealed that interest had been expensed. The loan agreement showed that the loan was repayable on or before 1st April 2018. After several meetings and discussions, the respondent communicated to the applicant a later revised tax liability of Shs. 912,934,373.58. Mr. Kasozi argued that the interest was sourced in Uganda.

The applicant submitted that it is not liable to pay withholding tax because it is exempt under S. 83(5) of the Income Tax Act. S. 83(5) exempts withholding tax on interest paid on debentures issued outside Uganda. The applicant submitted that the interest is to be paid outside Uganda to foreign lenders. Its witness, Sabiiti Ohionah Atulinda testified that the applicant borrows funds for buying agricultural stock and for operating expenses.

S. 83(5) of the Income Tax Act provides conditions for a debenture to be exempt which the applicant fulfilled. One condition is that debenture must be widely used. The applicant averred that the loans were widely used for the purpose of raising funds for its business in Uganda. He submitted that the Income Tax Act does not define the term 'widely issued'. However the Commissioner General issued a Practice Note which refers to the term 'widely issued' in respect of S. 83(5)(a) and not S. 83(5)(b) of the Income Tax Act which is under consideration in this matter. The Practice Note binds the Commissioner General but not the taxpayer. The applicant therefore referred to Cambridge English Dictionary which defines 'widely' to mean 'including a lot of different people'. The applicant submitted that the loans included a lot of different people. The applicant is financed by an agreement

with several parties serving several roles and different parties are involved. Therefore the debentures used to finance the applicant's business include a lot of different people and are therefore widely issued. The applicant therefore meets the conditions set out in S. 83(5) of the Income Tax Act.

Without prejudice, the applicant argued that withholding tax is not due as interest has not been paid by the applicant. The applicant contended that under S. 47(2) of the Income Tax Act withholding tax on deferred interest is only due when interest is paid. It submitted that under Black's Law Dictionary 4th Edition 'defer' means 'delay; out off; remand; postpone to a future time'. 'deferred payment' means 'payment of interest postponed to a future time; installment payment...' The applicant submitted that the loan agreement showed repayment of the loan was upon demand. The applicant's witness testified that interest on the loan has to date not yet been paid. This was because the applicant was and is still in a loss-making position. The applicant submitted that its audited financial statements for 2014 to 2017 indicate that the interest amount is not due and paid to Afgri Mauritius. Therefore the interest had been deferred. The applicant averred that the determinant of whether withholding tax is due on interest is not whether interest expense has been claimed as a deduction in the income tax returns but whether it has actually been paid as provided under S. 47(2) of the Income Tax Act.

The applicant prayed that the Tribunal awards it general damages for the huge economic and financial inconvenience caused by the respondent issuing eleven third party agency notices on its bank accounts between 30th January and 13th February 2019. The applicant cited S. 21(6) of the Tax Appeals Tribunal Act and urged the Tribunal to make orders as to damage, interest or any other remedies against the respondent. The applicant cited **Kabandize John Baptist & 21 others v KCCA** *CACA 36/2016* where the court held that the general rule regarding measure of damages is that the award is a sum of money that will put the party who has been injured in the same position as he would have been had he not sustained the wrong for which he is getting the compensation. The award of damages is at the discretion of the Tribunal.

In reply, the respondent contended that the interest paid to Afgri Mauritius was sourced from Uganda in accordance with S. 79 of the Income Tax Act. The respondent submitted that interest income derived by the applicant is chargeable under S. 83 of the Income Tax Act. The respondent submitted further that the interest income obtained by Afgri Mauritius is liable to withholding tax at a rate of 10% in light of the Mauritius – Uganda treaty. S. 120 of the Income Tax Act imposes an obligation on the person making the payment to withhold tax from payment.

The respondent submitted that *Black's Law Dictionary* 8th Edition page 4944 defines withholding tax as the practice of deducting a certain amount from a person's salary, income, wages, dividends, winnings or other income for tax purposes. The respondent further submitted that S. 2(kk) defines interest to include any payment made under a debt obligation. S. 83 of the Income Tax Act provides that a tax is imposed on every non-resident person who derives any interest from sources in Uganda. S. 79 of the Income Tax Act provides that income is said to be derived from sources in Uganda where the payer is a resident person or the borrowing relates to a business carried on in Uganda.

The respondent contended that the Income Tax Act defines a debenture to include any stock, mortgage, loan, loan stock or any similar instrument acknowledging indebtedness, whether secured or unsecured. Black's Law Dictionary 9th Edition page 460 defines a debenture as a debt secured by the debtor's earning power, not by a lien or any specific asset. The respondent further contended that the applicant presented a collateral management agreement, the fact that stock was availed as collateral disqualifies the applicant's loan as a debenture.

The respondent submitted that S. 83(5) of the Income Tax Act which provides that interest paid by a resident company in respect of debentures is exempt from tax where the following conditions are satisfied (a) the debentures were issued by the company outside Uganda for the purposes of raising a loan outside Uganda. (b) the debentures were widely issued for the purpose of raising funds for use by the company in a business carried on in Uganda or the interest is paid to a bank or a financial institution of a public character.

(c) the interest is paid outside Uganda. The respondent contended that the interest paid by the applicant is not exempt as it did not meet all the three conditions.

The respondent argued that the applicant's loans were not widely issued as envisaged under the law and did not meet the 'public offer test' as articulated in the Practice Note of 24th July 2018. According to the test, the respondent argued, that the loan ought to have been issued to (a) a reasonable number of people operating in a capital market, (b) to several investors with a history of previous acquisition of debt instruments or debentures; (c) as a result of negotiations for the loan in a public forum used by financial markets dealing in debt instruments; or (d) to a dealer, manager or underwriter for the purpose of placement of the debt instrument. The respondent contended that Afgri Mauritius does not provide financing to unrelated parties and hence fail the public offer test. The respondent contended that there is no evidence that Afgri Mauritius offers loans on capital markets or operates with a reasonable number of people. It contended that the applicant and the other group companies did not receive funding from third parties.

In respect of S. 79 of the Income Tax Act, the respondent contended that the income was derived from sources in Uganda. The respondent submitted that the property which was used as collateral for the loan was based in Uganda. The business for which the loan was advanced was in Uganda. The respondent submitted that the applicant was expensing the interest in its financial statements which were signed by its directors and reflect a true position of the company's affairs.

As regards payment, the respondent contended that payment is defined in S. 2(xx) of the Income Tax Act to include any amount payable. The respondent submitted that payable could be defined in two different ways; that which is due or must be paid; and that which may be paid or may have to be paid. The respondent contended that debt became due and payable once it featured in the books of accounts. The respondent contended that the term 'paid' was well described in **Kenya Revenue Authority v Republic (Ex parte: Fintel Ltd.)** *Civil Appeal 311 of 2013* to include "... Distributed, credited, dealt with or deemed to have been paid in the interest or on behalf of a person and; "pay", "payment"

and "payable" have corresponding meanings." The respondent submitted that interest paid or payable is one and the same thing. The respondent submitted that the applicant's interest when charged though not paid, remained a debt which was recognized in the applicant's book of accounts. When the interest was expensed in the profit and loss account, it reduced the profit chargeable as corporation tax. The respondent argued that any amount expensed in the books of accounts is "paid" within the meaning of S. 2 of the Income Tax Act.

As regards damages suffered by the applicant, the respondent submitted that the applicant has failed to prove that it suffered loss. The respondent having established that the applicant failed to withhold tax due on loan interest it cannot claim general damages for failing to pay dues to the Government.

Having listened to the evidence and read the submissions of the parties, the Tribunal gives its ruling as below:

The applicant is a limited company incorporated in Uganda. Afgri Agri Services Mauritius (called Afgri Mauritius) is a major shareholder (99% shareholding) of the applicant. Afgri Agri Mauritius was initially Afgri Investments (Uganda) Limited. It changed its name to Afgri Grain Management Mauritius Limited, then to its current name. The applicant entered into loan agreements with Afgri Mauritius before it changed its names. The purpose of the loans was to provide working capital to the applicant. The loans were repayable either on or before 1st April 2018. The borrower would repay the amount on demand. Sometime in 2017, the applicant in an Associated Party Disclosure disclosed the loans from the holding company. The respondent issued it a revised withholding tax assessment of Shs. 912,934,373.58 which is the subject of this dispute.

The respondent contended that Afgri Mauritius was obtaining interest from the loans it gave to the applicant. The Income Tax Act imposes tax on activities of non- resident persons involving international payments. S. 83(1) of the Income Tax Act provides:

"Subject to this Act a tax is imposed on every nonresident person who derives any dividend, interest, royalty, rent, natural resource payment, or management charge from sources in Uganda"

The applicant contended that the interest given to Afgri Mauritius was not sourced in Uganda. Income is derived from sources in Uganda under S. 79(k) of the Income Tax Act which reads:

"interest where –

(i) the debt obligation giving rise to the interest is secured by immovable property located, or movable property used, in Uganda;

(ii) the taxpayer is a resident person; or

(iii) the borrowing relates to business carried on in Uganda."

It is not in dispute that the applicant is a resident person. The loans were to provide working capital for the applicant which carried on business in Uganda. Therefore any interest payable or paid would be or is sourced from Uganda.

The applicant contended that the interest payable or paid to Afgri Mauritius is exempt under S. 83(5) of the Income Tax Act, which reads:

"Interest paid by a resident company in respect of debentures is exempt from tax under this Act where the following conditions are satisfied –

(a) the debentures were issued by the company outside Uganda for the purpose of raising a loan outside Uganda;

(b) the debentures were widely issued for the purpose of raising funds for use by the company in a business carried on in Uganda or the interest is paid to a bank or a financial institution of a public character; and

(c) the interest is paid outside Uganda."

The applicant argued that the interest paid or payable on the loans from Afgri Mauritius were debentures which satisfied the conditions in S. 83(5)

The applicant contended the loan it obtained was a debenture. A debenture is defined by S. 2(r) of the Income Tax Act to include "any debenture stock, mortgage, mortgage stock, loans, loan stock or any similar instrument acknowledging indebtedness, whether secured or unsecured;" The said definition is not exhaustive. A reading of S. 2(r) shows that a

debenture includes a loan. However S. 83(5) of the Income Tax Act limits exempt interest to debentures. One may ask whether there are loans which are not debentures. Black's Law Dictionary 10th Edition page 486 defines a debenture as "a debt secured only by the debtor's earning power, not by a lien on any specific asset ... 2. Acknowledging such a debt ... 3. A bond that is backed only by the general credit and financial reputation of the corporate issuer..." As of now, it is not clear why S. 83(5) was limited to debentures as it is not easily defined. Since S. 2(r) considers a loan as a debenture the Tribunal will consider the loans between the applicant and Afgri Mauritius as debentures.

The Tribunal has to consider whether the conditions in S. 83(5) were satisfied by the debenture between the applicant and Agfri Mauritius so as to be exempt. The conditions in S. 83(5)(a) and 83(5)(c) do not seem to be in contention. That is, the applicant issued the debentures outside Uganda to raise a loan. Afgri Mauritius is a non-resident company. The interest paid or payable by the applicant was payable to a company outside Uganda. The debentures satisfied the conditions in S. 83(5)(a) and S. 83(5)(c) of the Income Tax Act.

S. 83(5)(b) of the Income Tax Act, which is in contention, requires a debenture to be 'widely issued'. The Income Tax Act does not define the term "widely issued." The Tribunal agrees with the applicant's definition of "widely" to mean "a lot of different people". However the applicant omitted to define "issue." *Black's Law Dictionary* 10th Edition defines the term "issue" to mean "to send out or distribute officially". Companies are known to issue debentures to the public as a means of raising working capital. Unlike shares which are issued to a limited number of people by private companies debentures are issued to the public widely. Unlike shares where a shareholders gets a dividend, a debenture holder gets interest until the loan is paid off. A share is a unit of investment while a debenture is a unit of loan. Therefore that portion of S. 83(5)(b) that requires a debenture to be issued widely, meant that it has to be issued to different individuals, that is the public as opposed to a loan that is between two parties. Debentures can be issued to the members of the public unlike a loan which is inter-parties. That is why S. 83(5) is concerned with debentures and not loans. The debenture between the applicant and

Agfri Mauritius cannot be considered as one that was widely issued. It is between only two parties, actually one debenture holder, Agfri Mauritius. Therefore the debentures or loans between the applicant and Afgri Mauritius fails to meet the condition in S. 83(5)(b) of the Income Tax Act.

The Tribunal cannot leave the issue of the term "widely issued" without discussing the Practice Note of 24th July 2018 issued by the Commissioner General. The Practice Note provides that for interest paid by a resident person to be considered exempt, the public offer test must be met. The debenture loan must have been issued to (a) a reasonable number of people operating in a capital market, (b) to several investors with a history of previous acquisition of debt instruments or debentures; (c) as a result of negotiations for the loan in a public forum used by financial markets dealing in debt instruments; or (d) to a dealer, manager or underwriter for the purpose of placement of the debt instrument. The Tribunal notes that the said conditions are not in the Income Tax Act. The Commissioner General does not have powers to legislate; that is the duty of Parliament. The Tribunal therefore agrees with the applicant that the said Practice Note does not bind taxpayers.

The Tribunal having found that the debentures issued by the applicant do not satisfy the conditions in S. 83(5) of the Income Tax Act, meaning that they are not exempt, it has to determine whether the applicant was required to withhold tax on the interest paid to Afgri Mauritius. S. 120 of the Income Tax Act requires "Any person making a payment of the kind referred to in Section 83, 85 or 86 shall withhold from the payment the tax levied under the relevant Section."

The applicant contended that though the loan agreement provided for interest it had not paid any interest to Agfri Mauritius, which the respondent disputes. The respondent contends that the withholding tax is due as soon as the interests accrues or becomes payable. This raises the question: At what point in time should withholding tax have risen? Is it at the time of accrual or remittance? S. 47 of the Income Tax Act provides for payment of taxes on debt obligations with discount or premium. It reads:

"(1) Subject to subsection (2), interest in the form of any discount, premium, or deferred interest shall be taken into account as it accrues.

(2) Where the interest referred to in subsection (1) is subject to withholding tax, the interest shall be taken to be derived or incurred when paid."

The word "defer" is defined in Black's Law Dictionary 10th Edition page 513 to mean "To postpone; to delay until a later date". The interest payable by the applicant was payable on later dates, making S. 47(1) applicable. According to S. 47(2) which is specific and overrides the general provision, where interest is subject to withholding tax, interest is taken to be derived when it is paid. This means where interest is not subject to withholding tax it is taken into account as it accrues. However withholding tax is payable on international payments when it is paid.

The respondent relied on S. 2(xx) which reads: ""Payment includes any amount paid or payable in cash or kind, and any other means of conferring value or benefit on a person." The respondent argued that payment includes an amount that is payable. According to the respondent, withholding tax becomes due when the interest accrues. The Tribunal does not agree with that.

S. 2 of the Income Tax begins with: "In this Act, unless the context otherwise requires..." The context in S. 47(2) requires withholding tax to be charged when interest is paid on international payments. In **Cooper Motors v Uganda Revenue Authority** *TAT 67 of 2018*, the Tribunal stated:

> "The Tribunal notes that S. 2 of the Income Tax Act that defines payment is an interpretation section. The word payment is defined to include payment of any amount paid or payable in cash. In essence when interest accrues WHT becomes payable. On the other hand, S. 47(2) states that interest subject to withholding tax shall be taken to be derived or incurred when paid. In other words WHT tax on interest accrues when the interest is paid. If S. 2 of the Income Tax Act had been read as a whole one would have noted that S. 2 begins with "In this Act, unless the context otherwise requires..." S. 2 of the Act applies until the context so requires. The context in S. 47(2) requires that WHT on interest be withheld when it is paid. S. 2 is in consonance with S. 47(2). It does not conflict

with S. 47(2) of the Act. It gives room for S. 47(2) to apply. It is just a question of reading the whole Section without limiting oneself to only the definition of the term "payment"."

This was reiterated in **ATC Uganda Limited v Uganda Revenue Authority** TAT 17 of 2019. Therefore the Tribunal holds that withholding tax is charged on interest when it is paid and not when it accrues. Furthermore, a specific provision in a statue overrides a general provision. S. 47(2) which is specific overrides S. 2 of the Income Tax Act.

The respondent cited **Kenya Revenue Authority v Republic (Ex parte: Fintel Ltd.)** (supra) where the words whose construction gave rise to the appeal were "paid" and "upon payment". The words whose construction which give rise to this application are "payable" or "accrued" and "paid". The words in the Kenyan case are not synonymous with the words in this application. That is, the word "upon payment" is not similar to "accrued" or "payable". The statutes are not in *pari material.*

Having stated that withholding tax is due when interest is paid the Tribunal has to determine whether interest was ever paid. The applicant contends that it did not pay any interest to Afgri Mauritius, which the respondent disputes. The loan agreements do not specify the mode of payment by the applicant of the interest. It is only the agreement of 2016 that states that the loan is repayable on or before 1st April 2018. It also states that in case the borrower fails to repay the amount advanced by the lender within 7 days of being requested to repay the lender will add an additional margin on the monthly interest. This implies that the loan and or interest may be payable on demand. Apart from that, the rest is left to the imagination of the revenue collecting authority to discern whether interest was paid. The Tribunal is mindful that the loan in issue was an intergroup company arrangement. The applicant and Afgri Mauritius are free to agree on the mode of payment.

A perusal of the financial statements of the applicant for the financial periods 2014 to 2017 show that the applicant was expensing interest as financial costs. For the year ending 31st March 2014, at page 18 of the trial bundle, it shows interest expense as Shs. 597,550,000 and on page 21 the amount due to Afgri Mauritius is 15,592,798,000; for year ending 31st March 2015 at page 40 interest expense is Shs. 1,099,503,000; for the

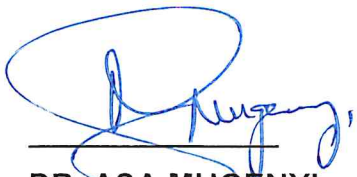
year ending 31st March 2016 at p. 65 interest expense is Shs. 2,423,494,000; for the year ending 2017 at page 103 interest expense is shs. 4,039,008,000. The Tribunal agrees with the respondent that financial statements are signed by the directors of a company and reflect the true position of a company's financial affairs. None of the directors of the company testified during the trial to contradict what was in the statement. The evidence of Sabiiti Phionah Atulinda an accountant with the applicant cannot override a statement signed by the directors as they are the ones entrusted to run the affairs of a company. Notwithstanding that, her testimony was that the interest accrued by the applicant was reported under a pre-programmed code 30302 as 'interest paid'. However a perusal of the financial statements does not mention the pre-programmed code in the notes.

The financial statements are collaborated by the income tax returns the applicant filed with the respondent. For the year ending March 2014 at page 236 of the trial bundle the applicant expensed interest as Shs. 597,550,000; for the year 2015 at page 258 interest expense is Shs. 1,099,503,000; for the year 2016 at page 284 interest expense is shs. 2,423,494,000; for the year 2017 at page 300 interest expense is Shs. 4,039,008,000. The representations in both the financial statements and income tax returns indicate that applicant paid interest to Agfri Mauritius. The result of the applicant's representation, expensing interest as deductible allowances meant that it paid less taxes. Where a tax payer makes representations, which another party acts on, as in this case the revenue collecting body resulting in it paying less taxes, the taxpayer cannot turn around and deny the representations. The doctrine of estoppel would come into play. Therefore if the interest was a deductible expense as it was paid then the applicant ought to have withheld tax from Agfri Mauritius. The applicant cannot have its cake and eat it. If it is in the income tax returns and the financial statements, the Tribunal cannot hold that what it stated therein is not correct. Therefore the Tribunal finds that the applicant paid interest to Afgri Mauritius which was liable to withholding tax.

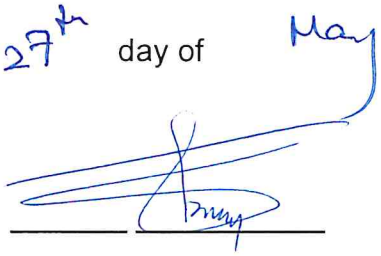
Having found that the applicant was liable to pay withholding taxes it is not necessary for the Tribunal to discuss whether it is entitled to general damages for the third party notices served on its bankers. Where the respondent is carrying out its statutory duty diligently

and taxes were due, it is difficult for the Tribunal to award general damages against it. The application is dismissed with costs to the respondent.

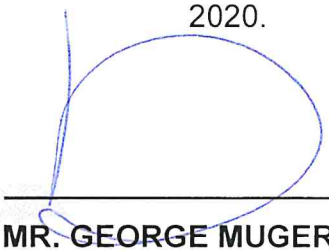
Dated at Kampala this 27th day of May 2020.



DR. ASA MUGENYI
CHAIRMAN



DR. STEPHEN AKABWAY
MEMBER



MR. GEORGE MUGERWA
MEMBER