THE REPUBLIC OF UGANDA

IN THE TAX APEPALS TRIBUNAL AT KAMPALA

TAT APPLICATION NO. 67 OF 2018

THE COOPER MOTOR CORPORATION (U) LTD ==========APPLICANT

V

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

BEFORE DR. ASA MUGENYI, MS. CHRISTINE KATWE, MR. SIRAJ ALI

RULING

This ruling is in respect of an application challenging the respondent's computation of Withholding Tax (WHT) in respect of interest on related parties' loans.

The applicant, a Ugandan registered company, supplies motor vehicles, spare parts and provides motor vehicle after sale services to its customers. The applicant borrowed monies from related parties which charged interest. An audit by the respondent on the applicant for the period January 2013 to December 2016, raised income tax, Value Added Tax (VAT) and Withholding Tax assessments of Shs. 3,018,722,532. On 7th August 2018 the applicant objected to the said assessments and an objection decision revising the tax liability to Shs. 2,935,562,315/= was issued by the respondent on 1st November 2018.The applicant paid Shs. 2,404,641,572 leaving a balance of Shs. 503,230,799 unpaid. The said amount is due to penal tax the respondent contends that the applicant ought to pay for late payment of WHT on interest.

The following issues were framed.

1. Whether the period considered by the respondent when computing withholding tax arising from the interest on related parties' loans was lawful?
2. Whether the applicant is entitled to the remedies sought?

The applicant was represented by Ms. Rebecca Nakiranda and the respondent by Ms. Hilda Bakanansa.

This dispute revolves on the period to be taken into account in computing WHT on interests paid on loans between the applicant and related companies. The respondent contends that the applicant ought to pay penalties on WHT it paid purportedly late. The Tribunal has to determine when WHT should have been charged and whether penal was due. Both parties adduced evidence and filed submissions to show when the interest should have incurred and payable.

The applicant's sole witness Mr. Joseph Sserwada, testified that the applicant is wholly owned by CMC Holding Limited, a company incorporated and domiciled in Kenya. From December 2013 to January 2016, CMC Holdings Ltd supplied motor vehicles and spare parts to the applicant. The said company gave loans to the applicant and charged interest on unpaid balances. On 31st March 2014, CMC Holdings Ltd was acquired by Al-Futtaim Group of Dubai in a 100% acquisition. Following the said acquisition, the shareholders of Al-Futtaim Group agreed to take over the debt under an arrangement of recapitalization. As a result the debt by the applicant was converted to equity in 2017. In June 2018, the respondent carried out an audit on the applicant for the period January 2013 to December 2016 and a disputed unpaid WHT penal liability of Shs. 503,230,799 arose. The applicant contended that the computation by the respondent was from the time interest accrued on the applicant's accounts and not interest was paid by conversion of the applicant's debt into equity.

The respondent's witness Ms. Damalie Nguna, its tax compliance officer testified that an issue audit on the applicant reviewed its income tax returns for the period 2013 to 2016 and found interest expenses which arose from related party loans. Interest had been charged on loans from related foreign companies namely CMC Holdings Limited, CMC Motors Group Limited and Hughes Motors (Tanzania) Limited. She contended that this implied that WHT of 2,757,771,459/= for the period 2013-2016 was due on the interest paid. She contended that this amount was arrived at by computing the WHT tax due

from the time the interest on the intercompany balances had been expensed by the applicant in its annual tax returns. The accrual basis of accounting dictated that withholding tax became due and payable the moment interest accrued on the outstanding intercompany loans.

In its submissions, the applicant contended that the loans and interests on related parties' loans were deemed paid on the re-capitalization of the applicant in December 2017 which was the month WHT on the interest due arose. The applicant submitted further that the period to be reckoned in computing the WHT was from January 2018 to June 2018, a period of 6 months. The applicant submitted that under S. 47(1) of the Income Tax Act, interest is taken into account as it accrues, however, as an exception under S. 47(2) interest is taken to be derived or incurred when paid. The applicant submitted that penal interest ought to have been computed starting from the period that interest was actually paid, up to the date when the administrative assessment was issued namely from December 2017 to June 2018.

In reply, the respondent submitted that S. 3 of the Income Tax Act defines WHT to mean any tax a withholding agent is required to deduct from payment to a payee. S. 2 of the Act defines payment to include any amount paid or payable in cash or kind, and any other means of conferring value or benefit to a person. S. 25(1) of the Income Tax Act provides for interest being allowed as a deduction. The respondent submitted that the applicant failed to withhold amounts due on loan obligations while he was treating the interest as a deductible expense.

The respondent argued also that payment of WHT is subject to S. 85 of the Income Tax Act which deals with taxation of payment to non-resident contractors or professionals. The respondent argued that S. 87(1) of the Act is to the effect that the liability of a non-resident person is satisfied after the tax payable has been withheld by a withholding agent under S. 120 of the Act and paid to the Commissioner under S. 123. S. 120 provides for WHT levied on an international payment. The respondent contended that the said Section should be read together with S. 2 of the Income Tax Act which defines

the term "payment" to include any amount paid or payable in cash or kind and any other means of conferring value or benefit on a person. The respondent submitted that the definition under S. 2(xx) extends to S. 47(2) and any construction of the term "paid" under S. 47(2) should be read as including amounts payable. The definition of payment includes amount paid or payable in cash. The respondent submitted that under the accrual basis of accounting, interest is taken into account as it accrues or becomes due and not when actual payment has been made. Therefore the applicant ought to have paid WHT on the interest as soon as it accrued and not when actual payment was made through the conversion of the applicant's debt into share capital.

The respondent submitted what amounts to payment can only be determined from the books of accounts. The applicant expensed interest in its financial statements and annual tax returns as they accrued. The applicant having expensed interest in its books of account took benefit by the reduction of its taxable liability and cannot now claim that no payment had been made.

In rejoinder, the applicant argued that S. 47(2) of the Income Tax Act ought to apply in preference to S. 2(xx) as the former is a specific provision while the latter is a provision of general application. The applicant relied on the rule of statutory interpretation known as "*generalia specialibus non derogant*" which states that when a matter falls under any specific provision then it must be governed by that provision and not by the general provision.

Having heard the evidence and read the submissions of the parties, this is the ruling of the Tribunal.

The applicant deals in motor vehicles, spare spares and provides after sale services. The applicant was wholly owned by CMC Holdings Limited which gave it a loan. It was agreed that the applicant pay interest on the said loan. On 31st March 2014, CMC Holdings Ltd was acquired by Al-Futtaim in a 100% acquisition. Following the said acquisition the shareholders of Al-Futtaim Group purportedly agreed to take over the

debt purportedly under an arrangement of recapitalization. As a result the debt was purportedly converted to equity in 2017. The respondent audited the applicant's books of accounts. The applicant had in the financial statements expensed the interest payable qualifying them as a paid amount. The respondent contended that the applicant ought to have withheld taxes on the dates the interest accrued and not the date of payment that is the time of conversion of the loan into equity. The applicant paid WHT taking into consideration the time of payment tax but objected to the penalties the respondent contends arose from late payment. The following table shows the payment made and the penalties due.

Table 1.

PERIOD	2013	2014	2015	2016	TOTAL
Interest paid on related party loans	2, 051, 617,000	2,701,224,000	5,776,305,000	2,890,739,000	13,419,885,000
15% WHT	307,742,550	405,183,600	866,445,750	433,610,850	2,012,982,750
Months delayed (respondent)	39	27	15	3	
Months delayed (applicant)	6	6	6	6	
Penal interest (respondent)	240,039,189	218,799,144	259,933,725	26,016,651	744,788709
Penal interest (applicant)	36.929,106	48,622,032	103,973,490	52,033,302	241,557,930
Disputed tax liability					503,230,779

From the table it is clear that there is a dispute in respect of the period penal tax arose. The applicant paid interest worth 13,419,985,000 and paid WHT of Shs. 2,012,982,750 excluding penal interest. The respondent computed the penal tax at Shs. 744,788,709 while the applicant at Shs. 241,557,930 which it paid leaving a balance of Shs. 503,230,779 which is the disputed tax. The dispute arose as to when the applicant should have withheld tax.

The applicant contends that it was required to pay interest to CMC Holding Limited which is a non- resident foreign company. WHT on international payments is imposed by S. 120 which provides that "Any person making a payment of any kind referred to in Section 83, 85 or 86 shall withhold from the tax levied under the relevant section. The relevant Section would be S. 83 which reads

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

It is not in dispute that the applicant was supposed to withhold tax on interest paid to related parties. The dispute between the parties arises as to when should the WHT have been paid or due. The applicant contends that when Al-Futtaim acquired CMC holding Limited it converted the debt into equity and that was when the interest was paid. That is when WHT ought to have been paid. The respondent contends that WHT on interest is due on the date interest accrues in the loan arrangement.

S. 47 of the Income Tax Act deals with debt obligations with respect to discount and premium. S. 2 of the Income Tax Act defines a debt obligation to mean an obligation to make a repayment of money to another person including accounts payable. S. 47 reads:

"(1) Subject to subsection (2), interest in the form of discount, premium, or deferred interest shall be taken 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."

According to the applicant, S. 2 implied interest was deferred till when its debt was converted into equity by Al- Futtaim. The respondent contended that S. 2 of the Act defines payment to include any amount paid or payable in cash or kind, and any other means of conferring value or benefit on a person. According to the respondent interest may became due when it is payable.

Both parties noted that the word 'paid' is not defined in the Income Tax Act. While the respondent relied on S. 2 to use the interpretation of "payment" to define paid, the applicant relied on S. 47(2) of the Income Tax Act. S. 47(2) is to effect that payment of WHT should be when interest is paid. While the applicant argued that where a statute is specific then the general rule does not apply, the respondent argued that a Statute should be read as a whole. To the respondent when reading S. 47(2) of the Act, S. 2 of the Act should also be taken into consideration. S. 2 is to the effect that payment of taxes may be effected when interest is payable. Here we have two rules of statutory

interpretation conflicting and giving different effects. The applicant argued that where there is an ambiguity in the law the taxpayer should be given the benefit of the doubt.

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". The Section is clear and should be given the effect it intended without the need of playing gymnastics with the various rules of statutory interpretation. A careful reading of both Sections shows that they are in harmony. Therefore the reading of payment of WHT in S. 47(2) prevails that is because the context so requires.

The respondent contended that CMC holding Limited was a non-resident company and therefore the payment of interest to it by the applicant was an international payment governed by S. 120 of the Income Tax Act. S. 120 of the Act reads that 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 relevant Section in this application is 83 which reads:

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

It is clear that the WHT is charged on interest derived by a non-resident person in Uganda. Under S.120 tax should be paid on an international payment under the relevant Section. In this case the relevant Section is also S. 47 which requires withholding tax to be charged when interest is paid.

Having stated that WHT is due when interest is paid, the Tribunal has to ask itself when interest was paid by the applicant in this matter. The applicant contends that it paid the interest when its debt was converted into equity when Al-Futtaim Group acquired CMC Holdings Limited. The applicant attached two resolutions, exhibits A8 and A9 showing increase of share capital of the applicant from Shs. 1,000,000,000 to Shs. 41,691,500,000 and an allotment of the said increase of share capital to Al- Futtaim respectively. The said resolutions do not mention about any conversion of the debt owed by the applicant to CMC Holding Limited into equity. The resolutions filed by the applicant are not dated. It is not clear when the increase of share capital was made. A casual reading of the resolutions indicates that Al- Futtaim after purchasing CMC Holdings Limited decided to inject capital into the applicant. It is difficult to understand how if the applicant owed CMC Holding Limited monies how that debt is settled by Al Futtaim being allotted shares. There is evidence lacking in respect of the debt, the acquisition of CMC Holding by Al Futtaim and the conversion of the debt into equity. That link is missing and it was left to the realm of speculation. There is no evidence as to the monies that were borrowed by the applicant from CMC Holding Limited, the interest due and the debt outstanding at the time of acquisition of CMC Holdings Limited and the conversion of the debt into equity.

The respondent filed a supplementary trial bundle which had the applicant's annual and Financial Statements for the years ending 31st December 2013, 2014, 2015 and 2016. The applicant did not object to them. In the year 2013, the amount due to related parties was Shs. 22,186,776,000. The report states that balances of 90 days to CMC Motors Group Limited bore interest of 24% p.a. In the said statement the debt owed to CMC Motors Group Limited is Shs. 22, 056,018,000 and to CMC Holdings Limited it is Shs. 130.758,000 which are different legal entities. The debt to the former attracts interest while to the latter the Statement is silent. The applicant's Financial Statement of 2014 show the amount owed to related parties was CMC Motors Group Limited Shs. 30,934,797 and CMC Holding Limited Shs. 681,000,000. The Statement shows that balances over 90 days owing to CMC Motors Group limited bear interest of 12% p.a.

The Financial Statement ending 31st December 2015 shows the amount due to related parties is CMC Group Limited Shs. 58,833,992,000. CMC holding Limited is not on the list of those who had amounts due to it. The said report indicates balances over 90 days to CMC Motor Group Limited bear interest of 12% p.a. The Financial Statement of 2016 shows that the amount due to related parties is Shs. 64,309,664,000 due to CMC Motors Group Limited. CMC Holding Limited is not on the list of companies owed monies. The report indicates that balances over 90 days owing to CMC Group Limited attract interest of 12 p.a. until May 2016 after which no interest was charged. It is not difficult to discern that when Al Futtaim acquired CMC Holdings Limited around 2017 there was no debt owed by the applicant to CMC Holdings Limited. Therefore the purported conversion of the applicant's debt to CMC Holding Limited is not borne by the evidence adduced. It also not difficult to discern that the loan that was bearing interest were those CMC Motors Group Limited and not those of CMC Holding Limited. Apart from the financial statements there is no other evidence to show when the interest to CMC Motor Group Limited was paid. One cannot fail to notice that there are glaring inconsistencies in the applicant's evidence. The story of the applicant does not add up. The Tribunal cannot fault the respondent for relying on the financial statements to indicate the time when the interest was paid.

Under S. 25 of the Income Tax Act a person is allowed a deduction for interest incurred during the year of income in respect of a debt obligation to the extent the debt obligation has incurred by the person. The said financial statement show that the applicant expensed interest as a deduction. The financial statement of 2016 shows interest charged on intercompany balances as Shs. 2,890,739,000 for 2016 and Shs. 5,776,305,000 for 2015. The financial statement for 2014 shows that the applicant expensed interest charged on company loans as Shs. 2,701,224,000 for 2014 and Shs. 2,051,617,000 for 2013. These are the expenses in the table 1. As a result of the expensing of the said interest as allowable deductions, the taxes payable by the applicant reduced in the said years. When an applicant expenses the said interest it is only logical that it should withhold tax on the interest income.

Under S. 91 of the Income Tax Act, the Commissioner has powers for the purpose of determining liability under the Act to re-characterize a transaction that was entered into as part of a tax avoidance scheme and disregard a transaction that does not have substantial economic effect. From the financial statements adduced in evidence the applicant was paying interest on monies owed to CMC Motor Group Limited and not CMC Holding limited. Therefore whether CMC Holding Limited converted its debt into equity, this had no substantial effect. The attempt by the applicant to declare the interest it expenses in its financial statement as a debt that was converted into equity is a tax avoidance scheme which the Commissioner re-characterized. The Tribunal will not fault the exercise of his discretion. It is a transaction that has no substantial effect and can be disregarded.

Lastly, the applicant did not tender in the loan agreements between the applicant and the related parties at the trial. The transactions between the applicant and the CMC Group involved an intra-group finance arrangement. The respondent ought to have examined the applicant's third party funding to determine whether the interest rates given to the applicant were at arm's length. It ought to have understood the creditworthiness of the applicant on a stand-alone basis, which it did not do. However this does not affect the outcome of this application.

Taking the above facts into consideration, the applicant has not discharged it burden of proof under S. 18 of the Tax Appeals Tribunal. It did not prove that the assessment was wrong or the tax authority should have decided it differently. This application is dismissed with costs to the respondent.

Dated at Kampala this 17th day of March 2020.

DR. ASA MUGENYI
CHAIRMAN

MS. CHRISTINE KATWE
MEMBER

THE REPUBLIC OF UGANDA

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TAT APPLICATION NO. 67 OF 2018

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V

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

RULING

I have had the opportunity of reading the ruling of my colleagues. The following is my ruling.

The first issue was: Whether the period considered by the respondent when computing withholding tax arising from the interest on related party loans was lawful? It would seem that both parties agree that interest ought to be taken into account as it accrues. The point of dispute between the parties lies in the assertion by the applicant that an exception to this rule has been created by S. 47(2). S. 47 states as follows;

> "(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 respondent's position is that the term 'payment' has already been defined under S. 2(xx), the interpretation section of the Income Tax Act. It is the respondent's contention that S. 2(xx) should be applied in preference to S. 47(2). S. 2(xx) states as follows: "Payment includes any amount paid or payable in cash or in kind and any other means of conferring value or benefit on a person".

It is clear that the two provisions are in conflict. The effect of S. 2(xx) is that the applicant's liability to withhold tax on the interest due on the sums owed to its related parties arose, the moment interest accrued and became payable. The effect of Section 47(2) on the other hand is that the applicant's liability to withhold tax on the interest arose when actual payment of the interest had been made not when the interest

accrued. The dispute between the parties therefore boils down to which of the two provisions should be applied in determining the meaning of the term "paid" as used under section 47(2).

In support of its contention that S. 47(2) should apply in preference to S. 2(xx), the applicant relied on the rule of statutory interpretation known as "*generalia specialibus non derogant*. We will proceed to determine whether this rule of statutory interpretation applies to the facts of this application. The following excerpt from ***Sullivan, R. Sullivan and Driedger on the Construction of Statutes,*** 4th Edition (London Butterworths, 2002) at page 273 provides a brief but concise overview of this rule.

> "When two provisions are in conflict and one of them deals specifically with the matter in question while the other is of more general application, the conflict may be avoided by applying the specific provision to the exclusion of the more general one. The specific prevails over the general; it does not matter which was enacted first. This strategy for the resolution of conflict is usually referred to by the latin name "generalia specialibus non derogant". The English term "implied exception" is adopted ...for in effect, the specific provision implicitly carves out an exception to the general one..."

The decision of Crabbe JA, in the East African Court of Appeal in **Dhanesvar v Mehta vs. Manilal M. Shah** *[1965] 1 EA 321* stated:

> *"The rule is that wherever there is a particular enactment and a general enactment in the same statute, and the latter taken in its most comprehensive sense, would overrule the former, the particular enactment must be operative, and the general enactment must be taken to affect only the parts of the statute to which it may properly apply....."*

From the above excerpts it is clear that for the above rule to apply the following conditions must be fulfilled. Firstly, there must be two different provisions in the same statute, both of which deal with the same matter. Secondly, one of these provisions should be of a general nature and the other of a specific nature. Thirdly, these provisions should be in conflict with each other so that each provision should lend itself to a different interpretation. In the instant case both section 2(xx) and section 47(2) of the Income Tax Act deal with the term "payment". Section 2(xx) is an enactment of a general nature because it relates to payments generally, while section 47(2) is an enactment of a

specific nature because it specifically determines the point at which interest subject to withholding tax is deemed to have been derived or incurred.

It is also clear from a perusal of both provisions that they are in conflict with each other. Section 2(xx) is wide enough to include the accounting concept of accrual through the use of the phrase "*amounts payable*" while section 47(2) is narrow and excludes the concept of accrual by the use of the word "paid". The rationale for the use of this rule is stated as follows in **Potter's Dwarris** at page 273; "The meaning of which is that when the law descends to particulars such more special provisions must be understood as exceptions to any general rules laid down to the contrary..." The following excerpt from the decision of Lord Donovan in **Mangin v Inland Revenue Commissioner** *[1972] AC 739* provides guidance on the construction of tax statutes.

> "...the words are to be given their ordinary meaning, looking only at what is clearly said. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used...in that process, the court is under a duty to adopt an approach that produces neither injustice nor absurdity; in other words, an approach that promotes the purpose or object underlying the particular statute albeit that such purpose or object is not expressly set out therein."

Relying on the guidance above it is apparent that the more specific provisions of S. 47(2) were intended to create an exception to the general provisions of section 2(xx).The approach that promotes the purpose and object of section 47(2) is to apply section 47(2) to the exclusion of section 2(xx) in interpreting the meaning of the term "paid" as used under section 47(2). This is borne out by the fact that under section 47(1) the concept of accrual is expressly provided for but under section 47(2) an exception is created in respect of interest to which withholding tax applies. This can only have been deliberate. It is apparent that it was the intention of the legislature that no hardship should be occasioned to withholding tax agents by requiring them to withhold tax in respect of interest payments which have not yet been remitted. In the absence of S. 47(2) a withholding agent's inability to pay interest would be compounded by unnecessary borrowings or penalties. The application of S. 2(xx) would in this case produce injustice. This could hardly have been the intention of the legislature.

For the above reasons and after much consideration I am of the opinion that the period considered by the respondent in computing withholding tax arising from the interest on related party loans was unlawful. I accordingly hold that the period which should apply is the period of six months beginning January 2018 to June, 2018.

In my considered opinion, I would have allowed this application with costs.

Dated at Kampala this 17th day of March 2020.

MR. SIRAJ ALI
MEMBER