

THE REPUBLIC OF UGANDA
IN THE TAX APPEALS TRIBUNAL OF UGANDA AT KAMPALA
APPLICATION NO. 80 OF 2021

APONYE UGANDA LIMITED ===== APPLICANT
VERSUS
UGANDA REVENUE AUTHORITY ===== RESPONDENT

BEFORE: DR. ASA MUGENYI, MR. GEORGE MUGERWA, MR. SIRAJ ALI

RULING

This ruling is in respect of an application challenging an assessment of Shs. 641,012,201 issued by the respondent on the ground that the applicant had overstated its interest expense contrary to S. 25 of the Income Tax Act (ITA).

The applicant, a company incorporated in Uganda, is engaged in commodity trading and transport services. In April 2021, the respondent conducted an audit of the applicant and issued an assessment of Shs. 641,012,201 for 2019 on the grounds that the latter purportedly overstated its interest expense as it belonged to a group of three companies which had a common underlying ownership. The applicant's objection to the assessment was disallowed.

The following issues were set down for determination.

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

The applicant was represented by Mr. Cephas Birungyi, Ms. Belinda Nakiganda and Ms. Lydia Namugoma while the respondent by Ms. Patricia Ndagire and Mr. Derrick Nahumuza.

The applicant's sole witness, Mr. Benson Tukwasibwe, its finance manager testified that the applicant applied and got loans from DFCU Bank, Uganda Development Bank,

Diamond Trust Bank and Stanbic Bank. The respondent conducted a desk audit on the applicant for the period January to December 2019 and informed the applicant that it had overstated its interest expense by Shs. 2,136,707,338. The witness stated that the applicant wrote to the respondent that it was entitled to the interest. On 21st April 2021, the respondent issued an assessment of Shs. 641,012,201. On 3rd June 2021, the applicant objected to the assessment. On 30th August 2021, the respondent made an objection decision maintaining its position.

The respondent's witness, Ms. Jolly Mutesi Uhiriwe, a tax officer in its domestic taxes division testified that the respondent conducted an examination of the applicant's income tax returns for 2019. It established that the applicant, Quality Bags (U) Ltd, Aponye Transporters Ltd and Aponye House Ltd have a common underlying ownership. The applicant claimed interest expenses of Shs. 3,927,919,280 which exceeded 30% of the tax earnings before interest, tax, depreciation and amortization (EBITDA) allowed under the law. As a result of the said examination the respondent issued the applicant an additional tax assessment of Shs. 641,012,201 on 21st April 2021 in which only 30% of the interest claimed by the applicant was allowed as deduction. The basis of the assessment was that the applicant was a member of a group with common underlying ownership, whose deductible interest in respect of all debts owed by the tax payer should not exceed 30% of EBITDA. The applicant was therefore obliged to claim interest expense up to only 30% of EBITDA. On 4th June 2021, the applicant objected to the assessment on the ground that the applicant is wholly owned by individuals and is not a member of any group of companies. On 19th July 2021, the respondent requested the applicant to avail documentation in support of its objection but none was furnished. Consequently, the respondent conducted a search at the Uganda Registration Services Bureau (URSB) and established that the companies mentioned above had a common underlying ownership under S. 25(5)(b) of the ITA. On 30th August 2021, the respondent issued an objection decision wholly disallowing the applicant's objection on the grounds that the applicant is a member of a group and hence ought not to have deducted more than 30% of its interest expense.

The applicant submitted that it is not liable to pay the tax assessed. It submitted that what is in dispute is not the loan amounts but whether it is allowed to deduct interest wholly or only up to 30% per year of income under S. 25 of the ITA. S. 25(1) provides that a person is allowed a deduction for interest incurred during the year of income in respect of a debt obligation to the extent that it has been incurred by the person in the production of income included in gross income. The applicant stated that it is entitled to deduct interest wholly on its debt obligations as the loans were incurred by it in the production of income. S. 25(3) of the Act provides that the amount of deductible interest in respect of all debts owed by a tax payer who is a member of a group other than a financial institution or person carrying on insurance business shall not exceed 30% of the tax earnings before interest, tax, depreciation and amortization. The applicant submitted that the above provision does not apply to individuals as they are not considered as being able to form a group of companies. The applicant submitted that its shareholders are individuals therefore it was erroneous for the respondent to issue additional assessments of Shs. 641,012,201 based on S. 25(3) of the ITA.

The applicant prayed for an order that it is not liable to pay the tax of Shs. 641,012,201. It prayed for a refund of 30% of the tax in dispute with interest of 2% per month from the date of payment until its payment in full. It also prayed for general damages of Shs. 20,000,000 and costs of the suit.

The respondent submitted that it issued an assessment against the applicant on the ground that it had overstated its interest expense deduction contrary to S. 25(3) of the ITA. It submitted that the general rule is that a person is allowed a deduction for interest incurred during the year of income in respect of a debt obligation incurred during the production of income included in gross income. For a tax payer who is a member of a group, other than a financial institution the deduction is limited to 30% of the tax earnings before interest, depreciation and amortization. The respondent broke down S. 25(3) of the ITA into the following requirements. Firstly, That there must be an amount of deductible interest in respect of all debts. Secondly, the debts should be owed by a tax payer who can be a member of a group, thirdly, that member of a group should not be a financial institution or a person carrying on insurance business and fourthly, if the tax

payer is a member of a group, that taxpayer's deductible interest should not exceed 30% of tax earnings before interest, depreciation and amortization.

The respondent submitted that the question to be determined is whether the debts were owed by a tax payer who is a member of a group. It submitted that under S. 25(5)(b) of the ITA the applicant is not an individual as it is a company incorporated. It submitted that the said provision does not exclude companies. The applicant being a company falls under the term 'member of a group'. The respondent submitted that the second part of the definition of a 'member of a group' is that the person must have a 'common underlying ownership'. It cited S. 2(xxx) of the ITA which defines the term 'underlying ownership' in respect of a person other than an individual to mean an interest held in, or over, the person directly or indirectly through interposed companies, partnerships or trusts by an individual or by a person not ultimately owned by individuals. The respondent broke down the above provision as follows; the interest should be held in or over the person directly or indirectly, this interest can be held through interposed companies, partnerships or trusts, the interest can be held by an individual or the interest can be held by a person who is not ultimately owned by individuals.

The respondent submitted that the applicant is not an individual and its underlying ownership is held by individuals who have common underlying ownership with companies like Quality Bags (U) Ltd, Aponye Transporters Ltd and Aponye House Ltd. A search at the Uganda Registration Services Bureau (URSB) registry revealed that the applicant, Quality Polybags (U) Ltd, Aponye Transporters Ltd and Aponye House Ltd had common underlying ownership as per exhibits R4, R12, R13, R14, R15, R16, R17, R18 and R19. Exhibit R2 showed that the applicant is a majority shareholder in Aponye House Ltd. The memorandum and articles of Aponye Transporters Ltd, exhibit R5, showed that Mr. Apollo Nyegamahe owned 60% shareholding while Mr. Peter Agaba and Mr. Harold Byamugisha each owned 10%. The respondent submitted that this denoted a common underlying ownership. There was a board resolution of the applicant filed with URSB on 30th January 2015 where the applicant guaranteed the debt of Aponye House Ltd to Equity Bank Ltd on the basis that it was a subsidiary of the applicant. Exhibit R15 showed the transfer of 170 ordinary shares from the applicant to Aponye House Ltd. The memorandum of

association of Aponye House Ltd, exhibit R16 showed the shareholders as the applicant, Mr. Apollo Nyegamehe and Mr. Harold Byamugisha. The return of allotment for Aponye House Ltd, exhibit R17, reflected the position in the memorandum of association above. The respondent submitted that the above evidence all proved that the applicant is a member of a group.

The respondent cited *Rukikaire Mathew v Incafex (U) Ltd* SCCA 3 of 2015 for the position that when a person either individual or corporate is allotted shares subsequent to the formation of the company that person becomes a shareholder, member or owner and stands in the same position as the subscriber. It submitted that there was sufficient evidence to prove that the applicant is a member of a group of companies and has a common underlying ownership under S. 25(3) of the ITA. It submitted that this implies that the applicant was only entitled to claim an interest expense of up to 30% of the tax earnings before interest, tax, depreciation and amortization (EBITDA). It cited *Rwenzori Bottling Company Ltd v URA* Application 21 of 2021.

The respondent submitted that if the applicant was right in its interpretation that the definition of the term 'underlying ownership' excludes companies not ultimately owned by individuals, the applicant would still fall within the definition of a member of a group since it has shareholding in other companies like Aponye House Ltd. The respondent submitted that the applicant falls within a group of companies with Aponye House Ltd as they both have a common underlying ownership. The respondent concluded that the additional tax assessment of Shs. 641,012,201 was lawfully imposed

In rejoinder, the applicant submitted that it is not a member of a group in spite of it being a company. S. 25(3) and S. 2 (xxx) does not apply to it. The fact that the applicant has shares in Aponye House Ltd does not show that it has a common underlying ownership within the meaning of S.2 (xxx) of the ITA. It is not in dispute that the applicant had a debt obligation of Shs. 3,927,919,280 which entitled it to deduct of all the interest incurred during the year of income in the production of income.

The applicant submitted that the literal interpretation of S. 25 of the ITA showed that the applicant is not a member of a group and was entitled to wholly deduct the interest expense incurred. It submitted that under S. 25(3) of the ITA a tax payer must be a member of a group to be restricted to claim only 30% of its interest expense after EBITDA. However, if the tax payer is not a member of a group it is entitled to claim all the interest. The applicant submitted that under S. 25(5) (b) of the ITA individuals cannot be part of a group but other persons with a common underlying ownership may form a group subject to S. 2 (xxx) and other provisions of the ITA. The applicant submitted that in construing S. 2 (xxx) above the words `trusts by an individual` should not be separated but should be read as one word. The applicant submitted that such an interpretation confirms that there is no partnership or trust by an individual. It submitted further that there are no interposed companies therefore the aspect of underlying ownership through interposed companies does not arise. The applicant submitted that the shares in the applicant are owned by individuals therefore S. 25(3) of the ITA does not apply.

The applicant submitted further that the company documents relied upon by the respondent are outdated and were selectively used by the respondent in spite of the existence of updated company documents. It stated that exhibit A12, the annual returns for Quality Polybags shows Mr. Apollo Nyegamehe and Mr. Harold Byamugisha as owners with 50% shares each while exhibit R2, the annual returns for Aponye House Ltd shows the applicant, Mr. Apollo Nyegamehe and Mr. Harold Byamugisha as shareholders with 950 shares, 30 shares and 20 shares respectively. The applicant stated that Aponye Transporters Ltd ceased business in 2008 while Aponye Hotel was a sole proprietorship which was sold in 2016, therefore both entities should not be considered. The applicant submitted further that while the companies have Mr. Apollo Nyegamehe as a common shareholder they do not meet the test set out under S. 25(3) of the ITA which requires that the underlying ownership should be in the applicant company and not the reverse. The applicant submitted further that an individual is not considered to form part of a group therefore the individuals in the applicant have no relation to other companies though they might have shares in those companies. The applicant submitted further that since the ultimate owners of Aponye House Ltd are individuals S. 25 (3) and S. 2 (xxx) of the ITA does not apply to them. The applicant stated further that neither S.25 nor S.2 (xxx)

mention that shareholders can form an underlying ownership. The applicant relied on the certificates of registration for Aponye (U) Ltd and the applicant to show that the said companies are separate legal entities with no common underlying ownership.

Having listened to the evidence and read the submissions of the parties, the following is the ruling of the tribunal.

The ITA provides for interest as allowable deductible allowance. S. 25(1) reads

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

Therefore, it is not in dispute that the applicant is entitled to interest. However, the ITA limits the interest where a taxpayer is a member of a group. S. 25(3) reads;

“(3) The amount of deductible interest in respect of all debts owed by a taxpayer who is a member of a group, other than a financial institution, microfinance deposit taking institution, tier 4 micro-finance institution or person carrying on insurance business, shall not exceed thirty percent of the tax earnings before interest, tax, depreciation and amortization.”

Both parties agree that under S. 25(3) of the ITA, a non-individual tax payer who is not a member of a group, is allowed interest expense not in excess of 30% of EBITDA. The applicant claimed for interest expenses up to 30% of EBITDA. The respondent refused on the grounds that the applicant was a member of a group and issued it with an assessment.

The question which must be determined by the Tribunal is whether the applicant is a member of a group within the meaning of S. 25(5)(b) of the ITA? A finding that the applicant is a member of a group would mean that the amount of deductible interest in respect of all debts owed by the applicant shall be limited to 30% of EBITDA with the result that the applicant will be liable to pay the tax assessed. A contrary finding on the other hand would mean that the applicant is not liable to pay the tax assessed.

Under S. 25(5)(b) of the ITA the word 'group' is defined as 'persons other than individuals, with common underlying ownership'. The applicant contended that it is an individual and therefore the S. 25(3) does not apply to it. S. 2(yy) defines a person. It reads:

““person” includes an individual, a partnership, a trust, a company, a retirement fund, a government, a political subdivision of a government and a listed institution.”

So, it is only individuals who under S.25(5)(b) cannot be part of a group with underlying ownership. The applicant is a limited company incorporated in Uganda and is not an individual.

Having found that the applicant is a company, the Tribunal has to determine whether the applicant is part of a group with underlying ownership. 2(xxx) of the ITA defines the term 'underlying ownership' It reads

“Underlying ownership”, in relation to a person other than an individual means an interest held in, or over, the person directly or indirectly through interposed companies, partnerships, or trusts by an individual or persons ultimately owned by individuals.”

The entire dispute boils down to the interpretation of the above provision. Under the interpretation favored by the applicant the phrase 'trusts by an individual' is construed as one indivisible term while the respondent's construction is that the term 'trust' should be separated from the phrase 'trusts by an individual' and construed with the terms 'interposed companies and partnerships'.

In *Cape Brandy Syndicate v the Commissioner of Inland Revenue IRC (1921) KB 64* Rowlatt J said that “in a taxing Act one has to look merely at what is said.” Therefore, we need to look at the word 'group' and 'underlying'. Words should be given their ordinary meaning. The word 'group' is defined *Oxford Advanced Learner's Dictionary* New 9th Edition p. 673 as “a number of people or thing that are together in the same place or that are connected in some way.” For there to be a group there should be more than one person. The word 'underlying' is defined by *Black's Law Dictionary* 10th Edition p. 1758 as “An asset or other factor that give rise to rights and obligations in a derivative contract.” *Oxford Advanced Learner's Dictionary* New (supra) p. 1041 defines 'underlying' as “1. Important in a situation but not always easily noticed or clearly stated... 2. Existing under

the surface of something else...". So, to determine a group, the Tribunal has to determine which companies are connected. There are many ways of determining whether persons are connected. One way is looking at ownership. Do they share the same owners or directors? Companies with the same owners usually fall in the same group of companies. The reason why deductible interest allowed is limited is because they maybe sharing the same funding.

In order to ascertain whether an individual is part of a group, ownership of shares in a company may assist in determining ownership. A search at the Uganda Registration Services Bureau (URSB) revealed that the applicant, Aponye (u) Limited, Aponye Transporters Ltd and Aponye House Ltd had common underlying ownership as per exhibits. The memorandum and articles of Aponye Transporters Ltd, exhibit R5, showed that Mr. Apollo Nyegamahe owned 60% shareholding while Mr. Peter Agaba and Mr. Harold Byamugisha each owned 10%. The special resolution transferring shares in Aponye Transporters to Aponye (U) Ltd, exhibit R4 shows that the former ceased to exist in 2008. Exhibit R14 and R15 are a resolution and transfer of shares respectively where Apollo Nyegamehe and Harold Byamugisha transferred 179 of their shares in Aponye House Limited to Aponye Uganda Limited. Exhibit R16 is the memorandum and articles of Aponye House Limited which shows the owners as Aponye (Uganda) Limited, Apollo Nyegamehe and Harold Byamugisha. The annual returns of Quality Polybags (U) Ltd exhibits A11 and A12 show that Apollo Nyegamehe and Harold Byamugisha are shareholders. The respondent submitted that this denoted a common underlying ownership. There was a board resolution of the applicant filed with URSB on 30th January 2015 where the applicant guaranteed the debt of Aponye House Ltd to Equity Bank Ltd on the basis that it was a subsidiary of the applicant. From the evidence adduced, the applicant, Aponye House Limited, Quality Polybags Limited, Aponye Transporters form part of a group. The applicant stated that Aponye Transporters Ltd ceased business in 2008 while Aponye Hotel was a sole proprietorship which was sold in 2016, therefore both entities should not be considered Though Aponye Transporters ceased to exist, the group was not reduced to less than two. Therefore S. 25(3) of the ITA would limit the interest claimed by the applicant to 30% and the respondent was justified to issue an assessment.

One of the rules of statutory interpretation is that words used in one place in a statute usually have the same meaning in every other place in the statute. In *St. Luke's Magic Valley Reg'l Med. Ctr. Ltd v Bd of Cty. Commissioners of Gooding Cty.*, 149 Idaho 584, the court stated that;

"Other portions of the same Act or section may be resorted to as an aid to determine the sense in which a word or phrase, or clause is used, and such phrase, word, or clause, repeatedly used in a Statute, will be presumed to bear the same meaning throughout the Statute, unless there is something to show that there is a different meaning intended, such as a difference in subject matter which might raise a different presumption."

The phrase 'interposed companies, partnerships or trusts' has been used in the definition of the term 'associate' under S. 3(2) of the ITA states without limiting the generality of subsection (1). It stated that the following are treated as an associate of a person...

"(h) Where the person is a company-

- (i) A person who, either alone or together with an associate or associates under another application of this Section, controls fifty percent or more of the voting power in the company, either directly or through one or more interposed companies, partnerships, or trusts; or (emphasis added).
- (ii) Another company in which the person referred to in subparagraph (i) of this paragraph, either alone or together with an associate or associates under another application of this Section, controls fifty percent or more of the voting power in that other company, either directly or through one or more interposed companies, partnerships, or trusts.
(Emphasis added).

The phrase 'interposed companies, partnerships, or trusts, has been used to denote different entities through which a company might control another company. In S. 3 (h)(i) and S. 3(h)(ii), no mention has been made of an entity known as 'trusts by an individual'. If S. 3(h) is applied as an aid to determine the phrase 'interposed companies, partnerships, or trusts' which has been used under S.2 (xxx), it is apparent that the words 'by an individual or by a person not ultimately owned by individuals' which follow the phrase 'interposed companies, partnerships, or trusts' sets out, the persons whose ownership of interests in, or over other persons, directly or indirectly through interposed companies, partnerships, or trusts, forms the last part of the definition of the term 'underlying ownership'. Applying therefore, the sense in which the above phrase has

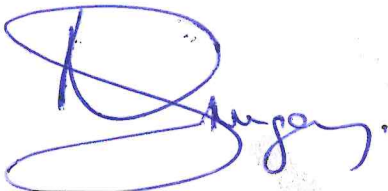
been used under S. 3(h), the term 'trusts' should be separated from the words 'by an individual' in interpreting S. 2 (xxx). The result is that in both S.2 (xxx) and S.3 (h) the phrase 'interposed companies, partnerships, or trusts' denote entities through which different persons might control the activities of other entities or persons. Credence is lent to this view by the fact that throughout the statute the term 'trusts by an individual' only appears in S. 2 (xxx), and that only, because the term 'trusts' is followed by the words, 'by an individual or by a person not ultimately owned by individuals'. On the other hand, the phrase 'interposed companies, partnerships, or trusts' appears more than once in different parts of the statute.

Furthermore, the interpretation favored by the applicant waters down some of the anti-avoidance provisions in the ITA. By reading the phrase '*interposed companies, partnerships, or trusts*' as '*interposed companies, partnerships, or trusts by individuals*' the applicant replaces the entity known as a 'trust' with an entity known as 'trusts by an individual'. This leads to two undesirable effects. Firstly, it means that in interpreting S. 2 (xxx) interests held in, or over a person directly or indirectly through a trust no longer fall under the definition of '*underlying ownership*'. Secondly, the persons whose ownership of interests in other entities through interposed companies, partnerships, or trusts, is essential in defining the term '*underlying ownership*' have been entirely removed from the above provision namely; *an individual or a person not ultimately owned by individuals*'. The definition of the term '*underlying ownership*' is also interlinked with the term '*associate*'. For instance, under S. 75 of the ITA, a company is not permitted to deduct an assessed loss in the year of income or in subsequent years if during the year of income there has been a change of fifty percent or more in the underlying ownership of the company. Under S. 77(3) of the ITA, the Commissioner may permit a resident company to treat a reorganization as not giving rise to the disposal of any business asset or the realization of any business debt where such company has been reorganized without any significant change in the underlying ownership. By altering S. 2(xxx) in the manner indicated above, the anti-tax avoidance measures created by the legislature through concepts such as '*underlying ownership*' or an '*associate*' are compromised. It is clear that the interpretation favored by the applicant leads to an absurd result. In *Mafabi v Uganda* (1969) 1 EA 179 (HCU), Sir Udo Udoma CJ, held that it is the duty of a Court

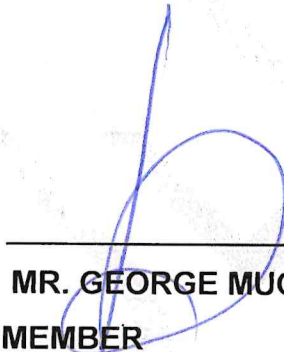
to interpret an Act of Parliament so as to avoid absurdity. Properly construed, S. 2 (xxx) is confined to a person other than an individual. It refers to an interest held in or over, this non-individual person. This interest is held over the person directly or indirectly through three different entities, namely; interposed companies, partnerships, or trusts. Further, this interest is held over this person through these entities either by an individual or by a person not ultimately owned by individuals.

For the above reasons, we do not agree with the assertion by the applicant, that an individual cannot be part of a group within the meaning of S. 25(3) of the ITA and that therefore the individuals in the applicant company have no relation to those other companies in spite of the fact that they might have shares in those companies. This application is accordingly dismissed with costs.

Dated at Kampala this 13th day of October 2023.



DR. ASA MUGENYI
CHAIRMAN



MR. GEORGE MUGERWA
MEMBER



MR. SIRAJ ALI,
MEMBER