THE REPUBLIC OF UGANDA

IN THE TAX APPEALS TRIBUNAL AT KAMPALA

TAT APPLICATION NO. 198 OF 2022

ESPERANZA DISTRIBUTORS LIMITED.....APPLICANT

VERSUS

UGANDA REVENUE AUTHOURITY.....RESPONDENT

BEFORE: MS. CRYSTAL KABAJWARA, MS. GRACE SAFI, MS. CHRISTINE KATWE.

RULING

This ruling is in respect of an application challenging VAT assessments of Shs. 882,658 and Local Excise duty of Shs. 54,624,445 on spirits manufactured by the Applicant.

1. Background Facts

The Applicant processes and distills spirits. In January 2022, the Respondent issued ten local excise duty (LED) assessments totaling to Shs. 182,331,735.82 and seven VAT assessments amounting to Shs. 20,891,749.

The Applicant objected to the assessments on the grounds that the Respondent wrongly classified the product as ready to drink yet as opposed to undenatured spirit with raw materials sourced from Uganda.

Further, the parties carried out a Tribunal guided mediation and on 27 June 2023, filed a partial consent where the Respondent revised the VAT assessment of Shs. 20,891,749.56 to Shs. 882,658 and LED assessment of Shs. 182,331,749.56 was to Shs. 54,624,445. The issues in respect of VAT Shs. 882,658 and LED 54, 624,445, were referred to the Tribunal for determination.

2. Issues for determination

The issue for determination is whether the Applicant is liable to pay the tax assessed by the Respondent.

3. Representation

The Applicant was represented by Mr. Ponsiano Turyamureba and Mr. Onesmus Mwesigye while the Respondent was represented by Ms. Christine Mpumwire.

The Applicant's sole witness was Mr. Tumukwasibwe Julius, a Manager. He stated that the Applicant produces Speranza waragi gin which was the only product that the Applicant dealt in at the time of the assessment. He stated that its ingredients were DM Water, extra neutral spirit and gin flavors sourced from Uganda. In January 2022, the Respondent issued ten local excise duty Assessments amounting to Shs.182, 331,735.82 and seven VAT Assessments amounting to 20,891,749.56.

He further stated that the Respondent's reasons for the assessments were that there were LED and VAT variances, misclassification of product type and unverified exports.

Mr. Tumukwasibwe Julius stated that the Respondent wrongly classified the Applicant's products as ready to drink spirits, yet they are undenatured spirits. Further, he testified that the Respondent applied the wrong ex-factory price when they issued the assessments.

The Respondent called one witness, Mr. John Nabembezi, an Officer in the Domestic Taxes Department of the Respondent. He testified that the Applicant misclassified the product type in the LED returns for Speranza Waragi Gin as undenatured spirits made from locally produced materials as per part 3(b) of the 2nd Schedule to the Excise Duty Act. The Respondent classified the products as ready-to-drink spirit as per the UNBS ready-to-drink standards and the analysis carried out by the Respondent.

The witness further testified that the Respondent revised the ex-factory price upwards in the LED returns for Speranza Waragi Gin and Speranza Water. He stated that the Respondent established inconsistencies between sales declared in the VAT and LED

returns, inconsistencies in ex-factory price reported in the LED returns, variance between quantities in DTS reports and LED returns, and unverified exports.

During cross examination, Mr. John Nabembezi stated that what differentiates ready to drink from undenatured spirits is that for the Applicant's products, the alcohol content is 40% which is less than the 80% for undenatured spirits.

He further stated that the law does not define un-denatured spirits and that he did not confirm the ingredients with the Applicant before the assessment was issued. However, he stated that the taxpayer registered their products with UNBS and in the URA system as ready-to-drink products. He testified that the Applicant's products were ready to drink based on UNBS standards 1 edition 2015. He also stated that the Respondent does not have its own guidelines on ready to drink standards.

During re-examination, Mr. John Nabembezi stated that the Applicant registered 200 mls spirits and 500 mls water in the Respondent's system. He further stated that no person in Uganda produces undenatured spirits. He also looked at other players like Uganda Breweries who make ready to drink products and all have 40% alcohol content.

4. Submissions of the Applicant

Whether the Applicant is liable to pay LED of Shs. 54,624,445?

The Applicant submitted that Item 3 of the Second schedule to the Excise Duty Act provides:

a) *"Un-denatured spirits made from locally produced raw materials at a rate of 60% or shs. 1500 per liter whichever is higher*
b) *Un-denatured spirits made from imported raw materials at a rate of 100% or shs. 2500 per liter whichever is higher.*
c) *Ready to drink spirits at a rate of 80% or shs 2000, per litre, whichever is higher".*

The Applicant submitted that if a spirit is un-denatured, then duty is imposed depending on whether that spirit is made from locally produced raw materials or imported raw materials. The Applicant's Speranza Waragi Gin falls under item 3(a) of the 2 Schedule

of the Excise Duty Act and ought to have got a tax treatment of 60% or Shs 1500 per liter whichever is higher.

Whether the Applicant's products are undenatured

The Applicant submitted that the Excise Duty Act did not define the term "un-denatured spirits" until the 2024 amendment which came in force after the assessments in question. The Applicant argued that the Respondent's reliance on the definition in the Excise Duty Amendment Act, 2024 is unfair because at the time of the assessment, the provision was not in place.

The Applicant submitted that the Respondent attempted to define un-denatured spirit in cross examination as spirit plus water. However, according to the Applicant, the term refers to spirits that are not mixed with any substance to render the spirit unfit for human consumption or capable of being rendered unfit for human consumption.

The Applicant submitted that making Speranza Waragi Gin, it mixes, DM Water, extra neutral spirit & permitted flavors. The spirit has been approved by UNBS and as such considered not harmful for human consumption. Speranza Waragi Gin is an undenatured spirit because it is not harmful to human consumption. The Applicant prayed that the Tribunal finds that the Speranza Waragi Gin is an undenatured spirit.

Whether the products are made from locally produced raw materials.

The Applicant submitted that the ingredients used in the manufacture of Speranza Waragi Gin are all locally produced. The ingredients are broken down below:

(i) Extra Neutral Alcohol

The Applicant submitted that Extra Neutral Alcohol (ENA) is the purest form of alcohol, with no taste or smell. It is made from different raw materials such as sugarcane molasses or grains like corn, rye, wheat, barley, and rice. It is used as a base for spirits and alcoholic beverages, and this ingredient is locally produced.

(ii) DM Water

The Applicant submitted that DM water stands for demineralized water. Collin's Dictionary defines demineralized to mean *"remove dissolved salts from (a liquid especially water)"*, This is a locally produced raw material.

(iii) Permitted flavors

The Applicant submitted that the permitted flavors used are locally sourced. The Applicant prayed that the Tribunal finds that the ingredients used in making Speranza Waragi Gin are locally sourced.

The Applicant submitted that since Speranza Waragi Gin is an un-denatured spirit made from locally manufactured raw materials, then it falls under item 3(a) of the second schedule to the Excise Duty Act and should be given the tax treatment thereunder.

The Applicant submitted that the Respondent relied on the UNBS definition of ready to drink. Paragraph 3 of the UNBS ready to drink standardization defines ready to drink to mean *"low strength carbonated and pasteurized or aseptically packaged alcoholic beverages derived from blending of neutral spirit as base with permitted food additives".*

The Applicant argued that Article 152(1) of the Constitution of Uganda provides that no tax shall be imposed except under the authority of an Act of Parliament. Therefore, the Respondent's act of raising tax assessments on the Applicant basing on UNBS standardization is unlawful.

The Applicant cited the case of ***Comfort Homes v URA Application No. 66 of 2022*** where the Tribunal stated:

"Before one is assessed for a tax liability, the law imposing the liability should be clear and unequivocal. In case of any ambiguity, it should be interpreted in favor of a taxpayer."

The Applicant cited the case of ***Cape Brandy Syndicate v Inland Revenue Commissioners [1920J1 KB 64*** which was cited with approval in ***Uganda Revenue Authority v Kajura SCCA 9 of 2015*** and other authorities. It was stated:

"In a taxing act, clear words are necessary to tax the subject in a taxing act one bas merely to look at what is clearly said. There is no room for intendment. There is no equity about tax. There

is no presumption as to tax. Nothing is to be read into it. Nothing to be implied. One can only look fairly at the words used."

The Applicant submitted that the Respondent was wrong in using UNBS standards to tax the Applicant. The Applicant's drink is not low strength because it contains 40% alcohol.

The Applicant submitted that the UNBS standardization is concerned with the labelling of ready-to-drink beverages and the words "ready- to-drink" should appear in close proximity with the brand name.

VAT

The Applicant submitted that the VAT assessments arose from the reclassification of the products as ready-to-drink. However, since the products are undenatured spirits, the VAT assessment of Shs. 832,653 should be vacated.

5. Submissions by the Respondent

The Respondent submitted that the Applicant's case hinges on whether operational costs such as trading costs are inclusive in the taxable value for VAT purposes and what amounts to ex-factory price.

Ex-factory price

The Respondent cited Paragraph 2(1) of Part II, Schedule 2 of the Local Excise Duty Act which provides:

"(1) The value of an excisable good shall be the normal ex-factory price of the good exclusive of any tax on the good.

(2) The normal ex-factory price of the goods shall include raw material costs, manufacturing costs, labour costs, profit margin, bank charges and interest and all other costs, charges and expenses incidental to the factory, production and sale".

The Respondent submitted that ex-factory price refers to the price the item is sold at the factory. Whatever does not fall under the scope of Paragraph 2(2) ought to be excluded in determining the ex-factory price.

The Respondent cited the case of ***Union of India V Bombay Tyre International Limited (1984) 1 SCC 467***, where it was held:

"Ex-factory price is the price at which goods are sold by the manufacturer at the factory gate"

The Respondent also cited the case of ***Century Bottling Company Limited v Uganda Revenue Authority TAT No. 33 of 2020***, where the Tribunal held:

"The Ex-factory price should therefore be able to capture the basic cost of producing the goods, up until the point they leave the factory. For this reason, it is vital that the only costs, which should be included in the ex-factory price, are costs which are essential for the manufacture of the goods and their sale at the manufacturer's premises."

Having ascertained what constitutes ex-factory price, the question for the tribunal to determine is whether the Applicant's operational costs such as trading costs are inclusive in the taxable value for VAT purposes.

The Respondent submitted that the Respondent rightly excluded the Applicant's operational costs such as trading costs in the taxable value for VAT purposes since the same did not form part of the ex-factory price of the Applicant's products. The Respondent prayed that the Tribunal find that the Applicant is liable to pay the tax.

LED & VAT variances

The Respondent submitted that it conducted a review of the Applicant's tax affairs and established inconsistencies between declared VAT sales and LED returns creating a variance of Shs. 85,582,241 leading to VAT liability of Shs. 832,653 and LED liability of Shs. 54,624,445 as revised by consent. This evidence was not contravened by the Applicant at objection and at hearing stage.

6. The Determination by the Tribunal

Having listened to the evidence and read the submissions of both parties this is the ruling of the Tribunal.

The dispute before the Tribunal is whether the Respondent rightly classified the

According to the facts, the Applicant had declared goods as denatured spirits made from locally produced raw materials as per part 3 (a) of the 2nd Schedule to the Excise Duty Act ("EDA"). However, the Respondent alleged that the goods were ready-to-drink spirits as per part 3 (c) of Schedule 2 of the EDA.

Item 3 of the 2nd schedule to the EDA provides:

a) *"Un-denatured spirits made from locally produced raw materials at a rate of 60% or shs. 1500 per liter whichever is higher*
b) *Un-denatured spirits made from imported raw materials at a rate of 100% or shs. 2500 per liter whichever is higher.*
c) *Ready to drink spirits at a rate of 80% or Shs 2000, per litre, whichever is higher".*

The Tribunal resolves the dispute as follows:

Whether the Applicant's products are undenatured or ready-to-drink spirits.

The Applicant argues that their products are undenatured spirits and are therefore dutiable at a lower rate of 60% as opposed to the higher rate of 80% for ready-to-drink spirits.

What are undenatured spirits?

Until 2024, the EDA did not define the term "undenatured spirits". The Applicant has argued that the Respondent relied on definition in the Excise Duty (Amendment) Act, 2024 which came into force after the assessments were issued in January 2022.

We agree with the Applicant that the law does not apply retrospectively. That said, in the absence of a definition in the EDA as it prevailed at the time, the Tribunal can turn to the ordinary / literal meaning of a term or phrase.

The Online Collins Dictionary (https://www.collinsdictionary.com/dictionary/english/denature) defines the term "denature" as follows:

"to change the nature of...

...to render (something, such as ethanol) unfit for consumption by adding nauseous substances."

Further, the Encyclopedia for Food and Health, 2016 defines denatured alcohol to refer to:

"... alcohol products adulterated with toxic and/or bad tasting additives (e.g., methanol, benzene, pyridine, castor oil, gasoline, isopropyl alcohol, and acetone), making it unsuitable for human consumption."

Therefore, when combined with the prefix "un" which serves to change the meaning of a word to its negative or reverse, it follows that the term "undenatured" in the context of spirits refers to those spirits whose nature has not been changed by adding substances that renders them unfit for human consumption. In other words, undenatured spirits are pure alcohol, free from any additives or contaminants.

The Applicant's witness also testified that the term undenatured refers to *"spirits that are not mixed with any substance to render the spirit unfit for human consumption or capable of being rendered unfit for human consumption."*

Therefore, based on the above definitions, two conditions must be met for a product to be considered undenatured:

(i) The spirits / alcohol must not be mixed with any substance: and
(ii) The added substances must not render the spirits unfit for human consumption.

In the present case, while the Applicant's products meet the second test, that is, they are fit for human consumption, they do not pass the first test because the spirit is mixed with other substances.

The Applicant's witness testified that the Applicant's products are mixed with different substances such as water, extra neutral alcohol and flavours. Therefore, having stated as such, it cannot be said that the Applicant's products are undenatured or pure or unchanged. Since the applicant's products do not meet both tests, it follows that they do not fall squarely in the definition of "undenatured".

Further, undenatured spirits typically have an alcohol content of 80% or more by volume (ABV). This means that the product is highly concentrated alcohol. The Applicant's products have an alcohol content of 40% indicating that the spirits have to a certain extent been denatured to reduce their alcohol strength.

Ready-to-drink spirits

The EDA does not define the phrase "ready-to-drink"; however, the phrase is self-defining.

An article in Forbes (a leading global business magazine), titled, *"The Rise and Future of Ready to Drink Beverage Industry"* published on 10 September 2024 states as follows concerning ready-to-drink (RTD) beverages:

"While there isn't an official definition, RTDs usually refer to canned alcoholic beverages that are premixed and ready for immediate consumption."

The Applicant's witness testified that their products are mixed with other substances such as water and flavours. In addition, the Applicant provided an exhibit of their products at exhibit 4 of the Joint Trial Bundle. The exhibit depicts a 200ml bottle of Speranza Waragi Gin with the caption:

"Excess consumption of alcohol is harmful to your health."

This shows a product, once purchased, that is ready for immediate consumption. There are no instructions on the product that show otherwise, e.g., requiring a consumer to do anything before consuming the product e.g. to add water or bring to boil before consuming.

In addition, the alcohol strength of the product is shown as 40% ABV which also indicates that the alcohol volume accounts for only 40% while other ingredients such as water account for 60%.

Therefore, having considered the three classes of products and their corresponding tax rates under Item 3 of the 2nd schedule to the EDA, namely:

a) *"Un-denatured spirits made from locally produced raw materials at a rate of 60% or shs. 1500 per liter whichever is higher*

b) *Un-denatured spirits made from imported raw materials at a rate of 100% or shs. 2500 per liter whichever is higher.*

c) *Ready to drink spirits at a rate of 80% or Shs 2000, per litre, whichever is higher".*

It is reasonable to conclude that the item which closely matches the Applicant's products is item 3 (c). Therefore, the Respondent correctly categorized the products as ready-to-drink. This is further corroborated by the UNBS' classification of the products in the same category.

VAT

It follows that the Respondent's VAT assessment stands as it arises from the discrepancy in the Applicant having classified its products as undenatured and accounted for LED at a lower rate as opposed to the higher rate for ready to drink products.

Therefore, the Applicant is liable to pay VAT assessed of Shs. 832,653.

Whether trading costs should form part of the ex-factory price

Paragraph 2(1) of Part II, Schedule 2 of the Local Excise Duty Act provides:

"(1) The value of an excisable good shall be the normal ex-factory price of the good exclusive of any tax on the good.

(2) The normal ex-factory price of the goods shall include raw material costs, manufacturing costs, labour costs, profit margin, bank charges and interest and all other costs, charges and expenses incidental to the factory, production and sale".

From the above provision, it is clear that ex-factory prices only includes costs that arise from production and all other activities involved until the sale at the factory gate. This means that the ex-factory price is the first price after manufacturing has been completed by the producer of the product. The price includes all manufacturing expenses until the product is sold off of at the manufacturer's premises.

Therefore, trading costs such as marketing costs, distribution costs, transport delivery, advertisement, retail related costs, among others do not form part of the ex-factory price as they are incurred after the product has left the factory. Therefore, the Respondent was right in excluding them and adjusting the VATable value accordingly.

In the circumstances, we find that the Respondent rightly assessed the Applicant. The Tribunal therefore makes the following orders:

(i) This application is dismissed.
(ii) The Applicant is liable to pay LED assessment of Shs. 54,624,445.
(iii) The Applicant is liable to pay VAT assessment of Shs. 832,653.
(iv) Each party shall bear its own costs of this application as per the partial consent dated 27 June 2023.

Dated at Kampala this 25th day of April 2025.

CRYSTAL KABAJWARA	GRACE SAFI	CHRISTINE KATWE
CHAIRPERSON	MEMBER	MEMBER