

THE REPUBLIC OF UGANDA

IN THE TAX APPEALS TRIBUNAL REGISTRY AT KAMPALA

APPLICATION NO. 008 OF 2023

KISOZI COMPLEX (U) LIMITED..... APPLICANT

VERSUS

UGANDA REVENUE AUTHORITY..... RESPONDENT

RULING

BEFORE: MS. CRYSTAL KABAJWARA, MR. SIRAJ ALI, MRS. CHRISTINE KATWE

This ruling is in respect of a claim for input tax credit arising from the purchase construction materials used in the construction of a building for letting.

1. Background facts

The Applicant is engaged in the construction and letting of properties for commercial purposes. In the period July 2020 – April 2020, the Applicant charged and accounted for output VAT on all taxable supplies made to it. In the same period, the Applicant incurred VAT on its purchases in the amount of Shs. 209,122,466.

The Applicant applied for a VAT refund arising from the excess of input VAT over the output for the period July 2020 – April 2020. The Respondent carried out an audit to verify the input tax credits and disallowed input tax credit arising from the purchase of construction materials for apartments under construction. The disallowance led to the issuance of administrative additional assessments totaling Shs.159,899,733.

The Applicant objected to the assessed tax on the grounds that the disallowed input tax was valid and creditable.

Whilst reviewing the Applicant's objection, the Respondent conducted a site visit and established that the input tax claimed by the Applicant related to the purchase of construction materials for a building still under construction, which had only reached 40% completion. The Respondent stated that the layout of building is indicative of residential apartments which supplies are exempt from VAT. The Respondent further stated that as the structure was incomplete, it could not serve as a serviced apartment as this use could not be ascertained.

The Respondent therefore maintained its earlier position hence this application.

2. Issues for determination

The issues for determination before the Tribunal are:

- (i) Whether the Applicant is entitled to the refund?
- (ii) What remedies are available for the parties?

3. Representation

The Applicant was represented by Ms. Jennifer Ruth Mugisha while the Respondent was represented by Mr. Edmond Agaba, Ms. Christine Mpumwire, Ms. Diana Prida Praff and Ms. Charlotte Katuutu.

Mr. Kabiito Baker Kiwanuka the Applicant's Managing Director in his witness testified that the dispute arose when the Respondent disallowed the input tax credit arising from supplies made to the Applicant for the construction of residential premises.

The witness testified that the Applicant charged and accounted for output VAT on all taxable supplies made to its business. The Applicant availed invoices and proof of payment of suppliers, VAT returns, and bank statements, marked A4, A1 and A5. The witness further testified that the Applicant incurred input VAT on its business purchases amounting to Shs. 209,122,466.

Mr. Echasa Patrick testified on behalf of the Respondent. His testimony was based on findings from a site visit conducted by the Respondent's objections team. Mr. Echasa stated that, at the time of the site visit, the construction was only 40% complete.

Mr. Echasa testified that he inspected the building, its layout included bedrooms, kitchens and living rooms. Therefore, the building is residential property, which is an exempt supply under the VAT Act.

4. The Submissions of the Applicant

The Applicant submitted that under Section 28 of the VAT Act, a credit is allowed to a taxable person for the tax payable for taxable supplies made during the tax period if the supply is for use in the business of the taxable person.

The Applicant submitted that it is not in dispute that it was engaged in the business of construction and letting out properties for commercial purposes. What is in dispute was whether or not the Applicant was entitled to input tax credit for the purchase of construction materials used in building a residential apartment.

The Applicant contended that it is entitled to input tax credit on grounds that the apartment being constructed was intended to form part of its business as a service apartment, which is a taxable supply.

The Applicant relied on Section 6 (1) of the VAT Act to define a taxable person as;

"A person registered under section 7 is a taxable person from the time the registration takes effect".

The Applicant cited Section 28 of the VAT Act which provides that a taxable person is entitled to credit for the input tax paid on goods and services used in the course of making taxable supplies.

The Applicant cited ***Enviroserv (U) Limited v Uganda Revenue Authority, Application No. 24 of 2017*** and ***Chestnut Uganda Limited v Uganda Revenue Authority, Application No. 94 of 2019***, where the Tribunal held:

“For the Applicant to be entitled to the input tax credit under this section, the Applicant has to prove the following;

- i) The Applicant is a taxable person*
- ii) Taxable supplies have been made to the Applicant during the tax period*
- iii) The taxable supplies were for use in the business of the Applicant.”*

The Applicant argued that the construction materials purchased were directly linked to its business of the real estate development/construction, which qualifies as a taxable activity under Section 18 of the VAT Act. The Applicant intended to lease out the property as serviced residential apartments which fell within the definition of a taxable supply under section 1(l) of the VAT Act.

The Applicant further contended that there is nothing in the VAT Act that suggests that a taxpayer should restrict a claim for input tax credit to one business activity. Therefore, the Respondent's argument that the Applicant's registration was only in respect of its commercial property in Nakasero, was erroneous. The Applicant cited section 6 of the VAT Act and stated that VAT registration is in respect of a person and not a business activity.

The Applicant submitted that a review of the Respondent's statement of reasons revealed no objection to the fact that taxable supplies were made to the Applicant during the relevant tax period. The Applicant further argued that the Respondent did not dispute the validity of the tax invoices demonstrating that the input tax claimed was properly accounted for and in compliance with the provisions of the VAT Act.

The Applicant argued that since the Respondent did not challenge the authenticity of the tax invoices or the fact that the supplies were made, there was no legal basis for disallowing the input tax claim. The Applicant contended that the disallowance was unjustified, as the VAT Act clearly entitles the Applicant to claim input tax on taxable supplies, provided the necessary documentation is in order.

In the present case, the Applicant furnished the Respondent with original tax invoices during the audit, and the Respondent had ample time to verify them right from the audit stage through to the objection process.

The supplies were for use in the Applicant's business

The Applicant submitted that the taxable supplies in question were for use in the Applicant's business of construction and real estate. Section 28 (7) of the VAT Act provides:

"For the purpose of subsections (1), (2) or (3) "business use" or "use in the business" applies only to the related business, generating a taxable supply."

The Applicant submitted that the above provision implies that a taxable person is entitled to a credit for input tax on goods and services acquired for the purpose of making taxable supplies in the course business. The materials and services for which input tax credits were claimed were directly linked to the construction and development of residential apartments, which formed part of its business. The Applicant asserted that the claim for input tax credit was valid, as the supplies were used wholly and exclusively for the business, satisfying the requirements of Section 28(7).

The purpose of the premises

The Applicant submitted that the intended purpose of the building under construction, whether residential or commercial has no bearing on the proper tax treatment of the input tax claim. The Applicant argued that at the time when the Applicant claimed the input tax that is the subject of this dispute, the VAT act did not have the definition of the terms "business use" or "use in the business". Since these terms were introduced in 2023, they had no bearing on the present case.

The Applicant further submitted that as the building is still under construction, its intended use will be ascertained upon completion depending on the forces of demand and supply.

The Applicant also submitted that if the Respondent's argument is that the building under construction will be used as a residential apartment, which is an exempt supply, the Respondent ought to have applied the apportionment formula in section 28 (9) of the VAT Act. However, even if the Respondent were to apply the apportionment formula, the Applicant would still be entitled to all the input tax credit for the period.

5. The Submissions of the Respondent

In reply, the Respondent maintained that the Applicant was not entitled to claim input tax on the construction materials used for building its residential apartments whose supply is exempt from VAT under paragraph 1(f) of the Third Schedule to the VAT Act.

The Respondent submitted that the key consideration is whether the taxable supplies made to the Applicant were used in a related business that generates taxable supplies.

The Respondent relied on section 28 (7) of the VAT Act, which provides as follows:

“For purpose of subsection (1), (2) and (3), ‘business use’ or ‘use in the business’ applies only to the related business generating a taxable supply”.

The Respondent submitted that during a site visit, the Respondent’s witness, Mr. Patrick Echasa established that the building in question was for residential use and its intended use as a service apartment could not be established due to its incomplete state. Further, since the letting or leasing of residential apartments is an exempt supply as stated in paragraph 1 (f) of the Third Schedule of the VAT Act, the Applicant was not entitled to claim for input tax credits incurred in the purchase of construction materials for the property.

The Respondent argued that the Applicant’s input tax credit claim must comply with the definition of “use in business”.

Regarding the use of the apportionment formular, the Responded stated the formular is not warranted in the present case as its application requires the taxpayer to have made both taxable and exempt supplies. However, as the Applicant’s building is still under construction and only 40% complete, it was not in position to make any supplies, whether taxable or not. Therefore, the formular could not be applied in respect to the Applicant’s claim for input tax credit.

Retrospective application of Section 28 (7) of the VAT Act

The Respondent submitted that the Applicant’s contention that Section 28 (7) of the VAT Act does not apply to its input tax credit claim was misconceived. The Applicant argued

that at the time of their 2022 application, the VAT Act did not define the terms “business use” or “use in business.” Therefore, the Applicant asserted that the subsequent introduction of Section 28(7) in 2023 could not apply to its claim since laws do not operate retrospectively unless explicitly stated.

The Respondent submitted that it is indeed a well-established principle of statutory interpretation that laws are presumed to operate prospectively, especially where they impose new burdens or alter existing obligations. This principle ensures that vested rights are protected, and individuals are not subjected to new legal obligations for actions that occurred before a statute’s enactment.

The Respondent submitted that Section 28(7) was not enacted to alter existing rights or impose new duties. Instead, it was introduced to provide clarification on the meaning of “use in business” concerning the application of input tax credit. The provision merely elucidates the legislative intent underlying Section 28(1) of the VAT Act, which already required that input tax be linked to taxable business activities.

The Respondent submitted that Section 28(7) meant that it applies to the Applicant’s input tax credit claim, even though the claim was lodged before the section’s enactment. Since the provision did not impair any vested rights under Section 28 (1) but only clarified existing obligations, its application to the Applicant’s case was proper and lawful. The Respondent requested the Tribunal to reject the Applicant’s objection and hold that the 2023 clarification in Section 28 (7) was intended to address ambiguities in prior practice, not to impose any new burdens retroactively. Thus, the Applicant’s input tax credit claim must be evaluated under the clarified standard of “use in business.”

In support of the above submission, the Respondent cited the case of ***R. Rajagopal Reddy v Padmini Chandrasekharan (1995)***, where the Supreme Court of India held that clarificatory amendments are presumed to operate retrospectively, as they explain the original legislative intent without altering vested rights. The Respondent urged the

Tribunal to apply Section 28 (7) retrospectively, as it reinforces that input tax is only creditable with taxable business activities.

The Applicant's claim for input tax being premature

The Respondent submitted that the Applicant's claim for input tax credit was premature pursuant to paragraph 1(f) (v) of the Third Schedule to the VAT Act. This provision exempts residential property from VAT unless it qualifies as commercial premises or serviced apartments.

The Respondent submitted that the building under construction lacked the essential characteristics of a service apartment. The property's incomplete state and absence of clear evidence demonstrating that it would generate taxable supplies suggested that it fell under the category of residential property, which is exempt from VAT. The VAT Act allows input tax credit only when the underlying goods or services were used to generate taxable supplies. Since the building had not yet been completed, or used for taxable purposes, any input tax claim at this point would be regarded to be premature. The Respondent stated that the Applicant's entitlement to input tax credit would only arise if the property's use aligned with taxable business activities upon completion.

The Respondent prayed that the Tribunal dismisses this application with costs to the Respondent.

6. The Applicant's Submissions in Rejoinder

In rejoinder, the Applicant submitted that the Respondent's reliance on certain sections of the VAT Act and its interpretation of input tax credits was misplaced and misapplied to the facts at hand. Regarding section 28 (7) of the VAT Act, the Applicant reiterated that the section could not operate retrospectively to disallow input tax credit on construction materials purchased prior to its introduction.

7. The determination by the Tribunal

Having listened to the evidence and studied the submissions of both parties, this is the decision of the Tribunal.

The Applicant is a company that is engaged in development and letting of properties on a commercial basis. It applied for a VAT refund due to excess input VAT over output VAT for the period from July 2020 to April 2022. The Respondent conducted an audit during this period to verify the Applicant's claimed input tax credits and disallowed input tax credit totaling Shs. 159,889,732 and issued an assessment for the said amount. The Applicant objected to the Respondent's assessment, arguing that the input tax was valid.

In December 2022, the Respondent issued objection decisions disallowing the input tax claims, stating that it could not be authenticated that the premises under construction would generate taxable income, given their residential nature.

Therefore, the issue for determination is whether the Applicant is entitled to the refund of input VAT arising from purchases of construction materials used to construct a building.

Pre-requisites for claiming input tax credits

Section 28 of the VAT Act provides for the circumstances under which a person may claim input tax credits for purposes of calculating the tax payable. The section provides:

*"(1)...a credit is allowed to the taxable person for the tax payable in respect of –
(a) all taxable supplies made to that person during the tax period;
if the supply or import is for use in the business of the taxable person."*

In ***Enviroserv (U) Limited v URA TAT 24 of 2017***, the Tribunal decided that for an Applicant to be entitled to the input tax credit under this section, the Applicant had to prove the following;

- i) The applicant is a taxable person;

- ii) Taxable supplies had been made to the Applicant during the tax period and
- iii) The taxable supplies were for use in the business of the Applicant.

All the above three elements must be present for a claim for input VAT to succeed.

In the present case, the Respondent does not dispute that the Applicant is a taxable person. The Respondent also does not dispute that fact that taxable supplies were made to the Applicant during the tax period.

The Respondent's contention is in respect to condition (iii) only. The Respondent argues that the taxable supplies were not for use in the business of the Applicant because the supplies were in respect of the construction of a building for residential purposes, which is exempt for VAT purposes. The Applicant disagrees with the Respondent's position.

Therefore, the task before the Tribunal is to determine whether the taxable supplies were for use in the business of the Applicant.

The phrase 'use in the business' is defined in section 28 (7) of the VAT Act. It states:

"(7) For the purposes of subsection (1), (2) or (3), "business use" or "use in the business" applies only to the related business, generating a taxable supply".

In view of the above, the key question is whether the Applicant's business is a "related business".

It is not in dispute that the Applicant is engaged in the business of letting properties for commercial purposes. The Applicant has a commercial property and the second property, which is the subject matter of the dispute is under construction. The Applicant stated that they intend to let the property out as serviced apartments depending on the forces of demand and supply at the time when construction is completed.

Whilst the Respondent does not dispute that the Applicant is in business, it seeks to ringfence the input tax claim to the construction project alone and not the entire business of the Applicant. The Respondent argues that the construction project is not a related business, generating a taxable supply.

The Tribunal has considered a similar set of facts in the case of ***Chestnut Uganda Limited v URA, TAT Application no. 94 / 2019***. In that case, the Applicant was constructing the Arena Mall and renting out advertising space as part of its business. The Applicant claimed input VAT arising from the purchase of construction materials used for the construction of the mall. The Respondent disallowed the input VAT credit on the grounds that the Arena mall, for which the Applicant was claiming VAT was still under construction. The Respondent also argued that the taxable supply the Applicant was making related to advertising.

The Tribunal, in finding for the Applicant, held that there was nothing in the VAT Act to restrict the credit for input tax to only one business and that once a taxpayer is registered for VAT, they are entitled to their input VAT.

The above decision of the Tribunal was made on 31 March 2021.

In 2023, the VAT Act was amended to clarify the meaning of the phrase “use in business”, which definition has been stated above.

The effect of the above definition is to restrict the input VAT claim to related businesses generating the taxable supply. This restriction was not in place at the time ***Chestnut*** was decided and hence the Tribunal’s decision regarding the absence of any restrictions in the VAT Act.

When the definition of “use in business” is superimposed into Section 28 (1) of the VAT Act, which lays down the conditions for a claim for input VAT, it effectively states that a

person will be allowed a credit for input tax on all taxable supplies made to that person during the period if the supply is for the related business, generating the taxable supply.

Therefore, the question that should be answered are:

- a) whether the supply of construction materials was in respect of a related business?
- b) whether the related business is generating taxable supplies.

There is no dispute that the Applicant is in business. What is in dispute is whether the Applicant's business, i.e. the development and letting of properties is a related business relative to the kind of supplies made to it, the supplies in question being building /construction materials.

What does the word "related" mean when used in the context of section 28 (7) of the VAT Act. The VAT Act does not define the term "related" and this leaves it open to interpretation. For example, does it mean that the VAT status of the supplies must match the VAT status of the business? Or, does it mean that the nature of the supplies/inputs must be relatable to commercial nature of the business, i.e., that the inputs purchased by that business must be those that the business is ordinarily expected to consume or use?

This raises more than one likely interpretation. Yet, it is a canon of interpretation of tax statutes that one must look at the plain language of the act without making assumptions or inferences (*Cape Brandy Syndicate v IRC (1920) KB 64*),

Therefore, what is the plain meaning of the word "related"?

The **10th Edition of Black's Law Dictionary at page 1479** defines "related" to mean:

"Connected in some way; having relationship to or with something else < a closely related subject".

In addition, the **9th Edition of the Oxford Advanced Learner's Dictionary** defines “related” to mean:

“to be connected with something or somebody”.

Having looked at the above definitions, the following questions come to mind– is the business of the Applicant, namely, the development and letting of commercial property connected to the use of construction materials? When one thinks of the inputs of such a business, what would come to mind? Would it be outlandish to think of the Applicant's business in terms of construction materials and vice versa?

In our view, the Applicant's business is a related business because it is connected with the kind of supplies that that it purchased in the form of construction materials.

The Applicant is in the business of real estate development and the letting of commercial properties. Naturally, its business is connected to the construction materials and likewise, construction materials are connected to real estate development. They are direct inputs in the business of the Applicant.

By way of illustration, let us assume that the business of the Applicant is the provision of car hire services and the Applicant has submitted an input VAT claim arising from the purchase of building / construction materials. One would rightly argue that there is no connection between construction materials and a car hire business. The absence of a connection between the supplies purchased and the nature of the business would render the business non-related.

The second test is whether the Applicant's business is generating taxable supplies? Again, the answer is yes. The proof is in the monthly VAT returns filed by the Applicant which show that in the taxable period for which the refund was sought, the Applicant made taxable supplies (see exhibit A1, pages 1 -119 of the joint trial bundle).

The Respondent has submitted on the intended use of the building under construction as well as the stage of completion being only 40%. In our view, whether the building is eventually let as service apartment or not is inconsequential at this point in time as this is merely speculative. At this stage, it is impossible to determine with certainty what the use of the property will be. Even the Respondent's submission that the property will be used for residential purposes is speculative.

In the present case, the Respondent is attempting to restrict the input VAT claim to an activity of the Applicant as opposed to the business of the Applicant. The Tribunal in ***Chestnut (supra)*** distinguished the business of a taxpayer from the commercial activities of a taxpayer. The Tribunal stated that while construction of the Arena Mall was a commercial activity, it was not the business of the Applicant. In the same vein, the Applicant is in the business of developing and letting properties for commercial purposes. Naturally, in the furtherance of its business objectives, the Applicant undertakes various activities such as the purchase of land, the conduct of surveys and feasibility studies, architectural drawings, obtaining permits and approvals, construction, interior design etc.

The Respondent is attempting to restrict the input VAT claim to the activities of as opposed to the business of the taxpayer. This amounts to reading into the Act non-existent language.

Therefore, in the absence of clear and unambiguous wording in the VAT Act that restricts claims for input VAT to activities which constitute a business, it was unjustified for the Respondent to deny the Applicant's claim.

Lastly, the spirit of input VAT credits is to encourage investment and promote economic activity. The Respondent desires to partake in the harvest only and wants nothing to do with the sowing / investment. Investment precedes and is the bloodline for income generation. Therefore, it is critical that tax administrations are seen to enable and not stifle investment activity.

In conclusion, we find that the Applicant is entitled to the input VAT credit as provided for in section 28 of the VAT Act for the following reasons:

- (i) The Applicant is a taxable person;
- (ii) Taxable supplies were made to the Applicant during the tax period
- (iii) The supplies made to the Applicant were for use in its business.
- (iv) The business of the Applicant is a related business as the Applicant's business of developing and letting properties for commercial purposes is connected to the supplies that were made to the Applicant.

The application is therefore allowed with costs to the Applicant.

Dated at Kampala this 31st day of October 2024



MS. CRYSTAL KABAJWARA
CHAIRPERSON



MR. SIRAJ ALI
MEMBER



MRS. CHRISTINE KATWE
MEMBER

