THE REPUBLIC OF UGANDA

IN THE TAX APPEALS TRIBUNAL OF UGANDA AT KAMPALA

APPLICATION NO. 27 OF 2022

PAC SPA LIMITTED.....APPLICANT

VERSUS

UGANDA REVENUE AUTHORITY.....RESPONDENT

BEFORE: DR. ASA MUGENYI, MR. GEORGE MUGERWA, MS. CHRISTINE KATWE.

RULING

This ruling is in respect of an application challenging corporate tax and Withholding Tax (WHT) assessments of Shs. 7,287,370,395 and Shs 308,096,773 respectively.

The applicant is a company registered in Uganda as a branch of a company incorporated in Italy. It provides construction engineering services to hydro power projects. On 21st June 2021, the respondent conducted a comprehensive audit on the applicant for July 2015 to June 2019. It issued corporation tax assessments of Shs. 7,287,370,395 and a WHT assessment which was eventually adjusted to Shs. 308,096,773. The applicant objected, but apart from adjustments the objection was rejected.

Issues:

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

The applicant was represented by Mr. Cephas Birungyi and Ms. Dorothy Bishagenda while the respondent by Mr. Donald Bakashaba, Mr. Samuel Oseku, Mr. Derrick Nahumuza and Mr. Samuel Kwerit

The applicant's first witness, Mr. Gilbert Rukiri Ariho, a senior tax manager at PKF Taxation Services Ltd, testified that the applicant is a branch of a company incorporated in Italy. It provides construction engineering services. The applicant is a designated WHT

agent. The witness participated in the audit process of the applicant by the respondent. The applicant used a profit margin of 1.1% for the group, for Achwa 1 and 2 projects a margin of 0.54% and for Kigati project 1.1% He stated the profit margin used by the applicant was prepared in accordance with S. 45 of the Income Tax Act. He also stated that there was no need to withhold tax because the goods were imported from a non-resident person. The respondent adopted an industry average profit margin of 4%. However, it failed to show the applicant which industrial averages it used to arrive at the 4% nor the legal authority to use industrial averages. He stated that he did not accept the respondent's rejection of the financial statements and the latter's tax computations relying on profit margin whose comparative indicators were not disclosed.

The respondent's first witness (AW1), Mr. Samuel Lwetutte, an officer in its domestic department testified that the respondent conducted a comprehensive audit on the applicant. It revealed that the applicant had a long-term project for over 12 months. It did not recognize its revenues and costs in line with S. 45 of the Income Tax Act. The applicant provided a profit margin of 1.1% but similar projects had margins of 3 to 5%. He stated that the applicant did not full account for WHT on payments of goods and services and WHT of Shs. 997,254,415 was payable. The respondent issued tax assessment of Shs. 8,115,948,862 for income tax, Pay as You Earn (PAYE) and WHT.

The witness testified that the applicant's deductions and income were not based on percentage of work completed. He contended that income should be reported based on percentage of completion. It is determined by comparing the total costs allocated to the contract, incurred before the year of income with the estimated total costs as determined at the time of commencement of the contract. The income of the period is the percentage of completion multiplied by the total contract sum.

Mr. Samuel Lutete stated that the applicant shared an indicative profit margin of 1.1% even when the industrial margin of similar projects ranges between 3% to 11%. Although the applicant provided bills of quantities, they reflected a breakdown of the contract sums. They did not show the profit margin as required. The respondent used S. 56 of the Income

Tax Act to apply other methods. Based on that the respondent used an estimated profit margin of 4% of similar projects and did not use the proposed 1.1% of the applicant

He stated that the applicant was a designated WHT agent effective 1st July 2018. It did not withhold tax on local supplies under S. 119 of the Income Tax Act. The unreconciled amounts were subjected to WHT resulting in additional WHT. He admitted that the WHT objection was partially allowed and the WHT assessment reduced from Shs. 817,421,421,651 to Shs. 308,096,772. On 31st December 2021, the respondent issued its objection decision increasing the applicant's principal tax to Shs. 8,157,845,322.

The respondent's second witness (AW2), Mr. Isaac Collins, also an officer in its domestic department repeated the evidence of its first witness. He stated that the estimates used were based on the bills of quantities. The respondent used a percentage of 4% profit margin. He stated that the financial statements did not indicate the profit margin. The respondent relied on S. 45 of the Income Tax Act which allows it to use estimates. He also stated that the bare minimum profit margin in construction is 10%. He testified that the applicant did not withhold tax on several suppliers.

The respondent's third witness (AW3), Mr. Henry Mwanji Kibunya testified that he is a quantity surveyor, registered with Uganda Surveyor's Registration Board. He stated that profit margin is determined by several factors. These include the size and magnitude of the project, the nature of the contract and the business environment. He stated that in order to arrive at the profit margin, the costs of the inputs are deducted, Gross profit is obtained and administrative overheads are deducted. After deducting the overheads net profit is obtained. He stated that average profit margin for construction industry is around 5%. For building projects, it is around 10%. The applicant's projects were civil.

The applicant submitted that S. 15(1) of the Tax Procedure Code Act provides that every taxpayer shall for the purposes of a tax obligation maintain, in the English language, records including electronic format, as may be required to determine the taxpayer's tax liability under a tax law. It availed the respondent with all the audited financial statements

and bills of costs of quantities for its project from July 2016 to June 2019. The income assessment for a company is based on its audited books of account. The applicant has consistently filed tax returns and made financial statements in accordance with internationally accepted standards.

The applicant cited *Anupama Chandrakandath v ACIT* (ITAT Cochin) where the court quoted *Nitta Jatiya (Acias & Nitajatia) v. Deit, Central Charge Range* where it was held that ".... the Authority should assess income based on the books of account provided by a taxpayer ...". The court further held that;

> "The Authority failed to discharge its duties properly by assessing using an estimate despite having the taxpayer's books of account which were audited and failing to bring on record any substantial materials to prove that the income estimated was correct."

The applicant provided its audited financial statements, revenue schedules, income booking, addenda to the contracts and cost accounts for each project.

The applicant submitted that the respondent adopted an industry average profit margin of 4% and failed to show the applicant which industry averages were used to arrive at it nor had legal authority to use industry averages. The respondent's witnesses testified that they were not able to provide details of similar projects from which the percent estimated profit margin was arrived at. The applicant submitted that the respondent did not consider any discrepancy or inflation that affects the sector at the time of performing the projects. The percentage cannot be the same for every person. Different companies have different expenses, gains and different losses. Hydropower projects are quite complicated and there are many unforeseen events which could have a negative impact on them.

The applicant submitted that the respondent did not rely on audited financial statements as stipulated by S. 15 of the Tax Procedure Code Act but an estimated profit margin which is not clear. Samuel Lwetutte (RWI) testified that the profit margin was estimated at 4 % and while Isaac Collin Ikuonzi (RW2) testified that it was estimated at 3 %. This evidence is contradictory. While RW2 testified that the estimates used to arrive at the tax payable

were based on the bill of quantities RW1 testified that the estimate was arrived at by looking at the average of other industries but did not provide their details.

The applicant submitted that the respondent's expert witness AW3 testified that he was not availed with the applicant's financial statements and valuations. He further testified that one cannot establish the actual profit margin without looking at the valuations. The question, is how was he able to arrive at a 4% profit margin without looking at the valuations. The witness failed to provide which companies have the same average that is being considered for this case.

The applicant submitted that in *R v Silverlock* [1894] 2 Q.B. 766 the court held that mere submission of opinion by an expert through any certificate or document is not sufficient. Although expertise could be gained from either a field of study or as a result of practical experience, before a court admits evidence of an expert, it must be satisfied that the witness has the appropriate expertise. The court is expected to rule on the qualifications of an expert witness, relying mainly on what the expert himself explains. In the instant case, that expertise was not established by any evidence whatsoever. The applicant also cited *Bamwenyana v Byanguye* (C.A No. 24/2017) where court relied on *Kimani v Republic* (2000) E. A 417 where it was held that;

> "...it is now trite law that while the courts must give proper respect to the opinion of experts, such opinions are not as it were, binding on the courts.... Such evidence must be considered along with other available evidence and if a proper cogent basis for rejecting the expert opinion would be perfectly entitled to do so."

The applicant prayed that the Tribunal finds the opinion by the expert witness inaccurate to form an independent judgment.

The applicant submitted that S. 45 of the Income Tax Act provides for the assessment of long-term contracts for a financial year where a project is not complete. It submitted that S. 45 of the Income Tax Act states that.

"(1) In the case of an accrual-basis taxpayer, income and deductions relating to a long-term contract is taken into account on the basis of the percentage of the contract completed during the year of income.

(2) the percentage of completion is determined by comparing the total costs allocated to the contract and incurred before the end of the year of income with the estimated total contract costs as determined at the time of commencement of the contract.

...

(b) "long-term contract" means a contract for manufacture, installation or construction or, in relation to each, the performance of related services, which is not completed within the year of income in which work under the contract commenced, other than a contract estimated to be completed within six months of the date on which work under the contract commenced."

The applicant submitted that in this case, the contract has been completed. Therefore, imposing a profit margin may not be relevant. Even if the provision was to be used it can only be implemented when the project is still going on. The applicant has since closed business and therefore it is not right to make estimates. One should use the actual costs incurred. The applicant provided supporting documents which the respondent should have relied on, rather than estimate.

The applicant submitted that the respondent acted illegally by applying industrial averages when books of accounts were provided. The applicant submitted that the crux of the matter revolves around the differing accounting methods. The applicant's objection was that the tax assessment was conducted using an accrual basis perspective, which does not align with its chosen cash basis accounting. The applicant submitted that its objection centered on the misapplication of accounting methods by the respondent, leading to variances in the assessment. The divergence between actual settlement and accrual basis accounting has contributed to the dispute

In reply, the respondent submitted that the applicant is liable to pay corporate tax of Shs. 6,944,537,839 and WHT of Shs. 308,096,772. The respondent submitted that the issues for the tribunal to determine are whether the applicant rightly recognized revenue and expenses under S. 45 of the Income Tax Act? And whether the respondent was justified

to disregard the applicant's provided profit margin of 1.1% and to use other methods of allocating costs and revenue to determine a profit margin at 4% based on its best judgment under S. 56 A of the Income Tax Act.

The respondent submitted that the applicant ought to have accounted for revenue under S. 45 of the Income Tax Act. S. 45(4)(b) of the Income Tax Act defines a "long-term contract" to mean;

> "A contract for manufacture, installation or construction or, in relation to each, the performance of related services, which is not completed within the year of income in which work under the contract commenced, other than a contract estimated to be completed within six months of the date on which work under the contract commenced".

The respondent submitted that, the applicant's audited financial statements for the two projects run from 2016 to 2019. It is not in dispute that the contract was a long-term one exceeding 12 months from the commencement date.

The respondent submitted that Note 3 Clause 2(c) of the applicant's financial statements provides for revenue recognition. It provides that contract revenue is calculated on the basis of the value of work completed during the year of income. The financials provide that revenue is recognized by reference to the stage of completion of the contract activity at the end of the reporting period. It is measured based on the proportion of contract costs incurred for work performed relative to the estimated total costs. The respondent submitted that this placed the applicant under the accrual method of accounting for long-term projects. Having established that the applicant was mandated to follow S. 45. In recognizing income and deductions, the respondent applied it. It cited S. 45 of the Income Tax Act, which is stated above. The respondent submitted that S. 45 of the Income Tax Act requires that for accrual basis taxpayers, income and deductions relating to a long-term contract are accounted for on the basis of the percentage of completion of a long-term project for any year of income. However, the applicant's income and deductions were not based on the percentage of works completed.

The respondent submitted that S. 42 of the Income Tax Act provides that;

"(1) A taxpayer who is accounting for tax purposes on an accrual basis- (a) derives income when it is receivable by the taxpayer; and (b) incurs expenditure when it is payable by the taxpayer.

(2) Subject to this Act, an amount is receivable by a taxpayer when the taxpayer becomes entitled to receive it, even if the time for discharge of the entitlement is postponed or the entitlement is payable by instalments.

The respondent submitted that in order to determine the total costs allocated to the contract, the bills of quantities play a crucial role in ascertaining the estimated costs allocated at the commencement of a project, invoices and receipts enable the contractor to determine the actual costs incurred on a project for the accounting year. The bill of quantities, invoices and receipts in totality enable the ascertainment of the percentage of completion for the accounting years.

The respondent submitted that a bill of quantities is a document used in tenders in the construction industry in which materials, parts, and labor (and their costs) are itemized. See (https://en.wikipedia.org/wiki/Bill of quantities cite_note-1). It submitted that the bill of quantities is issued by tenderers to prepare a price for carrying out the construction work. The bill of quantities assists tenderers in the calculation of construction costs for their tender, and, as it means all tendering contractors will be pricing the same quantities (rather than taking- off quantities from the drawings and specifications themselves). It also provides a fair and accurate system for tendering. The applicant's failure to provide bills of quantities rendered it impossible for the respondent to ascertain the costs and profits incurred in the project.

The respondent submitted that the applicant failed to discharge its burden to provide documents for the respondent to rely on in determining the costs allocated and incurred for the construction projects as per the law. The respondent requested the applicant to provide detailed workings showing the project revenues and corresponding estimated costs, which the applicant never availed. The respondent cited R*ed Concepts Limited v Uganda Revenue Authority* Application 36 of 2018 where the tribunal emphasized the crucial necessity of information and documentation when it observed that;

'Where a statute requires one to give information or other particulars, the said information should be accurate to enable public authorities act on it. If the information is false or misleading, the tribunal cannot turn a blind eye to it as this would be tantamount to condoning an illegality and perpetrating fraud.'

The respondent submitted that failure to provide proper documents as mandated by S. 45 of the Income Tax Act to enable it determine costs allocated and incurred in the projects constrained it to use other methods of doing so.

The respondent submitted that it was justified to disregard the profit margin of 1.1% presented by the applicant and use other methods of allocating costs and revenues in determining the profit margin and subsequently the tax payable by the applicant. It submitted that S. 56A of the Income Tax Act provides for methods of allocating costs and revenue. It reads "In determining the chargeable income of a person, use of input-output ratios and other methods of allocating cost and revenue may be applied."

The respondent submitted that, it is trite law that where a tax payer falls within the ambits of the law, it ought to be taxed unless expressly exempted. It cited *Halsbury's Laws of England* 4th Edition Vol. 23 Para. 22 which was quoted in the Kenyan case of *Primarosa Flowers Limited v The Commissioner of Income Tax Income Tax* Appeal 18 of 2013 wherein it was noted that;

"...it is a general principle of fiscal legislation that to be liable to tax the subject must fall clearly within the words of the charge imposing the tax, otherwise he goes free; ...."

The respondent submitted that taxes assessed against the applicant were lawfully levied under S. 4 of the Income Tax Act. The methods used to derive the tax payable were lawfully sanctioned under S. 56 A of the Income Tax Act and are payable by the applicant. The respondent submitted that in *Karl Evans Brown v Commissioner of Income Tax, Downer JA* said at p. 289;

"The cardinal features of the Income Tax Act are the obligation on the tax-payer to furnish particulars of his income to the tax gatherer and the inquisitorial power of the tax gatherer to require such particulars. There is no room for reversal of roles".

The respondent submitted that, the applicant is mandated by statute to file its returns and prepare financial statements in an honest clear manner to enable the respondent act on the same and determine the tax payable by the applicant. The respondent submitted that In *Dennis Murray v Commissioner of Tax Payer Appeals* Civil Appeal 70 of 2007, the Supreme Court of Jamaica held that;

> "It is incumbent on every tax payer to deliver a true and correct return of the whole of his income from every source."

The respondent submitted that the work breakdown schedules provided by the applicant only reflected a breakdown of the contract sums, these could not show the actual costs allocated and incurred as required under S. 45 of the Income Tax Act. That the applicant shared an indicative profit margin of 1.1 percent even when the industrial average of similar projects ranges between 3% to 11%.

The respondent submitted that the self-assessment scheme of the Income Tax Act is premised upon the tax payer making full disclosure of his income from all sources. Where the tax payer does not make full disclosure. The Commissioner has to establish if he has a reasonable or rational basis for believing the tax payer has a tax liability. The Income Tax Act under S. 56A provides for use of other methods of allocating costs and revenue in determining the chargeable income of a tax payer. The respondent submitted that where the tax payer has failed to make their declarations to the Commissioner as in this case, the Commissioner has the powers to use other methods to arrive at the correct tax liability of the tax payer.

The respondent submitted that the assessment was based on the best judgement of the commissioner on information availed to him and on a comparison of industrial averages. It submitted that "best judgement" was elaborately in *Uganda Revenue Authority v Tembo Steels Ltd* Civil Appeal 09 of 2006, where the court citing *Van Boeckel v Customs and Excise Commissioners* [1981] 2 ALL ER 505, 508 noted that Woolf J held:

> "As to this, the very use of the word judgment makes it clear that the commissioners are required to exercise their powers in such a way that they make a value judgment on the material which is before them. Clearly, they must perform that function honestly and bona

fide. It would be a misuse of that power if the commissioners were to decide on a figure which they knew was, or thought was, in excess of the amount which could possibly be payable, and then to leave it to the taxpayer to seek, on appeal, to reduce that assessment. **Secondly,** clearly there must be some material before the commissioners on which they can base their judgment. If there is no material at all it would be impossible to form a judgment as to what tax is due. **Thirdly,** it should be recognized, particularly bearing in mind the primary obligation to which I have made reference, of the taxpayer to make a return himself, that the commissioners should not be required to do the work of the taxpayer in order to form a conclusion as to the amount of tax which, to the best of their judgment, is due. In the very nature of things frequently the relevant information will be readily available to the taxpayer, but it will be very difficult for the commissioners to obtain that information without carrying out exhaustive investigations. In my view, the use of the words 'best of their judgment' does not envisage the burden being placed on the commissioners of carrying out exhaustive investigations. What the words 'best of their judgment envisage, in my view, is that the commissioners will fairly consider all material placed before them and, on that material, come to a decision which is one which is reasonable and not arbitrary as to the amount of tax which is due. As long as there is some material on which the commissioners can reasonably act then they are not required to carry out investigations which may or may not result in further material being placed before them."

The respondent further submitted that Justice Madrama in *Uganda Revenue Authority v Tembo Steels Ltd Civil* Appeal 09 of 2006 stated that.

"The case is persuasive for taking the view that the Commissioners should examine materials placed before them and if they are not satisfied, assess or estimate tax according to their best judgment".

The Court further cited Woolf J. where he quotes from a Privy Council case from India:

"The officer is to make an assessment to the best of his judgment against a person who is in default as regards supplying information. He must not act dishonestly, or vindictively or capriciously, because he must exercise judgment in the matter. He must make what he honestly believes to be a fair estimate of the proper figure of assessment, and for this purpose he must, their Lordships think, be able to take into consideration local knowledge and repute in regard to the assessee's circumstances, and his own knowledge of previous returns by and assessments of the assessee, and all other matters which he thinks will

assist him in arriving at a fair and proper estimate: and though there must necessarily be guess-work in the matter, it must be honest guess-work."

The respondent submitted that, the consistent thread in the above authorities is that an estimate should be based on all available records and materials and an honest assessment or estimate should be made based on these materials.

The respondent submitted that S. 56 of the Evidence Act provides for facts of which court must take judicial notice. It states that.

"(1) The court shall take judicial notice of the following facts-

(a) all Acts and Ordinances enacted or hereafter to be enacted, and all Acts of Parliament of the United Kingdom now or heretofore in force in Uganda;

(2) In all these cases and also on matters of public history, literature, science or art, the court may resort for its aid to appropriate books or documents of reference".

The respondent submitted that these include the Surveyor's Registration Act and the list of registered surveyors published by the surveyor's registration board. A perusal of the gazetted list of registered surveyors in Uganda indicates the respondent's witness (RW3) is duly registered with registration number 133. Therefore, the applicant's submissions on the expertise of the respondent's witness are baseless and without merit.

The respondent submitted that the applicant erroneously contended that the contract had been concluded. Therefore, imposing a profit margin may not be relevant. The applicant has since closed business and therefore it is not right to make estimates. The respondent argued that the contention of the applicant is misconceived and erroneous. S. 4 of the Income Tax Act imposes tax on chargeable income. The applicant's income was rightly subjected to income under S. 4. There is no evidence to support the assertions of the applicant and the same amounts to submitting from the bar.

The respondent submitted that S. 119(1) of the Income Tax Act states that.

"(1) Where the Government of Uganda... or any person designated in a notice issued by the minister, in this Section referred to as the "payer", pays an amount or amounts in aggregate exceeding one million shillings to any person in Uganda

(a) For the supply of goods or materials of any kind; or

(b) For a supply of any services, the payer shall withhold tax on the gross amount of payment at a rate prescribed in Part VIII of the Third Schedule to this Act and the payer shall issue a receipt to the payee."

The respondent submitted that Paragraph 5 of The Income Tax (Designation of Payers) Notice provides that;

"(1) Where any person designated in the Schedule to this Notice as a payer pays an amount or amounts in aggregate exceeding one million shillings to any person in Uganda-

(a) for a supply of goods or materials of any kind; or

(b) for a supply of any services,

the payer shall withhold tax on the gross amount of the payment at the rate prescribed in Part VIII of the Third Schedule to the Income Tax Act, and the payer shall issue a receipt to the payee.

(2) Where-

(a) there are separate supplies of goods or materials, or of services and each supply is made for an amount that is one million shillings or less; and

(b) it would reasonably be expected that the goods or materials, or services would ordinarily be supplied in a single supply for an amount exceeding one million shillings, subparagraph (1) applies to each supply".

The respondent submitted that the Section provides that a designated WHT agent has an obligation to withhold on payments of an amount or amounts which in aggregate exceed 1,000,000. The Income Tax (Designation of payers) Notice 2022 lists the applicant as a designated WHT agent since July 2018 with serial number 6626. The applicant was obligated to withhold on payments made to its suppliers in respect to supply of goods or material of any kind or of services. Where it is reasonably expected that the goods or services would ordinarily be supplied in a single supply for an amount exceeding one million, a payer is obliged to withhold tax. The respondent witness Samuel Lwetutte (RW1) testified that the applicant made payments on supply of goods and services to suppliers that were not exempt from WHT. The respondent submitted that the payments aggregated to more than one million and the applicant ought to have withheld tax on those payments. The applicant withheld tax on some of the payments but was adamant on

withholding tax on other amounts. The respondent submitted that this evidence was not controverted by the applicant.

The respondent submitted that the term 'aggregate' is not defined by the Act. However, the Commissioner General on 18th June 2007 issued a practice note setting out the meaning of the term 'aggregate' in relation to the Act as;

> "a) For purposes of Section 119(1) of the ITA, the word "aggregate" is interpreted to mean the TOTAL PAYMENTS to a supplier in respect of goods or services as provided for in a contract. The threshold of one million shillings is therefore in respect of the total contract value. This implies that separate supplies which constitute one contract of one million and above are subject to 6% WHT irrespective of whether the amount paid at any given time in respect of the supply is less than the threshold provided under Section 11(2)."

The respondent submitted that *Black's Law Dictionary*, 4th Edition defines it as;

> "Aggregate. Entire number, sum, mass, or quantity of something; amount: complete whole, and one provision under will may be the aggregate if there are no more units to fall into that class."

The respondent submitted that where the total combination of all separate supplies of goods or services made to the applicant exceed one million, the applicant is obliged to withhold tax on those payments. The total amounts in the contract sum are considered as a whole irrespective of whether they were paid independently or not as per the Practice Note above. The respondent submitted that in *Goal Relief Development v URA* Application 77 of 2021, the tribunal held that; "The payments should have been tendered in as evidence to show which year they were paid." The respondent submitted that the applicant's witness Gilbert Rukiri contended that WHT included purchases in respect to goods imported. The applicant did not attach WHT returns to show where it had declared the WHT, neither the workings where the applicant contends the respondent incorrectly reconciled its purchases. Gilbert Rukiri did not give any information. The applicant did not call directors or someone who worked on the financials to support the profit margin during the audit or at objection as witnesses

The respondent submitted that in *Uniworks Transporters and Logistics Ltd v Uganda Revenue Authority* Application 62 of 2018, the tribunal held that;

> "The purpose of a financial audit is to provide assurance that financial statements are accurately presently and in conformity with generally accepted accounting principles (GAAP) allowing business owners to make confident business decisions. They are supposed to be relied on by third parties who want to make decisions in respect of the company."

The tribunal also noted that;

> "An audited statement being a proper and correct statement of a company should serve all purposes whether is issued to the respondent or for bid purposes"

The tribunal further noted that;

> "Under the Income Tax Act, a revenue authority should be able to rely on audited financial statements to assess and to arrive at the correct tax payable"

The respondent submitted that the applicant having chosen to account under the accrual basis method, it is illogical for it to turn around and state that it was using cash basis method of accounting. The respondent prayed that the tribunal finds that the applicant is bound by its audited financial statements. It concluded that the liability of Shs. 6,944,537,839 being Income tax and WHT of Shs. 308,096,772 was correctly assessed by the respondent.

In rejoinder, the applicant submitted that it is a rule of the thumb that a tax should not be speculated upon but rather should be levied based on the law, in its exactness. The tax should be certain and not arbitrary. It submitted that even if the Commissioner is to make estimate, such an estimate should be reasonable, based on the applicants audited financial statements and bills of quantities and other information provided by it.

The applicant submitted that the first time the respondent presented a profit margin of 12 % the applicant pointed that it was unrealistic. According to the applicant's company records, the actual profit margin for its activities is usually about 1.1 % This figure can vary according to the factors that determine during the execution of the project.

The applicant submitted that the financial statements were prepared based on the completion method. S.45 of the Income Tax Act does not require the Commissioner to estimate tax based on best judgment. The respondent simply ignored the material documents provided. The applicant submitted that the return provided by the respondent does not provide a percentage of completion, total costs allocated to the contract costs as determined at the time of commencement of the contract. The applicant submitted that the 4% margin is not backed by law. That the respondent did not furnish calculations indicating the revenue to which the 4% was applied.

The applicant submitted that the Shs. 308,096,773 was explained as arising from Meta Camuna imports of raw materials amounting to Shs. 273,508,888 plus interest of Shs. 27,512,122 having been waived by law in the year 2020. The goods in question are under HS Code 9406.90.90, its rate is 25% for other. The respondent relied on S. 119 (1) Income Tax Act to charge WHT. However, S. 119(1) provides that the payer withholds if the payment is made to any local person in Uganda. In this case, the payment was made to Meta Camuna, that is in Italy. Therefore, S. 119 does not apply to the applicant. The applicant is not liable to pay WHT tax assessed. The applicant sought a declaration that it is not liable to pay the tax on the assessment made by the respondent on an estimated profit margin, refund and interest on the 30% tax paid and costs.

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

The applicant provides construction engineering services to hydro power projects. It is challenging corporate tax and WHT assessments of Shs. 7,287,370,395 and Shs 308,096,773 respectively. This corporate assessment was raised by the respondent using a profit margin of 4% which the applicant objected to. In respect of WHT, the respondent contended the applicant was a designated WHT but did not remit WHT.

The applicant witness testified that the applicant used a profit margin of 1.1% for the group and for Achwa 1 and 2 projects a margin of 0.54% and for Kigati project 1.1%. He stated

the profit margin used by the applicant was prepared in accordance with S. 45 of the Income Tax Act. The relevant portion of S. 45 of the Income Tax Act provides that.

"(1) In the case of an accrual-basis taxpayer, income and deductions relating to a long-term contract are taken into account on the basis of the percentage of the contract completed during the year of income.

(2) The percentage of completion is determined by comparing the total costs allocated to the contract and incurred before the end of the year of income with the estimated total contract costs as determined at the time of commencement of the contract.

S. 45((4) (b) defines long term contract. It reads—

(b) "long-term contract" means a contract for manufacture, installation or construction or, in relation to each, the performance of related services, which is not completed within the year of income in which work under the contract commenced, other than a contract estimated to be completed within six months of the date on which work under the contract commenced."

According to the above section it is clear that a long-term contract is one which is not completed within the year of income the contract commences. The respondent audit admitted that the applicant had a long-term project for over 12 months. That means they could not be completed within the year of income. Therefore, the applicant's contract was a long-term contract.

Accrual and cash-based method of accounting are provided for in the Income Tax Act. S. 42 of the Income Tax Act provides that;

"(1) A taxpayer who is accounting for tax purposes on an accrual basis-

(a) derives income when it is receivable by the taxpayer; and

(b) incurs expenditure when it is payable by the taxpayer.

(2) Subject to this Act, an amount is receivable by a taxpayer when the taxpayer becomes entitled to receive it, even if the time for discharge of the entitlement is postponed or the entitlement is payable by instalments.

(3) Subject to this Act, an amount is treated as payable by the taxpayer when all the events that determine liability have occurred and the amount of the liability can be determined with reasonable accuracy, but not before economic performance with respect to the amount occurs".

For a contract that exceeds a year of income, it is difficult to use a cash-based method of accounting as it is still running.

The respondent contended that the applicant's deductions and income were not based on percentage of work completed. It submitted that although the applicant provided bills of quantities, they reflected a breakdown of the contract sums. The applicant did not show the profit margin as required. It contended that the financial statements also did not indicate the profit margin. The respondent contended that income should be reported based on percentage of completion. It is determined by comparing the total costs allocated to the contract, incurred before the year of income with the estimated total costs as determined at the time of commencement of the contract. That the income of the period is the percentage of completion multiplied by the total contract sum. On the other hand, the applicant contended that the contract has been completed. Therefore, imposing a profit margin may not be relevant. Even if the provision was to be used it can only be implemented when the project is still going on. The applicant has since closed business and therefore it is not right to make estimates.

The Tribunal notes that thought the applicant contends that the contract has been completed, it does not state when it was completed. This contradicts the evidence of its witness testified that the applicant used a profit margin of 1.1% for the group and for Achwa 1 and 2 projects a margin of 0.54% and for Kigati project 1.1%. why would use a profit margin which is under an accrual method of accounting when it alleges that the contracts were completed? The applicant's audited financial statements for the two projects run from 2016 to 2019. The respondent's audit was from July 2015 to June 2019. The audited statements were made when the contract was ongoing. Note 3 Clause 2(c) of the applicant's financial statements provides for revenue recognition. It provides that contract revenue is calculated on the basis of the value of work completed during the year of income. The financials provide that revenue is recognized by reference to the stage of completion of the contract activity at the end of the reporting period. It is measured based on the proportion of contract costs incurred for work performed relative to the estimated

total costs. The respondent submitted that this placed the applicant under a burden to use an accrual method of accounting for long-term projects.

The respondent submitted that the applicant provided a profit margin of 1.1% but similar projects in Africa have margins of 3 to 5%. The applicant contended that the respondent acted illegally by applying industrial average when books of accounts were provided. The applicant submitted that the respondent adopted an industry average profit margin of 4% and failed to show which industry averages were used to arrive at it nor had legal authority to use industry averages. The applicant submitted that the respondent in coming up with the figure did not consider any discrepancy or inflation that affects the sector at the time of performing the projects. The percentage cannot be the same for every person. Different companies have different expenses, gains, and different losses. Hydropower projects are quite complicated and there are many unforeseen events which could have a negative impact on the project

The applicant failed to provide documents for the respondent to rely on in determining the costs allocated and incurred for the construction projects as per the law. In *Uniworks Transporters and Logistics Ltd v Uganda Revenue Authority* Application 62 of 2018, the tribunal held that.

> "The purpose of a financial audit is to provide assurance that financial statements are accurately presently and in conformity with generally accepted accounting principles (GAAP) allowing business owners to make confident business decisions. They are supposed to be relied on by third parties who want to make decisions in respect of the company."

The tribunal also further ruled that.

> "An audited statement being a proper and correct statement of a company should serve all purposes whether is issued to the respondent or for bid purposes."

The tribunal further ruled that;

> "Under the Income Tax Act, a revenue authority should be able to rely on audited financial statements to assess and to arrive at the correct tax payable."

In R*ed Concepts Limited v Uganda Revenue Authority Application* 36 of 2018, the tribunal emphasized the crucial necessity of information and documentation when it observed that;

> 'Where a statute requires one to give information or other particulars, the said information should be accurate to enable public authorities act on it. If the information is false or misleading, the tribunal cannot turn a blind eye to it as this would be tantamount to condoning an illegality and perpetrating fraud.'

that In *Dennis Murray v Commissioner of Tax Payer Appeals* Civil Appeal 70 of 2007, the Supreme Court of Jamaica held that "It is incumbent on every tax payer to deliver a true and correct return of the whole of his income from every source."

The Tribunal has already noted that the applicant's project could not be completed in one year of income. Therefore, it involved a long-term contract. Though the applicant alleged that the work was completed, and therefore it did not need to use profit margins, it contradicted itself when it applied them. The applicant failed to provide documents for the respondent to rely on in determining the costs allocated and incurred for the construction projects. Therefore, the applicant ought to have used percentages of the work completed. The respondent was justified in applying S. 45 of the Income Tax Act.

Having determined that the respondent was justified that to apply S. 45 of the Income Tax Act, the next question is whether it used the proper method to reach the assessment. S. 56A of the Income Tax Act provides for methods of allocating costs and revenue. It reads;

> "In determining the chargeable income of a person, use of input-output ratios and other methods of allocating cost and revenue may be applied"

The respondent is allowed to use other methods of allocating costs. The involves using its judgment. That is the respondent is allowed to use its best judgement when it queries the methods applied by the applicant where it has failed to provide relevant documents to enable it make an assessment. However, the best judgement should have a factual basis and should be reasonable. The respondent contends that the applicant did not provide a percentage of work completed in its audited books and bill of quantities. However, it recognizes that the applicant provided a profit margin of 1.1%. The respondent contends that similar projects in Africa have margins of 3 to 5%. The

respondent did not avail information on the similar projects. The respondent's witnesses testified that they were not able to provide details of similar projects from which the percent estimated profit margin was arrived at. Both Samuel Lwetutte (RWI) and Isaac Collin Ikuonzi (RW2) in examination in chief, testified that the respondent used a profit margin of 4%. The respondent's third witness. (RW3), Mr. Henry Mwanji Kibunya testified that the average profit margin for construction industry is around 5%. The evidence on the margins is contradictory. While two of the respondent's witnesses puts the percentage at 4% another puts it at 5%. Mr. Issac Collin Ikuounzi (RW32 in cross examination put the margin at 3%. in A small difference in percentage can make a huge difference in tax liability. These projects involve huge amounts of monies. An improper assessment using a wrong percentage may wipe away the profits a taxpayer has earned or exaggerate it. Therefore, it is important that the respondent gets its profit margin estimates correct. It ought to have looked at margins of similar projects. It should take into consideration, the size and magnitude of the projects, the nature of the contract and the business environment they operate in. Though AW3 put the margin at 5%, he did not indicate which similar civil projects he looked at. A surveyor looks at bill of quantities and is interested in cost management. He cannot determine the profit margin, unless he is privy to the revenue of the person carrying out the project or project amount. There is no evidence that the surveyor looked at incomes of other projects. However, there is no evidence of a financial consultant or analyst who looked at audited financial statements of similar projects. The Tribunal cannot work on assumptions and speculation. Since the respondent did not elaborate at how it come about the percentage of 4% its assessment was not justified. The corporate tax assessment of Shs. 7,287,370,395 is set aside.

In respect of WHT, it is not in dispute that the applicant is a designated WHT agent effective 1st July 2018. The respondent's audit shows that the applicant did not full account for WHT on payments of goods and services and WHT which was adjusted to Shs. 308,096,773. The respondent's audit of the applicant was from 2015 to 2019. The respondent does not indicate the period the applicant ought to have withheld tax. The applicant's witness testified that the WHT was on goods on which it has no obligation to pay WHT. The respondent's witness, Mr. Samuel Lwette testified that the audit

established that the applicant was not withholding tax on local supplies under S. 119 of the Income Tax Act. S. 119 (1) provides that the payer withholds if the payment is made to any local person in Uganda. S. 119 of the Income Tax Act provides that

> "(1) Where the Government of Uganda, a Government institution, a local authority, any company controlled by the Government of Uganda, or any person designated in a notice issued by the Minister, in this section referred to as the "payer", pays an amount or amounts in aggregate exceeding one million shillings to any person in Uganda—
>
> (a) for a supply of goods or materials of any kind; or
>
> (b) for a supply of any services, the payer shall withhold tax on the gross amount of the payment at the rate prescribed in Part VIII of the Third Schedule to this Act, and the payer shall issue a receipt to the payee".

The above Section is clear as it talks about any person in Uganda. Part VIII of the Third Schedule to this Act, does not mention any amount or percentage to be paid if the supply is paid to a non-resident. The applicant submitted that the payment for import of goods was made to Meta Camuna, which is in Italy. Pages 171 to 174 of the joint trial bundle refer to the supplier in Italy. Therefore, if the applicant imported goods, S. 119 of the Income Tax Act does not apply to it. None of the parties addressed us on S. 79 of the Income Tax Act for where income is sourced in Uganda. The Tribunal does not wish to delve into matters that were not addressed to it. Therefore, the applicant is not liable to pay WHT tax assessed under S. 119 of the Income Tax Act.

In the circumstances, this application is allowed with costs.

Dated at Kampala this 31st day of October 2023.

DR. ASA MUGENYI	**DR. STEPHEN AKABWAY**	**MR. GEORGE MUGERWA**
CHAIRMAN	**MEMBER**	**MEMBER**