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THE PROPOSED TAX AMENDMENT BILLS – 2020/2021

Introduction

The 2020/2021 Tax Bills were issued on 1st April 2020 for Income Tax, Value Added Tax, Excise Duty and Stamp Duty. Notably there is no Proposed Bill for the Tax Procedures Code Act yet.

Procedure for Drafting and Approving the Tax Bills.

The Public Finance Management Act 2015 (PFMA) provides prime legislative framework for parliamentary authorization and scrutiny of Government revenue and expenditure. (*Section 13 PFMA*)

The Act mandates the Minister responsible for Finance to present to Parliament tax and revenue bills which gives the Government power to obtain money from taxes, fees, charges and other impositions to be proposed in the annual budget.

The Minister is required to draft a Budget framework paper for the next fiscal year which is presented to Parliament by the 31st December. Parliament has to approval the Budget framework by the 1st of February.

Once the budget framework is approved, the Minister has the mandate to draft the tax bills for the next fiscal year.

Parliament's obligation is to consider and approve the annual budget and any other bills that may be necessary to implement the annual budget for the next financial year by the 31st of May of each year.

Consultation with Stakeholders is a Key Tenet of PFMA

Consultation with Stakeholders is a standard procedure in the process of Parliament approving the proposed budget.

Upon submission of the Bills, the Parliament through the Clerk requests for opinions/views from the Public about the proposed bills before they are deliberated on by Parliament.

The Clerk to Parliament published a notice stating that the Minister responsible for Finance tabled the aforementioned Bills on 31st of March 2020.

The public was informed to obtain the bills from the parliament website and submit views on the bills on line by the 7th of April 2020.



The key highlights of each Bill are expounded below;



Proposed Income Tax Amendments

1. Rental Income

The Bill proposes that a person who owns multiple buildings to file a separate return and pay tax for each building separately. **[Clause 3 (d)]**

Our Observations:

- a) The proposed amendment introduces a concept of taxation based on ownership of buildings in the law rather than taxing chargeable income.
- b) Charging tax on buildings separately would be a departure from the basic principle that charging income tax is based on the persons' "chargeable income" in a year of income. This is radically different from the way other businesses file tax returns and pay tax.
- c) This too will be cumbersome for persons with multiple properties.

The current practice is that a taxpayer aggregates his/her rental income from all sources and its attendant expenses in one return. The return includes details of each property, income from the property and related expenditure.

In the proposed amendment, if a taxpayer for example has 10 buildings, then he/she has to repeat the filing and payment process 10 times just to get the same result as one who filed one return.

- d) Further, the proposed amendment does not define a "building". If a taxpayer has a rented

house which has separate service quarters for workers, common facilities such as toilets, it may be assumed that it is one building.

If, however in the same compound there are four separate buildings with two service quarters but eight tenants. It is debatable how many tax returns and tax payments a taxpayer is supposed to make.

2. Allowable Rental Expenses

The Bill seeks to:

- Amend **Section 5 (3)** replacing the words individual with person. **[Clause 3 (b)]**
- Repeal **Section 5 (3) (c and d)** **[Clause 3 (c)]**
- Amend **Section 22 (1) (c)** by allowing a deduction of 50% of the rental income as expenditures and losses incurred by person. **[Clause 7 (c)]**

This is another major shift in taxation policy.

Our Observations:

- a) Currently, non-individuals (companies, partnerships) are allowed a deduction on all expenses and losses incurred in the production income while individuals are allowed a deduction up to 20%.

The proposed amendments aim to limit all allowable deductions in respect to rental income (for both individuals and non-individuals) to 50% of the gross income.

- b) This means that, persons in the business of real estate may not be able to claim fully, for interest expenses from loans obtained to acquire and construct the properties.



- c) The amendment does not recognise that a person with more than one building may have expenses that are shared, say administration, loan interest and insurance costs etc.

✚ **For example:** Musoke borrowed Ushs. 1 billion and bought property which has 10 semi-detached quarters in 2 Blocks of houses, 2 blocks of servant/guest quarters, 1 block with toilets, bathroom and kitchen. He has 10 tenants who pay Ushs. 1 million per month. He also pays interest on the loan of Ushs. 10 million per month.

Total rent	10,000,000
Interest on the loan	10,000,000
Allowable Deductions at 50%	(50% of 10,000,000) 5,000,000
Chargeable Income	(10,000,000 – 5,000,000) = 5,000,000
Tax at 30%	(30% of 5,000,000) = 1,500,000
Profit after tax	(10,000,000 – 1,500,000) = 8,500,000
Less Loan Interest	8,500,000-10,000,000 = -1,500,000

✚ Musoke will therefore need to find money to top up his loan repayment and cannot claim any deductions on the other expenses.

✚ Further, because of the increased number of returns for each building, bank charges increase which may not be claimable.

3. Corporation Tax

The Bill proposes to impose a tax of 0.5% on taxpayers whose declared tax liability for a consecutive period of five years is less than 0.5% of the gross income. [Clause 2 (c)]

We make the following assumptions in trying to understand the purpose of the policy behind this proposal:

- Every business which operates for years declaring tax losses is hiding the true profit, or

- If it is making losses it must still pay income tax anyway after the 5th year.

We are left to wonder, what has changed since the last time a similar proposal on losses was rejected

Our Observations:

- The provision does not address what happens after the 7th year and the subsequent years.
- It could cause more economic hardships on affected businesses which are at a near loss making position and barely breaking even.
- It goes against the basic principles that Income Tax is charged on “Chargeable Income” and not turnover or gross income.
- It could also discourage investment in capital intensive projects.



4. Investment in Industrial Parks, Free Zones and other business

The provision creates a new regime but doesn't provide a transition for the existing one. **[Clause 6 (b and d)]**

5. Sale or Purchase of Land



The Bill proposes to introduce WHT on a resident person who purchases land, other than land which is a business asset, from a resident person at a rate of 0.5% of the purchase price under S.118B (3). [Clause 8 (3)]

Our Observations:

This is a controversial proposal because:

- a) The Stamps (Amendment) Act, 2016 increased the stamp duty payable on transfer of property from 1% to 1.5% of the total value of the property. The new law would translate to double taxation since the stamp duty payable on transfer of land has not been amended.
- b) The Income Tax Act is silent as to designated withholding tax agent's contrary to the Value Added Tax Act. However, for all intents and purposes, the new law suggests that every purchaser of land will become a withholding tax agent. This will come with its challenges in terms of enforcement and realization of the tax payable.
- c) Further, income in form of capital gains, made on sale of land which is not a business asset is currently exempted from income tax under 21(k) of the Income Tax Act, therefore imposing a withholding tax on an already exempt transaction is creating uncertainty and conflict as to which provision takes precedence.
- d) The ITA (Amendment) Act, 2018 introduced WHT on a resident person who purchases a business or business asset but it did not specify

from whom the tax is withheld (resident or non-resident), however the tax was imposed on persons engaged in real estate business in the year 2019/2020. Could the tax have been illegal?

- e) Is there a minimum amount below which the withholding does not arise?
- f) Do parties have to interpret residence rules?
- g) What happens to person's without TINs?

Unless special regulations are introduced, and withholding agents appointed, it is very unlikely that this provision will be enforced.

6. Withholding Tax on Commission paid to Insurance and Advertising agents.

The Bill proposes to amend Section 118 to introduce Withholding Tax (WHT) on Commission paid to Insurance Agents and Advertising Agents at a rate of 10% of the gross amount. [Clause 9]

Our Observations:

Previously, guidance on taxing Insurance Agents was provided in a Practice Notice issued by the Commissioner General on 18th June 2007.

The questions are:

- Who is an advertising Agent?
- If the tax withheld is on gross payment, what happens when the actual commission is less than the tax withheld? For example, a taxpayer is paying premium of Ushs. 1 million through an agent to an insurance company and the agent receives a commission of 10% (100,000). The Insurance company will be required to deduct from the gross payment of the agent [Ushs. 100,000] at 10%

The rate of 10% may be too high.

7. E-invoicing

Clause 7 of the Bill proposes to disallow expenses of a person who purchases goods or services from a supplier who is designated to use the e-invoicing system unless the expenses are supported by e-invoices or e-receipts.

This follows the law under S.73A, B of the Tax Procedure Code Act.



Proposed Value Added Tax Amendments

1. Input Tax Credit for manufacturers

The Bill proposes that in the case of manufacturers, the supply or import should have occurred not more than 12 months before the date of registration. [Clause 2 (a)]

The VAT Act currently allows a tax credit on income tax incurred provided the supply or import of goods occurred not more than six months prior to registration (before the time they start making taxable supplies).

Our Observations:

- a) This is a very big incentive for manufacturers.
- b) But the question as to who a manufacturer is will remain an area of contention even if regulations and practices are issued.

2. Input Tax on Incomplete Buildings

Clause 4(b) of the Bill proposes that an owner of a commercial building should not claim tax credits on inputs used in the construction of an incomplete building against the tax collected from a completed commercial building.

- c) The amendment creates confusion because the VAT Act allows a registered person making taxable supplies to claim input tax. Sections 6,11,12,18,21, 25 have not been amended.
- d) There will also be challenges in apportionment of input tax when dealing with mixed supplies.
- h) Further, the word 'incomplete' should be defined. A building may have several floors, wherein some are complete and occupied thus making taxable supplies but some floors are incomplete, what happens then? Should the taxpayer not charge VAT because the building is incomplete?

3. Tax Accounting on Commercial Buildings

To run in tandem with the Income Tax provisions, *the Bill proposes that an owner of more than one Commercial building should account for tax for each building separately [Clause 2(b)].*

Our Observations:

- a) This proposal goes against both accounting and best tax practices whereby all transactions of the same person are treated uniformly.

This may discourage or kill investment in commercial property.
- b) In respect to accounting for each property separately, the logic vanishes when one considers the administrative charges where it become illogical to separate.
For example, in the case of a taxpayer who hires labour, and buys materials from the same supplier to repair 10 buildings.
- c) In order for this provision to work, it means the purchases for each building have to be on a separate invoice showing the name or location of the building. The tax payer will be required to file 10 separate VAT returns and make 10 payments for each building. For income tax if it is a company, file 10 returns every six months (20 in total) and payments.

If it is an individual 10 returns every three months and payments (40 in total) per year.

This will make it cumbersome for taxpayers to file separate tax returns and make several payments contrary to canons of simplicity and convenience.

Does this ultimately increase tax?

- d) What the owners of commercial properties are being required to do can be likened to a supermarket owner who is required in its tax return to separate returns for food, toys, clothes etc.

Other questions that arise are:

- ✚ Why does the Government want the real estate sector to account for taxes different from other sectors?
- ✚ Has this tax regime been tested elsewhere in the world and been found viable?
- ✚ Has the Government studied the administrative challenges that would face taxpayers affected by this amendment?



4. Offset and Refund

The Bill proposes to limit the offset period to three months after which the tax payer shall be required to apply for a refund [Clause 3].

The VAT Act currently allows a refund or credit for input tax incurred on goods that are destroyed, lost and cannot be recovered.

Our Observations:

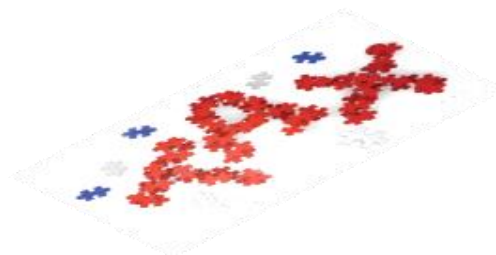
- a) This provision should be okay but practice depicts that some refunds may take up to two years.
- b) The process affects the taxpayers cash flows, it is time consuming and costly for taxpayers which makes the offset option better.
- c) For this provision to be effective, it is important that there should be more efficient refunds mechanism policies unlike the current practice were refunds are denied on the ground that every refund must follow an audit.

5. Exempt Supplies

The Bill proposes to exempt the following supplies:

- Digital Stamps
- Trailer for agriculture purposes and combine harvesters
- Cotton Seed Cake
- Royalties paid in respect of agriculture technologies
- Tourist Hotels and Lodges among others.

We note that the definition of a hotel or lodge is not provided.



STAMP DUTY

Proposed Stamp Duty Amendments

Professional Licences/Certificates

The Bill proposes to amend Schedule 2 of the Act by inserting Item 63A to provide for payment of Stamp Duty on professional licences or certificates amounting to Usbs 100,000 [Clause 1].

Our Observations:

- a) The Act provides for instruments chargeable with duty. Instruments are said to include; documents by which a right or liability is, or purports to be, created, transferred, limited, extended, extinguished or recorded. Is a licence an instrument?
- b) Professionals pay annual subscription and licence fees to their respective authorities / organizations. Adding an extra charge will be an unnecessary burden.



Proposed Excise Duty Amendments

Clause 2 of the Bill proposes to amend the Second Schedule to the principle Act to vary the duty on excisable goods focusing on alcohol, spirits, soft drinks and petroleum among others.

Our Observations:

- a) The Bill is seen to reduce the duty and give exemptions to boost businesses engaged in fresh juice, vegetables, tyres, mattresses, tooth paste among others. This may increase investment in those sectors.
- b) The Bill proposes to amend Part 1 of the Second Schedule by increasing excise duty rates on fuel (specifically gasoline) from UGX. 1100 to UGX. 1350 per litre, gas oil from 880 per litre to 1030 and Kerosene from UGX. 200 to UGX. 300 per litre.

Given the certainty of an effect of increase of fuel costs on many other sectors of the economy, the rate should be reconsidered.

Kerosene is an essential commodity used by many Ugandans; therefore, the rate should be reconsidered as it may render it expensive and hard to access.

Conclusion

As much as the objective of Government is to increase tax revenue, they should be guided not only by the principles and canons of Taxations but also the practicability of the taxes.



Readers are informed that the views, thoughts and opinions expressed in this article belong solely to the author and not anyone else.

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