THE REPUBLIC OF UGANDA

IN THE TAX APPEALS TRIBUNAL AT KAMPALA

TAT APPLICATION NO. 28 OF 2018.

PLATINUM CREDIT LIMITED :: APPLICANT

VERSUS

UGANDA REVENUE AUTHORITY :: RESPONDENT

BEFORE: DR.ASA MUGENYI, DR. STEPHEN AKABWAY MRS. CHRISTINE KATWE

RULING

This ruling is in respect of an application challenging an income tax assessment of Shs. 1,708,059,626 for bad debts written off and foreign exchange loss.

The applicant is engaged in the business of money lending. The respondent conducted an audit on the applicant's tax affairs for the period 2014 to 2015 and raised an assessment of Shs. 4,457,744,406. The applicant objected to the assessment on 19th March 2018. The respondent partially allowed the objection and revised it to Shs. 1,708,059,626. The objection was rejected on grounds that the applicant had not taken reasonable steps to recover bad debts before writing off and no evidence had been provided to prove foreign exchange loss.

The following issues were framed.

1. Whether the applicant is liable to the taxes assessed by the respondent?
2. What remedies are available?

The applicant was represented by b Mr. Patrick Kabagambe while the respondent by Ms. Diana Prida Praff and Mr. Tony Kalungi.

The applicant called one witness, Mr. Martin Muchimuti, its finance manager. He testified that the applicant provides credit facilities to employees. He testified that between 2009 and 2013 the applicant received funding worth US$ 3,300,000 from Platcorp Holding

Limited and Platcorp Management Limited to finance its business. Between May 2011 and December 2012, the applicant received an additional £ 620,000 from Platcorp Holding Limited. He testified that upon conversion of 620,000 British pounds into United Stated dollars ($), the total amount was US$ 4,242,338. He further testified that around September 2013, the applicant paid Platcorp Holdings Limited Shs. 2,177,424,824 at a dollar rate of 2,636 and Shs.1, 063,980 at a rate of 2,570. He testified that in 2014, the applicant paid Platcorp Holdings Limited US$ 678,093 and in 2015 US$ 2,500,000. In 2015, the applicant borrowed US$ 225,000 from Platcorp Management Limited and repaid Shs. 812,199,346 at the dollar rate of 3,493.

He testified that, on 31st March 2015 the applicant's board of directors wrote off bad debts of Shs. 675,000,000 for the year ending 2014, On 8th December 2015 the directors wrote off debts Shs. 40,900,000 from the private sector and Shs. 3,074,080,634 from civil servants. In 2016, the respondent issued an assessment of Shs.4, 475,744,406. The applicant objected to the assessment. The respondent revised the assessment to Shs. 1,708,059,625. Mr. Muchimuti testified that the applicant availed documents to the respondent to show the steps it took to recover bad debts. It hired debt collectors.

The respondent's witness, Mr. Bans Busingye, an Officer in its Objections and Appeals Unit testified that the respondent conducted a desk audit on the applicant for the period 2014 to 2015 and issued an assessment Shs. 4,475,744,406.70. The applicant objected to the assessment. Upon review of information availed by the applicant, the objection was partially allowed and the assessment reduced to Shs. 1,708,059,625. He testified that the applicant did not adduce evidence of foreign loans obtained and did not take adequate steps to recover the loans. He further testified that the applicant's audited accounts contradicted its bad debt schedules. When some of the debtors were contacted they confirmed that they had paid the loans. The applicant did not provide a memorandum of understanding with the police yet the majority of the debts written off were for them. The taxpayer did not provide information to show how much was recovered and what was outstanding at the time of recovery. The amount written off for one Stephen Segirinya was more than the principal and interest. The applicant failed to demonstrate the steps it

took to recover the loans before writing off. In cross examination Mr. Busingye testified that the respondent called only four defaulters out of a thousand. The respondent was aware that the applicant engaged a team of debt collectors.

In respect of the foreign exchange loss of Shs. 147,544,000 for the year ended 2014 and Shs. 1,708,419,000 for the year ended 2015, Mr. Busingye testified that the applicant did not provide sufficient proof of receipt and payment of the alleged loans from Platcorp Holding Limited. For the year 2014 the respondent could not trace a receipt of US$ 2,863,489. For the year 2015, the respondent could not confirm receipt of any loan other than Shs, 805,053,000 by the applicant from Platcorp Holding Limited.

The applicant submitted that the respondent disallowed the applicant's expenses for bad debts written off and foreign exchange loss. It cited S.24(3) of the Income Tax Act which defines bad debt to mean a debt claim in respect of which the person has taken all reasonable steps to pursue payment and which the person reasonably believes will not be satisfied. The applicant argued that the Income Tax Act does not define what is "reasonable". The applicant cited **Andes (eas) Limited v Akoong Wat Mulik Systems** Civil Suit No.184 of 2008 where Justice Hellen Obura held that the question of what was reasonable was not a question of law but fact in the circumstances of each case, the burden of proving being on the defendant. The applicant also cited **Black's Law Dictionary** 8th edition at page 1293 to define reasonable as fair, proper or moderate under the circumstances. The applicant submitted that it took all the reasonable steps to recover the bad debts. Its witness testified about recovery process. In the event of default, the applicant writes to employers demanding payment and the employer writes to the applicant stating the reasons for default. The applicant submitted that its debtors were civil servants who borrowed small amounts and it was not economically tenable to engage lawyers to sue defaulters. The applicant contended that it took reasonable steps before writing off bad debts.

As regards the foreign exchange loss, the applicant submitted that between 2009 and 2013, it borrowed in foreign currencies from Platcorp Holding Limited, Platcorp

Management Limited, Warren Barret and Dannyl Hill. In paying back the loans it incurred foreign exchange loss when converting the borrowings into dollars. The applicant declared the losses in the financial year 2014 to 2015. The applicant cited S. 48 (1) of the Income Tax Act which provides that foreign exchange gain is included in the gross income while foreign currency debt losses are deductible. S. 48 (3) provides that a foreign currency debt loss incurred by a taxpayer during a year of income is allowed as a deductible to the tax payer in that year. The applicant argued that it borrowed money at a dollar rate of 2,793 to 2,842 and at the time of repaying the loan in 2015, the dollar rate was ranging from 3,475 to 3,490. The applicant submitted that S. 48 (8) provides a tax payer incurs a foreign currency debt loss if a) Where the tax payer is a debtor, the amount in shillings of foreign currency debt incurred by the tax payer is less than the amount in shillings required to settle the debt or b) Where the taxpayer is a creditor, the amount in shillings of the foreign debt owed to the taxpayer is greater than the amount in shillings paid to the taxpayer in settlement of the debt. S. 48 (10) provides that a foreign currency debt loss is incurred by a taxpayer in the year of income in which the debt is satisfied. The applicant contended that it fulfilled the provisions of the law and the bank statements on record show that it borrowed the money between 2009 to 2013 and it paid back the loans in 2014 to 2015.

In reply, the respondent argued that the applicant is not entitled to claim for bad debts written off. The respondent argued that the provisions are only allowable deduction for financial institutions. The respondent cited S. 2 (dd) of the Income Tax Act which defines a financial institution as any person carrying on the business of receiving funds from the public. The respondent argued that provision for bad debts are only allowed to financial institutions as provided under the Practice Note issued 2nd November 2001. The applicant further submitted that the applicant is a money lender and does not receive deposits from the public. The respondent also contended that the applicant did not take reasonable steps to recover bad debt as required by S. 24 of the Income Tax Act.

The respondent submitted that the applicant did not incur any foreign exchange loss. The respondent contended that the applicant did not provide sufficient proof of receipt or

payment of the purported loans. There was variance in the amounts received and the documents in support of the loans some were not signed. The respondent contended that the applicant did not satisfy the requirements of S. 48 of the Income Tax Act. The respondent cited **Top Serve (T) Limited v Commissioner General** [2002] TTLR 78 where the tribunal noted that its task has been simplified by the fact that no receipts of acknowledging actual payments of the claimed foreign exchange losses of Tshs. 204,800,000 for the year 2000 and Tsh. 160,000,000 for the year 2001 were produced by the appellant company. For that reason the appellant company could not justify its claim of foreign exchange losses.

In rejoinder, the applicant reiterated that it took all the reasonable steps to recover the bad debts. It cited **Cape Brandy Syndicate v IRC** [1921] KB 64 where court held that in interpreting taxing Acts, one must look at what is clearly said. There was evidence of receipt of the loans and repayment of those loans. The applicant argued that it incurred foreign exchange loss in repaying its loans.

Having listened to the evidence of both parties, perused their exhibits and submissions this is the ruling of the tribunal.

The applicant is engaged in the business of giving credit. The dispute between the applicant and the respondent revolves around two issues. The first issue; whether the applicant is allowed a deduction for bad debts and secondly whether the applicant incurred any foreign exchange losses. The respondent contends that the provision for bad debts written off is only applicable to financial institutions which the applicant disputes.

S.15 of the Income Tax Act provides that the chargeable income of a person for a year of income is the gross income of the person for the year less total deductions allowed under this Act for the year. Deductions are provided for under S. 22(1)(a) which states that all expenditures and losses incurred by a person during a year of income to the extent to

which the expenses and losses were incurred in the production of income included in gross income are deductible. A bad debt is deductible under S. 24 of the Act which reads:

> "(1) Subject to subsection (2), a person is allowed a deduction for the amount of a bad debt written off in the person's accounts during the year of income;
>
> (2) A deduction for a bad debt is only allowed -
>
> a) if the amount of the debt claim was included in the person's income in any year of income;
>
> b) If the amount of the debt claim was in respect of money lent in the ordinary course of a business carried on by a financial institution in the production of income included in gross income.
>
> c) If the amount of the debt claim was in respect of a loan granted to any person by a financial institution for the purpose of farming, forestry, fish farming, bee keeping, animal, and poultry husbandry or similar operations."

The respondent contended that the applicant is not a financial institution. A financial institution is defined in S. 2 (dd) to mean

> "any person carrying on the business of receiving funds from the public or from members through the acceptance of money deposits repayable upon demand, after a fixed period, or after notice, or any similar operations through the sale or placement of bonds, certificates, notes or other securities, and the use of such funds either in whole or part for loans, investments or any other operation authorized either by law or by customary banking practices, for the account and at the risk of the person doing such business."

When interpreting a provision in an Act it is necessary to read the other provisions of it. A taxing Act has to be considered as a whole. In **Commissioner of Inland Revenue v Alcan New Zealand Limited** 1994 3 NZLR 139. Where it was stated that "… the true meaning must be consonant with the words, used having regard to their context in the Act as a whole and to the purpose of the legislation to the extent that it is discernable." In order to understand S. 24(2) clearly, one has to read S. 24(3) which reads:

> "In this Section,
>
> (a) "bad debt" means –

(i) a debt claim in respect of which a the person has taken all reasonable steps to pursue payment and which the person reasonably believes will not be satisfied; and

(ii) in relation to a financial institution, a debt in respect of which a loss reserve held against presently identified losses or potential losses, and which is therefore not available to meet loses which subsequently materialise, has been made; and

(b) "debt claim" means a right to receive a repayment of money from another person, including deposits with financial institutions, account receivable, promissory notes, bills of exchange, and bonds.

A reading of S. 24(3) shows that under clause (i) a bad debt applies to any person while under clause (ii) it is in relation to a financial institution. A person is defined under S. 2(yy) to include an individual, a partnership, a trust, a company a retirement fund, a government, a political subdivision of a government and a listed institution. While under clause 2(i) a person has to show that it has taken all reasonable steps to pursue payment under clause 2(ii) for a financial institution it has to show the debt is held against losses or is not available to meet losses. Therefore to say that bad debt maybe allowed as deductions for only financial institutions may defeat intentions of the legislature. It would also mean that all persons other than financial institutions cannot deduct their bad debts. That would be a discriminatory tax practice that would defeat business goals.

For a debt to be written off and deductions allowed, a taxpayer must satisfy the following conditions; Firstly, the amount of the debt claim must have been included in the person's gross income in any year of income and secondly, a debt claim in respect of which the person has taken all reasonable steps to pursue payment and which the person reasonably believes will not be satisfied. Having found that the bad debt provision is not limited to financial institutions, the Tribunal has to ask itself: whether the applicant took all reasonable steps to pursue payment? person reasonably believes will not be satisfied. The word reasonable is not defined by the Income Tax Act. In **Andes Limited v Akonng Wat Mulik Systems and another** Civil Suit 184 of 2009 Justice Obura cited **African Highland Produce Limited. v Kisora** [2001] EA 1 where it was stated that: "… The question of what was reasonable was not a question of law but of fact in the

circumstances of each particular case, the burden of proving being on the defendant." **Black's Law Dictionary** 10th Edition p. 1458 defines reasonable as"1. Fair, proper, or moderate under the circumstances; sensible." In order to perceive whether the measures were reasonable one has to look at them through the eyes of a reasonable person and not those of a banker, a lawyer, a tax offical or a judge. The term "reasonable person" is defined by **Black's Law Dictionary** (supra)p. 1457 as

> "1.A hypothetical person used as a legal standard, esp. to determine whether someone acted with negligence, specif., a person who exercises the degree of attention, knowledge, intelligence, and judgement that society requires of its members for the protection of their own and of others' interests. The reasonable person acts, sensibly, does things without serious delay, and takes proper but not excessive precautions."

Black's Law Dictionary 10th Edition p. 484 defines a bad debt as"a debt that is uncollectible and that may be deductible for tax purposes. So the question is: Did the applicant take reasonable measures to recover the bad debts?

So if one were to ask did the applicant take reasonable steps to recover the bad debts? The respondent contended that the applicant did not adduce sufficient evidence to justify writing of bad debts. There were inconsistencies in the figures reported as bad debts in the applicant's online returns. Whether a debt is wholly or partly and to what extent bad debt is irrecoverable is a question of fact to be decided by the tribunal using the lens of a reasonable person. Mr. Martin Muchimuti the applicant's finance manager testified that on 8th December 2015, the board of the applicant wrote off bad debts of Shs. 3,074,080,643 for 1,030 civil servants and Shs. 41,527,834 for private sector defaulters. The applicant contracted Quest Holdings Limited to recover the bad debts which wrote a report regarding bad debts written off for 2014. The reasons for writing off the bad debts in the report were due to death of the borrower, dismissal from work, abscondment from duty, off payroll, telephone numbers were off and unknown transfers.

The respondent is aware that the applicant hired debt collectors to collect the bad debts. The debt collector presented reports to the applicant, exhibits A13 to A15. The reports stated the measures that were taken by the debt collectors. The reasons varied. At this stage, the Tribunal is not interested in the reasons but the measures used by the

applicant. Appointing debt collectors to collect debts cannot be said to be unreasonable. The applicant also adduced evidence from the different district local governments and showing the reasons why defaulters working in the said institutions were not paying off their loans. The communications explaining the reasons cannot be said to be unreasonable. The fact that the debts were not recovered does not mean that the applicant did not take reasonable measures. A measure can still be reasonable though effective. In **F.E Dinshaw v The Commissioner of Income Tax Bombay (1934) 50 TLR 527** the court noted that a debt might be bad even though the debtor continues to trade. The respondent contended that the applicant did not sign a memorandum of understanding with the Uganda Police. A memorandum is a collection measure and not a recovery one. The respondent contended that approval of a debt write off is by a board resolution and not board minutes. Board resolutions are extracted from board meetings which are covered in minutes. The respondent was perturbed by the applicant's decision not to engage lawyers to sue defaulters because of the small amounts. This is best understood by an English saying: one cannot use good money to chase bad money. If the amounts are small and it would be cumbersome to sue, the applicant is entitled to its decision not to sue. In light of the evidence adduced by the applicant, there were reasonable steps taken to recover the bad debts.

Lastly, the respondent contended that the applicant declared in its online returns and audited accounts, exhibits R2 and A5, a bad debt of Shs. 135,000 for the year 2014. For the year 2015 the applicant did not declare any bad debts. There is no explanation as to why the figures declared in the online returns, and audited accounts differ from those in the board minutes. Did the auditors query the authenticity of documents tendered in by the company? S. 24 of the Income Tax Act allows a person a deduction for the amount written off in the person's accounts. The amount of bad debt in the minutes or a board resolution should be reflected in the person's account. Taxes are determined by what is stated in the audited financial accounts as it is signed by directors as a true and fair position of the company's state of affairs. The directors acknowledge that they are free of material misstatement, whether due to fraud or error. In the circumstance, in the absence of any other amended financial statement and returns, the respondent ought to go by

what is stated in the financial statements and returns. In short, the board minutes and other documents that contradict the financial statements and the returns should be ignored.

As regards the issue of foreign exchange loss S. 48 (3) of the Income Tax Act provides that a foreign currency debt loss incurred by a taxpayer during a year of income is allowed as a deduction to a taxpayer in that year. The applicant adduced evidence and or submitted that it borrowed from four lenders: Platcorp Holding Limited, Platcorp Management Limited, Danny Hill and Wayne Barratt to finance its operations. The applicant converted pounds into dollars for ease of payment. In exhibit A1, the applicant shows that in 2013 it borrowed US$ 3,300,000 and British pounds 620,000 from Platcorp Holdings Limited. The total value was US$ 4,242,338. It borrowed from Platcorp Management Limited US$ 225,000000 in 2015. The bank statements are attached in exhibit A2. In exhibit A3, the applicant shows that it paid back Platcorp Holding Limited US$ 225,000 in 2015 and made a loss of Shs. 38,337,750; in 2014 it paid borrowings of 678,093 and made a loss of Shs. 160,598,416. It repaid US$ 2,500,000 in 2013 and made a loss of Shs. 2,202,650,000. The respondent disputed the foreign exchange losses. The respondent contended that the taxpayer did not provide sufficient proof of receipt and repayment of the alleged foreign currency loans.

The Tribunal notes that there are no loan agreements. For the period under review the applicant has not provided sufficient proof of the repayment of the purported loans. The testimony of Mr. Martin Muchimuti and exhibits A1 and A2 were to the effect that the applicant borrowed from Platcorp Management Limited. The financial statements of 2014 and 2015 do not show any borrowings from Platcorp Management Limited. They show borrowings from NC Bank Uganda Limited and Danny Hill. NC Bank is situated in Uganda. The notes in the statements show that the loan of Danny Hill relates to a balance of British pound 100,000 from one of the related parties. The figures in exhibits A1 and A2 do not tally with those in the financial statements. The financial statement of 2014 show that the exchange difference in 2014 was a gain of Shs, 13,037,000 while there was a loss 16,176,000 in 2013. The financial statement of 2015 shows that in 2105 the exchange

difference was a gain of 78,396,000. Where the evidence is contradictory, the Tribunal will not take it into consideration. The witness who testified is a financial manager, his evidence is not sufficient to contradict what the directors have averred as accurate in the financial statements.

Taking the above into consideration, this application is dismissed with costs to the respondent.

Dated at Kampala this day of 2020.

DR. ASA MUGENYI
CHAIRMAN

DR. STEPHEN AKABWAY
MEMBER

MS. CHRISTINE KATWE
MEMBER