FOR GOD AND MY COUNTRY

PARLIAMENT OF UGANDA

REPORT OF THE COMMITTEE ON FINANCE, PLANNING AND ECONOMIC DEVELOPMENT ON THE INCOME TAX (AMENDMENT) BILL, 2020

OFFICE OF THE CLERK TO PARLIAMENT
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1.0 Introduction

The Income Tax (Amendment) Bill, 2020 was read for the first time on the 31st March, 2020 and referred to the Committee on Finance, Planning and Economic Development in accordance with Rule 128 of the Rules of Procedure of Parliament.

2.0 Object of the Bill

The object of the bill is to;

(a) introduce a minimum tax rate to apply to taxpayers whose declared tax liability for a consecutive period of five years is less than 0.5% of gross income;

(b) to revise the tax rate applicable to individuals and companies for purposes of rental income;

(c) to provide for a ceiling on deductible expenses on rental income;

(d) to provide for incentives of existing investors;

(e) to impose withholding tax on sale of land other than a business asset;

(f) to introduce a new tax regime for small businesses;

(g) to exempt the income of the Islamic Development Bank from Income Tax and the income of Deposit Protection Fund from Income Tax;

(h) to impose withholding tax on commissions paid to insurance and advertising agents; and for related matters.

3.0 Methodology

The Committee held meetings and received submissions from the following:

1. The Minister of Finance, Planning and Economic Development;
2. The Uganda Revenue Authority;
3. The National Social Security Fund;

4. The Private Sector Foundation;
5. The Civil Society Budget Advocacy Group (CSBAG);
6. The Tax Justice Alliance Uganda (TJAU);
7. The Uganda Law Society;
8. M/s Meera Investments ltd;
9. PricewaterhouseCoopers;
10. Hon. Agnes Kunihira
11. Hon. Dr. Michael Bukenya
12. Mr. Dunstan Sendiwala
13. Khadhar Investments Limited
14. Mr. Tindyebwa Obed
15. MK
16. Mr. Dunstan Sendiwala
17. Mr. Jim Middleton

4.0 OBSERVATIONS BY THE COMMITTEE.

4.1 Clause 2 of the Bill proposes to introduce a minimum tax rate to apply to taxpayers whose declared tax liability for a consecutive period of five years is less than 0.5% of the gross income. According to the Minister, "It has been discovered that most of them *(taxpayers*) take advantage of the generous tax provisions or engage into aggressive tax planning not to pay tax".

- This proposal has hitherto been rejected by Parliament for the last 2 FYs.

- The 0.5% is tax on turnover of companies that may be in a loss or near – loss income position and therefore goes against the basic principle that income tax is charged on income (not turn over).

- As the country strives to industrialize, this proposal will discourage potential long term investments which may take 10 and more years without making taxable profits but with potential for growth and employment, especially real estate, industrial and agricultural projects.

- Since the (loss or near – loss) tax liability is arrived at after allowing the tax payer tax deduction and other tax incentives, the proposed tax may indirectly result into non-recognition of tax deductions recognized under other tax laws,

- In order to curb any fictitious or incorrect tax declarations, URA should strengthen its tax administrative measures to identify such tax payers.

4.2 CHANGES TO THE TAXATION OF RENTAL INCOME.

4.2.1 Under the current Act, 20% of the rental income is allowed as expenditures and losses incurred by an individual in the production of the rent. However, **Under Clause 3 (b) read together with Clause 7(a)(i), the bill proposes that for rental income purposes, only 50% of the rental income should be allowed as expenditures and losses incurred by persons in the production of such income.**

- This means that whether it's an individual or company, the expenses or losses allowable for purposes of determining chargeable income will be capped at 50% of the rental income.

- This denies corporate persons deductions of legitimate capital and operational expenses incurred on deriving rental income thus contravening principles of taxation and unfairly disadvantage the taxpayer.

- Tax payers in the real estate sector should have the right to receive deductions for all the supportable expenses incurred in deriving the rental income.

4.2.2 Clause 3(d) proposes that a person who owns more than one building should account for income and expenses, and pay rental tax for each building separately.

- Currently, rental incomes and expenses from various buildings owned by the same person are aggregated while accounting for rental tax by that person.

- The proposal will increase the costs of administration from the companies who own several buildings. It further ignores the synergies that require a taxpayer, *for example*, a real estate developer, to run all their projects as part of one business with all the expenses incurred applying collectively across income from all buildings.

- Income tax is chargeable on the "gross income" of each tax payer which allows for accounting for income tax on the aggregated income of a single tax payer. Therefore, accounting for rental tax separately for each building may work against this principle that, for tax purposes, allows a tax payer to offset the losses incurred from one income stream from the profits in another income stream of the same tax payer.

4.2.3 Clause 16 proposes to increase the rate of tax for an individual from 20% to 30%. The proposal is intended to remove any distinction between the treatment of buildings owned by companies and those owned by individuals. It therefore means that individual and campiness will be subjected to the same rate of tax on their rental income.

4.3 Exemptions

4.3.1 Clause 6 (a) seeks to (i) exempt the income of the Deposit Protection Fund from income tax. The Deposit Protection Fund is a statutory body created under S.108 of the Financial Institutions Act, 2016 to provide insurance for the deposits for depositors in case of closure of a regulated financial institution. The proposed treatment is akin to that of Bank of Uganda whose income is exempt.

4.3.2 Clause 6 (b) to provide more clarity on how the incentives will be assessed, including manufacturers of tyres, footwear, mattress or toothpaste as persons entitled to the incentives and providing for incremental investments that can benefit from the incentives.

- Increase to seventy percent (70%) To ensure that this benefits a larger proportion of the local economy. This can also be instrumental in enhancing and strengthening forward and background linkages between the free zones and or industrial parks and Uganda's farmers, who comprise 80% of the local economy.

4.4 Deductions for expenses supported by e-invoices

Clause 7(b) of the bill proposes that expenses of a person who purchases goods and services from a supplier who uses the e-invoicing system shall not be allowed a deduction unless the expenses are supported by e-invoices or e-receipts.

The proposal aids the enforcement of the use of Electronic Fiscal Devices (EFDs) by denying a taxpayer deductions where they made a purchase from a person designated to use EFDs but did not receive an e-invoice/e-receipt and will enhance tax compliance.

4.5 Withholding tax on purchase of land.

Clause 8 proposes to introduce a Withholding tax on the purchase of land other than land which is a business asset, by a resident from a resident person at a rate of 0.5% of the purchase price;

- The income, in form of capital gains, made on sale of land which is not a business asset is already exempted from income tax under Section 21(k); it is therefore contradictory to impose a withholding tax, as a tax collection mechanism, where the law has exempted the income from tax.
- This is double taxation because there is already stamp duty to be paid on transfer of land
- It is likely to lead to an increase in land prices as many sellers might not want to incur this tax cost. Effectively, all land purchasers of non-business land would be withholding tax agents.
- This will negatively impact families who sell land for non-commercial purposes who are the majority in Uganda.
- Many Ugandans do not have TINs and this makes it difficult on how this tax will be accounted for.
- There is need for URA to improve tax administration before such a measure can be introduced.

4.6 Withholding tax on Commissions

Clause 9 provides that an insurance service provider who makes a payment of a commission to an insurance agent or advertising shall withhold tax on the gross amount of the payment at a proposed rate of 10%.

The objective is to enhance the revenue effort of withholding tax and ease tax administration considering that the majority of the persons who earn commissions do not keep records.

4.7 Re – introduction of withholding tax at 6% on agricultural supplies

Clause 10 seeks to reinstate 6% withholding tax on payments for agricultural supplies (which was introduced last FY) thereby of removing agricultural supplies from the list of items that were exempted from the 6% withholding tax on purchase of goods and services by designated withholding tax agents.

(1) There were practical challenges when 1% withholding tax was introduced on payments for agricultural supplies in 2018. The proposed rate of 6% withholding tax is even higher than 1% which failed to be implemented in 2018 and was scrapped.

(2) The current exemption enacted in 2019 should be maintained until a clear, equitable and practical mechanism is developed to tax the SMEs in the agriculture sector.

(3) There are likely to be challenges in implementation since farmers would prefer to sell to non-designated agent and where they have to sell to designated agent, the farmers are likely to increase the prices to cater for the 6%WHT.

4.8 Clause 12 seeks to oblige a taxpayer who provides a passenger transport service or a freight transport service to obtain a tax clearance certificate from the Commissioner before renewal of the operational licenses

- The proposal seeks to enhance revenue by improving compliance among transport operators who are doing business and avoiding tax on their income.

4.9 Introduction of a new tax regime for small businesses.

Clause 15 seeks to introduce a new computation of tax for small businesses.

- This is intended to provide a simplified tax regime for small businesses to enhance equity and improve tax compliance. This will encourage small and medium term enterprises to formalize their businesses since enterprises that keep records will bear relatively lower tax burden compared to those without records.

- However, for the last 12 years, prices and inflation have been consistently increasing. For the lowest paid workers who earns an average of shs.250,000/= the cost of living has become unmanageable if one considers the cost of rent, food and other basic necessities. There is therefore need to comprehensively review the PAYE tax rates to help low income earners have more disposable income. This will increase the purchasing power of low income earners and hence more revenue in from of indirect taxes.

5.0 Recommendations by the Committee

The Committee recommends that:

(i) The Uganda Revenue Authority strengthens its capacity to conduct the right tax assessment for companies which consistently declare tax losses or declare a tax liability of an arithmetic average of less than 0.5% of the gross turnover;

(ii) The URA may consider a PPP approach where URA partners with private tax experts licensed under strict regulations to conduct tax assessments on behalf of Government.

(iii) Government should conduct a study on rental income and how its performance can be improved without affecting growth in the real estate sector;

(iv) Uganda Revenue Authority increases sensitization and awareness campaigns to ensure compliance with tax laws;

(v) Government reviews the PAYE tax rates to enable low income earners meet the rising cost of living;

(vi) The Income Tax (Amendment) Bill be passed into law subject to the proposed amendments.

PROPOSED AMENDMENTS

- **CLAUSE 2. AMENDMENT OF CAP.340**

Delete clause 2.

Justification.

(1) This proposal has hitherto been rejected by Parliament for the last 2 FYs.

(2) The 0.5% is tax on turnover of companies that may be in a loss or near – loss income position and therefore goes against the basic principle that income tax is charged on income (not turn over).

- **CLAUSE 3. AMENDMENT OF SECTION 5 OF THE PRINCIPAL ACT**

Delete clause 3.

Justification.

(1) Limiting the amount of deductible expenses and losses denies corporate persons deductions of legitimate capital and operational expenses incurred on deriving rental income thus contravening principles of taxation and unfairly disadvantage the taxpayer.

(2) Under the Act, Income tax is chargeable on the "gross income" of each tax payer which allows for accounting for income tax on the aggregated income of a single tax payer. Therefore, accounting for rental tax separately for each building may work against this principle that, for tax purposes, allows a tax payer to offset the losses incurred from one income stream from the profits in another income stream of the same tax payer.

- **CLAUSE 4. AMENDMENT OF SECTION 7 OF THE PRINCIPAL ACT**

Delete clause 4.

Justification.

Consequential amendment arising out of deletion of clauses 3, 7 and clause

16 thereby maintaining the status quo. i.e. there is no change in the rate of rental income for a company as proposed under clause 7 (a) (i).

- **CLAUSE 5. AMENDMENT OF SECTION 8 OF THE PRINCIPAL ACT**

  Delete clause 5

  Justification.

  Consequential amendment arising out of deletion of clauses 3, 7 and clause 16 thereby maintaining the status quo. i.e. there is no change in the rate of rental income for a trust or retirement fund as proposed under clause 7 (a) (i).

CLAUSE 6. AMENDMENT OF SECTION 21 OF THE PRINCIPAL ACT

Under paragraph (b), in the proposed paragraph (af);

(1) Substitute for "***one million***" the words " ***three hundred thousand*** "

(2) insert the following immediately after the words "in the case of a citizen" the words " ***or one hundred thousand united states dollars, for a citizen whose investment is placed in a rural area***";

(3) Substitute for "*uses at least **fifty** percent of locally sourced raw materials and employs at least one hundred citizens*", the words "*uses at least **seventy** percent of locally sourced raw materials and employs at least seventy percent of its employees being citizens earning an aggregate wage of at least seventy percent of the total wage bill*"

Justification.

- The number 100 million may not be viable for some companies which work smart and do not need a total number of 100 employees; however this can be expressed as a percentage as is the case under the Value Added Tax Act.

- To ensure that this benefits a larger proportion of the local economy. This can also be instrumental in enhancing and strengthening forward and background linkages between the free zones and or industrial parks and Uganda's farmers, who comprise 80% of the local economy.
- Encourage development and investment in the rural areas as opposed to concentration of investments in the towns

- **CLAUSE 7. AMENDMENT OF SECTION 22 OF THE PRINCIPAL ACT**

Delete paragraph (a)

Justification.

(1) Consequential amendment arising out of deletion of clause 3

(2) The 50% limit on allowable deductions may not cover for all the expenses and losses incurred in generating the rental income being subjected to rental tax. The expenses may include interest on borrowed loans used to construct the buildings, regular maintenance costs, among others.

(3) It is also unfair and discriminatory against landlords who will not be allowed all qualifying deductions for rental tax purposes and yet all the other businesses enjoy all qualifying deductions.

- **CLAUSE 8. AMENDMENT OF SECTION 118B OF THE PRINCIPAL ACT**

Delete clause 8.

Justification

(1) The income, in form of capital gains, made on sale of land which is not a business asset is already exempt from income tax under Section 21(k); it

is therefore contradictory to impose a withholding tax, as a tax collection mechanism, where the law has exempted the income from tax.

(2) Furthermore, there is stamp duty of 1.5% on the transfer of land which is borne by the purchaser upon the title transfer. Adding an additional WHT of 0.5% on top of the price (however marginal) inflates the land price. The seller will obviously negotiate a net price which leaves the purchaser to incur a total overall 2% on the whole transaction.

(3) Most times, the purchaser is either buying land from their savings or using a bank loan. In the normal scenario savings have already been taxed while the interest paid is not even an allowable deduction to the individual purchaser.

(4) This is on top of other costs such as brokerage fees, legal fees, land transfer fees etc.

CLAUSE 10. AMENDMENT OF SECTION 119 OF THE PRINCIPAL ACT

Delete clause 10

Justification

1. There were practical challenges when 1% withholding tax was introduced on payments for agricultural supplies in 2018. The proposed rate of 6% withholding tax is even higher than 1% which failed to be implemented in 2018 and was scrapped.
2. The current exemption should be maintained until a clear, equitable and practical mechanism is developed to tax the SMEs in the agriculture sector.

CLAUSE 16. AMENDMENT OF THIRD SCHEDULE OF THE PRINCIPAL ACT

delete paragraph (a),

Justification

It's a consequential amendment arising out of deletion of clauses 3, and 7 (b) to effect that the current rate for rental income should be maintained.

CLAUSE 17. AMENDMENT OF SIXTH SCHEDULE OF THE PRINCIPAL ACT

Delete Clause 17.

Justification.

Part VI It provides for the rental tax rate of individuals at 20% which has been maintained through deletion of clauses 3, and 7 (b) to effect that the current rates for rental income should be maintained.

REPORT OF THE COMMITTEE ON FINANCE, PLANNING AND ECONOMIC DEVELOPMENT ON THE INCOME TAX (AMENDMENT) BILL, 2020

No	NAME	CONSTITUENCY	SIGNATURE
1	**Hon. Musasizi Henry, CP**	**Rubanda East**	
2	**Hon. Avur Jane Pacuto**	**DWR Pakwach**	
3	Hon. Lugoloobi Amos	Ntenjeru North	
4	Hon. Asiku Elly Elias	Koboko North	
5	Hon. Bategeka Lawrence N	Hoima Municipality	
6	Hon. Abala David	Ngora County	
7	Hon. Katoto Hatwib	Katerera County	
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