THE REPUBLIC OF UGANDA
IN THE MATTER OF THE TAX APPEALS TRIBUNAL
APPLICATION NO TAT 21/2008

DIAMOND SHIPPING COMPANY .....APPLICANT

Versus

UGANDA REVENUE AUTHORITY.....RESPONDENT

RULING

This applicant filed this application seeking to review a Value Added Tax (VAT) assessment of Shs. 236, 917,717/= by the respondent arising from services the applicant rendered.

During scheduling, the parties agreed on following facts: That the applicant is a Ugandan registered taxpayer with the respondent. Sometime in July 2008, the respondent carried out a VAT audit of the applicant for the period January 2004 to April 2008 and assessed VAT of the applicant as Shs. 236,917,717/= which it demanded.

That the applicant objected to the assessment on the following grounds:

1) The applicant provided international transport and forwarding services which were zero-rated supplies but the respondent treated them as standard rated.
2) The respondent had treated all payments received on behalf of the principals (shipping companies) as proceeds of supplies of the applicant, whereas the supplies were by the shipping companies and the applicant was merely a collecting agent.

That the respondent rejected the objection on the following grounds:

1) The applicant earns a commission from coordinating and handling transport but does not provide international transport services.

2) The applicant earns a commission for arranging hire of containers in international conveyance of goods.
3) The assessment is based on income earned by the applicant and not it's principal.
4) The applicant supplies services to the principal which are standard rated.
5) The input tax credit had been taken into account.

The following issues had been agreed:

1. Whether the services in dispute performed by the applicant are standard rated or zero-rated?
2. Whether the applicant is liable to pay VAT on the services rendered?
3. Whether the respondent took into account the input tax credit allowable to the applicant before arriving at the tax payable?
4. Remedies and other reliefs

Subsequently, issue 2 was dropped as it was similar to issue 1. The parties opted to settle issue 3 out of court. Hence the remaining issues were issues 1 and 4.

The applicant called one witness, Mr. Anard Poojar, who is its accounting manager. He described the applicant's business as shipping, clearing, forwarding, airfreight and tracking of containers to Uganda from various parts of the world and vice versa He explained that in respect to the shipping business, the applicant is an agent for ZIM and LNL shipping lines while in forwarding it has a network of agents who load containers for various shipping lines. For those activities, the applicant earns a commission.

The respondent called two witnesses. The first witness RW1, Ms Florence Kasiime, is a tax officer in the Domestic Taxes department of the respondent. She was part of the team that audited the applicant following its application for a VAT refund. She explained that the audit was necessary to justify the refund following many months of offsets. She testified that after looking at the input tax schedules, invoices, the output tax schedules, contracts and audited

tax accounts of the applicant and at the nature of business and relating it to S.11 (a) and S.13 (2) of the VAT Act, the team determined that the applicant provides services to the principals which include handling charges, demurrage, bank charges, agency fees, in which it earns a given percentage. According to her, international forwarding is done by the principal and the applicant earns a commission on the services it provides. The audit team accordingly treated the earnings of the applicant for the services it provides to the principals as standard rated and computed tax on that basis.

The second witness RW2, Ms Kobusingye Kelemensio is a supervisor of audit in the respondent. She explained that she took over the audit when it was in its final stages. She testified that after looking at the business of the applicant, and the documents presented, the respondent found that the services the applicant rendered were standard rated. She described the nature of the applicant's business as agency services for which it earns commission. The services provided include handling and container tracking. The audit team looked at other similar businesses and found that the applicant's services were not incidental to international transport because first the applicant is independent of the principal. Secondly, S.11 (1) (a) of the VAT Act defines the supply of services as performance of a service for another person. Further, she stated that because the applicant was performing services for the principal the services are standard rated in accordance with S. 13(2) of the Act. Finally, she testified that the genesis of the assessment was that the applicant was independent of the principal and that the services it renders are not incidental to the principal's activities. She concluded that the assessment was based on income derived from clearing and forwarding, and the commission earned from various activities set out in the agreement.

In its submission, the applicant contended that the testimonies of both RW1 and RW2 proved that the auditors neither understood the nature of the applicant's business nor did

they know what international transport and international forwarding was. The audit team in their audit report admitted that:

"(i) that the issue of commission earned by the agent on international transport needs to be more clarified in the VAT Act to avoid revenue loss, and

(ii) that there is need for a practice notice on the issue of commission on international transport"

This confirmed that the URA team did not understand the subject they were auditing.

The applicant further contended that the main ground in the notice of objection decision of 29/09/08 that the commission was liable to tax as required by S.13(2) and S.14 of the VAT Act is inapplicable since for a supply of service to be liable to VAT, it must be made in Uganda. According to S. 16(3) of the VAT Act "a supply of services of, or incidental to transport takes place where the transport commences" and since international transport starts outside Uganda, there was not taxable supply in Uganda related to transport. The applicant contended that the transportation of the goods for which the applicant provides services always commenced outside Uganda then there was no supply in Uganda. Shipping, forwarding or international transport are related to each other because there cannot be shipping or forwarding which does not involve transportation.

The applicant submitted that its services fall under S. 11(1) (b) of the VAT Act which provides for making available of any facility or advantage which it does for transportation of goods. Since that transportation of goods originates outside Uganda then it is international transport and the supply by the applicant is incidental to international transportation which is zero-rated under the Third Schedule Item 1(2).

Finally the applicant explained that ZIM is the principal. The applicant is merely an agent and that since the service by the principal is performed outside Uganda under S.16 (3) of the Act, there is no taxable supply. It is the applicant's submission that it provides services as an agent to ZIM and other principals.

In reply, the respondent contended that the applicant's role is intermediary or brokerage between the shipping line and transporters or exporters. It categorized the services the applicant performs in Uganda for the principal or shipping lines as: tracking and tracing of containers, debt collection and transfer of funds, marketing and sales for the principals, providing documentation for shipping lines clients for which the applicant earns a commission. The applicant's other activities include sourcing for clients (importers/exporters) and connecting them to international shipping lines for a commission. The applicant also hires trucks to deliver goods to or from the border.

The respondent further categorised the nature of the applicant's business as follows: The applicant has contractual obligations/agency agreements with specific lines, and it purely acts as a broker and connects importers/exporters to transporters/shipping lines. The respondent concluded that the applicant earns a commission for coordinating and handling but not transportation; it arranges for the transportation of the goods and earns a commission. The services it renders are therefore brokerage services and not transportation services and these fall under S.11(a) and S.13 (2) of the VAT Act and hence subject to VAT under S.4 of the VAT Act.

The Tribunal has carefully considered the submissions by the parties and the evidence adduced. Both parties tendered in written submissions on issues 1 and 4. However in reply to the respondent's submission the applicant in its final submission contended that issue 3 was not amicably resolved by both parties. The respondent rejected some of its invoices. Unfortunately the tribunal will not be able to address issue 3 as no evidence was adduced on it and therefore it cannot make a ruling on it. The applicant should have brought it to the attention of the tribunal before both parties had closed their cases and put in their submissions. It should have sought to re-open its case to tackle the said issue.

From the evidence adduced it is apparent that the applicant provides the following services. Firstly it is involved in international forwarding business. Here the applicant acts as an agent for a shipping company. It assists the shipping company deliver containers from one sea port to another. It treats this service as zero rated. Secondly the applicant is involved in international transport. This involves transporting the goods/ containers from one country to another for instance, the transport of goods from the Mombasa port to Kampala or vice versa. The applicant treats this service as zero rated. Thirdly the applicant is also involved in air freight services. This involves having cargo loaded on air freight for or from destinations abroad. It charges a commission which the applicant deems as zero rated. Fourthly the applicant was involved in container tracking services. This involves globally monitoring the movement of containers of goods being imported or exported. The applicant contended that this service is incidental/auxiliary to international transport as it enables the importer know the progress of the conveyance or whereabouts of its goods. The applicant earns a commission which it treats as zero rated. Fifthly the applicant is involved in local transport. The applicant assists an importer/ exporter transport it's goods/containers in Uganda. It treats the service as standard rated and charges VAT at 18%. Lastly the applicant provides clearing and forwarding services. It assists importers/exporters clear and forward goods. It also charges handover fees. The applicant treats these services as standard rated and charges VAT. Hence it is the first four services provided by the applicant that are the subject of this application. The last two services are not in dispute.

S. 24(4) of the VAT Act provides that the rate of tax imposed on taxable supplies specified in the Third Schedule is zero. The Third Schedule provides that

> "*1. The following supplies are specified for the purposes of section 24(4)—*
>
> *(a) a supply of goods or services where the goods or services are exported from Uganda as part of the supply;*
>
> *(b) the supply of international transport of goods or passengers and tickets for their transport;"*

The Act does not define international transport. However in paragraph 3 of the third schedule it states that

> *"For the purposes of clause (1) (b), international transport of goods or passengers occurs where goods or passengers are transported by road, rail, water or air—*
>
> *(a) from a place outside Uganda to another place outside Uganda*
>
> *where the transport or part of the transport is across the territory of Uganda;*
>
> *(b) from a place outside Uganda to a place in Uganda; or*
>
> *(c) from a place in Uganda to a place outside Uganda."*

Hence the international transport of goods involves the movement of goods from one country to another. One of the countries has to be Uganda.

The respondent contends that the applicant merely coordinates and handles transport but does not provide international transport services. It contends that the applicant does not own a railway line, airline or transport. The applicant earns a commission on arranging the hire of containers used in the conveyance of goods. The applicant in reply contends that the services it provides are ancillary and incidental to supply of international transport of goods. It retorts that one cannot talk of international transport without talking of international shipping and international forwarding. It argues that it acts as an agent for various principals without it international transport cannot be facilitated.

A question arises as to whether one has to own a mode of international transport in order to benefit under the Third Schedule. S. 1 of the VAT Act provides that a taxable supply has the meaning in S. 18. S.18 of the VAT Act provides that

> *(1) A taxable supply is a supply of goods or services, other than an exempt supply, made by a taxable person for consideration as part of his or her business activities.*
>
> *(2) A supply is made as part of a person's business activities if the supply is made by him or her as part of, or incidental to, any independent economic activity he or she conducts, whatever the purposes or results of that activity.*

Hence if a supply is made incidental to the supply of the main business activity then it should be deemed a supply within the Act. The Act does not distinguish between owners of modes of transport, drivers, pilots or brokers. It does not state how international transport should be conducted. A "supply of international transport of goods" is not about ownership of modes of transport. It is not about the physical driving of cargo trucks, or piloting of ships and airlines. It is a business activity that involves a number of players beginning from the managers down to the brokers, porters, transporters etc. While the tribunal agrees with the respondent that the applicant does not own any mode of transport it nevertheless is of the view that the applicant plays a vital role in facilitating the transportation of goods between exporters and importers. If we are to use the strict application used by the respondent it would mean that only the owners, drivers and pilots involved in international transport would qualify to charge zero rated VAT. What would happen to the other players who enable the owners, the drivers and pilots provide the said services? The Act does not distinguish the roles played in international transport. It does not limit it to the owners and pilots. Whereas the applicant may not own modes of transport, it is an agent of the owners of various modes of transport. It enables the owners transport goods from one country to another by providing intermediary services. The services provided for by the applicant are incidental and ancillary to international transport.

The respondent does not dispute that the applicant is an agent of various transporters and shipping lines. The applicant testified that it acts for various companies including Zim, LNL (Laurel and Navigation Lines), Messina as an agent. An agent is defined by Black's Law Dictionary 8th Edition p.68 as one who is authorized to act for or in place of another. It further states that

> *"Generally speaking, anyone can be agent who is in fact capable of performing the functions involved. The agent normally binds not himself but his principal by the contracts he makes; it is therefore not essential that he be legally capable to contract (although his duties and liabilities might be affected by his status)."*

The common law rule is that any person can act through an agent – *qui facit per alium facit per se*, the reason being one of practical convenience. An agent is not the same as an independent contract. An independent contractor is one who is *"in business on his own accoun.*" (see Commercial law 6th Edition p.9 by Robert Lowe). S. 13 of the VAT Act reads

> *(1) A supply of goods or services made by a person as agent for another person being the principal is a supply by the principal.*
>
> *(2) Subsection (1) does not apply to an agent's supply of services as agent to the principal.*

From subsection 1 it is clear that services rendered by an agent are deemed to be a supply by the principal. The respondent contends that S. 13(2) of the VAT Act should be applied. S.13 (2) refers to a situation where an agent supplies its services to a principal and not to a third party. For instance, if the applicant was to transport containers belonging to Messina then it would cease being an agent of Messina. Messina would be a customer and not a principal.

S. 11 of the VAT Act provides

> *"(1) Except as otherwise provided under this Act, a supply of services means any supply which is not a supply of goods or money, including—*
>
> *(a) the performance of services for another person;*
>
> *(b) the making available of any facility or advantage; or*
>
> *(c) the toleration of any situation or the refraining from the doing of any activity"*

The supply of international transport of goods is a supply of service. The respondent witness contended that S. 11(1) (a) applied because the applicant was performing services for another person, the principal. That interpretation is erroneous. The applicant as an agent performs services on behalf of the principal for another person. The "another person" referred in the subsection refers to a third party who is the customer who pays for the services. The principal does not pay for the services. It merely remits monies paid for by the importer or exporter. S. 11(2) (b) is more applicable to the current application. The services provided by the applicant make the transport of goods available to importers and exporters. That is by coordinating the interests of importers/ exporters and the transporters. It provides

important services aimed at facilitating international transportation on behalf of the principal in the territory, in this case Uganda. We agree with the applicant that a service must be regarded as ancillary or incidental to a principal service if it does not constitute for customers an aim in itself, but a means of better enjoying the principal service supplied. In this respect the Tribunal agrees that the applicant's services fall under S.11 (b) of the VAT Act.

The third schedule applies to the services of the applicant as it is involved in the business of international transport of goods, whether directly or indirectly. The Tribunal finds this to be similar to case of AON *Uganda Limited V Uganda Revenue Authority* HCCS 5 where the applicant claimed that the insurance brokerage services it provided were within the meaning of insurance services under the VAT Act. His Lordship Kiryabwire at p.23 stated

> *"It is my finding that looking at the language of the S.19(1) of the VAT Act and para 1 (d) of its second schedule, it would be fair to say that insurance services inter alia includes services provided by both insurance and brokerage companies."*

The court stated that what amounts to insurance services is a technical and practical matter. As a matter of law and practice the insurer and insurance broker provide the same service.

Likewise it would be difficult to draw a dichotomy between the services provided by the applicant and the owners of the modes of international transport. As a matter of law and practice they both provide the service of international transport of goods. The tribunal does not agree with Ms Kobusingye Kelemensio (RW2) that the applicant is independent of the principal. The view of the tribunal is that the applicant, as an agent of the principal, links the importers/exporters to the principal in a continuous process of providing international transportation of goods to their destinations. In other words, the applicant contributes to the smooth and fast movement of goods. The tribunal therefore finds that the services rendered by the applicant are incidental to international transport and are therefore zero rated.

Where the applicant, is independent of the principal and or is not in the business of international transport of goods, it should pay Value Added Tax (VAT) at the standard rate (i.e. 18%). However where the applicant is an agent to a principal who and or provides services that are incidental to international transport of goods the Value Added Tax charged should be zero rated.

The first issue is answered in the affirmative and in favour of the applicant. The Tribunal therefore allows the application in respect to issues 1 and 4. The VAT assessment of Shs. 236,913,717/= by the respondent is not tenable. The 30% of the VAT Tax deposit paid prior to filing this application should be refunded to the applicant. The applicant is awarded costs of this application.

Dated at Kampala this day of 2010.

Mr. Asa Mugenyi **Mr. George Wilson Mugerwa** **Mr. Stephen Akabway**

Chairman **Member** **Member**