IN THE COURT OF APPEAL OF TANZANIA

AT DAR ES SALAAM

(CORAM: MKUYE, J.A., MWAMBEGELE, J.A., And KWARIKO, J.A.)

CIVIL APPEAL NO. 218 OF 2019

KILOMBERO SUGAR COMPANY LIMITED ..... APPELLANT

VERSUS

COMMISSIONER GENERAL,
TANZANIA REVENUE AUTHORITY ..... RESPONDENT

(Appeal from the Judgment and Decree of the Tanzania Revenue Appeals Tribunal, at Dar es Salaam)

(Mjemmas, Chairman)

dated the 12th day of February, 2019
in
Tax Appeal No. 17 of 2016

.....

JUDGMENT OF THE COURT

19th February & 25th May, 2021

MWAMBEGELE, J.A.:

This appeal arises from the decision of the Tax Revenue Appeals Tribunal (henceforth "the Tribunal") in Tax Appeal No. 17 of 2016 rendered on 12.02.2016 by Mjemmas (Chairman). In that appeal, the Tribunal upheld the decision of the Tax Appeals Board (henceforth "the Board") requiring the appellant to pay the respondent; the Commissioner General of Tanzania Revenue Authority, Tshs. 469,739,933/= comprised in two

withholding tax certificates issued to the appellant by the respondent for the years of income 2004/5 – 2007/8 and 2009/10.

The material background facts are simple. To appreciate the appeal before us, we find it compelling to narrate them, albeit briefly. The appellant, Kilombero Sugar Company Limited, is a company incorporated in Tanzania dealing with sugar cane farming and sugar production. The respondent, the Commissioner General of Tanzania Revenue Authority, is a tax collection agent of the Government of the United Republic of Tanzania established under the Tanzania Revenue Authority Act, Cap. 399 of the Revised Edition, 2006.

On 09.04.1998, the appellant entered into an Operational and Technical Services Agreement with Illovo Project Services Limited (IPSL, henceforth "Illovo"), a South African Company, for the management and control of her factories and agricultural land from time to time. Among the terms of the agreement was that the appellant would pay a fixed amount of USD 30,000.00 per month for the services rendered by Illovo.

The respondent conducted an audit on the appellant's business for the years of income 2004/2005 to 2007/2008 and 2009/2010 whereas the

exit meeting note for the year 2004/2005 to 2007/2008 was issued on 23.02.2009 and that for 2009/2010 was issued on 03.11.2010. Findings of the audits were that the appellant had an obligation to pay withholding tax on the reimbursements paid as well as for payments to nonresidents. After several meetings conducted to discuss the audit report, the respondent issued Withholding Tax Certificate No. WHT/IR/7/2011 for the years 2004/05 to 2007/08 on 28.11.2011 requiring the appellant to pay withholding tax of Tshs. 276,547,628/= (being tax due Tshs. 147,087,800/70 and interest thereon Tshs. 129,469,827.30). On 28.06.2012, the respondent issued another Withholding Tax Certificate No. WHT/IRMD/21/6/2012 requiring the appellant to pay a total sum of Tshs. 193,192,205/= (Tshs. 134,598,375/= being the amount of tax due and Tshs. 58,593,830/= being interest thereon) for the year of income 2009/2010.

The appellant was discontented with the withholding certificates. She thus, having complied with the requirement of paying one-third of the tax complained of as required by the law, lodged an objection with the respondent. However, the respondent stuck to his guns. Consequently,

the appellant lodged two statements of appeal in the Board against the respondent in respect of each of the two Withholding Tax Certificates. The appeals, christened Appeals Nos. 2 and 64 of 2012, were consolidated and entertained as one. The kernel of contention before the Board, the Tribunal and certainly before us is twofold; **first**, that the reimbursements do not form part of the service fee paid to Illovo and, **secondly**, alternatively, that if the reimbursements are considered to be part of the service fee, they are still not subject to withholding tax in terms of the Tanzania - South Africa Double Taxation Agreement (henceforth "the Double Taxation Agreement").

The Board, in its judgment rendered on 01.07.2016, decided in favour of the respondent by dismissing the consolidated appeal and holding that service fees must include all costs incurred and that the respondent did not violate the provisions of the Double Taxation Agreement by charging withholding tax on payments made to nonresidents.

Still aggrieved, the appellant unsuccessfully appealed to the Tribunal which upheld the decision of the Board on 12.02.2019. Undeterred, the

appellant preferred this second and last appeal to the Court seeking to assail the decision of the Tribunal on five grounds, paraphrased as under:

1. By holding that costs were included in the term "service fee" the Tribunal misinterpreted the meaning of the term "service fee" under section 3 of the Income Tax Act, 2004 and the type of payments subjected to withholding tax as envisaged under the provisions of the law;

2. The holding of the Tax Tribunal that "if it was the intention of Parliament to separate costs from service fee it could have stated so clearly" was an error in law for not considering that if it was the intention of Parliament to include costs in the term "service fee" would have stated so clearly to make costs expressly taxable in terms of Article 138 of the Constitution of the United Republic of Tanzania, 1977;

3. The holding of the Tribunal that costs is part of service fee and thus taxable while determining the issue whether costs were part of service fee and later holding that costs were excluded from service fee while determining an issue whether service fee was covered and

not taxable under the Double Taxation Agreement between Tanzania and South Africa, the same matter and misinterpreting the provisions of the law;

4. Having held that "we agree that section 8 (2) of the Income Tax Act, 2004 directs that service fee is to be included in calculating a person's gain or profits from conducting business", the Tribunal erred in law for holding that service fee is not covered under Article 7 (1) of the Double Taxation Agreement; and

5. The Tax Tribunal erred in law by misinterpreting the meaning of the term "profit" as applied in the Double Taxation Agreement.

At the hearing of the appeal before us on 19.02.2021, Mr. Ayoub Mtafya, learned advocate, appeared for the appellant. Messrs. Hospis Maswanyia and Cherubin Chuwa, learned State Attorneys and Ms. Salome Chambayi, also learned State Attorney, joined forces to represent the respondent. Both parties had filed their respective written submissions beforehand for and against the appeal which they sought to be part of their oral submissions at the hearing. What the learned counsel for the parties did at the hearing was to clarify on some pertinent points.

In the written submissions earlier filed by the appellant, the third ground of appeal was abandoned and the fourth and fifth grounds were consolidated and argued together as one. The rest of the grounds were argued separately.

On the first ground of appeal, it was submitted that service fee is limited to the charges for skills and professional services that one rendered to another and not costs incurred for air tickets or costs of materials purchased from third parties. In this case, it was submitted, the appellant was not charged by the service provider (Illovo). The appellant reproduced the definition of the term "service fee" as defined by section 3 of the Income Tax Act, 2004 (henceforth "the ITA, 2004") as meaning:

> *"... a payment to the extent to which, based on market values, it is reasonably attributable to services rendered by a person through a business of that person or a business of any other person and includes a payment for any theatrical or musical performance, sports or acrobatic exhibition or any other entertainment performed, conducted, held or given".*

Mr. Mtafya also relied on the definition of the term "fee" provided for in **Black's Law Dictionary**, 9th Edition as meaning:

> *"A charge for labor or services, especially professional services."*

On the basis of the foregoing definition, the learned counsel surmised that the term service fee as used under section 3 of the Income Tax Act is referring to payment for the professional or labour of persons rendering services.

Mr. Mtafya also argued that the interpretation that costs are inclusive in the term "service fee" goes contrary to the type of payments subjected to withholding tax as provided for under section 83 (1) of the ITA, 2004 applicable to the case at hand before its amendments.

He underlined that the type of payments which are subject of withholding tax are service fee and insurance premium and those mentioned under sections 82 and 84 of the same Act. The learned counsel emphasized that these kinds of payments stand alone; no cost element is added to them. It was therefore incorrect for the respondent to impose withholding tax on costs or payments such as air tickets, air charter and

accommodation by "lumping all into service fee while they were separate (not deducted from service fee)", he argued. Those payments, the learned counsel charged, are not professional fees and are not mentioned in the law as the kind of payment which is subjected to withholding tax.

With regard to the second ground, the learned counsel argued that while justifying the imposition of withholding tax on payments such as air tickets, air charter and accommodation as part of the service fee, the Tribunal, at p. 780 of the record of appeal, was of the view that if Parliament intended to separate costs from service fee, it would have stated so clearly. He termed this finding as erroneous and argued that, in terms of Article 138 (1) of the Constitution of the United Republic of Tanzania, 1977 (henceforth "the Constitution"), if costs were subject of withholding tax as part of service fee, the law would have stated so in clear terms. The learned counsel relied on the book by Professor Florens Luoga titled **A Source Book of Income Tax Law in Tanzania**, 2007 to underscore the rule that where there is ambiguity, the tax statute should be construed in favour of the taxpayer.

Arguing, in the alternative, in respect of the consolidated grounds four and five, Mr. Mtafya relied on Article 7 (1) of the Double Taxation Agreement to argue that the Tribunal erred in holding that service fee includes costs and therefore not profit. He argued further that the Tribunal, in interpreting the Double Taxation Agreement, ought to have paid close attention to the words such as "business", "business profit", "categories or items of income" and "what makes up profit".

Mr. Mtafya also argued that the Tribunal, having agreed that section 8 (2) (a) of the Income Tax Act directs that service fee is to be included in calculating a person's gain of profits from conducting business, ought to have held that service fee is covered by Article 7 (1) of the Double Taxation Agreement which recognizes an item of income like service fee as profit in its own right. To buttress this point, the learned counsel also cited to us the **OECD Commentary** in the **Materials on International TP and EU Tax Law**, by Kees Van Raad and a book titled **International Tax Policy and Double Tax Treaties**, 2nd Edition, 2014 by Kevin Holmes.

Having argued as above, the learned counsel implored us to allow the appeal by quashing the judgment and decree of the Tribunal.

In response, Mr. Maswanyia, attacked the appeal with equal force. In the reply written submissions earlier filed, the respondent argued that the terms "reimbursement" and "costs incurred" are not one and the same. The respondent relied on the meaning of the terms in **Black's Law Dictionary** and submitted that while the former means "a duty to make good any loss or damage or ... compensation", the latter means "the amount paid or charged for something, price or expenditure" and that the one at issue in the present case is the latter.

Mr. Maswanyia clarified on the written submissions that section 3 of the ITA, 2004, defines the term "service fee" and the relevant words are "payment ... reasonably attributable to service rendered". It was argued that since the service provider could not have provided the required services without his travel to render such services then the respective costs of fare and air tickets are subject to service fee in terms of section 3 of the ITA, 2004. The respondent brands as misleading the assertion by the appellant that service fee is payment received for the skills or professional services because the definition does not provide for any type of services. What is relevant, he argued, is a payment which is attributable to service

rendered. The learned counsel referred us to p. 102 of the record of appeal where payments attributable to service rendered and thus taxable were termed as reimbursements while they were costs incurred by the service provider.

With regard to the alternative argument by the appellant, the subject of the fourth and fifth grounds of appeal, the respondent argued that the ITA, 2004 defines **person's income** from business for the year of income to be the **person's gains or profits**. When you talk of profit then you are talking of gains or income and that is what is taxable under the ITA, 2004, he contended. He argued further that Article 7 of the Double Taxation Agreement is irrelevant as it provides on the **profits** which is **cost exclusive** while in the case at hand an item at issue is **service fee** which is **cost inclusive**.

On the strength of the foregoing arguments, Mr. Maswanyia implored us to dismiss the appeal with costs.

In a brief rejoinder, Mr. Mtafya submitted that the professional fee of USD 30,000.00 was subject of withholding tax but not costs incurred and reimbursed. He added that the Double Taxation Agreement does not

provide for the definition of "profit" and that, as per Article 17 (1) (7), where profits include items of income which are dealt with in other articles, Article 7 (1) will not apply. Otherwise Mr. Mtafya agreed that in terms of section 83 (1) (b) of the ITA, 2004, imposition of withholding tax on nonresidents for the services rendered was correct; but not for costs incurred and reimbursed. He reiterated his prayer to have this appeal allowed with costs.

Having heard the learned rival submissions and arguments by the learned counsel for the parties, the ball is now in our court to determine the issues of contention which we think are, **one**, whether the costs incurred by Illovo and reimbursed by the appellant are part of the service fee and thus subject to withholding tax and, **two**, alternatively, if the answer to the first issue is in the affirmative, whether they are not subject to withholding tax in terms of the Double Taxation Agreement.

We wish to start our determination by stating that the learned counsel for the parties are at one that service fee paid to a nonresident person with a source in the United Republic of Tanzania is subject to

withholding tax in terms of section 83 (1) (b) of the ITA, 2004. The subsection reads:

> *"83. - (1) Subject to the provisions of subsection (2), a resident person who –*
>
> *(a) in conducting a mining business pays a service fee to another resident person in respect of management or technical services provided wholly and exclusively for the business; or*
>
> *(b) pays a service fee or an insurance premium with a source in the United Republic to a non-resident person,*
>
> *shall withhold income tax from the payment at the rate provided for in paragraph 4(c) of the First Schedule."*

The issue on which the learned counsel for the parties have locked horns is whether costs incurred by the service provider (Illovo) and reimbursed by the appellant are part of service fee and thus subject to withholding tax. In resolving this issue, the Tribunal reproduced the definition of the term service fee which we have just reproduced above. Having so done, the Tribunal agreed with the appellant's submission that

service fee includes payments for labour or professional services. However, it disagreed with him to restrict the definition to only labour or professional services. The Tribunal observed at p. 779 of the record of appeal:

> *"In principle we agree with the appellant's counsel that from the definition above, service fee includes payments for labour or professionalism. We however differ with him when he restricts the definition to labour or professionalism. That is to give a very narrow interpretation of the term service fee. Service fee, at least, from the definition given above may include payments for other services which are not necessarily related to labour or professionalism. But even in that case it does not follow that costs involved in rendering the service whether in the form of labour or profession are excluded. It is elementary that there is no activity which has no cost implications, directly or indirectly".*

We share the same reasoning and conclusion. The costs under discussion are air tickets, air charter, hotel accommodation etc. These costs were incurred by Illovo when rendering services to, and were

reimbursed by, the appellant. We agree with the respondent's counsel that these fall within the scope and purview of payments **reasonably attributable** to the services rendered in terms of the definition of the term "service fee" under section 3 of the ITA, 2004. We are alive to the fact that in terms of the Operational and Technical Services Agreement between the appellant and Illovo, the service fee and costs were separated and the appellant's counsel complained for the respondent's act of lumping them together for withholding tax calculations. That notwithstanding, we agree with the finding of the Tribunal that the separation was only for the convenience of the parties; the appellant and Illovo. In our considered view, the separation was not meant to dissuade the respondent from making it exclusive from withholding tax under section 83 (1) (b) of the ITA, 2004.

In the course of researching on the matter, we came across Practice Note No. 01/2019 titled **Withholding Tax on Payment for Goods and Services as per Income Tax Act, Cap 332** available at https://tra.go.tz/Images/headers/Withholding-Tax-on-payment-for-Goods.pdf, which we found useful in our determination of the appeal. The

Practice Note is made under section 9 of the Tax Administration Act, Cap 438 (henceforth "the Tax Administration Act"); which powers the Commissioner also wielded under the now repealed section 130 of the ITA, 2004. The Practice Note provides under clause 10.0 thereof:

> ***"10.0 Inclusion of value of benefits and facilities***
>
> *Where services are provided and payments are made to the withholdee of cash plus provision of benefits and facilities, the withholding tax base shall include the amount paid for the benefits or facilities. Where the benefits were not paid for, they shall be quantified at a market value at the time of payment. Furthermore,* ***where services are provided and payments are made to the withholdee in form of service fee and reimbursements then the withholding tax base will be the full amount that is service fee plus reimbursement amount.****"*
>
> [Emphasis supplied]

The Practice Note goes on to give an example:

> *"FLG Consultants were hired by Kinondoni District Council to carry consultancy work. The contract*

terms involved payment of reimbursement expenses which were used for accommodation in a 5 star hotel for 4 staff of FLG for 20 days by the client. The contract price was quoted at Tsh 150,000,000/= plus reimbursements. The Client Paid a total of Tsh 16,000,000/= as reimbursement expenses for accommodation of FLG staff.

DESCRIPTION	***AMOUNT (Tshs)***
Consultancy Fee	*150,000,000/=*
Reimbursements	*16,000,000/=*
Total	***166,000,000/=***

W/Tax Base

Consultancy fee 150,000,000/=

Reimbursements 16,000,000/=

W/Tax Base 166,000,000/="

The Practice Note above clarifies that **withholding tax shall be calculated on the gross amount paid without deduction of expenses or allowances**. In the above example, the withholding tax base was calculated on the consultancy fee (Tshs. 150,000,000/=) plus reimbursements (Tshs. 16,000,000/=). Thus the withholding tax base was Tshs. 166,000,000/=. We are of the view that the Practice Note depicts

the correct position of the law and that is what should have been done in the case at hand.

We are aware that the Practice Note was made under section 9 of the Tax Administration Act. However, we are certain that the position holds true to the one which obtained under the ITA, 2004. We say so because the Tax Administration Act cross-refers the definition of "withholding tax" in section 3 thereof to "tax which is required to be withheld by a withholding agent from a payment under Subdivision A of Division II of Part VII of the Income Tax Act". For the avoidance of doubt, section 83 (1) (b) falls under Subdivision A of Division II of Part VII of the ITA, 2004 cross-referred to by the Tax Administration Act.

For the avoidance of doubt, we are alive to the position that the Court is not bound by Practice Notes. This is so because, the task to interpret laws is the exclusive domain of the court. However, we are certain that the Practice Note is an external aid to construction providing guidance in the interpretation of a provision. At this juncture we find irresistible to associate ourselves with **Kanga and Pakhivala's the Law and Practice of Income Tax** by Arvind P. Datar, 11th Edition, at p. 35 on

the role of the courts in interpretation of laws in relation to Circulars, Forms and Interpretation by the Income Tax Authorities in India:

> *"31.* ***Circulars, Forms and Interpretation by the Income-tax Authorities****. - Circulars or general directions issued by the Central Board of Direct Taxes would be binding under s. 119 on all officers and persons employed in the execution of the Act, but they cannot bind the appellate authority, the tribunal, the court or the assessee. The Board cannot pre-empt a judicial interpretation of the scope and ambit of the provision of the act by a circular, as the task of interpretation of laws is the exclusive domain of the court. Circulars may be utilised to understand the scope and meaning of the provision to which they relate. These circulars, or the interpretations of provisions of the Act by the CBDT or the Income-tax Department are in the nature of contemporanea expositio furnishing legitimate aid in the construction of a provision."*

We subscribe to that exposition and hold that the same holds true in our jurisdiction as well.

The above stated, we, like the Board and Tribunal, find and hold that payments made by Illovo as costs incurred in rendering services to, and reimbursed by, the appellant are part of service fee subject to withholding tax under section 83 (1) (b) of the ITA, 2004. The first issue, the subject of the first and second grounds of appeal, fails.

We now turn to consider the second issue which was argued by the appellant in the alternative; the subject of the fourth and fifth grounds of appeal. Our starting point will be Article 7 (1) of the Double Taxation Agreement. It provides:

> *"**Article 7***
>
> ***Business Profits***
>
> *[Compare: OECD Model | UN Model]*
>
> *1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that*

permanent establishment."

Mr. Mtafya argued that this article is applicable to the case at hand. The thrust of his argument was that service fee is a charge on professional services or skills and has no cost element attached to it. Thus, he argued, it forms part of a business profit to Illovo carrying on business in Tanzania. He added that even if the Court finds that costs incurred by Illovo and reimbursed by the appellant are part and parcel of service fee, that notwithstanding, such service fee is not subject to withholding tax in Tanzania pursuant to Article 7 of the Double Taxation Agreement.

On the other hand, the respondent strongly argued that costs incurred by Illovo and reimbursed by the appellant were so incurred in the course of rendering services to the appellant and therefore cannot be excluded from the service fee component. Besides, the respondent argued, the article is not applicable to the present situation because it provides for **business profits** which is **cost exclusive** while in the case at hand the item at issue is **service fee** which is **cost inclusive**. The same argument arose in the Tribunal and it (the Tribunal) agreed with the reasoning of the Board that the relevant article here was not Article 7 (1)

but Article 21 of the Double Taxation Agreement. We hasten the remark that this, in our considered view, is the correct exposition of the law. We also find the argument by the respondent that Article 7 is not talking of service fees but business profits as making a lot of sense. We agree that the relevant provision in our case is Article 21 of the Double Taxation Agreement which provides for "other income". In demonstrating, we prefer to start with reproducing Article 20 thereof which states:

> *"**Article 20***
> ***Other Income***
> *[Compare: OECD Model | UN Model]*
> *Items of income arising in a Contracting State which are not dealt with in the foregoing Articles of this Agreement may be taxed in that State."*

Likewise, Article 21 provides on how double taxation shall be eliminated in Tanzania and South Africa:

> *"**Article 21***
> ***Elimination of Double Taxation***
> *[Compare: OECD Model | UN Model]*
>
> *Double taxation shall be eliminated as follows:*
>
> *(a) in South Africa, subject to the provisions of*

the law of South Africa regarding the deduction from tax payable in South Africa of tax payable in any country other than South Africa (which shall not affect the general principle hereof), Tanzanian tax paid by residents of South Africa in respect of income taxable in Tanzania, in accordance with the provisions of this Agreement, shall be deducted from the taxes due according to South African fiscal law. Such deduction shall not, however, exceed an amount which bears to the total South African tax payable the same ratio as the income concerned bears to the total income;

(b) in Tanzania, subject to the provisions of the law of Tanzania regarding the allowance of a credit to a Tanzanian resident against Tanzanian tax of tax payable in a territory outside Tanzania (which shall not affect the general principle hereof), South African tax paid by residents of Tanzania in respect of income taxable in South Africa, in accordance with the provisions of this Agreement, shall be deducted from the taxes due according to Tanzanian fiscal law. Such credit shall not exceed the amount of the tax

chargeable upon the income in respect of which the credit is to be allowed or upon each part of such income, as the case may be, computed in accordance with Tanzanian fiscal law."

Flowing from the above, as service fee is an item which does not feature anywhere in the Double Taxation Agreement, Article 20 becomes handy. The costs incurred by Illovo and reimbursed by the appellant (which we have already found and held to be part of service fee) will be taxable in Tanzania as per Article 21 of the Double Taxation Agreement. Put differently, it is our considered view that, as per the Double Taxation Agreement, service fees by a South African entity for provision of professional services to a Tanzanian entity, do not form part of business profits as provided for under Article 7 of the Double Taxation Agreement which is not taxable in Tanzania but fall under Article 21 of the Double Taxation Agreement and thus subject to withholding tax in terms of section 83 (1) (b) of the ITA, 2004. The alternative argument by the appellant, the subject of the fourth and fifth grounds of appeal, also fails.

The sum total of the above discussion is that we find nowhere to fault the findings of the Tribunal in upholding the decision of the Board, for

it is based on the correct interpretation of our tax legislation as well as the Double Taxation Agreement. This appeal is arid of merit. It stands dismissed with costs to the respondent.

DATED at **DAR ES SALAAM** this 19th day of May, 2021.

R. K. MKUYE
JUSTICE OF APPEAL

J. C. M. MWAMBEGELE
JUSTICE OF APPEAL

M. A. KWARIKO
JUSTICE OF APPEAL

The judgment delivered this 25th day of May, 2021 in the presence Mr. Eric Denga, learned counsel for the appellant, and Mr. Cherubin Chuwa, learned State Attorney for the respondent/Republic is hereby certified as a true copy of the original.

THE COURT OF APPEAL OF TANZANIA

S. J. KAINDA
DEPUTY REGISTRAR
COURT OF APPEAL