

Uganda suspends the implementation of withholding VAT

Our perspective



The Government of Uganda has heeded to the calls of the business community by suspending the implementation of withholding VAT which was one of the sweeping tax changes in the budget cycle for the financial year 2018/19. By notice in the Uganda Gazette published on 28th September 2018 but effective 20th September 2018, the Minister responsible for Finance revoked the earlier Value Added Tax (VAT) (Designation of Withholding Agents) Legal Notice issued in June 2018 that had appointed 680 taxpayers as withholding agents for VAT purposes.

Though well intentioned to curb tax fraud and evasion as well as get reluctant eligible enterprises register for VAT, the unrestrained reach of withholding VAT had imposed a cashflow strain on the business operations of many taxpayers that also have to bear with the 6% withholding tax deduction on their eligible payments unless exempted.

Withholding VAT is increasingly becoming popular with tax authorities in Africa as a means of collecting VAT. Though suspended by Uganda in the meantime, we believe that it will be reinstated in the near future once the concerns of taxpayers have been addressed.

Introduction of withholding VAT

The Value Added Tax Act was amended effective 1st July 2018 giving power to the Minister responsible for Finance to designate selected taxpayers as withholding agents for VAT purposes. The Bill presented to the Parliament for deliberation had initially proposed that the designated agents withhold half of the VAT payable to the vendors but this was revised by the final Act to cover the entire amount of the VAT due.

Uganda joined Kenya as the other country in East Africa applying withholding VAT albeit at a much lower rate of 6% compared to Uganda's entire VAT payable at the rate of 18%. The VAT rate in Kenya is 16%. Kenya also experienced challenges in implementing its withholding VAT system leading to its suspension in 2013 but eventually reintroducing it in 2016. Ghana and Zambia too have withholding VAT at 7% and 16% respectively though as explained further in this note, the Zambian regime is more equitable to the taxpayers.

Operation of the withholding VAT regime

Though final consumers bear the tax burden, the obligation to charge and collect VAT from customers/buyers as well as remittance to the tax authorities falls on the vendors under the normal accounting rules of VAT. The withholding VAT regime somewhat flips the rules requiring designated withholding agents to deduct at source the VAT that is due on payments to their vendors. The deducted VAT is then remitted to the Uganda Revenue Authority (URA).

In comparison to the Zambia system, Uganda's withholding VAT regime falls short on equity which is a key principle upon which sustainable tax systems are built. Vendors of goods and services are still required to account for the VAT due on payments received from their customers regardless of whether their customers who are withholding agents have deducted at source the VAT due on their payments. Vendors therefore have to borrow or dig into their cash reserves to fund the VAT shortfall arising from the deduction of VAT

at source and remittance to the URA by the withholding VAT agents.

It is however important to note that once the withheld VAT is accounted to the URA by the withholding VAT agents, the vendors are entitled to a credit of the withheld VAT subject to the generation of a withholding certificate.

Zambia's withholding VAT system is more equitable to the taxpayers compared to Uganda because it removes the vendor's obligation to pay VAT to the tax authorities where a withholding agent has deducted the VAT at source on payment and remitted the same to the tax authorities. This is a key omission in Uganda's regime and creates contradictions requiring vendors to account for the VAT on their payments even though the same has been deducted at source by their customers. The vendors obligation under the VAT system is to charge, collect and remit the VAT due from their customers to tax authorities. Requiring vendors to remit VAT on their sales even though the same has been deducted at source on payment by their customers is inequitable.

Assessment of the withholding VAT system

The withholding VAT system can help check tax fraud and evasion as well as encourage eligible enterprises register for VAT. Non VAT registered enterprises would lose out on a credit in respect of the deemed VAT deducted at source by their customers while making payments. It is our recommendation therefore that Uganda's withholding VAT system is reviewed to primarily focus on tax fraud and evasion.

Uganda's withholding VAT regime creates a cash flow strain for taxpayers as they are unable to collect the VAT ordinarily receivable from their customers and are also required to dig into their cash reserves or borrow to meet any shortfalls in the VAT remittances due to the URA arising from the VAT withheld at source by their VAT withholding customers.

Though the VAT deducted at source by the customers is ordinarily creditable to the vendors in the subsequent period, delays by

withholding agents in remitting the withheld VAT to the URA can delay the activation of this credit. There were also challenges experienced by taxpayers on how to generate withholding VAT certificates to enable the vendors access the credit for the VAT withheld at source in respect of their payments.

The withholding VAT system did not equally take into account the cost of modifying business and accounting systems to enable the calculation, deduction and remittance of withholding VAT to the URA. It creates non value adding work for tax administration as withholding agents need to process the transactions to file on the withholding VAT schedules and the continuous reconciliations that vendors have to carry out to match the withheld VAT with their payments.

The withholding VAT system also increases tax repayments due to taxpayers given that there is limited output VAT if any to offset against input VAT and would have to seek tax refunds. There are occasional delays by tax authorities in processing tax refunds and quite often refund applications trigger off comprehensive tax audits covering other tax heads other than VAT.

Conclusion

While the government needs to increase the ratio of tax collections to

Gross Domestic Product from the present under 14% to levels nearer the 24% benchmark recommended by the International Monetary Fund, there should be a careful balance as short term gains in terms of aggressive tax collections can affect economic productivity in the long run. Enterprises have pointed out that they may have to scale down their productive activities if they have to allocate their cash reserves or borrowings to funding tax payments a situation that the suspended withholding VAT regime had created.

There are also uncertainties that need to be clarified by the URA on how taxpayers should treat the VAT that had been withheld from 1st July 2018 to the time of suspension. There have been challenges in the generation of withholding VAT certificates and vendors who have already suffered this deduction may be unable to have the benefit of this credit unless this is addressed.

Uganda's withholding VAT system should be reconsidered to mainly address VAT fraud and evasion. It would also be important to lower the rate of VAT that is deducted but in any case the Zambian variant that exempts taxpayers who have suffered withholding VAT at source to account for the same while filing their tax returns is most equitable.



Though well intentioned to curb tax fraud and evasion as well as get reluctant eligible enterprises register for VAT, the unrestrained reach of withholding VAT imposes a cashflow strain on tax compliant businesses.



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From 2004 to 2008, he worked in Russia where he led Deloitte's oil and gas industry group and established Deloitte's office in Sakhalin. He moved to East Africa in 2009 leading Deloitte's energy and resources industry group in Uganda, Kenya, Tanzania, Rwanda, Ethiopia and Mozambique. He was initially based in Kampala, Uganda later relocating to Dar es Salaam, Tanzania. Bill returned to the UK in 2014 supporting Deloitte UK teams working on outbound projects investing in Africa and was a key member of Deloitte UK's energy and resource practice until his retirement from the firm in September, 2018.

Bill is a graduate of Oxford University and completed his inspectors' training with the UK Inland Revenue in 1989. ■



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Denis leads the energy and tax practice at Cristal Advocates. He is qualified both as a Lawyer and Chartered Accountant with vast experience serving various industries in Sub Saharan Africa. Before joining Cristal Advocates. He had worked for close to 10 years with Deloitte and Touche where he started his career and rose to senior managerial positions.

At Deloitte, he lived and worked in Uganda, Kenya, Tanzania and the United Kingdom for over 6 years and subsequently became the firm's chief of staff for the Energy and Resources Industry Group seeing him play a lead advisory role in Uganda, Kenya, Tanzania, Mozambique, South Sudan, Somalia and Ethiopia.

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Prior to joining Cristal Advocates, he had worked as a Private Secretary to the President of the Republic of Uganda. During this time, he participated in several public and private sector engagements that included advising and coordinating activities relating to oil and gas as well as infrastructural projects of national significance. John had earlier worked with the Post Bank Uganda Limited and Shonubi Musoke and Co. Advocates.

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Dickens leads the oil and gas practice at Cristal Advocates. He has an in depth appreciation of Uganda's oil and gas sector having served as the maiden Company Secretary of the Uganda National Oil Company (UNOC) and the Uganda Refinery Holdings Company Limited (URHC). UNOC represents the Government of Uganda commercial interests in the oil and gas sector while URHC represents government interests in the refinery project as well as managing the petrol based industrial park.

Dickens was instrumental in UNOCs formation and initial period of operation and also served as its head of Contracts, Negotiations and Advisory until May 2018. Prior to joining UNOC, Dickens was Legal Counsel at the Petroleum Directorate of the Ministry of Energy playing key legal advisory roles on the negotiation and implementation of PSAs, Joint venture and other oil and gas agreements. He was also part of the team that shepherded the process of enactment of the current Ugandan oil and gas Legislations and Regulations including the local content requirements.

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