Cristal Advocates

Closing the Value Added Tax Gap in Uganda

Will the registration of foreign vendors achieve this objective?

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1. Introduction

In a public notice recently issued in local newspapers but also uploaded on its website at this link https://www.ura.go.ug/Resources/webuploads/GNRART/Public%20Notice%20-%20E%20business%20(1).pdf, the Uganda Revenue Authority ('URA') announced that it will going forward, enforce the provisions of the Value Added Tax Act ('VATA') introduced by amendments in 2011 and 2018 that require non-resident vendors to register or appoint local agents to account for the VAT arising on their supplies in Uganda. Though many countries oblige non-resident vendors to register for VAT under specified circumstances, it remains to be seen whether this measure largely targeted at digital and intellectual property transactions would achieve the intended objective of closing the VAT gap and increase the tax revenue collections that have stagnated at under 14% as a ratio of Gross Domestic Product for the past 5 years a discussion that this publication delves into.

The rise of the digital economy has fundamentally altered the business landscape that has circumvented traditional tax systems. The information transferred over the internet has emerged as a key driver of global commerce and there is a worldwide push for countries to align their tax systems to the reality of the digital economy to protect but also expand their tax bases proportionate to the value generated by the digital economy. Countries that have recently introduced VAT on digital and electronic transactions or set out the requirement for non-resident vendors to register for VAT in-country under specified circumstances in their attempt to cope up with the digital economy include Singapore, Australia, New Zealand, Japan, Taiwan and South Africa.

2. Registration of non-resident vendors

Section 16 of the VATA sets out the circumstances under which services are deemed to be supplied in Uganda even though the vendor is without business presence creating an obligation to register for VAT including filing the applicable returns in relation to VATable sales. Failure to comply with the registration and attendant compliance requirements attracts sanctions. The supply of the following services below is deemed to take place in Uganda even if supplied by a non-resident if the recipient of the service is not a taxable person:

a) The services are physically performed in Uganda by a person who is in Uganda at the time of the supply;
b) The services are in connection with immovable property in Uganda;
c) The services are radio or television broadcasting services received at an address in Uganda;
d) The services are electronic services delivered to a person in Uganda at the time of the supply. Electronic services include the following when provided or delivered remotely: websites, web-hosting or remote maintenance of programs and equipment; software and the updating of software; images, text and information ; access to databases; self-education packages; music, films and games including games of chance; political, cultural, artistic, sporting, scientific and other broadcasts and events including television;
e) The supply is a transfer, assignment, or grant if a right to use a copyright, patent, trademark or similar right in Uganda;
f) The services are telecommunication services initiated by a person in Uganda other than a supply initiated by a supplier of telecommunications; or a person who is roaming while temporarily in Uganda.

3. Reverse charge VAT system

Uganda already operates the reverse charge VAT system and pundits could argue is sufficient to facilitate the collection of VAT on qualifying supplies by non-resident persons. Reverse charge VAT departs from the normal principles of VAT where the seller of goods and services charges, collects and remits the VAT to the URA. Under the reverse charge mechanism, the rules are however flipped. The recipient/buyer rather than the seller of services as is the norm self-charges output VAT on the imported services received and where applicable remit the VAT to the URA.

Reverse charge VAT in Uganda is provided for under Section 4(c) of the Value Added Tax Act (VATA) which imposes VAT on non-exempt services imported by any person. The standard Ugandan VAT rate is 18%. Reverse charge VAT is originally a European Union ('EU') concept. Before its introduction, there was rampant VAT fraud perpetrated through the use of false invoices purportedly issued by vendors in other EU member countries that would tempt some vendors to use these invoices to lodge fictitious VAT refund claims. Unless the recipient of the imported services is a final consumer or is a business with mixed supplies (exempt and VATable supplies), the international norm is that reverse charge VAT is tax neutral. This essentially means that there is no cash outflow by the business on declaration of the imported services eliminating VAT refunds.

Until 2012 when the VATA was amended, reverse charge VAT in Uganda was tax neutral. Taxpayers that imported services into Uganda for their business operations would self-charge VAT at the rate of 18% on the value of the services received. They would include the arising output VAT on the imported services in their VAT return but also claim a corresponding credit as input VAT.There would be no cash outflow as the input credit would net off the output VAT declared. This was however not the case with final consumers of services, non-registered persons or taxpayers that made both exempt and VATable sales. They would have some payment to make to the URA. With the amendment of the law in 2012, taxpayers' ability to claim as an input credit the output VAT declared on imported services was removed. This new position departed materially from international norms and practice. It is only Uganda and Rwanda that take this position in East Africa. The 2012 amendment was criticized by the business community and tax experts alike who decried its impact of increasing the cost of doing business in Uganda. Some services cannot be sourced locally and denying taxpayers a VAT credit for essential services procured to run their business operations creates an unnecessary expense.

The reverse charge system is an effective means of collecting VAT on supplies in a Business to Business situation (B2B) given that the compliance burden is shifted from the non-resident supplier to the customer/ purchaser who is within the reach of the tax authorities locally easing verification as well as enforcing compliance of the collection of the underlying VAT.The compliance costs are also lower because the supplier is not required to comply with tax obligations in the customer's jurisdiction.

4. Business to Consumer transactions

While the reverse charge VAT mechanism as explained above generally works well in a B2B context, it is ineffectual in a Business to Consumer (B2C) setting. Under the reverse charge VAT system, the final consumer accounts for the VAT on services and intangibles acquired from foreign suppliers to the local tax authorities.

The level of compliance with a reverse charge mechanism for B2C supplies is likely to be low, since final consumers who are not businesses may have little incentive to declare and pay the tax due, at least in the absence of meaningful sanctions and the inability of tax authorities to audit consumption and enforce the collection of small amounts of VAT from large numbers of final consumers with the costs outweighing the revenue involved.

It is for this reason and in line with the recommendation of the *'OECD report on the design and operation of mechanisms for the effective collection of VAT/GST in cases where the supplier is not located in the jurisdiction of taxation'* ('OECD Report') that Uganda now requires non –resident vendors to register for VAT in Uganda as a means of closing the gap on VAT collections with respect to B2C transactions.

5. Registration based collection regime

In enforcing the latent provisions of the VATA, Uganda is now implementing the registration based regime to collect VAT on B2C supplies of electronic supplies and intangibles by foreign suppliers. The registration based collection system is recommended by the OECD report noting that this regime should be implemented with minimal compliance and administrative burdens cognisant of the revenues involved.

The OECD report also recognises that the compliance for the non-resident foreign vendors can be facilitated by allowing such suppliers to appoint third party service providers or agents to act on their behalf in carrying out certain procedures, such as submitting returns. This measure is already embedded in Uganda's tax legislation whereby non-resident vendors can appoint local agents to facilitate their in-country VAT compliance.

The OECD report further notes that countries may opt to limit the scope of the requirement for non-resident persons to register for VAT which is the position that Uganda has adopted restricting the registration obligation to services that relate to intangibles, telecommunications and electronic transactions.

6. Conclusion

As the URA directive gets implemented, stakeholders potentially affected by this measure and neighbouring countries that may be interested in adopting the same will keenly follow its progress. It is undisputable that URA is thin on ground to be able to trace and track transactions of non-resident vendors. This therefore means that the effectiveness of the proposed registration based collection regime will depend on its ease of compliance and ownership by the stakeholders. It is not clear whether the URA has engaged and consulted the business community to seek its input on this proposed measure.

Further, as non-resident vendors with customers in Uganda ponder the implications of the URA directive, a number of queries requiring firm URA answers remain unanswered. It is likely based on the reading of the applicable legislation that all rights and obligations accruing to VAT registered persons such as filing returns, claiming input VAT suffered locally, raising compliant invoices, using the prescribed exchange rates and entitlement to VAT refunds would also apply to the registered non-resident vendors. If this is the case, it may increase the compliance costs for the non-resident vendors. The OECD report calls for simplified reporting and even recommends excusing foreign vendors from the routine monthly obligation of filing VAT returns by pegging this to thresholds determined by the tax administration and to allow these suppliers to report the VAT payable in a future filing period when reportable thresholds are met. Invoices in foreign currency are converted at official URA rates published on its website but the OECD report notes that it could be reasonable for tax authorities to allow non-resident foreign vendors to use reasonable and coherent internal business rates which are based on averages over time of the official rates with built-in tolerance for small differences. We also believe that non-resident vendors would be anxious to understand that registration for VAT purposes in Uganda would on its own not crystallise business presence (permanent establishment) in Uganda for income and other taxes.

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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 is the Managing Partner at Cristal Advocates where he also leads the energy and tax practice. 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.

Denis is widely published and a regular commentator in the local, regional and international media and speaker at various forums regarding the taxation and financing of energy projects as well as the protection of large capital projects within the framework of international investment law.

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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 Holding 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 UNOC's 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 enacting the current Ugandan oil and gas Legislations and Regulations including the local content requirements.

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He joined Cristal Advocates from Kizza, Tumwesige, and Ssemambo Advocates. He previously worked with the Advocates Coalition for Development and Environment (ACODE). He also undertook a traineeship with the oil and gas division of Webber Wetzel in Johannesburg, South Africa.

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