THE REPUBLIC OF UGANDA

IN THE MATTER OF THE TAX APPEALS TRIBUNAL

TAT APPLICATION NO. 4 OF 2011

1. **TULLOW UGANDA LIMITED**
2. **TULOW OPERATIONAL PTY LTD …….....…… APPLICANTS**

VERSUS

UGANDA REVENUE AUTHORITY …….....…….…… RESPONDENT

RULING

This ruling is in respect of an application brought by the applicants challenging initial assessments of income tax of US$ 472,748,128 by the respondent in respect of a transfer of their interests in Exploration Areas EA1, EA2 and EA3 to CNOOC and Total for the consideration of US$ 2,933,330,400. The said assessments were eventually revised by the respondent to US$ 467,271,971 being capital gains tax. The applicants being aggrieved by the said assessments appealed to the Tribunal.

This ruling is brought after the Tribunal has complied with S. 13 of the Tax Appeals Tribunal (TAT) Act. Mr. Martin Feeta, one of the members of the panel listening to the dispute passed away on the 20th May 2014. At the time of his passing away, all the parties had presented their evidence, closed their cases and made their submissions. Delivery of the ruling was pending. At the time of his passing away the then Tribunal had reached a decision. On the 16th June 2014, when the matter came up for ruling, the parties were informed that the Tribunal did not have the legally required Coram to deliver a ruling. Counsel for the parties agreed that a new member should be assigned to the panel to replace Mr. Martin Fetaa. It was also agreed that matter be reheard by the record of evidence being availed to a new member under S. 13(5) of the Tax Appeals Tribunal Act without the need of recalling witnesses. Mr. Pius Bahemuka was appointed to replace the deceased. The record of the evidence and the submissions of the parties have been handed to him. Though the Tribunal cannot say that this is a ruling of four members as the Coram is three, it can say that this is a unanimous decision.

1. SUMMARY OF CASE

The facts agreed upon by both parties are:

1. The first applicant, Tullow Uganda Limited (hereinafter called "TUL"), is registered under the laws of the Isle of Man and was formerly Energy Africa Uganda Limited ("Energy Africa"). The second applicant, Tullow Uganda Operations Pty Limited (hereinafter called "TUOP") is registered under the Corporations Act 2001 in Western Australia and was formerly Hardman Africa Pty Ltd ("Hardman"). The applicants are residents for tax purposes in Uganda.

2. On the 8th October 2001, both the applicants and the Government of Uganda ("GOU") executed a Production Sharing Agreement (PSA) under which they were granted exploration, development and production rights in Exploration Area EA2 (the "EA2 PSA"). It was signed by Hon. Syda N. M. Bbumba, Minister of Mineral and Energy Development for and on behalf of the Government, by Mr. Edward John Ellyard (Managing Director) on behalf of Hardman and by Mr. W.A Nel (Chief Operating Officer) on behalf of Energy Africa.

3. Another PSA, in relation to EA1, was entered into on the 1st July 2004 (the "EA1 PSA") between Energy Africa, Heritage Oil and Gas Limited ("Heritage") and the GOU. The EA1 PSA was signed for and on behalf of the GOU by Hon. Daudi Migereko, Minister of State for Energy, also holding the portfolio of the Minster of Mineral and Energy Development, by Mr. Brian Smith on behalf of Heritage and by Mr. Rhimwaan Gasaut on behalf of Energy Africa.

4. Another PSA, in relation to EA3A, was entered into on the 8th September 2004, between Energy Africa, Heritage and the GOU ("the EA3A PSA"). The EA3A PSA was signed for an behalf of the GOU by Hon. Syda N. M. Bbumba, Minster of Mineral and Energy Development, by Mr. Brian Smith on behalf of Heritage and by Mr. Andrew Wyndham on behalf of Energy Africa.

5. Heritage and Energy Africa agreed to continue with the Joint Operating Agreement ("JOA") between Heritage and Energy Africa entered into on the 29th August 2002 for EA3, under which the first applicant's participating interest was 50%.

6. Prior to 2009, Tullow Oil Plc, the parent company of both applicants, acquired the Energy Africa Group, which had a subsidiary, which later became TUL. Tullow Oil Plc later acquired the Hardman Group, including Hardman Africa Pty Limited, which later became TUOP. Tullow Oil Plc acquired the relevant subsidiaries' rights and interests in the PSAs in Uganda.

7. At this stage the interests in the PSAs were as follows:
   a. TUL held 50% of EA1, EA2 and EA3A;
   b. TUOP held 50% of EA2; and
   c. 50% of each of EA1 and EA3A was held by Heritage and the interests then held by TUL in EA1 and EA3A are hereinafter referred to as "the Other Original Interests".

8. The applicants through their exploration activities discovered hydrocarbons in the respective exploration areas.

9. On or about the 17th January 2010, TUL invoked its pre-emptive rights under the JOA for the purchase of 50% participating interests of Heritage in Exploration Areas EA1 and EA3A (the Heritage interests") at a consideration of US$ 1,450,000,000 (United States Dollars one billion four hundred and fifty million), subject to approval from the GOU.

10. On about the 26th January 2010, TUL and Heritage signed a Sale and Purchase Agreement (the "SPA") under which TUL would acquire Heritage's 50% participation rights in Exploration Areas EA1 and EA3A.

11. On the 6th July 2010, the GOU granted a conditional approval to the transaction between Heritage and TUL.

12. On the 18th October 2010, the respondent raised assessment number SA/LTO/2569 of US$ 390,924,460 and assessment number SA/LTO/2570 of US$ 84,999,660 on TUL and TUOP respectively being income tax (Capital Gains Tax).

13. On the 1st December 2010, the applicants objected to the assessments.

14. On the 24th February 2011, the respondent made an objection decision that adjusted the assessment on the TUL. The assessment No. SA/LTO/2569 of US$ 390,924,460 was amended to US$ 387,748,469, while assessment No. SA/LTO/2570 of US$ 84,999,660 was

unaffected, resulting in a total of US$ 472,748,128.

15. On the 15th March 2011, the applicant, the GOU and the respondent executed a memorandum of understanding ("MOU").

16. On the 25th March 2011, the applicants filed an application for review before the Tax Appeals Tribunal (TAT) contesting the assessments and the objection decision by the Commissioner of the respondent.

17. TUL acquired the Heritage Interests pursuant to the SPA and upon fulfilment of conditions in the MOU of 15th March 2011. Following the acquisition the holdings in the Exploration Areas were:
    a. TUL held 50% of EA2 and 100% of EA 1 and EA 3A; and
    b. TUOP held 50% of EA2.
18. The applicants disposed of 66.67% of their interests in EAs 1, 2, and 3A to CNOOC and Total at US$ 2,933,330,400 (United States Dollars two billion nine hundred thirty three million three hundred thirty thousand four hundred).

19. Following the disposal the holdings are:
    a. TUL holds 33.33% of the interests under the EA 1, and EA 3A PSAs.
    b. TUOP holds 33.33% of the interests under the EA2 PSA.
    c. CNOOC holds 33.33% of each of the interests under the EA1, EA2 and EA3A PSAs; and
    d. Total holds 33.33% of each of the interests under the EA1, EA2 and EA3A PSAs.

20. On or about the 22nd February 2012, the applicants paid US$ 141,824,438 (United States Dollars one hundred forty two million eight hundred twenty four thousand four hundred thirty eight) being 30% of the tax assessed.

2. ISSUES

The issues agreed upon by both parties are:

1. In respect of EA2

1.1 Whether Article 23.5 of the PSA for area EA2 covers capital gains/income tax arising from gains derived out of disposal of interests in the PSA?

1.2 Whether Article 23.5 of the PSA for EA2 entered into by and between the Government of Uganda acting through the Minister of Energy and Mineral Development is valid/lawful under Uganda Law?

1.3 Whether Article 23.5 is valid/lawful under international law?

1.4 If the answer of either issue 1.2 or 1.3 is in the affirmative, should Article 23.5 be enforced by the TAT, and if yes do the assessments fall to be discharged or not?

1.5 Whether the respondent is estopped by Article 23.5 from raising an assessment in respect of the gains made on the disposal of the applicants' interest in EA2, and if yes, do the assessments fall to be discharged or not?

1.6 Whether the reference to the respondent being estopped includes references to principles rooted in fairness including legitimate expectation?

2. In respect of the other PSAs

What is the gain, and how is that gain computed, on the disposal of the interests in the PSAs (a) purchased by TUL from Heritage; and (b) otherwise?

3. Reinvestment relief

3.1 Whether the applicants are entitled to reinvestment relief under S. 54(1) (c) of the Income Tax Act Cap 340?

3.2 If so what is the quantum of the disposal consideration in respect of which reinvestment relief can apply?

3. REPRESENTATION OF THE PARTIES

The applicants were represented by Mr. Stephen Brandon QC, Mr. Oscar Kambona, Ms. Amanda Hardy, Ms. Reshma Shah, Mr. David Mpanga and Mr. Bruce Musinguzi.

The respondent was represented by Mr. Ali Ssekatawa, Mr. Peter Mulisa, Mr. Matthew Mugabi, Mr. Martin Muhanji, Ms. Syson Ainebabazi and Mr. Geoffrey Mucurezi.

4. SUMMARY OF EVIDENCE ADDUCED AT TRIAL

All the parties agreed that the applicants shall be allowed to file witness statements. Their witnesses would then be cross-examined by the respondent. The respondent opted to call its witnesses for examination in chief instead of filing witness statements.

The applicants' first witness was Mr. Martin Graham, the General Counsel, of the Tullow Group (hereinafter called 'Tullow') which includes both applicants. In his statement, he stated that he dealt with the acquisition of Energy Africa Uganda Limited and Hardman Resources Limited by Tullow. He deponed that on their acquisition, Energy Africa Uganda Limited changed its name to TUL while Hardman changed to TUOP.

He further deponed about the signing of the PSAs between the GOU and the applicants. The PSAs gave exclusive rights to a party to explore for hydrocarbons in certain areas known as Exploration Areas (EAs). These areas included EA1, EA2 and EA3A. At the beginning of January 2010, TUL held 50% of the interests in EA1, EA2 and EA3A and TUOP held 50% of the interest in EA2. The other 50% interests in EA1 and EA3A were held by Heritage. On the 17th January 2010, TUL exercised its pre-emption rights and acquired Heritage's interests in EA1 and EA3A.

In February 2010, Heritage asked the GOU for consent to the transaction. The GOU gave consent subject to payment of tax. Heritage objected to the payment of tax. Later an arrangement was agreed upon where Heritage deposited the tax payable on an escrow account. The GOU and the applicant entered into a memorandum of understanding on the 15th March 2011 where TUL paid US$ 313 million tax as agent for Heritage.

According to Mr. Graham, Tullow acquired Heritage's interests in EA1 and EA3A with the express intention of selling them to third parties. It had intended to sell 50% of the interests in each of the PSA. However the GOU would not give its consent to a sale to only one party. It eventually sold 66.67% of its interests in each of the PSAs to CNOOC and Total on 21st February 2012, each purchaser taking 33.33% of the interests. He gave a background and history and the nature of oil exploration in Uganda in his statement, which we shall not repeat. He stated that the exploration areas had not yielded any income as yet.

Mr. Graham, in his statement, noted that under the PSAs the GOU gets its stake on oil in a number of ways which includes royalties, profit oil and 15% of the contractors' share of profit oil under the state participation provisions. If a project fails the GOU does not suffer any loss. The costs recoverable are pooled together each year, and the balance is reduced by the value of cost oil received. Unrecovered costs are carried forward to subsequent years until full recovery is completed. He argued that this is not a tax relief or any kind of relief like indemnity. It is simply the recovery of expenditure incurred by one party. Such recovery does not prevent the oil company from deducting what it expended in tax computation.

Mr. Graham discussed the protection of the oil companies in the PSAs. He stated that "it is common for governments to provide certain incentives to encourage oil exploration. These incentives take the form of exemption or reliefs that reduce the company's costs." According to him, the EA2 PSA contained a clause providing that no tax would be payable in respect of a farm down of TUL's interests in Article 23.5. Mr. Graham testified that Article 23.5 of the EA2 PSA provided that the assignment or transfer of an interest under the agreement would not be subject to any tax, fee or other impost or fee levied either on the assignor or the assignee. To him he was not sure whether Capital Gains Tax and transfer tax are the same. He stated that at the time the EA2 PSA was entered into, it was not certain that there were any hydrocarbon

deposits in Uganda and so potential investor's interest in the EA2 PSA was very low. He argued that Article 23.5 was advantageous to the GOU because it significantly increased the possibility of investment in Uganda. He argued that without any tax breaks it was unlikely that any companies would have invested in Uganda, especially where exploration involved a lot of monies. According to him, Article 23.5 of the EA2 PSA was certainly important to Tullow. It had incurred considerable expenditure. Tullow could not keep the whole of its interests in EA2, so a farmdown was inevitable. Mr. Graham testified that the applicants relied on Article 23.5 of the EA2 PSA when selling their interest as they wanted to benefit from the no tax on the farmdown of their interests.

Mr. Graham said that US$ 1.45 billion was paid by TUL for the acquisition of Heritage's interests. The money was raised from shareholders. He said farming down was a way of the applicants financing exploration activities and development. He referred to exhibit A46, a letter to the Minster of Energy, where the applicant expressly stated that upon acquisition of the interest in Blocks 1 and 3A, the applicants would farm down at least 50% of the interests in all the Blocks to one or more partners acceptable to GOU. He stated that the applicants were forced to sell an extra 16.67% of their interests. There was pressure from the GOU for the applicants to break the monopoly in oil exploration. There was no official communication that the applicants should sell 66.67% of their interests. However there were several meetings with GOU officials at different levels where it was indicated that the applicants should retain a third of their interests.

Mr. Graham said he did not engage in drafting the PSA for the farmdown. The legal team did it. However as head of the legal team he took responsibility. The tax department was working with him. Mr. Graham stated that he is not a tax expert. The applicants did not do a due diligence before they transacted with Hardman and others.

Mr. Graham said that the applicants sold first what was purchased from Heritage. The Heritage interest was the whole of the value that was presented in the PSA. They took over the costs incurred by Heritage. The monies the applicant used to pay the tax for Heritage came from Total and CNOOC.

The applicant's second witness was Mr. Paul McDade, the Chief Operating Officer of the Tullow. He noted that the respondent raised assessments on the 18th October 2010 in respect of the three blocks. However the farmdown had not taken place. It took place on the 27th February 2012. At the beginning of January 2010 TUL held 50% interests in EA1, EA2 and EA3A and TUOP held the other 50% of EA2. The other 50% of EA1 and EA3A was held by Heritage.

Mr. McDade gave a background to the farmdown in his witness statement, which is as stated in the agreed facts. He added that since the discoveries in 2006 and 2007, the applicants planned to farmdown in order to meet the substantial costs needed for exploration. One of the functions of the farmdown was to assist financing their projected investments.

Mr. McDade further testified that the GOU indicated to the senior Tullow executives that a 50% farmdown would not be acceptable to it. It was GOU policy to avoid a monopoly situation in the Albertine Graben. Mr. Richard Inch emailed to him about a conversation he had with Mr. Kiiza, the Director of Economic Affairs, Ministry of Finance, Planning and Economic Development that the GOU would not allow a 50% split. The applicants changed their position of a 50:50 split to a 33:33:33 split as the former proposal would not be allowed. Mr. McDade argued that the disposal of 16.67% was therefore an involuntary disposal. He further testified that at the time of disposal Tullow was planning to reinvest considerable sums from the farmdown proceeds in assets of a like kind within one year from the farmdown.

In cross-examination, Mr. McDade said that the intention to sell 50% of its interest was not expressed in any form of board resolution. Mr. McDade reiterated his earlier position that Tullow wanted to sell at least 50% of its interests. There was no correspondence between GOU and Tullow that indicated that the latter wanted to sell 50% of its interest. He stated that there was a draft SPA which was on a basis of 50:50 made in February 2010. He did not clearly understand what a re-investment relief was.

In re-examination, Mr. McDade stated that the monies obtained from the sale were to be spent on the exploration activities, drilling, appraisal activities, testing of oils and associated activities

or development studies. All the expenditures met prior to the farmdown were exploration and appraisals expenditures, drilling of wells, bridges, procuring of service studies, geological, etc.

The applicant's third witness was Mr. Richard Inch, the Head of Tax for Tullow. The applicants are subsidiaries of the Tullow. He is a Chartered Accountant and a Chartered Tax Advisor and has held a number of senior tax positions. His duties involved the overall management of the group's tax affairs.

He stated that following the acquisition of Heritage's interests in EA1 and EA3A, Tullow agreed to sell a part thereof to Total and CNOOC. Tullow had intended to sell 50% of the interests in EA1, EA2, and EA3A. However before the GOU would grant the necessary consent, it required Tullow to sell a further 16.67% of the remaining interests. He stated that in a meeting of the 2nd February 2010, with Mr. Lawrence Kiiza the Director of Economic Affairs, he was told that GOU was not going to allow a sale of only 50% of the PSA and wanted a single distinct operator for each PSA, with each taking 33.33% interest. Mr. Inch testified that there were no minutes for the meeting he had with Mr. Kiiza, It was a conversation. There was no official communication.

He deponed that, on the 18th October 2010, the respondent raised assessments on Tullow. The completion of the disposal took place on the 27th February 2012. In response to the assessments, Tullow filed an objection on the 1st December 2010.

Mr. Inch, in his statement, averred that before 2008, there was no specific taxation regime for oil companies in the ITA though the PSAs contained relevant tax provisions. In 2008, the Ministry of Finance introduced a specific code in relation to petroleum operations by the insertion in the Income Tax Act 1997 of a new Part IXA by the Income Tax (Amendment) Act 2008. The 2008 Amendment Act, which was published on the 30th June 2008 had retrospective effect from 1st July 1997. Part IXA under S. 89G (a) provides for taxation in cases of transfer of interests. The deponent felt that the said Act did not impact on Tullow, in particular the EA2 PSA, because it had obtained an exemption.

Mr. Inch testified that around the time the 2008 Amendment Act was passed, Tullow was in discussion with its banks regarding funding of its operations. A farmdown was an important part

in its financing plans. It assumed that the farmdown proceeds would be received tax-free. In relation to the EA1 and EA3A PSAs, he thought that the new Part IXA in the ITA provided for exemptions in relation to the interests in the said PSAs.

Mr. Inch emphasized that Tullow did not anticipate any taxes. This was because the EA2 PSA was a legal and binding agreement. It had an exemption from capital gains tax in Article 23.5. Mr. Inch stated that: “the obligations under the PSAs were negotiated in good faith on the basis of the stability and certainty of the Uganda fiscal regime...” However, he stated that Mr. Kiiza told Tullow that there were views within the GOU that the EA2 exemption was not valid. Tullow was informed that the URA had in mind a tax liability of around US$ 470 million which indicated that the GOU did not accept that Article 23.5 of EA2 PSA gave an exemption.

Mr Inch argued that the sovereign state of the Republic of Uganda had the authority to enter such agreement and therefore could not collect tax. According to Mr. Inch, the terms of the PSA prevailed in case there was a conflict with the ITA. Tullow had the right to expect GOU to keep its words as set out and agreed in Article 23.5 of the PSA. According to Mr. Inch, GOU has given exemptions to other companies, for example Bidco.

Mr. Inch also submitted that Tullow’s cost base was the Heritage gain subject only to any potential deduction in respect of excess costs. He stated in his statement that Tullow has no excess costs. Tullow paid the base price of US$ 1,350 million and a contingent consideration of US$ 100 million. Tullow also paid an additional US$ 13,937,116 in respect of the working capital at completion. Tullow paid a guarantee cost of US$ 46,061,058, stamp duty of US$ 14,500,0000 on acquisition and legal fees of US$ 1,079,077 giving to total incidental costs of US$ 61,140,135.

In cross examination, Mr. Inch testified that the ITA imposed capital gains tax subject to the provisions of the SPA. He also testified that the proceeds from the farmdown would be used for exploration, production and development.

Mr. Inch informed the Tribunal that Heritage and Tullow had indivisible interests. There was no way one could split and say what is for Tullow and what is for Heritage. Mr. Inch stated that

there was no letter saying that Tullow was buying the Heritage interests specifically to sell. The intention was not expressed in any board resolution. However Mr. Inch said that was the common understanding of the senior management team.

He said that Blocks 1 and 3A were sold by Tullow to CNOOC and Total at a loss of US$ 175,577,251. He stated that there were additional payments that were made to Heritage and they could not pass them to the buyers. They incurred an economic cost of US$ 100 million contingent and guarantee fees to the bank which cost around US$ 46 million. He stated that Tullow sold 66.67% of its interests at US$ 2.9 billion but 50% of that were interests that formerly belonged to Heritage. They sold Heritage interests at US$ 1.45 billion at a loss. He said the answer would have been different for tax computation if they had considered the asset as undivided. He said the loss arose because Tullow expensed it with the cost of the asset acquired in accordance with international accounting standards. Legally Tullow sold Heritage interest first.

He testified that there was a difference between the first disposal by Heritage and the second disposal by Tullow in respect of computing the cost base and deductions. The distinction is that for an initial disposal, the cost base of the asset is the amount paid, to which is added incidental costs of the acquisition and in the case of a subsequent disposal the cost base is the first seller's gain.

The respondent called two witnesses. The first witness was Mr. Ernest Tumwine Rubondo, the Commissioner Department of Petroleum Exploration and Production in the Ministry of Energy and Mineral Development in the GOU. Mr. Ernest Rubondo gave a lengthy history of petroleum explorations in Uganda which he stated dates back as far as 1910, when oil seeps were reported. Oil explorations started but ended around 1940 as a result of the onset of the Second World War. In the 1980s efforts on oil exploration were restarted. A successful survey was done which identified 3 large deposit centres in the Graben.

To cut a long story short, in January 1997, the GOU licensed Heritage to explore oil in EA3A. In November 1997, the GOU signed an agreement with Hardman for EA2 which the latter surrendered in 1999 because oil prices had gone low. Heritage was joined by Energy Africa in

2000. In 2002, Heritage and Energy Africa drilled Turaco 1 where they encountered oil shoals. The companies also drilled Turaco 2 and 3 where they encountered hydro carbons in 2004. In 2004, Heritage and Energy Africa actually surrendered Area 3 and reapplied for it from the GOU. In July 2004, the companies acquired another licence in the Pakwach Basin. In 2006 oil was discovered.

Mr. Rubondo testified that he was part of the GOU team that negotiated the EA1 PSA. GOU would do a due diligence on a company and if it was worth dealing with, it would send it a draft PSA. The parties would then agree on the terms. He testified that Article 23.5 was in the model PSA that was prepared in 1993. It was not negotiated by the parties. He said that the intention of GOU was that it did not want licensees to be encumbered with fees, imposts and taxes. The objective of the clause was to facilitate the licensees to bring on board partners to share risk without the need to pay fees and imposts like stamp duties and signature bonuses. He said clearly the clause was not meant to cover taxes on gains. Its purpose was to facilitate the sharing of risk and not to guide the taxation of a gain.

He further testified that TUL acquired Energy Africa in 2004. TUOP acquired Hardman in 2007. TUL had 50% interests in EA1 and EA2. TUL was together with Heritage in EA3 in a 50% each joint venture. TUL took over Heritage's interests on 7th April 2011 after it exercised it right of pre-emption. TUL acquired the rights of Heritage to develop and produce oil. He stated that the said interests in the agreements were indivisible.

On cross-examination, Mr. Rubondo reiterated his earlier position that Article 23.5 does not apply to farmdowns. He stated that the farmdown to CNOOC and Total was dependant on consent from GOU, more precisely the Ministry of Energy and Mineral Development.

The respondent's second witness was Mr. Moses Mesach Kajubi, its Commissioner Domestic Taxes. The Domestic Tax Department is responsible for collecting all domestic taxes in Uganda inclusive of income taxes.

Sometime in October 2010, the department received the SPAs of Tullow, Total and CNOOC. The department studied the SPAs and realised that Tullow was selling its interests to Total and

CNOOC. On the 18th October 2010, the respondent issued assessments to Tullow. The assessments were issued because it was a one off transaction and it was of substantial value. The respondent revised the assessments on the applicant. A revised assessment was issued in February 2012 which was again revised in November 2012. What changed between the earlier assessments was that the cost base changed from US$ 1.299 billion to US$ 1.3136871116 billion because Tullow paid an extra US$ 13.687 million dollars to Heritage. There was also new information that Tullow incurred more costs from US$ 57,000,000 to US$ 61,903,387. The effect of the changes was to reduce the total tax payable to US$ 467,271,974.

The respondent in computing taxes made some deductions. These included the signature bonus in respect of EA 1 and EA 3A. Excess costs were allowed. The recoverable costs that had been sold by Heritage Oil were subtracted. The incidental expenses incurred by Tullow of US$ 47 million were allowed. The net gain for TUL was computed at US$ 1,303,081,531 and the tax at 30% was US$ 390,924,460. For TUOP the net gain was computed at US$ 28,332,200 and taxed at 30% bringing the tax to US$ 84,999,660. The total tax payable was US$ 475,924,120.05. Tullow objected to the assessments of the said taxes on the 1st December 2010. An objection decision was made on the 24th February 2011.

The assessments did not remain the same. Costs of about US$ 10,586,638 were accepted. These costs were related to guarantee commitment fees and legal fees of US$ 457,397 dollars and stamp duty of US$ 14,500,000. The assessments were revised to US$ 387,748,468.65 for TUL and US$ 84,999,660 for TUOP bringing the total to US$ 472,748,128.65.

The respondent rejected the applicants' objection to have no tax paid in relation to EA2 as a result of Article 23.5 of the PSA. Mr Kajubi argued that Article 23.5 of the EA2 PSA was not part of the ITA. The PSA was not an international agreement. Tullow is not an international organisation and the PSA was not ratified in accordance with the ratification of laws. Mr. Kajubi also argued that the powers to levy tax in Uganda are vested in the Parliament. The said income was not exempted by Parliament. The Ministry of Energy could not take away the power of Parliament to grant exemptions. Mr. Kajubi argued that capital gains tax is not a transfer tax and therefore is not exempted by the ITA.

Mr. Kajubi argued that excess costs should be used in the computation of taxes. Excess costs are relevant in subsequent disposals. Tullow argued that excess costs were nil. However the respondent argued that excess costs were US$ 150 million. According to Mr. Kajubi, excess costs reduce the cost base on the subsequent disposal. Mr. Kajubi argued that when a subsequent disposal is made, a taxpayer is only restricted to excess costs.

Mr. Kajubi testified that the recoverable costs incurred by the applicants were rejected as deductions. This is because they are available for recovery under the SPA. To allow them would give the taxpayer a double benefit.

As regards the issue of reinvestment relief, Mr. Kajubi stated that the respondent did not get any evidence of an involuntary disposal. In order for an involuntary disposal to take place it must be done against one's will. Tullow was willing to sell its interests. There was no evidence to show that Tullow was forced to sell the extra 16.67% of its interest. According to Mr. Kajubi what was required to prove involuntary disposal would be a letter, a decree or something in writing. Secondly, the proceeds of an involuntary disposal should be reinvested in an asset of a like kind. This has to be done within one year of the disposal. He contended that the transaction was concluded in March 2012 and there is no evidence that there was reinvestment within one year from the date of disposal. Any expenses that would be brought to the attention of the respondent would be used to make an adjustment. Mr. Kajubi opined that the assets of a like kind should be an investment in an interest in another PSA..

Mr. Kajubi said the sale price for the interests in EA1 was US$ 775 million and on EA3 was US$ 575 million. These figures were picked from the SPAs. The cost base was US$ 746,152,777 for EA 1 and US$ 553, 597,222 for EA2.He also argued that the economic loss claimed by the applicants was a creation and not real. The purported economic loss arose from Tullow claiming that what were sold first were Heritage's interests. Out of the 66.67% interest sold, 50% was what was purchased from Heritage. Therefore the cost base for that should be accepted as a cost in the computation of the loss. The loss was a result of the 'last in first out' (LIFO) in the allocation of costs approach. If the 'first in first out' (FIFO) approach was used there would be no loss. The gain for FIFO approach is about 230 million dollars.

Mr. Kajubi stated that ‘excess costs’ is the difference between the costs that are available for recovery from the first person who sold, minus anything that is recovered. They apply to a subsequent sale. Heritage had recoverable costs of US$ 150 million. He said that excess costs are deducted from cost oil. He defined cost oil to mean a contractor’s entitlement to production as cost recovery under a PSA. He said that a company obtains cost oil at the commencement of commercial production. There has not been any commencement of commercial production and recovery of costs. None of the companies involved, Heritage, Total CNOOC and Hardman have recovered any expenditure.

Mr. Kajubi told the Tribunal that stamp duty was paid in the acquisition of interests from Tullow to CNOCC and Total. He said there was no exemption for stamp duty. In order to get an exemption the Minister of Finance would have to issue a statutory instrument to that effect as per the powers delegated to him by Parliament. He stated that no tax exemption is valid unless there is a specific provision in the ITA. Tax holidays and tax exemptions require a statutory instrument issued by Parliament. He said the respondent does not grant exemptions, it implements. It issues certificates but the exemptions are granted by Parliament.

Mr. Kajubi said the right to recover costs is one of the rights disposed of under the SPA as an assignable interest. He stated that Tullow received consideration for the transfer of the said right to CNOOC and Total. To obtain a benefit from such a relief after disposing of the same interest would amount to double dipping.

5. SUMMARY OF THE PARTIES’ MAIN ARGUMENTS

On issue 1.1, the applicants submitted that the completion of the sale and purchase between the applicants, CNOOC and Total occurred on the 21st February 2012 when the various conditions were met and the purchase price paid. As a result thereof the applicants transferred parts of their interests in the PSAs to CNOOC and Total on that date. The applicants contended that such disposals were governed by S. 89G of the ITA. Hence they attracted capital gains tax.

The applicants submitted that EA2 PSA Article 23.5 contained an exemption from taxes. It not only covered income tax but all other fees or imposts levied on an assignor. Such a wide

exemption cannot be said to exclude a charge to tax under the ITA. The income tax charge imposed by the Income Tax Act is clearly a charge to tax. According to them, Article 23.5 of the Agreement was wide and clearly covered income tax on capital gains accruing on assignment or transfer. The applicants argued that when a person passes an interest in an agreement to another contractor, he must assign or transfer that interest. The applicants cited *Black's Law Dictionary* which defines assignment as an "act by which one person transfers to another, or causes to vest in that other, the whole of the right, interest, or property which he has in any realty or personality..." According to them, Article 23.5 of the Agreement was wide and clearly covered income tax on capital gains accruing on assignment or transfer.

On issue 1.2, the applicants argued that any minister irrespective of whether he or she is the Minister of Finance could enter an agreement containing a term as found in Article 23.5. They contended that the Minister as an agent of the GOU had authority to sign the PSA on its behalf in respect of each provision. The applicants contended that RW1, Mr. Rubondo, admitted that when an agreement was reached the Ministry would send it to the cabinet before signing.

The applicants submitted that the Minster validly entered into the agreement on the basis of powers conferred under the Petroleum and Energy Production Act 1985 (PEPA). The applicants argued that under S. 2 of the PEPA, the GOU may enter into an agreement with any person in respect of, inter alia, the grant of a licence, etc and any matters incidental to or connected with the foregoing. The applicants argued that S. 2 applied to Article 23.5 of the PSA and granted necessary powers to the Minister to enter into the agreement where an exemption was granted. This was because Article 23.5 was incidental and connected with the foregoing, that is, the granting of a licence. The applicants cited the case of *Scottish Widows plc V RCC* [2010] STC 2133 where the court emphasised that "...the phrase 'in connection with' generally merits a wide interpretation..." it was their submission that "connected with" requires a very wide interpretation, akin to "having to do with" in PEPA, S.2. The applicants submitted that the fact that there may be specific exemptions in the ITA governed by particular rules does not mean that the GOU cannot grant a tax exemption under another Act.

The applicants argued that though the ITA was enacted after the PEPA, there is nothing in the ITA that could be said to amend or repeal the PEPA. A later law can only implicitly amend an

earlier law where two provisions in question cannot co-exist. S. 2 of the PEPA covers a number of possible matters, most of which have nothing to do with tax. Thus the taxing legislation cannot possibly be said to repeal implicitly a provision with wider import. S. 2 of the Act does not grant an exemption from tax, it empowers the Minister to grant such an exemption. It empowers the GOU to agree to refrain from enforcing the ITA in certain circumstances which are "incidental to or connected with" the matters in the PEPA.

The applicants submitted that there are other authorities given to the GOU acting through the Minister to enter the EA2 PSA, including Article 23.5. These authorities include pre-written constitution powers preserved by the Constitution. This is evidenced in Article 274 of the Constitution. The applicants contended that the existing common law or prerogative powers vested in the President and the rest of the executive continue to apply, including the power to waive or vary payment of tax which existed prior to the enactment of the Constitution. Therefore the pre-written constitution powers are one of the sources of the Minster's powers to enter into Article 23.5.

The applicants contended that under the Constitution of Uganda, the Minster had powers to enter the PSA Article 23.5. Objective I of the Constitution required all organs and agencies of the State to apply the objectives and principles in the Constitution in interpreting any other law or implementing any policy decisions. These objectives include the right to development (objective IX) and stimulation of industrial development by adoption of appropriate policies (objective XI(ii)). The terms of the PEPA are worded to support the honouring of obligations such as Article 23.5 as it encompassed policies aimed at stimulating industry and encouraging private initiative for the benefit of Uganda.

The applicants argued that Article 2 of the Constitution provides for the supremacy of the Constitution. The applicants argued that the Constitution does not make express provisions of granting tax exemptions or not. There is also no express provision that the general powers of the Constitution shall prevail over statute law where the two are inconsistent. The applicants argued that the vesting of executive power in the Constitution in the President gives him very wide powers. There is no specific provision preventing the President from granting a tax exemption in the Constitution. The applicants submitted that Article 11(2) of the Constitution also

confers wide powers on the cabinet. This is the source of the Minster's powers to enter into Article 23.5. Article 23.5 does not seek to amend the ITA.

In respect of issue 1.3, the applicants requested the Tribunal not to make any ruling on the application of international law to the present dispute. In short, the applicants abandoned the said issue.

As regards issue1.4, the applicants contended that the respondent was an agent of GOU. While its actions bind GOU, it is also bound by GOU. The Uganda Revenue Authority Act 1991 (URAA) established the respondent as a central body for the assessment and collection of specified revenue and to administer and enforce the laws relating to such revenue. Under the said Act, the Authority is an agency of the GOU. The applicants cited *Heritage Oil and Gas Limited v URA* Civil Appeal 14 of 2011 where the court said that URA is not autonomous of GOU. URA as a statutory agent is part and parcel of GOU. It cannot therefore be seen to disassociate itself from the PSA. Thus the PSAs are agreements entered into by the GOU but to which the respondent is also a party. The applicants argued that the effect of the decision in *Heritage* is that the GOU cannot simply ignore the EA2 PSA Article 23.5. The Minster signed on behalf of the GOU. The respondent as an agent of GOU clearly cannot ignore a legally binding obligation of the GOU, its principal.

The applicants argued the Tribunal should enforce Article 23.5 exercising the jurisdiction conferred on it by the TAT Act. The applicants contended that the Tribunal's powers are wide. They include the powers of it to "stand in the shoes" of the decision maker and exercise all the powers he or she had at the time the decision was made. The Tribunal can make a new decision in substitution of the original one.

Issues 1.5 and 1.6 dealt with the doctrines of estoppel and of legitimate expectation respectively. The applicants contended that estoppel refers to circumstances in which by the operation of law an individual or body is prevented from behaving in a particular manner. References to estoppel include reference to legitimate expectation. Legitimate expectation applies to prevent the GOU from ignoring its obligations under the EA2 PSA Article 23.5. Similarly, the principle of *pacta sunt servanda* may also operate to prevent unfairness.

The applicants also relied on “legitimate expectation”, a principle distinct from estoppel. The applicants argued that since estoppel cannot apply to the GOU, the references to estoppel in the objection refer to GOU being estopped by other principles of fairness particularly legitimate expectation and *pacta sunt servanda*. The applicants contended that legitimate expectation can and does apply to prevent the GOU from ignoring its obligations under the EA2 PSA Article 23.5. Similarly, the principle of *pacta sunt servanda* applies.

The applicants cited the case of *Council of Civil Services Union v Minister for Civil Service* [1985] AC 374, where Lord Fraser said:

> “A legitimate expectation may arise either from an express promise given on behalf of a public authority or from the existence of a regular practice which the claimant can reasonably expect to continue...”

The applicants argued that its legitimate expectation is clearly within the terms as defined. The applicants submitted that the principle of legitimate expectation applies so as to estop an agency of the state going back on its representation. The applicant submitted that the GOU through the Minister entered into the PSA. The GOU has bound the revenue authority, the URA, as its agent, to honour its agreement. The Tribunal should ensure that the respondent does this.

The applicants relied on the evidence of their witnesses to rely on the application of the principle of legitimate expectation. AW1 Mr. Martin Graham testified that: “Tax reliefs or exemptions are part of ensuring that the entering into a PSA is economically viable. .... It is common for governments to provide certain incentives to encourage oil production. ...” They concluded that Article 23.5 gave them the “confidence to proceed on the basis that there would be no tax.” AW3, Mr. Richard Inch, stated that in relation to EA2, there was “no concern as to the taxation position because of the exemption for capital gains tax in respect of a farmdown in Article 23.5...”

The applicants also argued that the use of “estopped” by them is not the use of the technical term “estoppel”. They argued that the term “estopped” has a wider meaning. *Black’s Law Dictionary* defines “estopped” to mean “to prevent, stop or bar something from happening.” The use of legitimate expectation is covered by estopped. The applicants cited the case of *R v IRC,*

ex p MFK Underwriting Agencies Ltd. [1989] STC 873 where Bingham LJ linked the concept of legitimate expectation and estoppel in saying:

> "If in private law a body would be ... estopped from so acting a public authority should generally be in no better position. The doctrine of legitimate expectation is rooted in fairness."

Therefore the respondent as an agent of the GOU, which had agreed that there would be no tax to be charged, should be estopped from acting unfairly by charging tax.

The applicants argued that while estoppel is a private law remedy, legitimate expectation is a public law remedy. While the doctrine of estoppel may not apply to the GOU or the respondent, this does not mean that public bodies have a "free rein" to behave in a manner which is unfair and prejudicial to the rights of the individual. The applicants contended that the doctrine of legitimate expectation was also confirmed in the decision of the House of Lords in *East Sussex County Council; ex parte Reprotech (Pebsham) Ltd.* [2002] 4 All ER 58, where Lord Hoffman stated at paragraph 35:

> "... It seems to me that in this area, public law has already absorbed whatever is useful from the moral values which underlie the private law concept of estoppel and the time has come for it to stand upon its own feet."

The applicants submitted that legitimate expectation can apply to restrict the activities of an agency of a state, including the discharge of its functions under a statute. The applicants cited the case of *Preston v IRC* [1985] AC 835 where the Court saw no reason why it should not review:

> "..... a decision taken by the commissioners [of Inland Revenue] if that decision is unfair to the tax payer because the conduct of the commissioners is equivalent to a breach of contract..."

In *R v IRC, ex p MFK Underwriting Agencies Ltd* [1989] STC 873 the court noted:

> "...If a public authority so conducts itself as to create a legitimate expectation that a certain course will be followed it would often be unfair if the authority were permitted to follow a different course to the detriment of the one who entertained the expectation..."

The applicants therefore argued that where the revenue authority so conducted itself to create a legitimate expectation that the state will not charge tax in particular circumstances, tax shall not be charged. If the taxpayer has a legitimate expectation the state must keep its word. Hence if a party were to show that the representations were made to it by a state or an agency of the state and it has legitimate expectation then the state would be bound by those representations.

The applicants argued that the development of legitimate expectation can be seen in a decision of the High Court of Kenya in *Republic and Others v Attorney General* [2006] 2 EA 265 where the court stated that:

> "The principle which justifies the importance of procedural protection has come to be known as legitimate expectation. Such an expectation arises where a person responsible for taking a decision has induced in someone who may be affected by the decision a reasonable expectation that he will receive or retain a benefit...."

The applicants argued that the doctrine of legitimate expectation has also been applied in a number of other cases in Kenya. These include: *Republic v Minister for Local Government and another ex parte Paul Mugeithi Joel [2008] KLR Miscellaneous Civil Application 480 of 2008*, *Republic and others v Attorney General and another [2006] 2 EA 265*. The applicants, therefore, argued the Tribunal should accept that the doctrine of legitimate expectation forms part of the law of Uganda. They contended that the principle was applied in the High Court of Uganda in the case of *Kato v Njuki* [2009] UGHC 23.

The applicants also relied on the doctrine of *pacta sunt servanda*, which requires those entering into contracts to honour their obligations. The applicant contended that respondent as agent of the GOU is not entitled to collect tax from the applicants in contravention of Article 23.5 of the EA2 PSA.

On issue 2, the applicants contended that they sold 66.67% of the interests they held in the blocks. Of the 66.67% interest, 50% interest was what they acquired from Heritage, 16.67% was their original interest. The applicants contended that they purchased the Heritage interests exercising their pre-emption rights for the purpose of selling them and to facilitate the development of the areas. The applicants objected to the respondent's argument that the interests they sold were indivisible. The applicants argued that there were no accounting principles which discourage transactions carried out in the way the applicants sold their interests to CNOOC and Total i.e. by selling all of the Heritage interests first and a small proportion of the original interests.

The applicants argued that the respondent's alternative proposal of 'first in first out' (FIFO) model was aimed at yielding the greatest amount of tax which overrides the clear provisions of

the SPAs. The applicants cited the case of *Stanton v Drayton* [1983] 1 AC 501 where the court noted that the consideration in any particular case must be determined by reference to the contract which the parties concerned concluded.

In respect of computation of capital gains, the applicants contended that this is determined by the rules set out in Part IXA of the ITA. The applicants submitted that S. 89B provided for inconsistencies. Where there is an inconsistency between Part IXA and other parts of the ITA, the former prevails. The applicants argued that S. 22 of the ITA is not applicable by virtue of S. 89B (2). S. 89C – 89F sets out the rules dealing with allowable deductions against the income, which is relevant when commercial production starts.

The applicants objected to the application of S. 22(c) of the ITA which provides for "recoverable costs". They argued that this prevents the applicants being allowed the costs of expenditure as their cost base in the computation of a chargeable gain. The applicant argued that the respondent's claim that the contractors obtained recovery of costs under an indemnity or agreement is unfounded. There is no such indemnity or agreement, it is merely to apportion turnover in accordance with what each partner has spend.

The applicants argued that S. 22 does not apply to a first disposal. They contended that S. 22 is not incorporated into Part IXA, in particular in S. 89(c) or Part VI. S. 22 is within Part IV, 'Chargeable Income'. S. 22 is only concerned with income, not gains. The applicants contended that there is nothing that stops allowable expenditure forming part of the cost base on the original interest. The applicants submitted that Sections 89C, 89G(c), 89F, the 8th Schedule and S. 52 contain the provisions of the taxation of disposals of interests in a petroleum agreement. S. 22 is not applicable as it is inconsistent with Part IXA. The applicants see no tenable reason why incidental expenditure incurred in improving or altering the assets under the PSA should not be deducted under S. 52(6).

In reference to the double dip point raised in the objection decision by the respondent, the applicants argued it can only have effect in two circumstances. The first in respect of the possible future use of the carried forward potential deductions against cost oil. The second in respect of the potential use by a transferee of the deduction against cost oil.

The applicants submitted that S. 89G, which is headed “Transfer of interests in a Petroleum Agreement”, sets out the rules for dealing with the allowable deductions upon the transfer of an interest. The applicants contended that there are separate charging codes for the original interests (First disposals) and subsequent disposals.

The applicants submitted that S. 89G(c) is used for determining the cost base where there is an original transfer of interest. The cost base will be determined in accordance with Part VI of the Act. Part VI comprises Section 49 – 54 of the ITA. In Part VI, the principal rules for the computation of the tax base are set out in S. 52 of the ITA. The applicants submitted where there is a first disposal the rules fix the cost base by taking into consideration what the taxpayer expended on the interest. The applicants contended that the transfer of the original interests and the EA2 interests were subject to the regime in S. 89G(c) of the ITA. The applicants contended that the cost base of the original EA1 and EA3A interests and the EA2 interests included incidental expenditure incurred to purchase, produce, construct or improve these interests. The incidental expenses that were communicated by the applicants to the respondent were 47 million

Part IXA contains separate charging rules for subsequent transfers of interests in petroleum agreements in S. 89G(d). Where there is a subsequent disposal the rules allow a deemed cost base, which is the gains made by the person the taxpayer bought from, then it is reduced by excess costs. The disposal of the Heritage interests to CNOOC and Total was a “subsequent disposal.” The transfer of Heritage interests was subject to the regime in S. 89G(d) for subsequent disposals. The applicants are the “transferee contractors” and Heritage is the “Transferor Contractor”. In determining the applicant’s cost base for the gain in the disposal to Total and CNOOC it is Heritage’s gain which was computed at US$ 1,450,000,000 as held in *Heritage Oil and Gas Limited v URA* Applications 26 and 28 of 2010. The transferor contractor’s gain is deemed to be the transferee contractor’s cost base.

The applicants submitted that deductions in income computation is dealt with by S. 89C of the ITA. The applicants further submitted that S. 89C allows expenditure on petroleum operations as a deduction in respect of income only against cost oil, if there is none, the expenditure is carried

forward. Cost oil is defined in S. 89A. S. 89C(1) provides the rules for deductions allowable against income by allowing them only against cost oil. Thus the income deductions are given against cost oil only from the year in which commercial production commences, which has not started. As the applicants have no cost oil, the applicants have not deducted anything. Therefore in respect of the original interests and EA2 interests there was no deduction allowed.

The applicants contended that excess costs are not defined. However reference to the term may be obtained from S. 89C(2) of the ITA. Excess costs under S. 89G(d)(i) are the excess of the total deductions given in relation to petroleum operations less the cost oil for the year of income. The applicants contended that excess costs cannot arise as commercial production has not started. There are no excess costs to be taken into account and none to deduct from the cost base under S. 89G(d)(i).

The third issue was in respect to the applicants' entitlement to reinvestment relief. S. 54 of the ITA provides for involuntary disposals and the entitlement to reinvestment relief. The applicants had to show that the disposal was involuntary and the proceeds are to be reinvested in assets of a like kind within the specified period.

The applicants farmed down an aggregate of 66.67% of their interests. The applicants argued that they intended to dispose of 50% of their interests. They needed GOU's approval for the sale. The GOU wanted three equal partners to invest in the Lake Albert Basin. Since the applicants needed that GOU's consent to proceed with the sale, they had no choice but to dispose 66.67% of their interests. The disposal of the extra 16.67% of the interests was not made voluntarily.

The applicants cited the authorities of *Building Society v Commissioners of Inland Revenue* 65 TC 265 and *URA V Bank of Baroda* HCT-00-CC-CA-05-2005, which broadly interpreted and discussed "involuntary" disposal. The applicants referred to the evidence of AW2, Mr. Paul McDade, who submitted at length the applicants' desire to dispose of 50% of their interest. The applicants submitted that investment in assets/rights which are dealt with under the PSAs constitutes an investment in assets of a like kind. The applicants also submitted that they had incurred US$ 164,721 as reinvestment relief for the period of March 2012 to February 2013.

However, the applicants also contended that, since the hearing before the Tribunal occurred before the one year period expired evidence of their expenditure on assets of a like kind would not be given.

Having discussed the powers and jurisdiction of the Tribunal, the applicants prayed that the assessments and the objection decision of the respondent be set aside. They also prayed that the Tribunal finds that Article 23.5 of the PSA is valid under the laws of Uganda and therefore they are entitled to exemption from payment of capital gains tax. They also prayed that all the costs incurred by the applicants, including exploration costs be allowable under S. 52 of the ITA. They prayed that the Tribunal finds that there is no restriction to be made for excess costs for purposes of S. 89(G)(d) of the ITA. They also prayed that the Tribunal finds that the applicants are entitled to reinvestment relief to a tune of 16.67% interests in EAs 1, 2 and 3A which is the sum of US$ 164,721 so expended for purposes of reinvestment. The applicants in short prayed that the Tribunal makes new assessments of nil liability on each of the applicants. In the event of such, they prayed that the 30% deposit by them on filing the application be refunded to them.

In its reply, the respondent submitted that this matter is an attempt by the applicants to avoid paying income tax on an enormous gain resulting from the largest transaction in the history of Uganda, the sale of interests worth US$ 2.9 billion to Total and CNOOC. It argued that this is through the inappropriate manipulation of figures and distortion of the Uganda tax law by the applicants.

On Issue 1.1, the respondent submitted that Article 23.5 of the EA2 PSA deals with what is referred to as transfer taxes which are distinct from taxes on income or gains resulting from transfers and is therefore irrelevant to the taxability of capital gains. The respondent argued that income or gains tax applies only to the extent that income of gain is actually realised whereas a transfer tax is charged on a transfer whether a gain or loss is realised and irrespective of whether consideration is paid for the transfer. The respondent argued that the language of Article 23.5 is concerned only with taxes that have “assignment or transfer” as the base of the tax. The respondent gave examples of transfer tax exemptions. It also referred to provisions of other countries - Angola and Equatorial Guinea, similar to Article 23.5 of the EA2 PSA.

The respondent submitted that provisions purporting to provide exemptions from tax must be narrowly construed. The respondent cited the authorities of *Babibasssa v Commissioner General Uganda Revenue Authority* [2013] UGCOMMC 21, *Helvering v Northwest Steel Rolling Mills, Inc.* Supreme Court (United States), 311 U.S. 46, *Commissioner of Internal Revenue v Jacobson,* Supreme Court (United States), 336, U.S. 28, *Mayo Foundation for Medical Education & Research et. al. v United States*, Supreme Court (United States), 131 S. Ct. 704, *Edward Maughan (Surveyor of Taxes) v The General Trustees of the Free Church of Scotland*, Court of Session (Scotland), (1893) 20R. 759.

The respondent referred to the testimony of Mr. Ernest Rubondo, and Mr. Moses Kajubi, who supported the position that Article 23.5 of the EA2 PSA did not confer a tax exemption. The respondent argued that there is no evidence on record that contradicted this testimony.

The respondent also referred to the 2010 SPA which was signed by the applicants and Heritage. The said SPA defined transfer tax to mean "stamp duty payable under the laws of the Republic of Uganda". Non- transfer Taxes were defined to mean "any taxes other than Transfer Taxes." Under Clause 7.1 of the Agreement, all transfer taxes were to be borne by the buyer. Under Clause 7.2 any Non-Transfer tax including any capital gains tax shall be borne by the seller. The SPAs executed between the applicants, CNOOC and Total maintained the clear distinction between transfer taxes which was to be paid by the buyer and capital gains tax by the seller.

As regards transfer tax, the respondent cited J. Rogers-Glabush, *IBFD International Tax Glossary* 6th Rev. ed., IBFD 2009 which perceives transfer tax as a "general term to refer to a tax levied on the transfer of goods and rights e.g. purchase and/or sale of securities and immovable property..." It also cited *Black's Law Dictionary* 9th ed. 2009, 1597 which defines transfer tax as: "a tax imposed on the transfer of property, exp. by will, inheritance, or gift", while *West's Encyclopaedia of American Law* 2nd ed. 2008, 79 defines it as "a charge imposed by the government upon the passing of title to real property or a valuable interest in such property." The respondent contended that under the OECD, taxes on income, profits and capital gains are separated from taxes imposed on other bases including taxes on financial and capital transactions. The respondent contended that transfer tax is a type of "indirect tax" while income or gains tax constitute "direct taxes".

The respondent submitted that in the US, there have been attempts to distinguish between transfer taxes such as stamp duty and property transfer taxes, and taxes imposed on gains resulting from a transfer. The respondent cited that authorities of *S&M Enterprises v the United States, Court of Appeals for the Federal Circuit (United States),* 199 F.3d 1317 where the court stated that if the tax is based solely on a gain, and not on the size of the transfer, it is not a transfer tax. The respondent also cited the case of 995 *Fifth Avenue Associates v New York States Department of Taxation and Finance* Court of Appeals for the Second Circuit (United States), 963 F, 2d 503 where the court emphasised that if the transaction yields no gain, there is no tax due. The nature of gains tax is different from stamp taxes and documentary transfer taxes.

The respondent also cited cases that have been addressed in UK courts. In *Carreras Group Limited v Stamp Commissioner*, Privy Council of the United Kingdom [2004] S.T.C 1377 the court pointed out that transfer tax is an ad valorem on the consideration for the property transferred, whereas the capital gains tax is a tax on capital gains.

The respondent objected to the applicants' reference of the words "any tax" in Article 23.5 to have a wide coverage. The applicants had leaped to the conclusion that any tax clearly covers income tax on a capital gain accruing on an assignment or transfer. The respondent argued that this was a result of confusion in the applicants between the nature and the base of the charge.

The respondent argued that Article 23.5 would be manifestly unlawful under Uganda law if the applicants' interpretation of it as an exemption is accepted. The respondent submitted that under the Constitution of Uganda a tax may be imposed through a law passed by Parliament. Likewise a tax can only be varied if a law confers such power on the person or authority purporting to grant the waiver. The respondent cited Articles 79, 99 and 152 of the Constitution of Uganda. The respondent contended that the said provisions make it clear that the executive does not have the capacity to waive the law. The respondent cited that authorities of the *Heritage* case, K.M. *Enterprises and others v Uganda Revenue Authority* HCCS No. 599 of 2001 and *Kampala Nissan Uganda Limited v Uganda Revenue Authority* Civil Appeal No. 7 of 2009 to support its arguments.

The respondent submitted that discretionary tax exemptions are no longer allowed under the ITA after July 1997. Exemptions are now statutorily provided. The ITA amended the 1974 Income Tax Decree and the 1991 Investment Code Act. The respondent contended that through the adoption of the 1995 Constitution and the ITA, Uganda eliminated discretionary tax exemptions which were replaced with statutorily provided ones.

The respondent contended that the applicants' argument that the 1993 PSA aimed at bringing companies into high risk investment involving enormous sums of money is not correct. When the 1993 PSA is compared to the 2001 PSA one can conclude that income tax exemptions are unlawful. It shows that Article 23.5 only excluded taxes and fees imposed on the transfer and not taxes on income resulting from a transfer. The respondent further contended that at the time Article 10 of the 1993 PSA was prepared, discretionary tax exemptions were lawful. After 1993 the GOU took a series of policy reforms which eliminated discretionary exemptions. The respondent contended that Article 11 of the EA2 PSA provided for all central taxes to be paid in accordance with the law.

The respondent submitted that the applicants' argument that the Minister could grant an exemption under S.3 of PEPA is defective. The respondent averred that the term "connected with" must be interpreted in the context of the phrase "incidental to or connected with the foregoing." The respondent cited the authority of *Scottish Widow Plc v RCC* (supra) already cited by the applicants. It contended that thus "connected with" must be read as part of the phrase "incidental to or connected with."

The respondent also contended that the applicants' argument ignores that the ITA is a specific statute governing income tax in Uganda and was adopted after the PEPA to consolidate and amend the law relating to income tax. It also contended that the ITA does not need to repeal or amend S. 3(e) of the PEPA. The respondent argued that the minister cannot have unbounded powers under S. 3 of the PEPA as it may have startling results. The respondent referred to an admission by the applicant's own witness Mr. Inch, the Head of Tax that "the constitution is clear that an increase in tax is by an Act of Parliament". Hence S. 3 of the PEPA does not confer power under Article 152 of the Constitution on a minister to waive or vary a tax.

The respondent submitted that the applicants' contention that the Minister was authorised to grant an income tax exemption on the basis of Article 274 of the Constitution was unfounded. Article 274 does not provide for the preservation of existing powers. It only provides that existing powers must be modified to bring them in conformity with the Constitution. The respondent cited the authorities of *Hon. Sam Kuteesa and others v Attorney General* Constitutional Petition No. 46 of 2011 and *Attorney General v Osotraco Ltd* Civil Appeal 32 of 2002, to support its argument. The respondent submitted that the applicants do not explain the basis of their assertion that "pre-written constitution powers include a power to grant exemption from tax."

The respondent asserted that Uganda law embraces the law that there can be no estoppel against a statute. If a contractual agreement is ultra vires the agreement is null, void and unenforceable. The respondent cited the authorities of *Major General David Tinyefuza v Attorney General* Constitutional Petition No. 1 of 1996, *KM Enterprises Ltd and others v Uganda Revenue Authority* [2008] UGCommC 21, *Heritage Oil & Gas Limited v URA* Civil Appeal 14 of 2011, *Pride Exporters Ltd v URA* HCCS 503 of 2006, *URA v Golden Leaves & Resorts Ltd and Apollo Hotel Corporation Ltd.* MA 0783/ 2007, *URA v Bwama Exporters Limited* Civil Appeal 6 of 2003, *Kampala Nissan Uganda Ltd. v URA* Civil Appeal 7 of 2009.

The respondent submitted that the applicants' arguments that the doctrine of estoppel should be restricted by that of legitimate expectation should not be taken seriously. The notion that the terms of a statute may be waived by an agreement that gives rise to a legitimate expectation is contrary to the rule of estoppel against a statute. The respondent argued that the applicants' citation of the case of *Kato v Njoki* (supra) was frivolous as the application of the doctrine of legitimate expectation was remote.

The respondent submitted that the doctrine of legitimate expectation cannot apply to ultra vires acts. The respondent cited the case of *Re: Watson's Application for Leave to Appeal for Judicial Review* (also known as *Dollingstown Football Club v The Irish Football Association*) [2011] NIQB 66 where the court stated that: "It is trite law that an expectation grounded upon an ultra vires representation cannot be legitimate." In *Rowland v Environment Agency* [2005] Ch.1 the Court of Appeal stated that "English domestic law does not allow the individual to retain the benefit

which is the subject of the legitimate expectation, however strong, if creating or maintaining that benefit is beyond the power of that public body." The respondent also cited the authority of *Al Fayed and others v Advocate General for Scotland* 2004 S.T.C 1703 where the court affirmed that an *ultra vires* agreement cannot give rise to a legitimate expectation. Other cases cited by the respondent included *Wilkinson v Inland Revenue* [2005] 1 W.l.R. 1718, *R v North and East Devon Health Authority ex parte Coughlan* [2001] Q.B, 213, *R v Inland Revenue Commissioners, ex parte MFK Underwriting Agents Ltd* [1989] S.T.C 873, *R (on the application of Corkteck Ltd.) v Revenue and Customs Commissioners* [2009] S.T.C. 681, *R v East Sussex CC ex parte Reptrotech* [2002] 4 All E.R.58, *Republic and others v Attorney General* [2006] 2 EA 265, *Republic v Minister for Local Government & Another, ex parte Paul Mugethi Joel* [2008] eKLR 6, *Republic v National Environment Management Authority ex-parte Sound Equipment Ltd* [2010] eKLR 8, *Republic v The Disciplinary Committee & another Ex-parte Prof. Paul Musii Wambua* [2013] eKLr 5. The respondent argued that most of the above cases were cited by the applicants who distorted their interpretations to suit their case.

The respondent argued that the applicants' invocation of the international law principle of *pacta sunt servanda* (sanctity of contract) provides no support that the principle overrides the *ultra vires* principle. The respondent contends that the applicants abandoned their arguments based on international law.

On issue 2, the respondent submitted that TUL purchased a 50% undivided interest in the licences and agreements in relation to EA1 and EA3A from Heritage. It therefore obtained 100% ownership interests in EA1 and EA 3A. TUL and TUOP owned 50% undivided interests in EA2. After a sale to CNOOC and Total the holdings were as follows: In EA1 TUL, Total and CNOOC had 33.33% interests each; in EA2 TUOP, Total and CNOOC had 33.33% interests each and In EA3A TUL, Total and CNOOC had 33.33% interests each.

After receiving the SPAs, the respondent raised assessments in October 2010. The applicants objected to the assessments on various grounds. In particular that they had incurred more incidental costs. Following a review of the applicants' objections, the respondent issued another objection decision and increased the incidental costs and disallowed other items. The respondent received further information from the applicants and increased the allowed incidental

costs to US$ 61,903,387 which resulted in a tax liability of US$ 467,271,974. The respondent communicated the current assessments to the applicants on 2nd November 2012. The applicants paid the 30% deposit of the tax before filing the application leaving a balance of US$ 325,447,536/=.

The respondent determined that the applicants had a taxable gain of US$ 1,113,332,200 from the sale of the EA2 interests, a taxable gain of US$ 449,831,550 for their sale of the 50% undivided interests in EA1 and EA3A (the "original interests") and a loss of US$ 25,590,503 from the sale of a portion of their 50% undivided interests in EA1 and EA3A (the "Heritage Interests) for a total taxable gain of US$ 1, 557,573,247.

In calculating the applicants' gains, the respondent disallowed pre-existing petroleum operations costs of US$ 320,545,819 from being included in the applicants' cost base because such expenses were deductible against cost oil pursuant to S. 89C of the ITA. The respondent also disallowed a deduction for interest expense of US$ 113, 429,096 under the thin capitalisation rules under S. 89 of the ITA, which it contended was not in dispute. The respondent also disallowed the applicants from using a loss of US$ 20,987,930 on EA3A to reduce their gain on the sale of their EA3A interests because such loss related to a separate contract area, EA3, and was only available to offset cost oil from the area under S. 89C of the ITA, which is not in dispute. The respondent also disallowed the applicants' claim that they are entitled to US$ 164,721,000 as reinvestment relief under S. 54(1) (c) of the ITA.

The respondent submitted that where a contractor as an original owner of interests disposes of them, S. 89G(c) is applicable. It provides that the cost base for calculating any capital gain or loss is determined under Part VI of the ITA. The general rules for the calculation of capital gains under Part VI are contained in S. 52 of the ITA. More specific rules for the treatment of expenditures incurred in relation to petroleum operations are set forth in S. 89C of the ITA. S. 89C (1) provides that the amounts deductible in relation to petroleum operations are allowed only as a deduction against cost oil. The respondent submitted that under S. 89C of the ITA a contractor's petroleum operations expenditures are allowed deductions, which when they exceed the cost oil for a given year, the contractor carries them forward into subsequent years.

The respondent submitted that the specification that deductions may be taken “only against cost oil” precludes them from being included in an assets’ cost base pursuant to S. 52(6) of the ITA.

The respondent agreed with the applicants that when the contractor disposes of an interest in a petroleum agreement previously acquired, S 89G of the ITA applies. The respondent submitted that regardless of whether the cost base is calculated under S. 89G(c) or S. 89G (d) the applicants are not entitled to include their exploration, development or production costs in their cost base in calculating the gain they realised on the disposal of their interest because the costs are only recoverable against cost oil. In contrast, under S. 89G (d) of the ITA, the applicants are not entitled to include incidental expenditures in their cost base.

The respondent contended that the applicants received US$ 150,000,000 as excess costs, from Heritage when they purchased the latter’s interest. The respondent argued that although CNOOC and Total may recover excess costs from cost oil, the applicants’ argument that their cost base should include the US$ 150,000,000 ignores the application of S. 89G (d) of the ITA. The respondent argued that under S. 89G (d) (i) the applicant’s cost base for purposes of calculating gain on the sale of Heritage’s interest cannot include the US$ 150,000,000. In calculating the applicants’ gain from the sale, the respondent reduced the applicants’ cost base by US$ 150,000,00 which were exploration costs that were deemed as excess costs under S. 89C(2) of the ITA and must be subtracted pursuant to S. 89G(d)(i) of the ITA. The respondent asked the Tribunal to allow the reduction of US$ 150,000,000 as excess costs that would be deductible by CNOOC and Total.

The respondent contended that the exploration costs of US$ 320,545,819 claimed to have been incurred by the applicants on EA1, EA2 and EA3A were not substantiated nor audited by the respondent. The applicants claim to have transferred these costs to Total and CNOOC, at the same time they seek to recover them by including them in their cost base. The respondent submitted that the US$ 320,545,819 were part of the bundle of rights and interests in the PSAs that was sold for the consideration of US$ 2,933,330,400. The respondent contended that they should not include them in the cost base because they are recoverable against cost oil. The respondent contended that Sections 89C (1) and 89C (2) do not disallow deductions for

petroleum operation expenditures in the years where there is no sufficient cost oil; they merely suspend the deductions until future years.

The respondent contended that the applicants' argument that prior to the commencement of commercial production, no deductions are allowed as there is no excess costs is a misreading of Part IXA of the ITA. The respondent argued that exploration, operation and development operations are by their very nature undertaken prior to the commencement of commercial production. S. 89C(1) of the ITA specifically permits deductions for exploration and development operations costs and limits these deductions to cost oil in the year they were incurred. The respondent concluded that the portion of excess costs that has been passed along to subsequent purchasers under S. 89G (a) of the ITA cannot be included in the applicants' cost base for purposes of calculating their gain.

The respondent argued that an alleged loss claimed by the applicants is fictitious. The respondent claims that the applicants transformed what was a profitable transaction into a loss for tax purposes by applying the 'last in, first out' accounting method. The respondent submitted that what the applicants sold were undivided interests. The respondent, inter alia, cited *Black's Law Dictionary* which defines "undivided interest" as "an interest held in the same title by two or more persons, whether their rights are equal or unequal as to value or quantity". The respondent submitted that given the nature of such an interest, a taxpayer cannot choose the cost base that it wishes to allocate to a subsequent sale. The respondent cited the case of *John K. McNulty v Commissioner of Internal Revenue*, Tax Court (United States), T.C. Memo, 1988-274 where the court held that "A taxpayer who owns two undivided one- half interests in property received at different times, and disposes of an undivided one-half interest, is deemed to have disposed of 50 percent of each of the halves he owned." The respondent also cited the ruling of the Internal Revenue Service of the United States, 1967, the US case of *Porter v United States*, Court of Appeals for the Sixth Circuit (United States), 738 F.2d 731 and the UK case of *Tod (Inspector of Taxes) v Mudd* [1987] S.T.C. 141. The respondent averred that "it is not possible to treat portions of an undivided interest as separate and distinct interests."

The respondent submitted that the LIFO accounting method is not only inappropriate but is also not acceptable under International Financial Reporting Standards. S. 40(1) of the ITA requires

that a taxpayer's methods of accounting shall conform to generally accepted standards. International Accounting Standard 2 specifies that "the Standard does not permit the use of the 'last in first out' (LIFO) formula to measure the cost of inventories." The respondent also cited the case of *Minister of National Revenue v Anaconda American Brass Ltd.* [1956] A.C. 85 where the application of the LIFO was vitiated in the case.

The respondent contended that the applicants' argument that "what the parties have agreed to sell must also determine what has been bought and sold for tax purposes" does not hold. Under S. 91 of the ITA, the Commissioner has powers to re-characterise a transaction that was entered into as part of a tax avoidance scheme, or does not have substantial economic effect or does not reflect the substance. The applicants contended that the cost base should be recalculated using either the FIFO method or the averaging method.

As regards incidental expenses, the respondent admitted that it accepted the applicants' incidental expenditures of US$ 61,903,387 incurred with respect to Heritage interests. However, the respondent asked the Tribunal to exclude those costs. The respondent contended that S. 89G (d) governs the calculation of the cost base for a subsequent disposal of an interest in a petroleum agreement. Nothing in the Section allows a transferor to increase its cost base in the subsequent disposal by the amount of incidental expenditures.

On issue 3, the respondent submitted that the applicants are not entitled to reinvestment relief. The respondent argued that under S. 54(1) (c) a taxpayer must meet four conditions; (i) the disposal of the asset must be involuntary, (ii) the proceeds from the reinvestment must be reinvested, (iii) the reinvestment must be in an asset of a like kind, and (iv) the reinvestment in an asset of a like kind must be made within one year of the disposal. The respondent contended that the applicants have not met any of the four conditions.

The respondent alleged that the applicants have failed to discharge the burden of proving that the disposal of 16.67% interest was involuntary. Most of the evidence was based on the testimony of Mr. Paul McDade, which was based on his belief. In cross-examination of Mr. McDade, he admitted that there were no correspondences from the GOU. According to Mr. Martin Graham, GOU communicated through meetings, but these were un-minuted.

Furthermore, Mr. Martin wrote a letter to the Minister of Energy and Mineral Development where he indicated that Tullow would farmdown at least 50% of their interest. The applicants requested the GOU to approve the creation of a basin-wide partnership where the applicants, CNOOC and Total were holding 33.33% interests each. According to Mr. Rubondo, it was Tullow that decided the award of 33.33% interests to each party. The respondent argued that the case of *Uganda Revenue Authority v Bank of Baroda* [2007] UGCommC 8 where the court held that the disposal by the bank of its shares was involuntary can be distinguished from the present case. In the said case there was an agreement unlike the current one before the Tribunal.

The respondent submitted that the applicants are not entitled to the reinvestment relief because they did not reinvest the proceeds in an asset of a like kind. The respondent contended that the applicants' claim that they used the proceeds from the sale of the interests in the PSA to fund pre-existing costs is incorrect. The respondent argued that S. 54(3) of the ITA required that the reinvestment be made in a "replacement asset". The commonly accepted definition of replacement is "something that replaces". The respondent claimed that from the evidence adduced the applicants did not use the proceeds from the sale of their interests to acquire new interests. According to the evidence of Mr. Graham, the proceeds from the sale were used to build infrastructure and others. The respondent argued that such expenditure was used to fund obligations under the PSAs that existed prior to the sale. It argued that such use of sale proceeds to fund pre-existing obligations is clearly not an acquisition of a replacement asset as required by S. 54(3) of the ITA. The respondent cited the US General Counsel Memorandum No. 39572 where it is stated that the reinvestment provision was intended to be a relief provision for a taxpayer to restore its economic position to the prior position. The respondent contended that the applicants by using the sales proceeds to fund their development obligations under the PSAs they are discharging pre-existing debt. This is not an asset of like kind acquired and there is no reinvestment at all. The respondent also argued that the applicant reinvestment was not made within one year of disposal.

The respondent submitted that in the event the Tribunal were to find that the applicants were eligible for reinvestment relief, the relief should be limited to a fraction of the amount to which they claim they are entitled. The involuntary disposal of interests represent 25% of the total

interests that the applicants sold (16.67%/66.67% = 25%) which is US$ 41.3 million of the US$ 165 million the applicants claimed have expended on the PSAs.

The respondent prayed that the Tribunal dismisses the application and orders that the applicants pay the outstanding tax liability plus interest. They also prayed that the Tribunal finds that Article 23.5 of the EA2 PSA does not purport to provide an exemption to the imposition of tax pursuant to the ITA. If the Tribunal were to find that Article 23.5 of the EA2 PSA purported to provide an income tax exemption it would be null and void *ab initio* under the laws of Uganda. The Tribunal should find that the respondent is not estopped from imposing tax from the disposal of the interests in the EA2. The respondent also prayed that the Tribunal finds that the concept of legitimate expectation provides no basis for not imposing tax as imposed by the ITA. The respondent also wanted the Tribunal to find that the applicants disposed 66.67% of its 100% interest and not the 50% acquired from Heritage. It was also prayed that the Tribunal applies the average cost accounting method or in the alternative the FIFO' method as the basis of calculating the gain obtained by the applicants. The respondent also wanted the Tribunal not to include the exploration, development or production costs including the excess costs acquired from Heritage in their cost base. The respondent also wanted the Tribunal to find that the applicants are not eligible for reinvestment relief. In the event the Tribunal finds otherwise, it should exercise its power under S. 19 of the TAT Act and remit the matter to the respondent for reconsideration. The respondent also prayed for costs of the application.

In its reply to the respondent's submissions, the applicants complained about the approaches used by the former. They argued the respondent has raised new issues and arguments that were not raised before. They complained about the language use by the respondent.. The applicants argued that the respondent's use of authorities from other jurisdictions does not take into consideration the weight such decisions may have and their relevance to the Tribunal. The applicants argued that some of the said authorities should be considered as evidence and not law. The respondent should not have relied on evidence improperly submitted to the court to which the applicants were not given an opportunity to challenge.

In respect of issue 1, the applicants replied that the respondent's application of the principles of statutory interpretation in the analysis of Article 23.5 was flawed and simplistic. They argued that

Article 23.5 of the PSA is a contractual provision and not a provision of a statute. What should be applied are the rules of interpretation of contracts and not statutory interpretation. The applicants argued that Article 23.5 of the PSA is not limited to transfer tax. The applicants argued further that it has never been any part of their case that income tax under Part IXA is a 'transfer tax'. They do not dispute that income tax on gains imposed by the ITA is not a transfer tax. The applicants argued that Article 23.5 does not restrict itself to a transfer tax. To them, the issue before the Tribunal is whether or not the income tax charge or gains under the ITA is "any tax, fee or other impost or fee". The applicants also argued that the language used in the ITA when considered in conjunction with the language used in Article 23.5, it is clear that an exemption was granted under the Article.

The applicants submitted that the evidence of Mr. Rubondo and Mr. Kajubi in interpreting Article 23.5 of the EA2 PSA is inadmissible. Neither of them was a signatory to the PSA, or involved in negotiating the terms of Article 23.5 of the PSA. What the Tribunal should take into consideration is what a reasonable man would have considered as the intent in light of all background knowledge. Mr. Kajubi's experience as Commissioner means that he is not likely to see the provision in the same way as the objective reasonable man. The applicants argued that the evidence of Mr. Richard Inch should be relied on. He testified that the intention of GOU was to bring on board partners who would share the risk of oil exploration.

The applicants also submitted that the respondent's attempt to point to the provisions in the SPAs to support its interpretations was wanting. The SPAs were between different parties and were negotiated at different times approximately ten years apart. At the time the EA2 PSA was signed it was considered unlikely that any commercial oil or gas would be found. The SPAs are not between the GOU and the applicants. There are between the applicants and other commercial parties.

The applicants argued that the Minister of Finance could enter into agreement containing Article 23.5on behalf of the GOU. There is a difference when an exemption is granted by the Government as opposed to statutory body acting outside its powers. The applicants submitted that as a matter of constitutional law, the GOU was empowered to enter into Article 23.5 and the Minister acting for and on behalf of the GOU, had authority to sign the PSA.

The applicants argued that Article 152(2) of the Constitution does not say that tax can only be waived or varied. Article 152(2) merely provides that where a taxing law passed in accordance with Article 152(1) grants a person authority to waive or vary tax there must be periodic reports to Parliament by the said person. The ITA which is the taxing authority, the applicants submitted, confer general power[s] on any person or authority to waive or vary a tax imposed by that law. The applicants also argued that Article 23.5 of the EA2 PSA is not a “waiver or variation”. It is an exemption from tax, which tax is therefore never chargeable. It is not a waiver or variation granted “pursuant to a law enacted under Article 152(1). The applicants also argued that Article 23.5 of the EA2 PSA does not violate Article 152 of the Constitution for the simple reason that it does not involve “imposing” a tax.

The applicants also argued that the respondent’s application of Article 79 of the Constitution is misconceived. Article 79 applies to the power to make laws, not to the terms of an agreement. The applicants also argued that the respondent’s submission on Article 99 of the Constitution is not correct. Article 99 does not mention a restriction on the President’s authority to “waive the law”. The applicant argued that the President has power to grant a tax exemption. Granting an exemption does not show the Government’s failure to act according to the Constitution. The applicants argued that Article 99 of the Constitution should be read in conjunction with Article 113 of the Constitution. It provides for the delegation of powers to cabinet ministers. The Minister was appointed by the President with inherent powers to enter into agreements such as the EA2 PSA.

The applicants argued that the respondent’s reference to the removal of broad discretionary exemptions under the Income Tax Decree and the Investment Code has no relevance to the matter before the Tribunal. Firstly, they relate to completely different specific statutory powers granted to a different minister, the finance minister. Secondly, the said Decree and Code ceased to have effect in 1997 and the EA2 PSA was entered into by the Minister in 2001. The respondent’s assertion that S. 12 of the Income Tax Decree granted broad discretionary exemptions is inaccurate. S.12 provided specific statutory exemptions. The applicants argued that respondent does not rely on evidence in making these sweeping allegations of facts.

The applicants argued that the granting of a capital gains tax exemption in relation to assignment or transfer of an interest in EA2 PSA is clearly connected with the granting of a petroleum licence, and exploration or development under the licence as from the evidence of the witness. There is no reason why such an exemption should not be regarded as incidental to the matters set above.

As regards estoppel, the applicants argued that the respondent failed to distinguish between an act of government and an act of a statutory body. Article 23.5 is not *ultra vires* because the government did have power to enter in the EA2 PSA Article 23.5. The GOU is not a statutory body. Consequently it does not have statutory powers. The applicants posed a question: “If the government is not able to grant tax exemptions, then who can?” There is no statutory prohibition on the GOU giving a tax exemption. The GOU as a principal has powers to bind URA, its agent, and has done so. The applicants argued that the cases cited by the respondent in respect to estoppel are therefore not applicable. The respondent cannot identify a statutory power Article 23.5 is said to be in excess of.

The applicants contended that the respondent’s argument on the sale of undivided interests was an attempt to introduce a new issue that was not raised at the scheduling. The applicants did not adduce any evidence in respect thereof because they were not notified. They therefore argued that it would be manifestly unfair for the respondent to be allowed to argue this new point. The applicants also argued that for there to be undivided interests, there have to be two or more joint owners. From the moment the TUL acquired Heritage interests it alone held the whole of the interests in those PSAs. From that moment there was no “tenants in common, there was no “co-ownership”, which concepts are in land law. The applicants argued that the Tribunal is not concerned with the disposal of land.

The applicants submitted that the respondent was aware that they intended to sell Heritage interests since the drafts of the CNOOC/Total contracts were sent to the GOU and the respondent in October 2010. The applicants submitted that GOU approved the draft PSAs where Heritage interests were sold. The word “interest” was defined in the draft agreements to include the 16.67% interest of the original interests. The respondent issued its assessments knowing that the applicants were transferring Heritage interests.

The applicants contended that the respondent did not give any authority as why it is opposed to the “last in first out” accounting method. They also argued that there is no support in Uganda or elsewhere for applying any other rule in respect of the disposal of an undivided interest.

As regards S. 89G of the ITA, the applicants argued that the cost base in respect of the Heritage interests comprises the Heritage gain less, if relevant, any “excess costs”. They are not seeking to “include the US$ 150,000,000 rather it is the respondent who should argue that such sum should be deducted from the Heritage gain as excess costs”. The applicants argued that there are no excess costs to date. The applicants argued that the respondent appears to be confusing the right to deduct expenditure under S. 89C with the deduction of excess costs from a transferee contractor’s cost base where it has disposed of its interest. The applicants submitted that S. 89C of the ITA limits the use of expenditure against profits from oil production but it does not cancel the relief in respect of a capital expenditure, in a computation of a capital gain under S. 52(6). To them, what S.89G(d) states is that what must be deducted from the transferor’s gain is the excess costs up to the date of the disposal deductible by the transferee contractor. At the date of disposal, there being no cost oil, there are no “excess costs” that can be deducted from the Heritage gain.

The applicants submitted that they are entitled to a deduction for their expenditure of US$ 320 million which was passed on to CNOOC and Total. As regards the respondent’s allegation that the applicants failed to substantiate the costs of US$ 320,545, 819 incurred as exploration costs, the applicants submitted that the said figure derives from communication between the parties in November 2012 and the tax returns for the year ended 31st December 2009, submitted in June 2012 and provided in the communication in November 2012.

The applicants referred to their computation where the applicants purchased their interests from Heritage at US$ 775 million for EA1 and US$ 575 million for EA3A from which they deducted the purchase price for the Heritage interests, US$ 773,134,258 for EA1 and US$ 573,635,740 for EA3A, producing a loss. The applicants contended that the respondent misread S. 22 of the ITA. It only relates to insurance situations.

As regards the sale of Heritage interests, the applicants submitted that Heritage wanted to sell its interests to ENI. The applicants exercised their pre-emption rights to prevent this. The applicants wanted to acquire Heritage interests and as soon as consent was given to sell them off. Tullow, CNOOC and Total executed documents showing what that transaction was and the respondent issued assessment on capital gain on that basis. Hence there is no tax avoidance scheme. The applicants cited the case of *Stanton v Grayton* [1983] 1 AC 501 where the court focused more on what the agreement said. The question is: "how would a businessman see the transaction? Having regard to a businessman's view, what one would conclude is that what were sold were Heritage's interests.

In respect of reinvestment relief, the applicants argued that they are in principle, entitled to reinvestment relief under S. 54(1)(c) of the ITA. The applicants reiterated their position that the affidavits of Mr. McDade, Mr. Graham and Mr. Martin all showed that the applicants did not dispose off the 16.67% voluntarily. The applicants also presented slides to the GOU which indicated their desire to sell 50% interest.

The applicants argued that involuntary should be widely construed. It does not "require force but rather an action taken by a person who has no choice". The evidence shows that the applicants acted involuntarily. They only wished to dispose of 50% of their interests but the GOU pressed them to dispose of another 16.67%. They argued that they did not provide evidence of "force", whether improper or proper, because force was not necessary. The applicants cited again the case of *URA v Bank of Baroda* HCT -00-CC-CA-05-2005 where it was held that "one has to look at the agreement itself to ascertain its true intention..." As regards the respondent's argument that the Bank of Baroda case involved an agreement unlike the one before the Tribunal, the applicants submitted that S. 54(1)(c) does not provide any proscription as to the circumstances in which the involuntary act must take place. Secondly the disposal of the 16.67% was contained in an agreement, namely, the MOU and the SPAs. It was an express condition of the MOU that GOU's consent was required to the farmdown.

The applicants also submitted that they could not present evidence at the hearing as to the expenditures incurred on the reinvestment relief as their one year period had not expired. This was because the respondent assessed the disposals before they had taken place. The

dispositions were completed on the 21st February 2012 and the one year period ran until 21st February 2013. The hearing was on 26th to 28th November 2012 and 19th to 21st February 2012. This was a result of the respondent assessing the gain over a year before the disposals actually took place. The Tribunal was only asked to rule if the applicants were entitled to relief in principle.

The applicants argued that the respondent's submission that the proceeds of sale can only be used to acquire an interest in a new PSA is not correct. The applicants cited *Black's Legal Dictionary* which defines it, inter alia, as: "The act or process of replacing or being replaced; substitution." The applicants have substituted the interests disposed of under the PSAs with interests in assets or rights which are dealt with under the PSAs. The reference in S. 54(1) (c) to "assets of a like kind" can simply be a reference to a contract, under which expenditure is made. The provisions do not require reinvestment in assets to be of an "identical" kind. Therefore, expenditures on "interest data" and "interest property" are expenditure on assets "of a like kind" within S. 54(1) (c). Expenditures were incurred on machinery, wells, facilities, offshore and onshore installations and structures.

6. FINDINGS AND DECISION OF THE TRIBUNAL

The Tribunal having read the witnesses' statements, heard the evidence adduced, read the parties' submissions and perused the authorities cited, wishes to rule as hereunder.

6.1 ARTICLE 23.5 OF THE EA2 PRODUCTION SHARING AGREEMENT (PSA)

On the 8th October 2001, the applicants and the GOU executed a PSA under which the former were granted exploration, development and production rights in EA2. There were two Articles in the PSA that referred to taxation. The first one was Article 11 of the PSA, which read as follows:

> "All central, local, district, administrative, municipal or other taxes, duties, levies or other lawful impositions applicable to the Licensee shall be paid by the Licensee in accordance with the laws of Uganda in a timely fashion."

The said Article does not seem to be in dispute. The applicants were aware that they were required to pay taxes. The second Article which is the bone of contention is Article 23.5 of the EA2 PSA which purportedly attempts to exempt transactions which involve the assignment or

transfer of an interest under the PSA from tax. It does not seem to be in dispute, that the effect of Article 23.5 was to carve out from the main Article of tax liability, (i.e. Article 11), an exemption or a waiver of tax to the licensee or its assignee in respect of an assignment or transfer of an interest. What is in dispute is the interpretation of Article 23.5 of the EA2 PSA in light of the ITA. The applicants argued that Article 23.5 of the EA2 PSA offered an exemption to capital gains tax which is disputed by the respondent.

The applicants sold a portion of their interests in, inter alia, EA2 to CNOOC and Total. The respondent assessed the applicants, capital gains tax on the gain they purportedly received. The applicants objected to the assessment of capital gains tax in Block EA2 and claimed an exemption. The applicants called two witnesses who testified that because of Article 23.5 of the EA2 PSA they were not liable to pay capital gains tax in respect of the transfer of interests in EA2. According to Mr. Graham, the applicants relied on Article 23.5 of the EA2 PSA in their decision to farmdown. The applicants had incurred enormous expenditures and expected to recoup them when they sold a portion of their interests. Though Mr. Graham was not part of the legal team that drafted the PSA, he was its head. According to him, Article 23.5 exempted capital gains tax. The second witness, Mr. Richard Inch, the Head of Tax, stated that the applicants assumed that in the event of a farmdown the proceeds would be received tax-free because of Article 23.5. He was of the view that the exemption under Article 23.5 was valid.

The respondent's witnesses gave evidence to the contrary. According to Mr. Rubondo, Article 23.5 was not negotiated by the parties. He testified that the GOU did not want licensees to be encumbered with fees, imposts and taxes. The intention of Article 23.5 was to facilitate the licensees to bring on board partners to share risk without the need to pay fees and imposts like stamp duties and signature bonuses. He said the clause was not meant to cover taxes on gains. Its purpose was to facilitate the sharing of risk and not to guide the taxation of a gain. According to Mr. Kajubi, the Commissioner Domestic Taxes, Article 23.5 was not part of the ITA. Capital gains tax is not a transfer tax. Hence it was not catered for under Article 23.5.

The Tribunal notes that while Mr. Rubondo and Mr. Kajubi were competent witnesses, the Tribunal does not think that they are the most appropriate persons to testify on the intention of the GOU in respect of Article 23.5. Firstly, there is no evidence that both were part of the

negotiating or drafting team of the EA2 PSA. Secondly, the most appropriate person to testify on the intention of the GOU should have been the Attorney General or an official from his/her chambers. Under Article 119(3) of the Constitution, the Attorney General is the principal legal advisor of GOU. Article 119(4) (b) of the Constitution reads that the functions of the Attorney General include:

> "to draw and peruse agreements, contracts, treaties, conventions and documents by whatever name called, to which the Government is a party or in respect of which the Government has an interest."

The Tribunal cannot say that Mr. Rubondo and Mr. Kajubi are officials of the Attorney General's chambers. Mr. Kajubi's interpretation might have carried some weight; however the Tribunal has to caution itself against such testimony, as it is likely to be skewed in favour of revenue collection which is entrusted to his employer, Uganda Revenue Authority.

Intention can still be ascertained from the use of the words in an agreement. In *Nile Bank (U) Limited v Translink (U) Limited* [2001 – 2005] 2 HCB 53 it was noted that court must discern intention from words in a document.

Both parties gave lengthy submissions on the interpretation of Article 23.5 of the EA2 PSA. The applicants submitted that the disposal of their interests under Article 23.5 of the EA2 PSA falls under the ITA and is governed by S. 89G(c) which reads:

> "Where a contractor, in this Part referred to as the "Transferor contractor" disposes of an interest in a petroleum agreement to another contractor or a person that as a result of the disposal will become a contractor in relation to those operations, in this Part referred to as the "Transferee contractor"-

The applicants submitted that there was a sale of interests as witnessed by the SPAs which transactions were completed on the 21st February 2012. The ITA is applicable to said transactions.

The respondent submitted heavily on rules of statutory interpretation to determine whether the parties intended to grant an exemption. It submitted that capital gains tax was not a transfer tax. Hence it was not exempted by Article 23.5 of the EA2 PSA. However, the applicants objected to the respondent's use of the rules of statutory interpretation as the EA2 PSA was an agreement and not a statute. The Tribunal agrees with the applicants on this point. The EA2 PSA is not a

statute, it is an agreement. The rules of statutory interpretation may not be appropriate when interpreting agreements. The rules of statutory interpretation may be important when determining whether an agreement is in compliance with a statute but not the intentions of the parties or to assign meanings to words or in determining how a reasonable man would interpret a document.

The applicants argued that in order to get a good interpretation of the Article, the intention of the parties is important. Did the parties intend Article 23.5 to include an exemption to capital gains tax? While the applicants' witnesses testified that Article 23.5 intended to cover an exemption, we cannot say what the position of the GOU is. There was no witness from the Attorney General's chambers. The Tribunal notes that the GOU which was a party to the PSA is not a party to the application before it. Under Article 119(4) (c) of the 1995 Constitution, the functions of the Attorney General include to represent the GOU in courts or any other legal proceedings to which the GOU is a party. However the TAT Act envisages one respondent, Uganda Revenue Authority. Though the Uganda Revenue Authority is an agent for GOU, it did not sign the EA2 PSA. The contractual obligations of the GOU cannot be determined when it is not a party before the Tribunal. However, the Tribunal is not interested in the contractual obligations of the parties. What is of interest to the Tribunal are the tax liabilities of the taxpayers, in this case the applicants. Tax liability is set by statute. Be what it may, what the parties say was their intention may not help when it comes to determining tax liability. Where an agreement is involved, the taxman should determine whether it is in line with the taxing legislation. Does Article 23.5 of the EA2 PSA afford protection to the taxpayers, the applicants? This involves interpretation of the Article 23.5 of the EA2 PSA in light of the ITA.

The taxman has to make an objective analysis or interpretation of the agreement in light of the statutory provisions. In *Investors Compensation Scheme Ltd V West Bronwich Building Society* 1998 1 ALL ER 98 Lord Hoffman LJ said:

> "(1) Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation which they were at the time of the contract.
>
> (2) The background was famously referred to by Lord Wilberforce as the matrix of fact; but this phrase is, if anything, an understated description of what the background may include.

Subject to the requirement that it should have been reasonable to the parties and to the exception to be mentioned next, it includes anything which would have affected the way in which the language of the document would have been understood by a reasonable man.

(3) The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action of rectification. The law makes this distinction for reasons of practical policy and in this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life.

(4) The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammar; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean..."

The said authority was cited in *Golden Leaves Hotels and Resorts Limited and Apollo Hotel Corporation V Uganda Revenue Authority* Civil Appeal 64 of 2008. The Tribunal is interested in how a reasonable man would have interpreted Article 23.5 of the EA2 PSA in light of the ITA rather than the intentions of the parties. As stated above, the previous negotiations of parties and their subjective intent are admissible only in an action of rectification. The Tribunal is not interested in rectifying the EA2 PSA. What is of concern to the Tribunal would be the meaning a reasonable man would convey to the document in respect to an exemption to capital gains tax and not the meanings of words. The meaning of words may not be the same as the meaning of a document as the latter involves the parties using the words against the relevant background.

Where the agreement involves government, for once, the taxman may have to forget that he is collecting taxes for the government. What should be considered is the use of the words in the agreement and the relevant background. The background that may be relevant, in this case, is that the EA2 PSA was entered into by GOU for the exploration, production and development of oil. By the time the EA2 PSA was signed no oil had been discovered. Article 23.5 was incorporated in the agreement to entice oil companies in the oil exploration venture. However what may not be clear is whether Article 23.5 was to encourage oil companies invest in the venture or was it to facilitate them transfer off their interests to other investors? This can only be resolved by looking at the wording of the Article in relation to the relevant statute.

In order to understand whether Article 23.5 included capital gains tax one would need to look at the statutory provisions which define the tax payable. It is a bit surprising that when the parties

were trying to interpret Article 23.5 of the EA2 PSA, none referred to the description of capital gains tax under the ITA and compared it with the Article. The relevant Sections in the ITA include S.18 which defines what business income is, and reads:

> "(1) Business income means any income derived by a person in carrying on a business and includes the following amounts, whether of a revenue or capital nature-
>
> (a) the amount of any gain, as determined under Part VI of this Act which deals with gains and losses on disposal of assets..."

S. 50 of the ITA which deals with disposals of assets reads:

> "(1) A taxpayer is treated as having disposed of an asset when the asset has been
>
> (a) sold, exchanged, redeemed, or distributed by the taxpayer;
>
> (b) transferred by the taxpayer by way of gift; or
>
> (c) destroyed or lost."

S. 18 states that a disposal of an asset is business income. S. 50 shows that a disposal of an asset includes when an asset has been sold or exchanged.

The applicants cited Article 23.5 of the EA2 PSA, as their shield against income tax liability arising from a capital gain. Article 23.5 read as follows:

> "The assignment or transfer of an interest under this Agreement and any related Exploration or Production Licence shall not be subject to any tax, fee, or other impost or fee levied either on the assignor or the assignee in respect thereof."

For an interest to be exempt from any tax there should be an assignment or a transfer. Is an 'assignment' or' transfer' under Article 23.5 of the EA2 PSA the same as a 'sale' or 'exchange' under S. 50 of the ITA? The *Black's Law Dictionary* 8th edition p, 128 defines assignment as follows"

> "1.The transfer of rights or property <assignment of stock options>. ... 2. The rights or property so transferred < the aunt assigned those funds to her niece, who promptly invested the assignment in mutual funds>."

A transfer is defined under *Black's Law Dictionary* (supra) p. 1536 as:

> "1. to convey or remove from one place or one person to another; to pass or hand over from one to another, esp. to change over the possession or control of. 2. To sell or give."

S. 50(1) (a) of the ITA provides for "sold, exchanged, redeemed, or distributed by the taxpayer." A sale is defined by *Black's Law Dictionary* (supra) p. 1364 as:

> "1. The transfer of property or title for a price... 2. The agreement by which such a transfer takes place. ● The four elements are (1) parties competent to contract, (2) mutual assent, (3) a thing capable of being transferred, and (4) a price in money paid or promised."

A transfer under Article 23.5 of the EA2 PSA involves a sale as provided under S 50 of the ITA.

The applicants contended that they sold their interests under Article 2 of the SPA. Article 2.1 of both the SPAs between the applicants, Total and CNOOC read as follows:

> "Subject as herein provided, Tullow hereby agrees to sell and transfer all of its legal and beneficial right, title and interests in and to the interest free from all Encumbrances whatsoever relating thereto (subject to the provisions of the Interest Documents) with full title guarantee to the Purchaser for the consideration referred to in Clause 3.1 and the Purchaser hereby agrees to purchase and acquire the interest. The transfer shall, as between the Parties, be deemed for purposes to be made with effect on and from the Effective Date."

Hence it cannot be denied that the applicants' sales of their interests in the SPAs were covered under S. 50 of the ITA and exempted by Article 23.5 of the EA2 PSA.

Without prejudice, Article 23.5 of the EA2 PSA mentions "any tax, fee, or other impost or fee levied either on the assignor or the assignee". The above net is so wide to include capital gains tax as long as it is a tax or other impost.

So would one be wrong if one stated that the exemption under Article 23.5 of the EA2 PSA covered a gain made by the applicants in the transfer of their interest in EA2 under the SPAs to CNOOC and Total and was therefore exempted? The Tribunal does not think so. To a reasonable man, an assignment or transfer of an interest under the PSAs if it involves a sale or an exchange is covered by both S. 50 of the ITA and Article 23.5 of the EA2 PSA. Therefore to a reasonable man the exemption under Article 23.5 purportedly covered capital gains.

The respondent argued that capital gains tax is not a transfer tax. A capital gain arises when there is a gain on an asset or an interest. It therefore is not a transfer tax. However the said gain cannot be realised and taxed unless there is a disposal, sale or transfer. While the Tribunal would agree with the respondent that capital gains tax is not a transfer tax, Article 23.5 of the EA2 PSA does not mention transfer tax. A transfer is one thing and a 'transfer tax' is another. The Tribunal does not think that the Minister of Mineral and Energy Development, who signed on behalf of the GOU or any reasonable person, would know what a transfer tax is, or whether

capital gains tax was a transfer tax. The Tribunal would not wish to import the terms “transfer tax” into Article 23.5. The term “transfer tax’ was defined in the SPAs and not the EA2 PSA and the parties are different. The SPAs were made long after the PSA. Any arguments by the respondent in respect of transfer tax are diversionary and shall not be accepted by the Tribunal. The Tribunal therefore finds that Article 23.5 of the EA2 PSA included an exemption to capital gains tax. Issue 1.1 is decided in favour of the applicants.

Issue 1.2 was in respect of the legal validity of Article 23.5 of the EA2 PSA under Ugandan law. In its objection decision, the respondent contended that in the event Article 23.5 of the EA2 PSA granted an exemption to the applicants in respect of capital gains tax, it would be manifestly unlawful under Uganda law. Firstly, the Minister was acting ultra vires the authority granted to him. Secondly, a tax can only be imposed or waived through a law passed by the Parliament.

On the contrary, the applicants, in their submission, submitted that the GOU was empowered to enter Article 23.5 of the EA2 PSA. Firstly, the minister would do so under the powers conferred by the Petroleum and Energy Production Act (PEPA). Secondly, the GOU would enter such agreement under the powers which pre-date Uganda’s written constitution and have been preserved after the introduction of the written constitution and under other powers expressly conferred by the Constitution.

The applicants argued vehemently that the Minister of Energy had powers to sign for a tax exemption under the PEPA. The long title of the PEPA reads:

> “An act to make provision for the exploration and production of petroleum and for other matters incidental thereto or connected”

S. 2 of the PEPA reads:

> “The Government may enter into an agreement, not inconsistent with this Act, with any person with respect to all or any of the following matters-
>
> (a) the grant of a licence;
>
> (b) the conditions for granting or renewing the licence;
>
> (c) the conduct by a contractor of explorations or development operations on behalf of any person to whom a licence may be granted and the arrangements in any such case for production sharing;

(d) the manner in which the Minister or the Commissioner will exercise any discretion conferred on him or her under this Act;

(e) any other matter incidental to or connected with the foregoing..."

The applicants argued that the Minister would exercise his powers under S. 2 (e) and grant an exemption to the transfer of interests as it was incidental or connected with the foregoing. With all due respect, to the counsel of the applicants' position, the Tribunal does not think that this is a correct interpretation of the powers conferred on the Minister under the PEPA. The granting of a tax exemption has nothing to do with the granting of a licence, renewal or regulation of oil exploration, oil production or development operations.

Counsel for the applicants cited the case of *Scottish Widow Plc v RCC* [2010] STC 2133 where the courts stated; "... the phrase 'in connection with' generally merits a wide interpretation..." However wide an interpretation the Tribunal may give to the words "incidental to or connected with the foregoing" under S. 2 of the PEPA, it cannot stretch its imagination and perceive how a minister can grant an income tax exemption under PEPA. In the above case, Lord Hamilton at para. 77 noted: "In some contexts, though not always, the problem may be solved by substitution of the words 'having to do with'". Granting a tax exemption has nothing to do with licensing or regulating the conduct of an oil operator. He cited *Bank of Scotland v Dunedin Property Investment Co Ltd* 1998 SC 657 at 671 where Lord Kirkwood observed:

> "For my part I am prepared to accept the words "in connection with" are capable of a wide construction and in a case of this nature I would be prepared to accept that it would be sufficient if it was demonstrated that there was a substantial relationship in a practical business sense."

Lord Hamilton noted on p. 2208, para. 78:

> "I doubt whether any useful guidance can be drawn from the construction of "in connection with" in these very different contexts. Here it is associated with the phrase 'part of '(a transfer of a business). The latter phrase would import that the addition (or transfer) of the amount was an integral element of the transfer of the business. 'In connection with' imports a less immediate but not a tenuous relationship with a transfer of the business. Perhaps 'in association with' would here be the closest equivalent."

The applicants should not give the phrase "incidental to or connected with the foregoing" an over- inflated application. The "connection with" should be practical and substantial. Licence do provide for tax exemptions.

Black's Law Dictionary (supra) p. 777 defines "incidental" as: "adj., Subordinate to something of greater importance; having a minor role". The Tribunal feels that this is the definition a reasonable man should use. It is difficult to understand how a reasonable man would perceive the ITA as being subordinate to the PEPA. The PEPA deals with exploration and production of oil, while the ITA deals with law relating to income. Income tax is created under the ITA. S. 4 of the ITA imposes income tax. The long title of the ITA reads: "An Act to consolidate and amend the law relating to income tax and for other connected purposes". If there is any connection between the ITA and the PEPA it is too remote to consider it under S. 2 of the PEPA.

All legal powers and authorities emanate from the Constitution. Under the Uganda Constitution a tax is imposed through a law passed by Parliament. This is clearly stated in Article 152 of the Constitution of Uganda which reads:

> "(1) No tax shall be imposed except under the authority of an Act of Parliament.
>
> (2) Where a law enacted under clause (1) of this article confers powers on any person or authority to waive or vary a tax imposed by that law, that person or authority shall report to Parliament periodically on the exercise of those powers, as shall be determined by Law."

The above Article reminds one of the Boston Tea Party of 16th December 1773 where American colonists had a problem of paying taxes to Britain when they had no representation in British Parliament. There is no Boston in Uganda. This is not a History lesson. However, it does not harm to use a historical perspective to understand the relationship between the legislature and the imposition of taxes. The framers of the 1995 Constitution of Uganda thought it wise that the people's representatives should be the most suitable persons to impose the taxes they should pay. So be it.

Where a power is vested in one arm of the government, another arm cannot usurp the said power unless it is legally provided for. This would infringe on the doctrine of separation of powers. It is the duty of the legislature to enact laws that impose taxes. Lord Wilberforce explained *in Vestey v IRC* [1980] STC 10 at 18 54 TC 503 at 581:

> "Taxes are imposed upon subjects by Parliament. A citizen cannot be taxed unless he is designated in clear terms by a taxing Act as a taxpayer and the amount of his liability is clearly defined."

This approach was echoed by his Lordship Madrama in *Kampala Nissan Uganda Limited V Uganda Revenue Authority* Appeal 7 of 2009, [2011] UGHC 80, where he stated:

> "For emphasis I need to state that no tax can be imposed except under the authority of an Act of `Parliament neither can an authority waive tax except under a law enacted by Parliament."

In *Heritage Oil and Gas Limited v Uganda Revenue Authority* Civil Appeal 14 of 2011, Her Lordship Obura said that:

> "Article 152(1) of the Constitution of Uganda provides that no tax shall be imposed except under the authority of an Act of Parliament. The ITA and other tax statutes specify the taxes payable and the URA is mandated to collect those taxes."

It cannot be doubted that powers to make tax laws are vested in the legislature. On the other hand, It is the duty of the executive to collect the said taxes and use the said taxes in the administration of public affairs. There would be a conflict of interest if the executive was to impose taxes, collect them and use them. It might get carried away with the so much power that would be vested in it. In order to avoid this, the constitution left the power to levy taxes with Parliament.

If the Parliament confers on a minister or the executive arm of government powers to grant or waive a tax, it has to expressly provide for it in an Act of Parliament. This authority under the ITA is bestowed on the Minister of Finance who has to report to Parliament on waivers or variations in taxes. The Tribunal has not come across any Act of Parliament where the Minister of Energy and Mineral development is given powers to grant tax exemptions.

The applicants argued that the GOU exercises powers which pre-date Uganda's constitution or expressly conferred by the constitution. The applicants submitted that such pre-written constitution powers include a power to grant exemption from tax (the "PC Exemption Power"). The Tribunal agrees with the applicants' citation of Article 274 of the Constitution that laws existing before the coming into force of the Constitution were not affected by it and could be construed with modifications, adaptations and qualifications as to bring them in conformity with the Constitution. The Tribunal also agrees that existing laws mean both written and unwritten law. The Tribunal also agrees with the respondent's citation of *Attorney General v Osotraco Ltd.* Civil Appeal No. 32 of 2002, [2005] UGCA 1 where the court noted that Article 274 of the Constitution:

> "... only empowers all courts to modify existing unjust laws without necessarily having to refer all such cases to the Constitutional Court. This provision enables the court to expedite justice by construing unjust and archaic laws and bringing them in conformity with the constitution, so that they do not exist and are void."

However the applicants have not cited any authority nor adduced any evidence to show that the President had powers to grant tax exemptions before the coming into force of the 1995 Constitution and that such powers survived its promulgation. The applicants merely argued that "simply because there is no express provision providing for a power to grant an exemption from tax does not mean that such a power does not form part of the President's executive authority" If such powers of the executive to impose tax exist they would be mythical. Such an assertion is based on speculation. Also the use of extra statutory materials advanced by the applicants on the derivation of the said powers from ancient common law prerogatives of the Crown are not useful aids in showing the source of the purported President's powers. The applicants did not cite any authority to show under which common can the Crown derives the power to grant any tax exemption.

The applicants also argued that the Minister could sign under other powers conferred by the Constitution. The applicants relied on Objective IX – the right to development, and Objective XI (ii) – stimulation of industrial development by adoption of appropriate policies. The objectives of the 1995 Constitution merely state the framework under which the Constitution will operate. A perusal of the said objectives does not show any grant of tax exemption. Similarly, the applicants' reliance on Articles 2, 99, 111 and 113 of the Constitution do not show any powers of the executive to grant tax exemptions.

In *Attorney General v Malalu Musene Wilson and others* Constitutional Appeal No. 7 of 2005 the constitutional court was of the opinion that "had the framers of the Constitution wanted to confer a tax exemption on emoluments of judicial officers, they would have said so expressly." As regards the exemption that was extended to judges, the court stated that:

> "We wish to add, however, for clarity that the Income Tax Act did provide for the Minister of Finance to grant a tax exemption to any person. The Cabinet did decide in 1991 to extend exemption from payment of tax to Judges."

The applicants do not argue that the Minister of Mineral and Energy Development was conferred powers under the ITA to grant exemption to any person, which is not the case. The applicants

do not refer to any constitutional provision which explicitly allows the Minister to grant tax exemptions. In the absence of the Constitution conferring powers to any other arm of the Government or institution to impose taxes, it can safely be said that the authority to impose taxes vests only in the Parliament or as it so provides.

The Constitution does not expressly state that Parliament shall grant an exemption. However S. 23 of the Interpretation Act provides that:

> "Where any Act confers a power on any person to do or enforce the doing of any act or thing, all such powers shall be understood to be also given as are reasonably necessary to do or enforce the doing of the act or thing."

S. 2 of the said Act defines a person to include a body of persons corporate or unincorporate. Applying the Interpretation Act, if the Parliament has powers to impose taxes it also has the powers to waive them. He who has powers to appoint, has powers to disappoint. If one has powers to impose a tax, then the power to dispose off would be implied. Therefore Article 152 implicitly provides that Parliament has the powers to make laws granting exemptions or to empower persons to grant them.

The applicants argued that Article 152(2) of the Constitution sets out the procedure applying to laws enacted under Article 152(1). Article 152 of the Constitution provides that where under a law enacted by Parliament, one is given powers to waive or vary a tax that person should report to Parliament periodically. There is no evidence to show that the Minister of Energy and Mineral Development who signed the EA2 PSA ever reported to Parliament on the exercise of such powers, if she had any. There is no evidence that she declared the grant of a tax exemption under Article 23.5 to Parliament. Such an omission is fatal as the Constitution is clear.

The applicants argued that Article 23.5 of the EA2 is not a waiver or variation of taxes at all. Secondly it is not a waiver or variation granted "pursuant to a law enacted under Article 152(1) of the Constitution, as it is in an agreement. "It is a *fait accompli*." An exemption is given by law. A waiver is given by an authority exercising its discretion taking into account special consideration. A waiver ends it an exemption. It is a question of semantics. An agreement to confer on a minister, powers to grant exemptions or waive taxes, there must be an enabling Act.

In the case of the EA2 PSA there was no enabling Act that empowered the Minister of Energy to grant exemptions or waivers or variations of taxes.

Therefore the Tribunal finds that the Minister of Energy and Mineral Development did not have legal authority to grant an exemption under Article 23.5 of the EA2 PSA. Any such grant offended the tax provisions of the tax laws including the ITA.

Issues 1.3 which was in respect of the application of international law to Article 23.5 of the EA2 PSA was abandoned by the applicants. The applicants however in the later issues discussed the principle of *pacta sunt servanda*. This is a principle of international law. We shall cross the bridge when we reach it.

Issue 1.4 was dependent on the findings on issues 1.2 and 1.3. However the applicants submitted that the respondent is an agent of the GOU. The applicants argued that as an agent it is bound by the EA2 PSA signed by its principal, the GOU. The applicants cited *Heritage Oil and Gas v URA* Civil Appeal 14 of 2011 where the High Court held that the URA is a statutory body established under S. 2 of the URA Act as an agent of GOU. The court noted that:

> "It follows that URA as a statutory agent is part and parcel of Government. It cannot therefore in my opinion be seen to disassociate itself from the PSA, which is the principle the Government lawfully signed with the Applicant. To attempt to do so would just be splitting hairs."

The applicants argued that the respondent is therefore bound by Article 23.5 of the EA2 PSA. It therefore should not deny the Minister's authority to enter into the PSA, including Article 23.5

The Tribunal does not deny that the respondent is an agent of GOU. However, the law establishing the Uganda Revenue Authority requires it to administer and enforce the laws of Uganda in respect of revenue collection. The Preamble of the Uganda Revenue Authority Act reads:

> "An Act to establish the Uganda Revenue Authority as a central body for the assessment and collection of specified revenue, to administer and enforce the laws relating to such revenue and to provide for related matters."

In *K.M. Enterprises and others v Uganda Revenue Authority [2008]* UGCommC 21 the court noted that;

> "The authority of the Uganda Revenue Authority is to administer certain tax laws, collecting the tax due. The Uganda Revenue Authority cannot, in breach of duties imposed by statute agree to collect less tax than due from any particular tax payer."

Therefore as an agent of the GOU one of the objectives of the respondent is to administer and enforce the laws relating to such revenue. The GOU, though is the principal, is still bound by the laws in respect to revenue collection. Any agreement entered into by the GOU should abide by the law in respect of revenue collection. The Tribunal does not think it is merely sufficient to argue that once a person is an agent of government it will not abide by a statute.

While issue 1.5 was raised in respect to the application of estoppel to Article 23.5 of the EA2 PSA, issue 1.6 addressed the application of the principles of legitimate expectation. The applicants attempted to merge the principle of estoppel with that of legitimate expectation. They argued that the two issues are heavily dependent on each other. They argued that "estopped" is not a technical term but simply refers to "circumstances in which by the operation of law, an individual or body is prevented from behaving in a particular manner." Legitimate expectation is a principle distinct from estoppel but shares a common origin with estoppel and is rooted in principle of fairness. Consequently the GOU is estopped by the principles of fairness. The applicants also argued that principle of *pacta sunt servanda* operates to prevent unfairness.

The respondent, on the other hand, argued that both estoppel and the principle of legitimate expectation are not applicable in the present application. The respondent argued that there can be no estoppel against a statute. Furthermore, an expectation grounded upon an ultra vires representation cannot be legitimate. The respondent contended that "the *pacta sunt servanda* argument by the applicants is no more than a recycling of the same untenable arguments discussed earlier under a different name."

The rule of estoppel is a rule of evidence. In order to understand it, we looked at various descriptions and definitions. Under the Evidence Act Cap. 6, estoppel is described as:

> "When one person has, by his or her declaration, act or omission, intentionally caused or permitted another person to believe a thing to be true and to act upon that belief, neither he or she nor his or her representative shall be allowed, in any suit or proceeding between himself or herself and that person or his or her representative, to deny the truth of that thing."

According to *Osborn's Concise Law Dictionar*y 6th edition, estoppel is defined as:

> "…. The rule of evidence or doctrine of law which precludes a person from denying the truth of some statement formerly made by him, or the existence of facts which he has by words or conduct led to others to believe it. If a person by a representation induces another to change his position on the faith of it, he cannot afterwards deny the truth of his representation..."

Black's Law Dictionary (supra) p. 589 defines estoppel as:

> "*n.*1. A bar that prevents one from asserting a claim or right that contradicts what one has said or done before or what has been legally established as true... 2. A bar that prevents the relitigation of issues. 3. An affirmative defense alleging good-faith reliance on a misleading representation ..."

From the above definitions a number of things are clear. It is a rule of evidence. Secondly, it is a bar or a shield and cannot be a sword to create liability. In *Mulji Jetha Ltd V Commissioner of Income Tax* [1967] E.A. 50 it was held, inter alia, that the claim must fail, because the plaintiff was seeking to use the principle of equitable estoppel to found a cause of action. It prevents a person from denying the truth of a representation made by another. The Tribunal does not think that the concepts of "truth" and "legality" are one and the same thing. Those are different concepts. From the above definitions, it is doubtable whether a party can rely on a representation made by a third party. In this case it was the GOU that purportedly made the representation to the applicants and not the respondent, which are different legal entities.

The respondent has argued that there is no estoppel against a statute. The respondent stands to be corrected. There has to be a distinction between a legal act, conduct or representation, which is *intra vires*, and one which is illegal or *ultra vires*.

Where an act, conduct or representation is legal, estoppel may operate. In *Regina v Inland Revenue Commissioners Ex parte M. F. K. Underwriting Agents Ltd* 1990 WLR 1545 the court in dismissing the application held that:

> "it was within the managerial discretion of the Inland Revenue to give assurances as to the taxation treatment which financial securities would receive albeit that might involve the revenue forgoing tax to which they might be entitled, for such assurances to be relied upon or form the basis, in the event of breach, of a successful application for a judicial review, they must have been given in response of full disclosure, by the party seeking them, of the clear terms of a specific transaction."

In *Reg. V I.R.C., Ex.p Matrix Securities Ltd* [1994] WLR 334 the court stated that:

> "It is now established that in certain circumstances, it is an abuse of power for the revenue to seek to extract contrary to an advance clearance given by revenue. In such circumstances, the taxpayers can by way of judicial review apply for an order preventing the revenue from seeking to enforce the tax legislation in a sense contrary to assurance given: *Reg. V Inland Revenue Commissioners, Ex parte Preston* [1985] A.C. 835. But the courts can only restrain the revenue from carrying out its duties to enforce taxation obligations imposed by legislation where the assurances given by the revenue make it unfair to contend for a different tax consequence, as a result of which unfairness, the exercise of its statutory powers by the revenue would constitute an abuse of power: see per Lord Templeman, at p. 864G. It is further established that if the taxpayer, in seeking advance clearance, has not made a full disclosure of the relevant circumstances, the revenue is not acting unfairly, and therefore is not abusing its powers, if it goes back on an advance clearance which it has only given in ignorance of all the relevant circumstances…"

Hence once an assurance is legal, the Tribunal does not see why Uganda Revenue Authority cannot be estopped. It all boils down as to whether the taxpayer is seeking for tax mitigation or tax avoidance as understood under S. 91 of the ITA.

Where a representation or act is illegal, estoppel cannot operate. In *Minister of Agriculture and Fisheries v Matthews* [1950] 1 KB 148 at 154 Cassels, J held that:

> ".. an ultra vires act done by a statutory body whose powers is limited by the statute or statutes which brought it into existence and subsequently regulate its action is not an act at all…"

In *Golden Leaves Hotels and Resorts Limited and Apollo Hotel Corporation v Uganda Revenue Authority* Civil Appeal 64 of 2008, the Court of Appeal held that the principle of estoppel can neither be used as a sword nor a shield against a statutory provision. The court cited the case of *York Corporation v Henry Leethan & Sons Ltd.* [1924] All. E.R. Rep 477 where it was held that:

> "A body charged with statutory powers for public purposes is not capable of divesting itself of those powers or of fettering itself in their use, and an agreement by which it seeks to do so is ultra vires and void. Such an ultra vires agreement cannot [be] intra vires by reason of estoppel, lapse of time, ratification, acquiescence, or delay..."

The Court of Appeal also cited the case of *Marine Electric Company Limited v General Diaries Limited* [1937] A.C. 610 at 620 where the House of Lords held:

> "….where the statute imposes a duty of a positive kind, not avoidable by the performance of any formality, for the doing of the very act which the plaintiffs seeks to do, it is not open to the defendant to set up an estoppel to prevent it… an estoppel is only a rule of evidence which under the certain special circumstances can be invoked by a party to an action; it cannot therefore avail

> such a case to release the plaintiff from an obligation to obey such a statute, nor can it enable the defendant to escape from a statutory obligation of such a kind on his part. It is immaterial whether the obligation is onerous or otherwise to the party suing. The duty of each party is to obey the law…"

In *K.M. Enterprises and others v Uganda Revenue Authority* [2008] UGCommC 21 the court had this to say:

> "These English cases set out the accepted position of the law within this jurisdiction with regard to the exercise of statutory powers. Exercise of statutory powers and duties cannot be fettered or overridden by agreement, estoppel, lapse of time, mistake and such other circumstances. To hold otherwise would be to suggest that an agreement between the parties can amend an Act of Parliament, and thus change what Parliament ordained by allowing the defendant's servants to choose to act, or operate outside or contrary to the provisions of the law, will-nilly. And that cannot be."

In *Pride Exporters Ltd V Uganda Revenue Authority* HCCS 563 of 2006 Justice Geoffrey Kiryabwire stated that a statutory body like the Uganda Revenue Authority when given powers under a statute cannot have those powers fettered or overridden by estoppel or mistake. He further went on to state that the act by the Commissioner General was clearly ultra vires and cannot stand. Such an act amounted to no act at all under the law and the doctrine of estoppel is not applicable in this regard.

The applicants had problems by the respondent's use of English, US and Canadian authorities. They argued, which the Tribunal agrees with, that the said authorities are not binding but persuasive. The Tribunal has combined some of the said authorities with those made by Uganda courts. This is to confirm that the said authorities were not only persuasive but were convincing to the extent that they were applied by the Ugandan courts. Likewise where we cite an authority, there should be no doubt that the Tribunal found the said authority convincing.

Coming back to the issue at hand, the question is, was Article 23.5 of the EA2 PSA *intra vires* or *ultra vires*? The Tribunal has already held in issue 1.2 that it was ultra vires. We referred to the decision, inter alia, of His Lordship Madrama in *Kampala Nissan Uganda Limited V Uganda Revenue Authority* Appeal 7 of 2009, [2011] UGHC 80, which we would like to repeat:

> "For emphasis I need to state that no tax can be imposed except under the authority of an Act of `Parliament neither can an authority waive tax except under a law enacted by Parliament."

He further stated that:

> "Disobedience to a statute enacted in public interest and couched in mandatory language in terms of what it commands to be done renders anything done in disobedience of the statute null and void."

Therefore if Article 23.5 of EA2 PSA was ultra vires, no act at all, then the applicants cannot rely on the doctrine of estoppel so as to create a tax liability.

However the applicants argued that the respondent is estopped by the principle of legitimate expectation. The applicants argued that:

> "Legitimate expectation is [thus] firmly established as the public law principle where a state (or its agency) has represented that it will act in a particular manner (contrary to a statutory rule and even if acting ultra vires) where the individual is entitled to expect that the state will keep its words."

Legitimate expectation arises from a conduct, practice or treatment whereby one reasonably expects a benefit to arise. In the Kenyan case of *Republic and others v Attorney General and another* [2006] 2 EA 265 the court commenting on legitimate expectation stated:

> "A legitimate expectation arises where a person responsible for taking a decision has induced in someone who may be affected by the decision a reasonable expectation that he will receive or retain a benefit or that he will be granted a hearing before the decision is taken..."

In the English case of *Council of Civil Services Unions v Minister for Civil Service* [1985] AC 374 Lord Fraser said:

> "A legitimate expectation may arise from an express promise given on behalf of a public authority or from the existence of a regular practice which the claimant can reasonably expect to continue."

He continued that:

> "Legitimate expectations such as are now under consideration will always relate to a benefit or privilege to which the claimant has no right in private laws, and it may even be to one which conflicts with his private law rights.

In *re Preston* [1985] AC 1835, it was held that:

> "...unfairness in the purported exercise of a power could amount to an abuse or excess of power if it could be shown that the Commissioners had been guilty of conduct equivalent to a breach of contract or breach or representation."

The principle of legitimate expectation arose from the need to ensure fairness in transactions involving public authorities and other persons. The applicants' whose right to an exemption,

arising from private contractual law rights under the EA2 PSA, being extinguished by the public doctrine of estoppel, wish to rely on the principle of legitimate expectation. The applicants argued that "the exercise of a statutory power must be restricted where to exercise it would frustrate a legitimate expectation." In essence, the respondent's attempt to invoke the exercise of the ITA against the applicants should be restricted by the legitimate expectation the latter had by virtue of the purported exemption granted by Article 23.5 of the EA2 PSA.

The applicants attempted to merge the principle of estoppel with that of legitimate expectation though they accept that the principles are not the same. The word 'estop' is defined by *Black's Law Dictionary* (supra) at p. 589 as "*vb*. To bar or prevent by estoppel". It is clear that 'estop' is used when referring to estoppel. We think that attempt by the applicants to use the word 'estop' so as to merge the principle of estoppel with that of legitimate expectation is to attempt to effect a 'marriage of convenience' that is aimed at creating confusion in the application of the two different principles. The principle of legitimate expectation is wider than of estoppel. It is aimed at ensuring fairness in the administration of public affairs by public bodies, while estoppel is a rule of evidence that can be used in private affairs. While estoppel is a shield, the doctrine of legitimate expectation may be used as a sword.

Both parties do not dispute that the principle of legitimate expectation is part of the laws of Uganda. What is in dispute is whether the applicants can rely on it to avoid paying taxes. The principle of legitimate expectation is a common law principle. S. 14 (2) of the Judicature Act allows the High Court, in the exercise of its jurisdiction, to apply subject to written law, common law and doctrines of equity. The High Court is a court of record. The law that is applicable in High Court is also applicable in the Tax Appeals Tribunal.

According to J.L Caldwell: "Legitimate Expectation and the rules of natural justice", the concept of legitimate expectation was first implanted in administrative law by Lord Denning in *Shmidt v Secretary of State for the Home Department* [1969] 2 Ch. 149, in a case where alien students of "Scientology" were refused extensions of their entry permits without being given a fair hearing. In his judgement, Lord Denning proffered the view that the application of rules of natural justice depended on "...whether he has some right or interest or I would add, some legitimate expectation, of which it would not be fair to deprive him without hearing what he has to say." J.L.

Caldwell stated in this way, the “notion was introduced without any analysis or fanfare.” In a dissenting opinion, in *Breen v Amalgamated Union of Engineering,*[1971] 2 Q.B. 175 (CA) Lord Denning declared that: “if a person has some right or interest or some legitimate expectation of which it would not be fair to deprive him without a hearing or reasons given then these should be afforded him...” The doctrine of legitimate expectation was nurtured by Lord Denning.

It is apparent that the doctrine of legitimate expectation arose sometime around 1969. As to how a common law doctrine that arose in the late 1960s can be applicable to current Uganda (which got independence in 1962), none of the counsel addressed the Tribunal on that. However, since the Tribunal notes that both counsel are agreeable on its application in Uganda, it will not rock the boat any further. After all, it is a principle arising from natural justice whose principles cannot be exhaustively articulated.

The applicants argued that they are entitled to fair treatment by the respondent in respect of the promise to grant them an exemption. In *IRC v National Federation of Self Employed and Small Business* [1981] STC 260 at 279, Lord Scarman said:

> “the modern case law recognises a legal duty owed by the Revenue to the general body of taxpayers to treat taxpayers fairly, to use their discretionary powers, so that, subject to the requirements of good management, discrimination between one group of taxpayers and another does not arise, to ensure that there are no favourites and no sacrificial victims. The duty has to be considered as one of several arising within the complex care and management of a tax, every part of which it is their duty, if they can to collect.”

Mr. Richard Inch, in paragraph 10.5 of his witness statement alludes to a tax exemption granted to Bidco, another investor. The applicants feel that if exemptions are granted to other companies, why should they be denied one if it is in the EA2 PSA. Unfairness may arise from unjustified unequal treatment of taxpayers. However, the circumstances to which an exemption was made to Bidco, the criteria and the law under which it was granted, are not clear. This was not substantiated to the satisfaction of the Tribunal for it to find that there was unfairness in the failure to grant an exemption to the applicants when one was granted to Bidco.

The application of the principle of legitimate expectation is not absolute. In *Council of Civil Service Unions v Minister for the Civil Service (supra)* the court was of the view that the Minister

had shown that her decision had in fact been based on considerations of national security that outweighed the applicant's legitimate expectation of prior consultation. In re *Preston* (supra) the court held:

> "that a taxpayer cannot complain of unfairness, merely because the commissioners decided to perform their statutory duties under section 460 to make an assessment and to enforce a liability to tax. The Court cannot in the absence of exceptional circumstances decide to be unfair that which the Commissioners by taking action against have determined to be fair."

In order to apply the principle of legitimate expectation, the Tribunal has to determine whether there was unfairness in the decision of the respondent, and whether there are exceptional circumstances.

The respondent merely enforcing its statutory duty to impose a liability to pay tax on the applicants may not be unfair especially where the liability is set by statute. There are a number of court decisions as to the effect of *ultra vires* acts on the application of the principle of legitimate expectation. In *Al Fayed and others v Advocate General for Scotland* [2004] S.T.C 1703, the court noted:

> "...under our domestic law a legitimate expectation can only arise on the basis of a lawful promise, representation or practice. There can be no legitimate expectation that a public body will continue to implement an agreement it has no power to do so. In our opinion, the petitioners could not have had a legitimate expectation that the respondents would have adopted a course of action which was outwith their powers, and continued to maintain a contract which was unlawful. While the petitioners may well have had an expectation, it was not, in the particular circumstances of this case and according to our common law, a legitimate expectation. Accordingly, we consider that the petitioner's case based on a breach of legitimate expectation must fail."

In *R v Inland Revenue Commissioners ex parte MFK Underwriting Agents Limited* [1989] S.T.C. 873 at 892, the court stated that:

> "Every ordinary sophisticated taxpayer knows that the Revenue is a tax-collecting agency, not a tax-imposing authority. The taxpayers' only legitimate expectation is, prima facie that he will be taxed according to statute, not concession or a wrong view of the law. ... 'One should be taxed by law, and not be untaxed by concession'."

The same court at p. 895 stated that:

> "It was argued for the applicants in the present case that unfairness amounting to an abuse of power could arise in any circumstances in which the Revenue had created a legitimate expectation in the mind of the taxpayer about how his affairs would be approached if, after he acted on that expectation, the Revenue resiled from the undertakings it had previously given. Such conduct would be unfair and an abuse of power and subject to estoppel within the principles laid down in Preston.
>
> 'Legitimate expectation' has been considered in a number of authorities. ... The correct approach to 'legitimate expectation' in any particular field of public law depends on the relevant legislation. In *R v A-G, ex p Imperial Chemical Industries plc* (1986) 60 TC 1, the legitimate expectation of the taxpayer was held to be payment of the taxes actually due. No legitimate expectation could arise from an ultra vires relaxation of the relevant statute by the body responsible for enforcing it. There is in addition the clearest possible authority that Revenue may not 'dispense' with relevant statutory provisions...
>
> ...
>
> I accept without hesitation that (a) the Revenue has no dispensing power, and (b) no question of abuse of power can arise merely because the Revenue is performing its duty to collect taxes when they are properly due."

In *Republic v National Environment Management Authority ex-parte Sound Equipment Limited* [2010] eKLR, the court stated that (p. 8-9):

> "A legitimate expectation cannot arise where the respondent had acted contrary to, i.e. the law...
>
> The law can not allow an individual to retain a benefit which is the subject of the legitimate expectation, if creating or maintaining the benefit is beyond the power of the public body or officer."

In *Republic v The Disciplinary Committee & another Ex-parte Prof. Paul Musili Wambua* [2013] eKLR, the court stated:

> "I would add that for an applicant to cite legitimate expectation, the promise made must be within the jurisdiction of the party making it. An illegal promise cannot be relied upon to form a claim for legitimate expectation."

In *Regina v Secretary of State for Education and Employment*, *Ex parte Begbie* 2000 1 W.L.R. 1115, the court in dismissing the appeal held that:

> "the courts would not give effect to a legitimate expectation if it would require a public authority to act contrary to the terms of a statute."

The above authorities are self-explanatory and do not need any further comments from the Tribunal.

The Tribunal has had the opportunity to read the above authorities. It notes that the said authorities are from court decisions outside Uganda. The applicants are apprehensive of the use of authorities from abroad. The said decisions are mostly persuasive. There are hardly any Uganda court decisions because the principle of legitimate expectation has not been addressed extensively before. However there is nothing wrong in relying on decisions from elsewhere especially where they are very persuasive. In *Attorney General v Musalu Musene and others* (supra) the Supreme Court noted:

> "We are of the considered opinion that the decisions in **HATTER** and **BEAUREGARD** from U.S.A and Canada, respectively, are very persuasive and ought to be applied in interpreting Article 128(7) of the Constitution."

If the Supreme Court sees no problem in applying authorities from courts of other jurisdictions in interpreting the Constitution, the Tribunal likewise sees no problem in relying on authorities from other jurisdictions.

In his letter of 17th September 2010, Exhibit A30, the Minister of Energy and Mineral Development wrote to Mr. Aidan Heavy the Chief Executive Officer of Tullow Oil Plc in respect of the acquisition of Heritage's interest and the farmdown of Tullow's interest inter alia as follows:

> "(iii) The transfer from Tullow to Total and CNOOC will attract capital gains tax as will be assessed by the Commissioner, Uganda Revenue Authority in accordance with the Laws of Uganda."

Mr. Aidan Heavey acknowledged receipt of the said letter in his letter of 19th September 2010. He did not object to the payment of capital gains tax. He merely stated that "Tullow will require clarification of the tax due by Tullow on its sale to Total and CNOOC..." In a letter of 1st October 2010 to the Minister, Mr. Graham Martin stated that:

> "Tullow has been seeking confirmation that the exemption from taxes enshrined in the EA2 PSA will be respected. This sanctity of contract is of critical importance to Tullow and its new partners."

From the above correspondences, the applicants cannot say that they did not expect to pay capital gain taxes in accordance with the laws of Uganda. Rather they preferred to abide to sanctity of contract. A contract cannot override a statute. Any expectation to the contrary would not be in line with the law and is not legitimate.

Even in the SPAs the applicants made with Total and CNOOC, the applicants were aware about the obligation to pay capital gains tax. Under Clause 11.2(b) of the SPAs dated 29th March 2011 it was provided that Tullow shall be responsible for and "shall pay any or all Tax in the nature of income, turnover, capital gains or similar taxes payable on or in respect of the transactions contemplated by this Agreement..." Hence it cannot be said that Tullow did not expect to pay capital gains tax.

The Tribunal notes that the respondent is a tax collecting body. Its mandate is to collect taxes according to the relevant statutes and law. The applicants seek to cite an expectation arising from Article 23.5 of the EA2 PSA that they will not purportedly pay capital gains tax from a sale of their interests in Block EA2. The said promise was done in contravention of the ITA. Hence it was not lawful. The Tribunal does not see any unfairness in the decision of the respondent to implement the ITA provisions against the applicants. The applicants, only legitimate expectation is that they should be taxed according to the ITA and not a wrong interpretation of the law. Any such promise or representation under Article 23.5 of the EA2 PSA cannot be relied upon to form a claim for legitimate expectation. A promise made on an illegal claim cannot form the basis of a legitimate expectation. It is an illegitimate expectation which the Tribunal cannot uphold.

Before the Tribunal can leave issue 1.5, it noted that the applicants cited the international law principle of *pacta sunt servanda* which requires those entering into contracts to honour their obligations. *William W. Bishops, Jr. "International Law: Cases and Materials"* 2nd Edition p. 133 states that: "One of the most fundamental rules of international law is that treaties must be performed in good faith; the rule of *pact sunt servanda.*" The applicants have not convinced the Tribunal that the EA2 PSAs are international agreements or treaties. The Constitution requires international agreements to be ratified by the cabinet. The applicants have also not convinced the Tribunal that they are international bodies. In the absence of any satisfactory submission, the Tribunal will not labour much to address the application of *pacta sunt servanda* in this application.

6.2 REINVESTMENT RELIEF/ INVOLUNTARY DISPOSAL

The applicants called a number of witnesses who gave testimony to the effect that Tullow did not wish to dispose of 66.67% but 50% of its interests. According to AW1, Mr. Graham, Tullow acquired Heritage's interests in EA1 and EA3A with the intention of selling them. It had wished to sell 50% of its interests in each of the PSAs. However the GOU would not give its consent to a sale to only one party. There was pressure from the GOU for the Tullow to break the monopoly in oil exploration. Mr. Graham informed the Tribunal that Tullow was forced to sell an extra 16.67% of its interests. Tullow sold 66.67% of its interests in each of the PSAs to CNOOC and Total on 21st February 2012, each purchaser taking 33.33% of the interests. There was no official communication that Tullow should sell 66.67% of its interests. However there were several meetings with GOU officials at different levels where it was indicated that Tullow should retain a third of its interests.

Mr. McDade, the Chief Operating officer of Tullow, testified that the GOU indicated to the senior Tullow executives that a 50% farmdown would not be acceptable to it. The GOU wanted to avoid a monopoly. He testified that Mr. Richard Inch emailed to him about a conversation he had with Mr. Kiiza, the Director of Economic Affairs, that the GOU would not allow a 50% split. Mr. McDade contended that the disposal of 16.67% was therefore an involuntary disposal. He testified that Tullow was planning to reinvest considerable sums from the farmdown proceeds in assets of a like kind within one year from the disposal of the Heritage interests. Mr. McDade told the Tribunal that the intention to sell 50% of its interest was not expressed in any form of board resolution. Furthermore, he testified that there was no correspondence between GOU and Tullow that indicated that the latter wanted to sell 50% of its interest. He stated that there was a draft SPA which was on a 50:50 basis made in February 2010. Mr. McDade admitted that he did not clearly understand what a re-investment relief was.

AW3, Mr. Richard Inch, the Head of Tax at Tullow, also told the Tribunal that Tullow had intended to sell 50% of the interests in EA1, EA2, and EA3A. However before the GOU would grant the necessary consent, it required Tullow to sell a further 16.67% of its interest. He stated that in a meeting of the 2nd February 2010 with Mr. Lawrence Kiiza the Director of Economic Affairs, he told him that GOU was not going to allow a sale of only 50% of Tullow interests and it wanted a single distinct operator for each PSA, with each taking 33.33% interests.

The respondent's first witness, RW1 Mr. Rubondo, testified that the GOU did not indicate to Tullow who to sell to, but the GOU wanted to avoid a monopoly in the Albertine Graben. He stated that Tullow decided on the percentages to sell in the three EAs.

The respondent's second witness, Mr. Kajubi objected to the applicants' entitlement to reinvestment relief. Mr. Kajubi stated that the respondent did not get any evidence of an involuntary disposal. In order for an involuntary disposal to take place, it must be done against one's will. Tullow was willing to sell its interests. There was no evidence to show that Tullow was forced to sell the extra 16.67% of its interest. According to Mr. Kajubi, what was required to prove involuntary disposal would be a letter, a decree or something in writing. Secondly, the proceeds of involuntary disposal should be reinvested in an asset of a like kind. This should be done within one year of the disposal. He contended that the transaction was concluded in March 2012 and Tullow had not re-invested in an asset of a like kind.

Having read and listened to the evidence and perused the submissions, the Tribunal notes the following in respect to involuntary disposal. S. 54(1) (C) of the ITA reads that no gain or loss shall be taken into account in determining chargeable income in relation to an involuntary disposal of an asset to the extent to which the proceeds are reinvested in an asset of a like kind within one year of the disposal. As the respondent noted for S. 54 of the ITA to apply, the following conditions must be satisfied:

1. There has to be an involuntary disposal,
2. There has to be a reinvestment,
3. The reinvestment must be in an asset of a like kind,
4. The reinvestment must be made within one year of disposal.

In order to determine whether the applicants made an involuntary disposal one has to discern the intention of the Act. There is no definition of involuntary disposal under the ITA. However, the definition of the term can be obtained by using rules of statutory interpretation. *Black's Law Dictionary* 9th Edition p. 539 defines a 'disposition' as "the act of transferring something to another's care or possession, esp. by deed or will; the relinquishing of property. 'Involuntary' is defined (at p. 908) as "not resulting from a free and unrestrained choice; not subject to control by will." Combining the said definitions, an involuntary disposal would arise out of one parting

with the possession or transferring ownership of something resulting not out of his or her choice or free will. In *URA V Bank of Baroda – India* HCT-00-CC-CA-05-2005, the court noted that "This letter does not show that the shareholder had a free will to decide what time to float shares even having regard to market conditions." Taking this into mind, as counsel for the applicants noted an involuntary disposal does not have to be done using force. A disposal to be involuntary does not need to involve coercion. The presence or absence of the element of free will or choice is an important ingredient in determining whether there has been an involuntary disposal.

In *Woolwich Building Society V Commissioners of Inland Revenue* 65 TC 265 where involuntary disposal was broadly interpreted, the court noted that:

> "It, is, in my view, necessary for the plaintiffs to do more than point to the provisions of the statute. They must show that the Crown by its servants was exercising, or threatening to exercise, powers under the statute in such a way as to constitute compulsion in law. A threat of proceedings for a pecuniary benefit does not make a payment thereafter involuntary; for the payer might have defended the proceedings and relied upon the unlawfulness of the demand (William Whiteley Ltd. v The King and Werrin v The Commonwealth). But a payment made under pressing necessity to avoid a seizure of goods, or to obtain the release of goods unlawfully detained, or to prevent some interference with or withholding of a legal right, is compelled and not voluntary and is recoverable in an action for money had and received."

A disposal may be a result out of a pressing necessity to prevent interference or enjoyment of one's legal rights or ownership.

A disposal can arise out of two circumstances. Firstly, it is a result of third party acts or through acts of God. Examples in point are where an asset is stolen or destroyed by fire or hit by lightening. The owner who had insured the item may obtain indemnity from the insurance company. The second circumstance may arise where the taxpayer disposes of the item but does not have a choice. To amount to an involuntary disposal, it is sufficient to show that a party though unwilling to dispose of an interest or had any intention to dispose of it, had no option but to dispose of it,

Having discussed what amounts to an involuntary disposal the question is, did the applicants disposal of 16.67% of their interests amount to an involuntary disposal? The Tribunal notes that there was no official communication from the GOU to the applicants to sell 66.67 % of their

interests. By official communication, it is understood to mean a letter or correspondence from GOU. There was no board resolution. There were also no minutes of a meeting to show that the applicants and GOU agreed that the former should sell the extra 16.67% of their interests. In fact, if there was a meeting where the parties agreed so, the Tribunal thinks the sale would not amount to an involuntary disposal. Mr. Graham testified that "there were several meetings with government officials at different levels where it was indicated that the applicants should retain a third of their interests." With due respect to Mr. Graham's testimony, though GOU is a legal entity it is not a physical one. Meeting Government is a myth. One can only meet its officials and agents. Mr. Graham did not inform the Tribunal which government officials the applicants met and who represented the applicants. The Tribunal will ignore the said evidence from Mr. Graham.

In the witness statement of Mr. Graham, he went at length to show that Tullow did not wish to sell more than 50% of their interest. This showed that Tullow had the intention of selling 50 % of their interest. The said evidence was not rebutted. Mr. Inch testified that he met Mr. Lawrence Kiiza the Director of Economic Affairs, who informed him that the GOU would not allow a 50% split. The GOU wanted the applicants to maintain 33.33% interest. There was an email to that effect by Mr. Inch to Mr. McDade. Mr. Lawrence Kiiza did not testify and rebut the said testimony. If the said testimony is uncontroverted it should be taken as the truth. Under S. 133 of the Evidence Act, no particular number of witnesses shall be required for the proof of any fact. Mr. Inch's evidence if unchallenged may suffice. There is no need to look at minutes of meetings or board resolutions. The Tribunal notes that the applicants testified that they would not sell their interest without GOU consent. Looking at the circumstances of the case, it can be seen that the sale of the 16.67% of their interest was not out of the applicants' choice or free will. The Tribunal feels that such a disposal amounted to an involuntary disposal.

The tribunal has already noted for an involuntary disposal to entitle one to a reinvestment relief, three other conditions have to be satisfied. The Tribunal will summarise the three conditions in one sentence. The taxpayer ought to have made a reinvestment, in an asset of a like kind, within one year from the date of disposal. Did the applicants meet these conditions?

The Tribunal notes that the respondent issued assessment SA/LTO/2569 of US$ 390,924,460 and assessment SA/LTO/2570 of US$ 84,999,660 on TUL and TUOP respectively on the 18th October 2010. On the 1st December 2010, the applicants objected to the assessments. On the 24th February 2011, the respondent made an objection decision. On the 25th March 2011, the applicants filed an application for review before the Tax Appeals Tribunal (TAT) challenging the objection decision. The SPAs between Total, CNOOC and the applicants were made on the 29th March 2011. So by the time the assessments were issued and the matter filed in the Tribunal the sale of the applicants' interests had not taken place.

In order to ascertain the date when the applicants disposed of their interests, one has to look at the SPAs they entered with CNOOC and Total on the 29th March 2011. Under Clause 2.1 of both SPAs the transfer as between the parties shall be deemed effective on and from the Effective Date. Effective Date was defined under Clause 1.1 to mean "00.01 hours (United Kingdom time) on 1st January 2010". Clause 4 of the Agreement dealt with the completion of transfer. Under Clause 2.2 of both SPAs, the obligations of the parties under Clause 2.1 and Clause 4 were conditional on the satisfaction of the Minister's consent having been duly obtained. Hence the effective date of the transaction and completion of the transfer were subject to the Minister's consent. The Minister's consent in respect of the farmdown of interest and transfer of operatorship (Exhibit A48) was obtained on the 15th February 2012. In the said letter the Minster looked forward to the applicants closing the transaction.

We already stated that completion of the transfer was provided for under Clause 4 of the SPAs. Under Clause 4.2 of the SPA:

> "Immediately upon the fulfilment of Tullow's obligation under Clause 4.1 the purchaser shall pay to them the interim consideration, minus the deposit (which Tullow shall become entitled to retain absolutely), by means of a direct transfer..."

The only way the completion of the transfer could be seen was by payment of the interim consideration. According to Mr. Graham the applicants eventually sold 66.67% of their interests in each of the PSAs to CNOOC and Total on 21st February 2012, each purchaser taking 33.33% of the interests. In a letter dated 21st February 2012, Exhibit A49, Mr. Eoin Mekie wrote to the Minister of Energy and Mineral Development indicating the completion of the farmdown, payment of taxes and transition of operations. This could have been immediately after the date

the purchasers paid the consideration. This date was not disputed by the respondent. Hence the Tribunal will take the 21st February 2012 as the date of the completion of the transfer or disposal. The applicants filed the application before the Tribunal, on the 25th March 2011, at a time when the transaction had not taken place. The respondent issued assessments on the 2nd November 2012 against the applicants totalling to US$ 467,271,974. The Tribunal started listening to the applicants' case on the 26th November 2012. The applicants closed their case on the 28th November 2012. The applicants had one year from the 21st February 2012, which period lapsed on the 13th February 2013, as to make a reinvestment in asset of a like kind. At the time the applicants closed their case, they were within the time period to make a reinvestment in an asset of a like kind. Hence it was premature for the applicants to adduce evidence of a reinvestment in an asset of a like kind. The applicants by the nature of this application could not fulfil the last three conditions. In the interest of justice the Tribunal will extend period by the applicants to make a reinvestment of an asset of a like kind within a period of one year from the date of the transaction.

6. 3 COMPUTATION OF TAX LIABILITY.

(i) WHAT DID THE APPLICANTS DISPOSE OF?

One of the most contentious sub-issues was what did the applicants dispose of. This is because the description of what was disposed of determines the gain or loss made and ultimately the tax liability. The applicants argued the issue of undivided interests was not an agreed one, it should be struck out. Issues can be added at any time of a trial as long as they do not cause prejudice to any parties. The Tribunal notes that both parties have addressed the said issue. Since it is a bone of contention and forms a basis in calculation of the gain or loss it cannot be ignored.

The applicants contended that they purchased the Heritage's 50% interests in exploration areas EA1 and EA3A with the intention of selling them. They argued that what they sold first was Heritage interests and then their original interests in EA2. The applicants used a 'last in first out' approach. The respondent objected to the applicants' approach and argued that the interests sold by the applicants were indivisible. Hence if the interests are indivisible, they argued, that the applicants are not in a position to "pick and choose" which interests they sold. They argued

that “it is not possible to treat portions of an undivided interest as separate and distinct assets”. The respondents contended that the best approach would be one of “first in first out”.

In the case of *Heritage Oil and Gas Limited v Uganda Revenue Authority* TAT Application 26 of 2010, the Tribunal noted that what was sold can only be ascertained by looking at the four corners of the pages comprised in the Sale and Purchase Agreement (SPA). What did the parties agree to buy and sell? In *Stanton v Drayton Commercial Limited* 1983 AC 501 the House of Lords focused on what was in the agreement. At page 508, the court noted:

> “The vendor [Eagle Star] will sell and the purchaser [the taxpayer company] will purchase all the securities in the said portfolio at the price of [pounds] 3,937,962 to be satisfied by the allotment by [the taxpayer company] to [Eagle Star] of 2,461, 226 ordinary shares of 25p each in [the taxpayer company], the issue price of each share for the purpose of satisfying the consideration being 160p.”

Hence in order to determine what was sold one has to look at the SPAs of the parties.

There were four SPAs dated 29th March 2011 in respect of the sale of the interests. Two were for the sale by Tullow to Total and two to CNOOC. Clause 2.1 of all the SPAs (Exhibits A19 and A20) between the applicants, CNOOC and Total read:

> “Subject as herein provided, Tullow hereby agrees to sell and transfer all of its legal and beneficial right, title and interests in and to the interest free from all Encumbrances whatsoever relating thereto (subject to the provisions of the Interest Documents) with full title guarantee to Purchaser for the consideration referred to in Clause 3.1 and Purchaser hereby agrees to purchase and acquire the interest.”

Clause 1.1 of the first two SPAs in respect of the sale of interests in only Block 2 to CNOOC and Total define interest as:

> “means an undivided eight point three three three three three percent. (8.3333%) legal and beneficial participating interest in Block 2, in and under the interest documents and all rights and obligations attaching thereto, including, but without limitation, such interest in the Interest Property and the Interest Data;”

Clause 1.1 of two of the SPAs in respect of the sale of interests in Blocks 1, 2 and 3A defines interest as:

(a) an undivided thirty three point three three three three percent. (33.3333%) legal and beneficial participating interest in Block 1(which shall comprise the Heritage Oil Block 1 Interest and the Pre-Existing Block 1 Interest);

(b) an undivided twenty five per cent. (25.0000%) legal and beneficial participating interest in Block 2: and

(c) an undivided thirty three point three three three three per cent. (33.3333%) legal and beneficial participating interest in Block 3A (which shall comprise the Heritage Oil Block 3A Interest and the Pre-existing Block 3A interest);

in and under the Interest Documents and all rights and obligations attaching thereto, including, but without limitation, such interest in the Interests Property and the Interests Data;

According to the first set of the SPAs, Tullow sold 8.6666% of its interest to CNOOC and Total. In the second set of SPAs Tullow sold its 66.6666% in Block 1 and Block 3A. In Block 2 Tullow sold 50% of its interest. The total interests Tullow sold were 66.67% as was adduced in evidence.

In order to determine what was included in the interests, Clause 2.1 defined "Interests Data" as follows, it

> "means all data, reports and other information held by Tullow relating directly to the Interests and forming part of the property jointly owned by Tullow and each party to each Joint Operating Agreement in accordance with its terms, but excluding all internal communications within Tullow and internal memoranda, reports, interpretations and documents created for Tullow's (or its affiliates') own use and excluding the Interest Documents;"

Clause 2.1 also defined "Interest Documents" as to:

> "mean the agreements, letters and other documents specified in Schedule1, Part 1;"

It then defines Interest Property as to:

> "means all of the property related to the Interests including any platforms, pipelines, plant, machinery, wells, facilities and all other offshore and onshore installations and structures."

In totality the interests sold included interests in data, documents and property.

The applicants alleged that they sold Heritage Oil Block 1 and 3A interests first and then Pre-Existing Block 1 and 3A interests. Heritage Oil Block interest was defined in all the SPAs by clause 1.1 as:

> "Heritage Oil Block 1 Interest" means an undivided twenty five per cent. (25.000%) legal and beneficial participating interest in Block 1 acquired by Tullow from Heritage Oil prior to the date hereof.
>
> "Heritage Oil Block 3A Interest" means an undivided twenty five per cent. (25.000%) legal and beneficial participating interest in Block 3A acquired by Tullow from Heritage Oil prior to the date thereof."

Pre-Existing Interests were defined as:

> "Pre-Existing Block 1 Interest" means an undivided eight point three three three (8.3333%) legal and beneficial participating interest in Block 1 held by Tullow and not acquired from Heritage Oil;
>
> "Pre-Existing Block 3A interest" means an undivided eight point three three three three (8.3333%) legal and beneficial participating interest in Block 3A held by Tullow and not acquired from Heritage Oil;"

A close perusal of Clauses 1.1 and 2.1 shows that the applicants purportedly sold all the Heritage Oil interests first and then the pre- existing/original Block 1 and Block 3A interests. According to the SPAs in respect of the sale of interests in Block 1, 2 and 3A all the interests (100%) acquired by Tullow from Heritage were sold to CNOOC and Total. Out of the 66.67% interest sold by Tullow to the CNOOC and Total 50% was Heritage interest and 16.67 % was pre-existing interests.

Taxpayers are allowed to arrange their affairs in such a way that they pay less tax. *In Levene V IRC* [1928] A.C. 217 it was stated by Viscount Sumner that:

> "it is trite law that His Majesty's subjects are free, if they can, to make their own arrangements, so that their cases may fall outside the scope of the taxing Acts. They incur no legal penalties and, strictly speaking, no moral censure if, having considered the lines drawn by the Legislature for the imposition of taxes, they make it their business to walk outside them..."

However for one to arrange his affairs in such a way he must comply with the law. Hence the applicant's interpretation of their sale can be acceptable as long as it is in line with the law.

However, S. 91 of the ITA allows the Commissioner to re-characterise a transaction. S. 91 of the ITA reads:

> (1) For the purposes of determining liability to tax under this Act, the Commissioner may-
>
> (a) re-characterise a transaction or an element of a transaction that was entered into as part of a tax avoidance scheme:

(b) disregard a transaction that does not have a substantial economic effect; or

(c) re-characterise a transaction the form of which does not reflect the substance.

(2) A "tax avoidance scheme" in subSection (1) includes any transaction, one of the main purposes of which is the avoidance or reduction of liability to tax.

Prof. D.J. Bakibinga *Revenue Law in Uganda* page 165 defines tax avoidance as:

> "…. some act by which a person arranges his affairs that he is liable to pay less tax than he would have paid but for the arrangement. Consequently the situation which he brings about is one which he is legally in the right, except so far as some rule may be introduced that puts him in the wrong."

According to S. 91(2) if the Commissioner feels the transaction entered into by a taxpayer has been entered into with the intention of reducing tax liability, he or she may exercise his powers under S.91 (a) of the Act and re-characterise it. Under S. 91(1) (b) the Commissioner may re-characterise a transaction where the form does not reflect the substance.

The respondent's contention can be summarised as twofold. The first argument as stated in the evidence of Mr. Kajubi is that the applicants structured their transaction in a way that they created a 'fictitious loss'. The second contention is to the effect that what the applicants sold as indicated in the SPA were indivisible. Undivided interest is defined by *Black Law Dictionary* 8th Edition p. 829 as "an interest held under the same title by two or more persons, whether their rights are equal or unequal in value or quantity." The applicants sold what were intangible assets, so how could they have determined what was sold.

The powers to re-characterise under S. 91 of the Income Tax Act are discretionary. The Tribunal cannot interfere with the Commissioner's exercise of his powers unless he exercised them illegally, irrationally or without procedural impropriety. In *Twinomuhangi Pastoli V Kabale District Local Government Council, Katarishangwa Jack & Beebwajuba Mary* [2006] 1 HCB 30 Kasule Ag. J. (by then) held inter alia that;

> "2.Illegality is when the decision making authority commits an error of law in the process of taking the decision or making the act, the subject of the complaint. Acting without jurisdiction or ultra vires, or contrary to the provisions of a law or it's principles are instances of illegality.
>
> 3. Irrationality is when there is such gross unreasonableness in the decision taken or act done, that no reasonable authority, addressing itself to the facts and the law before it, would have

made such a decision. Such a decision is usually in defiance of logic and acceptable moral standards.

4. Procedural impropriety is when there is failure to act fairly on the part of the decision making authority in the process of taking a decision. The unfairness may be in the non- observance of the rules of natural Justice or to act with procedural unfairness towards one to be affected by the decision. It may also involve failure to adhere and observe procedural rules expressly laid down in a statute or legislative instrument by which such authority exercises jurisdiction to make a decision."

The Tribunal has to ask itself, whether the Commissioner's disregard of the 'last in first out' method, and his use of the 'first in first out' method was illegal, or was it so irrational, or tainted with procedural illegality.

When one peruses Sections 91(1)(a) and 91(2) of the ITA one cannot avoid feeling that the framers of the Income Tax Act wanted to empower the Commissioner to shift goal posts when a tax payer is about to score. In other words, where a taxpayer uses mechanisms which may reduce its tax liability, the Commissioner is empowered to disregard them as long as it is plainly clear the taxpayer wanted to reduce its liability. It tilts the ground in determining tax liability in favour of the Commissioner. The Tribunal feels that where the law is clear it has to apply it as it is.

S. 91(1) (a) of the ITA allows the Commissioner to re-characterise a transaction where there is a tax avoidance scheme. It is not in dispute that the effect of the SPAs selling the purportedly Heritage interests first would be to restructure the payments and expenditures in such way that the gain for taxation purpose is minimal hence the tax liability would reduce. This would be as opposed as to when the payments and expenditures incurred in all the three blocks is evenly distributed or the 'first in first out' method is considered. One cannot deny that the applicants' purported sale of Heritage's interest first in Blocks 1 and 3A is an ingenious way of reducing tax liability. This is because when Heritage sold its interests in Blocks 1 and 3A to Tullow on the 26th January 2010 they ceased being Heritage's interests. They become Tullow's interests. In Clause 6.1(a) of the SPAs, Tullow warrants to the Purchaser that it is the legal and beneficial owner of the interest with the right to sell and transfer them to the purchaser. We have to call a spade a spade and not a big spoon. At the time, two years later, when Tullow sold its interests it was not holding powers of attorney for Heritage. The law deals with actualities and not suppositions. At

what point of time do the interests cease being Heritage interests and become Tullow interests, is it 2 years, 10 years or never? It should be at the time the sale is done and the transaction is completed. Between 2010 and 2012 when the interests of Heritage were acquired and when Tullow sold its interest a lot of water had flowed under the bridge. One cannot say that at time of sale the level of oil exploration, development, and the market forces in respect of oil in 2012 were the same as in 2010. Oil exploration is not static but dynamic. All these factors go to determine the nature of interests that were sold.

Under the SPAs, the applicants sold interest data, interest property and interest documents. The applicants sold indivisible interests. What the applicants sold were intangible assets. Intangible is defined by *Black's Law Dictionary 8th Edition* p. 823 as:

> "adj. Not capable of being touched; impalpable; INCORPOREAL.
>
> … n. Something that lacks a physical form; an abstraction, such as responsibility; esp., an asset that is not corporeal, such as intellectual property"

An intangible asset will always remain intangible. Labeling it does not make it tangible. In cross-examination when Mr. Inch was asked: "when you acquired 100% is there any way you could split and say this is for Tullow, this if for Heritage?" He answered, "No". The story would have been different if the applicants had sold a Block. For instance if the applicants had sold Block 1 to CNOOC and Block 3 to Total it would be clear what the applicants sold. However the applicants sold interests. An interest is not something that is tangible. For one to contend that with specificity what interests were sold would be tantamount to splitting atoms to determine which protons were sold. An example of how difficult it is to specify what intangible interests were sold is where one purchases one litre of unleaded petroleum and two litres of leaded petroleum mixes them and then sell one and half litres of petroleum. The said person cannot say that he sold one litre unleaded petroleum and a half a litre of leaded petroleum. To make such an allegation would be to descend in the realm of conjectures and abstracts. The law does not deal with illusions and fallacies. Therefore for the applicants to argue that they sold Heritage's interest first and then their pre-existing interests later is untenable. For contractual purposes parties may make the terms of the contracts as they wish, freedom of contract. However for tax purposes, the Uganda Revenue Authority has the powers to re-characterise a transaction to reflect the reality of the transaction. In *Weiss v Stearn*, Supreme Court (United States), 265 U.S. 242, Judgment dated 26th May 1924 the court noted that:

> "Questions of taxation must be determined by viewing what was actually done, rather than the declared purpose of the participants, and when applying the provisions of … income laws… we must regard matters of substance and not mere forms."

If the Uganda Revenue Authority did so, the Tribunal will not fetter its discretion.

In the US authority of *John K. McNulty and another v Commissioner of Internal Revenue*, T.C. Memo., 1988 – 274, the 2nd petitioner sold an undivided interest acquired from her ex-husband, Robert, to the 1st petitioner, John, the current husband. The 2nd petitioner, Babette, acquired the ex-husband's interest in the house for the purpose of selling it to the 1st petitioner, and was merely a conduit or agent for the ex-husband. The court noted that she took the title in her own name, and then waited for 6 months before deeding the one-half interest to the 1st petitioner. During that time, she was the owner, and could have disposed of the residence as she pleased. The court stated that "In appropriate circumstances a court will ignore the form of the transaction according to its substance." The court noted that "where we find the parties clearly intended the form they chose, and where that form had an obvious tax purpose". The court further noted that:

> "Moreover, Babette's and John's reporting of the sale does not comport with their 'conduit or agent' theory. Had Babette been a true conduit or agent, she would not have been considered the owner of Robert's interest at all, and would have had no gain, or even any sale, to report. Robert would be deemed to have sold the half interest to John."

The court held that:

> "A taxpayer who owns two undivided one half interests in property, received at different times, and disposes of an undivided one-half interest is deemed to have disposed of 50 percent of each of the halves he owned."

The Tribunal is mindful of the fact that the above case is an authority from the US. The Tribunal finds the said authority persuasive. The above authority dealt with undivided interests in immoveable property like the matter before the Tribunal. Like in the above authority, Tullow owned the purportedly interest of Heritage for a period of two years. During that time it could have disposed of the interest as it wished. Tullow chose the form it wished, which had an obvious tax purpose. If the Tribunal were to consider that Tullow was an agent for Heritage, Tullow would have no gain or loss to report of. The court would find it appropriate to ignore the form of the transaction and look at the substance. The acquisition of Tullow of different interests at different times shall be deemed to have been disposed proportionally to the number of blocks it owned.

S. 40 (1) of the ITA requires that a tax payer's method of accounting to conform to generally accepted accounting principles. Uganda already adopted International Accounting Standards. International Accounting Standard 2, inventories, IN13 is titled "Prohibition of LIFO as a cost formula". It reads: "The Standard does not permit the use of the last-in, first-out (LIFO) formula to measure the cost of inventories." Hennie Van Greuning, Darrel Scot and Simon Terbanche in *International Financial Reporting Standards* notes that:

> "IAS 2 does not allow the use of last-in, first-out (LIFO) because it does not faithfully represent inventory flows. The IASB has noted that the use of LIFO is often tax driven and concluded that tax considerations do not provide a conceptual basis for selecting an accounting treatment. The IASB does not permit the use of an inferior accounting treatment purely because of tax considerations."

In the circumstances, the Tribunal shall not use the LIFO method as a cost formula. This means that the Tribunal shall not accept the notion that the interests Tullow sold first were those of Heritage. The Tribunal also finds that the respondent's use of the 'first in, first out' (FIFO) is irrational like in the 'last in last out' (LIFO) method. If the interests were indivisible then how could the respondent determine which interests were purchased first and which interests were sold first. There is no reasonable justification as to why the respondent applied the FIFO method.

(ii) COMPUTATION OF CAPITAL GAIN ON TRANSFER OF INTEREST

In order to apply the provisions of the ITA, one needs to understand how the oil and gas sector works and the stage at which the oil operation in Uganda had reached at the time of the transfer of interests. It was an agreed fact that oil had been discovered in Uganda. However, there is no evidence that oil production had started. Oil exploration and production are upstream activities. Once oil is discovered, the considerable risk involved in oil exploration is removed. The costs involved in exploration are carried forward in the future where they can be recovered from revenue derived from production from the reserves. Hence the income tax provisions have to take into account the costs carried forward and to avoid a situation where there may be double deductions, losses incurred and excess costs.

The ITA provides for special provisions for the taxation of petroleum operations in Part IXA of the Act. Part IXA inter alia, deals with the transfer of an interest in a petroleum agreement. The relevant Section dealing with capital gain or loss in a transfer of interests in a Petroleum Agreement is S. 89G of the ITA which reads:

> "Where a contractor, in this Part referred to as the "transferor contractor" disposes of an interest in a petroleum agreement to another contractor or a person that as a result of the disposal will become a contractor in relation to those operations, in this Part referred to as the "transferee contractor
>
> (a) any excess costs under S. 89(2) attributable to the interest at the date of disposal, are deductible by the transferee contractor, subject to the conditions prescribed in that section;
>
> (b) the transferee contractor continues to depreciate any allowable contract expenditure attributable to the interest at the date of disposal in the same manner and on the same basis as the transferor contractor would if the disposal had not occurred;
>
> (c) the cost base for the purposes of calculating any capital gain or loss on disposal of an interest in a petroleum agreement will be determined in accordance with Part VI of this Act;
>
> (d) In a subsequent disposal of the whole or part of the interest disposed of under paragraph (c), the cost base for purposes of calculating any capital gain or loss on disposal is the amount of the transferor contractor's capital gain or loss on the prior disposal of the interest if any, less the sum of-
>
> (i) the excess costs up to the date of disposal that are deductible by the transferee contractor under paragraph (a);
>
> (ii) the depreciation of capital expenditure incurred up to the date of disposal that is deductible by the transferee contractor under paragraph (b); and
>
> (e) the amount of the transferor capital loss on the disposal of the interest, if any, is treated as income of the transferee contractor on the date of the transfer of the interest."

S.89A (1) of the ITA defines petroleum operations to mean "exploration operations, development operations and production operations authorised under a petroleum agreement." One wonders whether a transfer of interests under an SPA can be called an exploration operation, a development operation or a production operation under a petroleum agreement. The Tribunal does not think so. What is defined as exploration, development or production can be discerned from the activities whose expenditures are given in the Eight Schedule of the Act. A Contractor is defined under S.89A to mean a person with whom the Government enters into a petroleum agreement and includes a licensee. S. 89G deals specifically with "Transferee Contractor" and

“Transferor Contractor” which it defines to mean one who disposes and the person who will become a contractor as a result of the disposal respectively. A transfer of interest does not involve exploration, development or production. A transfer of interests under a PSA by an SPA cannot be considered as a petroleum operation under S. 89C. S. 89 B (3) provides that income earned by a contractor from activities other than petroleum operations shall be taxed in accordance with the Act. Hence, while Part IXA deals with petroleum operations and includes a transfer of interest under a petroleum agreement, the law in the ITA Part VI, in respect of capital gains applies as modified by S. 89G of the ITA. That is transferee contractors and transferor contractors are taxed in accordance with Part VI, as modified by Part IXA. The Tribunal does not see any inconsistency in applying Part VI of the ITA in respect of the initial disposal as it was provided by Part IXA. The inconsistency should be in respect to computation of the gains and not application of the parts.

Part IXA of the ITA, S. 89G deals with computation of the cost base and allowable deductions. S. 89G (a) provides for the deduction of any costs at the date of disposal. It provides for the computation of the cost base where there is a transfer of original interests under S.89G(c) and for subsequent disposal under S. 89G (d) of the ITA.

It is not in dispute that there were two disposals of interests in the transaction which before the Tribunal. The first disposal was the transfer of interest acquired by Tullow directly from the GOU which was an initial disposal of original interests. The second disposal was Tullow’s transfer of the interests acquired from Heritage to CNOOC and Total which is a subsequent disposal. S.89G deals with different computations for the calculation of the cost bases for initial disposals and for subsequent ones.

(a) Initial disposal/ disposal of original interests

In respect of the initial disposal or a disposal of original interests, S. 89G (c) provides that the cost base for purposes of calculating any capital gain or loss shall be determined in accordance with Part VI of the ITA.

Part VI of the ITA deals with gains and losses on disposal of assets. S. 49 of the ITA reads:

> "This Part applies for the purposes of determining the amount of any gain or loss arising on the disposal of an asset where the gain is included in gross income or the loss is allowed as a deduction under this Act."

S. 50 of the ITA specifically deals with gains and losses on a transfer of an asset. It reads:

> "(1) The amount of any gain arising from the disposal of an asset is the excess of the consideration received for the disposal over the cost base of the asset at the time of the disposal.
>
> (2) The amount of any loss arising from the disposal of an asset is the excess of the cost base of the asset at the time of the disposal over the consideration received for the disposal."

S. 52 of the Act deals with the determination of cost base. The relevant sections read:

> "(1) Subject to this Act, this Section establishes the cost base of an asset for the purposes of this Act.
>
> (2) The cost base of an asset purchased, produced or constructed by the taxpayer is the amount paid or incurred by the tax payer in respect of the asset, including incidental expenditures of a capital nature incurred in acquiring the asset, and includes the market value at the date of acquisition of any consideration in kind given for the asset.
>
> …
>
> (6) Unless otherwise provided in this Act, expenditures incurred to alter or improve an asset -which would not have been allowed as deductions are added to the cost base of the asset."

The cost base of the original interests is therefore determined taking into consideration S. 52 of ITA. S. 52 of the ITA allows in the calculation of the cost base to include incidental expenses of a capital nature incurred in acquiring the asset when disposing original interests.

S. 89G (a) modifies Part VI of the ITA by allowing excess costs under S. 89C (2) attributable to the interest to be deducted from the cost base at the time of disposal. S. 89C (2) of the ITA reads:

> "Where, in any year of income, the total deductions of a contractor in relation to petroleum operations undertaken in a contract area exceed the cost oil for that year of income arising from those operations in the contract area, the excess shall be carried forward to the next following year of income and is deductible for that year of income against the cost oil for that year of income arising from petroleum operations in the contract area until the excess is fully deducted or the petroleum operations in the contract area cease."

It is in dispute whether excess costs are deducted only when oil production starts. The Act does not define excess costs. S. 89C (2) of the ITA merely refers to them when it states that "where in

any year of income the total deductions of a contractor in relation to petroleum operations exceed the cost oil for that year of income". It further states that the excess shall be carried forward to the following year of income.

S. 89A of the ITA defines cost oil to mean a contractor's entitlement to production as cost recovery under a petroleum agreement. Cost oil means an entitlement. It is argued that a contractor has no entitlement until when production has started. An entitlement is defined by *Black's Law Dictionary* 8th Edition p. 573 as "an absolute right to a (usu. monetary) benefit, such as social security, granted upon meeting a legal requirement." Exploration expenditures are by their very nature incurred prior to the commencement of commercial production The Act is silent as to when the entitlement arises. Is it when oil is discovered or when oil production starts or when costs are deducted and the excess is carried forward? S. 89A (1) defines recoverable costs to mean a cost of a contractor that is recoverable under a petroleum agreement. Article 10 of the EA2 PSA and Article 12 of the EA1 and EA3A PSA state that the licencees shall carry forward to subsequent years all unrecovered costs until full recovery is completed. According to the PSAs, is any unrecovered costs excess costs? Once again the PSAs are also silent as to when the right to cost recovery becomes absolute. While the applicants' argument points to excess oil being due when oil production starts the respondent refers to them as any unrecovered costs.

S. 89C of the ITA states that excess costs may be deducted against cost oil until excess is fully deducted or the petroleum operations in the contract area cease. Petroleum operations have been defined to include exploration, production and development. According to the said Section, petroleum operations need not cease at production level, they may even cease at exploration level. This means excess costs are deductible before production starts. Excess costs which are in effect deductible or allowable costs are accumulated along the value chain until deducted or oil the oil operation ceases. If there is no oil production the contractor losses the opportunity to recover the deductible costs.

S. 89C (2) should be read together with S. 89G (a). S. 89G (a) states that any excess costs attributable to the interest at the date of disposal. The word "attributable" is defined by *Oxford Advance Learner's Dictionary* 6th Edition p. 63 to mean "probably caused by the thing

mentioned". According to S. 89G(a) if there are any excess costs that can be traced to the interest at the time of disposal they should be deducted. The time of disposal, as was in the case of the applicants was at exploration level. There is nothing that prohibits the respondent from deducting excess costs deductible by the transferee contractor from the cost base when production has not started. As long as the excess costs can be attributable to the interest at the date of transfer or disposal of interest, the S. 89C (2) provides for them. In reality excess costs are recovered against cost oil when oil production starts. For purposes of valuation, what are deemed excess costs are allowable or deductible costs even when oil production has not commenced. They can be considered as an asset.

As to what excess costs may mean one has to look at the intention of the Parliament. In interpreting statutes, courts may use a purposive approach where the term used is unclear. In *Crane Bank v Uganda Revenue Authority* HCT-00-CA-18-2010 his Lordship Kiryabwire stated that:

> "The position of the law is that if any doubt arises from the words used in the statute where the literal meaning yields more than one interpretation, the purposive approach may be used, to determine the intention of the law maker in enacting of the statute. (See Justice Choudry in the case of UGANDA REVENUE AUTHORITY V. SPEKE HOTEL (1996) LTD (CA No. 12 of 2008).
>
> The purposive approach has been used in several cases. In the case of Sussex Peerage (1844) 8 ER at 1057, it was held that
>
>> "If the words of the statute are in themselves precise and unambiguous, then no more can be necessary than to expound those words in their natural and ordinary sense. The words themselves alone do in such case best declare the intention of the law giver but if any doubt arises from the terms employed by the legislature, it has always been held a safe means of colleting the intention to call in aid the grounds and cause enacting the statute and to have recourse to the preamble which according to Dire CJ is 'a key to open the minds of the makers of the Act and the mischiefs they intend to redress."
>
> Lord Griffiths in the case of PEPPER V. HART [1993] 1 ALL ER 42 at p 50, also held that:
>
>> "The days have long passed when the courts adopted a strict constructionist view of interpretation which required them to adopt a literal meaning of the language. The court must adopt a purposive approach which seeks to give effect to the true purpose of the legislation and are prepared to look at much extraneous material that bears on the background against which the legislation was enacted."

Since the application of the term ‘excess costs’ may have different effects depending on its interpretation, the Tribunal will use the purposive approach to ascertain what was the intention of Parliament.

Black’s Law Dictionary 8th Edition page 222 defines a capital gain as “the profit realised when a capital asset is sold or exchanged.” It defines capital gains tax at page 1496 as a tax on income derived from the sale of a capital gain. The purpose of capital gains tax is to collect income tax from that gain. Under S. 52 (6) of the ITA, “expenditures incurred to alter or improve an asset -which would not have been allowed as a deduction are added to the cost base of the asset.” Under Petroleum Sharing Agreements a contractor is entitled to recover his cost. At the time the ITA was enacted, in 1997, petroleum operations and transfers of interests under the PSA had not been anticipated. It does not make economic sense to compute the cost base of an asset and exclude costs which the contractor will recover when production starts.

The result of the modification of Part IXA on Part VIA is to allow the taxman to compute the cost base as the amount involved in acquiring the asset plus incidental costs of a capital nature incurred. Excess costs that have been incurred at the time of the disposal of the interest should be part of the cost base. Likewise excess costs that have been incurred are allowable deductions as prescribed in S. 89C (2) of the ITA.

S. 89G (a) deals with the disposal of original interests. The disposal of Tullow’s pre-existing interests which were not purchased from Heritage would be considered as such. S. 89G (a) provides that any excess costs under S. 89(c) attributable to the interest at the date of the disposal are deductible by the transferee contractor. S. 89G defines a transferor contractor as one who disposes of an interest in a petroleum agreement and the ‘transferee contractor’ as a person who receives the interest or who as a result becomes a contractor in relation of the operations. From the said definitions it is clear that the applicants were transferor contractors while CNOOC and Total are transferee contractors. Therefore any excess costs are at the date of disposal are deductible by CNOOC and Total, as transferee contractors.

(ii) Subsequent disposal

Part IXA modifies Part VI of the ITA. In respect of subsequent disposals of interests under petroleum agreements, S. 89G (d) under Part IXA of the ITA provides that:

> "in a subsequent disposal of the whole or part of the interest disposed under paragraph (c), the cost base for the purposes of calculating any capital gain or loss on disposal of the interest is the amount of the transferor contractor's capital gain on the prior disposal of the interest if any, less the sum of –
>
> (i) the excess costs up to the date of disposal that are deductible by the transferee contractor under paragraph (a);
>
> (ii) the depreciation of capital expenditure incurred up to the date of disposal that is deductible by the transferee contractor under paragraph (b); and"

The effect of S. 89G (d) is to modify the application of Part VI of the ITA in respect to the latter's application to subsequent transfer of interests of petroleum agreements. What is peculiar about S. 89G (d) is that it computes the capital gain or loss on a disposal of an interest using the gain by the transferor contractor on a prior disposal of an interest which is unrelated to the gain made in the subsequent transfer.

iii) COMPUTATION OF THE APPLICANTS' TAX LIABILITY

The Tribunal having found that the exemption granted to the applicants in respect of EA2 cannot hold; that the doctrines of estoppel and legitimate expectation do not help the applicants and having discussed the rules that apply to the transfer of interests of petroleum agreements, have to apply what was discussed in computing the applicants' tax liability taking into consideration the evidence adduced.

(a) Receipts

It is not in dispute that the applicants disposed of their interests in EA1, EA2 and EA3A to CNOOC and Total for US$ 2,933,330,400. What was in dispute was whether the applicants disposed of Heritage's interests first and later their pre-existing interests. The Tribunal concluded that the LIFO accounting method, preferred by the applicants, was inappropriate. The respondent had proposed as an alternative the application of the FIFO accounting method. In

discarding the applicants' LIFO accounting method, the Tribunal noted that what the applicants sold were intangible interests. It is not feasible to separate intangible interests acquired at different times. One cannot treat portions of undivided interest as separate and distinct assets. Therefore if the Tribunal cannot tell whether the applicants sold their last interests purchased first, nor is it in a position to say that it was the interests purchased first that were sold first. There is no legal basis for the Tribunal to hold that it should apply the FIFO accounting method.

The Tribunal shall apply the averaging method or what is more or less an equitable apportionment method. The Tribunal shall apportion the interests of what was acquired at different times and sold proportionally. This method was applied in the case of John *K. McNulty et al. v Commissioner of Internal Revenue* (supra) p. 6 where the court held that (which we repeat):

> "A taxpayer who owns two undivided one-half interests in property, received at different times, and disposes of an undivided one half- interest, is deemed to have disposed of 50 percent of each of the halves he owned."

Similar to the matter before us, the above case involved the sale of an intangible interest in immoveable property. The Tribunal notes that the above case was from a US Tax court which makes it persuasive. To ignore decisions from other jurisdictions may lead to the Tribunal groping in legal darkness in an area where there are no decisions from courts of record in Uganda. What is good for a goose in the US or UK is good for the gander in Uganda. The Tribunal notes that accounting methods and taxation principles used in some of these jurisdictions are similar to those applied in Uganda.

(b) Expenses

Before the Tribunal can compute the gain of the applicants, it has to ascertain what expenses were incurred by the applicants and which of these should be brought into the cost base as permitted by the tax law.

In the agreed documents, the applicants' financial statements for the years ending 31st December 2009 and 31st December 2011 were tendered in as exhibits A9, A10, A 21 and A22. The financial statements for the year ended 31st December 2011, Exhibit A21, showed TUL's

costs included in the capital gains calculations for Blocks 1, 2 and 3A. These include interest expense of US$ 65,981,553, final completion payment of US$ 13,636,043, stamp duty on acquisition US$ 14,500,000, guarantee arrangement and commitment fees of US$ 46,549,850 and legal fees on Heritage acquisition as US$ 1,072,914. Interest on loan to acquire Heritage was put at US$ 103,017,401.

During the trial, the applicants' witness, Mr. Inch, testified on the expenditures incurred by the applicants. He testified that the applicants sold their interest at a cost base of US$ 1.35 billion. The applicants incurred costs of US$ 129 million for the pre-existing interest. He said the cost base for the pre-existing interest in EA1 was US$ 28,272,501. The applicants incurred an economic cost of US$ 100 million and guarantee fees of US$ 46,061,058. Mr. Inch testified that the total cost was US$ 840,408,344 for the Heritage interests in respect of Block EA1 and US$ 623,528,772 for EA3A. He testified that the applicants incurred a loss of US$ 175,577,251.

The applicants tendered in exhibit A40 (iii) a computation of the capital gains tax. The applicants' exhibit put Heritage acquisition costs at US$ 840,408,344 for EA1, US$ 623,528,772 for EA3A bringing it to a total of US$ 1,463,937,116. For the pre-existing interests, the total amount was US$ 320,545,815. Exhibit A40(iii) put the guarantee fees at US$ 46,061,058 comprised of guarantee arrangement fees of US$ 31,800,000 and guarantee commitment fees of US$ 14,261,058. Incidental expenses were broken down into US$ 46,061,058 for guarantee fees, legal fees of US$ 1,342,221, stamp duty of US$ 14,500,000 totalling to US$ 61,903,279. The total costs incurred by the applicants were put at US$ 113,429,096. The exhibit put a loss on Block 3 at US$ 20,987,930.

In his evidence, the respondent's witness, Mr. Moses Kajubi, mentioned some of the expenses incurred by the applicants as; guarantees fee of US$ 31,800,000 comprising of guarantee committee fees of US$ 10,829,241, legal fees of US$ 457,397 and stamp duty of US$ 14,500,000. A sum of US$ 339,999,660 was disallowed by the respondent because it was recoverable when commercial production begins. The excess costs of Heritage were put at US$ 150,000,000. Incidental expenses were put at US$ 61,903,387. Mr. Kajubi put the cost base of EA1 at US$ 746,152,777 and for EA2 at US$ 553,597,222.

In its submission, the respondent alleged that it allowed incidental costs as follows: guarantee arrangement fees of US$ 31,800,000, guarantee committee fee of US$ 10,829,241, legal fees of US$ 459,318 and stamp duty of US$14,500,000. The respondent submitted that it received further information from the applicants that increased the incidental costs to US$ 61,903,387 which reduced their tax liability to US$ 467,271,974.

The respondent disallowed items including interest of US$ 113,429,096, Tullow's pre-existing costs of US$ 320,545,815, loss from Block 3 of US$ 20,987,930 and reinvestment relief of US$ 93,125,950. In total it disallowed US$ 548,088,791. In disallowing the pre-existing petroleum operations costs of US$ 320,545,815 from being included in the applicants' cost base the respondent argued that such expenses are only deductible against cost oil pursuant to S. 89C of the ITA.

The respondent submitted that two items were disallowed which are not in dispute; interest expense of US$ 113,429,930, a loss of US$ 20,987,930 resulting from EA3A and non recognition treatment of US$ 164,721,000. However, a perusal of the applicants' exhibit A40 (iii) shows that an interest expense of US$ 113,429, 096 and loss of US$ 20,987, 931 were included in their computation. The financial statements of the TUL, Exhibit A22, put the interest expense from Heritage at US$ 65,981,553 which the Tribunal will consider as an incidental expense. The Tribunal shall not include the loss of US$ 20,987,930 because the transfer in question arose from Block 3 where there was no transfer of interest, and is not subject of the application before us.

When the Tribunal compares the expenses presented by the parties it notices that there are discrepancies in the figures advanced. For instance there are differing amounts on the guarantee fees, legal fees and incidental expenses incurred. When one compares exhibit A40 (iii) with the illustration/chart presented by the respondent in its submission one cannot fail to notice the glaring differences in the figures. Apart from the financial statements, there are no supporting documents attached to the exhibit A40 (iii) to substantiate the expenses incurred by the applicants. There are no clear breakdown expenses of the cost base in exhibit A40 (iii). The cost base of EA1 EA2 and EA3 was put at US$ 840,408,344, US$ 623,528,772 respectively totalling to 1,463,937,116. The applicants broke down the amounts to base price, settlement

account and Heritage acquisition costs. There are no expenses called ‘base price’, ‘settlement account’ and ‘acquisition costs’. Some of the information the applicants claimed to have been availed by email, but to whom? Exhibit A40 (iii) is neither signed nor bore a stamp of a firm of certified accountants or auditors. The maker of the said exhibit is not known. The failure by the applicants to present clear evidence in support of their expenditures led the Tribunal to ignore some of expenditures incurred.

The Tribunal has already noted that the applicants presented financial statement for the years ended 31st December 2009 and 31st December 2011 i.e. exhibits A9, A10, A 21 and A22. However the transactions in question, that is the transfer of interests in Blocks 1, 2 and 3A, took place in 2012. The applicants closed their case on 28th November 2012. At least the applicants should have tendered in an audited accounts of the relevant period of 2012, up to the closure of their case. An updated statement of expenses incurred by the applicants would have been reflected in the said accounts so as to enable the Tribunal properly calculate the gain. The Tribunal expected the applicants to submit an independent auditors’ special report on the expenses incurred in the absence of audited accounts. Article 5 of the PSAs for EA1, EA2 and EA3 makes provision for an advisory committee. Under Article 5.3.5, the Committee is supposed to ensure that the accounting of costs and expenses and maintenance of operating costs are made in accordance with the Agreement, accounting principles and procedures generally accepted in the international petroleum industry. The records of the said committee on expenses were not availed to tribunal. No reason was given as to this omission. The Tribunal has powers to summon any witness and the applicants ought to have taken advantage of this.

S. 18 of the TAT Act places the burden of proof on the applicants to prove that a taxation decision is excessive or should have been made differently. The applicants have not discharged the burden in respect of the exact expenses incurred by them. The Tribunal cannot rely on hypothetical figures to ascertain the expenses incurred by the applicants.

The respondent presented to the Tribunal different figures from the applicants as regards the expenses incurred. It is not denied nor is it in dispute that the applicants incurred expenses. If the Tribunal were to ignore the figures that were presented by the respondent, a miscarriage of justice would be occasioned to the applicants. The expenses or that portion that has been

admitted by the respondent would not be added in the computation of the gain. The Tribunal will allow the figures presented by the respondent as expenses incurred by the applicants as admissions under Sections 16, 17 and 28 of the Evidence Act. The Tribunal will also take into consideration the figures presented by the applicants in exhibit A21, the financial statements ending 31st December 2012 of TUL. Those figures presented by the applicants that are the same as the respondent's shall be considered in computing the gain.

Also in respect of the expenses incurred by the applicants, the Tribunal notes that the respondent's computation do not indicate whether the expenses computed were in proportion to the interests sold. The applicants sold 66.67% of their interests and therefore the expenses used in the computation should have been 66.67% of what was incurred. As prudent revenue collectors, the Tribunal will take it that, the respondent used this weighted costs approach in computation of the gain. That is the expenses incurred by the applicants corresponded to the interests sold in each block.

(c) Gain by the applicants and the tax payable

Having found that the applicants are liable to pay tax on the gain they obtained from the transfer of their interests in Blocks 1, 2 and 3A, the Tribunal now has to go into the mathematics of the tax due. The tribunal takes into consideration that the applicants sold pre-existing interests and interests acquired from Heritage. The Tribunal will also take into consideration that the income received was not in dispute. What was in dispute was the accounting method used and expenses incurred by the applicants. The Tribunal has already discarded the LIFO method of accounting proposed by the applicants. This was because the said interests were intangible assets. One cannot treat intangible assets as if there are tangible assets. The respondent proposed the FIFO method of accounting which the Tribunal found inappropriate. In situations where a party cannot state with precision which interests were sold, the rules of equity and fairness have to be considered. The rules of equity demand that interests acquired at different times but sold at the same time should be divided proportionately. The Tribunal shall use the averaging method or equitable apportionment in computing the gain obtained by the applicants. This was applied in the case of *John K. McNulty et al. v Commissioner of Internal Revenue* (supra) which also involved immoveable property. It was noted that a "A taxpayer who owns two

undivided one-half interests in property, received at different times, and disposes an undivided one-half interest, is deemed to have disposed of 50% of each of the halves he owned." The Tribunal thinks that this is good law. The Tribunal notes that there were pre –existing or original interests/holdings and those acquired from Heritage. In order to ensure a fair and equitable allocation of interests sold, the Tribunal will deem that equal proportions were sold from each holding. The Tribunal also notes that Tullow did not sell 100% of its total interests. It only sold 66.67% of its interests. Therefore 33.33% was sold from each holding

In its computation, the respondent used the illustration below to calculate the gain of the applicants using the FIFO method.

Table 1: Computation of the gain by the respondent

	Block	**% sold**	**Interest**	**Total Consideration**	**COST BASE**				**Gain**	**Tax at 30%**
					Signature bonus	**Cost base as per S.89G(d)**	**Incidental expenses S. 52(2)**	**Total Cost base**		
TUL	EA1	16,67% 50%	Pre-existing From HOGL	$ 258,332,300 $ 775,000,000	$ 99,999 $ -	$- $ 746,152,777	$- $ 26,981,481	$ 99,999 $ 773,134,259	$ 258,232,300 $ 1,865,740	$ 78,029,412
	EA3A	16.67 50%	Pre-existing from HOGL	$ 191,665,900 $575,000,000	$ 66,666 $-	$- $ 553,597,222	$- $20,018,518	$ 66,666 $573,615,740	$ 191,5999,233 $ 1,384,259	$ 57,895,047
	EA2	50%		$ 850,000,000	$-			$-	$ 850,000,000	255,000,000
Sub Total				$ 2,649,998,200	$ 166,666	$ 1,299,750,000	$ 47,000,000	$ 1,346,916,666	$ 1,303,081,533	$ 390,924,460
TUOP	EA2	16.67%		$ 283,332,200	S-			$-	$ 283,332,200	$ 84,999,660
TOTAL		66.66%		$ 2,933,330,400	$ 166,667	$ 1,299,750,000	$ 47,000,000	$ 1,346,916,667	$ 1,588,413,734	$ 475,924,120

The Tribunal has computed the gain and the tax arising from the transfer of interests in the PSAs of Blocks 1, 2 and 3A, using a similar tabulation as that of the respondent which as set out below: The percentage of interests considered as original/ pre-existing interests and the ones

considered as purchased from Heritage was 33.33% each using the averaging method or equitable apportionment instead of the LIFO and FIFO methods. Each was half of the 66.67% interest transferred in EA1 and EA3. The expenses were computed taking into consideration the proportion of interests sold. The tabulation was computed from the evidence adduced in the Tribunal.

Table 2 Computation of the gain by the Tribunal

	Block	% sold	Interest	Total Consideration	COST BASE				Gain	Tax at 30%
					Signature bonus	Cost base as per S.89G(d)	Incidental expenses S. 52(2)	Total Cost base		
TUL	EA1	33.33% 33.33%	Pre-existing From HOGL	$ 516,666,150 $ 516,666,150	$ 199,998 $ -	$- $ 497,435,185 + 75,000,000 (B)	$- $ 17,987,654 + 23,505,252 (A)	$ 199,998 $ 613,928,091	$ 516,466,152 $ - 97,261,941	$ 125,761,263
	EA3A	33.33% 33.33%	Pre-existing From HOGL	$ 383,332,950 $ 383,332,950	$ 133,332 $-	$- $ 369,064,815 + 75,000,000 (B)	$- $ 13,345,679 + 23,505,252 (A)	$ 133,332 $ 480,915,746	$ 383,199,618 $ - 97,582,796	$ 85,685,047
	EA2	50%		$ 850,000,000	$-			$-	$ 850,000,000	$ 255,000,000
Sub Total				$ 2,649,998,200	$ 333,330	$ 1,016,500,000	$ 78,343,837	$ 1,095,177,167	$ 1,554,821,033	$ 466,446,310
TUOP	EA2	16.66%		$ 283,332,200	S-			$-	$ 283,332,200	$ 84,999,660
TOTAL		66.66%		$ 2,933,330,400	$ 333,330	$ 1,016,500,000	$ 78,343,837	$ 1,095,177,167	$ 1,838,153,233	$ 551,445,970

Note (A) is the increase in the incidental expenditure arising from the rectification of legal fees, guarantee fees and interest expense.
Note (B) is the addition of the excess costs that were deducted by the respondent yet were not substantiated.

In its computation, the tribunal has put the expense of the signature bonus for the pre-existing interest at US$ 199,998 for EA1 and US$ 133,332 for EA3A. In its computation, the respondent had put the signature bonus at US$ 99,999 and US$ 66,666 for EA1 and EA2 respectively. If the pre-existing interests were 16.67% when they increase to 33.33% the signature bonus doubles.

Where the interests were 50% and are reduced to 33.33%, the expenses incurred in the cost base and incidental expenses are proportionately reduced. This means the cost base and incidental expenses are reduced by a third. The weighted costs approach or the costs incurred in proportion to the interests has the effect of reducing the cost base. The effect of using the averaging or equitable proportion method increases the gain in blocks EA1 and EA3A and hence the tax liability of the applicants. Using the above illustration the applicants' tax liability before pre- investment would be US$ 551,445,970.

In TUL's financial statements, Exhibit A22, it is indicated that the legal fees incurred were US$ 1,072,914. The respondent put it at US$ 459,318. That is a difference of US$ 613,596. The respondent submitted that the guarantee arrangement fees were US$ 31,800,000, guarantee commitment fees were US$ 10,829,241 totalling to US$ 42,629,241. The financial statements of TUL put the guarantee arrangement and commitment fees at US$ 46,549,850. That is a difference of US$3,920,609. The said financial statements had an interest expense of US$ 65,981,553 which the respondent did not consider. However the said interest expense is an incidental expense. The total of the above differences (i.e. 613,596 and 3,920,609) plus the interest expense of US$ 65,981,553 is US$ 70,515,758. TUL sold interests 33.33% of its interests from each block. The sale from both Blocks 1 and 3A constituted 66.67%. 66.67% of US$ 70,515,758 is US$ 47,010,505. Hence the above expenses should be proportionate to the interest transferred in the said block. Accordingly half of US$ 47,010,505 which is US$ 23, 505, 252 was added to the cost base of EA1 and EA2. See Note (A) on the incidental expenses in the cost base of EA1and EA3A.

The Tribunal agrees with the respondent's decision to disallow the applicants from using a loss of US$ 20,987,930 on EA3 to reduce their gain on the sale of their EA3A interests because the said loss related to a separate contract area, EA3.

The respondent submitted and Mr. Kajubi testified that Tullow had incurred costs of US$ 150,000,000 as excess costs. However he did not tell the Tribunal how he came to arrive at the said figure. There is no report from the joint advisory committee, nor any audited report to substantiate the excess costs incurred. The respondent also submitted that it disallowed pre-existing costs of US$ 320,545,819 on the ground that they should be deducted against cost oil.

However there is no evidence to show that the applicants ever presented the said figure to the respondent, nor is there any evidence to substantiate the said costs. There is no evidence that the said exploration costs of US$ 320,545,819 claimed to have been incurred by the applicants on EA1, EA2 and EA3A were audited. It is not clear which amount of recoverable costs were sold to Tullow by Heritage. In the absence of any certified excess costs the Tribunal will not allow the deduction of US$ 150,000,000 by the respondent from the cost base. The Tribunal has made adjustments as indicated in the table above by adding US$ 75,000,000 to the incidental expenses of Blocks 1 and 3A. Please see note (B) in the cost base of EA1 and EA3.

The respondent, in its submission, admitted that the applicants furnished further information that increased the incidental costs to US$ 61,903, 387 which resulted in a further reduction of tax liability from US$ 475,924,120 to US$ 467,271,971. That is a reduction of US$ 8,652,149. The respondents did not furnish the Tribunal with the further information that was given to it by the applicants. Hence the Tribunal did not include the said information in the tabulation. However the Tribunal will reduce the tax liability of the applicants before the pre-investment relief from US$ 551,445,970 by US$ 8,652,149 to US$ 542,793,821. The said tax liability has been arrived at by making adjustments according to the evidence adduced before the Tribunal. The amounts may not necessarily be the actual ones incurred by the applicants. However the Tribunal has to make its ruling on the evidence presented.

(d) Pre-investment relief

The Tribunal has already noted that the applicants wished to transfer 50% of their interests. However the applicants disposed of a further 16.67% of their interests which was held to be an involuntary disposal. 16.67% of 66.67% interests transferred is 25%. Hence the applicants are entitled to a tax relief of 25%. If the tax liability of the applicants before the pre-investment relief is granted is US$ 542,793,821 then the relief would amount to US$ 135,698,455 and the tax liability would be reduced to US$ 407,095,366 after the grant.

The respondent submitted that the applicants should re-invest the relief in an asset of a like kind. The re-investment must be made within one year of the disposal. The Tribunal already noted that at the time the disposal took place the applicants still had time to re-invest in an asset

of a like kind. The transfer of interests took place on the 21st February 2012. The applicants had up to the 21st February 2013 to re-invest in an asset of a like kind. The applicants closed their case on the 28th November 2012. They had about three months remaining to reinvest in an asset of a like kind.

S. 54(1) (c) of the ITA requires the proceeds to be reinvested in an asset of a like kind within one year from the date of disposal. S. 54 (3) mentions a replacement asset. The respondent argued that the use of proceeds to fund pre-existing obligations under the PSAs is not an acquisition of a replacement asset as required by S. 54(3) of the ITA.

The applicants are required to reinvest in an asset of a like kind by S. 54(1) (c) of the ITA. The word 'like' is defined by *Oxford Advanced Learner's Dictionary* 6th Edition p.66 as "similar to sb/sth..." The word similar is not synonymous with the word same. One may have similar products that are not the same. A similar product may not be the same as a replacement. Using that definition, S. 54(1) (c) of the ITA requires a taxpayer to invest in an asset of a similar kind. It does not have to be the same asset.

In order to find out what assets of a like kind the applicants would be required to reinvest in, one would need to know what they sold to CNOOC and Total. A perusal of the PSAs, show that the applicants transferred their interests which were defined to be:

> "mean an undivided ... legal and beneficial participating interest in ...., in and under the interest documents and all rights and obligations attaching thereto, including, but without limitation, such interest in the Interest Property and the Interest Data;"

In totality, the interests sold included interests in data, documents and property. The applicants did not only sell their rights to explore and produce oil. The Tribunal does not think that the applicants would be interested in re-investing in data or documents but in property. Under the PSAs 'Interest Property' was defined to mean:

> "means all of the property related to the Interests including any platforms, pipelines, plant, machinery, wells, facilities and all other offshore and onshore installations and structures."

Hence if the applicants were to invest in an asset similar to the interest property, they would be investing in an asset of a like kind.

Having taken note that the applicants had three months remaining to reinvest from November 2012, the Tribunal shall extend the time for the applicants to furnish the respondent with evidence of a reinvestment in a like kind to a tune of US$ 135,698,455. The applicants had one year from February 2012 to February 2013 to re-invest in asset of a like kind. Since the applicants closed their case in November 2012, they still had three months to February 2013 to re-invest in an asset of a like kind. Therefore the Tribunal will give them an extension of three months from the date of the ruling.

6.4 CONCLUSIONS AND ORDERS OF THE TRIBUNAL

Having taken into consideration the evidence adduced, the submissions of all parties the Tribunal wishes to summarise it findings as below:

1. **In respect to EA2**

1.1 The Tribunal finds that Article 23.5 of the EA2 PSA was intended to cover capital gains tax arising from the disposal of interests in the PSA.

1.2 The Tribunal further finds that Article 23.5 of the EA2 PSA is invalid under the tax laws of Uganda and therefore the applicants are not entitled to an exemption from the payment of capital gains tax.

1.3 The Tribunal also finds that the applicants cannot rely on the principle of legitimate expectation as their expectation was not legitimate.

2. **In respect of all the PSAs.**

2.1 The Tribunal also finds that the respondent is allowed to reduce the cost base by the excess costs incurred by the applicants in the subsequent transfer of their interests. However the respondent did not satisfy the Tribunal on how it arrived at the amount of the excess costs incurred by the applicants and adjustments were made accordingly.

2.2 The Tribunal finds that the applicants did not discharge the burden placed on them to prove to the satisfaction of the Tribunal the actual expenses they incurred in order for them to be allowable. However the Tribunal took into consideration the expenses admitted by the respondent and those that were proved to its satisfaction to compute and make adjustments to the gain made by the applicants.

2.3 The Tribunal finds that the 'last in first out' (LIFO) and "first in first out' (FIFO) accounting methods proposed by the parties have no legal basis. The Tribunal applied the averaging method or equitable proportions in apportioning the different interests that were transferred by the applicants.

3. In respect of the re-investment relief.

3.1 The Tribunal finds that the disposal of 16.67% of their interest by the applicants was involuntary.

3.2 The Tribunal finds that the applicants are entitled to a re-investment relief of up to 25% of the interests they disposed of.

3.3 The Tribunal also finds that the applicants are still entitled to an extension of time to furnish evidence of re-investment in an asset of a like kind.

Basing on the above findings the Tribunal orders that:

1) The applicants pay capital gains tax of US$ 407,095,366 basing on the evidence adduced before the Tribunal being the amount after the pre-investment relief. The total amount of capital gain tax before the pre-investment relief was US$ 542,793,821.

2) The applicants will deduct the statutory 30% paid from the US$ 407,095,366 and the balance outstanding shall attract an interest of 2% per month from the date of this ruling till payment in full.

3) The applicants are entitled to a re-investment relief of US$ 135,698,455.

4) The applicants shall furnish the respondent with evidence of re-investment in an asset of a like kind to the tune of the abovementioned amount in clause 3 within three months from the date of this ruling. The said re-investment in an asset of a like kind should have been made in the period between 21st February 2012 and 21st February 2013. In the event the applicant does not comply with this order the said relief or that amount of relief which has not been proved will crystallise into capital gain tax on the expiration of the said period and will attract interest of 2% per month till payment.

5) Under S.19(c) of the Tax Appeal Tribunal Act the portion in respect of the re-investment relief is remitted to the respondent to effect as stated herein above.

6) The Tribunal orders that the applicants pay two-thirds (2/3) of the costs of this application to the respondent. The Tribunal notes that the applicants were successful in some issues approximately a third and are entitled to a reduction in the costs.

Lastly, the Tribunal wishes to thank counsel of all the parties for the time and effort taken in the preparation and presentation of their cases. As the respondent had noted in their submission, that this is the biggest case (in monetary terms), involving the largest transaction of US$ 2.9 billion, in the legal history of Uganda. Both parties obtained representation from within and across the continent, which the Tribunal allowed in order to get to the bottom of the problem. We can say we have not been disappointed. The preparation by both parties was meticulous with a lot of effort put in. The submissions by the parties, though hefty, involved a lot of research. The applicants, as taxpayers are commercial enterprises aiming at profit maximisation are entitled to challenge any tax assessments imposed on them. The respondent, as a revenue collecting body, should not consider it as inappropriate or attempts at “manipulation of figures” when its assessments are challenged. In its collection of taxes the respondent should not attempt to kill the hen that lays golden eggs. The task of the Tribunal is clearly to resolve any tax dispute in accordance with the law, which we have done.

Dated at Kampala this …….day of……2014

……..... ....…….

Mr. Asa Mugenyi	Mr. George Wilson Mugerwa	Mr. Pius Bahemuka
Chairman	Member	Member