TL
versus
ZIMBABWE REVENUE AUTHORITY

HIGH COURT OF ZIMBABWE
N.T. MTSHIYA, AJ
HARARE; 1 June 2020 & 22 June 2020

INCOME TAX APPEAL

M.P. Mahlangu, for the appellant
S. Bhebhe & H. Muromba, for the respondent

MTSHIYA, AJ. This appeal seeks to determine whether or not it was proper for the respondent to disallow appellant's technical and management fees for the tax periods 2010 to 2016 in the sum of $14 442 262.36. The answer lies in the further determination of the question whether or not the technical services were actually rendered and paid for.

The Facts

The appellant, TL, is a registered company with limited liability duly in cooperated under the laws of Zimbabwe. TL carries on the business of milling, refining and selling sugar. It also sells by-products from sugarcane grown in the Lowveld of Zimbabwe.

On 25 November 2009, TSCL the holding company of the appellant, and on behalf and for the benefit of the appellant, entered into a Technical Assistance Agreement with Tongaat Hullet Sugar Limited (Tongaat) a company incorporated in the Republic of South Africa. TL accepted the agreement made on its behalf and has always complied with all rights and obligations in terms of that technical agreement.

The appellant has paid Tongaat all fees due for the technical assistance rendered to it and has paid the respondent the withholding tax as required by section 30 read with the seventeenth schedule of the Income Tax Act [*Chapter 23:06]* (ITA) on all such technical fees. The respondent has at all material terms accepted the withholding tax.

On 31 May 2018, through a letter addressed to the appellant, the respondent raised amended assessments in respect of income tax for the years 2010, 2011, 2012, 2013, 2014, 2015 and 2016.

On 11 June 2018 the respondent produced further amended assessments for the seven tax years between 2010 and 2016.

The appellant avers that the amended assessments in respect of the years 2010 and 2011 were unlawful in that the right of the Respondent to issue such amended assessments for these years had prescribed in terms of proviso (ii) to s 47 (1) of the Income Tax Act.

On 27 July 2018, the appellant objected to the amended assessments through their duly authorized agent. The objection was filed outside the stipulated period as stated in section 62(1) of the Income Tax Act but the Respondent accepted the objection in terms of section 62(2) after being satisfied by the reasons of the delay in lodging the objection.

On 19 November 2018 the legal practitioners, representing the appellant, duly lodged with the respondent a written notice of appeal to this Court.

The appellant states that between 7 April 2010 and 4 October 2016 technical representatives of the parent company visited TL to render technical assistance on the appellants' operations. Tongaat has been rendering services of a technical nature to TL since 25 November 2009, in accordance with the Technical Assistance Agreement. All payments made to Tongaat were in terms of the said agreement and were also in compliance with the relevant legislation in Zimbabwe.

It is the appellant's contention that all the seven amended assessments issued by the respondent did not specify the determination of taxable income and of credits to which the appellant was entitled to in terms of law. Each of the seven amended assessments was issued as an additional assessment in terms of s 47 (1) (a) of the Income Tax Act and not as an estimated assessment in terms of s 45.

The appellant goes on to point out that in each of the amended assessments, the figures attributable as technical fees had been assessed in a prior tax year in which the liability to pay was the following year.

The appellant also argues that the respondent failed to apply the provisions of section 16 (1) (r) of the Income Tax Act in that the fees paid by the appellant to Tongaat were not incurred as expenditure on administration and management but on the provision of technical fees

At the commencement of the hearing, the appellant applied for leave to introduce the issue of prescription. This issue had not been raised in the letter of objection. The respondent did not oppose the application. Leave to include the issue of prescription was therefore granted by consent.

The issues

At the pre-trial hearing on 11 March 2020, the parties agreed that the court should determine the following issues:

"1. Whether or not the additional assessments for the tax years 2010 and 2011 issued by the Respondent are unlawful by reason of prescription.

2. Whether or not the additional assessments for the tax years 2010 to 2016 were in any event invalid on the basis and on the grounds set out by the Appellant in both the objection and the appellant's case.

3. Whether or not Respondent erred in law in disallowing the deductions in respect of fees for technical services incurred by Appellant at all and in terms of s 16 (1) (r) of the Income Tax Act and further whether Respondent erred on the facts of the matter after applying the aforesaid sub-section 16(1)(r) to the deductions.

4. Whether or not, if a finding is made that the fees paid by the Appellant were in respect of administration or management services in terms of s 16 (1) (r) of the Income Tax Act, the Respondent erred in any event in not allowing such deductions to the level of at least 1% of the net income of the appellant.

5. Whether or not each of the original assessments for each of the relevant tax years that is to say 2010 to 2016 was made in terms of the practice generally prevailing at the time each of the assessments was made and therefore Respondent was by virtue of the proviso to s 47(1) of the Income Tax Act precluded from issuing additional assessments for those years."

Evidence

The appellant led evidence from two witnesses. The first was Miss Tapiwa Florence Makoni who is empolyed by the appellant as its Human Resources Director and Company Secretary. She is a Chartered Accountant by profession and joined the appellant on 1December 2014 as a Finance Training Manager. She testified that she was familiar with the operations of the appellant and had the knowledge of the technical assistance that the appellant was getting from Tongaat. She was able to testify on the history and the need for such technical services to the appellant. She expressly mentioned that the technical services rendered excluded managerial and administrative fees. She said there was no need for these as these services were specifically provided by the expertise from within Zimbabwe. She went on to explain the procedure followed for the technical fees to be paid. She said payment was made through the appellant's bank, which in turn communicates with the Reserve Bank of Zimbabwe, for the necessary approvals. She said the technical agreement is renewed annually with the approval of the Reserve Bank of Zimbabwe. She also explained that in order for the technical fees to be paid, audited statements and proof of the necessary withholding tax would have been remitted to the respondent before the Reserve Bank of Zimbabwe would approve any external payment.

I found her to be a credible witness who knew the processes followed to fulfill the obligations under the Technical Assistance Agreement.

The second witness who gave evidence for the appellant was Mrs Farmer, a tax expert and advisor to the appellant. She is a tax consultant and has vast experience in tax matters and is a former employee of the respondent. She left the employee of the Respondent and worked for Price –Waterhouse Coopers where she left and partnered with one of the partners from Price-water House Coopers to open up her own private practice. She is an examiner and marker for the qualifying examinations for the Chartered Institute of Secretaries Board in all tax modules.

She testified that she prepared the letter of objection to the Commissioner on behalf of the appellant on the amended assessments. She said the respondent had, upon its request, been furnished with a copy of the Technical Assistance Agreement which had been in force since 2009. She said the respondent had also been given the minutes of engagements of the consultants from Tongaat. She also emphasized the point that the respondent never disputed any of the documents it was furnished with.

Mrs Farmer also stated that the amended assessments were invalid due to certain deficiencies. She gave the 2013 tax year assessment as an example why the assessments were invalid. She pointed out the errors found in the assessments presented by the respondent.

Mrs Farmer said in addition to the objection letter she prepared, she had also verbally and through emails engaged an officer of the respondent on the objectionable aspects of the additional assessments. The officer approached had conceded that the amended assessments did not make sense and required revision. That revision never came until the appeal hearing. She was adamant that although there was nothing in the record to confirm her approach to the respondent's officer the conversation had actually taken place.

She spoke confidently and with authority on the subject and the court is persuaded to accept her evidence in its entirety. The court has no reason to doubt the truthfulness of her evidence.

The Law and Consideration of Issues

I shall now proceed to look at each one of the issues agreed to by the parties for determination in this appeal.

1. *Whether or not the additional assessments for the tax years 2010 and 2011 issued by the Respondent are unlawful by reason of prescription.*

The answer to this question is to be found in section 47of the Income Tax Act, which section in full provides as follows:

"**Additional assessments**

(1) If the Commissioner, having made an assessment on any taxpayer, later considers that –

(a) an amount of taxable income which should have been charged to tax has not been charged to tax; or

(b) in the determination of an assessed loss-

(i) an amount of income which should have been taken into account has not been taken into account; or

(ii) an amount has been allowed as a deduction from income which should not have been allowed;

(c) any sum granted by way of a credit should not have been granted;

he shall adjust such assessment so as to charge to tax such amount of taxable income or to reduce such assessed loss or to withdraw or vary such credit, and if any tax is due either additionally, or alternatively, call upon the tax-payer to pay the correct amount of tax:

Provided that-

(i) no such adjustments or call upon the taxpayer shall be made if the assessment was made in accordance with the practice generally prevailing at the time the assessment was made;

(ii) subject to proviso (i), no such adjustment or call upon the taxpayer shall be made after six years from the end of the relevant year of assessment, unless the Commissioner is satisfied that the adjustment or call is necessary as a result of fraud, misrepresentation or willful non-disclosure of facts, in which case the adjustment or call may be made at any time thereafter;

(iii) the powers conferred by this subsection shall not be construed so as to permit the Commissioner to vary any decision made by him in terms of subsection (4) of section *sixty-two*.

(2) Sections *forty-five* and *forty-six* shall apply to any assessments or to a call for the payment of any additional sum in respect of a credit made by the Commissioner under the powers conferred by subsection (1). "(My own underlining)"

It is clear from the above provision of the law that the Commissioner has a right to re-open audits after the lapse of the six-year period however the Commissioner is not satisfied that the taxpayer's returns disclose the correct amount or amounts for income tax purposes. However, in terms of (c) (ii) above, the Commissioner can only do that after he or she is satisfied that there is, on the part of the taxpayer, evidence of:

(a) Fraud

(b) Misrepresentation

(c) Willful or non-disclosure of facts

I am of the view that if the Commissioner has to re-open audits after the laps of the 6 years indicated under proviso (c) (ii) the Commissioner ought to prove that the tax payer has committed any one or all of the offences listed above. Obviously an allegation of such a nature would have to be placed before the tax payer for due process to take place.

However, *in casu* there is no evidence brought before me to show that the appellant was guilty of any of the offences listed in the act. There is also no evidence that the issue of misrepresentation captured in the respondent's submissions was ever placed before the appellant and interrogated in terms of law. In terms of the evidence before this court, what was paced before the appellant is the following:

> "Please find attached the amended income tax assessments. The assessments have been issued in terms of s 47 (1) (a). The assessments are in respect of disallowed management and technical fees on your final accounts account which the expense

> were claimed on the basis of 2% of turnover which is not supported by invoices that are supposed to be issued by Tongaat Hullets Limted. The expenses have been disallowed pending production of actual expenditure incurred as provided for in s 15 (2) (a) of the income Tax Act [*Chapter 23.06*]. (My own underlining)

Notwithstanding the production of the Technical Assistance Agreement, minutes of meetings with Tongaat consultants, audit certificates and evidence of approvals from the Reserve Bank of Zimbabwe, the respondents main concern was the production of invoices from Tongaat. The issue of misrepresentation was never raised. It could not be raised.

In view of the foregoing, I do not find any reason for me to hold that the additional assessments for the tax years 2010 and 2011 issued by the respondent were valid. The respondent did not place any evidence before me to prove that the taxpayer was guilty of fraud, misrepresentation and willful or non-disclosure of facts and thus justifying re-audit after 6 years. There was no valid reason for the respondent to act outside the prescription period. Accordingly, the additional assessments did not enjoy the protection of law. They are invalid.

2. *Whether or not the additional assessments for the tax years 2010 to 2016 were in any event invalid on the basis and on the grounds set out by the Appellant in both the objection and the Appellant's case.*

In order to answer this question there is need to understand and define what an assessment is. According to section 2 of the Income Tax Act [*Chapter 23:06*] an assessment is defined as follows:

> "assessment" means—
> (*a*) the determination of taxable income and of the credits to which a person is entitled in terms of the charging Act; or
> (*b*) the determination of an assessed loss ranking for deduction;
> and includes a self-assessment in terms of section *thirty-seven A*.

It is clear from the above definition that an assessment should reflect

1. Taxable income
2. Credits to which a person is entitled to
3. An assessed loss ranking for deduction.

Accordingly, in order for an assessment to be valid the above elements must be reflected and properly addressed. It is only when that is done that we can then have a proper income tax assessment in terms of the law.

In *Barclays Bank of Zimbabwe v Zimbabwe Revenue Authority* HH162/2004**,** where a similar issue arose**,** MAKONI J, as she then was, had this to say:

> "*on close scrutiny of Annexure "A" it is apparent that it does not show any taxable income or credits to which Applicant is entitled nor any assessed loss ranking for deductions. Annexure "A" only reflects the sums due to the Respondent in the form of taxes, penalties and interest.*
> *It is imperative that an assessment contains the requirements of the Act as the administrative functions bestowed by the Act on the Commissioner amount to a determination which is executable through a garnishee. He is also bestowed with the power to hear any objections in terms of the assessments made, after which he can insist on payment of the tax pending the determination of any dispute arising from an assessment. The legislature could only have envisaged granting the Commissioner power to execute pending determination in circumstances where the tax payer been clearly advised of the basis for the assessment."*

I am in agreement with my sister Judge that the lumping up of figures as happened *in casu* does not meet the requirements set out in section 2 of the Income Tax Act. It is incumbent on the part of the respondent to ensure that whatever information it gives to the tax payer can be properly understood and interpreted. The appellant's right to correct information is paramount in these matters and to that end lumped up figures without any explanation become meaningless. *In casu* the appellant's witness, Mrs Farmer, gave an example of an unchallenged discrepancy in the figures of technical fees where, in the audited financial statements for the year ended 31 March 2013 the amount was $4 022 170.00 but later appears as $2 983 800.00. This lives one wondering where such a discrepancy would have come from.

I therefore hold that the additional assessments are not valid and should be set aside.

3. *Whether or not Respondent erred in law in disallowing the deductions in respect of fees for technical services incurred by Appellant at all and in terms of section 16(1)(r) of the Income Tax Act and further whether Respondent erred on the facts of the matter after applying the aforesaid sub-section 16 (1) (r) to the deductions.*

   With respect to this issue, s 16 (1) (r) of the Income Tax Act provides as follows:

(*r*) in the case of expenditure incurred on fees, administration and management in favor of a company of which the taxpayer is an associated enterprise, or (where the company is a foreign company) the local branch—

(i) incurred prior to the commencement of trade or the production of income or during any period of non-production, any amount in excess of zero comma seventy-five per *centum* of the amount obtained by applying the following formula—

A - (B + C)

where—

A represents the total expenditure qualifying for deduction in terms of section 15;

B represents the expenditure on fees or administration and management paid outside Zimbabwe;

C represents expenditure qualifying for deduction in terms of section 15 (2) (f) (i);

(ii) incurred after the commencement of trade or the production of income, any amount in excess of *per* centum of the amount obtained by applying the above formula.

[Paragraph substituted by Act 2 of 2017]

We have, *in casu,* a Technical Assistance Agreement as evidence, that there was indeed an agreement between the parties, where the appellant has an obligation to pay for a service. The technical services are clearly spelt out in the agreement and with respect to fees Clause 3 of the agreement states:

> "3. Triangle shall pay Tongaat a fee for the services provided in terms of this Agreement calculated at 2% of the gross annual turnover of TL for each financial year, which fee shall be paid in the following manner:
>
> (a) As soon as possible after the end of each month the fee calculated to be due on that month's turnover as determined from that month's management accounts (if not in US$ then converted to US$ at an appropriate exchange rate) and confirmed in an audit certificate by Triangle's auditors shall be remitted to Tongaat in United States Dollars.
>
> (b) At the end of each financial year of Triangle and following upon production of the audited accounts of Triangle for that financial year, a calculation of the fee for the whole financial year shall be made and confirmed in an audit certificate by Triangle's auditors.
>
> (c) Following upon production of the auditors' certificate any adjustment of the fee paid monthly during the year shall be made and shall be taken into account, in the form of an addition or a deduction, as the case may be from future monthly payments of the fee."

The minutes of the meetings and schedules of the work done on the different site visits by Tongaat, were also brought before this court as evidence. The appellant's first witness Miss

Makoni, went further to explain the need for expertise on their plants because their machinery was very old and the service providers were assisting in replacing the obsolete machinery in phases.

Furthermore, in the objection letter of 27 July 2018, Miss Farmer made reference to a total of 24 visits undertaken by Tongaat to appellant's sites. The visits were all minuted and addressed technical issues. That evidence was not challenged. Audited accounts of the appellant were also attached to buttress its point that technical services were indeed rendered and paid for. Once again that evidence was not challenged.

It is also worth noting that the respondent has been recovering or receiving non-resident withholding tax from the appellant on the basis of the technical fees payments to Tongaat since 2010. The respondent then suddenly surfaces in 2017 stating that it was not convinced that the fees were indeed technical fees. This happens despites the fact that there is no change in the manner the appellant has been submitting its self-assessed income tax returns. There is no convincing explanation supporting the sudden change of approach on the part of the respondent. The appellant is entitled to know.

It is also important to note that the Technical Assistance Agreement also enjoys the approval of the Reserve Bank of Zimbabwe. Miss Makoni told the Court that "each foreign payment to be made has to be done through the Reserve Bank of Zimbabwe, after certain procedures and checks have been verified." I accept that payments to Tongaat were scrutinized by the Reserve Bank of Zimbabwe and were also audited by the appellant's auditors. It cannot be denied that for the 7 years the audited accounts reflected the technical fees payable to Tongaat in terms of clause 3 of the Technical Assistance Agreement quoted at page 11 of this judgment. Furthermore, the yearly renewals took into account the true execution of the agreement as reflected in the audited accounts.

In disagreeing with the appellant's objection, the respondent then suggests that the expenditure that the appellant claims to be technical fees was expenditure actually incurred on management fees and general administration fees. It should be noted that the broad provisions of the Technical Assistance Agreement do not preclude Tongaat from offering expertise to the appellant in the fields of administration and management. That kind of expertise does not in any way take away the technical nature of the agreement. There would certainly be need for expertise in the administrative and managerial spheres for the effective execution of the contract.

Accordingly, liaison between the contracting parties in relation to both administrative and management services cannot be ruled out. However, that liaison cannot, without evidence be taken to mean Tongaat was offering administrative and management services.

All in all, I do not agree that, given the evidence that was placed before the respondent, it was necessary to insist on invoices from Tongaat. My finding, on a balance of probabilities, is that Tongaat indeed rendered technical services which services were paid for in terms of the agreement. These were technical fees. The respondent, in my view, therefore erred in law in disallowing deductions in respect of the technical fees.

The finding that the fees were for technical services rendered, makes it unnecessary to proceed to deal with the 4th issue. This is so because the fees paid were not in respect of administration and management services offered by Tongaat. Tongaat did not offer those services. It rendered technical services for which it received technical fees from the appellant in terms of clause 3 of the Technical Assistance Agreement.

> 5 *Whether or not each of the original assessments for each of the relevant tax years that is to say 2010 to 2016 was made in terms of the practice generally prevailing at the time each of the assessments was made and therefore respondent was by virtue of the proviso to s 47 (1) of the Income Tax Act precluded from issuing additional assessments for those years.*

In addressing this issue, what the court has to determine is what was considered to be the practice generally prevailing and also the validity of the initial self-assessments, if they were lodged with the respondents in accordance with that practice.

In *CIR* v *SA Mutual Unit Trust Management Co Ltd* 1990 (4) SA 529 (A) at 536F-H CORBETT CJ said:

> "*a practice generally prevailing is one which is applied generally in the different offices of the Department in the assessment of taxpayers and in seeking to establish such a practice in regard to a particular aspect of tax assessment it would not be sufficient to show that the practice was applied in merely one or two offices. Moreover, the word "practice" in this context means a habitual way or mode of acting."*

The existence of such a practice could be established by showing that the Commissioner or his representative had issued a directive to that effect.

In this honorable court KUDYA J held in the case *DNS (Pvt) Ltd* v *Zimbabwe Revenue Authority* HH772/19 that:

> *"The appellant contended that at the time each self-assessment was filed there was a practice generally prevailing of accepting deductions pertaining to provisions. The respondent disputed the existence of the practice post 1 January 2010. I have already held in a CUT (Pvt) Ltd* v *ZIMRA HH 664/2019 at p 7 of the cyclostyled judgment that self-assessments are deemed to be assessments issued by the Commissioner. This is clear from the definition of an assessment set out in s 2 of the Income Tax Act and the clear and unambiguous wording of s 37A (11) of the same Act. I, therefore, dismiss the alternative argument raised by* Mr *Magwaliba that a self-assessment falls outside the contemplation of s 47 (1) of the Income Tax Act."*

The above case authorities give credence to the fact that there was a practice generally prevailing as at the time the appellant started executing the Technical Assistance Agreement. The respondent accepted taxes paid under that agreement. The income tax returns were based on an existing self-assessment system. There was no departure from that practice or system when the therefore of the view that the initial assessments from 2010 to 2016, having been presented in accordance with the practice generally prevailing at the time they were made, are valid. The respondent was therefore precluded from issuing additional assessments.

Dispositions

The respondent has failed to convince the court on the need for the appellant to be re-audited and have the initial assessments amended. The appeal has merit and should succeed.

I therefore order as follows:

1. The appeal succeeds.
2. The amended assessments from 2010 to 2016 be and are hereby set aside.
3. The initial self-assessment from 2010 to 2016 be and are hereby confirmed.
4. Each party shall bear its own costs.

Gill, Godloton& Gerrans, appellant legal practitioner
Kantor & Immerman, respondent's legal practitioners