

Summary of Judgment:

Case: TECHNO THREE UGANDA LIMITED Vs. UGANDA REVENUE AUTHORITY

Facts of the Case

Techno Three Uganda Limited is a construction company operating in Uganda. The company's shareholders had registered three other companies, that is, Satech Industries Limited, Roma Granite and Marbles Limited, and Naguru Hill Holdings Limited, with the intention of starting future businesses, but these companies never became operational, and so they were filing nil tax returns.

In January 2024, the Uganda Revenue Authority issued assessments to Techno Three Uganda Limited, totalling over Shs. 1.11 billion for the years from 2018 to 2020, claiming the Company had overclaimed interest expenses.

URA argued that because the Company shared common shareholders with these inactive companies, it formed part of a "group" under Section 25(3) of the Income Tax Act, which limits interest deductions to 30% of EBITDA. The company objected, arguing that the other companies were dormant, had no economic connection to it, and that the interest in question was paid to third-party banks, not to the related companies.

Ruling

The Tribunal ruled in favour of Techno Three Uganda Limited, setting aside the assessments. Although the company shared the same shareholders as the other three companies on paper, these companies were non-trading, hence dormant, and had no economic substance.

The tribunal moved away from the strict literal rule of interpretation historically associated with such cases like *Cape Brandy Syndicate v. IRC* [1921]1KB64, is clearly said." If that literal rule had been evoked, the Tribunal would have been bound by the strict wording of Section 25(3); because the companies shared shareholders, they would technically constitute a "group," and the interest restriction would apply regardless of the economic reality.

However, the tribunal applied a purposive interpretation of the law, which revealed that Section 25(3) was intended to target multinational companies using intra-group loans to shift profits and reduce taxable income in Uganda. The Tribunal concluded that applying the restriction to a local group with dormant entities and loans from taxable local banks would produce an absurd result never intended by Parliament. The principle of substance over form required that the economic reality, not just legal documentation, guide the tax outcome.

Implications

This ruling enriched the guidance on how tax laws should be interpreted in Uganda and confirms that URA must look beyond paper ownership structures and consider the actual economic activities of related companies before applying interest deduction restrictions.

Local businesses with multiple registered but inactive entities are now protected from assessments aimed at abusive multinational tax schemes. The Tribunal also recommended that the Ministry of Finance review Section 25(3) to ensure it aligns with national development goals, such as improving access to credit for the private sector.

The decision suggests that the law may need to be refined to distinguish between domestic lending, where interest income remains taxable in Uganda, and cross-border lending, which poses a genuine risk of profit shifting.

The Institute of Certified Public Accountants of Uganda (ICPAU) has always sought for clarity in context and purpose for section 25(3). Through its proposals to the Ministry of Finance, Planning, and Economic Development on this particular section.

ICPAU has always held a position that, apart from financial institutions, insurance companies, and other entities as provided under S.25(3), all other sectors are expected to abide by the 30% cap to claim interest deductibility.

That this, however, may be contrary to the original thin capitalization rules whose principal objective was to deter arbitrary repatriation of profits in the pretext of loan servicing.

The Base Erosion and Profit Shifting (BEPS) Action 4 Recommendation aims to limit base erosion through the use of interest expense to achieve interest deductions, particularly by restricting groups from using intra-group loans to generate interest deductions in excess of the group's actual third-party interest expense. The provision would thus have primarily intended to curb tax avoidance through interest deductions by members of international groups through interrelated lending and not domestic ones.