REPORTABLE (148)

NESTLE ZIMBABWE (PRIVATE) LIMITED
v
ZIMBABWE REVENUE AUTHORITY

SUPREME COURT OF ZIMBABWE
GUVAVA JA, MAVANGIRA JA, MAKONI JA
HARARE, 13 MAY 2021 & 23 NOVEMBER 2021

T Mpofu, for the appellant

S Bhebhe, for the respondent

MAKONI JA: This is an appeal against part of the judgment of the Special Court for Income Tax Appeals, handed down on 25 March 2020, which dismissed the appellant's appeal filed in terms of s 65 of the Income Tax Act [*Chapter 23.06*] (The Act) against the decision of the respondent. The respondent had dismissed certain aspects of an objection filed by the appellant against various amended assessments that the respondent had issued.

FACTUAL BACKGROUND

The respondent, which is the administrative body tasked with assessment, collection and enforcement of the payment of taxes leviable under the Act, carried out an investigation and audit into the appellant's tax compliance for annual income tax assessment returns for the period 2009 to 2013. The investigation constituted a review into the appellant's submitted tax self-assessment returns. Several documents were submitted to the respondent and a number of meetings were held between the parties. During the scope of the review, the

respondent noted numerous anomalies within the tax self-assessment returns submitted by the appellant. Thereafter, on 1 June 2016, the respondent issued five amended tax assessments for the 2009 to 2013 tax years on all the disputed issues claiming an aggregate amount of US$4, 905 776.34.

The appellant proceeded to note its objection to the amended income tax assessments in terms of s 62 of the Act. The appellant's objections centred on prescription regarding the 2009 income tax year, written off bad debts, disallowed excess capital, accrued expenses, management fees and excess royalty payments on brands.

On the 26 September 2016, the Commissioner determined the objections lodged by the appellant. The Commissioner held that he was entitled to issue amended tax assessments with regards to the tax year 2009 as a result of the various misrepresentations arising from excess capital allowances, unrealised exchange losses and bad debts that were deducted from the taxable income and were unsubstantiated. In respect of the other years the Commissioner largely disallowed the objections lodged by the appellant except excess royalty on grossed up payments due to adjustments on withholding tax which was paid late. The respondent ruled that the fifty per centum penalty on unpaid principal tax would remain in force to deter non-compliance.

The appellant, dissatisfied with the determination by the Commissioner appealed to the court *a quo*.

At the pre hearing meeting the parties settled ten issues to be determined by the court *a quo*. During the hearing, the appellant called evidence of two tax experts and produced

two sets of documentary exhibits. The respondent did not call oral evidence but relied on the pleadings filed of record.

The court *a quo* made the following findings in respect of the issues appealed against. It found that the respondent was entitled to re-open the 2009 tax assessment after six years in terms of s 47 (1) (ii) of the Act in light of the misrepresentation by the appellant of its tax affairs in its tax returns. It further found that the respondent correctly disallowed capital allowances for mark-ups on capital assets acquired by the appellant's related company exceeding the perimeter of the margins used by the appellant's group as these were in excess of the unconditional legal obligation to pay the related company.

It also found that the appellant had failed to prove that the basis of the deductions on management fees were equivalent to the cost mark-up formula provided in the appellant's Management Services Agreement and that the respondent had correctly disallowed the deductions in respect of the management fees relating to the appellant's related company. And, further, that the appellant could not claim deductions in respect of brands as this expenditure was indivisible from expenditure in respect of intellectual property.

The appellant, aggrieved by the decision of the court *a quo*, noted an appeal to this Court against part of the judgment on the following grounds.

GROUNDS OF APPEAL

"1. The learned President erred as a matter of law in determining that the word 'misrepresentation' as used in provisio (ii) to s 47(1) of the Income Tax Act [*Chapter 23:06*] fell to be interpreted as any error made by the taxpayer in submitting a return, regardless of the state of mind of the taxpayer.

2. The learned President erred on the facts in finding that the appellant had misrepresented any facts to the Respondent when it filed its self – assessment for the tax year ending 31 December 2009.

3. The learned President accordingly erred in finding that the respondent was entitled as a matter of law to issue an amended assessment in respect of the tax year ending 31 December 2009.

4. The learned President erred as a matter of law and fact in holding that the appellant was only entitled to a deduction in terms of s 15 of the Income Tax Act in respect of charges raised by and paid to a related party on the acquisition of capital goods on the basis of an unconditional legal obligation to pay rather than on the basis of expenditure, actually incurred in the tax year in which the deduction was made, forthe purpose of trade and producing income, and erred in imposing a ceiling of Swiss francs 8000 on such expenditure.

5. The learned President erred in fact by rejecting the evidence of the appellant as to the amount it had actually expended in each of the tax years in question in respect of management fees, which because of exchange control requirements had been capped at 2% of its annual turnover, and which amount had actually been paid to its regional management service company in the Republic of Kenya, and was thus expenditure actually incurred for the purposes of its business and in the production of income and as such deductible in terms of the legislation.

6. The learned President erred in fact and as a matter of law in holding that the appellant was not entitled to claim a deduction in terms of s 15 of the Income Tax Act in respect of expenses incurred on branding, and disregarded the fact that those

expenses were actually incurred for the purposes of its trade or the production of income.

7. The learned President erred both as a matter of law and as a matter of fact in holding that tax was payable on expenditure incurred in respect of branding yet having agreed that the expenditure was deductible for corporate income tax, being indivisible from expenditure incurred in the use and application of other intellectual property rights."

RELIEF SOUGHT

The appellant prays that the appeal be allowed and that an order for costs be made in its favour in terms of s 15(2) (bb) of the Income Tax Act [*Chapter 23:06*], and that para 2 of the order of the Special Court for Income Tax Appeal be altered as follows:

1. By the deletion from sub – paragraph c thereof of US$32 094.23 to the 2009 tax year;
2. By the deletion from sub – paragraph d thereof of US$303 379 to the 2009 tax year;
3. By the deletion therefrom of sub – paragraphs e, f, and h;
4. By the insertion at the end of sub – paragraph i of the words 'other than the 2009 tax year'.

SUBMISSIONS BEFORE THIS COURT

At the hearing of the appeal, Counsel for the appellant, Mr *Mpofu*, took two preliminary points which were not raised in the appellant's Heads of Arguments. His first point was that *a quo* the Respondent did not lead any evidence. It was only the appellant that led evidence. He stated that this has consequences in that in the absence of evidence led by the taxman, the *prima facie* case led by the Appellant coalesces into a conclusive case in its favour. For authority he relied on *CIR v Middleman* 1991 (1) SA 200 (C) and *A & Anor v Commissioner*

of Taxes 2018 ZATC 10. He submitted that in respect of issues relating to management fees, handling fees and branding fees it is only the taxpayer which established a case before the court *a quo*.

Mr *Mpofu's* second point was that the assessments before the court *a quo* for tax years 2010 to 2013 did not comply with the requirements of s 2 of the Act. He submitted that in effect there were no assessments. For authority he relied on *Barclays Bank of Zimbabwe v Zimbabwe Revenue Authority* 2004 (2) ZLR 151 (H). The assessment for the year 2009 would otherwise have been an assessment as contemplated in terms of s 2 of the Act but negated its validity upon being made "subject to an audit". It was his submission that the position of the law is that if a taxman is adjusting an assessment he cannot make that assessment subject to an audit because it is a correction of an assessment already accepted.

On the merits Mr *Mpofu* contended that the purported revised assessments did not contain a statement stating the respondent's reasons for undertaking the reassessment which is contrary to the law. He submitted that s 37A (13) of the Act provides that if the Commissioner intends to re-visit an assessment he is required to include, with the reassessment, a statement of reasons why he considers it necessary to make such an assessment. There were no such statements in respect of all the assessments in issue that were before the court *a quo*. Where the taxman intends to re-visit a prescribed assessment he must be satisfied that there has been fraud, wilful non-disclosure or misrepresentation. The existence of the fraud, wilful non-disclosure or fraud must be communicated in the statement. There is no such statement regarding the 2009 assessment. The factors that must be considered before a prescribed assessment can be reassessed do not exist. For that reason, the 2009 assessment must be with drawn.

Mr *Mpofu* further submitted that misrepresentation in terms of the Act must be construed with regard to the taxpayer's intentions or state of mind. He contended that, any contrary interpretation voids the statutory immunity provided in s 47 of the Act.

Regarding management fees, Mr *Mpofu* submitted that the taxman does not determine the necessity of expenditure or regulate how the taxpayer runs his affairs. He submitted that once expenditure has been incurred in the production of income, it is deductible.

He also submitted that on branding fees, the appellant led evidence on payments made for technical assistance which was not rebutted.

Per contra, Mr *Bhebhe*, counsel for the respondent submitted that in terms of s 63 of the Act, the *onus* to prove that one is not liable to tax lies with the taxpayer. Counsel submitted that detailed assessments were provided on p 98 of the record which negated the preliminary points raised by the appellant.

On the merits, Mr *Bhebhe* submitted that misrepresentation ought to be construed on an objective basis that does not delve into the intentions of the taxpayer. He also submitted that the respondent failed to show how the management fees were expended in the production of income. In respect of branding fees, he submitted that intellectual property expenditure could not be separated from branding. Hence, the court *a quo* was justified in disallowing the deduction.

On the need for a statement in terms of s 37A (13), Mr *Bhebhe* submitted the statements were provided to the appellant although they do not appear in the record. This is explained by the fact that the appellant did not raise these issues in its objection and in the court *a quo*. There was however an extensive exchange of documents between the parties in respect

of the tax period between 2009 and 2013. There is a document on p 123 of the record that reflect that the appellant was aware that the assessment of 2009 is being re-opened as it is the only year affected by prescription.

ISSUES FOR DETERMINATION

1. Whether the assessments that were before the court *a quo* complied with the provisions of s 2 of the Act.
2. What is the effect of failure by the respondent to lead evidence before the court a *quo?*
3. Whether or not the court *a quo* erred in its interpretation of 'misrepresentation' and finding that the Respondent had a legal basis to issue an amended assessment in respect of the tax year 2009.
4. Whether or not the appellant was entitled to a capital expenditure allowance in respect of handling fees paid in the acquisition of capital assets.
5. Whether or not the appellant was entitled to a deduction based on management fees.
6. Whether or not the appellant could claim deductions for branding costs as expenditure distinct from that incurred in the use and application of other intellectual property rights in the production of income

APPLICATION OF THE LAW TO THE FACTS

I will start by dealing with the points *in limine* raised by Mr *Mpofu* before delving into the merits of the appeal. In doing so I will deal with the second point *in limine* first as it might dispose of the appeal.

Mr *Mpofu's* second point *in limine* was that there were no assessments *a quo* as is defined in s 2 of the Act and as laid down in *Barclays Bank* case *supra*. He submitted that the assessment for the year 2019 could have passed as an assessment were it not for the remark

that 'the assessment is subject to an audit'. This also applies to the assessments for the year 2010 and 2011. They negate their validity by the endorsement 'subject to an audit. In respect of the years 2012 and 2013, the purported assessments do not meet the requirements of s 2 of the Act at all. Those kind of documents are not known in law. He further contended that our tax system is based on self-assessment. If the taxman accepts the self-assessment in terms of s 37A of the Act, it becomes his assessment. If he raises queries or adjusts that assessment what he then issues is a final assessment. It cannot be an estimate or subject to an audit. The assessments in issue are therefore invalid on that basis.

Mr *Bhebhe* started by pointing out that the issues being raised by Mr *Mpofu* were being raised for the first time in this court. They were not raised in the objection to the commissioner neither were they raised in the court *a quo*. He however submitted that for a taxpayer to object in terms of s 62 and to appeal in terms of s 65 of the Act there would have to be an assessment. Where there is no assessment, there can be no valid objection or appeal. If the appellant felt that there were no valid assessments, it should have approached the High Court seeking a *declaratur* to that effect.

On being engaged by the court in respect of the purported assessments for 2012 and 2013, he conceded that the documents do not meet the requirements of s 2. He however sought to explain that there is an endorsement that "a detailed assessment can be made available on request'. He then directed the court to p98 for the detailed statement of the taxable income, deductions and the tax payable.

On being further engaged on what the import of the term "this assessment is subject to audit" was he submitted that it meant that the assessment was as a result of an audit that was done and not that it is going to be the subject of a further audit.

I must observe that the points raised by Mr *Mpofu* were points of law which can be raised at any time. It is trite and requires no authority that a point of law can be raised at any time provided that there is no prejudice to the other party. Mr *Bhebhe* did not seriously contest the point. He also did not argue that the respondent would be prejudiced in any way.

As was stated in *Barclays Bank supra*, an assessment must contain the taxable income and the credits to which a person is entitled or the determination of an assessed loss ranking for deduction. Going by the above definition, the purported assessments for the years 2012 and 2013 fall far short of being assessments as defined in s 2 of the Act. The document on p 98 titled 'Income tax computation' did not and could not save the respondent. It is a detailed assessment covering the period 2009 to 2013. There is no provision in the Act for such an omnibus assessment. Mr *Bhebhe* conceded the point in respect of the assessments for the years 2012 and 2013. The concession is properly made.

The assessments for the years 2009, 2010 and 2011 would have met the requirements of the Act were it not for the endorsement that they were subject to an audit. Mr *Bhebhe* struggled when asked to explain the import of the endorsement "subject to audit".

Mr *Mpofu's* point, which I agree with, is that when the respondent issues an assessment, after having considered a taxman's self-assessment, that resultant assessment is final. It cannot be subject to an audit. There is no provision for such an assessment in terms of s 2 of the Act. The only endorsements permitted on an assessment are found in s 51 of the Act such as notice of the period within which to file an objection.

The rationale for the Commissioner to comply with the Act regarding assessments was given in *Barclays Bank supra* at p 154 F-G as follows:

> "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 assessment 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 taxpayer has been clearly advised of the basis for the assessment. In addition, s 51 requires the taxpayer to be given due notice of the assessment and the tax payable in the manner stipulated in that section. There should be no doubt as to whether the document sent by the Commissioner to a tax payer is an assessment in view of the taxpayer's right to object within 30 days.
> Annexure A is not headed "Notice of assessment" nor "assessment" and does not give 30 days' notice for objection as is required by the Act. Further, the document cannot be said to constitute an assessment as it falls short of the definition of assessment in terms of s 2 of the Act. In the process of serving the taxpayer with an assessment and hearing objection, the Commissioner should comply with the provisions of the Act as his administrative acts have far reaching consequences of a garnishee on the taxpayer."

Although the above remarks were made in a case where the Commissioner had issued a garnishee order to a disputed assessment they apply with equal force in *casu*. There should never be any doubt as to whether what the Commissioner would have issued is an assessment or not as any default by the taxpayer can be met with the administrative powers bestowed on the Commissioner in the Act.

In view of the above the assessments are null and void as they were issued contrary to the requirements of the Act. They were a nullity and cannot create any obligation to pay tax. What this means is that there were no proper assessments for the court a *quo* to relate to. Consequently, there is no proper appeal before this court.

Mr *Mpofu's* second point *in limine* has merit and is upheld.

Having made the above findings, it will not be necessary for me to deal with the first point *in limine* raised by Mr *Mpofu* and the merits of the matter.

This is an appropriate case to invoke the provisions of s 25(2) of the Supreme Court Act [*Chapter 7:13*] to set aside the proceedings of the court *a quo* as they are irregular. Costs will follow the cause.

Accordingly, I will make the following order:

1. In terms of the powers set out in s 25(2) of the Supreme Court Act, the proceedings of the court *a quo* in ITC 9/2016 be and are hereby set aside.
2. The respondent is to pay the appellant's costs in terms of s 15(2) (bb) of the Income Tax Act [*Chapter 23:06*].

GUVAVA JA : I agree

MAVANGIRA JA : I agree

Gill, Godlonton & Gerrans, appellant's legal practitioners

Kantor & Immerman, respondent's legal practitioners