IN THE COURT OF APPEAL OF TANZANIA
AT DODOMA

(CORAM: JUMA, CJ., MWARIJA, J.A., And MZIRAY, J.A.)

CIVIL APPEAL NO. 192 OF 2018

PANAFRICAN ENERGY TANZANIIA LTD ....APPELLANT

VERSUS

COMMISSIONER GENERAL (TRA)...RESPONDENT

(Appeal from the Judgment and Decree of the Tax RevenueAppeals Tribunal at Dar es Salaam)

(Dr.Twaib,J. Chairperson Mr.J.Kalolo Bundala And Mr.D.Mwaibula -Members)

dated the 2nd day of May, 2017
in
Tax Appeal No. 19 of 2015

JUDGMENT OF THE COURT

26th June & 5th July,2018

MWARIJA, J.A.:

This appeal arises from the decision of the Tax Revenue Appeals Tribunal dated 2/5/2017 in Tax Appeal No. 19 of 2015. The facts leading to the appeal can be briefly stated as follows: The appellant, a limited liability company dealing with the business of production and supply of natural gas, was involved in a tax dispute with the respondent, The Commissioner General of the Tanzania Revenue Authority.

The appellant was dissatisfied with the decision of the respondent of disallowing depreciation expenditure from the former's financial return for the year 2009. The appellant objected the respondent's disallowance by

the respondent of the amount of USD 9,294,832.00. The amount which was in respect of wells SS 10 and SSW (the Assets) was disallowed on the ground that the same did not meet the conditions for depreciation allowance as stipulated under S. 17 of the Income Tax Act, No 11 of 2004. (the Act). The conditions are; firstly, that the depreciable assets must be owned by the concerned person and secondly, they must have been employed in production by that person during the relevant year of income.

On the part of the respondent, it's case was that, although the assets were owned by the appellant hence meeting the first condition above, they did not qualify for the second condition because they were not used in the production of the appellant's income in the relevant year of income. As a result, the appellant was issued with Assessment No. 420700898 of the amount in question.

Aggrieved by the respondent's decision, the appellant appealed to the Tax Revenue Appeals Board (the Board). In its decision, the Board found that the amount was rightly disallowed as it did not qualify for deduction on account that, although according to the Third Schedule to the Act (the Schedule), the wells fall under class 4 of depreciable assets, they

were not employed in the production of the appellant's income for the year of income 2009.

The appellant was further dissatisfied with the decision of the Board and thus appealed to the Tribunal. Its appeal was unsuccessful hence this appeal.

In its memorandum of appeal, the appellant has preferred two grounds as follows:

> "1. *That the Tax Revenue Appeals Tribunal grossly erred in law by interpreting section 17 of the Income Tax Act, 2004 in isolation of paragraph 1(3) of the Third Schedule to the Income Tax Act as far as oil and gas exploration companies are concerned.*
>
> *2. That the Tax Revenue Appeals Tribunal erred in law by upholding the Tax Appeals Board's decision of disallowing depreciation allowance on capital expenditure amounting to USD 9,294,832 incurred in drilling and construction of Wells SS*

10 and SSW in 2009, on the basis of the Respondent's position."

At the hearing of the appeal, the appellant was represented by Mr. Fayaz Bhojani, learned counsel whereas the respondent was represented by Mr. Juma Beleko, learned counsel. Both learned counsel had filed their respective written submissions in compliance with Rule 106(1) and (8) of the Tanzania Court of Appeal Rules, 2009. As a result, during their oral submissions, they adopted their written submissions and by way of emphasis, highlighted some of the points which they considered to be of vital importance in support of their positions.

In his submission, after having made a brief reference to the factual background of the parties' dispute, Mr. Bhojani argued the two grounds of appeal jointly. He submitted that, the Tribunal erred in failing to find that the expenditure qualified for depreciation allowance under S. 17 of the Act read together with the Schedule particularly paragraph 1(3) thereof. He stressed that the disputed amount was incurred in respect of natural resource prospecting, exploration and development and therefore, qualify for deduction. He went on to argue that disallowance of the amount on the ground that the assets were not employed in the production of the

appellant's income was erroneous. He submitted that both the Board and the Tribunal arrived at that finding without having properly directed themselves on the meaning of the word "employed" as used in S. 17 of the Act. It was Mr. Bhojani's argument that, had the Board and the Tribunal considered the meaning of that word in the context of oil and gas industry, they would have come to the conclusion that under paragraph 1(3) of the Schedule the expenditure incurred in respect of natural resource prospecting, exploration and development is treated as if it were incurred in securing the acquisition of the Assets and therefore the same qualify for depreciation allowance.

He argued that from the nature of the expenditure, that it involved the business of production of natural gas, which is a risky business, even if the Assets were not actually used in the relevant year of income, the same are deemed to have been employed in the production of the appellant's income. He stated as follows in his written submission:-

> *"Natural resource prospecting exploration and development is one of the riskiest business in the world. It is with that in mind that the legislature allowed the insertion of paragraph 1(3) such that*

depreciation deduction would be allowed to take place as it is deemed to have been incurred in securing the acquisition of an asset that is used in the production of income. This is specific to natural resource prospecting, exploration and development; which is the business of the appellant..."

In his further submission, the learned counsel for the appellant argued that both the Board and the Tribunal erred in relying on the principle of residual value as regards the Assets and by reading S. 17 of the Act in isolation of paragraph 1(3) of the Schedule which, by virtue of S.25 of the Interpretation of Laws Act [Cap. 1 R.E.2002], is part of the Act. He stressed that paragraph 1(3) is a special provision intended to carter for natural resources prospecting, exploration and development. He added that, going by the interpretation accorded to S. 17 of the Act by the Board and the Tribunal, that section will become redundant if it is not read together with paragraphs 1(3) and 1(1) of the Schedule.

In the circumstances, Mr. Bhojani argued that, regard ought to have been had to the words *"to the extent not otherwise provided"* appearing in paragraph 1(3) of the Schedule which, he said, qualify the words:-

> *"expenditure incurred by a person wholly and exclusively in the production of the person's income from a business in respect of natural resource prospecting, exploration and development shall be treated as if it were incurred in securing the acquisition of an asset that is used by the person in that production."*

He thus submitted that, from the use of the wording of that proviso and the use of the words *"to the extent not otherwise provided"*, the assets ought to be treated as if they were used in the production of the appellant's income. He stated so in the following words:-

> " *These words provide for depreciation allowance to be in use ('shall be treated as if') – in other words, all that is required is for the expenditure to have been incurred for the purpose of the business...."*

He argued further that the proviso was intended to apply where the law does not specifically provide for depreciation allowance regardless of

whether or not the assets were in actual use as is the position in the mining industry in terms of S.145 of the Act.

Supporting his submission that paragraph 1(3) of the Schedule is intend to allow deduction of depreciation in the oil and gas industry, the learned counsel referred the Court to the position which is applicable in other countries. He cited as examples, Australia and India. With regard to the position in Australia, he submitted that the concept of accelerated depreciation is applied whereby depreciation allowance for assets used in the production of oil and gas is claimed right from the first year of the taxable income. He relied on S. 40 -102(5) of that country's Income Tax Act, 1997 which allows deduction of depreciation on the basis of **capped life** of the assets used in extraction of oil and gas. He urged us to take inspiration from the position of the law as applied in that country as regards depreciation allowance in the oil and gas industry.

As for the applicable position in India, the learned counsel cited the cases in which provisions of that country's Tax Act, which corresponds with the provisions of S. 17 of our Act, was interpreted to the effect that a depreciable asset must not have been actually used in the production of the income in the relevant year of assessment. He cited *inter alia,* the

cases of **Whittle Anderson Ltd v. Commissioner of Income Tax,** Tax Reference (1971) 079 LTR 0613 (High Court of Mumbai), **Commissioner of Income Tax v Bharat Aluminum Co. Ltd** (High Court of Delhi) and **M/s Swati Synthetics Ltd v. Income Tax Officer,** ITA No. 1165/M/2006 (Income Tax Appellate Tribunal, Mumbai).

Mr. Bhojani argued also in the alternative firstly, that since depreciation on the Assets was allowed in the two previous years of 2007 and 2008, the respondent was not justified in disallowing it in 2009. Secondly, that depreciation ought to have been allowed by virtue of article 13 of the Production Sharing Agreement between the appellant and the Government. On that contention, he cited *inter alia* the Indian Cases of **Grasin industries Ltd v CIT** 32 TTJ and **Western India Vegetable Products Ltd v. CIT,** 26 ITR 151 which decided to the effect that, once the asset is ready for use after production agreement, depreciation is allowable regardless of whether or not the asset was used in the production of the income.

Thirdly, it was the learned counsel's argument that the Assets were drilled in 2007 as spare wells and were, at the same time, used to analyze data for the purpose of production forecast. In the circumstance, Mr.

Bhojani argued, the same were employed in the production of the appellant's income. Fourthly, the learned counsel submitted that even if depreciation allowance was not available to the appellant for reason of non-use of the Assets, it was still entitled to claim for depreciation allowance because, apart from having been classified under class 4, they also fall under class 7 of depreciable assets as provided under the Schedule.

In his reply submission, Mr. Beleko opposed the arguments made in support of the appeal. He submitted that the grounds of appeal are devoid of merit. He argued that the conditions for depreciation provided for under S.17 of the Act; that the Assets must be owned and employed by the appellant in the production of the income from which depreciation allowance was sought. According to the learned counsel, the parties were not at issue as regards the fact that the Assets were not used for production of the income for the year 2009.

The respondent's counsel went on to argue that, the Schedule provides for classes of depreciable assets and the manner of calculating depreciation allowance on those assets. He stressed that the Schedule

does not in itself, entitle a person to depreciation allowance. The learned counsel states as follows on pages 3 and 4 of his written submission:-

> " *Once a person is satisfied that he has met the ownership and usage conditions set in section 17 of the **Income Tax Act, 2004** he can then refer to the third schedule to the Act to determine the respective class of depreciation allowance he is entitled to and the manner to calculate.... The appellant herein has claimed deduction on the basis of paragraph 1(3) of the Third Schedule. This is wrong as the Third schedule cannot be used as the basis of claiming deduction while it is not a deduction provision."*

With regard to the appellant counsel's interpretation of S. 17 of the Act in reference to the position of the law as applied in Australia and India, Mr. Beleko argued that S. 17 of the Act is self sufficient as regards the conditions which a person must meet so as to benefit from depreciation allowance. He submitted that the said provision is clear and applies universally to all depreciable assets. It does not, he said, provide for specific circumstances under which, the use of an asset can be deemed

from the nature of the business industry as interpreted by the appellant's counsel.

As for the alternative arguments that the depreciation allowance was not disallowed in 2007 and 2008 and that the Assets attracted depreciation allowance on the basis of Production Agreement between the appellant and the Government, Mr. Beleko's response was that the same have been based on misrepresentation of the facts and improper interpretation of the law. Starting with the argument that depreciation allowance should not have been disallowed because it was previous allowed in the 2007 and 2008 years of income, he submitted that such an inconsistence on the part of the respondent should not be relied upon as an estoppel because the doctrine does not operate against performance by an authority, of a statutory duty. To bolster his argument, he cited the case of **Roshani Meghjee & Co. Ltd v commissioner General, TRA,** Civil Appeal No. 49 of 2008 (unreported).

As for the argument on the Production Sharing Agreement, the respondent's counsel replied that entitlement to depreciation allowance cannot be derived from the Agreement because, in any case, the same

would not override the mandatory provisions of the Act. He stressed that the finding of the Tribunal on that aspect was correctly arrived at.

Regarding the argument that the Assets were in use in the relevant year of the income because of the purpose for which they were secured, the learned counsel replied that since the hearing before the Board, the appellant did not deny that the same were not used in the production of the income, the issue whether or not the Assets were in use in 2009 for any purpose, cannot be raised at this appellate stage of the proceedings.

On the fourth alternative argument, Mr. Beleko argued that deduction for depreciation on the Assets falls under class 4 of the depreciable assets. He added that, even if the appellant was entitled to claim for depreciation allowance under class 7 of the depreciable assets, it must satisfy the two conditions stipulated under S.17 of the Act, the requirement which it did not meet.

We have duly considered the submissions of the learned advocates for the parties. The main issue for determination is whether or not the Tribunal erred in upholding the Board's interpretation of S. 17 of the Act thereby agreeing with disallowance by the respondent, of depreciation

allowance of USD 9,294,832 sought to be deducted by the appellant from its income for the year 2009. S. 17 of the Act provides as follows:-

> " *17. For the purpose of calculating a person's income for a year of income from any business, there shall be deducted in respect of depreciation of depreciable assets* ***owned and employed*** *by the person during the year of income* ***wholly and exclusively in the production of the persons income*** *from the business the allowance granted under the Third Schedule."* [Emphasis added].

The assets giving rise to the dispute are classified under class 4 as per paragraph 1(1) of the Schedule as follows:-

> " *natural resource exploitation and production rights and assets referred to in subparagraph (3) in respect of natural resource prospecting, exploration and development expenditure."*

Subparagraph (3) of paragraph (1) of the Schedule states as follows:-

" (3) to the extent not otherwise provided, expenditure incurred by a person wholly and exclusively in the production of the person's income from the business in respect of natural resource prospecting, exploitation and development shall be treated as if it were incurred in securing the acquisition of an asset ***that is used by the person in that production."*** [Emphasis added].

The main argument by Mr. Bhojani is that the provisions of S. 17 of the Act read together with paragraphs 1(3) and 1(1) of the Schedule entitled the appellant to deduction of depreciation even where the Assets were not actually employed in the production of the appellant's income for the year 2009.

From our interpretation of these provisions, which have been relied upon by the learned counsel for the appellant, we are with respect, of the view that as submitted by the respondent's counsel, the same entitles a person to depreciation allowance only upon meeting the two conditions stipulated under S. 17 of the Act. The depreciable assets must be owned and employed in the production of the income in question.

It is true that paragraph 1(3) of the Schedule provides that expenditure incurred by a person in the production of income from the business of natural resource prospecting, exploration and development shall be treated as if it were incurred in securing the acquisition of an asset. The provision goes on to state however, that such an asset must be "an asset that is used by the person in that production."

In our view therefore, although the expenditure incurred in the production of the income from the business of natural resource prospecting, exploration and development shall be treated as if it were incurred in securing the acquisition of an asset hence entitling the person to depreciation allowance on that asset, such an asset must have been used in the production of the income. In our view, that is the import of paragraph 1(3) of the Schedule.

The position of the law in Australia and India, to which Mr. Bhojani urged us to take inspiration, is different from the applicable law in Tanzania. From the provisions of s.40-102(5) of that country's Income Tax Act relied upon by the learned counsel, deduction of depreciation is based on capped life of the asset as from the first year of production of the

income. That method of deduction of depreciation is clearly provided by law.

As for the position in India, from the cases cited by the appellant's counsel, it is true that once an asset is kept ready for use, it attracts depreciation allowance. This method was however introduced through amendment of the law whereby, unlike in Tanzania, the method of basing depreciation allowance on individual asset was done away with and the **block asset concept** was introduced. The amendment was introduced through Taxation Laws (Amendment and Miscellaneous Provisions) Act, 1986.

It is for this reason that, in the case of **Swati Synthetics Ltd** (supra) cited by the appellant's counsel, it was stated as follows:-

> *" ... the condition/requirement of section of word 'used for the purpose of business' as provided in section 32(1) of the Act for the concept of depreciation on block of assets can be summarized that the use of individual asset for the purpose of business can be examined only in the first year when the asset is*

purchased. In subsequent years use of block of assets is to be examined. Existence of individual assets itself amounts to use for the purpose of business."

Similarly, in the case of **Bharat Aluminum Co. Ltd Case** (supra) also cited by the appellant's counsel, it was observed that:-

> *"Once the various **assets are clubbed together and become block assets** within S. 2(11) of the Act, for the purpose of depreciation, it is one **asset**. Every time, a new asset is acquired, it is to be thrown into the common hotchpotch i.e. block assets on meeting the requirement of depreciation allowable at the same rate."*

As stated above, the position in Australia and India is different because in those countries the law specifically provide for specific method of deduction of depreciation allowance on depreciable assets in the oil and gas industry. In Tanzania, under S. 17 of the Act read together with paragraphs 1(1) and 1(3) of the Schedule depreciation allowance is not based on block assets and therefore, as held by the Tribunal, for an asset

to qualify for depreciation allowance, a person must meet the two conditions of owning and using the asset in the production of the income in the relevant year.

On the alternative arguments made by the learned counsel for the appellant, we agree with the respondent's counsel firstly, that the fact that depreciation allowance was not disallowed in the 2007 and 2008, does not operate as an estoppel on the part of the respondent because the doctrine of estoppel does not operate against an authority in the performance of a statutory duty. In the case of **Roshani Meghjee (**supra) cited by Mr. Beleko, the Court stated as follows:-

> *"It is now settled law that there is no estoppel against the performance of a statutory duty".*

As for the arguments relating to the purpose of construction of the Assets and existence of a Production Sharing Agreement, we have found above that under our law, for an asset to attract depreciation allowance, the same must be used in the production of the income. In the circumstances therefore, we find that the two reasons relied upon by the

appellant's counsel would not make the Assets qualify for depreciation allowance.

The finding above also answers the fourth alternative argument, that the Assets could attract depreciation allowance under class 7 of the Schedule. In our considered view, the conditions stipulated under S. 17 of the Act apply generally and therefore the assets falling under class 7 of the Schedule are not an exception.

On the basis of the above stated reasons, we find that the appeal is devoid of merit. The same is thus hereby dismissed with costs.

DATED at **DODOMA** this 4th day of July, 2018.

I.H. JUMA
CHIEF JUSTICE

A.G.MWARIJA
JUSTICE OF APPEAL

R.E. MZIRAY
JUSTICE OF APPEAL

I certify that this is a true copy of the original.

S.J. KAINDA
DEPUTY REGISTRAR
COURT OF APPEAL