



# DECODING THE UTILIZATION OF UNRELIEVED TAX LOSSES VIDE THE INCOME TAX ACT

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Did you know that there exists a dedicated section in our Income Tax Act (ITA) relating to “Losses from business or investment”?

This is S.19 of the ITA.

In June 2020, vide the Finance Act, S.19 of the ITA was amended by including the following subsection:

S.19(2):

31. The principal Act is amended in section 19, by-
- (a) adding immediately after subsection (1) the following:
- “(2) Income of a person for the year of income having chargeable income and unrelieved losses for the four previous consecutive years of income may, subject to other limitations imposed by this section, be reduced by reason of use of the unrelieved losses which shall not be below thirty per centum of that income before any reduction for losses:
- Provided that, the requirement under this subsection shall not apply to a corporation undertaking agricultural business or providing health or education services.”; and
- (b) renumbering subsections (2), (3) and (4) as subsections (3), (4) and (5) respectively.

It has been observed that tax auditors are often invoking this sub-section to restrict utilization of losses against chargeable income of taxpayers.

That is to say, when a taxpayer has a chargeable income in Year 5, and unused carried forward tax losses from Year 1 to Year 4, **tax auditors are restricting deduction of accumulated tax losses** carried forward from Year 4 to Year 5 against chargeable income of Year 5.

The utilization is restricted to only 30% of chargeable income of Year 5, thereby subjecting 70% of chargeable income of Year 5 to Income Tax. Tax auditors however allow carry forward of unused tax losses thereafter to Year 6 but will subject it to the same restriction in Year 6 should Year 6 have chargeable income.

In my humble opinion, I beg to differ with the aforementioned tax treatment; and my justifications for the same are articulated hereunder:

To begin with. I wish to take the liberty to reproduce S.19(2) of ITA but this time with my own emphasis:

*“Income of a person for the year of income having chargeable income and unrelieved losses for the four previous consecutive years of income may, subject to other limitations imposed by this section, be reduced by reason of use of the unrelieved losses which shall not be below thirty per centum of that income before any reduction for losses:*

*Provided that, the requirement under this subsection shall not apply to a corporation undertaking agricultural business or providing health or education services.”*

The sub-section makes use of the word “MAY” and not “SHALL” or “WILL”.

This further takes me to the Interpretation of Laws Act, Section 53(1):

***“Where in a written law the word “may” is used in conferring a power, such word shall be interpreted to imply that the power so conferred may be exercised or not, at discretion”***

Hence this cements the fact that the restriction to utilize tax loss as stipulated in S.19(2) of ITA **is not imperatively commanding**. The power to exercise the utilization therefore ideally rests with the taxpayer and not otherwise. In simple English terms, it is optional.



Secondly, if we closely re-read S.19(2) of ITA, the phrase “**may, subject to other limitations imposed by this section**” undoubtedly attracts my attention. The condition to restrict use of tax losses is therefore just not optional but also condition precedent.

At this juncture, this leads me to read the entire Section 19 of ITA more closely as follows:

*19.-(1) For purposes of calculating the income of a person, other than a partnership or a foreign permanent establishment, for a year of income from a business or investment, there shall be deducted*

*(a) any unrelieved loss of the year of income of the person from any other business or investment; and*

*(b) any unrelieved loss of a previous year of income of the person from any business or investment;*

*(2) Income of a person for the year of income having chargeable income and unrelieved losses for the four previous consecutive years of income **may, subject to other limitations imposed by this section**, be reduced by reason of use of the unrelieved losses which shall not be below thirty per centum of that income before any reduction for losses:*

*Provided that, the requirement under this subsection shall not apply to a corporation undertaking agricultural business or providing health or education services.”*

*For purposes of subsection (1), a person may deduct an unrelieved loss-*

*(a) in the case of a foreign source loss from an investment, only in calculating the person's foreign source income from an investment;*

*(b) in the case of other losses from an investment, only in calculating the person's income from an investment;*

*(c) in the case of other foreign source losses, only in calculating the person's foreign source income;*

*(d) in the case of loss incurred on agricultural business, only in calculating the person's income derived from agricultural business; and*

*(e) in the case of loss incurred in dealing with a speculative transaction, only in calculating the person's income derived from a speculative transaction.*

***(3) Where a person calculates income for a year of income from more than one business or investment of the person, and deducts an unrelieved loss in more than one such calculation, the person may choose the calculation or calculations in which the loss or part of the loss is deducted.***

*(4) For the purposes of this section -*

*“agricultural business” means the practice of rearing of crops or animals including forestry, beekeeping, aqua-culture and farming with a view to deriving a profit but excludes processing of agricultural produce other than preparing such produce for the purpose of sale in its original form;*

*“loss” of a year of income of a person from any business or investment shall be calculated as the excess of amounts deducted in calculating the person's income from the business or investment over amounts included in calculating such income; “speculative transaction” means-*

*(a) a transaction which is a contract for sale or purchase of a commodity including stocks and shares settled otherwise than actual delivery or transfer of the commodity; or*

*(b) any agreement for repurchase or resale, forward sale or purchase, futures contract, option or swap contract; and “unrelieved loss” means the amount of a loss that has not been deducted in calculating a person's income under subsection (1) or section 26(3).*

From the above citation I see no explicit limitation(s) on deductibility of tax losses against business income for a resident entity operating in the United Republic of Tanzania that is carrying on normal business that is not related to agricultural, health, and education.

**However, if one refers to S.19(3) of ITA, one can easily infer that the choice provided to the taxpayer as to how she can allocate her unused tax losses amongst different business segments/units is what is directly related to S.19(2).**

This means that when a taxpayer has, say 3 business units, under the same legal entity, she can choose how to allocate her unused tax losses between these 3 business units as long as the deduction or utilization of tax losses per business unit is not less than 30% of the chargeable of that business unit.

**Based on above dissection and analysis of Section 19 of the ITA, one can easily conclude that the introduction of S.19(2) vide Finance Act 2020 was aimed at streamlining tax treatment relating to S.19(3) of ITA. This will ensure that there is some form of consistency and clarity in the tax treatment of tax losses for businesses that have more than one business segment.**

Moreover, it also prohibits taxpayers from subjectively applying tax losses to those business segments that would give them undue tax advantages, especially those engaged in prospecting and mining businesses.



This can be further confirmed via S.65F of the ITA:

*65F.-(1) The provisions of section 19 shall apply to unrelieved losses of a person from a separate mining operation with the following conditions*

*(a) losses from the separate mining operations may be deducted only in calculating future income from that operation and not income from any other activity whether a mining operation under a different mineral right, processing, smelting, refining or a non-mining activity;*

*(b) income from the separate mining operations may not be reduced by a loss from any other activity whether a mining operation under a different mineral right, processing, smelting, refining or a non-mining activity; and*

*(c) income from the separate mining operation for any year of income may be reduced by reason of the use of unrelieved losses from that operation subject to other limitations imposed by section 19 but not below thirty percent of that income before any reduction for losses.*

*(2) The perpetual loss-making corporation rules shall not apply in conducting mining operations under a prospecting licence.*

**Therefore, to sum up, introduction of S.19(2) of ITA is not aimed at restricting utilization of tax losses relating to past 4 consecutive years against current year chargeable income. Tax auditors should avoid invoking S.19(2) unfairly on businesses.**

What remains to be more interesting is the fact that the taxpayers' e-filing portal is not designed to permit such blanket restrictions on deductibility of tax losses.

#### **Caveat**

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*Hanif Fattehali Habib has an extensive auditing, tax and accounting career with experience in various roles spanning over 20 years. Prior to establishing his audit and tax consultancy firm M/S Hanif Habib & Cco., he served in leading audit firms in Tanzania. Hanif's solid experience, across various functions, is a testament to his diverse background within Audit, Tax and Finance. Hanif also chairs the technical committee of the Tanzania Association of Tax Consultants (TATC).*

