

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
APPEAL NO. 13 OF 2020

KENYA ASSOCIATION OF MUSIC PRODUCERS.....APPELLANT

VERSUS

COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGEMENT

A. INTRODUCTION

1. The Appellant herein, is a non-profit company limited by guarantee duly registered under the Companies Act 2015 within the Republic of Kenya and licensed by the Kenya Copyright Board to operate as a collective management organization to collect license fees and fairly distribute royalties to performers enabling them to benefit and make economic gain from their intellectual property and investment.
2. The Respondent is a principal officer appointed under and in accordance with Section 13 of the Kenya Revenue Authority Act, Cap 469 of the Laws of Kenya. Under Section 5 (1) the Kenya Revenue Authority is an agency of the Government for the collection and receipt of all revenue. Further, under Section 5 (2) with respect to the performance of its functions under subsection (1), the Authority is mandated to administer and enforce all provisions of the written laws as set out in Part 1 & 2 of the First schedule to the Act for the purposes of assessing, collecting and accounting for all revenue in accordance with the various tax laws.

B. BACKGROUND

3. The Respondent conducted a compliance check on the Appellant's tax affairs leading to an assessment on various tax heads. As a result of various engagements that followed, the Respondent issued a letter dated 24th April 2019 to the Appellant. The said letter outlined the issues that had been agreed upon including re-consideration of the withholding tax due leading to a re-computation of Income Tax and VAT due from the Appellant totaling Kshs. 35,547,037.00.
4. Vide a letter dated 9th August 2019 the Appellant wrote to the Respondent alleging that its tax agent had failed to lodge an objection despite being instructed to do so. In the same letter the Appellant sought extension of time in order to file a late objection in accordance with Section 51 (6) & (7) of the Tax Procedures Act, 2015. On 27th October 2019, the Respondent conditionally accepted the Appellant's late objection and requested the Appellant to provide documents in support of its late objection within fourteen (14) days.
5. On 22nd November 2019, after the lapse of the fourteen days, the Respondent wrote to the Appellant informing it that on account of its failure to provide documents, its objection notice was invalid and the assessed taxes remained due and payable.
6. The Appellant being dissatisfied with the Respondent's decision, filed a notice of appeal with the Tribunal on 6th January 2020.

C. APPEAL

7. The Appeal herein is premised on the following grounds;

- a. That the Respondent erred in fact and law in its demand for Income Tax Kshs 2,565,224.00 and Valued Added Tax of Kshs. 32,981,813.00 for the year of income 2016 as the said demand is not based on any material facts that have been provided by the Respondent.
- b. That the Respondent erred in fact and law in its demand by alleging that the funds in the Appellant's account should be adjusted to Income Tax and VAT.
- c. That the Respondent erred in fact and law by alleging that the Appellant is a business generating income, while in fact the Appellant is a trade association involved in collection of license fees and distribution of royalties to its members.
- d. That aside from the definition of business for VAT purposes, Part II of the First Schedule does further confirm that a trade association was never meant to be subject to VAT.
- e. That the Respondent erred in fact and law in that it out rightly contravened the doctrine of legitimate expectation that rest a presumption on the Commissioner to follow certain procedures in arriving at the tax liability and the benefits that accrue from it.
- f. That the Respondent failed to consider the provisions of Section 21 (2) of the Income Tax Act, Cap 470 of the Laws of Kenya, that a trade association can choose or elect, by notice in writing to the Commissioner of Domestic Taxes to be considered to be carrying out business chargeable

to tax in respect of any year of income. The Appellant has not made such an election and therefore, cannot be subjected to Income Tax and VAT.

- g. That the Appellant is established under Section 46 of the Copyright Act No. 12 of 2001 as a non-profit entity charged with the responsibility to collectively administer the rights of its members by collecting license fees and distribution of royalties without making any profit and therefore the Respondent's treatment of the Appellant's transactions for taxes is misconstrued.
8. In line with the above grounds, the Appellant makes the following prayers;
- a. The Respondent's demand for tax amounting to Kshs. 35,547,037.00 be struck out in its entirety.
 - b. The Respondent's action to demand underpaid taxes despite logical and cogent explanation being given to them be declared arbitrary, capricious, unreasonable, unfair and contrary to the administration of justice and legitimate expectation of the Appellant.
 - c. The Respondent, its employees, agents/other persons purporting to act on its behalf be barred and or estopped from demanding or taking away any further steps towards enforcement or recovery of principal tax, penalties and interest on the Respondent's demand.
 - d. The costs of this Appeal.
 - e. Any other remedies that the Honorable Tribunal deems just and reasonable.

D. RESPONSE TO THE APPEAL

9. The Respondent on his part avers as follows in response to the Memorandum of Appeal;
- a. In response to ground 1 and 2 of the Memorandum of Appeal the Respondent states that the assessment of Income Tax and VAT was well grounded as the Appellant is not subject to any exemption under the Income Tax Act or the VAT Act as the services offered are of a business nature. The issue of VAT and income tax exemptions are both tied to Section 10 of the First Schedule to the Income Tax Act.
 - b. Given the nature of incorporation, the Appellant as a limited company was acting as an agent of the artists in collection of royalties together with other licensed entities. This therefore means that the services were rendered by way of business and therefore could not meet the requirements for VAT exemption. The Appellant therefore was to comply with the applicable VAT Regulations including operating VAT upon attaining registration threshold.
 - c. In response to grounds 3 and 4 of the Memorandum of Appeal, the Respondent states that the Appellant does not qualify for exemptions under Part II of the First Schedule of the VAT Act as it has not met the conditions therein.
 - d. The Respondent states that it did not contravene any legitimate expectation as it followed due process including affording the Appellant an opportunity to present documents to support its assertions and therefore ground 5 of the Memorandum of Appeal and Paragraphs 5, 6, 7, 8, 9, 10 and 18 of the Statement of Facts are vehemently denied.

- e. Further to the foregoing, the Respondent reiterates that the Appellant failed to produce the documents requested for and that there was not any malice in issuing the letter dated 27th October, 2019 requiring the production of supporting documents and puts the Appellant to strict proof of these allegations.
- f. For an objection decision to be validly lodged Section 51 (3) of the Tax Procedures Act requires that among other conditions, all relevant documents relating to the objection must be submitted. The Appellant did not fully exercise its rights under the objection framework prior to proceeding to the Tax Appeals Tribunal.
- g. Ground 6 of the Memorandum of Appeal and Paragraphs 12, 13 and 14 of the Statements of Facts are denied as the Appellant is not registered as a trade association as per the provisions of the Income Tax Act and further and particularly that the Respondent is empowered by Section 34 (6) of the VAT approve if the Commissioner is satisfied that a person eligible to apply for registration has not done so in the specified timelines.
- h. In response to ground 7 of the Memorandum of Appeal and Paragraphs 17 and 19 of the Statement of Facts, the Respondent is empowered by Section 24 (2) of the Tax Procedures Act to issue or vary an assessment based on the information at his disposal.
- i. The Respondent reiterates that the Appellant did not declare all his income for the years 2016 and did not provide any documentation to support its objection therefore the assessment was warranted. Section 29 of the Tax Procedures Act mandates the Commissioner to make an assessment based on available information which is what the Respondent did in this case.

- j. The Respondent further reiterates that the assessments were correctly issued and conform to Section 31 of the Tax Procedures Act 2015 as the Appellant had not declared the assessed amounts in the stated period and failed to provide additional supporting documents. Being a resident company its tax obligations together with the applicable rates are clearly spelled out in the Third Schedule of the Income Tax Act.
 - k. During the period under review the Appellant did not have any valid exemption certificate for any of its activities as provided for in the First Schedule of the Income Tax Act. The Appellant states that it is a nonprofit making entity serving welfare of the artists and should therefore not be subjected to tax. It is worth noting that even where the Act provides for an exemption based on an entity's activities, the exemption is granted under Paragraph 10 of the First Schedule of the ITA.
 - l. The Respondent contends that an Appellant does not have right to invoke the jurisdiction of the Honorable Tribunal as there was no validly lodged objection which would have required the Respondent to issue a decision thereby causing an appeal therefrom.
10. The Respondent makes the following prayers through its Statement of Facts;
- a. The Appellant's Appeal be dismissed for lack of merit.
 - b. The Respondent's assessment of Kshs. 35,547,037.00 be upheld.
 - c. The Respondent be awarded the costs of the Appeal.

E. ISSUES FOR DETERMINATION

11. Having carefully reviewed the parties' pleading, the evidence and the submissions we note that the Appeal herein raise the following issues for determination by the Honorable Tribunal, namely;

a. Whether the Appellant provided the Commissioner with documents in support of its late objection notice.

b. Whether the Appellant is liable to Income Tax and Value added tax

F. ANALYSIS

a) Whether the Appellant provided the Commissioner with documents in support of its late objection notice

12. The Appellant submitted that vide a letter dated 24th April 2019 the Respondent agreed with the Appellant's position regarding the treatment of withholding tax and vacated the same. However, the assessment regarding Value Added Tax (VAT) and income tax was maintained and deemed due and payable. Subsequently, vide a letter dated 9th August 2019 the Appellant lodged a late objection notice enlisting the grounds of disagreeing with the Commissioner's assessment in respect of VAT and Income Tax. Additionally, following various correspondences between the Appellant and the Respondent, the Appellant on 16th October 2019 forwarded to the Respondent documents in support of its objection notice.
13. The Appellant further averred that to its bemusement and surprise, the Respondent out of malice on 20th December 2019, served the Appellant with a letter dated 27th October 2019 purporting to request for documents required

to support the objection as if they had not been supplied. The effect of this letter was that the Appellant's objection notice was invalid in law hence the Appellant's decision to appeal following the objection decision of 22nd November 2019.

14. On his part, it was submitted for the Commissioner that the Respondent accepted the Appellant's late objection notice conditionally and responded to the Appellant on 27th October 2019 informing it to provide documents. The said letter outlined the documents that were to be submitted to the Commissioner within fourteen (14) days of notice in order to validate the Appellant's objection notice.
15. It was further submitted for the Commissioner that despite being given an opportunity to provide additional documentation in support of the objection, the Appellant failed, refused and/or neglected to provide the same. In fact the only documents provided were the audited financial statements. The Respondent wrote to the Appellant after the lapse of the fourteen (14) days, informing it that due to failure to support the objection, the notice of objection was invalid as per the provisions of Section 51 of the Tax Procedures Act (TPA) 2015. As such, the amount assessed was therefore due and payable by the Appellant.
16. We have appraised our minds to the contending submissions by the parties herein and note that the bone of contention under this issue for determination is whether the Appellant provided documents in support of its objection. As we have stated elsewhere in this Judgement, the Respondent accepted the Appellant's late objection notice per the provisions of Section 51 (6) & (7) of the TPA 2015. This objection notice was filed with the Commissioner on 9th August 2019. Vide a letter dated 16th October 2019, the Appellant forward to

the Commissioner documents in support of the objection notice; a letter which was received by the Commissioner on 18th October 2019.

17. Vide another letter dated 27th October 2019, the Commissioner wrote to the Appellant requesting for documents in support of the objection notice. Notably, this letter was served on the Appellant on 20th December 2019 together the Commissioner's objection decision dated 22nd November 2019. In his objection decision, the Commissioner informed the Appellant that following the decision allowing the late objection and the request for documents contained in the Respondent's letter dated 27th October 2019, the Appellant failed to provide the documents requested for and as such the assessed taxes remained due and payable.
18. We note from the record that the Respondent's objection decision was issued erroneously and dishonestly considering that the said letter of 27th October 2019 was not served upon the Appellant in order that the Appellant may comply. In fact, the evidence submitted by both parties in this Appeal indicates that the Commissioner's letter of 27th October 2019 together objection decision of 22nd November 2019 were served upon the Appellant on the same day; 20th December 2019. It is therefore baffling how the Respondent herein expected the Appellant to comply with the request for documents given that the very request was not served upon the Appellant.
19. There is no reasonable way the Appellant could have known that the Commissioner needed additional documents in support of its objection; that on the 27th of October 2019 the Commissioner wrote a letter requesting for these documents within 14 days, without the Respondent dispensing with the service of the same. Maybe the Respondent has taken the fictional notion of telepathic service of documents a tad too seriously. In any event it should be noted that in the Appeal before us, though the Commissioner wrote a letter

to the Appellant on 27th October 2019, the same was not served on the Appellant until on 20th December 2019, close to a month after the objection decision was rendered. In the premise therefore, the Tribunal finds that the Appellant filed a notice of late objection in line with Section 51 (6) & (7) of the TPA 2015; an objection which meets the validity threshold of Section 51 (3) of TPA. We further find that the Respondent has woefully failed to introduce an iota of doubt in our minds that the Appellant failed to provide documents in this Appeal in light of the evidence before us.

b) Whether the Appellant is liable to Income Tax and Value added tax

20. Under this second issue for determination, the Appellant submitted that the Respondent erred in alleging that the Appellant is a business generating income, while in fact the Appellant is a trade association involved in the collection of license fees and distribution of royalties to its members. It was further averred that the Respondent failed to consider the provisions of Section 21 (2) of the Income Tax Act Cap 470, that a trade association can choose or elect, by notice in writing, to the Commissioner to be considered to be carrying out business chargeable to tax in respect of any year of income. The Appellant has not made any such election and therefore cannot be subjected to income tax and VAT.
21. The Appellant further submitted that it is established under Section 46 of the Copyright Act No. 12 of 2001 as a non-profit entity charged with the responsibility to collectively administer the rights of its members by collecting license fees and distribution of royalties without making any profit and therefore the Respondent's treatment of the Appellant's transactions for taxes is misconstrued. It was further submitted for the Appellant that the definition of 'business' for VAT purposes, Part II of the First Schedule to the VAT Act 2013

does further confirm that a trade association was never meant to be subject to Value Added Tax.

22. On his part, it was submitted for the Commissioner that the assessment of income tax and Value Added Tax is well grounded as the Appellant is not subject to any exemption under the Income Tax Act or the VAT Act as the services offered are of a business nature. The Appellant did not meet the requirement of Paragraph 10 of the First Schedule of the Income Tax Act as well as those of Paragraph 11 of the VAT Act 2013. Further, during the period under review the Appellant did not provide any valid tax exemption certificate for any of its activities as provided for in the First Schedule to the Income Tax Act. The Appellant's activities therefore fall within the ambit of a business as defined by the VAT Act 2013.
23. The Respondent further averred that the Appellant cannot be allowed to approbate and reprobate its activities. There is no evidence before the Tribunal on its claim that it is a welfare society or that it has contracts with clients or registration or any payment schedules to support its assertion that it merely collects on behalf of its members. Additionally, despite christening itself as an association, the Appellant's registration is that of a limited company registered by the Registrar of Companies. Associations, clubs and societies in Kenya are registered under the Societies Act. By simply including the name 'association' into its trading name, the Appellant never ceased being a resident company and is required to comply fully with applicable tax laws.
24. The Respondent further averred that the Appellant has been acting as an agent of the artists in collection of royalties together with other licensed entities. This therefore means that the services were rendered by way of business and therefore could not meet the requirements for VAT exemption. The Appellant

therefore was to comply with the applicable VAT Regulations including operating VAT upon attaining registration threshold.

25. We have reviewed the totality of the competing submissions by the parties herein and note what falls for our determination is whether Appellant due to its mode of incorporation stands to benefit from the VAT and Income Tax exemptions afforded to associations, societies and charitable organizations among others in the VAT Act and Income Tax Act. In this regard therefore, we note that the Appellant herein was incorporated on 11th December 2003 as company limited by guarantee under the now repealed Companies Act Cap 486 of the Laws of Kenya. In addition to this, we also note that the Appellant holds a certificate of registration of a collective management society from the Kenya Copyright Board. Given this, we shall determine whether the Appellant falls within the parameters of the Paragraphs 10 and 11 of the First Schedules to the Income Tax Act and VAT Act, respectively.

26. In the above regard, a proper starting point for this determination will be the provisions of Section 21 (2) of the Income Tax Act which stipulates as follows;

“A trade association may elect, by notice in writing to the Commissioner, in respect of any year of income to be deemed to carry on a business charged to tax, whereupon its gross receipts on revenue account from transactions with its members (including entrance fees and annual subscriptions) and with other persons shall be deemed to be income from business for that and succeeding years of income.”

27. The above provisions must be read in line with the provisions of Paragraph 10 of the First Schedule to the Income Tax Act which provides as follows;

“Subject to Section 26, the income of an institution, body of persons or irrevocable trust, of a public character established solely for the purposes of the relief of the poverty or distress of the public, or for the advancement of religion or education—

(a) Established in Kenya; or

(b) Whose regional headquarters is situated in Kenya,

In so far as the Commissioner is satisfied that the income is to be expended either in Kenya or in circumstances in which the expenditure of that income is for the purposes which result in the benefit of the residents of Kenya:

Provided that any such income which consists of gains or profits from a business shall not be exempt from tax unless such gains or profits are applied solely to such purposes and either—

(i) Such business is carried on in the course of the actual execution of such purposes;

(ii) The work in connexion with such business is mainly carried on by beneficiaries under such purposes; or

(iii) such gains or profits consist of rents (including premiums or any similar consideration in the nature of rent) received from the leasing or letting of land and any chattels leased or let therewith; and provided further that an exemption under this Paragraph—

(A) Shall be valid for a period of five years but may be revoked by the Commissioner for any just cause; and

(B) Shall, where an applicant has complied with all the requirements of this Paragraph, be issued within sixty days of the lodging of the application.”

28. The Appellant has also placed reliance on Paragraph 11 of the First Schedule to the VAT Act 2013 which stipulates thus;

“The supply of the following services shall be exempt supplies—

(11) The supply of—

(a) Services rendered by educational, political, religious, welfare and other philanthropic associations to their members, or

(b) social welfare services provided by charitable organizations registered as such, or which are exempted from registration, by the Registrar of Societies under Section 10 of the Societies Act (Cap. 108), or by the Non-Governmental Organizations Co-ordination Board under Section 10 of the Non-Governmental Organization Coordination Act, (No. 19 of 1990) and whose income is exempt from tax under Paragraph 10 of the First Schedule to the Income Tax Act (Cap. 470), and approved by the Commissioner of Social Services:

Provided that this Paragraph shall not apply where any such services are rendered by way of business.”

29. Our understanding of the above quoted provisions of the Income Tax Act and the VAT Act 2013 is that there are instances when certain entities are exempt from both Income Tax and Value Added Tax. In order to be so exempt, the entity in question must be based in Kenya and is either established solely for the purposes of the relief of the poverty or distress of the public or for the advancement of religion or education, or supplies services rendered by educational, political, religious, welfare and other philanthropic associations to its members.

30. Noteworthy also, for income tax purposes, is the fact that there are instances when such entities or trade associations may write to the Commissioner and elect that the income of a particular year be deemed to be chargeable to tax. In such instances, the entity's gross receipts on revenue account from transactions with its members (including entrance fees and annual subscriptions) and with other persons shall be deemed to be income from business for that and succeeding years of income.
31. In the Appeal before us, the Appellant is registered as a company limited by guarantee and has argued that due to the nature of its incorporation, it stands to benefit from the exemptions afforded by both the Income Tax Act and the VAT Act 2013. The Commissioner's sole objection to the Appellant's exemption claim is that the Appellant is incorporated as a limited company and as such any activity it undertakes or renders must be viewed as being undertaken or rendered by way of business. We are disinclined to accept the Commissioner's line of argument of a number of reasons.
32. In the first instance, the Appellant is not a company limited by shares but rather one limited by guarantee. This mode of incorporation plays a prominent role in the Appellant's chargeability to tax; a role which the Respondent has utterly failed to appreciate, or one it simply preferred to treat with such czarist ignorance given that the Appellant pointed the Respondent to the legal provisions that justified its exempt status in the letter of 9th August 2019. The Appellant to choose to incorporate itself as a company limited by guarantee, in no small part, because companies limited by guarantee are the legally preferred structure for non-profit companies, clubs, charitable trusts and other similar sets. This therefore squarely places the Appellant within the parameters, and the benefit, of Paragraphs 10 and 11 of the First Schedules to the Income Tax Act and VAT Act respectively.

33. Our above position is further buttressed by taking into consideration the provisions of Section 46 of the Copyright Act, 2001. Section 46 (4) of the Copyright Act stipulates as follows;

“The Board may approve a collecting society if it is satisfied that—

(a) The body is a company limited by guarantee and incorporated under the Companies Act (Cap. 486);

(b) It is a non-profit making entity;

(c) Its rules and regulations contain such other provisions as are prescribed, being provisions necessary to ensure that the interests of members of the collecting society are adequately protected;

(d) Its principal objectives are the collection and distribution of royalties; and

(e) Its accounts are regularly audited by independent external auditors elected by the society.”

34. The above provisions of the Copyright Act empower the Copyright Board to issue certificates to collecting societies if satisfied that the society, and we use this term loosely, has met the cumulative conditions listed in Section 46 (4) (a) to (e) of the Copyright Acts. These conditions are that the body is a company limited by guarantee and incorporated under the Companies Act (Cap 486) (now repealed), is a non-profit making entity, its rules prescribe provisions necessary to ensure that the interests of members of the collecting society are adequately protected, its principal objectives are the collection and distribution of royalties; and its accounts are regularly audited by independent external auditors elected by the society. It is because the Appellant fulfilled these conditions that the Copyright Board issued the Appellant with a certificate of renewal of registration of a collective management society. As such, the Respondent cannot be heard to claim that the services rendered by the Appellant were rendered by way of business. Had this been true, then the Appellant would not be holding the certificate of a collective management society.

35. Our second basis of disagreeing with the Commissioner's argument is premised on the provisions of Section 21 (2) of the Income Tax Act. Section 21 (2) of the Income Tax Act which recognizes instances where a trade association, however incorporated, may elect by writing to the Commissioner that its income for a particular year be charged to tax. In this Appeal, the Appellant has not written to the Commissioner electing that year of the years under assessment be chargeable to tax. Neither has the Respondent claimed or proved that such an election was made by the Appellant.
36. We must note that the approach taken by the Commissioner, for the most part in this Appeal, is that because the Appellant is a limited company, its services are rendered by way of business, without due regard to the method of liability limiting chosen. As a consequence of adhering to read this error-filled book, the Respondent has sought to levy Income Tax and Value Added Tax upon the Appellant when in fact the law has granted reprieve to the Appellant through exemption. In the premises therefore, we find that the Respondent's Income Tax and VAT assessment has no legal basis.

G. CONCLUSION

37. In line with the foregoing analysis, the Tribunal makes the following Orders;
- a. The Appeal herein be and is hereby found merited.
 - b. The Respondent's assessment dated 24th April 2019 and confirmed on 22nd November 2019 be and is hereby vacated.
 - c. Each party to bear its own costs.
38. It is so ordered.

DATED and **DELIVERED** at **NAIROBI** on this **23rd** day of **July, 2021**.


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MAHAT SOMANE
CHAIRPERSON


.....
WILFRED GICHUKI
MEMBER


.....
ROSE WAMBUI NAMU
MEMBER


.....
JOHN KINYUA WANGARI
MEMBER


.....
TIMOTHY CHESIRE
MEMBER

