

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL AT NAIROBI
APPEAL No.6 OF 2015

SUNMATT LIMITED..... APPELLANT

=VS=

THE COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGEMENT

INTRODUCTION

1. **SUNMATT Limited** (hereinafter referred to as the Appellant) lodged this appeal against the decision of the Commissioner of Domestic Taxes (hereinafter referred to as the Respondent) dated 1st March, 2012 and confirmed on 20th May, 2013 being a demand of Kenya Shillings Four Hundred and Twenty Two Thousand Seven Hundred and Forty Five (Ksh:422,745/=) for withholding tax payments made by the Appellant to one Cybercash Limited, (exclusive of penalties and interest).

BACKGROUND

2. The Appellant's main activity is importation in bulk and retailing clothing items and other allied goods. The Appellant sells its merchandise through its various branches.
3. During the period 2008 – 2011, the Respondent conducted a post audit on the Appellant's activities. It found out that the Appellant had a merchant agreement with Cyber Cash Limited whereby the latter issues smart cards to the Appellant's customers. The Appellant then awards loyalty points on goods purchased to the card holder and redeem loyalty points upon presentation by the said card holder or customer. For every point awarded to the customer, the Appellant pays Cybercash Limited Ksh:3/= and Cyber cash pays out Ksh:2/= for every point redeemed. It is noted that for the transactions to be valid, the process has to be done through an electronic point of sale, which is provided or

approved by Cybercash Limited. Cybercash Limited would at its cost supply the equipment and software to the Appellant.

4. The Respondent's audit further established that the Appellant made monthly payments to Cybercash Limited under the Merchant Agreement between them for the maintenance of the system for points awarded and redeemed from smart card customers. The Respondent made a finding that the service rendered by Cybercash Limited was a management service subject to withholding tax and assessed the Appellant for the same. The Appellant objected to the said assessment.

ISSUES FOR DETERMINATION

5. The Tribunal has carefully considered the Memorandum of Appeal, the Statement of Facts, the Respondent's Response and all Pleadings filed together with the evidence adduced and submissions by the parties and is of the view that the issues for its determination are as follows:-
 - i) Whether what the Appellant received from Cybercash Limited was a virtual good?
 - ii) Whether the services offered by Cybercash Limited to the Appellant are in the nature of management services.
 - ii) Whether withholding tax is applicable herein?

ANALYSIS

6. The evidence adduced confirmed that the Appellant is in the business of selling various types of goods in an effort to have a competitive edge over its competitors. The Appellant saw the need to reward its loyal customers with points for every purchase which are redeemable in exchange for goods.
7. To manage this loyalty scheme the Appellant entered into an agreement with Cybercash Card Limited to install equipment in their shops/premises so that the latter can register and issue loyalty/reward cards to the Appellant's customers. The equipment is provided to the Appellant at a cost as per Clause 11 of the agreement entered into between

Cybercash Card Limited and Sunmatt Limited (the Merchant) dated 25th September, 2005 which states as follows;

“ Cyber Cash Card Limited shall supply (at a cost) to the Merchant such equipment, stationery, decals and other promotional materials as may be required from time to time which items the Merchant will display prominently about its premises”

8. The Tribunal notes that this is contrary to what the Appellant stated in their Pleadings that it was offered free of charge. This is in reference to the Memorandum of Appeal and in particular in the Appellant's Statement of Facts paragraphs 7 and 8.

FINDINGS

9. As much as the Appellant and Cybercash Card Limited are separate legal entities, the Tribunal finds that Cybercash Card Limited performs certain operations for the Appellant, namely, but not limited to issuing of loyalty cards and providing infrastructure that records details of customers.
10. The Tribunal hereby makes a finding that the Merchant awards points on goods and services to cardholders as per paragraph 2 of the agreement entered into between the Appellant and Cybercash Card Limited. This is in tandem with the evidence of the plaintiff's expert witness tendered before the Tribunal. The same corroborated with the audit conducted by the Respondent.
11. The contention therefore that Cybercash Card Limited sells points to the Appellant is not correct. Based on this finding that the merchant awards the points as per paragraph 2 of the merchant agreement, it is evident that the Appellant does not buy any goods from Cybercash Card Limited but instead performs the services for the Appellant as per the said agreement.

The basis of awarding points by the merchant is on the value of goods and services purchased by the loyalty cardholder e.g. 1 point for every

Ksh.100/= spent, therefore the Tribunal disagrees with the Appellant's assertion that they buy points before hand which they subsequently award to their customers.

12. It is the Tribunal's determination that the contract entered into between the Appellant and Cybercash Card Limited is for services rendered by Cybercash Card Limited to the Appellant. This therefore settles issue number ii above.
13. As to whether Withholding tax is applicable on payments made by the Appellant to Cybercash Card Limited the Tribunal notes that from the agreement the latter is not selling any goods to the Appellant but instead has installed its infrastructure at the premises of the Appellant, to enable it perform some services for the Appellant.
14. The upshot of the above is that the Respondent has proved that the whole loyalty program was not a virtual good but a service and the activities of Cybercash Limited Card Limited involved management of the Appellant's loyalty reward system which services were in the nature of management services which attracted withholding tax.

The Tribunal finds that the Appeal herein lacks merit and is hereby dismissed.

There will be no Order as to costs.

THESE ARE THE ORDERS OF THIS HONOURABLE TRIBUNAL.

DATED and DELIVERED at NAIROBI this 9th Day of December, 2016

In the presence of:-

VINCENT MUTAI
for the Appellant

BEATRICE MACHARIA
for the Respondent


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JOSEPHINE K. MAANGI
CHAIRPERSON


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JOSEPH WACHIURI
MEMBER


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BONIFACE DIMMO
MEMBER