REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
APPEAL NO.51 OF 2016

TRANSACTION PAYMENT SOLUTIONS (K) LIMITED.....APPELLANT

VS

KENYA REVENUE AUTHORITY.....RESPONDENT

JUDGEMENT

BACKGROUND:

1. The Appellant, Transaction Payment Solutions Kenya Limited, **(TPSK),** is incorporated in Kenya under the Companies Act Cap 486 of the Laws of Kenya and registered as a taxpayer under PIN No. P051300984B. TPSK is related to Transaction Payment Solutions International, (TPSI), which is incorporated in Mauritius. TPSK offers management services to TPSI Mauritius.
2. The Respondent Kenya Revenue Authority is established under Section 3 of the Kenya Revenue Authority Act, Cap 469 - Laws of Kenya and is empowered under Section 5 to assess and collect tax revenue for the Government and to administer the various tax laws of Kenya.

CAUSE OF ACTION:

3. The Respondent issued confirmed assessments for Corporate Tax, dated 23rd March 2016 for Kshs.17,320,647 inclusive of penalties and interest which was communicated vide a letter dated same day captioned **"attached find reconfirmed Additional Assessment for ease of reference".**

4. The last paragraph of the letter stated in part;

"In the meantime we draw your attention to the provisions of Section 52 of the Tax Procedures Act 2015 (TPA) read together with Section 12 of Tax Appeals Tribunal Act 2013."

5. The Appellant had filed its Objection Notice with the Commissioner on 6th November, 2015.

GROUNDS OF THE APPEAL:

6. The Appellant filed the following as grounds of the Appeal;

   (A) Notification of Commissioners Confirmation of Assessment was out of time and therefore time barred.

   (B) Corporation Tax on VAT adjusted from turnover is inconsistent with the VAT Law, erroneous and it amounts to double taxation.

   (C) Corporation Tax on alleged undeclared sales on invoice number TPSK 142

   (D) Assessment of interest on late VAT at 2% instead of 1% as provided in TPA.

7. ISSUES FOR DETERMINATION:

a) Whether Commissioners confirmation of assessment was out of time and therefore time barred.

b) Whether Corporate Tax on adjusted VAT from Turnover is validly and legally charged

c) Whether Corporate Tax on undeclared sales on invoice TPSK42 should stand

d) Whether interest is charged at the correct rate as per the TPA.

APPELLANTS ARGUMENTS:

(A) Late Notification of Objection decision.

8. The Appellant points out that Section 113(1) of Tax Procedures Act, (TPA), 2015, which came into effect on 19th January, 2016, deals with transitional provisions for matters previously addressed under Income Tax Act, Value Added Tax and Excise duty and it states;

> " *subject to this section, this Act shall apply to any act or omission that occurred or is occurring, for which no prosecution has been commenced or any assessment made against which no Appeal has been made before the commencement date."*

While Section 113(2) of TPA states:

> "*any Appeal which or prosecution commenced before the commencement date may be continued and disposed of as if this act had not come into effect."*

9. The Appellant then points out that based on the above provisions, that TPSK had not filed any Appeal by the time TPA came into effect and that its Appeal therefore is governed by the provisions of TPA and should therefore be dealt with and concluded under TPA.

10. That in the objection decision made on 23rd March, 2016, the Commissioner has drawn the Appellant's attention to the provisions of Section 52 of the TPA, which confirms that the Confirmation of the Assessment was carried out under the provisions of TPA.

Section 51(11) of TPA provides that;

> "*where the Commissioner has not made an Objection decision within 60 days from the date the tax payer lodged a notice of objection, the objection shall be allowed."*

11. The Appellant points out that the Commissioner issued the objection decision on 23rd March, 2016, which is more than 60 days after 6th November 2015 when the Appellant lodged its Notice of Objection. The Appellant adds that even if the 60 days are counted from the effective date of the TPA, the Commissioner's decision, (Confirmation of Assessment), is still well beyond the 60 days time limit provided by the TPA.

12. The Appellant further states that by the Commissioner's delay is in breach of the taxpayer's right to Administrative Action as enshrined **in Article 47 of the Constitution of Kenya,** which right entitles one to;

    a. "***administrative action which is expeditious, efficient, lawful, reasonable and procedurally fair".***

13. The Appellant wishes to rely on the Landmark case of **(Republic v Kenya Revenue Authority Ex Parte Universal Corporation Ltd. 2016, eKLR, where Justice Odunga** held that;

    " A body entrusted with the collection of revenue ought not to be seen to be lethargic, in the conduct of its affairs and whereas the law allows KRA a period in which to confirm its records, that period ought not to be taken as a derogation of Article 47 of the Constitution, that requires that administrative action be carried out expeditiously".

14. The Appellant adds that this position is further supported by the ruling in **Barclays Bank of Kenya Limited v Commissioner General, Civil Appeal Number 67 of 1998,** where ***Justice Ole Keiuwua*** stated that;

    "the explanation offered by the Commissioner is not seeing that the Appeal was within the prescribed time, is hardly convincing

and totally inadequate". He deemed the omission a pathetic excuse."

15. The Appellant urges this Tribunal to consider the provisions of TPA with respect to its Appeal and allow the Appeal as per the provisions in Section 51(11) of TPA,

(B)." Corporation Tax on VAT adjusted from Turnover: ***(Treatment of VAT on Sales where the same is not collected from the customers)."***

16. The Appellant presents its argument by defining the principle and the mechanism of VAT as a tax and its impact on the supplier and the consumer. The Appellant points out that VAT is borne by the end consumer and not by the supplier's business (Appellant). It is therefore never a cost to the business, by design.

17. That by allowing suppliers to recover input VAT from output VAT, the aim and the objective of the tax law is to leave businesses in a neutral position but with a legal duty to act only as appointed agents for collection of the tax (VAT) and accounting to the Revenue Authority.

18. The Appellant points out that its invoices to its customers have therefore to be taken as VAT inclusive, in line with the principles of VAT as a tax not on business but on the final consumer. The effect of this is that the VAT element in the invoice cannot be and it is not part of the Appellant's revenue and needs to be reduced from the invoice value to arrive at a true business turnover of the Appellant. The net after VAT is what the Appellant has accounted for in its turnover for Corporate Tax purposes.

19. The Appellant avers that this is the principle enshrined in the VAT tax law and that by virtue of the Commissioner assessing Corporate Tax

on the VAT element netted off from the Invoice value, the Commissioner is in effect introducing an unwarranted cost burden to the Appellant equal to the Corporate Tax on VAT element, which is not legally right.

20. The Appellant crowns its above position by quoting Section 13 of the VAT Act 2013 which defines taxable value as the total of:

    a) *The amount of money paid or payable directly or indirectly for the supply or the open market value of the supply; and*

    b) *any taxes, duties, levies, fees and charges (other than VAT), paid or payable for the supply.*

21. The Appellant argues that while The Respondent (KRA) raised the issue of whether the VAT is incurred wholly and exclusively in production of taxable income, the Appellant is of a different view as it seeks to answer the question: What is the revenue to TPSK after the transaction?

22. The Appellant points out that the fact the TPSK initially made an error, which it corrected later, should not be used by KRA to punish the Appellant as a business and as a taxpayer.

23. The Appellant also points out that it actually overpaid tax through wrong calculation while in the process of correcting this error and that TPSK is not claiming a refund of that overpayment from KRA.

24. The Appellant prays that the Tribunal evaluates these averments and their merits and rules in its favour.

(C). Under declared Sales for 2014 (Invoice number TPSK 142)

25. The Appellant explains that this particular invoice was in a transitional state between two accounting periods, whereby the transaction

deposit had been made in 2014 but the transaction had not yet been consummated till 2015, when it was fully consummated and accounted for in income and in corporate tax. Although the Respondent had required it to be accounted for in 2014, the Respondent has subsequently withdrawn its claim for this requirement upon satisfaction that the entire transaction was accounted for tax purposes in the 2015 year of income.

(D) Computation of interest;

26. The Appellant claims that in computing interest, The Respondent has used 2% per month as provided for in the **VAT Act 2013**. However, under **Section 38 (1) of the Tax Procedures Act 2015,** which became effective on 19th January 2016, the rate of interest for all tax arrears is provided as 1% per month on straight line basis.
27. The Appellant prays that the Tribunal reviews this rate and rules that the rate provided for by the TPA, which applies to all assessments confirmed after 19th January 2016, be deemed as applicable since this assessment was confirmed during the TPA regime.
28. The Appellant prays that Honourable Tribunal considers the Appellant's Submissions above and:
    (a) Allows the Appeal and
    (b)Orders the Respondent to pay costs of appeal to the Appellant

RESPONDENTS ARGUMENTS:

29. The Respondent opened its submissions with what it deemed as a suspicious way by the Appellant in trying to reduce taxable income for corporate tax and proceeds to give a summary of its case.

30. That upon being prompted by the demand from the Respondent, for records to confirm tax compliance on various taxes, the Appellant made a voluntary self-declaration of VAT amounting to Ksh.37,389,884 and proposed payments for the principal tax of Ksh.21,895,747 in three equal installments, which it subsequently honoured and applied to the Cabinet Secretary -Treasury for waiver of interest, relying on Section 21 of the VAT Act 2013. Approval is still awaited.

31. The Respondent on realizing that the voluntary disclosure did not cover PAYE, WHT, decided to carry out an in-depth Audit which was communicated vide its letter dated 10th November 2014, prompting the initial tax payer interview on 9th December 2014.

32. The in-depth Audit established that the Appellant had not been making self-assessment returns since inception in 2009 while it had chargeable income under Section 3(1) and (2)(a)(i) of the Income Tax Act Cap 470.

33. Additionally, the Appellant had adjusted the Output VAT, which it paid under the voluntary declaration, from its gross sales income to arrive at declared turnover for income tax purposes. The Respondent added this back for taxation purposes by invoking the provisions of Section 15(1) of the Income Tax Act Cap 470, which states that only expenses which are fully and exclusively incurred in the production of taxable income may be allowed. The Respondent argued that the Appellant could not therefore be allowed to deduct Output VAT, since it is not an expense incurred wholly and exclusively towards production of taxable income.

The Respondent assessed income tax (corporate tax), inclusive of penalties and interest at Ksh.16,353,131

34. Withholding tax was assessed at Ksh.649,120 and the Appellant paid the entire amount inclusive of penalties and interest.

35. PAYE was assessed for the entire period amounting to Ksh.25,937,402 including penalties and interest. The Appellant has since paid the Principal tax of KSh.12,587,113 and applied to Cabinet Secretary Treasury for waiver of penalties and interest.

36. On Late notification of the Objection decision, the Respondent's position is as follows:

a) That the Appellant tendered it's Objection on 6th November 2015 was before the TPA came into effect and that the Objection was therefore under the provisions of the Income Tax Act Cap. 470.

b) That Section 113(2) of TPA which the Appellant has relied upon to raise a preliminary objection with regard to the notification of objection decision out of time, came into effect on 19th January 2016.

c) That at the hearing on 5th August 2016, Tribunal dismissed the Appellant's Preliminary Objection and opted to give its reasons for doing so in the main judgment.

d) In the written submissions the Respondent is urging the Tribunal to hold that it already made its decision on the preliminary objection and to find that although the Commissioner in the Notice of Confirmation of the assessed tax dated 23rd March 2016, refers to Section 52(1) and (2) of the TPA, this was only by way of communicating the recourses available to the tax payer but it did

not mean that the objection decision was issued under the TPA guidelines

e) The Respondent states that the letter dated 23rd March 2016, confirming assessment, was not an Objection decision under the provisions of TPA and further points out that the Appellant made its objection under Section 84(1) of the Income Tax Act Cap 470 which did not have any time limit for the Commissioner's decision on the objection.

f) The Respondent rightly states that with TPA coming into effect on 19th January 2016, it repealed Sections 84 to 91 of the Income Tax Act, thus eliminating the Local Committees and leaving the Appellant with the only recourse to appeal to the Tax Appeals Tribunal if dissatisfied with the Commissioner's Confirmation of Assessment.

g) The Respondent also gave the domicile of the Company's Finance Manager in South Africa as a contributory factor to the conclusion of the discussions in Nairobi.

h) The Respondent argues that allowing Section 51(11) of TPA to operate here amounts to retrospective application of the TPA and quotes the authority in the ruling on ***Keroche Breweries limited V Kenya Revenue Authority and five others, by Justice Nyamu.***

i) The Respondent argues further that the Commissioner on 23rd, March 2016, did not make an objection decision under the TPA but made a confirmation decision under provisions of the Income Tax Act Cap 470, which was in operation when the Appellant filed its Objection to the Assessment on 6th November 2015.

37. **On Corporation tax, on adjustment of Output VAT from Revenue for Corporate Tax purposes**, The Respondent Advanced the following arguments:

a) Although the Appellant has correctly stated that revenue for financial statement purposes is declared net of VAT and that as per Section 13(1)of VAT Act 2013, the taxable value for VAT is the same as income for corporation tax purposes, The Respondent cites Section 13(1) of VAT Act 2013 which states that: Subject to this Act, the taxable value of a supply including supply of imported services shall be:

i) The consideration for the supply; or

ii) If the supplier and the recipient are related, the open market value of the supply,

Section 13(3) Subject to subsections (4), to (6) the consideration for a supply, including supply of imported services, shall be the total of;

i) amount of money paid or payable directly or indirectly by any person for the supply or,

ii) the open market value at the time of the supply or an amount in kind paid or payable directly or indirectly by any person, for the supply and

iii) any taxes, duties, levies, fees and charges(other than the value added tax) paid or payable on, or by reason of supply, reduced by any discounts, or rebates allowed and accounted for at the time of supply.

38. The Respondent argues further that, by the above definitions, VAT does not form part of the consideration for the supply and the invoices issued for the supply were not tax invoices. The Respondent states that the invoices of the Appellant to its customer cannot be taken to be VAT inclusive since they do not conform to the features of tax invoice as outlined in **Legal Notice No.195 (4),** which, among other things, states that VAT must be clearly indicated in the invoice and if the invoice is VAT inclusive then it must state so. The Respondent highlights in part Sections and Sub Sections of Legal Notice No.195 in support of its point above.

39. The Respondent points out that Appellant in their own declaration treated the VAT as if invoices were VAT exclusive and so should now be estopped from treating the invoices as VAT inclusive. The Respondent does not accept that this was an error as claimed by the Appellant and adds that VAT therefore should not be adjusted by reducing the turnover for corporate tax purposes. To allow this adjustment is to allow an afterthought meant to reduce corporate tax turnover.

40. The Respondent avers that under Section 15(1) of the Income Tax Act, only expenses incurred wholly and exclusively for the production of taxable income are allowed and that VAT does not meet this criterion.

41. The Respondent also states that the Appellant did not recover the VAT from its customer and so it should be the one to bear the cost of non-compliance

42. There was an issue about invoice number TPSK 142 which has since been resolved.

43. The other issue relates to accruing interest on assessed tax at 2% instead of 1% as per provisions of the TPA. The Respondent points out that the interest at 2% is computed as provided in Section 77 of the Income Tax Act Cap. 470, and (Not VAT Act), and that this accrual is up to the time the TPA came into effect i.e. 19th January 2016 and from there onwards it is computed at 1% as per the TPA.

44. The Respondent urges the Tribunal to dismiss the Appellant's Appeal for lack of merit as it is issued by an Appellant who seeks to misinterpret the strict provisions of taxation in its favour.

ANALYSIS AND FINDINGS:

A. On late notification of the Objection decision:

45. On 5th August 2016, the Tribunal ruled against this ground by the Appellant as a preliminary objection, because it created and introduced a technicality which would have the effect of allowing the Appeal. This would have curtailed the opportunity for the parties to be given a fair hearing as well as an opportunity to present their substantive submissions and to fully canvass their issues. The Tribunal stated that the reasons for its ruling would be given in the main judgment. In so doing the Tribunal took cognizance of Article 50(1) of the Constitution of Kenya, which deals with the right to fair trial as read together with Article 48, which requires that all litigants before Courts and Tribunals, be afforded adequate opportunity to be heard, which right enjoins Courts and Tribunals to ensure, that all litigants are not only allowed, but also enabled to present all arguments and evidence which they desire to present before such Courts and Tribunals.

46. The Tribunal has examined arguments placed before it by the parties and observes that first; the TPA came into effect after the Appellant had already filed its objection against the assessment. According to the wording of the Section 51(11) of the TPA, which states;

> *"this Act shall apply to any act or omission that occurred or is occurring, for which no prosecution has been commenced or any assessment made against which no appeal has been made before the commencement date."*

47. The Tribunal finds that by the commencement date of the TPA, the Appellant had made no prosecution and filed no Appeal. The Appellant had only filed an objection with the Respondent and was awaiting the outcome (decision by the commissioner) which is referred to in the TPA as "Objection Decision".

48. With regard to Section 113(2) of TPA which states;

> *"any Appeal which or prosecution commenced before the commencement date may be continued and disposed of as if this Act had not come into effect"*

49. The Tribunal finds that no Appeal and no prosecution had been commenced by the Appellant before the effective date of the TPA, as the Appellant was still awaiting the Commissioner's decision on its objection, (Objection decision) and therefore this Appeal cannot be handled under the repealed sections of the ITA.

50. The Respondent has argued that the law that was applicable at the time of the Confirmation was the repealed sections of the Income Tax Act Section 84 to 91, basing its argument on the date of filing the objection with the Commissioner. The Respondent also states elsewhere that

Local Committees, and actions under the repealed sections, were no longer in existence, hence the Commissioner had to guide the taxpayer on the provisions of the TPA and the TAT which were the only laws available to the Appellant. The Tribunal finds that with the coming into effect of the TPA on 19th January 2016, such repealed sections of ITA were no longer applicable to the Appellant's Appeal since there was no appeal in the first place at that time. The Appellant's Appeal came up after Confirmation of the Assessment on 23rd March 2016. Further, since the provisions of the repealed sections of the Income Tax Act were no longer available to the Appellant, they were equally not available to the Commissioner, hence the Commissioner was bound to make its decision on the pending objection under the provisions of the new law, the TPA which he did on 23rd, March 2016.

51. The Respondent appears to mislead the Honourable Tribunal by arguing that confirmation of assessment decision made by the Commissioner on 23rd, March 2016, is not an Objection decision under the TPA!!. Well, what else could it be since by the time this decision was made to confirm the assessment, the only law available to both the Appellant and the Commissioner was the TPA?

52. The Respondent has tried to take refuge under "Retrospective Application" of the TPA and has quoted ***Hon. J. Nyamu's Ruling in Keroche Breweries Ltd.*** However, the Tribunal sees no such retrospective application of this law since the law is being applied with reference to the decision made to confirm the assessment after the Appellant had lodged its objection and which decision was made long after the commencement date of the TPA, and which led the Appellant

to lodge its Appeal after the ***notification of that confirmation decision***, the ***"objection decision".***

53. The Tribunal has therefore clarified the above issue by ruling against the notification of confirmation out of time, being guided by the Constitution of Kenya Article 50(1), in order to give the parties opportunity to fully canvass their submissions and that this purpose was fully achieved. The Tribunal will therefore examine the substantive facts of the case as presented by the parties in reaching its determination.

54. The Tribunal finds itself guided by the Ruling by Hon. Odunga J in **Republic v Kenya Revenue Authority Ex Parte Universal Corporation Ltd. 2016, eKLR.**

B.On Corporate tax on VAT adjusted from Turnover.

55. The Tribunal takes note of the provisions **of Section 15(1)** of the ITA, on the "wholly and exclusive" rule for the allowable expenses. However, much as VAT does not qualify under this criterion, The Tribunal finds that it is a tax and not an operational expense.

56. The Tribunal appreciates that the Appellant has absorbed the full burden of this tax instead of recovering it from its customers, and that this has the effect of reducing the revenue turnover which the Appellant can account for to its shareholders and to other stakeholders who include the Respondent as the tax Authority. The Tribunal finds that as per the adjustment made by the Appellant to pay VAT out of the sales receipts and since such part of the receipts from sales has been isolated and paid to the Respondent as VAT, it cannot therefore be

available as part of Turnover accountable to the Stakeholders who include the Respondent.

57. The Tribunal also notes that the act of voluntary self-declaration took place post facto (after the fact), and that at that time Appellant could only exercise limited options which were (i) to deny itself part of the sales revenue for accounting purposes equivalent to the VAT computed and paid, and by so doing, (ii) introduce a voluntary self-determined discount to its customers under Section 13(3)(iii) of VAT Act 2013

58. This way the VAT paid can be said to have been recovered from the Customers since part of what the customers paid has been isolated from their remittances and paid to the Respondent, thus reducing the turnover that the Appellant can account for in its books as Revenue.

59. The Tribunal also notes that by the Appellant treating the tax as VAT exclusive and applying the full rate on the Turnover billings, it actually paid more tax than was due if the VAT had been taken as inclusive in its billings. The Appellant has further stated that it is not claiming a refund of the inherent overpayment of the VAT. This way the Appellant has already absorbed a bigger burden of the tax than was due to the Respondent, had the billings been treated as VAT inclusive.

60. The Tribunal notes that the Appellant did not heed the Provisions of Legal Notice No.195, which guides taxpayers on documentation, on how to bill for VAT. However, the Tribunal also sees a taxpayer who has been non-compliant in the past but who has now been brought under compliance and has reformed as evident from the voluntary declaration and subsequent settlement of the principal taxes

enumerated above. The Appellant in its submissions has averred that it has put mechanisms in place and has taken steps to ensure that the past tax mistakes leading to non-compliance will not be repeated. The Appellant sounds remorseful and most likely it will be resourceful to the tax revenue for the subsequent years. Companies should be encouraged to observe compliance with tax laws.

61. The Tribunal finds that if the assessment raised by the Respondent is allowed, this will amount to Tax on (VAT) which is exempted by Section 13(3) (iii) of the VAT Act 2013. The Tribunal also notes that this will amount to (Double taxation) because the VAT has not only been paid but has indeed been overpaid.

62. The Respondent wants the additional tax to be seen as cost of non-compliance. The Tribunal observes that costs of non-compliance are provided for by legislation in the relevant tax laws and that it is not for the Commissioner to come up with additional non compliance costs. In this case, the costs suffered by the Appellant over and above the statutorily enforceable costs are nonetheless substantial as analyzed above. Thus far the Respondent has not persuaded the Tribunal on the issue of additional compliance costs to the Appellant, outside the specific tax legislation.

63. The Tribunal observes that the law cannot always be comprehensive and imaginative enough to provide for all possible occurrences likely to be encountered in life and in business, such as this particular one.

64. The Tribunal sees this particular case as somewhat unique and the circumstances equally so. The Tribunal finds itself, guided by the principle of **"Substance over Form".** Tax due has been paid. By not

adjusting the VAT on billings (Turnover), The Appellant will suffer additional tax on tax already paid. This has to be avoided.

65. In addition, it is not in doubt that after accommodating the VAT by reducing sales, the reality is that the Appellant earned less Turnover by the amount of VAT so paid and adjusted, which it can account to both the taxman and to its shareholders, which is the normal way which is the normal way of conducting business. In actual fact, Income tax is a share of operating profit between the Tax Authority and the Shareholders. The Tribunal has to remain cognizant of the actual effects and the impact on the business after analyzing the transactions, which have taken place.

66. The Matters of invoice TPSK 142 and also interest at 2% instead of 1% have since been resolved between the parties.

TRIBUNAL DECISION:

68. Based on the above analysis of the facts presented by the parties, The Tribunal orders as follows:

A) On late notification of the objection decision, i.e confirmation of assessment on 23rd March 2016, Tribunal rules in favour of the Appellant. The Appeal is allowed.

B) This ruling is further reinforced by the findings of the Tribunal in the analysis above with regard to the Adjustment of paid VAT on turnover, which the Tribunal also rules in favour of the Appellant.

C) There shall be no orders as to costs.

DATED and DELIVERED AT NAIROBI this..13th..DAY OF ..July...2017

In the presence of:- ..Joseph Musau.....for the Appellant

..Kenneth Kirugi.....for the Respondent

.....
GEOFFREY C KATSOLEH
CHAIRPERSON

.....
PANAGIPALLI V R RAO
MEMBER

.....
DANIEL TANUI
MEMBER

.....
GABRIEL KITENGA
MEMBER

.....
FRANCIS KIVULLI
MEMBER