REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
APPEAL NO. 121 OF 2016

INTERACTIVE GAMING & LOTTERIES LIMITED..... APPELLANT

VERSUS

COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGMENT

BACKGROUND

1. The Appellant is a company incorporated in Kenya and duly licensed to carry out the business of gaming and lottery.

2. The Respondent is a principal officer of the Kenya Revenue Authority, established under Section 11 of the Kenya Revenue Authority Act and is charged with the responsibility of collecting and accounting for taxes on behalf of the Government of Kenya.

3. The Appellant was licensed by the Betting Licensing and Control Board ('BLCB') and operated a short message service ('SMS') based public lottery system in partnership with Flint East Africa Limited ('Flint') who were its Premium Rate Service Provider ('PRSP') agent. There was in place a revenue share agreement between the two parties.

4. Under the terms of a separate agreement between Flint and Safaricom Limited ('Safaricom'), Flint would use the Safaricom's network to offer its services and Safaricom would collect, on behalf of Flint, the charges paid by the subscribers accruing out of the use of the services and remit the amounts collected to Flint.

5. The Respondent issued the Appellant with an Estimated Assessment Notice dated 17th June 2014 totalling **KShs 363,043,057.00** inclusive of interest and penalties. The tax assessment covered the period September 2010 to December 2012 and the amount comprised:

    a) **VAT of KShs. 299,101,799.00**;

    b) **Withholding tax of KShs. 37,805,963.00;** and

    c) **Corporation tax of KShs 26,135,295.00**

6. The Appellant moved to the High Court by way of Judicial Review (**HCCC 251 of 2015**) challenging the Respondent's decision. However, the Court, in a Ruling delivered on 25th May 2016, struck out the application on the ground that the Appellant had not exhausted the available statutory remedies prior to seeking relief from the High Court.

7. Following the above decision, the Appellant filed a Notice of Objection to the assessment on 17th June 2016 stating its grounds of the objection and seeking the tax assessment to be set aside.

8. The Respondent dismissed the Appellant's Objection and confirmed the assessment in a letter dated 16th August 2016.

9. Being aggrieved, the Appellant filed an Appeal against the Respondent's Objection Decision on 13th September 2016.

APPELANT'S CASE

10. The Appellant's grounds for Appeal are:

    a) That the Respondent violated the provisions of Section 85(1) of the Income Tax Act ('ITA'), Section 51(8) of the Tax Procedures Act, 2015 ('TPA') and Section 32A of the repealed VAT Act (CAP 476) by failing

to consider the Appellant's Notice of Objection and refusing to amend the assessment or make a determination based on the Appellant's grounds of objection to the assessment.

S.85(1) of ITA:

> ***"Where a notice of objection has been received, the Commissioner may— (a) amend the assessment in accordance with the objection; or (b) amend the assessment in the light of the objection according to the best of his judgment; or (c) refuse to amend the assessment."***

S.51(8) of TPA:

> ***Where a notice of objection has been validly lodged within time, the Commissioner shall consider the objection and decide either to allow the objection in whole or in part, or disallow it, and Commissioner's decision shall be referred to as an "objection decision".***

S. 32A (1) and (2) of Cap 476:

> ***(1) A person who disputes an assessment made upon him under paragraph 9 of the Seventh Schedule may, by notice in writing to the Commissioner, object to the assessment.***
>
> ***(2) A notice given under subsection (1) shall not be a valid notice of objection unless it states precisely the grounds of objection to the assessment and is received by the Commissioner within 30 days after the date of service of the notice of assessment; but if the Commissioner is satisfied that owing to absence from Kenya, sickness or other reasonable cause, the person objecting to the assessment was prevented from giving the notice within that period and there has been no unreasonable delay on his part, the Commissioner may, upon application by the person objecting, admit the notice after the expiry of that period and the admitted notice shall be a valid notice of objection.***

b) That the Respondent's Objection Decision did not provide a statement of finding and the material facts relied upon contrary to the provisions of Section 51(10) of TPA.

S. 51(10) of TPA:

"An objection decision shall include a statement of findings on the material facts and the reasons for the decision."

RESPONDENT'S CASE

11. The Respondent issued Flint with an estimated assessment for the period May to November 2010, and proceeded to appoint Safaricom as its agent for the remittances of the taxes assessed.

12. However, the Appellant sued Flint, Safaricom and the Respondent (**HCCC 115 of 2011**)) claiming that the bulk of the funds held by Safaricom on account of Flint and which the Respondent was seeking possession of belonged to the Appellant. In a Judgment dated 30th April 2014, the court found that the bulk of the funds sought by the Respondent did indeed belong to the Appellant by virtue of being the lottery owner.

13. On June 2014, the Respondent issued the Appellant with an estimated assessment amounting to KShs 363,043,057.00 for VAT, Withholding Tax and Corporation Tax. The amount also included penalties and interest.

14. The Appellant moved to the High Court seeking Judicial Review orders to quash the Respondent's decision (**HCCC 251 of 2014**). The High Court however struck out the application, and held that the Appellant had not exhausted the alternative Statutory remedies available for resolving the matter.

15. The Appellant thereafter filed its Notice of Objection with the Respondent on 17th June 2016.

16. The Respondent submits that it sought more documents and information from Safaricom to assist it in preparing its Objection Decision. However, Safaricom refused to submit the documents requested.

17. The Respondent also avers that it then invited the Appellant for a meeting on 8th August 2016 to discuss the way forward, but the Appellant declined to attend the meeting prompting the Respondent to confirm the assessment and issue an Objection Decision.

18. In the Respondent's Statement of Facts the Respondent stated that upon scrutinizing the Appellant's Memorandum of Appeal and the Supporting documents, it sought to revise the assessments in accordance with the Appellant's audited accounts as follows:-

a) Income Tax	Kshs.4,262,471.00
b) Withholding Tax	Kshs. 975,709.00
c) VAT	Kshs.15,980,197.00

19. The Respondent prayed that the Tribunal enters Judgement in its favour against the Appellant in terms of these revised assessments.

SUBMISSIONS BY THE PARTIES

On the Corporation Tax Assessment

20. The Appellant avers that the Corporation tax assessment of **Kshs. 26, 135,295.00** be set aside on the following grounds:

    a) That the Respondent erred by issuing the tax assessment on the basis of Section 73(3) of the Income Tax Act. The Appellant submits that the

said section only applies in instances where a tax payer has not filed its returns for that year of income. That the Appellant had however filed its self-assessment returns for the years of income 2010 and 2011.

S.73(3) of ITA:

"Where a person has not delivered a return of income for any year of income, whether or not he has been required by the Commissioner so to do, and the Commissioner considers that the person has income chargeable to tax for that year, he may, according to the best of his judgment, determine the amount of the income of that person and assess him accordingly; but such assessment shall not affect any liability otherwise incurred by such person under this Act in consequence of his failure to deliver the return."

b) That the Respondent's assessment was not based on Appellant's income for the years 2010 and 2011. The Appellant submits that its income for the two years as per the company's audited Financial Statements was KShs 189,476,234.00, and not the amounts indicated in the Respondent's assessment.

c) The Appellant submits that it's profit before tax amounted to KShs 14, 208,237.00 and this is the amount that was subjected to income tax. That the Respondent had however based its assessment on KShs 82,969,189.00, an amount that exceeded the Appellant's taxable profits.

d) That the Respondent's actions are contrary to Section 3(2)(a) of ITA which provides that income tax is only chargeable on the gains or profits of a business.

Section 3(2) of ITA:

Subject to this Act, income upon which tax is chargeable under this Act is income in respect of

(a) gains or profits from-

(i) any business, for whatever period of time carried on;

(ii) any employment or services rendered;

(iii) any right granted to any other person for use or occupation of property;

21. The Respondent agrees that the Appellant had reported a taxable profit of KShs 14,208,237.00 in its self-assessment return for year 2011 which resulted in a Corporation Tax of Kshs 4,262,471.00. The Respondent however submits that the Appellant had proposed to offset this amount against its withholding tax credits of Kshs 7,322,782.00 but the set-off proposal was not acceptable to the Respondent. According to the Respondent, this amount (KShs 7,322,782.00) had been paid to the Appellant by Safaricom in accordance with the Judgment of High Court in **HCCC 115 of 2011**.

On the Withholding Tax Assessment

22. The Appellant submits that the assessment of withholding tax amounting to **KShs 37,805,963.00** be set aside for the following reasons:

    a) The Appellant submits that whereas it has incurred legal and consultancy expenses amounting to Kshs 18,814,174.00 and Kshs. 700,000.00, respectively, these amounts remained unpaid at the time of the assessment. That the Respondent had therefore erred in demanding withholding tax on these amounts by virtue of not having been settled.

b) The Appellant further contends that the Respondent had, in a letter dated 14th January 2011, appointed Safaricom as its tax agent in respect of all payments made to Flint who were the Appellant's PRSP agent. Accordingly, all the payments made to the Appellant had been paid net of Withholding Taxes.

c) That, in any event, the Withholding Tax amount is based on an unreasonable amount of KShs 395,763,035.00 which is more than the Appellant's income as per its audited financial statements.

23. Meanwhile, the Respondent is in agreement that the withholding tax demanded of KShs 975,709.00 is in respect of legal and consultancy services incurred and expensed by the Appellant amounting to KShs 18,814,174.00 and KShs 700,000.00, respectively. Whereas the Appellant contends that these fees remained unpaid, the Respondent submits these amounts had been expensed in Appellant's books of account and therefore the Withholding Tax liability had crystallized.

24. The Respondent contends that these amounts were deemed to have been paid within the meaning of Section 2 of ITA and therefore the tax was also due and payable. That "paid" in Section 2 of ITA is defined as follows:

> ***"paid" includes distributed, credited, dealt with or deemed to have been paid in the interest or on behalf of a person and "pay", "payment" and "payable" have corresponding meanings."***

25. The Respondent submits that its position is supported by the decision by the Court of Appeal in **KENYA REVENUE AUTHORITY-VS-REPUBLIC (EX-PARTE FINTEL LTD) [2019] eKLR.** In this case, the Court clarified the meaning of "paid" and stated as follows:

"The Income Tax Act has given the word "paid" a technical as opposed to an ordinary definition. Tax law is ever changing, complicated and highly technical. That is why we, with respect disagree with the learned Judge for insisting that "upon payment" must only convey the meaning that money or some valuable thing was delivered. He gave the phrase a very narrow construction. In the context of the Income Tax Act, payment is deemed to have been made even when no money has passed over. We therefore reject the contention that it was not practical to deduct and remit the tax without first actually paying the interest to the contractor. Although section 35(5) requires that where withholding tax is payable, the tax payer must "deduct" and remit the amount so deducted to the Commissioner, the sense in which the word "deduct" is used, as an accounting term refers to the act or process of subtraction of an item or expenditure from gross income to reduce the amount of income subject to income tax. This need not be done physically or practically but as a book entry."

26. The Appellant however argues that the aforementioned Court of Appeal judgment was delivered in February 2019 yet this dispute relates to the year of income 2011. That the Appellant had relied on the prevailing precedents of both the High Court and Court of Appeal that were applicable at that time and stated that Withholding Tax was due upon actual payment of the fees. These precedents included **STANBIC BANK KENYA LTD-VS-KENYA REVENUE AUTHORITY (CIVIL APPEAL NO. 77 OF 2008), REPUBLIC-VS-KENYA REVENUE AUTHORITY (*ex-parte* FINTEL): HIGH COURT MISC. APPLICATION NO. 1768 OF 2004 AND PRIMAROSA FLOWERS LIMITED-VS-COMMISSIONER OF INCOME TAX [2017] eKLR.**

On the VAT Assessment

27. The Appellant submits that VAT assessment of **KShs 299,101,799.00** be set aside on the following grounds.

a) The Appellant contends that it did not supply taxable goods or services within the provisions of the VAT Act. Services rendered by the Appellant were made through Flint which was its PRSP agent. Flint, in turn, had appointed Safaricom as its agent.

b) That the Respondent had, in a letter dated 14th January 2011, appointed Safaricom as its Withholding Tax agent. Any amounts due to the Appellant were paid net of any Withholding Tax and VAT pursuant to the Order of High Court in Civil Suit Number 115 of 2011.

c) The Appellant submits that the Respondent's assessment for VAT includes a period when the Appellant had not been incorporated and was not in operation. That part of the VAT assessment amounting to KShs 299,101,799.00 comprises penalties totalling KShs 100,000.00 (i.e., KShs 10,000.00 per month for the period January 2010 to October 2010) and interest amounting to KShs 166,231,095.00 for similar period. This is notwithstanding the fact that the Appellant was only incorporated in September 2010 and was not liable to file any VAT returns prior to its incorporation.

28. The Respondent submits that it relied on the provisions of Section 9(6) of the repealed VAT Act (Cap 476) which provided as follows:

"In calculating the value of betting and gaming services—

(a) the amount staked by a person shall be deemed to be the consideration for the supply of a service; and
(b) the taxable value of a supply under paragraph (a) for any tax period shall be the total amount staked less the amount of winnings (if any) during that tax period and the taxable value shall be deemed to be inclusive of tax"

29. The Respondent avers that it computed the VAT amount of KShs 15,980,197.00 by deducting KShs 89,600,000.00 from its declared income of KShs 189,476,234.00.

30. With regard to the Appellant's argument that the VAT had been deducted and withheld by Safaricom Limited, the Respondent submits that the Appellant still had an obligation to file its returns and account for taxes withheld in accordance to Rule 6 of the VAT (Withholding Tax) Regulations, 2004, but the Appellant did not do so.

31. The Respondent further submits that the Appellant did not make available a withholding VAT certificate to prove that the taxes had been withheld and accounted for by Safaricom Limited.

ISSUES FOR DETERMINATION

32. The Tribunal has framed the following to be the issues for determination:

i. **Whether the issue of taxes demanded from the Appellant by the Respondent had been determined by the High Court in Civil Case Number 115 of 2011 and the matter was therefore *Res Judicata*.**
ii. **Whether the Appellant is liable to pay the assessed Corporation Tax of KShs. 26,135,295.**
iii. **Whether the Appellant is liable to pay withholding tax of KShs 975,709.00.**
iv. **Whether the Appellant is liable to pay VAT of KShs 15,980,197.00.**

ANALYSIS AND FINDINGS

i. Whether the issue of taxes demanded from the Appellant by the Respondent had been determined by the High Court in Civil Case Number 115 of 2011 and the matter was therefore *Res Judicata.*

33. The main issue for consideration before the High Court in HCCC 115 of 2011 was to whom the sum of money in the possession of Safaricom belonged between the Appellant, the Flint and the Respondent. The Court clarified in Paragraph 65 of its Judgment in the said case that the claim by the KRA, the Respondent herein, was against the Flint (the 1st defendant in the suit), and not against the Plaintiff. The claim was in respect of Flint's liability for payment of taxes demanded by KRA.

34. Also, in the subsequent case filed by the Appellant (**HCCC No. 251 of 2014**) the Court held that KRA's claim for payment of taxes in **HCCC115 of 2011** was against Flint and not against the Appellant. That KRA was not making any claim for taxes against the Appellant.

35. In **HCCC No. 251 of 2014,** the Appellant had sought Judicial Review Orders of Certiorari & Prohibition against the Respondent's Notice of Assessment of Value Added Tax, Withholding Tax & Income Tax dated 17th June 2014, the subject matter of this dispute.

36. The Court in its judgment observed *inter alia* that this should not be interpreted to mean that the Appellant did not owe KRA any sums in form of taxes. In other words, the issue of the amount, if any, owed to KRA by the Appellant was never determined in the said proceedings. In the Court's view, KRA could not, by virtue of the said Judgement, be barred from making a claim for taxes against the Appellant.

37. The Appellant's argument that the matter is *Res Judicata* is, in the considered view of the Tribunal, not tenable.

ii. <u>Whether the Appellant is liable to pay the assessed Corporation Tax of KShs. 26,135,295.</u>

38. The Respondent's assessment of Corporation Tax of 6th June, 2014 was KShs. 26,135,295.00 which is the subject of the Appellant's Appeal. The Appellant has prayed that this assessment be set aside.

39. On the other hand, the Respondent submitted in its Statement of Facts that it intends to vacate the estimated assessment and enforce the Appellant's self-assessed tax.

The Appellant admits that it made a taxable profit of KShs 14,208,237.00 for the year of income 2011. This is also reflected in its audited Financial Statements for the year ended 31st December 2011. The Financial Statements further reflect a tax liability for that period amounting to KShs 4,262,471.00.

40. Additionally, the Appellant's self-assessment return for year 2011 which was filed with the Respondent on 10th June 2014 reflects a tax liability of KShs 4,262,471.00. However, the Appellant has set-off this tax liability against a Withholding Tax credit amounting to KShs 7,322,782.00 in its self-assessment return.

41. The Respondent has submitted that the Appellant has not attached or submitted any evidence to show payment of the Withholding Taxes that would entitle it to a set-off against its Corporation Tax liability either fully or partially.

42. It is this Tribunal's view that unless proof of payment of the Withholding Tax is provided to the Respondent then the Appellant's claim for a set-off shall fail and the Corporation Tax liability shall be due and payable.

43. Since the Respondent in its filings prays that its Assessments be revised, it means that the estimated assessment was erroneous without making any express admission. The Respondent's estimated assessment of KShs. 26,135,295 is not payable by the Appellant and is set aside.

44. In view of the conflicting positions between the Appellant and the Respondent on this issue, the Respondent will, in light of the new information availed, proceed to review the Corporation Tax payable and issue an amended assessment.

iii. <u>Whether Appellant is liable to pay withholding tax of KShs 975,709.00.</u>

45. The Appellant has claimed as deductible expenses KShs 18,814,174.00 and KShs 700,000.00 with respect to legal and consultancy services in audited financial statements.

46. The Respondent in support of its case has relied on the Court of Appeal decision in the ***Fintel*** case. The Court held that payment is deemed to be made even where no money has passed over. The Court defined "paid" to include distributed, credited, dealt with or deemed to have been paid in the interest or on behalf of a person. In doing so, the Court of Appeal overturned an earlier High Court decision which was in favour of the taxpayer. The High Court held that payment implies delivery of money or some other valuable thing and that payment was prerequisite for withholding tax to apply.

47. However, the Appellant argues that not only had it placed reliance on the earlier decisions of the High Court in the ***Fintel*** *and* ***Prima Rosa Flower*** cases, but also on the Court of Appeal decision in the ***Stanbic Bank*** case whereby the view was that Withholding Tax can only be due upon payment

48. The Withholding Tax demanded is in respect of a Notice of Assessment dated 17th June 2014 and the Notice of Appeal is dated 13th September 2016. On the other hand, the decision in the ***Fintel*** case was rendered on 5th February 2019.

49. It is the Tribunal's view that the Appellant's argument that it had relied on the earlier decisions which had held that payment was prerequisite for Withholding Tax to be due. The Tribunal finds that retrospective affirmation of the decision in the ***Fintel*** case would be unfair and occasion an injustice to the Appellant.

iv. <u>Whether the Appellant is liable to pay VAT of KShs. 299,101,799.00.</u>

50. The Appellant has averred that it was liable for payment of VAT on its supplies. Our perusal of the repealed VAT Act (Cap 476) however established that *winnings arising from betting, lotteries and gaming activities* were a taxable supply since they neither exempt nor zero-rated supplies under the Third Schedule or the Fifth Schedule to the Act.

51. In fact, Section 9(6) of Cap 476 even prescribed the method for determining the taxable value of winnings arising from betting, lotteries and gaming activities. The Tribunal therefore disagrees with the Appellant's argument that it did not make a taxable supply.

"Section 9 (6) of Cap 476:

In calculating the value of betting and gaming services—

(a) the amount staked by a person shall be deemed to be the consideration for the supply of a service; and

(b) the taxable value of a supply under paragraph (a) for any tax period shall be the total amount staked less the amount of winnings (if any) during that tax period and the taxable value shall be deemed to be inclusive of tax."

52. With regard to the Appellant's contention that the VAT had been deducted and withheld by Safaricom at source, it is the Tribunal's view that the burden of proving the same lies with the Appellant. Unless satisfactory evidence is provided to the Respondent to prove the same, then the VAT demanded is due and payable. In any case, if any VAT was deducted and withheld by Safaricom, then that would be on account of Fint's invoice to Safaricom as there was no direct nexus between the Appellant and Safaricom, such event would also not exempt the Appellant from its obligation to file its VAT returns and account for tax under the VAT Act and its Regulations.

53. Rule 6 of the VAT (Withholding Tax) 2004 provides as follows: -

"The withholding tax by a tax withholding agent shall not relieve a supplier of any obligation to file returns in accordance with the Act."

54. The Respondent relied on this rule and correctly pointed out that whether or not Safaricom withheld any taxes was immaterial as the Appellant had an obligation to file its returns and account for taxes withheld, if any, which the Appellant failed to do.

55. In the Respondent's submissions, it has varied the VAT demand made against the Appellant to Kshs 15,980,197.00 based on the declared income and urged the Tribunal to find that the revised sum is what is due and payable. The Tribunal refuses to be taken along this path.

56. This is yet another admission that the Notice of Assessment of 6th June, 2014 was erroneously arrived at and is as such not due. The Tribunal finds little difficulty in setting the same aside based on this admission.

57. With regard to the late filing penalty levied by the Respondent, the Tribunal notes that the Appellant was incorporated on the 17th of September 2010. As such it was not in operation and should not have been expected to file returns when it did not exist. As such the penalties levied for late filing for the period prior to the Appellant commencing its operations are set aside.

58. In view of the fact that the Respondent has substantially shifted ground with regard to the original assessments, it is appropriate for the Tribunal to direct that the Respondent reviews its assessments in respect of the Appellant and issues fresh assessments based on the available information.

FINAL DETERMINATION

59. The Tribunal makes the following final Orders:

    i. The Respondent's Corporation Tax, Withholding Tax and VAT assessments be and are hereby set aside.

    ii. The Respondent do proceed to review the Appellant's records and issue appropriate tax assessments.

    iii. Each party shall bear its costs.

60. It is so ordered.

DATED and **DELIVERED** at **NAIROBI** on this **16th** day of **April, 2021.**

.....
PATRICK LUTTA
CHAIRPERSON

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HELEN BILA
MEMBER

.....
MWAI MBUTHIA
MEMBER

.....
ELISHAH NJERU
MEMBER

.....
HABON FARAH
MEMBER