REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
TAX APPEAL NO. 329 OF 2019

SIDIAN BANK KENYA LIMITED ..... APPELLANT

VERSUS

COMMISSIONER OF DOMESTIC TAXES ..... RESPONDENT

JUDGMENT

BACKGROUND

1. The Appellant is a limited liability company incorporated in Kenya and is licensed under the Banking Act Cap 488 of the Laws of Kenya. The Appellant's principal business is the provision of an extensive range of banking, financial and related services.

2. The Respondent is a principal officer appointed under Section 3 of the Kenya Revenue Authority Act, Chapter 469 of the Laws of Kenya and is charged with the mandate of assessment, collection, and accounting of government revenue.

3. The Respondent carried out a review of the Appellant's published audited financial statements, audited annual reports and Excise Duty returns for the period January 2016 to September 2018.

4. Following the review, the Respondent issued the Appellant with an Excise Duty Assessment dated 11th March 2019. In the said Assessment, the Respondent demanded unpaid Excise Duty amounting to Kshs. 48,130,740.00, inclusive of penalties and interests.

5. The Appellant vide a letter dated 5th April 2019 objected to the Respondent's assessment disputing the amount of assessed Excise Duty relating to income earned from non- licensed activities such as money transfer services and rental income. The Appellant also objected to Excise Duty charged on income from card interchange fees, brokerage, commissions, and Held for Trade Treasury (HFT) bonds disposal.

6. The Appellant acknowledged underpayment of principal Excise Duty of Kshs.29,910,488.00 and proceeded to settle the same. The Respondent reviewed and considered the Appellant's objection letter of 5 April 2019 and the additional information provided. The Respondent also acknowledged the payment of Kshs.29,910,488.00 by the Appellant.

7. Subsequently the Respondent issued an Objection Decision dated 31st May 2019 confirming an Assessment of Kshs.10,000,058.00. relating to the following incomes.

    i. Excise duty amount of Kshs.2,529,548.00 relating to commission income from Mpesa on the basis that the commission was earned from the provision of transacting infrastructure in line with the Appellant's licensed financial services and hence falls within the purview of "other fees" subject to Excise Duty.
    ii. Card interchange fees amounting to Kshs.532,777.00 on the basis that the fees fall under the ambit of "other fees" as defined in the Excise Duty Act hence subject to Excise Duty.
    iii. Credit card cash advance fee of Kshs.38,028.00 on the basis that the fees fall under the scope of "other fees" as defined by the Excise Duty Act hence subject to Excise duty.
    iv. Management fees from Sidian Bank Insurance Agency Ltd (SIAL) of Kshs.18,062.00 on the basis that management fees are subject to Excise Duty.

8. The Appellant, being aggrieved and dissatisfied with the Objection filed a Notice of Appeal at the Tax Appeals Tribunal on 28 June 2019.

THE APPEAL

9. The Appellant filed its Appeal on the grounds that:
    i. The Respondent erred in law and in fact by imposing Excise Duty on M-pesa commissions since such commissions are not chargeable to Excise Duty as provided for under the Excise Duty Act 2015.
    ii. The Respondent erred in law and in fact by imposing Excise Duty on card interchange fees which are not chargeable to Excise Duty as provided for under the Excise Duty Act 2015.
    iii. The Respondent erred in law and in fact by demanding Excise Duty on interest income from credit cards which is not chargeable to Excise Duty as provided for under the Excise Duty Act 2015.

Appellant's Case

10. The Appellant submits that the issues that lie for determination by the Tribunal are.
    i. Whether M-pesa commissions earned by the Appellant fall within the purview of "other fees" which are subject to Excise Duty.
    ii. Whether card interchange fees fall within the purview of "other fees" which are subject to Excise Duty; and
    iii. Whether the Respondent's demand for Excise Duty on interest income from credit cards is in contravention of the law.

a) Whether Excise Duty is chargeable on Mpesa Commissions

11. It is the Appellant's submission that the Respond sought to charge Excise Duty on commissions earned by the Appellant from M-pesa money agency

services on the basis that the Appellant earns the income from providing transacting infrastructure. The

12. Appellant argues that based on the provisions of the Excise Duty Act, the fees/commissions earned from provision of transacting infrastructure are outside the purview of 'other fees' chargeable to Excise Duty.

13. The Appellant explained that it entered into an agreement with the telecommunication operator i.e. Safaricom for the provision of money transfer services on the platform maintained by the telecommunications operator. In exchange for the provision of the services, the Appellant earns a commission/income in respect of its customers' transactions.

14. Under the agreement, the Appellant avers, Safaricom agents desirous to acquiring a float issue instruction at any of the Appellant's branches of the amount they wish to have uploaded as float. The Agents give the amount in cash to the Appellant who then credits the agent's M-pesa account with the exact amount received. The money received by the Appellant is remitted to Safaricom.

15. The Appellant submits that the entire transaction takes place on Safaricom M-pesa platform and it is Safaricom that stipulates, charges and collect the tariffs due from the agent including Excise Duty payable. Safaricom thereafter nets off expenses payable on its end before allocating the income to the Appellant for provision of its infrastructure.

16. The Appellant argues that M-pesa commissions earned from Safaricom do not fall under the definition of *"other fees"* as per Part III of the First Schedule to the Excise Duty Act (before the amendments in the Finance Act 2019) which stated that;

> *"Other fees include any fees, charges or commissions charged by financial institutions relating to their licensed financial institutions*

but does not include interest on loan, or return on loan or an insurance premium, or premium based or related to commissions."

17. It is the Appellant's submission that the M-pesa commissions earned are exempted from the purview of Excise Duty for the following reasons.

    i. The Appellant does not charge a fee to the M-pesa agent for the infrastructure provided. Rather it is Safaricom that charges and account for Excise Duty payable on the whole amount; and
    ii. Provision of infrastructure does not qualify as a licensed function or activity under the Excise Duty Act.

The Appellant does not charge a fee to the M-pesa agent for the infrastructure provided.

18. According to the Appellant, its roles as a super-agent is exactly similar to that of an M-pesa agent only that it is dealing with M-pesa agents in the place of the common *"wananchi".* The amount of M-pesa float credited to Mpesa agent's account is the exact amount that is deposited, not a penny less or more.

19. The Appellant submits that it is Safaricom who determines the tariffs applicable, imposes charges and collects the same from the agent at a later date. It also avers that the platform on which the transaction takes place is the M-pesa platform which is owned by Safaricom and not the Appellant. The Appellant further submits that Part III of the First Schedule to the Excise Duty Act is emphatic in its definition of what constitutes *"other fees"*, and it adopts the word "charged" and not any other word.

20. The Appellant posits that the use of the word 'charge' in the Excise Duty Act prior to the amendment in the Finance Act 2019 is purposeful and not by mistake. The Appellant argues that the use of the word 'charge' is crucial in the determination of the tax incidence.

21. The Appellant submits that the tax incidence, which is the point when Excise Duty is payable, is the point when the M-pesa agent is charged by Safaricom. Thus, the Appellant argues, the obligation to account for Excise Duty payable rests with Safaricom as the party charging the tariff and collecting the same. The Appellant avers that Safaricom acknowledges this and accounts for the Excise Duty payable on the whole tariff before netting off expenses and allocating the fee to the Appellant for the infrastructure availed on a monthly basis.

22. The Appellant argues that by seeking to tax the commissions received by the Appellant, the Respondent is seeking a second bite on the cherry which is not only unfair but tantamount to double taxation. The Appellant avers that there is no revenue lost to the Respondent given that the whole amount has already been subjected to Excise Duty by Safaricom before allocating the income to the Appellant.

23. To support its position that Excise Duty should be accounted for by Safaricom, the Appellant relies on the case in ***Stanbic Bank Kenya Ltd versus Commissioner of Domestic Taxes, Tax Appeals Tribunal, Tax Appeal No. 176 of 2016*** where a similar concern arose as to who charges and as such, is liable to account for Excise Duty on local cross bank card ATM transactions. The Tribunal held that.

> *"...with regard to local cross Bank ATM transaction, it is clear that the customer facing bank charges the customer the fee for the use of the ATM as well as the Excise Duty on the fee. This customer-facing bank then submits the Excise Duty to KRA while the fees go to Visa which allocates the amount between the customer-facing bank and the Appellant. In this transaction, the fees were charged by the customer-facing Bank. It is, in the Tribunal's view, this bank that is tasked with charging Excise Duty. The sharing of the fees between*

the two banks later on does not trigger the provision of another service to which Excise duty applies. Thus, Excise Duty is not applicable".

24. The Appellant, placing reliance on the above ruling by the Tribunal submits that it is Safaricom, the party charging for the service to its M-pesa agents that should pay Excise Duty and has indeed been paying.

Provision of infrastructure does not qualify as a licensed function or activity under the Excise Duty Act.

25. It is the Appellant's assertion that the M-pesa commissions that the Respondent is seeking to subject to Excise Duty are commissions earned from non-licensed banking activities that are not part of its licensed core banking activities.

26. According to the Appellant, Part III of First Schedule to the Excise Duty Act provides for charging of Excise Duty on 'other fees' in relation to licensed financial institutions activities and defines "other fees" as.

"any fees, charges or commissions charged by financial institutions relating to their licensed financial institutions but does not include interest on loan or return on loan or an insurance premium or premium based or related commission."

27. The Appellant asserts that the Central Bank of Kenya (CBK) has licensed it to provide an extensive range of banking services under the Banking Act Cap 488. As a licensed bank, the Appellant maintains, its core activities are taking deposits from members of the public and subsequently lending or investing the money.

28. The Appellant asserts that banking services can only arise where the Appellant accepts money from members of the public and proceeds to employ the money or any part thereof for lending, investment or in any manner for the account and at risk of a person so employing the money. The Appellant submits that whereas it receives money from the M-pesa agent, which is uploaded as a float, it has no control whatsoever over what the agent does with the float. As such, the Appellant argues, the third limp requisite for a banking activity to arise in absent.

29. The Appellant further argues that the provision of the said infrastructure to Safaricom is not a preserve of the banks. The Appellant refers to the witness testimony by Doreen Gakii who confirmed that there are several super agents providing the same infrastructure provided by the Appellant who are not banks.

30. The Appellant posits that provision of infrastructure is not one of the activities it is licensed to perform under the Banking Act and demanding Excise Duty on the same would be tantamount to a breach of the Excise Duty Act and Article 210(1) of the Constitution of Kenya 2010 which provides that *"no tax or licensing fee may be imposed, waived or varied except as provided by the legislation".*

31. The Appellant avers that any demand for tax must be made on the basis of an express statutory provision. In support of its case, the Appellant refers to **Republic vs Kenya Revenue Authority Ex-Parte Cooper K-Brands Ltd (2016) eKLR** where Justice odunga was guided by the decision in ***Vestey Vs Inland Revenue Commissioners (1979) 3 ALL ER at 984*** where it was held that;

> *"taxes are imposed on subjects by Parliament. A citizen cannot be taxed unless he is designated in clear terms by taxing Act as a taxpayer and the amount of his liability is clearly defined".*

32. The Appellant further cites the case of ***Republic vs The Commissioner of Domestic Taxes ex-parte Barclays Bank of Kenya limited (Msc. Application 1223 of 2007)*** where the judge stated that: -

> *"the duty of the Respondent in assessing tax is to identify transactions or payments that attract tax liability especially where there are objections to search categorisation. The Respondent cannot exercise its duty like a trawler in the deep sea expecting to catch all the fish by casting its net wide. The Respondent's decision in this respect falls below this standard and the transactions and payments caught by the decision cannot be said to fall within the statutory definition of the tax".*

33. The Appellant also cites the decision in ***Keroche Industries Ltd vs Kenya Revenue Authority & 5 others*** where it was held that.

> *"...it does not matter that the respondents say and think they are owed over a billion Kenya shillings - what matters is whether* ***the amount is lawfully due and whether the law allows its recovery? It is not a question of impression or perception of what is owed, instead it is what if anything, is owed under the relevant law and whether its assessment and recovery is permitted by the applicable law.*** *If rightly due, the huge amount notwithstanding the court must uphold the right of recovery regardless of its consequence to the applicant and if not due under the law it must not hesitate to disallow it and must disallow it to among other things to uphold both the law the integrity of the rule of law.".*

34. Accordingly, the Appellant submits that based on the provisions of the Excise Duty Act and the cited legal precedence; the commission earned from M-pesa services should not be subject to Excise Duty since provision of infrastructure is not one of the licensed activities under the Banking

Act. The Appellant submits that these commissions are therefore beyond the scope of "other fees" chargeable to Excise Duty under the Excise Duty Act 2015.

b) Whether Excise Duty is chargeable on Interchange fees

35. The Appellant disputes the Respondent's assessment of Excise Duty on visa commissions and interchange fees earned from card transactions and argues that the same are outside the ambit of Excise Duty.

36. By way of background, the Appellant explained that interchange fees on card transactions arise as follows.

    i. Card services companies such as VISA or MasterCard provide a settlement platform network connectivity and a payment infrastructure to their members, which are banks or financial institutions comprising of issuing and acquiring Banks.
    ii. An issuing bank, which is a financial institution that buys card services, company's membership and licensed rights to issue customers with branded cards by international card service companies for the purpose of making payments, then issues a card to each customer (the cardholder).
    iii. A cardholder makes a purchase at a merchant outlet for example a supermarket and completes the card payment process by inputting their PIN at the point of sale (POS) selling machine. This serves as authorisation and authentication of the card transaction.
    iv. The Merchant submits a request to authorise the transaction to the acquirer who in turn forwards it to the card services company for onward transmission to the respective card issuer. The issuer receives electronic authorisation request instantly and undertakes validation checks on the transaction to confirm if a card is valid and has sufficient funds to cater for the transaction. Once it is confirmed, the

issuer sends a transaction authorisation code to the card services company which in turn transmits the same to the acquirer who is then tasked with forwarding the authorisation code to the Merchant Point of Sale. The authentication and authorisation are enabled by the network platform provided by the global service company. Once the transaction authorisation process is complete the merchants are able to provide the card holder the required services

v. At the end of the day, the Merchant electronically uploads the card transaction details from POS to the acquiring bank system via the settlement procedure protocols.

vi. The card services company generates transaction settlement reports and provides these to both the card acquiring and issuing members to facilitate the net settlement position.

vii. The cardholder is liable to make payment to the issuing bank for the full value of his or her transaction. The value deducted from the cardholder account is equivalent to the value of goods or services received from the Merchant with no charges levied by the issuing bank for this payment service.

viii. Upon receipt of the transaction agreement reports from the card services company, the card issuer remits the net funds to the acquiring bank via card services company appointed settlement agent.

ix. The acquiring bank received a settlement of the full value of merchant transactions done by the card holder from the issuer bank less any processing charges owed to the card services company.

x. The acquiring bank then deducts the contractual merchant service commission from the payment which ranges between 3 to 5% of the value of transactions and credits the merchant's account with the balance.

xi. The card services company requires the acquirer to cede part of the merchant service commission to the card issuer as an incentive to continue issuing cards. The card issuer typically receives 0.5 to 2% incentive fee called interchange reimbursement fee or card interchange fee.

37. Based on the above transaction flow, the Appellant avers that the income from card interchange fees is not subject to Excise Duty for the following reasons.

    i. That card fees earned from international transactions with non-resident banks relate to exported services thus exempt from Excise Duty.
    ii. That the Appellant does not charge card fees hence the same is not subject to Excise Duty; and
    iii. Imposing Excise Duty on card fees earned from transactions with local banks amounts to double taxation.

38. That card fees earned from international transactions with non-resident bank relate to exported services thus exempt from Excise Duty.

39. The Appellant submitted a chart to depict the transaction flow giving rise to interchange fees in an international transaction. Based on the transaction flow chart, the Appellant asserts that a portion of interchange fees arises from international transactions where the Appellant's customers use their card at an international automated teller machine or point of sale or undertake online purchase with an international merchant.

40. The Appellant submits that the international interchange fees earned when an Appellant's customer transacts at a non-resident merchant

amounts to income earned from export of services thus exempt from Excise Duty.

41. Citing section 2 of the Excise Duty Act 2015 which defines "a service exported from Kenya" and Section 7 of the Excise Duty Act 2015 which expressly exempts services exported out of Kenya from Excise Duty, the Appellant submits that the Respondent erred in law and fact by imposing Excise Duty on card fees income arising from international transactions as these relate to exported services.

42. The Appellant avers that imposition of Excise Duty on export services which is expressly exempted from the purview of Excise Duty contravenes the law and violates a well-established rule in tax that no taxes may be imposed unless expressly provided for under the law. In support of this, the Appellant relies on the cases of **Republic vs Kenya Revenue Authority Ex-Parte Cooper K-Brands Ltd (2016) eKLR, Vestey Vs Inland Revenue Commissioners (1979) 3 ALL ER at 984 and Keroche Industries Ltd vs Kenya Revenue Authority & 5 others (2007)**.

That the Appellant does not charge card fees hence the same is not subject to Excise Duty

43. The Appellant reiterates that as earlier described, interchange fees is a portion of the merchant service commission deducted by the acquirer bank and this is subsequently shared/allocated to the Appellant. The Appellant avers that in line with practice the world over in the banking industry, the Appellant does not charge the interchange fees, i.e., does not issue invoices or debit notes to demand for the interchange fees arising from the card transactions.

44. The Appellant argues that the First Schedule to the Excise Duty Act only provides for charging of Excise Duty on other fees charged by financial

institutions. The Appellant further argues that as per the provisions of the Excise Duty Act, Excise Duty should only apply to fees that are charged as opposed to an allotment of the interchange fee. The Appellant avers that the acquirer bank is the customer-facing bank and therefore the obligation to account for Excise Duty on the whole amount before it is allocated to the various parties rests with the acquirer bank.

45. In support of this position the Appellant relies on the Tribunal's ruling in the case of **Stanbic Bank Kenya Ltd versus Commissioner of Domestic Taxes, Tax Appeals Tribunal, Tax Appeal No. 176 of 2016.**

46. It is the Appellant's submission that it is well established in law that tax statutes are to be strictly interpreted as in the case of **Cape Brandy Syndicate v Inland Revenue Commissioners (1920) 1 KB 64** which relied on the ruling by the Court of Appeal in **Mount Kenya Bottlers Limited & 3 others v Attorney General & 3 others (2019)** where it was held that:

> *"...one has to look at what is clearly said. There is no room for intendment, there is no equity about a tax. There is no presumption as to tax. Nothing is to be read in. Nothing is to be implied. One can only look fairly at the language used".*

47. The Appellant also refers to the **Halsbury's Laws of England 4th edition volume 23 page 36** quoted in **Commissioner of Income-Tax v (E.A) Ltd (2018) eKLR** where the Court held that;

> *"in the construction of a taxing Act the court has primary regard to the statutory word themselves and their proper construction.... Taxing Acts are strictly construed in the sense that one looks at what is said; there is no room for intendment".*

48. To further buttress its point, the Appellant cites the case of **Stanbic Bank Kenya Ltd vs Kenya Revenue Authority: Civil Appeal No.77 of 2008**, where the Court of Appeal was of the view that:

> *"Tax law entails strict application and... there is no question of the exercise of discretion by the Court when dealing with matters pertaining thereto..."*

49. It is the Appellant's assertion that the Respondent erred in law and fact by imposing Excise Duty on interchange fees thus failing to take cognizance of the fact that Excise Duty should only apply on fees charged by the Appellant which is not the case for card interchange fees.

Imposing Excise Duty on card fees earned from transactions with local banks amounts to double taxation.

50. The Appellant avers that the interchange fees earned in respect to local transactions have already been subjected to Excise Duty on the respective customers who are charged the transaction fees. The Appellant thus argues that the action by the Respondent to impose Excise Duty twice on the same transaction amounts to double taxation.

51. The Appellant refers to the Black's Law Dictionary 6th edition which defines the term double taxation as;

> *" the taxing of the same item or piece of property twice to the same person or taxing it as the property of another person and again at the property of another, but this does not include the imposition of different taxes concurrently on the same property or income (e.g. federal and state income taxes) nor the taxation of the same property two different persons with different interest in it or when it represents different values in their hands."*

52. According to the Appellant, taxation should produce the right amount of tax at the right time, avoiding double taxation. The Appellant argues that double taxation is contrary and offends the principle of a good tax system enshrined under Article 201 (b)(i) of the Constitution of Kenya which provides that "*a public finance system in Kenya shall promote an equitable society and in particular the burden of taxation shall be shared fairly in relation to taxation*".

53. In support of its position, the Appellant cites the High Court Ruling in the case of **Raiply Woods (K) Ltd & another versus Baringo County & three others** where the judge in respect to double taxation held that:

> *"As the court has found that the taxation by way of cess is a charge on forest produce rather than a service charge, having paid for royalties to the National Government for the harvesting of forest produce, the levying of cess on the same forest produce must be deemed as double taxation.... in the strict sense of the word as defined by the Black's Law Dictionary 8th ed. (2004) as "the imposition of two taxes on the same property during the same period and for the same taxing purpose... search taxation of offends the principle of fair taxation under Article 201 (b)(i) of the Constitution."*

c) Whether Excise Duty is chargeable on Credit Cards

54. The Appellant explained that it earns interest income from credit cards whenever the card holders utilise their credit card and fail to pay the utilised amount before the deadline of the prescribed payment period of 50 days. According to the Appellant, this transaction is similar to a soft loan from which the Appellant earns interest income on the amount loaned to its customers.

55. The Appellant argues that interest on loan is excluded from the definition of "other fees" as defined in the Excise Duty Act which states that;

"other fees include any fees, charges or commissions charged by financial institutions related to their licensed financial institutions but does not include interest on loan, return on loan or an insurance premium or premium based or related commission."

56. The Appellant argues that since the Excise Duty Act falls short of defining what constitutes interest, it relies on the definition in the Income Tax Act which define interest to mean:

"interest (other than interest charged on tax) means interest payable in any manner in respect of a loan, deposit, debt, claim, or other right or obligation and includes a premium or discount by way of interest and a commitment or fee paid in respect of any loan or credit or an Islamic finance return."

57. The Appellant asserts that interest earned from credit cards falls squarely under the definition of interest as provided in the Income Tax Act. To support its reliance on the definition of interest as provided for in the Income Tax Act, the Appellant refers to the *Pari Materia* principle which allows the use of definition of interest in the Income Tax Act to resolve concerns under the Excise Duty Act as was in the case of **Stanbic Bank Kenya Ltd vs Commissioner of Domestic Taxes, Tax Appeals Tribunal, Tax Appeals no. 176 of 2016** where the Tribunal held that;

"The Tribunal notes that indeed there is no definition of interest in the Customs and Excise Act. As such it is forced to apply the principle of in pari materia. The principle states that where statutes are of the same matter or on the same subject, that is are so related as to form a system or code of legislation, such statutes are to be taken together as forming one system and as interpreting and enforcing each other. In J.K. Steel Ltd. Vs. Union of India ([1969] 2 SCR 481 it was held that cognate and pari materia

legislation should be read together as forming one system and as interpreting and enforcing each other

... The Tribunal is of the view that the Income Tax Act is so closely related to the Excise Duty Act that it can be considered to be pari materia thus the definition of interest provided in the Income Tax Act can be used to define interest under the Customs and Excise Act where the latter does not provide its own definition".

58. The Appellant also refers to a similar ruling made by the Tribunal in the case of **Co-operative Bank of Kenya Ltd vs Commissioner of Domestic Taxes, Tax Appeals Tribunal, Tax Appeals Number 45 of 2017** where it was held that;

"in the absence of a definition of interest in the Excise Duty Act, this Tribunal finds that the operational definition is found in the Income Tax Act".

59. The Appellant submits that the Respondent erred in law and fact by demanding Excise Duty on interest income on credit cards as this is expressly exempted from Excise Duty under the Excise Duty Act.

The Appellant's prayer

60. The Appellant prays that:

i. The decision of the Respondent be annulled or varied in such a manner that may appear just and reasonable to the Honourable Tribunal; and

ii. This Appeal be allowed with costs awarded to the Appellant.

THE RESPONDENT'S CASE

a) Response on whether Excise duty should be charged on Mpesa Commissions.

61. The Respondent rejects the Appellant's claim that Mpesa commissions are exempt from Excise Duty on the basis that they do not form part of the Appellant's licensed financial services. Instead, it argues that all the activities carried out by the Appellant are licensed and authorised and therefore the M-pesa services offered constitutes the Appellant's core activities since there is a valid agreement between the Appellant and Safaricom on the same.

62. The Respondent avers that M-pesa transactions are financial services and as such, issues of licensing raised by the Appellant in its statement of fact do not hold. Further, the Appellant in its website, has included M-pesa transactions as part of the services which it offers.

63. It is the Respondent's assertion that the Appellant even offers its clients a platform where they are able to link their accounts to M-pesa and purchase airtime and pay for utility bills as indicated in its website.

64. According to the Respondent, financial services are economic services provided by the finance industry which encompasses a broad range of businesses that manage money including credit union, banks, credit card companies, insurance companies, accountancy companies, consumer finance companies, stock brokerages, investment firms, individual managers and some government sponsored enterprises.

65. The Respondent cites the Banking Act which defines financial business as

(a) the accepting from members of the public of money on deposit repayable on demand or at the expiry of a fixed period or after notice; and

(b) the employing of money held on deposit or any part of the money, by lending, investment or in any other manner for the account and at the risk of the person so employing the money;

66. The Respondent avers that Mpesa commissions earned by the Appellant relate to services that fall within the definition of commission and agency services relating to money transfer services under the Excise Duty Act and are subject to Excise Duty at the prescribed rate.

67. To obtain a definition for other fees and commission, the Respondent refers to the Central Bank of Kenya Prudential Guidelines of January 2013 which provide a guideline on how banks in Kenya, the Appellant included, are to prepare their return and provides for definition of terms used including but not limited to; what constitute other fees and commission income. Clause 4.2 of the CBK Prudential guidelines defines other fees and commissions income as:

> *"This includes all charges and commissions relating to account operations (e.g., ledger fees), fees received from managing other institutions/group companies, commissions earned (e.g. charges on standing orders, safe-deposit facilities and ATMs) etc."*

68. The Respondent asserts that the Appellant's audited financial statements for the year ended 31st December 2018 indicates that the Appellant received non-interest income on fees and commissions. The Appellant's trial balance for the year 2018 shows that the Appellant received fees and commission income being Lipa na M-pesa commissions and M-pesa connect commissions.

69. In disputing the Appellant's claim that derived commissions are not subject to Excise Duty, the Respondent asserts that the amendments made by the Finance Act 2013 and the Excise Duty Act 2015 expressly

subject derived commission to Excise Duty. Such express laws, the Respondent avers, are not made in vain and must be followed. The Respondent cited Section 5 of the Excise Duty Act which states that:

"Subject to this Act, a tax, to be known as excise duty, shall be charged in accordance with the provisions of this Act on—

(a) excisable goods manufactured in Kenya by a licensed manufacturer;

(b) excisable services supplied in Kenya by a licensed person;

(c) excisable goods imported into Kenya.

Excise duty shall be charged at the rate specified in the First Schedule for the excisable goods or services in force at the time the liability arises for excise duty as determined under section 6."

70. The Respondent relies on the case of **Republic vs Kenya Revenue Authority Ex-Parte Bata Shoe Company Kenya Ltd (2014) eKLR** where the court held that;

"This brings me to the role and interpretation of tax laws payment of tax is an obligation imposed by law it is not a voluntary activity. That being the case a taxpayer is not obliged to pay a single coin more than is due to the taxman. The taxman on the other hand is entitled to collect up to the last coin that is due from a taxpayer."

71. The Respondent posits that the tax treatment of derived income was confirmed during a meeting held at the Times Tower on 19th August 2013 between Kenya Bankers Association (KBA) and the Kenya Revenue Authority. According to the Respondent, the KBA was advised in that meeting that derived commissions which include commissions received for top-up of airtime, inbound transfers, bills discounted, M-pesa connect commissions which include use of ATM third-party settlement are subject

to Excise Duty in accordance with the provision of the Finance Act 2012, Finance Act 2013 and the Excise Duty Act 2015.

72. Accordingly, the Respondent insists that there is no ambiguity in law as to what is subject to Excise Duty and the words should not be sustained so as to find ambiguity in law. To support this, the Respondent relies on the case of **Stanbic Bank Limited verses KRA (2009) eKLR** where the Court held that the meaning of words should not be strained so as to find ambiguity.

73. The Respondent avers that it is not in dispute that the Appellant earns commissions despite not raising invoices. The Respondent in supporting the fact that the Appellant earns commissions by virtue of participating in the financial system relies on the Tribunal's judgement in **TAT Appeal No. 203 of 2015, Insurance Brokers Ltd versus Commissioner of Domestic Taxes** where it was held that:

> *"The provisions of the Customs and Excise Duty Act and the amendments contained in the Finance Act of January 2013, financial service providers, communication providers are all intermediaries connection persons who need to do business with each other and further establishes that commissions earned by these intermediaries are the target of the Finance Act 2013."*

74. In responding to the assertion by the Appellant that it is Safaricom, the customer facing entity that should account for Excise Duty since it imposes the service fees, the Respondent cites the ruling in **Association of Gaming Operators - Kenya & 41 others versus Attorney General & 4 other (2014) eKLR** where the court stated the following insofar as impracticability of implementation of tax statute is concerned:

> *"Interpretation of the Act and impracticability of implementation.*

*The petitioners have attacked the Finance Act 2013 on the basis that it presents implementation problems. I must at once state that problems of implementation of the law are outside the Court's jurisdiction to resolve unless there is an allegation that there is a violation of the petitioner's fundamental rights and freedoms or of the Constitution. There is no allegation in the petition that the implementation of the Finance Act 2013, violates the constitution. I also reiterate what I stated in Kenya Union of Domestic, Hotels, Education, Institutions, and Hospital Allied Workers (KUDHEIHA) Union vs Kenya Revenue Authority and others Nairobi Petition No. 544 of 2013 (2014) eKLR, Before I deal with the constitutionality of the impugned provisions, I think it is important to establish the legislative authority of the legislature to impose taxes. Article 209 of the Constitution empowers the National Government to impose taxes and charges. Such taxes include income tax, value added tax, customs duties and other duties on import and export goods and excise tax. The manner in which the tax is defined, administered and collected is a matter for Parliament to define and it is not for the court to interfere mainly because the legislature would have adopted a better or different definition of the tax or provided an alternative method of administration or collection. Under Article 209 of the constitution the legislature retains wide authority to define the scope of the tax see (***Bidco Oil Refineries Vs Attorney General & others Nairobi Petition No. 177 of 2012 para 53 56)*** ".*

75. In response to the Appellant's claim that imposing Excise Duty on M-pesa commission would amount to double taxation since Safaricom had already paid Excise Duty on the same, the Respondent asserts that its role is confined to implementation of tax and the fact that an item is subject to the same tax when passed through different hands does not exempt it from taxation unless the law provides that the tax is final.

76. In light of the above ruling, the Respondent avers that it acted within the law in imposing Excise Duty on the M-pesa commissions earned by the Appellant.

b) Response on whether Excise duty should be charged on interchange fees.

77. The Respondent asserts that card interchange fees is subject to Excise Duty in line with the express provisions in the Excise Duty Act. To support of its position, the Respondent provides the following background information with respect to the transactions that give rise to the card interchange fees:

A typical card transaction flow entail.

i. A card holder makes a purchase at a merchant's outlet and completes the transaction by swiping their card at the swipe machine provided by to the merchant by the acquirer.

ii. The network platform then facilities authentication of the card employed at the merchant and clears the use of the card for concluding transactions.

iii. The Card Association network generates reports for merchant settlement and forwards these to the acquirer. The acquirer within a couple of days settles the account with the merchant after deducting a small percentage ranging from 3 to 5% as the MSC.

iv. MSC is a charge made by a merchant to an acquirer for processing transaction originated by the card purchases.

v. Out of the MSC retained by the acquirer, a percentage is shared with the issuer as "interchange fee" and with the card association as dues and assessment fees while the balance is retained by the acquirer.

vi. The Interchange sets the floor for the MSc which is always the Interchange fee plus an additional percentage taken by the acquirer and the Card Association.

vii. The acquirer and issuer have no direct contact among themselves but are guided and bound by the Association Rules for which they have subscribed to as members.

78. According to the Respondent, the Appellant's role is an Issuing Bank. The Respondent sought to charge Excise Duty on interchange fees charged by the Appellant to the Acquiring Banks. In determining whether or not the interchange fee is subject to Excise Duty, the Respondent averred that as an Issuing Bank, the Appellant earns interchange fees for assisting the merchants and Acquiring Banks process card transactions. In this case the Appellant offers banks a composite card payment processing service in the form of authorization, settlement and clearance to the Acquiring Bank. The Issuing Bank service begins when an authorization request is sent to the Appellant and is completed when the Appellant settles the account with the Acquiring Bank. The subsets of the Issuing Bank services comprise of the following activities:

a. Receiving the transaction information from the Acquiring Bank (or its processor) through card systems networks.
b. Checking to ensure, among others that the transaction information is valid.
c. Checking to ensure that the cardholder has sufficient balance to make the purchase.
d. Checking to ensure that the account is in good standing.
e. Responding by approving or declining the transaction.
f. Setting aside the amount authorized.
g. Sending authorization code through network on merchant terminal.
h. Agreeing to future remittance with Acquiring Bank and merchant customer.
i. Reimbursing the Acquiring Bank by sending funds to the Acquiring Banks.

79. The Respondent avers that the contractual obligation between the Issuers and Acquirers is governed by the various card scheme rules. The consideration for the above services is the interchange fee paid by the Acquiring Bank to the Appellant (the Issuing Bank). According to the Respondent, at the point at which the Appellant as the Issuing Bank is forwarding the funds subject to the transaction to the Acquiring Bank, it deducts the interchange fee due on the transaction.

80. The Respondent insists that the interchange fee is subject to Excise Duty. It avers that the Appellant in their own documents recognize this amount as income under other fees hence warranting charging of Excise Duty.

81. In reference to the Appellant's assertion that it does not charge interchange fees but rather gets allocated the commission, the Respondent argued that it is this fee that it sought to charge Excise Duty.

82. The Respondent cites the Tribunal's judgement in the **Appeal No. 29 of 2017 African Bank Corporation Ltd versus Commissioner of Domestic Taxes** where the court held that.

> *"....as compensation for risks and costs incurred to facilitate card transactions through its network, MasterCard will pay participation fees to the players in their network including merchant, acquiring bank and the issuing banks. The Tribunal found that only the fees received by the Appellant in form of participation fees were subject to Excise Duty."*

83. Further, the Respondent cites the ruling in **Nairobi HCCA No. 195 of 2017 Commissioner of Domestic Taxes Large Taxpayers Office vs Barclays Bank Ltd** where the Court of Appeal held that the Issuer provides services to the Acquirer for which they earn interchange fees which are therefore subject to tax.

84. The Respondent asserts that its mandate is confined to implementation of tax statutes. The fact that an item is subject to the same tax when passed through different hands does not exempt the service from taxation unless the law provides that the tax on an item is final.

85. The Respondent argues that challenges in implementing a tax law is not sufficient ground to deter recovery of taxes to support its case, the Respondent sought reliance on **High Court petition number 383 of 2013 between Mark Obuya & other verses Commissioner of Domestic Taxes under par 32 and 33** where the Judge ruled that;

> *"the fact that a particular provision of statute merely may be difficult to implement or inconvenient does not give the Court licence to declared it unconstitutional".*

86. The Respondent also cites the case of **Republic vs Commissioner of Domestic Taxes Large Taxpayers Office Ex-Parte Barclays Bank of Kenya Ltd (2012) eKLR** where the Judge held that;

> *"The approach to this case is that stated in the oft-cited case of **Cape Brandy Syndicate v Inland Revenue Commissioners (1920) 1 KB 64** as applied in the **T.M Bell v Commissioner of Income-Tax (1960) EALR 224** where Ronald. J stated, "in a taxing Act, one has to look at what is clearly said. There is no room for intendment as to a tax. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used.... if a person sought to be taxed comes within the letter of the law he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown seeking to recover the tax cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be."*

87. To buttress the need to ensure that taxes due are collected, the Respondent cites Article 210(1) of the constitution of Kenya, 2010 which states that *"no tax or licensing fee may be imposed, waived or varied except as provided by legislation".*

88. The Respondent submits that it acted within the proper law imposing Excise Duty on the card interchange fees.

(c) Response on Excise duty on interest income on Credit cards

89. The Respondent explained that credit cards let the cardholder borrow money up to a set limit, which must be repaid. Where the cardholder fails to pay the full statement of balance by its due date, the cardholder is charged interest as a penalty for late payment. It adds that other than interest, the cardholders incur other fees including:

    a. Late fees
    b. Annual fees
    c. Cash advance fees
    d. Balance transfer fees
    e. Foreign transaction fees etc

90. The Respondent contends the Appellant's treatment of interest income on credit card as non-excisable and argues that this income forms part of 'other fees" hence subject to Excise duty. The Respondent avers that other fees are defined to include *"any fees, charges or commissions charged by a financial institution but does not include interest on loan or return on loan.*

91. According to the Respondent, when a card holder uses a credit card at a store the merchant of the store has to pay a swipe charge that goes to the issuing bank. When a credit card holder utilizes the card and fails to pay within the limit period of 50 days, the Respondent states, they are charged both interest and penalty for late payment.

92. It is the Respondent's submission that it sought to charge Excise Duty on the late fees on credit cards which the Appellant charges for the late payment of credit cards. It argues that these fees form part of "other fees" as defined as by Part III of the Excise Duty Act 2015. The Act defines other fees as.

> *"other fees include any fees, charges or commission charged by financial institutions but do not include interest on a loan or return on loan or an insurance premium or premium based or related commission".*

93. The Respondent argues that the Excise Duty Act 2015 only exempts interest on loan or return on loan or an insurance premium or premium based commission from Excise Duty.

94. According to the Respondent, the phrase interest on loan or return on loan as used in the definition of other fees means the same thing and the return on loan is meant to capture or take care of the interest charged for the Islamic loan products.

95. The Respondent avers that for implementation of Excise Duty, the legislature has defined financial institutions and other fees, terminologies considered to be of paramount importance in the implementation of Excise Duty.

96. The Respondent rejects Appellant's reliance on the definition of interest as provided in the Income Tax Act and argues that the Income Tax Act is a different Act and cannot be used to define terms used in Customs and Excise Act or Excise Duty Act unless expressly provided for under the statute.

97. The Respondent avers that the Income Tax Act provides for taxation of income while the Excise Duty Act is chargeable on excisable goods and services. The Respondent however relies on the Central Bank of Kenya Prudential Guidelines 2013 for definition of interest. The Respondent avers that the Guidelines on page 14 define interest income on loans and advances as.

> *"...this covers interest income and discounts on loans and advances including bills and notes discounted/ purchased and interest on commercial paper and corporate bonds. Interest income should not include interest on non-performing loans, and this should exclude fees, commission and penalties on loan and advances."*

98. The Respondent argues that the definition of what constitutes interest income on loans and advances as provided by CBK Prudential Guidelines does not in any way apply to the fees which the Appellant receives whenever a credit cardholder makes a late payment since these the guidelines have excluded fees, commissions and penalties on loans and advances from the definition of what constitute interest income.

99. The Respondent posits that the Appellant distinctly and separately reported this line of income from interest income implying the two incomes are separate.

100. The Respondent avers that loan administration fees that is loan commitment and processing fees were correctly subjected to Excise Duty as these are other fees and not interest. The Respondent avers that the ordinary English meaning of loan administration fees is *"Administration fee is a banking term used to describe a fee charged by a lender to a borrower to compensate the lender for covering the administrative costs of processing the loan request".*

101. The Respondent relies on the treatment of administration fees in the Appellant's own account, international accounting standards and the Central Bank of Kenya guidelines. The Respondents avers that it subjected loan administration fees which are composed of commitment and processing fees charged by the bank to borrower in addition to the interest paid on amount borrowed as loans to Excise Duty as provided for under section 5(1)(b) of the Excise Duty Act.

102. The Respondent posits that KBA, the umbrella body for Banks which the Appellant is a member released Standard Banking Practices dubbed as Consumer Guide to Banking in Kenya wherein it provides that:-

"A customer applying for a loan should be familiar with the various fees and costs associated with the facility. Some of these costs are upfront, others are recurring (like the loan repayment) while others may come at the end of the loan repayment, depending on the contract. ...

General Costs

- *Application fees*
- *Negotiation fee or commission/Processing fee/*
- *Arrangement fee*
- *Interest rate charge*
- *Delayed penalty or penal interest*
- *Commitment fee [on overdrafts]*
- *Option fee [applicable for certain bank products]."*

103. The Respondent further avers that the KBA provides that these costs are in addition to the interest rate component and range from bank fees and charges to third-party costs such as legal fees insurance and government levies.

104. It is the Respondent's submission that loan administration fees and other facilitation fees are not subject to interest capping rules as provided for

under the Central Bank of Kenya Prudential guidelines since they are not interest. Thus, the Respondent maintains that the financial charge which accrues where the credit cardholder does not pay off the full balance before the lapse of the grace period amounts to charges as captured in the definition of other fees as provided in part III of the First Schedule to the Excise Duty Act.

105. The Respondent submits that technical banking terminology such as administrative fee should be understood as ordinarily used and comprehended in the banking industry. In support of this, the Respondent cites the ruling by Lord ***Simmons in the case of London and Eastern Co. Vs Berriman (1946) 1 ALL ER 255*** where he stated that;

> *"it is only by reference to the industry that a meaning can be ascertained it remains a question of evidence what the words mean in the industry. They are a term of art and it is by those skilled in the art that I must been instructed."*

106. The Respondent claims that Part III of the First Schedule to the Excise Duty Act 2015 defines financial institutions and other fees for the purpose of providing clarity to the persons mandated to collect Excise Duty, and the revenue streams subject to Excise Duty. Under this statute, the Respondent avers, other fees are defined to include any fees charges or commissions charged by financial institution but does not include interest.

107. The Respondent asserts that the legislature is the law-making organ, and it enacts the law to serve a particular object and need. In this case, the Respondent avers, that the object of Part III of the First Schedule to the Excise Duty Act 2015 was to bring into taxation, fees, charges and commissions but exempt interest which is a stand-alone in the financial statements.

108. The Respondent submits that it acted within the law to subject to tax, Excise Duty on interest charged on credit cards.

The Respondent's Prayer

109. The Respondent prays that.

i. That the Tribunal upholds the Respondent's decision to charge Excise Duty tax amount of Kshs. 10,000,058.00 inclusive of penalties and interest.

ii. That the Appeal be dismissed with costs to the Respondent as the same is without merit.

ISSUES FOR DETERMINATION

110. The Tribunal examined the submissions of both parties and determined that the issues for determination could be summarised as follows:

a. Whether the amount demanded in the Respondent's letter of Objection Decision was erroneous

b. Whether commissions earned by the Appellant from M-pesa Transactions are subject to Excise Duty.

c. Whether card interchange fees are subject to Excise Duty; and

d. Whether interest income from credit cards is subject to Excise Duty.

ANALYSIS AND DETERMINATION

a. Whether the Amount demanded in the Respondents Objection Decision was erroneous

111. According to the Respondent, the Assessment amount which it seeks to recover from the Appellant is Kshs.10,000,058.00 as stated in its Objection Decision of 31st May 2019. According to the Appellant, the outstanding assessment amount which is subject to the Tribunal's determination is Kshs.3,087,367.00. This is the amount arrived at after

taking into account the amounts vacated by the Respondent in its Objection Decision of 31st May 2019.

112. The Tribunal perused the evidence placed before it and attempted to reconcile the amounts as demanded by the Respondent against the amounts that the Appellant avers are due. The difference seems to stem from the penalties and interest charged by the Respondent. In its objection, the Appellant objected to the penalties levied. It goes on to state that it intends to apply for a waiver of penalties and interest.

113. No evidence of the grant of such waiver has been placed before us. Thus, we can only assume that such waiver was not granted. The Appellant also did not present its arguments regarding why the penalties were not applicable.

114. Consequently, the Tribunal adopted the figure of Kshs. 10,000,058.00 being the balance outstanding after the Appellant had paid the taxes that were not in dispute.

b. Whether commissions earned by the Appellant from M-pesa Transactions are subject to Excise Duty.

115. The Respondent assessed Excise Duty amount of Kshs.2,529,548.00 relating to commission income of the Appellant from Mpesa on the grounds that the commission was earned from the provision of transacting infrastructure in line with the Appellant's licensed financial services and hence falls within the purview of "other fees" subject to Excise Duty.

116. The issue of Excise Duty on commissions earned by banks from Mpesa transactions was dealt with by this Tribunal in **African Banking Corporation V Commissioner of Domestic Taxes Tax Appeal No 29 of**

2019. In that case the Tribunal found that commissions earned by banks from M-pesa transactions are other fees and are subject to Excise Duty.

c. Whether card interchange fees earned by the Appellant were subject to Excise Duty

117. The Appellant disputes the Respondent's assessment of Excise Duty on VISA commissions and interchange fees earned from card transactions and argues that the same are outside the ambit of Excise Duty. The Respondent asserts that card interchange fees is subject to Excise Duty in line with the express provisions in the Excise Duty Act.

118. The Tribunal following its ruling in **Appeal No. 246 of 2019 Barclays Bank of Kenya Ltd vs Commissioner of Domestic Taxes** determined that VISA commissions and interchange fees earned from international card transactions are exported services and therefore exempt from Excise Duty in so far as the consumers of the services are located outside Kenya. Interchange fees earned in respect to local transactions are however subject to Excise duty.

d. Whether interest income from credit cards is subject to Excise Duty

119. The Appellant disputes the assessment of Excise Duty on interest income from credit cards. This interest is earned whenever cardholders utilise their credit cards and fail to pay the utilised amount before the deadline of the period prescribed for payment (50 days). It argues that this transaction is similar to a soft loan which the Appellant earns interest on the amount loaned to its customers. The Respondent contests the Appellant's treatment of interest income on credit card as non-excisable and argues that this income forms part of 'other fees" hence subject to Excise duty. The Respondent avers that other fees are defined to include *"any fees, charges or commissions charged by a financial institution but does not include interest on loan or return on loan.*

120. The question then before the Tribunal was whether interest income from credit card is interest/return on a loan or a fee in the context of "other fees" as envisaged in the Excise Duty Act.

121. Black's Law Dictionary defines a "loan" as "anything furnished for temporary use to a person at his request, on condition that it shall be returned, or its equivalent in kind, with or without compensation for its use." It also defines a loan as "the creation of debt by the lender's payment of or agreement to pay money to the debtor or to a third party for the account of the debtor.

122. Casting these definitions in the present case, the Tribunal was of the view that interest income from credit cards was more in the nature of an interest on loan or return on loan than a fee, charge, or commissions charged by financial institution.

123. Noting that interest on loan is exempt from Excise Duty, the Tribunal determined that the Respondent erred in charging Excise Duty on interest from credit cards.

FINAL DECISION

124. Emergent from the foregoing, the Appeal partially succeeds, and the Tribunal makes the following Orders:-

    a. The assessed Excise Duty on card interchange fees and income from credit cards is hereby set aside.
    b. The amount confirmed in the Objection decision to be adjusted accordingly and paid by the Appellant.
    c. Each party to bear its own costs.

125. It is so ordered.

DATED and **DELIVERED** at **NAIROBI** on this **30th** day of **April, 2021.**

.....

ERIC N. WAFULA
CHAIRMAN

.....

CATHERINE N. MUTAVA
MEMBER

.....

GABRIEL M. KITENGA
MEMBER

.....

ABRAHAM K. KIPROTICH
MEMBER