REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

INCOME TAX APPEAL NO 4 OF 2013

MURAMATI DISTRICT TEA GROWERS

SACCO SOCIETY LTD (UNAITAS SACCO)……APPELLANT

VERSUS

KENYA REVENUE AUTHORITY………………….RESPONDENT

JUDGMENT

(Being a judgment against the decision of the Local Committee for Nairobi Tax District made on 28thMarch 2013 in an Appeal to the said Local Area Committee, dismissing the Appeal)

THE APPELLANT'S CASE

1. According to the Appellant, on or about 24th September 2008 and 27th September 2007 (sic), the Respondent served it with additional assessments of its income for 2004 and 2005 under Section 19(4)(d) of the Income Tax Act Cap 470 (Laws of Kenya) to which it objected. It was its contention that the dividend payments to members and interest income from members' loans were **"mutual income"** not taxable under Section 19 A (4) of the Income Tax Act as had been averred by the Respondent.
2. Upon dismissal of its objection by the Respondent, it filed an appeal at the Local Area Committee for Nairobi Tax District. However, the said Local Area Committee dismissed its appeal which resulted in the filing of the appeal herein. The same was brought pursuant to the provisions of Rules 4 and 6 of the Income Tax (Appeal to the High Court) Rules, Order 42 Rule 1 of the Civil Procedure Rules and all enabling provisions of the law.
3. There were numerous grounds of Appeal in the Memorandum of Appeal dated and filed on 6th May 2013 but the same could be summarised as follows:-

a. **THAT the said decision was made in contravention of the principles of natural justice as the Appellant's submissions were not considered at all, it was based on irrelevant considerations and was contrary to the weight of the Appellant's evidence in the Statement of Facts.**
b. **THAT the said decision was actuated by bias and bad faith.**
c. **THAT in confirming the additional assessment, the Local Area Committee failed to appreciate that the Appellant's main activity was to mobilise savings and provide loans to its members and not conduct business with its members.**
d. **THAT the Local Area Committee failed to appreciate that the Appellant had members who transacted with the Appellant and participate in any surplus realised in form of dividend payments and that the dividend payments to members and interest income from member's loans were "mutual income" not taxable in accordance with Section 19A (4).**

e. **THAT the said decision failed to give a concise statement of the case, the points for determination and reason for the decision as is required under Order 21 Rule 4 of the Civil Procedure Rules as read together with Rule 20 of the Income Tax (Appeals to the High Court) Rules.**

4. Its Written Submissions were dated 7th August 2014 and filed on 8th August 2014.

THE RESPONDENT'S CASE

5. The Respondent filed its Statement of Facts dated 30th May 2013 on even date. It was its case that the Appellant had refused to declare certain incomes for the years 2004 and 2005 in accordance with Section 19 (4) (d) of the Income Tax Act which resulted in understatement of the income tax payable for the said years. It therefore raised additional assessment in the sum of Kshs 2,603,207/= and 3,240,471/= for the two (2) years respectively.
6. It was the Respondent's further contention that the Appellant had introduced additional services in the form of Front Office Services (FOSA) from which it derived income from the sale of credit forms, service fees, appraisal fees, cheque commissions, ledger fees and sale of bank cards.
7. It was emphatic that the principle of mutuality did not extend to FOSA activities and that it was justified in the additional assessment. It thus prayed for the dismissal of the appeal herein with costs to it.

LEGAL ANALYSIS

8. It was not in dispute that the Respondent rightly assessed the Appellant under the provisions of Section 19 (4) of the Income Tax. The contentious issue for determination by the court was whether or not the income that was assessed was excluded as was contemplated under Section 19A (4)(a) of the Income Tax Act.
9. The Respondent had attributed the additional tax on the Appellant from FOSA activities which it said could only be compared to banking operation services charged on account holders by banks thus bringing the income in the realm of Section 3(2)(a)(i) and (ii) of the Income Tax Act.
10. Section 3 (2) (a)(i) and (ii) of the Income Tax Act provides as follows:-

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

1. **Gains or profits from:**

a. **Any business, for whatever period carried on;**
b. **Any employment or services rendered…"**

11. On the other hand, the Appellant argued that the levying of taxes on the FOSA services was erroneous as the Respondent had failed to appreciate the income from FOSA services and its mutuality and erroneously termed the same as taxable income. It was adamant that the Respondent had no authority to tax mutual income and that it was only Parliament that had the duty to impose such taxes.
12. As was rightly submitted by the Respondent, FOSA services were not contemplated as Sacco business under the Sacco Societies Act Cap 490B (Laws of Kenya). "Sacco business" is defined in Section 2 of the said Act being a:-

"Financial intermediation and any other activity by a Sacco based on cooperative principles in accordance with the Act by way of-

a. **Receipt of withdrawable deposits, domestic money transfer services, loan advances and credit facilities; or**
b. **Receipt of non-withdrawable deposits from members and which deposits are not available for withdrawal for the duration of the membership in a Sacco society and may be used as**

collateral against borrowings and domestic money transfer."

13. What constitutes total aggregate income of such a savings co-operative society is shown in Section 19A (4) of the Income Tax Act that provides as follows:-

    "In the case of a designated primary society which is registered and carries on business as a credit and savings co-operative its total income shall, notwithstanding any provisions of this Act, be deemed to be the aggregate of:-

a. **fifty per centum of its gross income from interest (other than interest from its members);**
b. **its gross income from any right granted for the use or occupation of any property, not being a royalty, ascertained in accordance with the provisions of this Act;**
c. **gains chargeable to tax under section 3(2)(f);**
d. **any other income (excluding royalties) chargeable to tax under this Act not falling within subparagraphs (a), (b) and (c) ascertained in accordance with the provisions of this Act.**

14. Bearing in mind the definition of Sacco business against the backdrop of the provisions of Section 19 A (4) of the Income Tax Act, the court found itself in agreement with the Respondent that it was not all income that was generated by a co-operative society could be deemed to be for the mutual benefit of its members. However, interest from a member would be excluded as seen in Section 19 A (4) (a) of the Income Tax Act and would be deemed to be for mutual benefit of the members.
15. It was clear that the Appellant was carrying on certain business and/or providing services that were within what was contemplated under Section 3 (2)(a)(i) and (ii) of the Income Tax Act.
16. Indeed, the Appellant's interpretation of what **"business"** was under Section 2 of the Income Tax Act did not represent the correct position on the ground as provision of FOSA services could not be said to have been trade, profession or vocation.Additionally, it was not correct for the Appellant to have averred that the income from FOSA services should not be taxed as it was not tainted with commerciality.
17. Nothing could have been further from the truth. Sale of credit forms, services, appraisal fees, cheque commissions, sale of crop forms and ledger fees/credit Sale of Bank Card had all the hallmarks of commerce and could not possibly come within what one would have considered to have been under the principle of mutuality as had been submitted by the Appellant. This was irrespective of whether or not at the end of day, the members were expected to benefit from the gains or profits emanating from the FOSA business.
18. It was the considered view of the court that any interest accrued on FOSA services was not for the mutual benefit of members as it fell within the ambit of provisions of Section 3 (2) (a) (i) and (ii) of the Act as taxable income. For all purposes and intent, the applicable provision relating to the income in question was therefore Section 19A (4) (d) of the Income Tax Act as had rightly been submitted by the Respondent.
19. The court noted the holding in the case of **H vs The Commissioner of I.T. (1958) E.A. 303** that was cited by Majanja J in the case **Republic vs Kenya Revenue Authority & Another Ex-Parte Kenya Nut Company Limited [2014] eKLR** and relied upon by the Appellant to the effect that it was the duty of the court to gives words of the sub-section their reasonable meaning. That is correct. Similarly, parties have a duty to assign the true meaning of words in any law but not to interpret the same to suit the unique circumstances of their case.
20. Having had due regard of all the facts of this appeal against the backdrop of the applicable law, the court was not persuaded by the Appellant's submissions that it was the intention of the legislation to exempt FOSA services from taxation. Indeed, if that were the position, nothing would have been easier than for the drafters of the legislation to have categorically stated so in the Income Tax Act. Appreciably, the Income Tax is so explicit and leaves little ground to manouvre around what income should or should not be taxed. The converse is therefore true, that FOSA services fell within income that could be taxed.
21. Turning to the issue of breach of rules of natural justice by the Respondent, the court noted that the Appellant had objected to the Respondent's additional assessment. It appealed that decision at the Local Committee for Nairobi Tax District under the provisions of the Income Tax (Appeals

Committee) where the said Committee upheld the Respondent's decision.

22. The question that was before the said Committee was the same that was before the court being, whether or not the Appellant's income from FOSA services ought to have been taxed under the provisions of Section 19A(4)(d) of the Income Tax Act. The decision was as follows:-

"The appeal failed and the service fees in question is chargeable to tax under section 19A (4) (d) of the Income Tax Act.

23. It does appear that the due process of the law was followed and the same culminated in a decision that the Appellant was not satisfied with. The onus was on the Appellant to demonstrate that the Local Committee acted contrary to the rules of natural justice, that the decision was accentuated by bias and bad faith or that the decision was contrary to the weight of evidence it presented before it.
24. Whereas it was its contention that the Local Committee considered an issue that was not before it by stating that **"the service fee in question"** was chargeable under Section 19A (4)(d) of the Income Tax Act which issue was not before the said Committee, the court found the submission to have been an extraneous issue. This is because **"service fee"** from FOSA services was the subject matter of the assessment. The said Local Committee could not have made an assessment that was not based on a tangible issue. It was therefore the view of the court that the Appellant's submission on this ground failed.
25. The Appellant also was required to show which submissions the said Local Committee failed to consider and how the same impacted on its right of being given a fair and reasonable opportunity to present its case and to be heard. It is trite law that he who alleged must prove. In the absence of any evidence to support the Appellant's assertions, the court came to the conclusion that the Appellant did not discharge its burden of proof on this issue.
26. The court was also not persuaded by the Appellant's submissions that the said Local Committee did not observe the provisions of Rule 20 of the Income Tax (Appeals to the High Court). On the other hand, the court was persuaded by the Respondent's submissions that the said Local Committee's decision could not be expanded beyond what was stated. It had found that the service fee in question was chargeable under Section 19 A (4) (d) of the Income Tax.
27. The court did not find the relevance of the Appellant's submissions regarding Rule 20 of the Income Tax (Appeals to the High Courts) Rules in the circumstances of this case.
28. The said Rule provides that rules applying to civil suit shall be applicable in Income Tax Appeals in so far as they are not inconsistent with the Income Tax Act service and stipulates as follows:-

"The rules determining procedure in civil suits before the Court in so far as those rules relate to recognized agents and advocates, to service, to consolidation, to admissions, to the production, impounding and return of documents, to the summoning and attendance of witnesses, to adjournments, to the examination of witnesses, to affidavits, to judgement and decree, to the execution of decrees, to the attachment of debts, to the death, bankruptcy and marriage of parties, to withdrawal, discontinuance and adjustment, to security for costs, to commissions, to corporations, to trustees, executors and administrators, and to the enlargement of time shall, to the extent to which those rules are not inconsistent with the Act or these Rules, apply to an appeal as if it were a civil suit but, save as provided in these Rules, the procedure relating to civil suits before the Court shall not apply to an appeal."

29. Accordingly, having considered the parties' pleadings and written submissions, the court was not satisfied that the Appellant had demonstrated that the Local Committee for Nairobi Tax District came to an incorrect decision or that its decision was actuated by bias or bad faith as the Appellant had contended.
30. However, as an *obiter*, the court was of the firm belief that analysing the evidence showing how a decision has been arrived at is good practise for the Local Committee to adopt in all its appeal cases to ensure that parties follow its argument during an appeal process.

DISPOSITION

31. The upshot of this court's judgment was that the Appellant's Appeal that was lodged and filed on 6th May 2013 was not merited. The same is hereby dismissed with costs to the Respondent.
32. It is so ordered.

DATED and **DELIVERED** at **NAIROBI** this **23rd** day of **March** 2015

J. KAMAU

JUDGE