Commissioner of Domestic Taxes & another v Integrated Payment Solutions Limited & another (Income Tax Appeal E180 of 2021) [2023] KEHC 3556 (KLR) (Commercial and Tax) (18 April 2023) (Judgment)

Neutral citation: [2023] KEHC 3556 (KLR)

REPUBLIC OF KENYA

IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)

COMMERCIAL AND TAX

INCOME TAX APPEAL E180 OF 2021

JWW MONG'ARE, J

APRIL 18, 2023

BETWEEN

THE COMMISSIONER OF DOMESTIC TAXES .... 1ST APPELLANT

THE COMMISSIONER OF DOMESTIC TAXES .... 2ND APPELLANT

AND

INTEGRATED PAYMENT SOLUTIONS LIMITED .... 1ST RESPONDENT

INTEGRATED PAYMENT SOLUTIONS LIMITED .... 2ND RESPONDENT

(Appeal from part of the Judgement & Orders of the Tax Appeals Tribunal in Tax Appeal Case No. 110 of 2019 dated 6/8/2021)

JUDGMENT

1. By a Memorandum of Appeal dated October 1, 2021 the appellant, the Commissioner of Domestic Taxes, Kenya Revenue Authority, filed this appeal against the respondent, Integrated Payment Solutions Limited, a Limited Liability company incorporated in the Republic of Kenya and licenced to operate within the Republic on the following grounds:

   " 1. That the Honourable Tribunal erred in law and fact in finding that there was nothing in the submission of both parties to show that KBA members were required to pay joining fees to the Respondent.

   2. That the Honourable Tribunal erred in law and fact in finding that it was logical to conclude that the funds used to establish the Respondent came from

KBA and it is not expected that these transfers could have changed KBA's ownership of Respondent from 100%.

3. That the Honourable Tribunal erred in law and fact in relying on assumptions to arrive at its decision on the classification of joining fees by KBA members.

4. That the Honourable Tribunal erred in law and fact in disregarding the Appellant's evidence by holding that there was no evidence adduced before it attesting to any payment of joining fees by members of KBA to the Respondent.

5. That the Honourable Tribunal erred in law and fact in holding that the Appellant erred in assessing VAT on estimated joining fees from KBA members.

6. That the Honourable Tribunal erred in law and fact in disregarding the Respondent's own admission in its pleadings of having claimed input VAT after six months."

2. The Appeal arises out of a decision of the Tax Appeals Tribunal (The Tribunal) in Tax Appeal No. 110 of 2019 dated 6th August 2021 where the Tribunal held as follows;

i. The Demands for VAT in respect of estimated joining fees by members of KBA is hereby set aside.

ii. The Appellant is liable to pay VAT on joining fees paid to the appellant by non-members of KBA.

iii. The claim for input VAT made within 6 months of the end of the tax period is hereby allowed.

iv. Each party to bear its own costs.

3. The appeal filed at the Tribunal challenged the tax demand issued by The Appellant after a verification of the respondents' affairs which established that the appellant had not levied VAT to KBA members for use of its Pesalink Platform and issued a VAT tax demand for Kshs.17,508,000/-. The demand triggered the Appeal before the Tribunal and the VAT tax demand was set aside after the hearing of the matter. This led to the appellant filing this appeal before the High court seeking orders to set aside the Tribunal's judgment. The respondent has opposed the Appeal and filed its Statement of Facts dated November 5, 2021.

The Appellants case:

4. The appellant has filed the memorandum of appeal and written submissions in which it seeks to rely on. The appellant argues that the Tribunal erred in law and fact in holding that the appellant erred in assessing VAT on the estimated joining fees from KBA Members since it had clearly laid the basis upon which the verification exercise was carried upon.

5. Having established that the respondent was not levying VAT for use of its Pesalink platform by KBA members, the appellant argued that it had computed the value of the supply in line with section 13(1)(b) of the VAT Act and assessed the tax payable based on the open market value of the supplied services. The appellant submitted that it established that non-members of KBA were charged Kshs.2,500,000/- as joining fee and it is this rate that the appellant applied to assess the VAT due on the taxable supply.

6. The appellant further argued that providing a platform for a consideration amounts to supply of service subject to VAT pursuant to section 5 read together with section 2 of the *VAT Act,* 2013. Further, section 5(3) of the VAT Act places the burden of accounting for VAT in the supplier of the service, in this case the respondent.

7. Accordingly, the time of supply, pursuant to section 12 of the *VAT Act*, and in the context of this case were on December 2017 and December 2018 when the respondent supplied the services by providing access to the Pesalink platform facility to KBA members. The Appellant maintains that once a supply was made, then VAT is chargeable on the value of the supply. It is the Appellant's position that the Tribunal failed to not only understand the basis of the assessment but equally the tax point of VAT with respect to supply of services.

8. Having therefore laid the basis of the basis of the assessment, the Appellant argued that it was the Respondent was obligated to discharge its burden of proof by demonstrating that the said assessment is not only erroneous but equally excessive. The appellant relied on the decision in the case of Kenya Revenue Authority v Man Diesel & Turbo Se, Kenya (2021) to buttress its arguments on the fact that in its finding that the:-

> "The burden of proof in tax disputes flows from the presumption of correctness which attaches to the Commissioner's assessment or determination of deficiency. The Commissioner's determination of tax deficiency are presumptively correct. Although the presumption created by the above provisions is not evidence itself, the presumption remains until the taxpayer produces competent and relevant evidence to support his position. If the taxpayer comes forward with such evidence, the presumption vanishes and the case must be decided upon the evidence presented, with the burden of proof on the taxpayer."...

9. The Appellant further argued that the respondent did not discharge its burden of proof and that equally the Tribunal also failed to appreciate this principle of the burden of proof and instead made wrong assumptions in arriving at its decision. Ultimately, the Appellant argued that the Tribunal arrived at a conclusion that was unsupported by the evidence on record. The appellant urged the court to find that the decision by the Tribunal was erroneous and set it aside and reinstate the VAT Tax Assessment.

10. The second issue that the Appellant raised was the finding by the Tribunal that the Respondent was entitled to claim its input tax after the expiry of the six months period within the window allowed by the law for a Taxpayer to lodge a claim for refund of input tax. According to the Appellant, it is only after it had carried out an assessment on the Respondent that the Respondent was registered for VAT. Subsequently the Respondent lodged a claim for refund of input VAT. The issue here is whether the same could be processed as it was brought outside the six-month window period. The Tribunal found that the same could be paid and so the Appellant is urging the court to find that the finding by the Tribunal was erroneous.

11. The Appellant has reiterated that section 17 of the *VAT Act*, 2013 is unambiguous and sets clear guidelines that Taxpayers have upto six month to claim input VAT and the same ought not to be claimed monthly when VAT returns are made. If no such claim is made, then that input VAT is no longer available to the Taxpayer.

The Respondent's case:-

1. The respondent opposed the appeal and filed its Statement of Facts dated November 8, 2021. The respondents stated that it was a wholly owned subsidiary of the Kenya Bankers Association, which is

an industry association of banks and institutions licensed and regulated by the Central Bank of Kenya comprising of 47 banks operating in Kenya.

2. The Respondent further stated that it is authorised by the Central Bank of Kenya to conduct the business as a service provider as per the National Payment Systems Act, Laws of Kenya. Through its platform branded Pesalink, the Respondent provides an online platform for real time clearing and settlement of payments between banks and payment solution companies.

3. Further, it is the respondent's submissions that the members of KBA financed the establishment of the Pesalink platform by contributing funds to KBA as shareholder loans and by virtue of financing the creation of the platform, they were not required to pay a joining fee or enlist to use the platform. The respondent however, charges a one off joining fee to non KBA members of Kshs.2,500,000/- which amount is levied VAT, under the Act.

4. The Respondent submits that the Tribunal was right in finding that the assessment by the Appellant on VAT by KBA members was premised on the wrong assumption that money contributed by the KBA members could be treated as joining fee and hence be deemed Vatable under the VAT Act. It is the argument of the Respondent that the two years under review, the funds so paid to the Respondent by KBA were loans to support its establishment that the same would be recoverable in the future in the event that the platform returned a profit. In the interim period, the KBA Members continue to use the pesalink platform at no cost

5. The Respondent has urged the court to dismiss the Appeal and uphold the decision of the Tax Appeals Tribunal dated 6th August 2021. The respondent, to buttress their submissions, filed a list of authorities, which they urged the court to be guided by in arriving at a decision on the appeal.

Analysis and Determination:-

6. The court has considered the pleadings and entire record of appeal including submissions filed by the respective parties and the authorities provided by both the Appellant and the Respondent to support their positions.

7. The issues arising from grounds of appeal can be condensed to the following issues for determination:

    i. Issue 1: Whether the Tribunal erred in law and in fact in holding that setting aside the Appellant's demands for VAT in respect of estimated joining fees by members of KBA for use of the Respondent's pesalink platform".

    ii. Issue 2: Whether the tribunal erred in holding that the respondent could lodge its Claim for input VAT made within 6 months of the end of the tax period "

    8. Issue 1: Whether the Tribunal erred in law and in fact in holding that setting aside the Appellant's demands for VAT in respect of estimated joining fees by members of KBA for use of the Respondent's pesalink platform".

Section 5 of the VAT Act, 2013, states as follows; "A tax, to be known as value added tax, shall be charged in accordance with the provisions of this Act on—

(a) a taxable supply made by a registered person in Kenya;

(b) ....

(c) ....

The Act further defines Supply of Service as follow;

> S. 2. "supply of services" means anything done that is not a supply of goods or money, including—
>
> (a) the performance of services for another person;
>
> (b) the grant, assignment, or surrender of any right;
>
> (c) the making available of any facility or advantage; or
>
> (d) the toleration of any situation or the refraining from the doing of any act;

9. In determining the above issue it is important to establish whether the Respondent supplied a taxable supply to the Members of KBA. It is not disputed that VAT is a consumption tax payable by the end consumer. However, Section 5(3) of the VAT Act places the burden of accounting for VAT in the Supplier of the service and hence the responsibility to collect and remit the said tax in the particular case was one to be borne by the Respondent; Section 5(3) Provides as follows; "(3) Tax on a taxable supply shall be a liability of the registered person making the supply and, subject to the provisions of this Act relating to accounting and payment, shall become due at the time of the supply."

10. It is the Appellants argument that the Tribunal erred in its finding that VAT on the services supplied in December 2017 and December 2018 when the Respondent supplied these services by providing services on its Pesalink Platform to KBA members was not payable.

11. The Appellant took the position that it was immaterial the argument by the Respondent that the KBA members did not pay any joining fees to use the platform. The fact that other non-members of KBA paid a sum of Kshs.2,500,000/- to use the platform was sufficient to confirm indeed the Respondent provided a taxable supply and that this was the basis upon which the assessment on the VAT due was premised.

12. The Respondent argued that KBA members made capital contributions as reflected in its financial statements of 2017 and 2018 towards the establishment and strengthening of the Pesalink platform and therefore were not expected to pay any joining fee. It is the argument of the Respondent. The counter argument to the position taken by the respondents is that making capital contribution towards the establishment of the Pesalink platform does exempt the respondent from levying VAT on services rendered to any party including KBA members. The Appellant further argued that VAT is chargeable at the instance where there is a supply of service to any person, regardless of the connection to the person has with the service provider/supplier.

13. The Appellant submitted that the period covered in the assessment was not in issue and that it was also not disputed that the KBA members did access services which attracted VAT under the Act and VAT, being a consumption tax, is chargeable on the value of the supply with respect to the taxable supply made by a registered person, and so , according to the Appellant, the determinant for VAT liability is at the point a vatable supply is made, rather than the confirmation of receipt of money by the supplier in accordance with section 5(3) and section 12 of the *VAT Act*. The Appellant argues the basis by the Tribunal that the Respondent did not receive any joining fees by the KBA members was therefore irrelevant and should not have influenced its decision.

14. The respondent has further argued that the respondent and KBA members are related and hence they did not pay any joining fees to access the platform and as such there is no consideration upon which to base the VAT. Under section 13 of the VAT Act, where to entities are related the Act requires

that to determine the consideration for purposes of computing the amount of VAT to be levied on a transaction, the market value of the transaction shall be used. Section 13(b) if the supplier and recipient are related, the open market value of the supply. Non-members of KBA paid a joining fee of Kshs.2,500,000/- upon which the respondent assessed and remitted VAT on the same. In line with the provisions of section 13(b) cited above, the appellant correctly applied the said amount of Ksh.2,500,000/- to ascertain the total consideration payable by KBA members as VAT for use of the Platform.

15. Accordingly, I am persuaded that according to the *VAT Act*, 2013, VAT being a consumption tax, is chargeable at the instance where there is a supply of service to any person, regardless of the connection the person has with the service provider or supplier. It matters not the relationship between the respondent and KBA and its members in the affairs of the Respondent. The determinant factor is that once the Respondent supplied a taxable service, then VAT became due and payable on the same. I therefore hold and find the position taken by the Tribunal in setting aside the assessment of the VAT due from the Respondent on account of services supplied to KBA members through its Pesalink platform was erroneous and misinterpretation of the VAT Act since section 5 of the Act does not provide a category for exemption.

16. On the second issue as to: "Whether the tribunal erred in holding that the respondent could lodge its Claim for input VAT made within 6 months of the end of the tax period ". Section 17 of the *VAT Act* states as follows;

> 17.
>
> (1) Subject to the provisions of this section and the regulations, input tax on a taxable supply to, or importation made by, a registered person may, at the end of the tax period in which the supply or importation occurred, be deducted by the registered person, subject to the exceptions provided under this section, from the tax payable by the person on supplies by him in that tax period, but only to the extent that the supply or importation was acquired to make taxable supplies.
>
> (2) If, at the time when a deduction for input tax would otherwise be allowable under subsection (1), the person does not hold the documentation referred to in subsection (3), the deduction for input tax shall not be allowed until the first tax period in which the person holds such documentation. Provided that the input tax shall be allowable for a deduction within six months after the end of the tax period in which the supply or importation occurred.

17. Section 17(2) of the *VAT Act* states:

> (2) If, at the time when a deduction for input tax would otherwise be allowable under subsection (1)—
>
> (a) the person does not hold the documentation referred to in subsection (3), or

b) the registered supplier has not declared the sales invoice in a return, the deduction for input tax shall not be allowed until the first tax period in which the person holds such documentation:

Provided that the input tax shall be allowable for a deduction within six months after the end of the tax period in which the supply or importation occurred."

18. My understanding of the provision above is that the claim for input VAT should be made no later than 6 months after the end of the tax period when the supply occurred. From a reading of the above section of the law, time to starts to run from the time a supply or importation occurred. The timeline does not depend on when a person files its VAT returns because it is not mandatory to make the input claim during the filing of the period of filing VAT returns.

19. I am persuaded by the decision in *Highlands Mineral Water Limited v Commissioner of Domestic Taxes* [2021] eKLR where Majanja J held:

> " In my view, sections 17 and 44 of the VAT Act should not be conflated as they deal with different subjects. Section 17 falls within PART VI of the Act dealing with deduction of input tax and provides for, "Credit for input tax against output tax" while section 44 falls under PART XI dealing with Invoices, Records, Returns and Assessment and provides for, "Submissions of returns". Both subjects are different and I hold that section 44 deals with submissions of returns and consequences of failure to submit such return within the time prescribed. The only power donated to the Commissioner under section 44, as it provided at the time, was to extend time for filing the return. I cannot locate any power donated to the Commissioner, either under sections 17(1) and (2) or section 44, to disallow input tax based on late filing of a return. Further, the power donated to the Commissioner to condone late filing is only in relation to the penalty for late filing and not whether the Tax payer is entitled to credit for input tax against output tax."

20. In this case, the respondent filed its VAT returns late, outside the 6 months period as prescribed by the VAT Act. In light of this, I find and hold that the Tribunal erred in finding that the claim of input tax by the respondent should be allowed

Conclusions and Findings: -

21. In conclusion I find that the Tribunal erred in its holding that the KBA members were exempted from VAT for use of the Pesalink platform of the Respondent and allowing the respondent to claim input tax outside the 6-month window set by the *VAT Act.*

22. I therefore hold and find that the appeal as filed has merit and I will allow it with costs to the appellant.

DATED, SIGNED AND DELIVERED VIRTUALLY AT NAIROBI THIS 18TH DAY OF APRIL 2023.

J. W. W. MONGARE

JUDGE

IN THE PRESENCE OF:

Mr. Nyapara for the Appellant

Ms. Ngugi for the Respondent

Sylvia- Court Assistant