



Commissioner of Domestic Taxes v Better Globe Forestry Limited (Tax Appeal E003 of 2022) [2023] KEHC 3645 (KLR) (Commercial and Tax) (28 April 2023) (Judgment)

Neutral citation: [2023] KEHC 3645 (KLR)

**REPUBLIC OF KENYA
IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)
COMMERCIAL AND TAX
TAX APPEAL E003 OF 2022
DAS MAJANJA, J
APRIL 28, 2023**

BETWEEN

COMMISSIONER OF DOMESTIC TAXES APPELLANT

AND

BETTER GLOBE FORESTRY LIMITED RESPONDENT

(Being an appeal against the judgment of the Tax Appeals Tribunal at Nairobi dated 12th November 2021 Tax Appeal No.135 of 2021)

JUDGMENT

Introduction and Background

1. The Respondent is a forest development agency company incorporated in Kenya whose principal business is to set up and manage forest trees on behalf of its clients by inter alia, raising seedlings, planting the seedlings either in its own plantations or with partner farmers, maintaining the trees and their environment up to maturity, and harvesting the trees. At the material time, the Respondent was contracted by its related company in Norway, Better Globe AS, to undertake the management agency activities on its behalf and its investors.
2. By a letter dated 12th April 2019, the Appellant (“the Commissioner”) evinced its intention to verify the Respondent’s tax declarations as reported in its returns for the income period 2015-2018. The Commissioner explained that this was necessitated by the low ratio of tax paid as compared to the gross turnover declared and the Respondent was required to furnish the Commissioner with Sales and Purchase invoices and ledgers, Income Statements and Payrolls and any other documents and records that may be requested for purposes of the verification.



3. In a letter dated 18th October 2019, the Commissioner, in its findings did not find any anomalies under the Corporation Tax and Pay As You Earn (PAYE) tax heads. However, it noted that the Respondent had received long term loans from overseas and that these loans were interest free and as such, Withholding Tax (WHT) on deemed interest on the said loans were computed in accordance with section 16(2)(j) of the *Income Tax Act* (Chapter 470 Laws of Kenya) (“the ITA”) and assessed at a sum of Kshs. 11,830,703.10 inclusive of penalties and interest.
4. In its objection to the assessment dated 3rd April 2020, the Respondent contended that the amounts received to set up the forests were not loans as the funds were not transferred to it for its own use and to be repaid later. That there was no provision for repayment as the funds were held in trust on behalf of the investors and utilised that capacity to set up the forests owned by the said investors who retained ownership of the trees and that attendant risks. It argued that a loan is a specific amount that must be returned to the lender with or without interest which was not the case as there was no borrowing of money, no security is presented, and the risk did not move to the Respondent.
5. The Respondent averred that the nature of the funds received is an investment because the trees are sold upon maturity and all the proceeds are paid out to the investors and none is retained. It urged that if the amounts had been loans, the Respondent not only would it have been required to provide security, it would also be required to repay the amount the amount advanced to it and ultimately it would own the trees and the proceeds of sale of the trees.
6. The Respondent stated that deemed interest only applies to interest free loans and if the amounts are not loans, then deemed interest does not arise. Nevertheless, the Respondent added that even if the amounts were to be regarded as loans, they would not be interest free as the reward for a loan is interest and the reward expected by investors is approximately 200% or 10% per annum which cannot be regarded as interest free.
7. The Respondent asserted that it is committed to contributing to tax collections and supporting the Kenyan economy and enhancing a better environment for all as it is a social entrepreneurship concept. It contended that it employs hundreds of Kenyans, largely women and the youth and that they are also enrolling communities to engage in tree planting, and this will be an additional income earner for the benefitting families while the environment is preserved and rehabilitated with trees. That the varieties of trees grown are arid and semi-arid varieties and this ensures that land that would otherwise be left to waste because it cannot be cultivated, is put to good use which provides income and also enhance the ecosystem of an environment.
8. The Respondent further noted that in 2015, the President awarded it as a distinguished taxpayer in the best corporation tax yield (small and medium enterprises) and that it also has a current tax compliance certificate. That these demonstrated its commitment to tax compliance and cooperation with the Commissioner that was not feasible that it would apply a wrong tax treatment. The Respondent therefore urged the Commissioner to revise the WHT assessment on deemed interest.
9. Having considered the objection, the Commissioner issued its objection decision dated 12th February 2021 (“the Objection Decision”). The Commissioner was not satisfied with the Respondent’s reasons that WHT was not applicable for various reasons. The Commissioner stated that during the review of the Lease Agreements where the forests are set up, it noted that the parties contracting were the Respondent and local owners and that it was also evident that the business conducted did not involve the overseas investors as alleged, which meant that the ownership of the trees belonged to the Respondent. The Commissioner also noted that the funds received from the Respondent’s related company, Better Globe AS were recorded as tree owners’ funds, a non-current liability in the Respondent’s books.



10. The Commissioner further found that the Respondent was unable to demonstrate that the remittances from overseas investors were the same funds that were received by the Respondent to the satisfaction of the Commissioner. The Commissioner noted that section 16(3) of the ITA defines "all loans" to mean loans, overdrafts, ordinary trade debts, overdrawn current accounts or any other form of indebtedness for which the company is paying a financial charge, interest, discount or premium. That the fact that the trees owners fund sat in the Respondent's books as a liability, then the funds would be repaid at a later date. The Commissioner therefore held that it was correct for it to classify the tree owners' funds as loans based on the above definition.
11. The Respondent, being dissatisfied with the Objection Decision, appealed to the Tax Appeals Tribunal ("the Tribunal"). Having considered the appeal, the Tribunal rendered a judgment on 12th November 2021. In the judgment, it framed one issue for determination; whether the funds remitted to the Respondent by Better Globe AS constituted an interest-free loan hence attracting WHT pursuant to sections 2, 16 and 35 of the ITA.
12. In reviewing the evidence before it, the Tribunal noted the Respondent's argument that the investors in Norway invest €17 per tree and expect a return of €191.25 per tree at maturity, after between 15 to 20 years depending on the specific location of the forest, soil, water and other environmental factors and that at maturity, the Respondent buys the trees from the tree owners, who receive approximately €208.25 per tree. The Tribunal observed that the € 17 per tree was not the same as the amount of Euros at the end of the 15 to 20 years, therefore, the concept of "interest-free" was not apparent to the Tribunal as the resultant amount in question was associated with an implied return of around 56%. However, the Tribunal kept the accounting treatment aside and proceeded to analyse where the risk of the tree planting and related reward stood. The Tribunal then proceeded to establish whether the underlying transaction was one that is return or interest free.
13. The Tribunal observed that in Clause 1.1. of the agreement between Better Globe AS and the investors, the investors acquire the ownership of the trees when they buy the seedlings. The investors also assume the risks relating to fire, insect attacks and other risks as soon as they buy them, acknowledging that the Respondent will work to minimize these risks as provided in Clause 3.1. From the totality of the documentation provided to it, the Tribunal understood that Better Globe AS, buys trees or seedlings and concurrently enters into a contract with the Respondent which takes care of the trees for between 15 to 20 years depending on environmental factors. It noted that there is also a formal agreement whereby the Respondent buys the trees in year 20 or earlier. Further, the Respondent enters into land leases from landowners and is required to tend the trees on the leased land. The Tribunal concluded that this mere fact of being a signatory, does not entitle it to full and complete ownership of the trees which could be owned, shared or caveated by Better Globe AS or its investors. The Tribunal concurred with the Respondent that ownership must be actual, legal, economic, and commercial and cannot be construed otherwise.
14. The Tribunal held that once the Respondent delivered its evidence by way of agreements between itself and Better Globe AS, the burden of proof shifted to the Commissioner especially given the formal correction of the Respondent's audited Financial Statements to amend the element of "biological ownership". The Tribunal noted that the International Accounting Standards allow for amendment of Accounts including the Respondent's actions whereby in 2016 and the subsequent years, it wrote-off the biological assets in its books. The funds from the overseas investors, the tree-owners' funds, were then booked as a noncurrent liability in the balance sheet of the Respondent. The Tribunal further noted that the accounts had been audited by Masambu and Associates and also noted that the Commissioner had stated in its pleadings that the Respondent had agreed to pay the amounts and had



requested for a payment plan for the same. However, the Tribunal held that there was no proof of such an agreement.

15. The Tribunal thus held that the Commissioner had failed to disprove the Respondent's argument that the sell-back price had an implied return of 56% and consequently, the Tribunal found that the funds remitted to the Respondent by Better Globe AS did not constitute an interest-free loan and therefore did attract WHT pursuant to the ITA. It allowed the Respondent's appeal and set aside the Objection Decision.
16. The Commissioner is dissatisfied with this judgment by the Tribunal and has now lodged an appeal to the court through its Memorandum of Appeal dated 6th January 2022. In response, the Respondent has filed its Statement of Facts dated 25th April 2022. The appeal was disposed by way of written submissions which are on record where the parties have rehashed their positions as outlined above.

Analysis and Determination

17. Turning to the appeal, even though the Commissioner raised three grounds in its Memorandum of Appeal, it has condensed the same into one singular issue in its written submissions. This is more or less similar to what the Tribunal dealt with; whether the amounts being remitted to the Respondent by Better Globe AS were interest free loans from a non-resident and thus subject to deemed interest attracting WHT.
18. In determining this appeal, I am cognizant that the court's appellate jurisdiction is circumscribed by section 56(2) of the *Tax Procedures Act*, 2015 which provides that "An appeal to the High Court or to the Court of Appeal shall be on a question of law only". The Court of Appeal in *John Munuve Mati v Returning Officer Mwingi North Constituency & 2 others* [2018] eKLR summarised what amounts to "matters of law" as follows:
 - (38) [T]he interpretation or construction of the *Constitution*, statute or regulations made thereunder or their application to the sets of facts established by the trial Court. As far as facts are concerned, our engagement with them is limited to background and context and to satisfy ourselves, when the issue is raised, whether the conclusions of the trial judge are based on the evidence on record or whether they are so perverse that no reasonable tribunal would have arrived at them. We cannot be drawn into considerations of the credibility of witnesses or which witnesses are more believable than others; by law that is the province of the trial court.
19. In essence, an appellate court restricted to determining questions of law may yet quite properly interfere with the factual conclusions of a tribunal if they are erroneous in points of law. Thus, if the tribunal arrives at a conclusion on the primary facts that a reasonable tribunal considering the same facts could not reasonably come to such a conclusion or decision, it becomes an error of law which the appellate court is entitled to intervene.
20. WHT is a method of tax collection whereby the payer is responsible for deducting tax at source from payments due to the payee and remitting the tax so deducted to the Commissioner. Under section 10(1) of the ITA, the resident company paying interest and deemed interest is required to pay WHT to the Commissioner as follows:
 10. Income from management or professional fees, royalties, interest and rents
 - (1) For the purposes of this Act, where a resident person or a person having a permanent establishment in Kenya makes a payment to any other person in respect of-



(c) interest and deemed interest

21. Under section 16(3) of the ITA “Deemed Interest” is defined as “....an amount of interest equal to the average ninety-one day Treasury Bill rate, deemed to be payable by a resident person in respect of any outstanding loan provided or secured by the non-resident, where such loans have been provided free of interest.” In essence, it is applicable on interest free borrowing and loans received from foreign-controlled entities in Kenya. Under section 35(1) of the ITA, a person upon payment of a non-resident person not having a permanent establishment in Kenya in respect of interest which is chargeable to tax is required to deduct withholding tax at the appropriate non-resident rate which is provided for in the Third Schedule to the ITA.
22. Whether the amount received by the local entity is a loan that attracts interest or deemed interest is a question of fact. Given the jurisdiction of the court, the duty of this court is to examine the record and satisfy itself that the determination of the Tribunal comports with the evidence.
23. The Commissioner contends that it was not satisfied with the Respondent’s explanation that the remittances by Better Globe AS were customer remittances as opposed to loans. It submits that the Respondent was severally invited to prove its allegation that the funds received were not interest free loans but it failed to do so. The Commissioner emphasizes that a taxpayer’s statements and assertions have to be supported by positive evidence.
24. The Tribunal, as I have summarised above, was satisfied with the evidence provided by the Respondent including the agreements between the Respondent and Better Globe AS and the formal correction of the Respondent’s audited financial statements which it used to conclude that the sell-back price of the trees had an implied return of around 56% and as such, the remittances made by the Respondent did not constitute an interest-free loan by Better Globe AS to the Respondent.
25. The Commissioner is correct to submit that section 56(1) of the *Tax Procedures Act* (“the TPA”) imposes the burden of proof on the tax payer to prove that an assessment is excessive or a tax decision is incorrect and that under section 59 (1), a tax payer shall produce records when required to do so by the Commissioner for the purposes of obtaining full information in respect of their tax liability. This position is fortified by section 54A of the ITA which requires a person carrying on a business to keep records adequate for the purpose of computing tax. In addition to the records being adequate, a taxpayer ought to ensure that they are also relevant and competent (See *Republic v Kenya Revenue Authority; Proto Energy Limited (Exparte)* (Judicial Review Application E023 of 2021) [2022] KEHC 5 (KLR) (24 January 2022) (Judgment).
26. From the record, I note that the Respondent, more times than not, responded to the Commissioner by availing the documents or information sought by the Commissioner with the last correspondence being on 23rd October 2020 where the Respondent availed extracts from Strype, a payment processing platform, indicating how the pooled purchases were captured and reflected on Better Globe AS’s Strype accounts. This information had been sought by the Commissioner who wanted to understand how the remittances flowed from Better Globe AS to the Respondent and back to Better Globe AS and whether the same had a correlation to the remittances by the said investors to Better Globe AS. It is my finding from a perusal of the record that the Respondent was able to at least meet the minimum threshold of competent and relevant information and documentation necessary to support its position. It should not be lost that what the Respondent was required by law to establish was a prima facie case and that the Commissioner ought to have measured these evidence on a preponderance of probabilities (See *Kenya Revenue Authority v Maluki Kitili Mwendwa* ML HC ITA No. E078 of 2020 [2021] eKLR).



27. I therefore do not agree with the Commissioner that the Respondent failed to discharge its evidential burden as required because the record demonstrates otherwise. I am unable to find fault in the Tribunal's conclusion that the remittances made by the Respondent to Better Globe AS were not loans attracting deemed interest but remittances from Better Globe AS's investors who got a Return on Investment from the said remittances. The Tribunal's overall conclusion was thus sound and I do not find any reason to intervene.

Disposition

28. For these reasons, I dismiss the appeal but with no order as to costs.

SIGNED AT NAIROBI

D. S. MAJANJA

JUDGE

DATED AND DELIVERED AT NAIROBI THIS 28TH DAY OF APRIL 2023.

F. MUGAMBI

JUDGE

Court Assistant: Mr Michael Onyango.

Ms S. Addah, Advocate instructed by the Kenya Revenue Authority for the Appellant.

Mr Tugee instructed by Munyao, Muthama and Kashindi Advocates for the Respondent.

