

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
APPEAL NO.99 OF 2015

SEAFORTH SHIPPING (K) LIMITED.....APPELLANT

VERSUS

THE COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGEMENT

1. The Appeal herein arises from a dispute between Seaforth Shipping (K) Limited hereinafter referred to as Appellant with The Commissioner of Domestic taxes, hereinafter referred to as Respondent. It is in respect of the confirmed Notice of assessment issued by the Respondent to the Appellant on 26/2/2013. The dispute relates to two issues, namely:-
 - a) Pay as You Earn hereinafter referred to as PAYE, charged as a benefit on the Appellant's director, One Mr. Knight.
 - b) Corporation Tax charged after disallowing travelling expenses incurred in prior years (i.e. 2007, 2008 and 2009) claimed in the year of income 2010.

2. The Appellant filed this Appeal on the following grounds:-
 - a) Passage for expatriate director is not taxable in the hands of the expatriate director contrary to the assertion of the Respondent.
 - b) Section 5(4) (a) of the Income Tax Act allows that passage for employees who are not Kenya citizens and are recruited outside Kenya to serve their employer are not taxable income in the hands of the employees.
 - c) A director is considered and treated as an employee under the Income Tax Act for the purposes of section 5(4)(a). Where the Income Tax purports a different treatment for tax for an employee and director e.g. Sections 5(2)(c) on termination of contract, 5 (2A) in regard to loan benefit, 5(3) in regard to housing benefit, and 5 (4)(b) in regard to medical benefit, then the Act clearly makes the distinction. The making of the passage taxable using the definition

under S5(2A) is not correct, as this definition only relates specifically to the taxation of benefits for loans given to employees.

- d) The expatriate director in question Mr. James Knight, the Appellant's executive director, is a foreigner and he was recruited outside Kenya to come and work for the Appellant in Kenya.
 - e) The Respondent erred in making the assessment on grounds that Mr. James Knight is excluded from Section 5(4) because he is also a shareholder in the Appellant.
 - f) The Respondent has disallowed travel expenses for the director for the years 2007 to 2009 on the grounds that these are not supported. However, original invoices, receipts, relevant pages from the director's passport with immigration stamps proving that the travel did indeed take place and details of clients visited were all availed to the Respondent.
3. The Respondent filed a statement of facts in response to the Appellant's Memorandum of Appeal. The Respondent stated as follows:-
- a) The Appellant incurred passage expenses in respect of one of the directors who is also a shareholder of the company. The shareholders of the Appellant include James Knight, Marianne Dunford and Sovrachat International Holding Australia with shares of 7650, 7651 and 14699 respectively. The director, James Knight, is not a Kenyan citizen but owns shares and he is the managing director of the Appellant and also a director in a related company namely, seatrade Agencies Limited.
 - b) The Respondent states that the director is not in Kenya solely for the purpose of serving the employer, but has vested interest through shareholding in more than one Kenyan company. Section 5(4)(2) of the Income Tax Act refers to employees recruited or engaged outside Kenya and who are in Kenya solely for the purpose of serving the employer. In this case, James Knight has other investment interests in the country and he is a shareholder of more than two local companies is not solely for the purpose of serving the employer. Therefore the expenditure on passage is a benefit on him.
 - c) The Appellant made payments to employees yet no deductions for PAYE were done on those employees earning above the minimum threshold as provided in the Income Tax Act section 5. The arguments by the Appellant that the amounts paid to drivers

included amounts that were to be passed over to the turn boys was not supported by any material evidence. No petty cash vouchers signed by the turn boys have been produced for verification.

- d) In the year of income 2010, the Appellant claimed as company expense amounts relating to one of the directors travels from earlier years i.e. 2007 to 2009. The same was disallowed on the basis that it was not wholly and exclusively incurred in the earning of that income and it could not be supported with relevant tickets.
- e) The Respondent states that the directors travelling expenses were from prior period i.e. 2007, 2008 and 2009. Section 15 of the Income Tax Act Cap 470 states in part, "For the purpose of ascertaining the total income of a person for a year of income there shall, subject to section 16, be deducted all expenditure incurred in that year of income which is expenditure wholly and exclusively incurred by him in the production of that income...."

It is on this basis that the Respondent maintains that these expenses should not be claimed against the income of 2010 as they were not incurred in the production of that income.

- 4. The tribunal notes from the evidence adduced that Mr Knight, an expatriate, is a British Citizen working in Kenya as the Managing Director of the Appellant. Mr Knight also holds 25% of the shares in the appellant company. In addition, Mr Knight also was a shareholder and director in Seatrade Limited, a related company of the appellant. During the years 2010 and 2011, the appellant incurred a total of Kshs.2,187,621/= towards home travel by Mr Knight. The appellant did not subject the amounts to PAYE as it treated the expenditure as passage allowances, which were exempt from PAYE under Section 5(4) of the Income Tax Act, which provides that *the taxable remuneration of an employee shall not include expenditure on the provision of passage for the benefit of an employee recruited or engaged outside Kenya and who is in Kenya solely for the purpose of serving the employer and is not a Citizen of Kenya.*
- 5. The respondent undertook an audit of the appellant company and challenged the exemption of the expenditure from PAYE on the basis that Mr Knight is not "*in Kenya solely for the purposes of serving the employer*". Accordingly, the respondents assessed PAYE for the years 2010 and 2011 amounting to Kshs.656,286/= penalty of

Kshs.164,072/= and interest of Kshs.262,740/= altogether totalling to Kshs.1,083,098/=

6. In addition to the above, during the period 2007 to 2010, Mr Knight incurred travelling expenses amounting to Kshs.2,545,975/= towards his travel within Kenya and to countries abroad including United Kingdom (UK), United States (USA), India, United Arab Emirates (UAE), Switzerland and France. This amount included local travel within Kenya amounting to Kshs.104,814/= and overseas travel of Kshs.2,441,161/= Hence, Mr Knight lodged a claim for reimbursement of Kshs.2,545,975/= in 2010 by filling the claim forms and attaching supporting documents, which included receipts and passport documents. The appellant reimbursed the full amount to Mr Knight and claimed the same as an expense in 2010.
7. When this Appeal came up for hearing, the parties agreed to prepare and file written submissions which were duly done. The Appellant's submissions were that Mr Knight was in the country only to serve as an employee of the Appellant and he spends all his time serving the company and does not engage in any other activity. Mr Knight could not be said to also be in the country as a shareholder as shareholding or investment was an act that did not require active effort or physical engagement in the company affairs. The Appellant argued that Mr Knight was recruited to be managing director and not to be a shareholder. He could have held shares and still not be present in Kenya.
8. The Appellant further argued that the provision "**solely for the purpose of serving the employer**" cannot be understood to mean that expatriates cannot be shareholders in Kenyan companies to qualify for tax-free passage. Further, the Appellant stated that Seatrade Limited where Mr. Knight was also a shareholder and director was formed as a business strategy so that it could bid for business for which the appellant was not eligible for. The Appellant stated that as a group director, Mr Knight also had the responsibility to supervise the other operations of Seatrade. This could not be construed as separate employment. Appellant also cited an example that group MDs supervise a number of companies within the same group under the same employment contract and they might even be appointed directors to satisfy legal requirements. The Appellant also

argued that it was a common practice that the staff (or directors) of one company in a group may provide support, on occasional basis, to a sister company within the same group.

9. The Appellant further argued that directorship in itself is not a full time engagement, except for full time directors. Therefore, Mr Knight's directorship in Seatrade could not be used as a basis to defeat a relief granted under Section 5(4) of the Income Tax Act.
10. Regarding Mr Knight's local and overseas travel expenditure amounting to Kshs.2,545,975/= the Appellant argued that the travel expenditure of Mr Knight was to visit a number of its clients whose head offices were based in Nairobi. They included *inter alia* GAPCO, Total Kenya, Vivo Energy, Hashi Petroleum. The Appellant insisted that Mr Knight's travel was for business and the same generated income in the year of travel as well as in subsequent years. Appellant further argued that the client relationship management and marketing always had the effect of generating income in future years.
11. The Appellant argued that the overseas travel of Mr Knight was to meet a number of customers including Gulf Agency, Shell London, Chevron London, EDF, Vital SA and GSE Logistics. Further, in India, Mr Knight visited a number of clients like Tata India, Reliance Industries and JM Baxi, to prospect for business. Similarly, Mr Knight visited USA to meet clients like USAID, Maersk and International Maritime Services. In 2008, Mr Knight travelled to Vienna and Paris (France) to meet clients, who included Louis Dreyfus.
12. The Respondent's submissions were that Mr Knight was the Managing Director of Sea trade & Transec and a director in Kazkazi, where he earned consideration for the services provided. He was the shareholder of the appellant company, Seaforth (holding 25% shares), Seatrade (holding 99% shares) and Transec (over 50% of shares). Mr Knight was the Managing Director of the appellant company and in addition he was also a director of Transec, Seatrade and Kazkazi.
13. Mr Knight earns a monthly salary from the appellant company and also from Transec as indicated in the self-assessment return (IT1) of Mr Knight and as evidenced by the PAYE returns filed by the two companies.

14. In view of the above, the Respondent argued that *Mr Knight was not solely in Kenya for the purpose of serving the appellant and hence did not qualify to claim tax-free passage under Section 5(4) of Income Tax Act.*
15. The respondents further argued that Mr Knight holds substantial shares in the three companies, whereas there is no other reason to qualify the three companies as group companies except the common shareholding of Mr Knight in all three companies and hence the argument of the appellant that all three companies were inter-related was untrue.
16. The travel expenditure of Mr Knight was claimed by the appellant in the year 2010 while the travel was related to prior years 2007, 2008 and 2009. The Respondent stated that the appellant did not provide any tickets to determine the nature of the expenses.
17. The respondents referred to Section 15 of the Income Tax Act which states as follows:-

“For the purpose of ascertaining the total income of a person for a year of income there shall, subject to section 16, be deducted all expenditure incurred in that year of income which is expenditure wholly and exclusively incurred by him in the production of that income and where under Section 27 any income of an accounting period ending on some day other than the last day of that year of income is, for the purpose of ascertaining total income for a year of income, taken to be income for a year of income, then the expenditure incurred during that period shall be treated as having been incurred during that year of income”.
18. The Respondents claim that none of the expenses disallowed was incurred for the year of income 2010 and hence the only remedy available to the appellant was an application under Section 90(1) of the Income Tax Act to the Commissioner for relief to amend its assessment, an application which was not done.
19. The self-assessment returns indicate that Mr Knight received higher remuneration (almost double) from Transec as compared to the remuneration received by him from the appellant company. The Tribunal notes that the Appellant failed to give material fact to the Tribunal on this issue. It was indeed brought out by the Respondent

and the same has not been rebutted by the Appellant. The Tribunal will draw adverse inference against the Appellant. Failure to do is indeed against the principles of equity and therefore against the maxim that “**He who comes to court must do so with clean hands**”. This material fact would be necessary to assist the Tribunal in arriving at a fair conclusion were it laid bare before it.

20. Moreover, the tribunal notes that if the companies referred to herein above do similar business it is possible that when travelling, Mr. Knight was carrying out activities relating to both companies. This is indeed admitted by the Appellant in their submissions filed on 18/4/2016, paragraphs 1.27 and 1.28. The Tribunal is indeed persuaded and makes a finding that the two companies activities are intertwined. Indeed when a person receives substantial remuneration from another company, he *cannot justify his argument that he was solely in employment of one company.*
21. The tribunal further notes that Mr Knight holds substantial controlling interest in Seatrade (holding 99% shares) and Transec (holding over 50% of shares). He cannot be considered as a normal part-time investor as any person holding substantial controlling interest in any company is expected to spend considerable portion of his time in the management and/or in overseeing the activities of that company. Hence the tribunal makes a finding that Mr Knight cannot be considered to be *in Kenya solely for the purposes of serving the employer, the appellant and hence does not qualify for the entitlement of tax-free passage as permissible under Section 5(4) of Income Tax Act.*
22. The tribunal notes that the Matching principle directs a company to report an expense on its income statement in the same period as the related revenues. If the future benefit of a cost cannot be determined, it should be charged to expense immediately. The Tribunal notes further that the Appellant failed to avail itself to the window of opportunity provided under section 9(c) of the
23. Income Tax Act in respect of the expenditure claims for the years 2007, 2008 and 2009. They only have themselves to blame for this failure.

24. The Tribunal has perused the authorities cited by the Appellant and note that the same are distinguishable as the issues therein are not relevant to the issues before the Appeal herein.
25. The Tribunal will not belabour on the same as it is trite law that in interpreting statutes, the principle of strict or literal construction applies. In the case of **Cape Brandy Syndicate versus I.R.C (1KB 64, 71** it was stated as follows,

“In a taxing statute one has to look merely at what is clearly said. There is no room for any intendment there is no equity about a tax. There is no presumption as to a tax. Nothing is to be read in; nothing is to be implied. One can look fairly at the language used”
26. The upshot of the above is that the Appeal herein has no merit and the same is hereby dismissed with no Order as to Costs and the Respondent’s Notice of Assessment is hereby upheld.
27. The Appellant has a right to Appeal against this decision.


THESE ARE THE ORDERS OF THIS HONOURABLE TRIBUNAL.

DATED and DELIVERED at NAIROBI this 9th Day of December, 2016.

In the presence of:-

SAMWEL KIOKO for the Appellant

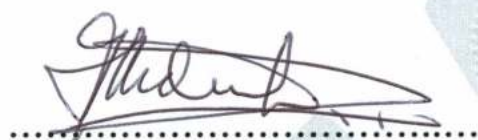
NAFTALI OYUGI for the Respondent



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A.G.N. KAMAU
CHAIRPERSON



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PONANGIP ALLI V. R. RAO
MEMBER



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WILFRED N. GICHUKI
MEMBER



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JOSEPHINE K. MAANGI
MEMBER