REPUBLIC OF KENYA

IN THE TAX APPEALS TRIBUNALAT NAIROBI

APPEAL NO. 5 OF 2015

GLAXOSMITHKLINE LIMITED .....APPELLANT

VERSUS

THE COMMISSIONER OF DOMESTIC TAXES .....RESPONDENT

RULING

GLAXOSMITHKLINE Limited (hereinafter referred to as the Appellant) lodged an appeal against the decision of the Commissioner of Domestic Taxes (hereinafter referred to as the Respondent) dated 29th November, 2012. The decision was as a result of the Respondent's comprehensive tax audit of the Appellant's operations for the years 2009 and 2010. The said audit resulted into a revised tax assessment in the sum of Kenya Shillings Thirteen Million One Hundred and Sixty Five Thousand Three Hundred Twenty Six (Kshs: 13,165,326/=) made up as hereunder:-

a) Corporation Tax being the disallowed Investment Deduction Claimed on renovation and rehabilitation works in the sum of Kenya Shillings Twelve Million, Five Hundred and Twenty Eight Thousand, Two Hundred and Fifty Three (Kshs: 12,528,253/=).

b) Withholding Tax applied on professional and contractual services rendered to the Appellant in the sum of Kenya Shillings Six Hundred and Thirty Seven Thousand, Seventy Three (Ksh: 637,073/=).

The Tribunal will hereunder summarize the facts that led to the appeal herein;

It notes that the Appellant has its factory which is located along Likoni Road, Nairobi. The factory was set up for the manufacture of its products in 1958. The Appellant conceded that this is the same factory currently in existence for manufacture. It underwent substantial renovation in the years 2009 and 2010. The renovations were as follows:-

a) The asbestos factory roof was replaced by iron sheets roof.
b) The terrazzo floor and corridor were removed and replaced by an anchorite floor.

The Respondent carried out a comprehensive tax audit of the Appellant's operations for the years 2009 and 2010 and raised an initial tax assessment of Kenya Shillings Thirty Million Three Hundred And Thirty Five Thousand Two Hundred And Sixty Two (Ksh. 30,335,2620). The Appellant paid a sum of Kenya Shillings Three Million Five Hundred and Twenty Three Thousand Five Hundred and Sixteen (Khs. 3,523, 516) on agreed areas and after several consultative meetings between the parties, the Respondent issued a demand of the said sum of Kenya Shillings Thirteen Million One Hundred And Sixty Five Thousand Three Hundred And Twenty Six (Ksh: 13,165,326) aforesaid; which the Appellant objected to and proceeded to file this Appeal.

The Tribunal has studied the Memorandum of Appeal, the Statement of facts, and the Respondent's Response together with all the documents filed and furnished by the parties together with the submissions of both parties. It has framed two issues for its determination herein, namely:-

1. **Whether the cost of substantial renovations or rehabilitations of an industrial building used for manufacture qualifies for investment deduction at 100%**

The appellant claims Investment Deduction (hereinafter referred to as ID), by virtue of paragraph 24(1c) of the Income Tax Act (ITA). The same states as follows;

"Subject to this schedule, where capital expenditure is incurred on or after the 1st January, 1992 on the construction of a building where the owner or the lessee of that building uses the building for the purposes of manufacture; there shall be deducted, in computing gains or profits of the person incurring that expenditure for the year income in which they were first used(hereinafter referred to as "the year of first use") provided that, prior to its first being used for manufacture after its completion, it has been used for no other purpose, a deduction referred to as investment deduction".

The tribunal notes that The Second Schedule of the Income Tax Act lists Capital allowance deductions in six parts. Under part V paragraph 24(1) (c) of the second schedule a taxpayer is allowed to claim ID in the year they first incur expenditure on construction of a building. The same is granted only once at 100% in the first year of use.

The Appellant contends that it undertook renovations of a used building which qualified for ID and relied on the definition of a building pursuant to paragraph 24(3)(e).The same states as follows;

"....building" includes any building structure and where the building is used for purposes of manufacture it includes the civil works and structures deemed to be part of an industrial building under paragraph 1(1A) of this schedule".

The Tribunal agrees with the Appellants argument on the definition of a building to the extent that the substantial renovations qualifies as construction of a building in accordance with paragraph 24(1c) of the Income Tax act. The Tribunal further agrees with the Appellant that the building which is the subject of this substantial renovation and rehabilitation has been used and is being used for the purpose of manufacture.

However, the Tribunal makes a finding that the fact that the building has previously been used for the purpose of manufacture runs contrary to the proviso that requires it to have been used for no other purpose pursuant to section 24(1c) of the said Act.

The requirement for this provision is that the Appellant renovated a building but did not install machinery which was to be used for manufacturing. The deduction is claimable in the year of first use. The year of first use excludes renovation under section 24(1c).

Moreover, the tribunal further notes that paragraph 1(A) (3) read together with paragraph 1(1A) of the said Act shows that the substantial renovations amount to construction of a building. However the building must not have been used for any other purpose.

2. **Whether payments made to persons offering professional services to contractors should be treated as professional or contractual fees liable to withholding tax.**

The Tribunal notes that both the appellants and respondents definition of professional fees is agreed upon to the effect that it means a payment made to a person, other than a payment made to an employee by his employer, as consideration for managerial, technical, agency, contractual, professional or consultancy services however calculated as per Section 2 of Income Tax Act.

The relevant section regarding the applicability of withholding tax on payments made to service providers is section 35(3)(f) of the Income Tax Act. This section has a proviso which states as follows;

".....Provided that for the purposes of this paragraph, the contractual fee within the meaning of 'management or professional fee' shall mean payment for work done in respect of building, civil, or engineering works".

The appellant has relied on this provision to deduct withholding tax at the rate of 3% on payments made for Architects, Engineers etc on the basis that the proviso to Section 35 defines the services they provide to be of a contractual nature.

It is the finding of this tribunal based on the definitions above and the provisions of the Income Tax Act in respect of the contractual and professional fees that the architects and other consultants were providing professional services to the appellant and were not engaged in building, civil or engineering works. Therefore the law clearly stipulates that upon payment to these professionals Withholding Tax ought to be charged at management or professional rate.

The upshot of the above is that the Appeal herein lacks merit and is hereby dismissed with no Orders as to costs.

THESE ARE THE ORDERS OF THIS HONOURABLE TRIBUNAL.

DATED and DELIVERED at NAIROBI this 8TH day of JUNE 2016.

JOSEPHINE KEMUNTO MAANGI

CHAIRPERSON OF THE PANEL

JOSEPH WACHIURI .....MEMBER

PHILIP KORIR .....MEMBER

RICHARD ROTICH .....MEMBER

BONIFACE DIMMO .....MEMBER