Commissioner of Domestic Taxes v Co-operative Bank of Kenya Limited (Tax Appeal E095 of 2020) [2022] KEHC 15973 (KLR) (Civ) (30 November 2022) (Judgment)

Neutral citation: [2022] KEHC 15973 (KLR)

REPUBLIC OF KENYA

IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)

CIVIL

TAX APPEAL E095 OF 2020

DAS MAJANJA, J

NOVEMBER 30, 2022

BETWEEN

COMMISSIONER OF DOMESTIC TAXES ..... APPELLANT

AND

CO-OPERATIVE BANK OF KENYA LIMITED ..... RESPONDENT

(Being an appeal against the judgment of the Tax Appeals Tribunal at Nairobi dated 30th July 2020 in Tax Appeal No. 45 of 2017)

JUDGMENT

DIVISION - Introduction and Background

PARA 1.

Before the court for determination is an appeal filed by the Appellant ("the Commissioner") dated 24th September 2020 against the judgment of the Tax Appeals Tribunal ("the Tribunal") dated 30th July 2020. The Respondent is a publicly listed bank licensed under the *Banking Act* (Chapter 488 of the Laws of Kenya) to carry on the business of banking.

PARA 2.

The facts giving rise to the instant appeal can be traced back to a compliance check exercise that was conducted by the Commissioner on the Respondent's financial and tax affairs for the years of income 2013 to 2015. The Commissioner communicated its findings to the Respondent through its letter dated 7th November 2016 where it issued additional tax assessments totaling Kshs. 1,025,206,410.00 under the tax heads of Value Added Tax ("VAT"), Pay As You Earn ("PAYE"), Withholding Tax ("WHT") and Excise Duty and which amount included penalties and interest.

PARA 3.

In its response to the findings, the Respondent, through its letter dated 5th December 2016 conceded and settled the principal tax assessments totaling Kshs. 5,456,181.00 in respect of its PAYE, VAT and WHT obligations but contested and formally objected to the rest of the assessments totaling KES 1,019,377,814.00

PARA 4.

The Commissioner, through its letter dated 1st February 2017 ("the Objection Decision") partly allowed the Respondent's objection by vacating the duty and tax demanded on some of the items in contention but then upheld its assessments of Kshs. 57,200.00 and KES 621,537,611.00 in respect of WHT on winnings and Excise Duty on financial transactions respectively.

PARA 5.

The Respondent lodged its appeal against the Objection Decision at the Tribunal on the ground that the demand for KES. 62,537,611.00 in relation to Excise Duty was erroneous in law and in fact and that it was based on material misunderstanding of the *Customs and Excise Act* (Chapter 472 of the Laws of Kenya) (Repealed) (''the CEA") and the *Excise Duty Act*, 2015 ("the EDA") which levies Excise Duty on ''Other fees'' charged by financial institutions and specifically exempts interest charge from the definition of "Other fees''. It contended that the Commissioner failed to take into account all information and explanations provided in order to appreciate all issues before it and that the it ignored and failed to take into account, inter alia, the definition of 'interest' under the *Income Tax Act* (Chapter 470 of the Laws of Kenya) ('the ITA").

PARA 6.

The issue framed by the Tribunal for resolution was whether the Commissioner erred in charging Excise Duty of total fees and commissions as appearing in the Respondent's financial statement. In this respect the Tribunal made several findings. First, it held that the Excise Duty charged for the period preceding 18th June 2013 would not be payable by the Respondent in view of the amendments introduced by the Finance Act, 2013 to the CEA. Second, it considered whether the bulk of the Commissioners assessment comprising moratorium, flexi interest, interchange commission and agency income from inbound money transfer was subject to Excise Duty. It adopted the definition of 'interest' under the ITA and held that moratorium and flexi interest were excluded from the EDA. It further held that interchange commissions and agency transfers were not in the circumstances chargeable with Excise Duty.

PARA 7.

The Commissioner being dissatisfied with the aforesaid decision now appeals to this court based on its Memorandum of Appeal dated 24th September 2020. The Commissioner challenges the Tribunal's findings on agency fees and commissions earned on money transfer services. It submits that Tribunal erred in making a finding on the moratorium and flexi interest as these were not subject to the objection and Objection Decision. It complains that the Tribunal erred in accepting the Respondent's position that the bulk of the "Other fees" comprised moratorium and flexi interest without the corresponding financial statements or balance figures which at the objection stage the Respondent had itemized it as other fees. The Commissioner also complained that the Tribunal erred in the applying the definition of interest under the ITA which was meant to be in the context of the ITA and cannot apply in the realm of Excise Duty chargeable under the EDA.

PARA 8.

The Respondent filed its Statement of Facts dated 26th October 2020. Both parties filed written submissions in support of their respective positions.

DIVISION - Analysis and Determination

PARA 9.

I have gone through the appeal, the record before the Tribunal and the parties' extensive and insightful submissions. In resolving this appeal, it is important to recall that the jurisdiction of this court is circumscribed by section 56(2) of the TPA which provides that, "An appeal to the High Court or to the Court of Appeal shall be on a question of law only". An appeal limited to matters of law does not permit the appellate court to substitute the Tribunal's decision with its own conclusions based on its own analysis and appreciation of the facts (see John Munuve Mati v Returning Officer Mwingi North Constituency & 2 others [2018] eKLR). In Mercy Kirito Mutegi v Beatrice Nkatha Nyaga & 2 others NYR CA Civil Appeal Mo. 48 of 2013 [2013] eKLR the Court of Appeal stated that when a court that is limited to dealing with matters of law has a concern regarding the issues that dealt on facts, then the court will also be limited to re-evaluation of the lower court's conclusions and if the conclusions are erroneous in the sense that they are not supported by evidence and the law, the matter becomes a point of law.

PARA 10.

The crux of the parties' dispute and this appeal turns on the interpretation of the *Customs and Excise Act* (Repealed) and the *Excise Duty Act*, 2015 and the extent of the application of the ITA. Since the matter concerns interpretation of tax legislation, I apprehend that the guiding principle is that the language imposing the tax must receive a strict construction leaving no room for intendment or implication (see Cape Brandy Syndicate v I.R. Commissioners [1921] 1KB 64, Mount Kenya Bottlers Ltd & 3 others v Attorney General & 3 others (supra) and Stanbic Bank Kenya Limited v Kenya Revenue Authority CA Civil Appeal No. 77 of 2008 [2009] eKLR). Further, that if there is any ambiguity in the statute, then the same must be resolved in the tax payer's favour. This principle was summarized and restated by the Court of Appeal in Commissioner of Domestic Taxes (Large Taxpayers Officers) v Barclays Bank of Kenya Ltd NRB CA Civil Appeal No. 195 of 2017 [2020] eKLR as follows:

> There is no doubt in our minds that the decisions in Adamson v Attorney General [1933] AC 247, Cape Brandy Syndicate v. Inland Revenue Commissioners [1920] 1 KB 64, T. M. Bell v. Commissioner of Income Tax [1960] EA 224, Republic v. Commissioner of Income Tax ex parte SDV Transami [2005] eKLR and the first judgment represent a correct statement of the law, namely strict construction of tax legislation, so that the tax demand must fall within the terms of the statute without ambiguity. If there's any ambiguity in the legislation, it is not to be rectified by considerations of intendment, but by amending the legislation. However, determination of whether there is clarity or ambiguity in the legislation or whether a tax demand is precise and within the terms of the legislation, is not an abstract or pedantic exercise. It must be based on the evidence and the circumstances of each case. We agree with the majority of this Court in Stanbic Bank Ltd v. Kenya Revenue Authority [2009] eKLR that meaning of words should not be strained so as to find ambiguity.

PARA 11.

Ultimately, this court is to determine whether the Tribunal erred in setting aside the Commissioner's Objection Decision that demanded Excise Duty on the Respondent's financial transactions.

PARA 12.

It is common ground that section 117(1)(d) of the *Customs and Excise Act* (Repealed) provided the basis of charging Excise Duty as follows:

> Subject to provisions of this Act, there shall be charged — (d) in respect to excisable goods and services specified in the second column of the Fifth Schedule, excise duties at the respective rates specified in the Schedule.

PARA 13.

Excise duty on financial services was introduced by the Finance Act, 2012 through amendments to Part III of the Fifth Schedule to the *Customs and Excise Act* (Repealed) as follows under Paragraphs 7 and 8:

SUBPARA 7.

Excise duty on fees charged for money transfer services by cellular phone service providers, banks, money transfer agencies and other financial service providers shall be ten percent

SUBPARA 8.

Excise duty on other fees charged by financial institutions shall be ten percent.

PARA 14.

Subsequently, the Finance Act, 2013 amended the said Part III of the Fifth Schedule to the *Customs and Excise Act* (Repealed) by deleting the words "financial service providers" appearing in Paragraph 7 above and substituting therefor the words "financial institutions". The said Finance Act, 2013 also introduced a new Paragraph 9 as follows:

9. For the purposes of items 7 and 8—

"financial institutions" means—

a. a person licensed under—

(i) the *Banking Act* (Cap. 488);

(ii) the *Insurance Act* (Cap. 487);

(iii) the *Central Bank of Kenya Act* (Cap. 491); or

(iv) the *Microfinance Act*, 2006 (Cap. 493D);

b. a Sacco Society registered under the *Sacco Societies Act*, 2008 (No. 14 of 2008); or

c. the Kenya Post Office Savings Bank established under the *Kenya Post Office Savings Bank Act* (Cap. 493B).

"other fees"

includes any fees, charges or commissions charged by financial institutions, but does not include interest.

PARA 15.

I do not think there can be any doubt that the amendment introduced by the Finance Act, 2013 in respect of what constituted "Other Fees" is more specific and definitive than the amendment introduced by the Finance Act, 2012 which did not specify or define what "Other Fees" was. Since the amendment introducing a more specific definition of "Other Fees" was effected as from 1st January 2014, it follows that the parties' interpretation prior to that date on what constituted "Other Fees" was subjective because the said term was general and bordered on or was out rightly ambiguous. I do not agree with the Commissioner's submission that the reason for the legislature introducing a more specific and definitive term for "Other Fees" was merely "administrative". To the contrary, I find that it was curative and intended to clear the air on what amounted to "Other Fees" and it is no wonder that it specifically excluded interest charged as subject to Excise Duty.

PARA 16.

Indeed, the Commissioner's decision to charge Excise Duty on the Respondent's financial transactions was based on the definition of "Other Fees" but then, I find that it could not rely on this definition in charging Excise Duty for the period prior to when the definition was introduced, that is, the year of income 2013 and on this, I am in agreement with the Tribunal's findings. Since the true meaning and definition of what constituted "Other Fees" was not really clear, the law at the time was ambiguous and could only be interpreted in the Respondent's favour (see National Bank of Kenya Ltd v Commissioner of Domestic Taxes (Income Tax Appeal E155 & 533 of 2020 (Consolidated)) [2022] KEHC 10549 (KLR) (Commercial and Tax) (26 May 2022) (Judgment)]

PARA 17.

It is not in dispute that as from January 2014, the position on what "Other Fees" entailed was now clear. As stated in the Finance Act, 2013, it was "any fees, charges or commissions charged by financial institutions, but does not include interest. The *Excise Duty Act*, 2015 expanded the definition to include "any fees, charges or commissions charged by financial institutions relating to their licensed activities, but does not include interest on loan or return on loan or any share of profit or an insurance premium or premium based or related commissions specified in the *Insurance Act* or regulations made thereunder". The aforementioned definitions are emphatic that Excise Duty is not applicable and chargeable on interest earned by the Respondent.

PARA 18.

The Respondent's position is that the Excise Duty that was being demanded by the Commissioner was in respect of financial transactions that were of "interest in nature and substance" and as such, not subject to Excise Duty. On the other hand, the Commissioner assails the Respondent's interpretation of the term "interest" and contends that the said transactions by the Respondent did not fit within the plain and obvious meaning and definition of the term "interest".

PARA 19.

The *Customs and Excise Act* (Repealed) and the *Excise Duty Act*, 2015 did not define the term "interest". The Respondent submitted that since the term "interest" is defined under section 2 of the ITA, then it follows that the same definition should be applied in this case based on the pari materia principle. On its part, the Commissioner submitted that the pari materia principle does not apply in this case as the ITA deals with a totally different tax head, that is, income tax as opposed to the *Customs and Excise Act* (Repealed) and the *Excise Duty Act*, 2015 that is, Excise Duty.

PARA 20.

Black's Law Dictionary (11th Ed.) defines "in pari materia" as "in the same matter" and "on the same subject". It is a canon of construction that statutes that are in the same matter or subject may be construed together, so that inconsistencies in one statute by may be resolved by looking at another statute on the same subject (see Martin Nyaga Wambora & 3 others v Speaker of the Senate & 6 others NYR CA Civil Appeal No. 21 of 2014 [2014] eKLR).

PARA 21.

While it is tempting to invite the court to borrow the definition of "interest" from the ITA, it should not be lost and I agree with the Respondent's submission that in the construction of tax statutes, the plain and literal meaning of the words used in the statute should be applied first so as to discern the intention of Parliament. The Respondent relied on the Oxford Dictionary of Finance and Banking that defines "interest" as "the charge made for borrowing a sum of money" and Halsbury's Laws of England definition that states that it is "the return or compensation for the use or retention by one person of a sum of money belonging to or owed to

another." I therefore agree with the court's pronouncement in National Bank of Kenya Ltd v Commissioner of Domestic Taxes(supra) which also stated as follows:

> The definition of interest in the *Income Tax Act* should not have been resorted to in ascertaining the intention of Parliament in Section 7 of the Finance Act, 2013. In the *Income Tax Act*, the term interest is used for the purposes of charge, assessment and collection of income tax; for the ascertainment of the income to be charged; for the administrative and general provisions relating thereto and for matters incidental to and connected therewith and not otherwise.

PARA 22.

I therefore reject the Tribunal's decision to apply the definition of "interest" under section 2 of the ITA. A strict interpretation of the Finance Act, 2013 coupled with a plain and literal interpretation of the term "interest" meant that all fees incidental to obtaining a loan such as moratorium, loan appraisals and applications, loan negotiations, mortgage commitment, micro-enterprise among others would be subjected to Excise Duty while the interest earned from the loan would be exempted.

PARA 23.

I note that this categorization of the fees charged by the Respondent was expressly provided for by the Respondent at Page 9 of its objection dated 5th December 2016, therefore I do not agree with the Commissioner that these were only introduced at the appellate stage before the Tribunal. In its Objection Decision, the Commissioner stated as follows:

> It is our considered opinion that "Other fees and Commission" income as reported in the financial statements and the relevant ledgers are not of interest in nature since they are a slice of the whole amount and not based on any rate of interest. Further, all income earned during the loan processing stage are commissions and not interest. We note that interest can only accrue after the loan has been granted...

PARA 24.

In any event, I find that the Commissioner was right to state that the said fees are not of interest in nature but commissions and that interest can only accrue after the loan has been granted. The Commissioner was therefore entitled to bring these fees to charge for Excise Duty after the introduction of the Finance Act, 2013, and in this case, from 18th June 2013.

PARA 25.

Turning to the other fees earned by the Respondent in respect of money transfer services by Moneygram/ Western Union and inter-bank ATM transactions, I am in agreement with the Commissioner that the same were neither raised by the Respondent in its objection nor in its memorandum of appeal before the Tribunal, thus, the Tribunal ought not to have made a determination on it. This is in line with section 3 of the Tax Appeals Tribunals Act which provides that the Tribunal can only deal with appeals filed against a tax decision made by the Commissioner. Since the Commissioner never made any decision on the said money transfer services and inter-bank ATM transactions, there was no tax decision capable of being heard and determined by the Tribunal on the same.

DIVISION - Conclusion and Disposition

PARA 26.

For the reasons I have set out, I allow the appeal. The Commissioner's Objection Decision on its assessment of the Respondent's Excise Duty liability on the said fees earned after 18th June 2013 is upheld. Consequently, the part of the Tribunal's judgment holding that the fees charged by the Respondent that are ancillary to the

loans it grants to its customers are in the ambit of interest and therefore exempt from Excise Duty be and is hereby set aside.

PARA 27.

There shall be no order as to costs.

DATED AND DELIVERED AT NAIROBI THIS 30TH DAY OF NOVEMBER 2022.

D. S. MAJANJA

.....

JUDGE

I certify that is this is a true copy of the original

Signed

DEPUTY REGISTRAR

Court Assistant: Mr M. Onyango.

Ms Wambui Ng'ang'a instructed by Kenya Revenue Authority for the Appellant.

Ms Milly Jalenga instructed by Iseme, Kamau and Maema Advocates for the Respondent.