



REPUBLIC OF KENYA
IN THE HIGH COURT OF KENYA AT NAIROBI
MILIMANI LAW COURT
CONSTITUTIONAL AND HUMAN RIGHTS DIVISION
PETITION NO. 476 OF 2013

BETWEEN

TATA CHEMICALS MAGADI LIMITED PETITIONER

AND

**THE COMMISSIONER OF DOMESTIC TAXES (LARGE TAXPAYERS)
RESPONDENT**

JUDGMENT

Introduction

1. The issue for consideration in this matter is whether the respondent has met its constitutional obligation to process and pay the petitioner Value Added Tax (VAT) refunds.
2. The petitioner is a limited liability company engaged in the business of manufacturing Soda Ash and salt in Kenya. The respondent is an office established under the Kenya Revenue Authority (“KRA”) and is mandated to administer Value Added Tax (“VAT”) and Income Tax in accordance with the applicable statutes under the general control and direction of KRA.
3. The petitioner exports approximately 90% of its soda ash and as a result it is in a perpetual credit position as a result of supplying zero rated goods. This entitles the petitioner to VAT refunds.

The Petitioner’s Case

4. The petitioner’s case is set out in the petition dated 1st October 2013, the supporting and further affidavit of Jackson Muchira Mbui, its Managing Director, sworn on 1st October 2013 and 25th February 2014 respectively. The petitioner seeks the following reliefs in the petition;
 - a. *This Honourable Court be pleased to declare that the respondent’s decision of 3rd September 2013 is arbitrary, illegal and is a violation of the petitioner rights under Article 47(1) of the Constitution 2010.*
 - b. *The Honourable Court be pleased to issue an order quashing the respondent’s decision of 3rd September 2013 setting off the sum of Kshs 235 million.*
 - c. *This honourable Court be pleased to declare that the respondent’s refusal to refund the sum of*

- Kshs 742,815,181/= is a violation of the petitioner's rights under Article 47(1) of the Constitution.
- d. This Honourable Court be pleased to issue an order of mandamus to compel the respondent to pay the VAT refund amounting of Kshs 742,815,181/- to the petitioner forthwith.
 - e. The respondent pays the petitioner interest on the sum of Kshs 742,815,181/= at the petitioner bank's current prevailing commercial lending rate.
 - f. The respondent be restrained from withholding the petitioner future VAT refund claims which have no connection whatsoever to the period of assessment.
 - g. Costs of this petition.
 - h. Such other orders as this Honourable Court shall deem just
5. This is not the first case in which the petitioner has sought to recover VAT refunds. It filed the **Nairobi Petition Number 140 of 2013** in Kshs 449,885,610/= on account of VAT refunds due from November 2009. Following the case, the respondent paid Kshs 461,586,405/=. In that period the respondent conducted an audit and as a result issued assessments for the period January 2007 to September 2012 by its letter dated 1st February 2013. The petitioner objected to the assessment by its letter dated 26th February 2013.
 6. The petitioner avers that the respondent did not deal with its objection but instead informed the petitioner in an email dated 3rd September 2013 that Kshs 235 million would be set off against refunds due to it. The petitioner's advocates issued demand letters dated 13th and 23rd September 2013 querying the unlawful set off but no response was forthcoming from the respondent. The petitioner seeks to quash the decision to set off the Kshs 235 million on the ground that the set off is unlawful and a violation of its right to fair administrative action under **Article 47** of the Constitution.
 7. The petitioner contends that the respondent has failed to make payment of VAT refunds totalling to Kshs 742,815,182/=. It is apprehensive that future VAT refunds will not be settled as well. The petitioner complains the failure by the respondent to pay VAT refunds has placed it in a precarious financial situation that has jeopardised its export market position and has had a negative impact on its customer base. In order to avert a financial crisis the petitioner avers that it has been driven to obtain expensive overdrafts. It further complains that if the VAT refunds are not forthcoming it may be forced to scale down its operations and ultimately close shop.
 8. The petitioner submits that a taxpayer claiming a VAT refund is entitled to receive it and the failure to process it timeously is a violation of its right to fair administrative action protected under **Article 47** of the Constitution. The petitioner cites **Republic v Kenya Revenue Authority ex-parte L.A.B International Kenya Ltd Mombasa HC Misc. No. 82 of 2010 [2011]eKLR** and **Kenya Data Networks v Kenya Revenue Authority Nairobi Petition No. 87 of 2012 [2013]eKLR** to buttress its argument that it is unfair, unreasonable and unjust for the petitioner to be forced to file a petition in order to compel the respondent to pay VAT refunds.

The Respondent's Case

9. The respondent opposes the petition based on the affidavits of George Obel, a Senior Assistant Commissioner, and the Margaret Masaku, Acting Chief Manager, sworn on 2nd December 2013 and 24th February 2014 respectively.
10. The respondent confirms that the petitioner was subjected to a VAT audit and the findings communicated by the letter dated 1st February 2013. The findings, which included assessments, were that out of the Kshs 1,147,601,158/= claimed, Kshs. 697,715,548/= would be disallowed sum and Kshs 449,885,610/= would be refunded. The respondent informed the petitioner that an issue had been raised by their Investigations and Enforcement Department over Kshs 234,968,183/=.
11. Thereafter the Commissioner, Investigation and Enforcement wrote the letter dated 16th April 2012 which demanded that the Kshs 234,968,183/= be paid within 30 days. The Commissioner

- claimed that the sum was due to under declaration and fraudulent clearance of goods. Mr Obel depones that the petitioner applied to review the demand by its letter dated 15th May 2012. He further depones that the parties held several meetings which culminated in an agreement that the respondent could withhold Kshs 235 million in escrow pending conclusive and expeditious resolution of the unresolved tax demand. The respondent avers that the petitioner's Managing Director affirmed the agreement by the letter dated 12th October 2012 addressed to the Commissioner General.
12. Mr Obel avers that as a result of the agreement, it included the Kshs. 235 Million as part of the tax refund disallowed pending the determination of the dispute. He states that the respondent was mindful of the petitioner's position hence it withheld the amount in five tranches between March 2013 and August 2013.
13. In regard to the petitioner's objection to the assessment, the respondent avers that there were further negotiations between the parties and by a letter dated 30th October 2013, the respondent communicated the decision on the petitioner's objection.
14. The respondent maintains that it has not refused to pay the refunds due to the petitioner. It complains that though the petitioner filed *Petition 140 of 2013* without prior notice, it did not contest the petition and has settled it by paying Kshs 461,586,405/= in four instalments, the last of which was paid in July 2013. The respondent states that it is faced with a huge VAT refund portfolio which stood at Kshs 20,703,469,906.43 as at September 2013 and that it only receives a paltry sum of Kshs 645,600,000/= per month from the Treasury. As this sum is inadequate to settle all refunds as and when they become due, it has devised a workable formula of paying out refunds on a first in first out basis. The respondent avers that the petitioner's VAT refund claim was delayed in processing due to outstanding audit issues and as such the position that they have been withholding payment to the petitioners is untrue.
15. Ms Margaret Masaku depones that from 2009 to date the respondent has processed and paid the petitioner Kshs 1,353,653,663/= through direct payments and setoffs against taxes owed by the petitioner. She avers that refund can only be made once the claim is authenticated and approved and subject to the availability of funds from the National Treasury. She also states that huge VAT refund claims are not paid at once but are spread over 2 or 3 months to enable the respondent pay other claimants.
16. Ms Masaku deposes that the approved refund claims for the petitioner for the period between June 2011 and May 2013 totalled Kshs 148,001,485/= which the respondent proposes to refund over five monthly instalments of Kshs 29,600,297/= each. She adds that during December – January 2013 period, the respondent has refunded a total of Kshs 180,015,248/= in three instalments. She avers that once the petitioners provide the outstanding documentation requested, then the respondent will process the pending claims and an affordable payment proposal communicated to them.

Determination

17. The facts and arguments outlined above call for determination of two issues in light of **Article 47** of the Constitution;
- a. Whether the respondent is entitled to set off the sum of Kshs 235 million from the petitioner's refunds.
 - b. Whether the failure to pay the petitioner's VAT tax refunds is a violation of the petitioner's rights.
18. This is not the first case our Courts have dealt with the obligation of KRA to process refunds in the context of **Article 47** of the Constitution which provides, in part, that;

47. (1) Every person has the right to administrative action that is expeditious, efficient, lawful, reasonable and procedurally fair.

(2) If a right or fundamental freedom of a person has been or is likely to be adversely affected by administrative action, the person has the right to be given written reasons for the action.

19. The purpose of **Article 47** is to uplift the standards of administrative action by providing constitutional standards (see ***Dry Associates Limited v Capital Markets Authority and Another Nairobi Petition No. 328 of 2011 [2012]eKLR***). The national values and principles of governance articulated in **Article 10** among them good governance, integrity, transparency and accountability must be infused in administrative action. In regard to processing of VAT refund claims, Ojwang' J., (as he then was) in the case of ***Republic v Kenya Revenue Authority ex-parte L.A.B International Kenya Limited (Supra)*** observed that, *"In practical terms, Government has a public duty to effect change to any unprogressive arrangements, such as those that may characterize the operational linkage of the respondent to slothful structures, so as to render the respondent, as well as such structures, capable of responding to the overriding demands of the Constitution; and in this regard, ordinary statutory arrangements cannot qualify the constitutional provisions. On this account, the respondent has no justification for failing to make VAT refunds timeously."*
20. The need for efficiency in processing VAT refunds was also articulated by Mumbi Ngugi J., in ***Kenya Data Networks Limited v Kenya Revenue Authority (Supra)*** where she stated that, *"The respondent had a duty to act on the petitioner's VAT refunds timeously. While recognising that it is mandated by statute to collect taxes, and while appreciating the pivotal role that collection of taxes plays in a country's economic development and provision of services for citizens, KRA must also be always cognizant of the possible ramifications of its actions or omissions in dealing with taxpayers, and the impact on investment, revenue collection and the general welfare of the country. While there is no statutory period within which KRA ought to make good tax refund claims, it cannot have any basis for failing to process tax refund claims several months, and in some cases several years after they were made. It is no answer to the petitioner's claim for tax refund for the respondent to demand in turn that the petitioner pays arrears of tax."* With this brief background in mind I now turn to consider the issues raised for determination.

Whether the respondent is entitled to set-off the Kshs 235 million

21. The issue of the sum of Kshs 235 million withheld is intimately connected with the pending objection. The letter of assessment from the respondent dated 1st February 2013 indicated that amount of unpaid taxes amounted to Kshs 234,968,183/=. The Commissioner, Investigation and Enforcement in the letter dated 16th April 2012 indicated that the amount was due in 30 days causing the petitioner to file a review of the decision by its letter dated 15th May 2012. While the parties agreed to hold the amount of Kshs 235 million in escrow as evidenced by the letter dated 12th October 2012, the respondent issued an amended assessment in accordance with **section 32A of the VAT Act (Repealed)**. However in respect of the disputed sum, the respondent noted as follows, *"For taxes amounting to Kshs. 234,968,183 raised by our Investigations and Enforcement Department (IED) - will address this issue directly under a separate cover."*
22. In light of the correspondence, I find that while there was an agreement to hold the sum of Kshs 235 million in escrow, the agreement was superseded by the letter dated 30th October 2013, in which the respondent addressed the objection and amended the assessment. The issue of the Kshs 234,968,183 remains unaddressed particularly in view of the fact that the petitioner had lodged an appeal against the decision by its letter of 15th May 2012.
23. It follows therefore that the email dated 3rd September 2013 stating that the sum Kshs. 235 million would be used to set-off claims is a clear violation of the petitioner's right to fair administrative action for several reasons. First, the agreement between the parties was that the amount of Kshs 235 million was to be held in escrow. The parties did not intend the amount to be set off against any other tax liabilities unless of course, a specific decision was made in that regard as an answer

to the objection lodged. The email is also objectionable because the respondent did not furnish any reasons why it had unilaterally decided to effect a set-off. Second, the sum was subject to a pending appeal that had been lodged contesting the findings contained in the demand letter of 16th April 2012 from the Commissioner, Investigation and Enforcement. The appeal remained unanswered in the respondent's letter of 30th October 2013 that revised the assessments. It is not disputed that the appeal/objection raised by the petitioner to the Commissioner's decision has been pending since April 2012, it must now be determined to enable the petitioner pursue any other legal remedies available to it.

24. I therefore find and hold that the purported set-off of Kshs 235 million is without legal basis and as such the decision contained in the email dated 3rd September 2013 is quashed. As no decision has been made in respect of the Kshs 234,968,183, the respondent is now directed to deal with the objection/appeal.

Outstanding VAT Refunds

25. The petitioner seeks an order directing the respondent to settle VAT refunds amounting to Kshs 742,815,181/=.

26. The duty imposed on the respondent to process and pay VAT refunds is, for purposes of this petition, to be found in the applicable **Value Added Tax Act (Repealed)**. The petitioner exports to foreign markets hence its business falls under the **Fifth Schedule** to the **Act**. The export of its goods is zero rated hence the petitioner charges 0% VAT on the goods its supplies. Under **section 11(2)** of the **Act**, it is provided that where, by reason of making zero rated supplies, there is no output tax to accord the supplier a set-off, the Commissioner shall refund to the affected supplier the input tax incurred by such a supplier. A supplier, like the petitioner, who incurs input tax is entitled to excess input tax under **section 11(2)(a)** of the **Act**. This, as I stated earlier, is why the petitioner is continuously in a credit position.

27. In *Ericsson Kenya Limited v Attorney General and Others Nairobi Petition No. 506 of 2013*[2013]eKLR, the Court considered the responsibility of the Commissioner under the **Act** in light of the Constitution, “[49] *Whether the respondents acted in accordance with Article 47 of the Constitution is a question of fact which calls for an examination of the circumstances under which the petitioner's refund claims were dealt with. The Court is not concerned with whether the petitioner is entitled to the amount but whether the process afforded was one that complied with the dictates of Article 47 of the Constitution. In considering the circumstances, it is important to recall that the fact that a taxpayer has lodged a refund claim in accordance with the VAT Act and regulations does not discharge the respondents from the responsibility of examining the claim and confirming that it meets the requirements of the law. The Commissioner, when processing the claim, is not merely a conveyor belt performing a perfunctory exercise. He is required to examine and verify the claim and where irregularities, fraud or other deficiencies are discovered draw the petitioner's attention to them. The Commissioner is also entitled to call for further information, if necessary, to satisfy himself that the claim meets the legal threshold for payment. Ultimately, the Commissioner is entitled to reject a VAT refund claim by giving written reasons which would entitle the taxpayer to appeal or challenge the decision.*” In my view, as long as the claim is lodged within the time limited and proper documentation is submitted and the claim is verified, the respondent has a duty to pay the claim. As Ojwang' observed in *Republic v Kenya Revenue Authority ex-parte L.A.B International Kenya Limited (Supra)*, the respondent cannot interpose that responsibility with reasons outside the provisions of the **Act** such as arrangements with other Government departments.

28. The petitioner argues that it is unfair, unreasonable and unjust for it to be forced to file a petition so that the respondent can pay their VAT refunds. The respondent has urged the court to take cognizance of the fact that the payments of VAT refund claims are effected subject to the availability of funds from the National Treasury. It further urges that any claims made have to

undergo authentication and approval before they are settled.

29. Out of the amount of Kshs 742,815,181/=, the petitioner has only received the sum of Kshs 180,015,248/= in instalments between December 2013 and February 2014. The respondent has confirmed that it is willing to pay the sum of Kshs 148,001,484/= in five monthly instalments of Kshs 29,600,297/=. The petitioner is rightly concerned that at the rate of payment, the outstanding amount will balloon to an estimated Kshs 1.7 billion at the end of next year taking into account an accrual rate of Kshs 54 million per month.

30. I am alive to the realities that have been laid bare by these proceedings. The cases I have cited clearly show that the process of processing and payment of VAT refunds is not serving the business community well. The Court cannot step into and prescribe the manner in which the respondent and by extension by the Exchequer should run its affairs. What the Court is concerned about is that legal rights protected by the Constitution are enforced and legal obligations are fulfilled. The taxpayer who carries on his business in accordance with the law and applies for a refund is entitled to the refund as a matter of right. The process of verification and processing the claim must, in the words of **Article 47(1)** of the Constitution, be efficient and expeditious.

28. Out of the total amount claimed, the respondent has not stated the position of Kshs 414,898,448/= outstanding being the amount of Kshs 742,815,181/= claimed in the petition less the Kshs 180,015,248/= already paid and Kshs 148,001,485/= proposed to be paid in instalments. The sum of Kshs 414,898,448 should be processed and paid expeditiously. I once again echo the words of Ojwang' J., in **Republic v Kenya Revenue Authority ex-parte L.A.B International Kenya Limited (Supra)** that, *"Given the safeguards in the Constitution, which clearly apply to the applicant herein, the Court does not accept the respondent's plea that it subject to certain structural inefficiencies which are traceable to other organs of Government, or to the provisions of ordinary statute law."*

Disposition

29. Under **Article 23** of the Constitution, the Court has broad discretion in granting appropriate relief to vindicate the right of the party aggrieved. The petitioner has also prayed for interest on the outstanding VAT refund at prevailing commercial rates. In **Ericsson Kenya Limited v Attorney General and Others (Supra)**, I held that **VAT Act** does not make provision for payment of interest and such a provision was not unconstitutional. I therefore decline the prayer for interest.

30. In light of the foregoing, I now grant the following orders;

- a. **I declare that the respondent's decision contained in the email dated 3rd September 2013 purporting to set-off the sum of Kshs. 235 million from the petitioner's VAT refunds is a violation of the petitioner's right under Article 47 of the Constitution and is consequently quashed.**
- b. **An order of mandamus be and is hereby issued directing the respondent to determine the appeal/objection relating to the sum of Kshs 234,968,183/= in any event within the next twenty one (21) days from the date hereof.**
- c. **An order of mandamus be and hereby directed to the respondent compelling it to expeditiously and in any case within a period of not more than ninety (90) days from the date of this judgment to consider, process and pay out in accordance with the law, part of the petitioner's VAT refund outstanding from the total of Kshs 742,815,181/= claimed.**
- d. **The respondent shall pay the costs of the petition.**

DATED and DELIVERED at NAIROBI this 14th April 2014.

D.S. MAJANJA

JUDGE

Ms Malik instructed by Kaplan and Stratton Advocates for the petitioner.

Mr Matuku, Advocate, instructed by the Kenya Revenue Authority for the respondent.