



REPUBLIC OF KENYA

High Court at Nairobi (Nairobi Law Courts)

Petition 352 of 2012

GEOTHERMAL DEVELOPMENT COMPANY  
LIMITED.....PETITIONER

AND

ATTORNEY GENERAL.....1<sup>ST</sup> RESPONDENT

KENYA REVENUE AUTHORITY.....2<sup>ND</sup> RESPONDENT

THE COMMISSIONER GENERAL KENYA REVENUE AUTHORITY.....3<sup>RD</sup>  
RESPONDENT

THE COMMISSIONER OF DOMESTIC TAXES LARGE TAX PAYERS OFFICE.....4<sup>TH</sup>  
RESPONDENT

JUDGMENT

Introduction and background

1. Although the petitioner has filed voluminous documents for consideration by the Court, the issue for determination having a bearing on the bill of rights is relatively straightforward. It concerns the nature of a notice issued pursuant to statute and whether the notice complies with the standard of due process contained in Article 47(1) of the Constitution which entitles every person to, “*administrative action that is expeditious, efficient, lawful, reasonable and procedurally fair.*”
2. The petitioner (“the Company”) is a limited liability company incorporated under the *Companies Act (Chapter 486 of the Laws of Kenya)*. It is also a State corporation with its principal object as its name suggests, being to develop and promote rapid growth of geothermal resources in Kenya.
3. In this judgment I shall refer to the 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respondents as the respondent and collectively as the Kenya Revenue Authority (“KRA”). KRA is incorporated under the provisions of **section 3** of the *Kenya Revenue Authority Act (Chapter 469 of the Laws of Kenya)* and is responsible for the collection of taxes in the country. The Commissioners, who are sued as the 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respondents, are officers of KRA and act on its behalf pursuant to the various statutes governing various taxes. The 1<sup>st</sup> respondent, the Attorney General, did not participate in these proceedings.
4. As part of its work, the company entered into a contract with Great Wall Drilling Company Ltd to provide drilling services for ten geothermal wells in Olkaria area. The total value of the contract was USD 39,615,890.88. The petitioner states that it paid substantial Value Added Tax (VAT) payments on this contract.
5. An Audit was carried out between the months of April and May, 2011, whereupon the KRA demanded VAT, withholding tax and Pay As You Earn (PAYE) under the *Valued Added Tax Act (Chapter 476 of the Laws of Kenya)* and the *Income Tax Act (Chapter 470 of the Laws of Kenya)*. The tax demand and subsequent enforcement is what precipitated these proceedings as the respondent issued Agency Notices on 8<sup>th</sup> August 2012 to the Company’s bankers which had the effect of freezing its accounts.

6. This case is not concerned with the constitutionality of the tax collection and administration statutes. For purposes of the present matter, the Company does not contest the results of audit nor require the court to address itself to the manner in which the audit was carried out. It's case is hinged on the question of due process in the enforcement of what was found due as revenue as a result of the audit. Consequently, I shall limit my find to the matters in issue.

### **The Tax Demand**

7. After the audit was completed, the petitioner's managing director received from the 4<sup>th</sup> respondent a letter dated 20<sup>th</sup> June 2011 ("the Tax Demand"). Attached to the letter were various schedules showing how the amounts demanded were arrived at. The Tax Demand read as follows;

The Managing Director

Geothermal Development Company

P O Box 100746-00101,

### **NAIROBI**

20<sup>th</sup> June 2011

Dear Sirs,

### **RE: TAX DEMAND**

Following the Audit undertaken covering the year 2009/2010 and 2010/2011, we would like to report that additional tax arrears were established on account of Reverse VAT, Withholding Tax and PAYE.

#### **A. Reverse VAT**

It was noted that your company made payments for services rendered by a non resident person, Great Wall Drilling Company. However, it did not subject the cost of the imported services to reverse VAT. The services it received were on account of drilling of wells and agency on handling of cement.

The amount of tax on handling services were Kshs.1,166,582 and that from drilling was Kshs. 600,034,134 inclusive of interests.

Additionally, it was found that your company has not been filing monthly VAT 3 returns since it was registered in July 2010. In that regard, it has suffered a penalty of Kshs.10,000 per month to the month of May 2010 amounting to Kshs.110,000.

Hence the total amount outstanding on VAT is Kshs.601,311,727. The attached schedule 1 contains the details.

#### **B. Withholding Tax**

Just like reverse VAT, withholding tax was not subjected to handling and some drilling fees paid to Great Wall Drilling company. Details of the same are attached in schedule 2. The amount of tax arising on above amounted to Kshs.25,002.482.

Besides there were other suppliers of contractual, consultancy and training services paid but we found no evidence of withholding tax deducted and remitted to the Commissioner. The amount of tax on the same was Kshs.7, 340,651. Schedule 3 proves the analysis of the same.

Therefore the total withholding tax payable is Kshs.32,343,134.

### C. PAYE

In the months of July and August 2009, two directors were paid their salaries net of tax. Hence, we have rectified that anomaly by computing their taxes appropriately amounting to Kshs.1,730,357 inclusive of penalties and interests as per Schedule 2 attached.

#### Summary of the taxes.

1. Reverse VAT	601,311,727
2. Withholding tax	32,343,134
3. PAYE	1,730,357

**Total Tax Due 635,385,218**

You are requested to pay up above taxes immediately through RTGS to avoid further interests accruing.

BANK	TAX TYPE(S)	ACCOUNT NAME	ACCOUNT NUMBER
Central Bank of Kenya	Corporation Tax Withholding Tax, Income Tax	Income Tax Main Collection Account	*****
Central Bank of Kenya	VAT	VAT main collection Account	*****
Central Bank of Kenya	PAYE	Income Tax PAYE Account	*****

Therefore ensure that you promptly file your VAT 3 Returns on or before 20<sup>th</sup> of the subsequent month following the end of the month in question.

For any further clarification please contact the undersigned or Mr Cheruiyot on telephone number 2815032 or 2815034 respectively.

Yours faithfully,

**M. Oray**

**For: Commissioner of Domestic Taxes**

#### Large Taxpayers Office

#### The Petitioner's Case

8. The petitioner's case is that the Tax Demand does not satisfy the requirement of a proper notice consistent with **Article 47(1)**. It contends that after the tax audit it was not issued with a VAT assessment in accordance with the provisions of **Paragraph 9** of the **Seventh Schedule** to the **VAT Act** to enable it exercise its right under **Section 32A** of the **VAT Act** to move the VAT Tribunal to contest the assessment.

9. Mr Wekesa, counsel for the petitioner, submitted that the Tax Demand was merely a letter that did not draw the Company's attention to the fact that it was an assessment and the consequences of non-compliance. Counsel maintains that by failing to do so, the Company was effectively denied the right to

lodge an objection to the VAT Tribunal to challenge the assessment.

10. Counsel also pointed to the fact that after the petition was filed, the respondent issued a Notice of Assessment dated 16<sup>th</sup> August 2012 (“Notice of Assessment”) which stated as follows;

**KENYA REVENUE AUTHORITY**

**VALUE ADDED TAX**

**NOTICE OF ASSESSMENT**

**TO: GEOTHERMAL DEVELOPMENT COMPANY LIMITED**

**VAT DISTRICT OFFICE      NAIROBI WEST**

**P.O. Box 310112 null**

**VAT NO \*\*\*\*\***

**ASSESSMENT NO. \*\*\*\*\***

**PIN      \*\*\*\*\***

**DATE OF ASSESSMENT:    24/06/2011**

**PERIOD OF ASSESSMENT 201002-201105**

**AMOUNT (KSHS):                    589,677,993.00**

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The examination of your books and records for the period specified above has shown that the correct amount of Value Added Tax (VAT) was not declared or assessed as tabulated on the tax schedule attached to this letter.

Consequently, the Commissioner of Value Added Tax, has made the assessment of tax tabulated on the schedule, by using powers granted by paragraph 9 of the Seventh schedule of the Value Added Tax Act, Cap 476. A detailed explanation of the reasons for this assessment and the associated calculations are given in the schedule which form part of this notice of assessment. The total amount of tax payable as shown should be paid IMMEDIATELY to avoid enforcement action being taken against you.

While making payments, please quote the above Assessment number. If you wish to object to this assessment, you may do so by giving precise grounds of objection and stating the amount of tax you are objecting to.

However the commissioner will only consider your objection and review your assessment if the objection, accompanied by new evidence is submitted within 30 days from the date of this letter.

If you object. and the assessment is thereafter reviewed and it is not amended in accordance with your objection for reasons that part or the whole of your objection lack valid grounds, the objected tax shall remain payable on the date it was payable and it shall attract further additional tax until it is paid in full.

**(SIGNED)**

**For: COMMISSIONER OF VALUE ADDED TAX**

**DATE 16<sup>TH</sup> AUGUST 2012**

**VAT57 (LETTER)**

11. According to Mr Wekesa, the Notice of Assessment was the proper notice and therefore the Company's agent, Pricewaterhouse Coopers filed a Notice of Objection to Assessment which is now pending determination. Counsel submitted that no notice has been issued in respect of the Income Tax element of the Tax Demand.

12. It is the petitioner's case that it was denied the right to fair administrative action when the respondent sought to enforce the tax due through issuance of agency notices against it on the 6<sup>th</sup> August 2012 and thereafter issuing a standard 'proper' Notice of Assessment dated 16<sup>th</sup> August 2012. The Company also contends that it was unreasonable to proceed to enforce taxes demanded in the earlier notice and then issue the Notice of Assessment requiring the Company to pay taxes and lodge its objection thereafter. The Company's position is that the Tax Demand could not amount to a notice of assessment envisaged by **Paragraph 9** of the **Seventh Schedule** of the **VAT Act**.

13. In the written submissions, the petitioner demonstrated various inconsistencies between the Tax Demand and the Notice of Assessment to support the proposition that the former could not have been a notice of assessment envisaged by the law. Counsel pointed out, for instance, that the letter of 20<sup>th</sup> June 2011 declares itself to be "*a report that additional tax arrears were established on account of Reverse VAT, Withholding Tax and PAYE.*" That there is nothing in the Tax Demand to disclose that it was meant or intended to serve as a Notice of Assessment and does not even give the date of assessment or the consequences of failure to comply with it. The petitioner further points to discrepancies in the amounts displayed in Tax Demand and the amount on the Notice of Assessment.

14. The Company contends that its right of fair administrative action was infringed by KRA by the initial failure to issue proper notices which would trigger the crystallization of the right to object to the assessment. The Company's case is that proper notices should be issued to it to enable it take advantage of statutory procedures. By failing to issue proper notices, the Company submits that it was denied the right to fair administrative action protected under **Article 47(1)**.

### **Respondents' Case**

15. KRA opposes the petition on the ground that proper notice was issued before taking enforcement action. In the replying affidavit of 27<sup>th</sup> September 2012 sworn by Mr. Maurice Oray, a Senior Assistant Commissioner, he avers that the Tax Demand served as an assessment of the outstanding Value Added Tax, withholding tax and PAYE tax found due after the audit. He states that it was not mandatory that the VAT assessments be raised using Notice of Assessment, which it termed as VAT 57 form, as it is not a statutory form and further, that withholding tax and PAYE tax lacked specific assessment forms under the **Income Tax Act**.

16. Ms Odundo, counsel for the respondent, contended that there was no requirement in law that the notice take a particular form and that the Tax Demand was in substance a demand for taxes. Furthermore, Counsel submitted that the Company did comply with the demand by making payment and it is only after a year that the issue of assessment arose. It is also the respondent's case that the timelines for lodging of objections under **section 32A** of the **VAT Act** were not observed and thus the objection lodged by the Company's agent was time barred under the provisions of **section 32A** of the **VAT Act**.

17. As regards the Notice of Assessment, the respondent avers that the "Notice of Assessment" is an administrative form which is computer generated and is not prescribed by legislation under the *Value Added Tax Act*. It is deponed that the form was not issued to the Company at the material time as it is computer generated and the KRA's computer systems were not working. Furthermore, by the time the Notice of Assessment was issued the Company had already entered into an arrangement to pay the taxes demanded after the audit.

18. It is the respondent's position that enforcement of the notice through issuance of the agency notices was proper in the circumstances and the petition must be dismissed. Counsel relied on several cases to support its case including ***Pili Management Consultants Limited v Commissioner of Income Tax and Kenya Revenue Authority CA Mombasa Civil Appeal No. 154 of 2007 (Unreported)*** and ***Uganda***

**Analysis and determination**

19. I have considered the pleadings, depositions and submissions by the parties and as I stated earlier in this judgment the only issue for determination is whether the Tax Demand and the context in which it was issued to the Company is consistent with the provisions of **Article 47(1)**.

20. **Article 47** enshrines the right of every person to fair administrative action. **Article 232** enunciates various values and principles of public service including “(c) responsive, prompt, effective, impartial and equitable provision of services” and “(f) transparency and provision to the public of timely, accurate information.”

21. In the case of **Dry Associates Ltd v Capital Markets Authority and Another, Petition No. 328 of 2011 (Unreported)**, I noted that, “Article 47 is intended to subject administrative processes to constitutional discipline hence relief for administrative grievances is no longer left to the realm of common law ... but is to be measured against the standards established by the Constitution.” In the case of **Republic v Kenya Revenue Authority ex parte Lab International Kenya Limited, Mombasa High Court, Misc. Civil Application No. 82 of 2010[2011]eKLR** the Court observed that, “The Common law in its evolution has defined the rules of conduct for a public authority taking a public decision, entrusting the overall control-jurisdiction in the hands of the Courts of law; but for Kenya a general competence of the Courts is now no longer confined to the terms of Statute law and subsidiary legislation, but has a fresh underwriting in the Constitution of Kenya, 2010, Article 47 which imposes a duty of fair administrative action and Article 10(2)(c) demands, “good governance, integrity, transparency and accountability.”

22. **Article 10** also requires that certain values and principles of governance be infused into the decision making process of any state organ. Such values as are relevant to these proceedings include good governance, integrity, transparency and accountability. **Article 48** also requires that the state, in its all manifestations, ensures access to justice of all persons. It is against this background of these provisions that I shall consider the petitioner’s case and whether the Tax Demand is a proper notice.

23. The respondent attributes the failure to send the ‘computerised’ Notice of Assessment to a computer malfunction. This may well be true, but it still does not answer the question as to whether or not the impugned notice was proper notice. In my view, the issue is not whether or not the notice was computer-generated, for it might as well have been hand written, the question is to be determined from the substance of the Tax Demand in whatever form; manual or electronic. A reading of the Tax Demand, shows that it communicates the results of the audit by setting out the amount of VAT, Withholding Tax and PAYE found due and requesting the Company to pay. The letter concludes by requesting the Company to contact the writer of the letter for any clarifications.

24. **Paragraph 9** of the **Seventh Schedule** to the **VAT Act** providing for issuance by Commissioner of Notice of Assessment notices does not provide for a specific or mandatory form of notice. However, that in itself does not exonerate KRA from meeting the constitutional standards set out in **Article 47(1)**. Gone are the days when sole reliance on statutory provisions would suffice. Now we have a higher law that dictates and requires higher standards of governance and that compute with the values of the Constitution. All statutory provisions in force must be read under the beam of the rich values and principles enshrined under the Constitution.

25. The issue of a notice is a key component of due process. In **Kenya Anti-corruption Commission v Lands Limited and Others Nairobi Misc. App. 583 of 2006** the court noted, “Constitutional provisions are procedural safeguards aimed at ensuring due process before any right to property can be taken away and also incorporating the right of hearing. The right of hearing are of fundamental importance to our system of justice and even when they are not expressed specifically in any law the supreme position of the Constitution must be implied in every Act especially, the right to due process and it cannot be taken away. Constitutional rights cannot be taken away without due process. [Emphasis mine]

26. From the material before the court, PricewaterhouseCoopers, the Company's tax agent by a letter dated 31<sup>st</sup> July 2012 wrote to KRA requesting to be served with copies of VAT Notice of Assessment. No response was forthcoming but instead it sent an email dated 8<sup>th</sup> August 2012 with copies of Agency Notices dated 6<sup>th</sup> August 2012 to Co-operative Bank of Kenya, the Company's bankers, and the Company's Managing Director. After the Agency notices were issued, the Notice of Assessment in respect of the VAT was then duly issued. This notice to the Company informed it that it could lodge an objection against the assessment within 30 days from the date of the letter.

27. Counsel for KRA argued that the Company had in fact accepted the Tax Demand and made partial settlement only to raise the issue of objecting to the assessment almost a year later. In fact when, the issue was raised by the Company's agent, the respondent replied, in a letter dated 16<sup>th</sup> July 2012, that, "*the issue of assessment was finalized when your client failed to exercise its rights under section 32A of the VAT Act and negotiated to liquidate the tax arrears in three equal instalments which the Commissioner accepted therefore there is no legal basis under the Act to review your clients matter.*" This may well be the position but it is difficult to understand why KRA then issued a Notice of Assessment a year later if it did not consider the Tax Demand such a notice of assessment. Coupled with the fact that the Notice of Assessment was sent after enforcement proceedings had commenced points to unreasonable administrative action. I would further hold that a party dealing with KRA had a legitimate expectation to be served with the Notice of Assessment in the form that it is usually issued, before enforcement of proceedings would commence.

28. As a component of due process, it is important that a party has reasonable opportunity to know the basis of allegations against it. Elementary justice and the law demands that a person be given full information on the case against him and given reasonable opportunity to present a response. This right is not limited only in cases of a hearing as in the case of a court or before a tribunal, but when taking administrative actions as well. (See ***O'Donoghue v South Eastern Health Board [2005] 4 IR 217***). Hilary Delany in his book, ***Judicial Review of Administrative Action, Thomson Reuters 2<sup>nd</sup> edition, at page 272***, notes that, "*Even where no actual hearing is to held in relation to the making of an administrative or quasi-judicial decision, an individual may be entitled to be informed that a decision which will have adverse consequences for him may be taken and to notification of the possible consequences of the decision.*"

29. Fair and reasonable administrative action demands that the taxpayer would be given a clear warning on the probable consequences of non-compliance with a decision before the same is taken; in this case, the Company should in no uncertain terms have received information as to the implication of the letter and the consequences of its failure to make good the payments demanded in the notice. (See Supreme court decision in ***TV3 v Independent Radio and Television Commission [1994] 2 IR 439***).

30. In many jurisdictions around the world, it has long been established that notice is a matter of procedural fairness and an important component of natural justice. As such, information provided in relation to administrative proceedings must be sufficiently precise to put the individual on notice of exactly what the focus of any forthcoming inquiry or action will be. (See ***Charkaoui v Canada [2007] SCC 9, Alberta Workers' Compensation Board v Alberta Appeals Commission (2005) 258 DLR (4<sup>th</sup>), 29, 55*** and ***Sinkovich v Strathroy Commissioners of Police (1988) 51 DLR (4<sup>th</sup>) 750***).

31. As to whether the notice issued passes the standards of procedural fairness is both a question of law and fact dependent on the circumstances of each particular case, the statutory provisions and the nature of the matter to be decided. In the circumstances of this case, I find that the **Tax Demand** letter of 20<sup>th</sup> June 2011 sent to the Company fell short of the requirements of a proper notice in as far as it did failed to disclose its nature and the implication and consequences of non-compliance as well as notifying the taxpayer of the avenues of appeal or review available to it. A notice of the nature issued to enforce collection of taxes must clearly state to be such a notice, state the amount claimed, state the legal provision under which it is made and draw the taxpayers attention to the consequences of failure to comply with the law and the opportunity provided by the law to contest the finding. Such a notice would give the opportunity to any Kenyan to know the case against it and utilise the legal provisions to contest

the decision. The right to fair administrative action and the right of access of justice now enshrined in our Constitution demand nothing less.

32. As I stated in *Samura Engineering Limited and Others v Kenya Revenue Authority, Nairobi Petition No. 54 of 2011 [2012] eKLR*, at Para. 58 “*I wish to emphasise that Kenya Revenue Authority as the State agency charged with the collection of taxes is bound by the provisions of the Bill of Rights to the fullest extent in the manner in which it administers the laws concerning the collection of taxes. The values contained in Article 10 must at all times permeate its functions and activities which it is mandated to carry out [of] by statute.*”

### **Conclusion and disposition**

33. I have come to the conclusion that the Company’s rights to fair administrative action afforded by **Article 47(1)** were violated by issuing the Tax Demand dated 20<sup>th</sup> June 2011 and acting upon it to enforce the collection of taxes. Consequently any action cannot base upon it cannot lie and as such the Agency Notices dated 6<sup>th</sup> August 2012 are hereby quashed. I find and hold that Notice of Assessment dated 16<sup>th</sup> August 2012 is a proper notice issued under the **VAT Act** therefore proceedings consequent upon it including the objection lodged by the Company through its appointed agent shall proceed in accordance with the law.

34. Although a notice of assessment was issued in respect of Value Added Tax, no such notice was issued in respect of the amount due under the **Income Tax Act**. I therefore restrain the 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respondents from enforcing collection of Withholding tax and PAYE set out in the Tax Demand until such time as a proper notice of assessment is issued to the Company.

35. The petitioner, in its amended petition dated 29<sup>th</sup> October 2012 has sought fifteen prayers. Under the **Article 23**, the Court’s duty is to frame appropriate relief which will vindicate the petitioner’s rights and in light of my findings, I grant the following reliefs;

- (a) I declare that the petitioner’s rights under Article 47(1) of the Constitution were violated by the 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respondents when it issued the Tax Demand dated 20<sup>th</sup> June 2011 and proceeded to enforce collection of taxes upon it.**
- (b) The Agency Notices issued on the 6<sup>th</sup> August 2012 by the 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respondents be and are hereby quashed.**
- (c) The 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respondents be and are hereby restrained from collecting or enforcing the collection of Withholding Tax and PAYE pursuant to the Tax Demand dated 20<sup>th</sup> June 2011 until a proper notice of assessment is issued to the Petitioner.**
- (d) The conservatory orders in force be and are hereby discharged.**
- (e) The 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respondents shall bear the petitioner’s costs.**

**DATED and DELIVERED at NAIROBI this 18<sup>th</sup> day of March 2013**

**D.S. MAJANJA**

**JUDGE**

Mr Wekesa, instructed by Wekesa and Company Advocates, for the petitioner.

Ms Odundo, instructed by the Kenya Revenue Authority for the 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respondents.