



REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

JUDICIAL REVIEW 710 OF 2008

REPUBLIC APPLICANT

AND

COMMISSIONER OF CUSTOMS & EXCISE 1ST RESPONDENT

COMMISSIONER GENERAL KENYA REVENUE AUTHORITY 2ND RESPONDENT

COMMISSIONER OF DOMESTIC TAXES 3RD RESPONDENT

EX PARTE

MASTERMIND TOBACCO LIMITED

JUDGMENT

Introduction

1. The *ex-parte* applicant (“the applicant”) is a well known Kenyan company which manufactures and sells various brands of cigarettes including Comet Rocket, Supermatch, Kings, Ralli and Summit Lights. It has also been issued with an excise manufacturing licence under **section 91** of the *Customs and Excise Act (Chapter 472 of the Laws of Kenya)*.
2. This matter concerns the assessment of the excise duty payable on Supermatch brand of tobacco products manufactured by the applicant. The dispute stems from a letter dated 24th June, 2008 in which the 3rd respondent demanded from the applicant a sum of Kshs 442,205,324.00 on account of an under declaration of excise duty for the year 2007/2008.
3. After the grant of leave on 18th November 2008, the applicant filed a Notice of Motion dated the 27th November 2008 where it sought, inter alia, the following main orders:
 - a. Orders of certiorari to quash the decisions contained in the demand letters/assessment notices dated 24th June, 2008 and 28th July, 2008 issued by the Respondents, basing the rate of excise duty in respect of the applicant’s supermatch cigarettes on category C instead of category B and demanding payment of a sum of Ksh 442,205,324.
 - b. An order of certiorari to bring to this Honourable court the agency notices dated 23rd October 2008 and 11th November 2008 issued by the Respondents to Kenya Commercial Bank Limited and

Consolidated Bank of Kenya for purposes of being quashed.

c. An order of prohibition do issue to prohibit the Respondents from enforcing recovery of the amount of Ksh 442, 205, 324 referred to in the letters/assessment notices dated 24th June 2008 and 28th July, 2008 or taking adverse action against the Applicant based on the decisions in the letter and assessment notice.

4. The application is supported by the Statutory Statement dated the 17th November 2008 and the affidavits sworn on 17th November, 2008 and the 26th April, 2011 by Robert Mugambi Mutuma, the applicant's company secretary. The applicant's case is also supported by written submissions dated 1st July 2011.

5. The respondents have opposed the application through the replying affidavit of Ann Nyaguthie Irungu, the Senior Assistant Commissioner in the Domestic Taxes Department, sworn on 15th January 2009. The respondent relies on written submissions dated 14th July 2009 and 20th January 2012.

Statutory provisions for charging excise duty on cigarettes

6. The modus of charging excise duty on cigarettes is governed by the **Customs and Excise Act** which is amended from time to time. For purpose of this case and before I proceed to consider the arguments for and against the applicant I think it is proper to set out the legislative enactments material to the dispute. As these are legal matters, I am entitled to take judicial notice of these enactments by virtue of **section 60** of the **Evidence Act (Chapter 80 of the Laws of Kenya)**.

7. **Subsection 117(1) (d)** of the **Customs and Excise Act** creates an obligation on all manufacturers licensed to pay excise duty in respect of excisable goods and services specified in the **second column** of the **Fifth Schedule** to the Act at the respective rates specific in the **fourth column** of the **Fifth Schedule**. The section provides as follows;

117. (1) Subject to the provisions of this Act, there shall be charged--

(d) in respect of excisable goods specified in the second column of the Fifth Schedule, excise duties at the respective rates specific in the fourth column of that Schedule:

8. By **section 17** of the **Finance Act, 2003 (Act No. 2003)**, the **Fifth Schedule** to the **Customs and Excise Act** was amended by adding **PART II** at the end of the said schedule. **Section 17(ii)** of the **Finance Act, 2003** amended the **Fifth Schedule** to the **Customs and Excise Act** **"in the manner specified in part II of the Fourth Schedule to this Act."**

9. **PART II** of the **Fifth Schedule** provides as follows;

(1) For purposes of this schedule, "Retail selling price" means the average price at which exercisable goods are sold to customers in an open market transaction where the seller and buyer are independent of each other.

(2) Cigarette shall be grounded into four categories for purposes of this schedule and the corresponding rate of duty will be shown as hereunder

Category	Retail Selling price	Excise Rate per mille
	Per mille	
A	Upto Shs,1500	Shs.450

B	Shs.1501 to Shs.2500	Shs. 650
C	Shs. 2501 to Shs. 3500	Shs. 900
D	More than Shs. 3500	Shs. 1,400

(3) The Commissioner may from time to time through notice in the gazette adjust the retail selling price for each category of cigarettes for purposes of this schedule.

(4) For purpose of adjusting the retail selling price, the Commissioner may require manufacturers and importers to submit any information relating to manufacturing and pricing of exercisable goods.

10. The various categories of retail prices were also gazetted by the Commissioner of Customs and Excise vide **Gazette Notice No. 6776** dated 23rd September 2003 as follows;

Gazette Notice No. 6776

THE CUSTOMS AND EXCISE ACT
(CAP 472)

ADJUSTMENT OF RETAIL SELLING PRICES FOR THE PURPOSES OF PART II OF THE FIFTH SCHEDULE

PURSUANT to Section 3 of Part II of the Fifth Schedule, the Commissioner of Customs and Excise has adjusted the retail selling prices of cigarettes for the purposes of that schedule. Consequently, cigarette brands specified in the second column shall be charged excise duty at the rate specified in the third column of the schedule herein.

CATEGORY

<u>CATEGORY</u>	<u>BRAND</u>	<u>EXCISE RATE PER</u>
<u>MILLE (Kshs.)</u>		
A	Rooster, Score, Crescent & Star, Comet, Rocker, Polo	450
B	Supermatch, Kings, Supermatch menthol, Safari Kings, Ralli, Horseman menthol, Horseman Kings, Safari Super, Safari Menthol, Champion, Crown Board	650
C	Sportsman King Size, Sweet menthol	900
D	Embassy King Size, Embassy Lights, Embassy Superlights Embassy menthol, Sportsman Light, Benson & Hedges Lights, Benson & Hedges Special Filter,	

all other cigarette brands

1,400

New applications for alternative categorization will be determined having regard to the packages, retail price and other relevant information to be provided by the applicant.

Dated the 23rd September 2003.

11. In the year 2005, the Minister of Finance through **Finance Act, 2005 (Act No. 6 of 2005)** increased the rate of duty by deleting section 2 of part II of that schedule and inserting the following;

Category	Retail Selling price	Excise Rate per mille
	<u>Per</u>	
	<u>mille</u>	
A	Upto Shs,1500	Shs.495
B	Shs.1501 to Shs.2500	Shs. 715
C	Shs. 2501 to Shs. 3500	Shs. 990
D	More than Shs. 3500	Shs. 1,540

12. In the year 2006, the **Finance Act, 2006 (Act No. 10 of 2006)** increased the rate of excise duty on cigarettes by an amendment of section 2 of part II of the **Fifth Schedule** as follows;

Category	Retail Selling price	Excise Rate per mille
	<u>Per</u>	
	<u>mille</u>	
A	Upto Shs,1500	Shs.495
B	Shs.1501 to Shs.2500	Shs. 715
C	Shs. 2501 to Shs. 3500	Shs. 990
D	More than Shs. 3500	Shs. 1690

13. In the year 2007, the paragraph 2 of part II of the **Fifth Schedule** was amended by the **Finance Act, 2007 (Act No. 9 of 2007)** as follows;

Category	Retail Selling price	Excise Rate per mille
	<u>Per mille</u>	

A	Upto Shs,1500	Shs.500
B	Shs.1501 to Shs.2500	Shs. 800
C	Shs. 2501 to Shs. 3500	Shs. 1200
D	More than Shs. 3500	Shs. 2000

14. In 2008, the Minister of Finance proposed through the **Finance Bill, 2008 (Bill No. 12 of 2008)** that the criteria for charging excise tax be based on the physical characteristics of the cigarettes or the retail selling price. The **Finance Act (No. 8 of 2008)** which became operational on 13th June 2008 adopted this proposal and **section 2** of part II of the **Fifth Schedule** was amended as follows;

PART II

Category Duty	Description	Rate of
A	Plain cigarettes with RSP of up to – Shs.2,500 per Mille.	Shs.700 per mille
B	Soft-cup cigarettes of 72mm or less, or soft cap Cigarettes of 72 mm or less with RSP of 2,501 to Shs.3,500 per mille.	Shs. 1, 000 per mille
C	Soft-cup cigarettes of 72mm or less, or soft cap Cigarettes of more than 72 mm with RSP of 3,501 to Shs.4,500 per mille.	Shs. 1,500 per mille
D	Hinge lid cigarettes or hinge lid cigarettes with RSP of more than Shs.4,500 per mille (RSP means, Retail Selling Price)	Shs. 2,500 per mille

Applicant grievance

15. The applicant's case is founded on a letter dated 24th June 2008. The letter addressed to the applicant by the Commissioner Domestic Taxes demanded Kshs.442,205,324/= being undeclared excise tax. The letter stated as follows;

24th June 2008

Managing Director,

Mastemind Tobacco Ltd

P.O. Box 68144,
NAIROBI

RE: UNDER DECLARATION OF EXCISE TAX YEAR 2007

It has come to our attention that you have not been charging excise tax on your flagship brand Supermatch cigarettes.

Part II of the second schedule of the Kenya Gazette Supplement Act 2007 (Nairobi 26th October 2007) and also the Finance Act 2007 describes brands as below:-

Category	Retail Selling price	Excise Rate per mille
	Per mille	
A	Upto Shs,1500	Shs.500
B	Shs.1501 to Shs.2500	Shs. 800
C	Shs. 2501 to Shs. 3500	Shs. 1200
D	More than Shs. 3501	Shs. 2000

The Finance Act 2007 put the effective date for the above charges to be 1st October 2007 – refer to attached abstract of the Act.

Your records reflect that from October 2007 to date, your Supermatch brand of cigarettes fall within category C (since your selling price is Kshs.2560 per mille) and you have been placing it under category B

This has resulted to excise under declaration as follows,

The total excise tax under declared is Kshs,

Principal tax	Kshs. 399,975,325
Penalty	<u>42,229,999</u>
Total	<u>442,205,325</u>

Refer to the attached workings.

Please note in the month of September 2007, you also charged excise at the rate of Kshs.715 instead of Ksh.1,200.

Please arrange to pay the above duty immediately to avoid further penalties.

(Signed)

For Commissioner Domestic Taxes - LTO

16. During the period material to this case, the applicant's Supermatch brand was placed in category B as it was retailing within that bracket. The decision was reached on the basis of price information supplied to the respondents by the applicant and calculated in terms of section 1 of part II of the **Fifth Schedule**. It is on the basis of the retail price information that the 3rd respondent moved from Supermatch from category B to C when the applicant raised the retail price from Kshs.1,900/= per mille to Kshs.2,560/= per mille with effect from 20th August 2007.

17. The applicant contends that its Supermatch brand of cigarettes had a retailing selling price of Kshs.2,560/= per mille which attracted an excise duty of Kshs.1,200/= per mille in 2007. Consequently, it should pay duty at a rate of Kshs.800/= per mille as provided in **Gazette Notice No. 6776**, which notice classified specific brands within the respective categories.

18. The applicant submits that the changes initiated by the **Finance Act, 2008** introduced immense, ambiguity, uncertainty and inequity in the taxation of cigarettes. According to the applicant, the **Finance Act, 2008** introduced new product descriptions that were not defined nor known within the tobacco industry. The Bill makes reference to 'soft-cup I' and 'soft-cup II' without stating which brands fall within these descriptions.

19. The proposal contained in the **Finance Bill, 2008** caused industry players to seek clarification and in a letter dated 4th November 2008, the Director of Economic Affairs wrote to the Kenya Revenue Authority stating that the existing regime would be reviewed to ensure clarity in order to bring stability and predictability to industry players and importers.

20. After the initial demand was issued, correspondence was exchanged between the parties setting out their respective positions. The parties also held meetings with a view to reach a consensus on the matter but there was no meeting of minds. On 23rd October 2008, the respondents issued two agency notices to the applicants bankers Consolidated Bank of Kenya and Kenya Commercial Bank directing both banks to pay the disputed excise duty of Kshs.442,205,324/00.

21. It is upon receipt of these notices that the applicant moved the court for orders of judicial review. The applicant seeks this Court's intervention on the ground that the respondent's conduct is unlawful, erroneous, unreasonable, arbitrary, unfair and capricious, an abuse of the power, a violation of the applicant's legitimate expectation that the respondents would apply the law consistently and equitably.

Issues for determination

22. I have considered the oral and written submissions made on behalf of the parties. Substantial arguments have been made and authorities cited by both sides and if I do not quote them in this decision it is not because they were not helpful. There are two substantive issues for determination. The first one concerns whether the respondents could charge the applicant excise tax in the manner they did and the second is whether the respondents had authority to collect and enforce the tax. I shall dispose of the second issue first.

23. In the statutory statement the applicant challenged the demand letter dated 28th July 2008 from the 3rd respondent to the applicant in so far as it premised or draws authority from the **Income Tax Act (Chapter 470 of the Laws of Kenya)** and that the challenged agency notice issued by the Deputy Commissioner in the Large Tax Payers Office of the Kenya Revenue Authority are illegal as **section 166A** of the **Customs and Excise Act** does not confer such authority.

24. In its replying affidavit and submissions the applicant did not contest the detailed arguments set out in behalf of the respondents that the Kenya Revenue Authority had the legal authority through its officers to

collect taxes. I am satisfied on the basis of the provisions of the **Kenya Revenue Authority Act (Chapter 470 of the Laws of Kenya)** that the officers of authority had the requisite capacity and mandate to take steps to assess and collect taxes in the manner they did.

25. I think the primary issue in this matter arising from the letter dated 24th June 2008 is whether the respondents' decision to place the applicants Supermatch brand of cigarettes in Category C and not B of **section 2** of part II of the **Fifth Schedule** for purposes of calculating excise duty was irrational, unreasonable, capricious, ambiguous and illegal.

Whether the decision to charge excise tax is illegal

26. The argument proffered by the applicant is that there was no basis to charge excise duty as the fourth column in the **Fifth Schedule** to the **Customs and Excise Act** referred to in **section 117(1)(d)** does not in fact exist. According to Mr Macharia, counsel for the applicant, since the rates are to be specified in the fourth column, it follows that there is no basis to charge the tax.

27. The question posed by the applicant is whether these provisions introduced by the **Finance Act, 2008** are ambiguous, uncertain and lack clarity in view of the fact that the fourth column referred to is non-existent and that the legislation introduced ambiguous and undefined terms such as "soft-cup" and "hinge lid". Mr Macharia has cited various authorities that support the proposition that tax laws must be clear and certain among them *Vestey v Inland Revenue Commissioners* [1979] 3 All ER 984, *Inland Revenue Commissioners v Baldnoch Distillery Co., Limited* [1948] 1 All ER 84 and *Keroche Industries Limited v Kenya Revenue Authority and Others* Nairobi HC Misc. Civ. App. 743 of 2006 (Unreported).

28. Mr Oraro, counsel for the respondents, maintained the position that what the court is called upon to decide is not the ambiguity of the statute, irrationality or caprice but a factual determination as to whether the rate is within the band where customs duty is charged. The respondents' stance is that the provisions governing the excise duty on cigarettes are clear and unambiguous.

29. The applicant's argument ignores the amendment introduced by the **Finance Act, 2003 (Act No 15 of 2003)** which amended the **Fifth Schedule** by inserting a new **part II**. Part II of the **Fifth Schedule** is the provision under which the excise duty rate on cigarettes was to be calculated instead of the fourth column referred to in **section 117(1)(d)** of the **Customs and Excise Act**. Mr Oraro, counsel for the respondents, pointed out, the **Finance Act, 2008 (No. 8 of 2008)** formally removed reference to "the fourth column of that schedule" in **section 117(i)(d)** of the **Customs and Excise Act**.

30. Even though there continued to be reference to the provisions of the fourth column, the intention of Parliament introducing the amendment to the **Fifth Schedule** by inserting part II was to provide a legal basis for the calculation of a rate for charging excise duty on cigarettes. Section 2 of part II of the schedule was amended from time to time through the various **Finance Acts** leaving no doubt as to the legislative intention. I would therefore agree and adopt the sentiments expressed by *Halbury's Laws of England Volume 44(1) paragraph 1260* where the learned authors state that, "Sometimes an error occurs in the inducing words e.g. the House of Commons disqualification Act, 1975 Section 10(2) (as originally enacted) provided that the enactments, specified in Schedule 4 to this Act are repealed. The Act contains no schedule 4. It did however contain Schedule 3 (now repealed), which was headed 'Repeals' and other internal evidence, suggests that fifth Schedule 3 (repealed is the one intended. In such a case the Court will not frustrate Parliament's intention by applying the literal meaning of the inducing words but will install and apply a corrected version (e.g as if the inducing words referred to the enactment 'specified Schedule 3')"

31. This is not a case of legislative ambiguity and clarity. The intention of the legislature to provide a basis for charging excise duty on cigarettes is cigarettes based on the retail selling price as provided in **part II** of the **Fifth Schedule** introduced by the **Finance Act, 2003 (Act No. 15 of 2003)** and amended from time to time through the various **Finance Acts**. Each **Finance Act**, as I have outlined at paragraphs 7 to 15 above, set out precise categories, that is A, B, C and D, and the rates of duties applicable to each category of cigarettes.

32. This brings me to the purpose of **Gazette Notice No. 6776**. This notice is central to the applicant's case as it contends that in so far as the cigarette brands were named therein and Supermatch placed in category B, it could not be removed from that category unless the gazette notice is amended or repealed.

33. The applicant's argument lacks merit as the power of the Commissioner to issue **Gazette Notice No. 6776** is derived from **section 3** of part II of the **Fifth Schedule** which states, "**The Commissioner may from time to time through notice in the Gazette adjust retail selling price from each category of cigarettes for purposes of this schedule.**" It is to be noted that the **Gazette Notice** does not amend the **section 2** of part II which sets out the basis for calculating the rate of excise duty based on the retail sale price. The basis for calculating the retail selling price and excise rate is already determined as part of the legislation. What the provision entitles the Commissioner to do is to adjust the retail selling price and he may do so by reference to brands and he does so by classifying the brand within a particular retail price category.

34. Furthermore, the reference to brands is a practical and efficient way of communicating to the taxpayer the brands falling within a retail price category. It is not in dispute that the taxpayer provides the Commissioner of Customs and Excise information indicating the retail price for their products from time to time. The information is aggregated by the Commissioner on the basis of cigarette brands and the classification, which informs the Gazette Notice, is for all intents and purposes for convenience and information.

35. It is also the applicant's contention that the **Gazette Notice No. 6776** has not been repealed therefore rate of excise duty for its Supermatch brand should be based on the rate in Category B. This argument lacks merit because the Gazette Notice is not the basis for the calculation of the excise duty on cigarettes. The manner of calculating the retail selling price is provided for in **section 1** of **part II** of the **Fifth Schedule** on the basis on the retail price information provided by the taxpayer.

36. Furthermore, **Gazette Notice No. 6776** has not been ossified, it was only valid for the period that the rates stated therein were valid. Once the rates were altered by the succeeding **Finance Act**, the Gazette Notice ceased to apply. In other words, the Gazette notice was valid as long as the rates stated therein were applicable and since the rates ceased to apply after the subsequent **Finance Act** was passed, the Gazette notice ceased to apply and can no longer be relied upon by the applicant.

37. I therefore find and hold that **Gazette Notice No. 6776** did not affect, change or bring in a new categorisation, it only placed the brands within the specific categories based on the existing and prevailing retail selling price.

38. I will now consider the factual basis for calculating the tax. According to the Replying Affidavit of Ann Nyaguthie, the applicant continued to pay excise duty on its Supermatch brand of cigarettes at an excise duty rate of Kshs. 800 based on the initial selling price of Kshs. 1900 per mille. She further depones that despite the applicant increasing its price to Kshs. 2560 per mille with effect from August 2007 the applicant continued to pay the Category B rate of tax rather than the applicable rate which is at Category C.

39. In response the verifying affidavit of Robert Mutuma does not dispute the selling price asserted by the respondents but contests that manner in which retail selling price is arrived at. According to the applicant, this price ought to have been calculated in accordance with **section 127C(2) and (3)** of the **Customs and Excise Act** which excludes VAT, cost of excise stamps and the cost of returnable package box or bottle so that by taking this into account the price per mille for Supermatch would place it category B.

40. As I have stated, the assessment of tax on cigarettes is clearly provided for in part II of the **Fifth Schedule**, it follows then that recourse cannot be made to the provisions of **sections 127(2) and 137(1)** or any other section of the **Customs and Excise Act**. The legislative intent is so far as the taxation of cigarettes is concerned is clearly set out in the provisions of part II of the **Fifth Schedule** as amended from time to time.

41. Finally, the applicant cannot have recourse to the provisions of any subsequent Finance Acts or legislative proposals as the subject of this matter as the letter dated 24th June 2008 was a specific demand for tax accrued within a specific time frame in which the law as I have demonstrated was clear in its purport and import.

42. A substantial part of the applicant's argument is founded on the provisions introduced by the **Finance Act, 2008**. Unfortunately, the respondents' demand is for the period October 2007 to June 2008 where the **Finance Act, 2008** was inapplicable. The applicant's claim seems to center on questioning the merits and the appropriateness of the legislation in so far taxation of cigarettes is concerned. The applicant seems to be dissatisfied with the mode of computation set out in the schedule claiming that excise duty was 'an agency tax' and by using the consumer retail selling prices, it was an erroneous approach. Unfortunately, this is not the appropriate forum for addressing the inadequacies of the tax the legislature has enacted. I adopt the sentiments in **Maharashtra State Board of Secondary and Higher Secondary Education and Another v Kurmarsteth [1985] LRC** where the court stated *inter alia*: "It is exclusively within the province of the Legislature and its delegate to determine, as a matter of policy, how the provision of the statute can best be implemented and what measures, substantive as well as procedural would have to be incorporated in the rules or regulations for the efficacious achievement of the objects and purposes of the Act. It is not for the court to examine the merits or demerits of such a policy because its scrutiny has to be limited to the question as to whether the impugned regulations fall within the scope of the regulation..."

43. I therefore find and hold that that the respondents' decision contained in the letter dated 24th June 2008 to place the applicant's Supermatch brand of cigarettes in **Category C** and not **B** of **section 2 of part II of the Fifth Schedule** for purposes of calculating excise duty is not irrational, unreasonable, capricious, ambiguous and illegal.

Conclusion and disposition

44. In view of my findings that the basis for the assessment and calculation of excise duty of cigarettes contained in the letter dated 24th June 2008 was proper and valid, the remedy of certiorari cannot lie. The consequence of this finding is that the respondents are entitled to proceed with the action to enforce payment of taxes.

45. **Section 166A** of the **Customs and Excise Act** entitle the Commissioner to issue demand letters and Agency Notices to the applicant's bankers. The agency notices are issued were valid and I do not detect any error, abuse of power, caprice or unreasonableness to warrant the issuing of any of the orders of judicial review to stay the legal process from running its course.

46. The net effect of my findings is that the Notice of Motion dated 27th November 2008 is dismissed with costs to the respondents.

DATED and DELIVERED at NAIROBI this 21st day of September 2012

D.S. MAJANJA

JUDGE

Mr T. Macharia instructed by Mbugua, Atudo and Macharia Advocates for the exparte applicant.

Mr G. Oraro instructed by Oraro and Company Advocates for the respondents.