THE REPUBLIC OF KENYA

IN THE ENVIRONMENT AND LAND COURT

AT NAIROBI

ELC APPEAL CASE NO 6 OF 2019

KENYA MEDICAL ASSOCIATION.....APPELLANT

-VERSUS -

MACHIRI LIMITED.....RESPONDENT

(Being an Appeal from the Judgment of the Chief Magistrate Court at Nairobi, Milimani,

delivered by Honourable Teresia Ngugi, Senior Principal Magistrate, on 11th June 2014

in Civil Case No. 2699 of 2013)

JUDGMENT

1. On 14/5/2013, the respondent in this appeal, Machiri Limited, filed Nairobi (Milimani) CMCC No 2699 of 2013 against the appellant. They sought the following verbatim reliefs against the appellant;

> **a. The sum of Kshs 702,564.00 being the VAT penalty levied against the plaintiff on behalf of the defendant, loss of benefits and costs under the said agreement that the plaintiff would otherwise have received thereunder.**
>
> **b. General damages for breach of contract on the footing of aggravated damages.**
>
> **c. Interest at commercial rates on items (a) and (b), until *payment in full.***
>
> **d. Costs of this suit together with interest thereon at such rate and for such period time as honourable court may deem fit to grant.**
>
> **e. Any such other or further relief as this honourable court may deem appropriate.**

2. The case of the respondent in the said suit was that on 25/9/2008, they entered into written tenancy agreements with the appellant, pursuant to which they leased to the appellant, for a period of twelve months, two dwelling units identified as **CG** and **DG,** located on Land Reference Number 12107/1, Komo Lane, Kilimani, Nairobi, at a monthly rent of Kshs 55,000 for each of the two units. During the subsistence of the tenancy, the appellant, without the knowledge and approval of the respondent, converted the user of the demised premises from residential to commercial. As a consequence of the said change of user, Value Added Tax penalties were levied against the respondent. Consequently, the respondent sought the above reliefs against the appellant.

3. In answer to the claim, the appellant filed a statement of defence dated 18/6/2013. They admitted that: (i) they entered into the two tenancy agreements; (ii) the monthly rent was Kshs 55,000 per unit; and (ii) the user of the demised premises was that of dwelling house, among other aspects of the agreements. They contended that the tenancy agreements did not specify whether the agreed monthly rent was inclusive of Value Added Tax (VAT) or whether VAT was to be charged separately. They denied liability for the VAT penalties. Further, they denied being in breach of any of the terms of the two identical lease agreements. They further contended that the plaintiff had "the alternative" of levying VAT on the rent the moment they realized that there was a "conversion" of user of the demised premises. They urged the court to dismiss the claim.

4. On 10/4/2014, the two parties to this appeal recorded the following verbatim consent before Hon Teresia Ngugi SPM:

> **"By consent, matter to be disposed off by way of written submissions on the basis of the written statements and copies of**

documents filed by the parties on record. Mention on 23/5/14".

5. Subsequently, the parties filed written submissions and invited the trial court to render a judgment. In a judgment rendered on 11/6/2014, Hon Ngugi found the appellant liable to pay the respondent the sum of Kshs 702,564. Further, she found the appellant to have breached the tenancy agreement and condemned them to pay the respondent general damages of "Kshs 110,000 (equivalent to 2 months rent)". Further, she awarded the respondent costs of the suit and interest at court rates from the date of judgment.

6. Aggrieved by the decision, the appellant brought this appeal and urged the court to set aside the findings and award of the trial court on the following verbatim grounds:-

1. That the learned magistrate erred in law and fact by entering judgment in favour of the plaintiff for VAT worth the sum of Kshs 702,564.00/=, the sum of Kshs 110,000 as general damages and also for costs of the suit.

2. That the learned magistrate erred in law and fact by giving judgment in favour of the plaintiff with regards to the VAT of Kshs 702,564.00/= without proof whatsoever from the plaintiff showing that the said VAT was being claimed by the Kenya Revenue Authority.

3. That the learned magistrate erred in law and fact by not requiring the plaintiff to show how the total value of Kshs 702,564.00/= as VAT was reached at.

4. That the entire ruling of the learned magistrate lacks merit as the learned magistrate did not address important aspects such as proof that the plaintiff actually paid the full sum claimed from it by Kenya Revenue Authority and the fact that the plaintiff continued to collect rent during the whole period that the defendant utilized the property.

5. That the learned magistrate erred in law and fact by failing to take into account the fact that nowhere in the tenancy agreement was the duty to pay Vat placed on the appellant.

6. That the learned magistrate did not take into account the fact that the defendant paid all monies that were required, on time as per the tenancy agreement and did not therefore owe anything to the plaintiff.

7. That the learned magistrate erred in law and fact by failing to take into consideration the fact that the appellant performed its duties under the terms of the tenancy agreement and ensured that all the monies as per the tenancy agreement were duly paid.

8. That the learned magistrate in view of the circumstances set out herein above totally misdirected herself in delivering the judgment in favour of the plaintiff by failing to consider and appreciate the evidence on record tendered on behalf of the appellant.

9. That the learned magistrate erred in law in failing to take into account the fact that while the appellant was still a tenant on the property, the plaintiff continued to promptly collect their rent as was due to them and therefore are estopped by their conduct to claim VAT charges which were not part of the tenancy agreement.

10. That the total sum that the appellant is required to pay is too large and it will therefore be unjust to require the appellant to pay considering that all the monies that were required to be paid by the appellant according to the tenancy agreement were duly paid.

11. That the learned magistrate in view of the circumstances set out herein above totally misdirected herself in delivering judgment in favour of the respondent by failing to consider and appreciate the submissions on record tendered on behalf of the appellant.

7. The appeal was canvassed through written submissions dated 5/5/2020, filed by the firm of *Rachier & Amollo Advocates.* Counsel for the appellant condensed the eleven grounds of appeal into the following six issues under which he submitted:

i. Whether the respondent was aware of the purposes for which the two premises were leased by the appellant.

ii. Whether, despite the knowledge, the respondent made any adjustments to the rent payable by the appellant.

iii. Whose statutory duty was it to pay VAT for the demised premises.

iv. Whether the sum of Kshs 702,564 claimed by the respondent amounted to special damages and whether the respondent specifically pleaded and strictly proved them at trial.

v. Did the appellant breach any contractual terms of the tenancy agreement dated 25/9/2008.

vi. Whether general damages were awardable for breach of contract and whether the appellant should be re-imbursed the same.

8. On whether the respondent was aware of the purposes for which the two units were leased by the appellant, counsel submitted that although it was uncontroverted that as per the tenor of the lease agreements, the two units were to be utilized as residential properties, it was apparent that the respondent had both express and implied knowledge of the purpose for which the premises were ultimately used. Citing clauses of the agreements and two letters dated 23/3/2009 and 11/2/2011, counsel argued that the respondent knew that the appellant was using the premises for commercial purposes.

9. On whether, despite the knowledge, the respondent made any adjustment to the monthly rent, counsel submitted that the respondent failed to adjust the monthly rent to factor in VAT despite knowing the purpose for which the premises were being used. On the statutory duty to pay VAT, counsel submitted that under **Section 6** of the repealed Value Added Tax Act, Cap 476, it was the duty of the respondent to pay VAT owed to Kenya Revenue Authority. Counsel contended that the repealed Act did not place any burden on the appellant to pay VAT.

10. On whether the sum of Kshs 702,564 was a special damages claim, counsel submitted in the affirmative and contended that the claim constituted actual expenses alleged to have been incurred by the respondent owing to the omission of the appellant. Counsel argued that the claim was neither specifically pleaded nor strictly proved. Counsel submitted that the respondent did not, during trial, prove that they had paid the money to Kenya Revenue Authority. Counsel added that the respondent had failed to lead evidence to explain how the figure was arrived at.

11. On whether the appellant breached any term of the contract, counsel submitted that the appellant fully adhered to all the terms of the tenancy agreement. Counsel contended that the obligation to pay VAT was that of the respondent and it was the duty of the respondent to levy it and remit it to Kenya Revenue Authority. On whether the remedy of general damages was available for breach of contract, counsel cited the decision in **Provincial Insurance Company EA Limited v Mordecai Mwangi Nandwa, Kisumu Court of Appeal Civil Appeal No. 179 of 1995 and Kenya Breweries Limited v Kiambu General Transport Agency, Civil Appeal No. 9 of 2000 [2002] EA 398** and contended that no general damages can be awarded for breach of contract. Counsel faulted the trial magistrate for making an award of general damages for breach of contract. Counsel urged the court to allow the appeal and set aside the Judgment of the trial court.

12. The respondent filed written submissions dated 11/6/2021 through the firm of *Kimani Richu & Associates*. Counsel for the respondent identified the following as the seven (7) issues falling for determination in the appeal: (i) Whether the purpose for which the appellant/defendant was to use the premises was well known between the parties prior to signing the tenancy agreement; (ii) Whether the appellant/defendant breached the terms of the tenancy agreement in changing the use of the property to commercial purposes instead of using it for residential purposes; (iii) Whether the tenancy agreement specified that the rent payable was inclusive of VAT or whether VAT was to be charged separately; (iv) Whether the appellant/defendant is liable to pay to the plaintiff VAT amounting to Kshs 720,564 levied upon the latter by the Nairobi City Council (sic) due to the change of user; (v) Whether the appellant/defendant breached the tenancy agreement herein; (vi) Whether the respondent/plaintiff is entitled to general damages for breach of contract; and (vii) Who is liable to pay costs of this suit.

13. On whether the respondent was aware of the purpose for which the two units were leased by the appellant, counsel for the respondent submitted that the tenancy agreements were clear that the units were leased as dwelling houses/residential properties, a fact which the appellant had admitted in their statement of defence. Counsel argued that the appellant was estopped by the law of contract against relying on other sources to contradict the express terms of the contract. On whether the respondent acquiescenced to the change of use by the appellant, counsel for the respondent submitted that no representation was made nor was there an express provision that the appellant could use the demised premises for commercial purposes. Counsel added that the respondent wrote several letters to the appellant reminding them that the premises were intended for residential use only. Counsel argued that it was bad faith for the appellant to allege acquiescence on the part of the respondent yet they were the ones who breached the tenancy agreement by using the premises for commercial purposes while aware that the premises were leased as dwelling houses.

14. On whether the respondent should have made adjustments to the rent payable by the appellant, counsel submitted that the respondent was not at any point required to make any adjustments to the rent because dwelling houses did not attract VAT. On whose statutory duty it was to pay VAT, counsel for the respondent submitted that dwelling houses did not attract VAT and that payment of VAT was an obligation hoisted on the respondent when the appellant changed the use of the demised premises. Counsel added that in ideal circumstances, the obligation of paying VAT would be on the respondent but because the premises were leased as dwelling houses, the obligation to pay VAT passed from the respondent to the appellant. On whether the appellant breached any of the terms of the contract, counsel for the respondent submitted that the two units were expressly leased as dwelling houses and contrary to that the appellant changed the use of the demised premises thereby attracting VAT. Counsel contended that the use of the premises for commercial purposes was contrary to the terms of tenancy contracts.

15. On whether Kshs 702,565 amounted to special damages and whether the respondent specifically pleaded and strictly proved the claim, counsel submitted that this issue was not canvassed before the trial court and was therefore misleading. Counsel contended that the issue before the trial court was whether the appellant was liable to pay for the VAT amounting to Kshs 720,564 (sic) levied upon the latter by the Nairobi City Council (sic) due to the change of user. Counsel contended that the trial court was not required to deal with an issue that was not raised by the parties. Counsel urged the court not to allow the appellant to raise this as an issue in this appellate court. Lastly, on whether general damages were awardable for breach of contract and whether the appellant should be re-imbursed the same, counsel for the respondent submitted that assessment of damages was an exercise of judicial discretion. Counsel cited various decisions and urged this court to uphold the award of general damages. Counsel for the respondent urged the court to dismiss the appeal.

Analysis & Determination

16. I have perused and considered the record of appeal in its entirety, including the grounds of appeal. I have also considered the parties' respective submissions. Further, I have considered the relevant legal framework and jurisprudence. As a general principle, the jurisdiction of the first appellate court is to re-evaluate and re-assess the entire evidence with a view to arriving at proper inferences of fact and independent conclusions. The court is, in this regard, guided by the decisions in A**bok James Odera t/a A J Odera & Associates v John Patrick Machira t/a Machira & Company Advocates [2013] eKLR** and **Mwana Sokoni v Kenya Bus Services Limited [1985] 931.**

17. From the record of the trial court, parties elected to go for an unconventional mode of trial. They elected to admit written submissions and bundles of documents and invited the court to render a decision based on the witness statements and bundle of documents without the statements and the documents being subjected to scrutiny through cross-examination. It is within this context of unconventional mode of trial that the court is invited to pronounce itself on evidence that was never subjected to scrutiny through cross examination. Within this unique context, four key issues fall for determination in this appeal: (i) Whether the appellant was liable to pay Value Added Tax (VAT) to the respondent as a consequence of using the demised premises for commercial purposes instead of using them as dwelling houses; (ii) Whether the respondent proved their claim for Kshs 702,561 as required under the law; (iii) Whether the respondent was entitled to general damages for breach of contract; (iv) What order should be made in relation to costs. I will make brief sequential pronouncements on the four issues in the above order.

18. The first issue is whether the appellant was liable to pay VAT to the respondent as a consequence of using the demised premises for commercial premises instead of using them as dwelling houses. There was common ground that under the relevant tenancy agreements, the two units were leased to the appellant as dwelling houses. There was also common ground that during the subsistence of the tenancy, the appellant used the premises for commercial purposes, leading to demand for Value Added Tax (VAT) by Kenya Revenue Authority. Further, there was commons ground that the applicable legal framework on VAT at the material time was the repealed Value Added Tax Act, Chapter 476.

19. It is not in dispute that under the repealed Value Added Tax Act (the repealed VAT Act), rent relating to dwelling houses (residential premises) did not attract VAT. It is also not disputed that under the said legal framework, rent relating to commercial premises attracted VAT.

20. From the evidence placed before the trial court, the demised premises were leased as dwelling houses. This fact was admitted by the appellant in their defence. There was no evidence of any formal agreement permitting the appellant to use the premises for commercial purposes. Similarly, there was no evidence of any formal approval from the relevant authority permitting the appellant to use the demised premises for commercial purposes.

21. In the absence of any formal agreement between the parties, relating to change of use, I entirely agree with counsel for the respondent that the VAT which the demised premises attracted was a direct result of the appellant's unilateral decision to depart from the agreed use (dwelling house) to commercial use. The appellant was therefore liable to bear the VAT liability that came with the change of use. That is my finding on the first issue.

22. The second issue is whether the respondent proved their claim for Kshs 702,561 as required under the law. The respondent was required to tender evidence in proof of the claim on a balance of probability. The proof to be tendered was to be in tandem with what the respondent pleaded in the plaint. In paragraph 8 of the plaint, the respondent pleaded thus:

> **"8. By reason of the matters aforesaid, VAT penalties were levied against the plaintiff and the plaintiff has lost the benefits under the tenancy agreement and lost the revenue it would otherwise have received thereunder and have suffered loss and damage."**

23. Further, the respondent particularized their loss as Value Added Tax penalties in the sum of Kshs 702,564. The respondent itemized their reliefs as set out in the opening paragraph of this Judgment. What evidence was required to demonstrate that the respondent had suffered the above loss? In my view, given that VAT was payable to Kenya Revenue Authority (KRA), the respondent needed to place before court evidence indicating that a specified sum in VAT had been levied on the rent they charged within a particular period in relation to the two demised units, and that they had paid to KRA the said VAT. This is what would be considered to be a loss attributable to the appellant's change of use of the demised premises. Regrettably, there was nothing presented to the trial court to demonstrate that the respondent had paid the money to KRA and thereby suffered the pleaded loss. In the absence of proof of payment of VAT to Kenya Revenue Authority (KRA) by the respondent, they would not be said to have suffered loss and damage as pleaded. My finding on the second issue therefore is that although the appellant was liable to be charged VAT as a consequence of changing the use of the suit property to commercial, the respondent did not present to the trial court evidence to prove that they had paid the VAT to KRA and that they had suffered loss and damage as a consequence. The claim of Kshs 702,564 as loss and damage suffered by the respondent was therefore not proved.

24. The third issue is whether the respondent was entitled to general damages for breach of contract. The law on damages for breach of contract is well settled. Our courts have been categorical that as a general principle of the law of contract, general damages are not payable for breach of contract. The Court of Appeal reaffirmed this principle in **Kenya Tourist Development Corporation v Sundowner Lodge Limited [2018] eKLR** in the following words;

> **"…. as a general rule general damages are not recoverable in**
>
> **cases of alleged breach of contract and that has been the settled position of law in our jurisdiction and with good reason. In Dharmshi v Karsan [1974] EA 41, the former Court of Appeal held that general damages are not allowable in addition to quantified damages, with Mustafa JA expressing the view that such an award would amount to duplication."**

25. The above principle prevailed at the time the Learned Magistrate made an award of general damages for breach of contract. Without saying much, therefore, this was an award that should not have been made. My finding on the third issue, therefore, is that the respondent was not entitled to general damages for breach of contract.

26. On costs, it is clear from the facts of this appeal that the appellant was the author of the dispute through the unilateral change of the use of the demised premises. They are off the hook because the respondent failed to place before the trial court evidence of payment of VAT relating to the two units to KRA; not because they were not liable. I will therefore not award them costs in either of the two courts.

Summary of Findings

27. In summary, my findings on the key issues in this appeal are as follows:-

a. As a consequence of changing the use of the demised premises from dwelling to commercial the appellant was liable to pay VAT to the respondent for onward transmission to Kenya Revenue Authority.

b. Based on the pleadings and evidence before the trial court, the respondent failed to prove loss as pleaded, in terms of the precise figure that the respondent paid to Kenya Revenue Authority.

c. As a general principle of the law of contract, general damages were not payable to the respondent for breach of the contract.

d. Because of the circumstances of this dispute, and the role which the appellant played in triggering the dispute, there will be no award of costs, both in this appeal and in the trial court.

Disposal Orders

28. In light of the above findings, this appeal is disposed in the following terms:-

a. The appeal herein is allowed and the judgment and decree of the trial court are set aside.

b. The judgment and decree of the trial court are substituted with an order dismissing the plaintiff's suit with no order as to costs.

c. Parties shall bear their respective costs in this appeal.

DATED, SIGNED AND DELIVERED VIRTUALLY AT THIKA ON THIS 26TH DAY OF OCTOBER, 2021

B M EBOSO

JUDGE

In the presence of: -

Mr Munyua for the Appellant

Ms Thenge for the Respondent

Court Assistant: Lucy Muthoni

NOTE:

This Appeal was heard and a Judgement date fixed when I was stationed at Nairobi (Milimani) Environment and Land Court Station. Subsequent to that, I was transferred to Thika Environment and Land Court Station. This is why I have delivered the Judgment virtually at Thika.

B M EBOSO

JUDGE