



**Commissioner of Domestic Taxes v CKL Africa Limited (Income Tax Appeal E050 of 2022)
[2023] KEHC 17270 (KLR) (Commercial and Tax) (12 May 2023) (Judgment)**

Neutral citation: [2023] KEHC 17270 (KLR)

**REPUBLIC OF KENYA
IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)
COMMERCIAL AND TAX
INCOME TAX APPEAL E050 OF 2022**

FG MUGAMBI, J

MAY 12, 2023

BETWEEN

COMMISSIONER OF DOMESTIC TAXES APPELLANT

AND

CKL AFRICA LIMITED RESPONDENT

*(Being an appeal from the decision of the Tax Appeals Tribunal
delivered on 4th March 2020 in Tax Appeal No. 297 of 2020)*

JUDGMENT

Introduction and background

1. The respondent in this case is a private limited company registered in Kenya and carrying on the business of manufacturing animal feeds. The facts leading to this appeal are that the respondent constructed an animal feeds supplements factory at Tatu City in Ruiru, Kiambu City for the purposes of manufacturing animal feed supplements. The cost of the project was given by the respondent as Kshs. 277,271,427/=. The respondent claimed from the appellant an investment deduction at the rate of 150% on the cost of building incurred for the year 2019.
2. The respondent audited the appellant's investment deduction costs and on 4th November 2020 made preliminary findings whereupon it disallowed the investment deduction allowance of Kshs. 423,033,494.00 in the year 2018/2019 and stated that the same would be claimed in 2019/2020.
3. On 29th January 2021 the appellant issued an audit report disallowing the investment and at the same time demanded corporation and withholding tax with penalties and interests amounting to Kshs. 29,440,260.00. The respondent objected to the assessment vide a letter dated 25th February 2021 and on March 2021 the appellant issued another assessment of Kshs. 21,697,944.00. The appellant issued



an objection decision dated 30th April 2021 and being aggrieved by the decision the respondent lodged an appeal at the Tax Appeals Tribunal (the Tribunal). The Tribunal delivered its judgment on 4th March 2020 allowing the appeal and setting aside the objection decision.

4. Being dissatisfied with the judgment, the appellant appealed to this court vide a Memorandum of Appeal dated 9th May 2022. The Memorandum of Appeal set out five grounds of appeal as follows;
 - i. The Honourable Tribunal erred in law and fact in finding that the appropriate provisions to be relied on in determining whether the building and machinery for the Respondent are subject to investment deduction is paragraph 24(1)(f) as read together with paragraph 24(2)(c) of the Second schedule (now repealed) of the *Income Tax Act* and not the Tax Laws (Amendment) Act, 2020 that amended the Second Schedule of the *Income Tax Act* that came into force on 25th April 2020.
 - ii. The Honourable Tribunal erred in law and fact by finding that the Respondent's building and machinery was first used in June 2019 when the first and second batch of Maclik Super was manufactured
 - iii. The Honourable Tribunal erred in law and fact in holding that the Respondent's building and machinery qualified for investment deduction of up to 150% as claimed.
 - iv. The Tribunal erred in law and fact by finding that the payments made by the respondent to local service providers resident in Kenya cannot be considered to be income of the non-resident consultants and therefore not chargeable to withholding tax.
 - v. The Tribunal erred in law and fact in holding that the appellant herein erred in its audit findings dated 29th January 2021 and consequently erred in issuing its objection decision dated 30th April 2021.
5. The appellants case was that the respondents building and machinery qualified for investment deduction in the year of income 2019/2020. According to the appellant the first year of use meant that one of the requirements for the investment deduction was the person claiming had to prove usage of the same. The appellant further submitted that since the certificate of completion was issued on 5th August 2019, it was not possible for the appellant to claim that manufacturing had begun before the completion of the mechanical and electrical works of the plant. It was the appellant's further contention that the certificate of building compliance ought to have been issued by the County Government of Kiambu City and not the Development Control Committee of Tatu City.
6. With respect to manufacturing the appellant contended that the respondent had not provided any evidence of it actually taking place save for the test runs conducted. The appellant submitted that the respondent was bound by the plant contract and the commissioning and performance tests and warranty clauses which required the appellant to sign the taking over certificate and execute guarantee before taking over the building. According to the appellant the said certificates were executed on 5th August 2019.
7. The respondent opposed the appeal vide its statement of facts dated 22nd July 2022. It was its case that the construction of the building was completed in January 2019. Thereafter the respondent commenced installation of electricity, a generator, fire equipment and machinery which was completed in June 2019. The respondent then took over the building on 12th June 2019 when the project architect issued a certificate and the Tatu City Development Control Committee inspected the building and issued a certificate of building compliance on 17th June 2019. Counsel submitted that the manufacture



of mineral supplements also commenced in June 2019 with the manufacture of batch 001 and 002 of Maclik Super for sale.

8. It was the respondent's further submissions that its claim for investment deduction was premised on paragraph 24(1)(f) as read with paragraph 24(2)(c) of the second schedule of the *Income Tax Act* (repealed). The respondent further submitted that the Act did not provide the definition of the word use and that the Tribunal had given a proper definition.
9. Counsel submitted that the building was utilized for manufacturing activities within the month of June 2019 and the law did not provide a restriction as to the volume of units that would have to be produced for a taxpayer to be considered to having manufactured a product. It was submitted that in the event the date of first use was taken to be August 2019, the new rates would still not be applicable as they would take effect in the period following 25th April 2020.
10. The respondent also responded to the issue of withholding tax demanded by the appellant stating that the payment of fees were made to local people and were not subject to withholding tax.

Analysis

11. The Court has carefully considered the pleadings, the record and the submissions of rival parties as well as the impugned judgment. The 1st, 2nd and 3rd grounds are related and will be determined together. They are to the effect that the Tribunal erred in finding that paragraph 24(1)(f) as read together with paragraph 24(2)(c) of the second schedule (now repealed) of the *Income Tax Act* was applicable in determining whether the building and machinery for the respondent was subject to investment deduction. The Tribunal is also faulted for holding that the respondent's machinery was first used in June 2019 and allowing the deduction up to 150% as claimed.

12. The amended paragraph 24(1)(f) provided as follows:-

Subject to this schedule, where capital expenditure is incurred on the construction of a building, or purchase and installation of machinery outside the city of Nairobi or the Municipalities of Mombasa or Kisumu whereof the value of investment is not less than two hundred million shillings: there shall be deducted, in computing the gains or profits of the person incurring that expenditure for the year of income in which they were first used (hereinafter referred to as the year of first use of the building or machinery referred in subparagraph (f)), a deduction referred to as an investment deduction.

13. Paragraph 24(2)(c) in turn provided that; -

The amount of investment deduction under subparagraph (1) shall in the case of an investment referred to in subparagraph (1)(f), be equal to one hundred and fifty percent of the capital expenditure.

14. This Court has on several occasions laid down the test for interpretation of tax statutes. For instance, in the case of *Republic v Commissioner of Domestic Taxes Large Tax Payer's Office Ex-Parte Barclays Bank of Kenya Ltd* [2012] eKLR the court held as follows:

The approach to this case is that stated in the oft cited case of *Cape Brandy Syndicate v Inland Revenue Commissioners* [1920] 1 KB 64 as applied in *T.M. Bell v Commissioner of Income Tax* [1960] EALR 224 where Roland J. stated, " ...in a taxing Act, one has to look at what is clearly said. There is no room for intendment as to a tax. Nothing is to be read in, nothing it to be implied. One can only look fairly at the language used... If a person



sought to be taxed comes within the letter of the law he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be.”

15. Similarly, the Court of Appeal in *Kenya Revenue Authority v Republic (ex-parte Fintel Ltd) NRB CA Civil Appeal No. 311 of 2013 [2019] eKLR*, cited with approval the dictum of Lord Atkinson in *Inland Revenue Commissioners v Duke of Westminster [1936] AC 1* where it was stated that;

It is well established that one is bound, in construing revenue Acts, to give a fair and reasonable construction to their language without leaning to one side or the other, that no tax can be imposed on a subject by Act of Parliament without words in it clearly showing an intention to lay the burden upon him, that the words of a statute must be adhered to, and that so-called equitable constructions of them are not permissible.

16. Further in *Commissioner of Income Tax vs. Westmont Power (K) Ltd Nairobi High Court Income Tax Appeal No. 626 of 2002*, the Court while citing *Inland Revenue vs. Scottish Central Electricity Company [1931] 15 TC 761* expressed itself as follows:

Even though taxation is acceptable and even essential in democratic societies, taxation laws that have the effect of depriving citizens of their property by imposing pecuniary burdens resulting also in penal consequences must be interpreted with great caution. In this respect, it is paramount that their provisions must be express and clear so as to leave no room for ambiguity...any ambiguity in such a law must be resolved in favour of the taxpayer and not the Public Revenue Authorities which are responsible for their implementation.

17. There is no dispute that the respondent was entitled to claim investment deduction. This is an incentive deduction granted on cost of a building and machinery installed therein as an incentive to encourage investments. It is based on the fact that the construction is a capital expenditure that is utilized to generate taxable income. Against this background, the dispute is more as to when the investment deduction ought to have been claimed and therefore the applicable law and rate allowed.

18. Before going any further, it is important to first determine which statute was applicable in this case. Is it the Tax Laws (Amendment) Act, 2020 as submitted by the appellant or is it its predecessor the *Income Tax Act* as submitted by the respondent? The Tax Laws (Amendment) Act, 2020 was assented to on 25th April, 2020. Section 1 of the Act provides as follows:

This Act may be cited as the Tax Laws (Amendment) Act, 2020 and shall come into operation —

- a. in the case of the amendment to section 5(2) of the *Value Added Tax Act*, 2013, on the 15th day of the next month following assent; and
- b. for all other provisions of the Act, on the date of assent.

19. It is clear from this that the Tax Laws (Amendment) Act, 2020 that amended the second schedule of the *Income Tax Act* came into force on 25th April 2020. Section 23 of the Interpretations and General Provisions Act, provides an overarching guide on the effect of repealing written law and provides that:-

Where a written law repeals in whole or in part another written law, then, unless a contrary intention appears the repeal shall not;

- a)



- b)
- c) Affect a right or privilege, obligation or liability acquired, accrued or incurred under a written law so repealed or
20. From the foregoing and in the absence of any contrary intention in the Income Tax Laws (Amendment) Act, 2020, the right and privilege that the respondent had acquired under paragraph 24(1)(f) as read together with paragraph 24(2)(c) of the second schedule, could not be affected by the repeal. The repeal came in after the construction was complete and even if it were to be decided that the first use was in August 2019 and not June 2019, still the existing framework at the time was the Income Tax Laws (Amendment) Act, 2020.
21. It is therefore my finding that the *Income Tax Act* in force prior to the coming into force of the Tax Laws (Amendment) Act, 2020 applied in this case and that the Tribunal was right in its finding on this point. The respondent qualified for investment deduction at the rate of 150% so long as it had met the requirements stipulated therein.
22. As to whether the respondent complied with the requirements set out for the deduction of investment deduction, there appears to be only one dispute, being whether the year of income when the building and machinery were first used is in 2019/2020 as alleged by the respondent or 2020/2021 as alleged by the appellant. The Statement of Facts filed by the respondent confirmed that the year of income for purposes of accounting by the respondent had ended on 30th June 2019.
23. The appellant, while accepting that there was production of batch 001 and 002 in June disagrees that this production falls within the definition of ‘first use’, that these were just test runs and that the actual use cannot have begun before August 2019 when the Certificate of Completion of installation of the machinery was dated. The respondent explains this by stating that the Certificate was issued in August after allowing the production of batches 001 and 002, so as to ensure that the machinery was working as required.
24. The Tribunal in its judgment held that the ITA did not provide the definition of the word use and relied on the Cambridge Dictionary which defined use to mean “to put something such as a tool, skill or building to a particular purpose.” To take this further, the purpose for which the project was constructed was to manufacturer animal feeds supplements. The question then would be when is it that the respondent put the project into manufacturing? The term ‘manufacturing’ was defined in paragraph 24(2)(e) of the second schedule to the repealed *Income Tax Act* as follows:
- Manufacture means the making (including packaging) of goods or materials from raw or partly manufactured materials or other goods ...but does not extend to any activities which are ancillary to manufacture such as design, storage, transport or administration.
25. This Court is therefore inclined to agree with the Tribunals decision that there was actual manufacturing of the 1st and 2nd batches of Maclik Super from June 2019. By this, the respondent had put into use the building and so the year of income when the project was first put to use was 2018/2019 and the investment deduction was due within the 2018/2019 financial year. This was all that was required to be proved and the respondent proved the same. Had the legislature intended to prescribe other requirements, this would have been expressly stated in the law.
26. The final ground of appeal is with respect to payment of withholding tax where the appellant faults the Tribunal in holding that payments made by the respondents to the local service providers resident in Kenya could not be considered to be income of non-resident consultants.



27. The Tribunal observed thus;

From the above facts, the appellant paid certain costs to local service providers on behalf of the consultant Buhler meaning the same was an expenditure not profit or income accrued by the consultant. As such the tribunal finds that the said payments made to local service providers resident in Kenya cannot be considered to be income of the nonresident consultant as the respondent implies. Consequently, then the tribunal further opines that the respondent was wrong in charging withholding tax on the amount which as seen above was not income of the profit accrued by the consultant Buhler.

28. It is the appellants case that the claim for Kshs. 1,622,842 was paid on behalf of the consultant who was considered a nonresident person for tax purposes. On its part, the respondent observed that the payments in question were not made to a nonresident person or for the consideration of managerial, technical, agency, contractual, professional or consultancy services.

29. Section 35(1) of the *Income Tax Act* provides that;

A person shall, upon payment of an amount to a non-resident person not having a permanent establishment in Kenya in respect of-

- a. a management or professional fee.....;
- b. a royalty;
- c. interest, including interest arising from a discount upon final redemption of a bond, loan, claim, obligation or other evidence of indebtedness measured as the original issue discount;

Provided that:

- (d)
- (e) interest which is chargeable to tax, deduct therefrom tax at the appropriate non-resident rate.”

30. Section 10 of the Act further provides that payment in respect of a management or professional fee is deemed to accrue in or to be derived from Kenya only when the payment is made by a resident person or a person having a permanent establishment in Kenya. This Court held in the case of *Motaku Shipping Agencies Limited v Commissioner of Income Tax* [2014] eKLR that three reference points, that is the payer, the payee and the place of accrual or derivation must be borne in mind in determining whether payment is subject to withholding tax or not.

31. Applying the above decision in this case, the respondent’s contention was that payments constituted income from the local service providers who were not subject to withholding tax. No evidence has been provided to dispute that fact by the appellant and it is my view that the respondent had discharged its burden in proving that the payments did not fall within the bracket of withholding tax. In the premises, this court finds that the appellant has not demonstrated that the Tribunal erred in law and fact by finding that the payments made by the respondent to local service providers resident in Kenya cannot be considered to be income of the non-resident consultants and therefore not chargeable to withholding tax.



Determination and orders

32. In conclusion I find no error and hence no reason to interfere with the decision of the Tribunal dated 4th March 2020. The appeal is therefore dismissed but with no orders to costs.

DATED, SIGNED AND DELIVERED IN NAIROBI THIS 12TH DAY OF MAY 2023

F. MUGAMBI

JUDGE

Court Assistant: Ms. Lucy Wandiri.

