



REPUBLIC OF KENYA



Commissioner of Domestic Taxes v Key Microfinance Bank Limited (Tax Appeal E031 of 2022) [2023] KEHC 19067 (KLR) (Commercial and Tax) (14 June 2023) (Judgment)

Neutral citation: [2023] KEHC 19067 (KLR)

**REPUBLIC OF KENYA
IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)
COMMERCIAL AND TAX
TAX APPEAL E031 OF 2022
DO CHEPKWONY, J
JUNE 14, 2023**

BETWEEN

COMMISSIONER OF DOMESTIC TAXES APPELLANT

AND

KEY MICROFINANCE BANK LIMITED RESPONDENT

(Being an appeal from the whole Judgment of the Tax Appeals Tribunal delivered on 4th February 2022 in Nairobi Tax Appeal Tribunal Appeal No. 251 of 2020)

JUDGMENT

Introduction

1. This is an appeal by the Commissioner of Domestic Taxes arising from the Judgment of the Tax Appeals Tribunal delivered on 4th February, 2022 which arose from the Respondent's objection dated 3rd July, 2022.

Background

2. The dispute in this appeal arises from the failure of the Respondent to remit excise duty of Kshs.1,630,944/= on additional interest charged on the late loan payment which it caps as interest for the period 2015 to 2017.
3. By a Notice of Assessment dated 8th February, 2019, the Commissioner informed the Respondent, "Key Microfinance Bank Limited" to clear the outstanding tax amount, and it was reminded of its right to object to the Assessment.
4. By a letter dated 30th October, 2019 the Respondent requested for enlargement of time to enable it file an objection out of time. The Commissioner allowed the Respondent to file a Notice of Objection



- vide a letter dated 20th December, 2019 and requested the Respondent to furnish the Commissioner with additional documents for its consideration within 14 days. The Respondent filed a Notice of objection on 2nd January, 2020.
5. A meeting between the Commissioner and the Respondent was held on 13th March, 2020 wherein the Commissioner called for more additional documents from the Respondent to be furnished within 14 days. In a letter dated 21st May, 2022, the Commissioner declared the objection invalid and confirmed the assessment for reasons that the Respondent had failed to furnish the Commissioner with the additional documents within the stipulated timelines. The Respondent had attributed the delay in complying with the Commission's directions on the Outbreak of Covid-19 which affected normal operations in its organization.
 6. Based on the actions of the Commissioner for declaring the Objection invalid, his led to the Respondent filing a Notice of Appeal dated 8th June, 2020 at the Tax Appeals Tribunal. Further, it filed a Memorandum of Appeal, Statement of Facts and supporting documents on 22nd June, 2020. The arguments raised by the Respondent in the appeal were that additional interest levied for late payment of loans by borrowers is not subject to Excise duty, and recoveries from borrowers intended to be used for the exclusive use of insurance of a loan are not subject to Excise duty.
 7. In opposing the appeal, the Commissioner filed a statement of facts dated 23rd July, 2020. Parties filed respective submissions. And on 4th February, 2022, the Appeals Tribunal allowed the appeal and upheld the objection.
 8. Aggrieved by the Judgment of the Appeals Tribunal the Commissioner filed the current appeal by a Memorandum of Appeal dated 30th March, 2022, citing the following grounds, that:-
 - a. the tribunal erred in law and in fact in finding that the additional interest levied for late payment of loans by borrowers is not subject to excise duty.
 - b. the Tribunal erred in law and in fact in adopting the definition of interest as provided for in the [Income Tax Act](#) in determining what constitutes additional interest on late payment of loans as the matter in issue was anchored on the [Excise Duty Act](#).
 - c. the Tribunal erred in law and in fact as it failed to appreciate the Respondent had recognized their Interest Income, Fees and Commission Income are different and that the same are reported differently.
 - d. the Tribunal erred in law and in fact in failing to consider the definition and appreciate the application of interest income as covered in the CBK Prudential Guidelines 2013 Clause II paragraph 1.1 page 218 thereby arriving at a wrong conclusion.
 - e. the Tribunal erred in law and in fact when it failed to appreciate that even the Banking Industry clearly defines what constitutes interest and other charges as in various documents which include the [Banking Act Amendment](#) 2016, Loan/ Cost of Credit Calculator, CBK Circular No. 4 of 2016, KBA Consumer Guide, Loan Agreements, and Section 44(A) [Banking Act](#) Cap 488 in *duplum* rule.
 - f. the Tribunal erred in law and in fact in failing to consider relevant material evidence placed before it and thus arriving at a wrong conclusion.
 9. On the foregoing, the Commissioner urged the court to allow the Appeal, set aside the Judgment of the Tax Appeals Tribunal, uphold its assessment and award costs to the Appellant.
 10. The Respondent opposed the appeal vide a statement of facts date 13th May, 2022.



11. By the directions of this Court the appeal was heard by way of written submissions.

Appellant's Submissions

12. The appellant's case is that the Tribunal erred in adopting the definition of interest as per the *Income Tax Act* and thus reached an erroneous decision. It based its argument on the basis that an Act of Parliament can only be applied to define a term in another Act only when the two Acts are of the same subject as per the doctrine on *pari materia*. Cited the case of *Raees -uz- zama & Anor v State NCT of Delhi* where the Court cited the four elements to be considered for two Acts to be in *pari materia*. The elements are as follows; "Acts which have a collective title, Acts required to be construed as one, Acts with short titles that are identical (apart from the calendar year), and other Acts which deal with the same subject matter on the same lines (Equal not Similar)."
13. The Commissioner bases its case on the provisions of the *Excise Duty Act* subject which subjects any charges to Excise duty, express laws are not made in vain and must be followed as they are specific and can't be applied interchangeably. Counsel relied on the case of *Cape Brandy syndicate -v- Inland Revenue Commission* [1920] 1KB Pg.240, where the Court held:-

"... in a taxing Act, one has to look merely at what is clearly said. There is no room for intendment as to a tax. Nothing is to be read in, nothing is 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 the subject is free, however apparently within the spirit of the law the case might otherwise appear to be."
14. In addition, the Commissioner urged the court to be guided by the principles of interpreting tax laws and to apply the literal meaning of interest to determine if the fees charged in late repayment of loans by borrower's amount to an interest in loans.
15. The Commissioner submitted that in the Absence of the definition of the word interest in the *Excise Duty Act*, the Tribunal ought to have adopted the meaning of the word interest as used in the Banking industry. In submitting what constitutes interest the Commissioner cited authorities: *Commissioner of Domestic Tax -v- National Bank of Kenya* [2022]eKLR, where the Court held:-

"from the foregoing it is crystal clear that interest is the compensation paid in consideration of using someone else money. or put differently, it is the consideration that is paid for keeping someone out of the use of his money. It is payable both when a lender lends money to a borrower and a lender takes a deposit from a depositor."
16. The Commissioner submitted the court ought to consider the definition as per the Banking Sector considering it is a very regulated sector. Citing the Supreme case in *Commissioner in GST and Central Exercise v M/s Citi Bank* N. A civil Appeal No.8228 of 2019 at paragraph 30 Pg.78 as per the holding of Lord Simmons in the case of *London and Eastern Co, v Berriman* [1946] 1 ALL ER 255 where it was stated:-

"it is only by reference to the industry that the meaning can be ascertained... it remains a question of evidence what the words mean in an industry."



17. The Commissioner submits the CBK guidelines defines “Interest” to mean:- “Loans and advances this covers interest income and

discounts on loans and advances including bills and notes discounted/purchased and interest in commercial paper and corporate bonds. Income interest should not include interest on non-performing loans and this should exclude fees, commissions and loans and advances.”

In addition, other income interests have been defined as:-

“ this represents other interest not captured above including income interest on repos. Income interest doubtful of recovery should not be recognized.”

18. The Commissioner submits that as per the above definitions, the interest charged by the Respondent for late repayment of loans cannot be taken to mean interest as per the definition of the Income Act excluded from tax. The Commission was proper in charging the Respondent excise duty for fees charged on late repayment of loans as the fees fell under the purview of other definitions of interest.

19. On the Second issue the Commissioner submits that additional interest levied for late repayment of loans by borrowers is subjected to excise duty as per Sections 5(1) B of the Excise Duty Act which deals with the Imposition of excise duty. 5 (1) subject to this Act, a tax, to be known as excise duty, shall be charged in accordance with the provisions of this Act on—

- a. excisable goods manufactured in Kenya by a licensed manufacturer;
- b. excisable services supplied in Kenya by a licensed person; or
- c. excisable goods imported into Kenya.

20. The Act further defines ‘others’ fees under Part III to mean:-

“includes any fees, charges or commissions charged by financial institutions relating to their licensed activities, but does not include interest on a loan or return on loan or any share of profit or an insurance premium or premium based or related commissions specified in the Insurance Act or regulations made thereunder;”

21. The Commissioner urged the court to find the fees to late payment as additional interest loan repayment is subject to excise duty having fallen within the meaning of fees in the CBK Prudential Guidelines. Interest income is Separate from other operating income, including fees and commissions on loans and advances.

22. It was submitted the Respondent failed to provide evidence to prove that the assessment was improper and maintained that the same was within the law.

23. In conclusion counsel urged the court to allow the appeal and find the Tribunal erred in holding that additional interests for late payment fall within the ambit of interest and are thus not subject to excise duty set the holding aside and substitute with an order that excise duty is chargeable on fees charged by the Respondent for late payment of loans. The commissioner urged the court to award the costs of the appeal.



Respondent's Submissions

24. The Respondent submits the Tribunal was proper in adopting the definition of interest as per the *Income Tax Act*. That ordinarily tax on income is charged pursuant to the provisions of the *Income Tax Act* and the *Excise duty* provisions do not regulate the payment of tax on interest on account of late payment of tax on interest.
25. The Respondent submits that tax obligation only arises when it is grounded on legislation. As per Provision of Article 209 (1) of the *Constitution* of Kenya 2010 which provides as follows:-
- Article 209 (1) only the National Government may impose:
- a. Income Tax,
 - b. Value Added Tax,
 - c. Customs Duties and other duties on imports and exports goods; and
 - d. Excise Tax.
26. The Respondent submits the point of departure is whether the tax obligation is legislated upon by the *Excise Duty Act* or the *Income Act*. The *Income Tax Act*, 2013 defines 'interest' as "Interest (other than interest charged on tax) means interest payable in any manner in respect of a loan, deposit, debt, claim or other right or obligation, and includes any premium or discount by way of interest and any commitment or service fee paid in respect of any loan or credit or an Islamic finance return."
27. The Respondent submits for interest to accrue there must be a principal, a higher interest rate is charged on the principal facility on account of default by the borrower, and the same cannot exist independently. Additional interest is not a fee that operates on its own as it is based on the principal amount, falls within the confines of Interest, and should be regulated by the *Income Tax Act* and not the *Excise Duty Act*.
28. The Respondent submits the Appellant's position that the additional interest arising on account of default by borrowers forms part of fees and excise duty is chargeable contradicts the law, as Interest is defined under the *Income Tax Act*.
29. According to the Respondent the appellant brought a case dealing with a tax obligation contained in the *Income Tax Act* and cannot fault the tribunal for excising its powers by relying on the definition of interest as provided in the Act.
30. The *Income Tax Act* is a tax statute which takes precedence over the Prudential Guidelines 2013 in matters dealing with payment of tax on interest. Relied on the case of *Zachariah Okoth Obado -v- Edward Akongó Oyugi and 2 others* SC Appl 7 of 2014: (2014) eKLR, where the court held:-
- "all statutes flow from the *constitution*, and all acts done have to be anchored in law and be constitutional, lest they be declared unconstitutional hence null and void."
31. The Respondent submits the appellant is inviting this court to legal instruments that do not regulate the imposition and payment of tax. It urged the court to uphold the definition of interest as contained in the *Income Tax Act*, of 2012.
32. The Respondent submits the *Excise Duty Act*, 2015 is clear on what goods and services are subject to the payment of excise duty under Section 5(1)(2) and Part III. The Definition of other fees as per the *Excise Duty Act* excludes interest or any returns made on loan and is not subject to excise duty. Relied



on the case of *Mount Kenya Bottlers Limited & 3 others v The Kenya Revenue Authority & 3 others* [2019] eKLR, where the Court of Appeal held as follows:-

“in our view there cannot be an equitable construction of income tax legislation. The norm is that taxing legislation must be construed with perfect strictness whether or not such construction is against the state if against the person sought to be taxed. If however there is any real ambiguity in a taxing Act, such ambiguity may be resolved in favour of the taxpayer in a taxing Act, such ambiguity may be resolved in favor of the taxpayer, or as it is sometimes stated *contra fiscum*.”

33. The Respondent submits attempts by the appellant to tax interest charged on late payment of loans under the *Excise Duty Act* amounts to double taxation contrary to the principles of Taxation and in violation of the *constitution*.
34. In conclusion the Respondent urged the court to find excise tax is not chargeable on additional interest accruing by virtue of default of the borrowers as it is not a fee but interest, dismiss the appeal and award costs to the Respondent.

Analysis and Determination

35. This being a first appeal, the Court is under a duty to re-evaluate the evidence presented before the Tribunal and make its own findings thereon; a principle well set in the case of *Selle v Associated Motor Boat Co.* [1968] EA 123 as follows:-

“An appeal to this Court from a trial by the High Court is by way of retrial and the principles upon which this court acts in such an appeal are well settled. Briefly put they are that this court must reconsider the evidence, evaluate it itself and draw its own conclusions though it should always bear in mind that it had neither seen nor heard the witnesses and should make due allowance in this respect. In particular, this court is not bound necessarily to follow the trial judge's findings of fact if it appears either that he has clearly failed on some point to take account of particular circumstances or possibilities materially to estimate the evidence or if the impression based on the demeanour of a witness is inconsistent with the evidence in the case generally (*Abdul Hameed Saif v Ali Mohamed Shalan* [1955], 22 EACA 270)” See also the case of *Jivanji v Sanyo Electrical Company Ltd.* [2003] KLR 425 at page 431.”

36. In due consideration of the appeal, the issue arising for determination is whether the tribunal erred in dismissing the assessment by the Appellant.
37. It is trite law that for an Authority to collect and charge taxes the imposition must be anchored under the law. As stipulated under Article 210(1) of the *Constitution* of Kenya which states; “No tax or licensing fee may be imposed, waived or varied except as provided by legislation.”
38. In the case of *Lab International (K) Ltd v. Kenya Revenue Authority* Misc. Appl. No.82 of 2010 and in the case of *Samura Engineering Limited and & Others v. Kenya Revenue Authority* HC Petition No.54 of 2011 [2012] eKLR where Majanja, J in Paragraph 58 emphasized 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 all times permeate its functions and activities which it is mandated to carry out of by statute.”



39. The Appellant submitted that the Respondent failed to pay excise duty on the fees charged for late payments by the defaulters. According to the Respondent, the fees collected from late payment of loans is not subject to excise duty as the same amounts to double taxation. The Respondent has contended that it paid taxes for the period in question save for the interest accrued from the late repayment of loan by defaulter.
40. In the case of *Republic v Kenya Revenue Authority Ex-parte Bata Shoe Company (Kenya) Limited* [2014] eKLR, where the Court expressed itself as hereunder:
- “This brings me to the role and interpretation of tax laws. Payment of tax is an obligation imposed by the law. It is not a voluntary activity. That being the case, a taxpayer is not obliged to pay a single coin more than is due to the taxman. The taxman on the other hand is entitled to collect up to the last coin that is due from a taxpayer.”
41. It is clear that under Section 5(1)(2) and Part III of the *Excise Duty Act*, 2015, goods and services subject to excise duty are elaborated. The Definition of other fees as per the *Excise Duty Act* excludes interest or any returns made on loan and is not subject to excise duty. In the absence of the definition of interest in the *Excise Duty Act*, the tribunal was correct in inferring to the definition as per the *Income Tax Act*.
42. In the circumstances, this Court is not persuaded that the Appellant has established that the Respondent ought to pay excise duty on the interest charge for late repayment of loans by borrowers.
43. In the case of *Mount Kenya Bottlers Limited & 3 Others v The Kenya Revenue Authority & 3 Others* [2019] eKLR, the Court of Appeal held as follows:
- “in our view there cannot be an equitable construction of income tax legislation. The norm is that taxing legislation must be construed with perfect strictness whether or not such construction is against the state if against the person sought to be taxed. If however there is any real ambiguity in a taxing Act, such ambiguity may be resolved in favour of the taxpayer in a taxing Act, such ambiguity may be resolved in favor of the taxpayer, or as it is sometimes stated *contra fiscum*.”
44. The upshot is the appeal is without merit and is dismissed, and the finding of the tribunal upheld.
45. Each party to bear its own costs.
46. It is so ordered.

JUDGMENT DELIVERED VIRTUALLY, DATED AND SIGNED AT KIAMBU THIS 14TH DAY OF JUNE , 2023.

D. O. CHEPKWONY

JUDGE

In the presence of:

Mr. Muturi holding brief for M/S Onyango for Appellant

M/S Odhiambo counsel for Respondent

Court Assistant – Mwenda Martin

