REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

CONSTITUTIONAL AND HUMAN RIGHTS DIVISION

PETITION NO.566 OF 2012

BETWEEN

CFC STANBIC BANK LTD.....PETITIONER

AND

THE KENYA REVENUE AUTHORITY.....1ST RESPONDENT

COMMISIONER OF DOMESTIC TAXES.....2ND RESPONDENT

JUDGMENT

Introduction

1. The Petitioner, CFC Stanbic Bank Ltd, is a limited Company licensed to operate a commercial bank in Kenya. It has filed this Petition alleging that the Respondents have deprived it of its property when it paid the principal tax total of Kshs.87,731,910/- and is in addition facing a claim in respect of penalties and interests of Kshs.51,987,891/- which amount the Petitioner contends that the Respondent should be restrained from demanding, as it is unlawful. It has also claimed that its right to fair administrative action and fair hearing had been violated as the 1st Respondent's Local Committee made no order to enjoin third parties pursuant to the provisions of **Section 89(3)(d)** of the **Income Tax Act** and thus its decision cannot have the force of law as against third parties that were never enjoined to the proceedings of the Local Committee.

2. In its Amended Petition dated 10th December 2012 and supported by the Affidavit sworn on 14th January 2013 by one, Kenneth Kanyarati, its Head of Legal and Compliance with the Petitioner seeks the following orders;

"a) A Declaration that the payment by the Petitioner of Kshs.87,731,910/- and the resultant penalties and interest of Kshs.51,987,891/- or such higher sum that may accrue was unlawful, null and void ab initio and the amounts are not payable.

b) A Declaration that the Respondent's reliance on the decision of the local tax committee dated 24th March 2011 to apply retrospectively and affect the Petitioner who was not party to appeal when the tax law regime was ambiguous, was contrary to the rules of natural justice, contravened the fundamental rights to the petitioner's rights to property and imposed an illegal tax obligation.(sic)

c) An Order of Certiorari be issued to remove into the High Court and quash the prior assessment on 2011 as regards software costs, penalties and interest prior to 1st January 2010 that caused the payment of Kshs.87,731,910/- and only that part of the decision and order of the 2nd Respondent's letter dated 14th November 2012 demanding penalties and interest of Kshs.51,987,891/- or any sum over and above this. (sic)

d) An Order of Prohibition be issued to prohibit the Respondents from demanding penalties and interest on the corporation tax assessed in respect of software costs for the periods prior to 1st January 2010.

e) An Order that the sum be paid back to the Petitioner by the Respondents with interest at 18.42% per annum at the bank's commercial rates with effect from 14th January 2013 until payment in full together with costs of the Amended Petition on the higher scale."

Factual Background

3. The facts leading to this Petition as I understand them are as follows;

4. Following the merger of the CFC and Stanbic Banks, the new banking entity styled and named CFC Stanbic *(the Petitioner herein)* acquired a core banking system worth Kshs.347,358,000/- in 2008. In the same year the Petitioner bank acquired other software worth Kshs.156,716,000. All these were capitalised as intangibles in the Petitioner's published financial statements. The Petitioner also acquired new core banking software in 2009 worth Kshs.760, 507,000.

5. For the additions of the two softwares in the two years, the Petitioner claimed in its tax computations, diminution in value of software amounting to Kshs.102,290,262/- and Kshs.356,885,695/- in 2008 and 2009 respectively.

6. Sometimes in 2011, the 1st Respondent conducted an audit of the tax affairs of the Petitioner for the periods 2008 and 2009. There were discussions between the Petitioner and the 1st Respondent and the final principal tax amount of Kshs.288,682,059/- was agreed upon and was paid by the Petitioner. On 26th May 2011, a payment of Kshs.103,161, 865/- was paid to the Respondent which amount included the sum of Kshs.87,731,910/- in respect of excess claim on software under **Section 15(2) (g)** of the **Income Tax Act.**

7. Among the areas of non-compliance by the Petitioner identified by the Respondents in its tax audit were the deduction of software costs which in the Respondents' view should have been at the rate of 12.5% for periods prior to 1st January 2010 but the Petitioner had made a deduction claim under **Section 15(2)(g)** at the rate of 33.3% for that period. The Respondents' deduction at the rate of 12.5% had been based on the Nairobi Income Tax Local Committee's decision of 24th March 2011 and the Petitioner claimed that it was not a party to the appeal lodged at the said Local Committee by the Standard Chartered Bank Kenya Ltd and therefore its decision could not be binding on it and could also not be used against it.

The Petitioner's case

8. The Petitioner claims that its legitimate expectation to continue paying the rate of 33.3% for the periods 2008 and 2009 was sound since the law in that period was ambiguous. Subsequently, that the law was clarified by the **Finance Act** of **2009** which introduced 20% deduction claim from 1st January 2010 and it is on this basis that the Petitioner claims that it is entitled to a refund of Kshs. 113,986,729.64/- for the overpayment it allegedly made to the Respondents.

9. The Petitioner also contends that the Respondents violated **Article 47** of the **Constitution** which sets out the requirements on fair administrative justice, by locking out all other banks in proceedings before the Nairobi Local Income Tax Committee and failing to enjoin the Kenya Bankers Association in the matter but later imposed the decision of the Local Committee on all of

them. It contends therefore that the Local Committee decision is not binding on the Petitioner because it was a decision in *personum* and it breached the rules of natural justice. It relies on the case of ***Kenafric Industries Ltd v Commissioner of Domestic Taxes & 4 Others (2012) e KLR*** where it was held that administrative processes are to be measured against the standards established under the Constitution.

10. It is the further submission of the Petitioner that the decision of the Local Committee also contravened the Petitioner's rights to property as stipulated under **Article 40** and also violated principles governing imposition of taxes as stipulated under **Article 210** of the **Constitution.**

11. With regard to the right to property, it is the Petitioner's argument that the Respondents have used the decision of the Local Committee to deprive it of its property contrary to the spirit of the **Income Tax Act** prior to the amendments in the **Finance Act, 2009**. It relies on the case of ***Ramsay Ltd v Inland Revenue Commissioner (1992) AC 300*** where the Court held that a subject should not be taxed where there are clear words of the tax obligation and not upon intendment or upon the equity of an Act. The case of C***ommissioner of Income Tax v Westmont Power (K) Ltd Nairobi Income Tax Appeal No. 626 of 2002*** where the High Court held that taxation laws must be clear of ambiguity and where there is ambiguity, the law should be interpreted in favour of the taxpayer and not the taxing authority. Reliance is also placed on the case o***f J. Astaphan & Co Ltd v Comptroller of Customs and Another (1999) 2 LRC 569*** where the Court of Appeal of Dominica considered protection against the compulsory acquisition of property by customs official and the legality of such an action.

12. The Petitioner contends that the **Finance Act** of **2009** introduced **Regulation 31B** to the **2nd Schedule** of the **Income Tax Act,** which regulation cannot apply retrospectively. It claims that in a business environment, certainty and predictability is crucial and denying a business entity those conditions amounts to a denial of an economic right. It referred the Court to the case of ***Keroche Industries Ltd v Kenya Revenue Authority (2007) e KLR*** where Nyamu J. addressed comprehensively the principles of taxation. I will revert to those principles enumerated in that decision later in this judgment.

13. It is therefore the Petitioner's claim that where ambiguities exist in tax law, the same must be construed in favour of the tax payer. It also claims that while addressing the issue of software costs, the Respondents were either entitled to classify the software costs firstly, under class IV of paragraph 7 of the Second Schedule of the Income Tax Act and claim at the rate of 12.5% on the basis that software being a cost of capital in nature which is used in business operations and whose life will span several years qualified as a plant. And secondly, the same could be classified in the computer's category since software cannot be used without computer hardware and therefore it would be justifiable for it to be categorized with computers under Class III of paragraph 7 of the Second Schedule and then a user can claim wear and tear at the rate of 30%, or follow the accounting treatment adopted by the Petitioner which is guided by International Financial Reporting Standards and lastly, a claim could also be made for wear and tear under **Section 15(2) (g)** of the **Income Tax Act** which covers all tools, utensils or articles which are not plant and machinery at the rate of 33.3%. And that the Petitioner actually claimed wear and tear under this latter heading and properly so, according to it.

14. It is therefore the Petitioner's claim that it is entitled to a refund of Kshs.113,986,729.64/- together with interest at 18.42% per annum at the Petitioner's commercial rates. It relies on the case of ***Woolwich Equitable Building Society v Inland Revenue Commissioner (1992) 3 WLR 366,*** where the House of Lords held that money exacted as taxes from a tax payer by the State Revenue Authority and which exaction was *ultra vires* is recoverable by the citizen as of right. It therefore prays for judgment to be entered as prayed in the Amended Petition together with costs.

Respondent's case

15. The 1st Respondent, Kenya Revenue Authority, and the 2nd Respondent, The Commissioner of

Domestic Taxes, oppose the Petition. In response to the Amended Petition, they filed a Replying Affidavit sworn on 22nd February 2013 by Rose Wasinda, the Assistant Commissioner in the Large Tax Payer's Office of the Domestic Taxes Department. They also filed written Submissions.

16. The crux of the Respondent's case is that; the Petitioner voluntarily agreed to pay tax on excess capital deduction claimed on software. And that the Petitioner was represented at all discussion on the subject by its senior officials, including officials from its parent company in South Africa. That its tax agents were also present at the discussions and meetings of audit findings conducted on the Petitioner on which the decisions to charge the Petitioner the tax were made. And that all parties, including the Petitioner's tax agents, agreed with the audit after a formal additional assessment as provided under **Section 77** of the **Income Tax Act** was issued. Further, that the Petitioner did not in any of their letters to the Respondents raise any objections under **Section 84** of the **Income Tax Act** to the 1st Respondent's decision to tax them according to the decision of the Local Committee pursuant to the provisions of Paragraph 7(3) (d) of the Second Schedule of the Income Tax Act.

17. It is also their contention that the Petitioner voluntarily agreed to pay the tax dues as assessed even before the 1st Respondent had reached the stage of taking any enforcement measures towards the collection of the amount due and it cannot now be heard, and is estopped from saying, that the Respondents acted unlawfully in any way.

18. It is the Respondents' further Submissions that the treatment of software for capital deduction purposes was a major tax audit issue in the banking sector prior to the enactment of Paragraph 31B of the Second Schedule to the Income Tax Act which became effective in 2010. Before that, different taxpayers, depending on the tax agents dealing with the tax computations treated software differently according to their own interpretations. That for instance, some tax payers claimed diminution under **Section 15(2)(g)** of **Income Tax Act**, while others claimed the same under the wear and tear allowance allowed under Class II of Paragraph 7 to the Second Schedule, which provides for 30% for deductions in respect of capital expenditure on machinery for wear and tear. That other tax payers did not claim any allowances on software at all.

19. It is the Respondents' position that on a strict interpretation of the law, at all material times the software neither qualified for diminution under **Section 15(2)(g)** of the Act nor for wear and tear allowance under the Second Schedule to the Income Tax Act and the Respondent disallowed the entire amount claimed by the banks on the premise that prior to 2010, the Income Tax Act did not have any specific provisions allowing capital deductions on computer software.

20. It submitts that as a result of the lacuna in the law, the Respondents successfully advocated for the amendment of the Act and thereafter under the Second Schedule, Part VI-Miscellaneous Provisions of the **Income Tax Act, Section 31B** was introduced in 2010. They claim that the fact that the amendment was made under the 2nd Schedule demonstrates that the treatment of tax for software ought to be in that area and not **Section 15(2) (g).**

21. They claim that if at all there were ambiguities in the law, the Local Committee was able to establish an interpretation that was most favourable to the Petitioners since in arriving at its decision, it had been guided by **Section 32(1)** of the **Second Schedule** of the **Income Tax Act** which defines 'machinery'.

22. They claim that M/s Deloitte and Touche represented the Petitioner in the Local Committee proceedings and it held the position later adopted by the Local Committee as was demonstrated by Annexture RW6, where they advanced the argument of the Petitioner being taxed under class II of paragraph 7 to the second schedule of the Income Tax Act and that was the argument upheld by the Local Committee.

23. It is their Submission that the first case on the issue was decided by the Local Committee sitting in Nairobi on 11th November 2010 involving EcoBank Kenya Ltd and the Local Committee decided

that software should be treated as 'other machinery' qualifying for wear and tear at 12.5% under class IV **Section 7(3)(d)** of the **second schedule** of the **Income Tax Act**. That none of the banks appealed against the decision and the Local Committee reaffirmed its decision in subsequent appeals.

24. On the allegation that the Respondents illegally acquired the Petitioner's property, the Respondents submitted that the Petitioner had voluntarily agreed to pay the tax in issue raised in the exit meeting, and that the 1st Respondent had not even reached the enforcement stage by the time the payment was made. And it exhibited emails that showed that the Petitioner had willingly agreed to pay the requisite taxes on wear and tear diminution at the percentage demanded by the Respondent.

25. That since the Petitioner did not at any point raise a formal objection in terms of **Section 84** of the **Income Tax Act** its claim was belated and that the aggrieved party is the one that moves the Committee and the Petitioner was at liberty to move the Local Committee to be enjoined to the other bank's proceedings but did not do so. And that in any case, **Section 89(3) (d)** of the **Income Tax Act** provides that the Local Committee may enjoin other parties if it so considers and is their submission therefore that the Petitioners were not locked out of the Proceedings, but instead they waived their right to utilise the legal channels provided under the Income Tax Act.

26. It is the further submission of the Respondents that pursuant to the provisions of **Article 210** of the **Constitution**, no tax or licensing fee may be waived or varied except as provided by legislation and accordingly, penalties could not be waived in the absence of consent by the Minister. That the Petitioner indeed applied for a waiver as it was its right by letter dated 5th August 2011 but the Minister declined to grant the waiver by his letter dated 31st October 2012 and that information was conveyed to the Petitioner. It was therefore the Respondents' submission that waiver of taxes is at the discretion of the Minister and further that a waiver cannot be granted on penalties and interests unless the principal tax sum had been paid.

27. On the principle of legitimate expectation, it is the Respondents' contention that the same does not arise in the instant case because the interpretation of the legal provisions was in dispute and so there was no regular practice that the Petitioner could rely on to sustain any legitimate expectation. They rely in that regard on the case of ***Ecobank Kenya Ltd v The Commissioner Domestic Taxes HCCC No. 8 of 2010.*** It was their further submission that the Respondents have treated all banks and industries in the matter equally and in any event that the Petition herein is an after thought and the Petitioner only filed it upon realizing that the question of penalties and interest due from it had not been concluded and has used the Petition to allege dissatisfaction with the entire agreement, despite having willingly paid all taxes due. That the Petitioner even went further in its self assessment returns for the years 2010 and 2011 and applied the treatment of software acquired prior to January 2010 at the rate of 12.5% which was according to the Local Committee ruling and that the current tax agents of the Petitioner, M/s Ernest and Young, have also advised the Petitioner to pay taxes according to the Local Committee ruling which reinforces the argument that the Petition is an abuse of Court process.

28. On the issue of retrospective application of the law relating to taxes, the Respondents contend that an assessment may be made under the Act at any time prior to seven years after the year of income to which the assessment relates and so the argument to the contrary is misguided. In conclusion, the Respondents have urged this Court to dismiss the Petition with costs.

Determination

29. Having set out the parties' contention as above, certain facts are indisputable. First, prior to 2010, there was a lacuna in the law on the question of assessment of capital deductions on computer software and many taxpayers treated software differently according to their own interpretation of that law. The Petitioner during the 2008/2009 period of assessment claimed diminution on software under **Section 15(2) (g)** of the **Income Tax** at the rate of 33.3%. The Respondent was not

in agreement with that interpretation and referred the matter to the Income Tax Local Committee which in its decision of 24th March 2011 applied the term 'software' to the wider definition of the word 'plant' which falls under the wider term, and 'machinery.' That software was to qualify for wear and tear at 12.5% under **Class IV Section 7(3) (d)** of the **2nd Schedule** of the **Income Tax Act.** It is this decision of the Local Committee that the Petitioner claims has violated its right to fair administrative action and the right to property as neither the Petitioner nor the Kenya Bankers Association had been enjoined at the hearings of the Local Committee and also that the decision was made to apply retrospectively to all banks including itself.

30. In my view therefore, the issue for determination is whether the assessment made by the Respondents has in any way violated the Petitioner's rights as alleged. In determining that issue I will consider whether the assessment made is retrospective and also the effect of failure to be enjoined in the proceedings as alleged by the Petitioner.

Retrospective application of the Local Committee's decision of 24th March 2011

31. All the parties are in agreement that prior to January 2010, the Law was ambiguous and that the audit on the Petitioner's computer software was carried out between February and March, 2011. It is the Petitioner's contention that the Respondents applied the decision of the Local Committee retrospectively and on their part, the Respondents contend that under **Section 79** of the **Income Tax Act,** an assessment may be made under the Act at any time prior to seven years of the year of income to which the assessment relates.

32. It is clear that the treatment of software for capital deduction purposes was a major tax audit issue in the banking sector prior to the enactment of Paragraph 31B of the Second Schedule to the Income Tax Act. During the ambiguity period, different tax payers treated software differently. For instance, some claimed diminution under **Section 15(2) (g)** of the **Income Tax Act** while others claimed wear and tear allowance under Class II of Paragraph 7 to the Second Schedule and others did not claim any allowances at all. The Respondents' position was that software neither qualified for diminution under **Section 15(2)(g)** nor for wear and tear allowances under the second schedule.

33. **Section 15(2) (g)** of the **Income Tax Act** provided as follows;

> ***"The amount considered by the Commissioner to be just and reasonable as representing the diminution in value of any implement, utensil or similar article, not being machinery or plant in respect of which a deduction may be made under the Second Schedule, employed in the production of gains or profits".***

It was against this provision that the Respondents disallowed the entire amount claimed by the Petitioners on the ground that the Income Tax Act did not allow capital deduction on computer software.

34. The issue of Computer software was then settled on 25th November 2010 by the Income Tax Local Committee which held that;

> ***"Software should be treated as other machinery and therefore subject to a 12.5% annual tear and wear deduction".***

However this decision was made out of an appeal filed by another bank and not the Petitioner.

35. Subsequently, **Section 31B** of the **Second Schedule, Part VI** was introduced in 2010 and it states as follows;

> ***"Subject to this Schedule, where a person incurs capital expenditure on the purchase or acquisition of the right to the use of a computer software, there shall be deducted,***

in computing his gains or profits for the year of income in which the software is first used and for subsequent years of income, an amount equal to one-fifth of that expenditure."

The effect of this amendment therefore meant that **Section 15(2)(g)** aforesaid was not applicable as the ambiguity in it had been cleared.

36.In ***Ramsay Ltd v Inland Revenue Commissioner (1992)AC 300*** the Court stated as follows;

> ***"A subject is only to be taxed on clear words not upon intendment, or upon the "equity" of an "Act". Any taxing Act of parliament has to be construed in accordance with this principle. What are "clear words" is to be ascertained upon normal principles; these do not confine the Courts to literal interpretation. There may, indeed should, be considered the context and scheme of the relevant Act as a whole and its purpose may, indeed should be regarded ..." …...A subject is entitled to arrange his affairs so as to reduce his liability to tax. The fact that the motive for a transaction may be to avoid tax does not invalidate it unless a particular enactment so provides. It must be considered according to its legal effect."***

37.In that regard, the issue therefore is whether the Respondents can then use the provisions of **Section 31B** to the **Second Schedule** of the Income Tax Act in tax assessment of the Petitioner for the prior years of 2008 and 2009 and if not what law was applicable.

38.The conceptual basis for the law on retroactivity and the need to regulate human activities has been well set, in my view, in the American case of ***Hurtado v California 110 US 51-0535-36 (1884)*** where the Court stated as follows;

> ***"Law is something more than mere will exerted as an act of power. It must not be a special rule for a particular person on a particular case but … the general law ..." so that every citizen shall hold his life, liberty, property and immunities under the protection of this general rules which govern society, and this excluding as not due process of law acts of attainder, bill of pains and penalties acts of confiscation ..."and other similar special, partial and arbitrary exertion of power under the forms of legislation. Arbitrary power, enforcing edicts to the injury of the persons and property of its subjects is not law, whether manifested as the decree of a personal monarch or an impersonal multitude."***

39.On that point, I will add that one of the ingredients of the rule of law is certainty of law. This is an important pillar of law that has been recognised by our Constitution. No one, including the taxman, should be allowed to violate this cardinal principle. This principle was also recognised in the Jamaican case of ***Philips v Erye (1870) LR QB 1 Exchequer Chamber*** in the following words;

> ***"Retrospective laws are no doubt prima facie of questionable policy an contrary to the general principle that legislation by which the conduct of mankind is to be regulated ought, when introduced for the first time, to deal with future acts and ought not to change he character of past transactions carried on upon the faith of the then existing law. Accordingly, the Court will not ascribe retrospective force to new laws affecting rights unless by express words or necessary implication it appears that such was the intention of the legislature."***

In the ***Keroche Industries case (supra)*** Nyamu J. stated as follows;

> ***"Imposing another tariff retrospectively is punitive and our Courts ought to frown upon any such practice because the effect of such imposition is the same as retroactive laws. A change of tariff just like most laws must be prospective to be fair."***

40. I am generally in agreement with the law as expressed by the learned judges and I note that **Section 31B** as reproduced elsewhere above was enacted by the **Finance Act NO. 8** of **2009** and it came into force on 1st January 2010. It therefore follows that it cannot be used retrospectively in assessing the tax payable by the Petitioners. Having so said however, I have not seen any evidence that the assessment for 2008/2009 was done in accordance with **Section 31 B** and to that extent the Petitioner cannot benefit from the general expression of the law above.

41. But that is not the end of the matter because the Respondents contend that the provisions of **Section 79** of the **Income Tax Act** allows tax assessment to be made at any time prior to seven years of the year of income to which that assessment relates. This section provides as follows;

"(1) An assessment may be made under this Act at any time prior to the expiry of seven years after the year of income to which the assessment relates, but-

(a) where fraud or gross or willful neglect has been committed by or on behalf of a person in connexion with or in relation to tax for a year of income, an assessment in relation to that year of income may be made at any time.

(b) in the case of income consisting of gains or profit from employment or services rendered, an assessment in relation thereto may be made at any time prior to the expiry of seven years after the year of income in which the gains or profits are received.

(c) in any case to which the proviso to paragraph (d) of Section 4 or paragraph 21 of the Second Schedule applies, an assessment in relation thereto may be made at any time prior to the expiry of seven years after the year of income in which the circumstances which gave rise to the assessment occurred.

(d) in the case of an assessment made upon the executors or administrators of a deceased person, the assessment shall be made prior to the expiry of three years after the year of income in which that deceased person died.

(2) The question whether an assessment has been made after the time set in this Section for the making thereof shall be raised only on an objection made under Section 84 and on any appeal consequent thereon."

A casual look at **Section 79 (c)** reveals that the assessments to be made prior to expiry of seven years are those relating to the items listed under **Section 4** of the **Act** and paragraph 21 of the Second Schedule. **Section 4** deals with income from businesses and paragraph 21 deals with sums received by vendors and treated as trading receipt. To my mind therefore, the law is very clear that only those items listed under **Section 4** and paragraph 21 of the second schedule can be assessed before the expiry of seven years. Had the law intended that all taxable items or deductions should be assessed at any time before the expiry of seven years, then I think nothing would have been easier than for the law to state so. It therefore follows that the interpretation given by the Respondents is improper. In so holding, I find support in the words expressed by Nyamu J. in ***Keroche Industries Case (Supra)*** as follows;

> ***"There is no enabling law which permits the backdating of the changed tariff (even assuming for a moment that it was proper to change it). This violates statutory provisions such as Sections 137, 91 and 218A of the Customs 7 Excise Act. Any backdating or retrospective application violates the rule of law. Certainty of law is an ingredient of the rule of law upon which our system of justice is anchored. A change to tariff 22.06 would also fail for these reasons. Retrospective application is unreasonable, irrational, oppressive, biased, discriminatory, male fides, unfair, arbitrary, procedurally improper and is an abuse of power. It is also lacking in proportionality. The retrospective laws, except where specifically allowed by the legislature, are generally frowned upon as a matter of policy."***

I am in total agreement and would adopt the above holding in the context of the present Petition and further, while in agreement that generally a law cannot be applied retroactively, in the instant case, there is no evidence whatsoever that the Respondent applied any aspects of the Income Tax Act retroactively and to the prejudice of the Petitioner and I so find.

Right to property

42. Having held as above, I must determine the law applicable at the assessment period (2008/2009). To determine that issue, I will recall that the law was ambiguous at the time and it was not clear on the treatment of computer software.

43. The Respondents have maintained that at all times, software was neither qualified for diminution under **Section 15(2) (g)** nor for wear and tear allowance under the Second Schedule as claimed by the Respondents. In that regard **Section 16(1)** of **Income Tax Act** provides as follows;

> ***"(1) Save as otherwise expressly provided, for purposes of ascertaining the total income of a person for a year of income, no deduction shall be allowed in respect of-***
>
> ***(a) expenditure or loss which is not wholly and exclusively incurred by him in the production of the income.***
>
> ***(b) capital expenditure, or any loss, diminution or exhaustion of capital."***

44. In that context, did the Respondents therefore violate the Petitioner's right to property? A literal reading of the above section demonstrates that a taxpayer cannot claim a deduction of capital expenditure or any loss or diminution or exhaustion of capital except where it is expressly provided in the Income Tax Act and yet the Income Tax Act did not have any specific provision allowing capital deductions in the case of computer software.

45. The facts show that because the law was unclear in that regard most of the banks that had been audited raised objections under **Section 84** of the **Act**. They eventually applied for a decision of the Local Committee when the Respondents decided against their objections. The Petitioner was not one of the banks that objected. The Respondents had infact conducted an audit on the Petitioner bank tax affairs for the period 2008 and 2009 on Corporation tax and in June 2008 to March 2011 on PAYE, withholding Income Tax and VAT. The final audit report dated 30th June 2011 was annexed as Annexture RW1. At page 7 of that audit report, it is stated that at the conclusion of the Audit, the Petitioners had agreed on the principal tax settled upon and willingly agreed to pay the taxes as evidenced in exhibit RW 2. I have seen the email dated 25th May 2011 from one Mwihia Beatrice an employee of the Petitioner, to the Respondents and which states as follows;

> ***"We will be making the payment of Kshs.202,576,708/- tomorrow by RTGS and I will send you a swift copy of the payment'***

46. That email had been as a result of various negotiations that had been held between the Petitioner and the Respondents on the issue of reaching an amicable settlement of the tax payable. It is therefore not true that the Petitioners were forced to pay the tax by the Respondents.The Respondents did not even reach the enforcement step towards the collection of that amount. The payment was made after the Petitioner had been informed of the position that the Respondents had taken with regard to computer software and its wear and tear. Indeed the email of 17th June 2011 demonstrates that the issue of computer software, wear and tear was never an issue. This email read as follows;

"Mr. Achieng,

"Further to our various email correspondence resting with your last one here below, we have

had discussions and agreed on the following;

1. The only contentious issue is VAT assessed on reposed collateral. This being a technical we have had in-depth and lengthy discussion in our past meetings as well articulated by John Gikima.

2. The above notwithstanding and in view of where we have come from and in a bid to conclude and close this matter wish finality, the bank will settle the balance of 88 Million"

Kind regards

Peter."

46. The Petitioner now contends that the payment of the taxes was made under mistake of law and the same violates their right to property. **Article 40** of the **Constitution** provides the right to property as follows;

"(1) Subject to Article 65, every person has the right, either individually or in association with others, to acquire and own property.

(a) of any description; and

(b) in any part of Kenya.

(2) Parliament shall not enact a law that permits the State or any person—

(a) to arbitrarily deprive a person of property of any description or of any interest in, or right over, any property of any description; or

(b) to limit, or in any way restrict the enjoyment of any right under this Article on the basis of any of the grounds specified or contemplated in Article 27 (4).

(3) The State shall not deprive a person of property of any description, or of any interest in, or right over, property of any description, unless the deprivation—

(a) results from an acquisition of land or an interest in land or a conversion of an interest in land, or title to land, in accordance with Chapter Five; or

(b) is for a public purpose or in the public interest and is carried out in accordance with this Constitution and any Act of Parliament that—

(i) requires prompt payment in full, of just compensation to the person; and

(ii) allows any person who has an interest in, or right over, that property a right of access to a court of law.

(4) Provision may be made for compensation to be paid to occupants in good faith of land acquired under clause (3) who may not hold title to the land.

(5) The State shall support, promote and protect the intellectual property rights of the people of Kenya.

(6) The rights under this Article do not extend to any property that has been found to have been unlawfully acquired. "

47. The above being the law, to my mind, the parties herein had extensively engaged in lengthy

discussion over the payment of taxes due and I do not see how the taxation of the Petitioner deprived it of its property because it paid the assessed and agreed taxes willingly following a decision of the Local Committee on the matter.

48. But suppose am wrong? Then I would still arrive at the same decision given the fact that the Petitioner never raised any objection to the assessment as provided by the law in terms of **Section 84** of the **Income Tax Act** whereby a person who disputes an assessment made upon him must raise an objection by notice in writing to the Commissioner object the assessment. **Section 84(1)** states as follows;

> ***"A person who disputes an assessment made upon him under this Act may, by notice in writing to the Commissioner, object to the assessment."***

The Petitioner never made such an objection as prescribed by law and having failed to object, to my mind the Petitioner is entitled to pay the assessed tax. The **Constitution** at **Article 210(1)** bears me out. It states as follows;

> ***"(1) No tax or licensing fee may be imposed, waived or varied except as provided by legislation."***

49. The legislation is the Income Tax Act and such taxes as are by the Respondents and as it can be seen, it is the duty of every person to pay such taxes as are assessed by the Respondents and I do not see how any such payment may violate a person's rights unless the assessment is draconian and has not been done in accordance with the law.

In any event, **Article 210(2)** empowers the Petitioner to apply for a waiver or variation of the tax. The Petitioner applied for such waiver or variation through its letter dated 5th August 2011 which was produced as annexture RW8 and the Minister declined to grant the waiver by his letter dated 31st October 2012. The payment and collection of taxes is a public interest matter and the Respondents have the statutory obligation under **Article 209** of the **Constitution** to assess and collect taxes on behalf of the national government.

<u>Right to fair Administrative Action</u>

50. It is the Petitioner's contention that the Respondents relied on the decision of the Local Committee to asses taxes on all persons including those that were not party to the appeal before the Committee. **Section 89(3)** states as follows;

> ***"(3) Where an appeal is brought under subsection (1) against a decision or act of the Commissioner which affects, or is likely to affect, the income of more than one person-***
>
> ***(a) where the same local committee has jurisdiction with respect to all the persons concerned, the appeal shall be heard by that local committee;***
>
> ***(b) where different local committees have jurisdiction with respect to the persons concerned, the appeal shall be heard by such one of those local committees as may be agreed upon by those persons or, in default of agreement, by the local committee having jurisdiction in relation to the person who first lodges and appeal;***
>
> ***(c) a person lodging an appeal shall serve a copy of all the appeal documents on all other affected persons who shall be entitled to appear on the appeal as if they were parties thereto;***
>
> ***(d) if the local committee before which an appeal is heard considers that any other person should be joined, it may order that a copy of all the appeal documents shall be served on that other person who shall be entitled to appear on the appeal as if he were a***

party thereto."

51. The above shows that there were many channels which were available to the Petitioner to be enjoined in the Local Committee proceedings to protect it interests. However, as stated elsewhere above, the decision of the Local Committee was reached on 25th November 2010 and the **Finance Act No. 8** of **2009** came into effect on 1st January 2010. Clearly, the law had since been clarified under **Section 31B** of the **Second Schedule** and it no longer mattered what the decision of the Local Committee was. I therefore find that the Petitioner has not demonstrated how its right to fair administrative action under **Article 47** of the **Constitution** were violated and I so declare.

52. On the allegation that the Petitioner's legitimate expectation was violated, my mind is clear that legitimate expectation does not arise in ambiguous situations. In ***R (Bibi) v Newham London Borough Councl, (1986) AC 1*** Schieman LJ gave a set of three practical questions for the Court to pose in ascertaining whether a claim based on legitimate expectation is properly grounded and these are as follows;

(i) What has the public authority, whether by practice or by promise committed itself to,

(ii) Whether the authority has acted or proposes to act unlawfully in relation to its commitment,

(iii) What should the Court do?

53. As already stated elsewhere in this judgment, the position before 1st January 2010 with regard to computer software was ambiguous. Different tax payers treated the issue differently and the Respondents also treated the issue differently. It appears that a consensus was always somehow reached as between the taxpayer and the tax man in different circumstances. That being so, I do not think that there was a general set practice that the Petitioner can use to claim legitimate expectation. And that is all there is to say with respect to that issue in this Petition.

Conclusion

54. I have endevoured to show that the Petitioner willingly paid an agreed sum as taxes and after seeking and getting professional advise from its tax consultants, it has not been shown that the Respondent in any way coerced or forced the Petitioner to do so. The payments were paid based on an agreed interpretation of the law. The Petitioner has not shown why that interpretation is faulty and why the decision of the Local Committee on the subject was wrong and why other banks including Standard Chartered Bank and Ecobank should have paid the taxes based on that interpretation and that it should, at a later date, be exempted from payments based on that interpretation. Give unto Ceaser what belongs to Ceasar and so it shall be.

55. For all the reasons given above, it follows that the Petition before me lacks merit and must be dismissed.

56. As to costs, there is not doubt that the Petition was filed with mischief and so the Petitioner shall pay the costs thereof.

57. Orders accordingly.

DATED, DELIVERED AND SIGNED AT NAIROBI THIS 7TH DAY OF MARCH, 2014

ISAAC LENAOLA

JUDGE

In the presence of:

Irene – Court clerk

Miss Lavuna for Respondent

No appearance for Petitioner

Order

Judgment duly read.

ISAAC LENAOLA

JUDGE