COMMISSIONER OF DOMESTIC TAXES..APPELLANT

VERSUS

STANDARD CHARTERED (K) LIMITED..RESPONDENT

J U D G ME N T

In or about 2000, the Respondent took out a Group Life Assurance and Dread Disease Benefit Policy (hereinafter "the policy") for its employees. Under that policy the lives assured was that of the Respondent's Eligible Employees whilst the amounts of benefits under the policy was payable to the policy holder. The Respondent paid premiums for the said policy which for the period 2005-2008 totalled Kshs.59,846,748/-

In the year 2009, the Appellant carried out in-depth audit of the Respondent's business for the period 2005 and 2008 and disallowed certain expenses incurred by the Respondent including that of the premiums paid by the Respondent on the policy. The Appellant issued additional assessment notices for the respective years for additional tax which together with penulty and interest amounted to Kshs.35,087,652/-.   The Appellant demanded payment of this sum. The Respondent was aggrieved and lodged an appeal with the Nairobi Income Tax Local Committee (hereinafter "the Local Committee"). In its decision made on 24th March, 2011, the Local Committee held that the benefit under the policy was not the benefit envisaged under Section 5(2) (f) of the Income Tax since the employees cannot enforce that benefit during their lifetime. The committee therefore allowed the Respondent's Appeal on that issue.

Being aggrieved by that decision, the Appellant has appealed to this court against that decision on the grounds that:-

1. The Local Committee erred in holding that the Group Life Insurance Scheme was for the Respondents benefit and therefore not a taxable benefit in the employees hands.

2. The Local Committee erred in failing to hold that the premiums paid by the Respondent on behalf of its employees under the policy was a gain chargeable under Section 5(2)(f) of the Income Tax Act Chapter 470 Laws of Kenya (hereinafter "the Act")

3. That the Local Committee erred in failing to note that under the policy the beneficiaries thereon are the Respondents employees, and

4. Finally that the Local Committee erred in freeing the Respondent from tax obligation on the insurance benefit yet the same was not paid to any pension scheme or as excepted under Section 5 of the Act.

The Appellant contended that a group life insurance is used to provide cost effective insurance benefit to members of a defined group, that in this instance the insurer was the British American Insurance Company (K) Ltd and the policy was held by the Respondent. Referring to the clauses of the policy, the Appellant contended that the claimant was an employee under the policy, that benefit accrued to the

employees although the premium was paid by the Respondent. That the group life insurance was a benefit/advantage/privilege that was taxable. It was further contended that under Section 5(2) (f) of the Act, the premium paid by the Respondent, for the life of its employees was a gain or profit in respect of which tax was chargeable.

For the Defendant, it was contended that Section 5(2) (f) applies to a premium paid for an insurance on the life of an employee or his dependent, that the policy in issue was a policy for eligible employees for the benefit of an employee of his dependant, that the policy in issue was a policy for eligible employees for the benefit of the Respondent, that under the policy neither the employees nor their dependants could make a direct claim to any benefit under the policy. That this was a policy taken to cover the Respondent as an employer for any financial exposure to eligible employees and it was therefore outside the provisions of Section 5(2) (f) of the Act.

To my mind, the issue for determination is whether the Local Committee properly applied the provisions of Section 5(2)(f) of the Act to the facts of this case. Section 5 (2) (f) of the Act provides:-

"2. For the purposes of Section 3(2) (a) (ii), "gains or profits" includes:-

(f) an amount paid by a employer as <u>a premium for an insurance on the life of his employee (and) for the benefit of that employee or any of his dependants</u> other than such an amount paid to a registered pension scheme, pension fund or provident fund." (Emphasis supplied)

The Respondent submitted that in construing statutory language, the court should be guided by the observation of Lord Up John in the case of **Customs and Excise Commissioner –vs- Top Ten promotions Ltd (1969) 1 WLR 1163** at 1171H wherein he stated:-

" The task of the Court in construing statutory language such as that which is before your Lordships is to look at the mischief at which the Act is directed and then, in the light, to consider whether as a matter of common sense and every day usage the known, proved or admitted or properly inferred facts of the particular case brings the case within the ordinary meaning of the words used by Parliament."

In ***BARNES –VS- JARVIS (1953) 1 W.L.R. 649 Lord Goddard***

C.J said:-

"A certain amount of common sense must be applied in construing statutes. The object of the Act has to be considered. If the words of the statute are themselves precise and unambiguous, <u>then no more can be necessary than to expound those words in their ordinary meaning and natural sense</u>. The words themselves alone do in such a case best declare the intention of the law giver."

In my view, the mischief that Sections 5(2)(f) and 3 (2) (a) (ii) of the Act seeks to address is to ensure that tax is chargeable on any benefit, gain or advantage which enures to an employee from his employer. This includes monies paid by the employer as a premium for a policy of insurance on the life of the employee. That life policy should be for the benefit of that employee or his dependants. The language of the section is very clear and does not need any technical interpretation. The central issue is that apart from the premium being paid by the employer, the benefit of the insurance must be for that employee or his dependents.

Does the Group Life Policy in issue here fit the parameters set by Section 5(2) (f) of the Act? The policy reads:-

"GROUP LIFE ASSURANCE AND DREAD DISEASE BENEFIT POLICY

This policy ("the policy") WITNESSES that British-American Insurance Company (Kenya) Limited (hereinafter called the company) <u>agrees to pay to the policy holder the amounts of benefits set out in the Register of Lives Assured</u> subject to the conditions and privileges in the schedules. The policy is

issued in consideration of the application of the policy holder a copy of which is attached hereto and made a part hereof and of the payment by the policy holder of the premium as herein provided.” (Emphasis supplied)

Policy holder has been identified on the Schedule to the policy as being Standard Chartered Bank (K) Ltd of P.O Box 30003-00100, Nairobi i.e. the Respondent. The Policy was to cover the lives of eligible employees who are persons whose names are in the Register of Lives that form part of that policy.

The Respondents contention was that since this was an annual cover, it did not amount to a life insurance in terms of Section 5(2) (f) of the Act. The Respondent further contended that the policy was not a life insurance for the reason that the policy did not cover the lives of employees of the Respondent.

I do not agree with the Respondents on this issue. The fact that the policy referred to the persons covered as **Eligible Employees** did not change the meaning of an employee. The use of the term eligible was only used to limit circumstances in which the persons who would be covered by the policy were to be on cover. All those covered however remained to be persons in the employment of the Respondent earning a salary for service rendered to their employer. Indeed Clause 2.2.1 provided that:-

“An ELIGIBLE EMPLOYEE must be at Work attending to all his normal duties on the ENTRY DATE failing which his ENTRY DATE shall be delayed until he submits evidence of his good health and insurability satisfactory to the company of complete eight consecutive weeks active service without absence…….”

In my view, the conditions imposed by the policy on the persons whose life was assured under the policy did not make them anything otherwise than employees of the Respondent.

On whether this was a life insurance, the answer is in the affirmative. The policy itself in the recital decreed,

“….British-American Insurance Company (Kenya) Limited …. Agrees to pay to the policy holder the amounts of benefits set out in the Register of Lives Assured……”

In the schedule to the policy, it is noted:-

“3. Names and dates of birth of Lives Assured. As specified in the Register of Lives Assured.

7. Event on the happening of which Death benefit becomes payable. The death of a life assured in the service of the employer whilst the policy is maintained in force.”

From the foregoing, it is clear that it was lives that were being assured and the event to trigger the payment of the benefit under the policy was the death of a life assured. In **Halsbury’s Laws of England Volume 25, paragraph 527, 4th Edition, Re-issue** while defining life insurance, the learned authors have observed:-

“…….., life insurance in the broader sense comprises any contract in which <u>one party agrees to pay a given sum upon the happening of a particular event contingent upon the duration of human life</u>, in consideration of the immediate payment of a smaller sum or certain equivalent periodical payments by another party.” (Emphasis supplied)

In the instant case, British American Insurance had bound itself to pay certain amounts set out in the Register of Lives upon the duration of the lives assured. There was immediate but periodical payments by way of annual premiums. Accordingly, I am of the view and so hold that the Group Life Assurance and Dread Disease Policy held by the Respondent was but a policy taken on the lives of its employees and therefore a life insurance in terms of the definition set out above.

Although the policy was taken by the Respondent on the lives of its employees whose names were in the

"Register of Lives Assured", the benefits set out therein were payable to the Respondent. It is clear from the recital that the policy was about the insurance company agreeing '***to pay to the policy holder' the Respondent, 'the amounts of benefits set out in the Register of Lives Assured'.*** Clearly, the benefit of the policy enured to or was to the Respondent and not its employees or dependants.

The Appellant submitted that Clause 1.6 describes a Claimant as an eligible employee in respect of whom a Death Benefit or a Dread Disease Benefit is payable and that **DEATH BENEFIT** under Clause 1.9 of the policy was what an eligible employee would become entitled to in the event that he became a claimant. Although those are the definitions given to the various words and terms used in the policy, nowhere in the policy is it indicated that there was any benefit payable to any of the employees. Indeed Clause 1.9 states that Death Benefit is the benefit payable on the death of an **ELIGIBLE EMPLOYEE**. It does not state that the benefit is payable to the employee. Reading the opening recital together with Clause 11.3 of the policy, it is obvious that the payment is made to the Respondent notwithstanding that the Eligible Employee may be a Claimant. That Clause reads:-

"11.3.1. Payment by the company to the POLICY HOLDER of the amounts due in terms of the POLICY shall be full and final discharge of the company's obligations in respect of such amount due."

Accordingly, my view is that since the benefits under the policy was to the Respondent, the Group Life Assurance and Dread Disease is not covered under Section 5(2) (f) of the Act. This is so because Section 5 (2) (f) of the Act envisages a situation where the benefit, advantage or gain from the life insurance enures to the employee.

This type of insurance covers are not unique. They exist in other jurisdictions. In the American Jurisdiction, the **COLI** and **BOLI** Contracts i.e. "**Corporate Owned Life Insurance'** and **"Bank Owned Life Insurance**", are prevalent but well regulated by statute. Unlike in Kenya where Section 5(2) (f) applies only where the benefit is to an employee, under the American system, the Internal Revenue Code **(IRC)** which the Appellant relied on, expressly prohibits the deduction of expenses in respect of the premiums paid for Life Insurance when the premium payor is also the beneficiary of the death benefit rather than the individual employee and their family. What the American Congress did was to amend the Internal Revenue Code accordingly and to provide for **"Returns and Records with respect to Employer-owned Life Assurance Contracts"** whereby certain regulations were introduced to limit the avoidance of tax by the corporate world by use of these **COLI** and **BOLI** Contracts. It limited, the amount of expenses to be excluded and also put in place stringent conditions to be met before they could qualify to enjoy the tax-free nature of death benefits. Our Parliament has not reached there yet. Until such time as Section 5 (2) (f) of the Act is amended, the expenses on premiums paid under such a Corporate Owned Life Insurance Contract in Kenya shall remain excluded from the income of an employer.

In view of the foregoing, I am of the view and so hold that the Local Committee arrived at a correct decision and I accordingly dismiss the appeals with costs to the Respondent.

DATED and delivered at Nairobi this 13th day of July, 2012.

...

A. MABEYA

JUDGE