Commissioner of Domestic Taxes v ICEA Lion General Insurance Company Limited (Income Tax Appeal E105 of 2023) [2025] KEHC 14865 (KLR) (Commercial and Tax) (23 October 2025) (Judgment)

Neutral citation: [2025] KEHC 14865 (KLR)

REPUBLIC OF KENYA

IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)

COMMERCIAL AND TAX

INCOME TAX APPEAL E105 OF 2023

H NAMISI, J

OCTOBER 23, 2025

BETWEEN

COMMISSIONER OF DOMESTIC TAXES ..... APPELLANT

AND

ICEA LION GENERAL INSURANCE COMPANY LIMITED ..... RESPONDENT

(Being an appeal from the Judgement of the Tax Appeals Tribunal delivered at Nairobi on 19 May 2023 in Tax Appeal Tribunal Appeal No. TAT 392 of 2021)

JUDGMENT

1. The Appellant is a principal officer appointed under section 13 of the *Kenya Revenue Authority Act*, Cap 469 and the Kenya Revenue Authority, mandated to collect and receive all Government revenue in accordance with the various tax statutes.

2. The Respondent is a limited liability company licensed to conduct insurance business in Kenya. The company focuses on products, services and activities related to general insurance.

3. The underlying dispute originated from a compliance review carried out by the Appellant on the Respondent for the years 2015 to 2018, which led to a notice of assessment for Corporation Tax and Value Added tax (VAT). Following the audit, on 5 November 2020, the Appellant issued a Notice of Assessment demanding additional taxes comprising of Corporation Tax of Kshs 122,109,291 and Value Added Tax of Kshs 88,805,225/-, inclusive of penalties and interest. Following Alternative Dispute Resolution proceedings at the Tribunal, the Corporation Tax assessment was settled. This left one issue unresolved: whether VAT is chargeable on the disposal of salvage motor vehicles by the Respondent, amounting to Kshs 88,805,225/-.

4. Upon hearing parties on the singular issue, the Tribunal, in its judgement dated 19 May 2023, found in favour of the Respondent. It held that the disposal of salvages is an integral part of the insurance business, flowing from the principles of indemnity and subrogation. It is, therefore, encompasses with the VAT exemption for insurance services provided under the *Value Added Tax Act*.

5. Being aggrieved by the judgement and order of the Tribunal, the Appellant lodged this appeal on the following grounds:

    i. That the Honourable Tribunal erred in law and in fact in finding that the sale of the motor vehicles salvages is part of insurance compensation;

    ii. That the Honourable Tribunal misdirected itself in finding that even if the insurer retains the salvages from the insured to either diminish the costs or reimburse itself does not amount to a sale;

    iii. That the Honourable Tribunal erred in law and in fact in failing to appreciate that the proceeds collected from the sale of motor vehicle salvages is to be treated as income and not compensation;

    iv. That the Honourable Tribunal erred in law and in fact in finding that the disposal of salvages is part of insurance industry business and does not attract any VAT liability;

    v. That the Honourable Tribunal erred in law and fact in failing to appreciate that the VAT Act 2013 does not list the sale of motor vehicle salvages as an exempt or zero-rated supply

6. The appeal was canvassed by way of written submissions.

Analysis & Determination

7. Having keenly read the Record of Appeal, Supplementary Record of Appeal and the respective submissions, it is clear that the Appellant's case is anchored on a strict and literal interpretation of the *Value Added Tax Act*. The grounds of appeal can be consolidated into a singular overarching argument: that the Tribunal erred in law and in fact by failing to find that the disposal of motor vehicle salvages constitutes a taxable supply of good subject to VAT at the standard rate.

8. The Appellant submits that the transaction in question is a straightforward sale of goods. Upon indemnifying an insured for a total loss, the insurer taken possession and ownership of the salvaged motor vehicle. The subsequent disposal of the salvaged motor vehicle by sale or auction is, in the Appellant's view, a distinct and separate transaction from the initial insurance service. It constitutes a taxable supply of goods as defined in section 2 of the Act. The proceeds generated from this sale are to be treated as income to the insurer, not as a form of compensation or cost recovery.

9. The Appellant contends that for a supply to be exempt from VAT, it must be expressly listed in the First Schedule of the VAT Act. The Appellant posits that the sale of motor vehicle salvages is conspicuously absent from the list of exempt supplies. In this regard, the Appellant invokes the canon of strict construction of tax statutes, arguing that tax exemptions must be narrowly construed and cannot be granted by implication.

10. The Appellant relies on the cases of Kenya Revenue Authority v Republic (Ex parte Fintel Limited [2001] 1EA 36 (CAK) and Commissioner of Domestic Taxes v Barclays Bank of Kenya Limited [2020] eKLR for the proposition that unless an exemption is clearly and unequivocally articulated in the statute, the default position is that VAT is chargeable.

11. The Appellant argues that the definition of 'insurance business' within the *Insurance Act*, Cap 487 cannot be imported to override the clear charging provisions of the VAT Act. The sale of salvages, while perhaps ancillary to the insurance business, is a distinct taxable event. The Appellant draws persuasive authority from foreign jurisprudence, such as Card Protection Plan Limited vs Customs and Excise Commissioners [1999] UKHL 37, where the House of Lords held that, "VAT is chargeable on services ancillary to insurance if those services can be separated from the insurance cover itself."

12. In opposing the appeal, the Respondent urges this Court to adopt a purposive and harmonious interpretation of the relevant statutes. The Respondent's argument is that the disposal of motor vehicle salvages is not a separate line of business but is an integral, indivisible, and incidental component of the provisions of insurance services, which are expressly exempt from VAT under Paragraph 2 of Part II of the First Schedule to the VAT Act. The Respondent argues that when an insurer indemnifies an insured for a total loss, the insurer by operation of the doctrine of subrogation, steps into the shoes of the insured. The subsequent disposal of the salvage is not a commercial transaction undertaken for profit, but a mechanism to mitigate the insurer's loss and give effect to the principle of indemnity. It is a recovery mechanism, not a trading activity.

13. The Respondent submits that section 2 of the *Insurance Act* defines insurance business in broad terms to include "any business incidental to insurance business as so defined." The disposal of salvage, being a direct and necessary consequence of settling a total loss claim, is an example of such an incidental activity. The Respondent relies on European jurisprudence established in the cases of Card Protection Plan Ltd -vs- Commissioners of Customs and Excise (Case C-349/96) and Levob Verzekeringen BV and OV Bank NV vs Staatssecretaris van Financien (Case C-41/04), and submits that the entire transaction should be viewed as a single composite supply of an exempt insurance service.

14. The resolution of this dispute turns on the proper interpretation of the VAT Act, read in conjunction with the *Insurance Act*, and an appreciation of the unique legal and economic nature of the transaction in question.

15. With regard to interpretations in taxing statutes, the primary and foundational rule, long established in common law and consistently applied by Court, is that a taxing statute must be construed strictly. A citizen cannot be taxed unless the language of the statute clearly imposes the obligation. This principle was enunciated in the English case of Cape Brandy Syndicate vs Inland Revenue Commissioners 1KB 64, where Rowlatt, J. stated:

> " ...in a taxing Act one has to look merely at what is clearly stated. There is no room for any intendment. There is no equity about a tax. There is no presumption as to a tax. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used..."

16. This principle has been adopted and reiterated in a long line of Kenyan judicial pronouncements. In REPUBLIC V COMMISSIONER OF DOMESTIC TAXES LARGE TAX PAYER'S OFFICE EX-PARTE BARCLAYS BANK OF KENYA LTD [2012] KEHC 1988 (KLR), this Court affirmed the Cape Brandy principle, holding that if the Crown cannot bring the subject within the letter of the law, the subject is free. Similarly, the Court of Appeal in

    Commissioner of Income Tax v Pan African Paper Mills (E.A) Limited [2018] KECA 585 (KLR) emphasised that in interpretation tax statutes, one looks at what said; there is no room for intendment.

17. However, the corollary to this rule is of equal importance: where the language of the statute is ambiguous or unclear, the ambiguity is to be resolved in favour of the taxpayer. In Mount Kenya Bottlers Ltd & 3 others v Attorney General & 3 others [2019] KECA 500 (KLR), the Court of Appeal

stated that a taxing law with penal consequences must be interpreted with great caution, and any ambiguity must be resolved in favour of the taxpayer.

18. The rule of strict construction does not command that a stature be read in isolation. Where statutes relate to the same subject matter, they are considered to be in pari materia and ought to be read together to discern the true legislative intent. This principle of harmonious construction ensures that the legislative scheme is understood as a coherent whole. The central tension in this appeal lies in the Appellant's insistence on a rigid, isolationist reading of the VAT Act's Schedules, against the Respondent's plea for a contextual approach that harmonises the VAT Act with the *Insurance Act*. Thus, a meticulous examination of the relevant statutory provisions is imperative.

19. The VAT Act provides the regulatory framework. Section 5(1) is the charging provision, imposing VAT on a taxable supply made by a registered person on Kenya. Section 2 defines a taxable supply as a supply other than an exempt supply made in Kenya by a person in the course or furtherance of a business. Section 2 further defines supply of goods to include a sale, exchange or other transfer of the right to dispose of the goods as the owner. The First Schedule to the Act lists supplies that are exempt from VAT. Paragraph 2 of Part II of the Schedule provides an exemption for "insurance and reinsurance services excluding the following – (a) management and related insurance consultancy services; (b) actuarial services; and (c) services of insurance assessor and loss adjusters.

20. The *Insurance Act* governs the conduct of insurance business in Kenya. Section 2 provides a definition of insurance business to mean the business of undertaking liability by way of insurance, and includes any business incidental to insurance as so defined. (emphasis added)

21. Looking at the two statutes, an immediate interpretative challenge emerges. The VAT Act exempts insurance services but provides no definition for this term. The *Insurance Act* defines insurance business in expansive terms to include activities that are incidental thereto. The question that arises is whether the scope of insurance services for VAT purposes can be properly understood without reference to the definition of insurance business in its parent statute. To read the VAT Act in a vacuum would be to ignore the legislative context and the interconnectivity of our laws. The provisions are pari materia, and a harmonious interpretation is not only permissible but necessary.

22. The next question is whether the sale of salvages is an exempt supply or whether it is a component of insurance services, which are exempt. The Appellant characterises the disposal of salvages as a simple sale of goods. This characterisation, however, fails to appreciate the unique legal nature of the transaction, which is rooted in the doctrines of indemnity and subrogation.

23. A contract of general insurance is a contract of indemnity. Its purpose is to restore the insured to the same financial position they were in before the insured peril occurred, but no better. Arising from this is the doctrine of subrogation, which allows an insurer, upon fully indemnifying the insured, to step into the insured's shoes and exercise ant rights and remedies the insured may have against a third party in respect of the loss. When an insured's motor vehicle is written off and the insurer pays the agreed value, the insurer acquires a right to the salvage. This is not a commercial purchase. No separate consideration is paid for the wreck. The acquisition of the salvage is a legal consequence of the contract of indemnity. In Castellain vs Preston (1883) 11 QBD 380, the doctrine of subrogation was elaborated by Bret LJ as follows:

> "Now it seems to me that in order to carry out the fundamental rule of insurance law, this doctrine of insurance must be carried to the extent to which I am now about to endeavor to express, namely, the underwriter is entitled to every right of the assured whether such right consists in contract fulfilled or unfulfilled, or in remedy for tort capable of being insisted

> on or already insisted on, or in any other right, whether by way of condition or otherwise, legal or equitable, which can be or has been exercised, or has accrued, and whether such right could or could not be enforced by the insurer in the name of the assured...
>
> That seems to me to put this doctrine of subrogation in its largest possible form, and if in that form, large as it is, it is short of fulfilling that which is the fundamental condition, I must have omitted to state something which ought to have been stated. But it will be observed that I use the words 'of every right of the assured' I think, the rule does require that limit."

24. The subsequent disposal of the salvage is, therefore, not a distinct trading activity but the final step in the process of indemnification. It is the realisation of the insurer's right of subrogation, aimed at mitigating the loss incurred from paying the claim. The proceeds are not trading income in the conventional sense. They are a recovered that reduces the net costs of claims. The Tribunal correctly observed that in accounting practice, these proceeds are treated as a reduction of claims expense, not as revenue from sale. While accounting treatment is not determinative of tax liability, it is highly persuasive as to the true economic substance of the transaction. The transaction is one of recoupment, not of trade.

25. On the issue of single versus multiple supply doctrine, the Appellant relied on the case of Card Protection Plan Ltd v Commissioners of Customs and Excise (Case C-349/96) to argue that ancillary services can be separated and taxed. However, the European Union VAT jurisprudence, which heavily influences Kenyan VAT structure, dictates that where two or more elements supplied to the customer are so closely linked that they form, objectively, a single indivisible economic supply, they must not be artificially separated.

26. The European Court of Justice decision in Faaborg-Gelting Linien A/S v Finanzamt Flensburg (Case C-231/94) ECR I-2395 established that a transaction comprising a number of elements is to be regarded as a single supply if those elements are not supplied independently. The determination depends on whether the elements are ends in themselves or merely incidental to the main service.

27. In the context of insurance, the primary contract for the insured is the transfer of risk and subsequent indemnification. The transfer of the salvaged property is intrinsically linked to the indemnification payment. The insurer acquires the salvage precisely to mitigate the compensation cost. It is a remedial step following the exempt principal service.

28. Therefore, the disposal of the salvage by the Respondent is not an end in itself, but merely a means for the Respondent to better enjoy the principal exempt insurance service, thus constituting a single, economically indivisible supply of insurance as correctly held by the Tribunal.

29. Accordingly, I find that the Tax Appeals Tribunal did not err in law or in fact when it held that the disposal of salvages is exempt from VAT.

30. In the premise, I find that the appeal lacks merit. The same is hereby dismissed with costs to the Respondent assessed at Kshs 50,000/=.

DATED AND DELIVERED AT NAIROBI THIS 23 DAY OF OCTOBER 2025.

HELENE R. NAMISI

JUDGE OF THE HIGH COURT

Delivered on virtual platform in the presence of:

For the Appellant: Ms. Wairimu h/b Sega

For the Respondent: Mr. Ruto

Court Assistant: Lucy Mwangi