IN THE COURT OF APPEAL

AT NAIROBI

(CORAM: W. KARANJA, F. SICHALE & J. MOHAMMED, JJA)

CIVIL APPEAL NO. 29 OF 2005

BETWEEN

COMMISSIONER OF INCOME TAX.....APPELLANT

AND

PAN AFRICAN PAPER MILLS (E.A) LIMITED.....RESPONDENT

(Being an appeal from the Judgment and Decree of the High Court of Kenya at Nairobi (Ransley, J) in dated the 1st October, 2003)

in

NBI HCCA NO. 511 of 2002)

****

JUDGMENT OF THE COURT

1. This is an appeal against the decision of the **High** Court (Ransley J.,) who upheld **PAN AFRICAN PAPER MILLS (E.A) LIMITED,** (the respondent's) contention that an amendment to the Finance Act, 2000 (Act No. 9 of 2000) which was made five (5) years after the importation of the capital goods in question, was applicable in entitling the respondent to obtain a refund. The effect of this decision was that the **COMMISSIONER OF INCOME TAX**, (the appellant) was to refund to the respondent sums in excess of Kshs 260 million.

2. The genesis of this appeal as can be gleaned from the record is that in 1995 the respondent commenced a project for the expansion of its paper plant situated in Webuye in Western Kenya; that the respondent utilized over United States Dollars US$67,000,000 for purposes of capitalization of the project; that as a result of this investment, an amount of Kshs.267,608, 271/= was paid as import duty to the appellant; that prior to the year 1995, there was no tax relief in respect of custom import duty payable on imports into Kenya of capital goods such as heavy machinery used in the manufacturing industry, that through a self-assessment return for the year 2001 the respondent claimed from the appellant a refund of a sum of Kshs.267,608,271 as unused tax credit pursuant to **Section 39A** of the Income Tax Act.

3. The Finance Act 1995 introduced a new Section 39A in the Income Tax Act. The said section provided, inter alia, that tax payers who pay import duty under the Customs and Excise Act on capital goods imported by them for use in approved investment projects would be entitled to set off such import duty against their tax liability.

4. Section 48 of the Finance Act 2000 (the amendment) amended the said section 39A of the Income Tax Act by providing that the import duty incurred by the taxpayer could be refundable to the extent that it had not been set off against income tax in the year following the year in which the investment was made.

5. Relying on the amendment, the respondent applied for a refund from the appellant for the import duty it had paid amounting to Kshs.267, 608,271/=. The appellant rejected the respondent's claim and in dismissing the respondent's application, stated as follows;-

> ***"The commencement date for the amendment to Section 39A contained in the Finance Act, 2000, allowing for refund of import duty was given as at 1st January, 2001. We wish to confirm that the provision for refund is applicable in respect of capital equipment imported on or after 1st January, 2001. It is regretted that under the circumstances no refund is due to your company."***

6. Aggrieved by the appellant's refusal to refund the import duty, the respondent appealed to the Income Tax Local Committee (The Local Committee). The Local Committee after considering the matter upheld the appellant's decision and ruled that the amendment to ***Section 39A (1) (viii)*** of the Income Tax Act was only applicable to duties paid after 1st January, 2001 and stated as follows:

> ***"The committee was of the view that the right of set off for 2000 and prior years still continues, the appellant was not losing and would benefit on the qualifying amount once in a tax paying position during any year in future. The "refund" was a new incentive by the Government to attract new investment in future and could not have retrospective effect… The amendment to Section 39A (1) viii only applies to Duties paid after 1st January, 2001 when this amendment came into force. Case dismissed."***

7. Dissatisfied with the decision of the Local Committee, the respondent appealed to the High Court. In a decision delivered on 1st October, 2003, the learned Judge upheld the appeal by the respondent and expressed himself as follows:

> ***"Those words do not appear to be limited to a future situation. This is also the case in sub-section (b), which restricts the amount to be refunded up to the amount of the duty that would have been set off if the investor had not claimed the investment deduction…It seems to me that what is being done is to give an investor a right to a refund subject of the limiting factors in sub-section (a) and (b). I would adopt Mr. Deverell's submissions that the right to refund applies in respect of the appellant import of capital goods subject to the limitations imposed in sub-section (a) and (b) referred to above. I hold that the wording is not retrospective but gives a benefit, which comes into effect on the passing of the amendment but in respect of circumstances, which are either in existence at the time of the amendment or come into existence at the time of the amendment or come into existence subsequently."***

8. The learned Judge also awarded costs and interest at 5% on the amount of refund from the date of judgment. Aggrieved by that decision the appellant preferred this appeal. The appellant's Memorandum of Appeal dated 17th February, 2013 lists seven grounds of appeal that the learned Judge erred in law:

> ***a) in failing to find that there was no intention, express or implied, under Section 1 and 48 of the Finance Act 2000 to amend Section 39 A (1) (viii) of the Act retrospectively or retroactively;***
>
> ***b) in holding that there was an intention in the amended Section 39A(1) (viii) of the Act (as amended by the Finance Act 2000) to give a benefit in respect of circumstances which existed before the commencement of the amendment;***
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> ***c) and in fact in finding that the right to refund the import duty under the amended Section 39A (1) (viii) of the Income Tax Act applied in respect of the import duty incurred by the respondent prior to the commencement of the said amendment;***
>
> ***d) by failing to find that unless a contrary intention appears, a new law cannot have retrospective or retroactive application and/or confer a retrospective or retroactive benefit;***
>
> ***e) and in fact in failing to find that applying the new law to circumstances which existed prior to the commencement of the new law would impair or take away vested rights acquired under previous laws and/or create new obligations and/or impose new duties and/or attach new disabilities in regard to events already past which is contrary to the law;***
>
> ***f) when he failed to find that, unless expressly stated therein, a new law cannot change the legal character of past transactions carried on lawfully upon faith of the then existing law;***
>
> ***g) and in fact in ordering that the respondent be paid interest on the amount of refund it is entitled to when the respondent had not sought interest in its pleadings.***

The appellant sought the following orders:

> (a) That this Appeal be allowed.
>
> (b) that the orders of the High Court made on 1st October, 2003 allowing the respondent's appeal with costs be set aside and the appeal be dismissed with costs.
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> (c) that the respondent do pay the costs of the appeal
>
> (d) that such further or other order be made as may be appropriate.

Submissions by Counsel

9. At the hearing of the appeal, both parties were represented by counsel. Learned Counsel, **Mr Waweru Gatonye** represented the appellant while learned counsel, **Mr Greg Karungo** represented the respondent. Pursuant to Rule 100 of the Court of Appeal Rules and by consent of the parties, the appeal was disposed of by way of written submissions. Both counsel opted to fully rely and adopt their respective written submissions and list of authorities. Counsel for the appellant condensed the grounds of appeal into two broad grounds:

a) The construction and/or interpretation of Section 39A (1) (viii) of the Income Tax Act

b) The award by the High Court of interest when the same had not been sought by the respondent.

Counsel for the appellant relied on ***Halsbury's Laws of England 4th June Volume 23 page 36***, and submitted that taxing Acts are strictly construed in the sense that one looks at what is said and that there is no room for intendment; and that if the words of a statute are capable of two interpretations it is right to adopt the one that will prevent confusion provided that this would not lead to some difficulty or injustice. Learned counsel for the appellant argued that under ***Section 23 (3) (a)*** of the ***Interpretation and General Provisions Act, Section 48*** of the ***Finance Act*** was to operate prospectively and not retrospectively. He contended that ***Section 48*** of the Finance Act could not affect anything done or suffered nor could it affect a right, privilege or obligation by the respondent. Counsel for the appellant placed reliance on the text**,** ***Bennion, Statutory Interpretation 4th Edition Section 97 at page 265***, and contended that unless a contrary intention appears an enactment is presumed not to be intended to have a retrospective operation.

10. Counsel for the appellant also relied on the case of ***Municipalty of Mombasa vs Nyali Limited [1963] EA 374***, where the predecessor of this Court held that if a legislation affects substantive rights it will not be construed to have retrospective operation unless a clear intention to that effect is manifested but if it affects procedure only, *prima facie* it operates retrospectively unless there is good reason to the contrary. It was counsel's further argument that the concept of substantive rights not only applies to the respondent but also to the appellant, to the effect that if the substantive rights of either party will be affected by legislation it should not be construed to have retrospective effect; that the respondent did not qualify for set off or refund in the first place since the respondent had been in loss position for the years of income between 1996 and 2000; the respondent was unable to offset the import duty against tax payable since Section 39A of the Income Tax Act contemplates a situation where an investor can only get a refund of import duty if it was in a profit making position. On the award of interest, counsel submitted that the learned Judge erred in awarding interest on the amount claimed when the same had not been specifically prayed for.

11. In opposing the appeal, counsel for the respondent relied on the case of ***Republic vs Kenya Revenue Authority & Another Ex-parte Kenya Nut Company Limited [2014] eKLR,*** and submitted that tax laws must be interpreted subject to strict construction and that when interpreting tax statutes courts should not imply into the provisions of the statutes. ***Republic vs Kenya Revenue Authority & Another Ex-parte Fontana Limited [2014] eKLR***, was relied on by the respondent to support its contention that tax statutes must be express and clear so as to leave no room for ambiguity and in case of any ambiguity the statute is interpreted in favour of the taxpayer; that from a strict and literal interpretation of Section 48 of the Finance Act, it is clear that no express provision was in place to the effect that the benefit of refund of custom duty would only apply to investors who made capital goods investments after 1st January, 2001; that if the intention of Parliament express provision was in place to the effect that the benefit of refund of custom duty would only apply to investors who made capital goods investments after 1st January, 2001; that if the intention of Parliament was that ***Section 48*** of the Finance Act was to apply prospectively so that the import duty refund could only be payable to taxpayers who made capital investments after 1st January, 2001 it should have expressly stated so and that this ambiguity in the interpretation of ***Section 48*** of the Finance Act should be construed in its favour.

12. Counsel for the respondent further submitted that a court will consider the presumption against retrospectivity as having been displaced if it can discern a necessary implication or intendment that the Act is to have a retrospective effect; that ***Section 48*** of the Finance Act amended ***Section 39A(1)(viii)*** of the Income Tax Act and identified the year from which the refunds would apply as the year following the year the investment is first put into use; that the language of **Section 48** of the Finance Act clearly identified the year from which refunds would apply; that the effect of ***Section 48*** of the Finance Act was to replace the prohibition on refund of import duty under ***Section 39A(1) (viii)*** of the Income Tax Act with the benefit of refund so that investors who had made qualifying investments under ***Section 39A*** of the Income Tax Act would be entitled to claim refund under ***Section 48*** of the Finance Act irrespective of the year of investment; that by virtue of ***Section 48*** *of the Finance Act*, a legitimate expectation was created that qualifying investors under ***Section 39A*** of the Income Tax Act would be entitled to refund of the import duty and that the appellant was in breach of this legitimate expectation by denying the respondent the refund.

On the issue of award of interest by the learned Judge, counsel for the respondent submitted that the learned Judge had discretion under ***Section 26*** of the ***Civil Procedure Ac***t to award interest whether or not the same was claimed by the successful party.

Determination

13. We have carefully considered the record, the written submissions, the cited authorities as well as the law. As this is a first appeal, it is our duty to analyze and re-assess the evidence on record and reach our own conclusions. (See ***Selle -v- Associated Motor Boat Co. [1968] EA 123*; *Jabane v Olenja, [1986] KLR 661, 664.***

14. The interpretation of **Section 48** of the Finance Act is pertinent in this appeal. It provides as follows:

"Section 39A of the Income Tax Act is amended in subsection (1) by deleting (viii) of the proviso and substituting therefor the following paragraph:

(viii) the import duty to be set off shall not be refundable except –

(a) to the extent of that amount of duty which has not been offset by the year following the year the investment is first put into use or any subsequent year; and

(b) upto the amount of the duty that would have been offset if the investor had not claimed the investment deduction on any investment."

Section 39A (1) (viii) referred to therein provides as follows:-

> ***"An amount of import duty which has been paid under section 117 of the Customs and Excise Act in respect of capital goods, qualifying for wear and tear deductions under Part II of the Second Schedule (excluding passenger cars) imported with the prior approval of the Minister, for private investment in a project the cost of which is not less than 5 million United States dollars within a period of two years from the date of first investment expenditure, if the Minister is satisfied that the investment is capable of generating net economic benefits to Kenya, shall be set off for the purposes of collection against the tax charged on the income of the person who incurred the investment expenditure:***
>
> ***Provided that -***
>
> ***(i) the set-off of import duty shall only be made against income tax payable on the income of the person who incurred the investment expenditure arising from the investment and other activities related or similar to the investment expenditure arising from the investment in the case of an extension or replacement of such capital goods in so far as the said capital goods and the new investment have been commissioned and become productive during the year; and***
>
> ***(ii) the capital goods are used wholly and exclusively in the production of the taxable income; and***
>
> ***(iii) the private investment is a project other than an official aid funded project or a project funded directly or indirectly by the Government; and***
>
> ***(iv) the import duty to be set-off does not form part of the cost of the capital goods for the purposes of wear and tear deductions;***
>
> ***(v) the amount of import duty to be set off shall not be treated as a withholding, advance or instalment tax or as a prepayment of that person's final tax liability;***
>
> ***(vi) the amount of the import duty to be set off shall be applied to reduce the person's final tax liability before taking into account any withholding, instalment or advance tax already paid in respect of that year of income;***
>
> ***(vii) the remainder of the import duty after having been applied in accordance with paragraph (vi) of this proviso shall be applied to reduce the person's final tax liability for the following and subsequent years of income before taking into account any withholding, instalment or advance tax already paid in that year of income;***
>
> ***(viii) the import duty to be set off shall not be refundable except –***
>
> ***(a) to the extent of that amount of duty which has not been offset by the year following the year the investment is first put into use or any subsequent year; and***
>
> ***(b) upto the amount of the duty that would have been offset if the investor had not claimed the investment deduction on any investment."*** *(Emphasis added)*

15. It was the respondent's contention that ***Section 48*** of the Finance Act affected investments undertaken before its enactment whereas the appellant contended that it is only applicable to investments after 1st January 2001 when the amendment took effect. Regarding the correct interpretation of ***Section 48*** of the Finance Act and whether it was applicable to situations before its enactment and hence was retrospective or was only applicable to future acts, we are guided by **Section 23(3)** of the ***Interpretation and General Provisions Act, (Chapter 2 of the Laws of Kenya)*** which provides as follows:

> ***"Where a written law repeals in whole or in part another written law, then, unless a contrary intention appears, the repeal shall not***
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> ***-***
>
> ***(a) revive anything not in force or existing at the time at which the repeal takes effect; or***
>
> ***(b) affect the previous operation of a written law so repealed or anything duly done or suffered under a written law so repealed; or***
>
> ***(c) affect a right, privilege, obligation or liability acquired, accrued or incurred under a written law so repealed; or***
>
> ***(d) affect a penalty, forfeiture or punishment incurred in respect of an offence committed against a written law so repealed; or***
>
> ***(e) affect an investigation, legal proceeding or remedy in respect of a right, privilege, obligation, liability, penalty, forfeiture or punishment as aforesaid, and any such investigation, legal proceeding or remedy may be instituted, continued or enforced, and any such penalty, forfeiture or punishment may be imposed, as if the repealing written law had not been made."***

16. We are guided by **Halsbury's Laws of England 4th Edition Volume 23 page 36** which states that:

> ***"In the construction of a taxing Act, the court has primary regard to the statutory words themselves and to their proper construction…Taxing Acts are strictly construed in the sense that one looks at what is said; there is no room for intendment…"***

17. Further, **Halsbury's Laws of England 4th Edition Re-Issue Volume 44 (i) para1433** states as follows:-

> ***"It is a principle of legal policy that an amending enactment should be generally presumed to change the relevant law only from the time of the enactment's commencement."***

We are further guided by the case of ***Municipality of Mombasa (supra)*** which held that:

> ***"Whether or not legislation operates retrospectively depends on the intention of the enacting body as manifested by the legislation. In seeking to ascertain the intention behind the legislation the courts are guided by certain rules of construction. One of these rules is that if the legislation affects substantive rights it will not be construed to have retrospective operation unless a clear intention to that effect is manifested; whereas if it affects procedure only, prima facie it operates retrospectively unless there is a good reason to the contrary. But in the last resort it is the intention behind the legislation which has to be ascertained and a rule of construction is only one of the factors to which regard must be had in order to ascertain that intention."***

Further, in the case of ***Samuel Kamau Macharia and Another v Kenya Commercial Bank Ltd and 2 Others*****, SCK Application No. 2 of 2011 [2012] *e*KLR,** the Supreme Court while considering the question whether the retrospective application of a statutory provision is unconstitutional stated as follows:

> ***"As for non-criminal legislation, the general rule is that all statutes other than those which are merely declaratory or which relate only to matters of procedure or evidence are prima facie prospective, and retrospective is not to be given to them unless, by express words or necessary implication, it appears that this was the intention of the legislature. (Halsbury's Laws of England, 4th Edition Vol. 44 at p.570). A retroactive law is not unconstitutional unless it:(i) is in the nature of a bill of attainder;(ii) impairs the obligation under contracts;(iii) divests vested rights; or (iv) is constitutionally forbidden"***

18. From the above authorities it is clear that there are exceptions to the general rule that a statutory provision is not retrospective. The important consideration being the intention of the legislature in enacting the statute.

We are guided by the case of ***Amalgamated Society of Engineers vs. Adelaide Steamship (1920) 28 CLR 129 at 161-2*** where **Higgins J** stated as follows:

> ***"The fundamental rule of interpretation, to which all others are subordinate, is that a statute is to be expounded according to the intent of the Parliament that made it; and that intention has to be found by an examination of the language used in the statute as a whole. The question is, what does the language mean; and when we find what the language means, in its ordinary and natural sense, it is our duty to obey that meaning, even if we consider the result to be inconvenient or impolitic or improbable."***

19. ***Section 1 (f)*** of the ***Finance Act*** indicates that ***Section 48*** of the Finance Act was to come into operation on 1st January, 2001. From the record, we note that Section **39A** of the Income Tax Act, 2000 was introduced through the Finance Act, 1995 and provided for set off of import duty paid against tax paid. This was later amended to the tax payable in the Finance Act, 2000 whose effective date was 1st January, 2001. Where there was no tax payable, the import duty would be carried forward to be offset against future tax payable in accordance with proviso (vii) to section 39A (1) of the Income Tax Act. The Finance Act 2000 introduced the amendment through which the import duty paid could be refunded if not offset through the income tax payable.

20. We are guided by the case of **Yew Bon Tew v Kenderaan Bas Mara [1982] 3 All ER 833** where the Privy Council held as follows:-

> ***"Apart from the provisions of the interpretation statutes, there is at common law a prima facie rule of construction that a statute should not be interpreted retrospectively so as to impair an existing right or obligation unless that result is unavoidable on the language used. A statute is retrospective if it takes away or impairs a vested right acquired under existing laws, or creates a new obligation, or imposes a new duty, or attaches a new disability, in regard to events already past. There is however said to be an exception in the case of a statute which is purely procedure, but only a right to prosecute or defend a suit according to the rules for the conduct of an action for the time being prescribed."***

21. From the record, the respondent's income tax returns and accounts indicate that it had been in loss position for the years of income between 1996 and 2001 and was therefore unable to offset the import duty against tax paid or payable. The import duty set off could only be refunded if the investor would have been in a profit position were it not for the investment deduction allowance. It could only be refunded to the extent of the tax that would have been paid had the investor not claimed investment deduction on any investment. The losses made by therespondent were not occasioned by the investment deduction claims except for the loss in the year of income 1996. Accordingly, even if the amendment to Section 39A (1) of the Act were to be retrospective, the respondent would not qualify for import duty set off except for the 1996 year of income.

22. It is notable that Section 39A (1) of the Act came into effect on 16th June, 1995, import duty set off rules were published on 14th April, 1996, Section 39A (1) of the Income Tax Act provided that the capital goods must be imported with the prior approval of the Minister. The Minister's approval was granted on 1st August, 1996 and hence all imports of capital goods prior to this date do not qualify for import duty set off.

23. From the foregoing, we are satisfied that Section 48 of the Finance Act was a tax incentive to attract new investments in future and was to operate prospectively and did not have a retrospective effect. Accordingly, the respondent did not qualify for refund of import duty.

24. On the issue that the learned Judge awarded interest despite the respondent not praying for it, it is not contested that interest was not sought before the High Court. The learned Judge granted it on his own motion. It is trite law that issues for determination flow from the pleadings and courts can only grant prayers that have been sought.

We are guided by the case of **Odd Jobs v Mubia, (1970) EA 476** where this Court held as follows regarding decisions on unpleaded issues:

> ***"a) a court may base its decision on an unpleaded issue if it appears from the cause followed at the trial at the issue had been left to the court for decision;***
>
> ***b) on the facts the issue had been left for decision by the court as the advocate led evidence and addressed the court on it."***

We are further guided by the case of **Lee G Muthoga v Habib Zurich Finance (K) Ltd & Another Civil Appeal No 50 of 2010** where this Court held as follows:

> ***"Interest is normally granted at the discretion of the court and in exercising that discretion, the court has to act judiciously and ensure fairness to the parties."***

25. In the circumstances of this case, we are satisfied that interest was not sought; the same was not made an issue before the learned Judge and the parties did not have an opportunity to submit on this issue. We therefore find and hold that there was no basis of the grant of interest in favour of the respondent and the learned Judge did not therefore exercise his discretion fairly and judicially.

26. Accordingly, we find merit in the appeal and allow it and set aside the orders of the High Court dated 1st October, 2003 allowing the respondent's appeal, and substitute therefore an order dismissing the appeal before the High Court. In the circumstances of this appeal, the order that commends itself to us on costs is that each party will bear its own costs.

27. We wish to apologize for the delay in the delivery of this judgment; it was occasioned by challenges presented by the transfer of all three members of the bench to new Duty Stations and the delay and inconvenience caused to the parties is highly regretted.

Dated and delivered at Nairobi this 25th day of May, 2018.

W. KARANJA

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JUDGE OF APPEAL

F. SICHALE

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JUDGE OF APPEAL

J. MOHAMMED

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JUDGE OF APPEAL

I certify that this a true copy of the original.

DEPUTY REGISTRAR