

# Tax Alert

## The Supreme Court of Kenya upholds the principles of fair administrative action and legitimate expectation in tax disputes

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In an appeal filed by the Kenya Revenue Authority (“KRA”, “the Appellant”) against Export Trading Company Limited (“the Respondent” “Export Trading”), the Supreme Court of Kenya (“Supreme Court”), on 17 June 2022, upheld the judgement of the Court of Appeal by finding that the Appellant acted unfairly in demanding for alleged short levied duty almost four years after the goods were imported.

The Supreme Court in its judgement, directed that the KRA denied Export Trading the right to fair administrative action and that the actions of the KRA in failing to respond to Export Trading’s letter seeking a clarification on the demanded duty amounted to an expectation that the Respondent had paid the correct duty.

### Background of the case

The KRA, through a letter dated 27 February 2013 demanded a sum of over **KES 375 million** from Export Trading, the Respondent, being short levied duty (inclusive of penalties and interest) on rice imported by the Respondent between the years 2008 and 2009 from Burma, Vietnam and Thailand.

The short levy resulted from the application of a duty rate of 35% on the Appellant’s SIMBA system (a platform used for customs clearance) instead of the duty rate of 75% prescribed through Legal Notice No. EAC/10/2007.

Important to note is that the Respondent had, through a letter dated 26 July 2009, sought to know the applicable rate, noting the difference between the rate on the SIMBA system and the rate in the Legal Notice. However, the Appellant did not respond to the letter. Please refer to our April 2019 **tax alert** for a detailed background and analysis of the High Court ruling.

### Determination by the Court of Appeal

Following the High Court’s ruling that the Appellant’s demand was an infringement of the Respondent’s rights under Article 47 of the Constitution, the Appellant proffered an appeal to the Court of Appeal (“CoA”).

The Appellant faulted the High Court for failing to find that the Tradex /SIMBA system did not oust the East Africa Community Customs Management Act, 2004 (“EACCMA”) and Legal Notice No. EAC/10/2007, and for finding that a legitimate expectation had arisen in favour of the Respondent.

The CoA noted that the Appellant’s act of omission in updating the SIMBA system to reflect the correct duty rate was further compounded by the fact that on 26 July



2007, the Respondent wrote to the Appellant seeking clarification on the applicable duty rate, which letter the Appellant failed and /or neglected to respond to. The CoA noted that although the Appellant disowned the letter, the same bore the Appellant's rubber stamp.

Having acknowledged that it is possible to have technological and human errors in a system the CoA questioned why it should take four years to detect the error even after it had been pointed out by an importer (such as was done through the letter of 26 July 2007).

The CoA dismissed the appeal through a ruling of 23 October 2020.

### **Determination by the Supreme Court**

Being further aggrieved, the KRA sought relief from the Supreme Court by arguing for dismissal of the CoA judgement on the basis that legitimate expectation cannot operate contrary to statutory provisions, among

other grounds. The Supreme Court distilled the appeal into two issues for determination:

- Whether the actions of the Appellant constituted a violation of the provisions of Articles 10 and 47 of the Constitution; and
- Whether a legitimate expectation arose.

In its analysis, the Supreme Court noted that the Customs law indeed granted the Appellant power to conduct post clearance audit and demand the short-levied duty. However, in its view, the issue under consideration was the manner in which the decision to demand the short-levied duty was made and whether the process followed was in conformity with Article 47 of the Constitution.

It noted that the two superior courts before it had acknowledged that the EACCMA empowers the Appellant to demand short levied duty but did not only concern themselves with

the power granted to the Appellant; they also concerned themselves with ensuring that the process of demanding the duty was fair.

The Supreme Court thus reiterated the findings of the High Court and the CoA and held that the Appellant acted unfairly in demanding for the alleged short levied duty almost four years after the initial assessment and payment of the duty.

Further the Supreme Court agreed with the CoA that a legitimate expectation arose since the Appellant failed to collect duty at the applicable rate, having applied the rate of 35% in its Tradex/SIMBA system.

The Supreme Court found that it was totally irrational and unreasonable to require the Respondent to carry the burden of being aware of any mistakes made by the Tradex/SIMBA system, a system run by the Appellant.

Further, the Supreme Court noted that the actions of the Appellant in failing to respond to the Respondent's letter seeking a clarification on the demanded duty amounted to an expectation that the Respondent had paid the correct duty. Consequently, the Supreme Court dismissed the appeal.

### **What does this Supreme Court judgement mean for both taxpayers and the revenue authority?**

The Supreme Court is the highest court in Kenya hence its judgements constitute binding precedents with no further avenue for appeal.

We therefore expect and hope that the judgement issued by the Supreme Court will be an apt reminder to the revenue authority and other public institutions to treat their stakeholders with consideration by being reasonable, upholding fairness and acting expeditiously.

In particular, we hope that going forward, the KRA will be more proactive in executing its mandate and responding to taxpayers' queries within reasonable timelines.

**Please feel free to contact your usual PwC contact or any of our experts listed herein should you wish to discuss this further.**

