



Tax Alert

Win for the insurance sector as High Court rules that tax amendment introducing VAT on insurance brokerage and agency services is unconstitutional

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The High Court of Kenya, in its Judgement issued on 16 December 2021, in the case of **The Association of Kenya Insurers (“AKI” hereafter “the Association”) versus The Kenya Revenue Authority & 2 others** (together, the “Respondents”), **Petition No. 201 of 2020**, ruled that paragraph 10 of part II of the First Schedule to the Value Added Tax Act as amended by the Tax Laws Amendment Act, 2020 is unlawful and unconstitutional. The effect of the amendment was to impose Value Added Tax (“VAT”) on insurance agency, insurance brokerage and securities brokerage services.

Background

The Tax Laws Amendment Act, 2020 which came into force on April 25, 2020, introduced VAT on insurance brokerage and agency services by deleting the services from the list of VAT exempt services under the First Schedule of the VAT Act.

The High Court of Kenya, in July 2020, had issued conservatory orders suspending the implementation of the amendment pending the determination of the matter, following an application by the Association.

Facts of the case

The Association had sought a declaration that the amendment is unconstitutional based on the following reasons:

- The introduction of VAT at a standard rate on insurance and brokerage services will affect the compliance of insurance companies with the provisions of the Insurance Act by breaching the prescribed limits on management fees to be charged by insurance companies as imposed by the Insurance Act;



- Lack of adequate public participation, openness, accountability, and dissemination of relevant information in the legislative process; and
- Contravention of articles 10 (2)(a), 10 (2) (d), 27 and 201 (a)(b)(i) of the Constitution of Kenya, 2010 (“the Constitution”).

The Respondents opposed the Petition and stated the following:

- AKI, being an unincorporated body, lacked the capacity to institute the suit since they were neither a legal person nor a natural person;

- the Court lacked jurisdiction to hear and determine the matter as the Court is bound by doctrine of judicial restraint and the Association had not proved that there was a breach of the Constitution or any other law; and
- legislation emanating from Parliament enjoyed an irrefutable presumption of constitutionalism.

Upon rendering the preliminary ruling to stay the application of the amendment, the Court dispensed with the petition on 16 December 2021. The summary of the salient points of the Judgement is as follows.

Issues for determination

- Whether there was public participation in the enactment of the Tax Laws (Amendment) Act 2020 that amended the VAT Act;
- whether the Amendment violates Articles 1, 10, 27, 35, 118(1)(b), 201(a), (b)(i) and 232 of the Constitution; and
- whether the Association is entitled to the reliefs sought.

Analysis

- *Whether there was public participation in the enactment of the Tax Laws (Amendment) Act 2020*

In this case, the Association claimed that the amendment made to the VAT Act had not undergone sufficient public participation. While the Association admitted that there were attempts made by the legislature to involve stakeholders in the legislative process, it asserted that not enough time was provided to AKI to provide their full views on the amendment and where their views were provided, these were not incorporated in the final amendment.

The Court held that the averment by the Association had no basis in law and that the enactment of the Tax Laws Amendment Act, 2020 did not violate the principle of public participation under the Constitution, given that reasonable steps were taken by the legislature to involve stakeholders.

The Court's pronouncement elucidates the purpose of public participation, which entails providing a platform for stakeholders across



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the country to have their proposals heard in a fair manner. The Court determined, however, that there is no guarantee that the views of the stakeholders will be incorporated in the final legislation.

- *Whether the Amendment violates various Articles of the Constitution*

The Court ruled that in the determination of the constitutionality of a section of a statute or Act of Parliament, the Court must consider the purpose and effect of the statute or section thereof. Accordingly, if

either the purpose or the effect of a statute's implementation infringes a right guaranteed by the Constitution the statute is unconstitutional.

The Court found that among the practical effects of the amendment, the most relevant was the actual cost of the imposition of VAT on insurance brokerage and agency services would be borne by the members of AKI.

This would controvert the spirit of the Constitution, by creating a situation full of uncertainty and unpredictability. In practice, the Court noted that the VAT expense would increase the management expenses of the insurance companies above the limits prescribed by the Insurance Act.

- *Whether the Association is entitled to the reliefs sought*

The Court determined that based on the nature of the petition and the powers provided to the Court by Article 165 of the Constitution it had the jurisdiction to determine this suit. Including the determination of the question whether any law is inconsistent with or in contravention of the Constitution.

Based on the foregoing, the Court found that the Association had proven that the Amendment violated the provisions of the Constitution and the



Amendment was therefore unlawful, unenforceable, null and void ab initio.

What does this Judgement mean for the insurance and securities brokerage sectors?

This is a welcome judgment and is a relief to the insurance and securities brokerage sectors as standard VAT will not be applicable on insurance brokerage, insurance agency and securities brokerage services.

A number of pertinent questions however, arise;

1. Can taxpayers seek refunds for the tax paid during the period within which an unconstitutional statute was in force i.e., April 25, 2020 to July 16, 2020, when conservatory orders were issued?
2. Can taxpayers who had continued to fully comply with the amendment obtain a refund of the VAT paid to the KRA? This is in light of the fact there are risk averse taxpayers who, in a bid to reduce the likelihood of paying penalties and interest on the tax should KRA have won the case, opted to make the VAT payments to the KRA, the conservatory orders notwithstanding.

These questions raise remedial issues that were not deliberated by the Court. Further, the Judgment rendered by the Court was not explicit

in stating that a refund should be made to taxpayers who had made the VAT payments to the KRA, however, there are probable grounds for a refund application on the basis that the law was null and void, meaning that the tax ought not have been paid in the first place. Affected taxpayers may consider pursuing a refund with the KRA.

Conclusion

This Judgment is part of a recent trend that goes to show that courts are willing to consider the process, application, and implications of amendments to legislation and to ensure that the Constitution is upheld. Taxpayers ought to be more aware of their rights. Where legislation is not consistent with constitutional provisions, there is room to challenge laws that infringe on clearly identified constitutional rights.

KRA has lodged an appeal against the Judgment at the Court of Appeal. In the absence of stay orders, the High Court judgment remains binding on the KRA and taxpayers alike. We will continue to monitor the developments on this matter and provide additional pertinent information as and when they arise.

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