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## LEGAL ALERT

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DEPOSIT BEFORE TAX APPEALS TO THE HIGH COURT: ANALYSIS OF THE PROPOSED AMENDMENT CONTAINED IN THE FINANCE BILL, 2022



Tax



## Background

On 7th April 2022, the Cabinet Secretary to the National Treasury (“the Cabinet Secretary”) read out the proposed 2022/23 National Budget to the National Assembly. One of the legislative amendments proposed therein was a requirement that all taxpayers appealing to the High Court against decisions of the Tax Appeals Tribunal (“TAT”) should deposit fifty percent (50%) of the total amount of the disputed taxes into a Kenya Revenue Authority (“KRA”) account at the Central Bank of Kenya (“CBK”) which amount would then be recoverable only if the taxpayer succeeds in the appeal to the High Court. The proposed amendment in the Finance Bill 2022 (“the Bill”) further proposed that KRA would be required to refund the same within thirty (30) days if the High Court issues a Judgment that is favourable to the taxpayer. The Cabinet Secretary justified this proposal on the basis that the KRA was experiencing difficulty recovering taxes from taxpayers upon issuance of TAT decisions and further claimed that the deposits would ease recovery of disputed taxes. The proposed amendment has elicited public uproar as it is perceived as an onerous requirement to the taxpayer.

The National Assembly’s Departmental Committee on Finance and National Planning (“the Committee”) has recommended the removal of the clause from the Bill on account of the significant negative impact it would have on the cashflow of businesses. The Committee was to submit its comments on the Bill to the National Assembly on 25th May 2022.

This article analyses reasoning behind the proposed

amendment and its effect on taxpayer’s access to appellate justice.

## The law on deposits pending appeals

The High Court of Kenya is empowered by the Civil Procedure Act (Cap. 21) Laws of Kenya to order a litigant to deposit funds into Court, or a joint interest earning account in the name of the parties Advocates name or provided security for costs pending the determination of an appeal. The Court generally exercises this power upon the application of one party and consideration of the parties’ arguments. Courts will only require a litigant to deposit part of the disputed funds if the adverse party provides compelling reasons that the party who the amount is claimed from may be unable to pay the disputed funds upon conclusion of the appeal. In essence, only the Court has the discretion to direct a litigant to deposit part or the entire disputed sum in Court, joint interest earning account or provide security for costs pending the outcome of the appeal. This system accords both parties a fair hearing before the Court considers ordering a party to deposit part of the disputed sum or security for costs.

Courts have been categorical that the purpose of security for costs is not to punish judgment debtors but simply to ensure performance of a decree. Further, Courts have the discretion to consider different types of securities. This discretion enables litigants offer securities that are reasonable and do not grind their operations to a halt. It is also noteworthy that an appellant aggrieved by the magnitude of the security ordered by the High Court can appeal on the same to the Court of Appeal.



### **Basis for the proposed amendment**

Before analyzing the effect of the effect on access to justice, it is important to analyse the reasoning behind the proposed amendment.

The primary reason for the proposed amendment was KRA's supposed difficulties in recovering disputed taxes upon obtaining a favourable decision from the TAT. Unfortunately, the Cabinet Secretary did not support this position with any data. An analysis of the number of disputes and the total taxes tied up in this conundrum would have provided a more cogent basis for the proposed amendment.

Ironically, the High Court has on numerous occasions found that KRA has delayed refunding monies to taxpayers for years. In addition, the East African Court of Justice has taken judicial notice of KRA's delays in refunding taxpayers. Based on the foregoing, this might be a good example of the pot calling the kettle black. Therefore, if average payment periods are relied on as the benchmark to assess KRA's and taxpayers' ability to adhere to Court decisions, KRA's claim may not be the strongest.

### **Access to justice**

Article 48 of the Constitution of Kenya mandates the state to ensure that all persons have access to justice. It further requires that any fee charged in the quest for justice be reasonable and shall not impede access to justice. Courts are therefore required to reasonably determine the need for security as well as the modalities of the same before hearing an appeal.

In determining the need for and magnitude of security, consideration ought to be taken of various factors such as the taxpayer's tax compliance history, its financial statements, and the impact the deposit would have on its cashflow. For example, if the proposed deposit would wipe out the taxpayer's cash and cash equivalents, it would practically render the taxpayer illiquid and would be an impediment to access to justice. In such an instance, the deposit requirement should be significantly reduced. The proposed amendment does not have any qualifications to cater to cases where the fifty percent (50%) deposit would be an impediment. The proposed amendment presents the following impediments to access to justice:

1. Strict imposition;
2. Failure to account for existing impediments to access to justice
3. Unfair treatment;
4. Excessive requirement;

#### **a. Strict imposition**

As stated above, Courts have the power and discretion to determine security payable by an appellant. This discretion enables courts to consider an appellant's circumstances and protect the vulnerable litigants. The Court, being an independent arbiter, is more likely to provide fairer security requirements, taking into consideration the circumstances of each party. The Court oftentimes directs that the funds, or a portion thereof, be deposited into a joint interest earning account which is beneficial to both parties when the funds are ultimately released to the successful party.



Whereas funds deposited in Court do not attract interest, accessing the funds when the matter is concluded is more straight forward as opposed to the proposal to have the funds refunded by KRA. The proposed amendment seeks to impose a deposit requirement without any regard to taxpayers' ability to pay the same and divests the Court of its lawful discretion, thereby raising issues as to the constitutionality of the proposed amendment.

### **b. Failure to account for existing impediments to access to justice**

Taxpayers who dispute assessment of taxes already have to contend with the following impediments when challenging the same:

1. The cost and frustration of lifting agency notices through Court intervention; Cost implications of lodging an appeal to the TAT. When the cost of lodging the appeal (filing fees of KES 20,000 and professional fees) in some instance exceeds the disputed taxes, taxpayers would opt to settle the disputed taxes even when not due and owing. This is an inconvenience that many Kenyans with tax issues have had to bear.
2. Delays in the hearing and determination of appeals from the TAT to the High Court due to case backlog. As a result of these delays, the Court will generally determine tax appeals within a year or two at best.
3. KRA's has poor track record in processing refund applications and remitting the confirmed tax refund.

If the amendment is passed into law and enforced, taxpayers would have to deal with the compounding of

these existing impediments with the additionally onerous task of depositing the required amount.

### **c. Unfair treatment**

Article 27 of the Constitution requires that all litigants be treated equally before the Court. Whereas the proposed amendment seeks to require deposits from taxpayers, it does not require the KRA to deposit funds when appealing to the High Court in cases where the taxpayer is seeking refund of overpaid taxes despite its notoriety for failing to adhere to Court orders.

KRA already has the upper hand in tax disputes. When issued with a favourable Judgment, it can recover the taxes adjudged to be due by using various methods such as agency notices, auctioning of the taxpayer's property, issuance of departure prohibition orders and arrest of taxpayers. Taxpayers, on the other hand have to file an appeal or application in Court, wait for the determination of the same, extract Court orders, issue a demand letter to the relevant KRA Commissioner and follow up with possible judicial review of administrative action seeking to compel payment of the refund.

Recently, KRA publicly displayed its upper hand when it sought to recover taxes from Keroche Breweries by shutting down its factory, issuing agency notices and having the directors arrested despite the business being a going concern engaged in manufacturing.

The proposed amendment seeks to further entrench KRA's upper hand in tax disputes and is lopsided in KRA's favour in that it does not offer any remedy to taxpayers in the event that KRA fails to adhere to a



## Court order.

### d. Excessive requirement

The proposed deposit requirement is high and likely to cause many taxpayers to wind up business or file for bankruptcy as, more often than not, the assessed taxes are high. In many instances, taxpayers are likely to face difficulties in complying with the proposed requirement as they are unlikely to be in a position to afford it, and even if they can afford it, they cannot survive operating with large amounts of capital tied up awaiting an appeal process that could take several years. For struggling businesses, the deposit requirement may well be a death knell and the proverbial final nail on the coffin.

### Conclusion

The proposed amendment prescribes a punitive deposit requirement and may effectively make the TAT a final Court for taxpayers who are not able to raise the required deposit. If enacted, there is a possibility that a party may petition the High Court to have the provision declared unconstitutional for violating Articles 27 and 48 of the Constitution of Kenya. Presently, the Committee has recommended the removal of the proposed amendment, and we await to see whether the National Assembly shall adopt the Committee's recommendation in as far as this particular proposal is concerned.

## Disclaimer

*This alert is for informational purposes only and should not be taken to be or construed as a legal opinion. If you have any queries or need clarification, please do not hesitate to contact [Renee Omondi](mailto:renee@oraro.co.ke) ([renee@oraro.co.ke](mailto:renee@oraro.co.ke)), [Nzioka Wang'ombe](mailto:nzioka@oraro.co.ke) ([nzioka@oraro.co.ke](mailto:nzioka@oraro.co.ke)) or your usual contact at our firm.*



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