Case Number:	Miscellaneous Civil Application 212 of 2004
Date Delivered:	06 May 2005
Case Class:	Civil
Court:	High Court at Nairobi (Milimani Law Courts)
Case Action:	Judgment
Judge:	Jackton Boma Ojwang
Citation:	Republic v Commissioner of Income Tax & another [2005] eKLR
Advocates:	Ms. Malik, instructed by M/s. Kaplan & Stratton Advocates For the Applicant Mr. Ontweka, Advocate For the Respondent
Case Summary:	Judicial Review-Order of Certiorari do remove into the High Court for purposes of being quashed the decision and order of the Commissioner of Income Tax whereby he has invoked the provisions of section 35(6) of the Income Tax Act to recover withholding tax which is allegedly payable by SDV Transami (KENYA) Limited-leave was to operate as a stay of the order of the Commissioner of Income Tax until the determination of the substantive application, or until further orders of the Court-Order LIII, rule 3 of the Civil Procedure Rules
Court Division:	Civil
History Magistrates:	-
County:	Nairobi
Docket Number:	-
History Docket Number:	-
Case Outcome:	-
History County:	-
Representation By Advocates:	-

Advocates For:	-
Advocates Against:	-
Sum Awarded:	-

REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

MISC. CIVIL APPLICATION NO. 212 OF 2004

REPUBLIC.....PLAINTIFF

-VERSUS-

THE COMMISSIONER OF INCOME TAX …RESPONDENT

Ex Parte

SDV TRANSAMI (KENYA) LIMITED……APPLICANT

JUDGEMENT

I. THE APPLICATION AND THE DEPOSITIONS

This is a judicial review application brought by virtue of Order LIII, rule 3 of the Civil Procedure Rules. The application for leave, which came by Chamber Summons of 26th February, 2004 was certified urgent and granted by ***Mr. Justice Lenaola*** on the same date; and leave was to operate as a stay of the order of the Commissioner of Income Tax dated 17th February, 2004 until the determination of the substantive application, or until further orders of the Court.

The originating motion, dated and filed on 10th March, 2004 carried two prayers:

(a) that, an Order of Certiorari do remove into the High Court for purposes of being quashed the decision and order of the Commissioner of Income Tax dated 17th February, 2004 whereby he has invoked the provisions of section 35(6) of the Income Tax Act to recover withholding tax which is allegedly payable by SDV Transami (KENYA) Limited;

(b) that, the respondent be made to bear the costs of the proceedings.

The premise of the application is expressed in eleven different grounds. These are as follows:

(i) the applicant has a contract with UPS Forwarding Inc., to perform certain services required by the applicant, in relation to the transportation of small packages throughout the world;

(ii) the said contract states that UPS is an independent contractor and that there is no agency relationship between UPS and the applicant;

(iii) the respondent is holding the applicant liable for failing to retain withholding tax while there is no agency relationship between the applicant and UPS;

(iv) the respondent has no legal basis to demand withholding tax, as there is no agency relationship between the applicant and UPS;

(v) the respondent has no legal basis for invoking the provisions of section 35(6) of the Income Tax Act,

as the section is not applicable to the contract between the applicant and UPS;

(vi) the applicant, not being a “payee” in the terms rule 7(1) and (2) of the Income Tax (Withholding Tax) Rules, cannot raise an objection to the impugned order by virtue of rule (2);

(vii) the applicant had a contract with a company known as SITA in Dublin, whereby the applicant accessed information from SITA pertaining to movement of containers;

(viii) SITA obtains such information from shipping lines all over the world, and the applicant would access the information for free;

(ix) the respondent has claimed that the payment made to SITA by the applicant was subject to withholding tax under s. 35 of the Income Tax Act as the applicant was paying a royalty;

(x) the respondent has no jurisdiction to invoke the provisions of s.35(6) of the Income Tax Act, as the payment to SITA does not translate to royalty as defined in s.2 of the Income Tax Act;

(xi) the respondent is likely to levy distress against the applicant and attach its bank accounts, thereby occasioning the applicant irreparable loss and damage.

The above grounds also appear in the Statement made under Order L rule 2 and filed with the aforementioned Chamber Summons of 26th February, 2004. Filed with the Chamber Summons and the Statement was the verifying affidavit of ***John Gerin Msafari*** sworn on 25th February, 2004 which the applicant also calls in aid.

The deponent states that the respondent seeks to recover withholding tax from the applicant on the basis of payments made by the applicant to (i) UPS, and (ii) SITA. He avers that the applicant’s contract with UPS has the express term that at all times, the applicant and UPS will operate as independent contractors, and that no agency relationship has been created. He depones that the respondent is alleging there was an agency relationship and that, on that account, payments made to UPS were subject to withholding tax.

The deponent avers further that the applicant had entered into a contract with SITA to access its website to obtain information on container movements. It is deponed that the respondent has been claiming that the payments to SITA constitute a royalty, for the reason that *software is scientific formulae and so the payments were royalty and on this account subject to withholding tax*. The deponent avers that on the contrary, the applicant did not at any time have access to the software that SITA utilised to compile the information used by the applicant, nor did it buy the software or sell it to anyone else — thus payments to SITA cannot be defined as royalty or royalties. It is deposed that the Commissioner of Income Tax has advised the applicant that the applicant if it wants to raise an objection, can only do so in accordance with *rule 7(1) of the Income Tax (Withholding Tax) Rules*. The deponent avers that the applicant stands to suffer irreparable harm should the respondent proceed to recover the amount claimed to be owed by the applicant.

The respondent’s replying affidavit dated 25th May, 2004 was filed on 26th May, 2004. The deponent**,** ***David Mugo Mwangi*** is a Principal Revenue Officer at the Large Taxpayers’ Office, the office under which the applicant’s tax matters are processed, in the administration of the Income Tax Act. He avers that he has been appointed under and in accordance with s. 122 of the Income Tax Act (Cap. 470), an Act administered by the Kenya Revenue Authority under the Kenya Revenue Authority Act (Cap. 469). He depones that he is seized of the facts pertaining to the dispute, and has been duly authorised to

make the affidavit on behalf of the respondent.

The deponent avers that the applicant had in 2002 been selected for audit for the years of income 1999, 2000 and 2001, in connexion with the implementation of withholding tax procedures. He states that such mode of selection is a normal tool of tax administration, and it entails officers scrutinizing taxpayers' records to ascertain their correctness with regard to tax liability. The audit of the applicant was completed on 9th May, 2002; and on 10th May, 2002 a demand letter for tax was sent to the applicant. It is deponed that during the audit, it was discovered that the applicant had made certain payments to non-resident persons — SITA (1999 and 2000), and UPS (2000 and 2001).

The deponent avers that the payment to SITA was for the use of SITA's communication network to access information on container movement; and the respondent treated this as payment of royalty subject to withholding tax, under section 35(1)(b) of the Income Tax Act.

The respondent had also found that the payment made by the applicant to UPS was for delivery of letters and packages to destinations outside Kenya, in fulfilment of a contract entered into between the applicant and UPS, and any fee payable thereon was *agency fees* which is subject to withholding tax under s.35(1)(a) of the Income Tax Act.

The deponent averred that the respondent is bound by statute to recover withholding tax from a payer who fails to deduct it as required under section 35(6) of the Income Tax Act. He further deponed that the tax demanded from the applicant was due, and had been computed in accordance with the provisions of the Income Tax Act.

The deponent also averred that a dispute such as the instant one, *should have been resolved by the procedure of dispute-resolution provided for under the Income Tax Act and the withholding tax rules* made thereunder.

II. AGENCY, AND LIABILITY TO TAXATION UNDER THE INCOME TAX ACT (CAP. 470): SUBMISSIONS FOR THE APPLICANT

Learned counsel, ***Ms. Malik*** made submissions based on the Income Tax (Withholding Tax) Rules, 2001 (Legal Notice No. 100 of 2001). Rule 6 provides:

"Upon making a payment and deducting withholding tax in any month, the person making the payment shall furnish the payee with a certificate showing the gross amount paid, the total tax deducted and such other particulars as the Commissioner may require."

Rule 7(1) then provides:

"If a person to whom pay ment is made under paragraph 6 is aggrieved by reason of the nature of a payment and the rate of withholding tax applied and is unable to reach an agreement with the payer —

(a) the payer may inform the payee of his rights under this rule and shall, at the request of the payee, furnish him with a written statement showing the manner in which the payer calculated the tax deducted;

(b) the payee may give a notice of objection in writing to the Commissioner…"

The "*payee"* is defined (Rule 2) as "a person who receives income from a payer after deduction of withholding tax; "*payer*" is defined as "a person who deducts withholding tax for the purposes of these Rules."

From those provisions, ***Ms. Malik*** observed that it is the *payee* who raises objections if he is minded so to do. Counsel further remarked that the Commissioner of Income Tax wanted TRANSAMI to deduct from the payments it had made to both UPS and SITA; and so in that case, TRANSAMI would be *payer*; and the *payee* would be SITA and UPS. By Rule 7, only the *payee* may make objections and not the *payer.*

In ***David Mugo Mwangi's*** replying affidavit (para 18) it had been stated that the present application was improper as a motion before this Court:

"…I am advised by counsel on record for the respondent which advice I verily believe to be true, that this application is meant to circumvent the procedure for dispute resolution provided for under the Income Tax Act and the withholding tax rules made thereunder."

Ms. Malik submitted, and in my view, correctly, that the applicant as *payer,* did not qualify to resort to the said dispute resolution procedure under the Income Tax Act and the withholding tax rules. I am in agreement with learned counsel that, for that reason, this judicial review application is properly brought, and was in the circumstances the only avenue open to the applicants.

There is a relevant persuasive authority in this regard, ***Republic v. the Commissioner of Co-operative Development & Another, ex parte David Mwangi & 15 Others***, High Court Miscellaneous Civil Cause No. 805 of 1990. In that decision ***Bosire*** and ***Tank, JJ*** held as follows:

"Certiorari is an order which issues from the High Court directing the removal from an inferior tribunal or authority and bringing it before itself for quashing a decision or order of that tribunal made in excess of or without jurisdiction. Two conditions must, however, be satisfied before such an order can issue. Firstly, that the tribunal must have legal authority to determine questions affecting the rights of subjects. Secondly, it must be duty-bound to act judicially…. The existence of a right of appeal or alternative remedy like review will not preclude an applicant from seeking this remedy…"

Annexed to the verifying affidavit of ***John Gerin Msafari*** dated 25th February, 2004 are the decisions of the respondent sought to be quashed. These decisions are conveyed in a letter the relevant parts of which may be quoted:

"…I wish to clarify that at no time have we ever offered to treat the payments by SDV Transami to UPS as contractual fees [except so as —]

· To bring this unending protracted correspondence to an end by conceding to your argument that your client is an independent contractor.

· [To] demonstrate to you that even if your client was an independent contractor…, payments to UPS were still subject to withholding tax.

However, our stand is, as it has always been, that payments made to UPS by Transami constitute agency fees subject to withholding tax under section 35(1)(a).

"UPS as a non-resident person does not have a permanent establishment in Kenya. The contract for the transportation of parcels and documents, for a customer in Kenya, is signed by Transami and not by UPS.

"It is therefore not true that UPS transports the parcels and documents on behalf of the consignor in Kenya as there is no contract between the consignor and UPS. The fact of the matter is that a contract is entered into between Transami and the consignor.

"Since Transami has no capacity to deliver the parcels and documents outside Kenya, it enters into a second contract with UPS where UPS delivers the parcel or document on behalf of Transami in consideration for a fee.

"The consignor in Kenya does not pay any fee to UPS since he has no contract with UPS. The fee is paid to Transami since the contract is between the consignor and Transami.

"If UPS was delivering parcels and documents on behalf of the consignor, then UPS would invoice the consignor and not Transami.

"If there exists a contract between the consignor in Kenya and UPS, then this contract could only have been signed by Transami on behalf of UPS. This is the case for the existence of an agency relationship between Transami and UPS."

With regard to Transami's relationship with SITA, the Commissioner had thus decided:

"Computer software is in fact a scientific [formula] and payment for its use constitutes a royalty. The applicable rate of withholding tax is 20% and not 15%."

The Commissioner then concluded his order in respect of UPS and SITA as follows:

"Having exhausted all discussions on the above two issues, I have invoked the provisions of Section 35(6) of the Income Tax Act. An objection to this decision may only be raised by the payee in accordance with rule 7(1) [of the] Income Tax (Withholding Tax) Rules."

Ms. Malik conceded that under s. 35(1) of the Income Tax Act, the Commissioner of Income Tax is entitled to be paid withholding tax for *management* or *professional* fees — and agency fees falls within the definition of management or professional fees. By section 2 of the Act, agency fees are fees paid to a person for acting on behalf of a person or government; and this excludes payment made by an agent on behalf of a principal when such payments are recoverable. Learned counsel considered the crucial issue in this matter to be that at all times, the relationship between the applicant and UPS was that of independent contractors. She stated that TRANSAMI only transports documents and letters on land; and where a small package crossed the seas, the consignor will hand over to TRANSAMI. It will be understood that TRANSAMI will only take the package as far as the customs desk at the Jomo Kenyatta International Airport in Nairobi; and from that moment UPS will take over responsibility and liability for the package, and will take it to its final destination. The consignor, counsel submitted, dealt directly with UPS on the basis that UPS would transport the package to final destination, and the consignor was invoiced by UPS and not by TRANSAMI. The waybill would be a UPS waybill filled out by the consignor.

Ms. Malik submitted that the contract between UPS and TRANSAMI is not an *agency* contract. The said contract is annexed to the verifying affidavit of ***John Gerin Msafari*** dated 25th February, 2004, and it bears the heading "SERVICES AGREEMENT (IMPORT AND EXPORT)". The purpose of the contract is

stated in the introductory part as follows:

"WHEREAS:

A. UPS desires that Contractor, as an independent contractor, perform services required by UPS in its transportation of small packages in Kenya (hereinafter referred to as "operating area') and Contractor is willing to do so, on the terms hereafter set forth, and in particular according to the Operating Plan set forth…; and

B. Contractor desires that UPS, as a worldwide freight forwarder, perform services required by Contractor in its transportation of small packages throughout the world, and UPS is willing to do so, on the terms hereinafter set forth."

The obligations of the contractor are thus defined:

"Contractor shall perform the services requested by UPS in the transportation of small packages in the operating area, including customs clearance, sorting, delivery and pick-up…"

The agreement provides (para.7) for the independence of the parties:

"Nothing in this Agreement shall be deemed to constitute a partnership, agency, or employment relationship between UPS and Contractor. Neither UPS nor Contractor shall have any authority to bind or to contract in the name of the other, or any of their respective affiliates, in any way."

From the foregoing terms of the contract, learned counsel submitted that it was not at all an *agency agreement*. The waybill was always signed by the consignor and was in the name of UPS and not TRANSAMI. Paragraph 9 of the waybill showed, counsel submitted, that liability was directly between UPS and the consignor — and it was trite law that an agent *is not liable to a third party*. Hence, if UPS failed to deliver at the final destination, then the consignor would hold UPS and not TRANSAMI liable. The consignor, counsel submitted, was at all times aware that UPS would transport the parcel on the terms and conditions set out in the waybill. Counsel further supported her argument by invoking the content of the invoice, annexed to the said affidavit of ***John Gerin Msafari***. This invoice shows that once the consignor gave instructions, the invoice was issued by UPS — an independent contractor and a service provider; and payment is not made to TRANSAMI. In these circumstances, UPS could not be TRANSAMI's agent or vice versa. It was clear to the consignor, counsel remarked, that as soon as the parcel got to the airport, UPS took over the responsibility.

Counsel submitted that in an agency relationship, the agent must have the power to affect the legal relations of the principal; but in the present instance TRANSAMI did not have that power.

Ms. Malik drew the Court's attention to a work, ***The Law of Agency***, appearing in ***Bowstead on Agency***, in ***The Common Law Library Series*** (No. 7); the author (15th edition: ***F.M.B. Reynolds***) writes:

"AGENCY is the fiduciary relationship which exists between two persons, one of whom expressly or impliedly consents that the other should act on his behalf, and the other of whom similarly consents so to act or so acts. The one on whose behalf the act or acts are to be done is called the principal. The one who is to act is the agent. Any person other than the principal and the agent may be referred to as a third party."

The author then describes the fundamental nature of agency by agreement (p.2):

"The mature law recognises that a person need not always do things that change his legal relations himself: he may utilise the services of another to change them, or to do something during the course of which they may be changed. Thus where one person, the principal, requests or authorises another, the agent, to act on his behalf, and the other agrees or does so, the law recognises that the agent has power to affect the principal's legal position by acts which, though performed by the agent, are to be treated in certain respects as if they were acts of the principal."

Learned counsel drew on another passage in the same volume, on the relationship between agent and independent contractor (p.18):

"The dichotomy of servant (or employee) and independent contractor stems from the law of tort: a person is more readily liable for the torts of his servants than for those of his independent contractors. The difference turns on the degree of control exercised. A servant has been defined as a 'person employed by another to do work for him on terms that he, the servant, is to be under the control and directions of his employer in respect of the manner in which his work is to be done' [Salmond and Heuston, *Torts* (18th ed.), p. 429]. An independent contractor has been defined as 'one who undertakes to produce a given result, but so that in the actual execution of the work he is not under the orders or control of the person for whom he does it, and may use his discretion in things not specified beforehand' [Pollock, *Torts* (15th ed), p.63]. Much space has been devoted in books to considering the relationship between these figures and the *agent*. It is submitted that the controversy is somewhat sterile. Some employees have agency powers…"

Although counsel has used the foregoing passage to illustrate the difference between the *agent* and the *independent contractor*, its essential point, I think, is that one can become an agent even though the original script did not say so; the character of *what is done* — i.e., whether the doer is changing the legal relationship of the other person — is what will determine whether or not there exists a relationship of principal and agent. Therefore, although the author relied upon was in the first place concerned with the question whether a *servant* or *employee* can for certain purposes be treated as an *agent*, this scenario *may be extended*; so that we are now legimately concerned with the question whether UPS, notwithstanding its independent-contractor status provided for in the contract, was not also capable of affecting the legal position of TRANSAMI, and on that account, of being properly treated as an *agent.* I will revert to this point later and, no doubt, it is a point that will be vital in resolving the issues in dispute herein.

Ms. Malik submitted that UPS has a discretion as to how it will get the parcel to the ultimate destination; and UPS incurs liability directly to the consignor, as shown in the waybill. Counsel further submitted that TRANSAMI was not liable for any tort such as may be attributed to UPS. She relied on ***Halsbury's Laws of England***, 4th ed. (1973) Vol. 1, paragraph 817: *"As a general rule, a principal is responsible for all acts of his agent within the authority of the agent, whether the responsibility is contractual or tortious. Similarly the principal will be bound by many dispositions of property made by the agent. In some exceptional instances, a principal may be criminally liable even where he does not himself take part in, authorise or connive at the act or default of the agent*." ***Ms. Malik*** submitted that TRANSAMI would not share in any such liabilities, where they fall upon UPS; and hence there was no agency relationship.

Learned counsel was then concerned with the possible inference from her submission that all transactions between TRANSAMI and UPS are not taxable. She submitted that such transactions would be taxed, under the terms of s.9(1) of the Income Tax Act. By that provision, it is the *air transport operator* itself that would withhold taxes on any profits made by UPS, and pay over to the Government of

Kenya. Counsel submitted that TRANSAMI's role in that respect was merely one of taking the parcel to the airport; and thereafter UPS contracts an airline to carry the parcel to the final destination: so it is for the airline in question to withhold any tax on the profits made by UPS, and pay the same to the Commissioner of Income Tax. If, for instance, UPS contracts Kenya Airways to convey the parcel abroad, then it is for Kenya Airways to withhold the tax and then remit to the Commissioner of Income Tax. In effect, then, learned counsel submitted, the transaction between TRANSAMI and UPS is already attracting tax; and in this regard the Court was invited to take judicial notice that Kenya Airways pays various taxes to the Commissioner of Income Tax.

III. ROYALTIES AND LIABILITY TO TAXATION UNDER THE INCOME TAX ACT (CAP. 470): FURTHER SUBMISSIONS FOR THE APPLICANT

Ms. Malik stated that SITA is a company which the applicant had contracted to facilitate access to information on the movement of containers. SITA would track the movement of containers, and put its information on website, to which its customers then linked up. TRANSAMI was just one of the many customers of SITA, using the SITA website upon payment of certain charges. The charge was only for accessing the website information; it was for dial-up connection. It is deponed by ***John Gerin Msafari*** in the verifying affidavit that "the applicant did not at any time have access to the software that SITA utilised to compile the information used by the applicant nor did it buy the software or sell it to anyone else"; and on this basis learned counsel submitted that the payments made by the applicant to SITA could not be defined as *royalties*, for the purpose of taxation. SITA in its invoices has not mentioned the world "royalty", as no royalty, it was submitted, was payable.

This runs counter to the claim by the Commissioner of Income Tax, that computer software was a scientific formula, and thus the payments made by the applicant amounted to royalties and were accordingly subject to the withholding tax rules.

"Royalty" as defined in s. 2(1) of the Income Tax Act, is a payment made in consideration for the right to use the *copyright of a literary or scientific work*. Counsel submitted that what the applicant was paying to SITA was only a charge for accessing information which had already been lodged on the website. Counsel argued that, whereas the Commissioner of Income Tax was charging tax in respect of computer software which he treated as a scientific formula, the applicant was not using software to produce some desired result; the applicant was not using SITA to produce some process or thing; all the applicant was doing was *clicking to SITA and finding there information regarding the movement of containers*. The applicant, counsel urged, was not paying for the use of software; indeed no software at all was being used; the applicant was only accessing information printed on the screen. Payment for such information, ***Ms. Malik*** submitted, could not be royalty for software. No formula, such as a patent, was being used to produce anything and, counsel submitted, there was no formula to be used.

To demonstrate the point that accessing information (as the applicant was doing) could not be compared with using a formula to produce something (which the Commissioner of Income Tax was claiming), counsel cited from ***The Concise Oxford Dictionary of Current English***, 9th ed (p.533); it thus defines formula:

"1. *Chem.* a set of chemical symbols showing the constituents of a substance and their relative proportions. 2*. Math*. A mathematical rule expressed in symbols. 3. *a.* a fixed form of words, esp. one used on social or ceremonial occasions. *b*. a rule unintelligently or slavishly followed; an established or conventional usage. *c.* a form of words embodying or enabling agreement, resolution of a dispute, etc. 4. *a*. a list of ingredients; a recipe….."

The same dictionary defines "*royalty"* as follows (p. 1203):

"…a sum paid to a patentee for the use of a patent or to an author etc. for each copy of a book etc. sold or for each public performance of a work…"

Learned counsel made the submission, in every respect meritorious, in my view, that *"royalty*" as defined, refers to some device, formula or contraption which the user applies to *make something else,* and in return for that advantage, the user must pay *the original creator of the capital asset*. So if the applicant had been repaying the ingenuity of a capital asset in that manner, then the applicant would have been paying royalties, which would then be subject to withholding tax. But in the present instance, SITA had created nothing; it had merely gathered information by ordinary process, and lodged the same on its website for general use by anyone who paid a certain charge.

IV. CHALLENGING THE RESPONDENT'S REPLYING AFFIDAVIT

As already noted, the replying affidavit of *25th May, 2004* is sworn by one ***David Mugo Mwangi***. The advocate whose name is endorsed as having drawn and filed the said replying affidavit is ***D.O. Ontweka***. Learned counsel for the applicant challenged the validity of that endorsement; for ***D.O. Ontweka*** only came on record on *28th August*, *2004* – i.e., three months after the replying affidavit was sworn and filed. ***Ms. Malik*** submitted that the name of ***D.O. Ontweka***, ***Advocate*** was being invoked in vain in the endorsement at the end of the affidavit; and that, consequently, the said affidavit is incompetent and ought to be struck out.

Counsel, on this point, raises an important point of law. I did not hear ***Mr. Ontweka,*** who turned up to represent the respondent, deny the factual statement that he only came on record some three months after the replying affidavit had been filed, and yet his name was still endorsed as the one who drew and filed the affidavit. First of all there is clearly a factual falsehood shown on the face of the replying affidavit that should be held to vitiate the validity of the same. Secondly, if the said endorsement of the name of ***Mr. Ontweka*** on the replying affidavit is invalid, then the affidavit is liable to be rejected for lacking endorsement, as required under sections 34 and 35 of the Advocates Act (Cap. 16) for a document filed for the purpose of being used in legal proceedings.

On those grounds I could very well have struck out the affidavit sworn on behalf of the respondent. Indeed the points noted above, which reveal the serious defect in that affidavit, justify a strong deprecation of such a document being tendered by a party to legal proceedings.

I have, however, laid the greatest significance on the fact that this is a judicial review matter which raises fundamental questions of law, on the basis of which, primarily, I should decide on the prayers made by the applicant. For this reason alone I will decline to strike out the respondent's defective affidavit.

Ms. Malik remarked that the lengthy correspondence attached to the respondent's affidavit, showed that the dispute has been pending for some two years. She wondered why the respondent had not moved to have the matter settled earlier if there had been the conviction on the part of the Commissioner of Income Tax, that withholding tax was truly payable by the applicant. By a letter of 10th May, 2002 (annexed to the replying affidavit) several heads of tax claim had been raised against the applicant; but subsequently these various heads were reduced to just two. The Income Tax Commissioner's letter sought to be quashed also proceeds, counsel submitted, on a misunderstanding of pertinent facts regarding the relationship between the applicant on one side, and UPS on the other side. It is claimed by the Commissioner that UPS does not sign contracts with customers in Kenya and that UPS was answerable to the applicant. Yet it is clear from the waybill that the contract is, in fact, between the

consignor and UPS and not between the consignor and the applicant; and the invoice is from UPS and not from the applicant. From this misunderstanding of fact, counsel submitted, it was clear that the respondent was imposing tax on the wrong premise.

Another annexure to the replying affidavit is a letter from the Commissioner of Income Tax (dated 4th September, 2003) which itself is attached to "notes of telephone conversation" held between ***Mr. G.M. Obbayi***, Senior Deputy Commissioner of Income, and ***John Msafari*** of the applicant organization. These notes record (under item 2):

"Obbayi told Msafari that he may agree with him (Msafari) that the payments made to UPS Worldwide by TRANSAMI may not be agency fees…"

They further record:

"To Obbayi's interpretation, Mr. Msafari was told, if this is what happens on the ground which is confirmed by the service agreement between the two parties it follows that TRANSAMI and UPS have entered into a contract for delivering packages in and out of Kenya, for which UPS pays TRANSAMI for inward-bound packages; and TRANSAMI pays UPS for outward-bound packages. The payment made by either party to the other is contractual fees. UPS being a non-resident company and TRANSAMI being a resident company, any payment made by the resident company to the non-resident company as contractual fee is subject to withholding tax at the non-resident rate…"

Ms. Malik submitted that in the notes of telephone conversation above-set-out, the Commissioner of Income Tax shows equivocation; he says the payments to the applicant "may not be agency fees", and then he invokes some other head called "contractual fees". The decision sought to be quashed speaks of "agency fees". Counsel contended that the Commissioner is unclear in his mind, yet he later imposes withholding tax, on the basis of "agency fees".

Learned counsel further questioned the Commissioner's decision in the light of the following passage in the said telephone conversation notes prepared and signed by ***Mr. G.M. Obbayi*** (and annexed to the replying affidavit):

"Mr. Msafari appeared convinced but requested that … [as] they do not have recourse to appeal to the Local Committee against Principal Tax (they can only appeal against penalties) as the matter involves withholding tax, they may consider appealing direct to Court. The reason for this will be mainly to make our laws dynamic as they appear static especially in relation to natural justice as taxpayers should have a right to be heard. Obbayi agreed with him that in order to develop our case law, he would appreciate [it] if they proceeded to appeal direct to the High Court as he (Obbayi) expects that the judgement would be interesting. This, Obbayi told Msafari, would be in t he interest of both parties because it has disturbed Obbayi that the law does not provide for an appeal against Principal Tax, to the Local Committee, especially … when it comes to a matter of interpretation. The Commissioner who is not supposed to be a dictator could at times be wrong in his interpretation…and could bang any figure on a taxpayer, yet that taxpayer does not have recourse to appeal."

Learned counsel perceived the communication excerpted above as an acknowledgement on the part of the Commissioner of Income Tax that he was indeed *not at all certain* whether his own imposition of withholding tax against the applicant was *right in law*. This would suggest, counsel submitted, that the tax collector had been placed under duty to collect tax even when he was not sure of the legal basis for exacting the tax charge. Counsel submitted that it was wrong in principle, and also oppressive to the taxpayer, if wrong and unjustified impositions of tax were made and the taxpayer then dared, "take it to

Court!"

V. SUBMISSIONS FOR THE RESPONDENT

.Learned counsel, ***Mr. Ontweka,*** restated the respondent's claim that the applicant had paid certain fees on *agency* and as *royalties*, and for these, the Commissioner of Income Tax was, justifiably, demanding withholding tax. The justification, as counsel submitted, was that any person who pays a non-resident person from moneys earned in Kenya was to retain withholding tax and pay it over to the Commissioner. He stated the respondent's position as based on s.35(6) of the Income Tax Act (Cap. 470); and that the applicant was making payment to a non-resident, and so was required to deduct withholding tax; the applicant did not; and therefore the Commissioner now required that the applicant pay the amount the applicant failed to retain as withholding tax.

Mr. Ontweka argued that the applicant had no locus standi before the Court (which is curious, given the Income Tax Commissioner's position, that the dispute should be brought before the Court). He maintained that by Rule 7(1) of the Income Tax (Withholding Tax) Rules, 2001 the payee was required to lodge an appeal once withholding tax is deducted by the payer; and that such timeous lodgement of an appeal by the payee would be the condition for the applicant (the taxpayer) to have audience before the Court. Learned counsel contended that the applicant had no right to come before the Court before the payees (namely UPS and SITA) had raised their complaint.

Unfortunately ***Mr. Ontweka*** did not explain the basis in law of such an interpretation of the position of the applicant (the payer) before the Court. I have, with great respect, been unable to appreciate the cogency of the argument, especially as it runs in diametric opposition to the trite practices under judicialism — that he who has a grievance against another, on a matter of legal character, has the perfect freedom to invoke the jurisdiction of the Court. The applicant comes to Court because the Commissioner of Income Tax demands that it make substantial payments of tax which it believes it has no legal duty to do; but counsel for the respondent maintains that: "*The payee is the one to be heard, namely SITA and UPS; only the payee has audience, not the payer [the applicant]; since SITA and UPS have raised no objection, the applicant should not be heard."*

Counsel then maintained that this is not a suitable matter for judicial review — as it carries issues of merits, and so oral evidence would need to be taken. Again, with much respect, there is something esoteric about the submission by counsel. I have been unable to see in these proceedings any crucial matter which is in such controversy that proof for it would require anything more than the depositions. Essentially, the questions involved in this matter are *questions of law*, and the relevant facts are so straightforward as not to require proof by oral evidence.

Mr. Ontweka contended that a decision to quash the order of the Commissioner of Income Tax would be inappropriate, because there would be no proper direction that can be issued to the Commissioner, who has a "duty of collecting tax." Counsel wondered whether the Commissioner would be hindered in tax collection, if a quashing order were issued.

Counsel contended that the applicant should not be treated as an independent contractor, because there was an agency relationship between it and UPS. In counsel's words, *"a customer in Kenya cannot walk into a place called UPS, to deliver a parcel, and no party can get such service [presumably the service provided by the applicant] without a consideration."* The argument here, obviously, is that UPS is getting a certain special service from the applicant. But that, I think, would entail that UPS is the one to pay to the applicant for the special service. The essence of the claim here, however, is that it is the applicant which pays out to UPS — and so UPS is the payee, and the applicant should withhold some of the

monies being paid out to UPS. So, *who is the agent"* And how do “agency fees” operate" ***Mr. Ontweka*** should have elaborated this point adequately, for it is critical to such legal basis as might exist for the intended tax charge.

As already noted, the waybill shows that the contractual obligation is between UPS and the consignor (and *not the applicant*). But learned counsel has challenged this perception of the waybill. He contended that the waybill was addressed to nobody, though there was no information on record regarding the “proper form” of waybills. Counsel did not contend that this particular waybill was in any manner unusual, or that the applicant had in any way denatured it to serve the applicant’s own cause.

Mr. Ontweka then made submissions on the nature of the export invoices. He noted that the export aspect of these invoices expressly mentioned the name of the applicant. He contested the validity of paragraph 7 of the agreement between the applicant and UPS — which stated that nothing in the contract shall constitute an agency relationship. In counsel’s words, *“No party can enter into an agreement with the sole purpose of ousting the provisions of a statute*.” Without much illustration, counsel contended that the said agreement is *“not consistent with the Income Tax Act (Cap. 470) which has a different purpose and design.”*

Learned counsel prayed for the exercise of the Court’s discretion to deny the applicant’s prayer for orders of certiorari. To support this prayer, ***Mr. Ontweka*** cited the High decision in ***Republic v. Kenya Revenue Authority, ex parte Aberdare Freight Services & Two Others,*** Misc. Civil Application No. 946 of 2004. ***Mr. Justice Nyamu*** in that matter observed:

“…it must not be forgotten that the Court has a discretion in giving or granting judicial review orders. In the circumstances described herein, I find myself unable to exercise that discretion in favour of an applicant who has contributed greatly in adding to the confusion in having the duty-free quota equitably and fairly managed by the relevant authorities.”

Mr. Ontweka contended that if orders of certiorari were granted, the Commissioner of Income Tax would have become subject to estoppel, in the discharge of his statutory duties in the collection of income tax. He urged that the application be dismissed for want of compliance with s. 35(6) of the Income Tax Act (Cap. 470) and with Rule 7(1) of the Income Tax (Withholding Tax) Rules, 2001.

VI. APPLICANT’S RESPONSE

Learned counsel, ***Ms. Malik*** restated the applicant’s position as being that of a payer; and observed that there was no provision under Rule 7(1) regarding the applicant’s (i.e. payer’s) right of recourse — where it was convinced withholding tax was not payable. The Act did not state what the payer must do; and therefore, counsel submitted, judicial review was the only recourse open to the payer. Counsel relied on ***Halsbury’s Laws of England, 4th ed*** (2001), vol. 1(1), para. 67:

“Exhaustion of alternative remedies. **The Courts in their discretion will not normally make the remedy of judicial review available where there is an alternative remedy by way of appeal or where some other body has exclusive jurisdiction in respect of the dispute. However, judicial review may be granted where the alternative statutory remedy is ‘nowhere near so convenient, beneficial and effectual or where there is no other equally effective and convenient remedy.’ This is particularly so where the decision in question is liable to be upset as a matter of law because it is clearly made without jurisdiction or in consequence of an error of law.”**

Ms. Malik submitted that judicial review was appropriate in the instant matter, and that the alternative

recourse being suggested by the respondent was not beneficial, convenient or effectual to the applicant. She contended that it was unlawful for statutory bodies to act in excess of jurisdiction, or to act where they have no jurisdiction. She submitted that it would amount to *abuse of power* if the Commissioner of Income Tax could make a tax demand any time, and upon anyone *without jurisdiction.* ***Ms. Malik*** contended that the Commissioner was in the habit of expecting payment of tax as soon as a demand was made, and the aggrieved person would raise a complaint only afterwards; and in her view, this makes tax demands punitive in nature.

Learned counsel submitted that the respondent had been unable to explain how the relationship between UPS and the applicant was an agency relationship; nor how payment by the applicant to SITA constituted a royalty.

VII ANALYSIS AND ORDERS

Most judicial review proceedings tend to be straightforward matters of *public law.* The instant one is not in that category. It firstly deals with taxation principles — and this, broadly, may be categorised as public law. Secondly it is concerned with *private law* questions founded in contract and the law of agency. It is essential to resolve the private law issues, as an entry point into questions relating to the *exercise of powers for imposing tax charges.* Have those public powers been properly exercised" Whether or not they have been duly exercised is the main consideration in the grant or refusal of the applicant's prayers for orders of certiorari to issue.

(a) Judicial Review as a Recourse

Under the Income Tax (Withholding Tax) Rules, an appeal procedure exists whereby the *payee* (i.e., the non-resident organization) may raise a complaint regarding the amount of withholding tax retained by the payer and remitted to the Commissioner of Income Tax. Although counsel for the respondent maintained that this *administrative appeal procedure* was the only recourse open to the applicant, it is clear that the procedure is open to the payee but not to the payer — such as the applicant. Counsel for the respondent also contended that the applicant would have no locus standi before this Court unless first the payee had exhausted the administrative appeal procedure. No authority was cited for this proposition, and no logical argument was attached to it. If that submission were to be accepted, it would mean that the applicant would have been denied a recourse for redress of grievances. That is not a tenable position; for any person aggrieved against another, on a matter bearing legal consequence, must have recourse to the Court. Therefore I do not accept the respondent's position, and hold that the applicant had every right to seek judicial intervention as it did.

What the applicant is questioning is the *exercise of a public power*, by a *public body;* and on this account judicial review is eminently an appropriate recourse.

(b) The SITA Question: Does access to Website constitute application of a Scientific Formula and must attract Royalty Tax"

It is my understanding that a royalty is a payment made to the *creator of an industrial or artistic work or design or contraption which bears a certain "capital" quality and which will serve intellectual or reproduction or entertainment purposes.* It is for the clear benefits flowing from such works, that their authors or creators are paid *royalties*. By virtue of the Income Tax Act (Cap. 470), s. 35(6), where a Kenya-based person makes such payments to a non-resident person, he is required to retain withholding tax, and to remit the same to the Commissioner of Income Tax.

Does this state of the law capture the payments made by the applicant to SITA, so that the applicant may log on to SITA's website and access information lodged thereon, regarding the movement of containers worldwide" I do not think so and, with respect, I would consider the Commissioner of Income Tax wrong in point of law, in treating payment for mere access to neutral information as payment for a regenerative scientific formula. Payment of such a kind cannot constitute royalties; and therefore it is wrong in law to require that the applicant should make deductions of withholding tax, when it pays for such website information If the Commissioner of Income Tax would consider it appropriate that payments made for such information be the subject of withholding tax, he would, I think, have to wait for the enactment of legislation bringing the same within the scope of such tax. As of now, I would hold that the Commissioner had misapplied the law, and on this account the applicant is justifiably aggrieved.

(c) Agency fees"

The Commissioner of Income Tax maintains:

"…our stand is, as it has always been, that payments made to UPS by TRANSAMI [the applicant] constitute agency fees subject to withholding tax under section 35(1) (a) [of the Income Tax Act]."

The relevant provision of the law thus reads:

"(1) A person shall, upon payment of an amount to a non-resident person not having a permanent establishment in Kenya in respect of —

(a) a management or professional fee…. which is chargeable to tax, deduct therefrom tax at the appropriate non-resident rate."

While there was no dispute as to whether "*agency fees"* falls within the category of "*management or professional fee",* learned counsel for the applicant has disputed the Commissioner's claim that the applicant did pay out any agency fees at all, in respect of which withholding tax should have been deducted. The recorded communications between the Commissioner and the applicant clearly show that the respondent lacks a clear mind on whether or not "agency fees" are payable by the applicant. The Commissioner took the decision not to apply the term "agency fees" to such payments as the applicant made to UPS; he preferred "contractual fees" instead. Yet the tax demand made (by the Commissioner's letter of 17th February, 2004) is made on the basis that there exists "an agency relationship between TRANSAMI and UPS." Is this a contradiction" Section 2 of the Income Tax Act thus defines "Management or professional fee":

"a payment made to a person, other than a payment made to an employee by his employer, as consideration for managerial, technical or consultancy services however calculated."

This, I think would cover *contractual fees*; and therefore if payments by the applicant to UPS are treated as contractual fees, then they will also be management or professional fees, and will thus be liable to withholding tax under section 35(1)(a) of the Income Tax Act (Cap. 470). It is, of course, confounding that the Commissioner should communicate with the taxpayer using the terms "agency fees" and "contractual fees" interchangeably; it creates confusion and may, indeed, be typified as a misunderstanding of the law and a possible ground for seeking quashing orders against decisions taken by the Commissioner.

Since what the Commissioner is demanding from the applicant is withholding tax in respect of *agency fees,* I have to determine whether, indeed, the agency relationship exists in the instant matter.

By the terms of the contract between UPS and the applicant, UPS is an *independent contractor,* and no agency relationship exists. ***F.M.B. Reynolds*** in ***Bowstead on Agency*** (15th ed), p.1 states that —

"Agency is the fiduciary relationship which exists between two persons, one of whom expressly or impliedly consents that the other should act on his behalf, and the other of whom similarly consents so to act or so acts. The one on whose behalf the act or acts are to be done is called the principal. The one who is to act is the agent. Any person other than the principal and the agent may be referred to as a third party."

Now, between TRANSAMI and UPS, who would be principal and who would be agent" It is most important that the Commissioner of Income Tax should be clear on this question, and if he is not, then he will not be invoking the agency relationship according to law. The Commissioner is not clear on the facts. He says in the letter of 17th February, 2004:

"The consignor in Kenya does not pay any fees to UPS since he has no contract with UPS. The fee is paid to TRANSAMI since the contract is between the consignor and TRANSAMI."

In line with that statement, learned counsel for the respondent did submit:

"a customer in Kenya cannot walk into a place called UPS, to deliver a parcel."

But counsel for the applicant produced depositions with supporting annexures, showing that the consignor is invoiced by UPS and not by TRANSAMI; that the waybill is a UPS waybill and not that of TRANSAMI; that UPS could not be regarded as the agent of TRANSAMI, because it had no power to affect the legal position of TRANSAMI; that any liabilities arising were to be settled between UPS and the consignor only; the contract between UPS and TRANSAMI provided for the independence of each party — with neither having the power to contract in the name of the other. Such are, quite clearly, attributes of a contract between independent parties, neither of which can rightly be said to be agent of the other.

I have to draw the conclusion, in these circumstances, that *"agency fees"* as such are, under the Income Tax Act (Cap. 470), inapplicable as between UPS and TRANSAMI; and any withholding tax such as may be applicable in respect of payments by TRANSAMI to UPS, must be categorised under a heading other than "*agency fees*."

It may well be that there is a heading under which the Commissioner of Income Tax may demand tax charges broadly falling in that category, but it must be expressly stated to be under a different name consistent with the Act. In the Commissioner's present demand, he has not achieved the clarity required, and consequently has caused confusion and anxiety to the applicant, and this amounts to a misapplication of the discretions entrusted to the Commissioner by law.

(d) Orders

The purpose of judicial review is to uplift the quality of public decision-making, and thereby ensure for the citizen civilized governance, by holding the public authority to the remit defined by law. I have found in these proceedings that the Commissioner of Income Tax is exercising far-reaching tax-levying powers in a rather haphazard manner which is not in accordance with the law. While the law entrusts tax-collection powers to the Commissioner, and it is indeed in the public interest that he should discharge that mandate, he must not apply methods that are random and wanting in regularity, with the result that unequal and oppressive conduct results.

I therefore, hereby, issue an *order of certiorari*, to remove into the High Court for purposes of being quashed the decision and order of the Commissioner of Income Tax dated 17th February, 2004 whereby he has invoked the provisions of section 35(6) of the Income Tax (Cap. 470) to recover withholding tax, on the basis of alleged agency relations and of royalty payments in respect of SDV TRANSAMI (KENYA) LTD in its dealings with UPS and SITA.

The respondent shall pay the costs of these proceedings.

Orders accordingly.

DATED and DELIVERED at Nairobi this 6th day of May, 2005.

J. B. OJWANG

JUDGE

Coram: Ojwang, J.

Court clerk: Mwangi

For the Applicant: Ms. Malik, instructed by M/s. Kaplan & Stratton Advocates

For the Respondent: Mr. Ontweka, Advocate