



# Grant Thornton

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## Kenya – Mauritius DTA Declared Void



The High Court at Nairobi delivered the long awaited judgement in the petition challenging the validity of the Kenya – Mauritius Double Taxation Avoidance Agreement.

It is important to note that the High Court did not invalidate the DTA because of a provision(s) contained therein. The invalidation was purely on the grounds that due process was not followed. It therefore remains open for the Cabinet Secretary - Treasury to publish the legal notice afresh and present it to parliament for scrutiny in compliance with law.

Whereas the Tax Justice Network Africa took issue with various provisions of the DTA, the court based its judgement on the fact that the legal notice aimed at domesticating the DTA was not tabled before parliament.

The judgment read in part “...It was not shown that the Legal Notice No. 59 of 2014 was laid before Parliament, and it is the duty of this court to declare that the said Legal Notice ceased to have effect and became void in accordance with Section 11(4) of the Statutory Instruments Act, 2013.”

We analyze in this alert the main issues highlighted in the Petition.



## Brief Facts

Kenya and Mauritius entered into a Double Taxation Avoidance Agreement (DTA) in May 2012.

The Tax Justice Network Africa, filed a petition before the Constitutional, Judicial Review and Human Rights Division of the High Court at Nairobi challenging the constitutionality of the DTA.

According to the Tax Justice Network Africa (the Petitioner) the DTA was enacted without public participation, integrity, transparency and parliamentary scrutiny. It was therefore in violation of the Constitution of Kenya.

## The Dispute:

The court framed the key issues in dispute as follows:

1. Was the making of the DTA in violation of constitution?
2. What laws govern the making of DTA's?
3. Is the petition merited?

## The Petitioner (Tax Justice Network Africa)'s Case:

Key provisions of the DTA violated Article 10 of the Constitution.

The petitioner's main contention include:

- Provisions relating to withholding tax on interest and royalties in the DTA serve to significantly reduce Kenya's opportunity to raise revenue for sustainable economic growth and development;
- The 0% withholding tax rate on services; management fees, insurance, commission etc. exposes government to a potential loss of revenue;
- Lack of Capital Gains Tax provision deprives Kenya of the opportunity to collect tax from sale of companies incorporated in Kenya and owned by foreign investors;
- Creates loopholes for Kenyan companies to avoid payment of tax on divided through share buy backs thus depriving government of development revenue;

- Creates a loop hole for Kenyan investors to dodge Kenyan tax by round tripping investments through Mauritius shell companies; and
- The DTA can only be terminated after five years

## The 2nd Respondent (Kenya Revenue Authority) 's Case:

In response to the Petitioner's case, the Kenya Revenue Authority, made the following submission:

- It is inappropriate to compare interest rate applicable to a non resident person with that of a resident person. – while Withholding Tax (WHT) on a non resident may appear low, the resultant tax may be more that that paid by the resident;
- The average withholding tax rate of 10% is competitive. A higher rate would result in Kenya losing investment;
- The 10% rate is comparable with those of other countries with DTA's with Mauritius;
- Advantages accruing to non residents pursuant to DTA's are meant to attract foreign investment;
- Contracting states to a DTA are at liberty to determine when the DTA shall be terminated and the minimum period before termination.



## The 1st (Cabinet Secretary for National Treasury) and 3rd (The Attorney General) Respondent's case:

The Cabinet Secretary for National Treasury and The Attorney General respectively made the following submission:

- The DTA was negotiated in strict adherence of the law and was aimed at promoting investment;
- The aim of a DTA negotiation is to reach a compromise between the tax rates currently in force in the respective jurisdictions – a similar or lower rate to that offered in the respective countries would beat the objectives of the DTA;
- The allegation that WHT rate on services; management fees, and insurance, commissions is 0% is misguided as these are taxable under the permanent establishment provisions contained in the DTA;
- At the time of negotiation, there was no Capital Gains Tax in Kenya; and
- The DTA, being a bilateral agreement relating to government business or relating to technical administrative or executive matters is not subject to ratification.

## The Court's Analysis:

1. Was the making of the DTA a violation of the constitution?

### Public Participation:

The constitution is clear, there must be public participation when enacting laws. However, there is need for creation of legislation to guide the process.

### Accountability, Transparency and Integrity

The involvement of KRA, the office of the Attorney General and the Cabinet which forms part of the Executive demonstrates accountability in modern day democracy.

2. What laws govern the making of DTA's?

### Tabling before parliament:

Legal Notice No. 59 of 2014 which is the subject of the petition is a Statutory Instrument.

The Statutory Instruments Act, 2013, required tabling of the Legal Notice No. 59 of 2014 before parliament for scrutiny.

Under the Act, Statutory Instruments ought to be tabled before parliament within 7 days after publication.

### Consequence of failure to table Legal Notice No. 59 of 2014 before parliament.

Section 11 of the Statutory Instruments Act, 2013 provides that a statutory instrument shall cease to have effect immediately after the last day for it to be so laid.

3. Is the Petition Merited?

### Violation of the constitution:

The Petitioner did not give specifics which the court would rely on in making a determination. Further, the Petitioner did not demonstrate which law provides for involvement of parliament in the process of making or entering into bilateral agreements.

### Determination:

The petition lacks merit on the issue of constitutionality of the bilateral agreement.

### Violation of laws governing making of DTA's:

It was not shown that Legal Notice No. 59 of 2014 was laid before parliament.

### Determination:

Legal Notice No. 59 of 2014 ceased to have effect and became void in accordance with Section 11(4) of the Statutory Instruments Act, 2013.



## Our Comment:

Whereas the Petitioner, Tax Justice Network Africa, pointed to revenue gaps and loopholes created by key provisions of the DTA, it is interesting to note that the High Court dismissed these claims as unsubstantiated. Had the Petitioner demonstrated how much it would lose due to the wanting provisions or point to companies found to be evading tax through round tripping perhaps the court would have been open to considering these issue.

## Conclusion:

The Judgement will perhaps trigger a review of existing DTA's to ensure procedural compliance. Save for a possible republishing of the legal notice, it remains to be seen whether or not the issues raised in the petition will be factored in to trigger renegotiations with Mauritius.

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## Get in Touch

Please get in touch with us to find out more about how this affects you.

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