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HH&M COURT HIGHLIGHT

MAY 2018

CHARGEES' POWER OF SALE SAFEGUARDED BY THE COURTS IN KENYA BANKERS ASSOCIATION V KENYA REVENUE AUTHORITY

Introduction

In an effort to discontinue the manual payment of Stamp Duty and Capital Gains Tax ("CGT"), in 2016 the Kenya Revenue Authority ("KRA") configured its systems to accept online payment of Stamp Duty simultaneously with the payment of CGT on a transfer of land. Previously, stamp duty was payable on a transfer before a transfer was presented for registration, and only upon registration would CGT need to be paid by the owner of the land. The consequence of this reconfiguration was that the burden of paying CGT essentially shifted to a lender enforcing its security through the exercise of its power of sale in a charge, effectively frustrating the process of enforcing a lender's power of sale. On this basis, the Kenya Bankers Association ("KBA"), a trade union comprised of 42 commercial banks, 1 mortgage finance bank and 2 microfinance banks, moved to the High Court to compel KRA to charge stamp duty without requiring payment of CGT vide Misc. Civil Case No. 510 of 2017.



Arguments by Counsel for KBA and KRA

We represented KBA who sought to have the move by KRA declared unreasonable, unfair and influenced by an error of law. It also sought a declaration that, upon a sale of land by a lender, CGT is payable only upon registration of the transfer by the chargor and not by the lender or the purchaser of the land. KBA submitted that, upon creating a charge over land, a lender does not qualify as an owner of the charged land and does not make any gain when enforcing the security. Moreover, the charge does not operate as a transfer of the land and as such, a lender is proprietor of the charge and not of the land itself.

KRA submitted in response that the lender is primarily responsible to account for CGT in the case of a forced sale as the lender

facilitates the transfer on behalf of its defaulting client. Furthermore, KRA submitted that lenders should take responsibility in accounting and paying for CGT as the gain can only be computed from the lender's records. KRA also argued that new systems inevitably face initial challenges but to take the step of allowing payment of stamp duty without payment of CGT in a forced sale would result in substantial loss to the Government in terms of tax revenue.

Findings by the Court

The High Court on 13 March 2018 observed that the scheme of land legislation in the country only seeks to create security over land and at no time does the lender step into the shoes of the chargor. Moreover, the court noted that it is imperative that, before imposing CGT, KRA must establish that a chargeable gain has

been made by the chargor which determination can only be done on a case-by-case basis.

The High Court declared that the requirement for lenders to pay CGT without first ascertaining whether there is in fact a capital gain is unreasonable, unfair and influenced by an error of law, and, in any event, if there is a surplus from the proceeds of sale after settling the amount due under a charge, the lender only holds such money as trustee for payment of CGT. In its final order, the High Court required KRA to permit purchasers of land in a forced sale to pay stamp duty without requiring the lender or the purchaser to first pay CGT. This decision has since seen KRA move the Court of Appeal seeking to overturn the decision by the High Court.

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