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It is increasingly common for tax practitioners to be involved in disputes that span multiple jurisdictions. We operate in a global economy. Supply chains cross continents, and the increasing role of technology accelerates the pace at which economic activity becomes divorced from the structures intended to tax it. The pace of economic and technological change potentially increases the gap between the reality of commerce and that of taxation.

Although supranational agencies, such as the European Commission and the Organisation for Economic Co-operation and Development, work hard to keep pace with change, there is an inevitable lag between intention and action. Of late we have seen individual countries start to take unilateral actions, with digital taxation being a prime example. In coming years, a combination of economic developments and unilateral actions by individual countries is likely further to emphasise the importance of double tax treaties and the OECD multilateral instrument.

As the chapters of this book were being written, there were already important changes taking place in the political landscape in the United States and Europe, and in the global economy, that will affect international cooperation on tax and trade. For example, the past year has seen a ground-breaking deal agreed by 136 countries, accounting for more than 90 per cent of global GDP, to impose a minimum tax rate of 15 per cent on multinational enterprises.

In the light of the economic effects of the global pandemic, tax authorities are under unprecedented pressure to increase tax yield, and this will only increase the pressure on tax authorities to collect what is seen as a fair share of tax from international businesses operating on their shores. For our profession, this means a likely increase in the frequency of tax disputes, an ever-increasing international element to them and the ensuing need to work more closely with international colleagues as complex, multi-jurisdictional issues arise. It comes as no surprise that the authors of many chapters continue to identify international tax issues and offshore structures as areas of key focus for their own domestic tax authorities.

Regardless of whether tax authorities increase in cooperation or increase in competition, one thing is certain: they will not stand still. Tax, and particularly the international approach to tax, is a permanent fixture on the political agenda. The resulting frequent (and sometimes abrupt) changes in key elements of tax law inevitably lead to high value and complex disputes which often take many years to resolve.

The purpose of this book is to provide insight into the issues that give rise to tax disputes in different jurisdictions, the procedures for resolving those disputes and the powers and approach of local tax authorities. It is hoped that it will provide valuable insight into the process, timescale and cost of resolving complex difficulties when they arise across more than one jurisdiction.
We are lucky to have contributions from many leading and impressive tax practitioners across a wide range of jurisdictions. Each provides an up-to-date insight into dealing with contentious tax issues in their jurisdiction. I have enjoyed and learned from reading their contributions and I hope you will do, too.

I would like to thank my colleagues Victor Cramer, Lee Ellis and Cristiana Bulbuc for their valuable assistance in compiling this edition.

David Pickstone
Stewarts
London
February 2022
I INTRODUCTION

Kenya has a self-assessment tax system where the taxpayer files tax returns to the Kenya Revenue Authority (KRA). However, the Commissioner General is not bound by a tax return or information provided by, or on behalf of, a taxpayer and the Commissioner may assess a taxpayer's tax liability using any information available to the Commissioner.\(^2\)

Tax disputes may arise from disagreements with the Tax Commissioner on taxable amounts, allowable taxes, imposition of penalties and interest as may be provided for by law, and refusal by the Commissioner or the Cabinet Secretary to waive such penalties or interest where a taxpayer has made an application, tax overpayment, interpretation of tax laws and dissatisfaction on administrative actions.

Before 2015, most tax disputes ended up in litigation. The KRA established an Alternative Dispute Resolution (ADR) Framework that is relatively affordable, confidential, and expeditious, compared to litigation. Disputes relating to unconfirmed tax, tax assessments that have been confirmed but whose parties mutually agree to a self-review and those before the courts or Tax Appeals Tribunal whose parties desire an out-of-court settlement are subject to ADR.

However, a tax dispute cannot be subjected to ADR where:

\(a\) a settlement would be contrary to the Constitution, the Revenue Laws or any other enabling laws;
\(b\) the matter borders on technical interpretation of law;
\(c\) it is in the public interest to have judicial clarification of the issue;
\(d\) there are undisputed judgments and rulings; and
\(e\) a party is unwilling to engage in the ADR process.\(^3\)

Considering the backlog of cases in the judicial system, it is difficult to know how long litigating the matter will take but the cost of a dispute can be inferred from the amount in question as per the pleadings filed, the settlement figure and or the decretal sum. This is different for the ADR process because parties are free to agree on the period they intend to take and the cost of resolving the dispute making it the most convenient way to resolve the disputes.

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1 John M Ohaga, SC is the managing partner and Isaac Kiche and William Muthee are senior associates at TripleOKLaw. The information in this chapter was accurate as at February 2021.
2 Tax Procedures Act No. 29 of 2015.
The Constitution does not limit the ability of the KRA or the Commissioner General to act. In fact, under Article 209, it only lists the different divisions of tax that may be imposed by the national and county governments.

II COMMENCING DISPUTES

A tax dispute is deemed to have commenced when a taxpayer raises an objection against a tax decision by the Commissioner under the Tax Procedure Act 2015.

The Commissioner will respond by either amending the assessment in accordance with the objection, amending the assessment in light of the objection according to the best of his or her judgement or decline to amend the assessment. If the Commissioner decides to amend the assessment partially or declines to amend the assessment altogether, the Commissioner in charge of dispute resolution may give that taxpayer an opportunity to engage in ADR if the taxpayer so wishes, before issuing an objection decision.⁴ The ADR mechanism available to the disputing parties is a voluntary facilitated mediation process. On the other hand, the taxpayer may decide to either accept the assessment and remit the taxes owed; or object to the notice by providing a written notice to the commissioner.

If the taxpayer and the Commissioner fail to agree, they will resort to the procedures under the Tax Procedures Act described hereunder.

i Internal dispute resolution mechanism

The taxpayer who wishes to dispute a tax decision lodges an objection against that tax decision by writing a notice of objection and lodging it with the Commissioner within 30 days of being notified of the decision before proceeding under any other written law.⁵ The notice should:

a state precisely the grounds of objection, the amendments required to be made to correct the decision, and the reasons for the amendments;

b in the case of an objection to an assessment, ensure that he or she has paid the entire amount of tax due under the assessment that is not in dispute or has applied for an extension of time to pay the tax not in dispute; and

c ensure that all the relevant documents relating to the objection have been submitted.

The Commissioner shall then notify in writing the taxpayer of the objection decision and shall take all necessary steps to give effect to the decision, including, in the case of an objection to an assessment, making an amended assessment.⁶

The Commissioner shall make the objection decision within 60 days from the date of receipt of the notice of objection or any further information the Commissioner may require from the taxpayer, failure to which the objection shall be deemed to be allowed.⁷

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⁴ Clause 6.1(c) of the ADR Framework by the KRA.
⁵ Tax Procedures Act, Section 51.
⁶ ibid., Section 51(9).
⁷ ibid., Section 51(11).
ii Tax Appeal Tribunal

After the Commissioner’s response, if the decision is appealable it is lodged with decision to the Tribunal in accordance with the provisions of the Tax Appeals Tribunal Act. However, a notice of appeal to the Tribunal relating to an assessment shall be valid if the taxpayer has paid the tax not in dispute or entered into an arrangement with the Commissioner to pay the tax not in dispute under the assessment at the time of lodging the notice. The taxpayer is also expected to pay a refundable fee of 20,000 shillings.8

A notice of appeal to the Tribunal is made in writing and submitted to the Tribunal within 30 days of receipt of the decision of the Commissioner. The appellant is required to file a notice of appeal followed by a memorandum of appeal, statement of facts and the tax decision, within 14 days from the date of filing the notice of appeal.9

An appellant is required to serve a copy of the Appeal on the Commissioner within two days of giving notice of appeal to the Tribunal and shall, unless the Tribunal orders otherwise, be limited to the grounds stated in the appeal to which the decision relates.10 The Tribunal hears and determines an appeal within 90 days of the date the appeal is filed with the Tribunal.11

To promote ADR, the parties to an appeal may apply in writing to settle the dispute outside the Tribunal. In such a case, parties are required to resolve or conclude the settlement outside the Tribunal within 90 days.

iii Litigation

A party to proceedings before the Tribunal that is dissatisfied with the decision of the Tribunal in relation to an appealable decision may, within 30 days of being notified of the decision or within such further period as the High Court may allow, appeal the decision to the High Court and subsequently the Court of Appeal.12

A taxpayer alleging violation, infringement or threatening of a fundamental right or fundamental freedom in the Bill of Rights may file a constitutional petition in the High Court against the Authority.

iv Timelines

When it comes to relevant dispute timelines, Section 42(1)(d) of the Limitations of Actions Act excludes statutory timelines when it comes to recovery of any tax or duty, the interest on any tax or duty, any penalty for non-payment or late payment of any tax or duty or any costs or expense in connection with any such recovery. The Authority can institute a suit against a taxpayer if it feels that there has been a breach of the revenue laws.

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8 Tax Appeals Tribunal Act, Section 12.
9 ibid., Section 13.
10 ibid., Section 13(5) and (6).
11 ibid., Section 13(7).
12 Tax Procedures Act, Section 54.
v Types of taxes

There is no difference in the procedure of handling disputes that may arise in the different types of tax be it personal, corporation, wealth, partnerships, indirect or stamp duty. An assessment is made, if there is an objection notice is given, the Commissioner will either amend the assessment or decline to amend it leading to the dispute resolution process described above. These taxes include:

- **Income tax** – which is charged for each year of income, upon all the income of a person whether resident or non-resident, which is accrued in or was derived from Kenya. In Kenya it is governed by the Income Tax Act.13
- **Corporate tax** – which is levied on corporate bodies such as limited companies, trusts and cooperatives on their annual income.
- **Indirect taxes** – which can be passed on to another entity or individual. They are usually imposed on a manufacturer or supplier who then passes the tax on to the consumer. The most common example of an indirect tax is the excise tax on cigarettes and alcohol, and value added tax (VAT).14
- **Stamp duty** – which is charged on the transfer of properties, shares and stock. It is collected by the Ministry of Lands, which has seconded the function to the KRA. It is governed by the Stamp Duty Act.15

III THE COURTS AND TRIBUNALS

A tax dispute can be litigated in three different forums in the Kenyan judicial system that are invoked on appeal. If the decision from the Commissioner is appealable, a tax payer may appeal to the Tax Appeal Tribunal. A party is further at liberty to file an appeal to the High Court of Kenya to an appealable decision of the Tax Appeals Tribunal, and to the Court of Appeal to an appealable decision of the High Court.

The Tax Appeals Tribunal comprises a chairperson and no less than 15 but no more than 20 other members appointed by the Cabinet Secretary upon such terms and conditions of service as the Cabinet Secretary may determine.16 Public servants, employees of the KRA, or tax agents are ineligible to hold office in order to maintain impartiality.

Disputes are handled by panels that have at least three members, at least one of whom shall be an advocate of the High Court,17 and it hears appeals filed against any tax decision made by the Commissioner. These are heard and determined within 90 days from when the appeal is filed with the Tribunal.18

The first step in a tax dispute is an objection to the decision to the Commissioner General; an appeal will lie from this forum to the Tax Appeals Tribunal. The taxpayer will

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16 Tax Appeals Tribunal Act, No. 40 of 2013, Section 4.
18 ibid.
be required to lodge a notice of appeal in writing within 30 days of the decision of the Commissioner. After filing the notice of appeal, he will be required to submit enough copies of the following documents within 14 days:

a. a memorandum of appeal (stating the grounds upon which the appeal is based);

b. statement of facts (setting out the circumstances leading to the KRA's decision on the objection notice submitted by the taxpayer); and

c. the KRA's decision on the objection notice submitted by the taxpayer.

The taxpayer is also required to serve a copy of the notice of appeal to the Commissioner within two days of filing the notice to the tribunal. The Commissioner thereafter is to serve a statement of facts and any other necessary document within 30 days. A hearing is conducted and evidence may be given orally or through affidavits as the Tribunal may direct. The Tribunal may call any person to attend at a hearing and give evidence including production of any document if the Tribunal believes it could assist its deliberations. The decision of the tribunal shall have effect and be binding as if it were the decision of a court. If the parties are unsatisfied by the decision, they may appeal to the High Court and finally to the Court of Appeal. Appeals are as a matter of right.

IV PENALTIES AND REMEDIES

While disputes are inevitable in any society; in Kenya, tax disputes usually arise following a tax assessment issued by the KRA to a taxpayer following an in-depth audit or a routine compliance check. In resolving such disputes, both the tax authority and the taxpayer usually have their interests and expected outcomes depending on the nature of the dispute. The interests of the tax authorities are usually connected to the work that they perform that is maximising revenue collected and enforcing the law taxation. On the other hand, the interests of the taxpayer are usually vindication and protection of their individual rights, self-interest maximisation and fair treatment.

A tax dispute can therefore result in either criminal or civil liabilities for either the taxpayer or the tax authority. In this case, criminal consequences refer to imprisonment. Most laws, however, lean towards imprisonment and the payment of fines.

i Criminal penalties: what they are and where they are available

Criminal penalties are the most common form of culpability in tax offences. Culpability accrues in the form of fines and imprisonment terms. For instance, failure to deduct PAYE, stamp duty, failure to pay exercise duty attract fines of between 5 and 25 per cent of the amounts in question an amount between 10,000 shillings and 1 million shillings.

The Income Tax Act further prescribes that a person guilty of an offence under the Act for which no other penalty is specifically provided shall be liable for a fine not exceeding 100,000 shillings or to imprisonment for a term not exceeding six months, or both.

19 Tran-Nam B and Walpole M, 'Independent tax dispute resolution and social justice in Australia', 477.
22 Income Tax Act, Part XII.
23 ibid., Section 107.
Further, the Refinery Throughout Tax Act provides that where an offence is committed under Subsection (1), every director of the refinery and every officer thereof concerned in its management shall also be guilty of that offence unless they prove that they did not know, and could not reasonably have been expected to know, of the commission of the offence, or that they took all reasonable steps to ensure that the offence was not committed.24

ii  Civil liability/administrative penalties: what they are and where they are available

Civil liabilities may apply when a person fraudulently acquires benefit of overpaid tax and no steps were taken to notify the tax authority or correct the error. This form of penalty is mostly given to corporations incapable of serving jail terms. It includes the withdrawal of a trading licence and freezing of assets.

A person is only liable for a penalty when the Commissioner notifies them in writing setting out the amount payable and the due date for the payment (which must be at least 30 days after the date of notification). In the event that several penalties are applicable, each penalty shall be calculated separately. If the same act results in more than one penalty, the Commissioner shall determine which penalty a person liable to a penalty or interest may apply in writing to the Commissioner for the remission of the penalty or interest payable and such application shall include the reasons for the application.

A person may apply for the remission of a penalty. The Commissioner may also decide to remit a penalty. Remission is possible for the following reasons:

- consideration of hardship or equity; or
- impossibility or undue difficulty or expense of recovery of the tax.

If the amount of the penalty or interest exceeds 1.5 million shillings, the Commissioner is required to seek prior approval of the Cabinet Secretary.

V  TAX CLAIMS

The procedure for recovery of overpaid taxes is provided for under the Tax Procedures Act. Section 47 of the Tax Procedures Act provides that overpaid tax may be recovered by writing to the Commissioner within five years of the overpayment. The Commissioner is then required to conduct an audit and communicate the verdict to the applicant within 90 days. If the claim is valid, the Commissioner is required to refund the amount within two years. Failure to do so will lead to interest accruing at a rate of 1 per cent per month on the unpaid amount.

There are no special measures applicable to commercial parties in a tax dispute. The Tax Procedures Act provisions apply to both individuals and commercial entities.

i  Challenging administrative decisions

Any administrative tax decision can be challenged by writing to the Commissioner within 30 days of being notified of the decision. The notice must contain grounds of objections and in cases of assessment the taxpayer is required to pay the amount that is not in dispute. The taxpayer may apply for an extension of time to lodge a notice of objection. After lodging the objection, the commissioner is expected to make an objection decision within 60 days, failure to decide the objection shall be allowed.

24 Refinery throughout Tax Act, Section 8(2).
A party that is dissatisfied with the decision of the Commissioner, they may appeal to the Tax Appeals Tribunal. In cases where a taxpayer is dissatisfied with the decision of the Tax Appeals Tribunal, they may appeal to the High Court within 30 days. If the taxpayer is dissatisfied by the decision of the High Court, they may appeal to the Court of Appeal only on the point of law.

Section 55 of the Tax Procedures Act gives parties an avenue to resolve their disputes out of court or the tribunal providing the settlement shall be made within 90 days of the date the court or the Tribunal permits the settlement.

Nevertheless, the Act places the burden of proving the incorrectness of the decision on the taxpayer. Moreover, despite allowing appeals to the High Court and the Court of Appeal, such appeals can only be on a question of law.

The Commissioner may issue private or public rulings on the interpretation of a tax law. A public ruling is issued by the Commissioner's own volition by publishing the ruling in at least two newspapers of nationwide circulation, stating that it is a public ruling and with a heading specifying the subject matter of the ruling and an identification number. The public ruling takes effect on the date specified in the public ruling or, when a date has not been specified, from the date the ruling is published. The ruling shall set out the Commissioner's opinion on the application of a tax law in the circumstances specified in the ruling. A public ruling is binding on the Commissioner but is not binding on the taxpayer.

A private ruling on the other hand is made by the Commissioner after an application in writing by the taxpayer regarding a transaction entered into or proposed. Upon the taxpayer making an application the Commissioner has 60 days to make the ruling, which is binding on the Commissioner. A private ruling is binding on the Commissioner but not on a taxpayer.

### Claimants and related parties

VAT refunds occur in instances where tax was paid in error on any supply, bad debt, excess input tax resulting from zero-rated supplies and overpayments or credits resulting from withholding VAT.

In the case of tax paid in error, the claim should be lodged within 12 months of the date the tax was paid. In the case of a bad debt, a tax refund is paid to a VAT-registered businessperson who has accounted for and paid tax on a supply but has not received any payment after a period of three years from the date of that supply.

Claims for refund for bad debt should be made within five years after which it becomes time barred. However, if the person recovers the tax from the recipient of the supply after receiving the refund, the tax should be paid within 30 days of the recovery date.

A tax refund is claimed online via itax to the KRA. For income tax, the documents required include a tax deduction card (Form P9) for claims relating to excess PAYE deductions, insurance policy certificates for claims relating to insurance relief, a mortgage certificate from a financial institution for claims relating to interest on mortgages and withholding tax certificates for claims relating to tax deducted at source.

A refund claim should be made immediately after filing a tax return for the respective year. Upon approval or rejection of a claim, the taxpayer automatically receives an approval order or rejection order via email.

If the claim is fully supported in all aspects, it is processed within 90 days from the time of the application was made.
VI COSTS

Usually, the court or tribunal is guided by the general principle that costs follow the event, which simply means that the successful party in litigation may recover the costs incurred in litigation. In certain instances, the court or tribunal will depart from this general principle and make no order as to costs, or direct parties to being their costs and will be required to state the reasons for making such orders.

The following examples demonstrate the different orders as to costs that the tribunal or court can make.

In the Miscellaneous Application case No. 32 of 2019, Emmanuel Trading Company Limited v. The Commissioner of Domestic Taxes, the Tax Appeal Tribunal directed each party to bear its own costs.

Further, in the case of Othaya Farmers Co-operative Society Limited v. The Commissioner of Domestic Taxes, the Tribunal upon dismissing the Applicant’s application did not make any order as to costs.

In the Court of Appeal case of Mount Kenya Bottlers Ltd & 3 others v. Attorney General & 3 others [2019] eKLR, the Court of Appeal allowed costs to the appellant against the KRA, the Commissioner General of the KRA and the Commissioner of Customs and Excise.

The cases cited above demonstrate that costs incurred in litigation are recoverable from either the taxpayer or the Tax Tribunal depending on the order made by the court or Tribunal. In essence, the party who is awarded costs will recover the amounts expended, such as filing fees, legal fees and disbursements.

VII ALTERNATIVE DISPUTE RESOLUTION

The ADR framework defines ADR as a voluntary facilitated mediation process of settling tax and customs disputes between a taxpayer and the commission outside the Tax Appeals Tribunal or court in the presence of a mediator or facilitator and upon seeking leave from the Tax Appeals Tribunal or appellate court.

The use of ADR in resolving a tax dispute is enshrined in the Constitution of Kenya and various pieces of legislation.

Article 159(2) of the Constitution provides that courts and tribunal shall be guided by alternative forms of dispute resolution such as mediation and arbitration in exercising judicial authority. The Tax Procedures Act, Section 55 provides that parties can settle the dispute out of court or a tribunal. The Tax Appeal Tribunal Act, Section 28 provides that parties can apply at any stage of the proceedings to be allowed to settle the matter outside the tribunal.

The KRA has also adopted new age dispute resolution in its tax disputes through the establishment of the ADR Division. The Division was formed in 2015 and has grown by leaps and bounds – if the number of tax disputes successfully resolved between the KRA and taxpayers in an efficient effective, timely manner and with finality is anything to go by.

Parties may use alternative means to solve disputes but must do so within 90 days. Where parties fail to settle the dispute within 90 days, the dispute is referred to the court or the tribunal that permitted the settlement. ADR may be initiated by either the taxpayer or the Commissioner.25 It is imperative to note that by 25 August 2020, the KRA had collected 25.8 billion shillings in financial year 2019/20, of which 9.5 billion shillings was credited

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25 The ADR Framework by the KRA, Clause 5.
to the ADR framework.\textsuperscript{26} It should be noted that ADR is voluntary and is structured as a facilitated mediation. The facilitator has no power to impose any decisions upon parties, but rather helps them to find a solution to the dispute. The facilitator is usually not a person involved in the tax audit or investigation or the disputed decision.\textsuperscript{27}

Therefore, the use of ADR is not only time- and cost-effective but also serves to expedite the resolution of tax and customs disputes with the KRA while preserving relationships. The process is voluntary, confidential, friendly and results in a favourable outcome for all parties. Furthermore, the ADR process is free of charge. The KRA encourages taxpayers with tax and customs disputes to consider the use of ADR.

\textbf{VIII ANTI-AVOIDANCE}

The Tax Procedures Act defines tax avoidance as a transaction or scheme designed to avoid paying tax under any tax law.\textsuperscript{28} Section 23 of the Income Tax Act also has anti-avoidance rules and gives the KRA power through the Commissioner to counter an arrangement if the main purpose or one of the main purposes of the arrangement is tax avoidance or reduction of tax liability.\textsuperscript{29} The rule also provides for a penalty that is considered quite high as it is equal to 200 per cent of the amount avoided by a taxpayer.\textsuperscript{30}

This penalty is not eligible for waiver by the Commissioner or the Cabinet Secretary. There are concerns that the law seeks to penalise tax avoidance and that the Commissioner may wield his or her immense powers when it comes to determining what constitutes a tax avoidance scheme to the detriment of taxpayers. This is because, unlike tax evasion, tax avoidance involves operating within the confines of legislation to minimise tax exposure. The Act also provides for tax avoidance by a tax agent as an offence.\textsuperscript{31} It is therefore very important that the Commissioner remains objective in determining and communicating offences and attendant penalties to taxpayers.

In Kenya, the strict rule of interpretation applies in the interpretation of tax legislation. Various court decisions articulate the strict rule of interpretation. In applying the rule, the courts look at what is clearly said in the tax statute. Further, there is no room for looking at the intention of the statute. Hence, the courts cannot and do not read into or infer something from the statute. They only look at the language used in the statute. Lastly, in interpreting tax statutes, the letter of the law rather than the spirit of the law must apply.\textsuperscript{32}

The High Court Judge Majanja, in the famous \textit{Barclays} case\textsuperscript{33} held:

\begin{quote}
The approach to this case is that stated in the oft-cited case of Cape Brandy Syndicate v. Inland Revenue Commissioners [1920] 1 KB as applied in T.M. Bell v. Commissioner of Income Tax [1960]
\end{quote}

\begin{itemize}
\item \textsuperscript{26} www.standardmedia.co.ke/business/article/2001383933/kra-nets-sh26b-from-annual-tax-disputes. Article titled, “KRA nets Sh26b from annual tax disputes by Dominic Omondi” for the Standard Newspaper on 26 August 2020.
\item \textsuperscript{27} Income Tax Act, Section 107.
\item \textsuperscript{28} Tax Procedures Act, Section 3.
\item \textsuperscript{29} Income Tax Act, Section 23.
\item \textsuperscript{30} The ADR Framework by the KRA, Clause 5, Section 85.
\item \textsuperscript{31} ibid., Section 92.
\item \textsuperscript{32} Mwanja, Mukami (2020) Rules on interpretation of tax legislation in Kenya.
\item \textsuperscript{33} Republic v. Commissioner of Domestic Taxes Large Tax Payer’s Office Ex-Parte Barclays Bank of Kenya Ltd [2012] eKLR.
\end{itemize}
Kenya is among the African countries that have signed but not yet ratified this multilateral instrument. Kenya follows the OECD’s transfer pricing rules as enshrined in Section 18 of the Income Tax Act and the Transfer Pricing Rules 2006. According to these, the Commissioner is entitled to adjust the profits of a person who carries on business in Kenya with a related non-resident person, where the business is such that it produces for the resident person either no profits or less than ordinary profits. All this requires the arm’s-length principle (i.e., the price charged for the transactions should be the same as that payable between independent enterprises), and it requires the appropriate documentation. Kenya also follows OECD regulation in other areas, for example, regarding the definition of a ‘permanent establishment’ or Base Erosion and Profit Shifting (BEPS) Action plans.

IX DOUBLE TAXATION TREATIES

i Case study: the Kenya–Mauritius double taxation agreement court case

The case was Tax Justice Network-Africa v. Cabinet Secretary for National Treasury & 2 others [2019] eKLR. The Tax Justice Network-Africa believed the agreement had a number of weaknesses that undermined Kenya’s ability to raise taxes, thus impeding the country’s development. The Network raised a number of concerns and touched on the constitutionality of the agreement. For example, the agreement opened up loopholes for multinational companies operating in the country and super-rich individuals to shift profits abroad through Mauritius to avoid paying appropriate taxes.34 Furthermore, domestic Kenyan investors could avoid Kenyan taxes by round-tripping their investments illicitly through Mauritian shell companies. Kenyan companies could also easily avoid Kenyan taxes in dividends paid to foreign investors through devices like share buy-backs, therefore denying the government development funds. The petitioners also stated that the publishing of the gazette notice was in contravention of relevant laws that required treaties to be brought before Parliament. In turn, the government defended its proceeding by arguing that those agreements were not of the same importance as treaties, which is why no parliamentary scrutiny and approval was required.35 The Court found that the legal notice published by the Cabinet Secretary was not done in accordance with relevant laws that required presentation of the Legal Notice No. 59 of 2014 before Parliament36 and therefore was void and in effect invalidated the entire agreement. Unfortunately, the Court stated that the Tax Justice Network-Africa failed to show how formation of the double taxation agreement was in violation of the Constitution of Kenya.

36 http://kenyalaw.org/caselaw/cases/view/169664.
The interpretation of tax treaties is strict. Terms are hardly ever implied. If there is no favourable treatment provided for with regard to a specific type of tax, national legislation is used.

X AREAS OF FOCUS

Kenya has no special rules on controlled foreign companies; however, there are restrictions on the deductibility of interest and foreign exchange losses of companies that are foreign controlled and thinly capitalised.37

As a rule, tax planning is not illegal, tax evasion is. However, this lacuna is exploited by MNCs who employ SPVs and other structures to avoid paying tax (e.g., incorporating in tax havens or states such as Delaware to reduce taxes payable). For this reason, the OECD has attempted to prevent BEPS.

In 2019, Kenya ratified the Convention on Tax Treaty Related Measures to prevent BEPS. Recently, the KRA has been conducting TP audits on many clients and issuing TP assessments in short order. (Many clients negotiate assessments, and some choose to settle because their TP affairs are not in order.)

You will find, for example, Company A (holding company) incorporates a subsidiary (subsidiary company) in Kenya to offer marketing and liaison services and these are not charged at arm’s length. The KRA has been auditing transfer pricing policies and issuing assessments.

The KRA is empowered to specify conditions and procedures for the application of the methods for determining the arm’s-length price and to adjust the prices if they do not conform to the arm’s-length principle. The policy should be prepared and submitted to the KRA upon request.

The transfer pricing rules are broadly modelled along the principles set out in the OECD’s Transfer Pricing Guidelines for Multinational Enterprises.

Kenya introduced a digital services tax that came into effect on 1 January 2021. This tax is payable by persons whose income from the provision of services is derived from or accrues in Kenya through a digital marketplace. It is chargeable at the rate of 1.5 per cent of the gross transaction value of the service and is payable at the time of the payment transfer for the service to the service provider. A dispute will arise on objection of a Commissioner decision and the resolution mechanism is governed by the Tax Procedures Act 2015.

XI OUTLOOK AND CONCLUSIONS

The KRA casts its nets wide; it fishes for anything and catches a lot. The KRA has invested in an expert team that conducts TP audits and the team is collecting a lot of money. The intention is to ensure all multinationals have updated TP policies that are well benchmarked. Compliance levels have shot up in the recent years, with clients even entering into voluntary disclosure agreements with the KRA and paying arrears before they have been assessed.

Recent developments in tax policy include the digital services tax targeting persons who acquire their income through digital marketplaces in Kenya. Further, the KRA has introduced a three-year tax amnesty window for individuals and businesses that have not disclosed their incomes over the last five years to come forward.

Under the Voluntary Tax Disclosure Programme introduced through the Finance Act 2020, tax defaulters will be granted a tax amnesty, waiver of interest and penalties on the outstanding tax liabilities where they have not disclosed their income to the KRA.

Although the voluntary tax disclosure programme will run for three years, how much of the interest and penalties will be waived will depend on when taxpayers make their applications. This means that the earlier a taxpayer makes its application, the greater the benefit from the amnesty programme. Taxpayers who apply within the first year of the programme, that is, in 2021, will enjoy a 100 per cent waiver of interest and penalties on their outstanding tax liabilities. Those who apply in the second year will only receive a 50 per cent waiver and applications made in the third year will attract a 25 per cent waiver.
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John M Ohaga is the managing partner and co-head of dispute resolution in the leading firm of TripleOKLaw, LLP and has more than 28 years’ post-qualification experience during which he has been involved in numerous complex litigations as well as high-value domestic and international arbitrations. He is a Senior Counsel and has been recognised for his high-quality work and expertise in dispute resolution by The Legal 500, Chambers Global and Best Lawyers. John was declared the 2010, 2016 and 2017 winner of the International Law Office (ILO) Client Choice Awards for Kenya in the category of litigation. He was declared the pupil master of the year, 2019 and was first runner up for Lawyer of the Year at the Nairobi Legal Awards held in May 2019. He is recognised as a leading individual in arbitration, April 2019, The Legal 500 EMEA Rankings 2019; Band 1 recognised as pre-eminent litigator and arbitrator Chambers Global Awards, 2019. He was declared the Lawyer of the Year, 2020 at the Nairobi Legal Awards held in December 2020. He was recently named in the Africa’s 30 Arbitration Powerlist 2020 by the Africa Arbitration Academy, Africa Arbitration and the Association of Young Arbitrators. John is also an expert arbitrator and is a chartered arbitrator, a trustee of the Chartered Institute of Arbitrators (Kenya Branch), a board member of the Nairobi Centre for International Arbitration and a member of the Mediation Accreditation Committee. He is also the chairman of the Kenya Sports Disputes Tribunal. He also chairs the Appeals Committee of the Advertising Standards Board and the National Committee on the Formulation of the ADR Policy for Kenya. He is a trustee of the M–Pesa Foundation. He also sits on the boards of several companies.

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