



Journal of International Business, Innovation and Strategic Management

2022: 6 (1): 26 - 39

ISSN: 2617-1805

---

## TAXATION OF THE PROCEEDS OF ILLEGAL INCOME IN KENYA: A CASE FOR LEGISLATIVE REFORMS

\*Ibrahim Kitoo

Corresponding Author Email: [ibrakito@yahoo.com](mailto:ibrakito@yahoo.com)

### To Cite this Article:

Taxation of the Proceeds of Illegal Income in Kenya: A Case for Legislative Reforms. *Journal of International Business, Innovation and Strategic Management*, 6 (1): 26 - 39

---

### ABSTRACT

Governments around the world have an obligation to provide basic services to their citizens. To fulfil this obligation, there must be made available public funds. The main source of government revenue is through taxation. Various countries have various systems of taxation and rules which they use to impose such systems. The incomes to be subjected to tax could be from legal or illegal sources. This paper examines the controversy around taxing income from illegal activities, around the globe in general and Kenya in particular. In discussing this topic, this paper reviews decided foreign cases and various interpretations of existing tax statutes. It also looks at the various decided cases in Kenya and makes a conclusion that if the tax statutes were clear and unequivocal as expected then there would be no litigation in this subject of taxation of illegal income hence a call for legal reforms in this area. The author proposes various amendments to the Income Tax Act and concludes that the amendments should permit the relevant bodies to tax income from all sources. Income from illegal sources should therefore be taxed.

**Key Words:** *Public Finance, Public Expenditure, Taxation, Income from Illegal Activities, Income Tax Act*



## BACKGROUND OF THE STUDY

Governments all have, to some extent, a commitment to provide services for the population, for example legal services, defence, health services, as well as infrastructure such as roads and energy. To fund this public expenditure, they must obtain funds; borrowing is a possibility but revenue is usually obtained through taxation. Taxation is therefore required to finance public spending. It is a system of compulsory levies or exactions imposed for this purpose on a variety of taxpaying subjects, but it may also be imposed for other social and economic objectives. Today we find enormous diversity in the types of tax systems used by governments around the world. The range of taxes used and the complexity of the rules used to impose them vary from country to country and can often be correlated with the stage of development of the country in question.<sup>1</sup> One controversial aspect of taxation is that of the taxation of income traceable from illegal activities. The prevailing opinion is that it must be taxed.

The rationale for this proposal is that taxation is part of public finance and the importance of public finance has increased in recent years. These days the government is considered responsible to stabilise the economic situation of a country. Similarly, the government plays an important role in the economic development process.<sup>2</sup> According to Attiya *et al*, tax is necessary in ensuring that Kenya meets its human rights obligations.<sup>3</sup> Government's rhetoric about promoting human rights is meaningless without an adequate effort to collect the necessary funds to provide food, water, clothing, shelter and basic medical care for the poorest and most vulnerable strata of the society'.<sup>4</sup>

---

\*The Author is an Advocate of the High Court of Kenya, Commissioner for Oaths & Notary Public, Certified Secretary, Governance, Ethics, Audit, Risk & Compliance Specialist, Public Procurement, Public Private Infrastructure Partnerships (PPP) and Projects Management Professional. He holds a Bachelors and Master's Degree – Public Finance & Financial Services Law in Law both from the University of Nairobi, School of Law. He is currently a PhD in Law Candidate at the Stellenbosch University, Cape Town, South Africa.

\*He is a Member of the Chartered Institute of Arbitrators (MCI Arb, Kenya & UK – London Chapters), Institute of Directors (K), Kenya Institute of Management, Certified Pension Schemes Trustee and a Certified Integrity Assurance Officer.

\*The author is currently the Chief Legal Officer, Projects & Disputes Resolution at the Kenya Electricity Generating Company PLC. He also serves as a member of the Audit Committee with the Office of the Attorney General & Department of Justice, Kenya, Board Member with the Anglican Development Services Eastern and also Rotary Club of Karura. He has previously served as Audit Committee Member with the Ministry of Environment & Forestry, Kenya.

<sup>1</sup> Miller A and Oats L, 'Introduction to taxation', 3<sup>rd</sup> ed, *Principles of international taxation*, A&C Black, 2012, 3.

<sup>2</sup> Saleemi NA, *Taxation simplified*, East Africa Edition, Nairobi, 2014, 1.

<sup>3</sup> Warris A, Kohenen M, Ranguma J and Mosioma A, 'Taxation and state building in Kenya: Enhancing revenue capacity to advance human welfare' *Kenya Report*, 2009, 6.

<sup>4</sup> Sebastian LN and Godoy B, 'Taxation as a human rights issue' -<http://www.ibanet.org/Article/Detail.aspx?ArticleUid=4d8668cb-473a-44ea-b8be-1327d6d9d977> on 28 June 2017.



Article 43 of the Constitution of Kenya,<sup>5</sup> entrenches and recognises that every person has the right to the highest attainable standard of health, which includes the right to health care services, including reproductive health care, right to accessible and adequate housing, and to reasonable standards of sanitation, to be free from hunger, and to have adequate food of acceptable quality, to clean and safe water in adequate quantities, to social security; and to education. It also provides that a person shall not be denied emergency medical treatment and that the State shall provide appropriate social security to persons who are unable to support themselves and their dependants.

Article 21(2) stipulates that the State shall take legislative, policy and other measures, including the setting of the standards to achieve the progressive realisation of the rights guaranteed under Article 43. The Bill of Rights applies to all and binds all State organs and all persons<sup>6</sup> and every person has a right to enjoy the rights and fundamental freedoms in the Bill of Rights to the greatest extent consistent with the nature of the right.<sup>7</sup> It is a fundamental duty of the State and every State organ to observe, respect, protect, promote and fulfil the rights and fundamental freedoms in the Bill of Rights.<sup>8</sup> The Bill of Rights remain enforceable<sup>9</sup> and the courts have the authority to enforce them by declaring of rights, issuance of injunction, conservatory orders among other reliefs.<sup>10</sup> These State obligations as laid out under Article 43 among others of the Constitution can only be met through effective and enhanced taxation regime. Important to note also is that effective fulfilment of these obligations plays a big role in the preservation of Kenya or any other nation as a Sovereign Republic<sup>11</sup> and where these obligations are not met or are compromised then the sovereignty of the nation is as well compromised.

### A review of decided Foreign Cases and Tax Statutes Interpretation

Before the decision in the case of *Kenya Revenue Authority v Yaya Towers Limited*<sup>12</sup> it appears that there had been no local decision emanating from the Kenyan courts on the taxability of income derived from illegal activities.<sup>13</sup> Taxation of illegal income has however been a topic of debate in different jurisdictions and if the long chain of authorities from the commonwealth is anything to go by, it can authoritatively be said that the proceeds are subject to taxation.

---

<sup>5</sup> *Constitution of Kenya* (2010).

<sup>6</sup> Article 20(1), *Constitution of Kenya* (2010).

<sup>7</sup> Article 20(2), *Constitution of Kenya* (2010).

<sup>8</sup> Article 21(1), *Constitution of Kenya* (2010).

<sup>9</sup> Article 22(1) and (2), *Constitution of Kenya* (2010).

<sup>10</sup> Article 23, *Constitution of Kenya* (2010).

<sup>11</sup> Article 4(1), *Constitution of Kenya* (2010).

<sup>12</sup> *Kenya Revenue Authority v Yaya Towers Limited* (2008) and the subsequent successful Appeal of *Kenya Revenue Authority v Yaya Towers Limited* (2016) eKLR.

<sup>13</sup> *Kenya Revenue Authority v Yaya Towers Limited* (2016) eKLR.



In the case of *Minister of Finance v Smith* Lord Haldane stated thus: -

*'the Income Tax Act is not necessarily restricted in its application to lawful business only. The Revenue merely looks at an accomplished fact. It brings the profit to tax but it does not condone or take part in the illegal enterprise. Prosecutions for the offence will not disentitle the Income Tax department from taxing the profits arising out of the commission of the offence'.<sup>14</sup>*

In the case of *James v United States*, the Supreme Court of the United States held that money obtained by a taxpayer illegally was taxable income, even though the law might require the taxpayer to repay the ill-gotten gains to the person from whom they had been taken.<sup>15</sup> In this case, the defendant was an official in a labour union where he had embezzled more than Seven Hundred and Thirty-Eight Thousand US dollars in union funds. His tax returns did not disclose this. During his trial for tax evasion, he claimed in his defence that embezzled funds did not constitute taxable income. His argument was that, just as the receipt of loan proceeds is not taxable to the borrower, the person who embezzles money should not be treated as having received income, the reason for this being that person is legally obligated to return those funds to their rightful owner. The Supreme Court ruled that under section 22(a) of the Internal Revenue Code of 1939 and section 61(a) of the Internal Revenue Code of 1954, the receipt of embezzled funds was supposed to be included in the gross income of the wrongdoer and was taxable to the wrongdoer, even though the wrongdoer had an obligation to return the funds to the rightful owner. The Court noted that the scope of the Sixteenth Amendment was not limited to "lawful" income, a distinction which *had* been found in the Revenue Act of 1913. The absence of the "lawful" modifier indicated that the framers of the Sixteenth Amendment had intended no safe harbour for illegal income. The Court ruled that James was therefore liable for the federal income tax due on his embezzled funds. Although Eugene James avoided criminal liability, the opinion of the Court left James in a situation where he would be required not only to repay the embezzled Seven Hundred and Thirty-Eight Thousand US dollars to the union, but would also be required to pay federal income taxes on the receipt of those funds, just as though he had been able to keep them.

In *Mann v Nash (H.M Inspector of Taxes)*,<sup>16</sup> the Appellant was in the business of providing automatic machines for public use, the use of which had been found to be illegal. The Appellant contended that part of his profits was immune from taxation on the ground that it had been earned by unlawful means. The court found that the state could not keep its eyes closed in spite of the illegality. Rowlatt, J in his judgment stated:

*'The question is whether as a matter of construction those words are to be cut down by an overriding consideration that the trade is tainted with illegality. The great mainstay of Mr. Field's argument, quite rightly from his point of view, was the case of Duggan (1), decided in the Irish Free State, and that the decision of the Supreme Court seems to have gone upon this principle, that no construction could be admitted which recognised that the State could come forward seem to take a profit from what the State prohibited because the State ought to have prevented it; and it was argued, if I may venture to say so, in a somewhat*

---

<sup>14</sup> *Minister of Finance v Smith* (1927), The United Kingdom Appeal Cases.

<sup>15</sup> *James v United States* (1961), The Supreme Court of the United States.

<sup>16</sup> *Mann v Nash (H.M Inspector of Taxes)* (1932), The United Kingdom Court of King's Bench.



*rhetorical style: Does the State keep its revenue eye open and its eye of justice closed? I must say, I do not feel the force of that observation at all.....In truth, it seems to me that all the consideration is misconceived. The Revenue representing the State, is merely looking at an accomplished fact. It is not condoning it; it has not taken part in it. It merely finds profit made from what appears to be a trade, and the Revenue laws happen to say that the profits made from trades have to be taxed, and they say: "Give us tax." It is not to the purpose in my judgment to say:*

*"But the same State that you represent has said they "are unlawful:" that is immaterial altogether and I do not see that there is any contact between the two propositions. It was said in the Irish case that *allegans suam turpitudinem non est audiendus*. I cannot see that the State are alleging their own turpitude; it is the Appellant who is alleging his own turpitude. The State says: "It is a business; " the Appellant says: "It is an unlawful one". He is alleging his own turpitude. It is said again: "Is the State coming forward to take a share "of unlawful gains?" It is mere rhetoric. The State is doing nothing of the kind; they are taxing the individual with reference to certain facts. They are not partners; they are not principals in illegality, or sharers in the illegality; they are merely taxing a man in respect of those resources.'*

In *Southern (H.M Inspector of Taxes v A.B)*<sup>17</sup> concerning profits of illegal vetting transactions the court held that although the businesses carried on by the respondents were unlawful, they nevertheless constituted a trade within the meaning of the Income Tax Acts and that the profits were therefore properly assessable to income tax. In *F.A. Lindsay, E.A Woodward & W. Hiscox v Commissioner of Inland Revenue*<sup>18</sup> the appellants contended that the transactions carried out by them were illegal and that the profit arising therefore was not assessable. In his judgment Lord Morison stated:

*'It is quite immaterial that the particular method of carrying on the trade involved the making of a false declaration to the Customs authorities or giving bribes to persons in America. In my opinion, these are entirely irrelevant considerations. When it is established that a trade has existed for a year, the question is whether it realised a profit as ascertained under the rules of the statute. It is quite in vain for the person who has realised the profit to prove that he made it by fraudulent trading., or to attempt to contend that the profit he has earned ought to escape chargeability because he might have been convicted of a breach of the law....It is, in my opinion absurd to suppose that honest gains are charged to tax and dishonest gains escape. To hold otherwise would involve a plain breach of the rules of the statute, which require the full amount of the profits to be taxed and merely put a premium on dishonest trading. The burglar and the swindler, who carry on a trade or business for profit, are as liable to tax as honest business man, and, in addition, they get their desserts elsewhere'.*

What is clear from the foregoing avalanche of cases is that the courts have agreed in principle that the Congress did not intend to create any distinction between honest and dishonest taxpayers. The defining theme is that income is taxable regardless of the illegality of its generation.

---

<sup>17</sup>*Southern (H.M Inspector of Taxes v A.B)* (1933), The United Kingdom Court of King's Bench.

<sup>18</sup> *F.A. Lindsay, E.A Woodward & W. Hiscox v Commissioner of Inland Revenue* (1933), The United Kingdom Court of King's Bench.





i. *The Kenyan Case: Kenya Revenue Authority v Yaya Towers Limited (2016) eKLR*<sup>19</sup>

This case began in August 2006 where the High Court decided in favour of Yaya Towers Limited which had argued that the income tax the Kenya Revenue Authority (KRA) had demanded from payments made to Mr. David Peter Saunder, a foreigner, illegally engaged by Yaya Towers Limited, was not justified in law. The learned Justice Joseph Nyamu in November 2008 ruled in favour of Yaya Towers citing the unlawful employment of Mr David Peter Saunder. In effect, the Kenya Revenue Authority was prohibited from demanding the tax from Yaya Towers Limited. The rationale for the ruling was that demanding such tax would go against public policy and would amount to the KRA benefiting from an illegality.

Afterwards, the KRA through its Legal Counsel Mr. Paul Matuku appealed the said decision. The taxman faulted the 2008 High Court decision citing Section 3(1) of the Income Tax Act, which provides for the taxation of “all the income of a person”. The taxman’s Legal Counsel relied on several English authorities a number of them discussed above to support his argument for the taxation of the income in question. The Court of Appeal’s ruling allowing taxation of illegal trade now clears the way for the taxman and hands the KRA a lifeline to pursue thousands of businesses whose incomes have largely remained elusive and outside the tax bracket on the basis of being derived from illegal activities.

### **Why the call for the amendment of the Income Tax Act?**

In this case, this author seeks to answer the question why amendment of the Income Tax Act, to expressly provide for the taxation of incomes from illegal activities, is important.

*Firstly*, income from illegal activities to mention but a few include, corruption, fraud, theft, embezzlement, extortion and by extension money laundering *strictly* interpreted may not fall within the scope of classes of income stated in sub-section 3(1) and (2) of the Act and thus may not be amenable to taxation. This is no doubt the reason why the high court decision was in favour of Yaya Towers Limited. One of the principles of taxation is that tax collection should be able to be done in an economical way. In other words, tax should be collected at the least cost. It therefore follows that if tax collection will necessitate court suits or any other form of litigation then it ceases being economical hence undermining this vital principle. Arguments about whether income from criminality is taxable or not have continued despite this recent judgement. In light of the foregoing and to ease tax compliance and administration of income from illegal activities there is no doubt therefore, that there is need to re-enact sections 3(1) and (2) in clear terms to bring the taxation of illegal income tax in the tax bracket. In the case of *Jafferli Mohamedali Alibhai v The Commission Income Tax* it was stated that the subject is not to be taxed unless the words of the taxing statute unambiguously impose the tax upon him.<sup>20</sup> Nothing summarises the above position better than the *Broom Legal Maxims*:

---

<sup>19</sup>This was an Appeal from the Judgment and Decree of the High Court of Kenya at Nairobi (Nyamu, J) made on 21 November 2008 in Nairobi High Court Miscellaneous Application No. 374 of 2006.

<sup>20</sup> *Jafferli Mohamedali Alibhai v The Commission Income Tax* (ETC VOL. 3 Par. 11 Case 84).



*'a remedial statute therefore shall be construed so as to include cases which are within the mischief which the statute was intended to remedy; whilst, on the other hand, where the intention of the Legislature is doubtful, the inclination of the court will always be against that construction which imposes a burden, tax or duty or the subject. It has been designated as "a great rule" in the construction of fiscal law, "that they are not to be extended by any laboured construction, but that you must adhere to the strict rule of interpretation; and if a person who is subjected to a duty in a particular character or answers that description, the duty no longer attaches upon him and cannot be levied. A penalty moreover must be imposed by clear words. The words of a statute shall be restrained for the benefit of him against whom the penalty is inflicted, and the language of the statute must be strictly looked at in order to see whether the person against whom the penalty is sought to be enforced has committed an offence to do with it.".....The principle remarked Lord Abinger "adopted by Lord Tenterden, that a penal law ought to be construed strictly is not only a sound one, but the only one consistent with our free institutions. The interpretation of statutes has always in modern times been highly favourable to the personal liberty of the subject and I hope will always remain so". "Nevertheless taxation is clearly "penal" within this section of the Code, and must not be enforced by the courts unless clearly imposed. As Evans LJ said in the context of tax legislation it is necessary to consider the legal analysis with the utmost precision so that the taxpayer shall not become liable to tax unless this is clearly and unequivocally the object of the statutory provisions ... The Courts are reluctant to adopt a construction permitting a person's tax liability to be fixed by administrative discretion'.*

The upshot of the above statement is simply that in a taxing Act, one has to look merely at what is clearly said. There is no reason for any inference or constraining the language used. Lord Russel of Killowen in *Inland Revenue Commissioner v Duke of Westminster* stated thus: *'the subject is not taxable by inference or by analogy, but only by the plain words of a statute applicable to the facts and circumstances of his case'*.<sup>21</sup> In the related case of *Ramsay Ltd v Inland Revenue Commissioner*<sup>22</sup> the court opined that *'A subject is only to be taxed on clear words not upon intendment, or upon the "equity" of an "Act". Any taxing Act of Parliament has to be construed in accordance with this principle'*.

Closely related to the foregoing is the principle of legality. As Lord Hoffman famously observed in *R v Secretary of State for the Home Department; Ex parte Simms*:

*'The principle of legality means that the parliament must squarely confront what it is doing and accept the political cost. Fundamental rights cannot be overridden by general or ambiguous words. This is because there is too great a risk that the full implications of their unqualified meaning may have passed unnoticed in the democratic process. In the absence of express language or necessary implication to the contrary, the courts therefore presume that even the most general words were intended to be subject to the basic rights of the*

---

<sup>21</sup>*Inland Revenue Commissioner v Duke of Westminster* (1936), The United Kingdom Appeal Cases.

<sup>22</sup> *Ramsay Ltd v Inland Revenue Commissioner* (1992), The United Kingdom Appeal Cases



Secondly, a vague law impermissibly creates dangers of arbitrary and discriminatory application. On his part Lord Diplock in *Black-Clawson International Limited v Papierwerke Waldhof-Aschaffenberg AG*<sup>24</sup> commented that the acceptance of the rule of law as a constitutional principle requires that a citizen before committing himself to any course of action should be able to know in advance what are the legal consequences that flow from it. Therefore, elementary justice or the need for legal certainty demands that the rules by which the citizen is to be bound should be ascertainable by him by reference to identifiable sources that are publicly accessible, clear and not vague. It is important to have clarity and certainty. It is therefore clear under the principle of legality, two principles emerge: (i) no one should be punished under a law unless it is sufficiently clear and certain to enable him to know what conduct is forbidden before he does it.; and (ii) no one should be punished for any act which was not clearly ascertainably punishable when the act was done.<sup>25</sup> It's this author's view that vague laws aren't just a threat to individual freedom but they also constrict economic growth and discourage legitimate enterprise. It is trite law that a statute may be called void for vagueness reasons when an average citizen cannot generally determine what persons are regulated, what conduct is prohibited or what punishment may be imposed or when tax is legally due and payable. As Justice Thurgood Marshall once wrote, '*vague laws lead citizens to steer far wider of the unlawful zone....than if the boundaries of the forbidden areas were clearly marked*'.<sup>26</sup>

It's important to create certainty in business. Certainty is an ingredient of the rule of law stated to be a lifeline of business and business plans and its enforcement has linkages to emerging and thriving economies.<sup>27</sup> It's my view that tax provisions should be clear and simple to understand so that taxpayers know where they stand. A simple tax system makes it easy for individuals and businesses to understand their obligations and entitlements. As a result, businesses are more likely to make optimal decisions. If anything, complexity favours aggressive tax planning, which may trigger deadweight losses for the economy.

Third, Article 210(1) of the Constitution provides that no tax may be imposed, waived or varied except as provided for by legislation. It therefore follows that any clear basis of taxation of income derived from illegal activities ought to be anchored in legislation as absence of this exposes the taxman to the technical challenges of taxing without a legal basis. Closely related to this provision is Section 196(2) of the Public Finance Management Act<sup>28</sup> which states that a public officer shall not raise revenues other than in accordance with the Constitution or an Act of Parliament.

---

<sup>23</sup> *R v Secretary of State for the Home Department; Ex parte Simms* (2000), The United Kingdom Appeal Cases.

<sup>24</sup> *Black-Clawson International Limited v Papierwerke Waldhof-Aschaffenberg AG* (1975), The United Kingdom Appeal Cases.

<sup>25</sup> *Law Society of Kenya v The Kenya Revenue Authority & Honourable Attorney General* (2017) eKLR.

<sup>26</sup> <https://www.forbes.com/2010/03/30/vague-laws-economy-government-opinions-timothy-sandefur.html>.

<sup>27</sup> *Keroche Industries Limited v KRA & 5 Others* (2007) eKLR.

<sup>28</sup> Section 196(2), Public Finance Management Act (2012).





*Fourth*, Article 201(b)(i) of the Constitution provides that the public finance system shall promote an equitable society and in particular the burden of taxation shall be fairly shared. Equity is an important consideration within a tax policy framework. This was one of the grounds upon which the taxation of capital gains tax on or before actual transfer of the property instead of upon registration of the transfer instrument in favour of the transferee was declared void in the case of the *Law Society of Kenya v The Kenya Revenue Authority & Honourable Attorney General*.<sup>29</sup>

Indeed, Article 210(3) calls for equality of treatment of everyone, including State Officers when it comes to the application and implementation of taxation under the Constitution. In the case of *Timothy Njoya & 17 Others v Attorney General & 4 Others*<sup>30</sup> M. Wasarme, J.A held that to accord or grant some state officers (in this case Members of the National Assembly by exempting them from payment of income tax) greater weight, recognition or respect than others for any reason was discriminatory and offensive to the letter and the spirit of the Constitution and that it is also an attempt to degrade, subvert and destroy the sovereign will of the citizens of Kenya.

*Fifth*, Article 10(1)(a)(b) and (c) read together with Article (2)(b) of the Constitution binds state organs, state officers, public officers and all persons to ensure that in applying or interpreting the Constitution, enacting, applying or interpreting any law, or making or implementing policy decisions they shall give regard to equity, social justice and equality. Taxation of this income would therefore bring fairness and equity which are key cannons of taxation.

*Sixth*, the non-payment of the tax out of income from illegal activities leads to absurdity in that, gains out of honest business are taxed whilst the ones from dishonest ones' escape taxation. Clearly it does not satisfy sense of justice to tax persons in legitimate enterprises and to allow those who thrive by violation of the law to escape. For this contention, this author is guided by the principles in the Constitution and the principles of statutory interpretation that there is need to construe a statute in a manner that does not lead to absurdity, contradiction, unworkable or illogical result and the need to adopt an interpretation that will best serve public interest, and guided by the letter and spirit of the Constitution.

The merit in this proposition is that holding otherwise would entitle a wrong doer to benefit from the illegal profits earned from unlawful business and on top of that be exempted from taxation. Echoing the words of Lord Morison to hold otherwise would lead to absurdity that gains of an honest business are taxed whilst the dishonest escape taxation. Secondly, if it was to be held that profits of such illegal business are not taxable, this would serve as an incentive to engagement in illegal activities and tax payers would endeavour to have their businesses tainted with illegality for the purposes of securing exemption from tax.

---

<sup>29</sup>*Law Society of Kenya v The Kenya Revenue Authority and Honourable Attorney General* (2017) eKLR.

<sup>30</sup>*Timothy Njoya & 17 Others v Attorney General and 4 others* (2013) eKLR.



## Emerging Constitutional issues / Legality Challenges

Under the Constitution of Kenya,<sup>31</sup> a number of provisions are likely to pose technical challenges for the KRA in its tax creation and enforcement efforts. For example, Article 47 of the Constitution provides that every person has the right to administrative action that is expeditious, efficient, lawful, reasonable and procedurally fair. The Fair Administrative Actions Act<sup>32</sup> gives effect to this provision. It therefore follows that the KRA will have to faithfully discharge its mandate whilst giving full effect to these provisions and where any taxpayer feels aggrieved, he or she has the right to approach the Courts for relief under these provisions putting spanner into the works for the taxman.

Under Article 49(1)(a) (ii) (iii) & (b) an arrested person has the right to remain silent while under Article 49(1)(d) s/he has a right not to be compelled to make any confession or admission that could be used in evidence against him/her. Article 50(2) provides that every accused person has the right to a fair trial, which includes the right:

- (a) to be presumed innocent until contrary is proved;
- (i) to remain silent, and not to testify during the proceedings;
- (k) to adduce and challenge evidence;
- (l) to refuse to give self- incriminating evidence.

It would therefore and literally appear that these rights are available to the tax payer and in this case not to self-incriminate him or herself for any undeclared illegal income. There is an arguable point however that the constitutional safeguards under Articles 49 and 50 are only available and accrue to the taxpayer once an arrest has already been effected and as at the time of trial.<sup>33</sup>

## CONCLUSION

Taxes are the most sustainable source of revenue for any government. Tax revenue is an enabler for the government to carry out the legal obligations of ensuring progressive realisation of human rights.<sup>34</sup> In fact, tax payment is the price citizens pay for the essential infrastructure and services provided by the government. Taxation thus remains a 'necessary evil' if the Kenya government is to shield and retain its citizen's sovereignty. To this extent, any tax system should be dynamic and have a wide enough tax base to keep pace with the ever growing Constitutional and International Legal Instruments State obligations to the citizens.

---

<sup>31</sup> *Constitution of Kenya* (2010).

<sup>32</sup> *The Fair Administrative Actions Act* (2015).

<sup>33</sup> For a detailed discussion refer to the following publications: - Maina E and Paranta E, 'Taxing income from illegal activity: The Kenyan perspective' *Strathmore Law Review*, 2017, 103 - 121; and also Mutile ME, 'Taxation of gains from illegal activities in Kenya: A case for legislative intervention' Unpublished LLM Thesis, University of Nairobi, 2018.

<sup>34</sup> Sebastian LN and Godoy B, 'Taxation as a human rights issue'.



The widening of the tax base should include income from illegal activities in the clearest way possible. The reason for this argument is that in a series of cases dating back to the 1920's, several courts have been called upon to decide whether earnings derived from unlawful activities constitute taxable income. These cases expound a number of issues among them rules of interpretation of tax laws and application of various tax law principles. Key to note is that tax has to be authorised in clear words and cannot be done on intendment or inference and certainty is an ingredient of the rule of law and a lifeline of business<sup>35</sup>.

Through the analysis of these cases, it's this author's conclusion that the Kenyan tax legislations and in particular the Income Tax Act contains no clear answer on this issue and that therefore the debate may appropriately be resolved from a legislative intervention. This author admits that there are arguable reasons against taxation of income from illegal activities, such as public policy<sup>36</sup>, possibility of prejudice to the defendants at trial among others. There are also technical challenges and emerging constitutional issues but this author contends that these problems can be resolved and should not in any be used or allowed to be invoked to deter taxation of income derived from illegal activities.

The upshot of my essay is that the National Assembly ought through the window created under Article 209(1)(a) and (2) of the Constitution have the Income Tax Act amended to have a 'catch-all' provision for taxation of 'all gains, profits and income' from *whatever source* derived (legal or otherwise). To this extent author associates himself with the views of Dr Bosire Nyamori.<sup>37</sup>This author remains conscious that taxation of income from illegal activities remain contentious and raise complex and competing questions of law that are not easy to resolve. This nevertheless should not dampen the clarion call for the proposed amendments as the benefits of the proposed amendments far outweigh maintaining the law as it is.

## CONFLICT OF INTEREST DECLARATION

The author registered no conflict of interest in this study.

## ARTICLE NOT UNDER CONSIDERATION ELSEWHERE

The Author declares that this article is not under consideration elsewhere and that it has not been published or pending publication elsewhere.

---

<sup>35</sup>*Keroche Industries Limited v Kenya Revenue Authority & 5 Others* (2007) eKLR.

<sup>36</sup> The principle of public policy was applied in the case of *Omega Enterprises (K) Ltd v KTDC & Others* (1998) which held:

*'If an act is void, then it is in law a nullity. It is not only bad, but incurably bad. There is no need for an order of the court to set it aside. It is automatically null and void without more ado, though it is sometimes convenient to have the court declare it to be so. And every proceeding which is founded on it is also bad and incurably bad. You cannot put something on nothing and expect it to stay there. It will collapse'.*

<sup>37</sup>Mwere D, 'Lecturer wants proceeds from illegal business taxed' The Star, 23 July 2016-< <https://www.the-star.co.ke/news/2016/07/23/lecturer-wants-proceeds-from-illegal-business-taxed>> on 17 April 2020.



## BIBLIOGRAPHY

### Books

Saleemi NA, *Taxation simplified*, East Africa Edition, Nairobi,2014.

### Cases

*Black-Clawson International Limited v Papierwerke Waldhof-Aschaffenberg AG* (1975), The United Kingdom Appeal Cases.

*F.A. Lindsay, E.A Woodward & W. Hiscox v Commissioner of Inland Revenue* (1933), The United Kingdom Court of King's Bench.

*Inland Revenue Commissioner v Duke of Westminster* (1936), The United Kingdom Appeal Cases.

*Jafferli Mohamedali Alibhai v The Commission Income Tax* (ETC VOL. 3 Par. 11 Case 84).

*James v United States* (1961), The Supreme Court of the United States.

*Kenya Revenue Authority v Yaya Towers Limited* (2008).

*Kenya Revenue Authority v Yaya Towers Limited* (2016) eKLR.

*Keroche Industries Limited v KRA & 5 Others* (2007) eKLR.

*Law Society of Kenya v The Kenya Revenue Authority & Honourable Attorney General* (2017) eKLR.

*Mann v Nash (H.M Inspector of Taxes)* (1932), The United Kingdom Court of King's Bench.

*Minister of Finance v Smith* (1927), The United Kingdom Appeal Cases.

*Omega Enterprises (K) Ltd v KTDC & Others* (1998).

*Ramsay Ltd v Inland Revenue Commissioner* (1992), The United Kingdom Appeal Cases.

*R v Secretary of State for the Home Department; Ex parte Simms* (2000), The United Kingdom Appeal Cases.

*Southern (H.M Inspector of Taxes v A.B)* (1933), The United Kingdom Court of King's Bench.

*Timothy Njoya & 17 Others v Attorney General and 4 others* (2013) eKLR.

### Chapter in Books

Miller A and Oats L, 'Introduction to taxation', 3<sup>rd</sup> ed, *Principles of international taxation*, A&C Black, 2012, 3.

### Journal Articles

Maina E and Paranta E, 'Taxing income from illegal activity: The Kenyan perspective' *Strathmore Law Review*, 2017.

Warris A, Kohenen M, Ranguma J and Mosioma A, 'Taxation and state building in Kenya: Enhancing revenue capacity to advance human welfare' *Kenya Report*,2009.



## Legislations

*Constitution of Kenya* (2010).

*The Fair Administrative Actions Act* (2015).

*The Public Finance Management Act* (2012).

## Newspaper Article

Mwera D, 'Lecturer wants proceeds from illegal business taxed' The Star, 23 July 2016-< <https://www.the-star.co.ke/news/2016/07/23/lecturer-wants-proceeds-from-illegal-business-taxed>>.

## Online Sources

Sebastian LN and Godoy B, 'Taxation as a human rights issue'-  
<http://www.ibanet.org/Article/Detail.aspx?ArticleUid=4d8668cb-473a-44ea-b8be-1327d6d9d977>.

<https://www.forbes.com/2010/03/30/vague-laws-economy-government-opinions-timothy-sandefur.html>.

## Thesis

Mutile ME, 'Taxation of gains from illegal activities in Kenya: A case for legislative intervention' Unpublished LLM Thesis, University of Nairobi, 2018.

