

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
TAX APPEAL NO. 115 OF 2017

DIGITAL BOX LIMITED.....APPELLANT

VS

**COMMISSIONER OF INVESTIGATION &
ENFORCEMENT.....RESPONDENT**

JUDGMENT

BACKGROUND

1. The Appellant is a limited liability company incorporated under the Companies Act (CAP 486) Laws of Kenya. The Appellant is in the business of buying and selling of electronics.
2. The Respondent is established under the Kenya Revenue Authority (KRA) Act, Chapter 469 Laws of Kenya and is mandated with the assessment and collection of all Government Revenue.
3. The Respondent obtained a search warrant through Nairobi Chief Magistrate Miscellaneous Criminal Application No. 545 of 2017 to search the premises of the Appellant.
4. On 21st February 2017 the Respondent raided and conducted the search at the Appellant's business premises located at Luthuli Avenue and the residence of one of its directors located in Parklands within the Nairobi County.
5. On 28th April 2017 the Respondent issued a notice of assessment to the Appellant for the period 2012 to 2016. In the assessment, the Respondent demanded tax amounting to Kshs. 532,798,033.00 being Income Tax on under-declared taxable income inclusive of interest and further Value Added

Tax (VAT) assessment on under-declared sales totaling Kshs. 175,113,469.00 plus interest of Kshs. 44,151,290.00.

6. The Appellant objected to the assessment vide a letter dated 24th May 2017. The Respondent issued its Objection Decision vide a letter dated 6th June 2017 confirming the assessment and demanding total tax of Kshs. 700,548,224.00 being Income Tax of Kshs. 481,521,086.00 plus VAT of Kshs. 219,027,138.00 inclusive of penalties and interest.
7. Being aggrieved by the objection decision, the Appellant filed its Memorandum of Appeal with the Tribunal on 19th July, 2017.

THE GROUNDS OF APPEAL

8. The grounds of Appeal presented in the Memorandum of Appeal filed on 19th July 2017 are:
 - i) The Respondent erred both in fact and in law by failing to predicate its Objection Decision on material facts and consequently, the reasons for its decision were based on extraneous considerations.
 - ii) The Respondent erred both in fact and in law by basing its assessment of the sales made and VAT payable by the Appellant upon purported delivery notebooks.
 - iii) The Respondent erred both in fact and in law by basing its tax assessment dated 28th April 2017 upon documents other than those kept and maintained by the Appellant to record sales and consequently arriving at a misapprehended finding that there existed alleged unbanked sales.
 - iv) The Respondent erred in its analysis of the Appellant's bank statement by misapplying the banking analysis test to establish the Appellant's income for the period under review consequently arriving at an incorrect and exaggerated figure of taxable income.

- v) The Respondent erred both in fact and in law in re-determining the Appellant's taxable income for the 2012, 2013 and 2014 years of income whereas the Appellant had paid up all the taxes due on its income for those years including a further demand levied by the KRA and paid by the Appellant in 2015.
- vi) The Respondent erred in finding that the Appellant is liable to pay Kshs. 700,584,224.00 whereas acknowledging that it had not considered the costs of the purchases for the years 2014, 2015 and 2016 in its computation.
- vii) The Respondent's assessment of the Appellant's taxable income for the year under review is erroneous for failing to consider that the Appellant has not yet concluded auditing of its accounts for the years 2015 and 2016 so as to self-assess and pay the resultant taxes thus resulting in an inappropriate condemnation of the Appellant for alleged failure to remit rightful taxes to KRA for the said years.
- viii) The Respondent erred both in fact and in law in assessing and re-assessing the Appellant's taxable income on considerations that are extraneous and in flagrant disregard for the Income Tax Act and the Tax Procedures Act.

The Appellant's Prayers

- i) The Respondent's Notice of Assessment dated 28th April 2017 be quashed and/or be set aside;
- ii) The Respondent's Objection Decision dated the 6th June 2017 be quashed and/or be set aside; and
- iii) Costs of this Appeal be borne by the Respondent.

THE APPELLANT'S CASE

9. The Appellant averred that the Respondent erred both in fact and in law by failing to predicate its Objection Decision on material facts and consequently based its decision on extraneous considerations.
10. The Appellant argued that the Respondent erred both in fact and in law by basing its assessment of the sales made and VAT payable by the Appellant upon purported delivery notebooks.
11. The Appellant submitted that the Respondent erred both in fact and in law by basing the tax assessment dated 28th April 2017 upon documents other than those kept and maintained by the Appellant to record sales and consequently arrived at the misapprehended finding that there existed alleged unbanked sales.
12. According to the Appellant, the Respondent failed to show that the delivery notebooks are in relation to transactions that are connected to the Appellant and hence entitling the Respondent to rely upon them to assess the Appellant.
13. The Appellant averred that the Respondent erred in its analysis of the Appellant's bank statement by misapplying the banking analysis test to establish the Appellant's income for the period under review. Consequently, it arrived at an incorrect and exaggerated figure of taxable income. The Appellant submitted what it averred was a summary of its bank records for the year under review as follows:

Year	2012	2013	2014	2015	2016
Amount Banked	61,440,299	78,924,500	37,597,300	17,653,260	20,362,653

14. To support this, the Appellant submitted copies of its bank statements from Barclays Bank in its bundle of documents dated 6th September 2019.

15. The Appellant further averred there is a sharp contrast between the amounts that the Respondent claims that the Appellant should pay in taxes vi-a-vis the amounts that the Appellant actually incurred in taxable income which is subject to taxation by the Respondent as shown in the table below:

Year	2012	2013	2014	2015	2016
Appellant's actual sales	72,682,954	101,447,691	39,086,139	18,442,361	14,021,999
Purported sales as per the Respondent	120,960,173	307,316,475	580,504,166	519,894,266	170,923,160
Difference	48,276,219	205,868,784	541,418,027	519,894,266 (presumption that the Appellant filled nil returns)	170,923,160 (presumption that the Appellant filled nil returns)

16. According to the Appellant, the records clearly show that the Respondent used unrealistic figures to arrive at the assessment that it made on the Appellant.
17. The Appellant argued that it filed a ledger at the Tribunal on 6th September 2019. The ledger, the Appellant averred, contains records of transactions that it undertook in the period under review which tally with the records that it shared with the Respondent from the time it was served with an assessment. The record, according to the Appellant, is as shown below:

Year	2012	2013	2014	2015	2016
Sales(Ksh)	72,682,954	101,447,691	39,086,139	18,442,361	14,021,999

18. The Appellant further averred that the assertion by the Respondent in its submissions that the information is not sufficient is misleading as the record indicates the transactions that the Appellant was involved in and the amounts that were involved.
19. According to the Appellant, the amounts that the Respondent levied upon the Appellant could not therefore represent the correct amounts that it was liable to pay taxes upon.
20. The Appellant further argued that it could not have generated such sums as the Respondent would wish the Tribunal to believe and if allowed to stand, will completely bankrupt the Appellant. To buttress its argument the Appellant relied on **Silver Chain Limited v Respondent Income Tax & 3 others [2016] eKLR**, where Justice S.J Chitembwe stated thus:

“The task of collecting taxes should not lead to discouraging taxpayers from carrying on with their businesses. If the taxpayers close shop, there will be no taxes to be collected. On the other hand, if no taxes are paid, there will be no funds to run government operations. This calls for a balance between the tax collectors and taxpayers whereby the process becomes inclusive as opposed to being unilateral. There must be fairness in the process of tax assessment”

21. The Appellant argued that the Respondent’s actions are manifestly unjust noting that the Respondent is subjecting the Appellant to unreasonable assessment which is over and above what it should pay.
22. The Appellant argued that the Respondent erred both in fact and in law in re-determining the Appellant’s taxable income for the 2012, 2013 and 2014 years of income whereas the Appellant had paid up all the taxes due on its income for those years including a further demand levied by KRA and paid by the Appellant in 2015.

23. The Appellant submitted that the Respondent erred in finding that the Appellant is liable to pay Kshs. 700,548,224.00 without taking into account the costs of the purchases for the years 2014, 2015 and 2016 in its computation.
24. The Appellant averred that the Respondent's assessment of its taxable income for the year under review is erroneous for failing to consider that the Appellant has not concluded auditing of its accounts for the years 2015 & 2016 so as to self-assess and pay the resultant taxes thus resulting in an inappropriate condemnation of the Appellant for alleged failure to remit rightful taxes to KRA for the said years.
25. The Appellant argued that the Respondent erred both in fact and in law in assessing and re-assessing the Appellant's taxable income on considerations that are extraneous and in flagrant disregard of the Income Tax Act and the Tax Procedures Act.
26. The Appellant submitted that it has instructed its auditors to undertake a thorough review of its accounts for the period under review as well as the Respondent's purported enforcement action including the Respondent's notice of the assessment dated 28th April 2017 and Objection Decision dated the 6th June 2017 with a view to highlighting on the Respondent's faults and the failures and the reasons the Appellant is not liable to pay the taxes assessed by the Respondent.
27. The Appellant submitted that it filed its returns as required under the law and at no point did it misrepresent itself as to the transactions it incurred for the period under review.

THE RESPONDENT'S CASE

28. The Respondent submitted it obtained a search warrant from court in Nairobi Chief Magistrate Miscellaneous Criminal application No. 545 of

2017 and pursuant to the search warrant, conducted a search at the Appellant's premises as well as that of its director.

29. The Respondent submitted that during the search, its officers obtained various documents and records for examination and analysis to confirm the veracity of the allegations that had been made regarding the Appellant's tax compliance. After the search, the Respondent's officers prepared an inventory of the goods seized and the same was countersigned by the representatives of the Appellant who were present during the search.
30. The Respondent submitted that it reviewed the Appellant's sales records to establish the total sales for the 2012 to 2016 years of income. The Respondent averred that it reviewed daily sales records maintained by the Appellant through delivery notebooks for sale of mobile phone accessories, televisions, cameras and other electronic items.
31. The Respondent observed that the Appellant's sales records were manual and involved data capture of the product, quantities, price and total sales. The sales summary, according to the Respondent was as follows:

Year	Sales in Kshs
2013	307,316,475
2014	580,504,166
2015	519,894,266
2016	170,923,160

32. The Respondent further averred that during the review of the delivery notebooks it observed instances where the Appellant categorized sales and recorded in the delivery notebooks as either Cash I, Cash II or credit sales.
33. The Respondent submitted that from the aforementioned inspection, it noted that the Appellant had under-declared sales as follow:
- a) The Respondent analysed the Appellant's bank statement from its Barclays Bank Account No. 2023640840 Queensway Branch and compared it with the sales reported in the audited accounts as follows:

Sales reconciliation with Banking A/C No, 2023640840	2012	2013	2014	2015	2016
Total	124,038,617	162,557,664	77,179,245	33,873,295	42,409,727
Less opening debtors	-	3,078,444	1,987,376	-	-
Sales Banked(a)	120,960,173	163,648,732	72,700,175	33,873,295	42,409,727
Self-Assessment return sales	(72,683,954)	(101,447,691)	(39,086,139)	-	-
Under-declared sales from bankings	48,276,219	62,201,041	33,614,036	33,873,295	42,409,727

The Respondent attached the Appellant's bank statement to support this.

- b) The Respondent averred that it carried out a test to check whether all sales were banked through a comparative analysis of the bankings with the sales from the delivery notebooks. The Respondent observed that cash and cheque deposits into the bank were lower than the recorded sales. The sales reconciliation is as hereunder:

	2012	2013	2014	2015	2018
Total sales from analysed(a)	-	307,316,475	580,504,166	519,894,266	170,923,160
Sales reconciliation					
A/C No. 2023640840	124,038,617	162,557,664	77,179,245	33,873,295	42,409,727
Less opening debtors	-	3,078,444	1,987,376		
Add closing debtors	(3,078,444)	(1,987,376)	(6,466,446)		
Sales banked(b)	120,960,173	163,648,732	72,700,175	33,873,295	42,409,727
Cash sales unbanked(a-b)		143,667,743	507,803,991	486,020,971	128,513,433
Total Sales	120,960,173	307,316,475	580,504,166	519,894,266	170,923,160
Less sales per self-assessment return sales	(72,683,954)	(101,447,691)	(39,086,139)	-	
Under declared sales	48,276,219	205,868,784	541,418,027	519,894,266	170,923,160

The Respondent submitted that the Appellant was yet to file returns for the year 2015 and 2016.

34. The Respondent submitted that a review of the purchase records provided for the 2011 to 2013 years of income indicated that the purchases were lower than the figures stated in the accounts. The Respondent therefore allowed all the costs claimed in the financial statements.
35. The Respondent averred that the Appellant deliberately failed to provide purchases records for years 2014 and 2016.

36. The Respondent averred that it computed Income Tax from the under-declared sales from the Appellant's bankings and the non-declared cash sales as demonstrated in the table below:

	2012	2013	2014	2015	2016	Total
Computation of Income Tax	Kshs	Kshs	Kshs	Kshs	Kshs	Kshs
Under declared sales from bankings	48,276,219	62,201,041	33,614,036	33,873,295	42,409,727	220,374,318
Non declared cash sales	-	143,667,743	507,803,991	486,020,971	128,513,433	1,266,006,138
Total under declared taxable income						
Tax at 30%	14,482,866	61,760,635	162,425,408	155,968,280	51,276,948	445,914,137
Period outstanding	48	36	24	12	-	
Interest at 1%p.m	6,951,776	22,233,829	38,982,098	18,716,194	-	86,883,896
Tax due and payable	21,434,641	83,994,464	201,407,506	174,684,473	51,276,948	532,798,033

37. The Respondent averred that it did not charge Income Tax on the Appellant for the 2016 year of income. According to the Respondent, the Income Tax for the year 2016 initially charged and communicated in the assessment was not included in its Objection Decision. Therefore, contrary to the Appellant's allegations, the taxable income for the year 2016 was not considered.

38. With regard to the 2015 year of income, the Respondent submitted that the Appellant is required under statute to file returns by 30th June 2016 and the Appellant was yet to do so.
39. The Respondent submitted that it further assessed VAT on the under-listed sales for the years under audit i.e 2013, 2014, 2015 and 2016 as outlined below:

	Additional sales	VAT(16/116)	Interest at 1%pm
2013	46,780,100	6,452,428	2,516,447
2014	555,673,185	76,644,577	24,977,899
2015	503,114,665	69,395,126	14,699,635
2016	164,004,700	22,621,338	1,719,689
TOTAL		175,113,469	44,151,290

40. The Respondent averred that it communicated its findings vide the notice of assessment dated 28th April 2017 and later, the Objection Decision dated 6th June 2017.
41. The Respondent further states that in a meeting on 22nd February, the Appellant was tasked to provide more documents, which request was not honoured.
42. The Respondent argued that both the notice of assessment and the Objection Decision gave elaborate reasons and computations on the tax assessed.
43. The Respondent averred that contrary to the Appellant's allegations, it only considered the documents obtained from the Appellant's premises during the search of 21st February 2017 in arriving at its assessment. It is therefore, according to the Respondent, not correct for the Appellant to allege that the Respondent considered extraneous considerations of other documents, when no evidence has been provided to support the said allegations.

44. The Respondent argued that unlike Income Tax whose returns are filed annually, VAT returns are, by law, filed every month. Consequently, the Respondent assessed the VAT due for 2016.
45. Contrary to the Appellant's allegations, the Respondent averred that the Appellant did not adduce any evidence of the alleged material facts that the Respondent allegedly misapprehended. The Respondent reiterates that all the records considered during the audit were obtained from the Appellant's premises.
46. The Respondent averred that the use of the banking analysis test/banking deposit method of proving income is legitimate and was necessitated by the Respondent's need to confirm its suspicions that the Appellant had unreported income. The Respondent argued that this test validated its suspicion that the Appellant had undeclared income.
47. The Respondent further averred that the Appellant did not provided any evidence of the Respondent's misapplication of the banking analysis test and as such this is a mere allegation.
48. The Respondent submitted that it is allowed to embrace a range of methods and techniques for determining and verifying a taxpayer's income. In some instances like in this case, detecting and deterring non-compliance requires more than examination of the taxpayer's books and records and necessitates an analysis of taxpayer's financial affairs to correctly assess tax liabilities. During such audits, the Respondent may use either direct or indirect methods.
49. The Respondent submitted that the bank deposit and cash expenditure method (Banking analysis test) is based on the premise that money received must either be deposited or spent. This approach, according to the Respondent, is particularly useful if an analysis of bank accounts and a taxpayer's cash expenditure indicates a likelihood of undeclared income

and the taxpayer makes regular payments into the bank accounts that appear to be from a taxable source.

50. The Respondent cited Section 29(1) of the Tax Procedures Act which provides for the circumstances under which the Respondent may issue a default assessment and which Section provides as follows:-

“Where a taxpayer has failed to submit a tax return for a reporting period in accordance with the provisions of a law, the Respondent may, based on such information as may be available and to the best of his or her judgement, make an assessment (referred to as a “default assessment”)”

51. The Respondent also cited the case of **Nairobi TAT No. 25 of 2016 Family Signature LTD Vs The Respondent of Investigations & Enforcement**, where in determining whether the Respondent was justified in employing an alternative and indirect method of assessing the Appellant’s estimated tax liability, the Tribunal held that:

“When the Respondent is prompted to resort to an alternative method of determining the income and in assessing the tax liability of a taxpayer, it has the onerous responsibility to act reasonably by exercising best judgement informed by pragmatic and reasonable considerations that do not in any manner result in a ridiculously high income margin.”

52. Contrary to the Appellant’s allegations, the Respondent averred that the Appellant did not adduce any evidence showing payment of the taxes due.
53. According to the Respondent, the burden of proving payment of taxes is on the taxpayer and nothing would have been easier than for the taxpayer to produce evidence in form of a copy of a cheque or transfer details evidencing the same. In any event, the Respondent’s records of the Appellant’s tax records indicate that no such payments have been made.

54. The Respondent submitted that **Section 56(1)** of the **Tax Procedures Act** provides that for any proceedings under that part of the Act (Tax decisions, Objections and Appeals) the burden shall be on the taxpayer to prove that a tax decision is incorrect.
55. To support its argument, the Respondent cited the case of **Primarosa Flowers Ltd v Respondent of Domestic taxes [2019] eKLR**, where the court inter alia considered the Appellant's contention and claim that "**extraneous factors**" were adopted by Tax Appeals Tribunal as a basis of rejecting the Appellant's actual loss on account of conversion of earnings in Yen into Dollar then into shillings. The court stated as follows:

"21. Section 107 of the evidence provides;-

"(1) Whoever desires any court to give judgement as to any legal right or liability dependent on the existence of facts which he asserts must prove that those facts exist.

(2) When a person is bound to prove the existence of any fact it is said that the burden of proof lies on that person."

*In the instant Appeal, I find the burden of proof that TAT Tribunal relied on extraneous factors and that the Appellant carried out multiple conversions lies with the Appellant. In the instant case, the Appellant has not produced any documentary evidence, that the currency of the transaction or export documents were in Dollars or payment were received in Dollars. I find the Appellant has not discharged the burden of proof to the required standard of proof. In **Mulherin vs Respondent of Taxation [2013] FCAFC 115** the Federal Court of Australia held that in tax disputes, the taxpayer must satisfy the burden of proof to successfully challenge income tax assessments. The onus is on the taxpayer in proving that assessment was excessive by adducing positive evidence which demonstrates the taxable income on which tax ought to have been levied."*

56. The Respondent further cited **Boleyn International Ltd Vs Commissioner of Investigations and Enforcement, Nairobi TAT Appeal no. 55 of 2018** where the Tribunal held that:

“We find that the Appellant at all times bore the burden of proving that the Respondent’s decisions and investigations were wrong. The Tribunal is guided by the provisions of Section 56(1) of the TPA, 2015 which states:

In any proceedings under this part, the burden shall be on the taxpayer to prove that a tax decision is incorrect.

*Further the Tribunal finds the following paragraph from **Pierson V Belder(H.M. Inspector of Taxes)(1956-1960) 38 TC 387** to be instructive:*

*But the matter may be disposed of, I think, even more shortly in this way: there is an assessment made by the Additional Commissioners upon the Appellant; it is perfectly clearly settled by cases such as **Norman v. Golder, 26 T.C. 293**, that the onus is upon the Appellant to show that the assessment made upon him is excessive or incorrect; and of course he has completely failed to do so. That is sufficient to dispose of the appeal, which accordingly I dismiss with costs.”*

57. The Respondent submitted that the Appellant failed to discharge the onus of proving that the Respondent relied on extraneous consideration and findings in its assessments and objection decision.

58. The Respondent submitted that it allowed all costs claimed by the Appellant in the financial statements since the purchases (from the record of purchase for 2011 to 2013) were lower than the figures stated in the accounts. This, the Respondent argued, is evidenced from its notice of assessment of 28th

April 2017. For the other years, no costs were allowed as no evidence was adduced to support the alleged costs.

59. The Respondent submitted that it duly explained to the Appellant both in the notice of assessment and in the letter of confirmation of assessment how it arrived at the outstanding tax arrears of Kshs. 700,548,224.00. The Respondent argued that nowhere in either the objection or in the pleadings before the Tribunal did the Appellant adduce evidence on why it deemed the said outstanding taxes as wrongly computed. The Respondent, therefore, averred that the outstanding tax arrears of Kshs. 700,548,224.00 as confirmed in the letter of 6th June 2017 are due and payable by the Appellant.
60. The Respondent argued that the Appellant's objection of 24th May 2017 was not a valid objection as stipulated in the Tax Procedures Act of 2015. The Appellant's objection, according to the Respondent, is merely composed of denial in all the tax heads and neither stated any amendments it proposed to be made on the assessment and reasons for the said amendments. This, according to the Respondent, does not meet the threshold raised under Section 51(3) of the Tax Procedures Act.
61. Further, that instead of dismissing the said objection, the Respondent looked at the objection as drafted on its own merits and explained to the Appellant as to how the assessment in each tax head was arrived at and as such should be confirmed.
62. Contrary to the Appellant's allegations, the Respondent averred that in arriving at its decision to confirm the assessment, the Respondent looked at the merits of the Appellant's objection. It is, therefore, the Respondent argued, not proper for the Appellant to allege that the Respondent deemed its objection inadmissible.
63. The Respondent submitted that it, as evidenced by the Objection Decision, explained in detail why it felt that the objection was not proper and the

reasons for its decision. The Respondent averred that even though the objection was not proper, the Respondent issued a decision based not on the fact that the objection was not proper but on its merits and content.

64. With regards to the Appellant's allegation that the Respondent based its assessment on "purported delivery notebooks," the Respondent averred that the Appellant is well aware of the existence of the delivery notebooks. The Respondent submitted that the Appellant in their letter of 18th July 2017, called for return of the said delivery notebooks.
65. In response to the submission by the Appellant that it had instructed its auditors to undertake review of its accounts, the Respondent argued that such measures ought to have been taken at the time of the objection. The findings of the audit would have then informed the Respondent's decision in confirming the assessment. Thus, the Respondent argued that it is too late to call for an audit.

THE RESPONDENT'S PRAYERS

66. The Respondent prays that the Tribunal finds that:
- i) The outstanding tax arrears of Kshs. 700,548,224 are due and payable by the Appellant.
 - ii) The confirmed assessment dated 6th June 2017 is valid in law.
 - iii) The appeal herein be dismissed with costs to the Respondent.

ISSUES FOR DETERMINATION

67. Having carefully considered the parties' pleadings, submissions and all documentation, the Tribunal is of the view that the issues for its determination are as follows:

- a) Whether the Appellant's objection is valid?
- b) Whether the Respondent used extraneous considerations and documents other than those kept by the Appellant to arrive at its findings and Objection Decision?
- c) Whether the Respondent misapplied the banking analysis test?

ANALYSIS AND FINDINGS

(a) Whether the Appellant's objection is valid?

68. The Appellant lodged an objection to the Respondent's assessment vide its letter dated 24th May 2017. The Respondent in its Objection Decision in part informed the Appellant that its Notice of Objection had not precisely stated the grounds of objection, amendments that are required to be made to correct the assessment or reasons for such amendments. Thus, the Respondent averred that the Appellant's objection does not meet the threshold as provided for under Section 51(3) of Tax Procedures Act and therefore not valid.
69. According to the Respondent, the objection dated 24th May 2017 is composed of denial in all the tax heads and neither stated any amendments it proposed to be made on the assessment and reasons for the said amendments.
70. The Respondent relies on the case of **Gashi v Respondent of Taxation [2012] FCA 638**, where the court stated that:

“it is not enough for the applicants to establish that the Respondent's estimations were mistaken or erroneous in some or even many respects. It is necessary that they go further and establish what their taxable incomes actually were. If, in the course of that project, they demonstrate that they were not in partnership, and/or that their own incomes did not contribute to accretions in the assets of other members

of the family, all well and good. But the bottom-line question, as it were, will always be: what were the taxable incomes of the applicants? It is for them to determine how they will go about answering that question.”

71. The Respondent submits that it expedited its response on the said objection and explained to the Appellant reasons why it was invalid pursuant to its obligations under Section 51(4) of the Tax Procedures Act.
72. On its part, the Appellant submits that it filed a valid objection on the basis of the information that was in its possession noting that the Respondent had confiscated the its documents therefore limiting the information that was within its purview.
73. The Appellant further submits that as soon as it was able to reconcile its records, it sought leave of the Tribunal to submit the documentation to prove it was not non-compliant with the requirements under the Income Tax Act with regards to truthfully filing its returns with the Respondent.
74. To support its arguments, the Appellant cites the case of **Dry Associates Ltd V Capital Markets Authority and Another**, petition No.328 of 2011(unreported), where the court held that:

“Article 47 is intended to subject administrative processes to constitutional discipline hence relief for administrative grievances is no longer left to the realm of common law...but is to be measured against the standards established by the Constitution.”
75. The Appellant submits that it was not given proper opportunity to defend itself before the Respondent noting that the Respondent had the upper hand having confiscated critical documents belonging to the Appellant at the time it was summoning the Appellant to appear before it. The Appellant therefore put up a spirited fight as best it could before the Respondent when it filed its objection and appeared before the Respondent upon being summoned.

76. Section 51 of Tax Procedures Act provides that:

“A notice of objection shall be treated as validly lodged by a taxpayer under subsection (2) if—

(a) the notice of objection states precisely the grounds of objection, the amendments required to be made to correct the decision, and the reasons for the amendments; and

(b) in relation to an objection to an assessment, the taxpayer 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 under section 33(1).

(c) all the relevant documents relating to the objection have been submitted.”

77. The Tribunal notes that on 24th May 2017, the Appellant lodged an objection with the Respondent. However, the said objection did not reiterate the grounds of objection, the correction required to be made and the reasons for the amendments. The Tribunal further notes that the Appellant did not provide the documents in support of its objection. The Appellant merely indicated that the 2015 and 2016 audits are underway and will furnish the Respondent with the financial statements in due course. The Tribunal further notes that this notwithstanding, the Respondent considered it and went ahead to explain how it arrived at the assessment.

78. The Tribunal further notes, from the Appellant’s submission, that the Respondent had confiscated critical documents belonging to the Appellant at the time the Appellant was summoned to appear before the Respondent. The Respondent returned the documents to the Appellant on 18th July 2017 which was after the Objection Decision has been issued.

79. The Tribunal is of the view that objections should be considered based on their merit rather than structure and technicalities. In reaching this finding,

the Tribunal is guided by Article 159(2)(d) of the Constitution, 2010 which provides that:

“In exercising judicial authority, the courts and tribunals shall be guided by the following principles...:

(d) Justice shall be administered without undue regard to procedural technicalities”

80. The Tribunal therefore finds that the objection was valid and the Appeal is therefore correctly sitting before the Tribunal.

(b) Whether the Respondent used extraneous considerations and documents other than those kept by the Appellant to arrive at its findings and Objection Decision?

81. The Appellant submitted that the Respondent took away documents during a raid on the Appellant's offices and the residence of one of its directors. The information was used to assess the Appellant despite the fact that the Appellant had already filled tax returns for the years 2012-2014 and was in the process of filling returns for 2015 & 2016. Further the Appellant availed its statements of account for the years under review all of which confirm that the Appellant properly filed its returns.

82. According to the Appellant, therefore, the Respondent should have been bound by its declarations and assessed it based on its declarations.

83. The Appellant is correct in its assertion that the Kenyan tax system applies a self-assessment system where the taxpayer assesses itself. The system finds effect in Section 24(1) of the Tax Procedures Act. However, despite it being a self-assessment system, the Respondent is not bound by the taxpayer's

self-assessment. Section 24(2) of the Tax Procedures Act in providing for this states that:

The Commissioner shall not be 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.

84. A reading of Section 24(2) of the Tax Procedures Act shows that the Commissioner has powers to assess a taxpayer even where the taxpayer has filed its return. The Section goes to allow the Commissioner to use any information available to it. In this case, the Respondent used the documents it collected during a raid and search conducted at the Appellant's business premises and the residence of the Directors on 21st February 2017.

85. According to its letter dated 23rd February 2017, the Respondent held a meeting with the Appellant and requested the Appellant to provide additional documentation. Minute. 5 of the minutes of the meeting between the Appellant and Respondent's representatives held on 22nd February 2017 states:

***"Records required** "The taxpayer requested time to bring documents covering the period under investigation 2012 to 2016 from the auditors including:*

- 1. Copies of Audited accounts for the years 2012, 2013, 2014, 2015, 2016*
- 2. Sales invoices and ETR reports*
- 3. Purchase invoices*
- 4. Copy of Audit report of findings for the prior audit by KRA*
- 5. Bank statements for the company and directors."*

The Appellant did not furnish the Tribunal with evidence that it had provided the requested documentation"

86. Section 107 of the Evidence Act provides that:

“(1) Whoever desires any court to give judgement as to any legal right or liability dependent on the existence of facts which he asserts must prove that those facts exist.”

“(2) When a person is bound to prove the existence of any fact it is said that the burden of proof lies on that person.”

87. The question of burden of proof in taxation matters is provided for under the Tax Procedures Act as well as the Tax Appeals Tribunal Act. Section 56(1) of the Tax Procedures Act states that:

“In any proceedings under this Part, the burden shall be on the taxpayer to prove that a tax decision is incorrect.”

Section 30 of the Tax Appeals Tribunal Act similarly provides that:

“In a proceeding before the Tribunal, the Appellant has the burden of proving—

(a) Where an appeal relates to an assessment, that the Assessment is excessive; or

(b) in any other case, that the Tax Decision should not have been made or should have been made differently.”

88. In this case, the Appellant is the one seized of the desire to prove that the Respondent used extraneous information in arriving at its assessment. Thus, according to the provisions of the Evidence Act, the Tax Procedures Act and the Tax Appeals Tribunal Act, the burden of proof falls upon the Appellant.

89. The Tribunal notes that in its attempt to discharge its burden of proof, the Appellant averred that the Respondent used extraneous documents to

determine its findings. The Respondent adduced evidence that it obtained the documents it relied upon from a search that was authorized by a court of law.

90. The Respondent further provided evidence that after the search, its officers prepared an inventory of the goods seized and the same was countersigned by the representatives of the Appellant who were present during the search.
91. The Appellant on its part failed to adduce evidence to refute the Respondent's position. It failed to show that the notebooks did not belong to it and were not in any way related to its business. It merely made averments. It did not furnish the Tribunal with any proof of its averments. Madan J in his judgment in **CMC Aviation Ltd V Cruisair Ltd (I) [1978] KLR 103** observed that:

"Pleadings contain the averments of the parties concerned. Until they are proved or disproved, or there is an admission of them or any of them, by the parties, they are not evidence and no decision could be founded upon them. Proof is the foundation of evidence. Evidence denotes the means by which an alleged matter of fact, the truth of which is submitted for investigation. Until their truth has been established or otherwise, they remain un-proven. Averments in no way satisfy, for example, the definition of "evidence" as anything that makes clear or obvious; ground for knowledge, indication or testimony; that which makes truth evident, or renders evident to the mind that it is truth."

Thus, these averments are not sufficient at proving its case.

92. It is the Tribunal's position that it was the responsibility of the Appellant to provide evidence that the Respondent had used extraneous information in arriving at its assessment.

93. The Tribunal is of the view that the Appellant did not discharge its burden of proof in showing that the Respondent used extraneous considerations and documents other than those prescribed by the law. The averments made by the Appellant did not amount to evidence.
94. The Tribunal therefore finds that the Respondent did not use extraneous considerations and documents other than those kept by the Appellant in arriving at its assessment and Objection Decision.

(c) Whether the Respondent misapplied the banking analysis test?

95. The Appellant contended that the banking analysis test applied by the Respondent led to the Respondent levying an unrealistic assessment upon the Appellant. To support its case the Appellant cited the assertions of Edmund Biber who in the article “*Revenue Administration: Taxpayer Audit-Use of indirect method*”, at Page 9 which states that:

“In general it can be said that courts have ruled that administrations;

(1) may use any method to reconstruct income that is reasonable under the circumstances;

(2) may not be arbitrary in the use of this authority;

(3)...

(4) must investigate all reasonable evidence presented by the taxpayer refuting the computation of income...”

96. The Appellant submitted that it provided the Tribunal with its ledgers as well as bank statements for the period under review that support its position on the amount of taxes that were due to it during the period under review. These records, according to the Appellant, clearly show that the Respondent did not arrive at the assessment justly and as such the assessment was wrong.
97. The Respondent on its part argued that the use of the banking analysis test/banking deposit method of proving income is legitimate and was

necessitated by the need to confirm its suspicions that the Appellant had unreported income.

98. The Respondent argued that this test validated its suspicion that the Appellant had undeclared income. The Respondent further averred that the Appellant did not provide any evidence of the Respondent's misapplication of the banking analysis test and as such this is a mere allegation.
99. The Respondent submitted that it is allowed to embrace a range of methods and techniques for determining and verifying a taxpayer's income. In some instances, as in the case at hand, detecting and deterring non-compliance requires more than examination of the taxpayer's books and records and necessitates an analysis of taxpayer's financial affairs to correctly assess tax liabilities. During such audits, the Respondent may use either direct or indirect methods.
100. The Tax Procedures Act empowers the Respondent to assess a taxpayer in instances where the taxpayer has filed a return and where a taxpayer has not filed a return. Section 31(1) of the Tax Procedures Act deals with instances where a taxpayer has filed a self-assessment return. The Section provides as follows:

"Subject to this section, the Commissioner may amend an assessment (referred to in this section as the "original assessment") by making alterations or additions, from the available information and to the best of the Commissioner's judgement, to the original assessment of a taxpayer..."

Similarly, in giving the Commissioner power to issue an assessment where the taxpayer has not filed a return, Section 29(1) provides:

Where a taxpayer has failed to submit a tax return for a reporting period in accordance with the provisions of a tax law, the Commissioner may, based on such information as may be available

and to the best of his or her judgement, make an assessment (referred to as a "default assessment")...

101. In both instances, the Respondent is allowed to use any information that is available to it and to use the best of his or her judgement in making the assessment.
102. The Respondent submitted that it used the banking analysis test in arriving at the assessment. The Appellant on its part argues that the banking analysis test was misapplied resulting in what it terms as an unrealistic amount of tax being assessed upon it. The Tribunal is therefore faced with the question of whether the banking analysis test was correctly applied in this situation.
103. The Tax Procedures Act in granting the Respondent powers to assess taxpayers does not specify the methods that may be used instead the law provides that the best judgment must be exercised. The first part of this analysis dealt with the information that may be used.
104. The Tribunal must then address itself on what amounts to best Judgement. This question has been dealt with severally by courts. In the case of **Van Boeckel v C & E QB Dec 1980, [1981] 5TC 290** Woolf J stated that:

“the very use of the word 'judgment' makes it clear that the commissioners are required to exercise their powers in such a way that they make a value judgment on the material which is before them Secondly, clearly there must be some material before the commissioners on which they can base their judgment. If there is no material at all it would be impossible to form a judgment as to what tax is due...What the words 'best of their judgment' envisage, in my view, is that the commissioners will fairly consider all material placed before them and on that material, come to a decision which is one which is reasonable and amount of tax which is due. As long as there

is some material on which the commissioners act then they are not required to carry out investigations which may or may not result in further material being placed before them.”

105. In Raghubar Mandal Harihar Mandal vs The State Of Bihar AIR 1952 Pat 235 the court held that:

"The officer is to make an assessment to the best of his judgment against a person who is in default as regards supplying information. He must not act dishonestly or vindictively or capriciously, because he must exercise judgment in the matter. He must make what he honestly believes to be a fair estimate of the proper figure of assessment, and for this purpose he must, their Lordships think, be able to take into consideration local knowledge and repute in regard to the assessee's circumstances, and his own knowledge of previous returns by & assessments of the assessee, & all other matters which he thinks will assist him in arriving at a fair and proper estimate and though there must necessarily be guess-work in the matter, it must be honest guess-work."

106. The Tribunal reviewed the evidence and submissions before it in a view to ascertain whether the Respondent exercised best judgement in arriving at the assessment. In applying the rules set out in the above-mentioned cases, the Tribunal could not find any evidence indicating that the Respondent acted dishonestly, vindictively or capriciously. The Respondent exercised its powers to make the decision based on the material before it. Thus we are of the view that the Respondent exercised best judgement under the circumstances as required by the law.

107. Further, the courts have in the past held that the banking analysis test (also known as bank deposit analysis) is an acceptable method of arriving at an

assessment. This was held to be so in the case of **Bachmann v. The Queen, 2015 TCC 51** where the court stated that:

“This Court has recognized that in an appropriate case a bank deposit analysis is an acceptable method to compute income.”

108. Once it is established that the method is allowed, the question is whether the method was applied in arriving at a reasonable assessment in the case at hand. The Tribunal is guided by the test set out in **CA McCourtie LON/92/191** where it was stated:

“ In addition to the conclusions drawn by Woolf J in Van Boeckel earlier tribunal decisions identified three further propositions of relevance in determining whether an assessment is reasonable. These are, first that the facts should be objectively gathered and intelligently interpreted; secondly, that the calculations should be arithmetically sound; and, finally, that any sampling technique should be representative and free from bias.”

109. From the evidence adduced before us, the Tribunal is of the view that the Respondent met the requirements as set out in **CA McCourtie** above. The facts were objectively gathered, we did not find any errors in the arithmetic computations and the sampling technique did not indicate any bias.

110. The onus then was on the Appellant to prove its averment that the banking analysis was misapplied in arriving at the assessment. The court in **Hole v. The Queen, 2016 TCC 55** the court opined that:

“There are two primary ways in which a taxpayer can challenge a bank deposit analysis. The first is to prove that his or her records were adequate and thus that his or her income should have been determined using those records. The second, and more common, method is to challenge the actual determination of income made by the Minister under the bank deposit analysis.”

111. The Appellant made averments on both accounts stating that its records were adequate and that the determination was erroneous. The Appellant disputed the Respondent's analysis and provided its own analysis showing what it deemed to be its sales. The Tribunal notes that in disputing the Respondent's analysis the Appellant did not specify the entries in the bank statement which the Respondent has used wrongly/misapplied or which should not have been included in the assessment and the reasons why the entries should not be included. Its averments remain founded upon the argument that the Respondent used extraneous information and that the applied method resulted in an unrealistic tax assessment.
112. The issue of the extraneous information has already been dealt with. The averment that the application of the test resulted in an unrealistic assessment is in and of itself not sufficient to discharge the burden on the Appellant. The Appellant must prove that the method was flawed.
113. The court in **Alfred Kioko Muteti v Timothy Miheso & another [2015] eKLR** held that a party can only discharge its burden upon adducing evidence. Merely making pleadings is not enough. In reaching its findings, the court stated that:

“Thus, the burden of proof lies on the party who would fail if no evidence at all were given by either party....Pleadings are not evidence and it is not enough to plead particulars of negligence and make no attempt in one’s testimony in court to demonstrate by way of evidence how the accident occurred and how the 1st defendant was to blame for the said accident. It is trite law that he who alleges must prove and that burden does not shift to the adverse party even if the case proceeds by way of formal proof and or undefended. “

114. The Tribunal finds that the Appellant failed to prove that the Respondent misapplied the bank analysis test. The Tribunal therefore finds that the Respondent did not misapply the bank analysis test.

ORDERS

The Tribunal having entered the above findings makes the following Orders:

1. The Appeal fails.
2. The Respondent to take into account costs from the Appellant's records for 2015 and 2016 years of income in the assessment.
3. Each party shall bear its costs.

DATED and DELIVERED at NAIROBI this 14th day of August, 2020.



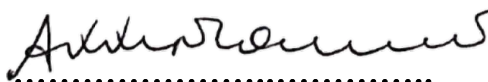
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CATHERINE N. MUTAVA
CHAIRMAN



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WILFRED N. GICHUKI
MEMBER



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GABRIEL M. KITENGA
MEMBER



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ABRAHAM K. KIPROTICH
MEMBER