

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL AT NAIROBI
APPEAL NO. 109 OF 2019

A ONE HEALTHCARE LIMITED.....APPELLANT

VERSUS

**THE COMMISSIONER INVESTIGATION
AND ENFORCEMENT.....RESPONDENT**

JUDGEMENT

BACKGROUND

1. The Appellant is a limited liability company and registered as CPR/2010324765 with the Registrar of companies. It has two directors namely: -
 - a) Njama Wambugu
 - b) Catherine Wanjiru NdunguThe Appellant deals in medical supplies.

2. The Respondent is a principal officer of Kenya Revenue Authority (KRA) and which Authority is established under the Kenya Revenue Act (Cap 469) and is charged with the mandate of assessment, collection and receipt of revenue as an agent of the government of Kenya.

3. The Respondent carried out a tax audit on the Appellant accounts for the years of income 2013-2017. The Respondent then issued a preliminary audit finding report vide its letters dated 12th and 15th October, 2018 for Kshs.8,419,730.00 inclusive of penalty and interests on Corporation Income Tax and Kshs.37,176,048.00 inclusive of penalty and interest on VAT.
4. The Appellant issued a notice of objection vide its letter dated 17th October, 2018 where the reasons for its objection was that the Respondent had omitted zero-rated and exempt sales which were not included in the monthly returns (VAT3) and further that the banking analysis was erroneous.
5. However, on 29th November, 2018 the Respondent again issued what it called an additional assessment for the years of income 2013-2017 for total tax of Kshs.122,564,387.00 being Corporation Tax of Kshs. 33,751,453.00 inclusive of penalty and interest and Kshs.88,812,934.00 being VAT inclusive of penalties and interest.
6. The Appellant, on the 21st December 2018 issued a Notice of Objection to the additional assessment, noting that the Respondent had not responded to their other notice dated 17th October, 2018. The Appellant reiterated their grounds of objection as stated in the same notice of 17th October, 2018.

7. On 20th February, 2019 the Respondent issued its Objection Decision in relation to the Appellant's objection notice of 21st December, 2018. The new tax demanded was Kshs. 46,985,255.00 inclusive of penalty and interest being Corporation Tax of Kshs.29,848,193.00 and Value Added Tax of Kshs.17,137,061.00 both inclusive of penalty and interest.
8. Being aggrieved by the verdict of the Respondent, the Appellant filed a Notice of Appeal dated 4th March 2019 and proceeded to file a Memorandum of Appeal together with Statement of Facts and served both documents on the Respondent on 15th March, 2019.

APPELLANT'S CASE

9. The Respondent confirmed the notice without due regard to the provisions of the Income Tax Act Cap 470, the Value Added Tax Act Cap 476, the facts and the circumstances of the case.
10. The Respondent did not take into account all the documentation, information and explanations provided in order to appreciate all the issues placed before it before arriving at the assessment.
11. The Appellant avers that all pending issues in relation to the Respondent's letter dated 12th October, 2018 on the audit were prior discussed. Documentation, data, evidence, information and records in a well detailed, referenced and analyzed form were provided to the Respondent both in soft and hard copies during the various meetings.

12. The Respondent's failure to consider all the facts and the information provided in the Appellant's case is tantamount to breaching the rules of fairness and natural justice.
13. In its reports dated 12th and 15th October 2018, the Respondent entitled them "**Preliminary investigation findings for the year 2013- 2017**". In the same reports the Respondent demanded principal taxes as computed and payable within seven days from their dates. It further stated that failure to make payments it would impose penalties and interest pursuant to Sections 94, 95 and 97 of the Tax Procedures Act 2015 (TPA).
14. According to the Appellant, the Value Added Tax raised amounting to Kshs.17,137,061.00 inclusive of penalties and interest is excessive and erroneous.
15. The Appellant demonstrated to the Respondent that the amount in dispute in VAT related to medical supplies which were erroneously omitted in the VAT3 filed but are exempt supplies as per the VAT Act Cap 476-First Schedule. Thus no revenue was lost as per the said Act.
16. The Respondent erred in facts by raising a VAT assessment based on the bank balance variances as the basis to charge tax.

17. The Appellant averred that Corporation Tax amounting to Kshs.29,848,193.00 inclusive of penalties and interest is excessive and erroneous.
18. The Respondent erred in facts by raising a Corporation tax assessment on bank balance variances as the basis to charge tax.
19. This was even after the Appellant had demonstrated to the Respondent that the amount in dispute in corporation tax was as a result of misunderstandings and disregards to the Appellant's various support Schedules of reconciliation provided to the Respondent.
20. The excess total additional assessment of Kshs.46,985,255.00 inclusive of penalties and interest raised is unwarranted since it is not backed by the provisions of the Income Tax Act Cap 470 and Value Added Tax Cap 476.

RESPONDENT'S CASE

21. The Appellant, vide its letter dated 17th October, 2018 purported to reconcile the variance noted by the Respondent by the introduction of exempted sales not reported in its VAT3 returns and without indicating the type of income it related to.
22. However, the Appellant provided its sales ledgers for consideration by the Respondent. The Respondent was satisfied that the documents

provided warranted adjustments to the assessments and the same were communicated to the Appellant vide its Objection Decision dated 20th February, 2019.

23. For items that had been raised but were not fully supported, the Respondent was constrained to raise assessments on the basis of the information availed by the Appellant, third party information and the Respondent's best judgement.
24. On analysis of the Appellant's banking, the Respondent noted that there was under-reported income for both Corporation Tax and VAT and the same was partly attributable to unreported income based on bankings.
25. The Appellant objected to the computation/banking analysis citing the Respondent's failure to adjust non-income items including container deposit refunds, deposit made for office rent, insurance and accident refunds and inter-party transfers.
26. The Respondent viewed the documents provided and made adjustments accordingly to arrive at the correct taxable sales and the same was communicated vide the Respondent's letter dated 20th February, 2019.
27. Contrary to the Appellant's assertion that the Respondent disregarded the Appellant's rights under Section 52 of the Tax Procedures Act and Section 13 of the Tax Appeals Tribunal Act 2013 by demanding security

for payment of tax, the Respondent maintains that it acted within the law in requiring the Appellant to furnish it with a Bank Guarantee as security for the payment of tax.

28. The Respondent maintains that in invoking its powers under Section 36 of the Tax Procedures Act it did not violate the Appellant's rights under Section 52 of the Tax Procedures Act and Section 13 of the Tax Appeals Tribunal Act 2013 as the Sections are not to be read together.

ISSUES FOR DETERMINATION

29. The Tribunal having considered the documentation, pleadings and submissions of the parties is of the view that the issues for its determination are as hereunder;

- a) **Whether the Respondent erred in law and facts by raising additional assessments based on VAT3 and income tax returns?**
- b) **Whether the Respondent erred in raising an additional VAT assessment by treating the medicaments and pharmaceutical products as taxable supplies?**

ANALYSIS AND FINDINGS

30. The Tribunal having considered the above issues wishes to analyze them herein-below.

a) Whether the Respondent erred in law and facts by raising additional assessments based on VAT3 and income tax returns?

31. The Respondent's letters dated 12th and 15th October, 2018 addressed to the Appellant entitled "Preliminary investigation findings for the years 2013 – 2017, stated on page 2 thereof that the Appellant ought to "arrange to settle the outstanding taxes or provide explanation where available within seven (7) days from the date of receipt of this demand letter".
32. Section 29 (2) (e) of the Tax Procedures Act states "the commissioner shall notify in writing a taxpayer assessed under subsection (1) of the assessment and the commissioner shall specify(e) the due date for payment of the tax, penalty, and interest, being a date that is not less than 30 days from the date of service of the notice". The Section requires the Respondent to specify the amount assessed, which the Respondent did; specify the due date of payment, which the Respondent did; ensure the due date for payment is not less than 30 days from the date of the notice, which the Respondent failed to do as the date had been given as seven (7) days. It is clear however that the Respondent made an assessment but did not strictly comply with Section 29 of the Tax Procedures Act.
33. It is worth noting that the Respondent gave the Appellant seven days' notice to pay what it termed as additional assessment without affording

the requisite statutory period to it to object to the demand. The Respondent's said action was capricious, arbitrary, unreasonable and in breach of the laid down legislation. The Tribunal refers to the case of **Noor Maalim Hussein & 4 others vs. Minister of state for Planning, National Development and Vision 2030 and 2 others [2012] eKLR**, where the court held as follows; "if statutory power is exercised in a manner contrary to the drafters or against public interest, the power can be said to have been exercised capriciously, irrationally or unreasonably. Thus irrationality and unreasonableness would play a major role and we shall as courts continue to assert our traditional duty and intervene in situations where authorities like ministers and persons act in bad faith, abuse power, fail to take account relevant considerations or act contrary to legitimate expectations."

34. The variance between the VAT3 returns and the credits in the bank accounts was due to some income from zero-rated sales as confirmed by the Appellant. Records of these sales were presented to the Respondent and the same ought to have assisted it to account and explain the variance between the VAT3 returns and the bank credits.
35. In view of the foregoing, the Tribunal finds that the Respondent erred in law and fact by raising additional assessments based on VAT3 and income tax returns.

b) Whether the Respondent erred in raising an additional assessment by subjecting the medicaments and pharmaceutical products as taxable supplies?

36. The Appellant's notice of objection on page one gives one of the reasons of objection by stating thus **“you have omitted zero-rated and exempt sales which were not included in VAT3 on the monthly returns”**. However, the Respondent's objection decision dated 20th February, 2019 under number 2.0 (sales as per VAT3 and IT2C) states, **“The explanation given in your objection that the variances between sales as per VAT3 and Sales in Account is as a result of exempt sales not reported in VAT3 and provision of sales ledger was adequate to warrant the amendment.”** Therefore the Respondent was in agreement with the Appellant on the issue of Sales as per VAT3 and IT2C which resulted into it amending the assessment on both Corporation tax and VAT downwards.
37. The Respondent opted to use the banking method in auditing the Appellant for tax. The Appellant in compliance provided copies of certified bank statements clearly showing the running balances for the respective years. The narration of the entries in the account is specific and should not be difficult to ascertain. Further the Appellant claims to have provided all documentation and analysis some of which were rejected by the Respondent. Without the benefit of knowing which documents were presented, the Tribunal cannot ascertain whether the Respondent

was justified in declining them. It would have helped if the Respondent had put it in writing and stated clearly what type of document it required.

38. In view of the foregoing analysis we make a finding that the Respondent erred in raising an additional assessment by subjecting the medicaments and pharmaceutical products as taxable supplies.

FINAL DECISION

36. The upshot of the above is that the Tribunal makes the following Orders:-

- a. The Appeal is merited and succeeds.
- b. The Respondent's Tax Assessment dated 20th February, 2019 for Kshs. 46,985,255.00 is hereby annulled and set aside.
- c. Each party to bear its costs.

DATED and DELIVERED at NAIROBI this 4th day of September, 2020.

**JOSEPHINE K. MAANGI
CHAIRPERSON**

**GEOFFREY KARUU
MEMBER**

**DELILAH KADZO NGALA
MEMBER**

**TANVIR ALI
MEMBER**