

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL AT NAIROBI
APPEAL NO. 113 OF 2019

CITIGATE DEVELOPERS LIMITED.....APPELLANT

VERSUS

COMMISSIONER OF INVESTIGATIONS &
ENFORCEMENT.....RESPONDENT

JUDGEMENT

BACKGROUND

1. The Appellant is a limited liability company incorporated on 12th June, 2010 and registered as CPR/2010/272804 with the Registrar of Companies it has three directors namely:
 - a) Njama Wambugu
 - b) Charity Gakenia Wambugu
 - c) Christopher Wanjohi Wambugu

2. The Respondent is a principal officer of Kenya Revenue Authority (KRA) which is established under Kenya Revenue Authority Act, Cap 469 laws of Kenya. It is an agency of the Government that is mandated to administer and enforce all provisions of the written law for purposes of assessing, collecting and accounting for all revenue in accordance with these laws.

3. The Respondent carried out tax investigations upon the Appellant's business for the years of income 2013-2017 with a view of establishing whether the Appellant had complied with its tax obligations during the period under review.
4. The Appellant had never traded and the only transaction that was ever done in the account is the fixed deposit of Kshs. 3,750,000.00 that was opened on the 18th September, 2013 with Equatorial Commercial Bank (now Spire Bank).
5. Between July 2018 and September 2018 the Respondent conducted a tax investigation on the Appellant's accounts for the accounting periods 2013 to 2017. The Respondent then issued preliminary audit findings vide its letter dated 12th October, 2018 for Kshs. 4,205,369.00 being principal Corporation Tax of Kshs. 2,742,632.00 and VAT of Kshs. 1,462,737.00 inclusive of penalty and interest.
6. The Appellant vide its letter dated 16th October, 2018 issued its notice of objection stating the following reasons:
 - a) That the bank account number stated for Citigate Developers Limited was incorrect.
 - b) That the company had never traded and that the Kshs. 3,750,000.00 was a fixed deposit opened by the director from personal funds.

- c) That the amount shown in the year 2014 is the same amount rolled over with interest and not a new amount.
 - d) That subsequent amounts shown in the periods 2015 – 2017 was interest income from the fixed deposit.
 - e) That both income tax and VAT are not applicable in this case.
7. However, on 29th November, 2018 the Respondent again issued what it called an additional assessment for the years of income 2013-2017 for Kshs. 5,991,999.00 being Corporation tax and Kshs. 1,462,737.00 for VAT, inclusive of penalty and interest for both taxes.
8. On a without prejudice basis the Appellant again issued a notice of Objection vide its letter dated 21st December, 2018 reiterating the same grounds of objection as stated in the earlier letter of 16th October, 2018.
9. The Respondent issued an Objection Decision vide its letter dated 20th February, 2019 for total tax of Kshs. 3,384,750.00 for Corporation tax and VAT, inclusive of penalty and interest.
10. The Appellant, being aggrieved by the verdict of the Respondent filed a Notice of Appeal on 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

11. The company had never traded and the Kshs. 3,750,000.00 was a fixed deposit account opened by the director from personal funds.
12. The Appellant demonstrated to the Respondent that the amount in dispute was a fixed deposit of Kshs. 3,750,000.00 into Equatorial Commercial Bank (now Spire Bank) where the source of funds was from already taxed sources of employment and dividend income. These funds were deposited on 18th September, 2013 and the fixed deposit account opened on 20th September, 2013.
13. The taxes due from the above income being PAYE and withholding tax were deducted and remitted to the Respondent. The Appellant availed P9A Form, annual self-assessment tax return, Employer's P10 Return and the dividend certificates but the Respondent did not take this information into consideration when issuing the assessment and objection decision.
14. The amount shown in the year 2014 is the same amount rolled over with interest and not a new amount and that subsequent amounts shown in the period 2015-2017 was interest income from the fixed deposit.
15. The Director, Mr. Njama Wambugu filed his income tax return for the year 2013 demonstrating taxed source of funds. The income tax return

of the year 2013 was acknowledged by the Respondent on 24th June, 2014.

16. The Appellant therefore avers that the excess additional assessment raised of Kshs. 3,384,750.00 inclusive of penalties and interest is unwarranted since it is not supported by the provisions of the Income Tax Act (ITA) Cap 470.
17. The Appellant therefore prays that, the Tribunal allows this Appeal and finds that:
 - a) The amount deposited as fixed deposit should not be subjected to further tax being VAT and Corporation tax.
 - b) The principal fixed deposit amount of Kshs. 3,750,000.00 was from taxed source of income of the shareholder Njama Wambugu through PAYE and should therefore not be deemed as a sale.

RESPONDENT'S CASE

18. The Appellant deposited Kshs. 3,750,000.00 as initial deposit in the year 2013. No other deposit was done in the subsequent years and the Appellant seems to be a dormant company. The source of the initial deposit however has not been explained to date. In the

circumstances, the Respondent treated the unexplained deposits therein as business income and charged income tax and VAT thereon.

19. The Respondent to buttress its argument sought to rely on Civil Appeal Number 154 of 2007, **Pili Management Consultant VS Commissioner of Income Tax -Kenya Revenue Authority.**
20. The Respondent prays that:
 - a) The Tribunal dismisses the Appeal in its entirety.
 - b) The Appellant provides for costs of this appeal.

ISSUES FOR DETERMINATION

21. 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 documents relied upon by the Appellant can support its claim that the source of funds for the fixed deposit was from the director's personal tax income?**
 - b) **Whether the Additional Assessment on the fixed deposit available in the Appellant's Bank Account was correctly issued?**

ANALYSIS AND FINDINGS

22. The Tribunal having considered the above issues wishes to proceed with its analysis as hereunder.

a) **Whether the document relied upon by the Appellant can support its claim that the source of funds for the fixed deposit was from the director's personal tax income?**

23. The Appellant avers that the source of Kshs. 3,750,000.00 fixed deposit was from employment income which had already been taxed. It is not in dispute that the director, Mr. Njama Wambugu had the financial capability to afford the said deposit, neither is it in dispute that he had been filing his individual tax returns. However, the lack of satisfactory audit trail that shows the movement of funds from the director's personal account(s) to the fixed deposit account does not support the Appellant's case. It is imperative to have this audit trail as it helps in the event of a dispute. In the absence of this it is difficult to determine the source of the funds used to open the fixed deposit.

24. During the hearing, the Appellant's agent submitted that the Director opened the fixed deposit account to take advantage of favourable interest rates. If indeed this was the reason, the account could still have been opened in the director's name. Further the Appellant being a limited liability company has three directors namely, Njama Wambugu, Charity Gakenia and Christopher Wanjohi Wambugu, therefore the funds in this account may well have belonged to any of the other directors.

25. In view of the above analysis we make a finding that the documents relied upon by the Appellant cannot support its claim that the source of funds for the fixed deposit was from the director's personal tax income.

b) Whether the Additional Assessment on the fixed deposit available in the Appellant's bank account was correctly issued?

26. As stated earlier there is no evidence to trace the movement of the funds from the director's personal account(s) to the fixed deposit account. There ought to have been a trail of the money moving from the Appellant's director, Mr. Njama Wambugu's personal account into the Appellant's company bank account. However, the only relevant document provided by the Appellant to support its argument is a deposit receipt/slip from the Appellant's bank. A deposit slip/receipt cannot conclusively illustrate that the money (deposit) emanated from the Appellant's account and neither can it support the argument that the money had been subjected to tax.

27. From the evidence adduced, the Appellant though incorporated on 12th June, 2010 had never traded. The fixed deposit of Kshs. 3,750,000.00 was the only credit in the Appellant's account. Though the Appellant never traded, the obligation of filing nil returns ought to have been met. However, the Appellant had not filed income tax returns despite being registered for the obligation.

28. Where there are no other records like financial accounts to be used to assess for tax, the Respondent may use bank deposits as was the case herein. Indeed, the issue of using bank deposits to issue additional assessment was dealt with in the case of **Pili Management Consultants Ltd versus Commissioner of Income Tax Kenya Revenue Authority (2010) eKLR**, where the Court of Appeal stated as follows, at page 12 of the judgement;

“Pili, as we have seen, made a nil return of income for the year 2004. It was alleged it was not trading for that year and therefore could not have earned any income upon which tax could have been levied. But we know now, and the Commissioner came to know in May 2006 that around 8th December 2004 Pili had a large amount of money in its accounts with the Bank. It may well be that Pili did not trade in the year 2004 and the money in its bank account did not come from trading. It may be that the money did not accrue in and was not derived from Kenya. But the money was in a Bank account in Kenya and it was in the account of Pili. Prima facie, it was Pili's money. Instead of declaring a nil return, why would Pili not declare the presence of the money and then explain to the Commissioner why tax was not payable on the money...”

29. Consequently, without the disclosure of the source of the Appellant's deposit in its account, the same is the Appellant's and it ought to be subjected to the relevant taxes. The Respondent was therefore correct in issuing the Additional Assessment in respect to income tax.
30. In respect of the VAT, there is no evidence that the Appellant was registered for VAT, nor was it registrable in accordance with the provisions of Section 34(1) of the VAT Act 2013. The same provides as follows;
- “ (1) A person who in the course of a business –
- (a) Has made taxable supplies or expects to make taxable supplies, the value of which is five million shillings or more in any period of twelve months; or
 - (b) Is about to commence making taxable supplies the value of which is reasonably expected to exceed five million shillings in any period of twelve months, shall be liable for registration under this Act and shall, within thirty days of becoming so liable, apply to the Commissioner for registration in the prescribed form. “
31. The Tribunal notes that the deposit herein was less than the VAT threshold of Kshs. 5,000,000.00. We therefore make a finding that the Appellant was not subject to VAT.

FINAL DECISION

32. The upshot of the above is that the Appeal partially succeeds and the Tribunal makes the following Orders:

- a) The Respondent's Tax Assessment dated 20th February, 2019 for Kshs. 3,384,750.00 is upheld, subject to exclusion of VAT of Kshs. 600,000.00 together with the resultant penalty and interest thereof.
- b) 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**