

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL APPEAL
NO. 124 OF 2015

LONDON DISTILLERS (KENYA) LIMITED.....APPELLANT

VERSUS

THE COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGEMENT

BACKGROUND

1. The Appellant is a Company involved in distillery, manufacturing, blending and the sale of various distilled portable spirits with its headquarters in Nairobi and factory in Athi River and depots in Mombasa, Eldoret and Nanyuki.
2. The Respondent is established under the Kenya Revenue Authority Act, Cap 469 of the Laws of Kenya, charged with the mandate to collect revenue and administer the tax regime on behalf of the Government of Kenya.
3. The Respondent conducted investigations on the Appellant's business with a view to verifying the accounting practices applied by the Appellant during the period January 1998 to March 2005 having received information that the Appellant was allegedly involved in accounting malpractices that were designed to evade tax. Pursuant to that the Respondent on 18th May 2005 issued Notice under Section 30

and 31 of Value Added Tax Act requiring the Appellant to produce records relating to its operations.

4. Upon issuance of the Notice the Respondent carted away the Appellant's records on the same day to commence examination and analysis thereof. The analysis revealed that the records were not complete and further that the Appellant was maintaining parallel sets of records with discrepancies in the different sets. As a result of this observation the Respondent tabulated and determined the percentages of omission for the periods documentation was available and based on the findings they concluded that the Appellant was reporting less than half of its yield and thus sales. The Respondent proceeded to compute taxes due based on an under declaration of 50% in accordance with the provisions of Section 28 of the VAT Act Cap 476 and the 7th Schedule paragraph 9(1)(a).
5. The Appellant was issued with the assessment demanding payment of Kshs.1,013,719,327.00 on 3rd August 2006 and upon receipt thereof raised an objection thereto vide letter dated 29th August 2006 and Respondent responded on 6th September 2006.
6. The Respondent confirmed the assessment on 13th March 2007 and demanded the settlement of the sum of Kshs.1,013,719,327.00 vide Confirmation Notice of Assessment No. 001243.

7. The Appellant being aggrieved by the Confirmation Notice on Assessment of outstanding Value Added Tax (VAT) issued pursuant to Section 32A of the Value Added Tax Act (Cap 476) now repealed for Assessment No.00999999999999 for the period January 1998 to March 2005 filed it's Memorandum of Appeal together with the Statement of Facts with the Value Added Tax (Appeals) Tribunal At Nairobi, now dissolved, on 12th April 2007.
8. The Respondent despite being served did not file it's Statement of Facts within the stipulated period and on 18th May 2007 sought leave for extension of time for filing the same vide their application of even date.
9. The Appellant filed a Notice of Preliminary Objection seeking *inter-alia*, to strike out the Respondent's Statement of Facts and Issues in Dispute on the following four Grounds that:-
 - a) *There is no provision in the VAT (Appeals) Rules, 1990 for extension of time at the instance of the Respondent.*
 - b) *Rule 4 of the VAT (Appeal) Rules, 1990 invoked by the Respondent is not applicable in the circumstances of this case and it does not confer any power on the Tribunal to exercise discretion to extend time at the instance of the Respondent.*
 - c) *In the absence of express powers conferred by the Rules, the Tribunal has no jurisdiction to exercise discretion to extend time for filing of Statement of Facts by the Respondent.*

d) Rule 11 of the VAT(Appeal) Rules, 1990 only applies to matters of procedure not provided for or envisaged under Rule 10 as opposed to substantive matters expressly set out by Rule 4 and 8 thereof.

10. The Preliminary Objection was heard and determined on 15th July 2008 when the Honorable VAT Tribunal, as it then was, considered the submissions by both parties and upheld the Preliminary Objection and struck out the Respondent's Statement of Facts and the Appeal was to proceed for hearing as an unopposed Appeal pursuant to Rule 10 (b) of the Value Added Tax (Appeals) Rules, 1990.

THE ARGUMENTS:-

11. When the matter came up for hearing on the 19th May 2016 the Appellant reiterated that the Appeal was to proceed unopposed in view of the Orders of the defunct VAT Appeals Tribunal of 18th May 2007 and opted to deal with the Appeal in two ways viz Counsel for the Appellant addressed the legal aspects and the Tax Agent addressed the Technical aspects.
12. The Respondent was directed to strictly confine themselves to the legal submissions and not introduce any new facts or issues and to solely rely on the Appellant's case and the documents filed in the Memorandum of Appeal and Statement of Facts.
13. Both parties did not call any witnesses but opted to make oral submissions.

14. Subsequent to the hearing of the oral submissions by the parties, the Tribunal directed the parties to file written submissions which the parties were to exchange and the submissions scheduled for highlighting on 13th July 2016. Both parties complied.
15. On the 13th day of July, 2016 the Respondent's Counsel Mr. Ado sought directions and raised concerns that the Appellant had filed a case at the High Court at Nairobi being HCCC. No.40 of 2008, which the Respondent stated raised substantial and similar issues as the Appeal before the Tribunal and that it would be an exercise in futility if the Tribunal was to make a finding while there was stay on the assessed amount and enforcement of the Notice of Confirmation of Assessment.
16. The Appellant's Counsel refuted the submissions and stated that they already indicated that they were abandoning the issue of stay at the High Court and that the issue of jurisdiction and the assessment was to be addressed by the Tribunal, whilst the High Court was only to deal with and determine the legality of the raid or otherwise.
17. The Tribunal after considering the submissions by the parties on the preliminary issue gave directions that it had the jurisdiction to hear the Appeal in the absence of orders staying proceedings before it from the High Court and further found that the issues in the High Court Case related to the raid and not the substance of the Appeal which was

whether the Confirmed Assessment was properly raised and if the amounts of tax demanded therein were due and payable.

18. The parties then proceeded to highlight their submissions relying written submissions filed by the Appellant on 14th June 2016 and 29th June 2016 which both parties adopted. The Tribunal directed that the decision would to be rendered on notice.
19. The Appeal by the Appellant against the Respondent's notice of confirmation dated 13th March 2007 of the additional tax assessment was premised on the grounds set forth in the Memorandum of Appeal dated the 12th April 2007 as under:-
 - a. The assessment is based on a biased estimate of 50% "under declared" yield and thus, sales which has no factual basis.
 - b. The Resident KRA officer at the factory maintains adequate excise records.
 - c. Large Taxpayer Office (LTO) also have audited the years in question.
 - d. KRA's own lab report confirms that we have declared correct yield.
 - e. KRA have used retrospective approach by using information of 2005 to calculate under declared sales for 1998
 - f. Other factory and industry factors were not considered.
 - g. We were not given an opportunity to verify the KRA findings exhaustively though we requested for KRA co-operation to demonstrate their findings to us on numerous occasions.

20. The Respondent's Statement of Facts was expunged from the record on 15th July 2008 and the Respondent's were confined to legal arguments whilst relying on the documents filed by the Appellant.

ISSUES FOR DETERMINATION

21. The issues for determination on the basis of both the oral and written submissions on record before the Tribunal are;
- i) Whether the assessment was excessive and not factual based;
 - ii) Whether previous audits had been conducted and if so what were the outcomes thereof;
 - iii) Whether the law allows the Respondent to re-open an audit that has been concluded ;
 - iv) Whether the Appellant was granted an opportunity to verify all the findings of the Respondent;
 - v) Whether the Appellant has challenged the legality of the raid at the Tribunal?

ANALYSIS

22. The Tribunal has perused the Memorandum of Appeal and Statement of Facts filed by the Appellant as well as it's written submissions and the Respondent's submissions and now proceeds to analyze the Appeal as follows;
23. The Appellant is a local distillery manufacturing, blending and selling various distilled potable spirits with its head office in Industrial Area

along Dunga Road and are registered tax payers. It is not in dispute that on 18th May 2005 the Respondent proceeded to the Appellant's premises and by notice pursuant to Sections 30 and 31 of Value Added Tax Act Cap 476, carried away the Appellant's records to conduct investigations to ascertain whether the Appellant was involved in accounting malpractice with a view to avoiding tax by maintaining incorrect records that did not reflect the production of the various factories of the Appellant.

24. The Appellant maintains that they were not involved in any of the alleged activities as the Respondent had a Revenue Officer permanently at the factory in Athi River who was the only authorized person to receive and issue molasses for use at the fermentation tanks and distillation process. According to the Appellant, notices would be issued to the said Officer for fermentation process as well as distillation so that the requisite approval would be given before commencement of production and records maintained on a daily basis under the custody of the said Officer. The Appellant therefore contends that with these procedures and overall control being with the Respondent's Revenue Officer, it was therefore not possible to understate production with a view to tax avoidance.
25. The Appellant further contends that the Respondent previously conducted audits for the periods January 1997 to December 1999 and January 2003 to August 2004 and no excise issues arose, as well as tax audits having been conducted on VAT, Excise, PAYE and Income Tax

up to the 2003 and having been subjected to various audits, disputes how the Respondent arrived at the conclusion that there was under declaration for excise purposes by 50%. The Appellant relies on a report prepared by the Respondent's Internal Auditors and Customs Laboratory that the yields stated were correct and tallied with their records with the rider that the amount of 163.95 litres was total alcohol and not potable alcohol as stated in the report and therefore there was no under declaration of yield and sales .

26. The Appellant contended that due to inefficiency of the plant equipment, aged 20 years old against a life span of 10 years, the distillery has corroded which in turn affects the vaporization and condensation process as well as quality of raw materials. High losses during transfer of molasses and manual handling reduces the yield by 33.5 litres to 130 litres. The leakages as a result of old columns cause further losses which the Appellant contends the Respondent noted it's report.
27. The Appellant contends that it is incorrect for the Respondent to rely on the memo dated 6th May 2005 to calculate excise tax as the distillery is unable to produce 233 liters from a ton of molasses and further the Memo on Spirit Cost on Molasses and Sugar dated 6th May 2005 from the Chief Chemist to the Appellant's Chairman that the Rate of Molasses -3,000.00 Kshs/ton from one ton of molasses they produced 235 liters of Alcohol and cost/ BL. 12.76/BL and Sugar Rate of sugar-5,000.00 Kshs/ton, from one ton of sugar they produced 433

liters of Alcohol and Cost/ BL. 11.54 Kshs/BL cannot be relied on. The Appellant has disputed the circumstances under which it was prepared and further that though the Chief Chemist Research and Development (R&D) considers many tests and does not deal directly with the Chairman of the company as protocol mandates that he report to the General Manager incharge of Production .

28. The Appellant has further discredited the authenticity of the Memo of 6th May 2005 on the grounds that the Appellant does not utilize sugar in it's production process and went ahead to produce a receipt for the purchase of sugar from a supermarket to demonstrate the market cost as Kshs.57.50 per kilogram or Kshs.57,500 per ton and not Kshs.5,000/= which would translate to Ksh.5.00 per kilogram. According to the Appellant it was impossible therefore to rely on the memo which stated and referred to incorrect prices for a commodity such as sugar.
29. The Appellant argues that the rate of molasses at Kshs.3,000/= per ton is also not realistic as they purchased their molasses from Mumias Sugar Company at the rate of Kshs.1,200/= per ton with every consignment of molasses giving different Production output depending on quality, efficiency, maintenance, temperature variation and quality of yeast among other relevant variables.
30. The Respondent relied on the Appellant's documents filed with the Statement of Facts and stated that the calculations are empirical not

estimates as averred by the Appellant with 50% under declaration of sales being noted at the time of audit which considered the documents availed for examination pursuant to the notice issued under Section 30 and 31 of the VAT Act and relied on the Inspection Report prepared by its Officers forwarded to the Appellant vide letter dated 4th October 2006 and the letter dated 11th July 2006 wherein the Respondent noted discrepancies in actual sales in the various factories and depots.

31. The Respondent contends that the fact that there was a resident Revenue Officer at the Appellant's premises did not address the fact the said officer only works between 8.00am and 5.00pm whereas the Appellant's plant functions on a 24 hour basis and therefore the Revenue Officer would not always have control of what goes on at night and indeed these were some of the risks captured in the audit report. The Respondent further contends that the Appellant never responded to the audit report.
32. The Respondent further avers that there was no retrospective approach applied as alleged by the Appellant as the entire exercise concentrated on the period 2004 to 2005 and relied on the yield, stocks and sales from the Nairobi depot.
33. The Respondent contends that the onus is on the Appellant to demonstrate to the Tribunal with evidence that the factors they intend to rely on relating to reduction of production from 235 liters to 135

litres for a ton of molasses and that the records maintained by the Resident Revenue Officer tallied with the documents maintained by the Appellant to rebutt the issue of understated sales.

34. The Respondent contends that the mere denial of the internal memo, which was addressed to the Chairman of the Appellant's business is not sufficient. To the contrary the existence of such a Memo lends credence to the findings by the Respondent that the Appellant was involved in malpractices aimed at understating its sales. The Respondent further asserted that the records were maintained by the Appellant and not its Revenue Officer.
35. It was the Respondent's case that previous audits had been carried out by the Large Taxpayer Office which is a sister department of the Commissioner of Investigation & Enforcement. They informed this Tribunal that the Commissioner of Investigation & Enforcement moved pursuant section 31 of the VAT Act which authorized them to enter premises to conduct searches and thus the two audits were distinct, different and mutually exclusive.
36. The Respondent further states that the Appellant was given sufficient opportunity to verify the Respondent's findings and relied on the various correspondences annexed to the Appellant's Statement of Facts and affirms that they acted within the set parameters of the law.

37. The Respondent was categorical that the Tribunal lacked jurisdiction as the issues on Appeal are similar to the issues raised *in High Court Case No.40 of 2008 London Distillers (K) LTD and Another Vs Kenya Revenue Authority* and wanted the Tribunal to stay its proceedings pending the outcome of the decision of the High Court.

- i) The Respondent admitted to not having filed its Statement of Facts due to circumstances beyond its control. They relied on Article 159(2)(b) of the Constitution of Kenya and averred that the Tribunal should not pay undue attention to procedural technicalities and requirements at the expense of substantive justice.
- ii) The Respondent urged the Tribunal to uphold the assessment of Kshs.1, 031,719,327.00 having conducted a search and confiscated the records, books and equipment containing accounting information necessary for determination of the tax payable by the Appellant pursuant to Article 210 of the Constitution of Kenya which legislation they relied on in determining the additional assessment. The Respondent maintains that from the evidence adduced by the Appellant, the Respondent was fair equitable and afforded the Appellant ample time to respond to all allegations leveled against it but they failed to provide evidence to support their grounds of Appeal and urged the Tribunal to dismiss the Appeal with costs.

FINDINGS

38. The Tribunal finds that despite having addressed itself on the issue of jurisdiction on 22nd March 2016 and 19th May 2016, the Respondent

has once again in their submissions challenged the authority and jurisdiction of the Tribunal to entertain this Appeal. The Tribunal therefore must once again reiterate that there wasn't and isn't an Order presented to the Tribunal to warrant the stay of the proceedings before it and it proceeded well within its powers to hear and determine the Appeal. The Respondent did not provide any Order in support of its submissions and in the absence thereof the Tribunal maintains that it has acted correctly by proceeding to hear and determine the Appeal.

39. The Tribunal further finds that the argument by the Respondent that the issues before it are similar to those raised in *High Court Case No. 40 of 2008 London Distillers (K) LTD and Another Vs Kenya Revenue Authority*, pending before the High Court, is baseless as the grounds of the Memorandum of Appeal are: -
- a. The assessment is based on a biased estimate of 50% "under declared" yield and thus, sales which has no factual basis.*
 - b. Resident KRA officer at factory maintains adequate excise records.*
 - c. Large Taxpayer Office (LTO) also have audited years in question.*
 - d. KRA's own lab report confirms that we have declared correct yield.*
 - e. KRA have used retrospective approach by using information of 2005 to calculate under declared sales for 1998*
 - f. Other factory and industry factors were not considered.*

g. We were not given an opportunity to verify ask the KRA findings exhaustively though we requested for KKRA co-operation to demonstrate their findings to us on numerous occasions.

There is no mention on the legality or otherwise of the raid which is the subject in issue at the High Court and further there is no indication that the Appellant has challenged the Assessment at the High Court.

40. The Tribunal further finds that issues relating to Appeals on objection to confirmed assessments by the Commissioner are within the mandate of the Tribunal as provided for under Section 3 of the Tax Appeals Tribunal Act, 2013 and the Procedures of Appeals from the decision of the Tribunal to the High Court are stipulated at Section 32 of the TAT Act, 2013 and The Tax Appeals Tribunal (Appeals to the High Court) Rules of 2015. The Tribunal agrees with the Appellant that the High Court therefore lacks jurisdiction to hear any dispute relating to the confirmed decision of the Commissioner in the first instance.

41. The Tribunal also finds that the Respondent admitted to filing their Statement of Facts out of time and this issue was effectively heard and determined by the VAT Tribunal At Nairobi and a Ruling delivered on 15th July 2008 and the attempt by the Respondent to reopen this issue is tantamount to this Tribunal sitting on Appeal to consider and interrogate the decision of a court with similar jurisdiction.

42. The Tribunal finds that indeed if the Respondent felt aggrieved by the decision of VAT Tribunal they ought to have appealed to the High Court. It is a misconception of the law that adherence to the set procedures is a mere technicality.
43. The Tribunal also finds that whereas discretion is granted to it to receive any other documents which may be necessary for review to assist it in its deliberations when rendering its decision, the documents referred to are supplemental to and additional to those which ought to have been filed together with the Statement of Facts and not the Statement of Facts itself. Section 15(2) of the TAT Act, 2013 further goes to provide that;

“The Tribunal may require the Commissioner to submit to the Tribunal additional documents that, in the opinion of the Tribunal, may be in the Commissioner's possession or control.”

44. The Tribunal does not operate in a vacuum and is guided by section 26 of the TAT, Act 2013 which provides;

The Tribunal shall ensure that every party to proceedings is given a reasonable opportunity to —

(a) Present his case; and

(b) Inspect any documents in relation to the proceedings and make submissions.

And Section 30 of TAT Act 2013 provides;

“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,”

45. From the foregoing provisions, the Respondent was given the opportunity to orally cross-examine the evidence adduced by the Appellant pertaining to this case, refer to the documents filed by the Appellant in their Statement of Facts and also the right to file their written submissions within the time frame given by the Tribunal. This is a right that cannot be taken away from the Respondent even though the VAT Tribunal has expunged their Response to the Appeal as contained in Statement of Facts.
46. The Tribunal finds that the confirmed assessment was raised upon the Respondent conducting a search at the Appellant's premises on 18th May 2007 and carting away documents, records and equipment which were subsequently utilized to prepare the audit report of 4th October 2006 wherein the Respondent considered various factors that in their view were likely to affect the production process and also reviewed the procedures applied by the Appellant with the involvement of the Revenue Officer who was charged with the responsibility of supervision of the Dips & Determination of Strength Register which the audit team found in the custody of the Resident Officer.

47. The Tribunal finds that the Appellant has failed to satisfactorily demonstrate that the audit by the Large Tax payer Office (LTO) and the Investigation and Enforcement Department considered the same factors and issues as the excise audit conducted previously was for the period January 2003 to December 2004 whereas the Assessment by the Investigations and Enforcement Department considered all the records maintained by the Appellant with regard to information on sales contained in the computers of the Appellant and the declared sales which were at variance, as The Appellant failed to demonstrate that the Accounts records found in the computer were ever considered by the Large Tax payer Officer at the time of conducting the audit, and The letter dated 11th November 2004 refers to documents availed to the Resident Officer and not the ones held in the Computers are found to be at variance with the information given to the said Officer.
48. The Tribunal finds that the audit report of 4th October 2006 faulted the outdated methods that were applied by the Appellant in their production process which would in effect result in errors and omissions and made various recommendations on improvement of procedures and methods to be applied to ensure better efficiency, maintenance of records and provision of equipment to the Resident Revenue Officer whose duty was to oversee the denaturing process.
49. The Tribunal finds that there was laxity in the manner in which the Appellant maintained relevant records which made it difficult for the Respondent to arrive at any other decision than the one they did

while assessing the additional Tax. It is trite law that the onus is on the Appellant to disprove the confirmed assessment by providing evidence to the contrary to the Tribunal for consideration to warrant setting aside of the Commissioner's assessment.

50. The Tribunal finds that other than the correspondence between the Appellant and the Respondent no other evidence has been placed before it for analysis and consideration to enable the Tribunal to determine the Appeal in favour of the Appellant.
51. The Tribunal finds that the burden shifted to the Appellant to prove their grounds of Appeal and that even in the absence of the Statement of Facts from the Respondent, as is the case herein, the Appellant is still required to provide cogent evidence to clearly demonstrate that they are not culpable of the charges of malpractice levelled against it which resulted in the Respondent invoking the provisions of Section 31 of the Value Added Tax Act in Confirming the additional assessment.
52. The Tribunal having reviewed the evidence adduced finds that there was under declaration of the yield and sales. No evidence has been placed before the Tribunal by the Appellant for consideration that they did not maintain two sets of accounts other than the denial of the computation of the assessment based on the internal memo which the Appellant is unable to explain the circumstances under which it was prepared.

53. The Tribunal further finds that the argument by the Appellant that the Respondent had already conducted previous audits for the same period and no anomalies were found to be untenable, as Section 31 of the Value Added Tax Act empowered the Respondent to enter into the premises and require, *inter alia*, production for examination records and books of accounts for interrogation. It was upon this basis that the Respondent having interrogated the documents availed noted the under declaration of sales which the Appellant was not able to explain.
54. Further the Tribunal notes that the Appellant has in its Statement of Facts stated that they do not utilize sugar in their production processes however at page 3 of the audit report among the raw materials listed therein reference is made to sugar as one of the raw materials purchased by the Appellant and therefore an attempt by the Appellant to disown the internal Memo contained in its Pleadings, which makes specific reference to *Spirit Cost on Molasses and Sugar* with computations made therein on the output of both Molasses and sugar in the production process, is an afterthought intended to mislead the Tribunal.
55. The Tribunal finds that the retail purchase receipts availed from the supermarket on the cost of sugar is of no relevance in this Appeal, this purchase was not related to the production process and secondly the laboratory test results dated 21st August 2006 also annexed to the Appellant's Statement of Facts supports the findings by the

Respondent. No independent tests were conducted nor evidence adduced to rebut the Respondent's findings and they remain unchallenged.

56. The Tribunal finds that a series of meetings were held between the parties prior to and after the confirmation of the assessment prior to hearing of the Appeal, however the parties were unable to amicably resolve this matter with some of the disputes ending at the High Court and this Tribunal. The Appellant misrepresented the facts on this ground of Appeal and the same of necessity fails.
57. The Tribunal finds that the present Appeal does not challenge the legality of the raid as this issue is pending before the High Court for determination in *High Court Case No. 40 of 2008 London Distillers (K) LTD and Another Vs Kenya Revenue Authority* and the Tribunal cannot in the circumstances delve into this matter and leaves the same for determination by the Superior Court.

DECISION

58. The Tribunal having entered the above findings holds that the amount of Kshs.1,031,719,327.00 is chargeable for Value Added Tax purposes pursuant to Section 32A(5)(b) of the Value Added Tax Act (now repealed).
59. The Tribunal therefore upholds the assessment of tax and accordingly finds that the Appeal has no merit and it is hereby dismissed with no orders as to costs.

DATED and DELIVERED at NAIROBI this 16th Day of November, 2016

In the presence of:-

MWATHE h/b for KIBE MUNGAI ADVOCATE
for the Appellant

FRIDAH MWONGERA for the Respondent

MOSES BUYUKA OBONYO
CHAIRPERSON

BONIFACE DIMMO
MEMBER

DANIEL TANUI
MEMBER

LILIAN RENEE OMONDI
MEMBER

FRANCIS KIVULLI
MEMBER