**Singapore Motors Limited v Commissioner of Domestic Taxes (Income Tax Appeal E039 of 2021) [2024] KEHC 2443 (KLR) (Commercial and Tax) (8 March 2024) (Judgment)**

Neutral citation: [2024] KEHC 2443 (KLR)

**REPUBLIC OF KENYA**

**IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)**

**COMMERCIAL AND TAX**

**INCOME TAX APPEAL E039 OF 2021**

**FG MUGAMBI, J**

**MARCH 8, 2024**

**BETWEEN**

**SINGAPORE MOTORS LIMITED ..... APPELLANT**

**AND**

**THE COMMISSIONER OF DOMESTIC TAXES ..... RESPONDENT**

***(An appeal from the Judgment of the Tax Appeals Tribunal dated 1st April 2021 in Tax Appeal No. 405 of 2019)***

**JUDGMENT**

## Background and Introduction

1. The respondent audited the appellant's taxes for the year 2013 to 2017 and raised a tax assessment on 4th September 2018, of Kshs. 62,914,058/= made up of corporate tax, VAT, penalties and interest. The respondent requested the appellant for further information in order to complete the audit.

2. The parties met on 14th and 25th September 2018 to discuss the findings contained in the aforementioned letter. The respondent revised the assessment and issued a notice of assessment dated 24th April 2019 for Kshs.99,960,219/- inclusive of Kshs.47,882,066/- corporation tax, Kshs.24,593,386/- income tax and Kshs.27,484,767/- VAT.

3. The appellant filed a notice of objection to the assessment, dated 22nd May 2022, to which the respondent issued its objection decision dated 23rd July 2019 amending the tax, inclusive of principle tax, penalties and interest, to Kshs.62,446,480/- composed of Kshs.41,998,014/- corporation tax and Kshs.20,448,466/ VAT.

4. Dissatisfied with this assessment the appellant filed an appeal at the Tax Appeals Tribunal (the Tribunal), in which it was partly successful. Through its judgment of 1st April 2022, the Tribunal

found that the tax assessment for the year 2013 was statute-barred and that the respondent erred by confirming a default assessment for the year 2017.

5. It further found that the appellant did not prove by way of evidence that the corporation tax assessments for the years 2014 to 2016 were wrong or excessive. The Tribunal held that the appellant was an importer of goods within the meaning of section 2 of the *VAT Act*; that the deregistration application for VAT purposes was not availed by the appellant and that the appellant was unable to prove that its income for the period 2013 to 2017 was below the Kshs. 5 Million threshold.

6. For these reasons, the Tribunal set aside the tax assessment for the year 2013 in respect to income tax and VAT; directed the respondent to reconcile the tax liability for the year 2017; upheld the respondent's corporation tax assessment for the years of income 2014 to 2016 and VAT tax assessment for the years 2014 to 2017.

7. Still dissatisfied by the finding of the Tribunal, the appellant instituted the present appeal vide the Memorandum of Appeal dated 7th May 2021. In response, the respondent filed its statement of facts dated 15th December 2021. The appeal was canvassed by way of written submissions. The appellant's submissions are dated 21st September 2022 and those of the respondent 7th February 2022.

**Analysis**

8. The Court has carefully considered the record of appeal, the statement of facts, the parties' respective submissions, authorities and the impugned judgment.

9. The issues arising for determination are whether the Tribunal erred in law and in fact in upholding the corporate tax assessment for the years of income 2014 to 2016 and the VAT assessment for the years 2014 to 2017 and whether the Tribunal erred by allowing the imposed penalty of 20% under section 84 of the *Tax Procedures Act*.

**On Corporate Tax**

10. The dispute between the parties arises from the respondent's treatment of the appellant as a net importer of cars and machinery for corporate tax purposes. It is also as a result of basing the appellant's tax assessments on the entirety of cash inflows recorded in the appellant's bank accounts, which were treated as business gains and profits in line with section 2 of the *Income Tax Act*.

11. The appellant disputes this interpretation, insisting instead that it is a broker whose function is to facilitate vehicle purchases, further arguing that only the commissions received for such services constitute taxable income. The appellant further contends that any funds exceeding these commissions, which were directed towards vehicle sellers or clearing agents, should not be considered as part of its income.

12. On this basis the appellant challenges the Tribunal's decision to uphold the Corporate Tax assessments for the fiscal years 2014 to 2016, which were predicated on the gross bank entries, arguing that this approach contravenes sections 3 and 15 of the *Income Tax Act*.

13. The respondent outlined the methodology applied for the tax assessment, which entailed scrutinizing the deposits into the appellant's accounts at Equity and Chase banks against their income tax and VAT submissions for the years 2013 to 2017. This examination was aimed at ascertaining the net banking balance, from which the net profit was calculated after accounting for cost of sales, expenses, loan disbursements, credit reversals, and contra entries.

14. The respondent then compared the appellant's net profit figures with those declared, to identify any discrepancies in declared income, forming the foundation for the assessed corporate tax. Additionally, the respondent acknowledged recognizing expenses as reported in the appellant's financial statements.

15. In assessing taxable income related to customs valuation, the respondent conducted a verification exercise. It found that the cost of sales totaling Kshs. 152,493,355/-, as claimed by the appellant, exceeded the amounts verifiable through its Simba System. Consequently, the respondent adjusted the allowable imports to the verifiable sum of Kshs. 79,363,101/-.

16. This Court has remained emphatic that under section 30 of the *Tax Appeals Tribunal Act* (TATA) and section 56 of the *Tax Procedures Act* (TPA), the burden of proving that an assessment is wrong or excessive remains upon the taxpayer. (See *Thwama Building Services Limited v Commissioner of Domestic Taxes*, (Income Tax Appeal E016 of 2022), [2023] KEHC 23308 (KLR) (Commercial and Tax) (12 October 2023) (Judgment)). The taxpayer's burden must be discharged and only then does it shift to the Commissioner to prove the correctness of its assessment.

17. The underlying principle for this approach was articulately outlined by this Court in the case of *Commissioner of Domestic Services v Galaxy Tools Limited*, [2021] eKLR, as per Majanja, J. The Court observed that Kenya operates under a self-assessment tax regime, which mandates taxpayers to calculate and remit taxes based on their own declarations and assessments of what they owe. Within this framework, tax laws empower the Commissioner to retrospectively review and determine the accuracy of the taxes remitted by the taxpayer.

18. Consequently, as per the Court's rationale, it is incumbent upon tax authorities to evaluate and determine the tax liability they believe a taxpayer owes. Under this system, the onus shifts to the taxpayer to contest and prove that the assessment or the demanded tax by the authorities is erroneous or inflated. This Court must therefore determine whether the appellant discharged this burden to the required standard as to disprove the tax assessment by the respondent.

19. The Tribunal, in its judgment, specifically noted at paragraph 34 that the appellant failed to submit evidence for items claimed to be exempt from corporate income tax. Upon reviewing the record, it is clear that the respondent had requested the appellant to produce specific documents to facilitate the tax assessment. While some documents were indeed provided by the appellant, which informed the respondent's determination of the tax due, not all requested documentation was made available.

20. The objection decision dated 23rd July 2019 reveals that crucial documents, including the appellant's sales ledger, purchase ledger, and an analysis of cash movements between Equity and Chase banks, among others, were not furnished to the respondent. This lack of comprehensive documentation has implications for assessing the accuracy and completeness of the tax obligations as determined by the respondent.

21. It is further noted that additional documentation, including vehicle purchase agreements, which would have substantiated the identities of the purchaser and seller of the vehicles, thus corroborating the assertion that the appellant served solely in a brokerage capacity, were not furnished in their entirety to the respondent. Furthermore, the vehicle registration documentation tendered for the relevant transactions was found inadequate to buttress the appellant's claim or explicate the nature of the deposits reflected in the bank statements.

22. Given the scarcity of evidence to adequately explain the origin of income in conjunction with the business's described activities, and considering the respondent's self-representation on its letter head as an importer of new and pre-owned vehicles and machinery, the respondent's evaluation cannot be deemed erroneous.

23. In *Commissioner of Domestic Taxes v Structural International Kenya Ltd*, (Income Tax Appeal E089 of 2020) [2021] eKLR, this Court held in respect of a situation where the Commissioner requests additional documents that:

> "If additional documents, which would be reasonably expected to be in [his] possession is requested for to verify the alleged transactions, he should produce the same to the commissioner. That is what is expected of a keen and diligent trader."

24. Accordingly, in alignment with the Tribunal's findings, I hereby affirm that the respondent's determination in the assessment of corporate tax for the 2014 to 2016 was devoid of any error and that indeed the appellant failed to account for corporation tax on bank deposits into the appellant's bank accounts held at Chase Bank and Equity Bank during the audit period.

**VAT Assessment**

25. The second issue is with respect to the VAT assessment for the years of income 2014 to 2017. The appellant contended that the Tribunal erred by holding that it was an importer of the vehicles despite the appellant providing documentary evidence of import documents showing the owners or persons beneficially interested on goods to be the importers whom it was acting for and that the appellant was not acting on its own capacity.

26. The appellant contended that there had been no supply of goods within the meaning of section 2 of the *VAT Act*, pointing out that it was not the owner of the goods or vehicles imported. Further, the appellant lamented that the respondent raised an assessment with respect to gross bank deposits yet the agency commissions that it earned were less than the Kshs. 5,000,000/= statutory threshold required for VAT registration. Additionally, the appellant highlighted that though it applied for VAT deregistration when its commissions fell below the threshold, the same was not processed by the respondent.

27. The respondent's case was anchored in the findings of the audit, which revealed that the appellant's income was underreported by Kshs. 88,714,204/= for the years 2013 to 2017, a figure that, even when averaged, went beyond the Kshs. 5,000,000/= threshold. The respondent persisted in its assertion that the appellant failed to adequately refute the allegation of underreported income to the Tribunal's satisfaction.

28. The record shows that on the 6th of June 2019, the respondent requisitioned the import documentation for the vehicles, specifically requesting proof that the vehicles were registered in the names of the customers. Contrary to the appellant's claims, these documents were not forthcoming as explained in the objection decision dated 23rd July 2019. The documentation proffered by the appellant did not effectively counter the respondent's assessment, a fact that was duly acknowledged in the adjudication. Consequently, the appellant's assertion that its submissions were disregarded by the respondent is misaligned with the reality that the respondent explicitly communicated the deficiencies in the documents that were submitted.

29. I also note that the appellant did not specify the contra entries in the bank account statements that were not considered by the respondent or to show that there was no under declared income. The appellant did not furnish evidence to substantiate its claim that its agency commissions were less than the Kshs. 5,000,000/= threshold, or to corroborate its assertion of having sought deregistration from VAT at any juncture of its business operations.

30. As emphatically noted by the Tribunal, section 2 of the *VAT Act* defines an importer as:

> " the person who owns the goods or any person who is, for the time being, in possession of or beneficially interested in the goods at the time of importation."

31. I concur with the Tribunal's determination that the appellant qualifies as an importer of goods as construed under the *VAT Act*, in light of the absence of contravening evidence. It is also my finding that the Tribunal did not commit an error in affirming the VAT Assessment for the fiscal years 2014 to 2017.

32. The final issue in this appeal is whether the respondent incorrectly imposed a penalty of 20% under section 84 of the *Tax Procedures Act*. The appellant argues that by imposing the 20% penalty, the respondent was inferring that the appellant knowingly made a false statement to the respondent in its tax returns.

33. In response the respondent defended its action and asserted that it correctly imposed the 20% penalty as it did not err in its assessment of corporate tax and VAT.

34. Section 84 of the *Tax Procedures Act* provides that:

> " (1) This section applies to a person-
>
> (a) if that person knowingly makes a statement to an authorised officer that is false or misleading in a material particular or knowingly omits from a statement made to an authorised officer any matter or thing without which the statement is false or misleading in a material particular; and
>
> (b) if the tax liability of that person or of another person computed on the basis of the statement made by that person is less than it would have been had the statement not been false or misleading (the difference being referred to as the "tax shortfall").
>
> (2) Subject to subsections (3) and (4), a person to whom this section applies shall be liable to a tax shortfall penalty of— (a) seventy-five per cent of the tax shortfall when the statement or omission was made deliberately. (b) deleted by Act No. 23 of 2019, s. 34."

35. Having found that the Tribunal's decision upholding the respondent's corporate tax assessment for the years of income 2014 to 2016 and VAT assessment for the years 2014 to 2017, I am of the considered view that the respondent cannot be faulted for imposing the 20% penalty on taxes due.

**Determination**

36. For all the foregoing reasons, the Court finds no merit in the appeal and the same is dismissed. The decision of the Tribunal dated 1st April, 2021 is upheld. There shall be no orders to costs.

**DATED, SIGNED AND DELIVERED IN NAIROBI THIS 8TH DAY OF MARCH 2024.**

**F. MUGAMBI**

**JUDGE**