REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT MILIMANI

COMMERCIAL & TAX DIVISION

INCOME TAX APPEAL NO. E220 OF 2024

COMMISSIONER OF DOMESTIC TAXES ..... APPELLANT

VERSUS

DINESH CONSTRUCTION LTD ..... RESPONDENT

(Being an appeal from the Judgement of the Tax Appeals Tribunal delivered at Nairobi on 28 June 2024 in Tax Appeal Tribunal Appeal No. TAT E356 of 2023)

JUDGEMENT

1. The Appellant is a principal officer appointed under section 13 of the Kenya Revenue Authority Act, Cap 469 and the Kenya Revenue Authority, mandated to collect and receive all Government revenue in accordance with the various tax statutes.

2. The Respondent is a private limited company incorporated in Kenya, whose principal activity is building and civil engineering contracts.

3. The genesis of the dispute lies in the Appellant's statutory mandate to assess and collect taxes. Sometime in 2021, the Appellant, relying on intelligence reports and internal data analysis, identified potential compliance risks in the Respondent's tax affairs. Consequently, the Appellant initiated a comprehensive compliance check and in-depth tax audit covering the Respondent's business operations for the period 2016 to 2021. The scope of

the audit was extensive, encompassing multiple tax obligations: corporation tax, value added tax (VAT), pay as you earn (PAYE) and withholding tax.

4. The audit process involved a series of engagements, including desk reviews of the Respondent's returns, comparisons with third-party data (such as withholding tax certificates and customs entries), and meetings between the parties. On 30 June 2022, the Appellant issued preliminary audit findings, which were discussed in meetings held on 4 August 2022 and 17 August 2022. Subsequently, on 30 August 2022, the Appellant issued a comprehensive tax audit preliminary assessment letter proposing a tax liability of Kshs 1,137,582,759/=. Following further representations by the Respondent's director on 27 September 2022 and a response letter dated 5 October 2022, the Appellant reviewed the figures downwards.

5. The audit culminated in the issuance of a confirmed Notice of Assessment dated 14 December 2022, demanding taxes amounting to Kshs 773,054,888/=. The breakdown of this assessment was:

   (i) Kshs 453,393,832/= for corporation tax, relating to under-declared income derived from banking analysis and disallowed purchases;
   (ii) Kshs 302,544,644/- for VAT, relating to input VAT claimed from alleged missing traders and undeclared sales;
   (iii) Kshs 17,004,471/= for PAYE, relating to undeclared motor vehicle benefits; and
   (iv) Kshs 111,941/= for withholding tax, relating to professional and management fees.

6. Aggrieved by this assessment, the Respondent lodged a Notice of Objection on 15 February 2023. Crucially for the determination of this appeal, the Respondent's objection focused primarily on the corporation tax and VAT assessments related to the disallowed purchases and banking variances. The

Appellant reviewed the objection and rendered an Objection Decision on 13 April 2023, confirming the assessment in its entirety.

7. The Respondent subsequently filed a Notice of Appeal at the Tax Appeals Tribunal on 10 May 2023, followed by a Memorandum of Appeal and Statement of Facts. In its judgement, the Tribunal partially allowed the appeal. Specifically, the Tribunal held that the Appellant's assessment regarding Income Tax for the period up to 13 December 2017 was time-barred under section 31(4) of the Tax Procedures Act and expunged it. It held that the Respondent provided sufficient documentation to support its purchases and that the Appellant had failed to prove fraud regarding the alleged missing traders. Consequently, the Tribunal set aside the assessments related to disallowed purchases. However, the Tribunal upheld the assessments relating to retention income, PAYE on vehicle benefits and withholding tax on professional fees, noting that the Respondent had not effectively contested these in its objection.

8. The Appellant, maintaining that the Tribunal erred in law and fact, lodged the instant appeal on 16 August 2024. The Memorandum of Appeal raises 13 grounds, which challenge the Tribunal's jurisdiction, its interpretation of the limitation of actions, its evaluation of evidence regarding the missing trader scheme, and its application of the burden of proof.

9. The appeal was canvassed by way of written submissions.

The Appellant's Submissions

10. The Appellant's case is anchored on the premise that the Tribunal committed fundamental errors of law that resulted in a miscarriage of justice and the loss of lawful revenue.

11. On the issue of jurisdiction, the Appellant submits that the Tribunal lacked the requisite jurisdiction to entertain the Respondent's appeal because the Notice

of Appeal filed on 10 May 2023 was invalid. This argument is predicated on section 52(2) of the Tax Procedures Act, which provides:

> *A notice of appeal to the Tribunal relating to an assessment shall be valid if the taxpayer has paid the tax not in dispute or entered into an arrangement with the Commissioner to pay the tax not in dispute under the assessment at the time of lodging the notice.*

12. The Appellant argues that during the objection stage, the Respondent failed to object to 3 specific components of the assessment issued on 14 December 2022, namely the VAT on retention payment, PAYE on motor vehicle benefit and Withholding Tax on professional and management fee. By failing to address these specific items in its Notice of Objection as required section 51(3), which mandates that a taxpayer state precisely the grounds of objection, the amounts became undisputed by operation of law. The Appellant submits that the total undisputed tax amounted to Kshs 22,258,103.56. The Appellant relies on the decision in ***Commissioner of Domestic Taxes vs Diara Limited eKLR***, where the Court held that an assessment to which no objection is made becomes final and conclusive, binding the taxpayer as a statutory obligation. Further reliance is placed on ***Medox Limited vs The Commissioner for SARS (20059/2014) ZASCA 74***, where the South African Supreme Court of Appeal affirmed that un-objected portions of an assessment crystallize into debts that must be settled.

13. The Appellant contends that at the time the Respondent lodged its appeal at the Tribunal, it had neither paid this undisputed sum nor entered into a payment plan with the Commissioner. Consequently, the condition precedent set by section 52(2) was not met. Citing ***Ken Iron and Steel Limited vs Commissioner of Investigations and Enforcement KEHC 2770 (KLR)***, the Appellant argues that the Notice of Appeal is the jurisdictional foundation of the proceedings. An invalid notice renders the entire appeal a nullity. The

Appellant faults the Tribunal for noting in Paragraph 76 of its judgment that these taxes were proved as due and payable yet failing to strike out the appeal for incompetence.

14. The second aspect of the Appellant's case is that the Tribunal's finding that the assessments for the years 2016 and 2017 were time-barred. The Tribunal expunged the assessment for the period up to 13 December 2017, relying on section 31(4) of the Tax Procedures Act, which generally limits the Commissioner's power to amend assessments to 5 years. The Appellant submits that the Tribunal misconstrued the computation of time under section 31(4)(b)(ii) of the Act. This section states that for self assessment, the 5-year period runs from the date the taxpayer submitted the self assessment return to which the self-assessment relates. The Appellant noted that the year of income was 2016, the statutory due date for filing was 30 June 2017, the actual date of filing by the Respondent was 15 December 2017 and the date of amended assessment was 14 December 2022. Based on this timeline, the Appellant argues that the 5-year window opened on 15 December 2017 and closed on 14 December 2022. Since the assessment was issued on the exact date the window closed, it was within time. The Appellant contends that the Tribunal erred by likely calculating the period from the end of the accounting period or the statutory due date, thereby ignoring the Respondent's delay in filing returns. It is the Appellant's argument that a taxpayer cannot benefit from their own non-compliance to shorten the audit window.

15. On the issue of missing traders and documentary evidence, the Appellant vigorously defends its decision to disallow input VAT and expenses related to purchases from alleged missing traders. The audit revealed that the Respondent claimed purchases amounting to Kshs. 689,081,913 from suppliers who exhibited badges of fraud: they had no physical location, shared addresses with unrelated entities, did not declare the corresponding sales, and in some cases, had been identified as missing traders in other tax disputes.

16. The Appellant submits that it requested specific documents to verify the commercial substance of these transactions, including Local Purchase Orders (LPOs), delivery notes, stock movement records, and supplier statements. The Respondent failed to provide these, relying instead on simple invoices and ETR receipts.

17. The Appellant argues that the Tribunal erred in law by relying on the decision in ***Shreeji Enterprises (K) Limited vs Commissioner of Investigations & Enforcement****,* which placed the burden on the KRA to prove the taxpayer's knowledge of fraud. The Appellant submits that this position has been overturned by binding High Court precedents, specifically ***Commissioner of Investigations & Enforcement vs Galaxy Tools Ltd eKLR*** and ***Commissioner of Domestic Taxes vs Structural International Kenya Ltd KEHC 152 (KLR*)**.

18. According to the Appellant, the correct legal position as established in ***Galaxy Tools case (supra)*** is that once the Commissioner disputes the authenticity of documents based on credible investigation, the burden shifts back to the taxpayer to prove the actual movement of goods using competent evidence beyond the invoice itself. The Appellant asserts that by accepting invoices as sufficient proof in the face of missing trader allegations, the Tribunal effectively facilitated tax evasion.

19. On the issue of the unreconciled variances, the Appellant defended its use of the banking analysis method to assess the undeclared income. The identified variances of Kshs. 157,712,644 in 2018 and Kshs. 29,622,829 in 2019 between the Respondent's bank deposits and its declared turnover.

20. The Appellant argues that under Section 24(2) of the TPA, the Commissioner is not bound by a tax return and may assess liability using any information available, including bank statements. The Appellant contends that the Respondent merely labelled these deposits as "contra entries," "loans," or

"director injections" without providing the necessary banking reconciliations, loan agreements, or board resolutions to substantiate the claims. The Appellant argues the Tribunal erred by accepting the Respondent's unsupported explanations, thereby shifting the burden of proof to the Commissioner to disprove the Respondent's bare assertions.

The Respondent's Submissions

21. On the issue of jurisdiction, the Respondent vehemently denies that the Tribunal lacked jurisdiction. It submits that Section 52(2) is only applicable where a taxpayer expressly admits to a tax liability but fails to pay it. The Respondent argues that it disputed the entire assessment in its Notice of Appeal and Memorandum of Appeal filed at the Tribunal.

22. The Respondent contends that silence on a specific tax head in the objection letter does not amount to a concession. It argues that the Appellant failed to adduce any evidence before the Tribunal demonstrating a clear admission of liability. Therefore, the Respondent argues, there was no undisputed tax to pay, and the Notice of Appeal was valid. The Respondent urges the Court to interpret Section 52(2) purposefully to facilitate access to justice under Article 48 of The Constitution, rather than using it as a procedural trap to shut out legitimate disputes.

23. The Respondent defends the Tribunal's finding on the time bar. It argues that the Appellant's notification of assessment on 14 December 2022 was issued more than 5 years after the end of the 2016 year of income. The Respondent asserts that the intention of Section 31(4) is to provide finality to tax affairs.

24. Furthermore, the Respondent argues that for the Commissioner to go back beyond five years, they must prove fraud, wilful neglect, or evasion. The Respondent submits that the Appellant failed to particularize or prove any fraud before the Tribunal. Citing Section 107 of the Evidence Act, the Respondent argues that he who alleges fraud must prove it. Since no fraud

was proven, the five-year statutory cap remained absolute, rendering the 2016 assessment illegal

25. On the issue of the missing traders, the Respondent maintains that it fully complied with Section 17 of the VAT Act by holding valid tax invoices, ETR receipts, and proof of payment for all its purchases. It argues that it cannot be held liable for the compliance failures of its suppliers. The Respondent characterizes the "missing trader" narrative as an attempt by the KRA to transfer its enforcement failures onto innocent taxpayers.

26. The Respondent argues that the Appellant's demand for LPOs, delivery notes, and supplier statements was unreasonable for the construction industry context. It relies on the Tribunal's finding that it provided all necessary documents. The Respondent distinguishes the ***Galaxy Tools case***, arguing that in that matter, there was proof of forgery, whereas in the present case, the Respondent holds genuine invoices generated from KRA's own ETR system.

27. Regarding the banking variances, the Respondent argues that the Appellant's method was flawed and relied on assumptions. The Respondent asserts that the deposits were clearly explained as inter-account transfers (contra entries) and director loans, which are not taxable income. It claims to have provided reconciliation statements which the Appellant ignored. The Respondent submits that treating all bank deposits as income ignores the reality of business operations where funds move for liquidity management purposes

Analysis & Determination

28. I have carefully considered the Record of Appeal, the Statement of Facts and the submissions by parties. The following issues lend themselves for determination:

    (i) Whether the appeal is competent before this Court;

(ii) Whether the Tax Appeals Tribunal had jurisdiction to entertain the appeal in light of the Respondent's alleged failure to pay undisputed taxes as required by Section 52(2) of the Tax Procedures Act;

(iii) Whether the amended assessment for the year 2016 was time-barred under Section 31(4) of the Tax Procedures Act;

(iv) Whether the Tribunal applied the correct legal test regarding the burden of proof and the evidentiary threshold for claiming input VAT and expenses from alleged missing traders;

(v) Whether the Tribunal erred in its treatment of the banking analysis evidence and the burden of proof regarding contra entries

29. On the first issue, the jurisdiction of this Court is circumscribed by statute. Under section 56(2) of the Tax Procedures Act, *"An appeal to the High Court or to the Court of Appeal shall be on a question of law only"*. An appeal limited to matters of law does not permit the appellate court to substitute the Tribunal's decision with its own conclusions based on its own analysis and appreciation of the facts. The Court of Appeal in ***John Munuve Mati vs Returning Officer Mwingi North Constituency & 2 others*** **[2018] eKLR** summarised what amounts to "*matters of law*" as follows:

> *[38] [T]he interpretation or construction of the Constitution, statute or regulations made thereunder or their application to the sets of facts established by the trial Court. As far as facts are concerned, our engagement with them is limited to background and context and to satisfy ourselves, when the issue is raised, whether the conclusions of the trial judge are based on the evidence on record or whether they are so perverse that no reasonable tribunal would have arrived at them. We cannot be drawn into considerations of the credibility of witnesses or which witnesses are more believable than others; by law that is the province of the trial court."*

30. This Court affirms that an appeal from the Tribunal must primarily concern a point of law. However, where a finding of fact is demonstrated to be so perverse or unsupported by evidence as to constitute an error of law, the Court may interfere.

Jurisdiction of the Tribunal and the Undisputed Tax

31. The threshold issue in this appeal is jurisdictional. Jurisdiction is the lifeblood of any judicial or quasi-judicial body, without it, any decision made is a nullity *ab initio*. The Appellant invokes section 52(2) of the Tax Procedures Act, which embodied a critical policy objective in tax administration: the "pay now, argue later" principle applied to admitted debts. It ensures that the appellate process is not used to delay the collection of taxes that the taxpayer has effectively conceded.

32. The crux of the dispute here is the definition of "tax not in dispute". The Appellant argues that the tax becomes undisputed if it is not specifically objected to in the Notice of Objection filed under section 51(3). The Respondent argues that tax is only undisputed if explicitly conceded.

33. Section 51(3) is prescriptive. It requires a Notice of Objection to state precisely the grounds of objection, the amendments required to be made to correct the decision, and the reasons for amendments. This statutory language is not merely procedural; it is substantive. It delimits the scope of the dispute. If an assessment covers 5 items, and the taxpayer only provides grounds objecting to 2, then remaining 3 items are legally accepted. The Commissioner is entitled to treat the unobjected portions as final and conclusive debts.

34. In ***Commissioner of Domestic Taxes vs Diara Limited [2022] KEHC 80 (KLR),*** the Court emphasized that the objection process is the primary mechanism for crystallizing the dispute. Once the objection window closes, any item not traversed by the objection becomes a crystallised debt

35. In the present case, the Tribunal made a specific finding of fact at paragraph 76 of its judgement:

> *"The Tribunal notes that the Appellant did not address the assessments regarding retention payments/income... vehicle benefit (PAYE), Withholding tax... in its objection. The Tribunal finds that the same had been proved as due and payable..."*.

36. This finding by the Tribunal confirms that, as a matter of fact, the Respondent did not dispute these specific tax heads in the manner prescribed by law. Yet, the Tribunal proceeded to hear the appeal without evidence that these amounts had been paid. This was a clear error of law. By entertaining the appeal while acknowledging that undisputed taxes remained unpaid, the Tribunal acted *ultra vires* section 52(2) of the Tax Procedures Act.

37. The Respondent's argument that it disputed the entire assessment in its Notice of Appeal in unavailing. A blanket denial in a Notice of Appeal cannot cure a failure to object to specific items at the statutory objection stage. The dispute resolution process is sequential: valid appeal grounds must spring from valid objection grounds. One cannot resurrect a claim at the Tribunal that died at the objection stage due to silence.

38. Accordingly, I find that the Respondent's Notice of Appeal was technically invalid for non-compliance with section 52(2). Strictly speaking, this finding is sufficient to dispose of the entire appeal by striking out. However, the dispute herein involves complex issues of missing traders and substantial sums that were genuinely disputed. To strike out the entire appeal based on the non-payment of the smaller undisputed portion would be draconian and perhaps inconsistent with Article 159(2)(d) of The Constitution.

39. Therefore, I will proceed to determine the substantive merit of the appeal to provide finality on the weighty matters raised.

Limitation of Actions

40. The Tribunal expunged the Appellant's assessment for the year 2016 on the grounds that it was time-barred. This finding was based on the assumption that the 5-year limitation period had expired by the time the assessment was issued on 14 December 2022.

41. Section 31(4)(b)(ii) of the Tax Procedures Act provides:

> *The Commissioner may amend an assessment—*
> *(b)in any other case, within five years of—*
> *(ii)for any other assessment, the date the Commissioner notified the taxpayer of the assessment:*

42. The interpretation of this section requires precise calculation of time. The law is unambiguous: the clock starts ticking from the date of submission, not the due date. Applying the dates to the law, the end of the 5-year period was 14 December 2022 as argued by the Appellant. The Appellant issued the assessment on 14 December 2022, which falls exactly on the last day of the 5-year statutory period. The Tribunal appears to have miscalculated the period.

43. Consequently, the Tribunal's decision to expunge the taxes for the period up to 13 December 2017 is set aside. The 2016 assessment is valid and reinstated.

Missing Traders and Documentation

44. This issue forms the substantial core of the tax liability. The Appellant disallowed over Ksh 689 million in purchases on the basis that they were procured from missing traders – entities that exist on paper to generate invoices for VAT input claims but do not supply actual goods or remit taxes.

45. The Tribunal allowed the Respondent's appeal on this point, relying on the precedent in ***Shreeji Enterprises case (supra)*****,** which held that the burden is on the KRA to prove that the taxpayer knew of the fraud. The Tribunal found that the Respondent had provided invoices and ETRs, which it deemed sufficient.

46. This Court must correct the legal standard applied by the Tribunal. The jurisprudence in Kenya regarding missing trader fraud has evolved decisively. The decision in ***Shreeji Enterprises case*** has been superseded by this Court's decisions in ***Commissioner of Domestic Services v Galaxy Tools Limited [2021] KEHC 5530 (KLR)*** and ***Commissioner of Domestic Taxes v Structural International Kenya Ltd [2021] KEHC 152 (KLR.***

47. In ***Galaxy Tools case***, the Court clarified the shifting burden of proof. While the taxpayer initially discharges the burden by producing an invoice, once the Commissioner—through forensic audit—raises credible doubts about the supplier, the burden shifts back to the taxpayer. At this stage, the invoice alone is no longer sufficient. The invoice is the subject of the fraud allegation; it cannot be the proof of its own validity.

48. The taxpayer must then produce competent and relevant evidence of actual supply. As established in the ***Structural International case,*** commercial reality dictates that the movement of goods worth hundreds of millions of shillings leaves a footprint beyond a paper invoice. A prudent business dealing in construction materials must have LPOs, Delivery Notes, Weighbridge tickets, stock records and site usage logs. In this case, the Appellant requested these specific documents. The Respondent failed to produce them, arguing that it is not required to keep such elaborate records or police its suppliers. This defence is legally unsustainable under section 23 of the Tax

Procedures Act and section 43 of the VAT Act, which mandate the keeping or records to ascertain tax liability.

49. By asserting that it cannot be held liable for its suppliers' non-compliance, the Respondent misunderstands the scheme of VAT. The right to deduct input tax under Section 17 of the VAT Act is premised on a valid supply. If the supplier is a "missing trader" who never bought or possessed the goods they purportedly sold, then no supply took place in law. The transaction is a fiction. If the Respondent cannot prove—via delivery notes and transport logs—that it actually received goods from these specific suppliers, it cannot deduct the input VAT, regardless of whether it holds a tax invoice.

50. The Tribunal erred by lowering the evidentiary threshold. It treated the invoice as conclusive proof of supply, ignoring the Appellant's forensic findings that the suppliers were missing. This approach makes the Tribunal an unwitting facilitator of the very fraud that the system seeks to prevent. The correct position is that where the Commissioner alleges missing trader fraud and provides *prima facie* evidence, the taxpayer must prove the transactional reality of the supply. In this instance, the Respondent failed to do so.

51. Accordingly, the Appellant's decision to disallow these purchases and input VAT was correct. The Tribunal's finding on the issue is set aside.

Banking Analysis

52. The final issue concerns the variances between the Respondent's bank deposits and the declared income. The Appellant used the banking analysis method, a standard audit tool authorized by Section 24(2) of the Tax Procedures Act, which allows the Commissioner to use any information available. The audit revealed unexplained deposits of Kshs. 157 million (2018) and Kshs. 29 million (2019). The Respondent claimed these were contra entries (inter-bank transfers) and director loans.

53. He who asserts must prove. If a taxpayer claims that a deposit is a loan, they must produce the loan agreement. If they claim it is a contra entry, they must produce the banking reconciliation showing the movement of funds from one account to another. A mere statement in pleadings is not evidence.

54. The Appellant's submissions indicate that the Respondent failed to provide the necessary banking reconciliations to support these assertions. The Tribunal accepted the Respondent's explanation without citing any specific documentary evidence that substantiated the contra entry claim. This was a misapplication of the burden of proof. Bank deposits are *prima facie* income unless explained. By failing to substantiate the non-income nature of these deposits with documentary proof, the Respondent failed to discharge its burden under Section 56(1) of the Tax Procedures Act.

55. In view of the foregoing, I find that the appeal is meritorious. I make the following orders:

    (i) The appeal is hereby allowed;
    (ii) The judgement of the Tax Appeals Tribunal delivered on 28 June 2024 in Tax Appeal No. 356 of 2023 is hereby set aside in its entirety;
    (iii) The Appellant's Objection Decision dated 13 April 2023 confirming the assessment of Kshs 773,054,888/= is hereby upheld;
    (iv) The Appellant is awarded the costs of the appeal assessed at Kshs 50,000/=;
    (v) The Appellant is awarded the cost before the Tax Appeals Tribunal.

Dated and Delivered at Nairobi this 21 day of NOVEMBER 2025.

HELENE R. NAMISI

JUDGE OF THE HIGH COURT

Delivered on virtual platform in the presence of:

For the Appellant: Mr. Kipng'eno

For the Respondent: Ms Wetunga h/b Mr. Dachi

Court Assistant: Lucy Mwangi