

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
TAX APPEAL NUMBER 55 OF 2016

ABDALLA ABDALLA MOHAMED.....APPELLANT

=VERSUS=

THE COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGEMENT

BACKGROUND: -

1. The Appellant is a tax payer who lives in Mombasa and owns two Swahili houses situated in Kisauni and a three floor residential building at Majengo, the buildings are all located in Mombasa County. The Appellant earns rental income from the said buildings. Additionally, the Appellant is a Director of a company named Minazini Enterprises Limited. The aforesaid Company is a supplier and a retailer of various building and construction materials.
2. The Respondent is established under Section 3 of the Kenya Revenue Authority Act Cap 469 and is mandated under Section 5 thereof to act as an agent of the Government of Kenya for the assessment, collection and receipt of revenue.
3. On March 2015, the Respondent carried out an audit on Minazini Enterprises Limited's books of accounts and examined the Company's Directors' personal tax returns and bank statements pursuant to Section 56 of the Income Tax Act (CAP 470) (ITA) and Section 48 of Value Added Tax (VAT) 2013 (CAP 476). The audit covered VAT and Income Tax for the period 2011 to 2013. The Respondent issued

provisional findings on 25th August 2015 wherein repairs and maintenance expenses charged against rental income were adjusted and restricted to 40% of gross rental received.

4. The findings of the audit and the assessment of the additional taxes payable was formally communicated to the Appellant vide the Respondent's letter dated the 15th October 2015
5. The Appellant objected to the aforesaid additional assessment of taxes under Assessment Number 01212011000016/4, 0121201200003/4, 01212013000016 for Kshs. 617,553/= as principal tax and a further Kshs. 571,924/= as interest and penalties vide a letter dated the 16th February 2016 addressed to the Respondent by Josiah Njenga & Associates, Certified Public Accountants.
6. The Respondent vide a letter dated 4th April 2016 confirmed the additional tax assessment thereby prompting the Appellant to file the present Appeal on 5th day of May, 2016 before the Tax Appeals Tribunal.

THE APPEAL: -

7. The Appeal by the Appellant against the Respondent's notice of confirmation of the additional tax assessment was premised on the grounds set forth in the Memorandum of Appeal dated the 14th May 2016 as under: -
 - i. **THAT** the objection decision by the Respondent dated 4th day of April 2016 is unlawful and/or tainted with illegality since it blatantly contravenes the express and unequivocal provision stipulated under section 51(11) of the Tax Procedures Act, 2015 wherein it states that where the Commissioner has not made an

objection within sixty days from the date the objection is lodged, the objection shall be allowed.

ii. **THAT** the objection by the Respondent dated 4th April 2016 is unlawful and/or tainted with illegality as it lacks a statement of findings on the material facts and the reasons for the decision which constitute the minimum compulsory requirement for an objection decision as clearly stipulated under section 51(10) of the Tax Procedure Act, 2015

iii. **THAT** the Respondent, without due regard to supporting documents duly submitted by the Appellant during the audit, erred in subjectively adjusting the rental income expenses to 40% of the gross rental income and that the 40% threshold is not anchored in any Tax Laws. As Sec 3(2) (a) of the Income Tax Act states "Subject to this Act income is income in respect of-

(a) gains from:-

- a) A business for whatever period of time carried on;
- b) Employment or services rendered;
- c) A right granted to another person for use or occupation of property

8. The Appellant in the Memorandum of Appeal prays for the Orders being: -

i. **THAT** this Appeal be allowed and the Assessment and/or objection decision by the Respondent be vacated.

THE RESPONSE BY THE RESPONDENT: -

9. The Respondent subsequent to being served with the Memorandum of Appeal proceeded to file the Respondent's Statement of Facts dated the 10th June 2016 before the Tribunal on the 13th June 2016.
10. The Respondent's Statement of Facts dated the 10th July 2016 signed by Andambi Chabala on behalf of the Respondent sets out under sub-headlines of the Background of the case, Appellant's case, Response to grounds by the Appellant in the Memorandum of Appeal with prayers being that the Tax Appeals Tribunal to find that the 40% adjustment to the rental expenses is a reasonable percentage of expenses claimable by the Appellant and that this Appeal be dismissed and the Respondent's confirmation dated 4th April 2016 be upheld.

THE HEARING: -

11. When the matter came up for hearing on the 28th September 2016 the parties by the very nature of the dispute informing the Appeal opted not to call any witnesses but proceeded by way of oral submissions.
12. The both parties had prior to the hearing filed written submissions before the Tribunal. On 28th September 2016 the parties duly highlighted their written submissions filed before the Tribunal. The Tribunal directed that the decision was to be subsequently rendered with a prior notice to the parties.

ISSUES FOR DETERMINATION

13. The issues for determination on the basis of both the oral and Written Submissions on record before the Tribunal are;
 - i. Whether the objection decision by the Respondent dated 4th April 2016 is unlawful and/or tainted with illegality for

contravening Section 51(11) of the Tax Procedures Act, 2015 (TPA) which stipulates that where the commissioner has not made an objection decision within sixty days from the date the objection was lodged by a tax payer, the objection shall be allowed.

- ii. Whether the objection decision by the Respondent dated 4th April 2016 is unlawful and/or tainted with illegality as it lacks a statement of findings on the material facts and the reasons for the decision which constitute minimum compulsory requirements for an objection decision as stipulated under section 51(10) of the TPA.
- iii. Whether the Respondent erred in subjectively adjusting the rental income expenses to 40% of the gross rental income.

ARGUMENTS: -

APPELLANT'S CASE

14. The Appellant received the letter of intention to audit on February 2015 and thereafter in March 2015 the Respondent commenced the assessment at the Appellant's premises. On 30th June 2015 the Respondent requested the Appellant to provide supporting documents regarding maintenance and repairs expenses. On 15th August 2015, the Appellant provided copies of receipts for repairs and maintenance to the Appellant. Subsequent to that, the Respondent made provisional findings wherein rental expenses were calculated at 40% of gross rent income and in effect resulted in undeclared rental income which was subjected to tax at 30% by the Respondent. On 15th October 2015 The Respondent made additional assessments for the years of income

2011, 2012, 2013 totaling Kshs. 1,189,476.96/= as shown below and communicated the same to the Appellant on 27th November 2015.

Year	Tax Kshs	Penalty Kshs	Interest Kshs	Total Kshs
2011	217,006.20	43,401.24	217,006.20	477,413.64
2012	214,782.30	42,956.46	159,153.68	416,892.44
2013	185,764.80	37,152.96	69,253.12	292,170.88
Total	477,413.64	416,892.44	292,170.88	1,186,476.96

15. The Appellant on 1st December 2015 lodged an objection to the said assessment and on 18th December 2015 provided an explanation and further supporting documents in relation to the aforementioned objection. The Respondent made further requests for documents on 7th March 2016 and at that point the Appellant made references to Section 51(11) of the TPA wherein it states;

Where the commissioner has not made an objection decision within sixty days from the date that the taxpayer lodged a Notice of Objection, the Objection shall be allowed.

16. The Appellant contends that the Respondent went ahead and confirmed the assessment of 15th October 2015 without due regard to the provisions of Section 51(11) of the TPA and that the said objection decision lacked statement of findings as stipulated in Section 51(10) of the TPA stated below;

An Objection Decision shall include a statement of findings on the material facts and reasons for the decision.

17. It is the Appellant's submission that the relevant sections of the TPA do not make provisions for an extension of time. The Appellant avers that the only lawful decision the Respondent would have made on 4th April 2016 was to allow the Appellant's Objection dated 1st December 2015 given that the Sixty (60) days time frame as envisaged by the Act had long since lapsed. Further, the Appellant argues that failure by the Respondent to make an Objection Decision within the sixty day timeframe renders their Objection Decision unlawful, void and unenforceable as the same contravenes the express provisions of Section 51(11) of the TPA.
18. The Appellant contends that Section 84 and Section 85 of the Income Tax Act are repealed and replaced with Section 51 and Section 113 of the TPA and the Respondent cannot supposed to have relied on the same. Further that the word "Appeal" and the word "Objection" are two different words and this has been explained properly in the TPA. The word "appeal" has been defined under the TATA to mean an appeal to the Tribunal against a decision of the Commissioner under any of the tax laws and it is not possible to bring a tax decision to the Tax Appeal Tribunal and that one can only bring an appealable decision.
19. On the retrospective application of the TPA and in particular Section 51(11) of the Act, the Appellant submits that the said Act can be applied retrospectively and to buttress their argument relied on judicial precedents in the case of **Municipality of Mombasa vs Nyali Limited (1963) E.A.371** and **Overseas Private Investment Corporation**

& 2 others V Attorney General (2013) eKLR wherein it the court stated “ whether or not legislation operates retrospectively depends on the intention of the enacting body as manifested by the legislation. In seeking to ascertain the intention behind the legislation the courts are guided by certain rules of construction. One of these rules is that if the legislation affects substantive rights it will not be construed to have retrospective operation unless a clear intention to that effect is manifested; whereas if it affects procedure only, prima facie it operates retrospectively unless there is a good reason to the contrary. But in the last resort it is the intention behind the legislation which has to be ascertained and a rule of construction is only one of the factors to which regard must be had in order to ascertain that intention”

20. As to whether a statute should be applied retrospectively, the Appellant argues certain rules guide the courts with regards to the presumption against retrospection and these are

- i. type of statute,
- ii. whether the statute affects substantive rights and
- iii. the intention of the legislation,

further the Appellant submits that the TPA qualifies under all the three rules analyzed herein and could thus be construed retrospectively.

21. The Appellant submits that the wording of sections 113 of the TPA being the transitional and saving clause as read together with section 51(11) is procedural hence prima facie it should operate retrospectively and ultimately there are no substantive rights of the Respondent which will be affected in applying the Act and relied on the case of **Mistry Jadva Parbat & Company Limited v Ameer Kassim Lakha & 2 others**

(2008) eKLR and *Yew Bon Tew vs Kenderaan Bas Mara* (1982)2 all ER where it was held; *“We hold, therefore, that the proviso to Rule 80 came into operation on 30th August 2002 when it was published in the Gazette and being a procedural rule operates retrospectively to all appeals which had been filed before the rule became operational. The present application is, thus caught by the time bar in the proviso. We strike it with costs to the respondents as being time-barred”* and *Orengo v Moi & 12 others (No.3) 2008* wherein the court stated *“..... the court’s duty is to interpret the law as it is gleaning the intention of parliament from the words used in the statutes being construed. That the plain words of a statute being precise and unambiguous should be given their ordinary and natural meaning. It is also an established Principle of construction of statutes and documents that Judicial Officers do not pronounce their own views as representing the intention of parliament nor do they put their own words in the statutes before them in the name of construing the intention of the law given. It is also known that the courts do not and should not construe the law to bring out what parliament ought to have legislated. The courts should and we are no exception, construe the intention of parliament as clearly expressed in the statute in question. Where a statute is ambiguous for any reason tending to some-not-so-clear a meaning, of course the court will look to the purpose of that statute as a whole and employ such other acceptable aids as are available to give meaning and effect to that law. This is because it is presumed that parliament passes law for the public good and benefit-not mischief”*.

22. The Appellant states that section 51(10) of the TPA has stipulated and relied on the word “shall” and as such the requirement that a decision by the commissioner should contain a statement of fact and reasons for the decision is not optional or discretionary and that the Respondent as a creature of statute is bound to abide by a mandatory statutory requirement and in their support mention the case of **Nizaba International Trading Company Limited v Kenya Revenue Authority (2000)KLR at pg. 594** where it was held *“It is therefore obvious that the Commissioner of Income of Tax is a creature of the statutes and can only do what the Act allows him to do. If he gets outside the powers granted to him by the Act or fails to perform his duties, he is amenable to be supervised by the High Court.”* The Appellant further states that the requirement to provide reasons for decision is paramount the same has been reiterated expressly under **Rule 12(b) of the Tax Appeals Tribunal Rules.**
23. It is the Appellant’s argument that the provision of documents, Audit queries and Audit findings cannot amount to statement of findings and reasons for an Objection Decision as alleged by the Respondent. Further, the Appellant asserts that these are system generated forms and in-depth finding summary that do not in any way explain in clear words how the Respondent reached his decision and that the Respondent considered all the issues raised in the assessment as envisaged in section 51(8) of the TPA which is a mandatory statutory requirement.
24. As to whether the Respondent erred by subjectively adjusting the rental expenses to 40% of the gross rental income, the Appellant

avers that the 40% threshold as applied by the Respondent is not anchored on any Tax Laws and the same was arrived at subjectively and without due regard to the supporting documents duly submitted by themselves during the audit. The Appellant argues that the Respondent termed the expenses as excessive, extravagant and do not make economic sense while all the data was available for the commissioner to make an informed decision.

RESPONDENT'S CASE

25. The Respondent contends that the Objection Decision by the Commissioner was as a result of assessments made against the Appellant on 18th November 2015 and an objection by the Appellant on 1st December, 2015 made under Section 84 of the Income Tax Act and that upon receipt of the objection, the Commissioner is governed by the provisions of Section 85 of the ITA on the next course of action. Further the Respondent avers that the Commissioner exercised his mandate pursuant to Section 85(3) of the ITA by not amending the assessment and instead issued a notice of Assessment. It is the Respondent's submission that the Appellant appealed against the assessment by objecting to the commissioner on 1st December 2015 by dint of Section 113(1) of the Tax Procedures Act 2015 and the Respondent confirmed the assessment using the same section of the Act.
26. Based on the foregoing therefore the Respondent contends that the notice of confirmation was not unlawful as Section 51(11) of the TPA came into force on 19th January 2016 and that the process leading to the confirmation of taxes was ongoing, in respect to alteration of the

law during the pendency of legal proceedings, the Respondent relied on the case of **Said Hemed Said vs. Emmanuel Karisa Maitha & Another Mombasa HCEP No.1 of 1998** in support of his submissions where it held *“The general rule is that when the law is altered during the pendency of an action or proceeding, the rights of the parties are to be decided according to the law as it existed when the action or proceeding was begun unless the new statute shows a clear intention to vary or affect such rights as such intention may be even by implication. But in the case of an enactment, which alters or affects only procedure or practice of the Court, the general principle is that it has a retrospective effect unless it has some very good reason against it”*.

27. Additionally, the Respondent contends that ITA does not provide a timeframe for the commissioner to make a decision on objections and that the TPA cannot be applied retrospectively, the Respondent further relied on the case of **Keroche Industries Ltd vs. Kenya Revenue Authority & 5 others (2007) eKLR** where the court stated that; *“Retrospective laws are no doubt prima facie of questionable policy, and contrary to the general principle that legislation by which the conduct of mankind is to be regulated ought, when introduced for the first time, to deal with future acts and ought not to change the character of past transactions carried on upon the faith of the then existing law”* and that in any case the objection decision was made in accordance with the transitional and saving part of section 113(1) of the TPA which specifically excluded this as the transitional and saving part of assessment relating to the Appellant provides that; *“Subject to*

this section, this Act shall apply to any act or omission that occurred or is occurring for which no prosecution has been commenced, assessment made against which no appeal has been made, before the commencement date”.

28. The Respondent argument is premised on the fact that the TPA which imposes time limit cannot be termed as procedural amendment as proposed by the Appellant since the said Act has the potential to adversely affect the substantive rights and liberties of the Individual. Further, the TPA has the effect of repealing certain sections of the ITA relied on Section 23(3) *Interpretations and General Provisions Act, Cap 2 Laws of Kenya* to buttress the argument that....

(a) “ where a written law repeals in whole or in part another written law, unless a contrary intention appears the repeal shall not affect the previous operation of a written law so repealed or

(e) anything duly done or suffered under a written law so repealed or affect an investigation, legal proceeding such investigation, legal proceeding or remedy may be instituted, continued or enforced, and any such penalty, forfeiture or punishment may be imposed, as if the repealing written law had not been made”.

According to the Respondent the date of issuance of Notice of Confirmation could therefore not affect the previous operations of a written law so repealed.

29. As to whether the Objection Decision dated 4th April 2016 by the Respondent is unlawful and/or tainted with illegality and as it lacks a statement of facts and reasons for the decisions, the Respondent reiterates that the confirmation decision was made under the ITA and

the same did not require a decision to contain a statement of facts and reasons for the decisions as alleged by the Appellant. Further, the tax decision is a culmination of efforts to resolve the objection and it was based on information already in possession of the Appellant such as audit queries, audit findings and additional assessment as well as the in-depth case schedules of additional income and tax forms which explained the Director's rental income and that all these documents were used in arriving at the tax decision.

30. The Respondent contends that it did not err in adjusting the Appellant's claimable expenses against rental income to 40% as it considers the same to be excessive, exaggerated and lacking economic sense. In the Respondent's view expenses formed 78% of gross rental income in 2011 and in the subsequent year's i.e 2012 and 2013 the percentage of expenses charged against rental income were 76.38% and 71.47% respectively. The Respondent asserts that the aforementioned expenses were claimed in contravention of Section 15(2)(f) of the Income Tax Act and in the circumstances the commissioner is therefore empowered by Section 77 of the Income Tax Act to assess and thus reduce to the said expenses to 40%.

TRIBUNAL ANALYSIS AND FINDINGS

31. For purposes of this Appeal the Tribunal is required to make a determination as to whether Section 51(11) of the TPA provides the applicable procedures and timeframe for lodging an objection to a tax decision wherein it is stated:

Where the Commissioner has not made an Objection Decision within sixty days from the date that the taxpayer lodged a Notice of the Objection, the Objection shall be allowed.

32. The Appellant lodged an objection to the assessment made by the Commissioner on 1st December 2015. The Tax Procedures Act came in force on 19th January 2016 and Section 51(11) of the said Act expressly states in the event that the Respondent does not object to objection lodged by the Appellant, then the Appeal shall be allowed. The Respondent confirmed the additional assessment on 4th April 2016 and 125 days after the Appellant lodged an objection and beyond the 60 days as expressly stated by the Act. The Tribunal notes that the Respondent has not advance any legitimate or convincing arguments as it pertains to exceeding the stated timeframe. In any case, the Act was assented to on 15th December 2015 and the Respondent being the body charged with revenue, collection was aware of the new law.
33. The Tribunal takes the view that Section 113(1) of the TPA as stated hereunder;

“Subject to this section, this Act shall apply to any act or omission that occurred or is occurring for which no prosecution has been commenced, or any assessment made against which no appeal has been made, before the commencement date.”

The above section is a transitional and saving clause and envisaged situations whereby tax assessment by Commissioner will be midstream and no appeal had been on the same. The TPA defines appealable decision as: -

“Appealable decision” means an objection decision and any other decision made under a tax law other than –

(a) a tax decision; or

(b) a decision made in the course of making a tax decision;

34. The Tax Appeals Tribunal Act 2013 defines an Appeal as thus: -

“means an Appeal to the Tribunal against a decision of the Commissioner under any of the tax laws;

35. The Tribunal therefore finds that Section 51(11) of the Tax Procedures Act is applicable and can be applied retrospectively. In the Case of Keroche Industries Limited v Kenya Revenue Authority and five others Judge Nyamu (as he then was) states that: -

“..... Retrospective laws, except where specifically allowed by the legislature, are generally frowned upon as a matter of policy.....”

The Tribunal agrees with the Appellant that the TPA relates to matters of procedure and rules and can thus be applied retrospectively as Section 113(1) of that Act expressly allow for the same wherein it is stated:-

“.....this Act shall apply to any act or omission that occurred.....before the commencement date”

Indeed, the Tribunal is alive to the purport of the Act wherein the preamble to the same reads: -

AN Act of Parliament to harmonize and consolidate the procedural rules for the administration of tax laws in Kenya and for connected.

36. The Tribunal has interrogated the procedures under the ITA which have now been repealed and notes that the Appellant could not proceed to

Appeal without having received the Confirmation of Assessment and in the circumstances the argument by the Respondent that the transitional and saving clauses removed the assessment from the full effect of the provisions of the TPA cannot be sustained. It is not in dispute that the Confirmation Notice of Assessment was issued on 4th April 2016 long after the TPA.

37. The Tribunal finds that the Respondent has misapprehended and misinterpreted the applicability of the transitional and saving clause as provided in Section 113(1) of the TPA as there was no appealable decision prior to 4th April 2016 and therefore the Appellant could not commence an Appeal without the Respondent making a final determination on the Objection made in December of 2015.
38. The Tribunal finds that the law assists the vigilant and not the indolent as the TPA was assented to in December of 2015 and therefore the Respondent ought to have expedited and made a decision prior to the commencement date of 19th January 2016 and the provisions of Section 23(3) of the *Interpretations and General Provisions Act, Cap 2 Laws of Kenya* cannot assist the Respondent in this case as Section 113 (1) is mandatory and further there was no appeal lodged before any other forum or this Tribunal.
39. The Respondent therefore ought to have proceeded within the ambit and provisions of law as stipulated in the TPA when issuing their decision and the attempt to rely on the repealed procedure is unfair as there are numerous correspondences availed by the Appellant requesting for a response from the Respondent which have not been refuted by the Respondent.

40. As to whether the objection decision by the Respondent is unlawful as it does not include a statement of facts and reasons for the decisions, the Tribunal is guided by the words of the statute particularly Section 51(10) of the TPA as stated below

“An Objection Decision shall include a statement of findings on the material facts and the reason for the decisions”

The Objection decision issued by the Respondent on 4th April 2016 did not include a statement of facts and reason for the decisions. The Respondent averments that the audit queries, audit findings and various correspondences as a substitute for a statement of facts or reasons for the decision is not convincing and as such the Tribunal does not attach any weight to the reasons so advanced. Indeed, the actions of the Respondent contravene the object and the purpose of the TPA as stipulated under section 2 is to provide uniform procedures for: -

- (a) consistency and efficiency in the administration of tax laws;***
- (b) facilitation of tax compliance by taxpayers; and***
- (c) effective and efficient collection of tax.***

41. From the undisputed facts above, it is clear to the Tribunal that the Respondent had ample time to familiarize themselves with the import of the Act and particularly Section 113. The TPA No.29 of 2015 was assented into law by the President on 15th December 2015 subsequently, through a Gazette notice dated 14th January 2016, the Cabinet Secretary for the National Treasury appointed the 19th of January 2016 as the date the Act came into force.

42. As regards adjusting rental expenses to 40% of gross rental income, the Respondent was provided with the material documents as requested in the letter dated 30th June 2015. The Tribunal finds that by providing copies of repairs and maintenance receipts, the Appellant has discharged its burden by presenting for verification the source documents. The Respondent proceeded to adjust the expenses terming the same to be excessive, exaggerated and not making economic sense without providing any further explanation.
43. The Tribunal is aware that the Respondent under section 77 of the ITA, the Commissioner is clothed with the powers to make additional assessment according to its best judgment, in this case, the Respondent flagrantly disregarded the documents presented and capped expenses to 40% of gross rental income. The Tribunal views this to be arbitrary as the Respondent has not tendered before it any evidence nor provided cogent and persuasive argument as to the reasons for adjusting the rental expenses. The Tribunal finds that it is well established in statute that expenses may only be deducted in calculating profits of a business where the expense have been incurred wholly and exclusively for the purposes of that business and agrees with the Appellant that Section 15(1) of ITA entitles a tax payer to deduct all expenses incurred wholly and exclusively in the production of income as stated below: -

“For the purpose of ascertaining the total income of a person for a year of income there shall, subject to section 16, be deducted all expenditure incurred in that year of income which

is expenditure wholly and exclusively incurred by him in the production of that income.”

TRIBUNAL DECISION

44. In light of the Tribunal's findings hereinabove the Appellant's Appeal dated 14th May 2016 has merit and is hereby allowed and consequently the following orders are issued;
45. The Respondent's demand against the Appellant for Income Tax on rental income for the period 2011, 2012 and 2013 and Notice of Confirmation of Assessment dated 4th April 2016 be and is hereby set aside.
46. The Tribunal awards costs of Kshs. 20,000/= to the Appellant.

DATED and DELIVERED at NAIROBI this ^{30th} day of January 2018

In the presence of: -

Irungu Macharia - Tax Agent
..... for the Appellant

deparan demiso w/o Victor Chabaler
..... for the Respondent

Liliani
.....
LILIAN RENEE OMONDI
CHAIRPERSON

Gabriel Kitenga
.....
GABRIEL KITENGA
MEMBER

Daniel Tanui
.....
DANIEL TANUI
MEMBER

Boniface Dimmo
.....
BONIFACE DIMMO
MEMBER

Abdulbasid Ahmed
.....
ABDULBASID AHMED
MEMBER