REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
TAX APPEAL NO. 25 OF 2017

KISIMA FARM LIMITED .....APPELLANT

=VERSUS=

COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGMENT

BACKGROUND:-

1. The Appellant is a limited liability company incorporated under the Companies Act No. 17 of 2015 having its registered office in Timau within the Republic of Kenya. The Appellant's principal business involves farming wheat, barley, peas and rape seed and eryngium.

2. The Respondent is a principal officer appointed under the Kenya Revenue Authority Act, Cap 469 of the Laws of Kenya, charged with the mandate to administer and collect tax revenue on behalf of the Government of Kenya.

3. Upon conducting an in-depth audit on the Appellant's books for the period January 2012 to December 2015, the Respondent assessed taxes on VAT, P.A.Y.E, Withholding tax and Corporation Tax of Kshs. 63,048,125/=, which was communicated to the Appellant through a letter dated 28th September 2016.

4. The Appellant paid Kshs. 10,033, 370/= to settle the principal taxes and interests on P.A.Y.E, Withholding Tax and VAT and requested for a waiver of penalties.

5. The Respondent raised Additional Tax Assessment on 21st October 2016 for Corporation Tax in the sum of Kshs. 25,835,886/=, which is the genesis of this Appeal.

6. The Appellant being dissatisfied with the above Assessment raised an Objection dated 17th November 2016 whereby the Respondent confirmed the assessment through its letter dated 13th January 2017.

7. Aggrieved by the above-mentioned confirmation the Appellant lodged this Appeal vide a Memorandum of Appeal dated 14th February 2017.

THE APPEAL

8. The Memorandum of Appeal which sets out Eighteen (18) grounds of Appeal which in the Tribunal's view, is long –winded and repetitive. Notwithstanding, it is important to replicate the said grounds for reasons that will become apparent later in this Judgment. The grounds are as hereunder:-

    a. *That the Respondent erred in law and in fact in failing to appreciate and/or apply the irrefutable and scientifically verifiable truism to the effect that all living organisms contain a significant quantity of moisture and that upon being dried (and consequently, upon losing moisture, there is always a significant reduction in both volume and mass.*

    b. *That the Respondent erred in law and in fact by failing to appreciate and apply the rational accounting and economic principle that every output must have a corresponding input; and failing to appreciate that it is impossible to have a harvest in one year of income that does*

not derive from seeds from the previous year of income. Accordingly, it is preposterous and extremely injudicious to assess for purposes of taxation the ENTIRE harvests for FOUR (4) succeeding years of income without making any allowance for the seeds drawn from the farm (assuming that the seeds are purchased from elsewhere) the market value of the seed.

c. *That the Respondent erred in law and in fact in failing to appreciate and /or consider that seeds that had been planted (and which had in fact yielded the harvest which resulted in the income that was being assessed for taxation) could not at the same time have been sold to yield additional income that was equally chargeable to tax; hence the absurdity of penalizing the Appellant for alleged failure to declare the value thereof.*

d. *That the Respondent erred in law and in fact in failing to appreciate the inveterate principle that tax can only be imposed by law and that under Section 3(2) of the Income Tax Act, Cap 470 of the Laws of Kenya) Corporation Tax is only charged on **"gains"** and/or **"profits"** of a business and not otherwise.*

e. *That the Respondent erred in law and in fact by failing to appreciate that no **"gains"** and/or **"profits"** whatsoever and howsoever is realized when agricultural produce that has been harvested is cleaned and dried therefore (through the concomitant loss of moisture and other impurities) decrease in quantity and /or mass.*

f. *That the Respondent erred in law and in fact by failing to appreciate that no **"gains"** and/or **"profits"** is realized when seeds that have been harvested are planted back into the ground.*

g. *That the Respondent erred in law and fact by failing to appreciate the difference (for tax and accounting purposes) between **" work in***

progress" *and "**stock"** and /or "**raw materials"** and **"the finished product".***

h. *That the Respondent erred in law and in fact in failing to appreciate that freshly harvested and undried grains from the far, which had not been cleaned (with the result that the same was not highly perishable but was also mixed with soil and other impurities) and which could not be bought by or sold to anybody would not be given the same value (even if the same could be assessed for tax purposes which is denied) as completely dried cleaned and packaged grains.*

i. *That the Respondent erred in law and in fact in failing to appreciate that freshly harvested and undried and uncleaned grains were mere work in progress (process) and was not a finished product capable of being sold. Accordingly, neither "gains" nor "profit" could result therefrom as to justify their being declared for tax purposes.*

j. *That the Respondent erred in law and in fact in failing to appreciate that in purporting to assess the variance between freshly harvested , undried and uncleaned produce and the dried cleaned produce to tax, the Respondent is effectively subjecting the Appellant to double taxation.*

k. *That the Respondent erred in law and in fact by falsely and maliciously including within the meaning of the word **"stock"** something that was still "raw" and which had not reached the stage of being considered, treated and/or dealt with as "stock-in-trade" or as product that could be sold and from the wholesale and income could be earned.*

l. *That the Respondent erred in law and in fact in failing to correctly conceptualize the word "undeclared tax "as used in tax generally.*

m. *That the Respondent erred in law by failing to notice that the assessment that he purported to confirm did not strictly comply with the formal procedure and requirements and was accordingly a nullity in law.*

n. *That the Respondent erred in law by failing to appreciate that under Section 51 of the Tax Procedures Act. The Appellant's objections to the assessments purportedly done vide the letter dated 28th September 2016 had already become allowed by operation of law.*

o. *That the Respondent erred in law and in fact in failing to appreciate that even if freshly harvested, undried and uncleaned produce were to be assessable for purposes of income tax(which is denied) then the value thereof had to be determined by **direct cost method** (which simply entails the costing materials and labour that had given rise to the same) rather than by **market price method** (which entails the use of prices at which the same could be purchased in the market) because there is no market for such produce.*

p. *That the Respondent erred in fact and in law in failing to allow a tax deduction with respect to the market value of the seeds that had been planted and which yielded income that was being assessed for taxation purposes.*

9. It is the Appellant's prayer that the Respondent's decision be annulled and the assessment be amended to Nil.

10. To bolster its case, the Appellant has filed the Statement of Facts dated 14th February 2017 accompanied by the bundle of documents of even date.

11. In response to the Appeal, the Respondent has filed an untitled document dated 13th March 2017 where it outlines the background and facts of the case and wherein upon outlining its contention, seeks that the Appellant be directed to pay the additional tax of Kshs. 25,835,885/=

12. The Respondents response is as follows:

a) *That the objection decision was made after reviewing of material facts presented by the appellant and considering the relevant legal provisions of relevant Acts. That this is evidenced by the fact that part of the appellant's objection was allowed.*

b) *That the appellant has not provided any records to support claim of seeds issued to planting and the adjustments were made after all relevant considerations as outlined in our workings*

c) *That the tax payer is in agreement of the issue of moisture content up to 6% as per our workings and they have even provided a lower moisture content of up to 3% in the response working.*

d) *That the workings were in line with acceptable accounting principle of determining expected sales and in so doing, all adjustments relevant to the reconciliations were taken into account among them being stock of processed seeds (opening & closing), transfers to planting, internal sales, feeds, rubbish, and requisite moisture levels.*

e) *That the workings and taxable amounts arrived at were not from harvest grains or un processed grains, but on the processed seeds based on the records maintained by the appellant. The produce of two seasons added to the opening stock of previous season, less the adjustments as above (opening & closing stock of processed seeds, transfers to planting, internal sales, feeds, rubbish, and requisite moisture levels) to arrive at expected seeds for sale, then compared with what was sold did not tally with what has been declared in the books.*

f) *That the workings and taxable amounts arrived at were not based on Direct cost method from harvest grains or un processed grains, but on the processed seeds after all requisite processes ready for market, as per records kept by the taxpayer (a fact they have admitted in their mails and notes of*

interview, and memorandum of facts about records used for tax returns) after being stored for either sale, stock, etc. Workings then sought to establish the quantity of seeds that were expected to be sold from what was in store at the end of each accounting period for year 2012, 2013, 2014.

g) *That the appellant used the same formulae as we did and introduced different figures for moisture, planting seeds that were not in the ledgers provided during and subsequent to the audit. That for all the accounting periods year 2012, 2013, 2014; the workings of the responded yielded to virtually nil variance a fact that they worked backwards, but all in all are in agreement to the principle we applied.*

h) *That the appellant admits that their records were not complete of all the documentation (email correspondences) especially on the seeds issued to planting and were of the opinion that we used the assumptions that logically what was harvested was planted from previous season seeds – these seeds are the subject of taxation. The question is, were these accounted for? Where are the records? It is not logical to assume it was from own stores. They would have also purchased for planting and whatever our variance we are questioning from the store would have been sold out of the books or planted and yielded more harvest that is not accounted for and it is the onus of the taxpayer to prove otherwise.*

APPELLANT'S CASE

13. At the plenary hearing, on 17th August 2017, both parties orally presented their cases and agreed to file written submissions. Therefore, in addition to the pleadings enumerated above, the Appellant filed its submissions dated 4th September 2017 on 21st September 2017.

14. The Appellant submitted extensively that the tax liability, which is greatly prejudicial, originates from the Respondent's misunderstanding of its ordinary farming activities. It is the Appellant's case that the harvesting

process results in a mixture of harvested produce (which contains a lot of moisture) with soil, chaff, husks pod, and shells etc. which must be removed before the produce is ready for use and / or sale. Thereafter, the harvested produce goes through a process of drying and cleaning to separate the good produce from impurities and achieve the required quality standard of a clean and useable produce. Practically, a bag of wheat that was originally 100 Kgs realizes about 60-70Kgs of clean weight.

15. It is the Appellant's position that the approximate annual weight variance between freshly harvested produce (unprocessed produce) and cleaned and dried produce (processed produce) is 60 Tonnes. That the aforesaid variance can be attributed to weight of moisture, residues, husks, soil, living insects , broken grains, shriveled grains, unsound grains, grains that have been attacked by pests, other cereals, extraneous matter, inorganic ,matter, ergot and other impurities that must be removed before sale of the produce.

16. Flowing from the above outline, the Appellant contends that unprocessed produce (where a record of the same is maintained) is not stock within the meaning of Section 17 of the Income Tax Act, Cap 470.

17. That once the unprocessed produce is cleaned and dried (processed produce) and it meets the required quality standard, the same is sold and the Appellant submits income tax returns therefrom.

18. The Appellant explains that the point of divergence which then informs the Respondent's assessment was due to the variance observed between the unprocessed produce and the processed produce during the Respondent's audit process. It is the Appellant's belief that the Respondent construed the variance as undeclared sales and raised additional assessment raised for Corporation Tax of Kshs. 25, 835,886/= pegged on a flawed assumption.

19. While submitting on the above, the Appellant contends that the assessments lodged against it are illegal as they are not contemplated by law. To support this, it relies on Section 17 of the Income Tax Act which provides for ascertainment of income from farming and states:-

"The stock owned by a farmer at the beginning and end of each period for which he makes up the accounts of his farming business shall, in computing the ***gains or profits from such business, be taken into account at such value as the Commissioner may determine to be just and reasonable****."*

20. Further, Section 17(5) of the Act provides that every farmer who has elected not to take account of the value of the stock shall furnish, upon the Commissioner's requisition, a statement setting out to the best of his knowledge and belief, the value of stock held by him at any relevant date. That in line with the above the Appellant explained that :-

a) Raw harvest is distinct from processed stock as there is necessity to clean before the same is ready for sale
b) An average moisture of 6% is experienced and the same is higher during the rainy season.
c) Some harvests are used as seeds to plant crops for the next year of harvest.
d) The average price to calculate the value of stock balances was erroneous as it failed to give room for price fluctuations in the years concerned.

21. That the seeds from one season that are planted to generate a harvest for the next income are in their nature, capital expenditure wholly and exclusively incurred for production of income. That by failing to allow a tax deduction with respect to market value of the seeds planted, the Respondent was in contravention of Section 15 of the Income Tax Act.

22. The Appellant maintains that despite providing detailed explanations on the variances, the Respondent confirmed the Assessment to its detriment.

23. In its submissions, the Appellant reiterated that no Objection Decision was rendered by the Respondent pursuant to Section 51 of the Tax Procedures Act, 2015. In its view, the letter dated 13th January 2017and received on 16th January 2017 was not a decision as deciphered from its title which read "additional assessment notice", it lacked citation of the legal provision it was brought under, it failed to include statement of findings and reasons for the said decision and that it did not make reference to the Appellant's objection.

24. In addition to the above, the Appellant submits that the Respondent failed to follow procedure laid out under Section 51(8) and (9) of the Tax Procedures Act. That going by the above provisions, the Respondent cannot, as in this case, issue a notice of amended assessment and notice confirming the assessed tax in one notice as that would amount to an affront of the Appellant's right to fair administrative action.

25. To reinforce the above, the Appellant relied on the sentiments of Honourable Justice Majanja in the case of **Geothermal Development Company Limited versus Attorney General & 3 Others** where he stated:

> " *A notice of the nature issued to enforce collection of taxes must clearly state to be such a notice ,state the amount claimed, state the legal provision under which it was made and draw the taxpayers attention to the consequences of failure to comply with the law and the opportunity provided by the law to contest the finding. Such a notice would give the opportunity to any Kenyan to know the case against it and utilize the legal provisions to contest the decision. The right to fair administrative action and the right of access of justice now enshrined in our Constitution demand nothing less*"

26. That the Confirmation notice purported to be the Respondent's decision is irregular, un-enforceable and un-procedural as the figures being confirmed (Kshs.25,835,885/=) therein are different from those contained in the assessment notice of 28th September 2016 (Kshs. 35,853,579/=).

27. In conclusion, the Appellant while reiterating its prayer that the Assessment should be amended to nil, submits that it should not suffer prejudice owing to the Respondent's misinterpretation of the law which has gone against principles of taxation in raising the impugned Assessments.

RESPONDENT'S CASE

28. In answer to the Appeal, the Respondent has filed its Statement of Facts as highlighted above and written submissions dated 23rd October 2017 and filed on 31st October 2017.

29. In its Statement, the Respondent has confirmed that an audit was conducted and the same revealed that the Appellant's production records had variances on the processed seeds after adjustment for all relevant issues to planting seed, stock, moisture, chaff, internal sales, feeds, rubbish etc for the period January 2012 to December 2015.

30. That a notice of additional tax was issued on 28th September 2016 and the Appellant was informed that additional Assessments would be sent under separate cover. Subsequently, Additional Assessments were raised on 21st October 2016 and acknowledged by the Appellant's tax agents on 26th October 2016, who computed the taxes not in dispute and requested for a waiver of penalties on 31st October 2016.

31. That on 17th November 2016, the Appellant lodged its Objection and the Respondent issued an acknowledgment of the Objection on 29th November 2016 and invited the Appellant to provide further documents in support of its objection.

32. In response to the Appellant's assertion that there was no objection decision, the Respondent maintained it rejected the Appellant's Objection on grounds that all the adjustments were made before arriving at the variances for the taxable period and issued its decision vide the letter dated 13th January 2017.

33. The Respondent has further pointed out that the above-mentioned letter dropped the PAYE assessment and confirmed Corporation tax. That to allege that the said letter is a decision on PAYE and not Corporation Tax is a bias against the maxim of *he who comes to equity must come with clean hands* and the said bias is employed to mislead the Tribunal.

34. While relying on the principle of estoppel, the Respondent submits that the Appellant should be estopped from pleading that moisture content loss was not taken into consideration as the adjustment of 6% of the said loss was provided by the Appellant in several meetings. Further, that the Appellant upon failing to maintain proper records should not expect the Respondent to employ the assumptions. Therefore upon the Appellant's failure to declare the value of seeds, the Commissioner exercised his powers to estimate the taxes payable. That in the case of **Republic versus Commissioner for Income Tax & Another *ex parte* Qplast Industries Limited [2015] eKLR** wherein the Honourable Judge cited the decision in **Contact Network Limited Versus Commissioner General , KRA & Another** where the Judge held :-

> *"It is clear from a reading of the said provisions that the Respondents are indeed clothed with powers to estimate taxes payable in certain circumstances. The Respondents have sufficiently shown that those circumstances existed in the Applicant's. .."*

35. As to the legality of the Objection Decision, the Respondent states that the contention is a non-starter. Particularly, on the alleged violation of Article 47 of the Constitution on due procedure being followed by administrative bodies, the Respondent states that the Appellant was given sufficient time to respond to the Assessment and that the Objection Decision was well explained. Further, that the Respondent allowed the Objection in part, which notably the Appellant has not appealed against.

36. The Respondent states that a reading of Section 51 (9) of the TPA that confirms in making the Objection Decision, the Commissioner may amend the assessment. In the same breath, the Respondent further confirmed that no amendment was made in regard to Corporation Tax was similar in both assessments.

37. In a very brief response to the tax liability raised, the Respondent states that the Appellant failed to provide sufficient documents that supported the figures raised in the revised computation. Following the above, the Respondent maintains the Assessment had been correctly raised and prayed that the Tribunal upholds the same.

ANALYSIS AND FINDINGS

38. The Tribunal has considered the record, the rival submissions, the cited authorities, the law and the Jurisdiction of the Tribunal particularly as set out under Section 29 of the Tax Appeals Tribunal Act. Pursuant thereto, the Tribunal notes that this Appeal presents itself in two limbs; the legality and the merit of the Objection Decision. The former needs to be dealt with first.

39. On the first limb, as to whether the objection decision dated 13th January 2017 is legally valid, a consideration of the clear set out provisions under Section 51 of the Tax Procedures Act will inform whether there is a single *bonafide* ground raised in order to warrant ventilation by this Tribunal.

Section 51 of the Act provides:-

(8)Where a notice of objection has been validly lodged within time, the Commissioner shall consider the objection and ***decide either to allow the objection in whole or in part, or disallow it, and Commissioner's decision shall be referred to as an "objection decision".***

(9) The Commissioner ***shall notify in writing the taxpayer of the objection decision and shall take all necessary steps to give effect to the decision, including, in the case of an objection to an assessment, making an amended assessment.***

(10) *An objection decision shall include a statement of findings on the material facts and the reasons for the decision*

40. Read as a whole, the wording of the above provision is quite clear on the responsibilities placed on the Commissioner upon receiving an Objection. Notably, the Legislature's use of the word **"shall"** dictates that the requirements are mandatory. They include vacating the Assessment as a whole, amending the Assessment and Confirming the Assessment. The Court of Appeal in the case of **Kenya Revenue Authority v Republic (exparte Fintel Ltd) [2019] eKLR** cited the learned Judges of the Supreme Court of India in **Reserve Bank of India V. Peerless General Finance and Investment Co. Ltd., 1987 SCR (2) 1.** who stated

> ***"No part of a statute and no word of a statute can be construed in isolation. Statutes have to be construed so that every word has a place and everything is in its place."***

41. In vacating, amending or confirming the objected Assessments, the Commissioner has to set out the statement of findings and the reasons therefor. A perusal of the letter dated 13th January 2017 marked as annexure E43 and produced under page 54 of the Appellant's bundle of documents demonstrates the following :-

a) The letter is titled "*Additional Assessment Notice*"
b) **Confirms** the Assessment on the Corporation Tax which was initially communicated in the letter of 28th September 2016. *An additional Assessment marked as Form 11. H.0* at Kshs. 25,835,886/=
c) **Vacates** tax on P.A.Y.E.
d) Advises the Appellant to make payment or appeal to the Tax Appeal Tribunal as provided under Section 52 of the Tax Procedures Act.

42. From the above context particularly ***"upon going through the explanations offered there is no tax liability on P.AY.E,"*** it is apparent that the Commissioner considered the Appellant's objection as anticipated under Section 51(8) (cited above) and subsequently allowed the same in part by assessing P.A.Y.E to Nil. Further, he disallowed the corporation tax. In regards to Section 51(9) (cited above) the Commissioner indeed notified the Appellant of the above decision through its letter of 13th January 2017. Therefore, the Tribunal rejects the assertion that the above was an Assessment and not an Objection Decision in light of the law outlined above.

43. As to whether there was an amendment of Corporation Tax, the Tribunal has perused the Respondent's letter dated 28th September 2016 where under Clause 6.0 it has computed the principal corporation tax at Kshs. 24,005,761/=, which upon accruing penalties and interests is Kshs. 35,853,579/=. Further, Additional Assessment dated 21st October 2016 where tax payable for the years 2012, 2013 and 2014 is Kshs.11, 204,377/=, Kshs.10,517,740/= and Kshs.14,131,462/=. As stated above, the letter of 13th January 2017 has assessed the Corporation tax at Kshs. 25, 835, 885/=. During the hearing, the Respondent maintained that no amendment had been made to the Corporation Tax. At this juncture the Tribunal shall hold that the corporation tax is Kshs. 24,005,761/= (exclusive of penalties and interests), as earlier assessed

44. The Tribunal is distinctly aware that the Respondent being an administrative body, which is a creature of Statute, is bound by the Constitutional decree set out in Article 47 of the Constitution. It is not a mere legal requirement but a constitutional one that all administrative bodies engage in fair administrative practices. Particularly Article 47 (2) provides:

"if a right or fundamental freedom of a person has been or is likely to be adversely affected by administration action, ***the person has a right to be given written reasons for the action****"*

45. In rendering tax decisions, the Tax Procedures Act, Section 51(8) (cited above) breathes life to Article 47(2) by requiring the decision to state the Statement of Findings on the material facts and the reasons for the Decision. This gives certainty to the taxpayer on how and why the decision was arrived at. A scrutiny of the letter dated 13th January 2017 shows that Respondent stated that it was not convinced on the revised computations as there was insufficient documents. To the mind of the Tribunal, having regard to the fact that the parties had held several discussions, it would have enlightened the Appellant if the Respondent pointed out what documents were not provided.

46. Notwithstanding, as stated during the hearing, the above issue being primarily on a point of law should have been raised by way of a Preliminary Objection. Having regard to the time expended by all parties and in order to put this matter to rest, the Tribunal is alive to the intention of Article 159 (2) (d) i.e. to administer justice without undue regard to procedural technicalities. Further, the High Court's sentiments in the case of **James Mangeli Musoo vs Ezeetec Limited [2014] eKLR** where it was held:-

" The other issue to fathom herein is the meaning of technicalities and what indeed is undue regard to technicalities? Nobody seems to have

defined or even attempted to define the term technicality, not even dictionaries of law.

A technicality, to me is a provision of law or procedure that inhibits or limits the direction of pleadings, proceedings and even decisions on court matters. Undue regard to technicalities therefore means that the court should deal and direct itself without undue consideration of any laws, rules and procedures that are technical and or procedural in nature. It does not, from the onset or in any way, oust technicalities. It only emphasizes a situation where undue regard to these should not be had. ***This is more so where undue regard to technicalities would inhibit a just hearing, determination or conclusion of the issues in dispute."***

47. From the above, the Tribunal finds that allowing the Preliminary Objection at this juncture will inhibit the just and final determination of the Appeal on merit. The Tribunal therefore proceeds to deal with the substantive aspect of the Appeal.

48. The preliminary issue having been settled, the scope of the dispute is considerably narrowed. The singular issue before the Tribunal is how the unprocessed seeds should be treated.

49. The undisputed facts about this case are the activities of the Appellant. It is the Appellant's case that the variance between the unprocessed seeds and processed seeds is attributed to the adjustments after moisture loss and foreign materials removed therefrom. On the other hand, the Respondent has maintained that in raising the Corporation tax, the aforementioned adjustments were considered. Further that the documents availed by the Appellant were insufficient and therefore the Commissioner invoked his powers to estimate the tax liability. Key to note, there cannot be processed seeds before unprocessed seeds. The resultant question is **Can the unprocessed seeds be treated as income?**

50. The proposition by the Appellant that unprocessed seeds are not gains and do not accrue any profit is not acceptable to the Respondent. Section 3 (2) of the Income Tax Act, cap 470 provides :-

> *(2) "Subject to this Act, income upon which tax is chargeable under this Act is income in respect of :-*
>
> *a) Gains or profits from-*
>
> *i. Any business , for whatsoever period of time carried on*
>
> *ii. Any employment or services rendered*
>
> *iii. Any right granted to any other person for use or occupation of property"*

51. The Act further under Section 17 provides for the ascertainment of income of a farmer in relation to stock:

> *17(1) the stock owned by a farmer at the beginning and end of each period for which he makes up the accounts of his farming business, shall , in computing the gains or profits from such business , be taken into account at such value as the Commissioner may determine to be just and reasonable.*
>
> *5)every farmer who has elected not to take into account the value of stock shall furnish, when the Commissioner so requires, a statement setting out to the best of his knowledge and belief the value of the stock held by him at any date relevant for the purpose of this section.*
>
> *7) In this section "stock" means all livestock and produce, and* ***crops which have been harvested*** *(emphasis added).*

52. The Tribunal finds that the Appellant has provided the Respondent with documents, information and explanations. The Appellant has also offered to provide any other additional documents, information and

explanations should the same be particularized or identified by the Respondent.

53. However, the Respondent did not identify the additional required documents, information and explanations.

54. Going by the submissions made and material available, the Tribunal finds that the Appellant complied with Section 17 (5) of the ITA.

55. For the Respondent to arrive at the Additional Assessment, Section 17(1) of the ITA requires the Commissioner to take into account such value as he may determine to be just and reasonable.

56. In order for the Respondent to arrive at a just and reasonable determination of the value of stock, it needed to have taken into account the accepted industry standards.

57. The Tribunal adopts the finding of Lord Fraser in **Willingale (Inspector of Taxes) and International Commercial Bank Ltd A.C [1978] 834**;

"it is well established that "the question of what is or is not profit or gain ***must primarily be one of fact, and of fact to be ascertained by the tests applied in ordinary business****", **Sun Insurance Company Office v Clark [1912] A.C 443m 455 per Viscount Haldane**. But that general rule is subject to the exception that where ordinary commercial principles run counter to the principles of income tax they must yield to the latter when computing profits or gains for tax purposes. In B.S.C Footwear Ltd, v Ridgway [1972] A. C. 544, 552G Lord Reid said;*
"The application of the principles of commercial accounting is, however, subject to one well-established though non-statutory principle. Neither profit nor loss may be anticipated. A trader may have made such a good contract in year one that it is virtually certain to produce a large profit in year two. ***But he cannot be required to pay tax on that profit until it actually accrues****".*

58. It is trite law as articulated under Section 56 of the Tax Procedures Act, 2015 that the burden of proof relating to an excessive assessment lies with the person assessed. From the evidence tabled and practical approach it is clear as day that a keen analysis of the records of unprocessed seeds maintained in the farm for the taxable years and the records of processed seeds should give an average of the loss suffered. Annexure 1 of the Appellant's List of Bundles includes minutes dated 2nd August 2016 where the variances are discussed at length and additional document sought which include the records, ledgers, rainfall intake to support the variance. Further in the email dated 15th December 2016, the Appellant's farm manager pointed out the glaring arithmetic errors made by the Respondent which include the seed figures, stock figures and moisture figures as reflected in the Appellant's ledger. To the Tribunal, the Appellant provided documents and raised issues that the Respondent should have addressed before confirming its Assessment.

59. The Respondent, in its submissions, did not see the need to highlight which documents were missing and as a result, the exact estimation employed to arrive at the computation of the impugned Assessment remains unexplained. Indeed Section 17(5) aforesaid gives the Commissioner the power to assess the income of the Appellant where records are not maintained. The clear wording of the statute is that the power should be exercised in a ***just*** and a ***reasonable*** manner which means that the power is not absolute.

60. The Honourable Justice Mr. J . Mativo in the case of **Robert K. Ayisi v Kenya Revenue Authority & another [2018] eKLR** stated:-

"As this Court has held time and again a taxing authority is not entitled to pluck a figure from the air and impose it upon a taxpayer without some rational basis for arriving at that and not another figure. Such action would be arbitrary, capricious and in bad faith. It would be an

unreasonable exercise of power and discretion and that would justify the Court in intervening"

61. Further the Supreme Court of India in **Hero Cycles (P) Ltd vs Commissioner of Income-tax (Central) Ludhiana [2015] 63 taxmann.com 308 [SC]** the court made the following important holding:-

> *"We are of the opinion that such an approach is clearly faulty in law and cannot be countenanced.... the Revenue cannot justifiably claim to put itself in the arm-chair of the businessman or in the position of the Board of Directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. It further held that no businessman can be compelled to maximize his profit and that the income tax authorities must put themselves in the shoes of the assessee and see how a prudent businessman would act. The authorities must not look at the matter from their own view point but that of a prudent businessman. Applying the aforesaid ratio to the facts of this."*

62. With regard to the seeds planted from the harvest, Section 15(1) of the Income Tax Act, is clear that in computing the total income of any person, all expenditure wholly and exclusively incurred in the production of that income shall be an allowed deduction. Proceeding to levy tax on the seeds that yield income at the end of the year is thwarting the Appellant's legitimate expectation.

63. Yet having made the above observations, in construing fiscal or tax legislation, the Tribunal is obliged to reach an outcome which is not only rational and just but achieve consistent results when applied. At this juncture, while the Tribunal appreciates the Respondent's need to collect revenue, the same must be guided by what tax amount is properly due from the tax payer upon taking the material as a whole and applying its best, just and reasonable judgment.

64. It is the Tribunal's view that the Respondent ought to have used the value of the processed seeds in determining the value to be attributed to the seeds that were used for planting .It is therefore improper to seek to impose tax on non-existent or theoretical profit that would have been made had the seeds been sold.

    It should be noted that sales include a mark-up (gross margin) which cannot and should not be imposed where there were no sales.

65. The Tribunal notes that both parties are in agreement that after harvest, there is loss of moisture in the seeds but disagree on the percentage of moisture loss to be taken into account. To resolve this issue, the Tribunal recommends that Industrial Standards which are available with the Ministry of Agriculture or other relevant governmental institution responsible for such matters, credible authority or the relevant farmers' association be obtained by the Respondent and adopted to determine the percentage of moisture loss.

66. Similarly, the Respondent do obtain appropriate information from the aforesaid bodies or institutions on the rate or recommended quantity of seed applied per acre to determine the produce used as seed.

FINAL ORDERS:-

67. The Tribunal therefore orders as follows: -

    i. The Appeal be and is hereby allowed.

    ii. The Assessment dated 13th January 2017 be and is hereby set aside with an order that the matter be referred back to the Commissioner for re- assessment.

    iii. Each party to bear its own costs.

DATED and **DELIVERED** at **NAIROBI** this **28th** day of **August, 2020**

.....

PATRICK LUTTA
CHAIRPERSON

.....

HELEN BILA
MEMBER

.....

MWAI MBUTHIA
MEMBER

.....

ELISHAH NJERU
MEMBER