

## RRA v. RUHANDO

[Rwanda SUPREME COURT – RCOMA0122/12/CS (Rugege, P.J., Mukandamage and Ngagi, J.) April 22, 2016]

*Tax law – Assessment without notice – The necessary documents annexed on the tax declaration – Assessment without notice is applied in case the tax declaration was not accompanied with all necessary documents provided for by the Commissioner General rules – Law N°25/2005 of 04/12/2005 on tax procedures, article 28(4) – Commissioner General rules N°001/2007 of 15/06/2007, article 2.*

*Tax law – The rate applied in the assessment without notice – In case of assessment without notice, the legally provided rate used in presumptive tax regime is the one applied – Law N°16/2005 of 18/08/2005 2005 on direct taxes on income, article 11.*

*Tax law – The time framework for tax assessment – RRA has the right to rectify the documents of tax declaration, but failure to do so within the period provided for by the law, that right ceases – Law N°25/2005 of 04/12/2005 on tax procedures, articles 26 and 27.*

**Facts:** RRA audited Ruhando and assessed him without notice on the income tax of fiscal years 2008 and 2010 on the ground that he did not attach the list of his creditors on the tax declaration he submitted. He was also charged the value added tax for the fiscal year 2008 with interest. Having not satisfied with the outcome of the audit, Ruhando appealed to the Commissioner General of RRA requesting those taxes to be waived. Subsequently, he was informed that his appeal has merit only in regard to the loss arising from the fiscal year 2007.

Ruhando appealed to the Commercial High Court which found his claim with merit and waived the income tax for the fiscal years 2008 and 2010. It also declared that the value added tax paid on input tax in 2008 is equivalent to 73,131,312Frw instead of 56,623,239Frw and ordered RRA to reimburse the counsel fees to Ruhando.

RRA appealed to the Supreme Court arguing that the Commercial High Court held that the assessment without notice was inconsistent with the law, disregarding the fact that RRA has the right to make assessment without notice if the tax declaration made by the taxpayer was not accompanied with all necessary documents including the list of his/her debtors and creditors as provided for by the law. In his defense, Ruhando argues that although the law provides that there are documents which must accompany the tax declaration but it does not specify them nor does it specify the authority to identify them, therefore, the Commissioner General endowed himself the authority which he is not legally entitled to by issuing the directives concerning the handing of the listing, thus he requests the court to rectify it.

Another ground of appeal advanced by the RRA is that the Court held that the tax imposed on Ruhando at a rate of 4% of the annual turnover is contrary to the law, ignoring the fact that in case of assessment without notice, the tax cannot be less than the one imposed under presumptive tax regime as provided by the law. Ruhando defends himself by arguing that the taxpayer, who is assessed without notice, is that one with income while he is not obliged to pay tax because of the loss he incurred.

In addition to the above, the other ground of RRA appeal is that the Commercial High Court disregarded that the value added tax paid by Ruhando should not be considered as paid because RRA could not carry out an audit for that tax period because of the prescription. In his defense, Ruhando states that if a taxpayer makes a tax declaration and the tax

administration fails to conduct the audit within the time provided by the law, the declaration of the taxpayer is considered as accurate.

**Held:** 1. Assessment without notice is applied in case the tax declaration was not accompanied with all necessary documents provided for by the rules of Commissioner General. Thus, computing the direct income tax through assessment without notice was in accordance with the law

2. In case of assessment without notice, the legally provided rate which is used in presumptive tax regime is the one applied. Thus, the fact that the tax was imposed on the taxpayer computed at the rate of 4% is in accordance with the law.

3. The RRA has the right to rectify the documents of tax declaration, failure to do so within the period provided for by the law; that right ceases. Thus, the value added tax paid by Ruhando for the fiscal year 2008 must be considered.

**Appeal has merit in parts.**

**The respondent must reimburse a half of the court fees to the appellant.**

**Statutes and statutory instruments referred to:**

Constitution of the Republic of Rwanda of 4/6/2003 as it was amended and complemented up to 13/8/20008, articles 201(1) and (2).

Law N°25/2005 of 04/12/2005 on tax procedures, articles 26, 27, 28(4) and 29.

Law N°16/2005 of 18/08/2005 2005 on direct taxes on income, article 11.

Commissioner General rules N°001/2007 of 15/06/2007 implementing the law N°16/2005 of 18/08/2005 on direct taxes on income, article 2.

**No case referred to.**

## **Judgment**

### **I. BRIEF BACKGROUND OF THE CASE**

[1] On 02/01/2012, Ruhando Ernest was given the audit report conducted on both direct income tax and value added tax, whereby he was charged the tax amounting to 162,068,634Frw for the years 2006, 2007, 2008, 2009 and 2010.

[2] Ruhando Ernest was not satisfied with the outcome of that audit and consequently on 08/02/2012 appealed to the Commissioner General of RRA who on 30/03/2012 replied that his appeal is founded only in regard to the point relating to the loss incurred in the fiscal year 2007 and therefore 11,240,413Frw was deducted from 162,068,634Frw of the tax he had been charged. Thus the unpaid tax remained worth 150,828,221Frw for the direct income tax of the fiscal years 2008 (amounting to 62,583,302Frw), 2010 (amounting to 12,701,584Frw) and 2009 (amounting to 8,915,139Frw), and the interests to be computed on the date of payment. With regard to the value added tax of the fiscal year 2008, the Commissioner General stated that the tax which RRA acknowledges to have been paid is 56,623,239Frw instead of 73,131,312Frw.

[3] Ruhando Ernest not being satisfied with that decision, appealed to the Commercial High Court. In the judgment RCOM0095/12/HCC rendered on 15/06/2012, the Court found his claim with merit and decided that the direct income tax amounting to 62,583,302Frw and 66,628,196Frw, of the fiscal year of 2008, 2010 respectively is waived. It also held that the input value added tax paid in 2008 amounts to 73,131,312Frw instead of 56,623,239Frw. It ordered RRA to pay 500,000Frw for counsel fees to Ruhando Ernest (Rwatole).

[4] RRA was not satisfied with that decision, therefore it appealed against it in the Supreme Court alleging that:

a) Concerning the direct income tax of 2008 and 2010 which was levied through the assessment without notice:

The Commercial High Court stated that if RRA wishes, the list of creditors may be availed after the declaration date of the tax, without providing legal basis, since as long as the audit has not yet been conducted after the declaration of the taxpayer, the RRA doesn't have any encounter with the taxpayer to request him or her to produce any document;

In spite the fact that the judge stated that the list may be availed after the declaration, it is not provided for by the law because during the declaration, the list is attached in accordance with the provisions of article 28(4°) of Law N°25/2005 of 04/12/2005 on tax procedures as amended and completed up to date, and article 2 of Commissioner General rules N°001/2007 of 15/06/2007 implementing the Law N°16/2005 of 18/08/2005 on direct taxes on income; as amended and completed up to date that list has to be annexed to the declaration;

The Commercial High Court wanted to highlight that RRA is not allowed to issue the assessment without notice in case it does not prove the prejudice caused by the fault committed, without demonstrating the provisions of the law which provides it and it disregarded the fact that assessment without notice constitutes another procedure of taxation;

b) Concerning the direct income tax which was computed on the rate of 4%, the Commercial High Court disregarded:

Article 29(3) of the Law N°25/2005 of 04/12/2005 mentioned above provides that in case of an estimated assessment, the amount of tax cannot be less than the tax which would be paid if the taxpayer was to pay under presumptive tax regime;

Article 11 of the Law N°16/2005 of 18/08/2005 mentioned above, provides that Intermediate business owners shall pay a lump sum tax of 4% on annual turnover;

c) Concerning the value added tax of fiscal year 2008; the Commercial High Court held that RRA has to acknowledge the input value added tax paid during 2008 which amounts to 73,131,312Frw, but it ignored that the tax that RRA acknowledges corresponds to audited months, from March to December 2008.

d) Concerning damages, it should not be ordered to pay 500,000Frw of counsel fees while it is obvious that Ruhando Ernest's claim lacks merit (*Accessorium sequitur principale*).

[5] The case was heard in public on 22/03/2016, RRA represented by Counsel Mugire Joseph while Ruhando Ernest was represented by Counsel Nsengiyumva Abel.

## II. ANALYSIS OF LEGAL ISSUES

### a. Whether the computation of direct income tax of the fiscal years 2008 and 2010 through the assessment without notice was legally conducted.

[6] Counsel Mugire Joseph argued that the Commercial High Court held that the assessment without notice was contrary to the law, but it disregarded the fact that RRA conducted that assessment basing on article 28(4) of the Law N°25/2005 of 04/12/2005 on tax procedures which provides that the Tax Administration is entitled to start the estimated assessment procedure when the tax declaration was not accompanied by all necessary documents, because Ruhando Ernest had not availed the list of his creditors as provided for by article 2 of the Commissioner General rules N°001/2007 of 15/06/2007 implementing the Law N°16/2005 of 18/08/2005 on direct taxes on income. He further state that the reason why RRA requests for the list of the creditors, is to get the real figure of the business's finance status since the debts reduces the taxable income especially that and it is possible to a taxpayer to declare inexistent debts.

[7] Nsengiyumva Abel, the counsel for Ruhando Ernest, states that article 28(4) of the Law N°25/2005 of 04/12/2005 on tax procedures, provides that there are necessary documents that accompany the tax declaration but it does not state neither those documents nor the competent person to identify them, thus the issue at stake consisting of establishing the necessary document and its importance in the tax assessment. He states further that in endeavor to determine the importance of that document, the mode of computation of the direct income tax should be considered where article 16 of the Law N°16/2005 of 18/08/2005 on direct taxes on income provides that the business profit is the difference between the income and expenses, while article 21 of the same law provides for the requirements for expenses to be considered as deductible. He continues to argue that another ground to prove that the list was not necessary, is the fact that during the audit of fiscal years 2006 and 2007, that list was not available and the audit was conducted and concluded. In 2008, Ruhando Ernest submitted the declaration which was accepted without being informed about missing documents or that the declaration was incomplete. He further states that in enacting those rules, the Commissioner General endowed himself with the power which he does not legally possess because the law does not endow it to him/her, and even if he was competent to do so, the list was not necessary. Thus if he overstepped his/her power, this should be rectified by the court. He concludes by stating that the list does not reduce the profit rather it demonstrates the names of the creditors, since the profit is indicated by accounts.

## THE VIEW OF THE COURT

[8] Article 28(4) of the Law N°25/2005 of 04/12/2005 on tax procedures as amended and completed up to date, provides that: “the Tax Administration is entitled to start the estimated assessment procedure when [...] 4° the tax declaration was not accompanied by all necessary documents” [...].”

[9] Article 2 of the Commissioner General rules N°001/2007 of 15/06/2007 implementing the law N°16/2005 of 18/08/2005 on direct taxes on income<sup>1</sup>, provides that: “a person whose annual business turnover is twenty million (20,000,000Frw) or more must attach the following annexes to the declaration: 1. Balance sheet; 2. Profit & Loss statement; 3. A table showing depreciation; 4. List of debtors; 5. List of creditors”.

<sup>1</sup> These rules has been published in the Official Gazette N°12 of 15/06/2007.

[10] The case file demonstrates that Ruhando Ernest was assessed without notice in the fiscal years of 2008 and 2010 for the reason that he did not attach the list of creditors on the declaration of those taxes. On the one hand, RRA argues that the list is a necessary document which must accompany the tax declaration, whereas on the other hand, Ruhando Ernest argues that the list is not a necessary document since the debt he owes to others are indicated in the balance sheet which accompanied the tax declaration, which implies that list can be submitted later in case RRA needs it and it is this reasoning of Ruhando Ernest which was considered by the Commercial High Court.

[11] The court found that as provided by article 28(4) of the Law N°25/2005 mentioned above, the rule is that the assessment without notice is conducted if the tax declaration was not accompanied with all necessary documents which were explained in article 2 of the Commissioner General's rules N°001/2007 mentioned above and the list of creditors was included in case the business annual turnover is more or equal to 20,000,000Frw.

[12] The court finds that since the aforementioned Commissioner General's rules N°001/2007 were published in the Official Gazette<sup>2</sup>, nothing is likely to prevent from being applied since they are not in conflict with the Law N°16/2005 of 18/08/2005 on direct taxes or income, therefore this implies that Ruhando Ernest had to comply with article 2 of those rules by annexing on the tax declaration the list of his creditors. The fact that the aforementioned Commissioner General's rules, order the taxpayer to avail the list of his/her creditors, cannot be considered as abuse of powers bestowed to him as held by the Commercial High Court, since he is the one in charge of the daily management of that institution<sup>3</sup>, especially that the basis of that list is obvious because during the tax declaration it helps to establish the existence of those creditors to clear the doubt of tax evasion since those debts reduces the taxable income as explained by the counsel for RRA.

[13] Pursuant to stated reasons, the Court finds that the computation of the direct tax on income of the fiscal years 2008 and 2010 through the assessment without notice was in conformity with the law, therefore the rulings of the judgment RCOMA0095/12/HCC concerning that ground has to be reversed.

**b. Whether Ruhando Ernest has to be taxed at the rate of 4% of the annual turnover.**

[14] Counsel Mugire Joseph representing RRA, states that after the Commercial High Court held that assessment without notice was inconsistent with the law, it went further to rule that the tax Ruhando Ernest was imposed on the rate of 4% was also inconsistent with the law disregarding that RRA proved that taxing at the rate of 4% is provided by the law, considering article 29 of the Law N°25/2005 of 04/12/2005 on tax procedures which provides that in case of an assessment without notice, the amount of tax cannot be less than the tax which would be paid if the taxpayer was to pay under presumptive tax regime provided for by article 11 of the Law N°16/2005 of 18/08/2005 on direct taxes on income stating that Intermediate business owners shall pay a lump sum tax of 4% on annual turnover.

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<sup>2</sup> The article 201 para.1&2 of the Rwandan Constitution of 4/6/2003 as it was amended and completed up to 13/8/2008, which was in force when that assessment without the notice was carried out, provided for that: "Laws, orders and other regulations of public interest can only enter into force after they have been duly published in accordance with the procedures determined by the law. Ignorance of a law which has been duly published is not a defense [...]"

<sup>3</sup> Article 21, para.1 of the Law N°08/2009 of 27/04/2009 determining the organization, functioning and responsibilities of Rwanda Revenue Authority (RRA), provides that the daily management of RRA shall be entrusted to its Commissioner General He/she has powers of directing and coordinating daily activities of RRA and shall be answerable to the Board of Directors for the implementation of its decisions, [...]"

[15] Counsel Nsengiyumva Abel for Ruhando Ernest argues that RRA bases the tax rate of 4% on article 29 of the Law N<sup>o</sup>25/2005 of 04/12/2005 mentioned above, but that this provision was not respected, since if assessment without notice is applied the tax must not be below 4% taxed basing on presumptive tax regime, which means that assessment without notice is applied to a taxpayer who ought to pay tax whereas for Ruhando Ernest, he is bankrupt, therefore was not obliged to pay tax, except if the tax of 4% is a penalty, which is provided by the law. He further states that paragraph 3 of article 29 mentioned above contains a sentence that “the tax should be paid by considering the presumptive tax regime” while fiscal legislation does not contain an expression “small income”, rather they contain “small enterprises” which is provided in article 2(6) of the Law N<sup>o</sup>16/2005 of 18/08/2005 on the direct income tax. He concludes by requesting the Court to consider the judgment RCOMA0009/11/CS between RRA and Mukagihana Emerthe, rendered on 7/3/2016 by the Supreme Court, which settled the same issue.

## THE VIEW OF THE COURT

[16] Article 29(3) of the Law N<sup>o</sup>25/2005 of 04/12/2005 mentioned above provides that: “[...] in case of an assessment without notice, the amount of taxes cannot be less than the taxes which would be paid if the taxpayer was to pay under presumptive tax regime”<sup>4</sup>.

[17] The last paragraph of article 11 of Law N<sup>o</sup>16/2005 of 18/08/2005 on the direct income tax provides for that “[...] Intermediate business owners shall pay a lump sum tax of 4% on annual turnover”<sup>5</sup>.

[18] The case file demonstrates that after Ruhando Ernest was assessed without notice for income of fiscal years 2008 and 2010, the Commissioner General, in his reply to the appeal lodged by Ruhando Ernest, confirmed that he must pay the income tax for the fiscal year 2008 amounting to 62,583,302Frw<sup>6</sup> which is the equivalent of 4% of 977,864,092Frw which is the annual turnover of that year (Annual turnover rectified), and the income tax amounting to 66,628,196Frw<sup>7</sup> for 2010 which is the equivalent of 4% of 1,041,065,567Frw as annual turnover of that year (Annual turnover declared). In addition to that, this rate of 4% is provided for by the last paragraph of article 11 of the Law N<sup>o</sup>16/2005 mentioned above.

[19] Through the analysis of aforementioned provisions, the Court finds that, the Legislator provided that the owner of intermediate business is the one who pays the lump sum tax of 4% on annual turnover, which means that instead of calculating the exact income, the tax is computed under the presumptive tax regime. Therefore, given that article 29(3) of the Law N<sup>o</sup>25/2005 mentioned above provides that in case of assessment without notice, the tax cannot be less than the tax which would be paid if the taxpayer was to pay under the presumptive tax regime, this implying that, since there is no other rate provided by the Law N<sup>o</sup>16/2005 of 18/08/2005 on the direct income tax, RRA had no other means of taxing other than applying the rate of 4% mentioned above.<sup>8</sup>

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<sup>4</sup> In case of an assessment without notice, the amount of taxes cannot be less than the taxes which would be paid if the taxpayer was to pay under presumptive tax regime.

<sup>5</sup> Intermediate business owners shall pay a lump sum tax of 4% on annual turnover.

<sup>6</sup> 62,583,302Frw consisting of 39,114,564Frw of the principal tax + 3,911,456Frw for fines for delay + 19,557,282Frw for penalty for understatement of the tax.

<sup>7</sup> 66,628,196Frw consisting of 41,642,623Frw of the principal tax + 4,164,262Frw for fines for delay + 20,821,311Frw for penalty for understatement the tax.

<sup>8</sup> This law is the one which is applied in the assessment of the direct income tax.

[20] Regarding the assertion of Ruhando Ernest that he should not pay the income tax for the above mentioned fiscal years because he incurred loss, the Court finds that, as stated in the letter written by the Commissioner General of RRA in response to his appeal, Ruhando Ernest (Rwatole) was exempted from the tax amounting to 11,240,413Frw and it also acknowledges he had incurred a loss of 202,021,082Frw for the fiscal year 2009 in lieu of payment position, this decision being taken after finding his appeal with merit on the ground regarding the loss originating from the fiscal year 2007 which was not carried forward to 2009. Therefore, Ruhando Ernest should advance that loss by arguing that he should not pay the income tax for the fiscal years 2008 and 2010, which was levied through the assessment without notice, while that loss was carried forward to the fiscal year 2009.

[21] Basing on stated reasons, the Court finds that Ruhando Ernest (Rwatole) being charged with the tax computed on the rate of 4% of the annual turnover through assessment without notice, does not contradict the law, therefore the decision of the Commercial High Court waiving the income tax of the fiscal years 2008 and 2010 amounting to 62,583,302Frw and 66,628,196Frw respectively must be reversed.

**c. Whether the value added tax amounting to 16,508,073Frw of the fiscal year 2008 should not be considered as paid due to the prescription of its assessment.**

[22] Counsel Mugire Joseph for RRA, states that the Commercial High Court disregarded the fact that during the fiscal year 2008, RRA acknowledged that Ruhando Ernest paid value added tax amounting to 56,623,239Frw, but RRA did not acknowledge that he paid 16,508,703Frw corresponding to months of January up to April of same fiscal year because it informed him that it cannot acknowledge the tax paid for which it cannot conduct an audit, because the period to do it had was struck by prescription and it therefore held that the value added tax paid by Ruhando Ernest is 73,131,312Frw. Furthermore, he states that the conduct of audit expires within three years and that period is binding on both RRA and the taxpayer, because on the side of RRA, accepting the statements of the taxpayer will have implications while both parties should equally bear consequences.

[23] Nsengiyumva Abel the counsel for Ruhando Ernest, argued that with regard to VAT, a taxpayer makes a declaration, and when RRA fails to conduct an audit within due time, the declaration made by the taxpayer becomes final and thus considered as true.

## **THE VIEW OF THE COURT**

[24] Article 26 of the Law N°25/2005 of 04/12/2005 on tax procedures provides that: “When the Tax Administration discovers a miscalculation, an omission, a misrepresentation, an understatement of income or any other error in the tax declaration or an assessment, it has the right to issue an adjusted assessment”.

[25] Article 27 of the Law N°25/2005 of 04/12/2005 on tax procedures as it has been amended and completed by article 3 of the Law N°74/2008 of 31/12/2008, provides that “In case the tax declaration form is rectified, the Tax Administration sends a rectification note to the taxpayer. The note contains a draft of the adjusted assessment and all the elements leading to the adjusted assessment. The rectification note contains fines determined by the Tax Administration in case of non-compliance with the tax laws [...]. The rectification note may be issued in a period of three (3) years, starting from the day of the filing of the tax declaration. A rectification note has to be issued at least on the last day of the three years period. The prescription mentioned in this paragraph is interrupted if the taxpayer has been

informed to be audited by the Tax Administration, when there has been an affidavit thereof or by other deeds of acknowledgement by the taxpayer concerning the tax liabilities and all other provisions provided in the other laws [...]".

[26] In the case at hand, the documents in the file indicate that RRA acknowledges that Ruhando Ernest (Rwatole) declared that he paid the VAT amounting to 73,131,312Frw, but the auditors only accepted the VAT payment of 56,623,239Frw due to the fact that the audit for the period of January to April 2008 had been struck by prescription therefore the VAT amounting to 16,508,073Frw for those months is not acceptable as paid.

[27] The Court finds that as RRA had the right to rectify the tax declaration within three years as provided for by article 27 mentioned above, this implies that it has to bear the consequences for its failure to do so by undoubtedly acknowledging the tax declaration made by the taxpayer. For that reason, RRA has to acknowledge all the input VAT paid by Ruhando Ernest (Rwatole) for the fiscal year 2008 which amounts to 73,131,312Frw.

[28] Pursuant to stated reasons, the Court finds that the VAT amounting to 16,508,073Frw of the fiscal year 2008 has to be considered as paid by Ruhando Ernest (Rwatole) because the failure to conduct the VAT audit for the fiscal year 2008 was not his fault, therefore the decision of the Commercial High Court confirming the payment of the input VAT for the fiscal year 2008 amounting to 73,131,312Frw has to be sustained.

#### **d. Whether RRA should be charged with damages.**

[29] Counsel Mugire Joseph argues that the institution should not be charged 500,000Frw of damages since what it did is provided for by the law, therefore they should be discharged.

[30] Counsel Nsengiyumva Abel adduces that the previous judge committed no error since it was RRA that dragged Ruhando Ernest in lawsuits.

### **THE VIEW OF THE COURT**

[31] The court finds that the Commercial High Court did not make any error in charging RRA damages because it had found that it was RRA which led Ruhando Ernest in lawsuit, thus he incurred expenses paying for the lawyer's service.

[32] The Court finds however that, at this appellate level, the decision charging damages has to be quashed since it was established that the assessment without notice was in accordance with the law, as motivated above, thus this ground of RRA has merit.

### **III. THE DECISION OF THE COURT**

[33] The appeal of RRA has merit in parts;

[34] It decides that the judgment RCOMA0095/12/HCC rendered on 15/06/2012 by the Commercial High Court has changed only with regard to the income tax and damages;

[35] It decides that computing the direct tax on income for fiscal years 2008 and 2010 amounting to 62,583,302Frw and 66,628,196Frw respectively which was done through assessment without notice on the rate of 4% of the annual turnover, was done in accordance with the law;



[36] It orders that the counsel's fees amounting to 500,000Frw which RRA had been charged is quashed;

[37] It orders Ruhando Ernest (Rwatole) to reimburse 50,000Frw equivalent to ½ of the court fees to RRA, because it paid a total of 100,000Frw for the court fees and some grounds of appeal have merit.