REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL
APPEAL NO.157 OF 2016

CIVICON LIMITED.....APPELLANT

VERSUS

THE COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGEMENT

INTRODUCTION

1. The Appellant is a limited liability company duly incorporated in Kenya. It is in the business of providing transport, civil and mechanical engineering.
2. The Respondent is established under the Kenya Revenue Authority Act, Chapter 469 Laws of Kenya and is charged with the mandate, under Section 5 thereof, of the assessment, collection and receipt of revenue as an Agent of the Government of Kenya.

BACKGROUND

3. The Appellant's principal activities are provision of civil, mechanical engineering and transportation services, which services are mainly exported to clients who are domiciled outside Kenya such as Civicon Uganda, Spedag Interfreight AG, Spedag Uganda, Civicon Congo SPRL Maweni in Tanzania, among others.
4. On 2nd October 2015, the Respondent wrote to the Appellant of its intention to Audit its operations covering the period January 2012 and July 2015 in respect of Corporation Tax for the years of income 2012 - 2014, Value Added Tax (VAT), Pay as You Earn (PAYE) and Withholding Tax (WHT).

5. Upon carrying out the Audit, the Respondent communicated its findings to the Appellant vide its letter dated 26th May 2016.

6. The Appellant Objected to the Respondent's Tax Audit Findings vide its Notice of Objection dated 10th August 2016. On receipt of the said Notice of Objection, the Respondent vide its letter dated 15th August 2016, stood over the taxes assessed pending review of the issues Objected to.

7. The Appellant proceeded to produce further documents to support its Notice of Objection in respect of transport services that the Respondent had subjected to VAT at 16%, which the Appellant had opined to be zero rated (0%).

8. The Respondent upon review of the additional documents revised its initial tax assessment thereby resulting in the parties agreeing on all the taxes save for the dispute on VAT.

9. The Appellant being aggrieved by the findings of the Respondent in respect of the Confirmation of Assessment for VAT dated 10th January 2016, proceeded to file its Notice of Appeal on 9th November, 2016 together with the Memorandum of Appeal and Statement of Facts on 23rd November 2016.

THE APPEAL

10. The Appeal as filed is premised on the following Grounds: -

    i) THAT the Respondent misdirected itself in fact and in law in finding that the Appellant ought to have charged VAT in respect to the transport/freight services offered by the Appellant to Companies that are domiciled outside Kenya.

    ii) THAT the Respondent erred in law in finding that services exported outside the country are subject to VAT at the standard rate of 16% (as opposed to being zero rated)

notwithstanding that the services are used and or consumed outside Kenya.

iii) THAT the Respondent failed to differentiate between the provision of freight services and provision of services ancillary to goods in transit.

11. The Appellant contended that VAT was not applicable on the transport services provided to its clients outside Kenya since the said services were zero-rated in accordance with Paragraph 1 of the Second Schedule to the VAT Act read together with Section 7 thereof.

12. According to the Appellant, what it is providing is not a service of goods on transit but a transport service which is consumed outside Kenya and therefore zero-rated for VAT purposes. In support of the contention, the Appellant invoked Section 2 of the Act which defines a service exported out of Kenya to mean a service provided for use or consumption outside Kenya.

13. The Appellant argued that it is involved in a supply of service for another person i.e. the consumer and the said service is freight/transport and it is across border trade service in nature as the person receiving or consuming the service is outside the Kenyan jurisdiction as shown in their invoices that have been availed to the Respondent.

14. The Appellant further relied on the OECD International VAT/GST guidelines to support its contention that the destination principle provides that internationally traded services and intangibles ought to be taxed in accordance with the rules of jurisdiction of consumption. In this case the Appellant's clients are located outside Kenya and therefore their respective countries of residence have

their taxing rights over the services provided. In furtherance of its argument herein, the Appellant referred to the case of **Unilever Kenya Limited v Commissioner Domestic Taxes 2005, eKLR** where the Court in making its judgment stated that:-

"We now leave in a global village and we cannot overlook and side-line what has come out of the wisdom of tax payers and collectors in other countries. He further stated that we must be prepared to innovate and apply creative solutions based on best practice available to us"

15. The Appellant argued that it is providing an export of service and not a service to goods on transit and according to Section 7 of the VAT Act, the service is taxable but at the rate of 0%.

16. The Appellant referred the Tribunal to various case law in support of its argument that no tax shall be levied except as provided by statute, that one must look at the facts on the ground with a view to connecting the same with the particular Section of the statute and further that clear words are necessary when imposing atax. The said cases are **Cape Brandy Syndicate v Inland Revenue Commissioner (1921) 1 KB 64, Astall v HMRC (2010)STC 137** at page 44, **Inland Revenue Commissioner v Duke of West Minister Commissioner and Inland Revenue Commissioner v Hinchy (1960).**

THE RESPONSE

17. The Respondent contended that the Appellant offered transport services to companies in Kenya and that the said services were subject to VAT at the rate of 16%. It based its assertion on the ground that most of the Appellant's services were mainly offered to Spedag Interfreight (K), which is a local company incorporated in Kenya with its offices based in Mombasa and therefore these

services were used and consumed by a local company based in Kenya.

18. The Respondent submitted that the period for the dispute herein is from 2nd September 2003 to 19th September 2004 and therefore the law applicable is Sections 2, 5 &7 of the VAT Act, 2013. In addition it referred to the Finance Act, 2014 and the Finance Act, 2015. It was the Respondent's submission that Section 5 (2) of the VAT Act, 2013, being the charging Section provides as follows:-

"A tax, to be known as value added tax, shall be charged in accordance with the provisions of this Act on a taxable supply made by a registered person in Kenya".

Whereas Section 5(2) provides as follows: -

"The rate of tax shall be: -

a) In the case of zero-rated supply, zero percent; or

b) In any other case, sixteen percent of the taxable value of the taxable supply made by a registered person in Kenya".

19. According to the Respondent, Section 5(2) of the VAT Act, 2013, provides that VAT shall be charged either at zero-rate or 16%. However for the supply of qualify for zero-rating under Section 5(2), (a), the supply must fall within the provision of Section 7(2) of the Act, which provides as follows:-

"A supply or importation of goods or services shall be zero-rated under this section if the goods or services are of the description for the time being specified in the Second Schedule".

20. Consequently, the Respondent submitted that since the supply of taxable services in respect of goods in transit was not specifically provided for in the Second Scheduleto the VAT Act 2013 at the relevant period, meant that the services were taxable at 16%.

21. The Respondent stated that vide the Finance Act No. 16 of 2014, which came into effect on 14/9/2014, the legislature expressly exempted the supply of taxable services in respect of goods in transit. This was done by listing under part II of the Second Schedule. Later, the Finance Act No. 14 of 2015, which came into force on 11th September 2015, made the supply of such services zero-rated by taking the said services to part A of the Second Schedule.

22. The Respondent further submitted that it ought to disregard the OECD Guidelines referred to by the Appellant, noting that the same are not relevant as there is in existence sufficient legislation inKenya to deal with taxation in respect of supply of transport services in transit, being the VAT Act, 2013. Consequently, it urged the Tribunal to uphold its confirmed tax assessment on VAT on transit charges, being Kshs. 22,203,642/= and dismiss the Appeal with costs.

ANALYSIS AND FINDINGS

23. The Tribunal has carefully and respectfully considered the parties' pleadings, documentation, submissions and authorities and is of the view that there is one issue for its determination herein, namely: -

Whether the Appellant's transport services with respect to goods on transit were zero-rated, or subject to VAT at 16%.

24. The Tribunal notes that the relevant audit period herein was July 2012 to July 2015, the same being in respect to Corporation Tax, for the years of income, 2012-2014, VAT, PAYE and WHT. Subsequently, before the filing of the Appeal, the parties reached a settlement on all the above tax heads save for VAT on the Appellant's transport services with regard to goods in transit. The

Respondent subjected the same to 16% VAT whereas the Appellant contended that the same were zero-rated.

25. It is worth noting that the VAT Act Cap 476, (repealed) provided for zero-rating of goods if they were of a description contained in the 5th Schedule or the 8th Schedule. Paragraph II of the 5th Schedule provided for zero-rating of the supply of the above services. Subsequently the VAT Act, Cap 476 was repealed and replaced with the VAT Act 2013, which came into force on 2nd September 2013.

26. Under the VAT Act, 2013, the charging Section is provided for in Section 5 which provides: -

"The rate of tax shall be: -

a) In the case of zero-rated supply, zero percent; or

b) In any other case, sixteen percent of the taxable value of the taxable supply made by a registered person in Kenya".

27. The Tribunal further notes that of relevance herein too is Section 7(2), which provides as follows:-

"A supply or importation of goods or services shall be zero-rated under this section if the goods or services are of the description for the time being specified in the Second Schedule".

28. A careful reading of the above Sections clearly stipulate that VAT shall be charged either at zero-rate or at 16%. However for a supply to qualify for zero-rating under Section 5(2) (a), the supply must fall under the provisions of Section 7(2) of the said VAT Act, 2013. The Tribunal therefore agrees with the Respondent's argument that the supply of taxable services in respect of goods in transit was not waived by the provisions of the VAT Act 2013 as Part A in zero-rated supplies to the Second Schedule of the VAT Act

2013 had expressly zero-rated items which did not include the supply of taxable services in respect of goods in transit, being the services that the Appellant provided. The zero-rated goods are as shown in the Respondent's attached Second Schedule, marked "DTD7" in its Statement of Facts filed on 23rd December 2016.

29. Moreover, the Tribunal takes cognizance of the fact that vide the Finance Act, No.16 of 2014, which came into force on 14th September 2014, the Legislature expressly exempted the supply of taxable services in respect of goods in transit by listing them under part II, First Schedule. Subsequently in the Finance Act No.14 of 2015 which came into force on 11th September 2015, the supply of taxable services in respect of goods in transit was taken to part A of the Second Schedule, thus making it a zero-rated supply.

30. Consequently the Tribunal makes a finding that during the Audit period of 2nd September 2013 to July 2015, the supply of the services was taxable at 16%. However, during the period July, 2012 to 1st September 2013 and 14th September 2014 to July 2015, the said services were exempt and therefore zero-rated, whereas during the period of 2nd September 2013 to 14th September 2014 they were not zero-rated.

31. In view of the foregoing the Respondent's Confirmed Assessment on VAT on transit charges, pursuant to its letter dated 10th October 2016, being for the period September 2013 to September 2014 is lawfully charged at 16%.

32. As to the Appellant's submission on the OECD guidelines, the Tribunal agrees with the Respondent's submissions that the relevant charging Section of the VAT Act is clear on the issue in dispute as the supply of transportation services in respect of goods in transit

has been provided for by the relevant legislation, as the transit service is wholly used and consumed in Kenya.

Consequently, it does not qualify as an exported service.

33. The upshot of the foregoing is that the Respondent's Assessment for VAT dated 10th January 2016 is hereby upheld.

34. The Appeal is hereby dismissed and each party shall bear its costs.

DATED and DELIVERED at NAIROBI this 26th Day of March, 2018.

In the presence of:

VINCENT MUTAHI & ALEX MURIUKI for Appellant

KEMUNTO OCHAKO for Respondent

.....
JOSEPHINE K. MAANGI
CHAIRPERSON

.....
GEOFFREY K. C. KATSOLEH
MEMBER

.....
WILFRED GICHUKI
MEMBER

.....
OMAR J. MOHAMMED
MEMBER

.....
JOSEPH M. WACHIURI
MEMBER