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Nestlé Zambia Limited Supreme Court Ruling

Court's decision marks a pivotal moment

The Supreme Court of Zambia, on 20 August 2025, handed down a landmark judgment in the appeal involving the Zambia Revenue Authority (ZRA) and Nestlé Zambia Limited (NZL).

This decision marks a pivotal moment in the country's transfer pricing (TP) jurisprudence, addressing core aspects of Zambia's evolving tax administration, TP principles, and the alignment of local practice with international standards, notably, the OECD Guidelines and the United Nations Manual on Transfer Pricing for Developing Countries.

Facts of the case

The ZRA issued a TP assessment of **ZMW 56,579,048** (circa USD 2.4 million at the time), with an additional tax liability of **ZMW 13,860,103** (circa USD 600,000) for the period 2010 to 2014.

Some of the issues arising were as follows:

Losses

NZL had made losses since its inception in 2010. It attributed its losses to commercial start-up factors, whereas the ZRA linked them to non-compliance with the arm's length principle.

The ZRA characterised NZL as a Low-Risk Distributor (LRD) due to the fact that it carried out limited functions and did very little on its own without the direction, assistance, and control from its related parties.

NZL argued that it was a fully-fledged distributor by virtue of bearing the inventory risk, purchasing from related parties, and having its own local board of directors.

Testing approach

NZL had entered into various transactions with its related parties, including debt financing, management services, distribution license agreements, and supply of Nestlé products.

The ZRA aggregated all the transactions and tested the overall operating margin result of the company on the basis that the transactions were closely linked.

The use of geographically restricted benchmarking studies

The ZRA dismissed NZL's benchmarking study and performed its own benchmarking exercise, resulting in a set of comparables from Western Europe. NZL argued that comparables from Western Europe were not comparable to NZL's business and macro-environment in Zambia.

NZL challenged the assessments raised by the ZRA at the Tax Appeals Tribunal (TAT), which ruled on several critical points, including loss-making operations, functional characterisation for TP purposes, and reassessment of periods.

The TAT ruled in favour of NZL on all the grounds, excluding the characterisation of NZL as a fully-fledged distributor. The TAT also ordered that the ZRA conduct a reassessment within 180 days.

Dissatisfied, the ZRA appealed to the Supreme Court.



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Appellant's arguments

Some of the arguments were as follows:

- The TAT erred by placing the responsibility on ZRA to demonstrate that NZL's approach to TP in its dealings with related parties was improper and led to NZL's financial losses.
- The TAT erred in law and fact when it held that the transactions between NZL and its related parties could not be aggregated but should have been tested individually, contrary to both the 2010 OECD Guidelines and the United Nations Manual on Transfer Pricing for Developing Countries.
- The TAT erred in its conclusion that there was no legal requirement for NZL to prepare transfer pricing documentation and to provide the requested information for periods prior to the introduction of the Income Tax Act (Transfer Pricing) Regulations No. 18 of 2018.
- The TAT failed to recognise that the characterisation of NZL as an LRD was crucial in selecting the tested party and the appropriate TP method.
- The TAT erred when, despite having correctly found as a fact that there were no internal comparables in Zambia and on the African continent, it still went ahead to hold that ZRA used benchmarks that were neither comparable to the nature of NZL's business in Zambia nor the macro or micro economic conditions in Zambia.

Respondent's arguments

Some of the key arguments were as follows:

- The TAT never shifted the burden of proof to ZRA. It merely considered the facts and evidence presented and made findings.
- NZL had discharged its obligation to prove that the amounts assessed were excessive by providing the documentation requested. The ZRA had disregarded the documentation without explanation. The ZRA should have provided the reasons for rejecting the methodology applied for the determination of non-arm's length transactions, before it proceeded to use its own.
- Once all the information was provided, the burden shifted to the ZRA to explain its rejection of NZL's documentation.

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- NZL argued that it was a fully-fledged distributor on the following basis:
  - It bore significant risks and performed strategic functions.
  - It was a private company limited by shares and duly incorporated in Zambia, which made it a separate entity from its shareholders and related companies.
  - It contracted for and paid for the services it received. Its financial statements revealed that it incurred expenses involving the distribution, selling, and marketing activities, which did not lie with its related parties.
  - It held a licence to use Group intellectual property in storing, supplying, importing, exporting, marketing, promoting, distributing, and selling the products strictly for its own purpose.
  - It could not be classified as an LRD as it obtained its products from all over the world, with the majority of the products being procured from Nestlé Zimbabwe and Brazil.

NZL also lodged a cross-appeal on the following issues:

- The classification of NZL as an LRD as opposed to a fully-fledged distributor. The ZRA's view was that NZL could not simply rely on the inventory risk in order to prove its classification as a fully-fledged distributor, but rather through a functional analysis.
- Whether the TAT had the power to order a reassessment.

The Supreme Court determination

The Supreme Court determined the issues in dispute as follows:

- The taxpayer bears the burden of proving the incorrectness of the assessment by providing evidence to support the objection. Further, the ZRA can request any documentation that is relevant for audit purposes.
- The Supreme Court sustained the appeal on the ground that aggregation is a much wider concept. Aggregation is permissible as long as the transactions flow from a common source. It recognised that while the OECD guidelines provided for a transaction-by-transaction approach, there were situations where transactions are separate but so closely linked that they can only be evaluated adequately by aggregating them. The aggregation encompasses transactions emanating from a common source, being an order or a contract, and that the transactions substantially flow from the said common source.



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- Where no local comparables are found in Zambia or on the continent, it is incumbent on the ZRA to find suitable and compatible comparables that represent as closely as possible the economic conditions in Zambia to avoid disparity in the analysis.
- NZL does very little administration on its own, and the ultimate risk lies with Nestlé South Africa. The appeal was allowed, and NZL was classified as an LRD.
- The TAT's order for reassessment goes beyond the scope of the initial assessment. The Supreme Court concluded that the ZRA is not precluded from initiating any reassessment.

Implications for multinational groups operating in Zambia

The decision made by the Supreme Court sets a major precedent for tax compliance among multinational groups and local entities operating in Zambia.

The following are the considered implications for Zambian taxpayers:

- **The use of geographically restricted comparables:** The decision provides for the use of regional comparables where there are no local comparables available. It remains to be seen whether regional sets provide more comparable companies than globally distributed sets.
- **Loss making distributors:** Persistent losses may indicate transfer pricing risk. LRDs are generally not expected to be loss-making over long periods. An LRD may be loss-making in specific limited instances such as pandemics like Covid-19 where even companies with guaranteed profit levels would be affected. Any losses incurred by an LRD would require appropriate justification to demonstrate that such losses are not due to transfer pricing. Where taxpayers are in such a persistent loss position, there is a higher evidence threshold to support such results.
- **Aggregation of transactions from a common source:** Distributors should be cautious when entering into related-party transactions with the principal/ entrepreneur. Such transactions include royalties and management. Where transactions are deemed to be from a common source, the ZRA might opt to adopt a whole entity approach as opposed to the more conventional transaction-by-transaction approach.

The Supreme Court ruled in favour of the ZRA on four out of its five grounds of appeal and ruled against NZL's cross-appeal.

Should you wish to discuss this further, kindly feel free to contact your usual contact at Deloitte or any of the contacts herein.

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