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Kenya | Tax | June 2019

Tax Alert

High Court yet again, rules in favour of the taxpayer on the VAT treatment of internationally traded services

The High Court of Kenya, at Nairobi, in its decision in *Panalpina Airflo Limited vs Commissioner of Domestic Taxes (Income Tax Appeal No. 5 of 2018)* has upheld the application of destination principle in determining the country with taxing rights over internationally traded services. In doing so, the Court held that the Appellant's services were exported and therefore zero-rated for VAT. The Court further held that the Appellant was entitled to the refund of any excess input tax arising from the provision of the impugned services.

Background

The Appellant, Panalpina Airflo Limited, a limited liability company registered under the laws of Kenya carries out handling services in an agency capacity for Panalpina Airflo BV. Panalpina Airflo BV is a company registered in Netherlands, which offers logistical services to its customers in the Netherlands.

The handling services provided by the Appellant included the following:

- Documentation;
- Cold room handling services;
- Vacuum cooling; and
- Security (x-ray) screening services.

The Appellant construed its services as falling within the scope of exported services under the Value Added Tax Act, 2013 and therefore zero-rated these services. As a result, the Appellant filed several VAT refund claim applications with the Kenya Revenue Authority ("the Respondent") relating to its VAT credit. However, the

Respondent held the view that the services in question were not exported and, as a result, no refund was due.

Aggrieved by this refund decision, the Appellant filed a notice of objection to the decision. However, the Respondent issued its objection decision confirming its position that the services offered by the Appellant did not qualify as exported in character.

The Appellant filed an appeal at the Tax Appeals Tribunal (TAT) challenging the Respondent's objection decision. The appeal at the TAT was founded on grounds that the Respondent erred in law in finding that the Appellant's services were not exported and that they should have been subject to VAT at 16%. The Appellant further averred that the Respondent erred in law in rejecting its filed VAT refund claims.

The TAT ruled in favour of the Respondent, a decision that resulted in the appeal at the High Court. At the High Court, the Appellant sought to challenge the TAT's findings that the beneficiaries of the Appellant's services were the exporters of flowers who were based in Kenya and that therefore the services were consumed locally.

The Appellant further challenged the TAT's view that pre-shipment services should be considered to have been consumed locally since they are performed before issuance of the bill of lading at which point exportation commences. Further, the Appellant challenged the Tribunal's view that the Organisation for Economic Cooperation and Development (OECD) guidelines on international trade in services were not applicable on the basis that there was no ambiguity in the law. This was despite the fact that the VAT law did not define place of use or consumption for purposes of determining export of service.

The High Court's ruling on this appeal case was in keeping with the recent ruling at the High Court (click here for the alert) on a similar matter in *Commissioner of Domestic Taxes vs Total Touch Cargo Holland*. In the said ruling, it was held that based on the destination principle, the services provided by KAHL in Kenya to Total Touch Cargo Holland in Netherlands qualified as exported in nature and therefore attracted VAT at the zero rate.

Our perspective

The High Court has recently pronounced itself on a couple of rulings on export of services and, in so doing, has set precedence that internationally traded services should be taxed in-line with the destination principle. In simple words, the destination principles aims to avoid double incidence of tax by setting the destination country (in international trade) as the country with taxing rights over goods or services.

Barring any contrary rulings on appeal by the KRA, we hope that these recent rulings will provide guidance and clarity to the KRA and taxpayers on how to tax services traded across borders. It is also hoped that the government will consider views from affected stakeholders and legislate clear guidelines on the taxation of services traded across borders.

Should you have any question on this, kindly contact your relationship manager at Deloitte who will be more than glad to offer you guidance and assistance as necessary.

Regards,

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