KAPLAN&STRATTON NEWSLETTER

K&S WINS MULTIPLE PRECEDENT SETTING TAX CASES

At Kaplan & Stratton we are proud of our long history of obtaining precedent setting judgements that have positively shaped Kenya's tax jurisprudence. Indeed, 2020 has been no different where, despite the global pandemic, our litigation team has won several landmark tax cases for its clients. In this newsletter we summarise these precedent setting decisions and highlight how each decision has brought clarity and confidence to Kenya's business sector.

VAT on Marketing Services Provided to Foreign Companies

The Tax Appeals Tribunal considered whether marketing services were used or consumed outside Kenya and therefore zero rated for VAT.

KRA in a decision issued to our client Coca Cola Central East and West Africa Limited (**CCCEWA**) in respect of marketing services provided by our client to other Coca Cola companies outside of Kenya claimed that the marketing services provided to the companies outside Kenya were locally consumed. Our client engaged Kaplan & Stratton to appeal against the decision to the Tribunal.

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As part of the detailed arguments we submitted to the Tribunal we also engaged an Organization for Economic Cooperation and Development (OECD) expert witness who along with a factual witness supported the position that the services were consumed outside Kenya. The Tribunal weighing this evidence against KRA's submissions and witness agreed with our submissions that the marketing services were consumed outside of Kenya and were therefore exported services.

The Tribunal also noted that the contract for the provision of the services was signed between our client and the Coca Cola Company outside Kenya. Therefore, under the OECD VAT Guidelines, the customer was the Coca Cola Company in the United States making the service an exported service which could not be charged VAT in Kenya.

In making its decision, the Tribunal departed from the previous Tribunal decision against Coca Cola, which had thrown the whole issue of exported services into confusion creating uncertainty for all businesses.

This ruling is of benefit to all international companies who have subsidiaries in Kenya that provide services to parent companies outside of Kenya. Companies now have clarity on the tax position and can properly assess whether VAT is applicable for any services provided within the group originating from Kenya.

PAYE Exemptions & Bilateral Agreement

Care International (**Care**) which is a humanitarian organization entered into a bilateral agreement with the Government of Kenya under which Care's expatriate employees were exempted from payment of pay as you earn (**PAYE**) tax in recognition of the humanitarian work Care undertakes in Kenya that is of benefit to the nation.

KRA however disregarded the exemption and raised a PAYE claim in respect of all the expatriate employees' earnings. Care first appealed against KRA's assessment to the Tax Appeals Tribunal however, the Tribunal only upheld the exemption in respect of four employees. Care then instructed Kaplan & Stratton to appeal the Tribunal's decision in the High Court.

Through a detailed analysis of the bilateral agreement, we successfully demonstrated to the High Court that the exemption was never intended to be limited to four persons but to all expatriates. The High Court in agreeing with our analysis categorically stated that the Tribunal could not re-write the agreement by restricting the exemption to only four expatriate employees. We therefore secured a setting aside of the Tribunal's decision and the KRA's assessment.

The decision is important as it creates certainty for governments and organizations that enter into bilateral agreements with the Kenyan Government that the agreements are respected and enforced.

Tax Payers should not Be Held Liable for KRA System Failures

Our client Rabai Operation and Maintenance Limited (**ROML**) operates and maintains a 90MW power plant. ROML experienced difficulties in uploading its profile on to the Integrated Tax Management System (**ITMS**) which had been set up by KRA.

On the basis of the PIN provided by KRA, ROML continued to deduct input VAT from output VAT and paid the resultant VAT to KRA. However, due to the technical issues with ITMS ROML was unable to file its VAT returns on time and was only able to file its returns after the technical issues had been resolved. KRA however, proceeded to disallow the input VAT claimed by ROML on the basis that ROML had failed to file its returns.

ROML instructed Kaplan & Stratton to appeal the decision. We lodged an appeal to the High Court having been unable to overturn the decision at the Tribunal stage.

The Court held that ROML had deducted its input VAT on time and could not be penalized for a fault in KRA's own system.

The Court's decision is important as it sets a precedent that KRA cannot be allowed to benefit from the inefficiencies of its own system especially where the tax payer produced evidence of complaints to the KRA of the system's failure. The Court correctly held that the tax payer's statutory right to deduct input VAT cannot be thwarted by a failure in KRA's own digital system, setting a clear precedent for the principle of administrative fairness.

Endorsing the World Customs Organization Harmonized System Classifications to Inform Applicable Customs Duty

Our client Associated Battery Manufacturers Limited (**ABML**) is a leading manufacturer in Kenya of automotive and solar batteries. ABML uses PE battery separators in the manufacture of its batteries and had always imported the batteries under the World Customs Organization

Harmonized System (HS) code 8507.90 which was a specific code for battery separators.

Over time ABML automated its process and begun importing its separators in sheets rather than in an already cut form. KRA raised an assessment against ABML for payment of extra duty on the basis that HS Code only applied to items that were ready to use and was therefore not applicable to the separators imported in the form of sheets which were required to be cut and then inserted into the battery.

ABML appealed to the then Customs & Excise Tribunal against the decision. The Tribunal upheld KRA's decision. ABML instructed Kaplan & Stratton to appeal the decision to the High Court.

Kaplan & Stratton successfully obtained a reversal of the Tribunal decision with the High Court agreeing with our argument that the importation of the product in the form of a sheet did not alter the technical specifications of the product.

More importantly the Court held that the Harmonized System is an international standard classification created by the World Customs Organization and the countries who are parties to it are guided by the General Interpretation Rules with the aim of ensuring fair international trade. KRA is therefore required to ensure fairness and avoid charging tax that would affect innovations by companies.

The pro-business decision helps bring consistency and certainty to businesses operating in Kenya or considering setting up business in Kenya because it confirms that international standards and agreed norms are adhered to.