



# **VAT LEGAL FRAMEWORK VAT REGULATIONS**

**16<sup>TH</sup> MARCH 2021**

BY LAW  
WE MUST  
COLLECT TAX

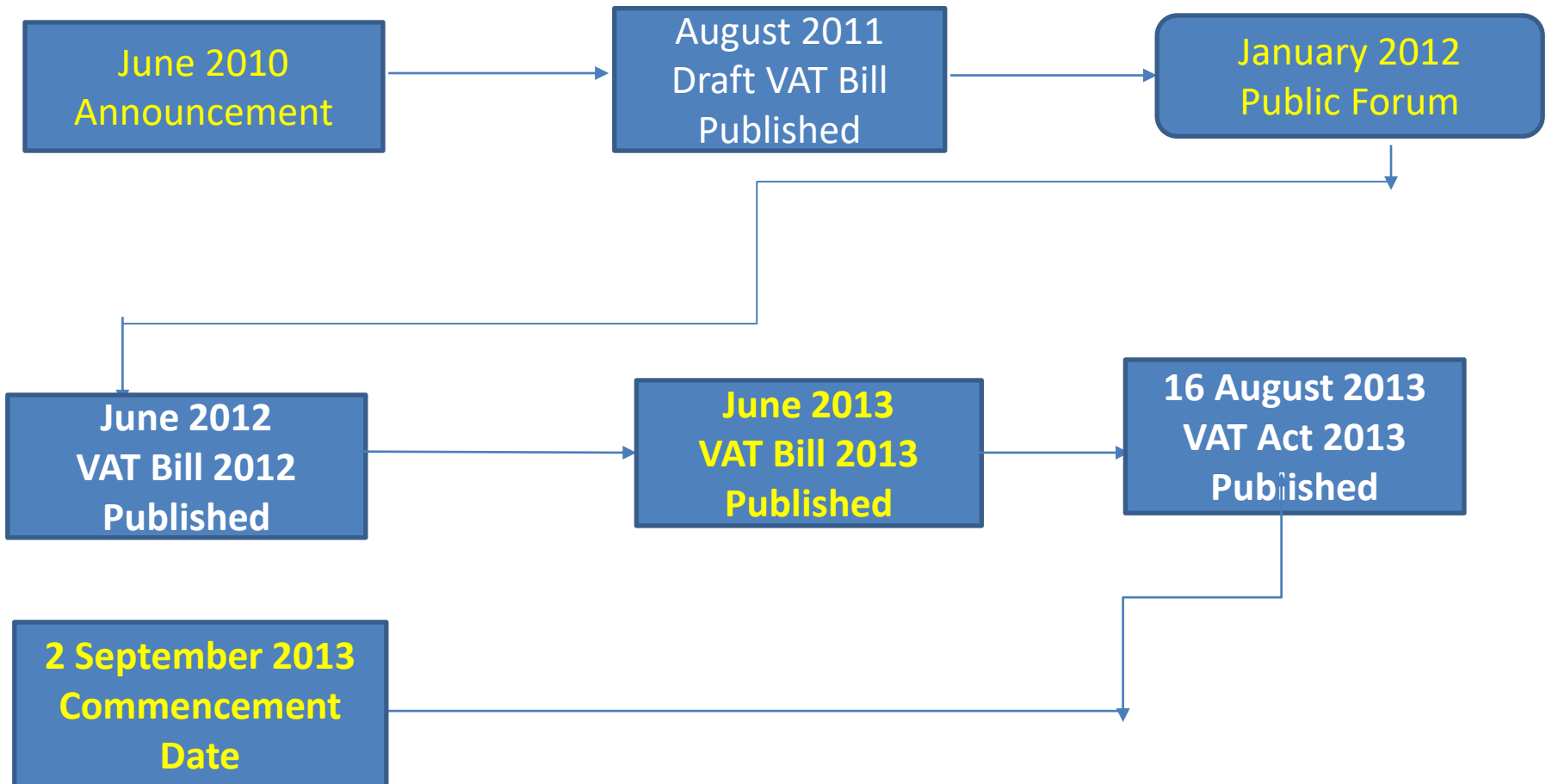
# Presentation Outline



- ❖ An overview of VAT
- ❖ Key issues around VAT
- ❖ VAT Regulations, 2017
- ❖ Interactive session

# Overview of Value Added Tax (VAT)

# VAT Act 2010 -2013 – The Journey



# VAT- Introduction



- VAT is a general consumption tax assessed on the value of goods and services
- Applies to all commercial activities involving production/distribution of goods or services
- Ultimately borne by the final consumer
- It is charged as a % of price i.e. 0%, 8% and 16%
- Popular tool for revenue generation - broad reach and easy administration
- Taxation by exclusion

# Levy of VAT



In Kenya VAT is levied on:

- Taxable supply made by a registered person;
- The importation of taxable goods; and
- Supply of imported taxable services



# Five pillars of VAT



A transaction is in scope of Kenyan VAT where:

- It is a supply or importation of goods or services
- Takes place in the Kenya
- Is a taxable supply
- Made by a taxable person
- Is made in the course or furtherance of any business



# Supply of goods & services



## Supply of goods means:

- a) a sale, exchange, or other transfer of the right to dispose of the goods as owner; or
- b) the provision of electrical or thermal energy, gas or water

## Supply of services means:

- a) any supply that is not a supply of goods or money;

# Supply of goods & services



- b) the performance of services for another person;
- c) the grant, assignment, or surrender of any right; and
- d) the making available of any facility or advantage.

Where is the place of consumption of exported services?

# VAT on exported services

# VAT on exported services



- The VAT treatment on export of services - no agreed position between the KRA and taxpayers
- The VAT Act defines “service exported out of Kenya” as a service **provided for use or consumption outside Kenya.**
- However, there is lack of clarity in the VAT Act on what constitutes ‘*use*’ or ‘*consumption*’ of services outside Kenya
- This is the crux of the controversy on exported services
- Additional complexity brought in by paragraph 13 of LN No. 54 of 2017 - VAT Regulations, 2017 (w.e.f 30 March 2017)

# VAT on exported services



- Regulation 13 of the VAT Regulations, 2017 provides that an export of service does not include:
  - ✓ taxable services consumed on exportation of goods unless they are in relation to transportation of goods which terminates outside Kenya; or
  - ✓ taxable services provided in Kenya but paid for by a person who is not a resident in Kenya
- The TAT and the Kenyan courts have ruled on exported services - FH Services, Total Touch Holland and Coca Cola
- Varied rulings - Courts leaning towards OECD destination principle

# Implications of the High Court Ruling in Total Touch Case

# Total Touch Case Implications



## **a) Place of consumption of the service is key**

- The location (or place) of use or consumption of that service determines whether the service is an export or local supply
- Therefore, the location of the “ultimate” consumer of the services determines the place of consumption

## **b) Where the service is performed is irrelevant**

- Where the service is provided does not determine the question of whether the service is exported or not



# Total Touch Case Implications



## **c) Who is the consumer of the services?**

- In determining who the consumer of the service is, the contractual agreement should be the primary reference
- Further, the internationally accepted VAT destination principle on international trade and services is important
- Taxpayers have to consider whether their transaction is a B2B (consumer is the business) or B2C (customer is the final consumer of the service provided)

# Total Touch Case Implications



## d) Applicability of the OECD destination principle

- The application of VAT globally is based on the destination principle as defined by the OECD Guidelines
- Para 3.5 of the OECD VAT/GST guidelines: “...the place of taxation rules for business-to-business supplies should therefore focus *not only on where the business customer will use its purchases to create the goods, services or intangibles that final consumers will acquire but also on facilitating the flow-through of the tax burden to the final consumer while maintaining neutrality within the VAT system*”

# Total Touch Case Implications



## d) Applicability of the OECD destination principle (cont'd)

- Under the destination principle, goods, services and intangibles are zero-rated when leaving one jurisdiction and are **taxed at importation in another jurisdiction**
- Under the destination principle, the jurisdiction of the final consumer of the goods has the taxing rights over a service supplied in cross-border transactions

# VAT Regulations

# VAT Regulation 13



- Are the VAT Regulations in force?
- Inconsistent with the provision of the Sec 2 of the VAT Act and international best practice on taxation of exports of services
- Effectively, Regulation 13 eliminates the zero-rating of export of services (does not consider services paid in Kenya by non-residents)
- The VAT Regulations, 2017 (in the current form) is bound to increase disputes between KRA and the taxpayers

# VAT Regulation 8



- Regulation 8 provides the input VAT refund formula:
- $R = Z/T \cdot e$ 
  - $R$  = Refund of input tax
  - $Z$  = Zero rated supplies
  - $T$  = Total taxable supplies
  - $e$  = Excess input tax
- Results in input VAT on standard rated supplies being carried forward
- Input tax is not restricted otherwise than under Sec 17

# VAT Exemptions



# VAT Exemptions



- Exempt items listed in the First Schedule to the VAT Act - the negative list principle
- Exemptions on official aid funded projects under paragraph 20 of Part II of the First Schedule to the VAT Act:
  - Requirement is for a project to be official aid funded
  - Approval by the National Treasury
- Legitimacy of administrative requirement by Commissioner to exempt the services?
- ***L.A.B International vs Commissioner of Domestic Taxes (2010)*** - Administrative procedures are internal to KRA and National Treasury

# Input VAT Claims and Auto Assessments

# Input VAT Claims



- Taxpayer entitled to offset output VAT against his input VAT
- Input VAT claimable under Section 17 of the VAT Act
- Requirements to claim input VAT:
  - a) Input VAT was incurred to make taxable supplies
  - b) Valid input VAT documentation - invoice and customs duty entry;
- If the supplier has not declared the sales invoice in a return, a taxpayer cannot claim the input VAT: Section 17(2) **w.e.f. 30 June 2020**

# Input VAT claims



- ***Mahageben kft vs Nemzeti (C80/11 and 142/11 EU)*** - “the question whether the VAT payable has or has not been paid to the public purse is irrelevant to the right of the taxable person to deduct input VAT”
- Right to claim input VAT can be refused if the taxable person “knew or ought to have known that the transaction was connected with fraud...”
- Legitimacy of VAT Auto Assessments (VAAs)?

# Thank You



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