

REPUBLIC OF KENYA
IN THE TAX APPEALS TRIBUNAL AT NAIROBI
APPEAL NO. 114 OF 2018

CMC DI RAVENNA-KENYA BRANCH.....APPELLANT

VERSUS

THE COMMISSIONER OF DOMESTIC TAXES.....RESPONDENT

JUDGEMENT

BACKGROUND

1. The Appellant is a branch entity of Cooperativa Muratori Cementisti (CMCDI Ravenna), a company incorporated in Italy. It is registered in Kenya under the Companies Act Cap 486. It is located in Nairobi with site offices in Molo and Kuresoi. Its principal activity is the construction of dams and water treatment plants.
2. The Respondent is a principal officer of the Kenya Revenue Authority and which Authority is established under the Kenya Revenue Authority Act, Cap 469 Laws of Kenya as an agency of the Government mandated to administer and enforce all provisions of the tax laws as set out in Part 1 and 2 of the First Schedule to the Act for the purposes of assessing, collecting and accounting for all revenues in accordance with those laws.
3. CMC DI RAVENNA Italy entered into a contract with Rift Valley Water Services Board (RVWSB) for Itare Dam Water Supply Project on 15th May, 2015. The project works were to be executed by the Appellant

and were valued at Kshs. 28,900,000,000/=which was financed through a consortium of Italian Banks as an official aid funded project.

4. The Respondent conducted an audit on the Appellant's tax affairs for the years of income 2016-2017. As a result, thereof it issued a tax assessment demand on 24th March, 2018 for a sum of Kshs. 923,768,641.00 inclusive of interest and penalties made up as follows:-

a) Corporation Tax	-	766,877,170.00
b) Pay As You Earn	-	156,891,471.00
c) Value Added Tax	-	<u>323,688.00</u>
Total		<u>923,768,641.00</u>

5. The Appellant vide its letter dated 20th April, 2018 objected to the said assessment and furnished the Respondent with supporting documentary evidence to mitigate the assessments demanded. It further admitted to a PAYE liability of Kshs. 35,330,731.98.98, which amount was settled on 29th May, 2018.

6. On 19th June 2018, after revising the Appellant's objection and the documentary evidence provided, the Respondent issued its Objection Decision and reduced the tax demand to Kshs. 898,170,524.00 made up as hereunder:-

a) CORPORATION TAX	-	787,792,002.00
b) PAYE	-	110,378,522.00
c) VAT	-	333,220.00

7. Being aggrieved by the said Respondent's Objection Decision, the Appellant lodged its Memorandum of Appeal together with the Statement of Facts on 19th July, 2018.

8. Upon service, the Respondent filed its Statement of Facts on 15th August 2018.
9. Subsequently, the Appellant and the Respondent, pursuant to the directions of the Tribunal filed their submissions on 18th December, 2019 and 5th February, 2020 respectfully.
10. The Tribunal notes that after the issuance of the Objection Decision and after the Appellant had lodged the appeal, the parties engaged on an amicable settlement of the matter. As a result, the Respondent dropped the demand on Corporation Tax.
11. Furthermore, the Tribunal notes that subsequently the matter was referred to ADR whereupon the parties agreed on the PAYE tax head.
12. Consequently, an ADR Agreement was entered into on 9th of October, 2018 which culminated in the filing of a partial consent on 23rd October, 2018. The same was duly adopted by the Tribunal on 23rd November, 2018 for a sum of Kshs. 28,538,751.00.
13. In view of the foregoing, the Tribunal will not delve into the issues of Corporation tax and PAYE as they are spent. It will only proceed to determine the VAT issue.

ISSUES FOR DETERMINATION

14. In view of the foregoing, the Tribunal having respectfully considered both parties' pleadings, documentation and submissions determines that the only issue left for its consideration is as follows;
Whether the Respondent's tax assessment demand for VAT was in breach of the Appellant's legitimate expectation occasioned by its letters dated 20th December, 2016 and 16th May, 2017?

THE APPELLANT'S ARGUMENTS

15. The Appellant submitted that the funding agreement between Kenya and Italy saw it fit for the two entities to work together to see that the people of Rift Valley have their water supply and that the donor funds would not suffer transactional taxes.
16. The Appellant stated that on the basis of the Respondent's private ruling dated 20th December, 2016 and the subsequent confirmation dated 16th May 2017, the Appellant claimed input VAT in 2017 and amassed VAT credits which it used to offset Kshs. 323, 699.00 being the output VAT charged on administrative fees levied on fuel sold to its subcontractors in the Itare Dam project.
17. Furthermore, it was the contention of the Appellant that the said Respondent's private ruling is yet to be withdrawn and communicated to the Appellant pursuant to Sections 67 and 68 of the Tax Procedures Act (TPA) and in the absence of the same, the Appellant ought not be penalized as the assessment is not supported in law.
18. According to the Appellant, the interpretation of Section 68(2) of the Tax Procedures Act (TPA) should be in future tense and therefore the overriding public ruling or enacted law is to be made after the private ruling. The Appellant to buttress its arguments relied on various case law inter-alia, namely:-
 - a) Republic –vs- KRA ex parte M-kopa (K) Ltd (2018) eKLR.
 - b) Republic –vs- KRA & Anor Ex parte Fontana Limited (2014) eKLR.
 - c) Republic –VS- KRA, Kenol Kobil Limited (interested party) Ex parte Rayz Logistics Ltd (2019) eKLR.
 - d) Republic –vs- KRA & Anor Ex parte, Kenya Nut Company Ltd (2014) E eKLR.

19. The Appellant concluded its arguments by stating that by issuing the private ruling, the Respondent created a legitimate expectation that the said ruling would remain binding on the Respondent until the Respondent issued a written notice to the Appellant of its withdrawal.

THE RESPONDENT'S ARGUMENTS

20. According to the Respondent, the Itare Dam project is an official aid funded project hence any supplies made to the project are exempt for purposes of VAT pursuant to the First Schedule of the VAT Act 2013 and are not zero rated.
21. The Respondent submitted that its private rulings dated 20th December, 2016 and 16th May, 2017 were issued long after the law exempting official aid funded projects had been enacted and therefore the same were null and void **ab initio** as it cannot rewrite a law that is already legislated. Consequently, it argued that it did not matter whether it was withdrawn or not.
22. On the issue of Section 68(2) of the Tax Procedures Act (TPA) being futuristic, it stated that it is only so to the extent that there is a lacuna on the existing law and such a private ruling stands withdrawn when a law is enacted to fill the gap. According to it, there was a clear law existing by the time the said letters allegedly creating legitimate expectation were issued.
23. In conclusion, the Respondent averred that since the Appellant charges an administrative fee on the cost of fuel and charges VAT as it sells the fuel to its subcontractors and leases some of its equipment to them, the same is taxable service. Therefore, after disallowing all the input VAT, the output VAT charged by the Appellant for the managerial services of Kshs. 333,220.00 is due.

24. The Respondent submitted that in view of the foregoing arguments the Appeal ought to be dismissed with costs.

ANALYSIS AND FINDINGS

25. The Tribunal notes that the First Schedule of the VAT Act 2013, Part II, paragraph 20 states as follows:-

“The supply of the following services shall be exempt supplies.... Taxable services for direct and exclusive in the implementation of official aid funded projects upon approval by the Cabinet Secretary to the National Treasury”. The First Schedule of the said Act deals with exempt supplies while the Second Schedule deals with zero rated supplies.

26. We are in agreement with the Respondent that the Finance Act 2015 introduced Paragraphs 51 to Part 1 of the First Schedule on exemption of goods supplied to an official aid funded project and Paragraph 20 to Part II of the Schedule First Schedule on exemption of services supplied. The commencement date of the said Paragraph was 12th of June 2015 and therefore thereafter the supplies to an official aid funded project were not zero rated under the VAT Act 2013.

27. The Tribunal notes that for the years 2016 and 2017, the Appellant claimed input VAT of Kshs.146,775,160.00. However, the Appellant should not have claimed the same as its sales to Rift Valley Water Services Board were exempt. The VAT Act 2013 commenced on 1st September, 2013 whereas the contract for construction of the Itare Dam Project was entered into on 15th May, 2015 when no remission was available for the project under the repealed VAT Act Cap 476. Indeed Section 68(4) of the VAT Act 2013 lends credence to the same. It provides as follows:-

“Where a remission of tax was granted under the repealed Act in respect of any taxable goods or services, such remission was to continue for a period of five years from the date of commencement of the Act”.

28. We note that in its documentation, the Appellant argued that it applied to the Respondent for a private ruling which was given vide a letter dated 20th December, 2016 and subsequently confirmed on 16th May 2017, but purportedly withdrawn by the Respondent on 20th December 2016, with the resultant effect of treating the Itare Dam Project as tax exempt and not zero rated, albeit retrospectively.

29. Noting that the gist of the appeal is grounded on the two letters dated 16th May 2017 and 20th December 2016, the Tribunal deems it necessary to reproduce the same. The letter dated 20th December, 2016 is written by the Respondent’s representative, one J.M Ojee, Deputy Commissioner in Policy Co-ordination to the partner, Alexander Richard LLP, a representative of the Appellant. It states:-

‘I refer to your letter dated 10th November, 2016 on the above subject. This is to confirm that the “Itare Water Supply Project-Contract No. RVWSB/AD/13/1” is an “Aid Funded Project” and supplies made to the project are therefore zero rated in accordance with VAT Act 2013 as amended by the Finance Act 2015. These supplies include services provided by CMC Di Ravenna (K) Branch to the said water project and are subject to the terms and conditions of the contract. Kindly note and be guided accordingly”.

30. Similarly, the letter dated 16th May, 2017 is written by the same Respondent’s representative addressed to the same Appellant’s representative. It states that:-

‘I refer to the above matter and our letter dated 16th December, 2016. This is to confirm that supplies made to Aid-funded Projects in accordance with the VAT Act 2013 as amended by Finance Act 2015 are

zero rated. Any excess input Vat over output Vat are therefore refundable subject to verification by KRA. Please note and be guided accordingly”.

31. We note that the Appellant for reasons known to itself did not attach these letters of 10th November, 2016 and 16th December, 2016 to enable the Tribunal appreciate their full tenor and effect more especially if the alleged application for the ruling met the threshold envisaged in the relevant legislation, to wit Section 67(3) of the Tax Procedures Act (TPA).
32. Section 65 of the Tax Procedures Act (TPA) provides that a taxpayer may apply to the Commissioner for a private ruling which shall set out the Commissioner's interpretation of a tax law in relation to a transaction entered into, by the taxpayer. We note that in Section 65(6), a private ruling that is consistent with a public ruling in existence shall supersede the public ruling to the extent of the inconsistency with the public ruling. Moreover, Section 67 of the Tax Procedures Act (TPA) provides that once the Commissioner makes a private ruling, he shall notify the applicant of the ruling in writing. Similarly, Section 68(1) provides that the Commissioner may for reasonable cause withdraw a private ruling by notifying the applicant in writing.
33. On perusal of the pleadings, we note that on 30th of May 2016, the National Treasury issued a letter to the Appellant exempting goods and services supplied to Itare Dam Project from customs duty and VAT as provided for under the EACCMA 2004 and VAT Act 2013. This clearly shows that the Appellant had been given prior advice that the goods were VAT exempt. Then one would pose and ask, why was the Appellant seeking for a private ruling when the Respondent's principal had already given the required advice?

34. In view of the foregoing, we note that the alleged advice in the two letters dated 20th December 2016 and 16th May 2017 stating that the supplies made to an official aid funded project are zero rated was in contravention to the VAT Act 2013 as the same letters were issued after the law providing that such supplies were exempt was enacted.

35. It is trite law that legitimate expectation cannot be created on instances where a private ruling is inconsistent with a clear provision of law. In the Supreme Court case of **Communication Commission of Kenya & 5 others –vs- Royal Media Services Ltd & 5 others (2014) eKLR**, the court while canvassing the principle of legitimate expectation stated thus;

“ a) there must be an express, clear and unambiguous promise given by a public authority;

a) the expectation itself must be reasonable;

b) the representation must be one which it was competent and lawful for the decision-maker to make; and

c) there cannot be a legitimate expectation against clear provisions of the law or the Constitution”.

36. In view of the foregoing, it is the Tribunal’s finding that the doctrine of legitimate expectation is not applicable herein and further that the Appellant’s input VAT claim for the years 2016-2017 was lawfully disallowed by the Respondent. Consequently, the output VAT charged by the Appellant was properly brought to charge.

FINAL DECISION

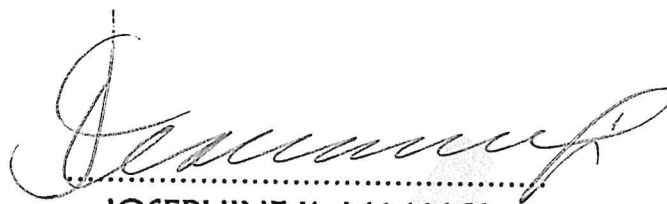
37. The upshot of the above is that the Appeal lacks merit and the Tribunal makes the following Orders:-

a) The Appeal is hereby dismissed.

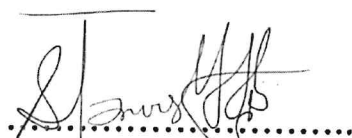
b) The Respondent’s Confirmed Tax Assessment for Kshs. 333,220.00 issued on 19th June 2018 is hereby upheld.

c) Each party to bear its costs.

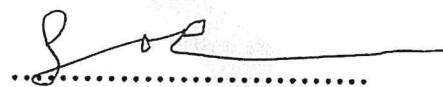
DATED and DELIVERED at NAIROBI this 21st day of August, 2020



JOSEPHINE K. MAANGI
CHAIRPERSON



TANVIR ALI
MEMBER



GEOFFREY KARUU
MEMBER

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DELILAH K. NGALA
MEMBER