



**Commissioner of Domestic Taxes v 3M Kenya Limited (Civil Appeal ITA E096 of 2021)
[2022] KEHC 12353 (KLR) (Commercial and Tax) (22 July 2022) (Judgment)**

Neutral citation: [2022] KEHC 12353 (KLR)

**REPUBLIC OF KENYA
IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)
COMMERCIAL AND TAX
CIVIL APPEAL ITA E096 OF 2021**

EC MWITA, J

JULY 22, 2022

BETWEEN

COMMISSIONER OF DOMESTIC TAXES APPELLANT

AND

3M KENYA LIMITED RESPONDENT

(Appeal from the decision of the Tax Appeals Tribunal dated 23rd April 2021 in Tax Appeal No. 505 of 2019, 3M Kenya Limited v Commissioner of Domestic Taxes)

JUDGMENT

Introduction

1. This appeal arises from the decision of the Tax Appeals Tribunal (TAT) dated April 23, 2021 in TAT No. 505 of 2019. On November 1, 2014, 3M Kenya Limited (3M Kenya), a company registered in Kenya, entered into an agreement with 3M Gulf, a company registered in Dubai. 3M Kenya was to provide 3M Gulf with marketing support services for its products within the East African Region, namely; Kenya, Uganda, Tanzania, Rwanda and Ethiopia, at a fee. On January 12, 2017, 3M Kenya applied for VAT input refund for Kshs. 934,711 for export services for the period February 2016 to January 12, 2017 under section 17 of the *VAT Act* as read with the Second Schedule to the *VAT Act*, 2013.
2. In July 2018, the Commissioner of Domestic Taxes (the Commissioner) issued a notice of intention to audit the input VAT refund claims for the period June 2015 to August 2015, November 2015, February 2016, April 2016, July 2016 and September 2016.
3. By letter dated December 21, 2018, the Commissioner disallowed the total input VAT refunds claims of Kshs. 3,938,591. Subsequently, the Commissioner issued an assessment order for Kshs.



22,720,762.57, encompassing principal tax of Kshs. 17,748,883.41 and interest of Kshs. 4,971,879 for the month of February 2016. 3M Kenya objected to the assessment on 8th August 2019. On 7th October 2019, the Commissioner issued an objection decision upholding the assessment.

4. 3M Kenya lodged an appeal to the TAT on November 19, 2019 and in a decision dated April 23, 2021, the TAT allowed the appeal and set aside the Commissioner's objection decision and the assessment.

This Appeal

5. The Commissioner being aggrieved with the decision of the TAT, lodged an appeal to this court through a memorandum of appeal dated June 21, 2021, raising the following 5 grounds, namely:
 - 1 That the Honourable Tribunal erred in law and in fact by finding that non-resident company 3M Gulf was the consumer of the services offered by the respondent whereas in contradiction it had also found that the services offered were meant at creating awareness of 3M Gulf's products to the Kenyan populations.
 2. That the Honourable Tribunal erred in law and in fact by finding that the respondent provided invoices requested by the appellant.
 3. That the Honourable Tribunal erred in law and fact in failing to find that there existed an agent/principal relationship between the respondent and 3M Gulf.
 4. That the Honourable Tribunal erred in law and fact in finding that the respondent did not provide marketing support services to the local distributors and/or customers of 3M products while disregarding express terms of the contract which identified the final consumer of such services.
 5. That the Honourable tribunal erred in law and fact in failing to correctly identify the user and consumer of the services offered by the contrary to the evidence presented by the appellant pointing out who the final consumer was.
6. The Commissioner prayed that the appeal be allowed with costs and that the judgment of the TAT set aside.

Submissions

7. This appeal was disposed of through written submissions with oral highlights. The Commissioner filed written submissions dated December 14, 2021 while 3M Kenya's written submissions were dated November 22, 2021.

The Commissioner's submissions

8. The Commissioner submitted that the marketing services 3M Kenya rendered were consumed and used in Kenya by schools, hospitals, offices and other institutions that 3M Kenya visited to market 3M Gulf's products. According to the Commissioner, since the marketing and advertising services were locally consumed they were subject to VAT. The Commissioner took the view that 3M Gulf could not be the consumer of its own products namely, the marketing and advertising services.
9. The Commissioner cited paragraphs 17 and 19 in decision of the case in *Commissioner of Domestic Taxes v Total Touch Cargo Holland* [2018] eKLR that the main consideration on whether the service is exported or not is the location of the consumer of the services. The Commissioner urged this court to consider who the consumer of the services offered by 3M Kenya is, and faulted the TAT for finding that the services rendered by 3M Kenya were consumed by 3M Gulf and were, therefore, exported services.



10. The Commissioner relied on Guideline 3.1 of the OECD International VAT and Gross Sales Tax Guidelines (OECD Guidelines) on the destination principle. The Commissioner further relied on Guideline 2.32 of the OECD Guidelines which provides that VAT normally flows through businesses so that the final consumer, not the business, bears the burden of tax.
11. The Commissioner contended that although the payer of the marketing and advertising services was 3M Gulf, company based outside Kenya, the services were never exported but were consumed locally by Kenyans who were the target audience and market. Applying the destination principle, the Commissioner argued, the final consumer was not the payer of the services but the local person who was targeted by the advertising service and who was influenced to make a decision to consume the 3M Gulf's products.
12. The Commissioner urged this court to allow this appeal with costs, set aside the TAT's decision dated April 23, 2021 and uphold the objection decision.

3M Kenya's submissions

13. 3M Kenya argued that the TAT correctly found that the marketing services rendered to 3M Gulf were export services. 3M Kenya relied on section 2 of the *VAT Act*, 2013 which defined an exported service as "a service provided for use or consumption outside Kenya." 3M Kenya also relied on the destination principle under Guidelines 3.2 and 3.3 of the OECD Guidelines for the proposition that the identity of the customer is determined by reference to the business agreement. 3M Kenya pointed out that even though the agreement dated 1st November 2014 refers to marketing and maintenance services; it was not disputed that the only services provided to 3M Gulf were marketing support services.
14. 3M Kenya asserted that its employees would visit hospitals, schools or other institutions and inform those institutions about 3M Gulf's products by word of mouth and did not put up any advertisements through newspapers or billboards. Once informed about those products, the companies or institutions would contact 3M Gulf directly and import the products directly. 3M Kenya made reference to invoices at pages. 187-192 of the bundle of documents showing that the invoices were sent by 3M Gulf to the companies or institutions that imported goods directly from it and not to 3M Kenya.
15. 3M Kenya maintained that the companies and or institutions did their own advertising through billboards or any other way they deemed fit. By way of example, 3M Kenya referred to page 187 of the bundle, an invoice for the billboard from Magnate Ventures, where an importing company, Window Plus EA Ltd, was advertising 3M Gulf's products. According to 3M Kenya, the basis of the Commissioner's claim was misplaced since the correct position is that the products were manufactured by 3M Gulf which was the consumer of the marketing services.
16. 3M Kenya disputed the Commissioner's argument that the marketing services were aimed at selling 3M Gulf's products. 3M Kenya again disagreed with the Commissioner's argument that the marketing services were for local use. 3M Kenya asserted that the advertising services were done on behalf of 3M Gulf and the Commissioner did not provide evidence of a single advertisement or billboards put up by 3M Kenya at the hearing before the TAT.
17. 3M Kenya maintained that the marketing services rendered to 3M Gulf were exported services. According to 3M Kenya the fact that the product may finally be consumed in Kenya did not mean that the marketing service were consumed in Kenya. 3M Kenya relied on *Coca Cola Central East and West Africa Limited v Commissioner of Domestic Taxes* (ITA No. 19 of 2013), [2020] eKLR where the court applied the OECD Guidelines and concluded that marketing services were exported services. 3M Kenya further cited para. 27 in the *Commissioner of Domestic Taxes v Total Touch Cargo Holland* (ITA



No. 17 of 2013) [2018] eKLR for the position that the customers' identity is normally determined by reference to the business agreement.

18. Reference was again made to para. 18 in *Commissioner of Domestic Taxes v W.E.C. Lines (K) Limited* (ITA No. E084 of 2020) where it was held that it was WEC BV that would benefit from the business that was marketed by the respondent. 3M Kenya urged this Court to dismiss the appeal with costs.

Determination

19. I have considered the appeal, submissions by parties and the decisions relied on. I have also perused the record of the TAT and the impugned decision. From the contestations and submissions, the issues that arise for determination are; whether the TAT was wrong in holding that the marketing services 3M Kenya rendered were export services and whether the TAT erred in holding that requisite invoices were supplied.

Whether marketing services were export services

20. The Commissioner argued in grounds 1 and 5 of appeal that the TAT was wrong in holding that 3M Gulf was the consumer and that the TAT did not correctly identify the user or consumer of the product. The issue raised here is whether the marketing services 3M Kenya rendered to 3M Gulf were export services. Put differently, who was the consumer or user of the marketing services? This issue, therefore, turns on the understanding of meaning of who the consumer or user of the marketing services was and where the marketing services were consumed and not necessarily where the services were marketed.
21. The Commissioner consistently argued before the TAT and before this court, that the services 3M Kenya rendered were consumed locally and could not be export services. 3M Kenya's position was and still is that the marketing services were exported services and were not subject to VAT. The TAT considered the issue and held that the marketing services were export services. According to the TAT, the agreement between 3M Kenya and 3M Gulf dated 1st November 2014 was for marketing and maintenance services. However, 3M had not embarked on rendering maintenance due to lack of capacity and had only concentrated on marketing services and the claim was limited in that respect.
22. 3M Kenya is a local company while 3M Gulf is a foreign registered company. The two companies entered into a marketing services agreement whereby 3M Kenya was to market 3M Gulf's products in Kenya by informing people and institutions about existence of those products with a view to attracting the would be customers to buy those products on a future date. From that agreement, there was no clause that the Commissioner pointed out to the TAT or this court that required 3M Kenya to sell any of those products. There is no doubt that this was a cross border business, which called on the applicability of the destination principle in the OECD Guidelines. The marketing services were only meant to bring people's awareness to the existence of those products and as a result, only 3M Gulf stood to benefit from that awareness and was the consumer of the service.
23. The TAT appreciated this fact and its decision captured the essence of the agreement between 3M Kenya and 3M Gulf and the services to be rendered when it stated:
 - (25) The appellant was contracted by 3M Gulf to market 3M Gulf's products in Kenya. 3M Gulf manufactures an array of items which the Appellant's employees would market to, inter alia, Hospitals and offices. Should these institutions be interested in purchasing these items, the same would be provided to them by 3M Gulf or independent distributors of 3M Gulf.



24. It is clear from the above statement that the TAT understood the nature of the relationship between the two entities. It is from that understanding that the TAT further stated:
- (28) ...yes, the marketing services by the Appellant were aimed at creating awareness of 3M Gulf's products to the Kenyan population, after all that is the object of marketing. However, actual benefit from this marketing, accrued to 3M Gulf who sold its products either directly or through distributors to the Kenyan populations. Inevitably therefore, these services qualify as export services in accordance with the provisions of the VAT Act 2013 and as such are zero rated.
25. The argument by the Commissioner that the TAT was wrong to hold that 3M Gulf was the consumer of the marketing services or that the TAT failed to correctly identify the user or consumer of the services cannot find support even from a logical argument regarding that relationship.
26. Section 2 of the repealed *VAT Act* 2013 did not define the word "consumer" or "user." However, a long line of decision of this court show that in a relationship like that between 3M Kenya and 3M Gulf, marketing services are consumed by the entity that commissions the contract depending on the location of entity commissioning the marketing services and not the entity that markets the services.
27. Dealing with a similar issue in *Google Kenya Limited v Commissioner of Domestic Taxes* (ITA No E 004 of 2021 (Consolidated with) *Commissioner of Domestic Services v Google Kenya Limited* (ITA No. E006 of 2021) (unreported), and after considering the OECD Guidelines on the issue and the statute then in force, this court stated:
- (39) The Marketing services were commissioned by Google Ireland with the ultimate goal of increasing sales. This fact was appreciated by the TAT in its decision, that the Marketing and services would ultimately increasing sales in Kenya and, therefore, both Google Kenya and Google Inc. were the beneficiaries. In this respect, the TAT correctly found that the consumer of the service is the person contracted to receive the benefit from the service and Google Inc. and Google Ireland were to benefit from the R&D and marketing services respectively.
- The court went on to state that:
- (42) ...There was no sale of Google Ireland's services to people in Kenya at the time of marketing of the services. Use or consumption of any of the marketed services would come at a later date, if and when, those products were offered for sale and the people persuaded or attracted, agree to take up Google Ireland's marketed services.
- (43) This view is informed by the fact that even after marketing of the services, there was no guarantee that people in Kenya would take up the products once offered for sale. Marketing of services cannot be taken to be sales because, quite often, products being marketed are given free of charge to persuade potential customers to take up the products or services at a future date. Those members of the public do not become consumers of those marketed services.
28. The Commissioner's argument that the TAT was wrong in holding that 3M Gulf was the consumer of the services or that the TAT did not correctly identify the consumer of the products cannot find favour here. (See also *Commissioner of Domestic Services v Total Touch Cargo Holland* [2018] eKLR; *Coca-Cola Central East and West Africa Ltd v Commissioner of Domestic Taxes* [2020] eKLR and *Panalpina Air Flow Limited v Commissioner of Domestic Taxes* [2019] eKLR)
29. Flowing from the analysis above, I find no merit in the complaint against the holding by the TAT that 3M Gulf was the consumer of the marketing services and that the marketing services were export services.



Whether requisite invoices had been supplied

30. The Commissioner again complained in ground 2 of appeal that the TAT was wrong in finding that 3M Kenya had provided the invoices required. I have read the impugned decision and in particular, paragraphs 20 and 21. The TAT observed at paragraph 20 that the Commissioner's letter dated December 21, 2018 at item (1), made reference to the invoices as the basis for concluding that 3M Kenya had under declared sales and indeed reproduced verbatim what was captures in that item.
31. At paragraph 21, the TAT also stated that the Commissioner's witness, a Mr. Maina Ndirangu, had admitted during the hearing that invoices had been supplied. The TAT concluded, therefore, that 3M Kenya had supplied the requisite invoices. With this finding of fact, and bearing in mind that this court is sitting on appeal and did not see the witness testify, there is no reason to fault a finding of fact by the TAT that invoices had been supplied.
32. The commissioner faulted the TAT for failing to find that there existed agent principle relationship between 3M Kenya and 3MGulf. I do not think the issued could be that of agent principle. The concern here was on the marketing servic3s agreement and whether the services were consumed locally or in a foreign company to amount to export services, which calls for determination whether OECD Guidelines applied and the answer is, yes; the OECD Guidelines on destination principle applied. The services rendered by 3M Kenya were for the benefit of 3M Gulf who was the consumer of the marketing services.

Conclusion

33. Having considered this appeal, submissions and the decisions relied on, and after a careful reevaluation of the evidence on record and analyzing it myself, I am unable to find error in findings and conclusions reached by the TAT that 3M Gulf was the consumer of the marketing services, that the marketing services were export services and that requisite invoices had been supplied. Consequently, this appeal fails and is dismissed with costs.

DATED, SIGNED AND DELIVERED AT NAIROBI THIS 22ND DAY OF JULY 2022

E C MWITA

JUDGE

