Koncar-Power Plant & Electric Traction Engineering v Kenya Revenue Authority (Income Tax Appeal E010 of 2022) [2024] KEHC 12716 (KLR) (Commercial and Tax) (17 October 2024) (Judgment)

Neutral citation: [2024] KEHC 12716 (KLR)

REPUBLIC OF KENYA

IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)

COMMERCIAL AND TAX

INCOME TAX APPEAL E010 OF 2022

WA OKWANY, J

OCTOBER 17, 2024

BETWEEN

KONCAR-POWER PLANT & ELECTRIC TRACTION ENGINEERING ..... APPELLANT

AND

KENYA REVENUE AUTHORITY ..... RESPONDENT

((An Appeal from the judgement of the Tax Appeals Tribunal delivered on 17th March, 2023 in Tax Appeal Tribunal No. 820 of 2021))

JUDGMENT

1. The Appellant herein, Koncar Power Plant & Electric Traction Engineering Inc., is a company incorporated in Croatia and has registered a Kenyan branch under certificate of compliance. The Appellant teamed up with another foreign company (Litostroj and entered into a contract with Kenya Electricity Generation Company Power Limited (Kengen) for the provision of highly specialized works at its Kiamburu Power Plant.

2. The Respondent is a government agency established under the *Kenya Revenue Authority Act*, Cap 469 Laws of Kenya. Under Section 5 (1) of the said Act, the Respondent is an agency of the Government for the collection and receipt of all revenue. Further, under Section 5 (2) of the Act, with respect to the performance of its function under subsection (1), the Authority is mandated to administer and enforce all provisions of the written laws as set out in Part 1 & 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. The iTax system detected inconsistency between the invoices used by the Appellant for VAT input claim and the VAT sales declared by various suppliers.

4. On 15th November 2019, the Appellant was auto assessed for VAT inconsistencies arising from its input taxes claimed in VAT returns filed for the months of January 2018 and March to May 2018.

5. The Appellant objected to the said assessment on the ground that all the invoices were correctly declared and claimed. Upon request by the Respondent for documents in support of its objection, the Appellant obliged and forwarded documents vide a letter dated 14th February 2020 for consideration by the Respondent.

6. The Respondent considered all documents and made correspondences requesting for further and specific documents for use in the review of the Appellant's objection.

7. The Respondent reviewed all the issues raised and documents provided by the Appellant, made relevant adjustments and particularly accepted the objection. To this end, the Respondent made an objection decision and issued the same to the Appellant together with a schedule of detailed analysis giving reasons for each disallowed invoice.

8. Aggrieved by the objection decision, the Appellant lodged the instant appeal at the Tax Appeals Tribunal.

9. The Tax Appeals Tribunal heard the appeal and rendered a verdict in favour of the Respondent herein on 29th October 2021.

The Appeal

10. Aggrieved by the decision of the TAT, the Appellant filed the instant appeal and listed the following grounds of appeal in the Memorandum of Appeal: -

    1. THAT the Tax Appeals Tribunal erred in law by addressing its mind to the wrong subject thereby arriving at a wrong decision.

    2. THAT the Tax Appeals Tribunal erred in law in determining that input tax incurred by the Appellant on hiring or leasing a passenger car is disallowable, when under Section 17 (4) of the VAT Act, 2013 hiring or leasing of passenger car is not among the supplies whose input tax is disallowable.

    3. THAT the Tax Appeals Tribunal erred in law in falling to understand that what is disallowed under Section 17 (4) (a) of the VAT Act 2013 is only the input tax incurred on the Acquisition of passenger cars or minibuses and the repair, maintenance thereof, including spares.

    4. THAT the Tax Appeals Tribunal erred in law in making a blanket holding that to qualify for input tax in accordance with the second part of Section 17 (d) (a), the taxpayer must be solely involved in the business of dealing in vehicles.

    5. THAT the Tax Appeals Tribunal erred in law in ignoring the provision of Section 1 7 (4) (a) in determining whether a taxpayer qualifies for deduction of input tax where the taxpayer hires or leases vehicles to make taxable supplies.

    6. THAT the Tax Appeals Tribunal erred in law by failing to read and interpret Section 17 in its entirety.

    7. THAT the Tax Appeals Tribunal erred in law when it failed to appreciate that for the service known as "hiring" or "leasing" to be excluded from input tax deduction, it should have been mentioned firstly, in the first part of Section 17 (4) (a) so that the second part would embrace

it, by use of the conjunction "unless"; and then disqualify the hiring or leasing service by dint of the Appellants nature of business.

8. THAT the Tax Appeals Tribunal erred in in not interpreting that the taxpayer referred to in the second part of Section 17 (4) (a) whose input is allowed to be deducted is only a taxpayer who acquires "passenger cars or minibuses" whose input tax would otherwise not have been deductible under the first part of Section 17 (4) (a), and not a taxpayer who incurs input tax on hiring and leasing.

9. THAT the Tax Appeals Tribunal erred in fact when it stated that the Appellant had submitted that Section 17 (1) of the VAT Act provides an exhaustive list of exceptions on deduction of input tax, when in fact the Appellant submitted at paragraph 8 that Section 17 (1) provides that input tax on taxable supplies ... be deducted by the registered person subject to the exceptions provided at the Section.

10. THAT the Tax Appeals Tribunal erred in law when it failed to understand that Section 17 of the VAT Act which is titled "Credit for input tax against output tax" is one of the Sections in the VAT Act, just like there are Sections 1 or 2 or 4 or 10 or 15 or any other Section in the Act, titled accordingly, according to the subject of the Section...

11. THAT the Tax Appeals Tribunal erred in law when it failed to interpret in totality Section 17 in the VAT Act, 2013 which deals with the issue of deduction of input tax, has several subsections under it, including Section 17 (1) or subsection (1) of Section 17; and Section 17 (4) or subsection (4) of Section 17.

12. THAT the Tax Appeals Tribunal erred in law by ignoring to put into account that Section 17 (4) of the VAT Act, 2013 had been amended by the Finance Act, 2021 by inserting the words "leasing" or "hiring", immediately after the word "acquisition" which came into effect on 1st July 2021, after hearing of the case and pending for judgement to be delivered on 29th October 2021.

13. THAT the Tax Appeals Tribunal erred in law in that, despite its full knowledge of the amendment which it highlighted at paragraph 22 on page 10 of its judgment dated 29th July 2021, it still went ahead to disallow the input tax incurred on leasing and hiring passenger cars prior to the period 31st June 2021.

11. In response to the Memorandum of Appeal, the Respondent filed its statement of facts wherein it explains the genesis of the case and states that: -

1. THAT, the Appellant, as well as M/S Litostroj Power Plant sends its highly specialized a staff from Croatia and Slovenia respectively to Kenya at various stages of the contract to perform the contract.

2. THAT, due to the strict deadlines set out in the contract and the remote location of the project, the foreign specialists have to be accommodated at the site, or the nearest available accommodation.

3. THAT, to facilitate the mobility of the specialists to and from the place of work; and to facilitate the obtaining of materials mainly from Nairobi that are needed at the site, the Appellant hires or leases passenger cars from registered persons who charge it VAT as it does not have its own transport in Kenya. The drivers of the of the vehicles are employees of the hirer or lessor.

4. THAT, the passenger cars that are hired or leased are hired or leased strictly to make taxable supplies and the VAT charged by the vehicle supplier is claimed in the Appellant's VAT returns (as well as the VAT returns of Litostroj Power Ltd respectively), in accordance with the provisions of Section 17 (1) of the VAT Act 2013 up to the date of amendment of Section 17 (4) of the VAT Act 2013, on 1st July 2021.

5. THAT, on 15th November 2019, the Respondent issued to the Appellant four Assessment orders for various VAT tax periods disallowing inter alia, some input tax claimed in the Appellant's returns, and upon objection to the Assessments on 28th November 2019, the Respondent required the Appellant to produce various documents as proof against the disallowed invoices which were produced by the Appellant on 20th February 2020.

6. THAT, on 10th July 2020, the Respondent communicated his Objection Decision to the Appellant which was resolved to the satisfaction of the Appellant save for the input tax incurred by the Appellant on hire or lease of the aforesaid passenger cars that the Respondent had disallowed and advised the Appellant to appeal to the Tax Appeals Tribunal.

7. THAT, the Respondent explained to the Appellant that it had disallowed the input tax on hire of the passenger cars on the grounds that the deduction of claimed input tax on the hiring of passenger cars is prohibited by Section 17 (4) of the VAT Act, 2013.

8. THAT, the Respondent had similarly disallowed the input tax incurred by Litostroj Power Ltd aforementioned and the company appealed to the Tax Appeals Tribunal.

12. The Respondent urged this court to dismiss the appeal.

13. The Appeal was canvassed by way of written submissions.

The Appellant's Submissions

14. The Appellant submitted that due to the strict deadlines set out in the contract, and the remote location of the project, the foreign specialists had to be accommodated at the site or nearest available accommodation. It was stated that in order to facilitate the mobility of the specialists to and from the place of work, and to also facilitate the obtaining of any materials mainly from Nairobi that are needed at the site, the Appellant hires or leases transport from tax registered persons who charge it VAT, as it does not have its own vehicles in Kenya.

15. It was submitted that the transport hired or leased is strictly to make taxable supplies and the VAT input tax charged by the transport supplier is claimed in the Appellants VAT returns. The Appellant observed that it is this input tax, incurred on leasing or hiring of passenger vehicles claimed in the Appellant's returns which has been disallowed by the Respondent that is the subject of this Appeal.

16. The Appellant isolated the issue for determination to be whether, before the 1st July 2021, a tax payer could, under the law as it was then under section 17 (4) VAT Act 2013, deduct input tax relating to leasing and hiring, of passenger cars or minibuses and the repair and maintenance thereof including spares

17. It was the Appellant's case that the Tribunal erred in law in holding that the input tax incurred by the Appellant on hire or lease of the vehicles is disallowable under section 17 (4) (a) of the VAT Act 2013.It was further the Appellant's case that section 17 (1) of the Act provides that input tax on a taxable supply .... made by a registered person may, at the end of the tax period in which the supply occurred, be deducted by the registered person, subject to the exceptions provided under the section. The Appellant noted that 17 (4) (a) of the Act provides a list of exceptions referred to in section 17

(1), for the supplies on which the input incurred thereon is not deductible, being, input tax incurred on acquisition of: -

i. Passengers cars or minibuses - being Goods; and

ii. The repair and maintenance thereof, including spare parts - being Services.

18. The Appellant submitted that that the list of exceptions with respect to which no input tax is deductible is exhaustive and is limited to "passenger cars and minibuses and the repair and maintenance thereof including spare parts" being the only goods and services respectively, with respect to which no input tax is deductible.

19. The Appellant faulted the Respondent for creating its own law in addition to the above exhaustive list contrary to the known principles of interpretation of taxation statutes. Reference was made to the English case of Cape Brandy vs. IRC (1921) KB 64, p 71, where RowlattJ. said:

> " In a taxing Act, one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax. There is no presumption as to tax. Nothing is to be read in, nothing is to be implied. One can only fairly look at the language used."

20. The Appellant cited the law amended on the 1st July 2021 to enlist leasing and hiring as input tax disallowable with effective date being the 1st July 2021 and noted that this case was active way back in the year 2020 and that as at the time the impugned decision was being made, the law had not been amended to include input taxes incurred on leasing and hiring as disallowable. It was submitted that all the laws cannot be effective retroactively unless it is specified on its effective date and that the amendments to the law effective 1st July 2021 were not defined to act retrospectively. According to the Appellant, it naturally follows that the Respondent could not disallow deduction of input taxes incurred on leasing and hiring in the year 2020. The Appellant observed that the law, as it were (V.A.T Act section 17 (4) 2013 was amended by Finance Bill of 2021 which enactment brought in an amendment to section 17 (4) by inserting the words leasing or hiring, immediately after the word acquisition.

21. The Appellant's case was that the effect of the amendment is not only to bar the deduction of input tax incurred on the acquisition of passenger cars and minibuses, and their repair and maintenance thereof including spares, but also to bar the deduction of input tax incurred on "leasing or hiring" of vehicles with effect from 1st July 2021.

22. It was submitted that the Tribunal was in error in adding leasing or hiring to the term acquisition which merely means purchase and that had leasing and hiring been included, the legislature would not have taken trouble to amend section 17 (4) to include leasing and hiring after the words acquisition and since leasing and hiring were not among the supplies whose input tax is disallowed before the 1st July 2021, Appellant was properly entitled to it.

The Respondent's Submissions

23. The Respondent submitted that the Tribunal correctly determined that the Appellant did not qualify for deduction of input tax under Section 17 (4) (a) of the VAT Act. The Respondent noted that the Appellant had claimed invoices which related to the hiring of passenger cars as well as invoices relating to hiring of private cars which is expressly prohibited under Section 17 (4) of the VAT Act.

24. The Respondent further submitted that the deduction of input tax incurred on leasing or hiring of passenger cars is prohibited by Section 17 (4) of the VAT Act which provides that;

> 17 (4) A registered person shall not deduct input tax under this Act if the tax relates to the acquisition of—
>
> (a) passenger cars or mini buses, and the repair and maintenance thereof including spare parts, unless the passenger cars or mini buses are acquired by the registered person exclusively for the purpose of making a taxable supply of that automobile in the ordinary course of a continuous and regular business of selling or dealing in or hiring of passenger cars or mini buses; or
>
> (b) ...

25. The Respondent's case was that the Appellant's input tax would only be allowed if they had exclusively hired the passenger cars for the purposes of making a taxable supply of that automobile in the ordinary course of a continuous and regular business of selling or dealing in or hiring of passenger cars or mini buses.

26. The Respondent further submitted that the Appellant's regular business was not hiring of passenger cars as the reason for hiring the vehicles was to transport its foreign specialists to and from the place of work and that the Appellant was therefore not entitled to claim the input tax.

27. The Respondent observed that since the word acquisition/acquire is not defined in the VAT Act, the ordinary meaning of the word is attributed to it.

28. The Respondent submitted that the ordinary meaning of the term "acquisition" means buying or gaining possession of property which encompasses leasing and hiring services.

29. The Respondent submitted that the Tribunal was correct in holding that in order to qualify for input tax in accordance with Section 17 (4) (a) of the VAT Act, the Appellant must solely be involved in the business of dealing with vehicles.

30. The Respondent submitted that the Appellant does not qualify for deduction of input tax under Section 17 (4) (a) of the VAT Act prior or after the amendment by the Finance Act, 2021 owing to the fact that they are not involved in the business of dealing with vehicles and that their taxable supply is not dealing with automobiles.

Analysis and Determination

31. I have carefully considered the Record of Appeal and the parties' respective submissions. I find that the main issue for determination is whether the TAT arrived at the correct verdict in disallowing the input tax incurred by the Appellant on hiring or leasing passenger cars.

32. The Appellant's case was that owing to the nature of its work, the remoteness of the location of the project and the strict timelines set out in the terms of the contract, the foreign experts had to be accommodated at the site or nearest available accommodation. The Appellant added that to facilitate the mobility of the specialists to and from the place of work and to facilitate the obtaining of materials, mainly from Nairobi, that were needed at the site, the Appellant hired or leased transport from tax registered persons who charged it VAT, as it does not have own vehicle in Kenya.

33. The Respondent, on the other hand, argued that the hiring of passenger and private cars were expressly prohibited under Section 17 (4) of the VAT Act which stipulates as follows: -

> 17 (4) A registered person shall not deduct input tax under this Act if the tax relates to the acquisition of—
>
> (a) passenger cars or mini buses, and the repair and maintenance thereof including spare parts, unless the passenger cars or mini buses are acquired by the registered person exclusively for the purpose of making a taxable supply of that automobile in the ordinary course of a continuous and regular business of selling or dealing in or hiring of passenger cars or mini buses; or
>
> (b) ...

34. The Respondent maintained that the Appellant's input tax would only have been allowed if they had exclusively hired the passenger cars for purposes of making a taxable supply of the motor vehicles in the ordinary course of a continuous and regular business of selling or dealing in or hiring of the vehicles.

35. It was the Respondent's case that the Appellant's regular business did not entail the hiring of passenger cars as the vehicles were hired to transport foreign specialists to and from work and therefore not eligible to claim the input tax.

36. The TAT made the following findings on the issue of hiring and leasing of vehicles by the Appellant: -

> " 24. Our task therefore is to determine whether the Appellant is entitled to the input tax deduction. Notably, this is not the first time the Honorable Tribunal as currently empaneled is dealing with the issue of deductions under Section 17 (4) (a) of the VAT Act 2013. In Tax Appeal No. 306 of 2020, Litostroj Power Limited vs Commissioner of Domestic Taxes, the Tribunal found that Section 17 (4) (a) can be divided into two parts; one part listing the exceptions to deduction of input tax and the second part allowing for inputs; all relating to the 'acquisition of passenger cars and minibuses'. [n the first part of the Section, the Act prohibits the deduction of input tax if the same relates to the acquisition of passenger cars or minibuses and the maintenance thereof including spare parts. The second part of Section 17 (4) (a) allows for deduction of input tax where a taxpayer acquires "passenger cars or minibuses exclusively for the purpose of making taxable supply in the ordinary course of a continuous and regular business of selling or dealing in hiring of passenger cars or minibuses".
>
> 25. The question remains, who falls under the deduction category of the Section, and more importantly, does the Appellant herein qualify for the said deduction. We are obliged at the onset to affirm the Respondent's argument that the Appellant herein does not qualify for deduction of input tax under Section 17 (4) (a) of the VAT Act 2013. In our humble view, to qualify for input tax deduction in accordance with the second part of Section 17 (4) (a) of the Act, the taxpayer must be solely involved in the business of dealing in vehicles; that is, their taxable supply is dealing in automobiles. As such, the taxpayers who stand to benefit from the deduction under Section 17 (4) (a)

are car dealerships as opposed to individuals who simply hire or lease cars from this dealer."

37. My finding is that the TAT correctly interpreted the import of Section 17 (4) of the VAT Act which is very clear on the circumstances under which input VAT may be deducted in respect to the hiring and leasing of vehicles. I find that the Section clearly states that such a claim can only be made where the hiring or leasing of motor vehicles is for the purpose of making a taxable supply in the ordinary course of continuous and regular business of selling or dealing in hiring of passenger cars or minibuses.

38. In the instant case, I find that the Appellant's regular or ordinary business was not the making of taxable supply or a dealer in hiring or selling of passenger cars or minibuses. I therefore find that Section 17 (4) was not applicable to the Appellant. It is trite that tax laws are to be given their ordinary meaning.

39. For the reasons that I have stated in this judgment, I find that the instant appeal is not merited and I therefore dismiss it with no orders as to costs.

40. Orders accordingly.

JUDGMENT DATED, SIGNED AND DELIVERED VIRTUALLY VIA MICROSOFT TEAMS THIS 17TH DAY OF 2024.

W. A. OKWANY

JUDGE