

**TO CHARGE VALUE  
ADDED TAX OR NOT ON  
TRANSPORTATION OF  
COFFEE FOR EXPORT?**

***JARS TRANSPORTERS  
LIMITED -VS-  
COMMISSIONER OF  
DOMESTIC TAXES: TAX  
APPEAL NO. 1432 OF 2022***

## I. BACKGROUND

This dispute relates to the treatment of the transportation of coffee for purposes of Value Added Tax (VAT)

The brief facts of the case are that the Jars Transporters Limited, the Appellant herein, engaged in the business of transportation of coffee and gunny bags. Based on its nature of business it was the Appellant's position that its supply of transportation services for coffee was zero rated and fell within Paragraph 4 of the Second Schedule of the VAT Act being the ***“supply of coffee and tea for exports to coffee or tea auction centers”***.

As for the Kenya Revenue Authority, the Respondent herein, it noted that it had undertaken a credit verification exercise which allegedly revealed that the Appellant had been filing for VAT credits but declared sales as either being zero rated instead of standard rated.

According to the Respondent, Paragraph 4 of the Second Schedule only envisaged the supply by the owner of the coffee and not the contracted transporter who did not directly export the coffee. The Respondent reviewed the VAT assessments and set aside assessments in respect of supplies to SEZ and time-barred assessment but confirmed the VAT assessment in the amount of **Kshs. 16,199,529**.

Based on the above divergent positions by the Parties, the Tribunal concluded the issues thereto as analyzed below:

## II. ISSUE FOR DETERMINATION

Whether the transportation services for coffee as provided by the Appellant formed part of the supply of coffee for export hence subject to zero rating under Paragraph 4 of the Second Schedule of the VAT Act?

## III. APPELLANT'S ARGUMENTS

The Appellant's arguments were as follows:

- i. That the transportation of coffee to the warehouse fell within the meaning of “supply of coffee for export” as provided under Paragraph 4 of the Second Schedule of the VAT Act;
- ii. That the ultimate consumer or place of use of the services in respect of the coffee was outside Kenya hence the transportation services were incidental to the supply of exported coffee and hence were exported services.

- iii. That the transportation of coffee was an auxiliary or preparatory activity and that the transportation element formed part of the commodity for export;

- v. That the coffee remained in the ownership of the farmers during transportation hence all related costs thereof are borne by the farmers until the point of sale;

- v. That the Appellant engaged the marketing agents on behalf of the farmers to transport the coffee and pay the transport costs which are reimbursed by farmers upon the sale of the coffee to the export market;

- vi. That the international tax practice was that if the product or service itself was not taxable, any charge for shipping or delivery was also not taxable;

- vii. That since the VAT Act was silent on the VAT treatment on the transportation of coffee to the warehouses, the VAT Act thus did not bring the same to tax at the standard rate in the absence of such express provision;

- viii. That the suppliers of the coffee, that is, the farmers were not registered for VAT hence could not recover input VAT paid in the course of making such supplies;

- ix. That the transportation of coffee to a registered warehouse in Nairobi for purposes of subsequent export was a pre-requisite for the same to be catalogued for sale in the Nairobi Coffee Exchange hence it formed part of the supply by the farmer;

## IV. RESPONDENT'S ARGUMENTS

The Respondent's arguments were that:

- i. That the supply envisaged under Paragraph 4 of the Second Schedule of the VAT Act referred to the supply of goods by the actual suppliers of the goods and not contracted transporters;

- ii. That the supply by the Appellant was a supply of goods in respect of the gunny bags and a supply of services in respect of the transportation of coffee hence standard rated for VAT purposes;

iii. That the supply of transportation services by the Appellant formed part of the value chain but the coffee was not directly exported by the Appellant;

iv. That the benefit of the services provided by the Appellant was utilized by the local farmers who engaged the Appellant as the transport service was supplied locally hence subject to VAT; and

v. That the destination principle did not apply to the supplies by the Appellant as the Appellant did not export any service.

## **V. ANALYSIS OF THE TRIBUNAL'S FINDINGS**

With each Party having presented their case, the Tax Appeals Tribunal reduced the Parties' arguments to one issue for determination, that is, ***whether the transportation of coffee to auction houses for export is zero rated as per paragraph 4 of the 2nd Schedule to the VAT Act.***

The Tribunal considered that the Appellant's position was that the transport services were ancillary or essential to ensuring that the coffee for export were ready for export. However, it was the Tribunal's considered view that the transportation services were not specifically listed in the Second Schedule as zero-rated supplies hence could not be zero-rated.

The Tribunal further noted that to determine whether the service was exported, the Tribunal must determine:

- the place of consumption of the services; and
- the location of the business or recipients of the services.

Additionally, the agreements entered into by the Appellant and various entities for transportation were contracts between local entities and were in respect of transportation from one local destination to another.

Based on the above, it concluded that the end consumer of the transport services and the person that bore the costs of preparation and transportation of the coffee were the coffee farmers and not the foreign buyers of the coffee. As such, the services were not exported hence could not be zero rated for the period under review. In that regard, the Tribunal proceeded to uphold the Respondent's objection decision and dismissed the appeal.

## **VI. IMPLICATIONS OF THE JUDGMENT**

With the judgment of the Tribunal confirming the standard rating of the transportation services for coffee, the same means that for companies in the transportation industry that have previously been treating the transportation services as zero rated, they are now at the risk of assessment by KRA in a bid to collect taxes for the same.

Apart from the above, there is a likelihood that the prices for the coffee and tea for export made to auction centres will increase as the prices for transportation will now be higher and suppliers will try to pass the said costs to the consumers. This is likely to affect the competitive advantage of the coffee and tea originating from the Kenyan market against other competitors in the same industry.

Further and from the Tribunal's perceptive, the reason for not considering the zero rating of the transportation of coffee for exportation was that the same was not explicitly included as part of the zero-rated items under the Second Schedule. Based on this, it is a high time for the members of the Kenya Transporters Association to consider lobbying for the inclusion of the same under the Finance Act, 2024 so as to protect their future interests especially for those transporting coffee and tea for export to auction centres.

## **VII. TAX CONTROVERSY**

A critical look at the arguments by the Appellant more so on the fact that the transportation services were incidental to the supply of exported coffee and hence were exported services and also noting the argument that the transportation of coffee was auxiliary or a preparatory activity to the export of the coffee, may justify the zero-rating pursuant to Paragraph 4 of the Second Schedule.

This is backed by the argument that looking at the provisions of Paragraph 4 of the Second Schedule, the same stipulates for the zero-rating of the supply of coffee and tea for exports to coffee or tea auction centers. The transportation services provided related to the supply of the coffee for export and hence ideally auxiliary to the export of the coffee hence backing the argument for zero rating.

It will thus be interesting to see how the High Court of Kenya exercises its mind in respect of the subject matter.

**CONCLUSION**

With the judgment of the Tribunal, It is therefore prudent for taxpayers to determine if services qualify as exported services in light of the above criteria and further ensure that a supply is expressly listed in the Second Schedule to qualify for zero-rating.

**LET'S TALK**

For more information or professional advisory and compliance with regards to charge value added tax or not on transportation of coffee for export or on any other tax matter kindly contact your regular Taxwise Africa Analyst or the contacts below



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