Sagamore Hill.

TAX NEWSLETTER.

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APPLEWOOD INVESTMENT VS CDT

Background of the case.

The case involved an audit of VAT transactions for the period between June 2015 and December 2016. This was after the appellant was flagged in an credit filer verification excise carried by the Kenya Revenue Authority and a notice of intention to carry on a compliance audit issued on 10th April.

The matters of contention was on disallowing of input VAT of Ksh 7,027,855 on grounds that two invoices that had been filed on the vat returns for the period June 2017. One was dated 3rd November 2014 and the other was dated 24th January 2015 as at August 2015. The invoices were 3months and one month late respectively late for the appellant to claim input, consequently reducing their net vat and putting them in a refund position.

The VAT Act of 2013, section 17(2) clearly outlines that the time allowed to claim input VAT is six months after the end of the tax period in which the relevant supply or importation occurred.

Upon the justification of the case that the input tax claimed was erroneous, the respondent required the appellant o amend their returns and disallow the claim a stand that the appellant contested.

However, we note that the appellant claimed that the tax procedure Act allowed the respondent to amend the self-assessment and allow the appellant to claim the input within five years. The tribunal noted that the TPA doesn't have such a provision and infact the correct stand is that TPA 31 (4) (4) The Commissioner may amend an assessment—

(a) in the case of gross or wilful neglect, evasion, or fraud by, or on behalf of, the taxpayer, at any time; or

(b) in any other case, within five years of—

(i) for a self-assessment, the date that the self-assessment taxpayer submitted the self-assessment return to which the self-assessment relates; or

(ii) for any other assessment, the date the Commissioner notified the taxpayer of the assessment.

Further comment of assessment;

(5) Despite subsection (4)(b) (i) the Commissioner shall make an amended assessment on an application of a self-assessment taxpayer under subsection (2) if the application was submitted within the time specified in subsection (4)(b)(i).

(6) Where an assessment has been amended, the Commissioner may further amend the original assessment—

(a) five years after—

(i) for a self-assessment, the date the taxpayer submitted the self assessment

return to which the self-assessment relates; or

(ii) for any other assessment, the date the Commissioner served notice of the original assessment on the taxpayer; or

(b) one year after the Commissioner served notice of the amended assessment on the taxpayer, whichever is the later.

In the year 2020, Kenya Revenue Authority seems to have noted that there was so many cases of persons claiming VAT credits which triggered it to do verification of most if not all VAT credit claims that were consequently denying the government a lot of revenue. This, the authority stated, came in many ways such as;

1. Utilisation of invoices more than once. This triggered to concept of invoice matching using their reference numbers.
2. Under declaration of outputs and overestimates of inputs. This is via the overstating purchases and understating sales.
3. Credit notes that were falsified.
4. Utilisation of fictitious invoices.
5. Claiming of withholding VAT credits without declaration of corresponding sales.
6. Post-dating of sales invoices. This is presumably for invoices that could have been passed by time or pushing forward to periods of uncertainty where the net VAT balance would require the person to pay a lot of VAT.

<u>Under what circumstances are businesses not allowed to deduct input VAT?</u>

The VAT Act stipulates in Section 17 (4) that the following activities do not allow the registered person to deduct input VAT if it relates to acquisition of;

1. 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;
2. Entertainment, restaurant and accommodation services unless—
   a. The services are provided in the ordinary course of the business carried on by the person to provide the services and the services are not supplied to an associate or employee; or
   b. The services are provided while the recipient is away from home for the purposes of the business of the recipient or the recipient's employer.

Supplying vatable and exempt goods?

There are businesses that engage in supply of vatable and exempt goods.

These two have different treatment in VAT in that a business can claim 100 % of input VAT if it engages in supply of vatable goods and services if the input VAT was incurred wholly during the purchase of goods and service for the production of the vatable goods, save for the aforementioned two circumstances 17(2).

On the other hand, business that supplies exempt goods will not be in a position to claim any of the input VAT incurred in the production of goods 17 (16) (b) no deduction of any input tax which is directly attributable to other use.

This is not to be confused with zero rated goods where the business can claim input VAT incurred in the production of the said goods as is mostly the case with a business that does export of goods.

The challenge comes, as earlier stated, if the business deals with both exempt and vatable goods and incurs input VAT on its purchases for the production such goods. In such a circumstance, then an appropriate formula is applicable for computation of how much is to be allowed as demonstrated below.

$$\frac{\text{Total input tax paid x Taxable supplies}}{\text{Value of all supplies made.}}$$

If the fraction of the formula above for a tax period—
(a) is more than 0.90, the registered person shall be allowed an input tax credit for all of the input tax;
or
(b) is less than 0.10, the registered person shall not be allowed any input tax credit for the input tax comprising component A of the formula.

In our analysis, we note that it is important to observe the six months rule for claiming input tax and further, how to deduct the correct input incase the business egages in vatable and exempt supplies.
Find the original case law on our site here https://bit.ly/3Bh5Ynr

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