



Tax Alert



VAT treatment of supplies to foreign tour operators: A different application

In brief

This case deals with an appeal by the taxpayer (KEN CC) to the Tax Court regarding additional VAT assessments raised by the Commissioner for the South African Revenue Service (SARS). This judgment, unless appealed by SARS and overturned by the Supreme Court of Appeal, is important for the tourism industry regarding the VAT implications for supplies to foreign tour operators (FTO).

In detail

General

KEN CC is a destination management company that provides tourism package assembly services to FTOs. For its services, KEN CC charged the FTO a commission. However, the commission was not disclosed separately on the tax invoice issued to the FTO. The commission was added onto the tour package costs recovered from the FTO.

KEN CC levied and accounted for VAT only on the commission that it received from the FTOs and did not account for any VAT on the full tour package price. VAT was additionally levied at the zero rate on the commission.

SARS disagreed with KEN CC's VAT declarations and assessed KEN CC for VAT at the standard rate in respect of the full tour package price.

The main issue in dispute was whether KEN CC supplied the actual tourism services (such as accommodation, transport and guides) to the FTOs as principal or whether it only supplied an arranging service and acted as an agent with regard to the tourism services.

Judgment

In coming to its conclusion, the court considered the witness' testimony, the factual background, previous cases and relevant SARS publications in addition to section 11(2)(l) of the VAT Act.

SARS' basis for its assessments was that the taxpayer was not an agent but rather a principal selling tourist packages to FTOs who in turn resold the same packages to individual foreign tourists. SARS regarded this to be the nature of the transactions / supplies made by KEN CC and in its view, output tax at the standard rate was leviable on the full tour package charged to the FTO.

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Let's talk

For a deeper discussion on how this issue might affect your business, please contact:

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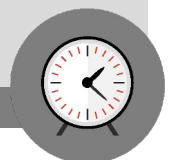
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KEN CC, however, testified that it had no assets such as hotels, buses or inventory to sell. It did not “buy” hotel rooms for on-sale and it did not take responsibility for the performance of the service by the local supplier. KEN CC merely booked these services if and when required to do so by the FTO on the FTO’s behalf. It was clear in this case that KEN CC was not involved in the actual provision of any of the services.

From a financial perspective, the transactions concluded on behalf of the FTO had no effect on KEN CC’s turnover, and only the commission earned for performing its duties was recognised as income. Further to this, KEN CC did not deduct any VAT paid to the suppliers as input tax.

The Tax Court, having regard to the above, concluded that the taxpayer’s arrangement with the local suppliers was inconsistent with the notion that it acquired and on-supplied the services to FTOs. The Tax Court was comfortable that the evidence in fact proved the contrary; that KEN CC merely facilitated the provision of the tourism services for the FTOs.

In arriving at its conclusion, the court reiterated that KEN CC was merely acting as a conduit between the FTOs and local suppliers and that KEN CC had no authority to take any decisions as to the constituent parts of tour packages.

The court referenced the recently updated Interpretation Note No. 42, which acknowledges that there are circumstances under which a vendor can act as an agent in the tourism industry. The court was satisfied that KEN CC met all of the requirements of an “agent” for VAT purposes and that there was no factual or evidential basis for SARS to treat KEN CC as a principal in supplying the tourism services to the FTOs.

The court considered SARS’ reliance on the XO Africa Safaris case* but found this to be misplaced as the facts and manner of doing business were distinguishable. In the XO Africa Safaris case, the vendor accounted for the full amount invoiced to the FTOs as its own sales and income and the invoices from local suppliers as its own expenses. The vendor in this instance deducted input tax on all its expenses and levied output tax at the zero rate on the full charge to the FTO. In the court’s view and interpretation, XO Africa Safaris conducted itself as acquiring the tourism services from local service providers (which constituted its cost of sales) which it then rendered to its own clients (the FTOs and tourists), whereas this was not the case for KEN CC. Further to this, XO Africa Safaris was responsible for providing the local services, whereas KEN CC was not.

The Tax Court concluded that this case “displays a careless disregard of the particular nature and modus operandi of KEN CC’s business, which emerges from even a rudimentary consideration of the various documents outlined above.”

[*https://www.sars.gov.za/wp-content/uploads/Legal/Judgments/SCA/LAPD-DRJ-SCA-2016-08-CSARS-v-XO-Africa-Safaris-CC-3-October-2016.pdf](https://www.sars.gov.za/wp-content/uploads/Legal/Judgments/SCA/LAPD-DRJ-SCA-2016-08-CSARS-v-XO-Africa-Safaris-CC-3-October-2016.pdf)

Takeaway

The outcome of this case serves as a reminder to a VAT vendor that although it may operate in the same industry, its VAT treatment on supplies may differ from others within the industry, as the applicable VAT treatment will depend on the specific facts and conduct of its business.

This case further serves as a reminder for vendors of the very important principle that VAT is a transactional tax and the correct treatment must be determined with reference to the contractual arrangement between the parties (refer to the *SARS v Respublica (Pty) Ltd** case).

To determine the applicable VAT treatment of a vendor’s supplies, it is therefore crucial to understand the vendor’s business operations clearly and to take note of any distinguishing factors that might result in a different application of the law.

The next PwC Synopsis publication will provide a more detailed analysis and discussion of the principles of this case.

[*https://www.sars.gov.za/wp-content/uploads/Legal/Judgments/SCA/LAPD-DRJ-SCA-2018-07-CSARS-vs-Respublica-Pty-Ltd-12-September-2018.pdf](https://www.sars.gov.za/wp-content/uploads/Legal/Judgments/SCA/LAPD-DRJ-SCA-2018-07-CSARS-vs-Respublica-Pty-Ltd-12-September-2018.pdf)



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