Tax & Exchange Control

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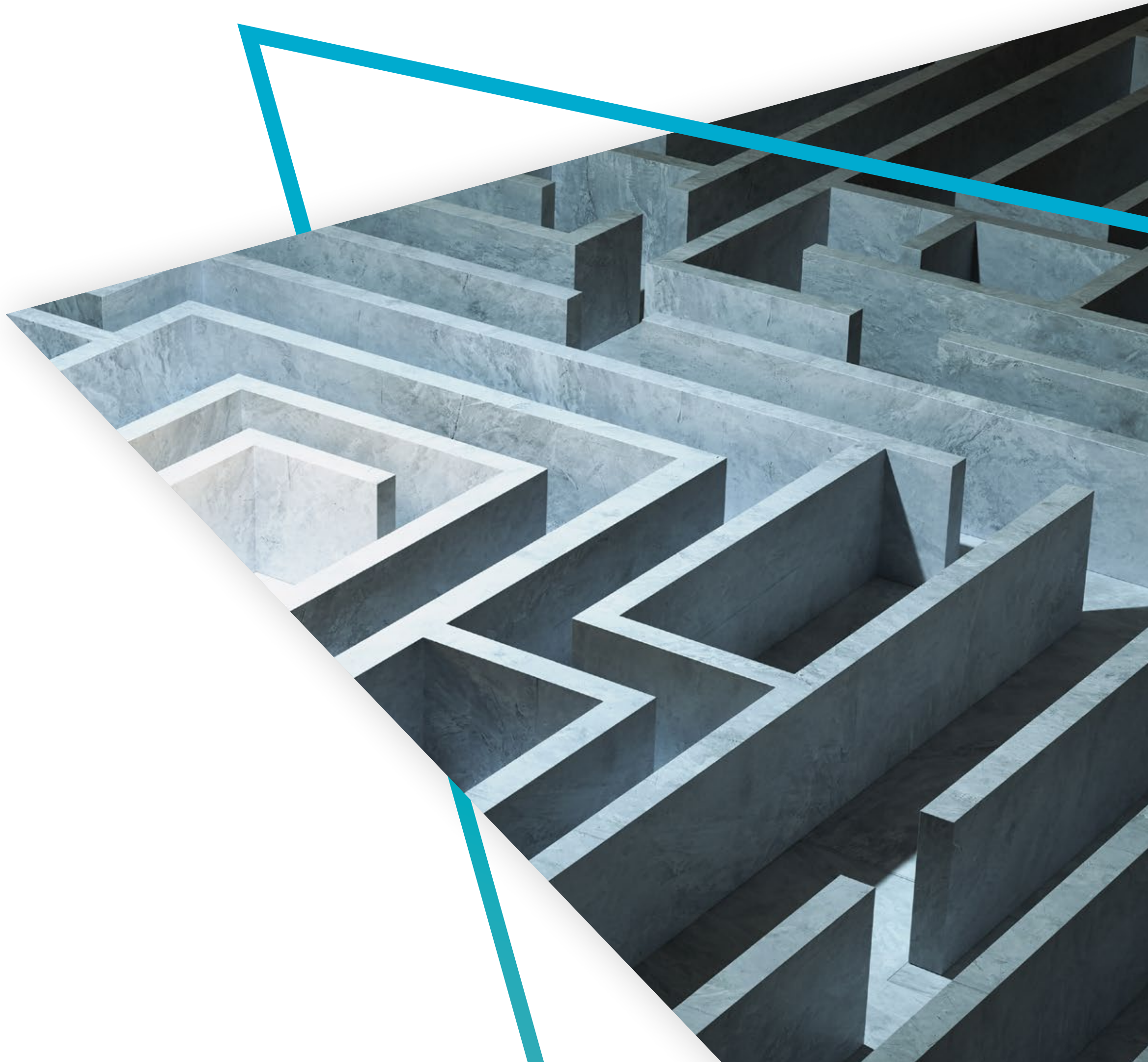

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Value-added tax in land transactions: Lessons from the *Sayani Investments* case

The charging of value-added tax (VAT) on the sale of land, whether developed or undeveloped, has long been a subject of contention in Kenya's tax regime. In the recent case of *Sayani Investments Limited v Commissioner of Legal Services & Board Coordination* (Tax Appeal E448 of 2023), the Tax Appeals Tribunal (Tribunal) provided much-needed clarity on this issue. The Tribunal held that for VAT purposes, the sale of land, including land with a structure (whether a commercial or residential building), is exempt from VAT under Part II, Paragraph 8 of the First Schedule of the VAT Act (Cap.476). This landmark decision highlights the importance of carefully interpreting tax provisions to ensure compliance and avoid unnecessary disputes.

Brief facts

In this case, the appellant, Sayani Investments Limited, owned a plot of land with a dilapidated commercial building. After receiving a notice from the Public Health Department to rehabilitate the property, Sayani opted to demolish the structure and redevelop the land. Before redevelopment began, a potential buyer expressed interest in purchasing the land. The resulting sale agreement included a condition that the building had to be demolished before the transaction could proceed. Sayani classified the transaction as a sale of land, which is exempt from VAT, and paid capital gains tax (CGT) on the proceeds. However, the Kenya Revenue Authority (KRA) disagreed, arguing that VAT should apply since a commercial building still existed when the sale agreement was executed. According to the KRA, the sale of commercial property, including the structure, was subject to VAT under the VAT Act.

This disagreement led the parties to seek resolution at the Tribunal, following the partial resolution of other tax matters through alternative dispute resolution.

Findings of the Tribunal

The central issue before the Tribunal was whether the sale of the land, which included a precondition for the building's demolition, qualified for VAT exemption under the VAT Act.

In its deliberations, the Tribunal considered several key points:

Legal definition of land

Referring to the Constitution of Kenya, 2010, the Tribunal emphasized that "*land*" encompasses both its surface and sub-surface. Therefore, whether land is developed or undeveloped does not alter its fundamental nature.

Plain language interpretation of the VAT Act

The Tribunal adopted the principle of interpreting tax statutes using their clear and unambiguous language. Paragraph 8 of Part II of the First Schedule to the VAT Act was examined, particularly the exemption in the phrase: "*Supply by way of sale, renting, leasing, hiring, letting of land or residential premises.*"

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The Tribunal noted that the commas in this provision create distinct clauses, separating the "*sale of land*" from other activities like "*letting of residential premises*". This grammatical distinction was crucial in determining that the sale of land, including the land in question, was VAT-exempt.

Sale of land v letting of commercial premises

Drawing from precedent, including the High Court's decision in *David Mwangi Ndegwa v KRA* (Civil Suit No. 541 of 2015), the Tribunal reiterated that VAT does not apply to the sale of land, regardless of whether the property includes buildings. It clarified that while the letting of commercial premises attracts VAT, the sale of land does not.

Ultimately, the Tribunal ruled in favor of Sayani Investments, finding that the transaction qualified as a sale of land and was therefore exempt from VAT. KRA's assessment was overturned.

Comment and way forward

The *Sayani Investments* decision is significant for both taxpayers and practitioners, as it reinforces the principle that tax liability is determined by the specific language of the law. The major takeaway from this case is that while the sale of land, whether commercial or residential, is exempt from VAT, the leasing or renting of commercial premises is subject to VAT.

A major point in the case was that the building on the land had no commercial value and had been condemned for demolition. The drafting of the agreement to document this fact was crucial. Careful drafting of agreements and tax advice is therefore important in commercial transactions. It could save you money.

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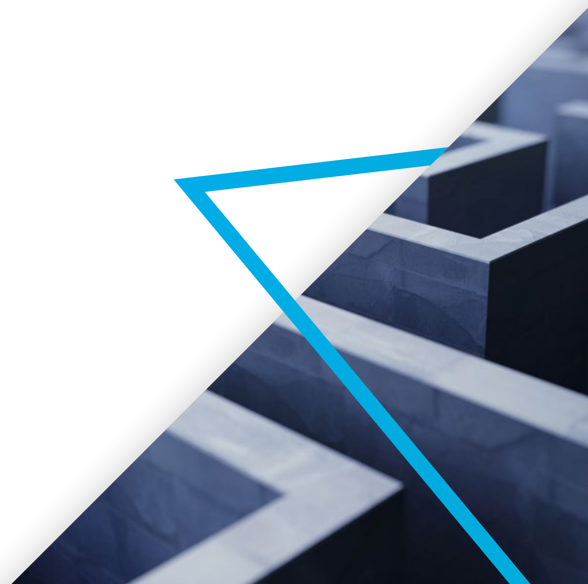

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