IN TAX THE COURT OF SOUTH AFRICA
(CAPE TOWN)

Case No.: VAT 22184

Before: The Hon. Mr Acting Justice Dickerson (President)
Ms Sunel Louw (Accountant Member)
Ms Yolisa Molefe (Commercial Member)

Hearing: 09 to 13 October 2023
Judgment: 08 December 2023

In the matter between:

KEN CC Appellant

and

THE COMMISSIONER FOR THE
SOUTH AFRICAN REVENUE SERVICE Respondent

J U D G M E N T

DICKERSON AJ

[1] The appellant ("KEN") is a close corporation and registered VAT vendor.

[2] KEN's VAT liability is governed by the provisions of the Value Added Tax Act, Act 86 of 1991 (the "VAT ACT").

[3] This matter concerns KEN's appeal to the Tax Court against additional VAT assessments raised by the respondent ("SARS").

[4] SARS issued additional VAT assessments ("the disputed assessments") to KEN in respect of its November 2013 to August 2018 VAT periods ("the disputed VAT periods"). KEN objected to these assessments under Chapter 9 of the Tax Administration Act 28 of 2011 ("the TAA"), but the objection was disallowed. KEN accordingly now appeals to this Court in terms of section 133 and following of the TAA.

[5] This Court sits as a court of revision, deciding the dispute *de novo* and exercising any powers as if it were the Commissioner.

The Central Dispute

[6] It is common cause that KEN, in the pursuit of its VAT enterprise, provides a supply of services to foreign tour operators ("FTOs"). What is in dispute is the nature of that supply, and whether it also constitutes in part a supply to the foreign tourists who subscribe to the FTO's tours.

[7] Section 7(1)(*a*) of the VAT Act, subject to certain exemptions and exceptions, requires the levying and payment of:

> "… a tax, to be known as the value-added tax—
>
> (*a*) on the supply by any vendor of goods or services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him…calculated at the rate of 15% on the value of the supply concerned ..."

[8] The term "supply" is defined in section 1 to include "performance in terms of a sale, rental agreement, instalment credit agreement and all other forms of supply, whether voluntary, compulsory or by operation of law, irrespective of where the supply is effected…".

[9] The term “services” is defined to mean “anything done or to be done, including the granting, assignment, cession or surrender of any right or the making available of any facility or advantage…”.

[10] In terms of section 11(2)(1) the supply of services, which would otherwise be charged with tax at the standard rate, is charged with tax at the rate of zero percent if: (1) the services are supplied to a non-resident; and (2) the services are not supplied directly to a person in the Republic at the time they are rendered. Section 11(2)(1) provides as follows (to the extent relevant):

> “The services are supplied to a person who is not a resident of the Republic, not being services which are supplied directly—
>
> …
>
> (iii) to the said person or any other person ... if the said person or other person is in the Republic at the time the services are rendered…”

[11] KEN contends that it provides a single supply: namely tourism package assembly services, to FTO’s which are outside South Africa when the service is rendered. The services are therefore (it contends) zero-rated under section 11(2)(1) of the VAT Act. KEN insists that it does not supply either the FTO’s or the foreign tourists with any of the accommodation, transport, guides, excursions or greeting services *(“the tourism services*”) which make up the tour packages. In accordance with this approach KEN levies output VAT only on the commissions which it charges, as zero-rated, and not on the costs of the tourism services paid by the FTOs. During the disputed VAT periods KEN submitted its VAT returns on this basis.

[12] SARS, on the other hand, maintains that KEN provides a *“supply of tour packages and related goods or services to non-resident tourists and/or foreign tour operators*”, i.e. that KEN supplies the actual tourism services rendered to the foreign tourists when they are in South Africa. On that basis, (SARS contends) subsection 11(2)(1)(iii) of the VAT Act operates to exclude the zero-rating. SARS consequently maintains that output VAT, at the standard rate, should have been levied on both (1) the commissions which KEN charges the FTOs and (2) the costs of the tourism services paid, where applicable, by the FTOs. The disputed assessments were raised on this basis.

The grounds of appeal

[13] Against the backdrop of this central dispute, KEN raises several grounds of appeal.

The Main ground of appeal

[14] The main ground of appeal turns on what KEN actually does in the conduct of its enterprise. If the grounds demonstrates that KEN's services were limited to travel package assembly services supplied to FTOs, and that the tourism services were merely booked or secured on behalf of the FTOs, the parties concur that the main ground of appeal should succeed, and the disputed assessment should be set aside.

[15] Even if KEN's main ground of appeal were to fail because the evidence does not gainsay SARS' stance that KEN acted as a principal (rather than an agent or conduit) in relation to the FTOs and therefore supplied the actual tourism services to the FTOs, there are a number of further and alternative grounds of appeal which come into play.

The first alternative ground of appeal

[16] The first alternative ground of appeal is based on subsection 8(15) of the VAT Act, which allows for different categories of a single supply to be treated separately. Section 8(15) of the VAT Act stipulates:

> "For the purposes of this Act, where a single supply of goods or services or of goods and services would, if separate considerations had been paid, have been charged with tax in part at the rate applicable under subsection 7(1)(a) and in part at the rate applicable under section 11, each part of the supply concerned shall be deemed to be a separate supply…"

[17] In this context KEN contends that the charge made by KEN to the FTO reflects three separate supplies relevant to section 8(15) of the VAT Act, namely:

(1) "tourism services" for consumption <u>in</u> South Africa (standard rated), but which KEN does not provide;

(2) "tourism services" for consumption <u>outside</u> South Africa, which are zero rated in terms of subsection 11(2)(1) of the VAT Act as neither the FTO nor the tourist is in South Africa when the service is rendered, which KEN does not provide; and

(3) travel package assembly services to the FTO (which KEN <u>does</u> provide) when both the FTO and the foreign tourists are outside South Africa, which is zero rated in terms of 11(2)(1) of the VAT Act.

[18] KEN contends, to the extent that any component of the supply is exempt from VAT in terms of subsection 12(*g*) of the VAT Act, by virtue of subsection 10(22), no VAT should be levied on the consideration received from the FTO attributable to that supply.

The second alternative ground of appeal: subsection 99(1) of the TAA

[19] The third ground of appeal arises from the resolution in 2018 of a dispute regarding four of the same VAT periods which are now in issue. In essence KEN contends that:

(1) SARS imposed VAT in respect of the four VAT periods (August 2016 to November 2016) at the standard rate on KEN's commissions – in the same way as it has done *in casu*.

(2) KEN filed objections to these assessments in terms of the dispute resolution procedures in Chapter 9 of the TAA, relying on the same arguments now put up: namely that it acted as an agent or intermediary for the FTO, and provided services to the FTO which was outside South Africa.

(3) SARS, acting in accordance with its powers under sections 106(2) and 106(3) of the TAA, upheld the objections.

(4) Consequently, because section 99(1)(e) of the TAA stipulates that "[a]n assessment may not be made in terms of this Chapter... in respect of a dispute that has been resolved under Chapter 9," SARS cannot revisit the August 20 November 2016 VAT periods as it now seeks to do.

[20] In contrast, SARS maintains that: the initial proceedings were based on an original assessment based on section 91 of TAA and following submission of the VAT returns; SARS required further documents in order to confirm or verify compliance of the invoices' with the Tax Act; and SARS conducted an audit in terms of section 92 of the TAA, which allows for additional assessments if SARS is satisfied that an assessment does not reflect the correct application of a Tax Act to the prejudice of SARS or the fiscus.

The third ground of appeal: late payment interest

[21] KEN alleges that if any part of the additional assessment is upheld, the imposition of "late payment interest" under section 39(1) of the VAT Act should not stand, and should be remitted under section 39(7)(*a*) of the VAT Act, which provides as follows:

> "Where the Commissioner is satisfied that the failure on the part of the person concerned ... to make payment of the tax within the period for payment contemplated in subsection (1)(*a*)…
>
> (*a*) was due to circumstances beyond the control of the said person, he or she may remit, in whole or in part, the interest payable in terms of this section".

[22] KEN contends that on the facts of the matter – principally having regard to the manner in which it had accounted for VAT since 1997, the disclosures made to SARS in 2005, and SARS' Interpretation Note issued in 2007 – it could not reasonably have known its failure to account for VAT on its supplies in accordance with how SARS would ultimately assess it; and the late payment was due to circumstances beyond its control and the interest should be remitted in whole.

The fourth ground of appeal: late payment penalty

[23] KEN contends that if any part of the additional assessment is upheld, reconsideration of the imposition of a "*late payment penalty*" under section 39(1)(*a*)(i) of the VAT Act is warranted and it should be remitted under section 217(3)(*c*) of the TAA.

[24] Section 217(3) refers to "percentage-based penalties" imposed under a tax Act for an amount "not paid as and when required under a tax Act". A penalty under section 39(1)(*a*)(i) of the VAT Act for late payment of VAT is such a penalty, and subsection 217(3) provides that in such a case SARS may remit the penalty if it is satisfied that: (1) the penalty was imposed in respect of a "first incidence" of non-compliance, or involved an amount of less than R2000.00; (2) reasonable grounds for the non-compliance exist; and (3) the non-compliance has been remedied.

[25] KEN contends that these three criteria are met, and that the 10% late payment penalty imposed should therefore be remitted.

The Onus

[26] Section 102 of the Tax Administration Act 28 of 2011 provides that a taxpayer bears the burden of proving *inter alia* that an amount, transaction, event or item is exempt or otherwise not taxable; the rate of tax applicable to a transaction, event, item or class of taxpayer; and/or whether a 'decision' that is subject to objection and appeal under a tax Act, is incorrect.

[27] It follows that KEN bears the onus of establishing – on a balance of probabilities – the disputed facts which are material to its appeal, and that the decision on objection and appeal were incorrect.

The evidence

[28] At the hearing 16 lever-arch files of documents running to more than 4000 pages *("the Bundle* ") was introduced into evidence.

[29] The probative value of the Bundle was agreed by the parties in the usual terms, namely that: unless evidence to the contrary has been led the documents are what they purported to be without admission as to the truth of the contents; items of correspondence were sent and received on or about the dates appearing thereon; and the documents came into existence on the dates ostensibly appearing thereon.

[30] At a pre-trial conference KEN requested SARS to agree that the tax appeal could be determined with reference to the discovered documents on the basis that they were representative of KEN's business methods and operations. SARS declined. I will return to this below, in the context of costs.

[31] It should be noted at this juncture – particularly given SARS' belated contention at the hearing that there had been inadequate production of documents – that both KEN's discovery and the preparation of the bundle of documents was conducted on the basis of representative samples of documents.

[32] At the time of effecting discovery, KEN's attorneys wrote to SARS' attorneys saying *inter alia:*

> "2. On the basis that the dispute spans a lengthy period (specifically, KEN's 2013/11 to 2018/08 vat periods) and encompasses the whole of our client's business conducted during those periods, it is impractical for KEN to discover all potentially relevant documents. The documents issued or generated in the course of conducting its business during this period exceed one million in number, as to the invoices issued by travel suppliers over the same period.
>
> 3. Accordingly, for certain categories of documents, our client has identified and made discovery of a representative sample of documents which reflects the manner in which its business is conducted. Such categories of documents are identified and expanded upon below."

This was followed by a detailed explanation of the categories of sample documents which had been discovered, whereafter the letter concluded:

> "15. We are of the view that the discovered documents provide a full picture of KEN's business methods and operations in the dispute period. KEN is of course willing to provide any further documentation specifically requested by the Commissioner that is relevant, should such documentation be within its possession".
>
> (emphasis supplied)

[33] It is common cause that there are no further documents which were requested by SARS and not provided.

[34] In addition to the documentary evidence, Ms Clean gave *viva voce* evidence on behalf of KEN. No other witnesses were called by either party.

[35] Ms Clean was a forthright, candid and impressive witness. She clearly has detailed knowledge of the nature of KEN's business and its operations, and extensive knowledge of the tourism industry.

[36] Ms Clean was not seriously challenged in respect of any of the material facts to which she testified. This was not surprising: virtually every facet of her evidence was corroborated and borne out by contemporary documents.

[37] SARS' counsel effectively challenged Ms Clean on only three aspects of her evidence questions, all of which concerned questions of inference or contention, rather than fact. In any event, the challenges proved fruitless.

(1) The first challenge concerned Ms Clean's evidence that KEN's commission was included but not disclosed in the invoices issued to FTOs. It was put to her that this indicated it was not a commission, but a "mark-up". In my mind this is a question of semantics, and was convincingly dealt with by Ms Clean.

(2) The second was a proposition put to Ms Clean that KEN had failed to produce documents reflecting any individual transactions "*from beginning to end*". This proposition was both opportunistic and disconsonant with the documents in the bundle. As Ms Clean also pointed out, no further or particular documents had been requested by SARS and refused or withheld, and SARS had moreover conducted a week-long audit at KEN's premises, where its representatives were afforded free access of KEN's records and documents.

(3) The third amounted to a proposition that KEN, by acting as a conduit between tourists and FTOs for resolution of complaints by the former whilst they were in South Africa, it was acting as a principal and rendering services in South Africa. Ms Clean testified convincingly that the function performed by KEN was essentially that of a conduit: it relayed complaints and problems raised by the foreign tourists to the FTOs, and then carried out the FTOs instructions to resolve such problems or address the issue.

[38] In consequence I have no hesitation in accepting Ms Clean as a credible and reliable witness.

The facts

[39] Given the stance adopted by SARS in relation to the assessments forming the subject matter of this appeal, it is appropriate to set out in summary form the evidence given by Ms Clean and corroborated by the documents in the bundle to which she referred, regarding the manner in which KEN conducts its business. This somewhat tedious exercise has been facilitated by KEN's comprehensive heads of argument which summarised the evidence, and in relation to which I did not understand there to be particularised or substantive factual challenges by SARS.

[40] Mrs Clean and her husband, Mr Clean are both Dutch nationals, who studied tourism at university and thereafter worked in the international travel industry.

[41] Shortly after 1994 they decided to settle in South Africa, where they identified scope for development of tourism products for the foreign tourist markets. They knew FTOs were always on the lookout to develop their own product (i.e. holiday packages) and expand their holiday destinations, and that the FTOs had not yet penetrated South Africa as a destination. They were aware of the need for an FTO to have a local tourism company to provide local knowledge.

KEN and its business operations

[42] In 1997 they founded KEN as a destination management company *("DMC'*), to exploit this need. KEN's intended role and function as such was essentially to provide local knowledge of South Africa, its services, and tourist potential, to FTOs and assist the latter in structuring tour packages for marketing and sale by the FTOs to their clients, who are foreign tourists.

[43] A DMC is a recognized actor in the international tourist industry: it is essentially an entity situate in the target country (i.e the destination) for tour packages, which the FTO intends creating and offering. An FTO relies on the DMC to serve as its "eyes and ears on the ground' and to manage its requests for information and act as a conduit for securing bookings of services on behalf of the FTO. A DMC is also referred to as a "ground operator" for an FTO, and essentially it provides the service of a "connector", with knowledge of the destination country.

[44] Since 1997 KEN has consistently performed this role and operated the same way: its service to FTOs has remained exactly the same. The only significant change in its *modus operandi* involved the introduction in 2005 of an automated Tourplan reservation system, prior to which everything had been done manually.

[45] KEN operated from offices in Hout Bay throughout and during the disputed VAT periods, with a staff comprising approximately 50 employees. Mr and Ms Clean are its executive managers, and oversee its operations. Mr Clean maintains KEN's relationships with the FTOs, who are its only clients. Mrs Clean is KEN's public officer for tax purposes.

[46] KEN has between 30 and 40 FTO clients of varying sizes. Assisting these FTOs is an everyday job, which is performed by KEN's consulting department. There are between 25 and 30 consultants, whose function is to workshop with the FTOs to create the latter's desired tour packages.

[47] KEN also has a contracting department, comprising approximately five employees whose function is to identify suitable local suppliers, negotiate rates and conclude into rates agreements on behalf of the FTOs. The contracting department maintain relationships with the local suppliers in order to negotiate the best rates with them on behalf of the FTOs.

[48] KEN also has a bookkeeping/finance department which, during the disputed VAT periods, comprised approximately three employees. This department captures the invoices issued by the local suppliers and the invoices issued by KEN to the FTOs on Tourplan. It is also responsible for preparing and completing month-end accounts and KEN's monthly VAT201 returns. KEN employs an external accountant to review its month-end accounts and produce its annual financial statements.

The Foreign Tour Operators

[49] FTOs are entities incorporated outside of South Africa (principally in northern Europe), which have no presence in South Africa, and whose clients are the foreign tourists who purchase tour packages from them.

[50] KEN's function is triggered by an FTO's request to assist in assembling a tour package for the FTO to market to its clients.

[51] KEN helps the FTOs assemble these packages by: providing on-the-ground information of local conditions and suppliers; by acting as a conduit between the FTO and the local suppliers who provide the actual tourism services (such as hotels, tours, guides etc); and by implementing the FTOs' requests regarding the standard, price, and type of accommodation, and the themes (such as a cultural aspect or sport) of the required tours.

[52] Throughout this process KEN has no contact with the foreign tourists, who are the FTO's clients, and does not sell or market any tour packages, accommodation, or services to them. KEN has no sales website, marketing arm, or other mechanism for foreign tourists or outsiders to contact it.

KEN's template Terms & Conditions letter

[53] When first dealing with an FTO, KEN issues it with a standard "Terms & Conditions" letter ("T&Cs Letter") which governs their relationship until they formalize a written agreement. If – as sometimes occurs – a written agreement is not thereafter concluded, the T&Cs Letter continues to apply. The terms and conditions of the T&Cs Letter have remained constant, also during the disputed VAT periods.

[54] The *T&Cs* Letter sets out the services KEN will provide and expressly records that it will secure the bookings on the FTO's behalf, and then only once the FTO has paid in full.

[55] KEN has 9 FTOs whose relationship is governed by the T&Cs Letter.

KEN's standard Co-operation Agreement

[56] If KEN and an FTO work together on a regular basis, they will generally execute KEN's standard "Co-operation Agreement", which supersedes the T&Cs Letter. This contract was drafted by its Cape Town lawyers in about 2005 and remains unchanged.

[57] KEN has twenty FTO clients who are party to Co-operation Agreements.

[58] In terms of the Co-operation Agreement, the FTO "hereby appoints KEN Travel as its exclusive representative in Southern Africa" to "carry out the purchase of tourist products and related bookings/reservations and payments in Southern Africa on behalf of the tour operator. This shall make KEN Travel the representative of the tour operator in Southern Africa, unless otherwise agreed as per written addendum to this contract" (emphasis supplied). The Co-operation Agreement also details what this representation encompasses, which is essentially to execute the FTO's instructions and requirements.

[59] The Co-operation Agreement stipulates that all information pertaining to the agreement "as well as all rates and commissions agreed upon between KEN Travel and the tour operator are confidential and may not be provided to any third party".

[60] Ms Clean testified that these commissions are percentage-based and are added to the cost of the tourism services before being included in a quotation and ultimately an invoice. Neither the quotation nor the invoice reveals the amount of this commission.

[61] FTOs which are more demanding and thus labour-intensive tend to attract a higher commission than those with more routine requirements. The commission percentages applicable to each FTO are loaded on the system, and can be automatically applied to any particular quote and invoice.

[62] The commissions are not disclosed in KEN's quotations and invoices for reasons of confidentiality and competitiveness, but all the FTO's know that the total amounts included in the quotations and invoices comprise both (1) the cost of the tourism service to be provided by the supplier and (2) KEN's commission.

FTO's in-house contracts

[63] Some FTOs refuse to sign a Co-operation Agreement, and require execution of their standard in-house standard agreements, to which KEN is unable to make changes if it wishes to work for that FTO.

[64] Even in these cases, however, the services which KEN provide remain the same.

KEN's services

[65] Ms Clean was at pains to emphasize that KEN's services do not comprise the assembly of tour packages, still less the provision of tour packages: its function is to assist the FTO to assemble – through a process of workshopping and connecting the FTO with appropriate service providers in South Africa – tour packages which the FTO believes will appeal to its clients, the foreign tourists.

[66] There are two types of tour packages: group travel bus tours ("*GT tours*"); and frequent individual traveller tours ("*FIT*") for individuals who travel in pairs, families, or small groups.

[67] In the disputed VAT period, FIT tours made up about 60% of KEN's business, and the remaining 40% was accounted for by GT tours.

[68] KEN establishes from an FTO, through an interactive process or workshopping, the advice and type of holiday package it requires. Once this has been ascertained, KEN furnishes the FTO with rates from the applicable local suppliers. Existing rates agreements may often have been negotiated by KEN on behalf of FTOs in advance, failing which it will obtain rates from the suppliers.

[69] KEN does not decide which local suppliers are included in a tour package: it merely advises on the suitable options available, and the FTO selects the suppliers and instructs KEN to book with these suppliers on its behalf.

[70] Once the FTO has finalised a proposed tour package, KEN advise it of the total cost by way of a quotation. The quotation combines the cost of the local suppliers with KEN's commission for all the work it has done in assisting the FTO to assemble the package.

[71] KEN, through its contracting department, introduces itself and the FTOs it represents to the local suppliers identified for potential inclusion in tours. The suppliers are notified that KEN is a DMC which acts on behalf of FTOs, and requested to provide the rates they are prepared to offer the FTO's, which KEN then proceeds to negotiate on behalf of the FTO. As a negotiating tool KEN will typically inform the local supplier of the volume of business which the particular FTO is likely to generate. The resultant agreed rate is called an "STO" (Standard Tour Operator) rate, which is a special discounted rate below the "rack rate".

[72] KEN then concludes a standard Rates Agreement ("Rates Agreement") with the local supplier, which binds the latter to maintain the agreed for a year to enable the FTO to market its package at a specified price. The period during which the Rates Agreement applies will coincide with the period during which the FTO advertise its packages.

[73] The Rates Agreement describes KEN as the "Incoming Tourism Agency", and the local supplier as "the Supplier". Often the local supplier (if large enough) will offer an "allotment" to FTOs. This is a reservation of a prearranged number of rooms for a particular FTO over a set period. These rooms are then not made available to other potential guests during that period, but because the allotment is merely a reservation, not a booking, no payment is required at this stage. FTOs require allotments for their GT tours, so that they are able to deliver to their clients the tour packages advertised in advance.

[74] Nearer to the commencement date of a tour the FTO will confirm the number of rooms it requires for that tour, and the names of the particular tourists on the tour. KEN then acts as a conduit to relay this information to the local supplier and make the bookings on the FTO's behalf.

Implementation of the tour

[75] The implementation of a tour varies, depending on whether it is a FIT or GT tour.

[76] GT tours are workshopped long in advance, and then marketed by the FTO in its brochures and on its website. If there is insufficient interest in the tour, the FTO reverts to KEN to make the tour more attractive to its clients, and workshopping resumes. If the FTO's marketing is sufficiently successful, it notifies KEN of the final number and names of its clients who have subscribed, and request KEN to confirm these with the local supplier: if there are fewer confirmations than the allotted spaces, the hotel is free to sell the remaining spaces to

others. When the FTO confirms the trip will proceed, and request KEN to confirm these with the local supplier: if there are fewer confirmations than the allotted spaces, the hotel is free to sell the remaining spaces to others. When the FTO confirms the trip will proceed, KEN thereupon issues it with an invoice.

[77] Once a workshopped FIT trip is accepted by the FTO, a similar process is followed. When the FTO receives bookings from its clients it notifies KEN. When the FTO confirms that the trip will proceed, KEN issues it with an invoice, and KEN's Tourplan system then automatically generates and sends confirmation-of- booking emails to the relevant suppliers. These are formatted in a standard layout, and all expressly state that the confirmation is "*On behalf of*" the named FTO.

[78] FTOs are required to pay KEN's invoices on issue, and before the tour starts. KEN will pay the local suppliers only after it has received payment from the FTO.

[79] After the local suppliers have been paid, KEN furnishes digital vouchers to the FTOs, which the latter issue to their clients. These vouchers serve as proof of payment (e.g. hotel accommodation) when the FTO's client, the foreign tourist, wishes to utilise the supplier's service (e.g. to check into the hotel). The voucher is linked to KEN's reservation system, which indicates which services have been paid on behalf of the FTO. The vouchers are all formatted in a standardised layout which states "*Note: Only Services listed are for KEN's account booked on behalf of:* [name of FTO]. *All extras are to be settled by clients directly*". (Emphasis supplied)

KEN's Commission

[80] KEN charges FTOs a commission for its services in workshopping and assisting in the assembly of packages.

[81] The confidential nature of the commission, and the FTO's knowledge that commission is charged, have been dealt with above.

[82] The way in which the total costs of a tour are calculated depends on whether it is a GT or a FIT.

[83] For GT tours, it is done by way of an excel spreadsheet which reflects the details of the tour. The various costs of the local supplier are inserted and the cost per person then calculated based on certain pax numbers of persons joining the tour. The commission percentage applicable to the particular FTO is then applied to the total costs, to determine KEN's commission on that tour. The cost per person (inclusive of KEN's commission) is then

calculated, and this is the amount quoted to the FTO. The excel spreadsheet is an internal document and is not provided to the FTO.

[84] For FIT tours, the rates for the specific FTO which have been finalised with the local suppliers are incorporated into KEN's Tourplan reservation system for application to that FTO's tour packages. The commission percentage applicable to that FTO is also hard-coded in Tourplan, which will therefore automatically apply it to the STO rate applicable to that specific FTO for which a tour is created on the system. The system generates a quote to the FTO, showing a globular cost or cost per service line (but not reflecting KEN's percentage separately).

[85] Ms Clean testified that the amount of com KEN's commission charges can readily be isolated in the system. This is routinely done, as the VAT returns and annual financial statements only reflect the commission as KEN's income for VAT and accounting purposes. It is possible to determine the amount charged as commission for each tour created on a Tourplan by generating a specific report reflecting this.

Layout of invoices

[86] KEN's invoice to FTOs never show the costs of the local supplier separately from KEN's commission and, depending on the FTOs requirements, either reflects a globular amount for the entire package, or the composite charge for each service line item including KEN's commission.

[87] Ms Clean emphasised that if KEN or its competitors disclosed their commission charges to the FTO's, it would invite attempts to negotiate the commission down, and undercutting by KEN's competitors.

[88] Ms Clean, based on her extensive experience in the foreign and domestic tourism industry, testified this manner of invoicing is standard practice. Industry players discuss these matters, and KEN is aware of what is being done by their competitors and sometimes sees competitors' invoices to FTOs. KEN has never received a complaint from an FTO regarding the layout of its invoices.

[89] None of this evidence was challenged or refuted by SARS. Instead, it adopted a formalistic argument, to the effect that KEN was invoking a trade usage, the evidential requirements for which were not met. I will deal with this below.

[90] SARS' counsel also put to Ms Clean that KEN's commission was in fact a "mark-up" on the cost of the local suppliers' charges. In response Ms Clean testified that one could say

that the cost of the tourism services to the FTO was "*marked up with our commission*", in other words that the direct cost was used as the basis for the commission calculation but only the total was charged to the FTO. The mere fact that the commission was not separately disclosed, she said, does not mean that it was not charged or that KEN supplied the actual tourism service at the total cost shown. There is no reason to discount this evidence: there is no clear legal distinction between a "mark-up" and a "commission", and the debate is consequently one of semantics.

[91] Before implementing KEN's Tourplan system in 2005, its accountant Ms Micha ("*Micha*") thought it prudent to confirm with SARS the acceptability of the proposed layout of the invoices. In an email sent on 15 February 2005 she provided SARS with two invoice layout options: the first showed KEN's commission separately, the second did not. She explained that KEN preferred the second layout, because a DMC's commission is confidential, and it is common industry practice not to disclose it.

[92] It is worth quoting the content of Micha's e-mail regarding KEN's *modus operandi*:

> "Please advise whether there are any specific requirements concerning tax invoices for services supplied at zero rate by an agent to a foreign principal who is not in the republic at the time the services are rendered. The agent in this particular instance renders the service of sourcing travel arrangements (including hotels, car hire, restaurants, air tickets, etc.) to a foreign principal who is a travel agent and/or tour operator in Europe and who, in turn, sells the packages to foreign tourists who enjoy the supplies in RSA. The supply of accommodation, car hire, etc. is not made by the agent and consequently no output vat is levied and no input vat is claimed on these elements, notwithstanding the fact that they are detailed on the invoice to the principal. The agent derives his income in the form of commission for the service of sourcing the components which the principal sells to his customers. Output vat is charged at zero rate on his commission. Input vats are only claimed on supplies relating to the commission earned e.g., rent, telephones, computers, etc.
>
> The vendor would prefer that the principle does not see his commission disclosed separately on the invoice. Would it be acceptable to include the commission in each line item even though it is not a mark-up as such."

[93] This explanation of the nature of KEN's business accords in all material respect with the documentary and *vivo voce* evidence before this court. In short, there was an accurate and comprehensive disclosure to SARS of the material facts.

[94] In an e-mail on 12 March 2005, SARS' VAT department responded that "SARS do not have any problem with layout two for the invoice to your clients, <u>but for your record keeping</u> it must be broken down as layout one." (Emphasis supplied)

[95] This exchange was not challenged or gainsaid by SARS during the trial, notwithstanding its allegation (in paragraph 11 of its reply to the statement of grounds of appeal in terms of rule 33) that its "approval of an invoice layout is not binding and does not constitute "full" knowledge of the nature and detail of [KEN's] business" SARS proffered no evidence or explanation as to what material aspects of the nature and detail of KEN's business and were not contained in Micha's e-mail.

[96] Consequently, SARS failed to explain why, or in what respects, its approval in 2005 of KEN's approach to invoicing was mistaken or misplaced. Whilst SARS is not bound by such approval, one would have expected some rational indication for its subsequent departure from the stance previously adopted by (presumably sentient) SARS officials in approving the invoice layout.

[97] KEN has consistently invoiced in the manner approved by SARS in 2005. In accordance with SARS' injunction regarding internal record-keeping, KEN has ensured that the amount of its commissions can be isolated in its system and reported separately.

KEN's Financial records and tax returns

[98] KEN's VAT201 returns consistently reflected its commission as zero-rated, and only claimed as a deduction the input tax paid on amount D incurred as operational expenses (e.g. rental, electricity, stationery etc). It never claimed, as a deduction for VAT purposes, input VAT charged by local suppliers. Its annual financial statements have similarly any consistently reflected its commissions from FTOs as its only income.

KEN's relationships with local suppliers

[99] Ms Clean testified that all the local service providers know KEN is an agent for FTOs. The documents routinely issued to them by KEN (for example, the introductory emails, confirmation of booking emails and vouchers referred to above) expressly and routinely say this. The local suppliers also regularly meet representatives of the FTOs, for whom it is no secret that KEN works and whose bidding it does. In addition, STO rates are often negotiated with the local supplier for specific FTOs, and the local suppliers refer to the names of the FTOs when discussing the STO rate with KEN representatives or invoicing KEN.

KEN's contact with the FTO's clients

[100] Upon arrival in South Africa the foreign tourists (who are the FTO's clients) receive a meet-and-greet service from a local supplier. which has been contracted by KEN on behalf of the FTO. These "greeters" identify themselves to the tourists as representatives of the FTO.

[101] Local tour guides are contracted by KEN on behalf of the FTOs to lead their tours. There guides received either in-person or online training by the FTOs, to ensure that their service is up to the FTO's required standard and does not damage their name.

[102] KEN has no contractual nexus with the foreign tourists, who are clients of FTOs. Nor does KEN have any contact with them whilst they are in South Africa, except for the limited purpose of serving as a conduit between the tourists and the FTO in case of emergencies or problems. The foreign tourists are given KEN's telephone number by their FTOs and advised to call KEN in case of emergency or difficulties experience in relation to the booked services.

[103] These types of situations rarely occur, but when they do any complaints or difficulties by the tourist must be dealt with by the FTO, not KEN. The latter merely serves as the conduit between the FTO and the local supplier and will convey this to any tourists who contact it directly.

Cancellations

[104] A GT tour may be cancelled if the FTO is unable to fill the bus sufficiently to make it commercially viable. It is the FTO who decides to cancel, and who instructs KEN accordingly and to cancel the allotments. The decision is that of the FTO alone and has no financial consequences for any of the parties as the rooms were merely reserved, and not booked.

[105] If an FTO cancels a tour after it has been confirmed, booked, and payment made to local suppliers on its behalf, the FTO will instruct KEN to notify the local suppliers and cancel the bookings. In such event the local supplier may be entitled to retain all or some of the payment because it kept that supply available for the FTO. The decision to cancel it is that of the FTO alone, and it bears any adverse financial consequences.

Findings on the central dispute

[106] KEN's assistance to FTOs in the assembly of tours can continue for protracted periods before the tours crystallise in accordance with the dictates and decisions of the FTO. KEN then makes the bookings on behalf of the FTO, collects payment from the FTO, and remits payment to the suppliers. Thereafter KEN has no involvement in the rendering of the tourism services between the local supplier, on the one hand, and the FTO / its clients on the other.

[107] Ms Clean also stressed that KEN has no assets such as hotels or buses, and no inventory to sell. It does not "*buy*" hotel rooms for on-sale to all comers, nor does it take responsibility for the performance of the service by the local supplier. Any complaints in that regard are directed to the FTO.

[108] KEN's arrangements with the local suppliers are therefore entirely inconsistent with the notion that it (KEN) acquires and on-supplies such services to FTOs. On the contrary, it merely facilitates the provision of the tourism services to the FTOs.

[109] SARS' heads of argument encapsulate its contentions regarding the central decisive issue as follows: "The appellants are not agents. They are principals, selling tourist packages to FTOs who in turn re-sell the same to individual foreign tourists in their respective countries. This is the nature of the transaction or, rather, the nature of supply that the appellant is engaged in."

[110] These contentions, in the light of the evidence outlined above, are untenable: the evidence plainly demonstrates that KEN's role is confined to (1) assisting the FTO's with their tour assembly and (2) providing assembly acting as a conduit between the FTOs and local supplier, for which it receives a commission. KEN does not sell tourist packages either to FTOs (as SARS contended) or to foreign tourists; it undertakes no personal or principal liability to local suppliers (all of whom are aware that it acts on behalf of FTOs'); and it plainly cannot and does not take any decisions as to the constituent parts of tour packages, whether they are to be cancelled, or the consequences of cancellation. These are all matters decided and determined solely by the FTOs, who are consequently the principals.

[111] On 2 April 2007 SARS issued an interpretation note (IN42) pertaining to the supply of goods and/or services by the travel and tourism industry. This was replaced in 2007 by Interpretation Note dated 12 December 2016, following publication of the judgment in *XO Africa Safaris v Commissioner: South African Revenue Service* [2016] ZASCA 160; 79 SATC 1.

[112] SARS' approach and arguments, in the light of the facts and evidence outlined above, is disconsonant both with the 2016 Interpretation Notes and the *XO Africa* – case.

[113] Both Interpretation Notes seek to identify the circumstances under which local entrepreneurs supplying services in the tourism industry will be viewed as acting on an agent and when they will be viewed as a principal. It is recognised that certain vendors merely act as suppliers of arranging services, and not suppliers of the tourism service themselves, whilst others may act as principals in supplying the actual tourism services. Paragraph 4.1.2 of the 2016 Interpretation Note contains the following table setting out the differences between an agent and principal from a VAT perspective:

Agent	**Principal**
Not the owner of the goods or services acquired on behalf of the principal.	Owner of the goods or services acquired on behalf of the principal by the agent.
May not alter the nature or value of the supplies made between the principal and the third parties.	May alter the nature or value of the supplies made to the third parties.
Transactions concluded on behalf of the principal will not affect the agent's turnover except for the commission or fee earned by the agent for performing the duties as agent.	The total sales represent the principal 's turnover whereas the mark-up is the principal's profit percentage. The commission charged by the agent is part of the principal 's expenses.
Only declares the commission for VAT purposes.	Declares gross sales for VAT purposes.
May issue and receive a tax invoice on behalf of the principal. The agent must maintain sufficient records to enable the name, address and VAT registration number of the principal to be ascertained.	If the agent issues a tax invoice in this instance, then the principal should not issue a tax invoice as well. Should the agent not issue a tax invoice, it remains the responsibility of the principal to issue the tax invoice.

[114] On application of the criteria set out in this table to the facts revealed by the evidence in this case, it is plain that KEN is not a principal. In particular:

(1) KEN is not the owner of the goods or services acquired on behalf of the FTO. As Ms Clean testified, KEN has no stock or inventory of rooms or services: it merely books these if and when required to do so by the FTO, and on the latter's behalf. It does not get involved in any way in the actual provision of the services.

(2) KEN stands apart from the relationship between the local supplier and the FTO, and having made the booking, may not alter the nature or value of those supplies.

(3) Transactions concluded on behalf of the FTO do not affect KEN's turnover except for the commission or fees earned by KEN for performing the duties as

agent (the assembly services). KEN reflects only the commission as its income for turnover purposes in its financial statements.

(4) It is competent, under section 54(2) the VAT Act, for an agent to receive a tax invoice on behalf of the principal as if it were the recipient of the supply. KEN maintains record of both the principal and the quantum of its commissions. KEN declares only its commission for VAT purposes, and not deduct the input tax in respect of the local supplier.

[115] KEN consequently meets all the requirements of an "*agent*" for VAT purposes as set out in the Interpretation Note. There was thus no factual or evidential basis for SARS to treat KEN as if it were the principal in supplying the actual tourism services to the FTOs: on the evidence KEN merely provides an arranging service and acts as a conduit between FTOs and local suppliers.

[116] SARS' reliance on the XO Africa – case is misplaced, because it is completely distinguishable on the facts. In particular:

(1) *XO Africa's* books of account reflected the full amounts invoiced to the FTOs as its own sales, and the invoices from local suppliers as its own expenses. It therefore understood and 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, KEN does the opposite: it does not account, either as income or expenditure, for the costs of local tourism services as it is neither the supplier nor the recipient of those services.

(2) *XO Africa 's* main witness testified that its contracts with FTO's required it to provide the local services listed in the itinerary, which the FTO purchased from it. Its main witness testified that it was entitled to deduct input VAT charged by the local suppliers. KEN, in stark contrast, is not involved at all in the provision of the services itself; has no control in that regard; and does not deal with customer complaints other than as a conduit to the FTOs.

(3) *XO Africa* was accordingly responsible for delivery of the local services during the tours. It employed consultants to supervise this. It was *XO Africa's* obligation to rectify any problems with the local suppliers, and FTO played no role in this. This is almost the converse of KEN's role.

(4) A further important distinguishing feature is that - in rejecting *XO Africa's* argument that its sole service was that of arranging the package – it was held:

> "The letter of agreement, standard terms of conditions of contract and the itinerary attached to the letter of agreement proclaimed unequivocally that XO was providing materials and services consisting of accommodation, meals, entertainment, gifts, transport and the like as specified in the itinerary. This is what XO undertook to provide to the FTO's; that is what it was paid to provide and that is what it provided."

(Emphasis supplied)

(5) KEN does not undertake to, or actually, provide the services: it merely books and arranges for payment on behalf of the FTOs. XO Africa charged FTOs at the zero rate, but (in contradistinction to KEN) also claimed the input tax on the invoices it received from local suppliers. In this regard the court rejected the argument that *XO Africa* was an agent on the grounds that it:

> "… is unsustainable because, if it is followed, it would mean that notwithstanding the fact that the services were consumed in the Republic and XO Africa would have a claim for input VAT in relation thereto, the fiscus would forego the 14% output tax levied on the supply of local services by XO Africa. This court has already held that the purpose of this provision is to ensure that when services are consumed in South Africa VAT is payable at the standard rate... "

Unlike *XO Africa*, KEN did not seek this additional 14% (or 15%) benefit by charging the FTO's a zero-rated amount whilst deducting as input tax the 14% (or 15%) VAT payable to SARS by the local suppliers and so permanently depriving the fiscus of that VAT. The same criticism cannot be levelled against KEN.

[117] In short: the approach adopted by SARS in relation to the assessments forming the subject-matter of this appeal is inconsistent with (1) the approach adopted in 2005, in which it approved the manner of invoicing based on an accurate description provided by Micha of the nature of KEN's business; (2) the criteria set out in the 2016 Interpretation Note; (3) the evidence in this case; and (4) the true import of *XO Africa*. Indeed, SARS misplaced reliance on the XO Africa – case displays a careless disregard of the particular nature and modus operandi of KEN's business, which emerges from even a rudimentary consideration of the various documents outlined above.

[118] SARS argues (in support of it contention that KEN is a principal) that for KEN to justify its failure as an agent to disclose the amount of its commission to FTOs, KEN was required to establish a "trade usage", in the sense referred to in *Golden Cape Fruits (Pty) Limited v Fotoplate (Pty) Limited* 1973 (2) SA 642 (C) at 645H, to that effect: namely a usage which is "universally and uniformly observed [trade usage] within the particular trade concerned, long-established, notorious, reasonable and certain, and does not conflict with positive law or with the clear conditions of the Contract."

[119] This argument is misplaced. A "trade usage " in this context denotes "*a custom having the force of law*"[1] which is relied on to import an implied term of the agreement.[2] Ms Clean's evidence merely sought to, and did, establish is that it is common practice in the industry to keep the amount of commissions confidential: not that this was a custom having the force of law, or as importing an implied term into KEN's contracts. There was no need to do the latter because it is an express term of KEN's contracts that a commission will be paid but is confidential. Consequently, the evidential requirements for establishing a trade usage, in the legal sense of that term of art, do not apply.

[120] SARS' further argument that KEN was not an agent, but rather a principal, vis-å-vis its FTOs because it did not disclose the amount of its commission is similarly specious. While it is generally correct that an agent who receives commission will or may be required to disclose the amount of such commission, that is not one of the essentialia of agency: it is perfectly permissible for an agent and as principal to explicitly agree that commission will be paid, but that the amount may not have to be disclosed. The evidence demonstrates that this was indeed what KEN agreed with FTOs, and Ms Clean's evidence is that agreements to this effect are standard in the industry. That is a factual question, not a matter of opinion.

[121] In all the circumstances the main ground of appeal must succeed, and unnecessary to consider the further and alternative grounds of appeal.

Costs

[122] In terms of section 130(1)(*a*) of the TAA the costs will only be awarded against a party if the Court is satisfied that the grounds relied upon by that party are unreasonable.

---

1 (as to which see generally Van Breda and Other Jacobs and Others 1921 AD 330).
2 (as to which see Golden Cape Fruits, supra at page 645G – H).

[123] It follows that SARS was grossly unreasonable in adopting the stance it did, both in relation to the challenged assessments and the stance it adopted throughout these proceedings.

[124] SARS disregarded both the facts of how KEN's business is conducted – which stand in stark contrast to the facts in the *XO Africa*-case on which SARS placed great reliance – and the criteria in its own 2016 Interpretation Note (which was evidently formulated and issued by SARS in the light of the *XO Africa*-case).

[125] No evidence was adduced by SARS in an attempt to explain or justify the stance which it adopted in the light of the known and objective facts, most if not all – of which are apparent from the documents in the Bundle. SARS seemingly recognised that the documents demonstrated a modus operandi at variance with its assessments and its contentions regarding agency: why else did it decline the request (referred to in paragraph 30 above) to agree to a determination of the appeal on the basis of the discovered documents?

[126] In consequence, it is appropriate that SARS bear the costs of these appeal proceedings, including the costs of two counsel.

[127] It remains only to consider the costs of an interlocutory application brought by KEN to compel SARS to produce its internal documents pertaining to its decision to allow the objection for the four resolved periods in 2016, in which it upheld KEN's objection to additional assessments raised on the same basis as those forming the subject matter of this appeal. Those documents were clearly relevant to the issues now before this court, inter alia because they pertained to some of the VAT periods currently in issue.

[128] SARS initially refused to provide these documents on the sole basis that they were privileged. KEN did not accept that privilege applied and brought the application to compel discovery.

[129] SARS then opposed the application on a novel and different ground: namely that the documents were protected from disclosure under the TAA as "SARS confidential information." Had this point been raised at the outset, KEN would almost certainly not have brought the application, recognizing (as it subsequently did) that it could not rationally challenge the alleged confidentiality of the information because of its lack of access thereto.

[130] Under the circumstances and given the ultimate success of the appeal (which effectively amounts to a confirmation of SARS' decision to uphold the objection to additional assessments in the 2016 VAT periods based on substantially the same grounds that form the

substratum of this agreement) it is appropriate that the costs of the interlocutory application also be borne by SARS, including the costs of two counsel where engaged.

[131] Under the circumstances the following order is made:

(a) The appellant's appeal is upheld.

(b) The VAT 217 notices of additional assessment for the appellant's 2013/11 to 2018/08 VAT periods are set aside.

(c) To the extent necessary, it is determined that during the VAT periods forming the subject matter of the above assessments, the appellant correctly zero-rated its supply of services to foreign tour operators.

(d) Respondent shall pay the appellant's costs of this appeal on the scale as between attorney-and-client, including the costs of two counsel.

(e) Respondent shall pay appellant's costs of the interlocutory application to compel discovery on the scale as between party-and-party, including the costs of two counsel where engaged.

J.G. DICKERSON
President of the Court
08 December 2023