



THE SUPREME COURT OF APPEAL OF SOUTH AFRICA
JUDGMENT

Case No: 395/15
Reportable/Not reportable

In the matter between:

XO AFRICA SAFARIS CC

APPELLANT

and

**THE COMMISSIONER FOR THE SOUTH AFRICAN
REVENUE SERVICE**

RESPONDENT

Neutral Citation: *XO Africa Safaris v CSARS* (395/15) [2016] ZASCA 160
(3 October 2016)

Coram: Navsa, Wallis, Saldulker and Mathopo JJA and Dlodlo
AJA

Heard: 5 September 2016

Delivered: 3 October 2016

Summary: Value Added Tax (VAT) – local company assembling package tours for foreign tour operators and individuals – whether supply of services attracting VAT at standard rate or whether zero rated in terms of s 11(2)(l) of Value Added Tax Act 89 of 1991 – services supplied to person not a resident of the Republic but supplied directly to other persons who were in the Republic at the time the services were rendered – VAT payable at standard rate.

ORDER

On appeal from the Tax Court, Johannesburg (Le Grange J) sitting as court of first instance):

The appeal is dismissed with costs including the costs of two counsel.

JUDGMENT

Mathopo JA (Navsa, Wallis and Saldulker JJA and Dlodlo AJA concurring):

[1] The appellant, XO Africa Safaris CC (XO), assembled tour packages for foreign tour operators (FTO's) arranging for group and individual foreign tours to this country. These packages included accommodation, travel, restaurant bookings and recreational activities, such as golf, safaris, whale watching and the like (local services). Some of the tour groups were in South Africa partly for business and partly for social purposes, in which event the packages included arranging meeting facilities and the like. XO accepted that this involved a supply of services to the FTO, but claimed that it was a supply that was zero rated in terms of s 11(2)(l) of the Value Added Tax Act 89 of 1991 (the Act). The Commissioner: South African Revenue Services (SARS) contended that these services did not fall within s 11(2)(l), but were subject to the standard rate of VAT of 14% in terms of s 7(1) of the Act.

[2] On 22 November 2010, after an audit, SARS gave a letter of audit findings to XO, indicating its intention to raise VAT at the standard rate on the supply of 'tour packages and services' to FTO's during the tax periods to February 2008 and 2009 and April 2010. XO's attorneys responded indicating that XO would object to any assessment raised on that basis. A letter of assessment to VAT, together with penalties and interest, was issued on 4 March 2011 and the promised letter of objection came on 25 March 2011. The

objection was upheld in regard to penalties and, interest, but disallowed in relation to the assessment to VAT. Aggrieved by this decision, XO took the decision of SARS on appeal to the Western Cape Tax Court (Le Grange J), which dismissed XO's case and held that XO directly supplied the local services to the FTO's and/or their customers on their behalves and accordingly VAT was payable at the standard rate. This appeal is with the leave of that court.

[3] At this stage it is necessary to set out in brief, in the paragraphs that follow, the relevant factual background. In doing so I borrow largely from the court a quo's judgment.

Background facts

[4] XO is a registered VAT vendor in terms of the Act. It operates a business involving the supply of services to FTO's which are non-resident in the Republic of South Africa. The accommodation would be used, the meals eaten and the other activities enjoyed, by the members of the tour groups assembled by the FTO's. They or, in some cases involving commercial groups, their employers would pay the FTO for the right to enjoy these services and activities. These individuals had no direct contractual connection with XO, which contracted with the FTO.

[5] According to SARS, XO contracted local suppliers to provide local services to itself and thereafter XO supplied the local services to the FTO or the FTO's customers when they were in the Republic. It did this, according to SARS, by concluding contracts for the supply of the local services with the hotels, restaurants and other providers of such services and contracting separately with the FTO's to provide those services to the members of the tour parties when they were in South Africa. When the agreements were concluded with the FTO's, neither the FTO's nor their customers were in the Republic. Once an agreement between XO and an FTO was concluded, XO arranged the local services with the local supplier if, it had not already done so, as was often the case. If prior arrangements had been made these would be confirmed. XO then invoiced the FTO for a lump sum which included the

local service provider's costs and its own mark-up. The FTO's were not advised and had no knowledge of the prices charged by the local suppliers.

[6] It is apparent that the mark-up set by XO was not fixed nor disclosed to the FTO's. The FTO's and their customers could not demand that the local supplier disclose the price it had charged. XO did not account to the FTO for the amounts which it received from them. The amounts charged by XO to the FTO were determined by reference to what the FTO was willing to pay for the local services. In its books of account, XO included the amounts invoiced to the FTO as sales and treated the costs invoiced to it by the local suppliers as expenses. In its annual financial statements the value of the services supplied by it to the FTO's was reflected in its gross revenue. XO's position in its books of account was therefore that it was acquiring services from the local service providers, which constituted its cost of sales, and included in its income amounts which it charged to the FTO's.

[7] In terms of the agreements with the FTO's it was the responsibility of XO to ensure that the local services were properly provided during the tours. XO employed consultants to make sure that the hotels and conference facilities were properly booked and set up. In the event of a problem with the local supplier it was incumbent upon XO to rectify the problem. The FTO and its customers played no role in this regard. This was because XO had a contract with the local supplier and FTO and its customers had no contract with them.

The evidence

[8] XO called three witnesses, Mr Charrieras, Ms Kimmich and Ms Mignot. Their evidence related to five group and individual leisure tours selected as typical.

[9] The documents in relation to these tours indicated that XO contracted with local suppliers to provide local services to XO. XO arranged for the local services to be made available to the FTO's customers. It is common cause that not all agreements between XO and the FTO's were reduced to writing.

The case was dealt with on the basis of these five inbound tours because they were accepted to be representative of XO's business operations and could be applied to all its dealings with FTO's.

[10] Mr Charrieras testified that although written contracts were not always concluded with an FTO, the contractual relationship between XO and an FTO was that XO would provide the local services listed in the itinerary, budget or programme provided to it, and that the FTO would purchase such services. It was his evidence that the local services were provided in the Republic. He further testified that XO's consultants were normally posted at the hotels to deal with any problems raised by the FTO's or their customers. In cross-examination he conceded that the consultants were necessary because 'that's what [XO] are paid for', to ensure that the local services were provided during the tours. It was his evidence that amongst the duties of the consultants would be to make sure that the conference facilities were correctly set up. At no stage were the complaints of the customers attended to by the hotel personnel. In relation to corporate tours the staff of XO were, on occasion, involved in checking that local suppliers were properly prepared to provide certain of the services. He said that XO had purchased the local services from the local supplier. Based on that he stated that XO was entitled to deduct input VAT charged by the local suppliers. Furthermore, his evidence continued, that in addition to the profit comprising its mark-up, XO made a further profit equivalent to 14% of the charges, because XO would claim an input VAT deduction in circumstances where XO did not pay output VAT. This, in other words, meant that if XO was not liable for output VAT charged at 14%, it was making profit at the expense of the fiscus.

[11] In cross-examination he conceded that the services were provided to the customers of the FTO when they were in the Republic, but denied that they were provided by XO.

[12] Ms Kimmich gave evidence about how XO entered into agreements with local suppliers for the services to be supplied to XO. According to her no other entity or party was involved in the agreement. The unchallenged

evidence of Ms Mignot centred mainly around her role with regard to the preparation of the documents and emails in respect of the tours arranged for an FTO called Preference Events.

[13] The emails reveal that XO was approached by Preference Events, and FTO's, to formulate a tour programme for a commercial entity, Total Lubrifiants. The programme included both business meetings and social events. It appears that Preference Events had to tender for the project because an email dated 11 November 2009 addressed to Ms Mingot by the FTO said that 'we have been selected for the Total tour' and she replied: 'I am delighted that we have won this great project together.' There was a good deal of correspondence thereafter concerning the different elements of the tour. Ms Mingot, on behalf of XO, contacted various local suppliers to arrange accommodation, restaurants and entertainment for the tour. As one might expect the programme was adjusted from time to time as the date of the tour drew near and more details emerged of the people in the tour party.

[14] On 11 November 2009 XO sent to Preference Events a detailed proposed itinerary for the tour, which was to take place from 28 March 2010 to 1 April 2010. It specified in great detail the entire programme for each day and the cost of each element of the package. On arrival in Cape Town XO would assist at the airport and greet the tour party. The first item for which a charge would be levied was portage at the airport. Provision was then made for a French speaking guide and transport in a coach to the hotel. The extent of the detail is apparent from the inclusion of an optional item of a bottle of water for each passenger on the bus to the hotel. The itinerary went on to detail gifts on arrival at the hotel, portage, and transport in the coach to the Waterfront in Cape Town. This was to be followed by a Sundowner Cruise and dinner at a restaurant in the Waterfront complex. Various options were offered under that head. Each item was separately charged for, some, such as the dinner, at a per person rate and some, such as the cruise, on a group basis. Finally, for that day, provision was made for the accommodation of the members of the touring party on a sharing basis (with the possibility of paying a single room supplement) in a hotel.

[15] The itinerary continued on that basis for each day of the proposed tour. Its closing entries are relevant. After dealing with the return of the party to Europe and what are described as 'Global services throughout the program', the notation 'End of our services' appears. The final portion deals with the cost and records that the 'Total for services quoted in ZAR' is R792 669. If the reader wanted more information about XO's general terms and conditions they were referred to XO's website.

[16] The itinerary was updated from time to time during the preparation of the tour with the final version being dated 5 May 2010, after the tour was over. It was always in the same form. Also forming part of the trial bundle before the Tax Court were the supporting invoices from the local suppliers, that is, the hotel, the restaurants and the providers of entertainment. They were all addressed to XO and were payable by XO, not the FTO. An examination of the invoices shows no consistent relationship between the prices set out in the itinerary, that is, the prices XO was charging Preference Events and the prices charged to XO by the local suppliers.

[17] In the case of the Total Lubrifiants tour a written contract was concluded on XO's standard general terms and conditions. It was accepted in argument that all the contracts giving rise to the appeal were on the same terms. They are revealing. The Letter of Agreement commences by saying that and Preference Events:

'Have agreed that XO Africa will provide and PREFERENCE EVENTS will purchase materials and services for the Programme or referred to therein ...'

The group's name is given as Total Lubrifiants and the Programme is identified as being annexed to the letter of agreement as 'annex 1 – Budget B' That is the document already described. Under the heading 'Budget' it was said that:

'The fully itemised Budget specifying all fares, prices and fees for all materials and services purchased in relation with the Programme has been attached to the present Letter of Agreement. See annex 1 – Budget B.'

Lastly, in the letter of agreement, a payment schedule was set out under which 30 percent of the initial budget was payable upon signature of the letter of agreement; a second deposit of 40 percent was payable three months before the group's departure; a deposit of 95 percent of the estimated land arrangements and air travel and charter arrangements would be paid at the latest thirty days before departure, and the final billing would be eight days after completion of the programme, that is, by 9 April 2010.

[18] Under the heading, 'General Terms and Conditions' the following appears:

'XO Africa and PREFERENCE EVENTS have agreed that for the consideration described herein, XO Africa will provide and PREFERENCE EVENTS will purchase materials and services described in the attachments for the Programme described or referred to therein (the "Programme") on the following conditions:

1. **Services:** XO Africa shall perform services listed. Services will be limited to those outlined, unless otherwise agreed to in writing.

...

3. **Prices:** Payment and consideration to XO Africa for services described herein shall be in accordance with prices listed herein, subject to terms and conditions hereof:

a. Prices stated herein have been quoted by XO Africa with respect to the Programme described herein and shall not bind XO Africa with respect to any other Programme.

b. Prices are subject to compliance with timelines outlined.

c. Prices have been based on the specified number of people and travel dates shown on this letter of agreement, and will be adjusted accordingly if the number of participants and/or dates change.

d. The quoted land prices for this Programme is based on negotiated tariffs and applicable taxes. In the event that these rates are revised by XO Africa's suppliers (transportation, carriers, hotels, guides, sightseeing contractors, etc.) or destination government prior to the operation of this Programme, XO Arica will notify PREFERENCE EVENTS of any necessary price deviations.

e. XO Africa's services are labelled in specific currencies being the South African Rand (ZAR), the Euro (€) or the US Dollar (\$) applicable to the destination of travel or the type of services to be provided. The different parts of the budgets will be invoiced in their respective applicable currencies and payment should be received as

such. [On Programmes to foreign destinations, the pricing has been calculated on a specific currency exchange rate (listed on the attached budget spread sheet), which may change prior to travel dates. As a result, XO Africa will notify PREFERENCE EVENTS of any necessary price revisions. Note that only average exchange rates will be applied. XO Africa can also offer PREFERENCE EVENTS the benefit of advance purchase options on currencies. It will however be PREFERENCE EVENTS's full responsibility to make use or not of this service.]

...

12 XO Africa: acts as agent or intermediary to arrange the means of transportation, lodging and other services as described . . .'

[19] All XO's dealing with FTO's followed the pattern set out above. That was all undisputed. It is in the light of those facts that I turn to consider the applicable law and the contentions of XO and SARS.

The law

[20] The issue in this case is primarily concerned with the application of s 11(2)(l) to XO's activities. The cardinal consideration in determining the intention of the legislature is to interpret the provision in the context of the Act as a whole, and its history and the explanatory memoranda in the event of any uncertainty. See for example *Natal Joint Municipal Pension Fund v Endumeni Municipality* [2012] ZASCA 13 593 (SCA) para 18, where this court set out the relevant principles to be used in interpreting statutes. Those principles are equally applicable to taxing statutes. *Commissioner, South African Revenue Service v Bosch and Another* 2015 (2) SA 174 (SCA) para 9.

[21] Section 7(1)(a) of the Act imposes value added tax and applies to the whole of the Republic. It provides as follows:

'(1) Subject to the exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the National Revenue Fund 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;

(b) on the importation of any goods into the Republic by any person on or after the commencement date; and

(c) on the supply of any imported services by any person on or after the commencement date,

calculated at the rate of 14 per cent on the value of the supply concerned or the importation, as the case may be.'

[22] It was submitted on behalf of XO that the services rendered by XO were not subject to VAT at the standard rate in terms of s 7(1)(a), of the Act, but that such services should have been zero rated in terms of s 11(2)(l) of the Act. Section 11(2)(l) provides as follows:

'(2) Where, but for this section, a supply of services . . . would be charged with tax at the rate referred to in section 7(1), such supply of services shall, subject to compliance with subsection (3) of this section, be charged with tax at the rate of zero per cent where —

. . .

- (l) the services are supplied to a person who is not a resident of the Republic, not being services which are supplied directly —
 - (i) in connection with land or any improvement thereto situated inside the Republic; or
 - (ii) in connection with movable property (excluding debt securities, equity securities or participatory securities) situated inside the Republic at the time the services are rendered, except movable property which —
 - (aa) is exported to the said person subsequent to the supply of such services; or
 - (bb) forms part of a supply by the said person to a registered vendor and such services are supplied to the said person for purposes of such supply to the registered vendor; or
 - (iii) to the said person or any other person, other than in circumstances contemplated in subparagraph (ii)(bb), if the said person or such other person is in the Republic *at the time the services are rendered.*' (My emphasis).

[23] Before us, XO contended that its services should be zero rated because it did not supply or render the local services directly to the FTO or its customers. XO submitted that it entered into a back-to-back agreement with

the FTO in terms whereof the local supplier would give XO an undertaking that it would render the local services to the customers identified to it by XO. According to XO the local supplier would then supply the customer with local supplies when the customer arrived in the Republic, thereby discharging its obligations to XO by performance in favour of the *adjectus solutionis gratia* nominated by it. On this basis it was contended that the local suppliers rendered services to XO by performing their contracts in favour of the tourists; that XO rendered the service of organising the package to the FTO and the FTO had a contract with the foreign tourists to ensure that they would receive services while in South Africa from the local suppliers

[24] The argument was that there needed to be, a direct connection between the party that supplied the services i.e. XO and the recipient thereof, and since there was no direct relationship or connection between XO and the FTO or its customers in relation to the local services, these services were not directly supplied by XO. The nub of XO's case was that the local services were rendered by the local supplier directly to the FTO or its customers because XO had no direct relationship with the customers. It was XO's case that the service which it provided to the FTOs in terms of the back-to-back agreement was not a local service and attracted VAT at zero per cent, because it was a service supplied to a person who was neither resident nor present in South Africa.

Discussion

[25] It is clear that the resolution of this dispute requires consideration of the following: (a) what services did XO supply? (b) to whom did XO supply such services? (c) were the parties to whom such services were supplied, residents of, or present in the Republic when such services were supplied? To resolve this regard should be had to the applicable statutory provisions as well.

[26] A subsidiary issue which can be disposed of summarily relates to the argument raised by XO in its heads of argument that SARS sought to widen its grounds of assessment in para 16.4 of its statement of assessment. XO's objection was that SARS was bound by its amended grounds of assessment

when it stated that the local services were rendered by the hotel to the customers, and could not widen its grounds by stating that XO directly supplied the local services to the customers. SARS contended that XO misconstrued the context in which the averment was made and denied that the paragraph introduced a new ground. Paragraph 16.4 read as follows

‘[XO] arranged the tours, including inter alia the Local Services. [XO] did so by entering into agreements with the local service suppliers (the “Local Service Suppliers”) in terms of which the Local Service Suppliers agreed to supply the Local Services to the Customers when they undertook the tours in the Republic.’

[27] In my view para 16.4 was clearly foreshadowed in the notice of findings and the notice of assessment, as well as the responses to these in the letter of objection by XO’s attorneys and described the manner in which XO performed its contractual obligations vis-à-vis the local service suppliers. There was no merit in this point. At all stages the issue was whether XO admitted the supply of services to the FTO’s fell within s 11(2)(l) of the Act.

[28] Turning to the factual issues referred to in para 26 above, the difficulty confronting XO’s argument was that it was wholly inconsistent with the facts as they emerged from the evidence and the documents. It was correct insofar as it said that XO contracted with local suppliers to provide local services to foreign tourists, whom XO would identify. It was wholly incorrect when it said that the only services XO supplied to the FTO’s were the organisational services involved in assembling the tour package and nothing else.

[29] The letter of agreement, standard terms and 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. That is what XO undertook to provide to the FTO’s; that is what it was paid to provide and that is what it provided. The fact that in order to perform its obligations towards the FTO’s it in turn had to acquire those goods and services from local suppliers was neither here nor there. Its contract was to provide those goods and services. How it did so was no concern of the FTO.

And it provided those goods and services, not directly to the FTO, but to other persons who were in the Republic at the time that the goods and services were provided. That served to exclude these services from the class of services that enjoy zero rating under s 11(2)(l). SARS was accordingly correct in saying that the supply of the services attracted VAT at the standard rate.

[30] We were taken to the various amendments of this section which led to the current version of the section around which the dispute between the parties revolves. That history showed that the statutory purpose underlying s 11(2)(l) was to ensure that where services were rendered to a foreigner by a person liable to pay VAT, but the services themselves were rendered in South Africa and the benefit of them was enjoyed in the Republic, they would not enjoy the benefit of zero rating. VAT would be payable at the standard rate.

[31] The argument of XO is unsustainable because, if it followed, it would mean that notwithstanding the fact that the services were consumed in the Republic and XO 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. 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 (see *Master Currency v CSARS* 2014 (6) SA 66 (SCA)).

[32] In the result the appeal is dismissed with costs including the costs of two counsel.

R S MATHOPO
JUDGE OF APPEAL

APPEARANCES:

For appellant: S A Cilliers SC (and T S Emslie SC and M W Janisch SC)

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