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40 YEARS

1979 2019 2019

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PRESUMPTIVE TAX

Newsletter

MBAYA AND ASSOCIATES January 2019 | Issue 043 | Volume 5

Introduction

Happy New Year from all us at M&A. Welcome you to our first edition of year 2019 tax newsletter. The newsletter covers a variety of the recent changes in the tax and accounting regime in Kenya to keep you current and updated on tax matters and the latest in business trends.

On the right column of the newsletter you will find contact details for the senior members of our team who can help answer any questions you may have about the issues highlighted in this newsletter or any other questions.

We are interested in your feedback on the items covered and what topics you would like covered in the future.

Please provide any feedback at **tax@mbaya.co.ke**

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Happy New Year from all us at M&A!

» MBAYA & ASSOCIATES

In this issue

From the Tax Desk

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From the *Tax***Desk**

Introduction

The two changes discussed below are effective **1st January 2019** and it is important we take note of them early in the year. The Finance Act, 2018 was assented to by the President on 21st September 2018. The Act introduced various taxation measures in support of the Big Four Agenda which is the government's main focus for the fiscal year 2018/2019.

Through the Big Four Agenda, the Government targets to boost manufacturing activities, enhance food and nutrition security, achieve universal health coverage and support the construction of at least 500,000 affordable houses by 2022. Following the mandatory public participation and after deliberation of the Finance Bill 2018 (the "Bill") in Parliament, the Bill was sent to the President for assent. The President sent back the Bill to Parliament with a memorandum proposing certain changes, all of which were contentiously adopted by the National Assembly on 20th September 2018 and the Finance Act was passed into law on 21st September 2018.

The main tug of war between the National Assembly and the Executive arose from the initial decision by the National Assembly to extend the exemption of VAT on petroleum products by another two years, an initiative which was not acceptable to the Executive due to the effect that it would have had on the budget estimates.

Based on the Provisional Collection of Taxes and Duties Order, 2018 made by the Cabinet Secretary of the National Treasury and published on 21st June 2018, a number of the tax provisions in the Finance Act, 2018 have an effective date of 1st July 2018.

However, in a ruling delivered by Justice Okwany in Petition No 253 of 2018, it was held that "…the Finance Bill 2018, or any parts or provisions thereof, including on taxation, cannot be implemented before the Bill becomes the Finance Act after it goes through the parliamentary legislative process laid out in the Constitution for approval and adoption by Parliament, and assent by the President."

In our previous tax newsletters, we have highlighted various tax amendments and introduction of clauses. In this issue we now highlight one of the key amendments introduced by the Finance Act, 2018 with an effective date of 1st January 2019

Presumptive Tax

This is a tax payable by a resident person whose turnover from business does not exceed Kshs. 5 million during a year of income. The Income Tax Act relating to turn over tax have been repealed and replaced by presumptive tax.

Persons liable to pay a Presumptive Tax shall be:

- Resident persons whose gross turnover from business does not exceed Kshs. 5 million during a year of income; and
- Who are issued or are liable to be issued with a business permit or trade license by a County Government.

The rate of presumptive tax shall be amount equal to 15% of the amount payable for a business permit or trade license issued by a County Government and it shall be a final tax.

The due date for payment of the tax shall be at the time of payment for the business permit or trade license or renewal of the same.

Exceptions

The Presumptive Tax regime will not apply to:

- A person whose income is exempt from tax under the First Schedule of Income Tax Act and has a valid exemption certificate.
- A person who would otherwise pay tax under this regime but elects by notice in writing to the Commissioner not to be subjected to the Presumptive Tax.
- A resident person whose gross turnover from business exceeds Kshs. 5 million in a year of income
- Any income derived from:
    i. Management and professional services; or
    ii. Rental business; or
    iii. Incorporated companies

NB: The Taxpayers under Presumptive Tax Regime are not required to file a tax return on the income from the business that qualifies under presumptive tax regime.

Eligible taxpayers will have to log onto **iTax** to make payment for Presumptive Tax. The taxpayers shall be required to generate a **Payment Registration Number (PRN)** on iTax under Presumptive Tax Payment, after which they can pay through M-Pesa Pay Bill Number **572572** or any other partner bank.

Presumptive Tax is a final tax. This means, you are not required to declare the tax in your Annual Tax Returns.

Our Analysis:

The amendment to replace turnover with presumptive tax is aimed at promoting tax compliance in the informal sector by entrepreneurs and businessmen following the failure of the turnover tax regime to capture this sector.

However, the presumptive tax payable will be significantly lower than the income tax payable by an employee in formal employment and may need to be reconsidered to ensure that the burden of tax is shared equitably as per Article 201 of the Constitution of Kenya.

[Image Source: https://www.diapason-treasury.com/wp-content/uploads/2018/01/ifrs-16.png]

Leases - A Summary of IFRS 16 and its Effects

The International Accounting Standards Board (IASB or Board) issued IFRS 16, which requires lessees to recognize assets and liabilities for most leases. For lessors, there is little change to the existing accounting in IAS 17.

The new standard will be effective for annual periods beginning on or after **1 January 2019**. Early application is permitted, provided the new revenue standard, IFRS 15 (*Revenue from Contracts with Customers)* has been applied, or is applied at the same date as IFRS 16.

The new standard will significantly change the accounting for lessees 'leases and may have far-reaching implications for a company's finances and operations

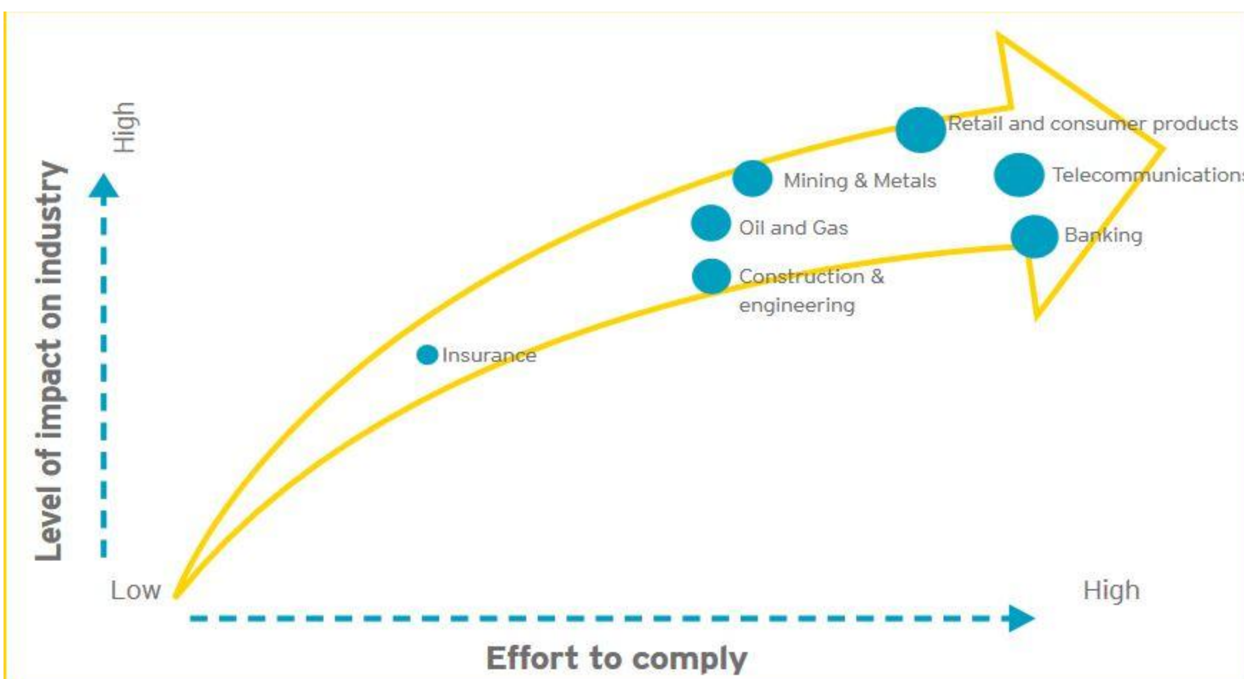
Entities most likely to be Affected by the Changes

The effects of IFRS 16 will need to be assessed on the facts and circumstances relevant to each entity. This will further be impacted by the different capital structures that entities have adopted, for example an entity that typically rents office space, which is being accounted for as an operating lease, will be more significantly impacted than an entity that has purchased office space.

It is expected that certain industries will be more significantly impacted than others. Some of the types of contracts that entities would need to consider include:

a. **Retail and consumer product entities** are expected to be most significantly impacted by the changes in the new lease requirements. This is especially the case where leased retail space forms a significant part of the entity's business model.
b. **Telecommunications entities** are expected to be significantly impacted by the new lease requirements. Telecommunications will need to consider tower arrangements, signal transmission devices as well as data and fixed line agreements. In addition, telecommunication entities will need to analyse contracts where equipment is provided to their customers. In such instances, consideration would need to be given to whether the contract contains a lease and if so, how the lease payments should be allocated to products and services provided.
c. **Banking and other financial services entities** that have extensive branch networks as well as large administration and call centres will need to consider any lease arrangements carefully. In addition, contracts over ATMs and the related space occupied by such machines will need to be assessed under the new lease standard's requirements.
d. **Metals and mining entities** will need to carefully consider all major arrangements that they have entered into that may give rise to on balance sheet lease accounting under the new leases standard, such as mining equipment, vehicles as well as land and buildings. Similarly, construction and engineering entities will need to consider all major arrangements that they have entered into such as leases over construction equipment, vehicles as well as land and buildings.
e. **Oil and gas entities** may be impacted by arrangements in respect of land and buildings, vehicles and equipment as well as arrangements that contain a lease.
f. **Insurance entities** will need to consider all arrangements entered into in respect of land and buildings, vehicles and equipment that are not currently accounted for on balance sheet.

The diagram below illustrates the potential impact of the adoption of IFRS 16 on the specific industries:



How will your Business be Affected?

- **Impact for lessees?**

For many companies, leases play a critical role in their business operations. However, because most lease transactions (e.g. operating leases) are off-balance sheet today, accounting for leases under current lease standards often does not require a significant effort.

The new standard will require a company to do more than simply convert its existing operating lease commitments disclosure to reflect lease assets and liabilities. Its implementation could result in changes to the policies, processes, controls and IT systems that support lease accounting and possibly lease procurement, lease administration and tax. Companies may also wish to consider the implications for financial statements and metrics as they negotiate contracts that are, or may contain, leases.

These activities will require involvement from a variety of **departments** across the company example:

Tax Considerations

Adoption of the new standard will result in additional tax related considerations. These include understanding the impact of the lease accounting changes on existing tax positions, initial adjustments to deferred taxes and tracking book/tax differences.

Companies will need to determine necessary changes to tax-related processes and controls required to identify and track tax adjustments. The impact on taxes will, of course, depend upon the requirements of the specific tax jurisdiction and whether and how they are changed to reflect the requirements of the new standard.

- **Impact on lessors**

Although the accounting by lessors is substantially unchanged from current accounting, lessors will have new disclosure requirements.

However, lessors should understand how the new standard could affect their lessee's behaviour. This would help lessors negotiate lease arrangements that meet the needs of their customers.

Tax Due Dates

Withholding Tax | 20th Day of the following month
Pay as You Earn | 9th Day of the following month
VAT | 20th Day of the following month
Balance of Tax on Self-Assessment | 4th Month after year end
Monthly Rental Income | 20th Day of the following month

Instalment Tax

1st Instalment |20th day of the 4th month after year end
2nd Instalment | 20th day of the 6th month after year end
3rd Instalment | 20th day of the 9th month after year end
4th Instalment | 20th day of the 12th month after year end
Kindly note that all the returns must be filed on I tax while the payments e-slips must be generated from the I-Tax platform.