Growing tomorrow's economy
VAT reforms

National Budget 2012/2013

Reforming the tax system for efficiency and effectiveness

Finance Bill, 2012 VAT Act schedules harmonised Customs tariff codes

The long awaited VAT Bill is finally released

Tax payers have less time to claim input tax

Ease of compliance on imported services for registered persons

Burden of paying tax on supply of imported services to non-registered person s is with the supplier

No clarity on export of services

Partial exemption attribution simplified; however, threshold limit increased from 5% to 10%

Process of tax disputes expedited; concept of rulings introduced

Tax base broaden–zero and exempt items significantly reduced

No relief for refunds!!

The long awaited VAT Bill is now here with us

Is it simplified, modernised and broad based?

While there is no significant departure from the draft *VAT Bill*, we highlight some of the key changes in the *VAT Bill* compared to the *VAT Act*.

A big blow: VAT Remission scrapped

There was hope in the draft *VAT Bill* to grant VAT remission to businesses who:

- Import and locally purchase capital equipment;
- Are in hotel construction businesses; and
- Are in the oil exploration business.

Such was in the "public interest" to do so at the discretion of the Cabinet Secretary.

The Bill has scrapped VAT remission altogether, which is a big blow to investors seeking investment opportunities in Kenya.

Expectations not met

The huge backlog of refunds at KRA continues to frustrate taxpayers. To compel KRA to pay taxpayers on time, it was envisaged that the Bill would require the Commissioner to pay interest on any delayed refund settlement. There are no such provisions in the Bill.

Time limit for deduction of input VAT reduced

Taxpayers will no longer have the luxury of deducting input tax within 12 months since it has been reduced to only three months.

This calls for a high level of efficiency within businesses to ensure VAT systems and processes are modernised in order to recover the input VAT within the stated time limit.

Place of supply rules of goods clarified

The Bill proposes to introduce place of supply of goods which occurs in Kenya,

- where the goods are made available by a supplier in Kenya;
- the supply of the goods involves installation or assembly at a place in Kenya; and
- the goods were in Kenya when the transportation commenced.

A shift in application of partial exemption

While the existing methods for determining the deductibility of input tax attributable to mixed supplies has been retained, the Bill introduced has increased the diminimis limit from 5% to 10%.

The impact of this is that businesses that could originally recover 5% of input tax relating to mixed supplies would now incur additional irrecoverable VAT.

However, businesses whose taxable supplies are more than 90% shall be allowed full deduction of input tax.

VAT on Imported Services simplified?

Ease of compliance for registered persons

Currently, the Act requires importers of services to declare and pay VAT to the KRA. The registered person thereafter deducts the reverse VAT paid as input VAT in the VAT return in the subsequent month.

The Bill now requires registered persons to account for reverse VAT only if they are not able to claim this VAT. This is a welcome move as it will ease the burden of compliance through elimination of multiple forms.

Supplies to Non resident persons

Where imported services are rendered to non-registered persons the Bill proposes appointment of a tax representative by non-residents or by the Commissioner to facilitate collection of tax. However, we foresee difficulty enforcing this measure given the minimal connection between the Kenya Revenue Authority and the persons it seeks to tax. It is also not without its controversies.

Although the Bill has made an effort to simplify the accounting of reverse VAT for registered persons, more clarity is required for supplies made to non-registered persons to address the possibility of revenue leakage.

Could VAT on e-commerce become a reality?

The Bill seeks to broaden the tax net by targeting e-commerce undertaken by non-residents without a fixed place of business in Kenya. This includes supply of electronic services such as web-hosting, remote maintenance of programs and equipment, updating of software and self education packages through a telecommunications network to unregistered persons in Kenya. The non-residents may be deemed to be making taxable supplies in Kenya.

Taxable value of imported services now amplified

Upon the importation of taxable services a person is required to take into consideration the value of:

- the amount of money paid or payable;
- the open market value at the time of the supply;
- any taxes, duties, levies, fees and charges (other than VAT) paid or payable.

This amendment now requires the recipient of imported taxable services to be more cost-sensitive in determining the value of the service.

Export of Services still foggy

As is the case with the Act, there are inconsistencies in the Bill in determining the export of services. In the Bill, a service will be considered an export of service if it is provided for use and consumption outside Kenya; however it also proposes that a service shall be deemed to be supplied in Kenya if the place of business of the supplier is in Kenya.

Timely resolutions to objections

The Bill proposes to introduce a time limit when the Commissioner should respond to taxpayers' objections to assessments issued within 60 days.

This shall assist in expediting the process of tax dispute resolution.

Public and Private Rulings

In the past the KRA has been issuing rulings and technical circulars through the media with no backing of the Law.

The Bill now requires the KRA to make public and private rulings by publishing them in at least two daily newspapers of national circulation.

12% VAT rate scrapped

The Bill proposes two rates of tax

- 0% for zero-rated supplies; and
- 16% for any other supply.

This means that electrical energy which was previously charged at 12% will now be subject to 16% rate of VAT.

However the standard rate can be increased or decreased by up to 25% by the Cabinet Secretary (this will be the title given to the Minister after the first general elections under the Constitution).

Time limit set for change of status of goods and services

Exempt supplies like petroleum products and zero rated goods like medicaments and medical equipment will remain in their current tax status for a period of three years after which they will become taxable at a standard rate.

Significant Changes in status of taxable goods and taxable services

Significant changes have been proposed in the Bill with regard to the goods and services which at present are exempt or zero-rated for VAT purposes

Some exempt goods which will become taxable at 16%

- Cut flowers;
- Wood charcoal;
- Helicopters;
- Aircrafts;

Some exempt services which will become taxable at 16%

- Postal services;
- Management of unit trusts or collective investments
- Entertainment performed by Kenyan artistes;
- Hiring, leasing and chartering of aircrafts and helicopters including air ambulance aircrafts;
- Tour operation and travel agency services;

Some zero-rated goods which will become taxable at 16%

- Milk and cream (except unprocessed milk which will be except);
- Maize and wheat flour;
- Ordinary bread, gluten bread and unleavened bread;
- Infant Formula;
- Computer software;
- Sanitary Towels and tampons;
- Medical dressings and plasters;
- Writing or drawing chalk;
- Newspapers, journals and periodicals;
- Exercise books and printed books;
- Cinematographic cameras and projectors;

Some zero-rated services which will become taxable at 16%

- Electrical energy to domestic households;
- Services in respect of goods in transit;
- Landing and parking services provided for aircrafts;
- Water drilling services;
- Services to film producers.

Some zero-rated goods which will become exempt

- All electrical and mechanical appliances including generators.
- Kerosene type jet fuel;
- Mosquito nets;

The Bill proposes to introduce zero rating of the taxable supplies imported or purchased by any company which has been granted oil or gas exploration or prospecting licence in accordance with the production sharing contract with the Government. Previously such supplies were eligible for VAT remission. This is a welcome move for the oil and gas industry as it will spur growth in this important sector and result in spin off effects.

However, there was great expectancy for similar incentives to be extended to similar extractive investors such as the mining and geothermal sector.

Privileged persons and bodies and special goods

The list of persons, bodies and special goods entitled to zero-rating by virtue of their privileged status has been reduced. For example the following will no longer be subject to the entitlement:

- The president;
- The Kenya Armed Forces;
- Charitable Institutions;
- Safari Rally Drivers;
- Goods used by an aircraft operator;
- Materials and equipment for use in construction or refurbishment of tourists hotels.

So is it really simplified, modernised and broad based?

A simple answer would be yes, however more work needs to be done by the Government to achieve the Vision 2030 goals and objectives. We expect that this will result in economic growth and stability in Kenya.