Tax Alert

VAT Auto Assessment: An update from the Kenya Revenue Authority

April 2019

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The Kenya Revenue Authority ("KRA") through the use of technology continues to introduce measures targeted at enhancing Value Added Tax ("VAT") compliance. The VAT Auto Assessment ("VAA") has been improved by taking on board views and feedback provided by taxpayers and other stakeholders.

In October 2018, we issued a tax alert on the KRA's renewed focus on VAT compliance. In the referred alert, we highlighted the fact that the KRA had commenced issuing of notices to taxpayers highlighting VAT inconsistencies and its intention to issue assessments.

For ease of reference, click on this ***link*** to access the above referenced tax alert. In this update, we analyze a recently issued Public Notice by the KRA in relation to VAA inconsistency reports and its impact on taxpayers.

The KRA issued a Public Notice on 29 March 2019 informing taxpayers that system improvements have been undertaken to the VAA module within iTax following feedback received from taxpayers and other stakeholders.

In October 2018, the KRA had issued similar VAA inconsistency notices to taxpayers for VAT returns relating to the period of January 2018. However, due to limitations with the iTax system many taxpayers were not able to address the identified inconsistencies.

In the current Public Notice, the KRA has indicated that the updated system cross-validates invoice details in both the buyers' and sellers' VAT returns and subsequently identifies inconsistencies that the affected taxpayers are required to resolve within the given period from the date of the system notification.

Further, the KRA indicates that taxpayers affected by verification of the January 2018 VAT return have been granted a period of 60 days from 29 March 2019 to amend their VAT returns. Where input tax inconsistencies remain unresolved after the stated period, the VAT claims will be disallowed.

The KRA has further indicated it will commence issuing VAA inconsistency notices to taxpayers for the VAT returns relating to the periods from February 2018 to date, as from 29 March 2019.

We highlight below some of the improvements the KRA has indicated to have been made to the VAA module in iTax and our comments on the impact to taxpayers:

1. Introduction of threshold to cater for minimal margins of inconsistencies

One of the challenges observed by taxpayers with regards to the VAA, was inconsistencies occasioned by rounding off and foreign exchange rate differences and the administrative challenges associated with reconciling these amounts.

The KRA has pointed out that a threshold to cater for minimal variances in VAT amounts has been introduced and amounts within this

threshold will not form part of VAA inconsistency reports.

Whilst this is a welcome feature to the VAA module, what remains unclear is the threshold amount and whether or not considerations such as the nature of the taxpayer's business, value of transactions, etc. have been factored into the threshold. In our view, the KRA needs to consider factors specific to taxpayers or sectors such as turnover and volume of transactions to ensure fairness and ease of reconciling the inconsistencies.

2. Increased number of characters and format, including leading and lagging spaces

During stakeholder engagement sessions, it was noted that the iTax system limits the number and the type of characters that can be input as an invoice number. The KRA has updated the VAA module by increasing the number of characters that are accepted in an invoice number i.e. from 20 to 40 characters. iTax will also accommodate alphanumeric data and special characters which may form part of an invoice number.

In addition, the KRA acknowledges some of the inconsistencies were merely as a result of simple data capturing errors e.g. where a supplier uses upper case text and the purchaser uses lower case in their VAT return or where spaces are left in-between characters.

The KRA states that these issues have now been addressed in the current module. This in our view is a welcome improvement for taxpayers as it will save on time spent reviewing mundane inconsistencies.

3. Increase in the limit of transaction entries in the VAT return

A significant shortcoming of the iTax has been its limitation on the number of monthly sales and purchases transactions that can be reported. The KRA has increased the maximum number of entries in the VAT return from 50,000 to 75,000.

This change will affect both standard rated sales and standard rated purchases sheets in the VAT 3 Form.

While this is a welcome improvement there are still taxpayers who will require more entries to correctly report their monthly transactions, especially to registered customers. Sectors such as retail businesses, utilities and telecommunication operators will generally have a transaction base of more than the 75,000 per month.

Further, in certain sectors, vendors do not necessarily obtain or maintain Personal Identification Numbers (PINs) of all their customers and the process of obtaining them will require significant time and monetary investment.

In our view, KRA needs to engage further with taxpayers in the said sectors with a view to providing guidance and/or make exceptions for taxpayers in specific sectors engaged in high-volume transactions until a sustainable solution is agreed upon.

4. Back-end amendment of VAT returns by KRA

The KRA officers will be available to assist taxpayers file amended VAT returns through the back office (data correction) where taxpayers are unable to amend the same through their iTax profile.

The iTax system normally does not allow amendment of returns outside the six months window allowed for input tax recovery. Taxpayers with January 2018 amended VAT returns will be required to liaise with their respective or nearest tax service office for their returns to be uploaded by officers.

In our view, this is a commendable effort by the KRA on realizing that taxpayers would not have been able to file VAT returns from their iTax profiles due to the time limit imposed by the VAT legislation.

Legal considerations

The VAT legislation as is currently written does not impose any obligation on the buyer of goods/services to ensure VAT charged to him/her by the seller is declared and remitted to the KRA.

The law requires any VAT claimed as input tax should be incurred for the purpose of making supply and the claimant should be in possession of certain prescribed documentation to evidence entitlement to the claim. In our view, the VAA imposes this as an additional obligation which is not supported in law on the buyers of goods/services.

Further, the Tax Procedures Act, 2015 ("The TPA 2015") provides for the time limit of five (5) years from the date of filling tax for taxpayers to amend their tax returns if required. While KRA has increased the requirement to make amendments from the previously stated 15 days to 60 days, this still appears to go against the TPA.

In our view the VAA should operate within the confines of the VAT legislation in order to avoid legal headwind with taxpayers.

Conclusion

While there are still unanswered questions, it is commendable that the KRA continues to use tax technology tools including data analytics to enhance VAT compliance and remains open to feedback from taxpayers.

Please note that the KRA has started issuing VAA inconsistency notices to taxpayers through iTax – be on the lookout!