2020'S TURNOVER TAX: A NEW DAWN OR A VISIT TO THE PAST

For years on end the Government of Kenya has grappled with the conundrum of roping the informal sector to tax with missed revenues sieving through the KRA's efforts.

KRA's endeavors to address the tax challenges of taxing the informal sector have proved fruitless despite statistics reporting a growing sector.

With the reintroduction of the turnover tax in 2020, has the KRA found the right formula or is the same tune being sang?

Through the Finance Act, 2019, the Government has reintroduced turnover tax this year after being repealed for one-year in a bid to net more tax revenues from the elusive informal sector.

Introduction of TOT

Turnover tax was first introduced in Kenya in 2007 to enhance tax compliance in the informal sector by simplifying tax procedures and compliance requirements by prescribing a flat tax rate of 3% on gross revenue earned per month.

However, by the turn of 2018, the regime had been crippled by rampant tax evasion, laxed administrative structures, ineffective enforcement mechanisms and non-compliant taxpayer behavior.

Replacement with Presumptive Tax

To address these challenges, the KRA replaced turnover tax with the presumptive tax set at a 15% rate of business permits or trading license fees in 2019.

By tying taxes to permits and license fees, the KRA intended to compel small business owners and the larger informal sector to certain levels of taxation before engaging in any business activities.

As such, the success of presumptive tax was pegged on a seamless cooperation network between the KRA and the County Government since the tax would be collected at the point of processing business permits or trading licenses.

However, presumptive tax ended up grossly underperforming, collecting a paltry KShs 35 million for the national coffers against a projection of KShs 2 billion within a span of one year.

The KRA attributed the underwhelming performance to inadequate assistance from the County Government along with the lack of an integrated revenue collection system for both administrative bodies.

It was also noted that the County Government, visualized as an agent of enforcing tax compliance, issued business permits and trading licenses without ensuring taxpayers accounted for presumptive tax negating the tax's blueprint.

Re-introduction of Turnover Tax

After much deliberation, the KRA redesigned a hybrid system of a presumptive and turnover tax regime aimed to beef up KRA's revenue collection efforts as noted by Deputy Commissioner Corporate Policy Maurice Oray during a public sensitization forum mid last year.

"One of the key issues is treating (roping to tax) the sectors that have largely remained untaxed, particularly the informal sector where we have proposed that we have a hybrid system of what is currently the presumptive tax and the turnover tax," confirmed Mr. Oray.[1]

As effective from 1st January 2020, small and medium taxpayers with annual revenues not exceeding five million shillings are expected to timely account for presumptive tax and turnover tax at their respective rates.

Presumptive tax acting as an advance tax may be utilized to offset any turnover tax payable during the year.

It's noteworthy that the taxes are not applicable to incomes derived from management and professional services, rental businesses, or incorporated companies.

In addition, taxpayers may opt out of the presumptive and turnover tax regime through a written request to the commissioner.

The KRA also issued draft Income Tax (Turnover Tax and Presumptive Tax) Regulations, 2019 late last year for public participation and wide consultation as required in Kenya's constitution.

The new regulations are similar to the previous turnover requirements that provide guidelines on how the tax shall be administrated and prescribes compliance obligations to taxpayers.

It's interestingly observable that the new regulations exclude VAT registered taxpayers from turnover and presumptive tax regime.

Income tax and VAT are two separate forms of taxation; one being a direct tax and the other an indirect tax. By KRA excluding VAT registered taxpayers from turnover and presumptive tax, the taxman might be limiting voluntarily VAT registered SMEs from enjoying a simplified income tax regime which could encourage tax compliance among taxpayers.

Conclusion

KRA's revamped efforts to tighten the noose in the informal sector is a commendable measure noting that the informal sector has for long remained untaxed thus exacting unequal pressure on the formal sector.

The reintroduction of turnover tax coupled with presumptive tax might ensure the informal sector contributes fairly to the Kenyan economy.

[1] https://www.standardmedia.co.ke/business/article/2001331413/tax-flop-on-small-traders-to-hit-kra

However, the KRA face the risks of being haunted by their previous administrative challenges unless they address their previous shortcomings, improve coordination with the County Government and introduce an integrated revenue collections system that harmonizes operations of different arms of the Government's executive bodies.

Going forward, it's prudent for taxpayers including *mama mboga* to familiarize themselves with impending taxes in 2020.

As once noted by Benjamin Franklin, "An ounce of prevention is worth a pound of cure." Complying with tax legislation will shelter taxpayers from punitive fines and aggressive enforcement measures from the taxman which will in turn garden a healthy environment for business growth and development.

Let's talk

For further information on how the enacted tax provisions will affect your business or assistance on any other matter kindly contact your regular Taxwise Africa analyst or the contacts below.

- 020 2025320
- ewanjau@taxwise-consulting.com
- Info@taxwise-consulting.com
- https://taxwise-consulting.com/