CAPITAL GAINS TAX

Introduction

What is Capital Gains Tax (CGT)? - CGT is a tax on the profit when you sell or dispose of property that has increased in value. It's the gain you make that's taxed, not the amount of money you receive. Example You bought a painting for Kshs 5,000 and sold it later for Kshs 25,000, there will be a tax on the gain of Kshs 20,000. The gain is calculated as the difference between the cost at which the property was bought and the price at which the property is sold, this is after deducting any costs of improvement to the property and any incidental costs incurred on the transfer of the property for example advertising fees and lawyer costs.

In Kenya CGT, was re-introduced on 1st January, 2015 after being suspended in 1985. It is a tax chargeable on the whole of a gain which accrues to a company or an individual on the transfer of property situated in Kenya. It applies on all transfers of Property after 1st January, 2015 regardless of the year in which the same acquired. Property transactions that are exempt from CGT include among others disposal of property to administrator the estate of a deceased person, the vesting of property to a liquidator, and the selling of individual residence occupied by the seller for at least 3 years before the transfer and transfer of assets between spouses and former spouses and their immediate family. What is interesting to note is that this is not a new tax. The tax is to be paid by the person transferring the property, that is, the seller. The rate of tax is 5% of the net gain, and the 5% is a final tax, meaning after the same is paid the Seller is under no obligation to pay other Taxes and cannot be offset against other income taxes.

Issue

The Kenya Revenue Authority (KRA) issued a public notice requiring that the payment of stamp duty and capital gains tax must be initiated through the iTax platform effective 1st October 2016 (iTax is an online integrated system for managing the payment of all taxes). Full implementation begun on the 30th of January, 2017, when KRA demanded that CGT must be paid before property is transferred simultaneously with the payment of Stamp Duty, , whilst previously, CGT was payable before the 20th of the month in which the transfer was done. This is probably, in recognition of the fact that Real Estate Property transactions are the largest sources of CGT in Kenya with the exemption on listed securities, and therefore an attempt to ensure effective tax collection as proof of payment of Stamp Duty must be given to the Lands Registry before any transfers are done.

KRA was taken to court over this by the Law Society of Kenya (LSK) under a certificate of urgency. The LSK argues that this requirement limits the right of enjoyment of Property as enshrined in Article 40 of the Constitution by introducing unnecessary constraints and delays.

The Court upon hearing the application ordered that KRA or its agents, servants, or employees should not implement the provisions of that paragraph 11A of the eighth schedule to the Income Tax Act until the court has heard the matter and made a final decision.

Conclusion

As it is, the courts have just given breathing time, it is a temporary injunction, and is now up to the LSK to present before them a strong case as to why the conservatory orders that were issued by the courts should be made permanent. In my view, CGT should only be payable after the Property has been transferred to the Buyer and the Buyer is in receipt of the Purchase Price This is especially so since most transactions are structured so that funds are usually held in escrow either jointly by the Buyer and Seller or their Advocates until the transfer is formalised. Further with the method we currently have other questions may arise for example where the transaction falls through and neither party is at fault, how would the seller who has already paid the CGT amount then recover it from KRA? We all know how tedious it is to recover money from. It is notable that it's not only Kenya that charges CGT, Uganda charges CGT at the rate of 30% and is applicable on business assets, Tanzania charges CGT at a corporate tax rate of 20%, while South Africa charges CGT at the rate of 40%. In Uganda, to pick out an example the

Capital gains are added to the other income of the taxpayer for that year of income and not taxed separately. We should perhaps look to these jurisdictions for a solution that works.