

ANNUAL BUDGET REVIEW AND EMERGING TAX ISSUES SEMINAR

MANAGING KRA AUDITS AND EMERGING TAX ISSUES BY

CPA. Joash Kosiba

Parliamentary Budget Office (PBO) –Kenya

1

Green Hills Hotel, Nyeri

JUNE 23rd -24th , 2016

OBJECTIVES OF THE PRESENTATION

By the end of this presentation the participants should be able to understand and explain salient issues regarding tax audit programmes, conduct of audits and emerging tax issues including:

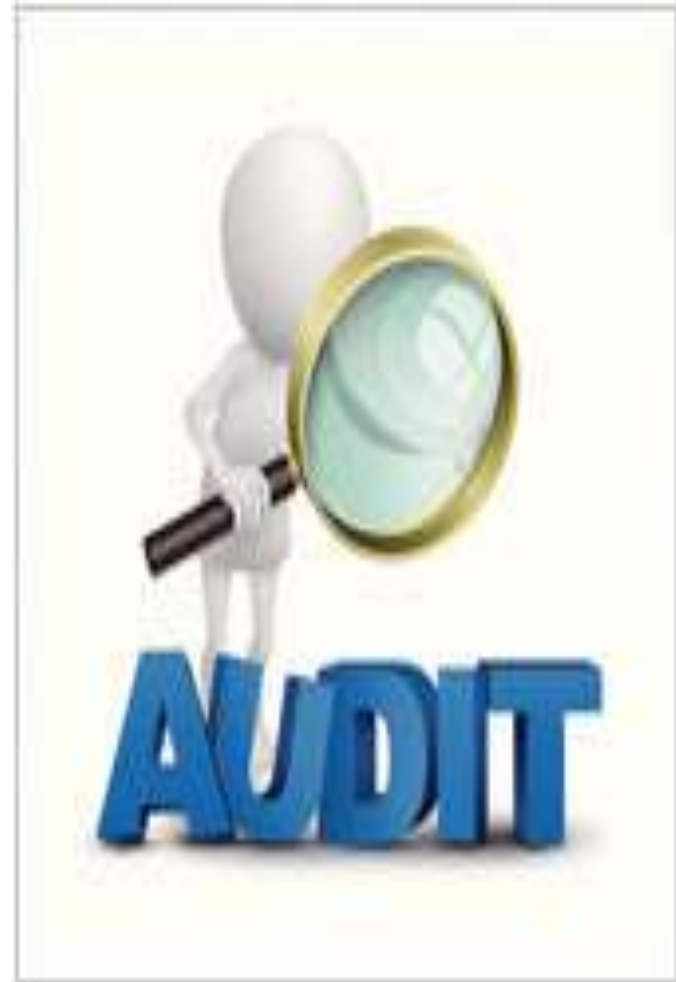
- What is tax audit and the role of tax audit activities.
- Tax Audit Scope and Intensity.
- Tax Audit techniques and support tools.
- Why increase in KRA Tax Audits.
- KRA Lifestyle audits of tax payers and Tax Officials.
- KRA Tax audit improvement and governance framework.
- Emerging tax issues

INTRODUCTION

- The primary goal of a revenue body's (KRA) compliance activity is to improve overall compliance with the tax laws, and in the process instill confidence in the community that the tax system and its administration are fair.
- Instances of failure to comply with the law are inevitable whether due to **taxpayers' ignorance, carelessness, recklessness and deliberate evasion, or weaknesses in administration.**
- Tax audits remain **a major tool for tackling non-compliance** and constitute the largest deployment of resources for administration of the of the various tax laws

WHAT IS A TAX AUDIT?

- A tax audit is an examination of whether a taxpayer has **correctly assessed and reported their tax liability** and fulfilled other obligations.
- Tax audits are often more **detailed and extensive** than other types of examination, such as general desk checks, compliance visits/ reviews or document matching programmes.



ROLE OF TAX PAYER AUDIT PROGRAMMES

- **Promote voluntary compliance:** The primary role of the audit program is to promote voluntary compliance by taxpayers with the tax laws.
- **Detect non-compliance at the individual taxpayer level:** By concentrating on major areas of risk (e.g. unreported cash income) and those individual taxpayers most likely to be evading their responsibilities, audits may bring to light significant understatements of tax liabilities, and additional tax revenue collections.
- **Gather information on the “health” of the tax system (including patterns of taxpayers’ compliance behaviour):** Audits conducted on a random basis can assist overall revenue administration by gathering critical information required to form judgments on overall levels of tax compliance.



ROLE OF TAX PAYER AUDIT PROGRAMMES...CONT

- **Gather intelligence:** Audits may bring to light information on evasion and avoidance schemes involving large numbers of taxpayers that can be used to mount major counter-abuse projects.
- **Educate taxpayers:** Audits can assist clarify the application of the law for individual taxpayers and to identify improvements required to record-keeping and thus may contribute to improved compliance by taxpayers in the future.
- **Identify areas of the law that require clarification:** Audits may bring to light areas of the tax law that are causing confusion and problems to large numbers of taxpayers and thus require further efforts by the revenue body to clarify the laws' requirements and/or to better educate taxpayers on what they must do to comply into the future.

TAX AUDIT SCOPE AND INTENSITY

- *Full audits* – The scope of a full audit is all-encompassing. It typically entails a comprehensive examination of all information relevant to the calculation of a taxpayer's tax liability for a given period. The objective is to determine the correct tax liability for a tax return as a whole.
- *Limited scope audits* – Limited scope audits are confined to specific issues on the tax return and/or a particular tax scheme arrangement employed by the taxpayer. The objective is to examine key potential risk areas of non-compliance.
- *Single issue audits* – Single issue audits are confined to one item of potential non-compliance that may be apparent from examination of a taxpayer's return.

AUDIT EXAMINATION TECHNIQUES

- **Analytical review** - An analytical review of financial statements and returns as filed is often completed during the preliminary stages of the audit
- **Investigative approach** - Such an approach uses information obtained through observation, discussion, documents or records obtained from either the taxpayer/registrant or from other sources.
- **Records Examination** - the main approaches to detect false accounting include the examination of books and documents conducted at the taxpayer's business office or branches, counterpart examinations and examination of bank accounts.
- **Third party information/Counterpart examinations** - Where warranted, information can be obtained during the course of an audit from third parties to verify the taxpayer's income,

KEY TAX AUDIT CHARACTERISTICS

- A comprehensive legal framework, including an appropriate regime of sanctions.
- Well-defined organizational and management processes, including a comprehensive performance measurement framework.
- Well-defined audit techniques and adequate support arrangements; and.
- Adequate human resource management and development programs.

WHY INCREASE IN KRA TAX AUDITS

- ❖ **The need for increasing government revenue has necessitated a rise on KRA audits on taxpayers**
- ❖ **Missing of revenue targets by KRA has also fueled this matter.**
- ❖ **This has led to increased cost of tax compliance.**
- ❖ **The widening budget deficit is putting pressure on the KRA**
- ❖ **The need to generate adequate revenues to pay debts owed by the country**

LIFE STYLES AUDIT OF TAX PAYERS

- ❖ Lifestyle audits on taxpayers
 - ❖ Aimed at widening the tax base by bringing into the tax net more taxpayers.
 - ❖ Aimed at increasing government revenue through sealing leakages and loopholes.
 - ❖ Aimed at ensuring tax compliance by all taxpayers
 - ❖ Proposal to give powers to KRA to have unfettered access to individual M-PESA statements.
- What your view?**

KRA TAX AUDIT IMPROVEMENT AND GOVERNANCE FRAMEWORK

The Key objective of KRA Tax Audit improvement and Governance Framework is three fold:

- Comply with constitutional requirement Art 47(1)**
- Improve on efficiency and effectiveness of audit activities**
- Positive response to public feedback**

TRANSPARENCY OF AUDIT AND INVESTIGATION CASE SELECTION BY KRA

- a) **Independent case selection and risk analysis unit-** To deal with identification of specific risk issues to be addressed during the audits. The unit collect and collate data from various internal and external sources to direct audit.
- b) Focus of all audits on specific issues (issue based audits) as opposed to comprehensive audits
- c) To enhancement resource capacity within BIO to expand the capacity to generate sufficient quality intelligence

QUALITY OF KRA AUDIT NOTICES

- a) To implement a template for notices which specifies issues under audit or investigation. Any offshoots or widening of scope to be approved and formalized
- b) Notices for different interventions to be differentiated by their purpose, scope.
- c) The nature of documents requested to reflect the scope of the intervention
- d) Specimen notices have been developed and implemented by 1st of November 2014 as directed.
- e) Various manuals to be amended to reflect amended notices.
- f) Notices to include express disclaimer restricting findings to work done thus future audits/investigations can be conducted when new information emerge

SCOPE OF WORK UNDER COMPLIANCE, AUDITS AND INVESTIGATIONS BY KRA

- a) Enforcement of compliance with agreed scope e.g. One year for compliance checks and two years for audits except under approval for a period not exceeding 7 years
- b) Enforcement should be through close supervision and continuous monitoring through quality assurance processes.
- c) iTax to assist in addressing scope of compliance interventions as actions will be generated through the system.
- d) Specification of issues to address coverage of issues not specified at planning stage.

CONDUCT OF SEARCHES AND RETENTION OF RECORDS BY KRA

- a) Regional/Station managers to be informed once a search is undertaken for information.
- b) Search guidelines to be shared with other departments for a better understanding of process.
- c) Records seized to be returned within a reasonable period and the departments to be notified to enable them proceed with any necessary interventions.
- d) I & E to return records seized that have been outstanding for a long time and departments notified as appropriate

KRA TAX AUDIT REPORT

- a) All reports to be standardized to include key components e.g. Taxpayer identity, period of audit, tax type audited, risk identified under preliminary analysis, tests done, outcomes and tax charged.
- b) Reports to be uploaded on the rulings database for ease of access by all with effect from July 2014 reports.
- c) All reports and findings letters to taxpayers to contain a disclaimer that the findings are limited to the issues covered during the intervention and that a different enquiry can be initiated where new information becomes available.

CONTROL OF AUDIT AND INVESTIGATION ACTIVITIES BY KRA

Complaints have been reported about audit and investigation staff on integrity, low quality work and lack of capacity.

- a) Increased supervision of audit and investigation officers by Chief Managers and Audit managers. The Small taxpayers segment in MST is to establish **Regional Audit centers of Excellence** to follow the pattern of central control in LTO and MTO gradually beginning 1st March 2015.
- b) Build staff capacity in terms of skills, numbers and resources at the quality monitoring units for effectiveness. Centralization of audit policy units is recommended for synergy and effectiveness
- c) Standard reporting across the audit and investigation programs- Currently the reporting is not standard

ADDRESSING INTEGRITY OF KRA AUDITORS AND INVESTIGATORS

- ❖ **Uploading of audit settlement reports in the database.** This will not only create transparency, but also reduce duplications of audit by the various tax compliance programs including investigation and also provide valuable knowledge based on risk behavior of taxpayers based on the audit records
- ❖ **Increased staff supervision.**
- ❖ **Lifestyle audits**
- ❖ **Working closely with the ethics and Integrity program** to develop a testing program relevant to audits and investigations to effectively deal with any integrity cases that may emerge.
- ❖ **Standardize the process of resolving objections through technical committees.**
- ❖ **Implementing a structured ADR process**

EMERGING TAX ISSUES... ADR

- ❖ Alternative Dispute Resolution (ADR) Mechanism is a voluntary, participatory and facilitated discussion over a tax dispute between a taxpayer and the KRA
- ❖ It is not arbitration since the ADR facilitator has no powers to decide the case.
- ❖ The objectives of ADR are:
 1. **Provide a focused approach to dispute resolution**
 2. **Provide for timelines for resolving tax disputes**
 3. **To compliment the existing internal disputes resolution mechanism**

BENEFITS OF ADR.

- ❖ **Expedite resolution of tax disputes.**
- ❖ **Decreases cost of court litigation.**
- ❖ **Enhances and manages relationships between KRA and Taxpayers.**
- ❖ **It provides confidentiality (away from the glare of public and business competitors)**



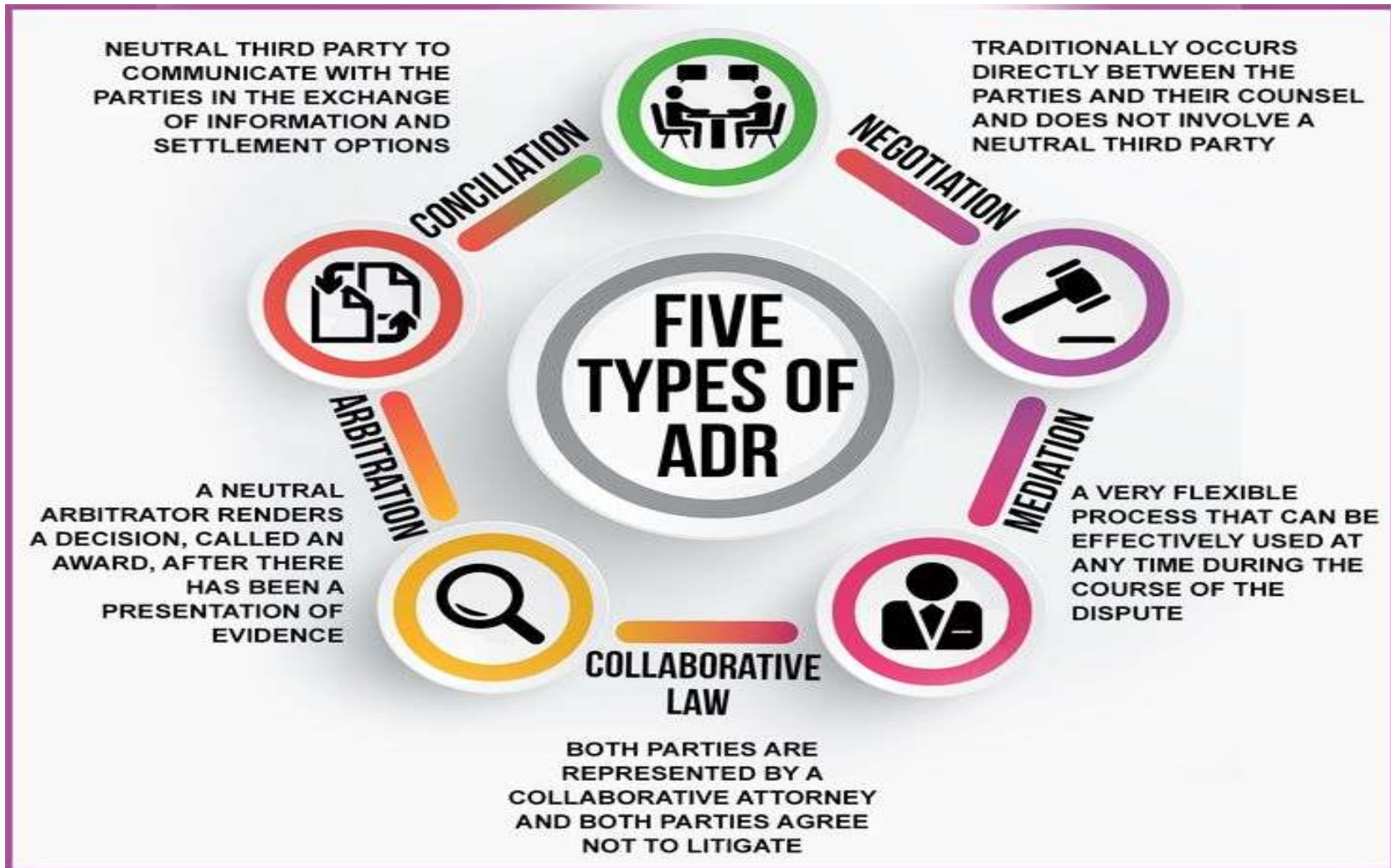
DISPUTES FOR ADR

- ❖ Those with complex factual or quantum issues in contention
- ❖ Cases with evidential difficulties
- ❖ Cases whose settlement will promote tax compliance by the tax payer

The following Disputes are inappropriate for ADR

- ❖ Tax evasion or fraud disputes
- ❖ Disputes whose settlement will be against laid down statutes
- ❖ Disputes which require judicial clarification

TYPES OF ADR



EMERGING TAX ISSUES.... I TAX

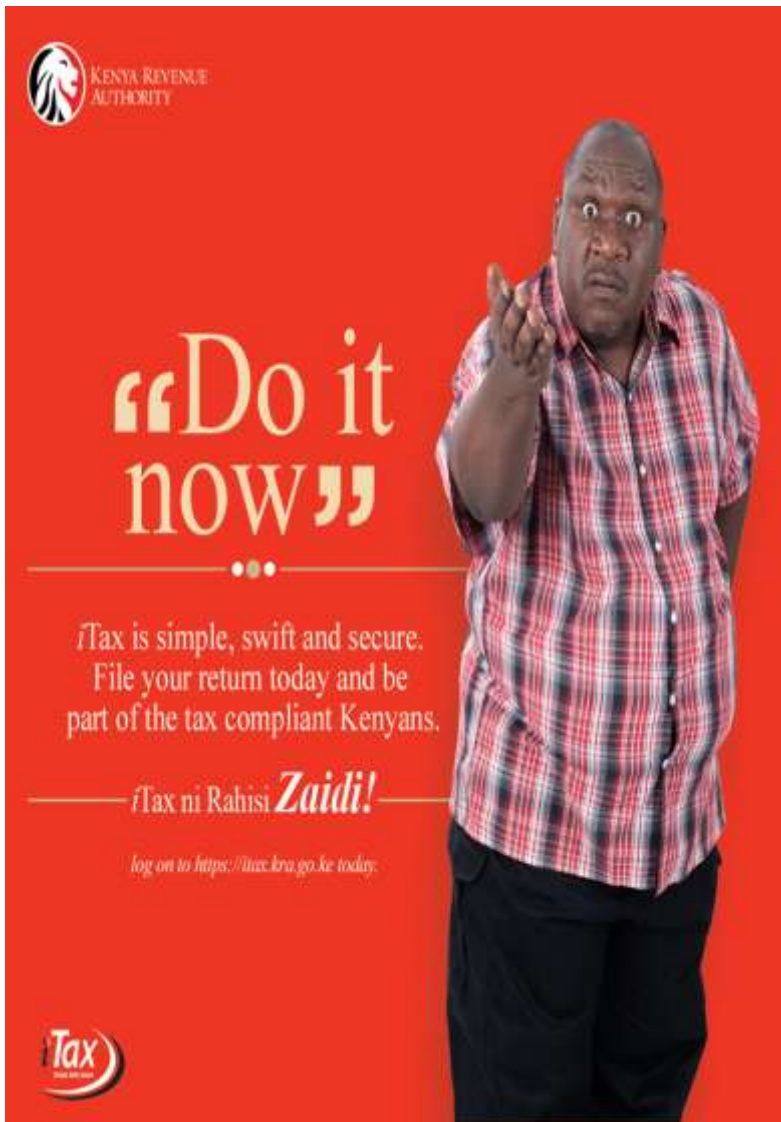
- ❖ Online tax filing and payment system launched by KRA.
- ❖ Kenya Revenue Authority (KRA) digitized tax collection system, which is linked to 37 commercial banks
- ❖ More than 2 million taxpayers have filed their returns online
- ❖ Has helped facilitate VAT refund audits
- ❖ KRA is not accepting manual returns anymore.
- ❖ Between January 1 and June 8 this year, the iTax platform's payment gateway featured more than 3.5 million active taxpayers.
- ❖ i tax processed transactions worth Sh 280 billion in just five months this year.

EMERGING TAX ISSUES.... BENEFITS OF I TAX



- ❖ Reduction in the cost of tax administration.
- ❖ Improvement in the transparency of tax administration.
- ❖ Increase in the level of tax compliance.
- ❖ Has reduced the cost of tax compliance to the taxpayer

CHALLENGES FACING I TAX



KENYA REVENUE AUTHORITY

“Do it now”

iTax is simple, swift and secure.
File your return today and be part of the tax compliant Kenyans.

iTax ni Rahisi Zaidi!

log on to <https://itax.kra.go.ke> today.

iTax

- ❖ Difficulty in accessing the system during peak periods.
- ❖ Lack of knowledge by users on how the system operates.
- ❖ Filing of returns for 2012 and the prior years

What are the threats and opportunities in i-tax for ACCOUNTANTS????.... LETS DISCUSS

TAX AMNESTY



For rental income
that is **above**
Ksh 10 million, the tax
payable will be calculated
using the graduated scale with taxes
ranging from 10% to 30%



#RentalIncomeTax

- ❖ Aimed at increasing tax compliance.
- ❖ Aimed at widening the tax base by netting in more landlords into the tax bracket.
- ❖ Increase government revenue.
- ❖ Can help in sealing revenue leakage

RECENT TAX AMNESTY BY GOVERNMENT



- ❖ Government is providing **tax amnesty for individuals taxpayers who own assets and businesses outside the country** and would be willing to reinvest back home.
- ❖ The government also provided **tax amnesty to landlords** and targeted to collect Kshs. 3 billion from rental income in 2015/16 FY. **How effective has this been and what are the challenges?**

TAX PROCEDURE ACT 2015

- The Tax Procedures Act (TPA) 2015 was assented into law on 15th December 2015 and effected through a legal notice issued on 14th January appointing 19th January as the commencement date.
- The procedures outlined in the new act apply to all taxes in Kenya, unless provided in a tax law specifically for the administration of a specified tax, from 19th January 2016.
- **Registration of Taxpayers (Sec 8 & 10):-** TPA Act requires persons who have attained the tax liability age or expect to accrue tax liability under the Income Tax Act or the VAT Act- to apply to the Commissioner for registration within 30 days.

TPA 2015 KEY PROVISIONS

- **Tax Agency(Sec 19-22):-**TPA provides for the registration of individuals or partnerships wishing to discharge the role of a tax agent, through an application to the Commissioner. The provision also bars persons, other than tax agents, from representing tax payers or discharging the roles of a tax agent. *This provision intends to promote accountability through the regulation of tax agents.*
- **Interest on Late Payment:-** TPA has reduced the late payment interest rate from 2% to 1% per month, *providing relief to tax payers.*
- **Extensions for Filing of Returns & Payment of Taxes:-** TPA for the extension of time to file returns and pay taxes, through an application to the commissioner prior to the due dates.

TPA 2015..... OFFENCES AND PENALTIES

OFFENSE		PENALTY
1.	Failure to Register or deregister for tax purposes	KES 100,000 per month but not more than KES 1 Million
2.	Failure to retain records and documents	10% of the amount payable to which the document relates Where no tax is payable for the reporting period, KES 100,000 shall apply as the penalty
3.	Late submission of returns	<ul style="list-style-type: none"> •PAYE – the higher of 25% of the amount due or KES 10,000 •Turnover Tax – KES 5000 •In the case of any other return- the higher of 5% of the tax payable or KES 20,000
4.	Failure to comply with electronic tax system	KES – 100,000
5.	Tax Avoidance	Double the tax liability

..... **THANK YOU**

