

IAS 12 Income Tax Issues Relating to SMEs

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Agenda



-
- 01** Introduction
 - 02** Taxation of SMEs in Kenya
 - 03** Turnover tax
 - 04** Deferred tax
 - 05** Q&A



Introduction



Introduction

Companies Act 2015

1

Revenues < KES 50M



2

Employees < 50



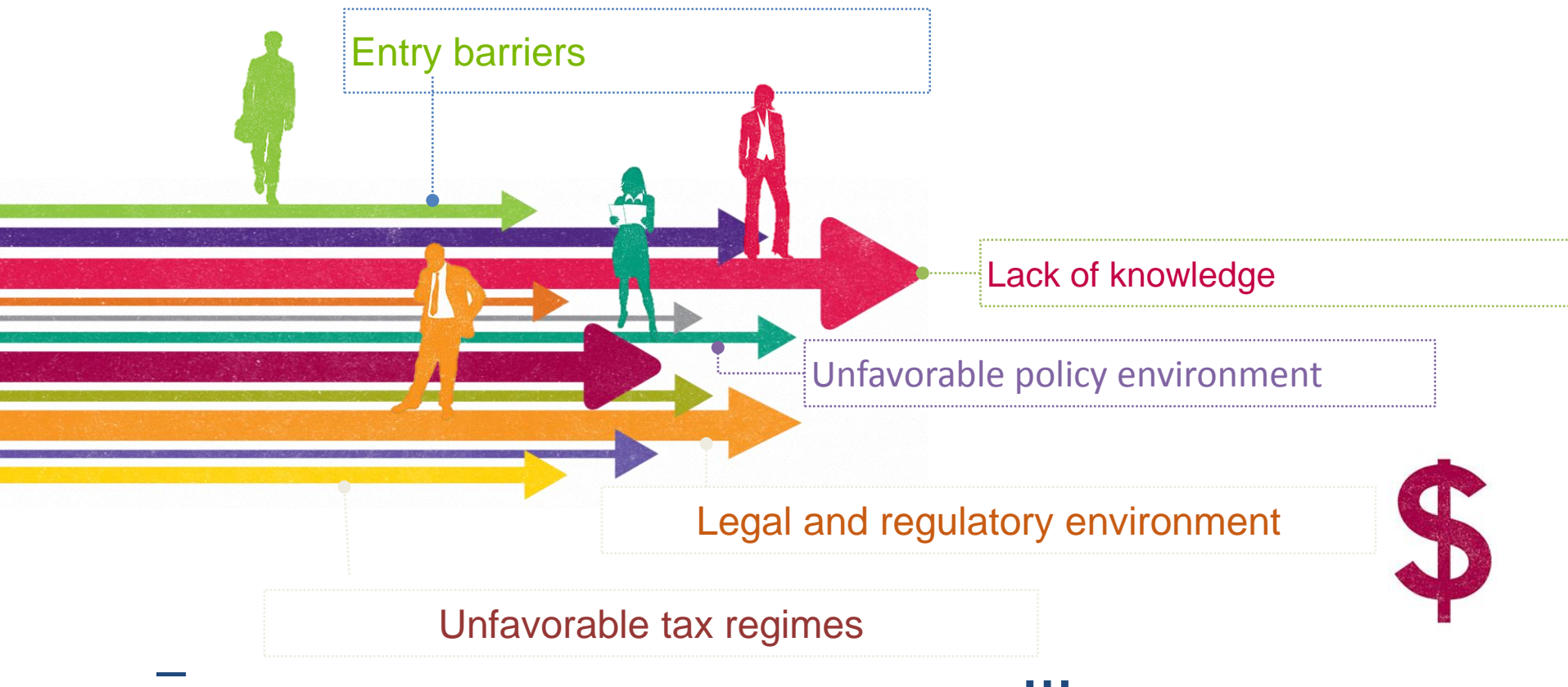
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Assets < KES 20M

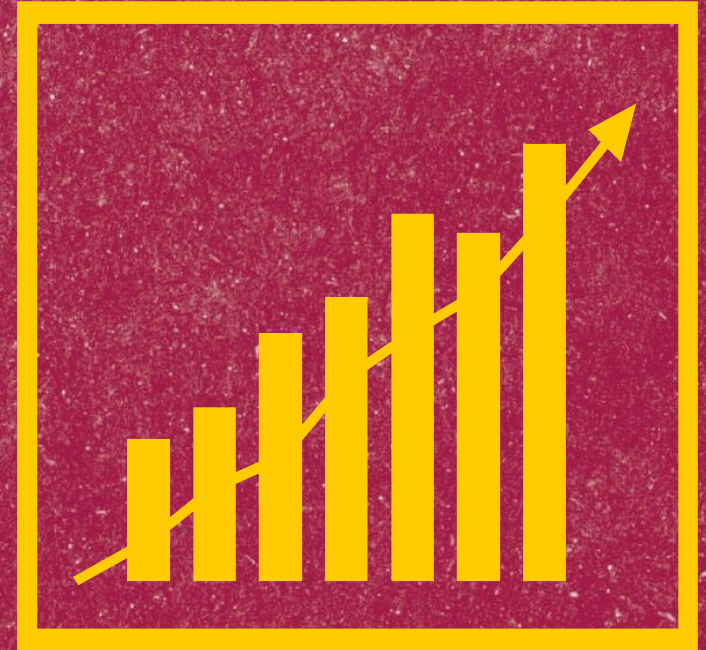


Introduction

– Some tax/economic factors...



Taxation of SMEs in Kenya: Thoughts?



Taxation of SMEs



**Taxes
applicable:**



Corporation tax



PAYE



Withholding tax



Turnover tax



Value Added Tax

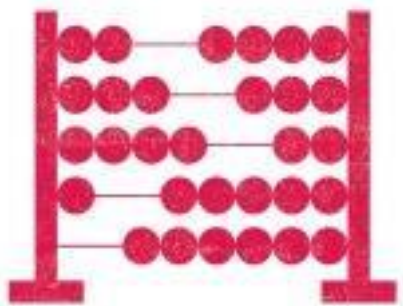


Customs & Excise
Duty



Taxation of SMEs

Incomes taxable:



Business



Rent



Employment
income



Dividend or
interest



Agricultural income



Pension



* Any amount deemed under the ITA to be the income of a person

Taxation of SMEs

What is business?

1

– **Includes:**

any trade, profession or vocation, and every manufacture, adventure and concern in the nature of trade,



2

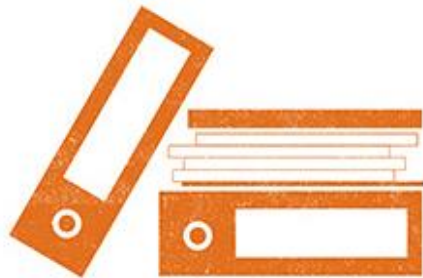
– ... but does not **include:**

Employment!



IAS 12

Disclosure in the
notes to the profit
and loss account :



Tax expense is the aggregate amount included in the determination of profit or loss for the period in respect of current tax and deferred tax (12.5)

Deferred tax movement:



prior period under/over provision
deferred tax asset not previously recognised (12.79)



Current Tax



Computation of taxable income



	Ksh	Ksh
Net profit per accounts/ ledger for a source		XX
ADD		
Non-allowable expenses for the source	XX	-
Expenses relating to exempt income	XX	XX
LESS		
Capital Allowances		
Other deductible expenses for the source	(XX)	
Exempt Income	<u>(XX)</u>	<u>(XX)</u>
Adjusted Profit/(Loss) for Tax		XX

Allowable expenses



Expenditure wholly and exclusively incurred in the production of income for that year of income

Legal expenses and stamp duties on acquiring a lease on premises not exceeding 99 years

Legal and other costs in publicly issuing shares and debentures

Capital allowances

Expenses incurred prior to the commencement of business that would have been deductible if incurred after the date of commencement

Allowable expenses



Expenditure on agricultural land clearance and planting of semi/permanent crops

Cost of structural alterations to premises, incurred by a landlord to maintain the rent (non-capital)

Expenses incurred by a lessee, in leasing transactions

Interest paid on borrowings made to generate investment income (but restricted to the amount of investment income earned)

Expenditure on scientific research

Allowable expenses



Donations to approved charitable organisations

Bad debts written off which satisfy the following:

- ✓ Commissioner's guidelines: The debt was wholly and exclusively incurred in the normal course of business;
- ✓ The debt is not of a capital nature; and
- ✓ The debt has become uncollectable

Bad debts



A debt is uncollectable where:

- ✓ The creditor loses the contractual right of a debt through a court order;
- ✓ No form of security or collateral is realizable;
- ✓ The securities or collateral realized are unable to cover the entire debt;
- ✓ The debtor is adjudged insolvent or bankrupt by a court of law;
- ✓ The costs of recovering the debt exceeds the debt itself; or
- ✓ Efforts to collect the debt are abandoned for another reasonable cause

Capital Allowances



Capital Allowances	Rate (%)
Investment Deduction	100/150*
Industrial Building Allowance	10
Wear & Tear Allowance	
Class I (tractors, combine harvesters, heavy earth-moving equipment and such other heavy self-propelling machines)	37.5
Class II (computers and peripheral computer hardware, calculators, copiers and duplicating machines)	30
Class III (other self-propelling vehicles, including aircraft)	25
Class IV (all other machinery, including ships)	12.5
Section 15 2 (g) (diminution in value of any implement, utensil or similar article)	33.33
Farm works deduction	100
Software allowance	20
*150% rate applies to investments outside Kisumu, Nairobi & MSA	

Disallowable



Expenditure not wholly and exclusively incurred in the production of income

Capital costs and losses

Income tax, compensating tax and similar taxes

Personal expenses, other than those incurred specifically in the course of business

Expenses of non-resident persons relating to certain types of income – interest, management fees, royalties etc

Pension contributions to unregistered pension schemes

Corporation taxes



- Current year
- Prior year
- Estimation of current years tax
- 25% of 110% of tax assessed for the previous year



“Current year basis is more appropriate where the operating results fluctuate substantially. In case of variance of 10% or more, penalties and interest are levied”



Turnover Tax

“Who does this apply to?”



TOT

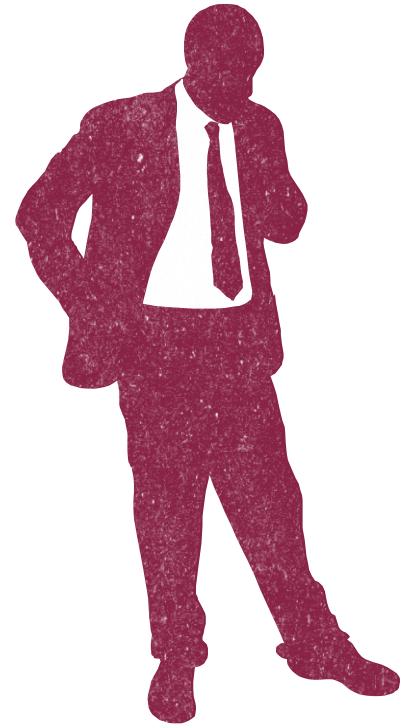


Applicable to any resident person whose income from business does not *exceed KES 5M* during any year of income

The tax rate is **3% on gross income**

Turnover tax not applicable to:

- a) rental income, management or professional fees or training fees;
- (b) the income of incorporated companies; or
- (c) any income which is subject to a final withholding tax



Deferred Tax



Accounting for the tax consequences of the future recovery/settlement of the carrying amount of assets/liabilities in a company's balance sheet.

IAS 12 (effective from 1998) uses the balance sheet liability method (as opposed to the deferral method) and focuses on 'temporary differences' existing at the balance sheet date



Deferred Tax



Temporary differences are differences between the carrying amount of an asset or liability in the statement of financial position and its tax base. Temporary differences may be either:

- (a) taxable temporary differences; or
- (b) deductible temporary differences.



Deferred Tax



The IAS 12 approach to calculating deferred tax

Carrying amount of asset/liability	X
Less: tax base of asset/liability	(X)
Temporary difference	<hr/> X
@applicable tax rate	X%
Deferred tax asset/liability	<hr/> <hr/> X

Deferred Tax



Loss as per accounts		(264,209,255)
Add:		
Unrealised forex loss	23,344,822	
Depreciation	17,516,525	
General Penalties and Fines	3,407,482	
Increase in bad debts provision	1,298,950	
Gifts & Donations	660,000	
Expensed Assets	531,771	
Amortisation	412,493	
Telephone Benefit	298,096	
Prior year unrealised Foreign exchange gain	26,723	47,496,862
Less:		
Unrealised forex gain	(27,825,564)	
Wear and tear allowance	(13,267,267)	
Section 15(2)(g) allowance	(131,192)	
Software allowance	(756,626)	
Prior year Unrealized forex loss	(333,121)	
Gain on disposal	(63,062)	(42,376,832)
Adjusted loss for the year		(259,089,225)
Loss BF		(393,898,309)
Loss CF		(652,987,535)



	Opening balance KShs	Closing balance KShs	Movement KShs
NBV on Property, Plant and equipment	70,076,986	59,978,355	(10,098,631)
NBV on Software	101,017	3,262,924	3,161,907
Non-qualifying element on motor vehicles	(6,535,206)	(5,332,659)	1,202,547
	63,642,797	57,908,620	(5,734,177)
Wear and Tear WDV	(66,496,083)	(60,824,126)	5,671,957
Software allowance	(136,903)	(2,950,740)	(2,813,837)
Section 15(2)(g)	(106,074)	(91,160)	14,914
Temporary differences on PPE	(3,096,262)	(5,957,406)	(2,861,144)
30%	(928,878.73)	(1,787,221.83)	(858,343.09)
Other temporary differences			
Unrealised exchange loss	(333,121)	(23,344,822)	(23,011,701)
Unrealised exchange gains	26,723	27,825,564	27,798,841
provisions	(1,927,260)	(3,226,210)	(1,298,950)
Tax Losses	(393,898,309)	(652,987,535)	(259,089,225)
	(396,131,967)	(651,733,003)	(255,601,036)
30%	(118,839,590)	(195,519,901)	(76,680,311)
Total Deferred tax	(119,768,469)	(197,307,123)	(77,538,654)



Proof of Tax



				KShs	KShs
Current tax charge				-	
Deferred tax movement				(77,538,654)	(77,538,654)
Accounting profit/(loss) before tax				(264,209,255)	
Theoretical tax thereon @		30.0%			(79,262,777)
Variance					1,724,123
Items increasing tax charge					
Ineligible depreciation				1,782,426	
Permanent differences					
General fines and penalties				3,407,482	
Gifts and donations				660,000	
Telephone benefit				298,096	
PPE differences				(337,867)	
Gain on disposal of assets				(63,062)	
				5,747,075	
Tax @ 30%					1,724,123
Variance					0



Reconciliation of PPE



		KShs	KShs
	Depreciation charge for the year	17,516,525	
	Ammortisation	412,493	
Less: Non-qualifying portion:			
	Non-qualifying element of motor vehicles	(1,782,426)	16,146,592
Capital allowances			
	Wear and tear allowance	(13,267,267)	
	Software allowance	(756,626)	
	Section 15(2)(g)	(131,192)	
			(14,155,085)
Add:			
	Capital items expensed		531,771
	Movement in temporary differences on PPE		(2,861,144)
	Variance		(337,867)



Q&A



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