

**PROVISION REQUIRING PAYMENT OF CAPITAL GAINS TAX BEFORE TRANSFER OF PROPERTY DECLARED
UNCONSTITUTIONAL**

The High Court has declared Paragraph 11A of the Eighth Schedule of the Income Tax Act unconstitutional, null and void. This was after the Law Society of Kenya (LSK) filed a petition challenging the constitutionality of the provision which they argued was inconsistent with paragraph 2 as read with paragraph 6 (1) of the same Schedule. Further to this, the LSK argued that paragraph 11A violated Articles 10 (1) and (2), 40 (2) (a) and 201 (b) (i) of the Constitution.

The Kenya Revenue Authority (KRA) had through a notice issued in October 2016 required that payment for Capital Gains Tax (CGT) and stamp duty be done through its ITAX platform. Further, the notice provided that the tax point for the payment of CGT would be on or before an application for transfer of the property was done.

Effectively, these requirements put the process of transfer of real property in disarray as it meant that the vendor had to account and pay the CGT before the process of conveying real property, as known in Kenya, was complete.

The LSK argued that the charging section of the Act, Section 3 (2) (f), provides for chargeability of the gain which accrues on the transfer of the property. Further, that paragraph 2 of the Eighth Schedule provides for charging of the tax only upon transfer of the property.

The KRA, in its defense, asserted that paragraph 11A was enacted to provide certainty and clarity as to the tax point for the charge of CGT. Further, that the section was in tandem with International Accounting System which recognize revenue when earned as opposed to when it is received.

The court, in coming up with the decision, analyzed the principles governing interpretation of statutes. In that, the court looked at the objects, purpose and effects of the particular provision of the ITA to

determine whether it was constitutional or not. Further, the court stated that one of the fundamental ingredient of the rule of law is certainty. In this sense, for a law to qualify as constitutional, it has to be explicit in its mandate, explicit in its enforceability and provide definition of potentially vague terms.

The court went further to illustrate the vagueness produced by paragraph 11A in that it contradicted the paragraph 2 and 6 (1) (a) of the same schedule by giving the due date for CGT as on or before transfer of property whereas paragraph 6 (1) (a) indicates that a transfer occurs when property is sold, exchanged, conveyed or otherwise conveyed.

The definition of "transfer" as per the Land Registration Act was also referred to show that it denotes transfer as having taken place after filing of the instrument and registration of the buyer as the proprietor of the property.

In addition, the court stated that the effect of paragraph 11A meant that a vendor who is not financially able to pay the CGT out of their pocket could not enjoy the constitutionally guaranteed right to dispose of his property. Ultimately, the court found that the paragraph did not meet the constitutional test of rationality and proportionality and was therefore unconstitutional.

The effect of this decision is that the KRA has lost the power to collect CGT before transfer of property. As such, for now, they only have powers to collect CGT only after the buyer of property has been registered as the proprietor of such property.

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☎ 020 2217150

✉ Info@taxwise-consulting.com

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