

Tax Alert

Errant landlords snared

Rental income has always been taxable...so why the fuss?

Kenya has witnessed unprecedented growth in the real estate sector, more notably in Nairobi and its outskirts, which according to the KRA is not commensurate to the contribution to the tax kitty.

This has been interpreted to mean that errant landlords do not remit tax to the exchequer as prescribed by the tax legislation.

To cure this mischief, the Finance Minister in his budget statement read on 14 June 2012 outlined measures Kenya Revenue Authority intended to bring non-compliant landlords into the tax net.

This has brought about speculations of rent hikes to offset the tax man's demands.

In an effort to clarify the issue, the KRA issued a public notice on 6 September 2012 on taxation of rental income.

This is not a new law

Rental income, comprising of rent, a premium or similar consideration, has been subject to income tax. In addition, rent on non-residential buildings is also VATable under the VAT Act.

Rental income unless specifically exempted is taxable.

Taxation

Resident companies receiving rental companies will be required to assess such income to tax at the corporation tax rate of 30%.

Rent income in the hands of a resident individual will be subject to tax at the graduated scale illustrated below.

On the first KES 121,968	10%
On the next KES 114,912	15%
On the next KES 114,912	20%
On the next KES 114,912	25%
On all income over KES 466,704	30%

However, non-residents will suffer withholding tax at 30% on rental income on immovable property which will be a final tax. Non-residents do not qualify to claim any expenses.

Rental income arising from non-residential buildings is subject to VAT at the rate of 16%.

In case of deceased landlords, the estate administrator or legal personal representative is expected to account for the relevant taxes.

Declaration of rental income

Taxpayers are required to declare the gross rent income but pay tax on net income. This means that property owners should first deduct all expenses that are wholly and exclusively incurred in the production of income in line with the provisions of section 15 of the Income Tax Act (ITA) e.g. interest, repairs, maintenance, caretaker costs, land rates, etc.

Where loans are taken out to finance the acquisition or construction of rental property, the principal payment towards the loan is not deductible but the interest is deductible.

In the event that the above computation results in a tax loss position, the tax payer is allowed to carry forward the loss for the subsequent four years of income or apply to the Commissioner for an extension where the tax payer is unable to extinguish the loss within the four-year limit.

Property owners will also be entitled to capital allowances in line with the provision of the Second Schedule to the ITA.

Tax incentives available for landlords

Landlords are allowed to claim:

- Industrial building allowance on the cost of construction as per paragraph 1(1) of Second Schedule to the ITA. The applicable rates will depend on the nature, use and area the building constructed.
- Commercial building allowance at 25%, effective 1 January 2013 on a building in use as an office, shop or showroom provided the

To set the record straight, net rental income has always been taxable.

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- investor provides roads, power, water, sewers and other social infrastructure
- c) Wear and tear allowance on machinery and equipment as per Paragraph 7 of the Second Schedule to the ITA.

Tax incentives available for developers

The incentives that exist for property developers include:

- a) Real Estate Investment Trusts (REITs): Income in respect of a REIT is not taxable under the ITA. A REIT is a vehicle which allows investors to pool resources together and invest in real estate. The shareholders of REITs acquire units which are tradable at the stock market. The mode of taxation is the same as that of unit trusts which are tax exempt on their investment income. Although this incentive is available effective 1 January 2012, the implementation is dependent on the regulations yet to be issued by the CMA.
- b) VAT remission on low income housing projects: This incentive is meant to encourage housing provision to low income earners.
- A low income earner means a person whose monthly gross earning amount to KES 35,000 or less.
 - A low income house means a house put up at a construction cost of not more than KES 1,600,000 and of plinth area of not less than 30 square meters.

- A low income housing project means a project of not less than 20 housing units intended for low income earners.

No provision of amnesty

Amnesty is a tax waiver (forgiveness) granted by the Finance Minister in respect of an amount of tax evaded in the past and penalties therein or any interest and penalties payable on any previously undisclosed income but not the tax itself.

Presently, there's no provision for tax amnesty presently.

Should you require clarification or guidance please contact.

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