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Advanced Payment of CGT Declared Unconstitutional

On 14th March 2017, in a constitutional petition filed by the Law Society of Kenya (LSK), the High Court declared paragraph 11A of the Eight Schedule to the Income Tax Act (ITA) (Paragraph 11A) as unconstitutional. The offending paragraph was introduced in an amendment to the ITA under the 2015 Finance Act. Essentially, in an attempt to create certainty on payment of capital gains tax (CGT) and streamline operations of the Kenya Revenue Authority (KRA), paragraph 11A requires capital gains tax on the transfer of real property to be made on or before the date of application for transfer of the property at the relevant Lands Office. This contradicted the general provisions of the ITA which require CGT to be paid on the transfer of property as read with the Land Registration Act (LRA) which provides that a transfer of property is completed by filing of the relevant instrument and registration of the transferee as proprietor of the land at the Lands Office.

The effect of Paragraph 11A was to make CGT payable prior to the transfer of the property. In practice, this meant that a seller was required to have CGT funds in place before conclusion of the transaction and make payment to KRA before legal ownership passed to the buyer.

This placed a seller without the requisite CGT funds in a precarious position in completing a transaction. Accordingly, the Courts held that Paragraph 11A violates Article 40(2) (a) of the Constitution as it is a law which arbitrarily deprives the public of their right over property and is therefore unconstitutional.

It should however be noted that, in spite of demands made by LSK, KRA has not updated its i-Tax portal to comply with the court order. The online portal still requires assessment and payment of CGT before: (i) stamp duty is paid and; (ii) the property transfer is completed in accordance with the provisions of the LRA. LSK has reserved its right to cite KRA for contempt in this regard.

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