

10 Tax Mistakes Small Businesses in Kenya Make (And How to Avoid Them)

Introduction

Navigating the tax landscape in Kenya can be challenging for small businesses. The Kenya Revenue Authority (KRA) continuously updates its regulations, and staying compliant is crucial to avoid penalties and foster sustainable growth. This guide highlights ten common tax mistakes made by small businesses in Kenya and provides practical advice on how to avoid them, ensuring a smoother tax journey for your enterprise.

1. Failing to Register for the Correct Tax Obligations

Many small businesses, especially startups, often fail to register for all necessary tax obligations with KRA. This can lead to non-compliance and future penalties.

How to Avoid:

- **KRA PIN Registration:** Ensure your business has a KRA Personal Identification Number (PIN). If operating as a company, the company must also have its own PIN.
- **VAT Registration:** If your annual turnover exceeds KES 5 million, you are legally required to register for Value Added Tax (VAT). Even if below the threshold, you might opt for voluntary registration if most of your clients are VAT-registered businesses.
- **PAYE, NHIF, NSSF:** If you have employees, you must register for Pay As You Earn (PAYE), National Hospital Insurance Fund (NHIF), and National Social Security Fund (NSSF) deductions.
- **Turnover Tax (TOT):** Businesses with gross turnover between KES 1 million and KES 50 million are eligible for TOT, which is simpler than corporate income tax.

Ensure you are registered for the appropriate tax regime.

2. Poor Record-Keeping

Inadequate or disorganized record-keeping is a common pitfall. KRA requires businesses to maintain proper records for at least five years.

How to Avoid:

- **Digital Records:** Utilize accounting software (e.g., QuickBooks, Sage, or even robust spreadsheets) to keep track of all income and expenses.
- **Categorize Transactions:** Clearly categorize all transactions. This simplifies tax computations and makes audits easier.
- **Retain All Documents:** Keep all invoices, receipts, bank statements, M-Pesa statements, and other financial documents, both physical and digital.

3. Missing Filing Deadlines

Late filing of tax returns is a direct route to penalties and interest charges from KRA.

How to Avoid:

- **Calendar Reminders:** Set up reminders for all KRA deadlines (e.g., VAT by 20th, PAYE by 9th, Income Tax by 30th June for previous year).
- **Automate:** Consider using accounting software that can generate reports quickly or engage a tax consultant to manage your filings.
- **File Even When No Tax is Due:** Always file NIL returns if you have no transactions for a period, to avoid penalties for non-filing.

4. Incorrectly Calculating Taxable Income and Deductions

Errors in calculating taxable income or claiming incorrect deductions can lead to underpayment of tax and subsequent KRA audits.

How to Avoid:

- **Understand Allowable Expenses:** Familiarize yourself with what constitutes an allowable expense for tax purposes. Personal expenses are generally not deductible.
- **Professional Advice:** Consult with a tax expert to ensure accurate calculations and to maximize legitimate deductions.
- **Review Regularly:** Periodically review your financial statements and tax computations.

5. Non-Compliance with eTIMS

The Electronic Tax Invoice Management System (eTIMS) is mandatory for all businesses. Failure to comply can lead to significant penalties.

How to Avoid:

- **Register for eTIMS:** Ensure your business is registered and actively using an eTIMS-compliant solution for issuing invoices.
- **Training:** Train your staff on how to correctly use the eTIMS system.
- **Integration:** If using an accounting system, ensure it is integrated with eTIMS for seamless invoice generation and transmission to KRA.

6. Ignoring Withholding Tax (WHT) Obligations

Many small businesses overlook their duties as withholding agents, failing to deduct and remit WHT on certain payments.

How to Avoid:

- **Identify WHT Applicable Payments:** Understand which payments attract WHT (e.g., professional fees, consultancy fees, royalties, rent).
- **Deduct and Remit:** Ensure WHT is correctly deducted at the prescribed rates and remitted to KRA by the 20th of the following month.
- **Issue Certificates:** Provide WHT certificates to the payees.

7. Commingling Business and Personal Finances

Mixing personal and business funds makes it difficult to track business expenses and income accurately, complicating tax computations and audits.

How to Avoid:

- **Separate Bank Accounts:** Open a dedicated bank account for your business.
- **Avoid Personal Use of Business Funds:** Do not use business funds for personal expenses and vice-versa.
- **Clear Documentation:** Ensure all transactions are clearly documented as either business or personal.

8. Not Reconciling KRA Statements

Ignoring KRA statements or failing to reconcile them with your internal records can lead to discrepancies and unresolved tax issues.

How to Avoid:

- **Regular Reconciliation:** Periodically download your KRA ledger statement from iTax and reconcile it with your business records.
- **Address Discrepancies Promptly:** Investigate and resolve any differences immediately with KRA.

9. Lack of Tax Planning

Many small businesses focus only on compliance and neglect proactive tax planning, missing opportunities to legally reduce their tax burden.

How to Avoid:

- **Annual Tax Review:** Conduct an annual review of your business structure and operations with a tax consultant.
- **Utilize Incentives:** Be aware of any tax incentives or reliefs offered by the government for small businesses or specific industries.

- **Budget for Taxes:** Incorporate tax payments into your financial planning and budgeting.

10. Not Seeking Professional Tax Advice

Attempting to handle all tax matters internally without expert knowledge can be costly in the long run.

How to Avoid:

- **Engage a Tax Consultant:** Partner with a qualified tax consultant or CPA who specializes in Kenyan tax law.
- **Stay Informed:** While consultants handle the heavy lifting, stay generally informed about major tax changes.
- **Regular Check-ins:** Schedule regular meetings with your tax advisor to discuss business changes and their tax implications.

Conclusion

Avoiding these common tax mistakes is vital for the financial health and compliance of your small business in Kenya. By maintaining diligent records, adhering to deadlines, understanding your obligations, and seeking professional guidance, you can navigate the KRA landscape with confidence and focus on what you do best – growing your business. Tax Home Kenya Limited is here to simplify your tax journey, offering expert advice and services tailored to your needs.