Banks sue to fight 15pc tax on hedging deals

Cont. from p1

respondent (Treasury CS) did not prepare a regulatory impact statement prior to making the regulations, as required by law," the KBA, which has 47 members among the banks and microfinance institutions, said in the petition.

The regulations require Kenyan entities transacting with foreigners to cushion themselves from volatility in financial markets to account for any profit made by foreign parties and remit the tax to the Kenya Revenue Authority (KRA).

Interest rate risks materialise when such borrowing is adversely affected by fluctuations in the price (interest rate) attached to it. The Treasury said the tax was meant to help widen Kenya's revenue base with a focus on non-resident transactions.

Banks, however, said the law imposes an unreasonable and oppressive burden on residents to assume that their losses on derivative transactions equate to gains of non-residents.

Further, the banks claim that the law was passed without stakeholder input. The association wants the court to suspend the regulations temporarily, saying KRA can still recover the tax in case KBA loses the case, but it will be an uphill tax for the taxpayer to get back their money in case they are successful in the petition.

"It is, therefore, in the interest of justice and balancing the rights of the parties that this case warrants protective measures in terms of the interim orders as prayed," the petition reads.

Justice John Chigiti certified the case as urgent and directed KBA's lawyers to serve the Treasury CS, KRA and the Attorney General with the court documents. The case will be mentioned on June 5.

The KBA says in the petition that the regulations do not say how the gains will be computed for non-residents and it is impossible for a resident to calculate the gains of a non-resident person.

It was revealed that Parliament called for the submission of memoranda on the regulations from stakeholders but when KBA was ready to present its position, it was informed that the regulations started working on January 27.

47

The KBA membership

The KBA said KRA may proceed and implement the regulations and demand payments from banks.

The banks also said financial derivative transactions are entered into using a standard international Swap Dealers Association master agreement, pursuant to which there is a grossing-up provision.

The provision, KBA says, requires the party in Kenya to 'gross up' the payment made to the non-resident person on account of any taxes charged in Kenya and the ultimate cost of any tax would be borne by the Kenyan party.

"In instances where no payment is made to a non-resident, Kenya Revenue Authority would be seeking to collect a payment from a party which has already made a tax loss for Kenyan purposes," KBA said, adding that the regulations impose a further unfair tax burden on the resident person by characterising the gains from a financial derivative as a separate income.