

# THE MISSING TRADER FRAUD SCHEME

## The Kenyan Experience

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*“Rather fail with honor than succeed  
by fraud.*

*-Sophocles-*

# BACKGROUND

- Missing Trader arose early 2016 when the Authority realized that taxpayers were claiming input VAT while no authentic purchase documents were presented.
- In fact, with a robust investigative process, it was realized that some taxpayers were indeed in the business of issuing Tax Invoices.
- This prompted KRA in 2019, to introduce the VAT Auto Assessment (VAA) leveraging on the *iTax* platform to enhance compliance.

# INSTANCES OF MISSING TRADER

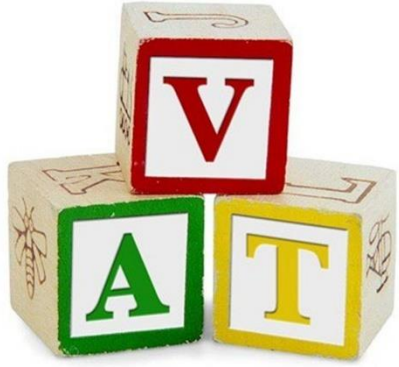
- Missing traders opening fictitious companies
- Fictitious invoices
- Several companies involved in the buying of input tax invoice credit
- Construction companies claiming input on raw materials bought by clients.
- Manufacturers and most of the big companies selling invoices for their sales made to final consumers.
- Double claiming of invoices outside the 6 months window.

# The VAA System

VAA is a system-based solution that will:

- detect inconsistencies between purchase and sales invoices which have been declared in the VAT returns,
- communicate the inconsistencies to both the buyer and the seller and;
- automatically disallow input tax relating to unresolved inconsistencies.

# Reason for VAA



- To get rid of claiming of fictitious inputs by taxpayers.
- To dispose of claiming of unsupported inputs by taxpayers.
- Clean data and ensure proper filing of return.
- Broaden the tax base.
- Increase compliance.

# How VAA Works

1. System checks buyer's return for corresponding sale declared by the seller.
2. If the system identifies inconsistencies, notification is sent to both the buyer and the seller.
3. System runs another check after 15 days and if the identified inconsistencies remain outstanding, a reminder notice is sent to both buyer and seller.
4. After a further 15 days and the inconsistency is still outstanding, the system will disallow all the input tax as per the outstanding inconsistencies.

# VAA MECHANICS

6. If after 30 days, the assessed amount remains unpaid, debt enforcement and recovery measures will take effect
7. A re-configurable threshold has been pre-set in the system (address low risk inconsistencies, rounding of errors etc)
8. Taxpayers can make multiple amendments for the affected VAA VAT returns.
9. System uses the invoice date as declared by the buyer to check the corresponding sellers return hence it is not necessarily a month to month matching.



# VAA Issues and Mitigation

|    | Issue Raised  | Enhancement Provided  |
|----|---|---|
| 1. | Amending of invoice details for input tax in returns where return period is past six months | Provision to file amended returns with validated invoice details (number, supplier PIN, date) through back office (Data Correction) <u>for VAA cases</u> where taxpayers are not able to amend the same through their profile as the system considers them to be time barred. |
| 2. | Limited entries in the VAT Excel return (50,000 for the different sheets)                   | Increase in the limit of entries in the VAT excel return to 75,000 entries for sheets 'B' (General Rated Sales) and 'F' (General Rated Purchases)   |
| 3. | Special characters in invoice numbers   | A wider range of special characters are now allowed as part of invoice numbering  |

# VAA Issues and Mitigation

|    | Issue Raised  | Enhancement Provided  |
|----|---|---|
| 4. | Generation of inconsistencies where invoice number has alphanumeric characters as part of the invoice number.<br>E.g. p123 and P123 | Invoices with same alphanumeric invoice numbers; where alphabets are captured as lower case and upper case by seller and buyer; will be validated as same invoice number                |
| 5. | Generation of inconsistencies where invoice number has leading and lagging spaces in the invoice number                             | Invoices with leading and lagging spaces as captured by either buyers and sellers will be considered as matching and will therefore not form part of the generated inconsistency report |
| 6. | Upon uploading return errors displayed are limited to the first 100   | Line entries of errors displayed upon uploading a return in iTax has been increased to 200  |

# VAA Issues and Mitigation

|    | Issue Raised  | Enhancement Provided   |
|----|---|--|
| 7. | Errors as a result of Rounding off of numbers   | Invoice entries with inconsistencies relating to rounding off errors will be validated and will therefore not form part of the generated inconsistency reports |
| 8. | Limited length of invoice number (maximum of 20 characters)   | Number of characters for the invoice column have been increased to 40  |
| 9  | Legal challenges on VAA-<br>Notion of doing the role of the revenue Authority<br>( Case of <u>Feradon Associates Limited v Commissioner of Domestic Taxes</u> ) | Amend the law to require that Input tax is only deductible when the corresponding input tax has been declared by the seller.                                   |

# TECHNOLOGY SOLUTION TO MISSING TRADER

- KRA is in the process of implementing a Tax Invoice Management System (TIMS)
- **TIMS is an enhancement of the current ETR regime.** It aims at plugging loopholes resulting from weaknesses in this regime through:
  - ❑ **Integration with trader systems**, i.e., ETRs, ERPs and Point of Sale systems (POS).
  - ❑ **Standardization and authentication** of tax invoices issued by VAT traders on a real time basis.
  - ❑ **Seamless integration with iTax.**
  - ❑ **Verification of the validity** of a tax invoice for use by officers, traders and the general public through the Tax Invoice Checker on the iTax portal or Mobile app. Amongst other modules.

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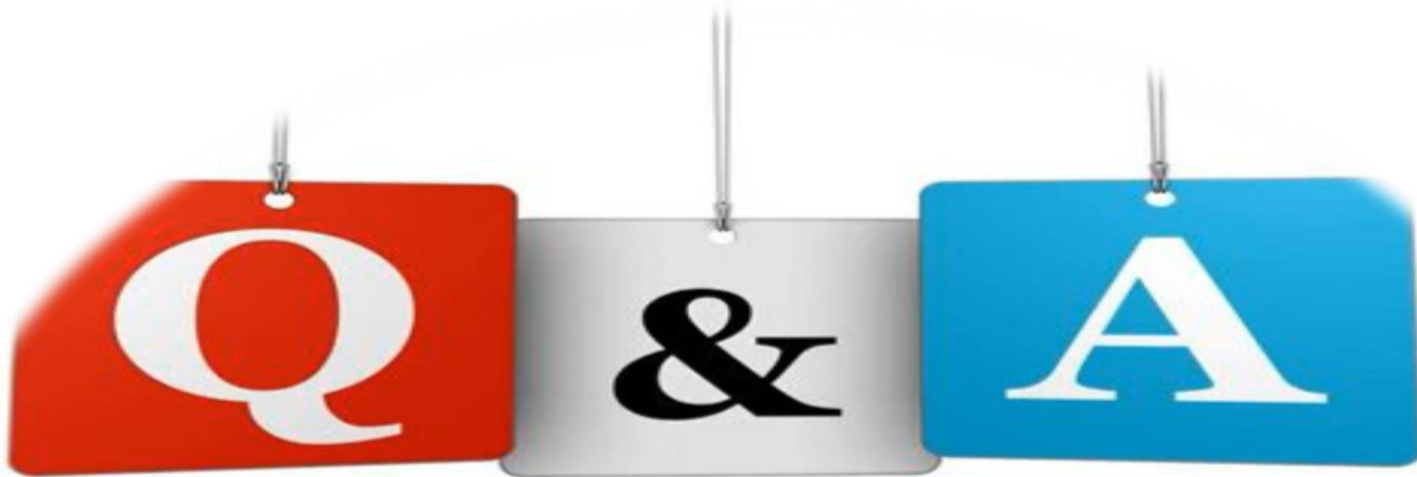
**Overall Objective: To increase VAT compliance, minimize on VAT fraud (VAA) and increase tax revenue.**

This will be achieved through:

- Real time validation of invoices at the trader tills prior to issuance to the customer and transmission to KRA tax system.
- Improving accuracy in automated VAT data management for transactional purchases and sales information (**to address invoice discrepancies**).
- Minimizing VAT fraud through verification of invoice data.
- Standardization of tax invoices and receipts
- Simplification of return filing through auto population of the VAT returns

# TECHNOLOGY SOLUTION TO MISSING TRADER

- The ultimate solution is a cloud-based system that will not require gadgets as implemented in other jurisdictions such as Rwanda.



THANK  
YOU!