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NEWSFLASH KENYA

TAX LAWS (AMENDMENT) ACT, 2020

Issue:
5 May 2020

Latest news on law, tax and business in Kenya

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→ Background

The President of Kenya assented to the Tax Laws (Amendment) Act, 2020 on 25 April 2020.

A good portion of the changes is directed towards addressing the detrimental effects of the Covid-19 pandemic. This Act makes various changes to the following tax laws: *The Income Tax Act (ITA)*, *Value-Added Tax (VAT)*, *Excise Duty Act*, *Tax Procedures Act*, *Miscellaneous Fees and Levies Act* and the *Kenya Revenue Authority Act*. It is important to note that the reduction of the rate of VAT from 16 per cent to 14 per cent became effective on 1 April 2020 pursuant to a legal notice issued by the Cabinet Secretary in charge of the National Treasury. We had pointed this out in our earlier alert released in March.

In this issue, we will analyze the key changes brought about by the Act.

→ Corporate tax changes

Effective: 25 April 2020

1. Reduction of resident corporate tax rate from 30 per cent to 25 per cent

The lower corporate tax rate is a welcome move as it serves to make Kenya a competitive investment destination in East Africa. The corporate tax rate is now the lowest in the region as economic peers, Uganda and Tanzania still maintain a rate of 30 per cent. It will also cushion businesses against the adversity of Covid-19, as they are likely to suffer production and operational losses.

2. Reduction of turnover tax for all Micro, Small and Medium Enterprises (MSMEs) from 3 per cent to 1 per cent on gross receipt of a business and scrapping of presumptive tax.

The removal of presumptive tax has made compliance easy for MSMEs. The lowering of the turnover tax is a welcome move, as it will promote setting up of MSME affiliated businesses.

3. Revision of turnover tax threshold: KShs 1,000,000 to KShs 50 million.

The Act has stated that turnover tax will now be payable by a resident persons who record an annual turnover between KShs 1 million to KShs 50 million. It should however be noted that turnover tax will not apply to:

- Rental income;
- Management, professional or training income; and
- Any income, which is subject to final withholding tax.

The extension of the upper annual turnover limit for registration of turnover tax to KShs 50 million will now eliminate the privilege of not registering for VAT where a business meets the KShs 5 million annual turnover threshold. However, the extension of the upper threshold also means that if a resident person's annual revenue falls under KShs 50 million, they would not be required to prepare audited statements, as prescribed under the Companies Act.

Taxpayers who fall under the turnover tax regime but wish to opt out, will have to make an application to the Commissioner stating that they elect to be under the corporate tax alternative.

4. Removal of the 30 per cent additional tax deduction on electricity cost. (electricity rebate)

Manufacturers will now lose the 30 per cent deduction on electricity costs introduced last year as the Act has done away with the electricity rebate. This will increase manufacturing costs leading to reduction in profits.

5. Expansion of the definition of qualifying interest

"Qualifying interest" refers to interest received by a resident individual from commercial banks or a financial institution licensed under the *Banking Act*, the Central Bank of Kenya (CBK) and a registered Building society.

Withholding tax (WHT) on qualifying interest is final at a rate 15 per cent.

The definition of 'qualifying interest' has been expanded to include all interest received by a resident individual. This is a positive development, as it will encourage investment by individuals in various interest-bearing instruments.

6. The Act also has repealed the reduced corporate income tax rates in relation to:

- Companies whose shares are listed on the Nairobi Securities Exchange (NSE)
- which were subject to tax at rates ranging from 20 per cent to 27 per cent for a defined period following the listing of the shares.
- Companies operating a plastics recycling plant which were subject to tax at the rate of 15 per cent effective 2019.

Corporate tax rates applicable to companies in special operating framework arrangement agreed between a company and the Government remain in force until expiry of such arrangements.

→ Changes in Capital Allowances

Item	Previous rate	New rate
Machinery used for Manufacture	100 %	50 % for the first year and 25 % for subsequent years on reducing balance
Hospital Equipment	12.5 %	50 % for the first year of use and 25 % for subsequent years on reducing balance
Aircrafts	25 %	50 % for first year of use and 25 % for subsequent years on reducing balance.
Ships	100 %	50 % for year of use and 25 % for subsequent years on reducing balance
Filming equipment purchased by a local producer	100 %	25 % on reducing balance
Motor Vehicles	25 %	25 % on reducing balance
Heavy earth moving Equipment	37.5 %	25 %
Computer and peripheral computer hardware and software, calculators, copiers and duplicating machines	30 %	25 % on reducing balance
Computer Software	20 %	25 % on reducing balance
Furniture and Fittings	12.5 %	10 % on reducing balance
Telecommunications Equipment	20 %	10 % on reducing balance
Other Machinery	12.5 %	10 %
Purchase or an acquisition of an indefeasible right to use fibre optic cable by telecommunication operator	20 %	10 % on reducing balance
Machinery used to undertake operations under an exploration or mineral prospecting right	37.5 % or 12.5 % depending on nature of machinery.	50 % on first year of used and 25 % for subsequent years on reducing balance
Farm Works Deduction	100 %	50 % and 25 % from subsequent years on reducing balance

OUR COMMENTS

The government has highly reduced the rate of claimable Capital Allowances. This will lead to more taxable income and is likely a move by the government designed to cushion the effect that reduction of corporate tax from 30 per cent to 25 per cent will have on tax revenue.

Independent power producers (IPPs) who do not supply to the national grid seem to have been left out under the allowances for manufacturers.

There is however an incentive to hospitals in relation to claiming Capital Allowances on their equipment following the increased rate. This makes hospitals the greatest beneficiary of the capital allowances revision.

→ Other corporate tax changes

TAXATION OF EXEMPT INCOME

The Act through deletion has done away with various incomes that were previously exempt from tax. Parastatal entities have majorly appeared in the changes. Some of them are currently moribund and the exemption provisions were no longer useful. These include:

- Tea Board of Kenya
- The Kenya Dairy Board
- The Pig industry Board
- The Sisal Board of Kenya
- The Canning Crops Board
- The National Irrigation Board
- The Mombasa Pipeline Board
- The Cotton Board of Kenya
- The Settlement Fund Trustees
- The Central Agricultural Board
- The Pyrethrum Board of Kenya
- The Pineapple Development Authority
- The Kenya Tea Development Authority
- The Kenya Post Office Savings Bank
- The Horticultural Crops Development Authority

The following sources of income, which were previously exempt income, will now be taxable:

- Dividends received by venture Capital Company, Special Economic Zones Enterprises, Developers and operations licensed under the SEZ Act;
- Gains arising from the trade in shares of a venture company earned by a registered venture capital company within the first ten years from the date of first investment in that venture company by the venture capital company;
- Interest income generated from cash flows passed to the investor in the form of asset backed securities;
- Interest earned on contributions paid into the deposit protection fund established under the Banking Act;
- Income from employment paid in the form of bonuses, overtime and retirement benefits payable to employees in the lowest tax band;
- Dividends paid by an SEZ enterprise, developers or operators to any non-resident person;
- Compensating tax accruing to a power producer under a power purchase agreement; and
- Income of the Export-Import Bank of the United States of America.

OUR COMMENT

In addition to the listed government parastatals, which are mostly defunct, the repeal of the provisions under the First Schedule will mean a wider tax base that may increase government revenue.

→ Withholding tax (WHT) changes

Effective: 25 April 2020

1. Increase of WHT on dividends for non-residents

The rate on dividends paid to non-resident persons has been increased from 10 per cent to 15 per cent. However, where relevant double tax agreements exist, the non-residents will enjoy lower WHT rates if lower than the effected one.

2. Withholding Tax on marketing, sales, promotion and advertising provided by non-residents

The WHT will apply on the above services provided by non-residents at the rate of 20 per cent. In effect, payment by a resident person or a person having a permanent establishment (PE) in Kenya to any other person with respect to the above services will be deemed income that is accrued in or derived from Kenya.

3. Withholding tax on transportation of goods by non-residents

The tax will apply to non-residents at the rate of 20 per cent. It will however not apply to those in the air and shipping transport as well as East African Community Citizens.

4. Withholding tax on re-insurance premiums

It will apply on reinsurance premiums paid to non-residents at the rate of 5 per cent with an exception of payments in the aviation industry.

OUR COMMENT – WHT CHANGES

The government has widened the tax base with these changes most likely due to the potential revenue loss on lowering of corporate and employment taxes. The WHT changes may make Kenya an unattractive investment destination for foreigners following the increased rate on dividends payments to non-residents. The changes are also likely to lead to reduced investment in the transport sector by foreigners with the introduction of the 20 per cent WHT. This new tax is set to greatly cover common online advertising platforms like You Tube, Facebook, Google, Yahoo etc. Similarly, it may affect international courier service companies where they outsource air or ship transportation.

→ Changes in Employment taxes

Effective: 25 April 2020

Income scale	Annual income bracket (KShs)	Monthly income bracket (KSHs.)	Tax rate in %
On the first KShs. 288,000	0 - 288,000	0 - 24,000	10 %
next KShs. 200,000	288,001 - 488,000	24,001 - 40,667	15 %
next KShs. 200,000	488,001 - 688,000	40,668 - 57,333	20 %
Over KShs. 688,000	688,001 & above	57,334 & above	25 %

WIDENING OF PAYE TAX BANDS AND INCREASE IN PERSONAL RELIEF

The individual tax rates bands have been expanded with the minimum monthly taxable income rising to amounts above KShs 24,000. The new graduated tax bands are shown above.

The individual annual tax relief has also been increased from KShs 16,896 (KShs 1,406 per month) to KShs 28,800 (KShs 2,400 per month).

However, income accrued in prior periods (e.g. gratuity) but paid out now will still be taxable using the graduated tax bands and rates applicable in the year of accrual.

PENSION WITHDRAWAL TAX RATES

Reduction in highest tax band on pension withdrawals from registered retirement funds after 15 years to 25 per cent, for amounts exceeding KShs 1,200,000 per annum.

In addition, the Act has widened the tax bands on income withdrawals from retirement funds before the expiration of 15 years in line with the individual tax rates highlighted above.

These changes will go a long way in increasing the disposable income available to retirees amid the financial hardships brought on by the COVID-19 pandemic.

→ VAT Changes

Effective: 15 May 2020

VAT BASE OF PETROLEUM PRODUCTS: VALUE OF SUPPLY TO INCLUDE EXCISE DUTY, FEES AND OTHER CHARGES.

The change will increase the taxable value of the products and thus the amount of VAT resulting in price increases of petroleum products and corresponding increases on downstream products and services. This will seem to be against the government's stated intention of cushioning Kenyans against the economic effects of the COVID-19 pandemic.

Effective date: 15 May 2020

ADDITIONAL CRITERIA FOR ISSUANCE OF A CREDIT NOTE

Businesses will now be able to issue a credit note within 30 days after the determination of a commercial dispute in court relating to the price payable.

Previously, businesses were only allowed to issue credit notes within six months after the issuance of the relevant tax invoice. Given the tendency for cases in Kenya to be drawn out, this will provide relief to taxpayers in cases where the court resolution of disputes ordinarily takes longer than the prescribed period.

REDUCTION IN PERIOD WITHIN WHICH TO APPLY FOR VAT REFUNDS ARISING FROM BAD DEBTS

The time limit of applying for a VAT refund on bad debts has been reduced from five years to four years from the date of supply. The change will require businesses to be prompt in seeking refunds, relating to bad debts, from the KRA as the window for claim has been reduced by one year.

CHANGE TO REQUIRE ALL PERSONS TO MAINTAIN RECORDS OF THEIR TRANSACTIONS

Previously, only VAT-registered persons were required to maintain records. The new provisions will require all persons conducting business in Kenya will to maintain records of their business transactions for a period of five years and be ready to provide such records to authorized officials at all reasonable times for inspections. This may lead to increased audits by KRA, as they will have a wider base to target through taxpayers' documentation.

Changes in VAT status

Item	Previous rate	New rate
Personal protective equipment, including facemasks, for use by medical personnel in registered hospitals and clinics, or by members of the public in the case of a pandemic or a notifiable infectious disease	14 %	Exempt
Insurance agency, insurance brokerage and securities brokerage services	Exempt	14 %
Vaccines for human and veterinary medicine	0 %	Exempt
Medications	0 %	Exempt

Plants and machinery of Chapter 84 and 85 used for the manufacture of goods	Exempt	14 %
Taxable supplies, excluding motor vehicles, imported or purchased for direct and exclusive use in the construction of a power generating plant, by a company, to supply electricity to the national grid approved by Cabinet Secretary for National Treasury upon recommendation by the Cabinet Secretary responsible for energy	Exempt	14 %
Taxable supplies, excluding motor vehicles, imported or purchased for direct and exclusive use in geothermal, oil or mining prospecting or exploration, by a company granted prospecting or exploration license in accordance with *Geothermal Resources Act*, production sharing contracts in accordance with the provisions of *Petroleum (Exploration and Production) Act* (Cap. 308) or mining license in accordance with the *Mining Act* (Cap. 306), upon recommendation by the Cabinet Secretary responsible for energy or the Cabinet Secretary responsible for mining, as the case may be	Exempt	14 %
Taxable supplies procured locally or imported for the construction of liquefied petroleum gas storage facilities with a minimum capital investment of four billion shillings and a minimum storage capacity of 15,000 metric tons as approved by the Cabinet Secretary for National Treasury upon recommendation by the Cabinet Secretary responsible for liquefied petroleum gas	Exempt	14 %
Plastic bag biogas digesters	Exempt	14 %
Biogas	Exempt	14 %
Leasing of biogas producing equipment	Exempt	14 %
Parts imported or purchased locally for the assembly of computer, subject to approval by the Cabinet Secretary for the National Treasury, on recommendation by the Cabinet Secretary responsible for matters relating to information technology	Exempt	14 %
Taxable goods purchased or imported for direct and exclusive use in the construction and infrastructural works in industrial parks of one hundred acres or more including those outside special economic zones approved by the Cabinet Secretary for the National Treasury	Exempt	14 %
Museum and natural history exhibits and specimens and scientific equipment for public museums	Exempt	14 %
Chemicals, reagents, films, film strips and visual aid equipment imported or purchased prior to clearance through the customs by the National Museums of Kenya	Exempt	14 %
Goods falling under tariff number 4907.00.90 "Unused postage, revenue or similar stamps of current or new issue in the country in which they have, or will have, a recognised face value; stamp-impressed paper; bank-notes; stock, share or bond certificates and similar documents of title"	Exempt	14 %
Materials and equipment for the construction of grain storage, upon recommendation by the Cabinet Secretary for the time being responsible for agriculture	Exempt	14 %
The transfer of a business as a going concern by a registered person to another registered person	Exempt	14 %
Taxable goods supplied to marine fisheries and fish processors upon recommendation by the relevant state department	Exempt	14 %
Goods imported or purchased locally for direct and exclusive use in the implementation of projects under a special operating framework arrangement with the Government	Exempt	14 %
Taxable services provided for direct and exclusive use in the construction and infrastructural works in industrial parks of one hundred acres or more on the recommendation by the Cabinet Secretary responsible for Industrialization including those outside special	Exempt	14 %

economic zones approved by the Cabinet Secretary for the National Treasury		
Taxable services procured locally or imported for the construction of LPG storage facilities with a minimum capital investment of four billion shillings and a minimum storage capacity of a total value of fifteen thousand metric tons as approved by the Cabinet Secretary for National Treasury upon recommendation by the Cabinet Secretary responsible for LPG	Exempt	14 %
Asset transfers and other transactions related to the transfer of assets into real estate investment trusts and asset backed securities	Exempt	14 %
Services imported or purchased locally for direct and exclusive use in the implementation of projects under special operating framework arrangement with the Government	Exempt	14 %

→ Other changes in Tax Laws

Effective: 25 April 2020

TAX PROCEDURES ACT: PRIVATE RULINGS

The time limit for the Commissioner to issue a private ruling has been increased from 45 days to 60 days on receipt of an application by a taxpayer. The Act has also repealed the requirement by the Commissioner to publish a private ruling. The repeal of the requirement to publish private rulings means that other taxpayers will not be privy to decisions and legal arguments that may assist them in their own disputes with KRA.

The law has also not provided for clear implications where the Commissioner does not respond within the stipulated timeline. This leaves the Commissioner with a lot of discretion with respect to taxpayers.

EXCISE DUTY ACT

Definition of *“other fees”* has been amended to clarify that only other fees as defined in the Act, which relate to licensed activities, are subject to excise duty. This makes it clear that fees earned from non-financial activities are not subject to excise duty.

The following items were previously exempt but are now subject to excise duty:

- Goods imported or purchased locally for direct and exclusive use in the implementation of projects under special operating framework arrangements with the Government
- One personal motor vehicle, excluding buses and minibuses of seating capacity of more than eight seats, imported by a public officer returning from a posting in a Kenyan mission abroad and another motor vehicle by the spouse and which is not exempted from Excise Duty under the Second Schedule.

MISCELLANEOUS FEES AND LEVIES ACT

1. Amendment of scope of the Railway Development Levy (RDL) fund

The scope of utilization of the funds raised through collection of RDL on imported goods expanded to include operation of the standard gauge railway network to facilitate transportation of goods.

Previously, the funds were limited to the construction of the standard gauge railway network.

2. Imposition of a processing fee on duty free motor vehicles

Introduction of new processing fees amounting to KShs 10,000 on motor vehicles excluding motor-cycles imported or purchased duty free prior to clearance through customs under the Fifth Schedule to the East African Community Customs Management Act, 2004.

Introduction of a processing fee on duty free items is intended to be a recovery measure of the costs of customs clearance of duty-free motor vehicles.

3. Exemption from RDL and IDF

Goods which are imported or purchased for the construction of bulk storage facilities for supporting the standard gauge railway operations (with a minimum storage capacity of one hundred thousand metric tons of supplies) exempted from both RDL and import declaration fee.

4. Imposition of Import Declaration Fees (IDF)

IDF introduced on the following items that were previously exempt:

- Gifts and donations by foreign residents to their relatives in Kenya for their personal use
- Samples which in the opinion of the Commissioner have no commercial value
- Raw materials for direct and exclusive use in construction by developers or investors in industrial parks of one hundred acres or more located outside the municipalities of Nairobi and Mombasa
- Goods imported for the construction of liquefied petroleum gas storage facilities

5. Imposition of Railway Development Levy (RDL)

RDL introduced on the following items that were previously exempt:

- Raw materials for direct and exclusive use in construction by developers or investors in industrial parks of one hundred acres or more located outside the municipalities of Nairobi and Mombasa
- Goods imported for the construction of liquefied petroleum gas storage facilities
- Goods imported for implementation of projects under special operating framework arrangements with the Government

THE KENYA REVENUE AUTHORITY (KRA) ACT

- Appointment of enforcement agencies

Commissioner now has powers to appoint a person registered under the *Banking Act* to act as an agent for revenue banking services through an agreement. Such a person will be required to submit the funds collected to the designated CBK account within two days.

Failure to submit the funds collected within the stipulated two days will result in a penalty of 2 per cent of the amount collected compounded daily for the period the funds are not submitted to the Central Bank. This is meant to enhance the collection of revenue for the Government.

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