Kenya’s Finance Act 2015

An Update on Kenya’s Taxation Regime
INTRODUCTION

Every year, the budget process in Kenya culminates in the enactment of a finance act. For the FY 2015/2016, the Finance act was assented to on 11th September 2015 by His Excellency the President and provides the legislative framework pertaining to taxes, duties, exemptions and reliefs for this fiscal year.

This update aims to highlight the amendments the Finance act introduces to various tax statutes as well as the changes to the Kenya tax regime in order to educate professionals on the implications for both business and the economy.

VALUE ADDED TAX (VAT)

The changes relating to VAT are effective from 12 June 2015.

1. Tax Refunds
   (Amendment to Section 17 of the VAT Act)

Taxpayers are now allowed to lodge their VAT refund claims for a period of up to 12 months from the date the tax becomes due and payable.

Previously, the statute had not provided a time limit to lodge refund claims.

The VAT Law and the Tax procedures bill, however need to provide for the introduction of a period within which the KRA settle VAT refund claims or apply an interest rate to delayed payments by KRA on outstanding VAT refunds.

2. Appointment of ‘other’ withholding VAT agents
   (Amendment to Section 25A of the VAT Act)

This provision allows the Commissioner to appoint other persons other than government agencies to be Withholding VAT agents.

The KRA has reiterated that the introduction of withholding VAT is to collect information on taxpayers and not to collect revenues, having recruited 3,200 Withholding VAT Agents mainly LTO and MTO taxpayers. We anticipate that this provision will enhance the KRA’s capacity to gather tax payer information.

Exempt Supplies
(Amendment to the 1st Schedule of the VAT Act 2013)

3. Construction & Infrastructure works for Industrial & Recreational Parks

Goods and services for the construction of infrastructure works in industrial and recreational parks of 100 acres or more in Nairobi, Nakuru, Kisumu, Mombasa and Eldoret are now exempt from VAT subject to approval of the CS – National Treasury. This is a means of encouraging investment in industries and recreational parks.

4. Aid Funded Projects

Raw materials (other than motor vehicles) and taxable services utilized in official aid funded projects are now exempt, subject to approval of the CS – National Treasury.

5. Film Industry

Goods imported or purchased locally for use by the Kenya Film Commission are now exempt to boost the film industry in Kenya.

This VAT exemption focuses on the actual taxpayers in the film industry as opposed to their umbrella organization, the Kenya Film Commission.

6. Special Economic Zones (SEZ)

The supply of taxable goods and services to special economic zones enterprises, developers and operators licensed under the Special Economic Zones Act will be VAT exempt and is intended to boost investment.
A SEZ is a designated geographical area where business-enabling policies will be implemented. These zones have been established within the Special economic Zones Act, 2015 and come into effect on 15th December 2015.

This provision is intended to harmonize the provisions of the VAT act and the SEZ legislation, in order to provide certainty around tax exemption so as to encourage growth of industries.

7. Manufacturers of Agricultural Machinery
Inputs and raw materials locally purchase or imported for use by the manufacturers of agricultural machinery and implements are now exempt.

8. Biogas Production
Plastic biogas digesters, biogas and the leasing of biogas producing equipment is now exempt in order to encourage the use of biogas by households.

9. Laptop Project
Parts imported or purchased locally for the assembly of primary school laptops and tablets are now exempt from VAT in encourage the implementation of the Government’s primary school laptop project.

10. Duty Free Goods
Goods purchased from duty free shops by passengers departing to places outside Kenya now zero-rated.

11. Aircrafts
The VAT Act now exempts Aircraft parts from VAT. This provision was incorporated following the intense lobby by the aviation industry to remove VAT on aircraft parts that had caused airlines to incur huge VAT costs.

**Exempt Items Now Zero-Rated**
*(Amendment to the 2nd schedule of the VAT Act 2013)*

12. Goods in Transit
Taxable Services provided in respect to goods in transit are now zero rated.

Previously the VAT Act 2013 was silent on the classification of these services. Thereafter the Finance Act 2014 which took effect in August 2014 exempted them from VAT.

This provision is intended to restore competitiveness within the Kenyan transport service and encourage sustained growth in the transport sector.

13. Medicaments and Pharmaceuticals
The second schedule of the VAT Act 2013 has been expanded to include various vaccines for both human and veterinary medicines such as; Infusion solutions, penicillin, antibiotics, hormones and various other vitamin products of various HS codes ranging between 3002.20.00 to 3004.90.90.

This provision is intended to reduce the costs associated with medication in order to enhance access to healthcare.

ICPAK – PUBLIC FINANCE & TAX SUBCOMMITTEE
INCOME TAX

The changes relating to Income Tax take effect from 1st January 2015

1. Film Industry
   a. Withholding Tax (WHT)
   Payments made by filming agents and filming producers approved by the Kenya Film Commission to actors and crew members shall be exempt.

   The current WHT rate on payments to nonresident actors and crew is 20%.

   b. Capital deduction
   Buildings in use for the training of film producers, actors or crew now qualify for 100% industrial building allowance.

2. Rental Income
   a. Tax Amnesty
   The Commissioner of Income Tax shall with effect from 1st July 2015 refrain from assessing or recovering taxes (including penalties and interest) for the year 2013 and prior years, in respect of gains or profits for the use or occupation of property.

   For an individual to take advantage of this tax amnesty the 2014 and 2015 tax returns must be filed by 30th June 2016 and the applicable principal taxes paid.

   b. Residential rental income
   The introduction of a simplified regime for landlords with income not exceeding KES 10 Million during any year of income, intended to improve compliance.

   This taxable at 10% of the gross rental receipts of a taxable resident person. Taxpayers can however choose to remain under the current regime by notice in writing to the Commissioner of Income Tax.

   This provision is intended to broaden the tax net and simplify tax Administration. It is worth noting that only agents appointed by KRA will be responsible to withhold. Further, this may prove cumbersome as the tax withheld is greater than the tax rate which is 10% while the withholding tax rate is 12%.

   c. Withholding Tax
   Payments in respect of a rent, premium or similar consideration for the use or occupation of immovable property, are subject to WHT at 12% of the gross amount payable.

   The Finance Act has deleted the provision enabling the application of WHT and appointment of agents but has at the same time introduced WHT at a rate of 12%. This should also have been deleted if the intention was to remove the WHT provisions.

3. Tax Losses
   Companies shall now be able to carry forward tax losses for up to 10 years.

   Previously, (1 July 2010), a company could only utilize tax losses for future taxable income for up to five years.

   This provision implies that for tax losses incurred in 2010 and prior years, an application to the Treasury Cabinet Secretary for the carry forward of the tax losses would still be required.

4. Shipping Industry
   The rate of Investment Deduction (ID) on ships has now been increased to 100% from 40%.

   The qualifying tonnage for ID for ships has also been reduced from 495 tons to 125 tons.

   This is intended to incentivize investment in the sector and is targeting the anticipated increase in shipping activity due to the modernization of the ports.
5. Special Economic Zones (SEZ)
Taxes on SEZ enterprises will be as follows:
   a. Exemption on dividends received by licensed SEZ enterprises developers and operators.
   b. Corporation Tax Rate for the first 10 years at 10% and 10-20 years at 15%.
   c. Application on a 10% withholding tax on payments (other than dividends) by a SEZ enterprise, developer and operator to non-residents.

The limited tax incentives introduced by the Finance Act seem to be inconsistent with the SEZ Act which grants a blanket exemption on all taxes. The Income Tax Act provides that tax exemptions provided in other acts of parliament are legally valid. This conflict will need to be resolved prior to the issuance of licenses under the SEZ Act.

6. Extractive Industry
The Finance Act 2014 introduced a new regime for taxation of the extractive sector, through an overhaul of the Ninth Schedule to the Income Tax Act. The Finance Act 2015 has introduced additional changes to the Ninth Schedule, in order to bring uniformity between the taxation of mining and oil/gas sub-sectors.
   a. WHT on training services and contractual fees
      Training services shall now be subject to a withholding tax rate of 12.5% and contractual fees subject to a 5.625% rate. Previously, the rate applied was 20% for training services.

   b. The Import Declaration Fee (IDF) has also been lowered to 2% from 2.25% of Cost Insurance and Freight (CIF) as part of the harmonizing initiatives of the East Africa Community.

   c. Various definitions have been introduced, including “petroleum operations”, which are expected to provide clarity for interpretation of the Ninth Schedule.

   d. Schedule nine also introduced a new source of income relating to income from mining blocks and petroleum blocks.

The Act has amended section 15(7) (a) by introducing an additional separate source of income to reflect this change in the Schedule. This provision categorizes incomes and expenses into specific income sources.

   e. Schedule nine also contains provisions which exempt withdrawal of income from a rehabilitation fund from tax.

The Act has extended this exemption to include investment and interest income derived from the rehabilitation fund. This is expected to ease the burden of mining entities when restoring the environment after decommissioning of mines.

7. Indirect Sale of entities in Kenya
Taxation on the transfer of interests in a person has now been extended to all sectors, other than the extractive industry. The chargeable tax will be computed entirely in proportion to the value of interest derived directly or indirectly from Kenya. This is an anti-avoidance measure targeting offshore group restructuring options.

8. Capital Gains Tax
   i. Exemptions from CGT
      a. Shares
         • The act has abolished CGT on shares listed on the Nairobi Securities Exchange. Unlisted shares will continue to be taxed under the current CGT regime.
• Shares traded on the NSE will now be subject to WHT. The rate proposed in the Finance Bill was 0.3% of the transaction value without adjusting for the costs.

• This rate seems to have been erroneously omitted from the Act implying that neither WHT nor CGT is chargeable.

b. Transfer of property as part of a divorce settlement to immediate family members

c. Transfer of land whose transfer value does not exceed KES 3 million or transfer of agricultural property with an area below 50 acres, situated outside a municipality, gazetted township or urban area.

d. The transfer or sale of property completed within 2 years from date of finalization of a court case administering the estate of the deceased person.

ii. Tax point on Land transactions

The tax point for transfer of property has been clarified to be on or before the date of lodging a transfer for registration at the relevant Lands Office.

This may prove to be a challenge because the tax point is no anchored in law. CGT is paid by the seller, while registration is undertaken by the purchaser, and hence the seller may not necessarily be aware whether a transfer has been lodged by the purchaser. The seller will further not be in a position to receive the sale price until registration has occurred. This implies that they may not have the funds to pay for CGT.

9. Betting Industry

The Act has amended the withholding tax rate applicable to winnings from betting from 20% to 7.5%, which is final tax.

The responsibility to withhold tax is with the bookmaker and the tax should be remitted by the 20th day of the subsequent month in accordance with the withholding tax rules.

The use of the term “winnings” in the context of a bookmaker is contradictory to the definition of winnings provided in the Finance Act.

It is also unclear as to the purpose of a withholding tax on gross profits of a resident bookmaker who is subject to the Kenya income tax law.

10. Incentives for Listing in the NSE

The Finance Act has introduced a tax incentive for companies that list at least 25% of their shares in the stock exchange through introduction.

Such companies shall be taxed at a reduced rate of 25% for the subsequent five years instead of the current rate of 30%. Previously the incentive was for companies that list through Initial Public Offer (IPO).

11. Incentives for apprenticeship

Any employer who engages at least ten university graduates as apprentices for a period of six to twelve months during any year of income shall be eligible for a tax rebate in the year subsequent to the year of such engagement.

The Cabinet Secretary is expected to issue regulations on application of these provisions.

12. NSSF

The fund is to be administered by the Kenya revenue Authority.