

# **TAX PROPOSALS AND THE FINANCE BILL 2016**

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**ICPAK ANNUAL BUDGET REVIEW SEMINAR,**  
**23<sup>RD</sup> -24<sup>TH</sup> JUNE, 2016.**  
**GREEN HILLS HOTEL, NYERI**

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# **OBJECTIVES OF THE PRESENTATION**

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**This presentation seeks to explain to the participants the various revenues raising measures proposed by the Cabinet Secretary, National Treasury and proposed amendments to various national tax laws including miscellaneous amendments to various Regulatory laws**

# FILING OF RETURN IN I-TAX SYSTEM

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- ✘ Empower the Commissioner to collect information in advance from selected tax payers for purposes of pre-populating the information in the i-Tax system.
- ✘ Effective Date: In the Minister's Policy Statement– not in the Bill

## Tax Modernization

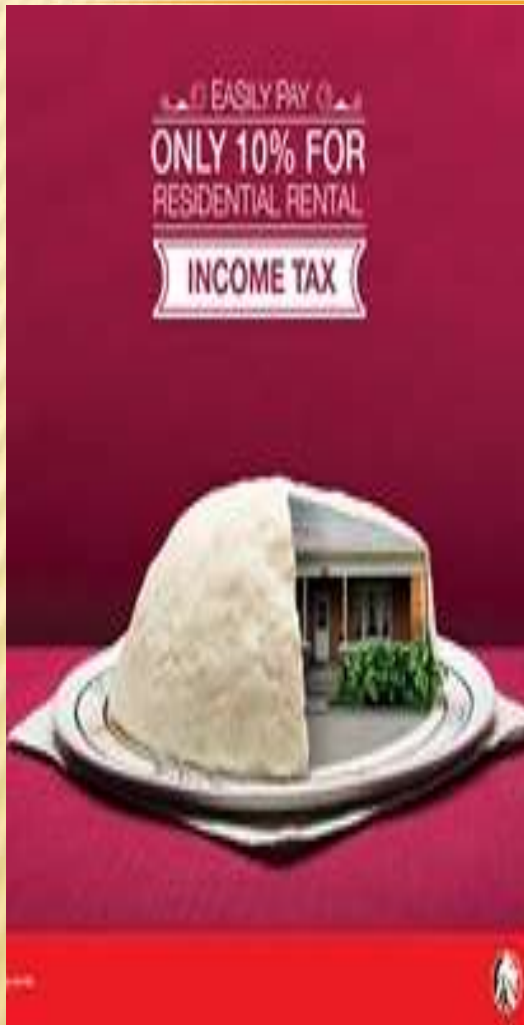
- ✘ Income Tax Bill to be tabled in parliament in the course of the financial year.
- ✘ Proposals to re-introduce presumptive income tax.
- ✘ Effective Date: In the Minister's Policy Statement– not in the Bill

# DEFINITION OF DEEMED INTEREST

- ✘ Definition of “deemed interest” is under Section 16 (3) of Income Tax Act (ITA).
- ✘ The 2016 Finance Bill deletes this definition under Section 16(3) of ITA and re-introduces the same under Section 2 of ITA.
- ✘ Deemed interest arises where a non-resident entity advances interest free loan to a related resident taxpayer.
- ✘ The term “deemed interest” appears in other sections of ITA: Section 10 (taxable interest payments) and Section 35(1)(e) (obligation to deduct withhold tax on interest and deemed interest).
- ✘ The amendment enables the application of the definition across the entire act.
- ✘ **Effective Date: 09 June 2016**



# THRESHOLD FOR RESIDENTIAL RENTAL INCOME TAX



- ✘ Under Section 6A of the Income Tax Act (ITA), residential Rental Income Tax is a turnover tax regime for landlords whose gross rental income amounts to KShs 10 M and below. The turnover tax rate is 10%.
- ✘ The 2016 Finance Bill introduces a lower rental income threshold of KShs 12,000 per month. The gross rent below this amount is therefore not taxable.
- ✘ Amendment is to: cushion the taxpayers under this regime, encourage more tax payers to remain in this regime and to reduce administration of tax collection.
- ✘ The residential rental income tax rules have been gazetted.
- ✘ Implementation bottlenecks:
  - + The turnover tax rate is too high compared to the turnover regime under Section 12C (3%)
- ✘ **Effective Date: 09 June 2016**

# AMENDMENT TO SECTION 12 – PRESUMPTIVE INCOME TAX



- ✘ Instalment tax, which is addressed under Section 12 of ITA, allows for deduction of tax including presumptive income tax which was taxable under the repealed Section 17A of ITA.
- ✘ The 2016 Finance Bill removes the mention of Section 17A under Section 12.
- ✘ Effective Date: 09 June 2016

# APPOINTMENT OF RENTAL WITHHOLDING TAX AGENTS

- ✘ The 2015 Finance Act introduced rental withholding tax through amendment of Paragraph 5 (ja) of the Third Schedule to the ITA. The implementation hurdle around this amendment was that the drafters of the law failed to amend Section 35 of ITA (deduction of income from certain income)
- ✘ To address the above implementation hurdle, the 2016 Finance Bill has amended Sections 35(1) and 35 (3)(j) of ITA. Further amendment under Section 35 (3A) gives the Commissioner powers to appoint (in writing) agents for collection of this tax.
- ✘ The 2016 Finance Bill has further amended Paragraph 5 (ja) of the Third Schedule to the ITA hence reducing the withholding tax rate from 12% to 10%.
- ✘ Effective Date: 09 June 2016





# EXEMPTION OF BONUSES, OVERTIME AND RETIREMENT BENEFITS

- ✘ Under Section 5 of the Income Tax Act (ITA), individual taxpayers are taxable on their basic income plus their other taxable benefits.
- ✘ The 2016 Finance Bill introduces a new Paragraph 53 of the First Schedule to ITA that exempts Income from employment paid in the form of bonuses, overtime and retirement benefits:
  - ✘
    - + This is on premise that the exemption shall only apply to employees whose taxable employment income before bonus and overtime allowances does not exceed the lowest tax band (KShs 121,968 pa/ KShs 10,164 pm).
- ✘ Implementation bottlenecks: there is already an existing exemption under this same legislation (monthly or lump sum pension to a person above 65 years).
- ✘ **Effective Date: 09 June 2016**



# EXEMPTION OF INTEREST ON BONDS ISSUED BY EADB

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- ✘ Under Section 3 (2) (b) of the Income Tax Act (ITA), interest is a taxable income but the Act has given a few exemptions. Existing exemptions do not include interest of bonds issues by East African Development Bank (EADB).
- ✘ The 2016 Finance Bill introduces a new Paragraph 54 of the First Schedule to ITA that exempts interest income on bonds issued by the East African Development Bank.
- ✘ This proposal will bring parity within the rest of the EAC partner states, who have granted exemption status to these bonds.
- ✘ Effective Date: 09 June 2016



# INCREMENT OF PERSONAL RELIEF



- ✘ For the past decade, Personal Relief has been Kshs 13,944 pa (Kshs 1,162 pm).
- ✘ The Finance Bill 2016 has amended Head A (Item 1) of the Third Schedule to ITA hence increasing this amount to Kshs 15,360 pa (Kshs 1,280 pm).
- ✘ Effective Date: 09 June 2016

# EXPANSION OF TAX BANDS

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- ✖ From 2005, tax bands have remained static to date
- ✖ The Finance Bill 2016 has amended Head B (Item 1 and Item 1(A)) of the Third Schedule to ITA hence expanding the bands as follows:
- ✖ Effective Date: 1<sup>st</sup> January 2017

# PROPOSED TAX BANDS

Current tax bands	Amended tax bands	Rate
on the first Sh 121,968	On the first Shs.134,164	10%
on the next Sh 114,912	On the next Shs.126,403	15%
on the next Sh 114,912	On the next Shs.126,403	20%
on the next Sh 114,912	On the next Shs.126,403	25%
on all income over Sh 466,704	On all income over Shs.513,373	30%



# CORPORATE TAX RATE FOR HOUSING DEVELOPERS

- ✖ Housing developers pay tax like other ordinary businesses and the applicable tax rate is 30% as stipulated under Paragraph 2 (a)/(b) of Third Schedule to ITA.
- ✖ The 2016 Finance Bill introduces a new Paragraph 2(i) of the Third Schedule to ITA that reduces the corporate tax rate to 20% a company that constructed at least one thousand residential units annually, subject to approval by Cabinet Secretary responsible for Housing.
- ✖ Implementation bottlenecks:
  - + The threshold for 1,000 units is too high
  - + The requirement for approval by Ministry responsible for Housing may delay this incentive
- ✖ Effective Date: 09 June 2016

# CAPITAL GAINS TAX (CGT)

- ✗ Capital Gains Tax was suspended in 1985 and was reintroduced with effect from
  - + January 2015 through Finance Act 2014.
- ✗ Under Paragraph 2(h) of the Eighth Schedule to ITA, the transfer of an asset between spouses, or former spouses or their immediate family, as part of a divorce settlement or bona fide separation agreement is exempted from CGT.
- ✗ The 2016 Finance Bill has deleted Paragraph 2(h) of the Eighth Schedule and reintroduced the following exemptions.
  - ✗ transfer of assets between spouses;
  - ✗ transfer of assets between former spouses as part of a divorce settlement or a *bona fide* separation agreement;
  - ✗ transfer of assets to immediate family;

# CAPITAL GAINS TAX (CGT).....CONT

- + transfer of assets to immediate family as part of a divorce or *bona fide* separation agreement; or
- ✗
- + transfer of assets to a company where spouses or a spouse and immediate family hold 100% shareholding.
- ✗ Paragraph 3 of the Eighth Schedule to ITA defines “immediate family” as: “children of the spouses or former spouses”.
- ✗ This is a step in the right direction and has addressed tax complexities during succession and inheritance
- ✗ Implementation challenges:
  - + May contradict the law of succession and trusts and the case law around it
- ✗
- ✗ **Effective Date: 09 June 2016**

# AMENDMENTS UNDER ITA DUE TO DUPLICATIONS UNDER TAX PROCEDURE ACT (TPA)

- ✘ TPA was enacted on 19 January 2016. Upon enactment of TPA, various contradictions and duplications emerged when the same was read together with ITA. The followings deletions under ITA have been made under Finance Bill 2016:
  - + **Section 35 (6)** – Penalties under withholding tax regime
  - + **Section 37 (6&7)** – Appeals against PAYE
  - + **Section 51A** – Language on returns and records
- ✘ **Section 72** – Failure to furnish returns
  - + **Section 75A** – Assessment of leavers and persons in liquidation
  - + **Section 98** – collection of tax from leavers
  - + **Section 105** – Tax refunds
  - + Thirteenth Schedule – Transactions requiring a PIN
- ✘ **Effective Date: 09 June 2016**



# EMPLOYERS' SET OFF REBATE FOR APPRENTICESHIP

- ✘ Finance Act 2015 introduced Section 39B of ITA under which 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 tax rebate in the year subsequent to the year of such engagement.
- ✘ The Minister now gazette the regulations that facilitate the implementation of this tax incentive. The regulation include the definitions of apprentice by the employer.
- ✘ The rebate is 50% of the salaries and wages paid to the apprentices, which is in addition to the normal salaries and wages deductible under Section 15(1).
- ✘ The time limit to claim this deduction is 3 years.
- ✘ **Purpose:** Encourage employers to engage interns and to train/mentor them.
- ✘ **Effective Date:** In the Minister's Policy Statement– not in the Finance Bill 2016

# TAX PROCEDURES ACT (TPA) 2015

- ✘ Section 3 of TPA (definition of “Tax Return”) has been amended to identify the changes made under the Income Tax (PAYE) rules of ITA in which Paragraph 13(1) of the rules was deleted.
- ✘ **Effective Date:** 06 June 2016
- ✘ Section 19 (1) of TPA requires an individual or partnership to apply to the commissioner for a license as a tax agent. Section 19 (2) of TPA stipulates that that the above application shall be in the prescribed form and fee.
- ✘ Finance Bill 2016 has introduced a new Section 19(3) stipulating that in addition to the requirements set out above, the applicant shall be required to be recommended for registration by the Tax Agents Committee.
- ✘ **Effective Date:** 01 July 2016

# TAX PROCEDURES ACT (TPA) 2015 ....CONT

- ✗ Duty to furnish Third Party Returns
- ✗ Section 24 of TPA requires a taxpayer to submit a tax return. The Commissioner is not bound by this return or information provided and he may assess a taxpayer using the information available to him.
- ✗ Finance Bill 2016 has introduced a new Section 24A stipulating that a person shall, upon being required to do so by the Commissioner, furnish the Commissioner with returns showing such information, in such form and manner and within such time as the Commissioner may prescribe.
- ✗ **Effective Date: 01 July 2016**

# TAX PROCEDURES ACT (TPA) 2015 ....CONT

- ✖ Timelines for Commissioner to respond to taxpayers
- ✖ Article 47 of the Constitution and the Fair Administrative Practices Act connote the need for timely and expeditious decision making process by public bodies.
- ✖ In the above spirit, the following sections have been amended:
  - + **Section 33(3)** – extension of time to pay tax: Commissioner to respond within 30 days of receiving application for extension of time to pay tax.
  - + **Section 42(7)** – power to collect tax from person owing tax to a taxpayer: Commissioner to respond within 30 days of receiving the notification of inability to honor agency notices.
  - + **Section 47(3)** – refund of overpaid tax: Commissioner to notify applicant for a refund within 90 days of receiving the application for a refund.
- ✖ The Minister scratched the surface and did not address all the obligations that are required to be undertaken by the Commissioner under TPA
- ✖ **Effective Date:** 01 January 2017



# TAX PROCEDURES ACT (TPA) 2015 ....CONT

- ✗ Tax Amnesty for Landlords
- ✗ Section 123C of ITA became effective from 01 January 2016 under which the Tax Amnesty for landlords was introduced. Upon enactment of TPA on 19 January 2016, the tax amnesty was deleted hence withdrawing this incentive.
- ✗ Key amnesty provides for:
  - + 2013 and prior years: principal tax, penalties and interest
  - + 2014 and 2015: Penalty and interest .
  - + The landlord must file the self-assessment returns for 2014 and 2015 by 30 June 2016 and pay the principal tax due. No amnesty for those under assessment by KRA on years noted.
  - + No documentation: 40% of the expenditure allowed.
- ✗ 2016 Finance Act has reinstated this incentive through the introduction of Section 37(A) of TPA and backdating the same to 19 January 2016.
- ✗ **Effective Date: 19 January 2016**

# TAX PROCEDURES ACT (TPA) 2015 ....CONT

- ✗ Tax Amnesty for Assets Held Overseas
- ✗ Through introduction of Section 37(B) of TPA, the 2016 Finance Bill has extended Tax Amnesty for assets held overseas.
- ✗ Key amnesty provides for:
  - + The Commissioner shall refrain from assessing or recovering taxes, penalties or interest in respect of any year of income ending on or before the 31December, 2016, and from following up on the sources of income under the amnesty where—
    - ✗ that income has been declared for the year 2016 by a person earning taxable income outside Kenya; and
    - ✗ the returns and accounts for the year 2016 are submitted on or before the 31December, 2017;
    - ✗ Provided that this section shall not apply in respect of any tax where the person who should have paid the tax: has been assessed or investigated on income in question
- ✗ Effective Date: 01 January 2017

# TAX PROCEDURES ACT (TPA) 2015 ....CONT

- ✖ Tax overpaid
- ✖ Section 47 of TPA requires that when a taxpayer has overpaid a tax under a tax law the taxpayer may apply to the Commissioner, in the approved form, for a refund of the overpaid tax within one year of the date on which the tax was paid.
- ✖ Section 31 (4) (b) (i) of the TPA allows taxpayers to amend self assessment returns within 5 years from the date the return fell due.
- ✖ 2016 Finance Act has amended Section 47 of TPA to increase the period to 5 years so that the same is in harmony with Section 31 (4) (b) (i) of the TPA.
- ✖ **Effective Date: 01 January 2017**

# TAX APPEALS TRIBUNAL...KEY AMENDMENTS

- ✘ **Section 7:** The Secretary must be knowledgeable in procedures of a tribunal; and have a minimum of five years' experience in finance, economics or legal practice.
- ✘ **Section 11:** The clerk of each panel will act as its secretary and will be designated by the tribunal. Previously, this task belonged to Cabinet Secretary. A person shall be qualified to be appointed as a clerk unless that person is qualified to serve as a court clerk.
- ✘ **Section 15:**The Commissioner shall serve the appellant with a copy of the statement of facts and other documents required under this section within two working days from the date of submission to the Tribunal.
- ✘ **Effective Date: 01 January 2017**



# EXCISE DUTY ACT... AMENDMENTS

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- ✘ New Tariff 2710.19.22 Illuminating Kerosene to be charged at a rate of **Ksh. 7,205** per 1,000 litres
- ✘ Cosmetic and beauty products at 10%
- ✘ Excluding bottled drinking water from the 10% Excise duty
- ✘ Excise duty on second hand motor vehicles reverts back to 20%

# .....QUESTION AND ANSWERS.....

