Direct Tax Amendments through the Finance Act, 2018

Presentation by:

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CPA
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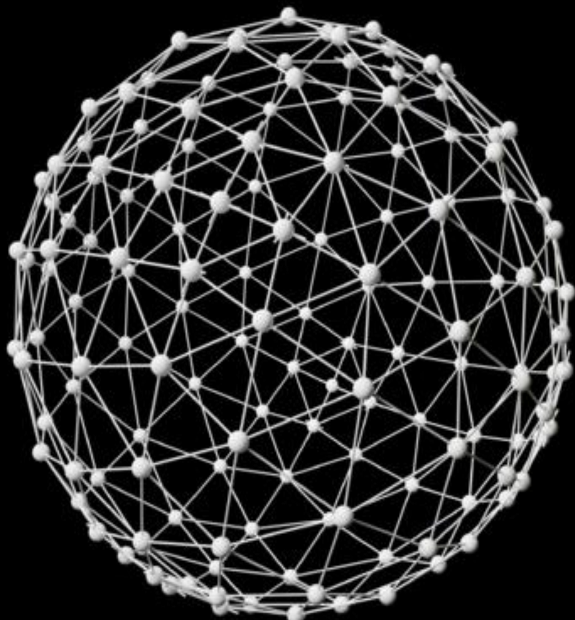
Corporate Income Tax



Deemed Dividends

The Finance Act 2018 has amended the Income Tax Act (ITA) by expanding the scope of deemed dividends to include the following:

- Distribution of any cash or assets to a shareholder or person related to the shareholder;

- Discharge of any obligations or settlement of debt on behalf of a shareholder or a connected/ related party to the shareholder;

- Use of any amount for the benefit of the shareholder or related party; and

- Transfer pricing adjustments made by KRA – i.e. amounts representing additional taxable income or reduced tax losses arising from adjustments by virtue of any transactions with a shareholder or a shareholder's related party.

- Any other benefit advanced to shareholders will be considered dividends

- If a company forfeits a loan receivable from a shareholder/ person related to the shareholder, the amount so forgiven/ forfeited will be considered a dividend. distribution;

Compensating Tax

- The current compensating tax provisions under Section 7A of the ITA have been repealed and replaced with a corporation tax of 30% if a company makes distributions out of ***untaxed profits***
- In our view, there may be challenges in implementing this tax. For instance, how will a company be required to determine dividends distributed out of untaxed profits?
- There may therefore be need for guidelines on how this tax will operate
- **Scenario:** Company A made profits before tax of KES 1m. The adjusted taxable income was 500k. The reserves as at 31 Dec 2018 was 800m which was to be distributed in full to company B which owns 100% share capital of company A and later to the individual shareholders of B. Compute compensating tax for both Company A and B before and after the change in the law.

Compensating Tax

Scenario

	Company A	Company B	
Income	500,000	800,000	
Tax on Income	150,000		
Current Law			
Distribution	800,000	800,000	
Dividend received *30/70		342,857	
Dividend paid *30/70	342,857	342,857	
Tax paid	150,000	Nil	
Balance- Compensating tax	192,857	Nil	**192,857**
Effective 1 Jan 2019			
Distribution	800,000	800,000	
Taxed reserves	350,000	Nil	
Balance not taxed	450,000	800,000	
Compensating tax	135,000	240,000	**375,000**

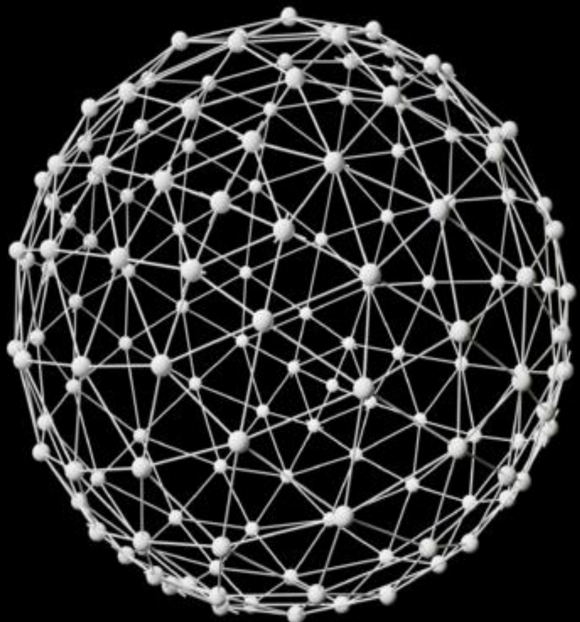
Presumptive Income Tax

- Presumptive tax of 15% of the business permit or license fee introduced for businesses whose turnover is below KES 5 Million per annum.
- Does not apply to corporate entities; rental income or income from management and professional services.

Others

- Manufacturers to be eligible to claim an additional 30% of their electricity bills subject to conditions set by the Ministry of Energy.
- Clarification that transfer of property by general insurance companies to be taxed as capital gains.

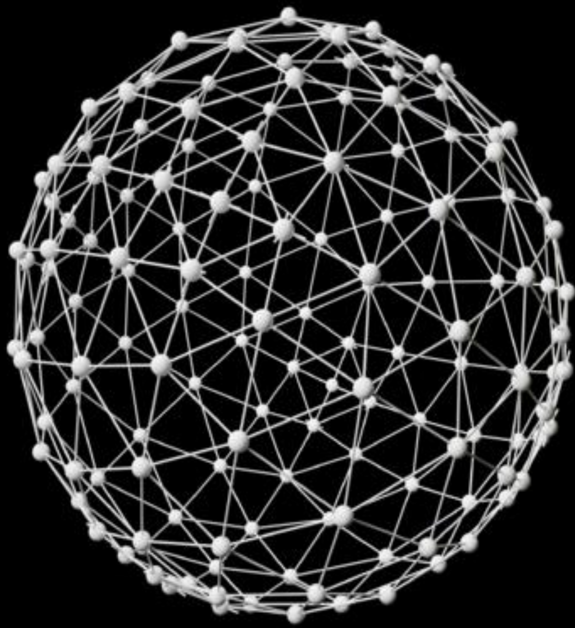
Withholding Tax



Demurrage and Insurance premium

- *<u>Demurrage charges</u>* defined as penalties paid for exceeding the period allowed for taking delivery of goods or returning equipment used to transport goods
- Withholding tax of 20% introduced on demurrage charges paid to non-residents.
- 5% withholding tax introduced on insurance premiums paid to non-residents excluding insurance premiums paid for insurance of aircrafts

PAYE



National Housing Development Fund

- The Employment Act has been amended to introduce a levy of 1.5% of an employee’s gross monthly emoluments and a matching contribution by the employers towards the National Housing Development Fund, subject to a maximum of KES 5,000
- Unless an amendment is introduced, all employees, regardless of how much they earn will be eligible to contribute the housing levy.
- The introduced law as envisaged does not also provide for an employee to be entitled to a deduction of the amount contributed or a relief. It would therefore be recommended that an amendment to the Income Tax Act is introduced to this effect

National Housing Development Fund

- Non eligible employees to either get a refund, transfer to pension or dependents at the earlier of expiry of 15years or retirement.
- Amounts paid in cash to be included in the employees taxable income and taxed.
- 5% penalty for failure to remit by the ninth of the following month.
- Effective upon gazettement of regulations by the CS.

Q & A

Contact details

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