TAX PRINCIPLES AND EMERGING ISSUES SEMINAR

Presentation by: Nickson Omondi

Tax Incentives in Kenya
Wednesday,17th Feb 2021

Uphold public interest

Tax Incentives

"I contend that for a nation to try to tax itself into prosperity is like a man standing in a bucket and trying to lift himself up by the handle". *Sir W. Churchill (US President)*

The Tough Balancing Act

- The issue has been how to strike an appropriate balance in meeting the ever-increasing competing needs (Tax revenue) vis a vis encouraging investment through lower taxes (Incentives).
- The International Bureau of fiscal decentralization defines "tax incentives" as "fiscal measures that are used to attract **local** or **foreign** investment capital to certain economic activities or particular areas in a country

Why and why not Tax incentives

Advantages

- A policy tool to attract increased foreign direct investment through lower tax burdens
- Encourage private sector participation in economic and social programs where government plays a key role

Disadvantages

Tax incentives make the tax system

- Less transparent
- Less predictable and
- Potential investors are likely to perceive taxation as less stable
- Has led to the tax problem referred to as the "*The race to the bottom*"

Corporate Tax Incentives

- Tax holidays or reduced tax rate
- Tax credits
- Investment allowances
- Accelerated depreciation
- Reinvestment or expansion allowances

Other Tax Incentives

- ✓ Exemption from or reduction of withholding taxes
- ✓ Exemption from import tariffs
- ✓ Exemption from export duties
- ✓ Exemption from sales, wage income or property taxes
- ✓ Reduction of social security contributions

EPZ and Related Activities

- ✓Export Processing Zones and related incentives EPZs were established in 1990 under the Export Processing Zones Act in order to attract FDI and turn Kenya into an export-based economy.
- ✓The zones were also intended to create jobs for the growing unemployed, lead to technology transfer and create linkages between domestic producers and exporters.

EPZ Tax Incentives

Numerous tax incentives are provided in the EPZs, the most significant of which are:

- ✓A 10-year corporate tax holiday for the first 10 years of operation, meaning they pay no corporation tax in this period;
- ✓After the 10-year holiday, EPZ entities are subject to a reduced CIT rate of 25% for another 10-year period;
- ✓Exemption of imports from import duty as well as VAT;
- ✓All goods and services supplied by local persons to the EPZ entities are treated as exports and are therefore subject to zero-rated VAT;
- ✓Exemption from stamp duty, which is a tax on the transfer and/or registration of certain assets such as land, shares among others;
- ✓Foreign directors are exempt from income tax.

SEZ Tax Incentives

A SEZ is defined as a designated area where 'business-enabling' policies, different land uses, and infrastructure and utilities are provided. Tax incentives include;

- Reduced corporate taxes of 10% for the first 10 years, then 15% for the subsequent 10-year period;
- Dividends paid to non-resident shareholders are exempt from tax;
- Management, training and professional fees payments made by an SEZ enterprise to non-resident persons are taxed at a reduced rate of 5%;
- Royalties or natural resource payments made by an SEZ to non-residents are subject to tax at the reduced rate of 5%;
- Interest on loans paid by an SEZ to a non-resident person is subject to a reduced tax rate of 5%;
- Exemption of imports from import duty as well as VAT;
- All goods and services supplied by local persons to the SEZs are zero-rated for VAT purposes

Foreign Tax Credit

- There is no tax credit for foreign tax paid on business income except as provided for by a DTA (if applicable) between Kenya and the other country.
- Kenya has 15 Tax Treaties.
- The Treaties provide various rates of tax which would be more favorable compared to non-DTA Rates.
- There is an incentive to do business in a country which has a DTA with Kenya

Instalment Taxes and Minimum tax

Non-Agricultural entities will pay instalments/minimum tax in 2 instalments instead of the 4 installments.

.

Investment Allowances

(a) Buildings–

(i) Hotel building - 50% in the first year of use

(ii) Building used for manufacture- 50% in the first year of use

(iii) Hospital buildings- 50% in the first year of use

(iv) Petroleum or gas storage facilities- 50% in the first year of use

(v) Residual value to item (a) (i) to (a)(iv) - 25% per year, on reducing balance

(vi) Educational buildings including student hostels -10% per year, on reducing balance

(vii) Commercial building -1 0% per year, on reducing balance

(b) Machinery –

(i) Machinery used for manufacture -50% in the first year of use

(ii) Hospital equipment- 50% in the first year of use

(iii) Ships or aircrafts - 50% in the first year of use

Investment Allowances

(iv). Residual value items (b) (i) to (b)(iii)- 25% per year, on reducing balance

(vi) Motor vehicles and heavy earth moving equipment- 25% per year, on reducing balance.

vii) Computer and peripheral computer software, calculators, copiers and duplicating machines- 25% per year, on reducing balance

(viii) Furniture and fittings- 10% per year, on reducing balance

(viii)Telecommunications equipment- 10% per year, on reducing balance

(ix) Filming equipment by a local film producer licensed by the Cabinet Secretary responsible for filming- 25% per year, on reducing balance

Investment Allowances

(x) Machinery used to undertake operations under a prospecting right - 50% in the first year of use and 25 per year, on reducing balance

(xi) Machinery used to undertake exploration operations under a mining right- 50% in the first year of use and 25% per year, on reducing balance .

(xii) Other machinery- 10% per year, on re.ducing balance

(c) Purchase or an acquisition of an indefeasible right to use fibre optic cable by a telecommunication operator- 10% per year, on reducing balance.

(d)Farmworks- 50% in the first year of use and 25% per year, on reducing balance

Other Incentives

- Legal expenses and stamp duties on acquiring a lease on premises not exceeding 99 years
- Expenditure on agricultural land clearance and planting of semi/permanent crops
- Cost of structural alterations to premises, incurred by a landlord to maintain the rent (non-capital)
- Expenses incurred by a lessee, in leasing transactions
- Interest paid on borrowings made to generate investment income (but restricted to the amount of investment income earned)
- Expenditure on scientific research

Other Incentives

In the case of a company that constructed at least four hundred residential units annually, fifteen per cent for that year of income.

Subject to approval by the Cabinet Secretary responsible for housing,.

Where a company is engaged in multiple activities , the rate of fifteen per cent shall be applied proportionately to the extent of the turnover arising from the housing activity.

Thank you