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TAX ALERT

Analysis of the Finance Act 2022

July 2022

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INCOME TAX

INCOME TAX - CORPORATION TAX

Definition of "fair market value"

The issue
The Act has introduced a definition of term "fair market value" to mean the comparable market price available in an open and unrestricted market between independent parties acting at arm's length and under no compulsion to transact, which is expressed in terms of money or money's worth.

Effective 1 July 2022

Implication
The amendment provides clarity on provisions in the Income Tax Act that relate to fair market value.

Deferral of foreign exchange losses where interest exceeds 30% of EBITDA

The issue
The Act has repealed the provisions of the ITA on deferral of claims of foreign exchange losses by thinly capitalized companies and replaced the same with restriction of foreign exchange losses realized by a company whose gross interest paid or payable to related persons and third parties exceeds 30% of the company's earnings before interest, taxes, depreciation and amortization ("EBITDA") in any financial year.

Effective 1 July 2022

Implication
This is aimed at aligning the provisions of the Income Tax Act following deletion of the thin capitalisation provisions and its replacement with the use of fixed profit ratios (EBITDA) to determine deductibility of foreign exchange losses.

INCOME TAX - CORPORATION TAX

Expansion of scope of deductibility of donation expenses

The issue
The Act has widened the scope of claims of deductions on donations to include any donation to a charitable organization whose income is exempt from tax under Paragraph 10 of the First Schedule to the ITA, or to any project approved by the Cabinet Secretary responsible for matters relating to finance. Initially, the deduction was only available in relation to cash donations to charitable organisations that are registered under either the Societies Act or the Non-Governmental Organisations Coordination Act and whose income is exempt from tax under Paragraph 10 of the First Schedule to the Income Tax Act or any project approved by the cabinet secretary responsible for finance

Effective 1 July 2022

Implication
The amendment is a recognition that an increasing number of charitable organizations are being registered under other legal regimes such as the Companies Act 2015 which provides for Companies Limited by Guarantee (CLGs) and the Trustees (Perpetual Succession) Act which provides for charitable trusts. Previously, entities which sought to donate to entities which were not registered under the Societies Act or the Non – Governmental Organizations Coordination Act could not claim a deduction of the cash donations against their taxable income. This therefore discouraged donations to such otherwise charitable organizations.

Going forward, donations to charitable organizations which are exempt from tax under Paragraph 10 of the First Schedule to the ITA will be tax deductible. This will hopefully increase donations to charitable organizations.

INCOME TAX - CORPORATION TAX

Additional institutions excluded from the interest restriction

The issue
The Act has expanded the list of entities exempted from the EBITDA based interest limitation introduced by the Finance Act, 2021 to include the following:

I. Microfinance institutions licensed and non – deposit taking microfinance businesses under the Microfinance Act, 2006;

II. Entities licensed under the Hire Purchase Act;

III. Non – deposit taking institutions involved in lending and leasing business;

IV. Companies undertaking the manufacture of human vaccines;

V. Companies engaged in manufacturing whose cumulative investment in the preceding five years from the commencement of this provision is at least five billion shillings (KES 5,000,000,000);

VI. Companies engaged in manufacturing whose cumulative investment is at least five billion shillings, provided that the investment shall have been made outside Nairobi City County and Mombasa County; and

VII. Holding companies that are regulated under the Capital Markets Act.

Effective 1 July 2022

Implication
The list seeks to grant relief to entities which traditionally have a high interest expense and would have suffered from an unusually high tax burden due to the disallowance of part of the interest expense. This move is welcome and will likely see increased investments as they will be in a capacity to take on more debt to expand their operations without the restrictions on the deductibility of the interest expense.

INCOME TAX - CORPORATION TAX

Expansion of accelerated capital allowance

The issue
Initially the second paragraph to the Income Tax Act provided for accelerated investment allowance of 100% to any person where: the cumulative investment value in the preceding 3 years outside Nairobi City County and Mombasa County is at least KES 2B.

The Act has amended the Income Tax Act in order to provide for an accelerated investment allowance of 150% where the cumulative investment of at least KES 2B is made outside Nairobi or Mombasa County and it relates to the period being:

(a) the preceding 4 years from the date the provision comes into force (01 July 2022); or

(b) the succeeding 3 years from the date from 01 July 2022;

Effective 1 July 2022

Implication
The amendment is in line with the big 4 agenda which seeks to stimulate substantive capital investments. It will likely encourage the decongestion of investments within Nairobi and Mombasa Counties. In addition, the amendment will increase the attractiveness of Kenya as an investment hub for investors seeking for an accelerated return on their investment with minimal tax leakages.

INCOME TAX - CORPORATION TAX

Expansion of the definition of the term manufacture

The issue

The Act has amended the definition of the word "manufacture" by deleting the words "for the supply to the national grid" which appear in the definition of the word manufacture. Effectively manufacture is now defined by Second Schedule to mean "the making, including packaging, of goods from raw or semi-finished goods, **or the generation of electrical energy**, or the transformation and distribution of electricity, but does not include design, storage, transport, administration or any other ancillary activity**.**

Effective 1 July 2022

Implication

This amendment means that transformation and distribution of off-grid electricity qualifies as manufacture, and any machinery that is used for such purposes shall qualify for capital allowances of 50% in the first year of use, and 25% per annum thereafter

This amendment will allow entities to take a capital allowance deduction on the often-expensive investments incurred in a bid to shift reliance from grid power to onsite generation of electricity. Previously, such investments were not eligible for capital allowance deduction as they were deemed to not be in the realm of manufacture as the power generated was utilized on site and not distributed through the national grid.

INCOME TAX – EXEMPTIONS

Exemptions for companies manufacturing human vaccines

The issue

The Act has introduced the following exemptions in relation to entities involved in the manufacture of human vaccines :

i. Deemed interest in respect of an interest free loan advanced to a company undertaking the manufacture of human vaccines.

ii. Payments made to non-resident service providers not having a permanent establishment in Kenya in respect of services provided to a company undertaking the manufacture of human vaccines.

iii. Compensating tax accruing to a company undertaking the manufacture of human vaccines.

iv. Dividends paid by a company undertaking the manufacture of human vaccines to any non-resident person.

v. Income of a company undertaking the manufacture of human vaccines.

These exemptions were not included in the Bill.

Effective 1 July 2022

Implication

The Amendment seeks to grant tax exemptions to entities engaged in the manufacture of human vaccines which aligns with the government's agenda in ensuring that Kenya is better prepared for global pandemics and in line with the government's intent to make Kenya a hub for vaccines manufacturing.

INCOME TAX – EXEMPTIONS

Reintroduction of exemptions available for Special Economic Zones

The issue

The Act has reintroduced tax exemptions on the following in relation to Special Economic Zone entities:

i. Dividends paid by Special Economic Zone enterprises, developers and operators licensed under the Special Economic Zones Act.

ii. Dividends paid by Special Economic Zone enterprises, developers and operators to any non-resident person.

Effective 1 July 2022

Implication

the Act reintroduces the exemption from income tax on dividends paid by a Special Economic Zone enterprises which was deleted by the Tax Laws (Amendment) Act 2020. This is a welcome move and further affirms the government commitment to ensuring that Special Economic Zones remain a key attraction for investments.

INCOME TAX – TRANSFER PRICING

Expansion of the scope of transfer pricing for entities operating in a preferential tax regime

The issue

Currently, the ITA requires that transfer pricing(TP) provisions apply in relation to dealings between a ***resident entity operating in a preferential tax regime*** and ***a related resident entity not operating in a preferential tax regime***. The Finance Act has expanded the scope of TP to include transactions between resident entities and:

- ✓ a non-resident person located in a preferential tax regime; or
- ✓ an associated enterprise of a non-resident person located in a preferential tax regime; or
- ✓ a permanent establishment (PE) of a non-resident person operating in Kenya where the non-resident person is in a preferential tax regime.

The term "preferential tax regime" has been defined to mean any Kenyan legislation, regulation or administrative practice which provides a preferential rate of tax to such income or profit, including reductions in the tax rate or the tax base or a foreign jurisdiction which does not tax income, taxes income at a rate that is less than 20%, does not have a framework for the exchange of information, does not allow access to banking information or lacks transparency on corporate structure, ownership of legal entities located therein, beneficial owners of income or capital, financial disclosure, or regulatory supervision.

Effective 1 January 2023

Implications

Initially the arm's length requirement only applied to transactions between resident persons operating in a preferential tax regime and related resident persons operating outside a preferential tax regime. The change has widened the scope of transactions to which transfer pricing requirements apply by including non-resident persons operating within the preferential tax regime. This will increase administrative and compliance burden on entities whose transactions fall within the broader ambit of transfer pricing.

INCOME TAX – TRANSFER PRICING

Country by country reporting notification

The issue

The Act has introduced a requirement for multinational enterprise groups (MNE) or constituent entity resident in Kenya with a gross turn over of KES 95B (Approx. USD 820M) to notify the Commissioner as to whether it is the ultimate parent entity (UPE) or surrogate entity in the group or where it is neither the UPE or surrogate, the tax residence of the constituent entity that is the UPE or surrogate entity in the group.

The notification is required to be made to the Commissioner not later than the last day of the reporting financial year of the Group

Effective 1 July 2022

Implication

While the notification requirement may increase tax compliance and administration burden on taxpayers, the same will assist the Commissioner identify the entity responsible for submission of the country-by-country report within the group. In addition, the change aligns the local reporting requirements to international best practice for instance by introduction of a reporting threshold in line with the OECD regulations.

INCOME TAX – TRANSFER PRICING

Country by country filing requirement

The issue

The Act has introduced CbC filing requirements for MNE group entities resident in Kenya with gross turn over of KES 95Billion. The report should detail the group's financial activities in Kenya and other jurisdictions it operates in and should be filed not later than 12 months after the last day of the reporting financial year of the Group.

An MNE not headquartered in Kenya will not be required to file a CbC report with the commissioner if:

- ✓ The UPE is required to file a CbC report in its jurisdiction of residence;
- ✓ The jurisdiction where the UPE is resident has an international agreement for exchange of tax information with Kenya; or
- ✓ The commissioner has not notified the resident constituent entity in Kenya of any systematic failure to comply with the exchange of information (if any).

In addition, the Act has introduced the requirement for MNE's resident in Kenya to file a local file and a master file not later than six months after the last day of the reporting financial year of the MNE group. The local file should contain material transactions of the local taxpayer while the master file contains standardized information relevant for all the MNE group members.

Effective 1 July 2022

Implication

This change is in line with international best practice and in particular the OECD BEPS action 13 report which proposes a three thronged approach to documentation namely, master file , local file and the country-by-country report. While the detailed reporting requirement will definitely increase the burden of tax compliance and administration on MNEs, the same will go along way in enhancing transparency in relation to taxation of multinations.

INCOME TAX – CAPITAL GAINS TAX

Increase tax rate on capital gains from 5% to 15%

The issue

The Act has amended the Income Tax Act by increasing the rate of tax on capital gains from 5% to 15% provided that in the case of a firm certified by the Nairobi International Financial Centre Authority that:

(a) Invests KES 5B in Kenya; and

(b) The transfer of such investment is made after five years. The applicable rate shall be the rate that was prevailing at the time that the investment was made.

Effective 1 January 2023

Implication

This amendment follows previous failed attempts by the government to increase the capital gains tax (CGT) rate. Following the introduction of the capital gains tax in 2015, the government has continuously insisted that the previous rate of 5% was well below the CGT rate in the neighbouring countries, some of which have a relatively higher tax CGT rate of 30%.

While the Act has increased the CGT rate, taxpayers cannot benefit from indexation in order to take into account gains which relate to inflation. As such, the increase in the rate of CGT is a blow to taxpayers as many taxpayers will end up being taxed on gains related to inflation which is prohibitive. Further, the abrupt three – fold increment in the rate of CGT will likely lead to an increase of instances of tax evasion and avoidance. In addition, the increased CGT rate will be a drawback to the attractiveness of Kenya as an investment hub.

The exemption to firms certified by the Nairobi International Financial Centre Authority while welcome will only offer a short-term relief considering that there may be investments which may be scheduled to take place after 01 January 2023 and which will not be covered by the exemption.

INCOME TAX – WITHHOLDING TAX

Withholding tax on gains accruing to non-residents from a financial derivative contract with a resident

The issue

The Act has introduced withholding tax at the rate of 15% on gains accruing to non-resident persons from a financial derivatives contract with a resident person in Kenya. The term "financial derivative" is defined as a financial instrument whose value is linked to the value of another instrument underlying the transaction which is to be settled at a future date. The Cabinet Secretary for National Treasury and Planning ("CS") is expected to publish regulations for implementation of the amendment.

Effective 1 January 2023

Implication

This Amendment is a move by the government to increase the tax revenue base by bringing into the tax ambit gains from financial derivatives derived from the Kenyan market. This is also a response move by the government to earn revenue from the increased use of hedging by local entities caused by the need to navigate the volatile international market due to the ongoing conflict in Eastern Europe. Due to the often-complex nature of financial derivatives contracts, the proposed regulations will be critical in the operationalization of the provision .

BOWMANS

THE VALUE OF KNOWING

PAY AS YOU EARN (PAYE)

PERSONAL INCOME TAX – PAYE

Clarification on the definition of permanent home

The issue

The Act has introduced a definition of "permanent home" to mean a place where an individual resides or which is available to that individual for residential purposes in Kenya, or where in the opinion of the Commissioner the individual's personal or economic interests are closest.

Effective 1 July 2022

Implication

The inclusion of a definition of permanent home will provide the much-needed clarity on what qualifies an individual as a tax resident in Kenya. However, the discretion granted to the Commissioner to determine an individual's personal and economic interest is subjective and will lead to ambiguity in relation to the question of tax residency for individual. Some clarity and or guidelines should be provided on how the Commissioner will make the determination.

PERSONAL INCOME TAX – PAYE

Change in determination of taxable benefit accruing from employee share ownership schemes (ESOPS)

The issue

Initially, the Income Tax Act provided that a taxable gain in relation to ESOPS was the difference between the offer price and market price as at the point the option is granted by the employer. The Act has amended the computation of the benefit to be the difference between market value of the share at the point the employee exercises the option and the offer price at the point of granting the option by the employer. Further, the benefits will now accrue on the date the employee exercises the option as opposed to the end of the vesting period.

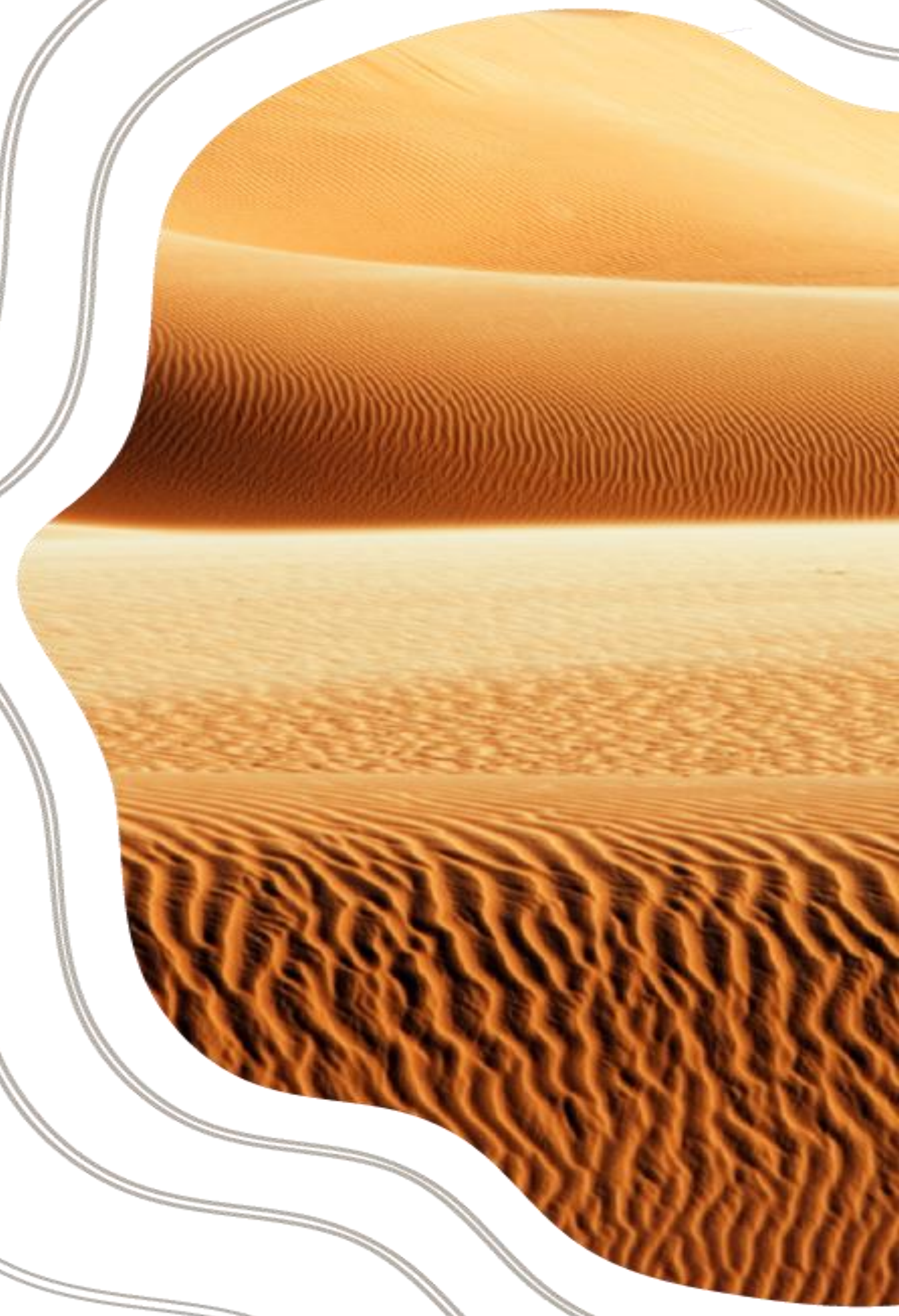
Effective 1 July 2022

Implication

The effect of the change is to harmonize taxation of ESOPS as there is no longer reference to registered or unregistered ESOPs. The change on determination of taxable value will inevitability mean that employees may bear a higher tax charge as compared to when the value of benefit was the difference between the market value of the shares and the offer price at the date of the grant of the options.

With respect to the date the benefits are deemed to have accrued, the benefits are deemed to have accrued at the exercise date rather than the end of the vesting period which in our view is more favorable since an employee was taxed at the end of vesting period even if they had not exercised their options.

VALUE ADDED TAX(VAT)



VALUE ADDED TAX

Additional Requirement For Deduction of Input Tax

The Provision

The Act has amended the Value Added Tax Act, 2013(VAT Act) by linking the deduction of input tax to the filing of the return for the tax period in which the taxable supply occurred.

Effective 1 July 2022

Implications

The proposal seeks to impose further obligations on the claiming input VAT by VAT registered taxpayers. The new provision requires (among others) that a taxpayer can only be held to have claimed input VAT once he files a VAT return for the period in which he claims input VAT.

Interest and Penalties on late payment of Import VAT

The Provision

The Act has amended the VAT Act to provide that the provisions of the Tax Procedures Act regarding imposition of interest and penalties shall apply on late payment of import VAT. Further, the Act also clarifies that in cases where interest becomes payable, it shall not, in aggregate, exceed the principal tax.

Effective 1 July 2022

Implications

This amendment is welcome since it seeks to harmonize the administrative provisions and have a unified and predictable regime on the application of penalties and interest. Going by the Tax Procedures Act, the penalties and interest are less punitive to the taxpayer which offers relief to importers. In this regard, the late payment interest under the Tax Procedures Act is one percent (1%) per month as compared to the East Africa Community Customs Management Act where the late payment interest is two percent (2%) per month.

Value Added Tax on Liquefied Petroleum Gas (LPG)

The Issue

The Act has amended the Value Added Tax Act, 2013(VAT Act) by introducing a new provision which imposes VAT of 8% on the supply of liquefied petroleum gas (LPG) including propane. Previously, the supply of LPG was subject to 16% VAT.

Effective 1 July 2022

Implications

This provision comes into force barely a year after the Government re- introduced VAT of 16% on LPG after zero-rating LPG in 2016. Overall, the amendment is aimed at reducing the cost of LPG which is a common fuel in many Kenyan households and in turn increasing access to clean fuels and the disposable income of low-income families.

The amendment ties in with the Government's agenda to achieve 100% clean energy access by the year 2028.

VALUE ADDED TAX

Changes Relating To supplies made over a digital marketplace

The Issue

The Act has amended the definition of a digital marketplace under the VAT Act to mean an online platform which enables users to sell goods or provide services to other users.

Further it has excluded supplies made through a digital marketplace from the ambit of VAT on imported services and accounting under the reverse charge VAT mechanism.

In addition, the Act has amended the VAT Act to exclude persons supplying imported digital services from the VAT registration threshold.

Effective 1 July 2022

Implications

- The amendment in the definition of the digital marketplace is a clarification of the provisions of the VAT Act as it deletes the word property which is not defined in the VAT Act. Under the VAT Act, the only supply that can be made is either a supply of goods or a supply of services.
- The exclusion of supplies made over the digital marketplace from the reverse charge VAT mechanism now means that business will no longer have the ability to account for VAT using the reverse VAT mechanism for supplies made over the digital marketplace. This amendment coupled with amendments made under the VAT (Digital Marketplace Supply) (Amendment) Regulations, 2022 now mean that suppliers of digital services will be required to charge VAT when making digital supplies to businesses. Previously, businesses were not subject to VAT for digital supplies provided that they notified the relevant supplier that they were accounting for VAT under the reverse charge mechanism.
- The exclusion of foreign digital service suppliers from the VAT registration threshold will mean that all suppliers must register for VAT regardless of the value of their transactions which may pose administrative challenges especially where the supplies made are low value or low volume.

VALUE ADDED TAX

Claim of Input Tax by Oil Marketing Companies

The Provision

The Act has amended the Value Added Tax Act, 2013(VAT Act) by providing that to claim input tax, a participant in the Open Tender System for the importation of petroleum products that have been cleared through a non-bonded facility shall in addition to the usual documentation required to claim input tax, be required to produce the custom entry showing the name and PIN of the winner of the tender and the name of the other oil marketing company participating in the tender.

However input tax incurred by oil marketing companies (OMCs) that have participated in the open tender system prior to this provision coming into force can be claimed within twelve months.

Effective 1 July 2022

Implications

The amendment is aimed at ensuring that input is only claimed where it can be proven that the petroleum products were declared at the point of entry and import duties paid by the winning bidder, who subsequently sold the petroleum to other OMCs. This is in line with a recent Tax Appeals Tribunal decision (***Libya Oil Kenya Limited vs. Commissioner of Investigations and Enforcement)*** which held that the tax point with regard to petroleum products for the payment of the various duties and levies is when the goods are imported and entered for home use and before release of the product to OMCs.

The twelve month window will however allow OMCs to claim input tax that has already been incurred and allow them time to become compliant with the new provisions.

VALUE ADDED TAX

Repeal of The Provisions For Refund of Taxes Paid in Error

The Issue

The Act has deleted the provisions under the VAT Act relating to refund of VAT paid in error.

Effective 1 July 2022

The Implications

While this provision has been repealed under the VAT Act, it has now been introduced in the Tax Procedures Act as part of a clean up exercise that seeks to harmonise the tax administrative procedures under one law which is the Tax Procedures Act.

VALUE ADDED TAX

Change of VAT Status Of Goods/Services

The Issue

The Act has amended the first and second schedules to the VAT Act by changing the VAT treatment of various goods as services as summarized below and in the subsequent slides.

Effective 1 July 2022

The Implications

We discuss the implications of changes against each item below.

Item	Old VAT Treatment	New Treatment	Implication
*Taxable goods for the direct and exclusive use in the construction and equipping of specialized hospitals with a minimum bed capacity of fifty, approved by the Cabinet Secretary upon recommendation by the Cabinet Secretary responsible for health and taxable services for direct and exclusive use for the construction of specialized hospitals with accommodation facilities upon recommendation by the Cabinet Secretary responsible for health. Approvals granted by the Cabinet Secretary before the commencement of the change in respect of the supply of taxable goods/services to continue to apply until the supply of the exempted construction of specialized hospitals is completed	Exempt	Standard rated	Standard rating of these goods does not resonate with the government's agenda on promoting access to affordable healthcare. It will likely make investments in healthcare unattractive and costly. However, the parliament has included a savings provisions which ensures that any person who had been granted the exemption will continue enjoying the exemption until the supply is completed.

VALUE ADDED TAX

Change of VAT Status Of Goods/Services (Cont….)

Item	Old VAT Treatment	New Treatment	Implication
• Plant and machinery of Chapter 84 and 85 imported by manufacturers of pharmaceutical products or investors in the manufacture of pharmaceutical products upon the recommendation of the Cabinet Secretary responsible for matters relating to health; • medical oxygen supplied to registered hospitals • Urine bags, adult diapers, artificial breasts, colostomy or ileostomy bags for medical use.	Standard rate	Exempt	This amendment is meant to increase access to quality and affordable healthcare in line with the Big 4 Agenda. The exemption of medical oxygen from VAT is fueled by the COVID 19 pandemic that saw an increase in demand of the product. The exemption of urine bags, adult diapers, artificial breasts and colostomy bags is part of a wider initiative to reduce the cost of treatment for cancer and terminal illnesses.
Inputs and raw materials used in the manufacture of passenger motor vehicles and locally manufactured passenger motor vehicles (total value comprises at least thirty per cent of parts designed and manufactured in Kenya by an original equipment manufacturer operating in Kenya)	Standard rated	Exempt	The exemption is meant to attract investments in the automotive sector as well as promote manufacturing in line with the Government's Big 4 Agenda. In addition, this exemption is likely to lower the cost of locally assembled cars which should increase the sales of local car manufacturers.
Goods, inputs and raw materials imported or locally purchased by a company; • engaged in business under a special operating framework arrangement with government and; • incorporated for purposes of undertaking the manufacture of human vaccines with a capital investment of at least ten billion shillings.	Standard rated	Exempt	The proposed exemption is meant to drive research and development in the medical sector and spur the production of vaccines in Kenya. Overall, this would make healthcare accessible as well as promote economic growth in Kenya in case these vaccines are exported outside Kenya.

VALUE ADDED TAX

Change of VAT Status Of Goods/Services (Cont.…)

Item	Old VAT Treatment	New Treatment	Implication
Bioethanol vapour (BEV) stoves under HS Code 7321.11.00 (cooking appliances and plate warmers for liquid fuel)	Standard rated	Exempt	This exemption is meant to reduce the cost of importation of BEV stoves and simultaneously drive the use of clean fuel in Kenya with the aim of transforming every household to clean energy by 2028.
Exportation of taxable services	Exempt	Standard rated	The change in status of exported services comes a year after exported services were rendered exempt. The change is unprecedented, and it goes against the Organisation of Economic Cooperation and Development (the **OECD**) destination principle which provides that tax should be charged in the place where consumption takes place. This change is likely to make the exportation of services expensive for consumers (outside Kenya) as they will be charged Kenyan VAT and may also be subject to reverse charge VAT in their home countries which is applied on the importation of services.
Exportation of taxable services in respect of business process outsourcing	Exempt	Zero rated	The zero rating of taxable services with respect to business process outsourcing is designed to make it attractive to set up business processing outsourcing entities in Kenya.

VALUE ADDED TAX

Change of VAT Status Of Goods/Services (Cont.…)

Item	Old VAT Treatment	New Treatment	Implication
Fertilizers of chapter 31	Exempt	Zero Rated	The zero-rating is aimed at reducing the cost of fertilisers by allowing suppliers to claim refunds. This would then promote access to quality fertilisers by farmers and overall promote agriculture.
Fuel pellets for household and commercial use	Standard rated	Exempt	This increases the list of exempt fuels and is aimed at encouraging single use of clean energy in Kenyan households.
Inputs or raw materials locally purchased or imported by manufacturers of fertilizer as approved from time to time by the Cabinet Secretary responsible for Agriculture.	Standard rated	Zero rated	The zero-rating of these goods will make production less costly and ultimately lead to affordability of fertilizer which in turn lowers the cost of food. This is in line with the government's agenda on promoting food security.
Capital goods the exemption of which the Cabinet Secretary may determine to promote investment in the manufacturing sector Provided that the value of such investment is not less than two billion shillings.	Standard rated	Exempt	This is a huge welcome for persons who wish to invest in the manufacturing sector and it underscores the government's intention to support manufacturing in the country.

VALUE ADDED TAX

Change of VAT Status Of Goods/Services (Cont.…)

Item S	Old VAT Treatment	New Treatment	Implication
Supply of protective apparel, clothing accessories and equipment	Zero rated	Standard rated	It is not clear why the supply of protective clothes and equipment for use in registered hospitals and clinics or local authorities in fire fighting have been standard rated. This is likely to increase the prices of these items which are critical for service provision in hospitals and during fire fighting.

EXCISE DUTY

EXCISE DUTY

Exemption of Specified Products From Inflationary Adjustment By The Commissioner

The Issue

The Act has amended provision of the Excise Duty Act on inflationary adjustment to allow the Commissioner to exempt specified products from the inflation adjustment after considering the circumstances prevailing in the economy in that year in respect of such products. However, this is subject to approval by the Cabinet Secretary (CS) for the National Treasury and shall be communicated through a notice in the Kenya Gazette.

Effective 1 January 2023

The Implications

The annual inflationary adjustment of Excise Duty on products with specific rates has had the negative impact of increasing the cost of such products since its introduction vide the Finance Act 2020. Even though the provisions that introduced the annual review were not framed in mandatory terms , there was no express provision for exemption of products from the review. The introduction of the Commissioner's discretion to grant exemption is a good change since it will protect certain sectors and consumers from the negative economic effects of price increases, especially on essential products. However, the amendment does not provide details on what the Commissioner will consider in granting the exemption.

EXCISE DUTY

Penalties And Interest In Relation To Excise Duty On Imported Goods To Be As Per The Tax Procedures Act

The Issue

The Act has amended the Excise Duty Act to provide for application of the provisions of the Tax Procedures Act with regards to imposition of penalties and interest on excise duty on imported goods. In addition, the *in duplum* rule on interest payable will now apply with respect to excise duty.

Effective 1 July 2022

The Implications

Prior to the amendment, late payment interest of 2% per month as provided for under the East African Community Customs Management Act (EACCMA) would apply on Excise Duty on imported goods. (EACMMA was silent on whether the interest was simple or compounded). With the amendment, interest of 1% per month (simple interest subject to the *in duplum* rule) and 5% penalty will apply as provided for under the TPA. This will amount to lower interest which will be capped to the amount of the principal tax and thus cushion importers from punitive interest regime under the EACCMA. In addition, the change will harmonize the administration of Excise Duty under the TPA

EXCISE DUTY

Increase Of Excise Duty On Specific Products

The Issue

The Act has amended the First Schedule to the Excise Duty Act by increasing the excise duty rate on various goods and services mostly products considered as "harmful products" and "luxurious products" as per the table below:

Product Description	Old Rate	New Rate
Fruit juices (including grape must), and vegetable juices, unfermented and not containing added spirit, whether or not containing added sugar or other sweetening matter	KES 12.17 per litre	KES 13.30 per litre
Cosmetics and Beauty products of Tariff Heading No. 3303, 3304, 3305 and 3307	10%	15%
Beer, cider, perry, mead, opaque beer and mixtures of fermented beverages with non-alcoholic beverages and spirituous beverages of alcoholic strength not exceeding 6%	KES 121.85 per litre	KES 134 per litre
Wines including fortified wines, and other alcoholic beverages obtained by fermentation of fruits	KES 208.20 per litre	KES 229 per litre
Spirits of undenatured ethyl alcohol; spirits liqueurs and other spirituous beverages of alcoholic strength exceeding 6%	KES 278.70 per litre	KES 335.30 per litre
Cigars, cheroots, cigarillos, containing tobacco or tobacco substitutes	KES 13,906.04 per kg	KES 15,296.6 per kg
Cigarette with filters (hinge lid and soft cap)	KES 3,477.61 per mille	KES 3,825.99 per mille
Cigarettes without filters (plain cigarettes)	KES 2,502.74 per mille	KES 2,752.97 per mille

EXCISE DUTY

Increase Of Excise Duty On Specific Products (cont.)

Product Description	Old Rate	New Rate
Other manufactured tobacco and manufactured tobacco substitutes; "homogenous" and "reconstituted tobacco";	KES 9,734.45 per kg	KES 10,707.88 per kg
Imported sugar confectionery of Tariff Heading 17.04	KES 36.74 per kg	KES 40.37 per kg
White chocolate, chocolate in blocks, slabs or bars of tariff numbers 1806.31.00, 1806.32.00 and 1806.90.00	KES 220.31 per kg	*KES 242.29 per kg
Jewellery of tariff heading 7113 and imported jewellery of tariff heading 7117"	10%	15%
Products containing nicotine or nicotine substitutes intended for inhalation without combustion or oral application but excluding medicinal products approved by the Cabinet Secretary responsible for matters relating to health and other manufactured tobacco and manufactured tobacco substitutes that have been homogenized and reconstituted tobacco, tobacco extracts and essences	KES 1,259.64 per kg	KES 1,500 per kg

Effective date 1 July 2022

The implications

The affected products are mostly the traditional "harmful" and luxury products. While the change is aimed at generating more revenue for the Government, it will result in an increase in the prices of the products, bearing in mind that there may be a further review of the excise duty on the same via the annual adjustment later in the year. In the long run, the sustained price increases may push consumers to find alternative products or forgo the products altogether and thus reduce the revenue the Government intends to earn from the increases.

EXCISE DUTY

Introduction and Deletion of Products from the Excise Duty Schedule

The Issue

The Act has amended the First Schedule of the Excise Duty Act by introducing the following products to the excise duty regime:

Product Description	Excise duty rate
Articles of plastic of Tariff Code 3923.90.90 (other articles of plastic for conveyance or packing)	10%
Imported potatoes of Tariff Code 0710.10.00, 2004.10.00 and 2005.20.00	25%
*Electronic cigarettes and other nicotine delivery devices	40%
**Liquid nicotine for electronic cigarettes	KES 70 per mille
Imported ready to use SIM cards	KES 50 each
Fees charged by digital lenders	20%
Importation of cellular phones	10%
3907.91.00 Imported unsaturated polyester	10%
3907.50.00 Imported Alkyd	10%
3905.91.00 Imported emulsion VAM	10%
3903.20.00 Imported emulsion-styrene Acrylic	10%
3905.19.00 Imported homopolymers	10%
3906.90.00 Imported emulsion B.A.M	10%

**Replaced electronic cigarettes which attracted duty at KES 4,171.59*
***Replaced cartridges used in electronic cigarettes*

EXCISE DUTY

Introduction and Deletion of Products from the Excise Duty Schedule (Cont…..)

The Act has further amended the First Schedule of the Excise Duty Act by deleting the following items from the excisable goods schedule:

Product Description	Excise duty rate
Imported furniture of any kind used in offices, kitchen, bedroom and other furniture	25%
3907.91.00 unsaturated polyester	10%
3907.50.00 Alkyd	10%
3905.91.00 Emulsion VAM	10%
3903.20.00 Emulsion-styrene Acrylic	10%
3905.19.00 Homopolymers	10%
3906.90.00 Emulsion B.A.M	10%
Betting on horse racing	7.5%

Effective 1 July 2022

The Implications

While generally the widening of scope of Excise Duty is meant to increase Government revenue, some of the measures are aimed at discouraging consumption of certain products by increasing their costs and protecting local industries by imposing duty on imported items or raw materials that are available locally.

The introduction of duty on imported potatoes, sim cards and cellular phone and the various raw materials (local products deleted from the excise duty schedule) appears to be aimed at protecting the local farmers and manufacturers of the items and encouraging local manufacture of the items.

EXCISE DUTY

Introduction of additional products in the exemption schedule

The Issue

The Act has amended the Second Schedule of the Excise Duty Act by introducing the following new items to the exemption schedule:

Product Description
Neutral spirit imported or purchased locally by registered pharmaceutical manufacturers upon approval by the Commissioner
*Locally manufactured passenger motor vehicles

*Provided that in this paragraph,

"locally manufactured passenger motor vehicle" means a motor vehicle for the transportation of passengers which is manufactured in Kenya and whose ex-factory value comprises at least thirty percent of local content;

"local content" means parts designed and manufactured in Kenya by an original equipment manufacturer operating in Kenya.

Effective 1 July 2022

The Implications

Prior to the change, excise duty was payable on neutral spirit. However, the Act provided for refund of Excise Duty on spirits used for manufacture of unexcisable goods. The exemption will reduce the cash flow challenges faced by manufacturers due to delays from processing of refund of Excise Duty and lower the cost of the relevant pharmaceutical products and lead to affordable health care.

The Excise Duty Act generally excludes locally assembled motor vehicles from the ambit of excise duty. The change provides for exemption of locally manufactured passenger vehicles that may not qualify for exemption under the current regime. This will reduce the cost of locally manufactured passenger vehicles that meet the conditions

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TAX PROCEDURES

TAX PROCEDURES

Requirement of a PIN to Register a Trust and Notification Requirement for Changes of the Details of a Trust

The Issue

The Act has amended the Tax Procedures Act, 2015 ("TPA") to require trusts in Kenya(whether carrying out business or not) to notify the Commissioner of any changes in the identity and addresses of the trustees and beneficiaries of the trust, within 30 days of the occurrence of the change.

The Act further amends the TPA's First Schedule to include the registration of a trust as among the transactions for which a tax PIN is required.

Effective 1 July 2022

The Implications

The effect of the change is to impose notification requirements on trusts whether the trust is carrying on a for-profit business or not. Further a person who wishes to set up a trust in Kenya, must registered for tax and have a PIN number.

Ultimately the changes are aimed at increasing transparency on the tax affairs of trusts in line with the latest developments in Kenya and in other jurisdictions and disclosure of beneficial interest under the Companies Act 2015 .

TAX PROCEDURES

Amendment of Self-assessments with Respect to Input VAT to be Limited to a 6-month Period

The Issue

The Act has amended the TPA to restrict amendments to a taxpayer's VAT self-assessment so that input tax is only allowable for deduction within six (6) months after the end of the tax period in which the supply or importation occurred.

Effective 1 July 2022

The Implications

This change aligns with requirement to claim input VAT within 6 months of the supply/importation under the VAT Act 2013. The effect of this will be to lock out any claims of input tax in relation to returns amended more that six months from the transaction date and is contrary to the provisions of TPA which allows for amendment of self-assessment returns for other tax heads within five years from the date of original returns.

TAX PROCEDURES

Increased scope of property to be used as security for unpaid taxes

The Issue

The Act has repealed Section 40 of the TPA and widened the scope of property that the Commissioner may use as security for unpaid tax to include land, buildings, aircrafts, ships motor vehicles and any other property that the Commissioner may deem sufficient as security. Prior to the change , the Section 40 provided for the use of only land and buildings as security for tax arrears. A taxpayer who receives a notice of attachment is required to settle the tax arrears within two months failure to which the Commissioner may dispose the asset at the taxpayer’s cost.

Effective 1 July 2022

The Implications

The amendment allows the KRA greater access to a taxpayer’s assets by widening the pool of the property that may be encumbered or used as security for unpaid taxes hence the KRA will have greater chance to recover unpaid taxes. Giving priority to registered prior restraints once the property is sold is proper as it recognizes competing interests and allows parties who have interests in the property a claim to the proceeds. However, the two month-period for settlement of tax arrears is short and may prejudice taxpayers.

The above said, we note that the new provisions overlap to some extent with those of Section 41 of the TPA which empowers the Commissioner distress orders against movable property for recovery of taxes from a taxpayer.

Changes to Provisions on Agency Notices

The Issue

The Act has made the following changes to the provisions on issuance of agency notices:

- Increasing the time within which an agent who has been served with an agency notice but has failed to comply by reason of lack of monies held on behalf of or due to the taxpayer is required to notify the Commissioner of his inability to comply from seven (7) to fourteen (14) days of receiving the notice;
- The Commissioner is required to concurrently serve the agency notice on both the agent and the taxpayer. Initially, while the Commissioner was required to serve the taxpayer with a copy of the notice served on the agent, the timelines for the service were not specified; and
- An agency notice may only be issued after the Commissioner has either confirmed its assessment through an objection decision and the taxpayer has defaulted to appeal to the TAT

Effective 1 July 2022

The Implications

The issue of the characterization of agency notice (the courts have determined agency notices to be appealable decisions) and whether agency notices can bee issued prior to any assessments and demands have been contentions and subject to litigation at the TAT and the Courts. The change clarifies the issuing by expressly stating when an agency notice may be issued. This will protect taxpayers and potential agents from haphazard issuance of agency notices by KRA.

Further, the expansion of the time frame allows the agent more time to notify the Commissioner of their inability to comply with the notice. In addition , the requirement to serve the notice concurrently on the agent and the taxpayer will avert ambushing of the taxpayer and allow them enough time to seek recourse against the notice such as seeking injunctive orders against the Commissioner where the same is unprocedural or premature.

TAX PROCEDURES

Appointment of Value Added Tax withholding agent

The Issue

The Act has amended the provisions of the TPA on withholding VAT to exclude from the ambit of withholding VAT registered manufactures whose value of investment in the preceding three years from the commencement of the TPA is at least three (3) shillings.

Effective 1 July 2022

The Implications

Such manufactures are likely to incur material input VAT in relation to making their supplies. This amendment appears to be aimed at protecting the specified manufacturers from the cash flow challenges that may arise as a result of withholding VAT by their customers. This is more so in light of the deletion of the provision on exemption of suppliers from withholding VAT by the Finance Act 2021.

TAX PROCEDURES

New Rules To Govern The Application For Refund Of Overpaid Tax

The Issue

The Act has repealed Section 47 of the TPA and replaced it with a new Section, which provides that where a taxpayer has overpaid a tax under any tax law, including instalment taxes, the taxpayer may apply to the Commissioner to either offset the overpaid tax against future tax liabilities or refund the overpaid tax within 5 years, or 6 months (from the date of the overpayment)in the case of VAT. Further the new section provides as follows:

- ✓ The Commissioner must make a determination regarding the application for refund or set-off within ninety (90) days of receipt of the application failure to which the same shall be deemed to have been approved.
- ✓ Where the Commissioner approves a refund , the same must be paid within a period of two years from the date of the application, failure which, the same shall attract interest at the rate of 1% per month or part thereof for the period it remains outstanding.
- ✓ Any taxpayer aggrieved by the Commissioner's decision with respect to this section can appeal to the Tax Appeals Tribunal ("TAT") within thirty (30) days of the date of the decision (appealable decision). Under the old section 47, such decision were a tax decision subjection to an objection as opposed to an appeal.

Effective 1 July 2022

The Implications

The new section provides clarity and certainty around the issue of treatment of tax overpayments. Particularly it provides for clear timelines within which the Commissioner must act, grants the taxpayer an option to either offset the overpayments against subsequent tax liabilities or apply for refund of actual cash and provides for payment of interest to taxpayers in case of delays in processing refunds by the Commissioner.

It is hoped that the process will be straight forward and will encourage taxpayers to utilize such overpayments.

TAX PROCEDURES

New Rules to Govern the Application of Refund of Tax Paid in Error

The Issue

The Act has introduced new provision on the refund of tax paid in error and consequently deleted the provisions on refund of tax paid in error under the VAT Act 2013. The procedure on refunds of overpaid tax apply in regard to refund of tax paid in error including the taxpayer's choice between either a cash refund or set off against future liabilities. In addition, where a tax is paid in error as a result of failure to effect the exemption or zero-rating of a supply within the specified period due to circumstances beyond the taxpayer's control, the Commissioner may, upon the approval of the CS refund such taxes.

Effective 1 July 2022

The Implications

The change provides the legal for refund tax paid in error, which initially, for lack of express provisions (save for VAT paid in error), was handled under the repealed section 47. Further, the provision provides recourse for VAT registered taxpayers who pay VAT in error in cases where the KRA delays to effect exemption or zero rating of supplies on iTax in good time following changes in the law.

TAX PROCEDURES

Timelines Governing Decisions to be Issued by the Commissioner Relating to Objections

The Issue

The Act has amended the provisions if the TPA govern objections to tax decisions as follows:

- ✓ Where an objection has not been validly lodged, the Commissioner is required to notify a taxpayer about the invalidity of their objection within fourteen (14) days. Initially the notification was required to be made immediately ;
- ✓ The Commissioner is required to consider and issue a decision on an application for extension of time to file a notice of objection within 14 days. Initially there were no timelines for issuance of such decisions; and
- ✓ The Commissioner is required to issue an objection decision within sixty (60) days from the date of receiving a valid notice of objection from a taxpayer failure to which the objection will be deemed to have been allowed. The change implies that the Commissioner will be required to issue the decision within one cycle of 60 days Initially the sixty-day cycle would restart any time the Commissioner requested for additional information.

Effective 1 July 2022

The Implications

The provision of the fourteen-day timeline for notifying taxpayers whether an objection notice is valid and consideration of a request for extension of time is a welcome move as it provides for certainty in the objection process. The ambiguity occasioned by the use of subjective terms like "immediately" under the earlier provision led to confusion and disputes between KRA and taxpayers

Further, the process of issuance of objection decisions was marred with delay and uncertainty. Every request for information made by the Commissioner resulted into fresh cycle of sixty days for the Commissioner. The entire process involving further requests, review and issuance of the objection decision will now take one cycle of sixty days. While this move is meant to eliminate unnecessary delay, it is hoped that quality of decisions issued by the Commissioner will not be affected negatively due to time constraints.

MISCELLANEOUS FEES AND LEVIES

Various changes to the levies applicable

The Issue

The Act has introduced various changes as summarized as follows:

Item	Old treatment	New treatment
Inputs and raw materials used for manufacture of pharmaceutical products	IDF & RDL applicable	IDF & RDL exemption upon recommendation by the CS for Health
Iron ores and concentrates, including roasted iron pyrites	No export levy	Export levy at USD 175 per tonne
Raw hides and skins	Export levy 80% or USD 0.52 per Kg	Export levy 50% or USD 0.32 per Kg
Inflationary adjustment of export levies	1 July of every year	A date before 1 October of every year
Delay in refund of overpaid levies (unpaid 2 years after application for refund)	No payment of interest by the Commissioner	Interest to apply per the provisions of the TPA

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THANK YOU