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Tax Alert
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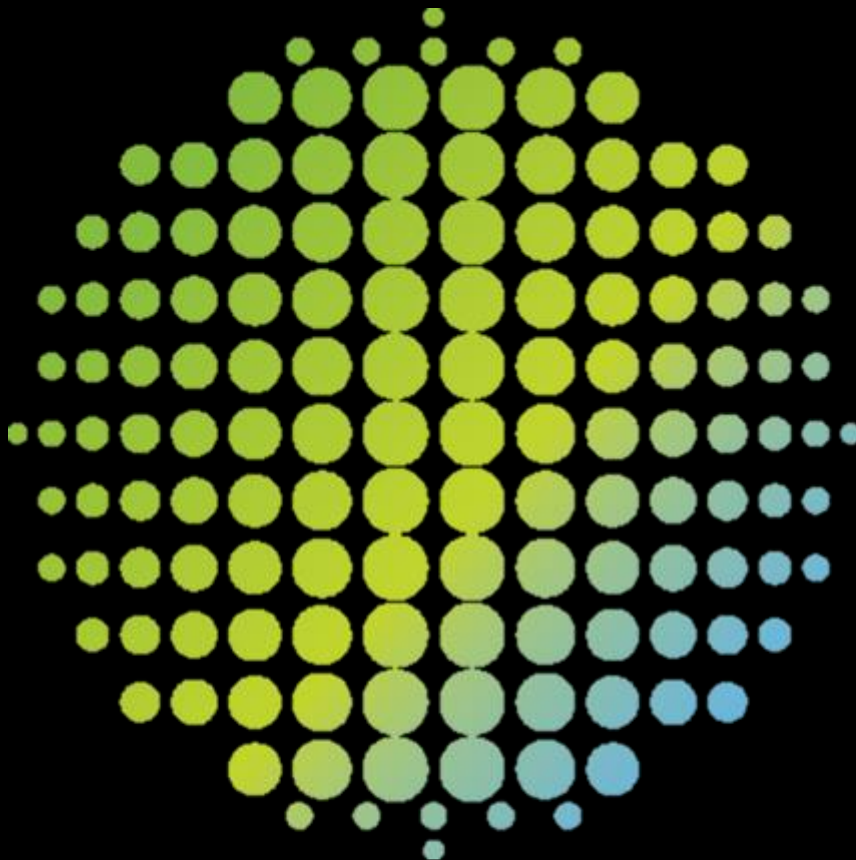

The Finance Act, 2021

Tracking the changes

The President signed the Finance Act, 2021 ("the Act") into law on 29 June 2021. The Act has introduced amendments to the various tax statutes in Kenya, the Capital Markets Act, the Insurance Act, the Retirement Benefits Act, 1997, and the Central Depositories Act.

The amendments introduced by the Act largely mirror those under the Bill. However, there are some notable changes in the Act that we wish to bring to your attention. You are advised to read this analysis together with our analysis of the Bill that we issued in May 2021. Please click here to read our analysis of the Finance Bill, 2021.

Income Tax Act Highlights

EBITDA-based interest limitation replaces the thin capitalization interest limitation

The Finance Act has repealed the thin capitalization interest limitation rule and replaced it with an EBITDA-based interest limitation rule.

The thin capitalization interest limitation prohibits a foreign controlled entity, except a bank, from claiming an interest deduction corresponding to the debt in excess of the debt-to-equity ratio of 3 to 1. For extractive sectors (mining and petroleum sectors), the prescribed debt-to-equity ratio is 2:1.

Under the EBITDA-based interest limitation rule, only interest up to 30% of the Earnings Before Interest, Depreciation and Amortization (EBITDA) will be allowed as a deduction. Any amount above 30% of EBITDA shall be disallowed.

Banks and financial institutions licensed under the Banking Act, and micro and small enterprises registered under the Micro and Small Enterprises Act, 2012 shall be excluded from the EBITDA-based interest limitation rule. Persons who do not fall within this category (including individuals, locally controlled entities, branches of foreign entities and entities that operative in the extractive sectors) shall be affected.

The introduction of the EBITDA-based interest limitation rule will likely discourage borrowing and punish early-stage capital intensive businesses that have significant finance costs to fund their investments and other entities that significantly rely on debt funding non-registered financial/ lending institutions. In the long run, this could adversely affect investment in the country, as investors may consider diverting their investments to other countries. There is need to revise the provisions to reduce the adverse impact of the interest limitation rule.

Effective date: 1 January 2022.

Removal of the tax loss carry-forward limitation

The Act has deleted the provision in Section 15(4) of the Income Tax Act that allowed taxpayers to only utilize tax losses in the year in which they arise and the subsequent 9 years, or such other longer period that may have been approved by the Minister. In its place, a new provision that allows taxpayers to utilize tax losses indefinitely has been introduced.

The removal of the tax carry-forward limitation may have been informed by the introduction of minimum tax, effective 1 January 2021. Minimum tax would still be expected to apply regardless of whether a person is in tax losses or not.

Effective date: 1 January 2022.

Definition of the term “control”

The Act has introduced an expanded definition of the term *“control”* in the Income Tax Act. A person would be deemed to control another person if:

- The person (not being an unrelated financial institution):
  - advances a loan to the other person and the loan constitutes 70% or more of the other person’s total assets’ book value; or
  - guarantees 70% or more of the total indebtedness of the other person;
- The person or assignee of the person:
  - supplies 90% or more of the other person’s purchases, or purchases 90% or more of the other person’s sales; and
  - the Commissioner upon assessment, deems influence in the price or other conditions relating to the other person’s purchases or sales, as the case may be;
- The person has authority and mandate to appoint more than half of the other person’s board of directors or at least one director or executive member of the governing board;
- The person is the owner or has the exclusive rights over intellectual property over which the other person wholly depends on for the manufacture or processing of goods or articles, or business;
- The person deals or relates with another in a way which the commissioner deems to constitute control; and
- In the case of a company, the person holds 20% or more of the voting rights the company. The threshold was previously 25%.

The introduction of the “control” definition corrects the inadvertent deletion of the term by The Tax Laws (Amendment) Act, 2020 in April 2020. However, the new definition is very broad and will significantly widen the scope of transfer pricing by extending the meaning of related entities. The definition will also impact the deductibility of foreign exchange losses on loans advanced to controlled persons. The exchange losses shall be deferred and not be allowed until the debt-to-equity ratio of such persons falls below 3 to 1.

Effective date: 1 July 2021.

New definition of “permanent establishment”

The Act has deleted the definition of permanent establishment (“PE”) in the Income Tax Act and replaced it with an expanded definition as follows:

- A fixed place of business through which business is wholly or partly carried on. This includes a place of management, a branch, an office, a factory, a workshop, a mine, an oil or gas well, a quarry or any other place of extraction or exploitation of natural resources, a warehouse in relation to a person whose business is providing storage facilities to others, a farm, plantation or other place where agricultural, forestry plantation or related activities are carried on and a sales outlet;
- A building site, construction, assembly or installation project or any supervisory activity connected to the site or project, but only if it continues for a period of more than 183 days;
- The provision of services, including consultancy services, by a person through employees or other personnel engaged for that purpose, but only where the services or connected business in Kenya, continue for a period of, or periods exceeding in the aggregate, 91 days in any 12-month period commencing or ending in the year of income concerned;
- An installation or structure used in the exploration for natural resources where the exploration activities continue for periods not less than 91 days;
- A dependent agent of a person who acts on their behalf in respect of any activities which that person undertakes in Kenya including habitually concluding contracts or playing the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the person.

The new definition captures the concept of a service PE in the domestic legislation and excludes activities of a preparatory or auxiliary character from being regarded as a PE.

The expanded definition aligns, to a large extent, the domestic legislation with international best practice, as captured in Article 5 of the UN and OECD Model Tax Conventions, which are widely used as the basis for negotiating tax treaties.

The introduction of the new PE definition is likely aimed at minimizing the opportunity for tax avoidance through strategies to circumvent the existence of a PE.

However, the Model Tax Conventions normally use a threshold of 12 months (OECD) or 6 months (UN) to determine the existence of a PE. The definition introduced by the Act has lower time thresholds of 91 days for services and exploration activities which increases the risk of PE for non-resident entities engaged in service provision or exploration activities in Kenya.

The introduction of the new PE definition is likely aimed at minimizing the opportunity for tax avoidance through strategies to circumvent the existence of a PE.

Effective date: 1 July 2021.

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Country-by-Country reporting by Kenyan headquartered MNEGs

The Act has introduced a Country-by-Country reporting (CbCR) requirement on any Kenyan headquartered multinational enterprise group (MNEG), referred to in the Act as an "ultimate parent entity" (UPE).

A UPE will be required to file a return of its financial activities in Kenya, where its gross turnover exceeds the prescribed threshold, and in all other jurisdictions where it has taxable presence.

The return will be due within 12 months of the MNEGs financial reporting period. It will contain the Group's aggregated information relating to the amount of revenue, the profit or loss before income tax, the income tax paid, the income tax accrued, stated capital, accumulated earnings, number of employees and tangible assets other than cash or cash equivalent regarding each jurisdiction that the MNEG operates.

The CbCR requirements will enable the Kenya Revenue Authority to have visibility of financial and related information that will aid in assessing the transfer pricing risk or any BEPS-related risk and make determinations on how to allocate tax audit resources. For the taxpayers who are part of a multinational group, this means additional transfer pricing reporting requirements.

There is need to set a threshold for reporting to avoid overburdening smaller entities.

Effective date: 1 January 2022

Minimum tax

The Act has amended the Income Tax Act and exempted the following persons from the minimum tax regime:

- Persons engaged in manufacturing and whose cumulative investment in the preceding four years from the date of assent is at least ten billion shillings;
- Persons licensed under the Special Economic Zones Act, 2015; and
- Persons engaged in distribution business and whose income is wholly based on a commission

The above is in addition to the persons that were added to the exemption list by the Tax Laws (Amendment) No. 2, Act, 2020. The persons include:

- Persons engaged in business whose retail price is controlled by the Government; and
- Persons engaged in insurance business

Although the exemption of more persons from the minimum tax regime is welcome, there is still more to be done for the regime to be friendlier. For instance, the 1% tax rate is on the higher side compared to the rates applicable in other jurisdictions and there is need to revise the provisions to only apply to entities reporting several years of consecutive losses (3-5). It would also be welcome if the government introduced a turnover threshold below which minimum tax should not apply.

Effective date: 1 July 2021.

Investment allowance at 100%

The Act has introduced an accelerated investment allowance at 100% in a given year where:

- The investment value outside Nairobi City County and Mombasa City County in the year is KES 250 million;
- The cumulative investment in the preceding 3 years outside Nairobi County and Mombasa County is at least KES 2 billion; or
- The investment is incurred in a Special Economic Zone.

This move is aimed at encouraging investment in Special Economic Zones and outside the two counties of Nairobi and Mombasa, which are relatively more developed compared to other counties. It is a welcome relief for qualifying investors.

Effective date: 1 January 2022.

Investment allowance on bulk storage facilities

The Act has amended the Income Tax Act to provide that Paragraph 24E of the repealed Second Schedule shall continue to apply until 31 December 2022.

The Paragraph, which was expected to apply until 31 December 2021, entitles a person to investment allowance at 150% if the person incurs capital expenditure of at least KES 5 billion on the construction of bulk storage and handling facilities of at least 100,000 MT storage capacity for supporting the Standard Gauge Railway operations..

We believe the intention of extending the application of the provision to 31 December 2022 is to accord persons who had taken advantage of the provision full benefit upon completion of their projects.

Effective date: 1 July 2021.

Basis of computing investment allowance

The Act has amended the basis of computing investment allowance from reducing balance to straight-line.

Computation of capital allowances on a straight-line basis is simple and reduces the period of recovery of capital costs.

Effective date: 1 January 2022.

Income from registered trusts

The Act has amended Section 11 of the Income Tax Act to restrict the application of subsection 3 (which deems any amount received by a beneficiary from a trustee to have already been taxed as per the Income Tax Act) in the case of a registered trust to the following:

- any amount that is paid out of the trust income on behalf of any beneficiary and is used exclusively for the purpose of education, medical treatment or early adulthood housing;
- income paid to any beneficiary which is collectively below ten million shillings in the year of income; and
- such other amount as the Commissioner may prescribe from time to time and at such rate as prescribed in paragraph 5 of the Third Schedule. To this effect, the Finance Act, 2021 has also introduced a rate of 25% in the Third Schedule.

The amendment introduced by the Finance Act will lead to taxation of income from registered trusts paid out to beneficiaries that do not fall under the categories outlined above.

Effective date: 1 July 2021.

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Income from settlement

The Act has amended the definition of "settlement" as used in Section 25 and 26 of the Income Tax Act, as discussed below.

- The amended definition under Section 25 excludes the "transfer of assets made through a family trust" in the definition of "settlement". Section 25 deems the income paid by a settler to, or for the benefit of his/ her child during the settler's life to be income of the settler. The section shall therefore not be expected to apply to the transfer of assets made through a family trust.
- The amended definition in Section 26 excludes a registered family trust from covenants that qualify as "settlement". Section 26 deems the income accrued to or received by a person under a settlement from assets remaining the property of the settlor, to be income of the settler. With the change introduced by the Finance Act 2021, income received under a family trust covenant shall not be covered by Section 26.

Deeming of income settled on children to be income of the settler means that tax on the income (if any) is borne by the settler and the child shall receive the income free of tax. We believe the changes to Section 25 and 26 of the Income Tax Act are aimed at encouraging persons to use family trusts for succession purposes.

Effective date: 1 July 2021.

Exemption of the income of a family trust and transfers of property to a family trust

The Act has introduced the following incomes into the Income Tax Act's exemption list:

- The income or principal sum of a registered family trust;
- Capital gains relating to the transfer of title of immovable property to a family trust; and
- Capital gains accruing to an individual on the transfer of property, including investment shares, for the purpose of transferring the title or the proceeds into a registered family trust;

The above changes are welcome as they will encourage use of family trusts for succession purposes.

Effective date: 1 July 2021.

Double taxation agreements

The Act has repealed the provisions of Section 41 of the Income Tax Act, which gives effect to double taxation agreements that the Government of Kenya has entered into with other countries.

The repealed provisions have been replaced by new provisions that largely mirror the repealed provisions. A key highlight of the new provisions is the presence of an express provision, which provides that any agreement that the government enters into shall be subject to the provisions of the Treaty Making and Ratification Act, 2012, (TMRA). The TMRA provides the procedure for the making and ratification of treaties and connected purposes. This amendment is, in our view, aimed at voiding any arrangement that has not complied with the provisions of the TMRA. This aligns with recent court ruling on, for instance, the Kenya-Mauritius DTA.

Effective date: 1 July 2021.

Tax rebate on graduate apprenticeships

The Act has amended Section 39B of the Income Tax Act and extended the tax rebate on graduate apprenticeships to technical and vocational graduates.

Employers who engage at least 10 university, or technical and vocational graduates for 6 to 12 months, under an apprenticeship contract, will be entitled to an additional deduction equivalent to 50% of the employment costs expended on the apprentices. Previously, only the cost incurred on university graduates was eligible for the rebate.

This amendment shows that the government is keen to create opportunities for not just university graduates, but also other institutions that train individuals to acquire skills for the job market. However, given the low uptake of the apprenticeship program since its introduction in 2016, the government should consider relaxing the strict requirements set out in the Income Tax (Set-Off Tax Rebate for Graduate Apprenticeships) Regulations, 2016 to improve the uptake.

Effective date: 1 January 2022.

Personal income tax changes

The Act has expanded the scope of insurance relief to also cover contributions made to the National Hospital Insurance Fund ("NHIF"). The relief is computed at 15% of the premiums paid, subject to a maximum of KES 60,000 per annum. This is expected to encourage voluntary NHIF contributions

Effective date: 1 January 2022.

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Digital service tax changes

The Act has introduced the following changes on digital service tax (DST):

- Expansion of the scope of application of digital service tax (DST) to capture any income from a business carried over the internet or an electronic network, including through a digital marketplace. Previously, digital service tax was only applicable on income accruing through a digital marketplace.
- Amendment of the definition of "digital marketplace" to cover any "online platform, which enables users to sell or provide services, goods or other property to other users".
- Exemption of resident persons from the DST regime. This is a positive move, as the imposition of DST on residents would have increased the backlog of refunds given that residents were entitled to an offset of the DST paid against their income tax liability. However, it is worth noting that non-residents operating in Kenya through PEs have not been excluded from the DST regime despite their income being taxed in Kenya through the self-assessment regime. We believe the PEs should be exempted for the same reasons that residents are.
- Aligning the due date for paying DST with the due date for filing the DST return. The law previously required DST to be paid at the point of paying the digital service provider. A person may therefore defer the payment of DST up to 20th of the following month.
- Exemption of income subject to withholding tax and that of a non-resident person who carries on the business of transmitting messages by cable or radio communication, optical fibre, television broadcasting, Very Small Aperture Terminal (VSAT), internet or any other similar method of communication, from the DST regime. It is noteworthy that this was already anchored in the Income Tax (DST) Regulations, 2020, but may have been introduced in the main legislation, perhaps to cure any contradictions.

Effective date: 1 July 2021.

Value Added Tax Highlights

VAT on imported services

The Finance Act, 2019 expanded the scope of persons subject to VAT on imported services to cover persons not registered for VAT. However, the changes did not conclusively amend the applicable sections of the VAT Act 2013.

The Finance Act 2021 has now introduced a raft of changes to Sections 2, 10 and 19 of the VAT Act 2013 to clean this up.

Effective date: 1 July 2021

VAT on supplies through digital marketplaces

The Act has been amended to clarify that supplies made over the internet or an electronic network through a digital marketplace are chargeable to VAT. In addition, the definition of "digital marketplace" under the VAT Act to mean *"online platform which enables users to sell or provide services, goods or other property to other users"*.

This change is aimed at widening the VAT net. The previous definition only envisaged a platform that enabled direct interaction between sellers and buyers of goods and services electronically. This definition may have been deemed restrictive, and hence the move to make the definition broader to capture more supplies. Players in the digital space, whose transactions may not have been previously covered based on the prior definition will therefore need to consider if they now fall within scope.

Effective date: 1 July 2021

Deductibility of input tax

The Act has amended Section 17(4) of the VAT Act to prohibit the deduction of input tax suffered on the hiring or leasing of passenger cars and minibuses. However, in line with existing provisions of the law, this prohibition applies to the extent that a registered person does not hire or lease such vehicles to exclusively deal in the business of selling, dealing in or hiring of such vehicles.

Businesses that may acquire, hire or lease passenger cars and minibuses should take note of this change and accordingly not deduct the attendant input tax.

Effective date: 1 July 2021.

Exemption of exported services

The Act has changed the status of export of taxable services from zero-rated to exempt. This move is aimed at reducing cases of VAT refund claims and is probably a reaction to the numerous disputes on the matter of VAT on export of services.

As a result of this change, affected businesses (those providing services for use/consumption outside Kenya) will have to absorb input tax as a business cost.

The move to exempt the export of taxable services offends the neutrality and destination principles of VAT. It negates international best practice. While the move may be driven by the desire to reduce cases of VAT refund, its impact on businesses engaged in cross border trade in services, including shared services, may be dire.

Effective date: 1 July 2021.

Ordinary bread to remain zero-rated

The Finance Bill 2021 had proposed to delete the supply of ordinary bread from the list of zero-rated items. As a result, it was argued that the deletion rendered ordinary bread taxable at 16%. However, it has been clarified that there was a drafting error and the exempt schedule still exempted ordinary bread from VAT.

The Act now deletes the supply of ordinary bread from the exemption schedule and retain the same under the zero-rated schedule.

This is a welcome move, as bread remains an essential dietary item. A move to either exempt or standard rate the product would have negatively impacted its affordability.

Transportation of goods from Kenya to another country to be zero-rated

The Act has introduced the transportation of goods originating from Kenya to a place outside Kenya into the zero-rating schedule.

This move may be geared towards ensuring the transport sector does not suffer the effects of changing the status of exported services, hence, keeping the sector at par with competitors from other countries in the East African region.

Effective date: 1 July 2021.

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Transportation of sugar-cane from milling firms to factories to be zero-rated

The Act has introduced the transportation of sugarcane from farms to milling factories into the zero-rating schedule.

This move may be seen as an effort to support the revival of the ailing sugar sector.

Effective date: 1 July 2021.

Zero-rating of maize flour, cassava flour and wheat or meslin flour

The Act has introduced the supply of maize (corn) flour, cassava flour, wheat or meslin flour and maize flour containing cassava flour by more than ten percent in weight into the zero-rating schedule/

This makes these essential products more affordable.

Effective date: 1 July 2021

Retention of veto power over regulations

The Finance Bill 2021 had proposed to delete the requirement to table VAT regulations before the National Assembly before they become effective. This would have accorded the Cabinet Secretary in charge of Treasury unchecked delegated legislative authority.

The Act has done away with this proposed change and, as such, VAT regulations made by the Cabinet Secretary in exercise of delegated law-making authority will remain subject to approval by the National Assembly.

Retention of group registration

The Finance Bill 2021 had proposed the repeal of the group registration provisions under Section 34(9) of the VAT law. This proposed repeal has however been deleted upon enactment of the Bill into law. In effect, group registration provisions will remain under the VAT Act 2013.

However, due to lack of regulations to support implementation of group VAT registration, this provision has not been applied in recent time. Perhaps it's the high time the Cabinet Secretary puts in place the applicable regulations.

Other VAT changes

The Act has retained the proposed changes in the Finance Bill 2021, which sought to introduce several items into the exemption schedule. A full listing of these items is as contained in our tax alert for the Finance Bill 2021.

The following additional items have been introduced into the exemption schedule, effective 1 July 2021:

- Taxable supplies including fish feeding and handling, water operations, cold storage, fish cages, pond construction and maintenance, and fish processing and handling, imported or purchased for direct and exclusive use on the recommendation of the relevant state department,
- Pre-fabricated biogas digesters,
- Biogas,
- Sustainable fuel briquettes for household and commercial use,
- The supply of denatured ethanol of tariff number 2207.20.00, and
- Tractors other than road tractors for semitrailers.

The Act has also retained the proposed clean up of tariff codes. Further details are contained in our Finance Bill 2021 tax alert.

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Excise Duty Act Highlights

Introduction of excise duty

The Act has introduced excise duty on various products as outlined below.

Product	Rate
Locally manufactured white chocolate, chocolate in blocs, slabs or bars of tariff code 1806.31.00,1806.32.00 and 1806.90.00.	KES 209.88 per kg
Jewellery of tariff heading 7113 & imported jewellery of tariff heading 7117	10%
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.	KES 1,200 per Kg
Articles of plastic of tariff heading 3923.30.00	10%
Imported pasta of tariff heading 1902 whether cooked or not, stuffed (with meat or other substances) or otherwise prepared such as spaghetti, macaroni, noodles, lasagna, gnocchi, ravioli, cannelloni, couscous, whether or not prepared	20%
Imported furniture of any kind used in offices, kitchen, bedroom and other furniture of tariff heading 9403	25%
Imported eggs of tariff heading 0407	25%
Imported onions of tariff heading 0703	25%
Imported potatoes, potato crisps & potato chips of tariff heading 0701	25%
Unsaturated polyester of tariff code 3907.91.00	10%
Alkyd of tariff code 3907.50.00	10%
Emulsion Vinyl Acetate Monomer (VAM) of tariff code 3905.91.00	10%
Emulsion-styrene acrylic of tariff code 3903.20.00	10%
Homopolymers of tariff code 3905.19.00	10%
Emulsion B.A.M of tariff code 3906.90.00	10%
Betting and Gaming	7.5% of the amount wagered or staked
Price competition	7.5% of the amount paid or charged to participate in the competition
Lottery (excluding charitable lotteries)	7.5% of the amount paid or charged to buy the lottery ticket.

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The introduction of excise duty on imported onions, potatoes and eggs is aimed at shielding local farmers of these products from competition arising from cheap imports. This measure is in line with similar import duty changes on agricultural products introduced through the East African Community Gazette of 30 June 2021 and is aimed at promoting growth of the agricultural sector and improve the livelihoods of most Kenyans in the rural areas who rely on farming as a primary source of income. However increased taxes on imports is not the answer if other challenges affecting the agricultural sector are not addressed and therefore this may only lead to increased cost of products for consumers without necessarily improving local production.

The Finance Bill had proposed to reintroduce excise duty on betting at 20%. However, the 20% excise rate was quite significant and would have potentially curtailed the operations of betting firms in the Kenyan market. In this regard, the Act has apportioned the 20% excise duty amongst other activities under the Betting Lotteries and Gaming Act (gaming, price competition and lottery) that are currently not subject to excise duty.

The introduction of excise duty on imported furniture is in line with the increase in the import duty on furniture and is aimed at promoting local manufacture of these products. However, given other factors that affect local production such as availability of raw materials and cost of production, it may not achieve the desired goal.

Effective date: 1 July 2021

Increase of excise duty rates

The Act has increased the excise duty on imported sugar confectionary of tariff heading 1704 from KES 20.99 per kg to KES 35 per kg. The Finance Bill 2021 had proposed to introduce excise duty on locally manufactured confectionery. However, the National Assembly did not approve this proposal, as it would go against the Government`s agenda of promoting local manufacturing. The increase of excise duty on imported sugar confectionery could be aimed at bridging the revenue that would have been expected from locally manufactured confectionery.

The Act has also increased duty on telephone and internet data services from 15% to 20%. This measure will likely increase the cost of communication via telephone and access to internet.

Effective date: 1 July 2021

Amendment of the definition of other fees charged by financial institutions

The Act has amended the definition of "other fees" in the Excise Duty Act (EDA) by deleting the words *"fees or commissions earned in respect of a loan".* The revised definition of *"other fees"* is as follows.

"*Other fees" means any fees, charges or commissions charged by financial institutions relating to their licensed activities but does not include interest on loan or return on loan or any share of profit or an insurance premium or premium based, or related commissions specified in the Insurance Act or regulations made thereunder."*

The intention of the amendment may be to bring loan related fees and commissions within the ambit of excise duty. However, it is likely that the measure will create ambiguity on the scope of interest that is exempted from excise duty since the term "interest" is not defined in the EDA.

Excise duty on loan related fees would have the impact of increasing the cost of accessing credit as the tax will likely be passed on to the consumers.

Effective date: 01 July 2021

Relief of excise duty on bulk internet data purchased for resale

The Act has amended Section 14 of the EDA to allow for offset of excise duty paid by licensed persons on purchase of bulk internet data against excise duty payable on resale of the internet data

This amendment will potentially reduce the cost of providing internet, as it will avoid double payment of excise duty on internet data.

Effective date: 1 July 2021

Removal of excise duty

The Act has removed the excise duty of 25% on imported glass bottles (excluding glass bottles for packaging pharmaceutical products) imported from the East African Community (EAC).

Glass bottles imported from countries outside the EAC will continue attracting excise duty at 25%.

Excise duty on imported glass bottles was introduced in March 2020 through the Business Laws (Amendment) Act, 2020. The removal of excise duty on bottles imported from the EAC partner states may be intended at removing the barriers to the EAC integration.

Effective date: 1 July 2021

Exemption from excise duty

The Act has introduced an excise duty exemption on illuminating kerosene supplies to licensed or registered manufacturers of paint, resin or shoe polish in such quantities as the Commissioner may approve. Section 29 (1)(b) of the EDA also provides for refund of excise duty paid on illuminating kerosene used for manufacture of unexcisable goods (including paint, resin and shoe polish).

This measure is in line with the manufacturing pillar of the Big 4 Agenda, as it is aimed at promoting local manufacturing by reducing the cost of manufacturing paint, resin and shoe polish.

The Act has also exempted excisable services supplied in Kenya by a mobile telecommunication service provider on the sale of a ring back tune to a subscriber. The cost of procuring ring back tunes, such as Safaricom's SKIZA tunes and Airtel's Hello Tunes, is likely to reduce based on this exemption.

Effective date: 1 July 2021

Ambiguity on excise duty applicable on some manufactured tobacco products

The Act has imposed excise duty on other manufactured tobacco and tobacco substitutes that have been homogenized and reconstituted tobacco, tobacco extracts and essences at KES 1,200 per kg. However, the First Schedule of the EDA separately provides for excise duty on similar products at the rate of KES 9,273.55 per kg.

This measure will create confusion amongst manufacturers and importers of tobacco products regarding the applicable rate of excise duty and will potentially result to tax disputes particularly where the KRA and manufacturers/importers take varying positions on the applicable rate.

Effective date: 1 July 2021

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Gazette notice on remission of excise duty to be tabled before the National Assembly

The Act has introduced a requirement, to table before the National Assembly, Gazette notices granting remission of excise duty on beer or wine made from sorghum, millet or cassava or any other agricultural products.

The Gazette notice shall be laid before the National Assembly without unreasonable delay and the National Assembly will be required to pass a resolution either approving or annulling the Gazette within 21 days after the Gazette is tabled. Where the Gazette notice is annulled, it shall become void but without prejudice to the validity of anything previously done thereunder, or to the issuing of a new notice.

This measure is in line with the scrutiny and operation process of other statutory instruments and will ensure public participation before approval of excise duty remissions.

Effective date: 1 July 2021

Definition of "possession"

The Act has defined "possession" to mean *having, owning or controlling any excisable goods including:*

a) having in one's possession any excisable goods;

b) knowingly having any excisable goods in the actual possession or custody of any other person;

c) having any excisable goods in any place, whether belonging to or occupied by oneself or not, for the use or benefit of oneself; or

d) having any excisable goods for the use or benefit of another person.

Provided that if there are two or more persons and any of them with the knowledge or consent of the others has any excisable goods in his custody or possession, such goods shall be deemed to be in the custody and possession of all of them.

Proposals that were not approved by the National Assembly

The following excise duty measures that were contained in the Finance Bill were not approved by the National Assembly:

1. The proposal to amend the rate of excise duty on motorcycles from KES 11,608.23 per unit to 15% of the excisable value;
2. Introduction of excise duty on locally manufactured sugar confectionery of tariff heading 1704 at KES 20.99 per Kg;
3. Removal of 25% excise duty on imported glass bottles, except glass bottles imported from the EAC;
4. Introduction of excise duty on betting at 20%. In its place, the Finance Act has reduced the rate to 7.5%, and introduced excise duty on gaming, price competition and lottery (excluding charitable lottery) at 7.5%; and
5. Introduction of excise duty at KES 5,000 per kg on 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 health matters and other manufactured tobacco and tobacco substitutes that have been homogenized and reconstituted tobacco, tobacco extracts and essences. In its place, the Act has reduced the excise duty rate to KES 1,200 per Kg.

Miscellaneous Fees and Levies Act Highlights

Removal of anti-adulteration levy on kerosene used by licensed paint, resin and shoe polish manufacturers

The Act has amended Section 8A of the Miscellaneous Fees and Levies Act (MFLA) to delete sub section (4) that doesn't seem to exist. The intention seems to have been to delete sub section 3 that provides for refund of adulteration levy paid on illuminating kerosene that has subsequently been used for manufacture of paint, resin or shoe polish by licensed or registered manufacturers.

The Act has, instead, removed adulteration levy on illuminating kerosene used for manufacture of paint, resin or shoe polish by licensed or registered manufacturers.

This is a welcome move that will relieve registered manufacturers of paint, resin and shoe polish from the administrative burden of applying for refund of adulteration levy.

Effective date: 1 July 2021

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Application for refunds based on Section 47 of Tax Procedures Act, 2015 (TPA).

The Act has amended the MFLA to allow taxpayers to apply for refund of overpaid fees and levies imposed under the MFLA based on Section 47 of the TPA. Specifically, Section 47 of the TPA will be relied upon for the purposes of:

a) Application for refunds, ascertainment and repayment of fees and levies overpaid or paid in error under the MFLA; and
b) The determination by the Commissioner of penalties and interests on fees that remain unpaid.

Prior to this amendment, the MFLA did not provide for refund of fees and levies covered under this Act. In practice, however, refunds for Import Declaration Fee (IDF) and Railway Development Levy (RDL) paid in error are processed as though they are import duty under Section 144 of the East African Community Customs Management Act (EACCMA).

This is a welcome move as it provides a legal basis for refund of fees and levies paid in error under the MFLA. The proposal will also allow importers to seek for refund for fees and levies paid in error over a period of 5 years as opposed to the 1-year period allowed for import duty under the EACCMA.

Effective date: 1 January 2022

Introduction of additional items in the IDF and RDL exemption schedules

The Act has reinstated IDL and RDL exemptions on goods, the exemption of which the CS may determine is in the public interest, or to promote investment the value of which is not be less than KES 5 billion.

This exemption had been deleted last year through the Finance Act 2020.

This measure will reduce the cost of qualifying projects, mostly Government projects. We note that the threshold of investments eligible for this exemption has been increased from KES 200 million to KES 5 million perhaps in a bid to limit the number of projects eligible for this exemption and to attract high value investments in Kenya.

Effective date: 1 July 2021

Amendments to the Tax Procedures Act, 2015

Implementation of the Common Reporting Standards regime in Kenya

The Act has amended the Tax Procedures Act, 2015 by inserting a new Section (Section 6B) that introduces the Common Reporting Standards (CRS) regime in Kenya to effect automatic exchange of financial accounting information on tax matters. The reporting is to be done by all financial institutions that are resident in Kenya, including Kenyan branches of non-resident financial institutions but excluding foreign branches of Kenyan financial institutions.

The Act requires the Cabinet Secretary to publish Regulations providing the due diligence procedures and record-keeping requirements, guide on how a reporting financial institution will identify reportable accounts, the date and the manner of filing the information or "nil" returns and any other relevant information.

The Act has provided for penalties and sanctions for any non-compliance.

The amendment demonstrates Kenya's effort in joining global tax transparent jurisdictions in relation to exchange of information on foreign accounts for tax purposes. It is in line with the current global drive to increase transparency for purposes of combatting tax evasion among other crimes. It is a noble move and one of the avenues for increasing compliance and tax revenue.

In the meantime, a Kenyan tax resident should take note of:

- Increased pressure internationally on verification of tax residency of account holders;
- Automatic exchange of information on accounts held in the participating countries thus such information will be accessible to KRA; and
- Need to review compliance on tax matters regarding income and assets held abroad. Where one did not take advantage of the tax amnesty that had been introduced in 2016, it may be prudent to consider the current amnesty that commenced in January 2021.

We will keep a close eye on the Regulations and provide further updates on the developments relating to its full implementation. Though the effective date of this provision is 1 July 2021, we do not think it will be practical to implement it prior to publication of the Regulations by the CS.

Effective date: 1 July 2021

Miscellaneous fees and levies to be governed by the Tax Procedures Act, 2015

In a move seen to enhance consistency and efficiency in administration of miscellaneous fee and levies, the Act has amended the TPA to include the Miscellaneous Fees and Levies Act 2016 ("MFLA") and any Regulations or other subsidiary legislation made under it within the definition of tax law.

Effective date: 1 July 2021

Grounds for abandonment of taxes by the Commissioner to be widened

In a move seen to enable the Commissioner exercise his discretion in abandoning tax if there is any reasonable justifiable basis, the Act has amended Section 37 of the Tax Procedures Act, 2015 to allow the Commissioner to refrain from assessing or recovering unpaid tax from a taxpayer if there is *"any other reason occasioning inability to recover the unpaid tax"* .

In addition, the Act has introduced a requirement for the Commissioner to submit biannual reports by 30th June and 31st December to the Cabinet Secretary containing details and amounts of taxes abandoned for purposes of enhancing accountability.

Effective date: 1 July 2021

Removal of the withholding VAT exemption for suppliers with perpetual credits

The Act has deleted the provision that allowed suppliers with perpetual VAT credits for at least 2 years to apply for exemption from withholding VAT.

Going forward, suppliers in perpetual credit arising from withholding VAT will only be expected to lodge an application for refund in accordance with the provisions of the VAT Act.

Effective date: 1 July 2021

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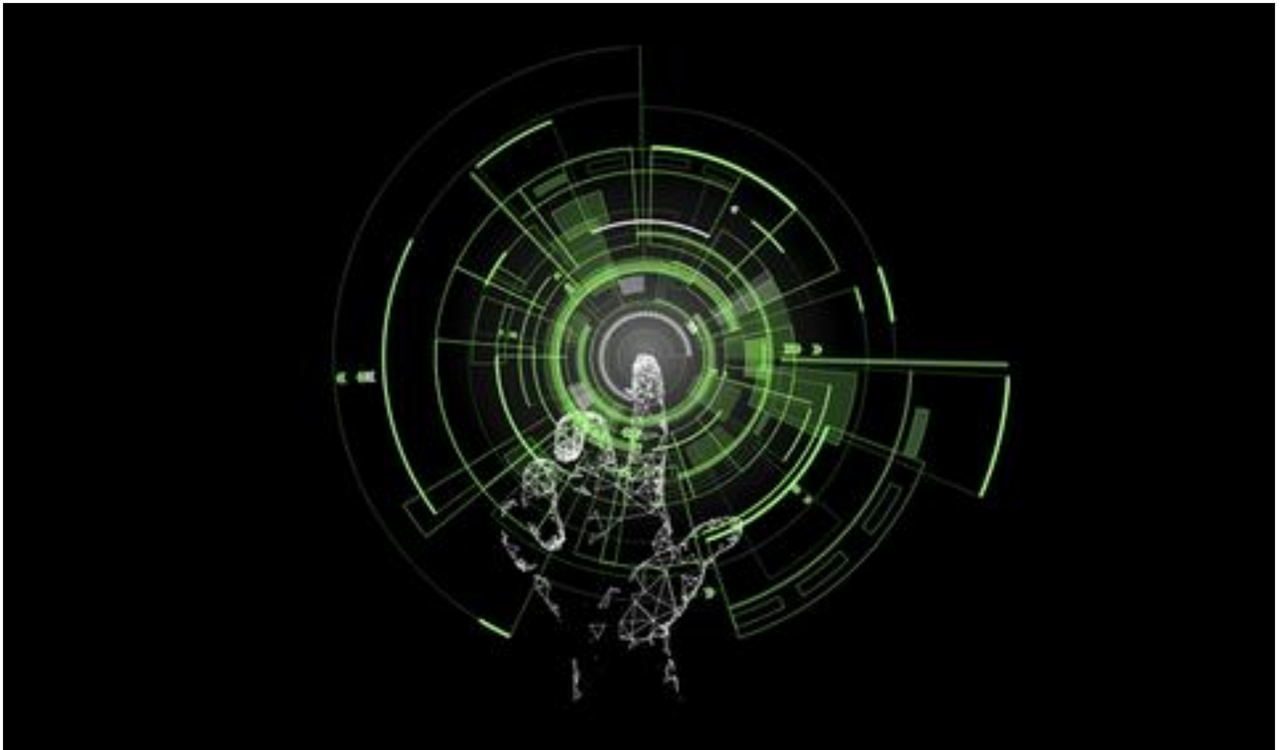

Accrual of penalties and interest in relation to offset of tax due against refund amount to stop accruing only after notification by the Commissioner

The Act has amended Section 47 of the Tax Procedures Act 2015 to provide that where a taxpayer has applied for refund of overpaid tax and the Commissioner applies the credit to offset against unpaid tax, penalties or interest shall stop to accrue on the amount applied to offset the outstanding tax from the date the taxpayer is notified that the application for refund has been ascertained.

We still hold the view that this is punitive, and the penalties and interest should stop accruing at the date when the tax refunded was paid to the KRA.

In what is seen to somewhat address the issue on offset of tax overpayment against tax due, the Act has further amended Section 47 of the Tax Procedures Act to provide that once the Commissioner notifies a taxpayer of a decision under application for refund of overpaid tax and the Commissioner is satisfied that there is an overpayment of tax, the overpayment is deemed to have been offset against the taxpayer's future liability.

This is a new addition to the Act since it was not covered in the Bill. That said, the new addition is likely to create more confusion, as it is subject to varying interpretations and may be used to deny taxpayers an opportunity to offset overpayments against taxes that are payable in current or past periods.

Effective date: 1 January 2022

DST collection and recovery measures

The Act has amended the Tax Procedures Act, 2015 to allow the Commissioner to seek the intervention of relevant authorities to enforce compliance with the provisions of taxes from persons who provide services over the internet or an electronic network including through a digital marketplace.

Enforcement of taxes may include restriction of access to the digital marketplace in Kenya. This amendment is likely to enable KRA to collaborate with other authorities especially on enforcement of the recently introduced Digital Service Tax (DST) and VAT on taxable services supplied through a digital marketplace.

Effective date: 1 July 2021

Digital service providers required to register for tax in Kenya

The Act has amended the First Schedule to the Tax Procedures Act, 2015 and imposed a requirement for persons carrying out business over the internet or an electronic network including through a digital marketplace to have a Personal Identification Number (PIN). This implies that all digital service providers who have income accrued in Kenya, including non-residents will have to be registered for tax in Kenya.

Effective date: 1 July 2021

Proposals in the Bill but dropped under the Act

The Bill had proposed to increase the statute of limitation from 5 years to 7 years. Effectively this would have increased the period required for maintaining tax records, amending the returns and assessments by the Kenya Revenue Authority (KRA). The proposal was rejected in its entirety. This is a welcome move.

The Bill had also proposed that criminal and civil proceedings on the same tax dispute can run concurrently and that none shall act as a ground for stay, prohibition or delay of the other. This proposal was rejected.

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Other changes

In addition to the amendments to the tax statutes, the Act has also introduced the following amendments with effect from 1 July 2021:

- Amendment of the Capital Markets Act to allow the Capital Markets Authority tribunal to hear and determine appeals within 90 days from the date of filing of appeals;
- Amendment of the Insurance Act to bring foreign brokers that carry out business in Kenya within the regulation of the Insurance Act. In addition, the Act introduced the concept of closed fund business in the Insurance Act;
- Amendment of the Retirement Benefits Act (RBA Act) to introduce a requirement for corporate trustees to be registered and regulated under the RBA Act. Previously, the Act only envisaged individual trustees as trustees of scheme funds; and
- Amendment of the Kenya Revenue Authority Act to increase the reward payable to people who provide intelligence leading to the identification or recovery of unassessed taxes or duties.
    - A person who supplies information leading to the identification of unassessed duties or taxes will stand to receive KES 500,000, an increase from the current KES 100,000.
    - On the other hand, an informant who provides information leading to the recovery of unassessed duties or taxes stands to gain KES 5 million up from KES 2 million.

New changes that were not in the Finance Bill

The Act has amended the RBA Act to allow Trustees to appoint the KRA as an agent to collect unremitted contributions from employers. Where an employer fails to comply with KRA's pension contribution request, the KRA has the power to issue agency notices through the Bank of the employer and attach the bank account of the defaulting employer. The cost of the recovery of unremitted contributions shall be borne by the defaulting employer; and

The Act has also amended the Stamp Duty Act to exempt from Stamp Duty voluntary disposition of gifts among living persons if such a transfer is through a registered family trust. Further, registered family trusts have also been exempted from payment Stamp Duty.

The Act has amended the RBA Act to allow Trustees to appoint the KRA as an agent to collect unremitted contributions from employers.

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