



## THE FINANCE ACT 2020 ANALYSIS

## A. INTRODUCTION

On the 30<sup>th</sup> of June 2020, the President assented the Finance Bill 2020 thereby making it a law. Contrary to previous presentations, this year's Finance Bill came to the public domain prior to the budget reading as has always been the norm.

The Finance Act herein referred to as the Act has several amendments targeted at cushioning Kenyans from the adverse effects of the Covid-19 pandemic whilst outlining mechanism to ensure continued revenue collection.

We have analyzed the Act and its impact on business going forward and presented our reasonings as laid out in this analysis as follows:

## B. INCOME TAX

### Taxation of Residential Rental Income

The Act has changed the threshold for residential rental income tax regime. Previously the threshold stood at Kes 144,000 to Kes 10M per annum. The Act has changed the threshold to Kes 288,000 to Kes 15M per annum. The tax rate still remains at 10% of the gross rental income earned by landlords payable and accountable on a monthly basis.

The changes adopted widen the scope by bringing in landlords earning a higher rental income than previously allowed. The landlords who do not fall within the new thresholds will still have to account for the tax under the corporation tax regime at the reduced corporation tax rate of 25% for residents and 37.5% for non-residents.

**Effective date: 1<sup>st</sup> January 2021**

### Minimum Tax

The Act has brought forth a new tax to be known as minimum tax which shall be payable by a person if the person's:

- a) Income is not exempt under the ITA;
- b) income is not from employment, residential rent, capital gains, mining or oil exploration, capital gains or subject to turnover tax; or

- c) Minimum tax payable is lower than the instalment tax payable.

It was expected by the general public that this proposal would not make it to the final Act. However following its implementation the tax will be charged at a rate of 1% of gross income and paid on the 20<sup>th</sup> day of the fourth, sixth, ninth and twelfth months.

Further if the installment tax is higher than the minimum tax then the installment tax shall be paid and vice versa. This will essentially ensure that the tax base is widened hence more revenues.

The aim of the tax was to ensure that all companies pay tax regardless of whether they make a taxable profit or loss. In some countries the tax is also applied as an anti-tax avoidance measure in the event that a company is making artificial losses to prevent paying taxes.

The tax has been implemented in various jurisdictions such as Nigeria, India and Canada and closer home Tanzania. In Tanzania and Nigeria the tax rate is lower at 0.05% of the gross turnover and is applied in the event a company has made tax losses for two plus years consecutively and exemptions applying to specific industries such as agricultural, health, education and exploration activities.

**Effective date: 1<sup>st</sup> January 2021**

### Digital Services Tax

Following the introduction of digital service tax (DST) in 2019, various questions were raised as to how the tax would be implemented. The Act clarified this by introducing various measures namely;

- a) The tax would be charged at 1.5% of the gross value of the transaction and will be deducted upon payment; and
- b) The tax will be treated as an advance tax and can be deducted from the tax owed on the same by a resident or non-resident with a permanent establishment.

These changes provide some clarity on how the tax will be implemented and is set to affect persons transacting over a digital market place.

**Effective date: 1<sup>st</sup> January 2021**

**Income of Home Ownership Savings Plans (HOSPs) to be taxed**

A Home Ownership Savings Plan (HOSP) is a savings plan established by an approved institution and registered with the Commissioner of Domestic Taxes for receiving and holding funds in trust for depositors.

A HOSP aims to benefit first-time home owners by allowing the depositors to deduct the contributions made to a registered HOSP from their tax computations for a maximum of 10 years.

The Act has repealed the provisions in the Income Tax Act relating to HOSP which will effectively mean that there will be no tax deduction allowed in respect to contributions made to a registered HOSP.

The aim of deleting it is that the scheme had not achieved its intended purpose or uptake.

**Effective date: 1<sup>st</sup> January 2021**

**Deductible Expenses**

The Act has deleted the following tax allowable expenses:

- a) entrance fees or annual subscriptions paid to a trade association (in that year of income) which has made an election to be deemed to carry on a business charged to tax;
- b) expenses on legal costs and other expenses incurred on issue of shares for purchase by the general public;
- c) expenses incurred on legal costs and other expenses in listing on the Nairobi Stock Exchange;
- d) club subscriptions paid by an employer on behalf of an employee; and
- e) Expenses incurred on the construction of a public school, hospital, road or a similar kind of social structure.

**Changes in VAT status of goods and services**

The aim of these changes was to reduce the allowability of certain expenses that were not wholly and exclusively incurred in generating income.

**Employment income paid as bonus, overtime and retirement benefits**

The following income were treated as exempt where the employment income before adding these amounts fell below the lowest tax band. This benefit has been removed and thus the income will be taxable.

**Effective date: 30<sup>th</sup> June 2020**

**C. VALUE ADDED TAX**

**Value Added Tax Auto Assessments**

The Act has introduced new requirements to the procedure of claiming input VAT which include;

- a) A taxpayer will not be allowed input VAT deduction where the registered supplier has not declared the respective sales in their VAT return; and
- b) Input VAT can't be allowed where the taxpayer does not hold documentation supporting the input VAT.

Further the input VAT shall be allowable for deduction within six months of the supply. This puts the burden of verification of filing of VAT on the buyer who has to ensure that the seller has filed for their input to be valid.

This however is unfair given the input was validly incurred and it should not be the buyer's responsibility to ensure that the seller declares their outputs.

**Effective date: 30<sup>th</sup> June 2020**

Item	Previous status	Current Status
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Ambulance services	Standard rated	Exempt
P111.Maize (corn) seed if Tariff no 1005.10.00	Standard rated	Exempt
LPG (zero rated for a period of 12 months)	Zero rated	Standard rated
Inputs for electric accumulators and separators used to manufacture automotive and solar batteries in Kenya	Zero rated	Standard rated
Hiring and leasing of helicopters	Exempt	Standard rated
Inputs or raw materials for electric accumulators and separators including lead battery separator rolls whether or not rectangular or square supplied to manufacturers of automotive and solar batteries in Kenya	Zero rated	Standard rated
<ul style="list-style-type: none"> <li>•8802.11.00 &amp; 8802.12.00: Helicopters an unladen weight not exceeding and exceeding 2,000 kg respectively;*</li> <li>•8802.20.00 Airplanes and other aircraft, of an unladen weight not exceeding 2,000 kg.*</li> <li>•8803.30.00 Other parts of airplanes and helicopters</li> <li>•8805.21.00. Air combat simulators and parts thereof.*</li> <li>•8805.10.00 Aircraft launching gear or similar gear and parts thereof.*</li> <li>•8805.29.00 Other ground flying trainers and parts thereof.*</li> <li>•8309.90.90 Aluminum pilfers proof caps with EPE liner.</li> </ul>	Exempt	Standard rated
P47. Tractors other than other than road tractors for semitrailers*	Exempt	Standard rated
P45. Specialized equipment for the development and generation of solar and wind energy, including deep cycle batteries which use or store solar power.	Exempt	Standard rated
P50. Goods of tariff no 4011.30.00-Pneumatic tires	Exempt	Standard rated
P65.Taxable goods imported or locally purchased for manufacture of clean cook stoves	Exempt	Standard rated
P67. Stoves, ranges, grates cookers and similar appliances	Exempt	Standard rated
P104.One personal motor vehicle imported by a public officer or his spouse as provided for in the VAT Act	Exempt	Standard rated
P108.The supply of maize corn flour, cassava flour, wheat flour or meslin flour by more than 10% in weight for a period.*	Exempt	Zero rated for a period of 6 months after the assent.

The various amendments have been made to effect various changes as follows;

- a) To introduce relief for key essential services as is the case of ambulance services;
- b) To give relief by making these items affordable to the taxpayer as is the case for various flour items;
- c) To tax non-essential items as is the case with hiring and leasing helicopters. Although where such are used to provide relief services such as disaster

rescue or medical lift services then they would not be deemed as luxury hence the tax would not be fit.

- d) To align treatment of items with similar items as is the case of maize seeds.
- e) To raise tax revenues by making these items taxable as is the case of LPG gas supply, clean cook stoves and materials used to manufacture solar power batteries. However this makes these items more expensive where as they are key commodities for tax payers. Further

in the case of LPG gas it is also interesting that the government has will tax LPG at 14% while other petroleum products are taxed at the lower rate of 8%.

**Effective: 30<sup>th</sup> June 2020**

**Effective: \* 1<sup>st</sup> July 2021**

### **Special Operating Frameworks**

Goods imported or locally purchased for use in projects under the special operating frameworks which were previously exempt are now taxable. The Act introduced provisions stating that projects that had already been granted these exemptions will be able to apply the exemptions for the duration of the Special Operating Framework arrangement.

**Effective: 30<sup>th</sup> June 2020**

## **D. EXCISE DUTY ACT**

### **A. Expansion of the definition of License**

The Act expands the definition of the term “**licence**” to include the licence required to carry out activities in Kenya as gazetted by the Commissioner and requiring an excise license. This aligns the definition to the provisions on licensing as provided for in the Excise duty Act.

**Effective: 30<sup>th</sup> June 2020**

### **B. Adjustment of Inflation**

The Act now requires the Commissioner to seek approval from the Cabinet Secretary before issuing the Gazette Notice adjusting the specific rate of excise duty. Such notice shall be laid before the National Assembly within 7 days from the date of publication. Thereafter, the National Assembly shall within 28 sitting days of receipt of the notice, consider it and make a resolution either accepting or rejecting it. Where the said notice is disapproved, the same shall cease to have effect.

Previously, such adjustment of the specific rates was done unilaterally by the Commissioner by issuing a notice published in the Gazette.

**Effective: 30<sup>th</sup> June 2020**

### **C. Reduction of alcohol strength on Alcoholic Drinks**

The Act reduces the percentage of the alcohol strength on alcoholic drinks from 10% to 6% as follows: -

- Beer, Cider, Perry, Mead, Opaque beer and mixtures of fermented beverages with non-alcoholic beverages and spirituous beverages of alcoholic strength **not** exceeding 6%
- Spirits of undenatured ethyl alcohol; spirits liqueurs and other spirituous beverages of alcoholic strength exceeding 6%

The implication of this is to re-align the taxation of items in the sector by redefining the items subject to tax by lowering qualifying items to those with an alcohol percentage not exceeding 6%.

### **D. Removal of Excise Duty on betting**

The Act deletes Paragraph 5 of Part II of the First Schedule which previously imposed Excise duty on betting at the rate of 20% of the amount wagered or staked. The implication of this is that excise duty is no longer chargeable on betting.

The introduction of the said amendment is largely been influenced by the negative effect that the introduction of the said tax had on the betting industries for which majority of them opted to leave the Kenyan market. However, with the Covid-19 pandemic and the need for the government to generate more revenues, the move to remove the imposition of excise duty on betting is moves to ensure that more betting firms invest in the Kenyan market hence more revenues for the government.

**Effective: 30<sup>th</sup> June 2020.**

## E. TAX PROCEDURES ACT

### Voluntary Tax Disclosure Programme

The Act introduces a voluntary tax disclosure programme for a period of 3 years with effect from the 1<sup>st</sup> January, 2021. It is a programme where a taxpayer discloses his tax liabilities to the Commissioner for the purpose of being granted a relief on the penalties and interest for the tax obligations disclosed. Persons who wish to take advantage of this programme may apply to the Commissioner for relief in respect to tax liabilities that accrued within a period of 5 years prior July 1, 2020, that is, until June 2015.

A taxpayer who volunteers under this programme shall not be prosecuted with respect to the tax liability disclosed. Further, he shall be granted a remission of the interest and penalty due on the tax liability as follows: -

Period of Disclosure	% Remission
1 <sup>st</sup> Year	100%
2 <sup>nd</sup> Year	50%
Final Year	25%

An application shall be voluntary and the taxpayer will be required to disclose all material facts regarding the taxes payable.

Upon fulfillment of all the requirements, the Commissioner shall grant the relief, provided the relief shall not result in the payment of a refund to the taxpayer.

Once the relief is granted, the Commissioner shall enter into an agreement with the taxpayer setting out the terms of payment of the tax liability and the period within which the payment shall be made. This period shall not exceed 1 year from the date of the agreement.

Where a taxpayer fails to meet the terms agreed, the taxpayer shall be liable to pay the full penalties and interest that had been remitted under the agreement.

Once a taxpayer has been granted the relief, he shall not seek any other remedy including the

right to appeal with respect to the taxes, penalties and interest remitted by the Commissioner.

In instances where there is a discovery that full disclosure was not made to the Commissioner, then, there will be a withdrawal of any relief granted; assess and collection of any balance of the tax liability and commencement of prosecution of the Taxpayer. However, a Taxpayer can appeal against the decision of the Commissioner.

The application to the voluntary programme shall not be applicable where a Taxpayer is under audit, litigation, investigation or has been notified of a pending audit as relate to the tax liability the subject matter.

The introduction of voluntary tax disclosure programme is meant to boost tax compliance at a time when the taxman is struggling to hit revenue targets

With many businesses struggling due to the current pandemic engaging in court disputes may not yield favorable results. Therefore, the voluntary disclosure comes in handy to boost compliance. It will be worth following on how the taxpayers will respond to the introduction of this programme.

**Effective: 1<sup>st</sup> January 2021**

### Appointment of Digital Service Tax Agent

The Act introduces the appointment of a Digital Service Tax Agent by the Commissioner for the purpose of collection and remittance of digital service tax. These appointments are in furtherance of the introduction of the digital service tax.

Moreover, the Commissioner will have the powers of revoking the appointment. Of note is that the Act does not provide the circumstances upon which the Commissioner may revoke the appointment, which leaves the Commissioner with so much discretionary powers hence prone to abuse.

**Effective: 1<sup>st</sup> January 2021**

## **F. TAX APPEALS TRIBUNAL ACT**

### **Documentation used in Appeal at TAT level**

The Act limits the grounds relied upon by an Appellant to the appeal and the **documents** to which the decision relates. The implication of this is that an Appellant cannot rely on new documents but only those filed with the Commissioner and relating to the Commissioner's decision.

The implication of this is that the Appellant can't therefore introduce new documentation at the Tribunal stage and has to fully rely on what the Commissioner reviewed before making the Objection decision.

**Effective: 30<sup>th</sup> June 2020**

## **G. MISCELLANEOUS FEES AND LEVIES ACT**

### **Import Declaration Fee on goods imported under duty remission scheme**

The Finance Act introduces a change on Import Declaration Fee (IDF) for goods imported under the East African Community Duty Remission Scheme from the current flat rate of Ksh.10,000 to an ad-valorem rate of 1.5% of the Customs value.

The implication of the change is to harmonize the treatment of manufacturers under duty remission scheme with manufacturers not in the scheme who pay IDF on an ad-valorem basis.

**Effective: 30<sup>th</sup> June 2020**

### **Duty on goods from EPZ imported for Home use.**

The Act has introduced an additional duty at a rate of 2.5% of the customs value payable in respect of goods entered for home use from an export processing zones (EPZ) enterprises.

This is a move seen to foster the primary objective of the EPZ model i.e. export of

commodities outside the EAC region while discouraging local consumption of the same. The increase of the duty will have far reaching implications on the cost of goods purchased from an EPZ and a decline on demand on goods manufactured from EPZs.

**Effective: 30<sup>th</sup> June 2020**

### **Exemption from Import Declaration Fees**

The Act has removed exemptions from IDF on the following items;

- a) IDF in respect on aircrafts and substituting it with aircrafts excluding aircraft of unladen weight not exceeding 2,000kg and helicopters;\*
- b) Goods the CS may determine to be in public interest or to promote investment whose value shall not be less than 200M; and
- c) Goods imported and to be used in Special Operating Framework arrangements.

These items shall now be subject to IDF.

The Act further introduces an exemption of IDF on equipment, motor vehicles and machinery to be used by the KDF and National Police Service.

**Effective: 30<sup>th</sup> June 2020**

**Effective: \*- 1st July 2021**

### **Exemption from Railway Development Levy**

The Act has removed exemptions from RDL on importation of goods the CS may determine to be in public interest or to promote investment whose value shall not be less than 200M.

The Act further introduces an exemption of RDL on;

- a) Equipment, motor vehicles and machinery to be used by the KDF and National Police Service; and
- b) Currency notes and coins imported by the CBK.

The changes made are either to eliminate exemptions eroding the tax base or introduce exemptions for essential items

**Effective: 30<sup>th</sup> June 2020**

## **H. MISCELLANEOUS**

All changes to Miscellaneous Section **shall be effective as at 30<sup>th</sup> June 2020**. We review the various changes below;

### **i. Public Road Toll Act CAP 407 of the Laws of Kenya**

#### **Expansion of the definition of Toll Collector**

The definition of the toll collector has been expanded to include private and public entities. In essence, this means that the same is no longer restricted to public entities that the Cabinet Secretary or road authority may also appoint private entities to collect tolls. This move is meant to lure the private sector to partner with the government towards provision of Infrastructure.

#### **Removal of requirement for National Assembly Approval of Agreements**

Further, the Act has removed the requirement to have an agreement entered into by the CS or road authority to get the approval of the National Assembly. This is a welcome move as it will fasten the process of concluding Agreements as entered into by the government.

#### **Levying of Tolls**

The Act has amended the levying of tolls pursuant to an agreement such that the levying is no longer limited to the levying on erected tolling stations. With the amendment, the agreement may include other alternative arrangements for the levying, collection and administration of tolls and management of toll infrastructure. Moreover, the CS may prescribe the base toll rate in the agreement and permit the person to adjust, vary or otherwise revise the toll in accordance with an adjustment mechanism provided in the agreement. Such a person will also be allowed to collect the unpaid tolls from defaulters as a civil debt recoverable summarily.

### **Establishment of the National Roads Toll Fund**

The Act has established the National Roads Toll Fund where all tolls collected shall be remitted to. The fund shall be administered in accordance with the Public Finance Management Act.

These changes pave way for the establishment of toll roads regime in Kenya, more so under Public Private Partnership investment schemes which the government is encouraging.

### **ii. Capital Markets Act ,485A Laws of Kenya**

#### **Regulation of Private Equity and Venture capital companies**

The Act has expanded the functions and scope of the Capital Markets Authority (CMA) to include the licensing, approval and regulation of private equity and venture capital companies that have access to public funds. Currently, the CMA does not have regulatory oversight over private equity and venture capital companies. This move will enable Retirement Benefits Investment Schemes to invest in such companies.

#### **Unclaimed Dividends**

The Act has excluded the payment to beneficiaries from collected unclaimed dividends, as a function of the Investor Compensation Fund. This function is currently administered by the Unclaimed Financial Assets Authority which is responsible for tracing beneficiaries of unclaimed assets.

### **iii. Insurance Act, Cap. 487 Laws of Kenya**

#### **Time Limit for Filing Appeal to the Insurance Tribunal**

The Act has set the time limit for filing an appeal as against the decision of the Commissioner of Insurance to the Insurance Tribunal to be within 30 days of issuance of the decision. Currently, there is no specified time limit within which an appeal can be filed to the Tribunal. This is to ensure appeals are lodged on time and parties are not prejudiced.

### **iv. Standards Act, CAP 496 Laws of Kenya**



### **Change in definition of Consolidation**

The Act has introduced a new definition for the term “consolidator” to mean a firm that is licensed to consolidate goods belonging to different consignees at the country of export, which shall be under one Master Bill of Lading or Master Airway Bill, and breaks the consignment into smaller consignments at the port of destination for the different consignees for the purpose of individual customs declaration. With this proposed definition, consolidators will now be required to possess a license. Moreover, consolidator will be required to break consignment into smaller parts for custom declaration and payments hence curbing revenue leakages.

### **v. Road Maintenance Levy Fund Act, No. 9 of 1993**

#### **Removal of remittance of Transit Tolls**

The Act has removed the remittance of transit tolls to the Road Maintenance levy Fund. This is in line with the amendments to the Public Roads Toll Act where a Fund has been established for the remittance of the said tolls.

This measure will ensure that there is a separate Fund tasked with collection of transit toll levies only.

### **vi. Kenya Revenue Authority Act, No. 2 of 1995**

#### **Establishment of an institution on Capacity Building and Training**

The Act has established an institution for the provision of capacity building and training for the better carrying out of Authority’s functions. The Act has mandated the Board of Directors of KRA to make regulations in respect to the training and capacity building.

#### **Commissions to constitute funds of the Authority**

The Act has broadened the scope of what constitutes the funds of the Authority to include any commission received by the Authority for collecting any revenue on behalf of a county government or government agency. Such commission has been capped at 2% of the total

revenue collected on behalf of the county government or government agency.

#### **Limitation of Action against the Authority**

The Act has introduced a limitation of action provision as against the Authority as follows: -

- a) It is commenced within 12 months after the act, neglect or default complained of;
- b) In the case of continuing injury or damage, within 6 months after the cessation of the act; and
- c) At least 1 month written notice is issued specifying the particulars of the claim and intention to commence the action or legal proceeding. This provision is meant to prevent random institution of suits as against KRA and also to ensure that KRA effectively prepares for the same.

### **vii. Retirement Benefits Act, No. 3 of 1997**

#### **Penalty for failure to remit Actuarial Evaluation Report**

The Retirement Benefits Authority Act provides for Submission of actuarial evaluation reports by retirement benefit schemes within the specified timelines but does not provide for any penalties on non-compliance.

The Finance Act 2020 has imposed penalties of Kshs. 100,000 and a further Kshs1,000 per day on continuing default by the schemes in failure on trustees who fails to submit the actuarial evaluation report within the specified timelines. The move will ensure compliance by RB schemes and also assist the Retirement Benefit Authority in making informed decisions on the funding on the scheme.

### **viii. Insolvency Act, No. 18 of 2015**

#### **Ranking of claims in case of liquidation**

The Act has included amounts held on behalf of Kenya Revenue Authority by an appointed agent under the Banking Act as falling under the

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Second priority claims where such Bank falls under liquidation or receivership.

This amendment will ensure that the monies held on behalf of KRA by a Bank as an agent are treated as a debt owing to KRA hence prioritized and remitted to KRA regardless of the Bank being liquidated.

### **Let's talk**

For further information on how the tax provisions will affect your business or assistance on any other matter kindly contact your regular Taxwise Africa Analyst or the contacts below.



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