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FINANCE BILL, 2018

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CONTENTS

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The Finance Bill, 2018 has been published and in this alert, we set out some of the key legislative amendments proposed.

1. Income Tax Act ('ITA')

(a) Special Operating Framework Arrangements

A company that conducts business with the Government under a Special Operating Framework Arrangement (an 'Arrangement') will be subject to tax to the extent provided under the Arrangement.

Finance Bill, 2018 has also introduced amendments that will see firms operating under such Arrangements benefit from the following:

- VAT Exemption on goods and services imported or purchased locally for use in their projects;
- Excise Duty Exemption on goods purchased locally or imported for use in the projects;
- Exemption of Import Declaration fees and Railway Development Levy on imported goods used in the projects;

These amendment introduce significant tax incentives for companies to do business with the Government. Whilst this will give the Government greater flexibility in carrying out projects, there is uncertainty arising from the fact that none of the affected tax legislation defines what a 'Special Operating Framework Arrangement'. There is therefore need for greater clarity before the changes take effect.

Effective dates:	**1 January 2019**	Para. 2 of the Third Schedule to the ITA
	1 July 2018	First Schedule to the VAT Act, 2013
		Second Schedule to the Excise Duty Act, 2015
	1 October 2018	Second Schedule to the Miscellaneous Fees & Levies Act, 2016

1. Income Tax Act ('ITA') (continued)

(b) 20% Withholding Tax on Demurrage

Demurrage charges paid to non-resident ship operators will be subject to Withholding Tax at the rate of 20%. This move will increase the cost of importing goods into Kenya.

Ensuring compliance with this obligation by every single consignee of goods into Kenya is bound to be an onerous task given the sheer numbers involved.

Effective date:	**1 July 2018**	S. 2, 10, 35, Para. 3 of the Third Schedule to the ITA

(c) 5% Withholding Tax on insurance premiums paid to non-residents

Insurance premiums paid to non-resident insurers will be subject to 5% Withholding Tax. Premiums paid for the insurance of aircraft have however been excluded.
This will increase the cost of obtaining insurance from offshore providers as this tax is likely to be borne by the insured.

Effective date:	**1 July 2018**	S. 10, 35, Para. 3 of the Third Schedule to the ITA

(d) Deemed dividend distributions

The scope of deemed dividend distributions has been amended to cover the following situations:

- the distribution of cash or assets to a shareholder or a person related to the shareholder;
- discharge of any obligation or settlement of debt on behalf of a shareholder;
- use of any amount for the benefit of a shareholder or related person; and
- additional taxable income or reduced tax losses arising from transfer pricing adjustments.

Effective date:	**1 July 2018**	S. 7 of the ITA

(e) No more Compensating Tax

Compensating Tax which previously applied at the rate of 42.86% on dividend payments made out of untaxed profits has been scrapped. Instead, the untaxed gains or profits will be subject to Corporate Income Tax at the rate of 30%.

This tax will not apply to registered collective investment schemes.

Effective date:	**1 January 2019**	S. 7A of the ITA

(f) Turnover Tax replaced by Presumptive Tax

Turnover Tax will be done away with and replaced with a Presumptive Tax. The Presumptive Tax will be payable by Kenyan-resident persons who are issued or are required to be issued with a business permit by a County Government and whose turnover does not exceed KShs 5 million. The tax will apply at the rate of 15% of the value of the business permit or trading license fee charged by the County government and this amount will be payable at the time of payment for the business permit/ trade license or the renewal of the same.

The Presumptive Tax does not apply to income generated from management and professional services, rental income and incorporated companies.

Effective date:	**1 January 2019**	S. 12C, Para. 9 of the Third Schedule to the ITA

1. Income Tax Act ('ITA') (continued)

(g) 130% Electricity deduction for manufacturers

Manufacturers will be able to deduct 130% of their cost of electricity subject to conditions to be set by the Ministry of Energy.

This will cushion manufacturers of goods from the high cost of electricity.

Effective date:	**1 January 2019**	S. 15 of the ITA

(h) Capital Gains Tax on transfers by General Insurance companies

It has been clarified that gains arising from the transfer of property by general insurance companies are subject to Capital Gains Tax. Life insurance companies have been specifically excluded from this provision.

Effective date:	**1 July 2018**	S. 19 of the ITA

(i) And finally, an amendment that never was

In his Budget Statement, the Cabinet Secretary proposed to introduce Corporate Income Tax at the rate of 15% for developers who construct at least 100 housing units in a year. Finance Bill, 2018 does not include any express amendments to this effect hence it remains to be seen how and when these legislative changes will be made.

2. Value Added Tax Act, 2013 ('VAT Act, 2013')

(a) Giving with one hand...

Equipment used for the construction of grain storage facilities has been exempted from VAT. Previously, only the materials used in the construction had been exempt from VAT. The exemption will only apply upon the recommendation of the Cabinet Secretary responsible for agriculture.

Effective date:	**1 July 2018**	First Schedule to the VAT Act, 2013

(b) ...and taking with the other

Maize corn seed, which had previously been VAT exempt, will now be standard rated.

Effective date:	**1 July 2018**	First Schedule to the VAT Act, 2013

(c) More uncertainty on the VAT status of Transhipment

The transportation of cargo to destinations outside Kenya is no longer provided for as being exempt. Since the amendment was introduced to exempt these services, there have been conflicting views as to their VAT status especially in the case of cargo transhipped through Kenya.

Despite the VAT exemption being provided for in 2017, there has been an opposing position to the effect that transhipment of cargo constitutes an export of service and is therefore zero-rated. This issue is yet to be resolved conclusively.

Effective date:	**1 July 2018**	First Schedule to the VAT Act, 2013

(d) Exempt goods

The list of exempt goods and services has been widened to include:

- Specialized equipment used for development and generation of solar and wind energy including deep cycle batteries which use or store solar power.
- Parts imported or purchased locally for the assembly of computers subject to approval by the Cabinet Secretary of the National Treasury upon the recommendation of the Cabinet Secretary for Information Communications & Technology.
- Goods used to equip specialised hospitals with a bed capacity of 50. Previously, the exemption only applied to goods, equipment and apparatus used in the construction of such hospitals.
- Wheat, Meslin and Barley seeds.
- Cereal straw and husks, unprepared, whether or not chopped, ground, pressed or in the form of pellets falling under tariff No. 1213.00.00.
- Lucerne (alfalfa mean) and pellets falling under tariff No 1214.10.00.
- Beet pulp, bagasse and other waste of sugar manufacture falling under tariff No. 2303.20.00.
- The supply of both alcoholic and non-alcoholic beverages to the Kenya Defence Forces Canteen Organisation.
- Postal services.
- Asset transfers and other transactions related to the transfer of assets into Real Estate Investment Trusts and asset backed securities.

Plant and machinery of Chapters 84 and 85 are currently VAT exempt. This exemption has now been restricted to only Plant and Machinery of chapter 84 and 85 which are used for the manufacture of goods.

Effective date:	**1 July 2018**	First Schedule to the VAT Act, 2013

2. Value Added Tax Act, 2013 ('VAT Act, 2013') (continued)

(e) Standard-rating of previously exempt goods

The following goods which had been previously exempt are now standard rated:

- Garments and leather footwear, manufactured in an Export Processing Zone at the point of importation.

(f) Zero-rated goods

The zero-rating of medicaments falling under Heading 30.04 has been limited to the following items:

- 3004.41.00 containing ephedrine or its salts
- 3004.42.00 Containing pseudoephedrine (INN) or its salts
- 3004.43.00 Containing nor ephedrine or its salts
- 004.49.00 Other

Effective date:	**1 July 2018**	First Schedule to the VAT Act, 2013

3. Excise Duty Act, 2015

(a) Exemption

Exemption from Excise Duty on goods has been restricted to only those goods that are received and consumed by an exempt person.

The Act does not define an 'exempt person' hence it remains to be seen how this provision will apply.

Effective date:	**1 July 2018**	S. 7(5) of the Excise Duty Act, 2015

(b) Annual inflation adjustments

The adjustment of Excise Duty rates to take into account inflation will now happen on an annual basis. Previously the rate was adjusted every two years.

Effective date:	**1 July 2018**	S. 10 of the Excise Duty Act, 2015

(c) Suspension of an Excise License

Generally, where the Commissioner must give notice to a licensee where an Excise Duty licence is to be suspended, revoked or not renewed.

No notice will be required where the affected persons are engaged in tax fraud, are found in possession of counterfeit stamps on excisable goods, have been in possession of goods bearing counterfeit stamps or have violated any regulations relating to health and safety standards.

Effective date:	**1 July 2018**	S. 23 of the Excise Duty Act, 2015

(d) Increased penalty for operating without an Excise Duty license

The penalty for manufacturing or importing goods without an Excise Duty license has been increased to the higher of double the Excise Duty payable or KShs 5 million.

Previously, the penalty was only double the Excise Duty payable. This is in line with the general introduction of more stringent penalties that is meant to encourage compliance.

Effective date:	**1 July 2018**	S. 38 of the Excise Duty Act, 2015

3. Excise Duty Act, 2015 (continued)

(e) Forfeiture of goods where offence committed

In addition to the increased penalties, the commission of an offence under the Excise Duty Act, 2015 may result in the forfeiture of any plant or excisable goods or materials to the Commissioner.

Effective date:	**1 July 2018**	S. 39 of the Excise Duty Act, 2015

(f) 'Robin Hood' Tax

Excise duty of 0.05% of the amount transferred has been introduced on money transferred by banks, money transfer agencies and other financial service providers where the amount transferred exceeds KShs 500,000 or more.

Effective date:	**1 July 2018**	First Schedule to the Excise Duty Act, 2015

(g) Excise Duty Rates

The Bill has proposed the following changes to the Excise Duty rates:

	Proposed rate	Current rate
Private passenger vehicles with an engine capacity of 2000 cc for petrol engines and 3000 cc for diesel engines	30%	20%
Sugar confectionary (including white chocolate) of tariff heading 17.04; chocolate in blocks, slabs or bars of tariff Nos 1806.31.00, 1806.32.00 and 1806.90.00	KShs 20/ kg	
Fees charged for money transfer services	12%	10%
Illuminating kerosene	KShs 10,305 per 1000l @ 20 degC	KShs 7,205 per 1000l @ 20 degC

Effective date:	**1 July 2018**	First Schedule to the Excise Duty Act, 2015

(h) Exemption for beverages supplied to the Kenya Defence Forces

Beverages, both alcoholic and non-alcoholic, supplied to the Kenya Defence Forces Canteen Organization are now exempt from Excise Duty.

Effective date:	**1 July 2018**	Second Schedule to the Excise Duty Act, 2015

4. Tax Appeals Tribunal, 2013 ('TAT Act, 2013)

(a) Panels to hear Appeals

Where a member of a panel hearing a dispute is not available, the hearing will not be adjourned but rather the Chairman of the Tax Appeals Tribunal ('TAT') will be free to appoint another member to the panel and have the proceedings continue without any delay.

This amendment is therefore likely to expedite the hearing and determination of tax disputes.

Effective date:	**1 July 2018**	S. 10 of the TAT Act, 2013

(b) Timelines to resolve tax disputes

The TAT is required by law to hear and determine appeals within 90 days. Taxpayers are, however, also permitted to attempt to resolve disputes out of the TAT such as through the Alternative Dispute Resolution mechanism. This often results in disputes taking longer to be determined.

The time spent in attempting to settle tax disputes out of the TAT such as through the Alternative Dispute Resolution mechanism will now not be taken into account in determining the 90 day timeline within which matters ought to be heard and determined.

Presently, the TAT rarely resolves tax disputes within the 90 day timeline but there is no statutory penalty for this failure.

Effective date:	**1 July 2018**	S. 13 of the TAT Act, 2013

5. Tax Procedures Act, 2015 ('TPA, 2015')

(a) Tax Representatives responsibilities

Tax representatives who act for taxpayers will now only be responsible for the tax obligation for which they have been appointed. Previously, where a taxpayer had more than one tax representative, each tax representative would be held responsible for all the obligations of the taxpayer regardless of the role they had been appointed for.

Effective date:	**1 July 2018**	S. 16(3) of the TPA, 2015

(b) Extension of time to submit tax returns

Persons seeking to file returns out of time will have to make an application to do so at least 15 days before the due date in the case of a monthly return and at least 30 days before the due date in the case of an annual return. Previously a person was free to apply for extension of time as long as it was done before the due date of the return.

The Commissioner is also required to communicate whether or not the extension has been granted at least 5 days before the due date. Where no notification is granted, the application will be deemed to have been granted.

Taxpayers will be limited to a single extension in respect of a tax period and where an extension is granted, late submission penalties will not apply.

Effective date:	**1 July 2018**	S. 25 of the TPA, 2015

(c) Applications for amended returns

The Commissioner will no longer have to approve or reject applications to file amended returns within 30 days. Whereas the timeline to consider such applications is now open ended, the Commissioner will have to provide reasons where the application is rejected.

Effective date:	**1 July 2018**	S. 31 of the TPA, 2015

(d) Tax Amnesty on foreign income extended

The Tax Amnesty on foreign income has been extended. The amnesty will now apply to income earned in the 2017 year of income and the deadline for filing the requisite filings has been extended to 30th June 2019.

Additionally, funds repatriated to Kenya will be exempt from the provisions of the Proceeds of Crime and Anti-Money Laundering Act, 2009 or any other Act relating to reporting and investigation of financial transactions provided such funds are not derived from proceeds of terrorism, poaching and drug trafficking.

Effective date:	**1 July 2018**	S. 37B of the TPA, 2015

(e) Late payment interest

Late payment interest will apply at the rate of 2%, up from the previous rate of 1%.

Effective date:	**1 July 2018**	S. 38 of the TPA, 2015

5. Tax Procedures Act, 2015 ('TPA, 2015') (continued)

(f) Requirement to pay taxes not in dispute before objecting to assessments scrapped

A Notice of Objection will now be deemed to have been validly filed where a taxpayer has made an application for the extension of time within which to pay taxes that are not in dispute.

This amendment will allow taxpayers seek redress on contentious issues even in instances where they are unable to immediately settle taxes that are not in dispute.

An express amendment has been introduced to the effect that all relevant documents must be provided with a Notice of Objection. This amendment will severely limit any scope that taxpayers may have to file supplementary/ additional information.

Effective date:	**1 July 2018**	S. 51 of the TPA, 2015

(g) Penalties...

Amendments have been introduced which ensure that all penalties for the late submission are charged under the TPA, 2015 and not the substantive statutes. The late submission penalties will be as follows:

- CIT returns – The higher of 5% of the tax due or KShs 20,000.
- VAT & Excise Duty returns – The higher of 5% of the tax due or KShs 10,000.
- Individual returns – The higher of 5% of the tax due or KShs 2,000.

A 20% penalty has also been introduced where a taxpayer fails to pay taxes by the due date.

Effective date:	**1 July 2018**	S. 83 of the TPA, 2015

(h) ...and a little more on penalties.

The Commissioner will now only impose one tax penalty in instances in which multiple penalties may apply. Previously the Commissioner had the discretion to determine whether one or all of the penalties would apply.

The Commissioner has also been granted express powers to remit penalties and interest of up to KShs 1.5 million in cases where there is hardship, inequity or it is impossible to collect taxes.

Where the penalties and interest in question exceed KShs 1.5 million, the Commissioner will have to obtain the prior approval of the Cabinet Secretary.

The Commissioner will also be required to make quarterly reports to the Cabinet Secretary setting out the remissions granted. Previously, these amounts were reported to the Auditor-General.

Effective date:	**1 July 2018**	S. 89 of the TPA, 2015

5. Tax Procedures Act, 2015 ('TPA, 2015') (continued)

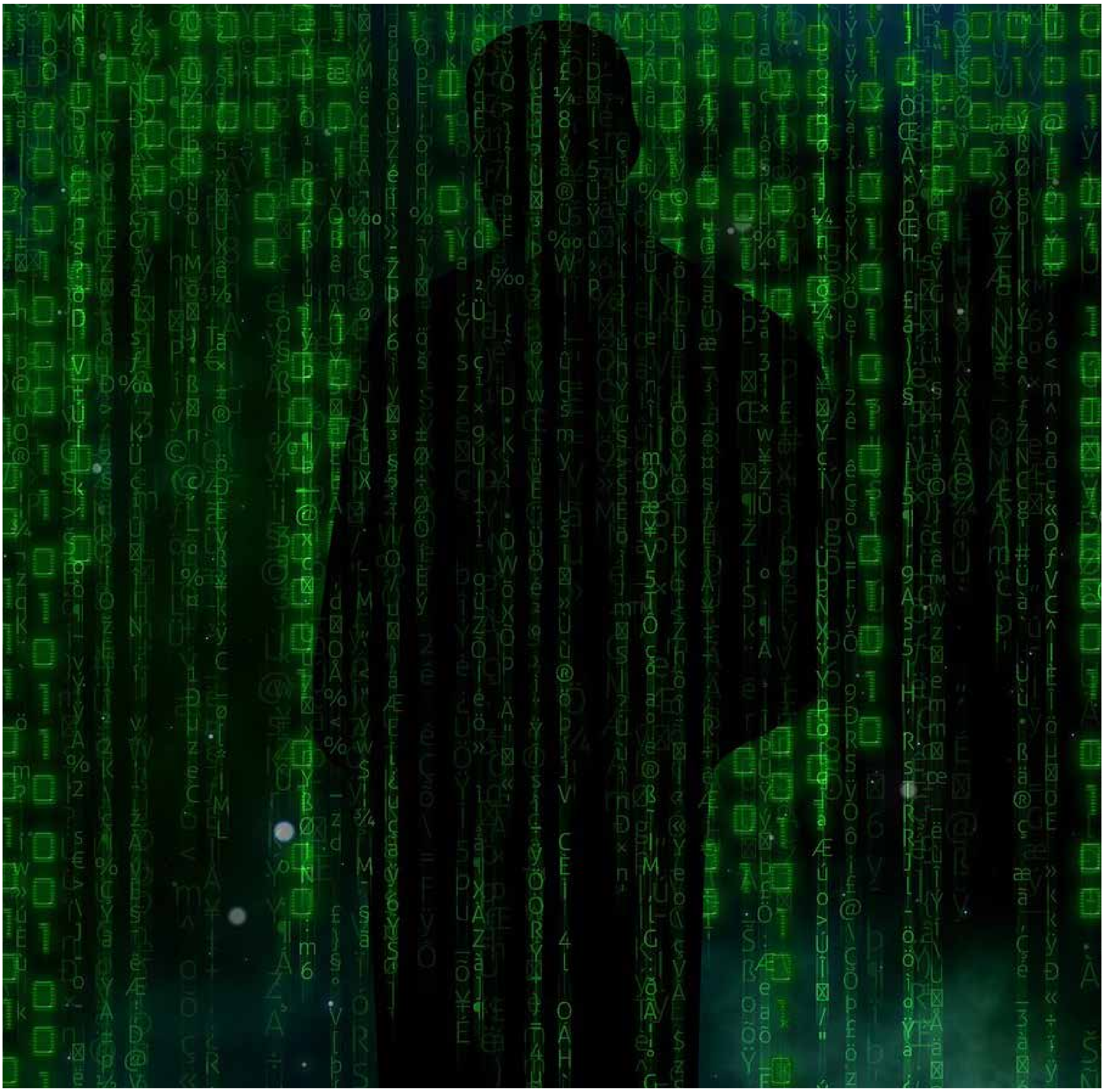
(i) Unauthorized access or improper use of computerized tax system

In a move to deter hacking, it will now be an offence to gain access or to attempt to gain access to a computerized tax system; or to disclose information obtained from a computerised tax system without authorisation. The punishment for such an offence is a prison term not exceeding two years or a fine not exceeding KSH 400,000 or both in the case of an individual or a fine not exceeding KSHS 1,000,000 in the case of a body corporate.

Additionally it will be an offence to falsify or damage information stored in a computerised tax system. Offenders will be liable to a prison term for a period not exceed three years or a fine not exceeding eight hundred thousand or both.

Previously, only the VAT Act, 2013 made reference to such offences.

Effective date:	**1 July 2018**	S. 103A, 103 B of the TPA, 2015



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6. Other Amendments

(a) Contributions to the National Housing Development fund

The CS has proposed the introduction of new employer and employee contribution to the National Housing Development fund. Both employers and employees will contribute 1% of the employees' gross earnings up to a maximum of KShs 5,000.

Effective date:	**1 October 2018**	S. 31 of the Employment Act, 2007

(b) Abolishment of the Interest Rate Cap

The CS has proposed the amendment of the Banking Act by removing the interest rate cap to ensure access to credit facilities.

Effective date:	**1 October 2018**	S. 33B of the Banking Act

(c) Penalties and Interest for non-payment of taxes by the betting and gaming industry

The Bill has proposed the amendment of the Betting, Lotteries and Gaming Act, CAP 131 by introducing a late payment penalty of 20% of the tax payable and interest at the rate of 2% simple interest per month where a person fails to pay tax on the due date. The late payment interest however will be limited to the value of the principal tax liability. The person liable to pay the penalty or interest will however be able apply to the collector in writing for remission of the penalty or interest. Remission may be granted where a person is in hardship or it is difficult to recover tax with the approval of the CS where the penalty or interest exceeds one million five hundred thousand shillings.

Effective date:	**1 October 2018**	S. 69B of Betting, Lotteries and Gaming Act

(d) Stamp Duty Exemption

Amendments have been proposed to the Stamp Duty Act to exempt the following:

- instruments relating to the business activities of Special Economic Zone enterprises, developers and operators; and
- instruments executed for purposes of the collection and recovery of tax.

Effective date:	**1 October 2018**	S. 117 of the Stamp Duty Act

(e) Penalties for non-remittance of Employee Pension Contribution

New penalties have been proposed for employers who fail to remit employee pension contributions of the higher of 5% or unremitted contributions or twenty thousand shillings.

Effective date:	**1 January 2019**	S. 53B of the Retirement Benefits Act, 1997

(f) 20% Export Levy on Copper waste and Scrap

The export of copper waste and scrap will be subject to an export levy of 20%. This will serve as a disincentive to vandals of high voltage electricity cables and similar copper products.

Effective date:	**1 October 2018**	First Schedule to the Miscellaneous Fees and Levies Act, 2016

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