Tax Alert

Issue No. 6 of 2020

The Finance Act, 2020

The Finance Act, 2020 was assented into law by the President on 30 June 2020 with a majority of the proposals in the Finance Bill, 2020 being enacted. Our tax alert analyses the Finance Act, 2020 and clarifies the effective dates for each of the amendments.

The most significant changes implemented through the Act are as follows:

- A new voluntary tax disclosure programme (amnesty from penalties, interest and prosecution) to run for the next 3 years covering income for the 5 years to 1 July 2020
- Increase in the upper and lower income threshold for residential rental income tax
- Minimum tax introduced based on gross turnover
- New digital service tax introduced based on gross transaction value
- Significantly increased compliance threshold where input VAT can only be claimed if declared by the seller as output VAT.

We welcome the introduction of the voluntary tax disclosure programme as this sets-up a win-win situation for both KRA and willing taxpayers. We also welcome the increases to the thresholds for residential rental income tax as it will also seek to enhance compliance.

The introduction of minimum tax and in particular whether its equitable and its administration are questionable. Administration of the digital service tax is also expected to be challenging. We are of the opinion that placing the responsibility and burden of ensuring VAT compliance by suppliers on claimants of input tax is not justified.

The East African Community Gazette Vol. AT 1 – No. 10 that was published on 30 June 2020 contains all the Customs Duties changes that were effective across the East African Community from 1 July 2020. A copy of this EAC Gazette is available on the EAC website.

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Tax Procedures Act

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Voluntary Tax Disclosure Programme	The Act has introduced a voluntary tax disclosure programme. Under this programme, taxpayers would be required to disclose their past tax liabilities to the Commissioner in exchange for relief from penalties and interests accrued on the disclosed principal taxes. The programme is for a period of five years prior to 1 July 2020. The programme will commence from 1 January 2021 and will be available for uptake for a period of three years. Taxpayers qualifying for relief of penalties and interest under the proposed programme will also not be prosecuted with respect to the tax liability disclosed. 100%, 50% and 25% waiver of penalties and interest will be granted if the voluntary disclosure is made and principal taxes are paid within the 1st, 2nd and 3rd year respectively. It is imperative for taxpayers to disclose all material facts otherwise they risk not getting approval or KRA would demand the penalties and interest even if approval for the waiver had previously been granted. The programme will not be applicable to persons who end up in refund positions after taking it up.	This presents a much needed opportunity and window for taxpayers to declare any past unpaid taxes and also presents the KRA with a significant opportunity to increase tax collections. **Effective Date: 1 Jan 2021**

Income Tax Act

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Residential Rental Income Tax (RRIT)	The Act has increased the upper limit for residential rental income from KShs 10 Million to KShs 15 Million per annum and has also increased the lower limit from KShs 144,000 to KShs 288,000 per annum.	Those earning annual residential rental income of between KShs 288,000 to KShs 15 million qualify for RRIT. RRIT is still payable on a monthly basis at the rate of 10%. **Effective Date: 1 January 2021**

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Minimum Tax	The Act has introduced a new tax known as minimum tax at the rate of 1% of the annual gross turnover. Minimum tax shall be computed at the rate of 1% of the annual gross turnover and shall be payable on the twentieth day of the fourth, sixth, ninth and twelfth month of the year of income. Where the computed minimum tax is higher than the estimated instalment tax, a person will pay minimum tax, otherwise, a person shall be liable to pay the estimated instalment tax. Minimum tax will not be applicable to: • incomes that are exempt from tax; • employment income; • income subject to turnover tax; • residential rental income; • gains from property transfers that are subject to Capital Gains Tax; and • income earned from the extractive industry.	Loss making entities will now have to pay the minimum tax. This is against the basic principles of charging income tax on gains/profits and is also punitive to entities that are in a loss position as a result of significant investments on which they have enjoyed capital allowances. Entities with high revenues but low margins will also have to pay the minimum tax which may not be covered by the tax that would otherwise arise on their net income. There is however a drafting error suggesting that profit making entities have to pay both minimum tax and estimated instalment tax even where the estimated instalment tax is higher than the minimum tax. However, our interpretation is that taxpayers are required to pay the higher of minimum tax or estimated instalment tax. There are no guidelines on how the minimum tax paid will be offset against the final or future tax payable or refunded to a taxpayer. There is also no guidance on the modalities of computing the minimum tax due, i.e. whether the new tax is pegged on the prior year or the estimated current year turnover and whether quarterly payments are meant to be equal (25% of the minimum tax per quarter)? **Effective Date: 1 January 2021**
Digital Service Tax	The Act has introduced digital service tax for persons earning income through the digital market place which is: • Applicable to any person on income derived from or accrued in Kenya from provision of services through a digital market place. • Payable at the rate of 1.5% of the gross transaction value at the point of transferring payment to the service providers. Resident persons and non-resident persons with a Permanent Establishment in Kenya will offset the digital service tax against income tax payable for that particular year of income. The Commissioner now has powers to appoint digital service agents for purposes of collection of the digital service tax.	This has brought clarity on administration and collection of digital service tax particularly on non-resident persons. However, it is not clear how the appointed agents will remit the tax deducted to the Kenya Revenue Authority. Administrative challenges and push back from international services providers on online platforms might hinder KRA from realizing the anticipated taxes from this amendment. Given that most non-resident persons require payment net of tax, there is a possibility that the tax will be borne by the consumer of the service. **Effective Date: 1 January 2021**

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Allowable deductions	The Act has deleted the following allowable deductions from Section 15 of the Income Tax Act: • Registration and annual subscription fees for trade associations; • Capital expenses incurred on legal costs and incidental expenses relating to: • authorisation and issue of shares, debentures and other securities for purchase by the general public; and • listing on a securities exchange operating in Kenya without raising additional capital; • Capital expenses incurred on rating for purposes of listing on any securities exchange in Kenya; and • Club subscriptions by an employer on behalf of an employee.	The amendment is in tandem with the Government's efforts to increase tax revenue. The Finance Bill had proposed to also restrict tax deductibility for expenditure incurred on public schools, hospitals, roads and similar social infrastructure that were pre-approved. It is good to see this proposal having been dropped. **Effective Date: 1 January 2021**
Registered Home Ownership Savings Plan	The Act has scrapped the provision that allowed depositors to enjoy a tax deduction on deposits placed with an approved institution registered home ownership savings plan (HOSP)as well as the income tax exemption enjoyed by a registered HOSP.	Depositors will no longer enjoy tax deduction on savings made to a registered home ownership savings plan. Further, interest income earned on deposits to a registered HOSP will be now be subject to tax. Additionally, a registered HOSP will no longer be exempt from income tax. **Effective Date: 1 January 2021**
Income Tax Exemptions	The Act has scrapped income tax exemptions on employment income paid in the form of bonuses, overtime and retirement benefits to low income earners. This income will now be subject to tax.	It is good to note that proposals in the Finance Bill to scrap income tax exemptions on NSSF income and monthly pension granted to persons aged sixty-five years and above were not enacted. Therefore, these incomes are still exempt from income tax. **Effective Date: 1 Jan 2021**
Income not chargeable to Capital Gains Tax	The Act has aligned the Eighth Schedule to the Income Tax Act with the new Second Schedule on capital allowances in respect of capital gains tax exemption on transfer of assets that qualifying for wear and tear allowances.	This is not a new provision but an alignment for clarity.

Value Added Tax

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Deductibility of input VAT by taxpayers	The Act bars taxpayers from claiming input VAT on purchases if suppliers have not declared output VAT on the sales invoices in their VAT returns.	VAT Auto Assessments have now effectively been legalized. Taxpayers will now have an onerous task of following up with their suppliers to ensure output VAT is declared before they can claim input VAT. This will be an administrative challenge and will deny taxpayers the right to claim legitimate input VAT in most instances. **Effective Date: 30 June 2020**
Reclassification of supplies from exempt to standard rate at 14%	The Act has reclassified the following items from exempt status to standard rate: • Helicopters of an unladen weight not exceeding 2,000 kg of tariff 8802.11.00 • Helicopters of an unladen weight exceeding 2,000 kg of tariff 8802.12.00 • Airplanes and other aircraft of an unladen weight not exceeding 2,000 Kg or tariff 8802.20.00 • Other parts of airplanes helicopters of tariff 8803.30.00 Other parts of airplanes helicopters of tariff 8803.30.00 • Aircraft launching gear and parts thereof; deck-arrestor or similar gear and parts thereof of tariff 8805.10.00 • Air combat simulators and parts thereof of tariff 8805.21.00 • Other ground flying trainers and parts thereof of tariff 8805.29.00 • Tractors other than road tractors for semitrailers • Hiring, leasing and chartering of helicopters of tariffs 8802.11.00 and 8802.12.00.	This provision will increase the cost of these items. **Effective Date: 1 July 2021**

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Reclassification of supplies from exempt to standard rate at 14%	The Act also reclassifies the following from exempt to standard rate: • specialized equipment for the development and generation of solar and wind energy, including deep cycle batteries • Goods of tariff 4011.30 (New pneumatic tyres, of rubber of a kind used on aircraft) • Taxable goods locally purchased or imported by manufacturers or importers of clean cooking stoves for direct and exclusive use in the assembly, manufacture or repair of clean cooking stoves. • Stoves, ranges, grates, cookers (including those with subsidiary boilers for central heating) barbeques, braziers, gas-rings, plate warmers and similar nonelectric domestic appliances, and parts thereof, or iron or steel of tariff numbers 7321.11.00, 7321.12.00, 7321.19.00, 7321.81.00, 7321.82.00, 7321.83.00 and 7321.90.00 • One personal motor vehicle, excluding buses and minibuses of seating capacity of more than eight seats, imported by a public officer returning from a posting in a Kenyan mission abroad and another motor vehicle by his spouse. • Aluminum pilfer proof caps with EPE liner under tariff number 8309.90.90.	This provision will increase the cost of these items. **Effective Date: 30 June 2020**
Reclassification from Standard rate to Exempt status	The Act has reclassified the following supplies from standard rate to exempt: • Maize (corn) seeds under tariff no. 1005.10.00 • Ambulance services.	The exemptions of maize seeds and essential ambulance services is welcome. **Effective Date: 30 June 2020**
Reclassification from zero rate to standard rate	The Act has reclassified the following supplies from zero rate to standard rate: • Supply of liquefied petroleum gas (LPG) including propane • 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.	This will result in price increases to the final consumer. **Effective Date: 30 June 2020**
Reclassification from exempt to zero rate	The Act has reclassified the following items from exempt to zero rate for a period of six months from 30 June 2020: Supply of maize (corn) flour, cassava flour, wheat or meslin flour and maize flour containing cassava flour by more than 10% percent in weight.	The essential commodities will be more affordable to consumers. **Effective Date: 30 June 2020**

Tax Appeals Act

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Limitation of Grounds of Appeal	The Act now states that an appellant can only rely on grounds stated in its documents and not on any other grounds.	This change prevents an appellant from submitting new documents after lodging appeal documentation. By extension, it prevents appellants from introducing new grounds of appeal. **Effective Date: 30 June 2020**

Excise Duty

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Definition of licence expanded	The definition of licence has been expanded to capture all activities i.e. services, goods and any other activity that requires excise duty licensing in Kenya.	This change clarifies and removes ambiguity on the license requirements for excise duty purposes in Kenya. **Effective Date: 30 June 2020**
Excise duty on alcoholic beverages	Currently, alcoholic beverages i.e. beers, cider, perry etc. with an alcohol strength of 10% or less attract excise duty of KShs 105.20 per litre. On the other hand, spirits and spirituous beverages with an alcoholic strength exceeding 10% attracts excise duty at KShs 253 per litre. The Finance Act has adjusted the alcoholic strength threshold in both cases from 10% to 6% and therefore, alcoholic beverages and spirits with an alcoholic content of above 6% will now attract excise duty at the higher rate of KShs 253 per litre.	This is expected to further increase government revenue from alcoholic beverages and spirits. **Effective Date: 30 June 2020**
Excise duty on betting	Excise Duty of 20% on the amount wagered has been deleted.	This proposed change is a welcome move for players in the betting industry. However, the National Treasury later released a statement on its plans to reintroduce Excise Duty on betting activities within the next 6 months to mitigate against the social vices associated with betting. **Effective Date: 30 June 2020**
Adjustment for inflation	Section 10 of the Excise Duty Act is amended to require the Cabinet Secretary National Treasury to seek the National Assembly's approval before adjusting the specific rate of excise duty.	This is a welcome move aimed at ensuring there is scrutiny to the proposed excise duty inflation adjustments. **Effective Date: 1 January 2021**

Miscellaneous Fees and Levies Act

	Finance Act 2020 (Act) Amendments	Remarks & Effective Date
Import Declaration Fees (IDF) changes	The Finance Act makes the following changes: • Goods imported under the East African Community Duty Remission Scheme moved from KShs 10,000 to 1.5% of the customs Value; • IDF at the rate of 2.5% was proposed on goods entered for home use from an export processing zone; • IDF at the rate of 3.5% was proposed on previously exempt aircraft of unladen weight not exceeding 2,000 kg and helicopters of tariffs 8802.11.00 and 8802.12.00; • IDF at the rate of 3.5% was proposed on previously exempt goods that the Cabinet Secretary may determine are in public interest, or to promote investments which value shall not be less than KShs 200 million; • IDF at the rate of 3.5% was proposed on previously exempt goods imported for implementation of projects under special operating framework arrangement with the Government; and • IDF to be exempted on all equipment, machinery and motor vehicles for the official use by the Kenya Defense Forces and National Police.	These changes are expected to increase government revenue. **Effective Date: 30 June 2020** **Effective Date for amendment on introduction of IDF on aircraft is 1 July 2021.**
Railway Development Levy (RDL) changes	The Finance Act makes the following changes: • RDL to be exempt on currency notes and coins imported by the Central Bank of Kenya; • RDL to be exempt on equipment, machinery and motor vehicles for the official use by the Kenya Defence Forces and National Police; and • RDL at the rate of 3.5% was introduced on previously exempt goods that the Cabinet Secretary may determine are in public interest, or to promote investments whose value exceeds KShs 200 million.	These changes are expected to increase government revenue. **Effective Date: 30 June 2020**

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