

**CLIENT ALERT:**  
**TAX ALERT: FINANCE ACT, 2019**



SIMBA & SIMBA  
ADVOCATES

## INTRODUCTION

Simba & Simba Advocates is one of Kenya's leading full-service law firms, with a rich professional history built over a period of over twenty-eight (28) years.

In this bulletin, we highlight the key legislative changes in the **Finance Act, 2019 (the Act)** which was recently assented into law. The Act introduces various changes to the legal and tax landscape. The changes took effect on 7th November 2019 with the exception of those highlighted in this alert which will take effect on 1st January 2020.

We outline the changes in this Tax Alert including the impact they will have on businesses.

## INCOME TAX

### Taxation of Digital Market Places

Income accruing to a digital market place will be subject to taxation. A digital marketplace has been defined as: *"a platform that enables the direct interaction between buyers and sellers of goods and services through electronic means."* The Act empowers the Cabinet Secretary (**CS**) for Treasury and National Planning to make regulations on mechanisms for taxation of digital marketplaces.

It will be interesting to see how the income accruing to online platforms without a permanent establishment in Kenya (e.g. Netflix) will be taxed in view of the fact that the definition of a permanent establishment under the Income Tax Act has not been amended to cater for digital marketplaces.

### Tax On Untaxed Profits

Vide the Finance Act, 2018, companies are required to charge a 30% corporation tax on distribution of dividends from untaxed profits. The Kenya Revenue Authority (**KRA**) sought to clarify this position vide a public notice dated 11<sup>th</sup> February 2019 (the **Notice**). The Notice outlined that this provision does not apply to distribution of income as dividends where such income (a) is received by a registered collective investment scheme; (b) is a dividend received by a resident company from a subsidiary, whether local or foreign; (c) has been subjected to a capital gains tax; or (d) has been subjected to final tax.

Notably, declaration of dividends out of income exempt from tax was not listed as one that would be exempt from the 30% corporation tax. The Act has now amended this provision by providing that where a company declares a dividend out of tax-exempt income, such distribution will not be subject to 30% tax. Such exempt income would include capital gains arising on the sale of shares listed on the Nairobi Securities Exchange (**NSE**) and capital gains arising from the disposal of agricultural land of less than 50 acres located outside a municipality.

### **Withholding Tax (WHT)**

Demurrage charges shall no longer be considered as income subject to WHT.

Reinsurance premiums have been included in the list of incomes subject to WHT. WHT will be applicable on re-insurance premiums paid to non-residents except those paid in respect of aircraft. The Income Tax Act was silent on whether these premiums should be subject to WHT.

Under the Income Tax Act, permanent establishments are not eligible for a tax deduction on payments made to their head offices. Such payments are also not subject to WHT. The Act requires that where such expenses are deductible under the provisions of a double taxation agreement, such amounts will now be construed as being accrued in or derived from Kenya and therefore subject to non-resident WHT rates.

### **Turnover and Presumptive Tax:**

Turnover tax which ought to be paid by residents whose business turnover does not exceed KES 5 Million during any year of income shall be calculated at a rate of 3% of a business' gross receipts. This tax will however not apply to rental income, management, professional or training fees, the income of incorporated companies and any income which is subject to a final withholding tax under the Income Tax Act.

A taxpayer who is eligible to pay this tax may, through a notice in writing to the Commissioner, elect not to be subject to these provisions.

Important to note is that persons required to pay turnover tax shall be subjected to payment of presumptive tax at the rate of 15% of the business permit or trading licence issued by the county government. This tax shall be payable at the time of payment for issuance or renewal of such licence.

Returns in respect of turnover tax should be submitted and tax paid by the 20<sup>th</sup> of the month following the end of the calendar month.

***With effect from 1<sup>st</sup> January 2020***

## Thin Capitalization

The Act exempts a company implementing a project under an affordable housing scheme from thin capitalisation rules upon recommendation by the CS for housing. Thin capitalisation rules are to the effect that where a resident foreign controlled company has a debt to equity ratio exceeding 3:1 (the **thin capitalisation ratio**), any interest paid in excess of the thin capitalisation ratio and any realised foreign exchange losses are disallowed for tax purposes. In effect, upon recommendation by the CS for housing, resident companies which are foreign controlled and which will implement projects under the affordable housing scheme will not need to maintain the thin capitalisation ratio for the interest expenses to be allowed for tax purposes.

***With effect from 1<sup>st</sup> January 2020***

## Collective Investment Schemes

An investee company of a real estate investment trust (**REIT**) has been included in the list of collective investment schemes whose income is exempt from tax. An investee company is a company fully owned by a REIT through which that REIT holds property and where the income of the investee company flows directly to the REIT. Previously, only REITs registered by the Commissioner were exempt from tax.

## Registered Home Ownership Savings Plan (HOSP)

Registered HOSPS shall be dealt with in accordance with the investment guidelines issued by the Capital Markets Authority alongside the prudential guidelines issued by the Central Bank of Kenya. Further, approved institutions that qualify as registered HOSPs will include a fund manager or investment bank registered under the Capital Markets Act.

***With effect from 1<sup>st</sup> January 2020***

## Penalty On Unpaid Tax

The provision in the Income Tax Act which required a penalty of 20% where any amount of tax remains unpaid after the due date has been deleted by the Act. In effect, the penalty set out under the Tax Procedures Act for unpaid tax will apply going forward. The Tax Procedures Act provides for a penalty of 5% of the tax that remains due and payable.

## Exempt Income

The following incomes have been exempted from tax:

- a. The income of the National Housing Development Fund.
- b. Income earned by an individual who is registered under the Ajira Digital Program for three years beginning 1<sup>st</sup> January, 2020 provided that the individual has paid the registration fee of KES 10,000 per annum.



- c. The amount withdrawn from the National Housing Development Fund to purchase a house by a contributor who is a first-time home-owner.
- d. Interest income accruing from all listed bonds, notes or other similar securities used to raise funds for infrastructure, projects and assets defined under Green Bonds Standards and Guidelines, and other social services, provided they have a maturity period of at least three years.

***With effect from 1<sup>st</sup> January 2020***

### **Plastics Recycling Companies**

The income tax of a company operating a plastics recycling plant shall be 15% for the first five years from the year its operations commenced. Previously, such investors were subjected to the usual 30% corporation tax. This measure is aimed at incentivizing companies which recycle plastics in a bid to conserve the environment.

### **Capital Gains Tax (CGT) Exemption**

The Act has introduced exemption from CGT on the transfer of property resulting from internal restructuring of corporate entities where the transfer is a legal or regulatory requirement, as a result of derivative or compulsory acquisition by the Government, an internal restructuring within a group which does not involve transfer of property to a third party or in the public interest and approved by the CS. This is a welcome move noting that the CGT rate has been maintained at 5% despite previous proposals to increase it to 12.5%.

## **VALUE ADDED TAX (VAT)**

### **Reverse VAT**

The scope of persons subject to payment of VAT on imported services has been widened to include any person. Therefore, non-registered persons importing taxable services will now be required to account for reverse VAT.

### **Digital Marketplace**

Income from supplies made through a digital marketplace shall be subjected to VAT. The CS shall make regulations to provide the mechanisms for implementing this provision.

### Special Economic Zones (SEZ) Incentive

Previously, goods were only considered to have been imported when removed from an export processing zone (**EPZ**). The Act has now extended this consideration to SEZs. The time for supply for goods removed from an SEZ shall accordingly be at the time of removal for home use.

### VAT Exemptions

1. The supply of specialized equipment for the development and generation of solar and wind energy, including deep cycle batteries which use or store solar power shall be exempt from VAT on the recommendation of the CS for energy. Previously, supply of these items were automatically exempt from VAT and there was no requirement for a recommendation from the CS.
2. The following items have also been added into the list of exempt supplies:
  - a. Locally manufactured motherboards.
  - b. Inputs for the manufacture of motherboards approved by the CS for information, communication technology.
  - c. Plant, machinery and equipment used in the construction of a plastics recycling plant.
  - d. 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.
  - e. Goods imported or purchased locally for the direct and exclusive use in the construction of houses under an affordable housing scheme approved by the CS on the recommendation of the CS for housing.
  - f. Musical instruments and other musical equipment, imported or purchased locally, for exclusive use by educational institutions, upon recommendation by the CS for education.
- The above items shall not attract any VAT whatsoever. This amendment has a positive effect on production and supply of the listed goods and industries as it will lower the cost of production. There is a likelihood that the decreased costs of production will trickle down to the consumers by way of fair prices.

### Zero Rating

1. Agricultural pest control products have henceforth been included under the list of zero rated products. This means that VAT on these products shall be charged at a rate of zero (0) % and suppliers will be in a position to fully deduct input VAT. This amendment will lead to a decrease in prices of pest control products which in turn makes them affordable to persons in the agricultural sector.
2. Propane is now zero-rated alongside liquefied petroleum gas. Previously, propane was a taxable supply at the standard rate of 16%.

## EXCISE DUTY

### Betting

Beginning 7<sup>th</sup> November 2019, excise duty on betting activities will be applicable at a rate of 20% of the amount wagered or staked. Currently, betting companies are subject to betting tax at a rate of 15% and corporation tax at the rate of 30%. Winnings from betting are also subject to WHT at a rate of 20%. This provision will lead to an increased tax burden on betting companies.

With regard to betting, the time of supply shall be the time the time a person wagers or stakes money on a platform or other medium provided by a bookmaker.

### General Penalty

A penalty has been introduced where there is no specific penalty for contravention of the Excise Duty Act or regulations. The penalty for such contravention, upon conviction, shall be a fine not exceeding KES 2 Million or imprisonment for a term not exceeding two years or both. This provision seeks to impose stiffer penalties to discourage non-compliance.

### Annual inflationary adjustments on excisable goods

Most of the excisable goods that have specific rates of excise duty are subject to an adjustment for inflation every 1<sup>st</sup> day of July of each year. The adjustment date has now been changed from the 1<sup>st</sup> day of July to the 1<sup>st</sup> day of October every year.

### Insurance Commission

The Act has excluded fees or commissions earned in respect of a loan or any share of profit from the definition of “other fees” effectively exempting the same from excise duty. It further excludes insurance premiums or premium based or related commissions specified in the Insurance Act or regulations made under it, from excise duty.

### Rates of Excise Duty On Specific Excisable Goods

The new rates on certain excisable goods are tabulated in the schedule to this alert

## TAX PROCEDURES

### PIN Requirements

The Commissioner may exempt any person or class of persons from the requirement for a PIN upon receipt of the requisite application made by or on behalf of such a person. This exemption will be limited to the transactions for which a PIN is required under the Tax Procedures Act.

The waiver of PIN requirement for foreigners will improve the ease of doing business in Kenya which at times is an onerous process.

Further, the following transactions shall henceforth require production of a KRA PIN:

- a. Registration and renewal of membership by professional bodies or other licensing agencies. Examples of such bodies include ICPA-K, ICPS-K, Law Society of Kenya among others; and
- b. Registration of mobile cellular pay bill or till numbers by telecommunication operators.

### Tax Amnesty for Companies Listed On the Growth Segment

For a period of three (3) years from 7<sup>th</sup> November 2019, the Commissioner shall refrain from recovering penalties and interests from companies that have been listed on the growth enterprise market segment (**GEMS**) of the NSE with respect to any year of income prior to the date of listing. Such a company ought to have made full disclosure of its past income, assets and liabilities for the two (2) years immediately preceding the date of listing. Further, the company's principal tax ought to have been paid in full.

This provision shall however not apply in respect of any tax where the person who should have paid:

- i. has been assessed in respect of the tax or any matter relating to the tax;
- ii. is under audit or investigation in respect of the undisclosed income or any matter relating to the undisclosed income.

Important to note is that a company which delists from the NSE before the expiry of five (5) years from the date of listing shall be assessed for all taxes, penalties or interest for the years it was in operation prior to listing.

The amnesty will encourage SMEs to list under the GEMS and increase economic activity at the NSE.



## **WHT Penalty**

Where a person fails to withhold and remit WHT to the Commissioner, the Commissioner shall have the power to recover the taxes from such a person. Effectively, amounts not deducted or withheld shall be treated as if they were tax due and payable by the person required to account for WHT.

## **Withholding VAT**

The withholding tax on VAT (**WHVAT**) has been reduced from 6% to 2% of the taxable value on the taxable supplies. This is aimed at reducing the accumulation of WHVAT credits. Such WHVAT shall however not apply to the taxable value of zero rated supplies.

## **Departure Prohibition Order**

Under the Tax Procedures Act, where the Commissioner has reasonable grounds to believe that a person may leave Kenya without paying tax that is or will become payable by him or by a company where he is a controlling member, he may issue a departure prohibition order against the person. The Act has amended this provision to include tax representatives to be among the people against whom a departure prohibition may be issued. A person's tax representative under the Tax Procedures Act includes chief executive officers, managing directors, company secretaries, treasurers, trustees, resident directors or similar officers.

## **Objection Decision**

The Tax Procedures Act has been amended to allow the Commissioner to issue an objection decision beyond the 60-day period, where additional information is to be provided by the taxpayer. Previously, the Commissioner was required to issue an objection decision within 60 days of receipt of the notice of objection.

This provision may increase the period required to resolve a dispute as the Commissioner could ask for additional information from the taxpayer indefinitely thereby increasing the period required to issue a tax decision.

## **Late Submission Penalty**

The Act provides that the late submission penalty (currently 5% of the unpaid tax) shall be calculated after deducting the tax already paid and WHT credits from the total tax liability.

## **Tax Shortfall Penalty**

The penalty for tax shortfall shall be applied at a rate of 75% of the tax shortfall when the statement or omission was made deliberately. The previous 25% of the tax shortfall in any other case has been deleted and will no longer apply. This means that the penalty for tax shortfall shall be applied only to taxpayers who made a false statement or omission deliberately.

## OTHER AMENDMENTS

### 1. The Miscellaneous Fees and Levies

#### a. Import Declaration Fee (IDF)

IDF has been increased from 2% of the customs value to 3.5%. IDF the rate of 2% is however chargeable on the following:

- (i) Raw materials and intermediate products imported by approved manufacturers;
- (ii) Raw materials and intermediate products imported by manufacturers approved by the CS upon the recommendation of the relevant CS; and
- (iii) Inputs for the construction of houses under an affordable housing scheme approved by the CS on the recommendation of the CS for housing.

#### b. Railway Development Levy (RDL)

The rate of RDL has been increased from 1.5% to 2% of the customs value while a rate of 1.5% has been introduced on the following:

- (i) Raw materials and intermediate products imported by approved manufacturers;
- (ii) Raw materials and intermediate products imported by manufacturers approved by the CS upon the recommendation of the relevant CS; and
- (iii) Inputs for the construction of houses under an affordable housing scheme approved by the CS on the recommendation of the CS for housing.

#### c. Anti-Adulteration Levy (AAL)

The Act introduces a provision on the refund of AAL, upon written application by importer, where the Commissioner is satisfied that the levy was paid in respect of illuminating kerosene that has subsequently been used by a licensed or registered manufacturer to manufacture paint, resin or shoe polish.

### 2. The Capital Markets Act

The Capital Market Authority will have power to recover summarily as civil debts the financial penalties imposed or chargeable under the Capital Markets Act.

### 3. The Banking Act

The Act repeals the interest capping rate under the Banking Act.

It is important to note that loan agreements or arrangement entered into prior to the repeal of the interest capping law shall not be varied and such terms shall continue to be in force provided that the interest rate on such loans may be varied downwards.

#### **4. The Standards Act**

All cargo consolidators will need to be registered by the Kenya Bureau of Standards in consultation with the KRA prior to importation of cargo into Kenya. A company shall qualify for registration if it:

- a) is tax compliant;
- b) is a member in good standing with a recognized association for consolidators;
- c) has a warehouse in the country of origin and country of destination; and
- d) has not committed any offence relating to importation of substandard or counterfeit goods.

Importation of cargo by a consolidator without such registration is an offence punishable by a fine of KES 1 Million and/or one (1) year imprisonment.

Notably, companies already in the consolidation business will be allowed to continue operating as such to provide them with a grace period for complying with the above requirements.

#### **5. The Retirement Benefits Act**

An approved issuer will be required to transfer funds out of the asset class within twelve (12) months or such shorter period after the termination of the agreement investing a scheme's assets into a Guaranteed Fund Asset Class.

Further, where the liquidator of a scheme is unable to trace any member of the scheme within a period of two years from the completion of winding up proceedings, the accrued benefits will need to be forwarded to the Unclaimed Financial Assets Authority. The trustee may treat such benefits as accrued benefits if:

- a) the member has not made a claim and the trustee is unable to locate such member;
- b) the member has made a claim but the trustee is unable to locate such member;
- c) the member or beneficiary has not:
  - (i) increased or decreased the principal;
  - (ii) accepted any payment in respect of the accrued benefits;
  - (iii) communicated with the scheme concerning the accrued benefits; or
  - (iv) indicated any other interest in the accrued benefits as evidenced by the record prepared by the trustees.

#### **6. The Employment Act**

The Act amends the Employment Act by deleting the definition of the term "employee earnings" as the same is not used elsewhere in the Employment Act and introduces the

definition of the term “basic salary” to mean “*an employee’s gross salary excluding allowances and other benefits.*”

## 7. The Housing Act

The Housing Fund established under the Housing Act will now be referred to as the National Housing Development Fund.

Further, the general penalty for an offence under the Housing Act is a fine not exceeding KES 10 Million and/or imprisonment not exceeding three (3) years.

Where a person’s act or omission results to loss of money from the National Housing Development Fund, that person shall be liable to a penalty equivalent to twice the amount lost.

## 8. The Stamp Duty Act

The transfer of a house constructed under an affordable housing scheme from the developer to the National Housing Corporation is now exempt from stamp duty.

## SCHEDULE OF EXCISE DUTY RATES

The new excise duty rates shall be as follows:

Item	New Rate In Kenyan Shillings (Kshs.)
<b>Cigars, cheroots, cigarillos, containing tobacco or tobacco substitutes</b>	Kshs. 12,624 per kg.
<b>Electronic cigarettes</b>	Kshs. 3,787 per unit
<b>Cartridge for use in electronic Cigarettes</b>	Kshs. 2,525 per unit
<b>Cigarette with filters (Hinge lid and</b>	Kshs. 3,157 per mile

soft cap)	
<b>Cigarettes without filters (plain cigarettes)</b>	Kshs. 2,272 per mile
<b>Other manufactured tobacco and manufactured tobacco substitutes; “homogenous” and “reconstituted tobacco”; tobacco extracts and essences</b>	Kshs. 8,837 per kg.
<b>Wines including fortified wines, and other alcoholic beverages obtained by fermentation of fruits</b>	Kshs. 189 per litre
<b>Spirits of undenatured ethyl alcohol; spirits liqueurs and other spirituous beverages of alcoholic strength exceeding 10%</b>	Kshs. 253 per litre
<b>Motor vehicles of tariff heading 87.02, 87.03 and 87.04 excluding:</b> <ul style="list-style-type: none"> <li>i. locally assembled motor vehicles;</li> <li>ii. school buses for use by public schools;</li> <li>iii. motor vehicles of tariff no.8703.24.90 and 8703.33.90; and</li> <li>iv. imported motor vehicles of cylinder capacity exceeding 1500cc</li> </ul>	20%



Imported motor vehicles of cylinder capacity exceeding 1500cc of tariff heading 87.02, 87.03 and 87.04	25%
Motor vehicles of tariff no. 8703.24.90 and 8703.33.90	35%
100% electric powered motor vehicles of tariff no. 8702.40.11, 8702.40.19, 8702.40.21, 8702.40.22, 8702.40.29, 8702.40.91, 8702.40.99 and 8703.80.00	10%
Imported sugar confectionary of tariff heading 17.04	Shs 20 per kg
Imported white chocolate, chocolate in blocs, slabs or bars of tariff Nos. 1806.31.00, 1806.32.00, 1806.90.00	Shs 200 per kg
Imported gas cylinders	35%

For feedback or any questions in relation to this alert, kindly contact our Tax Division on the below contacts:-



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She also advises clients on real estate taxes including stamp duty and capital gains tax.

In addition, Dorcas represents clients in complex tax audits and disputes with the Kenya Revenue Authority at the Tax Appeals Tribunal and the High Court. Her experience also includes providing advice on legal and tax due diligences, corporate restructuring and reorganization, oil and energy.

Dorcas is an Advocate of the High Court of Kenya. She is a certified public accountant (CPA) graduate from Strathmore University, holds a Bachelor of Laws Degree from Catholic University of Eastern Africa and a Post-Graduate Diploma in Law from the Kenya School of Law. She is an Alumnus of Jomo Kenyatta High School.



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