Resolute
BUSINESS ADVISORY

Tax Alert 2022

TAX ALERT

Highlights of the Tax Changes as per the Finance Act, 2022.

Introduction

The Finance Act, 2022 was assented by the President into law on 21 June 2022 thus becoming an Act of Parliament . It has introduced various changes affecting several tax laws including; the Income Tax Act, Excise Tax, Value Added Tax (VAT, Excise Tax and the Tax Procedures Act.
 Most of the changes made to the various tax laws will be effective as from 1 July 2022 while a few others will come into force on 1 January 2023.

Our detailed analysis of the changes is summarised below

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Commited to the end.

1. Income Tax

1.1 Capital Gains Tax (CGT)

Change

The capital gains tax (CGT) rate has been increased from **5%** to **15%**

Exemption: Firms certified by the Nairobi International Financial Centre Authority that invests five billion shillings in Kenya and transfers such investment after five years the applicable rate for capital gains tax will be the rate prevailing at the time that the investment was made.

Effective date: 1 January 2023

1.2 Employee Share Ownership Plan (ESOP)

Change

The tax point for ESOP has been changed from the date “the option is granted by the employer” to the date “when the employee exercises the option.

The value of the taxable benefit is the difference the offer price, per share at the date the option is granted by the employer and the market value, per share on the date when the employee exercises the option

Further, there is no requirement for an ESOP plan to be registered with the Commissioner as a collective investment scheme within the meaning of the Capital Markets Authority Act (Cap 485A)

Effective date: 1 July 2022

1.3 Donations as tax deductible expenses

Change

Any donation in that year of income to any charitable organization whose income is exempt from tax under paragraph 10 of the First Schedule to the Income Tax Act, or to any project approved by the Cabinet Secretary responsible for matters relating to Finance, are tax deductible expenses.
Currently only donations to charitable organizations registered under the Societies Act or the Non-Governmental Organisations Co-ordination Act and whose income is exempt from taxation under the First Schedule of the Income Tax Act are allowable tax expenses.

Effective date: 1 July 2022

1.4 Realised foreign exchange losses

Change

Realised foreign exchange losses for a thinly capitalized company are deferred until the thin cap position reverses.
This is with the exception of banks, non deposit taking micro finance businesses under Micro-Finance Act,2006, entities

A thinly capitalized company is defined as that whose gross interest paid or payable to related persons and third parties exceeds thirty percent (30%) of the company’s earnings before interest, taxes, armortisation and depreciation (EBITAD)

Effective date: 1 July 2022

Income Tax

1.5 Investment Deduction

Change

Introduction of enhanced investment deduction at the rate of one hundred and fifty percent (150%) on investments made outside the counties/cities of Nairobi or Mombasa if they meet either of the following criteria;

- The cumulative investment value for the preceding four years as from 1st July 2022 or
- The cumulative investment for the succeeding three years is at least two billion shillings.

Further for purposes of investment deduction, manufacture definition is widened to include generation of electricity for own use.

Effective date: 1 July 2022

1.6 Financial Derivatives

Change

Bring into the ambit of taxation gains accruing to a non-resident person from a financial derivatives contract with a resident person.
The applicable withholding tax rate shall be 15%.
The taxation shall be in accordance with regulations made by the Cabinet Secretary
Exemption: gains from derivatives traded at the Nairobi Stock Exchange (NSE)

The term 'financial derivative' is defined to mean a financial instrument the value of which is linked to the value of another instrument underlying the transaction which is to be settled at a future date

Effective date: 1 January 2023

1.7 Exemption from Interest restriction

Change

Currently, only banks and financial institutions licensed under the Banking Act and Micro and Small Enterprises registered under the Micro and Small Enterprises Act, 2012, are exempt from interest restriction due to thin capitalisation.

The Act now exempts the following additional entities from interest restriction:

- Microfinance institutions licensed and non-deposit taking microfinance businesses under the Microfinance Act, 2006;
- Entities licensed under the Hire Purchase Act;
- Non-deposit taking institutions involved in lending and leasing business;
- Companies undertaking the manufacture of human vaccines;
- Companies engaged in manufacturing whose cumulative investment in the preceding five years from the commencement of this provision is at least five billion shillings;
- Companies engaged in manufacturing whose cumulative investment is at least five billion Shillings provided that the investment shall have been made outside Nairobi City County and Mombasa County; and
- Holding companies that are regulated under the Capital Markets Act.

A thinly capitalized company is defined as that whose gross interest paid or payable to related persons and third parties exceeds thirty percent (30%) of the company's earnings before interest, taxes, armortisation and depreciation (EBITAD)

Effective date: 1 July 2022

Income Tax

1.8 Business with preferential tax regime

Change
In order to ensure compliance with the arms-length principle, the Income Tax Act provides guidelines on the taxation of gains or profits arising from transactions between related parties where one person is a resident and the other one is operating in a preferential tax regime. Such transactions would be where the business produces no gains or produces less gains than those which would have been expected to accrue from that business if the business activity was not with a party in a preferential tax regime. The gains or profits of the resident person from that business are deemed to be the amount which would have been expected to accrue if that business had been conducted by an independent person dealing at arm's length, or if none of the parties were located in a preferential tax regime

The Finance Act, 2022 expands the scope such transactions to include where a resident person carries on business with -:

i. a non-resident person located in a preferential tax regime; or
ii. an associated enterprise of a non-resident person located in a preferential tax regime; or
iii. a permanent establishment of a non-resident person operating in Kenya where the non-resident person is located in a preferential tax regime

A preferential tax regime is defined to mean:

i.Any Kenyan legislation, regulation or administrative practice which provides a preferential tax rate to such income of profit, including reductions in the tax rate or the tax base; or
ii. A foreign jurisdiction which;

- Does not tax income
- Taxes income at a rate that is less than 20%
- Does not have framework for exchange of information
- Does not allow access to banking information; or
- Lacks transparency on corporate structure, ownership of legal entities, beneficial ownership or regulatory supervision.

Effective date: 1 January 2023

1.9 Reduced tax rates

The Third Schedule to the Income Tax Act is amended to provide for reduced tax rates on the following income streams

- Carbon market exchange or emission trading systems by companies that have been certified by the Nairobi International Finacial Centre Authority - Tax rate of 15% for the first ten years from the year of commencement
- Shipping Business - tax rate of fifteen per cent for the first ten years from the year of commencement of its operations for a shipping business in Kenya
- Bearer Bond – withholding ax rate of 7.5% on gross interest and deemed interest payable to non-residents arising from a bearer bond issued outside Kenya of at least two years' duration and interest, discount or original issue discount.

Effective date: 1 January 2022

Income Tax

1.10 Additional incomes exempt from taxation

The first schedule is amended to include the following income to be exempt from taxation;

- Deemed interest in respect of an interest free loan advanced to a company undertaking the manufacture of human vaccines.
- Payments made to non-residents service providers not having a permanent establishment in Kenya in respect of services provided to a company undertaking the manufacture of human vaccines.
- Compensating tax accruing to a company undertaking the manufacture of human vaccines.
- Dividends paid by a company undertaking the manufacture of human vaccines to any non-resident person.
- Income of a company undertaking the manufacture of human vaccines.
- Dividends paid by Special Economic Zone enterprises, developers and operators licensed under the Special Economic Zones Act.
- Dividends paid by Special Economic Zones enterprises, developers and operators to any non-resident person.

Effective date: 1 July 2022

1.11 Special Operating Framework Arrangement

A company which;

- is engaged in business under a special operating framework arrangement with the Government;
- incorporated for purposes of undertaking the manufacture of human vaccines ;
- whose capital investment is atleast ten billion shillings

Shall be subject to the rate of tax specified in the special operating framework arrangement with the Government

Effective date: 1 January 2023

Income Tax

1.12 Removed Commissioner's powers to waive / remit penalties and interest for PAYE

Change
The Finance Act, 2022 repeals the provision empowering the Commissioner to remit in whole or in part, any penalty imposed on the employer for failing to deduct, account for and/ or remit PAYE.

Previously , the Commissioner could, and with the prior written approval from the Minister in cases where the amount of penalty remitted was more than Kshs. 500,000 per employer per annum, remit in whole or in part, any penalty imposed.

Effective date: 1 July 2022

1.13 Country by Country Reporting

Change
The threshold for CbCR is a turnover of KES 95 per annum and the commencement date for reporting is 2022 year of income

Effective date: 1 July 2022

1.14 Definitions

The following terms have been included in section 2 of the Income Tax Act and defined as follows:

Fair market value: means the comparable market price available in an open and unrestricted market between independent parties acting at arm's length and under no compulsion to transact, which is expressed in terms of money or money's worth.

Financial derivative: means a financial instrument the value of which is linked to the value of another instrument underlying the transaction which is to be settled at a future date

Permanent home: means a place where an individual resides or which is available to that individual for residential purposes in Kenya, or where in the opinion of the Commissioner the individual's personal or economic interests are closest.
The definition is critical because a permanent home is one of the tests applied in determining the tax residency status for individuals for purposes of taxation in Kenya

Effective date: 1 July 2022

2. Value Added Tax (VAT)

2.1 Claiming input VAT

Change
Section 17 of the VAT Act,2013 has been amended to provided that that input tax should be claimed in a return for the period when the taxable supply or importation of taxable supplies occurred. This created a conflict in the law because the provision that allows for the deductibility of input tax within 6 months after the end of the tax period in which the supply or importation occurred has not been revoked.

Further, there are additional requirements for the Oil Marketers Companies (OMCs) participating in the Open Tender System (OTS)
The scope of documentation required has been expanded in order to claim input tax claimable for imported petroleum products cleared through a non-bonded facility by taxpayers participating in the Open Tender System (OTS). The additional documents required include a custom entry form showing the name, Personal Identification Number (PIN) of the winner of the tender and the name of the other oil marketing company participating in the tender.

However, for input tax incurred prior to the coming into force of this amendment can be claimed within a period of 12 months with effect from 1 July 2022

Effective date: 1 July 2022

2.2 Reduced VAT rate Liquefied Petroleum Gas

The VAT rate on the supply of liquefied petroleum gas including propane has been reduced to eight percent (8%) from the current rate of sixteen percent (16%).

Effective date: 1 July 2022

2.3 Services provided through a Digital Market Place

They are now excluded from the reverse charge VAT.
Persons supplying imported digital services over the internet or an electronic network or through a digital marketplace in respect to a turnover threshold of five million shillings are exempted from VAT registration.

Digital marketplace is defined as an online platform which enables users to sell goods or provide e-services to other users.

Effective date: 1 July 2022

2.4 Refund of excess Input Tax

Manufactures who make taxable supplies to an official aid funded project have been allowed to lodge VAT refund claims accumulated before 1 July 2022 within a period of 12 months

Effective date: 1 July 2022

2.5 Interest & penalty

Change
That imposition of interest and penalty under the VAT Act,2013 will be as per the provisions of the Tax Procedures Act, 2015 .
Interest is subject to induplum rule in that it shall not exceed the principal tax

Effective date: 1 July 2022

2.6 Tax paid in error

Change
The refund of tax paid in error to be governed under Section 47A of the Tax Procedures Act, 2015.

Effective date: 1 July 2022

Value Added Tax

2.7 Change of VAT Status

2.7.1 Exempt to zero-rated

Effective date: 1 July 2022

	Description of Supply	Current Status	Proposed Rate
1.	Fertilizers of Chapter 31	Exempt	Zero Rated
2.	Inputs or raw materials locally purchased or imported by manufacturers of fertilizer as approved from time to time by the Cabinet Secretary for Agriculture	16%	Zero Rated
3.	The exportation of taxable services in respect of business process outsourcing	Exempt	Zero Rated

2.7.2 Standard-rated to Exempt

Effective date: 1 July 2022

	Description of Supply	Current Status	Proposed Rate
1.	Plant and machinery of Chapter 84 and 85imported by manufacturers of pharmaceutical products or investors in manufacture of pharmaceutical products	16%	Exempt
2.	Medical oxygen supplied to registered hospitals	16%	Exempt
3.	Urine bags	16%	Exempt
4.	Adult diapers	16%	Exempt
5.	Artificial breasts	16%	Exempt
6.	Colostomy or ileostomy bags for medical use	16%	Exempt
7.	Sustainable fuel pellets for household and commercial use	16%	Exempt
8.	Inputs and raw materials used in the manufacture of passenger motor vehicles*	16%	Exempt
9.	Locally manufactured passenger motor vehicles	16%	Exempt
10.	Medical oxygen supplied to registered hospitals	16%	Exempt
11.	Taxable goods, inputs and raw materials imported or locally purchased by a company which is (a) engaged in business under a special arrangement with the Government; and (b) incorporated for purposes of undertaking manufacture of human vaccines; and whose capital investment is atleast 10 billion shillings. Subject to approval by CS for Finance on recommendation of the CS for Health, such capital goods the exemption of which the CS may determine to promote investment in the manufacturing sector. Provided that the value of such investment is not less than 2 billion shillings *Locally manufactured passenger vehicle" means a motor vehicle for the transportation of passengers which is manufactured in Kenya by an original equipment manufacturer operating in Kenya*	16%	Exempt

2.7.3 From zero-rated to standard rated

Effective date: 1 July 2022

	Description of Supply	Current Status	Proposed Rate
1.	The supply of articles of apparel, clothing accessories and equipment specially designed for safety or protective purposes for use in registered hospitals and clinics or by county government or local authorities in fire fighting	Zero-rated (0%)	16%

2.7.4 From exempt to standard rated

Effective date: 1 July 2022

	Description of Supply	Current Status	Proposed Rate
1.	Syringes, with or without needles of tariff no. 9018.31.00	Exempt	16%

3. Excise Tax

3.1 Exemption from excise tax

Change

The following supplies are now exempted from excise tax:

- Locally manufactured passenger motor vehicles in order to attract, encourage and retain investment in this sector and enhance competitiveness of locally manufactured passenger motor vehicles.

  "Locally manufactured passenger motor vehicle" means a motor vehicle for the transportation of passengers which is manufactured in Kenya and whose exfactory value comprises atleast 30% of local content
  "Local content" means parts designēd and manufactured in Kenya by an original equipment manufacturer operating in Kenya.

- Neutral spirit imported or purchased locally by registered pharmaceutical manufacturers upon approval by the Commissioner.

Effective date: 1 July 2022

3.2 Interest & penalty for imported goods

Change

Interest and penalty on late payment of excise tax for imported goods to be charged under the Tax Procedures Act 2015 of Kenya.

As per the said Act, late payment penalty is 5% and simple interest of 1% per month

The interest will not exceed the principal tax as per induplum rule

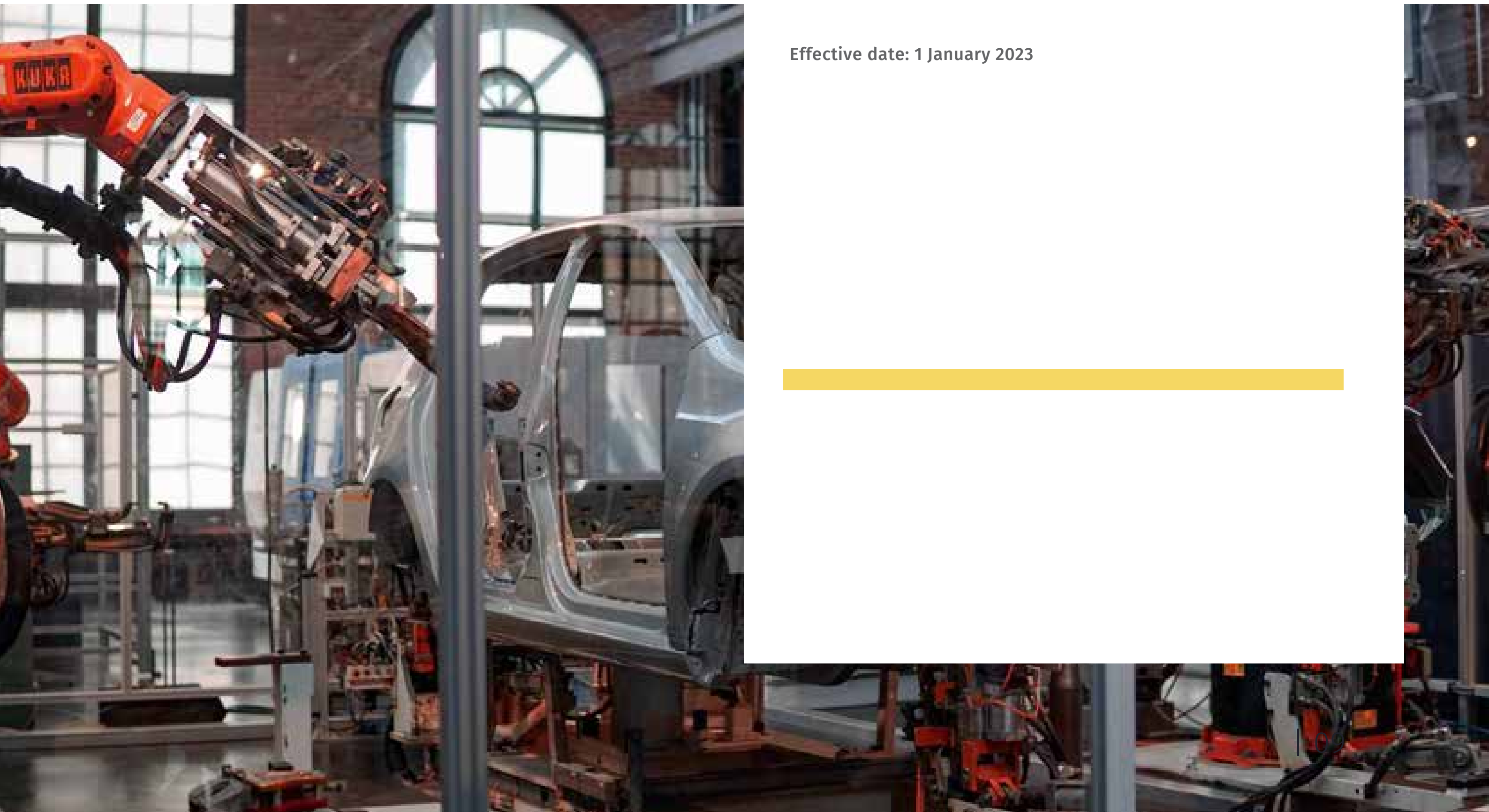
Effective date: 1 July 2022

3.3 Inflationary adjustment

Change

With the approval of the Cabinet Secretary the Commissioner is now empowered to exempt specified products from inflation adjustment after considering the circumstances prevailing in the economy.

Effective date: 1 January 2023



Excise Tax

3.4 Change of Excise tax rates

Effective date: 1 July 2022

	Description	Current Status	Proposed Rate
1.	Beer, Cider, Perry, Mead, Opaque beer and mixture of fermented beverages with nonalcoholic beverages and spirituous beverages of alcoholic strength not exceeding 6%	Sh 121.85 per litre	Sh 134.00 per litre
2.	Fruit juices (including grape must), and vegetable juices, unfermented and not containing added spirit, whether or not containing added sugar or other sweetening matter	Sh 12.17 per litre	Sh 13.30 per litre
3.	Cosmetics and Beauty products of tariff heading No. 3303, 3304, 3305 and 3307	10%	15%
4.	Spirits of undenatured ethyl alcohol; spirits liqueurs and other spirituous beverages of alcoholic strength exceeding 6%r	Sh 278.70 per litre	Sh 335.30 per litre
5.	Wines including fortified wines, and other alcoholic beverages obtained by fermentation of fruits	Sh 208.20 per litre	Sh 229.00 per litre
6.	Other manufactured tobacco and manufactured tobacco substitutes; "homogenous" and "reconstituted tobacco"; tobacco extracts and essences	Sh 9,734.45 per kg	Sh 10,707.88 per kg
7.	Cigars, cheroots, cigarillos, containing tobacco or tobacco substitutes	Sh 13,906.04 per kg	Sh 15,296.60 per kg
8.	"Imported potatoes, potato crisps and potato chips of tariff heading 07.01 and imported potatoes of tariff numbers 0710.10.00, 2004.10.00 and 2005.20.00	NIL	25%
9.	Cigarette with filters (Hinge lid and soft cap)	Sh 3,447.61 per mille	Sh 3,825.99 per mille
10.	Cigarettes without filters (plain cigarettes)	Sh 2,502.74 per mille	Sh 2,752.97 per mille
11.	Imported sugar confectionery of tariff heading 17.04	Sh 36.74 per kg	Sh 40.37 per kg
12.	White chocolate in blocks, slabs or bars of tariff Nos. 1806.31.00, 1806.32.00, 1806.90.00	Sh 209.88 per kg	Sh 242.29 per kg
13	Liquid nicotine for electronic cigarettes	NIL	Sh 70.00 per millilitre
14	Electronic cigarettes and other nicotine delivery devices	NIL	40%
15	Imported potatoes of tariff numbers 0710.10.00, 2004.10.00 and 2005.20.00	NIL	25%
16	Articles of plastic tariff heading 3923.90.90	NIL	10%
17	Product containing nicotine or nicotine substitute intending for inhalation	Sh 1,200 per kg	Sh 2,500 per kg
18	Imported ready to use SIM cards	NIL	Shs 50 per SIM Card
19	Fees charged by digital lenders	NIL	20%
20	Importation of cellular phones	NIL	10%
21	Jewellery of tariff heading 7113, and imported jewellery of tariff heading 7117	10%	15%
22	Imported furniture of any kind used in offices, kitchen, bedroom and other furniture	NIL	25%

4. Tax Procedures Act

4.1 Trusts

Change

All trusts, whether in operation or not are required to notify the Commissioner within 30 days of any changes pertaining the full identity of the trust including the address details of the trustees and beneficiaries of the trust.

Further, it is now mandatory for trusts to have a Personal Identification Number (PIN) during the time of registration.

These changes will effectively enable the Commissioner have more scrutiny on trusts.

Effective date: 1 July 2022

4.2 Agency Notices

Change

Under the provisions of the Tax Procedures Act (TPA), The Commissioner is empowered to collect tax from an agent owing money to the taxpayer by issuing an agency notice to the agent to settle the demanded tax on behalf of a taxpayer.

The time period within which an agent shall respond to the Commissioner on their inability to comply with an agency notice has been increased from 7 days to 14 days from the day of receipt of the agency notice.

Further, the Commissioner shall serve the taxpayer with a copy of the agency notice when serving the agent.

The Agency notice can only be issued after confirming the assessment through an Objection Decision and the tax payer fails to appeal to the Tax Appeals Tribunal within the prescribed timelines.

Effective date: 1 July 2022

4.3 Security on property for unpaid tax

Change

The scope of property to secure unpaid taxes expanded and defined to include: land or building, aircraft, ship, motor vehicle, or any other property which the Commissioner may deem sufficient to serve as security for unpaid taxes

The Commissioner is now empowered to direct in writing the Land Registrar, the Registrar of Ships, Director General of the National Transport and Safety Authority ("NTSA") and any other person who the Commissioner is satisfied has authority to hold Property (collectively referred to as "Registrars") to register securities over properties owned by taxpayers as security for the unpaid tax. The Commissioner will be required to inform the taxpayer of their direction to the registrar within 7 days of the notification

The Commissioner or an authorized officer is now empowered to recover unpaid tax by disposing the property subject to the security if the taxpayer does not pay the unpaid tax within two months of notification. The disposal to recover the unpaid tax would be either by public auction or private treaty. The taxpayer shall be required to bear costs associated with the Commissioner's recovery efforts

Effective date: 1 July 2022

Tax Procedures Act

4.4 Exemption from Withholding VAT regime

Change
manufactures whose value of investment in the preceding three years from 1 July 2022 is at least three billion shillings have been exempted from withholding VAT regime. Meaning, the appointed withholding VAT Agents will not be withholding VAT when making payments to the qualifying manufacturers.

Effective date: 1 July 2022

4.5 Refund of overpaid tax

Change
Where a taxpayer has overpaid a tax under any tax law, the tax payer may apply to the commissioner (a) to offset the overpaid tax against the taxpayer's future tax liabilities or (b) for a refund of the overpaid tax within five years, or six months in the case of VAT,after the date on which the tax was overpaid.

Upon application, the Commissioner may subject a claim to an audit and has to respond to an application for offset or refund within 90 days, else, the application shall be deemed approved.
Should KRA fail to refund the overpaid tax within 2 years of an application, interest will accrue at a rate of 1% per month.

A taxpayer with overpaid instalment taxes can utilize the overpaid instalments against future instalment tax liabilities without subjecting the amount to a refund process. However, where the Commissioner later determines that there was no overpayment of instalment tax, the overpaid instalment taxes used to offset the taxpayer's future instalment shall be treated as a tax due in the subsequent period from the date the Commissioner applied the amount to offset the instalment tax liability.

Effective date: 1 July 2022

4.6 Tax paid in error

Change
Where tax has been paid in error, the Commissioner shall, except as otherwise provided in the Tax Procedures Act or relevant tax law, refund such tax.
Further, the Commissioner may, upon approval by the Cabinet Secretary, refund a tax paid in error in any case where the supply is exempt or zero rated under the Act but such exemption was not processed within the specified period due to circumstances beyond the control of the taxpayer.

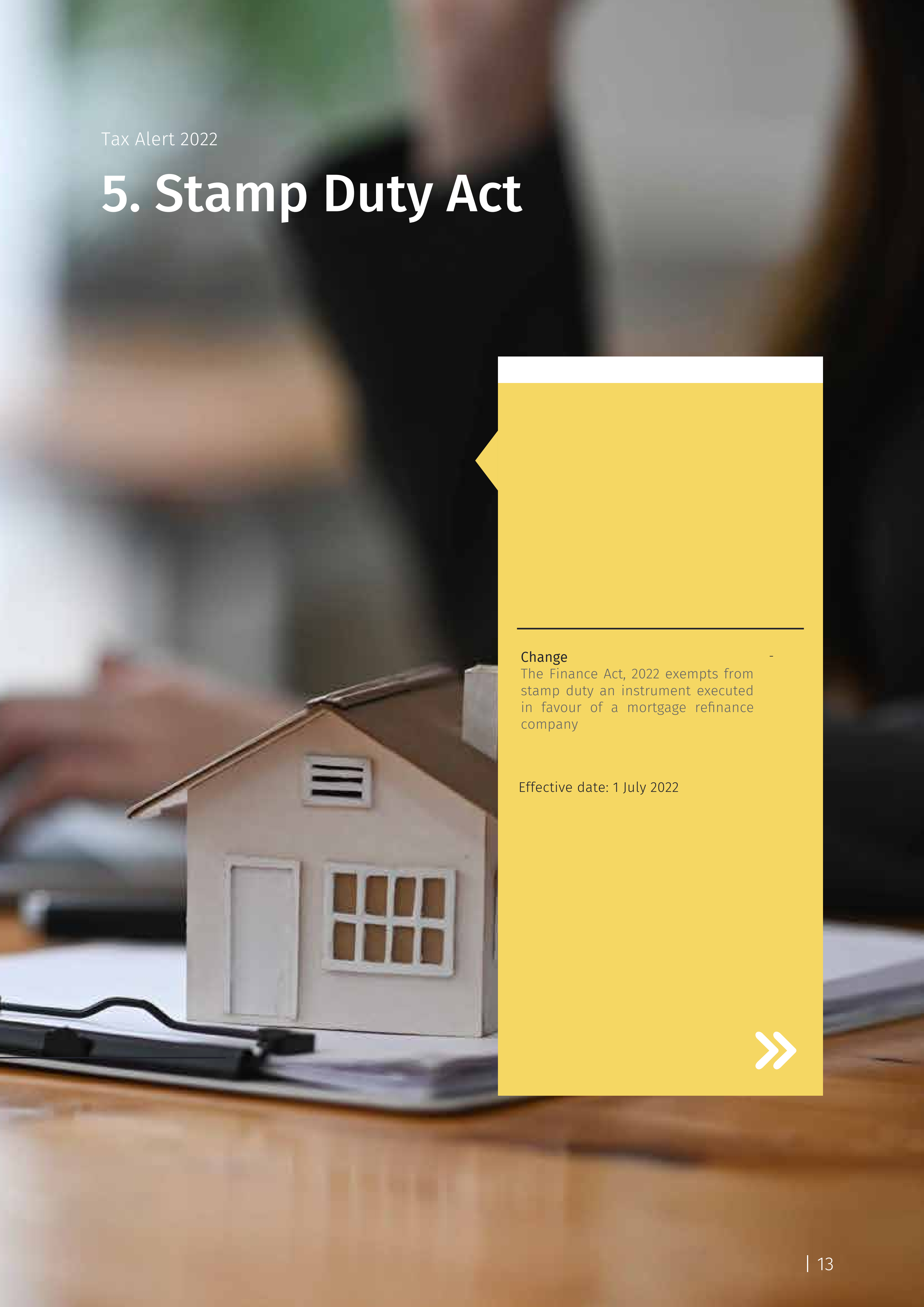
Tax paid in error means any tax which the Commissioner is satisfied ought not to have been paid

Effective date: 1 July 2022

4.7 Timelines for objection decisions and Appeals

Change
The Commissioner is required to communicate to a taxpayer on whether a tax objection is validly lodged to 14 days from the day the objection was filed.
Further, the Commissioner is now compelled to issue an objection decision within 60 days from the date of receipt of a valid notice of objection failure to which the objection shall be deemed to be allowed.
A taxpayer who is dissatisfied with the Commissioner's decision may appeal to the Tribunal within thirty days after being notified of the decision.

Effective date: 1 July 2022



5. Stamp Duty Act

Change

The Finance Act, 2022 exempts from stamp duty an instrument executed in favour of a mortgage refinance company

Effective date: 1 July 2022

Disclaimer

This publication has been prepared for guidance and does not constitute professional advice. Please contact us should you require our support

Commited to the end.

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