A&A

ANCHINGA AND ASSOCIATES

Certified Public Accountants

www.pna.co.ke

KENYA FINANCE BILL 2017/ 2018 UPDATE

The Kenya budget statement speech for the financial year 2017/ 2018 was made on 30th March 2017 by the Cabinet Secretary for the National Treasury, Henry Rotich. This year, the budget was read two months early because parliament has to be dissolved at least 60 days before the General Elections slated for August 8th 2017.

In FY 2017/18, overall expenditure and net lending are projected at KSh 2,627 billion. Development expenditure in FY 2017/18 is projected at KSh 640.3 billion. Revenue collections are projected at Ksh 1,549.4 billion. A mix of domestic & external borrowing plus aid will finance the revenue gap.

From a fiscal perspective, the budget has made proposals for amendments to various tax and related statutes. The objectives of the said amendments are to:

a) Support growth and domestic production;
b) Reduce income inequality;
c) Promote job creation;
d) Improve tax administration and compliance; and
e) Enhance social security and welfare.

The proposed fiscal amendments to aid in realization of the above objectives are discussed below under each tax head. This publication incorporates changes based on the subsequent Finance Bill 2017 that was published in April 2017. Some changes may arise when the Finance Act 2017 is published later this year. Below is our analysis.

VALUE ADDED TAX (VAT) ACT PROPOSED CHANGES		
MEASURE	**CHANGES**	**EFFECTIVE DATE**
Place of Supply of Goods	The Bill proposes changes to the VAT Act on the *place of supply of goods.* Currently, the following three conditions have to be met, for a supply of goods to be considered as made in Kenya: • The goods are delivered or made available in Kenya by the supplier; • The supply of the goods involves their installation or assembly at a place in Kenya; **and** • For goods delivered outside Kenya, the goods were in Kenya when their transportation commenced. Finance Bill 2017 proposes to delete the word "and" and replace it with "or" and therefore a supply of goods will be deemed to be made in Kenya if it meets *any* of the above three criteria and this will widen the VAT tax base for the Kenyan government.	3rd April 2017
VAT Zero-rating	The Bill proposes changes to the Second Schedule of the VAT Act to zero-rate: • Supply of maize (corn) flour, wheat or meslin flour and ordinary bread. Currently VAT-exempt, zero-rating status for these will mean that manufacturers will be able to claim input VAT, thus reducing the VAT payable and improving the bottom-line. • Taxable goods supplied to marine fisheries and fish processors upon recommendation by the relevant state department. Currently vatable at 16%, this incentive will stimulate the development of the *blue economy*, identified as a key potential for untapped economic opportunities.	3rd April 2017
VAT Exemptions	For taxable medical equipment and apparatus for the direct and exclusive use for construction of specialized hospitals with a minimum bed capacity of 50, the Bill seeks to specify the qualifying bed capacity. This is meant to encourage more investments in the healthcare sector, which is currently in need for more qualified personnel and aptly equipped facilities. The 1st Schedule of the Act has been amended to exempt materials, articles and equipment for the educational, scientific or cultural advancement of the disabled (not just the blind, as was	3rd April 2017

previously exempted) for the use of an organisation approved by Government for purposes of exemption.

The Bill proposes to exempt Liquefied Petroleum Gas (LPG), currently zero-rated. Unfortunately, removal of the zero-rated status will mean that manufacturers will not be able to claim input VAT, to reduce the VAT payable, likely leading to an increase in LPG prices as the cost is passed on to the end consumers. Similarly, goods for use in the manufacture of LPG cylinders, currently VATable, used by licensed manufacturers shall be exempt, upon recommendation by the CS responsible for Energy and Petroleum. This is meant to encourage the local manufacture of LPG cylinders which are mainly imported at the moment.

Unused postage, revenue or similar stamps with a recognised face value, stamp-impressed paper, bank-notes, cheque forms, stock, share or bond certificates and similar documents of title, currently VATable, shall be exempt from VAT.

Spare parts imported by aircraft operators or persons carrying on the business of aircraft maintenance upon recommendation by the Kenya Civil Aviation Authority (KCAA). Currently, propellers and related parts and aircraft under-carriage together with related parts are VATable and the Bill proposes to make them VAT exempt. Currently, propellers and related parts and aircraft under-carriage together with related parts are VATable and the Bill proposes to make them VAT exempt.

Inputs for the manufacture of pesticides, currently VATable, shall be exempt, upon recommendation by the Cabinet Secretary for Agriculture.

Further, the Bill seeks to exempt specially designed locally assembled motor vehicles for transportation of tourists, purchased before clearance through Customs by tour operators upon recommendation by the competent authority responsible for tourism promotion, provided the vehicles meet the following conditions:

- the vehicles shall at all times be registered and operated by a company that is licenced under the Tourism Vehicle Regime;
- the vehicles shall be used exclusively for the transportation of tourists;
- the vehicles shall have provisions for camping, rescue and first aid equipment, luggage compartments and communication fittings; and

- any other condition the Commissioner may impose:

The tax on the vehicle shall become applicable upon change of use or disposal of the vehicle for other use. This is intended to revive the tourism industry, which has been in the doldrums in the recent past. However, clarity will be needed on this exemption, as the vehicles are locally assembled yet the provisions refer to imported units. It is our view that the exemption applies to parts imported for the local assembly of vehicles to be used in the tourism sector.

VAT Exemption for Islamic financial products:

With a view to providing uniform application of VAT incentives in the financial sector, the Bill proposes the same treatment of Islamic financial products with the normal non-Islamic products. Therefore, *Sukuk* and *Islamic Finance Return* (treated as interest) will now be VAT exempt.
The Bill proposes changes to both Section 2 of the VAT Act and Section 2 of the Income Tax Act to include the following definitions relating to Islamic Finance:

- *Islamic finance arrangement* to refer to all financial arrangements structured in line with Islamic law.
- *Islamic finance return* to refer to amounts received or paid in relation to Sukuk or an Islamic finance arrangement.
- The definition of *interest* to include *Islamic finance return*

Islamic finance is fast growing, both locally and regionally. Clarity on the treatment of Islamic Finance products and harmonization of the VAT treatment in line with the other financial products will spur uptake of existing funding, both by the private and public sector.

The Bill also seeks to exempt from VAT asset transfers and other transactions related to the transfer of assets into Real Estates Investment Trusts and Asset Backed Securities. This incentive is meant to create tax neutrality in the alternative means that firms may use to raise funds for infrastructure projects.

INCOME TAX ACT PROPOSED CHANGES		
MEASURE	**CHANGES**	**EFFECTIVE DATE**
Allowable Donations	Finance Bill 2017 proposes to allow tax deductions for expenditure incurred in that year of income on donations to the Kenya Red Cross, county governments or any other institution responsible for the management of national disasters to alleviate the effects of a national disaster declared by the President. This move will encourage more donations to be channeled to needy causes, for instance the current drought being faced in some parts of the country.	3rd April 2017
Special Economic Zones (SEZs)	To encourage more investment and also employment opportunities in this sector, the Bill makes the following proposals: • Dividends paid by SEZs, developers or operators to any non-resident person, currently at 10%, shall be exempt from Withholding Tax. • Capital Expenditure by SEZs on buildings and machinery shall qualify for a 100% investment deduction in the year in which the building or machinery is first used. • Reduced Withholding Tax rates shall also be applicable to payments made to non-residents as follows: - Management, professional & training fees (from 20% to 5%) - Royalties (from 20% to 5%) - Interest (from 20% to 5%)	1st January 2018
Preferential Tax Regimes	The Bill further seeks to amend the Income Tax Act to provide for a new section on the ascertainment of gains or profits of business in a preferential tax regime in light of the growth of SEZs, expected to have dealings both within and outside the zones. Where a resident entity operating in a preferential tax regime carries on business with a related resident person not operating in a preferential tax regime and the business produces to the resident person not operating in a preferential tax regime either no profits or less than the ordinary profits which would have been expected to accrue from that business if there had been no such relationships, then, the gains or profits of that resident person from that business shall be deemed to be the amount that might have been expected to accrue if the course of that business had been conducted by independent persons dealing at arm's length. *Preferential tax*	3rd April 2017

regime with respect to an item of income or profit, means any legislation, regulation or administrative practice which provides a preferential rate of taxation to such income or profit, including reductions in the tax rate or the tax base.

This therefore introduces transfer pricing provisions from SEZs, in trade where one entity is in a preferential tax regime and the other one isn't.

PAYE changes

Further to the changes effected in the Finance Act 2016 (effective 1st Jan. 2017), there are proposals to expand PAYE bands by a further 10%.

Proposals for changes to take effect from 1st Jan. 2018 are as follows:

Current Monthly Taxable Pay (KES.)	Proposed Monthly Taxable Pay (KES.)	Tax Rate (%)
Up to 11,180	Up to 12,298	10
Next 10,534	Next 11,587	15
Next 10,534	Next 11,587	20
Next 10,534	Next 11,587	25
Above 42,781	Above 47,059	30
Monthly Relief: KES. 1,280	Monthly Relief: KES. 1,408	

The expansion of income tax bands, together with the exemption of bonuses, overtime and retirement benefits of low income earners will marginally reduce the PAYE burden. Even though this doesn't translate to a 10% PAYE reduction, this will increase the take home income for employees, with a significant impact on low income workers, thus marginally improving their purchasing power and helping mitigate the effects of inflation.

1st January 2018

Corporate Tax on Motor Vehicle Assemblers	Finance Bill 2017 proposes to reduce the corporate tax for companies assembling motor vehicles, from 30% to 15%, applicable for the first five years from the year of commencement of operations. This incentive will boost investor profits and provide more employment opportunities to Kenyans.	1st January 2018
Investment Deductions in the Maritime Sector	There is a proposal to increase the investment deduction on the capital expenditure incurred by industries in the maritime (*blue economy*) sector to 150%, as an incentive for more development into the sector, identified as a key potential for untapped economic opportunities.	1st January 2018
Pension Fund Withdrawals	The Bill proposes to expand the tax bands for the taxation of withdrawals from registered pension funds, provident funds and the National Social Security Fund (NSSF) (before the expiry of fifteen years from the date of joining the fund), for withdrawals in excess of the tax free amounts specified in the Income Tax Act, in a given year. The Bill proposes the same expanded tax bands as those proposed for PAYE in Pg. 6 above.	1st January 2018

EXCISE DUTY ACT PROPOSED CHANGES		
MEASURE	**CHANGES**	**EFFECTIVE DATE**
Licencing of Illuminating Kerosene Usage	Finance Bill 2017 proposes an amendment to the Excise Duty Act to include the use of illuminating kerosene in the manufacturing of paints and resin by registered manufacturers as one of the activities requiring an excise licence in Kenya. This is meant to protect local manufacturers of paint and resin from adulterated kerosene.	3rd April 2017
Excise Duty refund for Spirits and Illuminating Kerosene	The Bill further proposes to make provisions allowing for the refund of excise duty paid for spirits or illuminating kerosene by registered manufacturers upon application to the taxman. This is meant to encourage the local manufacture of paints and resins.	3rd April 2017
Excise Rate Changes	The rate of Excise duty on alcoholic spirits has been increased from KES. 175 per litre to KES. 200 per litre. This is commensurate with the alcohol consumption trends in the country where the demand for spirit is ever increasing. However, this might inadvertently lead to increased	3rd April 2017

<table>
<tr>
<td></td>
<td>consumption of illicit liquor amongst low income consumers, as manufacturers pass the additional tax burden on to them.

The rate of excise duty on cigarettes has been reviewed from the single rate of KES. 2500 per mille to a two tier tax structure follows:

<table>
<tr><th>Description</th><th>Rate of Duty (KES./Mille)</th></tr>
<tr><td>Cigarettes with filters (hinge lid and soft cap)</td><td>2500</td></tr>
<tr><td>Cigarettes without filter (plain cigarettes)</td><td>1800</td></tr>
</table>

This will enhance equity in the excise taxation of the tobacco industry.</td>
<td></td>
</tr>
<tr>
<td>Other Excise Duty Changes</td>
<td>The Excise Duty Act has also been amended to define powdered beer as follows: any powder, crystals or any other dry substance which, after being mixed with water or any other nonalcoholic beverage, ferments to, or otherwise becomes an alcoholic beverage.

Goods imported or purchased locally by both the Kenya Red Cross and St. John Ambulance for official use in the provision of relief services in Kenya shall be exempt from Excise Duty. Initially granted to the Kenya Red cross, the inclusion of St John Ambulance in the exemption is meant to recognize the importance of these relief services and facilitate the same.

As an exempt excisable good, returning residents will now be allowed to buy a new right hand vehicle whose current retail selling price shall not exceed that of the previously owned left-hand drive vehicle in a foreign jusrisdiction. This is meant to address the challenges faced by Kenyans in the diaspora when replacing their vehicles upon returning to the country.

The Act has also been amended to include both imported and locally purchased goods, for the direct use in the manufacture of sanitary towels, as exempt from excise duty. This is aimed at cushioning local manufacturers from undue competition from imported products.</td>
<td>3rd April 2017</td>
</tr>
</table>

TAX PROCEDURES ACT (TPA) CHANGES		
MEASURE	**CHANGES**	**EFFECTIVE DATE**
Tax Amnesty Extension on Voluntarily Declared Offshore Income	Through the Finance Act 2016, taxpayers were granted an amnesty for 2016 and prior years of income on principal taxes, penalties and interest on undeclared foreign income, on condition that they file their 2016 return, with full declarations, by 31st December 2017. The Kenya Revenue Authority (KRA) subsequently issued guidelines on the operationalization of these guidelines, albeit met with some administrative challenges. In his budget statement, the CS instructed the KRA to revisit and issue clearer guidelines, hence a deadline extension from 31st December 2017 to 30th June 2018. Through this initiative, the taxman will be able to widen the tax base by bringing other taxpayers into the tax net, thus helping the government meet its revenue targets.	3rd April 2017
Enhancing powers of KRA Officers	The Bill also proposes to enhance the powers of KRA offices by introducing a section which gives them power to enter and search any premises or vessels and seize, collect and detain evidence and produce such evidence in any proceedings before a court of law or tax appeals tribunal. As per the current law, the Tax Procedures Act does not offer the officers the power to use evidence obtained, in a court of law and this is meant to ease the initiation and speedy conclusion of cases investigated, without having to involve the police.	3rd April 2017
Amendments to Withholding VAT (WHVAT)	The Bill proposes to make the following changes touching on WHVAT: • A supplier may be exempted from WHVAT requirements if they sufficiently demonstrate that due to the nature of his business, and due to the WHVAT application, they are going to be in a continuous credit position for a period of more than twenty-four months. • WHVAT withheld shall be remitted to the KRA within 14 days after the tax is deducted (currently due by the 20th of the following month). • Failure to withhold the whole amount due or failure to remit within 14 days of withholding shall now constitute an offence.	3rd April 2017
Meaning of *tax liability*	The current definition of a *tax liability* in the TPA excludes penalties relating to the same liability and the Bill proposes to include *penalty* as part of the same.	3rd April 2017

<table>
<tr><th colspan="3">MISCELLANEOUS CHANGES</th></tr>
<tr><th>MEASURE</th><th>CHANGES</th><th>EFFECTIVE DATE</th></tr>
<tr><td>Betting, Lotteries & Gaming Taxes</td><td>Finance Bill 2017 proposes to amend the current taxation of betting, lotteries, gaming and prize competitions as follows:
<table>
<tr><th>Tax Head</th><th>Current Tax Rate</th><th>Proposed Tax Rate</th></tr>
<tr><td>Betting Tax</td><td>7.5% of the betting revenue, with gaming revenue being gross turnover minus the amount paid out as winnings.</td><td>50% of the betting revenue, with gaming revenue being gross turnover minus the amount paid out as winnings.</td></tr>
<tr><td>Lottery Tax</td><td>5% of a lottery's turnover.</td><td>50% of a lottery's turnover.</td></tr>
<tr><td>Gaming Tax</td><td>12% of gaming revenue</td><td>50% of gaming revenue</td></tr>
<tr><td>Prize Competition Tax</td><td>15% of the turnover</td><td>50% of the turnover</td></tr>
</table>
This proposal has been met with harsh criticism from the industry players as the taxman aims to get a bigger slice of the exponentially growing sector whilst other related stakeholders influence the higher taxation as a means of mitigating against the societal ills of partaking in these competitions. We await to see if these changes will take effect in the Finance Act 2017 or if alternatives will be offered.</td><td>1st January 2018</td></tr>
<tr><td>Other Miscellaneous Changes</td><td>Finance Bill 2017 further makes changes to the following Acts:
The Stamp Duty Act, Public Finance Management Act, Co-operative Societies Act and the</td><td>Various</td></tr>
</table>

	Sacco Societies Act, to allow for the recognition of Islamic Financial products. • The Retirement Benefits Authority (RBA) Act to increase the powers of the RBA and introduce new compliance requirements. • The Tax Appeals Tribunal Act to clarify the timelines for the hearing of appeals. • The Public Procurement and Asset Disposal Act to bolster the Public Procurement Regulatory Review Board.	

This publication incorporates changes based on the Kenya Finance Bill 2017. Some changes may arise when the Finance Act 2017, currently in its third reading in Parliament, is published later in the year.

TALK TO US TODAY

For further information or assistance, please get in touch with us through the contacts below:

Peter Anchinga,
Anchinga & Associates,
Office Lines: +254 700 16 16 99, +254 780 16 16 99
Mobile: +254 722 72 15 50
Email: anchinga@pna.co.ke or info@pna.co.ke
Web: www.pna.co.ke

DISCLAIMER:

This publication contains the 2017/18 Kenya Finance Bill information in summary form and is therefore intended for general information purposes and guidance only. It is not a substitute for detailed research or the exercise of professional judgment. It is also not meant to address the circumstances of any particular individual or entity nor is it intended to serve as substitute for any professional services required. Anchinga & Associates cannot accept any responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication. Please consult your professional tax advisor to ascertain that the information contained herein applies to your pertinent circumstances.