Finance Bill 2017 Analysis

April 2017

<table>
<tr><th>Focus area</th><th>Proposed change and KPMG comments</th><th>Effective date</th></tr>
<tr><td>Taxation of Islamic Financial Arrangement
Proposed amendment to Section 2</td><td>The Bill proposes to make amendments to Section 2 to include definitions relating to Islamic banking:
- Islamic finance arrangement to refer to all financial arrangements that are structured in accordance with Islamic law
- Islamic finance return to mean any amount received or paid in relation to Sukuk or an Islamic finance arrangement
- The definition of interest to be expanded to include Islamic finance return, which was previously not provided for
The amendments to the ITA will provide clarity on the taxation of Islamic banking products which are fast becoming a major source of funding for development worldwide. Locally, the government is looking to tap into Islamic Finance as an alternative source of funds for development projects.
These provisions are replicated in the changes that the Finance Bill has proposed to the VAT Act, 2013.</td><td>3 April 2017</td></tr>
<tr><td>Deductible donations
Proposed amendment to Section 15(2)</td><td>Currently, donations are only allowable if they meet the Income Tax (Charitable Donations) Regulations, 2007. Key among the conditions in the Regulations is that the donation should be in cash and that it should be made to a charitable organisation with an exemption certificate from the Kenya Revenue Authority (KRA).
The Bill proposes to allow tax deductions for donations made to the Kenya Red Cross, County Governments or other national disaster management bodies to alleviate the effects of calamities which have been declared national disasters by the President.</td><td>3 April 2017</td></tr>
<tr><td>Ascertainment of gains or profits of business in a non-preferential tax regime
Section 18 of the ITA</td><td>As a result of the promotion of special economic zones (SEZs) whose scope will cover a wide spectrum of economic activities, there will be significant transactions between entities within and those outside the zones. The Bill proposes to introduce a new section, 18A, to provide for the pricing of transactions between related resident entities, where one of the entities is based in a preferential tax regime, and the other does not. These entities are required to operate at arm's length.
Where the gains attributed to the entity operating outside the preferential tax regime are deemed to be understated, the KRA will have the power to adjust the gains to reflect the gains that would be expected if the entities were transacting on an arm's length basis. This provision, effectively introduces transfer pricing provisions for local companies where one company is located in a preferential tax regime and the other is not.</td><td>3 April 2017</td></tr>
<tr><td>Changes affecting Special economic zones:</td><td>The Finance Bill includes a number of provisions which are designed to encourage investment in the special economic zones. These are as follows:
▪ Dividends paid by SEZ Enterprises, Developers or Operators to non-resident persons are exempt from withholding tax (First Schedule to the ITA).
▪ Capital expenditure by a SEZ enterprise on the construction of a building or on the purchase and installation of machinery for use by the enterprise in carrying out its business are eligible for 100% investment deduction in the first year of use (Paragraph 24C of the Second Schedule to the ITA).
▪ Preferential withholding tax rates for payments to non-resident persons as follows (Third Schedule):
<table>
<tr><th></th><th>Current non-resident rate (%)</th><th>Proposed SEZ rate (%)</th></tr>
<tr><td>Management, professional and training fees</td><td>20</td><td>5</td></tr>
<tr><td>Royalties</td><td>20</td><td>5</td></tr>
<tr><td>Interest</td><td>15</td><td>5</td></tr>
</table></td><td>1 January 2018</td></tr>
<tr><td>Reduction of tax rate for motor vehicle assemblers (Third Schedule)</td><td>The Bill proposes a reduced corporation tax rate of 15% for companies incorporated to carry out local assembly of motor vehicles. The reduced rate is applicable for the first five years from the commencement of operations</td><td>1 January 2018</td></tr>
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Pay As You Earn (PAYE) Changes

Focus area	Proposed change and KPMG comments	Effective date
Enhancement of PAYE tax bands by a further 10%	For the second year in a row, the Cabinet Secretary has proposed to expand the Individual PAYE bands by 10%. This follows an expansion of the bands by a similar margin with effect from 1 January 2017. The new bands are as follows: The above changes will provide a welcome cushion to taxpayers whose income has been adversely affected by inflation.	1 January 2018
Enhancement of Personal Relief by a further 10%	Similarly, the personal relief has increased by a 10% from ***KES 15,360*** p.a. to ***KES 16,896*** p.a. Following the change, the lowest taxable income will increase from ***KES 12,260*** p.m. to ***KES 13,486*** p.m.	1 January 2018
Enhancement of tax rates in respect of payments or withdrawals from pensions	In line with the changes to the PAYE bands, the Bill proposes to enhance the tax bands for taxation of withdrawals from NSSF, registered pension funds and provident funds (before the expiry of fifteen years from the date of joining the fund) where the withdrawals are in excess of the tax-free amounts specified under Section 8(4) and 8(5) of the Income Tax Act, in any one year. The new tax bands for withdrawals in excess of the tax free amount, will be as follows:	1 January 2018

PAYE tax bands:

New bands (KES)	Old bands (KES)	Rate
First 147,580	First 134,165	10%
Next 139,043	Next 126,403	15%
Next 139,043	Next 139,043	20%
Next 139,043	Next 139,043	25%
Over 564,709	Over 513,374	30%

Pension withdrawal tax bands:

New bands (KES)	Old bands (KES)	Rate
First 147,580	First 121,968	10%
Next 139,043	Next 114,912	15%
Next 139,043	Next 114,912	20%
Next 139,043	Next 114,912	25%
Over 564,709	Over 466,704	30%

Changes to the Tax Procedures Act

Focus area	Proposed change and KPMG comments	Effective date
Enhancing powers of an Authorised Officer	The Finance Bill, 2017 proposes to enhance the powers of an Authorised Officer as contained in Section 7 of the Tax Procedures Act, 2015 (TPA) by introducing a Subsection 2 which gives KRA officers **power to enter and search any premises or vessels and seize, collect and detain evidence and produce the evidence in any proceedings before a Court of Law or Tax Appeals Tribunal**. Currently, the TPA offers Authorised Officers all the powers, rights, privileges and protection of a Police Officer in the performance of their duties but does not expressly authorize the use of the evidence gathered by the Authorised Officers in a judicial or quasi-judicial process.	3 April 2017
Tax amnesty on voluntary declaration of offshore income	The Bill proposes to extend the amnesty deadline for voluntary declaration of taxable offshore income by 6 months from 31 December 2017 to 30 June 2018. Self-Assessment Returns for year of income 2016 and prior should be filed by 30 June 2018 to qualify for the amnesty. Further, the Bill introduces a new condition that the voluntarily income should be repatriated to Kenya as part of the amnesty application.	3 April 2017
Withholding VAT (WHVAT)	The Finance Bill has proposed the following changes to WHVAT: ● Exemption from WHVAT requirements where a supplier proves to the Commissioner that they are likely to be in a credit position for more than 24 months due to the nature of their business and imposition WHVAT obligation. ● WHVAT is to be remitted to the KRA within 14 days from the date the tax is deducted. The practice has been to remit WHVAT by the 20th of the month following the month of deduction. ● Failure to withhold and/or remit WHVAT deducted within the 14 days is now an offence.	3 April 2017
Clarification of the meaning of 'tax liability'	The TPA defines tax liability to include any late payment interest payable in respect of a tax liability. This definition excludes penalties relating to the tax liability. The Bill proposes to include penalties accruing from the tax liability by expanding the definitions as follows: ***a tax liability of a taxpayer includes any penalty or late payment interest payable in respect of the liability.'***	3 April 2017

Value Added Tax Changes

Focus area	Proposed change and KPMG comments	Effective date
Place of supply of goods (Section 11)	The Bill proposes to amend Section 11(b) on the place of supply for goods. Previously, for goods to have been deemed to be supplied in Kenya, the supply had to meet the following three conditions: - The goods are delivered in Kenya; - The supply involves installation or assembly of goods at a place in Kenya *and* - Where the goods are delivered outside Kenya, the goods were in Kenya when their transportation commenced The Finance Bill proposes to delete the word "*and*" and replace it with '*or'.* Following the change, a supply of goods will be deemed to be made in Kenya if it meets any of the above three conditions.	3 April 2017
Exemptions from VAT	First Schedule of the VAT Act has been amended to exempt a number of transactions from VAT as follows:	3 April 2017

Particulars	New rate	Old rate
Taxable equipment and apparatus for the direct and exclusive use for construction of specialized hospitals with at least 50 beds capacity. Previously the exemption did not specify the bed capacity.	Exempt	Exempt
Materials, articles and equipment, including motor vehicles intended for the educational, scientific or cultural advancement of the disabled for the use of an organisation approved by the national Government for purposes of exemption. Previously the exemption only applied to materials, articles and equipment for use by the blind.	Exempt	16%
Liquefied Petroleum Gas (LPG) is now exempt while previously it was zero-rated. As a result of the change, marketers will not be eligible for deduction of input VAT incurred to make the supply. It is expected that they will pass on the cost to customers resulting in possible increases to the price of LPG.	Exempt	0%
Taxable goods for use in the manufacture of LPG cylinders by licensed manufacturers upon recommendation by the CS responsible for Energy and Petroleum	Exempt	16%
Unused postage, revenue or similar stamps with a recognised face value, stamp-impressed paper, bank-notes, cheque forms and documents of title such as stock, share or bond certificates.	Exempt	16%
Spare parts imported by aircraft operators or persons carrying on the business of aircraft maintenance upon recommendation by the Kenya Civil Aviation Authority (KCAA). Previously the exemption did not include propellers and related parts and aircraft under-carriage together with related parts. These are now covered. The change also requires that importers obtain recommendation from the KCAA to benefit from the exemption.	Exempt	16% and Exempt
Inputs for the manufacture of pesticides upon recommendation by the Cabinet Secretary for Agriculture	Exempt	16%
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 vehicle 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 Tax on the vehicle shall become payable upon change of use or disposal of the vehicle for other use. While the above exemption may lead to reduction in the cost of the vehicles. It is also contradictory since the vehicles are to be locally assembled yet the exemption applied on imported vehicles. It is likely the intention was to exempt parts for the local assembly of tourist transportation vehicles.	Exempt	16%

Value Added Tax Changes continued…

Focus area	Proposed change and KPMG comments	Effective date
Exempt services	The Finance Bill proposes to amend Part II of the First Schedule to the VAT Act that deals with Exempt services to exempt the following supplies from VAT: ▪ Asset transfers and other transactions related to the transfer of assets into Real Estate Investment Trusts and Asset backed Securities as Paragraph (n); ▪ The Finance Bill has clarified that financial services which are structured to conform to Islamic Finance principles.	3 April 2017
Zero-rating	The Finance Bill has amended the Second Schedule to the VAT Act to zero-rated the following products:	

Particulars	New rate	Old rate
Supply of maize (corn) flour, wheat or meslin flour and ordinary bread	Zero rate	Exempt
Taxable goods supplied to marine fisheries and fish processors upon recommendation of relevant state departments	Zero rated	16%

Excise Duty Provisions

Focus area	Proposed change and KPMG comments	Effective date
Section 15 of the Excise Duty Act Activities requiring a license in Kenya	Finance Bill proposes to amend Paragraph 15(1)(d) to the Excise Duty Act, 2015 (Excise Duty Act) to include illuminating kerosene for use in products manufactured in Kenya. Following the amendment, manufacturers who use illuminating kerosene to produce un-excisable goods will be expected to apply to the Commissioner for a licence.	3 April 2017
Section 29 of the Excise Duty Act. Refund of excise duty	The Finance Bill proposes to delete Paragraph 29(b) to the Excise Duty Act and substitute it with a provision allowing the refund of excise duty paid in respect of spirits or illuminating kerosene used by a licensed or registered manufacturer to manufacture un-excisable goods upon written application to the Commissioner. This is an incentive that aims to promote the competitiveness of locally manufactured paints and resins.	3 April 2017
First Schedule of the Excise Duty Act Excise Duty Changes	The following are changes to the First Schedule to the Excise Duty Act: (see table below) Amending Part III to expand the definition of powdered beer to include any powder, crystals or any other dry substance which, after being mixed with water or any other non-alcoholic beverages, ferments to, or otherwise becomes an alcoholic beverage.	3 April 2017
Second Schedule of the Excise Duty Act Excise Duty Changes	Amending paragraph 5 of part A by inserting the wording 'or St John's Ambulance' immediately after the words Kenya Red Cross. Paragraph 5 provides that excisable goods imported or purchased by Kenya Red Cross for official use in the provision of relief services in Kenya will be exempt from Excise Duty. This amendment is intended to recognize and facilitate the St John Ambulance plays in responding to emergencies.	3 April 2017
Paragraph 10 of the Excise Duty Act	Amending paragraph 10 of the Second Schedule to the Excise Duty Act which provides exemptions on excise duty for excisable goods imported for direct use in the manufacture of sanitary towels to include 'or purchased locally' immediately after the word imported. This now provides that goods purchased locally and used in the manufacture of sanitary towels are exempt from Excise Duty, and is aimed at lowering the cost of the sanitary products.	3 April 2017

Particulars	New rate	Old rate
Spirits of un-denatured ethyl alcohol; spirit liqueurs and other spirituous beverages of alcoholic strength exceeding 10%	KES 200 per Litre	KES 175 per Litre
Cigarettes without filters	KES 1,800 per mille	KES 2,500 per Mille

Miscellaneous Provisions

Focus area	Proposed change and KPMG comments	Effective date
Taxation of the Gambling Industry Sections 29A(1), 44A(1), 55A(1) and 59B(1) of the Betting, Lotteries and Gaming Act	The proposed amendment raises the taxes for betting, lottery, gaming and competition from the current rates of 7.5%, 5%, 12% and 15% to a uniform tax rate of 50%. This tax shall be chargeable to betting and gaming companies and it remains to be seen whether the 50% tax will be in addition to the normal corporation tax of 30%. The move is an attempt by the Cabinet Secretary to the Treasury to cash in on the phenomenal growth that this industry has experienced in the recent past.	1 January 2018
Recognition of Islamic financial products Sections 2, 5, 27, 68A, 96B and Paragraph 4 of the Schedule to the Stamp Duty Act; Section 2, 205 (3A) & (3B) of the Public Finance Management Act; Section 4 of the Co-operative Societies Act and 2, 23 & 68 of the SACCO Societies Act	The proposed amendments relate to inclusion of various definitions and Sharia compliant products in the substantive laws to facilitate the operationalization of Islamic financial products in Kenya, these include amendments to: a) ***The Stamp Duty, Act*** – amendment intended to create tax neutrality for Islamic financial products to enable them favourably compete with other conventional financial products in the Kenyan market; b) ***The Public Finance Management Act*** - amendment intended to create tax neutrality for Islamic financial bonds to enable them favourably compete with other conventional bonds in the Kenyan market; c) ***The Co-operative Societies Act*** - amendment seeks to address the lack of recognition of Islamic financing in the cooperative sub-sector of the Kenyan market; and d) ***The SACCO Societies Act*** - amendment intended to define "deposits" and "deposit taking SACCO business" to include the principles of Islamic law for recognition of Islamic SACCOs in Kenya.	1 January 2018 1 July 2017 1 January 2018 1 January 2018
Increased Powers of the RBA and additional compliance requirements Section 5, 26 and 34 of the Retirement Benefit Act	The objects and functions of the Retirement Benefit Authority are proposed to include the approval of the remuneration of the trustees as approved by the members during the annual general meeting to be held every three years. There is also a proposed amendment that requires a person who fails to submit any statutory return by the due date to the Authority to pay a penalty of ***KES 100,000*** and a further fine of ***KES 1,000*** for each day or part thereof during which the offence continues and where the return remain un-submitted. This additional functions and penalties are intended to ensure that the RBA has a clear indication as to how the operations of a retirement scheme are being carried out.	1 January 2018
Appeals under the Tax Tribunal Proviso to Section 13(7) of the Tax Appeals Tribunal Act, 2013	The Tax Appeals Tribunal Act provides that the Tribunal can hear and determine an appeal within ninety days from the date the appeal is filed with the Tribunal, ***provided that during the period of one year from the date of its first sitting, the Tribunal may extend the period for the hearing an appeal for a period of up to sixty days if there are sufficient grounds to do so.*** Since the Tribunal has been in existence for over a year, this proviso is no longer relevant hence its deletion.	1 January 2018
Strengthening of the Public Procurement and Asset Disposal Act, 2015 Sections 10, 29 and 114 of the Public	The Public Procurement and Asset Disposal Act, 2015 is proposed to be amended to address the three main issues that are critical to the successful implementation of the Act: 1) The composition of the Public Procurement Regulatory Review Board; 2) The composition of the Public Procurement Review Board; and 3) The introduction of specially permitted procurement method as an alternative procurement method.	1 July 2017

Miscellaneous Provisions continued…

Procurement and Asset Disposal Act, 2015	While the reconstitution of the two Boards is aimed at addressing the Constitutional challenges with regards to gender balance and public participation, the specially permitted procurement may be seen as a way of enabling public entities to procure outside the Act and this will definitely have its own challenges. The procedures for the special procurement will be prescribed by the Cabinet Secretary to the National Treasury.	
Exemption from export levy and IDF **Part II of the First Schedule and item (ii) of Part A of the Second Schedule to the Miscellaneous Fees and Levies Act, 2016**	The proposed amendment is aimed at exempting Special Economic Zone Enterprises from export duty and Import Declaration Fees.	1 January 2018

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