ALN KENYA
Anjarwalla & Khanna

Proposed Tax Changes Under The Finance Bill, 2022

LEGAL ALERT

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Introduction

The Finance Bill, 2022 (the **Bill**) was published and gazetted on 8 April 2022. The Bill proposes to make amendments to a raft of tax-related laws in Kenya, including the Income Tax Act (Chapter 470, Laws of Kenya), the Value Added Tax Act, 2013, the Tax Procedures Act, 2015, the Miscellaneous Fees and Levies Act, 2016 and the Excise Duty Act, 2015, among others. Additionally, the Bill proposes changes to other statutes such as the Capital Markets Act, the Insurance Act, the Unclaimed Financial Assets Act, the Statutory Instruments Act and the Evidence Act.

Generally, bills come into effect either on the date of assent by the President or on the date of operation specified within the bill, whichever is earlier. We note that in the Bill, some of the proposed amendments, particularly those relating to income tax, have an effective date of 1 January 2023, while majority of the other proposed amendments have been indicated to come into force on 1 July 2022.

The proposals in the Bill can be seen to target an increased tax base with the proposed introduction of income tax on gains received by non-residents from financial derivatives and a proposed increase in the rate of tax for Capital Gains Tax and Digital Services Tax. Further, the Bill has proposed an increase in excise duty rates for certain products. We have also seen that some amendments in the Bill are for purposes of streamlining the amendments that were introduced by the Finance Act, 2021.

It should be noted that the National Assembly has requested comments on the Finance Bill 2022 prior to enactment into law. The comments should be received by the Clerk to the National Assembly on or before 4 May 2022.

We summarise, in this legal alert, the key proposed amendments in the Bill as well as their potential impact to businesses in Kenya.

1. Amendments to The Income Tax Act, Chapter 470, Laws of Kenya (ITA)

a) Casting a wider net on income tax on financial derivatives for non-residents

Proposed Effective Date: 1 January 2023

The Bill proposes to amend the ITA to the effect of introducing income tax to gains or profits derived by non-resident persons from financial derivatives. To this end, the Bill proposes that any gains accruing to non-resident persons from a financial derivative contract with a resident person shall be subject to withholding tax at the rate of 15% of the gains earned. In this regard, the Bill has proposed to introduce a new definition of a "financial derivative" as "*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*."

This proposal is aimed at increasing government revenue by targeting gains and profits made by non-resident persons trading in financial derivatives in Kenya, including hedging, futures, and options.

The Bill also proposes that the Cabinet Secretary for National Treasury and Planning (the **Cabinet Secretary**) shall publish regulations to govern the implementation of these provisions. We further note that the proposed amendments refer to "gains" and not "income", and it is not clear how the gains would be computed or ascertained. It is hoped that the Regulations which will be issued by the Cabinet Secretary will clarify this issue.

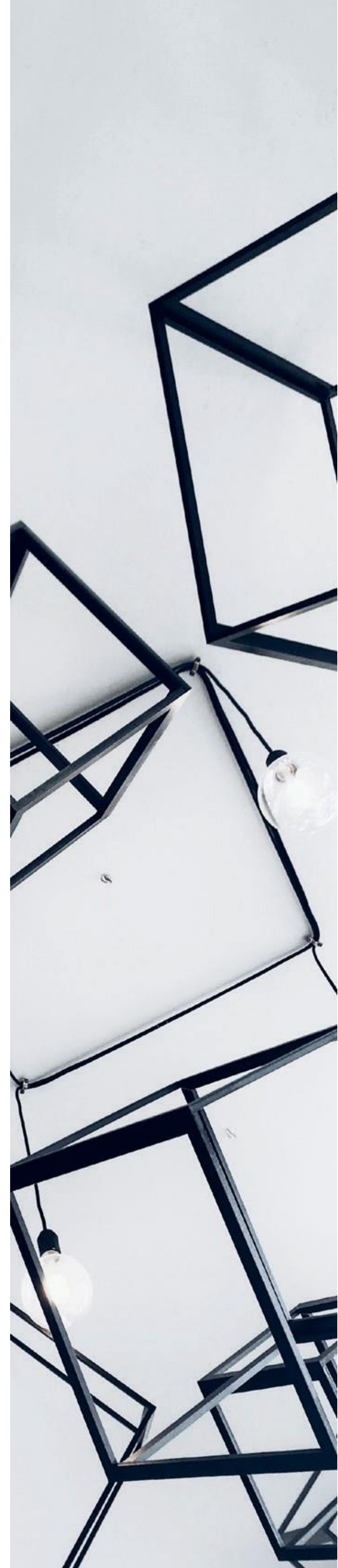
b) Permanent Home defined in the ITA

Proposed Effective Date: 1 July 2022

Currently, the ITA provides that one of the tests to determine whether an individual is tax resident in Kenya, is whether the individual has a "permanent home" in Kenya and was present in Kenya in that year of income under consideration. However, the term "permanent home" is not defined under the ITA. The Bill proposes to introduce a definition for the term to mean "*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*."

This definition codifies into law the meaning of a "permanent home" since taxpayers have been relying on the definitions provided under double tax treaties and case law.

Nonetheless, the proposed definition would need to be considered carefully, depending on the circumstances of each individual. For example, it would be important to understand whether an individual would be required to own a home or whether a home owned by a third party may be deemed to be a "permanent home" if it is available for exclusive use by an individual. Case law in foreign jurisdictions such as the UK (which would be persuasive to Kenyan courts) would provide guidance on interpretation of these provisions.



c) Aligning the EBITDA test on the treatment of deferred foreign losses

Proposed Effective Date: 1 July 2022

Currently, the ITA provides that foreign exchange (**forex**) losses realised by a business in Kenya shall be deemed to be deductible expenses in the computation of gains and profits of a business in that year of income when the loss was realised. However, the ITA provides that forex losses shall be deferred and therefore not taken into account in that year of income where the forex loss realised by a company in respect to a loan from a person who is in control of that company, and the highest amount of all loans by that company outstanding at any time in the year of income is in line with the 3:1 debt to equity ratio.

The Finance Act, 2021 amended the ITA and the provisions relating to thin capitalisation restrictions were amended from the 3:1 debt to equity ratio test to 30% of earnings before interest taxes depreciation and amortisation (**EBITDA**). The Bill now proposes to align the provision on deferring of forex losses arising from loans from a person in control of a company, to comply with the EBITDA test as opposed to the 3:1 debt to equity ratio.

d) Taxation of Employer Share Ownership Plans redefined

Proposed Effective Date: 1 July 2022

The Bill proposes to amend the ITA provisions relating to taxation of Employer Share Ownership Plans (**ESOPs**) in relation to computing the taxable value of the benefit accrued from such arrangements. Currently, the ITA provides that the taxable benefit accruing to an employee under an ESOP shall be the difference between the market value per share and the offer price per share at the date the option is granted by the employer for ESOPs registered by the Commissioner as a Collective Investment Scheme. The benefit is deemed to accrue at the end of the vesting period.

The Bill proposes to amend this provision in relation to taxation of employment benefit arising from ESOPs. Under the proposed amendments, the value of the taxable benefit shall be the difference between 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, the Bill proposes that the tax point on the benefit shall be the date the employee exercises the option, but not the vesting date.

This proposal seeks to eliminate the vesting period requirements. Under the ITA, the benefit would accrue on the employee at the end of vesting period even when the employee has not exercised the option. Further, if this proposal is passed, the tax treatment for registered and unregistered ESOPs shall be accorded similar tax treatments.

e) Repeal of reliefs provided to beneficiaries of registered trusts

Proposed Effective Date: 1 July 2022

The Finance Act, 2021 introduced various reliefs with regards to income from registered trusts including an exemption from tax on the following:

i) funds received by beneficiaries for the purpose of education, medical treatment or early adulthood housing;
ii) income of a registered family trust;
iii) income paid to a beneficiary which is collectively below KES 10 million in a year of income; and
iv) any other amount as may be prescribed by the Commissioner of Domestic Taxes from time to time.

Notwithstanding that the above exemptions were introduced barely a year ago, the Bill proposes to repeal the exemptions effective 1 July 2022. However, we note that the exemptions in relation to capital gains tax and stamp duty on transfer of immovable property to a family trust have been retained. This means that should the Bill be passed into law as is, income of a registered family trust would not be exempt from income tax and the income of the trust would be assessed on the trustees.

However, with the withdrawal of the income tax exemption for registered trusts, it would have been expected that the 25% tax rate imposed on distributions to beneficiaries of registered family trusts would have been repealed as well, as there would be a risk of income being taxed on beneficiaries whilst it has already been taxed on trustees.

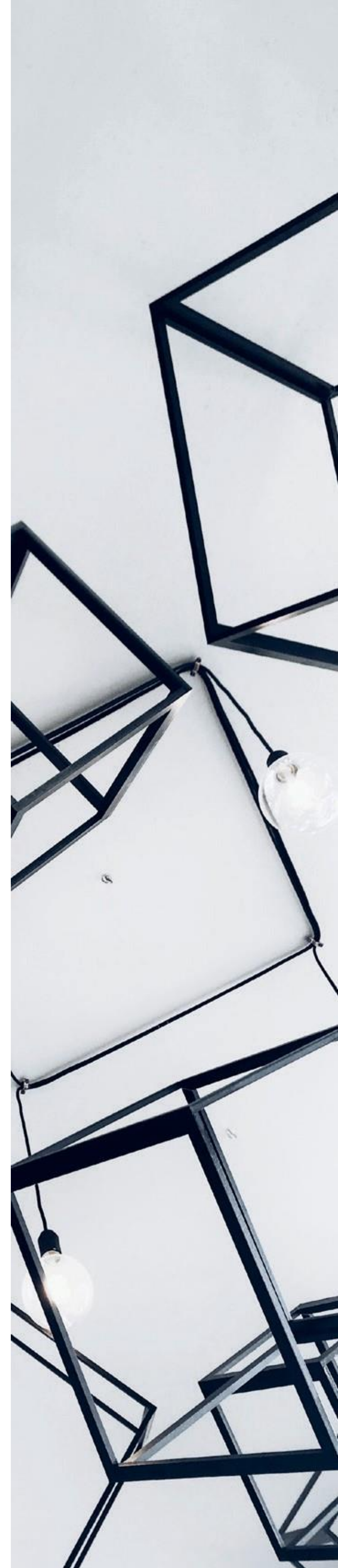
With the proposed repeal of these exemptions, the tax treatment of registered family trusts which hold hard assets such as land and buildings would need to be considered carefully.

f) Clarification on Permanent Establishments of foreign entities in relation to Digital Services Tax

Proposed Effective Date: 1 July 2022

The Finance Act, 2021 limited the application of Digital Services Tax (**DST**) to non-resident persons only, without any mention of its application on a permanent establishment (**PE**) of a non-resident person. The Bill proposes to clarify that the DST provisions will be limited to non-resident persons who do not have a PE in Kenya.

This would mean that a non-resident person who has a PE in Kenya would not be subject to DST and would be expected to comply with the corporate income tax regime, as is the case with resident entities which provide electronic services.



g) Deductibility of donations to charitable organisations

Proposed Effective Date: 1 July 2022

Currently, the ITA provides that only entities who make cash donations to charitable organisations that are registered or are exempt from registration under either the Societies Act or the Non-Governmental Organisations Coordination Act, and whose income is exempt from income tax, are allowed to deduct these expenses from their computation of taxable income.

The Bill has proposed to amend the ITA to allow entities to deduct from their taxable income any donations (cash or in-kind donations) made to a charitable organisation, whether or not they are registered under the Societies Act or the Non-Governmental Organisations Coordination Act, and whose income is exempt from tax under the ITA, or to any project approved by the Cabinet Secretary.

This proposal broadens the type of donation to also include in-kind donations and further allows donors to deduct donations made to charitable organisations that are not necessarily societies or non-government organisations such as companies limited by guarantee, foundations, trusts and other forms of entities who engage in providing much-needed charitable relief to members of the society.

h) Microfinance Institutions exempted from thin capitalisation provisions

Proposed Effective Date: 1 July 2022

The Finance Act, 2021 amended the ITA to the effect of exempting banks or financial institutions licensed under the Banking Act and micro and small enterprises registered under the Micro and Small Enterprises Act, 2012 from the EBITDA based thin capitalisation provisions on interest on loans paid or payable to related persons and third parties in excess of 30% of EBITDA.

The Bill proposes to also exempt microfinance institutions licensed under the Microfinance Act, 2006 from thin capitalisation rules. This is a welcome relief for microfinance institutions who were subject to thin capitalisation provisions, yet they engage in financial services.

i) Insurance relief provisions applicable to both spouses

Proposed Effective Date: 1 July 2022

The current provisions in the ITA on insurance relief imply that a resident male taxpayer shall be entitled to a personal insurance relief where they pay life insurance premiums on his life or his wife or child's life. The Bill proposes to amend this provision to the effect that any individual taxpayer, both male and female, will be entitled to a personal insurance relief where they pay life insurance premiums on their lives, or their spouses' or children's lives.

While this proposal provides clarity that insurance relief may be claimed by both male and female taxpayers, the Bill ought to have extended this gender-neutral language to the other sub-sections in Section 31 of the ITA which refer to employers paying the premiums on behalf of their male and female employees.

j) Proposed changes in rates of tax

i. *Capital Gains Tax (CGT)*

Proposed Effective Date: 1 January 2023

The Bill proposes to increase the rate of Capital Gains Tax (**CGT**) from 5% to 15%. We note there was a previous proposal set out in the Finance Bill, 2019 to increase the rate of CGT from 5% to 12.5% which was aimed at aligning the CGT rates with that of the East Africa region which is at 30%. However, the proposal to increase the rate to 12.5% provided for an indexation allowance to cater for inflation adjustments on the historical cost of the property. In the present circumstances, the Bill does not provide for any indexation formula to cater for inflation.

In our view, the proposal to increase CGT rate to 15% should also factor in an indexation allowance to cater for inflation, to mitigate the high CGT cost that is likely to arise on transfer of property.

ii. *Digital Services Tax (DST)*

Proposed Effective Date: 1 July 2022

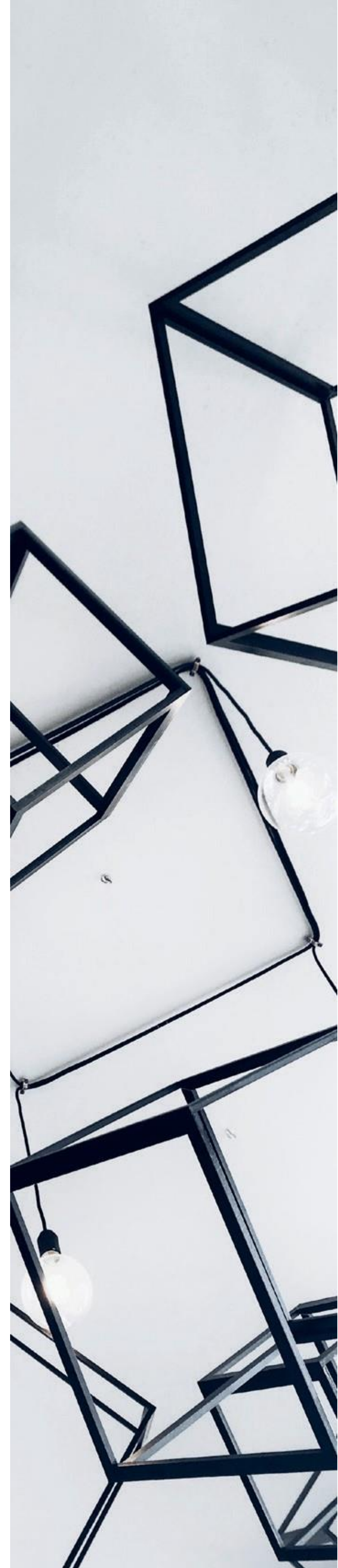
The Bill proposes to increase the rate of DST by one hundred percent, from 1.5% to 3%. The Finance Act, 2020 introduced new provisions in relation to DST to the effect that it would be charged on income accruing from a "digital marketplace" at the rate of 1.5% of the gross transaction value, effective 1 January 2021. The proposed increase in the DST rate is being introduced barely one year after introduction of DST and this begs the question whether the Government's strategy of promoting the digital economy is fully supported by all regulators, with the proposed hike being introduced in the same week that the CS for Information Technology launched Kenya's Digital Masterplan. Notably, with the introduction of DST in Kenya, most of the non-resident service providers passed on the additional cost to consumers of digital services, and this is likely to be the case if the proposed increase of DST is approved by Parliament.

k) Limitations relating to Investment Allowance

Proposed Effective Date: 1 July 2022

The Bill proposes to amend the Second Schedule of the ITA to grant an investment deduction at the rate of 100% for capital expenditure incurred on hotel buildings and buildings used for manufacture where:

a. the cumulative investment value in the preceding three (3) years outside Nairobi and Mombasa is at least KES 2 billion;
b. the investment value outside Nairobi and Mombasa in that year of income is at least KES 250 million; or
c. the person has incurred investment in a special economic zone.



The Bill also proposes to limit the nature of investments that would benefit from this enhanced rate of investment deduction by providing that those investments which due to their nature of business have to be located in places outside Nairobi or Mombasa, would not qualify. The proposed provisions create ambiguity, and the objective of the proposed amendments is not entirely clear, specifically in relation to which types of investments would be deemed to be required to be located outside Nairobi or Mombasa ''because of their nature''.

l) Casting the Transfer Pricing net wider

The Bill has introduced a raft of changes around preferential tax regimes and Country by Country reporting in an aim to increase international tax transparency and to improve access to information regarding the global allocation of the income, the taxes paid, and certain indicators of the location of economic activity among tax jurisdictions in which Multinational Enterprises (**MNE**) Groups operate.

Below we discuss these changes and their impact on doing business in Kenya.

i. Preferential tax regime

Proposed Effective Date: 1 January 2023

The Bill proposes to repeal the current Section 18A of the ITA to the effect of expanding the transactions subject to transfer pricing rules between resident persons and persons in a preferential tax regime. The proposed amendment will subject the gains or profits of a business in a preferential tax regime carried out with a resident person to transfer pricing rules. Person in a preferential tax regime include:

a. related resident person operating in a preferential tax regime;
b. non-resident person located in a preferential tax regime;
c. an associated enterprise of a non-resident person located in a preferential tax regime; or
d. a permanent establishment of a non-resident person operating in Kenya where the non-resident

The Bill further defines a preferential tax regime to mean "*any Kenyan legislation or administrative practice which provides a preferential rate of tax…*" such as:

a. the Special Economic Zones; or
b. a foreign jurisdiction which does not tax income, or taxes income at a rate less than 20%; or
c. a foreign jurisdiction which does not have a framework for exchange of information or allow access to banking information or lacks transparency on corporate structures, ownership of legal entities and their beneficial owners.

Firstly, we note that the proposal does not define the term "associated enterprise" and neither does it provide the parameters of who will be regarded as associated to a non-resident person located in a preferential tax regime. The Black Law's Dictionary defines the term "*as any persons who are directly or indirectly under common control*." This definition is similar to the definition of related parties in the ITA and the OECD guidelines.

Secondly the definition of preferential tax regimes captures a lot of tax regimes in the world with a worldwide average corporate income tax rate of 23.54%, notably tax regimes such as the United Kingdom and Mauritius will be regarded as preferential tax regimes. In this regard, we foresee an increased scrutiny on resident companies dealing with companies in preferential tax regimes especially the UK, where there was an estimated trade of 1.4 billion pounds, on exports of vegetables, cut flowers and black tea, and Mauritius where a growing number of MNEs have set up their holding companies. With the expanded definition of control, and inclusion of the term "associated enterprise", this is likely to impact many companies operating in Kenya, and we foresee an increase in transfer pricing audits by the KRA.

ii. Contemporaneous transfer pricing compliance requirements

Proposed Effective Date: 1 July 2022

The Finance Act, 2021 introduced a requirement for the ultimate parent entity (**UPE**) of an MNE to submit an annual prescribed return to the Commissioner detailing the group's financial activities in Kenya as well as in other jurisdictions where the group has a taxable presence. The Bill proposes to repeal this section and a more detailed disclosure requirement for MNEs has been introduced as follows:

a. Notification to the Commissioner

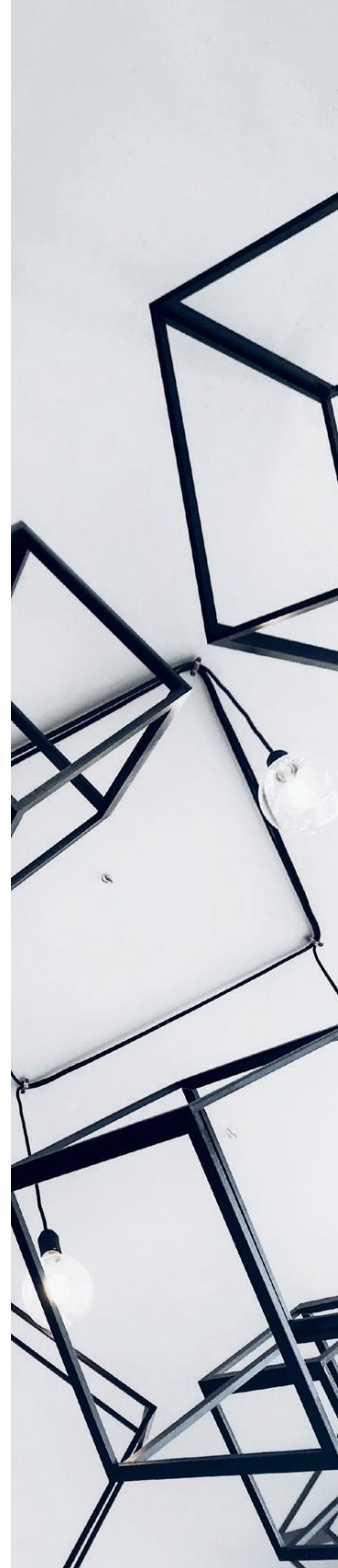
The Bill proposes that MNEs or a constituent entity (other than an excluded MNE Group) resident in Kenya, shall notify the Commissioner in a manner prescribed by the Commissioner, not later than the last day of the reporting financial year of that group, whether or not it is the UPE of the group, a surrogate parent entity, or the identity of a constituent entity which is the UPE and its tax residency status.

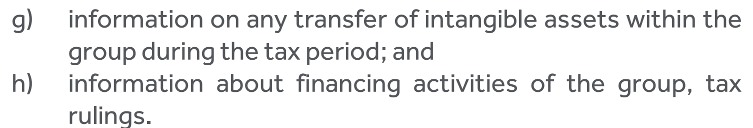
b. Filing of Country-by-Country (CbC) report, Master file and Local file

Resident UPEs or a constituent entity of an MNE with a gross turnover of KES 95 billion (including extraordinary or investment income) will be required to file a CbC report with the Commissioner of the group's financial activities in Kenya as well as in other jurisdictions where the group has a taxable presence, within 12 months of the group's financial reporting.

Further, the Bill introduces a requirement to file the Master File and the Local file not later than 6 months after the last day of the reporting financial year of the MNEs. The Master file is required to contain the following:

a) a detailed overview of the group;
b) a description of the supply chain of key products and services;
c) the group's growth engines;
d) the group's research and development policy;
e) a description of each related entity and their contribution to the value chain;
f) information about the intangible assets and the group intercompany agreements;





g) information on any transfer of intangible assets within the group during the tax period; and
h) information about financing activities of the group, tax rulings.

The Local file is required to contain the following:

a) details and information on the resident constituent entity's activities;
b) management structure of the resident constituent entity;
c) business strategies including description of the material-controlled transactions, the resident constituent entity's business and competitive environment; and
d) international transactions and amounts paid to the resident entity.

The KRA in 2021 released draft CbC Regulations outlining the filing procedure, notification procedure, contents and penalties regarding the CbC filing with the KRA. The Regulations are similar to the template provided for in the OECD Base Erosion and Profit Shifting (BEPS) Action 13 which requires large MNEs to prepare CbC reports with aggregate data on the global allocation of income, profit, taxes paid and economic activity among tax jurisdictions in which it operates.

The introduction of CbC reporting will result in additional transfer pricing documentation and reporting requirements for MNEs as parent entities or constituents of MNE's that have a turnover of KES 95 billion and are resident in Kenya, will now be required to file CbC reports, a Master file and a Local file. This will not only lead to increased compliance costs on reporting, but also increased tax and transfer pricing audits from the KRA. In addition, taking into consideration that the transfer pricing audits in Kenya involve extensive and sometimes inordinate requests for information by the KRA, it is likely that these reports will provide an avenue for KRA to make extended enquiries on operation of the MNEs and prolong the audit process, which then is also a burden on the taxpayer.

c. Penalties for non-compliance

Under the ITA, the Commissioner requires that upon request of transfer pricing documentation, the taxpayer should produce the same. However, we note that currently there are no penalties for failure to produce a transfer pricing document.

The Bill proposes to impose a penalty for failure to provide such information under the Tax Procedures Act, 2015 (**TPA**) and for offences with respect to filing a return for the UPE, its constituent entity and filling of the CbC reports, Master File and Local File. Section 93 of the TPA provides for the offence of failure to keep, retain, or maintain a document required by a tax law. Further Section 82 (a) of the TPA imposes a penalty for this offence, i.e., ten percent of the tax payable to which the document relates or if no tax is payable, KES 100,000, whichever is higher.

2. Proposed Amendments to The Value Added Tax Act, 2013 (The VAT Act)

Proposed Effective Date: 1 July 2022

a) Clarity on the operation of VAT on digital marketplace supplies

i. Revised definition of digital marketplace

The Bill proposes to amend the definition of the term '*digital marketplace' provided* for under Section 5 (9) of the VAT Act by deleting the words, "*other property".* Currently, the VAT Act defines the term "digital marketplace" to mean an online platform which enables users to sell or provide services, goods or *other property* to other users.

The definition of the term 'digital marketplace' which included the term "other property" as introduced by the Finance Act, 2021 resulted to ambiguity of what the other property meant given the definition of goods under Section 2 of the VAT Act encompasses movable and immovable property.

ii. Exemption of digital marketplace supplies from reverse charge provisions

The Bill seeks to carve out taxable supplies made over the internet or an electronic network or through a digital marketplace from being subject to reverse charge VAT upon importation of such services.

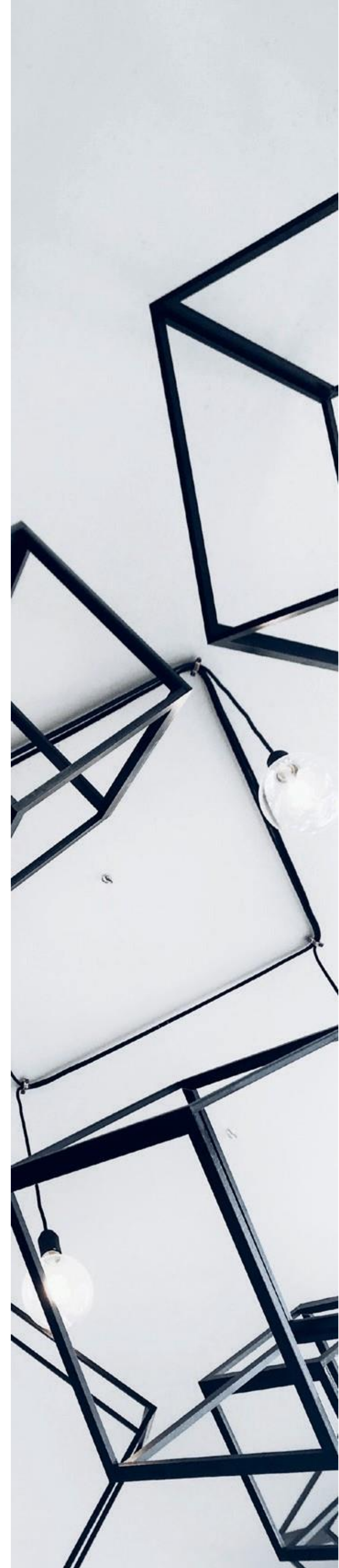
The VAT Act was amended by the Finance Act, 2021 to require any person (registered or non-registered) importing taxable services to account for reverse charge VAT. However, the Value Added Tax (Digital Marketplace Supply Regulations), 2020 (the **DMS Regulations**), placed the obligation to account for VAT on imported services on the non-resident supplier only to the extent that the supply is made on a Business-to-Customer basis (B2C). Currently, supplies made on the digital marketplace on a Business-to-Business (B2B) basis are exempted from digital marketplace supply VAT as they are subject to VAT through the reverse charge VAT mechanism.

Given that the obligation to account for VAT on taxable supplies made by non-resident persons through the internet, electronic means and digital marketplace is on the supplier, the proposal under the Bill to exempt such taxable services from reverse charge VAT aligns the treatment of such services as envisaged under the DMS Regulations.

However, it is not clear how B2B supplies would now be treated as it seems that such supplies would not be subject to VAT once the proposed amendments are passed by Parliament.

iii. Exclusion of persons supplying imported digital services from VAT registration

The Bill proposes to exclude persons supplying imported digital services over the internet, or an electronic network or through a digital marketplace from registering for VAT. This proposal seeks to align with the simplified VAT registration framework for non-resident persons providing supplies over a digital marketplace under the DMS Regulations.



b) Amendments relating to deduction of input VAT

i. Requirement to deduct input VAT in the return in which the supply was made

Currently, the VAT Act allows for deduction of input VAT within six months after the end of the tax period in which the supply or the importation occurred. The Bill proposes to amend the process of input tax deduction to introduce a requirement that input VAT on a taxable supply or importation shall be deducted by a registered person in a return for the period in which the input VAT is incurred. This means that input tax should be deducted in the month the supply or importation was made.

In our view, this amendment contradicts the provision that allows taxpayers up to six months to make a deduction of input tax on taxable supplies or importation. It may be the case that owing to the increased disputes between taxpayers and the Commissioner arising from VAA inconsistencies, the Commissioner is therefore seeking to codify the requirement for input VAT to be deducted in the month the output is declared to reduce the onerous and numerous cases of VAA mismatches.

ii. Wider powers to request for additional information to verify input VAT deduction

The Bill proposes to increase the documents that the Commissioner would ordinarily request to verify input VAT deduction by the taxpayer. Such documents include an original tax invoice, duly certified customs entry and a receipt for the payment of tax, customs receipt and a certificate signed by the proper officer, a credit note, and a debit note. The Bill proposes to amend this requirement to also include any other documentation that the Commissioner may require for the purposes of validating input tax.

In our view, this proposal is overly broad and creates uncertainty as to the nature of additional information the Commissioner may request and the documents the taxpayer should maintain. This proposal is likely to lengthen the process of input VAT verification and further delay the process of VAT refunds for eligible taxpayers.

iii. Departure from the penalty regime under EACCMA for import VAT

The Bill proposes to impose penalties and interest in relation to import VAT under the provisions of the Tax Procedures Act, 2015 (the **TPA**) as opposed to the provisions of the East Africa Community Customs Management Act, 2004 (the **EACCMA**) as currently is. This proposal will yield a higher position as regards to late payment penalty of import VAT at 5% under the TPA instead of 2% under EACCMA.

iv. *Provisions relating to the refund of VAT paid in error now covered under the TPA*

The Bill proposes to repeal provisions relating to refund paid in error under the VAT Act and introduce these procedures under the TPA. This proposal aligns tax administrative procedures including those relating to VAT, under the TPA. Consequently, under the proposal in the TPA, a person who has paid VAT in error will be required to make the application within six months.

c) Tax rate changes

Description	New rate	Old rate
Supply of taxable goods and services for the direct and exclusive use of construction of specialized hospitals with minimum bed capacity of 50 patients. Provided that, any exemptions already granted under these provisions shall continue to apply until the supplies of the exempted taxable goods or services have been made in full.	16%	Exempt
Harmonisation of provisions relating to applicability of VAT on the supply of maize (corn) flour, cassava flour, wheat or meslin flour and maize flour containing cassava flour by more than 10% in weight (Flour). The Bill proposes to clean up the provisions relating to the VAT treatment of these items by deleting Paragraph 108 of the First Schedule and Paragraph 20 of the Second Schedule to the VAT Act which provides for exemption and zero rating of 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 (Flour) respectively. These provisions were appearing under both the exempt schedule (which was introduced vide Finance Act, 2020 effective 30 June 2020 but were to be suspended for six months since date of assent) and under the zero-rated schedule provision which was to be in operation for the six months effective 30 June 2020 (that is in operation during the period the suspension of the exemption). The effect of the above proposal is that the supply of maize (corn) flour, cassava flour, wheat or meslin flour and maize flour containing cassava flour by more than 10% in weight, will be zero-rated under Paragraph 22 of the Second Schedule to the VAT Act.	Zero-rated	Zero-rated and Exempt
The Bill proposes to exempt plant and machinery of chapter 84 and 85 imported by manufacturers of pharmaceutical products or investors in the manufacture of pharmaceutical products upon the recommendation of the Cabinet Secretary responsible for matters relating health. The Bill implies that both investors and manufactures of pharmaceutical products will qualify for this exemption. It would be helpful if a definition of the term ''investors'' can be provided to provide further clarity on the criteria for accessing the exemption. This is a welcome proposal to pharmaceutical companies as it will reduce the cost of manufacturing pharmaceutical products in Kenya. It is important to note that whereas finished pharmaceutical products are exempted from VAT, VAT is currently applicable on machinery, plant and raw materials that are used to manufacture pharmaceutical products. By way of illustration, whereas vaccines are exempt from VAT, some organic compounds such as nucleic acids and amino acid phenols that are used to manufacture vaccines are subject to VAT. This exemption will encourage pharmaceutical manufacturers to set up in Kenya and effectively reduce the cost of pharmaceutical products in Kenya.	Exempt	16%

The Bill proposes to exempt from VAT medical oxygen, urine bags, adult diapers, artificial breasts and colostomy or ileostomy bags for medical use. This proposal is a welcome move to manage the soaring cost of healthcare in Kenya with a particular focus on the cost of developing Covid-19 vaccines and the cost of medical products that are used by patients who suffer from terminal illnesses.	Exempt	16%
The Bill proposes to exempt locally manufactured passenger vehicles which are defined as, "*a motor vehicle for the transportation of passengers which is manufactured in Kenya and whose total value comprises at least thirty percent of parts designed and manufactured in Kenya by an original equipment manufacturer operating in Kenya*." Currently, only locally assembled motor vehicles for transportation of tourists are exempt from VAT. The Bill also proposes to exempt from VAT inputs and raw materials used for the manufacture of passenger motor vehicles. These proposals seek to incentivize investment in the local manufacturing of motor vehicles and the local manufacturing of motor vehicle parts. That said, there is need to clarify the definition of the term passenger motor vehicles and whether this exemption extends to two and three wheelers used for transportation of passengers.	Exempt	16%
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 firefighting.	16%	Zero-rated

3. Proposed Amendments to The Excise Duty Act, 2015 (EDA)

Proposed Effective Date: 1 January 2023

a) Proposed changes to annual inflation adjustment for excise duty

The Bill proposes to amend the EDA to empower the Commissioner, with the permission of the Cabinet Secretary of the National Treasury to exclude, whilst adjusting the excise duty rates on account of inflation, some products, depending on the prevailing economic circumstances.

Currently, the Commissioner is required to adjust the excise duty rates on all products regardless of the economic repercussions of such an adjustment. This is a welcome amendment as it acknowledges that the current blanket adjustment is inappropriate for some products especially in the wake of a skyrocketing cost of living.

b) Departure from the penalty regime under EACCMA for import excise duty

Proposed Effective Date: 1 July 2022

The Bill proposes to bring under the provisions of the TPA, the penalties and interest payable in relation to import excise duty. This amendment now provides that penalties and interest that accrue on import excise duty shall be computed in accordance with the TPA but subject to the *in-duplum* rule.

Currently, demand of penalties and interest payable on import excise duty has been undertaken in accordance with the provisions of the EACCMA. If this provision is enacted, the applicable penalties and interest under the provisions of the TPA will be as follows;

- Late payment penalty at the rate of 5% of the tax due;
- Penalty for late submission of returns at the rate of 5% of the tax payable or KES 10,000 whichever is higher; and
- Penalty for late payment at the rate of 1% (on simple interest) per month.

c) Increase of excise duty rates

The Bill proposes to increase the excise duty rates applicable in respect of the following products. The proposed increase is instigated by the need to raise additional revenue which will in turn result in consumers bearing higher prices for the following products:

Product	Previous Excise Duty Rate	Proposed Excise Duty Rate
Fruit juices (including grape must), and vegetable juices, unfermented and not containing added spirit, whether or not containing added sugar or other sweetening matter.	KES 12.17 per litre	KES 13.30 per litre
Cosmetics and beauty products of tariff heading No. 3303, 3304, 3305 and 3307.	10%	15%
Bottled or similarly packaged waters and other non-alcoholic beverages, not including fruit or vegetable juices.	KES 6.03 per litre	KES 6.60 per litre
Beer, cider, perry, mead, opaque beer and mixtures of fermented beverages with non-alcoholic beverages and spirituous beverages of alcoholic strength not exceeding 6%.	KES 121.85 per litre	KES 134 per litre
Powdered beer	KES 121.85 per kg	KES 134 per kg

Wines including fortified wines, and other alcoholic beverages obtained by fermentation of fruits.	KES 208.20 per litre	KES 229 per litre
Spirits of undenatured ethyl alcohol; spirits liqueurs and other spirituous beverages of alcoholic strength exceeding 6%.	KES 278.70 per litre	KES 335.30 per litre
Cigarettes with filters (hinge lid and soft cap).	KES 3,447.61 per mille	KES 3,825.99 per mille
Cigarettes without filters (plain cigarettes).	KES 2,502.74 per mille	KES 2,752.97 per mille
Other manufactured tobacco and manufactured tobacco substitutes; "homogenous" and "reconstituted tobacco"; tobacco extracts and essences.	KES 9,734.45 per kg	KES 10,707.88 per kg
Motorcycles of tariff no. 8711 other than motorcycle ambulances and locally assembled motorcycles.	KES 12,185.16 per unit	KES 13,403.64 per kg
Imported sugar confectionary of tariff heading 17.04.	KES 36.74 per kg	KES 40.37 per kg
White chocolate, chocolate in blocks, slabs or bars of tariff nos. 1806.31.00, 1806.32.00, and 1806.90.00.	KES 220.31 per kg	KES 242.29 per kg
Jewellery of tariff heading 7113 and imported jewellery of tariff heading 7117.	10%	15%
Products containing nicotine or nicotine substitutes intended for inhalation without combustion or oral application but excluding medicinal products approved by the Cabinet Secretary responsible for matters relating to health and other manufactured tobacco and manufactured tobacco substitutes that have been homogenized and reconstituted tobacco, tobacco extracts and essences.	KES 1,259.64 per kg	KES 2,500 per Kg

d) Changes in excise duty rates

i. Introduction of excise duty on Articles of plastic of tariff heading 3923.90.90

The Bill proposes to introduce excise duty at the rate of 10% on Articles of Plastic of tariff heading 3923.90.90. Previously, only Articles of Plastic of tariff heading 3923.30.00 were subject to excise duty at the rate of 10%.

ii. Introduction of excise duty on imported potatoes of tariff numbers 0710.10.00, 2004.10.00 and 2005.20.00

The Bill proposes to introduce excise duty at the rate of 25% on imported potatoes of tariff numbers 0710.10.00, 2004.10.00 and 2005.20.00. Currently, only imported potatoes, potato crisps and potato chips of tariff heading 07.01 are subject to excise duty.

iii. *Introduction of excise duty on all glass bottles (excluding glass bottles for packaging of pharmaceutical products)*

Previously, only imported glass bottles (excluding imported glass bottles for packaging of pharmaceutical products) from outside the countries within the East Africa Community were subject to excise duty. The Bill proposes to amend the EDA to subject all glass bottles (excluding glass bottles for packaging of pharmaceutical products) to excise duty, including glass bottles imported from the East Africa Community partner states. This amendment will increase the prices of goods that are packaged in glass bottles and would prejudice Kenya's goal of being plastic-free, as glass is one of the most preferred alternatives to plastics.

e) Excise duty on betting and gambling-related activities increased

Services	Previous Excise Duty Rate	Proposed Excise Duty Rate
Betting	7.5% of the amount wagered or staked	20% of the amount wagered or staked
Gaming	7.5% of the amount wagered or staked	20% of the amount wagered or staked
Prize competitions	7.5% of the amount paid or charged to participate in a prize competition.	20% of the amount paid or charged to participate in a prize competition
Lottery (excluding charitable lotteries)	7.5% of the amount paid or charged to buy the lottery ticket.	20% of the amount paid or charged to buy the lottery ticket

f) Introduction of excise duty on advertisement fees for alcoholic beverages, betting, gaming, lottery and prize competitions

The Bill proposes to introduce excise duty at the rate of 15% on fees charged by all television stations, print media, billboards, and radio stations for advertisements for alcoholic beverages, betting, gaming, lottery and prize competitions. The introduction of excise duty on these fees is instigated by the need to raise government revenue and dissuade the abuse of alcoholic beverages as well as discouraging the growing betting and gambling activities in Kenya. Should this proposed amendment be passed into law, media stations would be required to comply with the provisions of the EDA, and to re-configure their systems to enable excise duty to be charged on their excisable services.

g) Introduction of excise duty on electronic cigarettes and other nicotine delivery devices, liquid nicotine for electronic cigarettes and ice cream and other edible ice whether or not containing cocoa of tariff number 2105.00.00

The Bill seeks to introduce excise duty on electronic cigarettes and other nicotine delivery devices at the rate of 40%, liquid nicotine for electronic cigarettes at the rate of KES 70 per millilitre and ice cream and other edible ice whether or not containing cocoa of tariff number 2105.00.00 at the rate of 15%. This amendment is a revenue increase measure by the Government as well as discouraging its citizenry from consumption of these products.

h) Exemption from excise duty on certain products

i. Exemption from excise duty on fertilized eggs of tariff numbers 0407.11 and 0407.19 imported by hatcheries

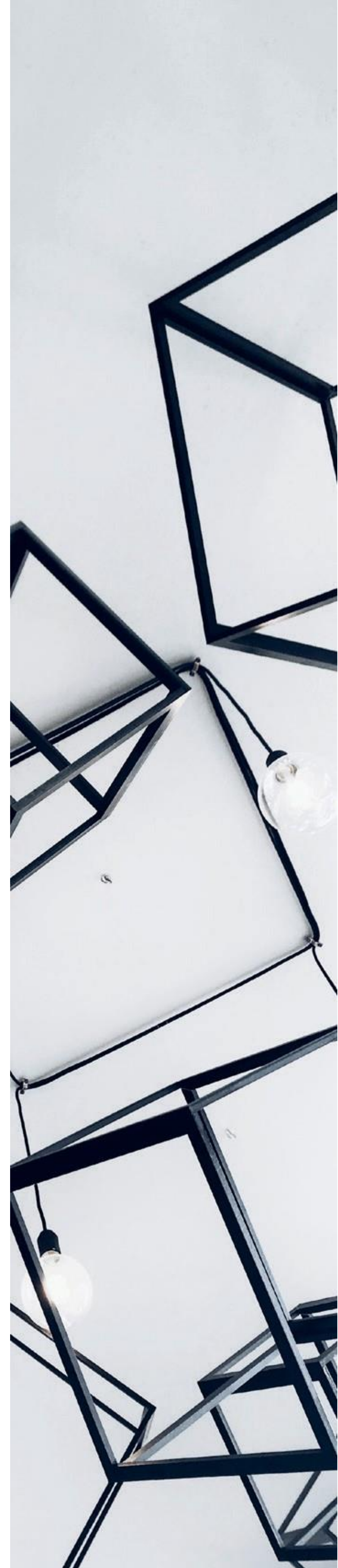
The Bill proposes to exempt from excise duty, fertilized eggs of tariff numbers 0407.11 and 0407.19 imported by hatcheries, upon recommendation by the Cabinet Secretary responsible for matters relating to livestock. The Finance Act, 2021 introduced excise duty on all imported eggs of tariff heading 04.07 at the rate of 25%. This tax negatively affected the hatching industry as there is insufficient local capacity to supply all the required eggs for hatching. This amendment will aid in the local production of chicken and eggs and boost Kenya's food security.

ii. Exemption from excise duty on neutral spirit imported or purchased locally by registered pharmaceutical manufacturers

The Bill proposes to exempt neutral spirits used by registered pharmaceutical manufacturers upon approval by the Commissioner General. This exemption seeks to create a conducive environment for manufacturers of pharmaceuticals in Kenya as it will lower the cost of production of the pharmaceutical products that use neutral spirit as a raw material.

iii. Exemption from excise duty on locally manufactured passenger motor vehicles

In addition to the VAT exemption proposed by the Bill on locally manufactured passenger vehicles, the Bill proposes to exempt from excise duty, all locally manufactured passenger motor vehicles. This proposal seeks to incentivize more investment in the local assembly of passenger motor vehicles and making the price of such vehicles competitive in the market.



4. Amendments to The Tax Procedures Act, 2015 (TPA)

Proposed Effective Date of all amendments: 1 July 2022

a) Input VAT deductible within six months after end of tax period

The Bill proposes to amend the TPA by introducing a new subsection (5) which provides that in respect of VAT, the input tax shall be allowable for a deduction within six months after the end of the tax period in which the supply or importation occurred.

We note that this is contrary to the proposal made by the Bill in relation to the VAT Act to require that input tax should be deducted in the month the supply or importation was made. Further, the TPA in Section 31 already has a subsection (5) and it is not clear whether this new provision will repeal or replace the existing subsection.

b) Commissioner to have power of disposal of any property that is subject to security

The Bill has proposed to repeal Section 40 of the TPA relating to security on property for unpaid tax and to replace it with a new provision. The proposed new section is similar to the current section with the addition of the power of disposal of the property by the Commissioner in order to recover the tax if the taxpayer fails to pay the tax liability within two (2) months after receipt of the notification by the Commissioner that the property is the subject of a security for the unpaid tax. Note, however, that any prior restraint on a property shall have priority if the property is disposed of by the Commissioner.

Currently, Section 40 refers to security over land or building, however, the new provision refers to property in general which includes aircrafts, ships, motor vehicles or any property which the Commissioner may deem sufficient to serve as security.

c) Taxpayers can now choose to offset or apply for refund of overpaid taxes

Section 47 of the TPA relating to refund of overpaid tax is proposed to be repealed and replaced with a new provision. The proposed Section 47 gives taxpayers who have overpaid a tax the opportunity to either apply the overpaid tax against future tax liabilities or to apply for a refund of the overpaid tax within five years or six months in the case of VAT.

While the proposed amendment is substantially similar to the current provisions, it gives taxpayers the opportunity to decide whether they want a refund or they want to utilise the overpaid taxes against future tax liabilities. The process of refund remains similar to the existing provisions whereby the refund claimed is first applied to payment of other taxes owing under the tax law, payment of tax under any other laws and any remaining amount is refunded.

d) Refund of tax paid in error

The Bill proposes to introduce a new Section 47A which relates to refund of tax paid in error, which is defined as any tax paid which the Commissioner is satisfied ought not to have been paid. We note that this definition is rather restrictive since it depends on the opinion of the Commissioner on whether a tax ought not to have been paid.

e) Refund of tax paid in error where supply is exempt or zero-rated

The Bill proposes to introduce a new Section 47B which relates to refund of tax paid on exempted or zero-rated supplies. In this case, the Commissioner may, upon the 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 or zero rating was not processed within the specified period due to circumstances beyond the control of the taxpayer.

f) Various amendments to Section 51 of the Tax Procedures Act

The Bill proposes to amend subsection (4), which relates to notifications where a notice of objection is not validly lodged, to the effect of specifying that the Commissioner has a period of fourteen (14) days to notify the taxpayer that the notice of objection is not valid.

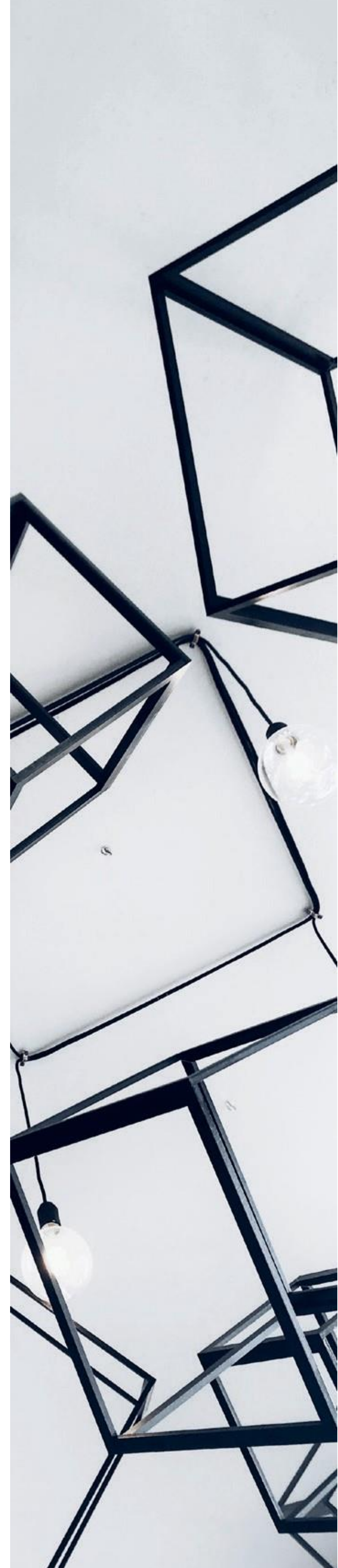
The Bill also proposes to amend subsection (7) and to introduce a new subsection (7A) which would require the Commissioner to notify the taxpayer of its decision on whether or not they can extend the time to lodge a notice of objection.

Subsection (11) is proposed to be amended to require the Commissioner to make an objection decision within 60 days of receipt of a valid notice of objection. The current provisions of the TPA allow the Commissioner the make a decision within 60 days of receipt of a valid notice of objection or any further information required by the Commissioner which meant that the time would begin running again once a taxpayer furnished the Commissioner with additional information. Therefore, this proposed amendment is expected to make the requirements for the Commissioner more stringent.

Further, the Bill proposes to introduce a new subsection (12) to the effect that a person who is dissatisfied with a decision of the Commissioner may appeal to the TAT within 30 days after being notified of the decision.

g) Requirement to have PIN for registration of a trust

The Bill proposes to make registration of a trust a transaction for which a PIN is required, and this requirement seems to have been introduced in line with the various amendments relating to taxation of trusts.



5. Amendments to The Miscellaneous Fees and Levies Act, 2016 (MFLA)

Proposed Effective Date of all amendments: 1 July 2022

a) Addition of new tariff subject to export levy

The Bill proposes to amend the First Schedule to the MFLA relating to export levy as follows:

Tariff No.	Tariff Description	Current Export Levy Rate	Proposed Export Levy Rate
2601	Iron ores and concentrates including roasted iron pyrites	-	USD 175 per ton

b) Revision of export levy rates on animal hides and skins

The Bill proposes to reduce the export levy for various products as follows:

Tariff No.	Tariff Description	Current Export Levy Rate	Proposed Export Levy Rate
Deleting and substituting the export levy rates as follows:			
4101.20.00	Whole hides and skins, of a weight per skin not exceeding 8 kg. when simply dried, 10 kg. when dry-salted, or 16 kg. when fresh, wet-salted or otherwise preserved.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4102.21.00	Raw skins of sheep or lambs (pickled, but not tanned, parchment-dressed or further prepared), without wool on whether or not split, other than those excluded by Note 1(c) to Chapter 41.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4102.29.00	Other raw skins of sheep or lamb (fresh, or salted, dried, limed, pickled or otherwise preserved, but not tanned, parchment-dressed or further prepared), with wool on, whether or not split, other than those excluded by Note (c) to Chapter 41.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4103.20.00	Other raw hides and skins (fresh, or salted, dried, limed, pickled or otherwise preserved, but not tanned, parchment-dressed or further prepared), whether or not debarred or split, other than those excluded by Note 1 (b) or (c) to this Chapter, of reptiles.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4103.30.00	Other raw hides and skins (fresh, or salted, dried, limed, pickled or otherwise preserved, but not tanned, parchment-dressed or further prepared), but not debarred or split, other than those excluded by Note 1 (b) or 1 (c) to this Chapter, of swine.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4103.90.00	Other raw hides and skins other than of reptiles, swine, goats or kids.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.

4104.19.00	Other tanned or crust hides and skins of bovine (including buffalo) or equine animals, without hair on, whether or not split, but not further prepared, in the wet state (including wet - blue).	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4301.60.00	Raw furskins of fox, whole, with or without head, tail or paws.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4101.40.00	Hides and skins of equine animal.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4101.50.00	Whole hides and skins, of weight exceeding 16 kg.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4101.90.00	Other, including butts, bends and bellies.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4102.10.00	Raw skins of sheep or lamb (fresh, or salted, dried, limed, pickled or otherwise preserved, but not tanned, parchment-dressed or further prepared), with wool on, whether or not split, other than those excluded by Note 1(c) to Chapter 41.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4301.10.00	Raw furskins of mink, whole, with or without head, tail or paws	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4301.80.00	Other raw furskins, whole, with or without head, tail or paws	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4301.90.00	Heads, tail, paws, and other pieces or cuttings, suitable for furriers' use.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4302.11.00	Whole skins, with or without head, tail or paws, not assembled, of mink.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4302.19.00	Other whole skins, with or without head, tail or paws, not assembled.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4302.20.00	Heads, tails, paws and other pieces or cuttings, not assembled.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.
4302.30.00	Whole skins and pieces or cuttings thereof, assembled.	80% or USD 0.52 per kg.	50% or USD 0.32 per kg.

c) Change in timelines for inflation adjustments

The Bill also proposes to amend the inflation adjustment of export levy, which takes place at the beginning of every financial year, to a date not later than 1 October of every financial year.

d) Exemption of inputs and raw materials used for pharmaceutical products from IDF and RDL

The Bill also proposes to add a new exemption under Part A and B of the Second Schedule relating to Import Declaration Fee and Railway Development Levy. The new items proposed to be exempt from these fees are *'inputs and raw materials imported by manufacturers of pharmaceutical products on the recommendation of the Cabinet Secretary responsible for matters relating to health.'*

This proposal has likely been introduced to encourage global pharmaceutical companies to set up base in Kenya and engage in manufacturing of pharmaceutical products, particularly following Kenya's interest to set up a vaccine manufacturing plant to manufacture Covid-19 vaccines.

6. Amendments to The Tax Appeals Tribunal Act, 2013

Proposed Effective Date of all amendments: 1 July 2022

Requirement to deposit 50% of the disputed fees before appeal to High Court

The Bill proposes to introduce a new requirement for a taxpayer who wishes to appeal the decision of the TAT to the High Court, to deposit with the Commissioner fifty percent (50%) of the disputed tax in a special account at the Central Bank of Kenya. This requirement shall not apply where the appeal is filed by the Commissioner.

In our view, the proposed change is punitive and will discourage taxpayers from defending themselves since it requires them to deposit 50% of the disputed fees, which can run into billions of shillings, failure to which they would not be able to proceed to the High Court. This would hamper access to justice and would be in contravention of the Constitution of Kenya, as it impinges on the right to a fair trial and the right to access to justice, by introducing financial hurdles in lodging appeals to a higher court.

7. Miscellaneous Amendments

Proposed Effective Date of all amendments: 1 July 2022

Amendment to the Statutory Instruments Act, 2013

The Bill seeks to amend Section 21 of the Statutory Instruments Act which relates to automatic revocation of statutory instruments. The amendment involves addition of a new section that provides that the automatic revocation shall not apply to statutory instruments issued under the Income Tax Act, Stamp Duty Act, Value Added Tax Act, Tax Appeals Tribunal Act, Excise Duty Act and Tax Procedures Act. This will be a welcome move as uncertainty had arisen in relation to the validity of tax exemptions granted under the Income Tax Act, for example exemptions granted to the energy and infrastructure sectors, as it was not clear whether the exemptions would have the force of law upon the expiry of the 10-year period for statutory instruments.

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