

TAX NEWSLETTER

FINANCE ACT 2023



Tax Insight: Unveiling the Transformative Changes in the Finance Act 2023

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In this month's newsletter, we highlight the changes introduced in the Finance Act 2023. We note, some of the proposals in the finance bill, have either been dropped, changed or retained as they were in the bill. We will focus with those that were either changed, or retained.

Type of tax change	Effectuated Change.	Further notes.
Turn over tax	This has changed from 1% on gross sales to 3% of gross sales. Further, there will be a change in the threshold of those who meet the criteria for registration from the current 1M – 50M gross sales per calendar year to 1M – 25M sales per year. We note this was the same rate(3%) during pre-covid season and the rate had been reduce to act as a precaution measure for businesses during the covid season.	In Turn over tax regime, payers do their monthly filling as a percentage of gross sales. In this case, the tax payer will submit 3% of their monthly gross sales to the commissioner before 20th of every month following the month of sale. This means that the tax payer doesn't have an option to deduct what would be allowable expenses when arriving at the taxes due. The upside of turnover turn over tax is that it reduces on the complexities of computing taxable income that in most cases has landed many tax payers in penalties and interest. It is also important to note that Turn over tax is final tax and tax payer who enroll for this regime are not required to file the corporate tax. Consequently, the taxpayer is not required to pay installment tax. The penalty for late filling is Ksh 1,000 and a late payment penalty of 5% of taxes due with a monthly accrued interest of 1%. Turnover Tax is not applicable for those in the following areas of business. 1. Rental income

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		2. Income that is subject to final withholding tax according to Income Tax. 3. Management, Professional and Training Fees 4. Business with less than 1M in gross sales PA and above 25M PA.
VAT on Fuel products	VAT on fuel products has since been changed from the reduced rate of 8% to the standard rate of 16% .	The cabinet secretary noted that this was motivated by the fact that it gives the traders in fuel industry an unfair advantage by giving them an upper hand as they will always be in perennial refund position for VAT. We emphasize that this is the case since the traders claim the input tax at a higher rate of 16% while their output tax is at a reduced rate of 8%. This being a very emotive topic, it is important to note that LPG has been moved to exempt and this will greatly reduce the cost of cooking gas for Kenya households.
Rental income tax	Reduced rate of the MRI from the current 10% to 7.5% of the gross rent collected. The commissioner will also have power to elect withholding tax agents who will be required to withhold the 7.5% and submit it within 5days from the earlier proposal of 24Hrs.	Monthly Rental tax is filed by landlords with income of between Ksh 288,000 – 15M PA. The change is such a welcome move as it aims to bring on board more landlords who feel the earlier rate of 10% was high. In the monthly rental income regime, the landlord is not allowed to deduct expenses such as maintenance, rates e.t.c In the instance where there is no rental income received in a month, the landlord is required to file nil returns before 20th of the following month.

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		Landlord who's income is more than 15M per year or less than Ksh 288,000 PA, are required to file their annual returns together with other sources of income such as interest income, business income e.t.c at a rate of 30%. The penalty for failing to file returns is Ksh 5,000 for individuals or Ksh 20,000 for corporates or 5% of the tax due for both instances, whichever is higher. It is expected that a big majority to the appointed withholding agents will be the property managers who collect taxes on behalf the landlords and deduct the tax of 7.5% before submitting the same.
Advance Tax	This has been increased for vans, pick-ups, trucks, prime movers, trailers and lorries from the current Ksh 1,500 Per tonne or 2,400 PA to Ksh 2,500 per tonne or Ksh 5,000 P.A which is higher and, For vans, pick-ups, trucks, prime movers, trailers and lorries from Ksh 60 to Ksh 100 per passenger or Ksh 2,400 up to Ksh 5,000 P.A whichever is higher.	Every years, all commercial cars are subject to the advance tax at the stated rates. The changed rates may not have a significant effect as the marginal changes are not as high yet the transport sector has been performing well in the recent years.
Withholding Tax on digital content monetization	These include payments made in relation to digital content monetization and the applicable withholding tax rate is 15%. This includes payment to persons who engage in activities such as;	This has been a touchy subject since this is primarily targeted to the young population who engage in such activities. It is, however a welcome move as it increases tax base as a method of increasing government revenue, unlike increasing taxes on commodities already being taxed.

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	1. Fundraising for specific goals for the content creator another person. 2. Where a content creator is paid by a brand owner for promotion and content creation. 3. Adverts on social media, websites including endorsements from sellers. 4. Where an audience pays subscription fees to have access to content created by the content creator. 5. Membership services/programs with exclusive content for the subscribers. 6. Affiliate marketing	It is, however a welcome move as it increases tax base as a method of increasing government revenue, unlike increasing taxes on commodities already being taxed.
Withholding Tax on marketing services	Payment made for sales promotions, marketing and advertising services will now be subject to withholding tax of 5% for residents persons, and as well non-resident person who have permanent establishments in Kenya.	This is a reintroduction as it had earlier been suspended in the prior years by prior finance bill. This is solely aimed at enhancing compliance and declaration of incomes by the players in the industry as failure to deduct the WHT becomes a non-compliance on the withholder yet, the service provider has to declare the income while filing their annual income and as well claim the credit for the Withheld tax. This seeks to have fairness as the same services are taxed for non-residents albeit at the rate of 20%. We note, such re-introduction of earlier scrapped provisions in the law bring with them a lot of uncertainty to

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		the tax payers and we hope such scenarios will be streamlined by the Tax Policy that is still in draft once enacted.
Digital Asset Tax	This will be at rate of 3% on the gross transfer value or exchange value payable by the owner of the exchange platform.	We note this is an upcoming area in Kenya and aligns with the government need to increase it's tax base. It is a welcome move though it may hinder or limit activities in the forex arena
Limitation of Interest deferral of forex losses	Limitation of interest will only apply to loans only from non-residents. The Forex losses realized shall as be distributed evenly in the next three years if the interest payable to non-resident fall above the 30% restriction on EBITDA.	The tax payer was only allowed to deduct interest up to 30% of EBITDA in interest both from local and foreign borrowing, save for manufacturing firms that met the threshold for exemption. The current provision is that, the 30% limit will only be restricted on interest from non-residents. While this cap was introduced to stop structuring companies that allowed non-residents to lend money and erode the tax base via repatriating interest payments, this is such a great move as this will encourage local borrowing, spur local economy and at the same time ensure money circulation is retained within the country. As for the realised forex losses, this is a welcome move as this is now exclusive to non-resident persons.
Generation of invoices through e-TIMS	Losses and expenditures shall not be allowable for deduction if the invoices are not generated via e-TIMS	This is aimed at ensuring that all business transactions done via the revenue authority. This may compel businesses that do not meet the threshold to register for VAT to ensure they have rolled out for e-TIMS.
Taxation of Branch reduced from 37.5% to 30%	Previously, the branches of foreign companies have been taxed at a special corporate tax of 37.5% but this has been reduced to 30%.	The taxation of foreign companies now is harmonized with that of local companies. However, it is important to note that payments done to head office by the branch are not allowable for deduction

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	Additionally, the profit repatriated by the branch to the parent company is to be taxed at a rate of 15% calculated as follows. $R = A1 + (P - T) - A2$ R - Repatriated profit; A1 - Net assets (Book value of assets except revaluation) at the beginning of the year P - Net profit for the year of income T - Tax payable A2 - Net assets at the end of the year.	in line with OECD recommendation since this is considered to be transfer within the same company and not an actual expense.
Increase of tax bands for personal income tax	Two new tax bands introduced as follows. Monthly income between Ksh 500,000 –Ksh 800,000 is to be taxed at an increased rate of 32.5% Income over Ksh 800,000 Per Month is to be taxed at an increased rate of 35%	This change is certainly not expected to bring a lot of tax into the kitty as the individuals earning in the described brackets are few within the country. In addition, those who earn high incomes are in most cases experts and expatriates and this may drive such skillful labour into other jurisdictions with lower tax rates. This will as well create instances of tax refunds where employees earn significantly higher than other months for non-usual scenarios such as special allowances and bonuses.
House levy at 1.5%	All employees incomes are to be subjected to a monthly tax levy at 1.5% of their gross pay. The employer is required to match the contribution of the employee of 1.5%	While this has elicited a lot of discussion, we wish to state that the change of status of this deduction from a fund to a levy and therefore, those who contribute are not entitled for a refund of the same. This will certainly have a negative effect on tax payers on their already squeezed monthly deductions.

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	It is important this is based on gross pay and not Basic pay.	Additionally, this will have an impact on business as they may seek to reduce their workforce with the increased requirement of matching the employees contributions.
Mileage reimbursement to an employee to be tax free	The amount reimbursed to an employee as mileage expenses for travelling will be tax free. However, this has been capped to a standard rate being the rates published by Automobile Association of Kenya.	This is a welcome move as it brings more clarity and uniformity of taxation of mileage reimbursement that may come with a lot of ambiguity and personal judgement, albeit, in most instances KRA has been already applying these rates while making assessments and checking compliance.
Contribution to Post-retirement medical schemes	Contributions made to post-retirement medical schemes are to be allowed for deduction at 15% of the contribution made, however this is to be capped at Ksh 60,000PA	This is a new development that is aimed to encourage tax payers to consider making contribution to post-retirement medical funds. However, we feel the cap should have been a little higher as this translates to roughly Ksh 33,333 P.M contribution. Nonetheless, this is a welcome move.
Club fees, welfare contribution and joining fees	Club joining and subscription fees is to be benefit taxable on the employee, where the same has been allowed for tax on the employer	The initial confusion around this has been cleared as the tax is to be incurred by the employee as far as the employer has allowed it for tax purposes.
Deferral of taxation for award of shares of a start-up to employees	Taxation of the benefit from shares allocated to an employee by an eligible start-up shall be deferred and taxed within thirty days of the earlier of: a) expiry of 5 years from the end of the year of the award of the shares;	The start ups that qualify are those that; 1. Have annual turnover of not more than KES 100 million shillings; 2. Do not carry on management, professional or training business; 3. Have not been formed as a result of splitting or restructuring of an existing entity; and

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	b) disposal of the shares by the employee; c) the date the employee ceases to be an employee of the start-up	4. Have been in existence for a period of not more than 5 years. We have recently published a newsletter on the changes earlier made and can be accessed here .
Tax Shortfall penalty.	This is tax payable by those who qualify to pay installment tax, being the tax payer who has a tax liability of over Ksh 40,000 for any year excluding PAYE and those who pay the Turn Over Tax. The finance Act has amended the TPA to have the tax payer penalized double the amount of tax short fall.	The installment tax is calculated in two ways. 1. Prior year basis - Prior year tax payments are multiplied by one hundred and ten per cent. 2. Current Year basis - In this method, especially for new business or those who were in losses and turned to profitability, installment tax is determined by estimating the current year profit and tax payable thereon. The installments are spread evenly at 25% of the tax due and payable on the 20th day of the 4th, 6th, 9th and 12th months of the year of income for all taxpayers except those in the Agricultural Sector. Taxpayers in the Agricultural Sector pay in installments of 75% in the 9th month and 25% in the 12th month.
Record keeping	Tax Payer no longer required to keep records in Kenya	This is in line with the technology advancement and an acknowledgement that records can be maintained in soft and in the cloud.
Tax refunds on bad debts	The Act has changed the time frame for which the tax payer can make an application for refund of taxes paid on goods supplied and the supply	This is an exceptionally good introduction into the VAT act as we have seen the government reduce it's motivation to want to refund taxes to tax payers tax refunds.

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Tax refunds on bad debts	becomes a bad debt from the current 4 years to 10 years. The tax payer can claim under the following circumstances have been fulfilled. 1. The tax payer has not received any payment after three years after the supply was done. 2. Where the person to whom the supply was made has been placed under a statutory management through a receiver, a liquidator or an administrator. In addition, the amount being claimed for refund may be credited in the tax payers VAT account and applied to clear future VAT liabilities. Further, the Act states that when the recovery of the amount declared as bad debt has been done a refund done to the tax payer, then the tax payer is to pay the amount refunded after sixty days after which an interest of 2% P.M will be applicable.	The extension of the period which the tax payer can claim the vat refund has been extended from the upper limit of four year to ten years will ensure that the tax payer has a better window to utilize the application for a refund. Additionally, there's more reprieve in that the tax payer can now make an application not only when the person to whom the supply was made to is declared insolvent, but also when they are placed under receivership, liquidation or administration. Notably, this is a welcome move as some of the aforementioned administrations may take considerable to time in execution therefore locking out tax payers previously available window to claim the
VAT on Insurance Compensations	The Act introduced VAT on insurance compensation for compensation received of loss of Vatable good. The following two scenarios are explained.	The implication of this is that we expect the cost of premiums to go high. It rarely is the industry practice to insure the goods at their cost plus vat as most are covered at their cost.

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VAT on Insurance Compensations	a) if the compensation includes value added tax, the compensation shall be declared and the value added tax thereon remitted to the Commissioner; or (b) if the compensation does not include value added tax, the compensation shall be declared and subjected to value added tax and the tax remitted to the Commissioner	It is expected that where the insurer will be expected to make the compensation at cost + vat, then we expect the cost of the premiums to go high
Expansion of VAT obligations for suppliers of services without a fixed place of business in Kenya.	The suppliers of goods and services to customers in Kenya are now required to register for VAT	The Non- Residents suppliers are hence forth required to register for VAT by the virtue of making supplies to customers in Kenya.
VAT on export of services	The act has retained the proposal of taxable export services as zero rated.	This is such a relief to many Kenya businesses and it puts them right back in a competitive space. We have authored a newsletter giving more details why this was necessary and who the international best practices well align with this. Access the newsletter here .

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