BUDGET SYNOPSIS 2020-2021

Taxpert Consultants highlights on the finance bill 2020

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PROPOSED AMENDMENTS TO THE INCOME TAX ACT

EXTENDING THE UPPER LIMIT OF THE RESIDENTIAL RENTAL INCOME TAX (CLAUSE 2)

1. **Extending the upper limit of the Residential Rental Income Tax** (clause 2): - the current residential rental income tax is applicable for annual rental income of between Kshs. 144,000 to Kshs. 10 million. The amendment shifts the upper limit from Kshs. 10 million to Kshs. 15 million.

The aim of this proposed amendment is to extend the upper limit so as to grant landlords with rental income of between Kshs. 10 million and Kshs. 15 million the more concessional tax rate of 10% of gross income, and reduce administrative costs of ascertaining profit for such landlords. This is likely to increase that tax base but on condition that enforcement is robust. This is an information collection exercise. Once the landlords are fully in the basket, the normal taxation shall be enforced.

Introduction of Minimum Tax (clause 3, 4, 7 and 9): - a new tax to be known as minimum tax is proposed to be introduced at the rate of 1% of the gross turnover. This new tax is intended to enhance tax fairness, promote equity and also facilitate the raising of additional revenue by targeting a portion of gross turnover of businesses since the loss making position does not attract corporation income tax. This new tax captures the taxation neither of an income that is exempt nor from employment, residential rental, turnover, gains from property and extractives. This will occasion an expansion of the tax base and facilitating the enhancement of revenue yield. This is because businesses will pay the higher of either minimum tax or instalment tax. The withholding tax regime ensures that so many incomes are subject to 3% or 5% withholding Tax on contractual income and 15% on interest income. The clause is likely not to spur much revenue collection

3. **Introduction of Digital Service Tax** (clauses 4, 7 and 9):- a new tax known as digital service tax is proposed to be introduced at the rate of 1.5% of the gross transaction value. It shall be payable by persons who derive income from provision of services through the digital market place. This tax targets non-residents without permanent establishment in Kenya. This is because for both resident and non-resident persons with permanent establishment in Kenya, this tax shall be offset from the tax payable for the year of income. Nonetheless, it is a considered view that the base of tax should be clarified as to whether it is charged on fees for the service or the gross transaction value.

The main bottleneck is implementation and instances of double taxation.

4. **Removal of existing allowable deductions** (clauses 5 and 6): - the Bill proposes to remove seven types of allowable deductions from the income tax law, and which are estimated to yield additional revenue amounting to **Kshs. 3 billion**. This would help align the Income Tax statute with the Constitution and the Public Finance Management Act, with regard to the principles of public finance. The Bill proposes to remove:

i) Entrance fee or annual subscription paid during that year of income to a trade association which has made an election under Section 21(2) of this Act. *This will deny associations like Aptak, ICPAK, revenue since the contributions will become taxable i.e. contributions will be disallowed on the contributing employer and be subjected to tax. This is not withstanding the fact the associations have employees who remit PAYE on their salaries as well as hosting events and trainings on which they pay indirect taxes like VAT*

ii) Expenditure of capital nature incurred in that year of income by a person, on legal costs and other incidental expenses, relating to authorization and issue of shares, debentures and similar securities offered for purchase by the general public. *This will discourage public listing of companies on the stock exchange due to high listing costs. This will not attain the intended tax goal since the costs might not be incurred at all.*

iii) Expenditure of capital nature incurred in that year of income by a person, on legal costs and other incidental expenses, for purposes of listing on any securities exchange operating in Kenya, without raising additional capital

iv) Expenditure of capital nature incurred in that year of income by a person on rating for the purpose of listing on any securities exchange operating in Kenya

v) Club subscription paid by an employer on behalf of an employee. *This is considered a benefit and thus taxed on the employee currently. If it is disallowed then the employee will not be taxed, therefore the expected revenue collection is flat i.e. moving from employee to employer.*

vi) Expenditure of capital nature incurred in that year of income with prior approval by the Cabinet Secretary, by a person on the construction of a public school, hospital, road or any similar kind of social infrastructure. *This will discourage corporate Social responsibility (CSR) activities by companies and individuals. It will therefore reduce the indirect taxes earned from the CSR activities purchases.*

vii) Registered home ownership savings plan. *The HOSPis being replaced by National housing relief .*

5. **Removal of existing tax incentive, that is, income exempt from tax** (clause 8): - several types of existing income that is exempt from tax are proposed to be removed, with the effect of making a tax saving of about **Kshs. 1.5 billion.** They are:

i) Income of a registered home ownership savings plan.

ii) Income of NSSF*. This should be the best Pension scheme because of the high membership numbers. The taxation of NSSF income will expose other pension schemes to tax in future removal of tax exemptions. Example of Tanzania and Uganda NSSF which are big corporate players.*

iii) Bonus, overtime and retirement benefits not exceeding 10%*. This exemption was made irrelevant by the increase of the tax free threshold to Kshs.24,000*

PROPOSED AMENDMENTS TO THE VALUE ADDED TAX (VAT)

The proposed amendments to the VAT are covered in clauses 10 - 12 of the Finance Bill, 2020. In summary, the key proposed amendments include:

1. A new condition for claiming input VAT (clause 10): - the proposed amendment introduces a new condition (requiring taxpayers to ensure their suppliers declare their invoices in the tax return) for them to qualify to claim the input VAT. This measure is likely to enhance compliance. Nonetheless, it may also be cumbersome for taxpayers due to logistics and the associated compliance cost, considering that the burden is being transferred from KRA to taxpayers. This clause negates the clause no .3,4 and12 of the same VAT act

(3) Tax on a taxable supply shall be a liability of the registered person making the supply and, subject to the provisions of this Act relating to accounting and payment, shall become due at the time of the supply.

(4) The amount of tax payable on a taxable supply, if any, shall be recoverable by the registered person from the receiver of the supply, in addition to the consideration.

12. (1) Subject to subsection (3), the time of supply, including a supply of imported services, shall be the earlier of –

(a) the date on which the goods are delivered or services performed;

(b) the date a certificate is issued by an architect, surveyor or any other person acting as a consultant in a supervisory capacity;

(c) the date on which the invoice for the supply is issued; or

(d) the date on which payment for the supply is received, in whole or in part.

The clause will lead to tax leaks where suppliers delay declaration of output VAT

2. Items to be removed from VAT exemption list (clause 11): - several items that are currently in the VAT exemption list have been proposed to be removed so as to apply the standard rate of 14%. This measure is likely to yield about **Kshs. 4 billion**. These items include:

i. Some helicopters and aero planes not exceeding 2,000 kg

ii. Tractors, other than road tractors for semi-trailers. *VAT on tractors will increase cost of agricultural machinery and thus affect food production*

iii. Aircraft pneumatic tires. *This will increase aircraft operational costs since local travel income is exempt and international travel is zero rated.*

. Goods for clean cooking stoves. *This will load output VAT on the stoves thus making them expensive and thus revert the population to the traditional jiko. It also negates the initial attraction to investors in this industry*

v. Stoves, cookers, barbecues

vi. One motor vehicle imported by a returning public officers from foreign posting

vii. Plant, machinery and equipment for the construction of plastic recycle plant

viii. Services such as hiring of helicopters

However, some tax incentives have been introduced. They are such as the VAT exemption on maize (corn) seeds as well as ambulance services. The VAT exemption on maize seeds is likely to disadvantage local producers of such seeds.

3. Removal of some items from VAT Zero rated category (clause 12): - It is also noted that some two items have been proposed to be removed from VAT zero rate list. They are the liquefied petroleum gas and materials for the manufacture of automotive and solar batteries. *The implication is that LPG will be subject to 14% VAT which will make it more expensive and thus revert many users to wood fuel since Kerosene is already very expensive due to direct taxes and VAT imposed at 8%.VAT on automotive batteries and solar batteries will negate the green energy effort*

AMENDMENTS TO THE TAX PROCEDURES ACT

The proposed amendments to the Tax Procedures Act are covered in clauses 15 - 16 of the Finance Bill. In summary, the key proposed amendments include:

1. Introduction of voluntary tax disclosure programme (clause 15): - this clause seeks to introduce this programme as a form of amnesty for taxpayers who may choose to disclose the tax liability from July 2015 to July 2020 for the purpose of being granted relief from paying penalty and interest. The amnesty will be granted at 100% waiver of penalty and interest if payment of assessed or disclosed tax is paid in the first year of being granted relief, 50% in the second year and 25% in the third year. Finally, this amnesty shall not apply to ongoing process such as audit, investigation or litigation.

2. Provides for appointment of digital tax service agent (clause 16): - the proposed amendment seeks to provide for the appointment of digital tax service agent, a new tax that is proposed to be introduced under clause 4. It also provides for revocation of the appointment.

QUESTIONS AND ANSWERS

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