

Promises and delivery: Kenya's 2015/16 National Budget

Direct tax

PwC analysis and outlook

Budget highlights
2015/16

Income Tax

Relief for investors as tax loss carried forward, period extended

The Finance Act 2009 restricted the carry forward period for tax losses to four years. Any carry forward beyond this would require the approval of The National Treasury.

The Cabinet Secretary (CS) has proposed amendments to the Income Tax Act to allow the carry forward of tax losses for ten years.

This amendment is important to companies undertaking huge capital projects which are likely to have tax losses due to accelerated /enhanced capital allowances.

Although the effective date of the proposed amendment was not stated, it is expected that this will apply retrospectively to include tax losses accrued prior to 2015.

It is hoped that taxpayers will still be able to apply to The National Treasury for extension of the ten year period where the tax losses have not been utilised within such a period subject to compelling commercial reasons.

Relief for stockbrokers but more clarity needed

The re-introduction of tax on capital gains on transfer of property situated in Kenya came with significant challenges mainly attributable to the fact that the 1986 legislation that was reinstated last year was antiquated

and did not take into account changes in the Kenya economy.

One of the key issues was that there was a lack of clarity on the stockbrokers' obligation to withhold tax on the sale of shares of their clients.

The CS has proposed the following amendments to the Income Tax Act:

- Introduced withholding tax provisions in respect of the sale of shares
- Stipulated a rate of 0.3% on the transaction proceeds of the sale of shares, thus removing the administrative complexity of determining the capital gain in relation to each share

The proposed changes to the ITA simplify and clarify the stockbroker's tax obligations.

It will however levy a tax even in cases where there is a net loss which was not the case in the previous legislation.

The 0.3% rate on transaction value is only applicable on listed shares as unquoted shares are still taxable at 5% of the net gain. The difference in tax rates between listed and non-listed shares may be viewed in some quarters as inequitable.

However, the changes to the capital gains legislation do not address issues such as:

- the due date for tax on capital gains,
- accounting for tax on capital gains by residents on property other than listed shares especially on gains from property other than shares listed in the NSE and
- indexation allowances to avoid taxing inflationary gains.

New measures to increase tax compliance in the rental income sector

Tax collection from the real estate sector has still been low despite efforts made by the KRA.

The National Treasury has now proposed new measures to address the low level of tax compliance in this sector.

In a bid to simplify and bring landlords into the tax net, landlords earning gross rental income of less than KES 10 million per annum from residential property will now pay tax at a rate of 12% of their gross rental income which shall be final tax. It is expected that tax payers will have the option to elect between the proposed gross rate or the current net rate.

The CS has proposed a tax amnesty for landlords who have not fully declared their rental income. The landlords will be required to pay the principal tax for 2014 and 2015 and the Commissioner will waive all taxes, penalties and interest arising for all years prior to 2014. It will also waive the penalties and interest arising on the tax payable for the 2014 and 2015 year of income.

The intent of the tax amnesty is to ensure that landlords are brought in to the tax system.

Enhanced allowances for the shipping industry

The eligible tonnage for capital allowance in the shipping sector has been reduced from 495 tons to 125 tons. Further, the rate of investment

deduction has been increased from 40% to 100%.

The tax incentive appears to be an attempt by the Government to attract investments in the maritime industry in line with the anticipated developments in port infrastructure, offshore energy and shore operations.

Tax rebates on hiring graduates

Although the details are still unclear, the CS has proposed a tax rebate for apprenticeship where a company engages at least ten graduates for a period of 6-12 months during a year of income. The tax rebate would then be available in the subsequent year.

Gaming tax

The CS has introduced a simplified gaming tax, which will be a direct charge on the gross gaming revenue. The tax covers public lotteries which will be taxed at 5% of the lottery turnover and bookmakers at 7.5% of the gross betting revenues. Also, all prize competitions where the costs of entry are premium shall be taxable at 15% of the total gross revenue.

Creation of a favourable filming destination

Foreign actors and crews will now not be subject to Kenyan withholding tax. This is intended to promote Kenya as a premier filming destination by attracting renowned personalities and technical expertise to enhance the quality of local productions.

Changes affecting the extractive industry

Payments to non-resident mining sub-contractors will now be subject to withholding tax at the rate of 5.625% (which is a final tax) on the gross amount of the service fees. This amendment aligns the withholding tax rate on service fee payments to the petroleum exploration and production sector.

Training fee paid to non-resident entities by a petroleum company or a mining company will be subject to a lower withholding tax rate of 12.5% on the gross amount payable. This is to bring uniformity in the rate of

withholding tax applicable to management or professional services. The withholding tax rates applicable on payments to resident entities remain unchanged at 5%.

However, there appears to be a lack of clarity on whether mining companies are also eligible to apply the lower rate of 12.5% withholding tax to non-resident providers of management or professional services as is available to petroleum companies on such payments. Further, the distinction between a non-resident provider of management or professional fees and a sub-contractor has not been clarified. This could potentially complicate the correct applicable withholding tax rate, i.e., 5.625% or 12.5%

Given the significant pressure on the prices of commodities (including the recent fall in oil prices) in the recent past and the resultant slowdown in exploration activity, there was the expectation that the CS would propose additional measures to support investment in the industry, such as:

- introduction of relief from capital gains tax on reinvestment of disposal proceeds,
- enhancement of the cost base for capital gains tax purposes to include post acquisition and incidental cost,
- limiting the taxation of indirect transfers to gains attributable to Kenya,
- exemption on inter-group reorganizations or restructuring transactions and
- exclusion of mobilization and demobilization costs from service fees.

Missed opportunities

While there have been a number of proposed amendments in this year's Finance Bill, it is noted that some of the expectations of taxpayers were not fully addressed. We have listed some of these missed opportunities below.

- Treasury has retained the unilateral limitation on benefits in the Income Tax Act which dilutes the effect of Double Tax Treaties.
- Having restricted the carry forward of tax losses and introduced tax on capital gains, it would have been expected that the compensating tax would have been removed as it is punitive for companies which have accelerated capital allowances.
- While Treasury has exempted asset transfers into REITs from stamp duty, tax on capital gains is still applicable on such transfers.
- The individual tax bands have not changed for over ten years despite the increased cost of living and year-on-year increase on the minimum wage. The expectation was to have expanded tax bands to cushion the low income earners and achieve equity by taxing the high income earners more.
- With Kenya increasingly becoming a regional hub, the government should have provided incentives from an employee perspective to ease movement and sharing of human resources.