Tax Alert
Budget 2013 / 2014

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Following the budget statement read by the Cabinet Secretary, the Finance Bill 2013, Value Added Bill 2013 and the Tax Appeals Tribunal Bill 2013 have now been published. We highlight some of the proposed changes to the tax laws contained in these three bills. However, the Provisional Collection of Taxes and Duties Order which authorizes the enforcement of the taxes and duties has yet to be published.

5 July 2013

Finance Bill, 2013

For the first time this year the budget statement was not accompanied by the Finance Bill as was traditionally the case. This is in accordance with the Constitution of Kenya, 2010 and the Public Finance Management Act, 2012. Amid much anticipation from the public, the Finance Bill, 2013 (FB, 2013) has now been published.

We have highlighted in this tax alert some of the proposed changes introduced by the FB, 2013 together with their effective dates. As pertains to Customs and Excise, we have also highlighted amendments to the East African Community Customs Management Act, as agreed by the EAC Finance Ministers and the Sectoral Council on Trade, Industry, Finance and Investment (SCTIFI).

Income Tax

The following are the proposed amendments under the Income Tax Act. The effective date for all of them is 1st January 2014.

Group life insurance premium for employees not taxable

The FB, 2013 has clarified that group life insurance premium paid on behalf of an employee by the employer is now tax exempt. However, such premiums will remain taxable if there is a benefit accruing to an employee or his dependants.

It remains unclear what the value and the tax point of the taxable benefit is where a benefit accrues. Is the value the premiums paid or the compensation received? Further, any group life policy benefit would only accrue when the event crystallises (upon death of the employee).

Winnings from betting and gaming

A final withholding tax of 20% of gross winnings will apply to both residents and non-residents.

30% of disputed tax payable on appeal against refusal of notice of objection

The FB 2013 now provides that a person aggrieved by the refusal of the Commissioner to admit a notice of objection may, on paying to the Commissioner that part of the amount of tax assessed that is not in dispute and 30% of the tax in dispute, and on paying any interest due, appeal to a local committee whose decision shall be final.

You can now apply to the Commissioner to compound offenses

In order to expedite dispute resolution, the Commissioner has been given additional powers to impose fines in lieu of prosecution where an offense subject to a fine has been committed by a taxpayer. He can only exercise this power if the taxpayer admits in writing that he has committed the offense and requests the Commissioner to deal with the offense under this provision.

A committee of not less than three officers will be constituted by the Commissioner to consider applications for the compounding of offenses. The Commissioner will not be able to delegate power to compound offenses.

Court order for payment of taxes by corporate officials

Under the Income Tax Act, directors and senior officers of corporate bodies can be held personally liable for tax offenses committed by the corporate body. The court can now direct such persons to make payment to the Commissioner of the whole or such part as remains unpaid of the tax assessed by the Commissioner either in addition to, or in substitution of, any other penalty.

KRA given powers to search and seize without warrant of court

The Commissioner or an authorised officer may, without warrant of court, search and seize relevant information while looking into the affairs of a person where the person has or is reasonably suspected of committing an offense under the Income Tax Act.

Previously, a warrant from a magistrate to search and seize any information was required.

Free exchange of information between treaty countries

The FB, 2013 provides that there shall be free exchange of information relating to income taxes or taxes of a similar character between Kenya and countries with which it has entered into a Double Tax Agreement. This change extends the waiver from the official secrecy provisions under the Income Tax Act, to such information.

Income tax exemption to armed forces revoked

The FB, 2013 has excluded Paragraph 26(a) of the First Schedule to the Income Tax Act which previously allowed for exemption on the income of the armed forces of a country to which section 95 of the old constitution applied. The Constitution of Kenya, 2010 provides no such tax exemption.

Assignment of rights by Oil Companies

The Finance Act 2012 introduced a withholding tax on the consideration from the assignment of rights by an oil company. This was a final tax. The FB, 2013 proposes an amendment to make the tax paid not a final tax for oil companies. An oil company has been defined to mean a petroleum company within the meaning of the Ninth Schedule to the Income Tax Act i.e. companies that have entered into a petroleum agreement with the Government of Kenya.

Value Added Tax

Zero-rated sports goods and equipment

The FB, 2013 has made changes to the definition of sport goods and equipment which can be zero rated; Goods and equipment intended solely for the development of sports in Kenya and not for sale, imported or purchased by , or donated to, registered sports organization upon recommendation by the Ministry responsible for sports, shall be zero rated.

The effective date is 18th June 2013

However, the Value Added Tax Bill 2013 proposes to make all the above items taxable.

Customs duty

Customs warehouse rent on cleared goods

Customs warehouse rent shall now be charged on cleared goods that remain at the port of discharge for a period exceeding 21 days from the date of *commencement of the discharge of the carrier. Previously such customs warehouse rent was only* applicable to goods not cleared and stored in a customs warehouse.

Restoration of seizures

The Sectoral Council on Trade, Industry, Finance and Investment ("SCTIFI") has amended section 218 of EACCMA to empower the Commissioner to restore seizures.

Customs agency license renewal

Customs agency licenses shall be renewed for a period not exceeding three years to address the challenges associated with renewal of customs agent's licenses at the end of every year.

Amendments to Part B of the Fifth Schedule of EACCMA

- ***Software deleted***

  Software shall be deleted from exemptions under the Fifth Schedule as the item is provided for at 0% duty rate in Chapter 85 of the EAC Common External Tariff (CET).

- ***Exemption of plastic biogas digesters***

  Plastic biogas digester shall be exempt of customs duty.

  The effective date is 1st July 2013

- ***Exemption of goods used to facilitate railways operations***

  Specific goods used to facilitate railways operations shall now be exempt from duty.

  The effective date is 1st July 2013

- ***Exemption of water treatment effluent plants***

  Water treatment effluent plants shall now be exempt from duty.

  The effective date is 1st July 2013

Railway Development Levy

A Railway Development Levy shall be paid on all goods imported into the country for home use at the rate of 1.5% of the customs value of the goods. This levy shall be for the construction of a standard gauge railway network in order to facilitate the transportation of the goods.

The amendment under the Customs and Excise Act provides for a levy on all goods imported into the country.

The effective date is 1st July 2013

Duty remission

The following items shall enjoy duty remission as specified;

- Duty on wheat grain remitted by 90% to a rate of 10% for one year.
- Duty on glucose and glucose syrup has been reduced from 10% to 0% for one year.
- Duty on a number of paper and paperboard products has been reduced to 10% from 25%.

The effective date is 1st July 2013

Amendments to the EAC CET

Duty has been increased on the following items as specified to protect local industries:

- Welding electrodes from 10% to 25%
- Millstones and grindstones from 0% to 25%
- Plastic tubes for packaging of toothpaste, cosmetics and similar products from 10% to 25%
- Towers and Lattice masts to stay at 10% instead of 0% for another one year

The effective date is 1st July 2013

Excise duty

Refusal to grant license for manufacture of excisable goods

The Commissioner shall be required to furnish an applicant with reasons for refusal to grant such applicant a license for manufacture of excisable goods.

Reasons shall also be given where the Commissioner refuses to grant an application by a licensee to manufacture another class of excisable goods on his ceasing to manufacture in that factory the class of excisable goods specified in the license.

The effective date is 18th June 2013

"Financial institution" defined

The FB, 2013 now provides a definition for the term financial institution. The term "financial service providers" will be substituted with the term "financial institution" in the Fifth Schedule of the Customs and Excise Act.

For purposes of excise duty on fees charged for money transfer services and other fees, "financial institution" means

- A person licensed under the Banking Act, the Insurance Act, the Central Bank of Kenya Act or the Micro Finance Act, 2006;
- A Sacco registered under the Sacco Societies Act, 2008; or
- The Kenya Post Office Savings Bank Act.

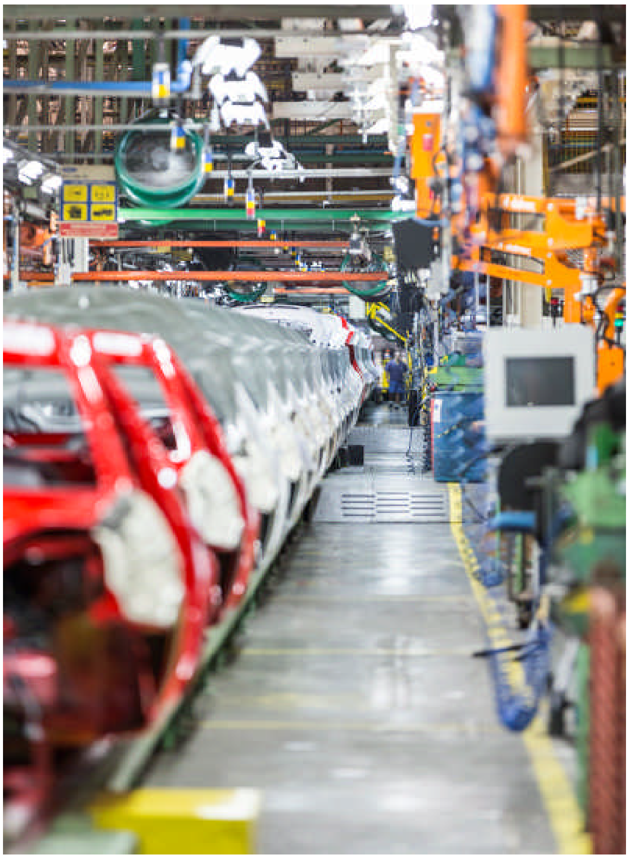
The effective date is 18th June 2013

There is still lack of clarity on who is responsible for the collection and payment of the excise duty on these services.

Wait for it…

In the Cabinet Secretary's budget statement, mention was made of the following which have not been included in the FB, 2013.

- Capital gains tax on real estate, marketable securities and other saleable assets.
- Tax incentives to tax compliant employers who engage college and university graduates who have no job experience.
- The Cabinet Secretary proposed to exempt both group life and group personal accident premiums from tax, the FB, 2013 only refers to group life covers.



VAT Bill 2013

VAT on basic commodities still on

The Value Added Tax (VAT) Bill, 2013 has been gazetted. The VAT Bill, 2013, is to a large extent similar to the then VAT Bill, 2012. It has retained provisions of the former Bill which seeks to streamline the administration of VAT and to ease compliance.

But contrary to the expectation of many and despite promises to reduce the cost of living for the "mwananchi" the Bill has come out as a big disappointment. The Bill proposes to tax basic foodstuffs and medicaments. In this alert we have focused on the changes in the VAT Bill, 2013, to the VAT Bill 2012.

What is new?

The VAT Bill, 2013 has made minimal but significant changes to the VAT Bill 2012.

- Tax disputes arising under the VAT Act to be handled by the proposed centralised Tax Appeals Tribunal. The Bill (Tax Appeals Tribunal Bill, 2013) establishing this Tribunal is already published. A transition period is provided for those cases presently under appeal to the VAT Tribunal.

- In line with the above amendments, sections on appeals, offences and evidence have been deleted from the VAT Bill, 2013 and inserted in the Tax Appeals Tribunal.

- Fertilisers under Chapter 31 have been brought into the list of exempt goods. This could make imported fertiliser relatively cheaper to locally manufactured fertiliser.

- The VAT Bill, 2012 had provided for the zero rating of medicaments and medical supplies on a three (3) year transition basis. The VAT Bill, 2013 proposes to immediately tax at 16%, the said goods.

- Taxable supplies to official aid funded projects will be taxed at the standard rate.

Key concerns ignored

Some of the key areas that this Bill was expected to address but which were ignored all together include:

- VAT on basic commodities such as sugar, unga bread, milk products & dairy inputs, text books and newspapers have been retained at 16%.

- We expected mining and petroleum exploration to be treated similarly, with their inputs being zero rated. However VAT on inputs to the mining sector has been retained at 16%. This will have a negative impact on this nascent industry.

- Medicaments and medical supplies have been brought to tax at 16%. This is despite Government's pledges of improving access to healthcare.

- Machinery under chapter 84 and 85 of the Common External Tariff (CET) has been classified as exempt as opposed to being zero rated. This is likely to have a negative impact on the local producers of such machinery as they will not be able to recover the input VAT incurred.

- There are no transitional clauses on projects currently under VAT remission scheme.

The Tax Appeals Tribunal Bill, 2013

This bill establishes a Tax Appeals Tribunal (“the Tribunal”) for the management and administration of tax appeals and will come into effect on such date appointed by the Cabinet Secretary in a Gazette notice.

The move to introduce a single appeal body resourced by professionals is a positive move in the tax dispute resolution mechanism. However, the current administrative simplicity of the tax dispute resolution mechanism should be maintained. The tax appeal body set up under the bill is more judicial in nature, in fact it will be headed by a person qualified to be a judge of the High Court of Kenya. Any sitting panel has to be chaired by an advocate of the High Court of Kenya and the decision thereof will have the force of law as a subordinate court.

The underlying tax laws have to be brought in line with the Tax Appeals Tribunal Bill as the right to appeal has been made subject to the relevant tax laws. This will ensure that the right to appeal to the Tribunal against any decision of the Commissioner is preserved

We provide further analysis of the bill below.

Right of appeal

The bill gives a right of appeal to the Tribunal to a person who disputes the decision of the Commissioner on any matter arising under the provisions of any tax law. The term “tax laws” has been defined to include the Income Tax Act, the Customs and Excise Act or the Value Added Tax Act. Tax has also been defined to include duty, tax or any imposition levied under any tax laws.

The right of appeal under the bill has however been made subject to the provisions of the relevant tax law. This could potentially create a conflict as, for example, under the Income Tax Act the right to appeal to the local committee or tribunal has to be conferred by an enabling section of the Act.

For a more effective and speedy dispute resolution process, the bill should make it clear that tax payers have a right to appeal to the Tribunal against any decision made by the Commissioner under any of the tax laws.

A non-refundable appeal fee of KES 20,000 is payable by the appellant before appealing.

Repeal of existing appeal tribunals

The bill amends the tax laws to be in conformity with the introduction of the Appeals Tribunal by repealing section 82 (and any notice made thereunder) and 83 of the Income Tax Act, section 32 of the VAT Act and section 127E of the Customs and Excise Act. Any on-going appeals before the legacy appeal tribunals will be granted a period of 6 months after the commencement of the Tax Appeal Tribunal Act to conclude. Any cases which are not concluded within the 6 months will be taken over by the Tribunal.

There are other provisions which have not been amended in the Acts which refer to the legacy tribunals – local committee and tax tribunal. These need to be made consistent to avoid creating confusion on the appeal process.

Membership

The membership of the Tribunal shall consist of a chairperson, who needs to be qualified to be appointed as a judge of the High Court, as well as a maximum of twenty other members. The members being of high moral character and integrity need to be tax compliant and holders of degrees in law, business, finance, economics, insurance or related discipline with at least five years relevant experience.

A panel hearing any matter shall be constituted by the Chairperson and shall be made up of at least three members one of whom shall be an advocate of the High Court. Where the chairperson is not a member of a sitting panel he shall designate one of the members of the panel who has to be an advocate of the High Court to preside over the proceedings.

Procedure for appealing

A notice of appeal shall be submitted to the Tribunal within 30 days upon receipt of the Commissioner’s decision. The appellant shall then within 14 days submit a memorandum of appeal, statements of facts and the Commissioner’s decision. The bill requires the appellant to serve a copy of the appeal to the Commissioner within two days after giving the notice of the appeal to the Tribunal. This appears to be a very short time within which to serve the appeal and perhaps they meant the notice of appeal?

Power to issue an order to stay

The Tribunal has been given the power to issue an order staying the implementation of the Commissioner’s decision under review as it determines it.

Power to summon a witness

The Tribunal shall have the powers of a subordinate court to summon a person to appear before it to give evidence or produce books or documents. It shall also have the power to interrogate witness and examine witnesses abroad.

Contempt of Tribunal

This is a punishable offense on conviction which attracts a fine not exceeding KES 100,000 or imprisonment for a term not exceeding 6 months or to both. Refusal to obey a summons or failure to adequately respond to the information requested is an offence liable on conviction to a fine not exceeding KES 100,000 or to imprisonment for a term not exceeding 3 years or to both.

Settlement out of Tribunal

The parties to a dispute may at any stage during the proceedings apply to the Tribunal to be allowed to settle the matter out of the Tribunal. This is supported by the power to compound offenses given to the Commissioner under the ITA.

Order for costs

The Tribunal has the power to award costs in any appeal. The legacy tribunals did not have such power which has traditionally been a reserve of a court of law. The parties to the dispute would be required to pray for such orders in their submissions.

Decision in writing to be served on each party

The Tribunal shall give reasons in writing for its decision, including its findings on material questions of fact and reference to the evidence or other material on which those findings were based. This decision shall be served on each party to the proceedings and shall take effect on the date the notice of the decisions is given or such other date as may be specified by the Tribunal in the notice.

Right of further appeal to the High Court

A party has a right to within 30 days of the Tribunal decision appeal to the High Court. The ITA has rules prescribing the appeal process to the High Court and provides for the appeal to be made within 15 days. This is an example of some of the conflicts between the two legislations that need to be addressed before the bill passes into law.

Please speak to you usual PwC contact or any one of us for guidance and clarity.

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Other bills published

In accordance to his budget statement the Cabinet Secretary has also published other bills aimed at deepening the financial sector. These include:

- The Capital Markets (Amendment) Bill, 2013
- The Microfinance (Amendment) Bill, 2013
- The Insurance (Motor Vehicle Third Party Risks) (Amendment) Bill, 2013
- The Insurance (Amendment) Bill 2013
- The Kenya Deposit Insurance (Amendment) Bill, 2013

We will issue a separate alert on these.