Global Tax Alert

Kenya issues 2015/2016 Budget

Executive summary

On 11 June 2015, the Kenyan Government issued the budget policy and revenue raising measures for fiscal year 2015/2016. The tax measures proposed through the Finance Bill, 2015 (the Bill) are intended to facilitate public sector growth so as to accelerate industrialization and the creation of jobs; promote equity and fairness; deepen tax administration reforms and ease compliance while reducing the cost of doing business; and finally encouraging growth and stability in the financial sector.

Some of the key changes proposed include amendments to the capital gains tax regime, introduction of a tax on residential rental income and tax measures affecting the film industry.

This Alert outlines the key income and indirect tax changes as proposed in the Bill. The changes are proposed for the income tax year 2016 and would take effect as of 1 January 2016.

Detailed discussion

Business and personal taxation

Capital gains tax (CGT)

*Taxation of gains from investment shares*

Under the Bill, gross consideration payable to both a resident and nonresident person in respect of a transaction relating to securities listed on any security exchange approved under the Capital Markets Act has been brought under the ambit of withholding tax. The withholding tax rate applicable is 0.3% of the transaction value. However, only transactions by nonresident investors appear to have been covered through amendments in the Finance Bill which is silent on the rate applicable to residents. This seems to be an inadvertent omission which is expected to be addressed before the Bill is signed into law. Stockbrokers are charged with the responsibility of collecting and remitting the tax to the Commissioner.
Currently, gains from investment shares are subject to CGT at a rate of 5% on the excess of transfer value over adjusted costs.

This proposal is aimed at simplifying the taxation of such gains. The adjusted and incidental cost will not be deductible since the tax will be on gross proceeds which may lead to taxation of loss making counters.

**Taxation of gains on property other than investment shares**

The Eighth Schedule of the Income Tax Act (ITA) is amended to exclude the following transfers from the ambit of CGT:

- Transfer of land where value is not more than three million shillings. Currently, the transfer value was capped at thirty thousand shillings.
- Transfer of agricultural property having an area of less than fifty acres if the property is situated outside a municipality, gazetted township or an area declared by the minister, by notice in the Gazette, to be an urban area for the purpose of this Act. Currently, the acreage is capped at one hundred acres.
- Administration of an estate of a deceased person within two years of the death of the deceased or after finalization of a court case regarding such estate.
- Transfer of property between spouses, or former spouses or their immediate family (children of the spouses or former spouses) as part of divorce settlement or bona fide separation agreement).

CGT will however be applicable on compensation for property acquired by the Government for infrastructure development. This is currently exempt from CGT.

CGT is to be payable on or before the date of application for transfer of the property is made at the relevant Lands’ office.

The above amendments seek to harmonize the tax law to the prevailing economic and social conditions in addition to increasing revenue collection, as well as streamlining the collection of the tax with the other government fees upon transfer of property.

**Tax loss utilization period**

The period within which a taxpayer must utilize their tax loss utilization had been limited to the year the loss occurred and the subsequent four years. This change was introduced in January 2010.

The Finance Bill had attempted to amend this by empowering the Commissioner to extend the loss utilization period to 10 years. However, the amendments as proposed still maintain the utilization period to four years with tax payers still being required to apply to the Minister (through the Commissioner) for any further extensions. It is expected that the correct amendments will be introduced before the Finance Bill is signed into law.

The increase in the loss utilization period is aimed at boosting investment in capital intensive industries such as power generating companies, manufacturers and hotel operators that accrue tax losses in the earlier years of operation.

**Definition of training fees**

The definition of “training fees” has been clarified through a proviso which specifically states that training fees does not include:

(i) fees paid for educational services provided by a prep-primary, primary or secondary school; (ii) a technical college or university; and (iii) an institution established for promotion of adult education, vocational training or technical education.

**Income from residential property**

A resident person making a rental payment for the occupation of immovable property will be required to deduct and remit withholding tax on this payment. The Commissioner has been empowered to appoint agents who will be required to remit withholding tax on rent paid to resident landlords.

Currently, only a rental payment made to a nonresident person for occupation of property is subject to withholding tax.

Collection of income from residential property has been hindered by a number of administrative challenges. This measure is aimed at bringing this income into the tax bracket and accelerating collection of tax on rental income.

**Film Industry**

The taxation changes in the film industry are aimed at spurring growth as well as promoting talents of the Kenyan youth.
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Payments made to actors and crew members
Payments made by producers approved by the Kenya Film Commission to nonresident actors, crew and supporters of appearance or performance of an activity for the purpose of entertaining the audience are included in the list of payments exempt from withholding tax.

Capital deduction
Capital expenditures on buildings in use for training of film producers, actors and crew are to be granted an Industrial Building Allowance at a rate of 100%. Currently, the applicable rate is 50%.

Rebate to employers with apprenticeship programs
Employers who engage at least ten university graduates for a period of six to twelve months during any year of income are eligible for a tax rebate. The amount of rebate is to be stipulated by the Cabinet Secretary through issuance of regulations.

The move is targeted at improving the quality of the skilled manpower in the country.

Capital deductions
An investment deduction of 150% is available on building and machinery installed outside the municipality of Nairobi, Kisumu or Mombasa of value not less than 200 million scrapped. The applicable investment deduction on investments outside the mentioned municipalities shall be at the standard rate of 100%.

An investment deduction on purchase of a new and previously unused power driven ship increased to 100% from 40% and the tonnage of qualifying ships reduced from 495 tons to 125 tons.

Corporate tax rate
A company introducing its shares through listing at the Nairobi Securities Exchange will enjoy a reduced rate of 25% rather than the standard rate of 30%. Currently, the preferential rate of 25% can only be enjoyed by companies which have listed at least 20% of their issued share capital.

This is to encourage companies to list in the securities exchange to spur capital markets’ growth.

The extractive industry
Fees payable to subcontractors in mining operations will be subject to withholding tax at a rate of 5.625% down from 20%. This harmonizes the tax treatment of payments to subcontractor in the mining and petroleum exploration operations.

In addition, training fees payable by contractors will be subject to withholding tax at 12.5% down from 20%.

This is aimed at harmonizing the tax treatment of the players in the extractive industry and stimulating foreign direct investment in the sector.

Finally, investment income from a rehabilitation fund is exempt from taxation.

Value Added Tax (VAT)
The effective date for all VAT amendments in the Finance Bill, 2015 is 12 June 2015.

Definitions
The definition of “supply of imported services” is revised by deleting the words “or a non-registered person.”

This clarifies that a non-registered person has no obligation to account or pay VAT on imported services.

“Duty-free shop” is defined to mean “a bonded warehouse licensed by the Commissioner of Customs for deposit of dutiable goods on which duty has not been paid and which have been entered for sale to passengers departing to places outside Kenya.”

Lodging of VAT claims
The Finance Bill 2015 proposes to limit the time of lodging VAT claims to 12 months from the date the tax becomes due and payable.

Withholding VAT agents
Withholding VAT agents will now include any person appointed by the Commissioner to withhold VAT. Effective 19 September 2014, only Government Ministries, Departments and agencies were mandated to withhold VAT.

Tax modernization
As part of reforming the general tax administration regime, the following changes have been made and/or proposed:
• Tax Appeals Tribunal Act, 2013:
  – The Bill proposes that for a period of one year from the date of the Tribunal's first sitting, it may extend the period of a hearing up to sixty days should there be sufficient grounds to do so
  – The bill further proposes that the Tribunal shall hear and determine appeals relating to a tax decision made before its first sitting within a period of one year from the date of this first sitting

• Income Tax Bill expected to be completed by 30 September 2015

• Tax Procedures Bill has been released:
  – Bill tabled in parliament aimed at simplifying tax administration processes and also promoting consistency and efficiency in the tax laws as well as facilitating compliance and effective collection of taxes under the ambit of Income tax, VAT and Excise Duty

Endnote
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