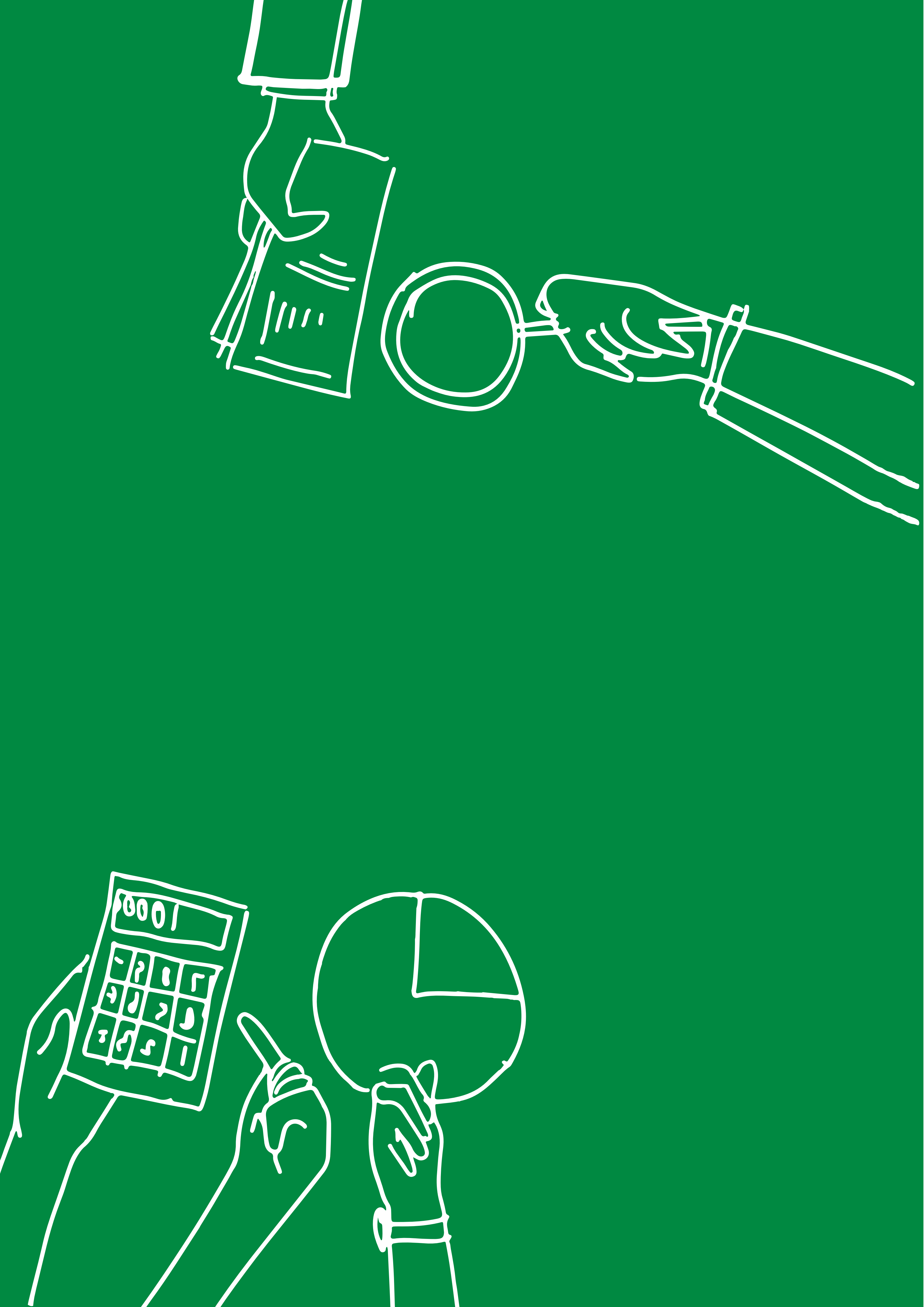
MZALENDO TRUST ANALYSIS OF THE FINANCE BILL 2023

MZALENDO

MAY 2023



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1.0 Background Information

The Bill formulates proposals announced in the Budget for 2023/2024 relating to liability, and collection of taxes. The Finance Bill 2023 amends finance related legislation including the Income Tax Act, the Value Added Tax Act, The Excise Duty Act, the Tax Procedures Act, 2015 and the Miscellaneous Fees and Levies Act, 2016. The Bill seeks to amend sections of other laws including: THE Betting, Gaming and Lotteries Act, the Kenya Roads Board Act, 1999, the Kenya Revenue Authority Act, 1995, The Employment Act, 2007, the Unclaimed Financial Assets Act, 2011, the Statutory Instruments Act, 2013, and the Retirement Benefits (Deputy President and Designated State Officers), Act, 2015.

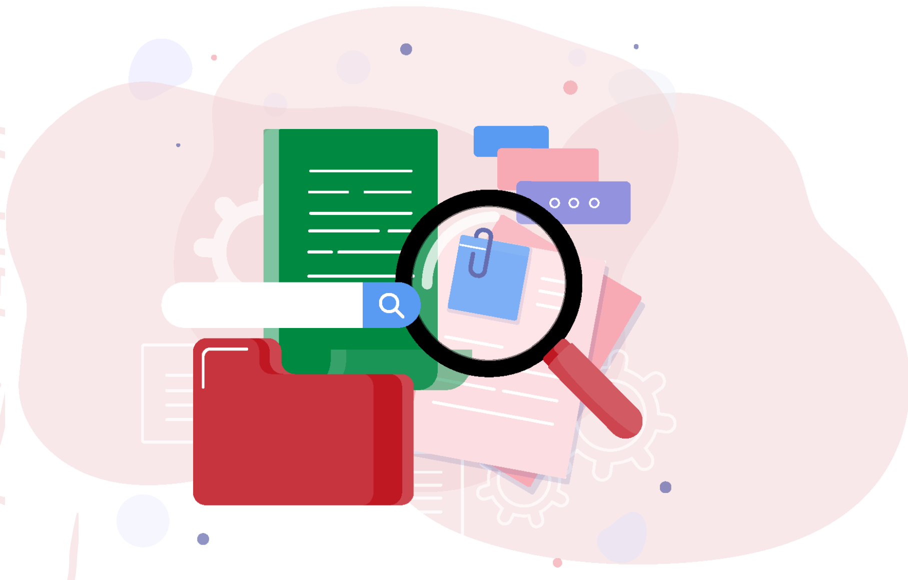
The Public Finance Management Act 2012 under section 39 and 40 stipulate principles for submission, consideration and passing of the Finance Bill.

Section 39A. of the PFM Act on Submission, consideration and passing of Finance Bill

1. The Cabinet Secretary shall submit to the National Assembly, on or before 30th April, the Finance Bill setting out the revenue raising measures for the National Government.
2. Following submission of the Finance Bill by the Cabinet Secretary, the relevant committee of the National Assembly shall introduce the Bill in the National Assembly.
3. The National Assembly shall consider and pass the Finance Bill, with or without amendments, in time for it to be presented for assent by 30th June each year.

Section 39(A)(4) of the PFM Act states that any recommendations made by the relevant committee of the National Assembly or resolution passed by the National Assembly on revenue matters shall—

a) ensure that the total amount of revenue raised is consistent with the approved fiscal framework;
b) take into account the principles of equity, certainty and ease of collection;
c) consider the impact of the proposed changes on the composition of the tax revenue with reference to direct and indirect taxes;
d) consider domestic, regional and international tax trends;
e) consider the impact on development, investment, employment and economic growth;
f) take into account the recommendations of the Cabinet Secretary as provided under Article 114 of the Constitution; and
g) take into account the taxation and other tariff arrangements and obligations that Kenya has ratified, including taxation and tariff arrangements under the East African Community Treaty.



2.0 Summary of The Provisions of the Finance Bill 2023

2.1 PROPOSED AMENDMENTS ON THE INCOME TAX ACT

#	Clause	Provision of the Bill (Income Tax Act)	Potential Impact
1	Clause 2(a): Amendment of Section 2 of Cap 470	The Bill proposes to amend Section 2 of Cap 470 "winnings" means the payout from a betting, gaming, lottery, prize competition, gambling or similar transaction under the Betting, Lotteries and Gaming Act without deducting the amount staked or wagered.	The proposed amendment seeks to provide clarity and elaborate on the definition of the term winnings in the Income Tax Act.
2	Clause 2(b): Digital Content monetization	The Bill provides a new definition, "digital content monetization" to mean the following: a) advertisement on websites, social media platforms or similar networks by partnering with brands including endorsements from sellers of such brands. b) sponsorship where a brand owner pays a content creator for content creation and promotion. c) affiliate marketing where the content creator earns a commission whenever the audience of the content creator clicks on the product displayed. d) subscription services where the audience pays a periodic fee to access the content and support the content creator. e) merchandise sales where physical goods and services are sold featuring a logo, brand, or catchphrase to the audience of the content creator, eBooks, courses, or software. f) membership programmes for exclusive content including early access. g) licensing the content including photographs, music or other businesses or individuals for use in the user's own projects; or h) crowdfunding for raising funds for specific goals for a content creator or another person.	The ever-increasing digitalization of businesses has accelerated the need to address the many challenges and issues around the corporate income tax regime. This has widened the scope for digital service tax with digital content monetization as defined now subject to Withholding tax at the rate of 15%.
3	Clause 9: Amendment of Section 12C. Turnover and Presumptive Tax	The Bill amends section 12C.onTurnover and Presumptive Tax by changing the bands for Turnover tax from the current KES 1 million to KES 50 million to KES 500,000 to KES 15 million. Furthermore, the Bill proposes to increase the turnover tax rate from 1% to 3%	This amendment expands the turnover tax base by targeting persons with turnover between KES 500,000 and KES 1 million who were not covered. Further, the Bill caps Turnover tax to persons with turnover of KES 15 million down from the previous KES 50 million. The change is important in bringing on board tax informal businesses and the sector into the tax bracket.
4	Clause 10: Digital Asset Tax	This is a new insertion to the Income Tax Act. The Income Tax Act is amended by inserting the following new section immediately after Section 12E- 12F. (1) Notwithstanding any other provision of this Act, a tax to be known as digital asset tax shall be payable by a person on income derived from the transfer and exchange of digital assets. (2) The owner of a platform or the person who facilitates the exchange or transfer of a digital asset shall deduct the digital asset tax and remit it to the Commissioner	The definition targets digital assets or technology related to such as convertible virtual currency, cryptocurrency or any platform used to facilitate exchange of such.

2.0 Summary of The Provisions of the Finance Bill 2023

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#	Clause	Provision of the Bill (Income Tax Act)	Potential Impact
5	Clause 12: Enhancement of the Electronic Tax Invoice Management Systems (eTIMS) compliance	Section 16 of the Income Tax Act is amended- in subsection (1) by inserting the following new paragraph immediately after paragraph (b) c) any expenditure or loss where the invoices of the transactions are not generated from an electronic tax invoice management system except where the transactions have been exempted in accordance with the Tax Procedures Act, 2015	This proposal in essence enhances compliance with eTIMS by disallowing expenses that are not supported by eTIMS compliant invoices. eTIMS is a software solution which provides technological convenience that aims at reducing the cost of compliance for VAT registered businesses. Through integration with eTIMS businesses will benefit from real time invoice transmission providing accuracy in tax invoice declarations and reconciliation between filed returns and payments. The proposal promotes the adoption of eTIMS by ensuring that taxpayers only conduct business with suppliers who are VAT compliant. Nevertheless, most MSMEs and businesses are still grappling with challenges of onboarding eTIMS.
6	Clause 15: Filing of country-by-country report, master file and local file	The Bill amends Section 18D on Filing of country-by-country report, master file and local file to provide that "Each ultimate parent entity that is resident in Kenya shall file a country-by-country report with the Commissioner." This requires each ultimate parent entity resident in Kenya to file a Country By Country (CbC) report with the Commissioner. The Finance Bill further obligates a constituent entity (CE) of an MNE that is resident in Kenya to file a CbC report. It attaches the following conditions have to be fulfilled for a CE to file CbC report in Kenya. a) If the ultimate parent entity is not obligated to file a country-by-country report in its jurisdiction of tax residence b) The jurisdiction in which the ultimate parent entity is resident has a current international tax agreement which Kenya is a party to but does not have a competent authority agreement with Kenya at the time of filing the country-by-country report for the reporting financial year; c) There has been a systemic failure of the jurisdiction of tax residence of the ultimate parent entity that has been notified by the Commissioner to the constituent entity resident in Kenya.	This is an important provision in international taxation. By definition globally, a Country by Country (CbC) reporting requires Multinational Enterprises (MNE) to file annually, a report containing information on their international allocation of the MNE's income, taxes and details of their economic activities in the various jurisdictions they have operations in. These conditions are aimed at ensuring that the CE resident in Kenya can be held responsible for submitting the CBC report.
	Clause 17: 21. Members' clubs and trade associations	The Bill proposes an amendment to Section 21 of Cap 470 on Members' Clubs and Trade Associations to in effect tax their entire business income. The Amendment reads as follows: "A body of persons which carries on a members' club shall be deemed to be carrying on a business and the gross receipts on revenue account (including entrance fees and subscriptions) shall be deemed to be income from a business"	This is to bring incomes of members' Clubs and Trade Associations under the ambit of taxation. It is important to note that currently, the income of clubs and trade associations is not taxed as long as 75% or more of the income for such an organization is from the members. The current stipulation has a proviso, *"Provided that where not less than three-quarters of such gross receipts, other than gross investment receipts, are received from the members of such club, such body of persons shall not be deemed to be carrying on a business and no part of such gross receipts, other than gross investment receipts, shall be income."* The Amendment further deletes subsection 2 of Section 21 which provides for the option of a trade association to decide on whether to be taxed. This in essence will see trade associations taxed on their business income.

2.0 Summary of The Provisions of the Finance Bill 2023

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<tr><th>#</th><th>Clause</th><th>Provision of the Bill (Income Tax Act)</th><th>Potential Impact</th></tr>
<tr><td></td><td>Clause 19: Post-retirement medical fund relief</td><td>The Bill amends Section 31A of the Income Tax Act by proposing to exempt from tax any investment income from a post-retirement medical fund including where the income is not part of a retirement benefits scheme, it reads as follows:

“A resident individual who proves that in a year of income the person has contributed to a post-retirement medical fund shall for that year of income be entitled to a personal relief in this Act referred to as the post-retirement medical fund relief”</td><td>This amendment is aimed at encouraging individuals to take up or make arrangements for post-retirement medical schemes.

Globally such schemes provide medical benefits to individuals looking to save towards their medical cover in retirement and their employers contributing to their employees’ post-retirement medical benefit</td></tr>
<tr><td></td><td>Clause 20: Amendment to Section 35 of the Income Tax Act</td><td>The Finance Bill 2023 amends Section 35 of the Income Tax Act by introducing withholding tax on sales, promotion and advertisement paid to residents’ persons in excess of Kshs. 24,000 per month at the rate of 5% of the gross amount</td><td>This brings marketing and advertisement services into the ambit of withholding tax</td></tr>
<tr><td></td><td>Clause 20:

Amendment to Section 35 of the Income Tax Act</td><td>The Bill proposes to charge Withholding tax at 15% on “digital content monetization”. This includes offering payment for entertainment, social, literal, artistic, educational or any other material electronically through any medium or channel, in the following forms:</td><td>The proposal intends to bring into the tax net, digital content creators or influencers in the wake of their mushrooming lucrative digital content business.</td></tr>
<tr><td>7</td><td>Clause 23: Second Schedule to the Income Tax Act Introduction of industrial building and dock allowances</td><td>The Bill proposes to introduce industrial building and dock allowances at a rate of 10% in equal instalments. Proposed definitions for an industrial building and a dock are as follows:
Industrial building: includes a building in use for the purpose of transport, bridge, tunnel, inland navigation water and electricity or hydraulic power undertaking.
Dock: Includes a container terminal berth, harbour, wharf, pier, jetty, storage yard, or other works in or at which vessels load or unload merchandise but does not include a pier or jetty used for recreation</td><td>The new amendment supports the shipping industry and encourages resident shipping businesses given the significant capital outlay in the set-up and operationalization of such businesses.</td></tr>
<tr><td></td><td>Clause 24: The Third Schedule

Monthly Rental Income rate</td><td>The Bill Finance Bill 2023 reduces the rate of Monthly Rental Income tax rate from 10% to 7.5%.

It is important to note that Monthly Rental Income Tax only affects residential rental income. Landlords, are required to pay rental income tax at a rate of stipulated under the Third Schedule on the gross rent received and is payable when they receive rent from their tenants either monthly, quarterly, semi-annually, or annually</td><td>This rate has been reduced to encourage tax compliance of property owners and boost the government’s revenue collection from rental income.</td></tr>
<tr><td></td><td>Pay-As-You Earn (PAYE)</td><td>The Finance Bill proposes to introduce a new PAYE tax band with a tax rate of 35% on employment income above KES 6,000,000 per annum. The updated tax bands are as tabled below:<table><tr><th>Amount per annum</th><th>PAYE Rate</th></tr><tr><td>On the first KES 288,000</td><td>10%</td></tr><tr><td>On the next KES 100,000</td><td>25%</td></tr><tr><td>On the next KES 5,612,000</td><td>30%</td></tr><tr><td>On all income over KES 6,000,000</td><td>35%</td></tr></table></td><td>The main objective of this amendment is to increase the tax revenue by increasing tax on employees earning more than KES 500,000 per month.</td></tr>
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2.0 Summary of The Provisions of the Finance Bill 2023

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2.2 PROPOSED AMENDMENTS ON THE VALUE ADDED TAX

#	Clause	Provision of the Bill (VAT)	Potential Impact
1	Petroleum products (excluding Liquid Petroleum Gas) to VAT at a standard rate of 16%.	The Finance Bill 2023 proposes to subject petroleum products (excluding Liquid Petroleum Gas) to VAT at a standard rate of 16%.	The VAT rate of 8% on petroleum products was introduced in the year 2018. This amendment, if assented to, will increase fuel prices and subsequently the prices of transport and production of goods
2	Liquefied Petroleum Gas	The Finance Bill 2023 exempts Liquefied Petroleum Gas (LPG) from VAT. VAT of 16 % on LPG was introduced through the Finance Act of 2020 but the implementation was suspended to July 2021 to deal with the high living costs. However, the Finance Act 2022, reduced the VAT on LPG to 8%	This is a welcome relief to consumers and households. Nevertheless, any input VAT incurred by the suppliers of LPG will become a cost and this may be passed on, to the consumers.
3	Clause 31: Clarification on VAT registration requirements for digital service providers	Section 34 of the Value Added Tax, 2013 is amended in subsection (1) by deleting the proviso and substituting therefor the following new proviso- "Provided that a person supplying imported digital services over the internet, an electronic network or through a digital marketplace shall register whether or not the taxable supplies meet the turnover threshold of five million shillings"	The Bill proposes to amend Section 34 of the VAT Act to explicitly require persons supplying imported digital services over the internet or an electronic network or though a digital marketplace to register for VAT, whether or not they have met the KES 5 million threshold.

2.0 Summary of The Provisions of the Finance Bill 2023

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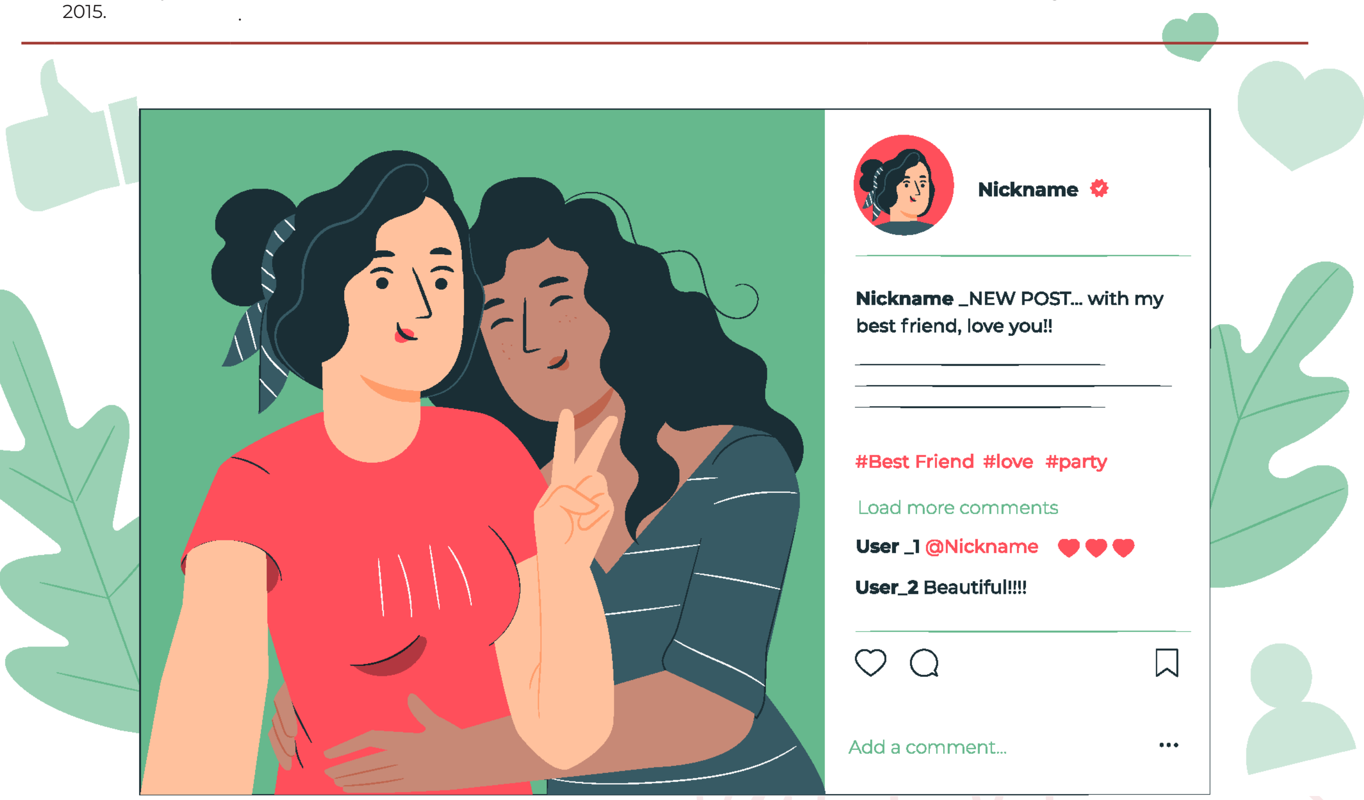
2.3 PROPOSED AMENDMENTS ON THE EXCISE DUTY

#	Clause	Provision of the Bill (VAT)	Potential Impact
	Annual Inflationary Adjustment	The Bill repeals the annual inflation adjustment. Currently, the Commissioner General has powers to adjust the specific rate of excise duty once a year to consider inflation.	This is important to the taxpayers and business since it brings certainty in taxation and planning.
	Clause 41: Payment of Excise Duty within twenty-four hours	The Excise Duty Act, 2015, is amended by inserting the following new section immediately after section 36- 36A(1) Despite the provisions of section 36, excise duty on betting and gaming, offered through a platform or other medium ,shall be remitted to the Commissioner by a bookmaker within **twenty-four** hours from the closure of the transactions of the day.”	The amendment proposes remittance by a bookmaker of excise duty on betting and gaming within 24 hours of the closure of transactions of the day. It may be difficult to administratively implement this process to meet the tight timelines.
	First Schedule Part III- Interpretation of the first schedule of Excise Duty Act, 2015. Inclusion of gaming	The amendment expands the definition of amount wagered or staked to include the amount of money placed by a person for an outcome in a transaction. It defines this as “*amount wagered or staked” means the amount of money placed by a person for an outcome in a betting transaction*”;	This brings clarity on the scope of amounts staked or wagered proposal will lead to the widening of scope of the amount subject to excise duty and this leading to increase to revenue collected by the government.
	First Schedule Part III- Interpretation of the first schedule of Excise Duty Act, 2015.	The amendment provides fees for digital lending. “Excise duty on fees charged by digital lenders at a rate of twenty percent.” .	This brings into the excisable duty net any costs related to digital lending transactions. The amendment will increase the cost of borrowing through digital platforms such as Tala, Branch among others.



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<tr><th>#</th><th>Clause</th><th>Provision of the Bill (VAT)</th><th>Potential Impact</th></tr>
<tr><td></td><td>Clause 43: Changes in rates for excisable services</td><td>The proposed changes include:
<table>
<tr><th>Item</th><th>Old rate</th><th>New Rate</th></tr>
<tr><td>Excise duty on Telephone and internet data services</td><td>20%</td><td>15%</td></tr>
<tr><td>Excise duty on fees charged for money transfer services by banks, money transfer agencies and other financial service</td><td>0%</td><td>15%</td></tr>
<tr><td>Excise duty on fees charged for money transfer services by cellular phone</td><td>2%</td><td>15%</td></tr>
<tr><td>Excise duty on betting</td><td>7.5%</td><td>20%</td></tr>
<tr><td>Excise duty on gaming</td><td>7.5%</td><td>20%</td></tr>
<tr><td>Excise duty on prize competition</td><td>7.5%</td><td>20%</td></tr>
<tr><td>Excise duty on lottery (excluding charitable lotteries)</td><td>7.5%</td><td>20%</td></tr>
<tr><td>Excise duty on fees charged on advertisement on television, print media, billboards and radio stations on alcoholic beverages, betting, gaming, lotteries and prize competitions</td><td>N/A</td><td>15%</td></tr>
</table></td><td>The decrease in excise duty on telephone, internet, and fees charged on money transfer services by banks, money transfer agencies and other financial services is a welcome move and will likely lead to an increase in the number of transactions.
Increase in excise duty on fees charged for transfer services by cellular phone will likely lead to a decrease in the number of transactions.
The increase in excise duty on betting, gaming, prize competition and lottery is more on a moral perspective to curb against these services</td></tr>
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2.0 Summary of The Provisions of the Finance Bill 2023

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#	Clause	Provision of the Bill (VAT)	Potential Impact
	Clause 43: Changes in rates for excisable services	Introduction of excise duty on more goods	There has been hue and cry on some of these taxes and potential to lead to job losses in some sectors in the economy. However, taxes on imported cement and imported furniture is aimed at boosting local production.

Item	New Rate
Imported fish	KShs100,000 per metric tonne or 20%, whichever is higher
Locally manufactured Sugar confectionery (including white chocolate), not containing cocoa.	Kshs 242.29 per kg
Locally produced Pasta of tariff 1902 whether cooked or not cooked or stuffed (with meat or other substances) or otherwise prepared, such as spaghetti, macaroni, noodles, lasagne, gnocchi, ravioli, cannelloni, couscous, whether or not prepared	20%
Powdered juice	Kshs 25 per kg
Sugar excluding sugar imported or locally purchased by a registered pharmaceutical manufacturer	Kshs 5 per kg
Human hair and other products of heading	5%
Wigs, false beards, eyebrows and eyelashes, switches and the like, and other products of heading	5%
Artificial nails	5%
Imported furniture excluding furniture originating from East African Community Partner States that meet the East African Community Rules of Origin	30%
Imported cement	0% of value or KShs 1.5 per kg, whichever is higher
Imported paints, varnishes and lacquers	15%

2.0 Summary of The Provisions of the Finance Bill 2023

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2.4 PROPOSED AMENDMENTS ON THE TAX APPEALS TRIBUNAL ACT

#	Clause	Provision of the Bill (VAT)	Potential Impact
	Security on Appeal to the High Court	The Finance Bill 2023 amends the Tax Appeals Tribunal Act to introduce a requirement to deposit 20% of the tax in dispute or a security of an equivalent amount with the Commissioner before filing an appeal to the High court.	This proposal could hamper access to justice especially where taxpayers are unable to pay in case of huge amounts in dispute.
	Refund of Security upon successful appeal	The Bill proposes to impose a timeline for refund of security paid where a taxpayer's appeal is successful.	The 30-day timeline for refund of the deposit paid for appeal is welcome.

2.0 Summary of The Provisions of the Finance Bill 2023

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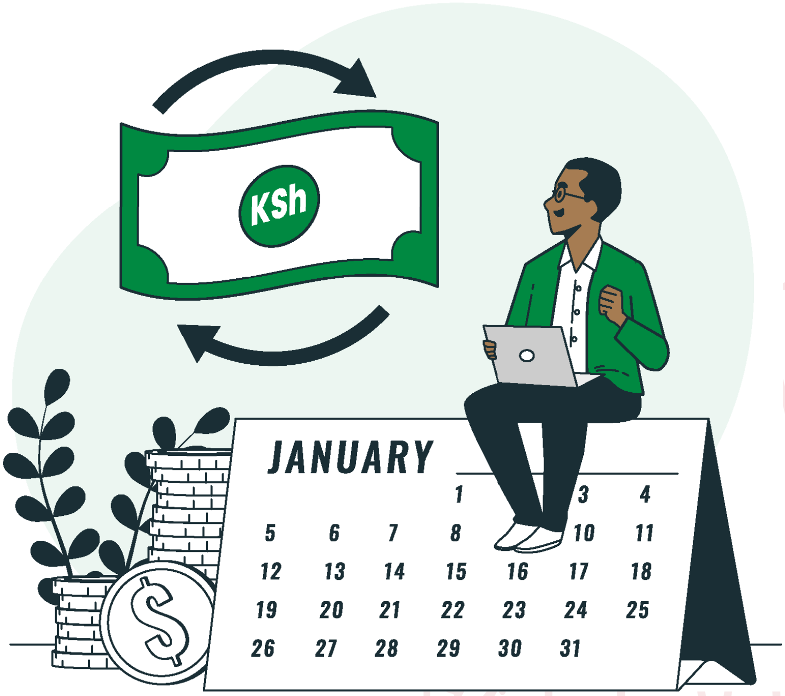
2.5 PROPOSED AMENDMENTS ON THE TAX PROCEDURES ACT

#	Clause	Provision of the Bill (VAT)	Potential Impact
	Record Keeping Requirements	The Bill brings resident trustees who administer trusts registered in or outside Kenya within the ambit of the record keeping provisions in the Tax Procedures Act. This amendment stipulates that the resident trustees will keep all documents required under a tax law and produce to the KRA on demand, whether the income is generated in Kenya or not.	Resident trustees will now be required to keep records for a period of 5 years as stipulated in the Tax Procedures Act.
	Amnesty on interests, penalties or fines on unpaid tax	The Bill proposes to restrict the Commissioner from recovering penalties, interest, and fines on a tax debt where a taxpayer had paid the principal tax before 31st December 2022. Where the principal tax had not been paid before that date, a taxpayer may apply for amnesty of interest, penalties or fines accrued up to 31 December 2022. The taxpayer will also be required to propose a payment plan for the outstanding amount.	The amendment is positive. It will ensure that of 100% waiver of penalties and interests on principal taxes before 31 December 2022 are settled. Where tax is agreed for the period on or before 31 December 2022 but not yet paid, the proposed amendment extends an amnesty for taxpayers to apply to the Commissioner for approval of the waiver involvement of the Cabinet Secretary as is the case currently.
	Refund of overpaid tax	The Bill proposes to allow taxpayers to offset outstanding liabilities and future tax liabilities against overpaid taxes	This is a welcome move for taxpayers who shall now be able to offset past liabilities against overpaid taxes. At the moment, the law only allows taxpayers to offset future liabilities against any overpaid tax.
	Timeline for processing refunds	The Bill proposes to reduce the time taken by the Commissioner to process a refund from 2 years to 6 months	This will deal with the challenge of delays in processing the refunds. For a long time, this has posed a challenge to taxpayers and led to cashflow issues



2.0 Summary of The Provisions of the Finance Bill 2023

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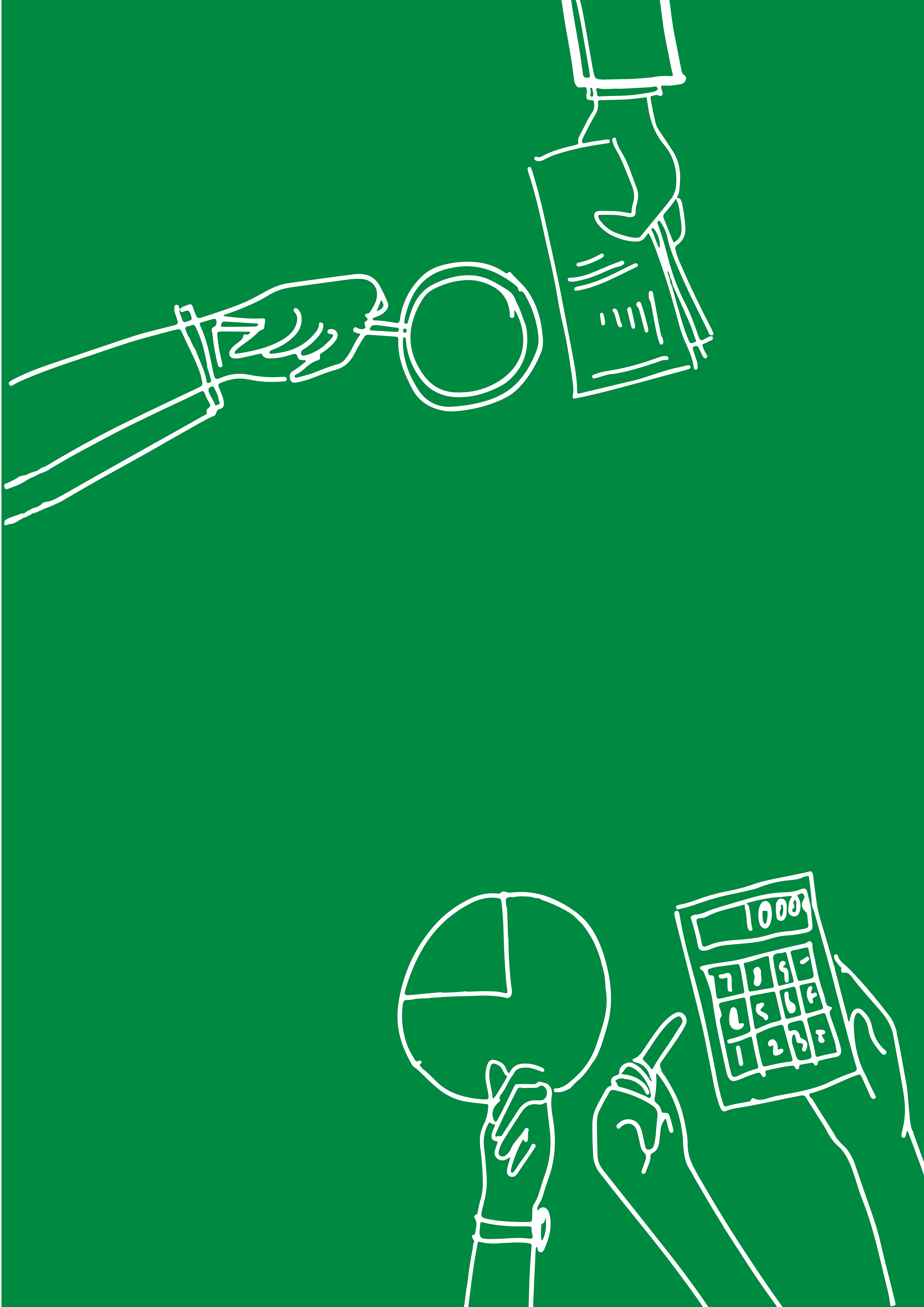
2.6 MISCELLANEOUS AMENDMENTS & OTHER PIECES OF LEGISLATION

#	Clause	Provision of the Bill (VAT)	Potential Impact
	The Betting gaming and Lotteries Act	The Bill proposes the collection of taxes in relation to gaming revenue, lotteries shall be in line with the Tax Procedures Act, 2015.	This is a clean-up to align collection of taxes under the Act with the Tax Procedures Act 2015; and avoid confusion in relation to collection of taxes in the sector.
	Kenya Revenue Authority Act	The Bill amends the Kenya Revenue Authority Act to confer authority of the Kenya Revenue Authority to establish an institution to provide capacity building for its staff, the general public and other jurisdictions.	The proposed amendment shall provide clarity on the purpose for establishment and mandate of the KESSRA and KRA to provide capacity building.
	Clause 76: Deductions into the National Housing Development Fund deductions under the Employment Act, 2007	The Finance Bill 2023 introduces mandatory contributions by both the employer and employee to the National Housing Development Fund at a rate of 3% of the employees' basic salary provided that the sum of the employer and employee contributions do not exceed five thousand shillings a month. This contribution will be used to fund the purchase of a home for those who qualify for affordable housing scheme and for those not eligible may after seven years, or upon attaining retirement age whichever is earlier transfer the contributions to a pension scheme, their staff or dependent children or receive in cash.	This proposal is aimed at achieving the government's commitment to access to affordable housing for Kenyans under the Bottom-Up Economic Transformation Agenda. Already public sector trade unions have opposed this move.



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