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Newsletter

MBAYA AND ASSOCIATES May 2023 | Issue 095 | Volume 9

Introduction

Receive our May 2023 greetings! We are pleased to release the fifth edition of our tax newsletter as we appreciate the good relations that we have had over the period. We have had a lot of feedbacks and engagements in our previous editions and we hope for the same to continue into the future

This edition covers the recent tax developments in the country. We are grateful for your interaction and are happy to be of service to you.

On the right column of the newsletter, you will find contact details for the senior members of our team who can help answer any questions you may have about the issues highlighted in this newsletter or any other matter.

We are interested in your feedback on the items covered and what topics you would like covered in the future.

Please provide any feedback at tax@mbaya.co.ke

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Contacts

Head Office
3rd Floor, Western Heights

Karuna Road, Westlands
P. O. Box 45390 – 00100
Nairobi, Kenya

Tel. +254(20)4443868
254 20 4448938
254 20 4446466

Fax: 254 20 4449819

Mike Mbaya | Managing Partner
Email: mike@mbaya.co.ke

Muhungi Kanyoro | Partner
Email: mkanyoro@mbaya.co.ke

Andrew Bulemi | Partner
Email: abulemi@mbaya.co.ke

Leah Nganga | Partner
Email: lwambui@mbaya.co.ke

Abner Fundi | Outsourcing Dept. Manager
Email: abner.fundi@mbaya.co.ke
Kevin Njenga | Tax Manager
Email: knjenga@mbaya.co.ke

Darlyn Mbaya | Manager and Partner

Savanna Associates

Email: darlyn@mbaya.co.ke

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Fringe Benefit Tax and Deemed Interest Rate

Through a public notice dated 24th April 2023, KRA wishes to notify the general public of the recent changes with regard to the Fringe Benefit Tax and the Deemed Interest Rate as below. The Low Interest Benefit still remains at 9% up to and including June 2023.

Fringe Benefit Tax (FBT) » This is a tax applicable when employers provide loans to their employees and charge an interest lower than the prescribed rate (ITA-section 12(b)). This becomes a benefit to the employee, for which the employer needs to file and pay Fringe Benefit Tax. FBT is paid by the employer at the corporate tax rate of 30 % on total taxable value each month. The tax is payable to KRA on or before the 9th day of the month following the month of contribution. For the purposes of Section 12B of the Income Tax Act, the Market Interest Rate is 10%. This rate is applicable for the three months of April, May and June 2023.

Deemed Interest Rate » This is the amount of notional interest assumed to be payable by a resident person in relation to any outstanding loan provided or secured by a non-resident person, where such loan has been provided interest free. For purposes of section 16(5), the prescribed rate of interest is 10%. This is applicable for the months of April, May and June 2023.

Withholding tax rate of 15% on the deemed interest shall be deducted and paid to the Commissioner by the 20th day of the month following the month of computation.

An example of a Fringe Benefit Tax computation: On 1st April 2023, an employee gets a loan of Kshs 3 million from his/her employer at a rate of 5%. FBT will be calculated as follows:

Loan Amount:	**Kshs. 3,000,000**
Interest Charged:	5% per annum
Market Interest Rate for the month:	10% per annum
Fringe Benefit Rate on saving by employee:	10% - 5% = 5% per annum
Fringe Benefit:	3,000,000 x 5% = 150,000 per Annum. i.e., Kshs. 12,500 per Month.

Fringe Benefit tax payable by the employer for the month of April 2023 is therefore Kshs. 3,750 (12,500 x 30%). The tax should be payable by the 9th of May 2023 together with the PAYE for the same month of April 2023.

The FBT computation should be done and tax paid monthly using the applicable rates until the loan has been cleared in full.

Enforcement of the Electronic Tax Invoice System (TIMS & E-TIMS)

Kenya Revenue Authority (KRA) is currently rolling out eTIMS. This is the software approach to ensure that all VAT registered taxpayers generate electronic tax invoices that are transmitted to KRA on real time or near real time basis.

Through a public notice dated 4th May 2023, the Commissioner General wishes to notify the public that **effective 1st June 2023,** all VAT registered taxpayers are required to only accept electronic tax invoices from registered taxpayers in compliance with the VAT (Electronic Tax Invoice) Regulations 2020 for purposes of claiming input tax and processing of refunds.

This requirement exempts registered non-resident suppliers of digital services. The non-resident digital service suppliers are however required to issue invoices or receipts showing the value of the supply and tax charged.

For VAT registered taxpayers who have not complied with VAT (Electronic Tax Invoice) regulation 2020, the Tax Compliance Certificate will not be issued unless they comply.

Similarly, VAT refunds shall be only processed and paid for taxpayers who are compliant with the Regulations.

KRA takes this opportunity to thank all compliant VAT registered taxpayers who are already supporting the enforcement of the Regulations.

Finance Bill 2023

The National Treasury submitted the Finance Bill, 2023 (“Finance Bill”, “The Bill”) to the National Assembly for consideration and enactment into the Finance Act. The bill was tabled to the National Assembly on 04 May 2023 for the first reading.

Whilst the Finance Bill is yet to be officially published, the proposals in the Bill are significant and may have an impact on the businesses of several taxpayers.

The Finance bill which evolves to Finance Act after approval and assent, is a statute that brings into effect fiscal measures proposed by the government as part of the annual budget process.

In this Alert, we provide an analysis of the key changes proposed by the Bill. The effective date for these changes is 01 July 2023, unless specified otherwise in the sections herein.

- **Personal Income Tax Rates** » Proposal to introduce a higher personal income tax rate of 35% on the income of individuals above KES 6,000,000 per year (KES 500,000 per month).

- **Deductions into the National Housing Development Fund** » The Bill seeks to introduce a new Section 31B in the Employment Act, 2007 to provide that an employer shall pay to the National Housing Development Fund established under Section 7 of the Housing Act, in respect of each employee, a 6% shared between the employer and the employee equally:

- **Taxation of branches with permanent establishments** » Proposal to reduce non-resident corporate tax rate from 37.5% to 30% from January 2024. Related thereto, the bill proposes to tax the repatriated profits of branch/permanent establishment.

- Repatriated profit is determined by assessing the profits of a branch for a year of income against the increase in the value of its assets.

- **Changes on EBITDA based restriction of interest expense** » Proposal to restrict the applicability of EBITDA-based interest restriction rules to interest payable on loans only from non-resident lenders. Currently the interest on all loans including from resident lenders was subject to the restriction.

- In addition, the restricted interest expense may be deducted within the subsequent three years provided that even then such interest expense together with other interest expenses on foreign loans does not exceed 30% of EBITDA. Further, the Bill proposes to exclude companies involved in manufacturing from exemption from the restriction of interest expenses under the EBITDA rule.

- **Taxation of ESOP benefits for employees of start-ups** » Proposal to defer taxation of benefits for ESOP employees and be taxed within 30 days of the earlier of:

» The expiry of 5 years from the date the option was granted;

» The disposal of the shares by the employee; or

» The date the employee ceases to be an employee of the eligible startup.

A start-up is one set up in Kenya, whose income is below KES 100 million and which has been in existence for less than 5 years.

- **Withholding tax scope expansion** » Proposal to subject to withholding tax the following payments to resident persons:

» Payments made in relation to sales, promotion, marketing and advertising services at the rate of 5% of the gross amount the aggregate value of which is at least Kshs. 24,000 in a month

» Payments made in relation to digital content monetization at the rate of 15%. This would capture so-called "influencers" and charge their income to tax.

- **Introduction of tax on digital assets** » Proposal to impose a new Digital Asset Tax at the rate of 3%. This will be applicable to the income derived from the transfer or exchange of digital assets. Digital assets will include anything of value that is not tangible and cryptocurrencies, token codes, numbers held in digital form and generated through cryptographic means or otherwise, by whatever name called, providing a digital representation of value exchanged with or without consideration that can be transferred, stored or exchanged electronically.

- **Investment allowance deductions** » Proposal to introduce investment deduction claims on capital expenditure incurred on the construction of docks at the rate of 10% per annum. In addition, there is a proposal to reintroduce investment deduction claim on capital expenditure incurred on industrial buildings at the rate of 10% per annum.

- **Deduction of expenditure whose invoice is not generated through an electronic tax invoice system** » Proposal to scrap a claim of expenditure not supported by TIMs compliant invoices.

- **Restriction of accelerated capital allowance** » Currently, the Income Tax Act provides for accelerated investment allowance as follows:

» 100% where the investment value outside Nairobi City County and Mombasa City County in the year is KES 250 million. The cumulative investment in the preceding 3 years outside Nairobi County and Mombasa County is at least KES 2 billion or the investment is incurred in a Special Economic Zone; and

» 150% where the cumulative investment value for the preceding four years from 1 July 2022 or the cumulative investment for the succeeding three years outside Nairobi City County or Mombasa County is at least KES 2 billion.

» Bill proposes to limit the applicability of the 100% and 150% investment deduction allowance to hotel buildings, buildings and machines used for manufacture. It further proposes that the investment deduction allowance of 100% shall not apply to investments which due to the nature of their business, must be in places which are outside Nairobi City County and Mombasa County.

- **Capital gains tax changes** » Proposal to levy capital gains tax on gains derived from the alienation of shares or comparable interests in a partnership or trust if during the year preceding the alienation, the shares or comparable interests derived more than twenty per cent of their value directly or indirectly from immovable property situated in Kenya.

- **Exported services** » Proposal to exempt from VAT exported services is proposed to be reintroduced. This had been removed by the Finance Act 2022 and its re-introduction is a welcome move.

- **Transfer of a business as a going concern** » Proposal to make the transfer of a business as a going concern exempt from VAT. Such transfers are currently subject to VAT at the standard rate.

- **Exemption of Liquified petroleum gas (LPG)** » Proposal to delete the 8% VAT applicable to LPG and exempt it from VAT. The rate of 8% was introduced barely a year ago and prior to that, LPG was subject to VAT at the rate of 16%. In addition, the importation of LPG is proposed to be exempted from import declaration fees and railway development levy. This will make LPG quite affordable.

- **VAT on insurance compensation** » Proposal to introduce VAT on insurance compensation in relation to assets on which input vat had been claimed.

- **24 Excise duty payment from closure of transactions** » Proposal to introduce a requirement for excise duty on betting and gaming offered through a platform or other medium to be remitted to the KRA by a bookmaker within 24 hours from midnight of the relevant day.

- **KRA's power to adjust excise duty rates for inflation dimmed** » Proposal to repeal section 10 of the Excise Duty Act which empowers KRA, with the approval of the Cabinet Secretary, to by notice in the Gazette adjust the specific rate of excise duty once every year to take inflation into account.

- **Tax amnesty** » Proposal to grant a tax amnesty on fines, penalties and interest on debt where a person pays the principal taxes not later than 30 June 2023, does not incur a further tax debt and signs a commitment letter to settle all outstanding taxes owed.

- **Tax appeals tribunal fees** » Proposal requiring to deposit with KRA a 20% of the disputed tax before lodging an appeal at the High Court. This is aimed to provide a security equivalent to 20% of the disputed tax before filing an appeal of a decision of the Tax Appeals Tribunal at the High Court. If the Court makes a decision in favour of the taxpayer, the KRA would be required to credit the amount or security within 30 days after the determination of the appeal.

- **Reduction of Import declaration duty rate and railway development levy** » Proposal to reduce the import declaration fees from 3.5% to 2.5% and that of railway development levy from 2% to 1.5%

Tax Quote by Bob Dole*: "The purpose of a tax cut is to leave more money where it belongs, in the hands of the working men and working women who earned it in the first place."*

From The Secretarial Desk

Duties, Liabilities of Officers of the Company - Cont.....

In a previous edition, the secretarial desk looked at the duties of the officers of a company, with a special highlight to Directors. In this edition, we would like to continue to look at directorship and the civil consequences of breach of their general duties.

Civil Consequences of Breach of General Duties

The consequences of breach or threatened breach of the general duties of directors set out in the Act are the same as would apply if the corresponding common law rule or equitable principal applied. The Act also provides that the breach of general duties (other than the duty to exercise reasonable care, skill and diligence) will be enforced in the same way as any other fiduciary duty owed to accompany by its directors.

Liabilities of Directors

Directors are agents of the company in transactions they enter into though they are not agents for individual shareholders or members. Directors' liabilities arise because of their positions as agents or officers of the company. Some of these liabilities are in contract, tort, statutory, and others are under criminal law.

- **Liability to Outsiders** » Directors are not personally liable to outsiders if they act within the scope and powers vested in them. The general rule is that wherever an agent is liable, those directors would be liable, but where liability would attach to the principal only, the liability is the liability of the company.
- **Liability to the Company** » The directors shall be liable to the company in the following cases.
- Where they have acted ultra vires the company, for example, they have applied the funds of the company to objects not specified in the memorandum or when they pay dividends out of capital.
- When they have acted negligently. (Negligence may give rise to liability, there need not be fraud).
- Where there is a breach of trust resulting in a loss to the company, they are bound to make good the loss.
- Where there is Misfeasance - Wilful misconduct or wilful negligence.
- **Criminal Liabilities** » The Act provides penalties by way of fine or imprisonment particularly when directors omit to comply with or contravene certain provisions of the Act. Where the directors of a company act on its behalf, they are personally liable for contracts which they make provided they act within the scope of their authority and they do not make contracts in their personal names.

It is held generally that "whenever an agent is liable, directors would be liable, where the principal would be liable; the liability is the liability of the company".

Examples of Liabilities (Directors)

a) **Contractual Liability** » A director will personally be liable on a company contract when he has accepted personal liability either expressly or impliedly.

- Express liability will usually arise only when a director has personally guaranteed the performance of a contract.
- Implied liability - Will arise when a director signs a contract for a company or mentioning the name but failing to add the vital word limited "Limited".

a) **Pre-incorporation Liability** » A company cannot make a contract before it is incorporated as it has no legal existence. A company after incorporation cannot ratify a contract previously made. It has to make afresh contract. Those who act on behalf of unincorporated company may find themselves personally liable.

b) **Liability of Directors for Torts of the Company** » Directors are not liable for torts or civil wrongs of their company. However, for a director to be personally liable for a tort e.g., negligence, trespass, it must be shown that he was himself the wrong doer or the principal of the wrong doer in relation to the act complained of, or that the tort was committed in his instructions.

c) **Tax Liability** » When a private company is wound up and tax assessed cannot be recovered then every person who was a director of the private company shall be jointly and severally liable for the payment of such tax.

d) **Statutory Liability** » Where a company has issued misleading prospectus, a director is liable to compensate a person who has subscribed shares on the faith of prospectus which contained untrue statement.

e) **Liability for Illegal Acts** » Where directors have used their powers to part with monies of their company in a manner or for a purpose which the law forbids, they shall be personally liable. These include:

- Negligent misrepresentation
- Liability for fraud
- Misconduct in the course of winding up
- Falsifying the company's books
- Material omissions from statements relating to the company's affairs
- False representations to creditors

Sample Offences and Penalties under the Companies Act 2015

Section	Duty	Officer	Penalty
151	To declare interest in proposed or existing transaction agreements.	Director	Fine not exceeding Kshs. 1,000,000.
635 (3)	To prepare individual financial statements	Director	Fine not exceeding Kshs. 1,000,000.
635 (4)	To prepare individual financial statements after conviction	Director	Further fine not exceeding Kshs. 100,000.
652	To approve and sign financial statements	Director	Fine not exceeding Kshs. 1,000,000.
659	Duty of directors of quoted companies to prepare directors' remuneration report	Director	Fine not exceeding Kshs. 1,000,000 or to a term not exceeding three years imprisonment or both.
664	To send out copies of financial statements and reports.	Director / Secretary	Further fine not exceeding Kshs. 100,000 for each offence.
708	To lodge annual returns on time	Director / Secretary	Further fine not exceeding Kshs. 200,000 for each officer.
191	To keep available for inspection a copy of each director's service contract with a company or its subsidiary.	Director / Secretary	*Fine not exceeding Kshs. 200,000 for each officer.
134	To keep a register of its directors, which complies with the prescribed requirements and to keep such register open during ordinary hours for inspection.	Director / Secretary	**Fine not exceeding Kshs.1,000,000.

Key

* The Company and each officer of the company is charged a fine not exceeding Kshs.50,000 on each day they fail to comply with the above offences.

** The Company and each officer of the company is charged a fine not exceeding Kshs.100,000 on each day they fail to comply with the above offences.

DISCLAIMER: The publication on the secretarial desk has been prepared for general guidance on matters of interest only, and does not constitute professional advice. You should not act upon the information contained in this publication without obtaining specific professional advice. No representation or warranty (express or implied) is given as to the accuracy or completeness of the information contained in this publication, and, to the extent permitted by law, Mbaya & Associates, its members, employees and agents do not accept or assume any liability, responsibility or duty of care for any consequences of you or anyone else acting, or refraining to act, in reliance on the information contained in this publication or for any decision based on it.

Tax Due Dates

Withholding Tax | 20th Day of the following month

Pay as You Earn | 9th Day of the following month

VAT | 20th Day of the following month

Balance of Tax on Self-Assessment | 4th Month after year end

Monthly Rental Income | 20th Day of the following month

Instalment Tax

1st Instalment |20th day of the 4th month after year end

2nd Instalment | 20th day of the 6th month after year end

3rd Instalment | 20th day of the 9th month after year end

4th Instalment | 20th day of the 12th month after year end

Kindly note that all the returns must be filed on I tax while the payments e-slips must be generated from the I-Tax platform.

Digital Service Tax (DST)

20th day of the following month