

# Financial Services Sector Report

Q4 2020



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## BANKING

### I. Guidelines, Notices & Circulars

#### Expiry of Suspension of The Listing of Negative Credit Information for Borrowers

On 1st October 2020, the CBK issued a [press release](#) with respect to the expiry of the suspension of listing of negative credit information for borrowers. In effect, the statement allowed financial institutions to give borrowers notice of intention to list such information with Credit Reference Bureaus following the assessment of their performance from after lifting of the suspension.

#### Expiry of Emergency Measures to facilitate Mobile Money Transactions and the Introduction of Principles to Guide Pricing

On 17th December 2020, the CBK issued a [press release](#) regarding the expiry of emergency measures to facilitate mobile money transactions. In view of the measures and Covid-19 pandemic, the regulator noted a significant increase of mobile money usage stating for instance:

- i. the volume of person-to-person transactions increased by eighty seven percent (87%);
- ii. the volume of transactions below Kes 1,000.00 increased by one hundred and fourteen percent (114%); and
- iii. an additional 2.8 million mobile subscriber customers used mobile money.

CBK stated that it would allow the measures to expire on 31st December 2021 so as to

consolidate the gains made so far and facilitate a transition towards sustainable growth of the mobile money eco-system. Effective 1st January 2021, Payment Service Providers are required to introduce revised pricing structures with the following elements:

- i. no charges for person to person transfers of up to Kenya Shillings One Hundred (Kes 100.00) to any customer and network;
- ii. no charges for transfers between mobile money wallets and bank accounts;
- iii. to facilitate the integration of SACCOs into the mobile money ecosystem, SACCOs regulated by SASRA may charge a levy for transfer between SACCO accounts and mobile money wallets; and
- iv. Payment Service Providers will propose pricing structures reflective of principles on the pricing of mobile money services ('Pricing Principles) introduced by the CBK.

The regulator stated that the Pricing Principles aim to support the development of efficient, safe and stable payments and mobile money ecosystems where customer and public interests are adequately protected.

The Pricing Principles are:

- i. Customer Centricity;
- ii. Transparency and Disclosure;
- iii. Fairness and Equity;
- iv. Choice and Competition; and
- v. Affordability.

Implementation will be carried out on a gradual basis and the CBK will be periodically engaging Payment Service Providers to ensure alignment, identify and promote best practices.

# FINTECH

## I. Subsidiary Legislation

### **The Income Tax (Digital Service Tax) Regulations, Legal Notice 207 of 2020 ([Find link here](#))**

These regulations introduce the digital service tax. This tax applies to various services that are delivered over a digital marketplace. Regulation 3 lists out all the digital services that are eligible for this tax. These services include;

- a) subscription-based media including news, magazines and journals;
- b) electronic data management;
- c) electronic booking and ticketing services;
- d) downloadable digital content;
- e) over-the-top services including streaming television shows, films, music and podcasts;
- f) sale, licensing or any other form of monetising data collected about Kenyan users that has been generated from the users' activities on a digital marketplace;
- g) provision of a digital marketplace;
- h) provision of search engine and automated held disk services;
- i) online distance training through pre-recorded media or e-learning including online courses and training; and
- j) any other service provided through a digital marketplace.

Digital services that are exempt from this tax include online services provided by Government institutions and those that facilitate payment, lending or trading financial instruments carried out by financial institutions and service providers as approved by the Central Bank of Kenya.

This tax is applicable to the income of a resident or non-resident person accrued in Kenya from the provision of digital services. It is payable by digital service providers and digital marketplace providers. They shall also submit a return in the prescribed form and remit the tax due by the twentieth day of the month following the end of the month that the digital service was offered.

### **VAT (Digital Marketplace Supply) Regulations, 2020 ([Find link here](#))**

These regulations seek to regulate the payment of Value Added Tax on services supplied in the digital marketplace.

The regulations provide for what are taxable services in the digital marketplace which include; downloadable digital content, e-books and film, subscription-based media, over-the-top services, software programmes, electronic data management, online data warehousing, file-sharing and cloud storage services, music and games, search engine and automated helpdesk services, tickets, distance teaching and other electronic services.

The regulations call for the supplier of the taxable service to register for tax in Kenya through a simplified tax registration framework, created under the regulations.

## INSURANCE

### I. Guidelines, Notices & Circulars

On 5<sup>th</sup> October 2020, the Commissioner of Insurance [reported](#) that up to a third of insurance companies in Kenya, are yet to comply with capital requirements introduced earlier in July.

In conducting a mid-year review on satisfaction of the requirements, the Insurance Regulatory Authority noted that it gave underwriters a 6-month extension to meet the capital adequacy requirements owing to reduced premium collections and increased claims following the onset on the Covid-19 pandemic.

## INVESTMENTS

### I. Acts of Parliament

**Tax Laws (Amendment) Act No. 2 of 2020 published on 24.12.2020 amends the Income Act Cap 480 Laws of Kenya [\(Find link here\)](#)**

The decision to withdraw some of the measures aimed at cushioning businesses from the effects of the COVID-19 pandemic has seen the rate of corporate income tax revert from 25% back to the pre-pandemic rate of 30%.

The Act has amended Section 2 (a) of the Third Schedule of the Income Tax Act by inserting sub-paragraph (ix) immediately after sub-paragraph (viii). This additional sub-paragraph states that the applicable corporation rate of tax shall be 30% and that the same shall apply to income earned from the 1st of January 2021. The Act has also amended section 17(8) of the Value Added Tax Act covered under Part VI. The amendment under that section now provides that a registered person being a manufacturer may make a deduction for input tax with respect to taxable supplies made to an official aid funded project. However, for the input tax to be effective, the project has to be approved by the Cabinet Secretary of the National Treasury. The deduction must be in accordance with the 1st Schedule.

In that same regard, Paragraph 51 of the 1st Schedule Part I and Paragraph 20 to the 1st Schedule Part II of the VAT Act exempts taxable goods & services, imported or purchased for direct and exclusive use in the implementation of official aid funded projects upon approval by the Cabinet Secretary in-charge of National Treasury.

This means that only manufacturers who make supplies to official aid funded projects are set to enjoy the benefits of input tax deduction. It does not cater for other suppliers, inclusive service providers making supplies to official aid funded projects but are not manufacturers.

#### **Restoration of the 16% VAT rate from 14%**

The Cabinet Secretary in-charge of National Treasury published an order in the Gazette, Legal Notice No. 206 dated 2nd December 2020 [\(Find link here\)](#) amending the VAT rate back to the pre-COVID rate of 16% from 14% WEF from 1st January 2021. The move was quickly approved by Parliament on 22nd December 2020. What does this mean? It means that taxpayers are required to make the necessary configurations to their systems to issue tax invoices and account for VAT at the rate of 16% WEF 1<sup>st</sup> January 2021.

## II. Subsidiary Legislation

**The Value Added Tax (Amendment of the Rate of Tax) Order, Legal Notice 206 of 2020** ([Find link here](#))

This order seeks to amend Section 5 of the Value Added Tax Act of 2013 by changing the tax rate from fourteen percent to sixteen percent. This change is effective from 1<sup>st</sup> January 2021.

**VAT (Electronic Tax Invoice) Regulations, 2020** ([Find link here](#))

These are new regulations that require the use of an electronic tax invoicing or receipting system (“Register”) by a tax registered person. This is to allow for a shift from the current manual tax invoicing system.

The regulations provide that the user of a register shall ensure that (a) each sale is recorded with the use of the register; (b) an invoice is generated in respect of each sale; (c) each invoice generated in respect of each sale. The regulations further provide for the rules of use of the register mand reportion on the same.

purpose of this review is to address stakeholders’ concerns and facilitate the development of a robust asset management sector. The regulator’s chief executive Mr. Wycliffe Shemiah noted that there is a need to review the eligibility and regulatory requirements for different regulated entities to ensure responsiveness to market dynamics that included an emerging need for property developers to pool funds in support of projects such as affordable housing which is aligned to the Government’s ‘Big 4’ agenda.

On 4<sup>th</sup> December 2020, the National Treasury issued a [press statement](#) announcing the return to pre-Covid-19 tax rates on income tax and value added tax. Due to the easing of some of the containment measures imposed by the Government, the Cabinet Secretary for National Treasury and Planning noted that in order to enable the implementation of the government budget, it became necessary to return to the tax rates before the onset on the pandemic. Effective 1<sup>st</sup> January 2021:

- i. Corporate Tax rate would revert to 30% from 25%;
- ii. Individual Income Tax rate would revert to 30% from 25%; and
- iii. Value Added Tax rate would revert to 16% from 14%.

On 8<sup>th</sup> December 2020, the National Treasury published a [media brief](#) announcing that the Government of Kenya signed a credit guarantee scheme with seven participating commercial banks. Owing to the disproportionate impact the Covid-19 pandemic has had on MSME businesses, the brief noted that this arrangement aims to improve MSMEs access to credit for their operational and growth requirements.

## III. Guidelines, Notices & Circulars

On 11<sup>th</sup> November 2020, the CMA issued a [press release](#) announcing that it has teamed up with twenty three (23) regulators across the world to test innovative financial products, services, business models and regulatory technology. This test environment aims to give regulators opportunities to learn from the outcomes of tests in other regions and apply the same in their respective jurisdictions to enhance innovative financial market solutions.

On 1<sup>st</sup> December 2020, the CMA posted a [press release](#) stating that it engaged a consultant to review the Capital Markets (Collective Investments Schemes) Regulations, 2001. The

## IV. Judicial Decisions

**Income Tax Appeal 19 of 2013: Coca-Cola Central East and West Africa Limited v Commissioner of Domestic Taxes [2020] eKLR**  
[\(Find link here\)](#)

Judgment delivered on November 23, 2020

### TAX LAW

**Imposition of VAT on exported services amounts to double imposition of VAT and is contrary to the neutral application of VAT in International Trade law.**

### Brief Facts:

The appellant, Coca-Cola Central East and West Africa (Coca Cola Africa), provided marketing and promotional services for all of Coca-Cola's world-famous brands. Coca-Cola Africa is a subsidiary of the Coca-Cola Company which is incorporated in the United States of America and the owner of the Coca-Cola trade mark. The Coca-Cola Company and its subsidiaries manufacture and sell proprietary concentrates used to prepare Coca-Cola beverage products with one such subsidiary being Coca-Cola Export which manufactured concentrates in various locations around the world but not in Kenya. The concentrates were sold to authorized bottlers who purchased, imported and in turn used the concentrates in preparing and packaging beverage products that bore the Coca-Cola trademarks. Value Added Tax was in turn paid for the concentrates by the bottlers at the point of import.

Contention arose between Coca Cola Africa (appellant) and the Commissioner of Domestic Taxes (respondent) on the instance and impact of Value Added Tax on Coca-Cola products being advertised in Kenya but meant for foreign

market consumption. On one hand, Coca-Cola Africa postulated that the benefit of the marketing and promotion services accrued outside Kenya and that therefore, it should be treated as 'exported services' as per the provisions of the VAT Act (Cap 476) (repealed). On the other hand, the respondent put forward an argument that marketing and promotion services provided by Coca-Cola Africa were consumed locally as the target audience was Kenya and they therefore ought to be treated as services locally consumed in Kenya.

The VAT Tribunal (the Tribunal) held that the marketing and promotional services were heard, seen, enjoyed and perceived by persons and households resident in Kenya and therefore physically consumed in Kenya, thus leaving no place for an interpretation of section 2 of the VAT Act, cap 476 (repealed). Therefore, VAT ought to have been charged at the point of consumption since the same was a destination-based tax levied on commercial activities on the consumer as opposed to a charge on the business.

### Judgment of the High Court

Aggrieved by that finding, the appellants lodged an appeal before the High Court and the appeal succeeded on the following grounds:

- a) The target audience for Coca-Cola Africa's promotional activities was the Kenyan public who were either existing or potential buyers of the Coca-Cola drinks. However, that did not out rightly make them the consumers of the promotional and marketing services.
- b) A person became a user or consumer of Coca-Cola Africa's services only when, at the instigation or

encouragement of the services, he consumed the Coca-Cola products. Persons who saw, enjoyed, heard, perceived or even enjoyed an advertisement but failed to act on it could not be said to have used or consumed the products.

- c) A promotion or marketing activity did not necessarily lead to a sale or consumption of the promoted or marketed product. Consumption of the soft drink therefore ought not to have been confused with consumption of the promotional and marketing services. The marketing and promotional agreement between Coca-Cola Africa and Coca-Cola Exporters was to increase brand awareness resulting in increased consumption of Coca-Cola soft drinks which translated to increased sales and profits for Coca-Cola Exporters.
- d) The marketing and promotional services were not provided so that members of the target audience could merely hear, see, enjoy, feel or perceive them. They were so provided in the hope that it would trigger a purchase or a desire to purchase a Coca-Cola product.
- e) For VAT purposes, the final consumer of the Coca-Cola drink was the consumer of the marketing and promotional services. In that regard, Coca-Cola Africa supplied the marketing and promotional services to Coca-Cola Export at a fee by the latter.

- f) Coca-Cola Africa did not receive any compensation for the performance of the promotional services from local independent bottlers who were the consumers of the services. The bottlers, whilst not paying for the promotional services, were a major beneficiary of the marketing and promotional services as it could lead to an increase in sales of the Coca-Cola brands. If Coca-Cola Africa did not provide marketing and promotional services, then the bottlers would have to undertake them. Payment for those marketing and promotional services would have attracted VAT in Kenya and that would have been passed to the final consumer.
- g) The Commissioner failed to prove that there was a leak in tax from Kenya and further that the business arrangement led to unintentional non-taxation given that no tax similar to VAT was imposed on the services in the State where Coca-Cola Export was domiciled. The business model adopted by Coca-Cola Africa and Coca-Cola Exporters did not therefore lead to an avoidance or minimization of VAT.

**Orders: -**

The Appeal was allowed, and the decision of the VAT Tribunal dated 26<sup>th</sup> November 2013 set aside with costs to the appellant.



## RETIREMENT BENEFITS

### I. Acts of Parliament

Tax Laws (Amendment) Act No. 2 of 2020 (TLAA 2) published on 24.12.2020 amends the Income Act Cap 480 Laws of Kenya ([Find link here](#))

The decision to end some of the Covid-19 relief measures has also affected the retirement benefits industry, particularly benefits to be paid out to members of retirement benefits schemes. There has been a re-introduction of the top tax band for payment of a pension or

any withdrawal made after the expiry of fifteen years from the date of joining a registered fund, or on the attainment of the age of fifty years, or upon earlier retirement on the grounds of ill-health or infirmity of body and mind, from a registered pension fund.

Whereas previously the top tax band applied to all amounts in excess of KES 1,200,000 at the rate of 25%, the amendments will now re-introduce the previous to tax band which will apply to all amounts in excess of KES 1,600,000 at the rate of 30% as provided below:

Rate of Tax %	Income (KES)
10%	On the first 400,000
15%	On the next 400,000
20%	On the next 400,000
25%	On the next 400,000
30%	Income of 1,600,000 in excess of the tax-free amounts

### II. Subsidiary Legislation

Retirement Benefits (Umbrella Retirements Benefits Scheme) (Amendment) Regulations, 2020 ([Find link here](#))

These regulations are an amendment to the Retirement Benefits (Umbrella Retirements Benefits Scheme) Regulations.

Some of the key amendments include the amendment of the definition of an umbrella scheme to refer to a scheme established by a sponsor for the benefit of members employed by participating employers including schemes established under written law.

The regulations have also increased the criteria that the Authority shall use in determining the suitability of a sponsor.

### Retirement Benefits (Mortgage Loans) (Amendment) Regulations, 2020 ([Find link here](#))

These regulations are an amendment to the Retirement Benefits (Mortgage Loans) Regulations. Some of the key amendments includes;

- increasing the definition of institution to incorporate a developer or entity offering residential houses for sale.
- amending the definition of a house to include a house that partly offers residential accommodation. This incorporates multiuse houses.
- Incorporation of a member's spouse so that where spouses are members of the sale or different schemes, the

- trustees shall prescribe rules where spouse may combine their accrued benefits and utilise the total amount for the purchase of a residential house.
- The incorporation of provisions that allow members to utilise a portion of their accrued benefits, (of no more than 40 % or 7 Million whichever the lower) to purchase a house. This then means that one can have a partial withdrawal of their accrued benefits to purchase a house in place of using the accrued benefits only as collateral.

## OTHERS

### I. Parliamentary Bills

The Public Debt Management Authority Bill, 2020 published on 29 October 2020 ([Find link here](#))

1. With concerns about rising public debt and the revenue shortfalls, Parliament is keen on monitoring public debt at national government and county level. In this regard, the Public Debt Management Authority Bill (**PDMA Bill**) seeks to establish a Public Debt Management Authority (**Authority**), as an independent body tasked with among other roles, managing public debt.
2. Once enacted to law, the Authority will succeed the Public Debt Management Office, currently set up as a directorate under the National Treasury.

3. The Authority's key functions include:

- implementing the national government's public debt management policy of minimising financing costs over the long term, including facilitating debt rescheduling and restructuring
- formulating policies and strategies to achieve the following objectives:
  - ensuring national government's financing needs and payment obligations are met at the lowest cost possible
  - developing a domestic public debt market
  - developing market institutions for government debt securities
  - equitable sharing of benefits and costs to of the public debt

- between current and future generations
  - maintaining a register (to be published in the Kenya Gazette) detailing all loans advanced to the national government, county government and their respective entities, including all loans guaranteed by the national government
  - preparing and implementing the national government's borrowing plan and servicing of outstanding public debts
  - issuing government public debt securities on behalf of the national and county governments on an agency basis
  - monitoring and evaluating public debt related transactions ensuring that they are within the guidelines and risk parameters of the public debt management strategy
  - processing the issuance of loan guarantees including assessment and management of risks in national government securities
  - transacting in derivative financial instruments in accordance with best international practices
  - participating in negotiations with creditors and advising the Cabinet Secretary on all borrowings
  - tracking and recovery of any payments including interest and other costs incurred by the national government with regard to the honouring of outstanding guarantees
  - processing borrowing requests from public agencies and county governments
  - keeping in safe custody the records of all loan contracts and public debt instruments.
4. It is intended that the management of the Authority will be vests in a board comprising of the following persons:
- a chairperson nominated by the President and approved by Parliament
  - Cabinet Secretary National Treasury
  - Attorney General
  - Governor of the Central Bank of Kenya
  - Chief Executive Officer of the Capital Markets Authority or a representative designated in writing
  - Chief Executive Officer of the Nairobi Securities Exchange a representative designated in writing
  - Chief Executive Officer of the Kenya Institute for Public Policy and Research or a representative designated in writing
  - One person nominated by: (i) Institute of Certified Public Accountants, (ii) the Kenya Bankers Association, (iii) the Kenya Private Sector Alliance and (iv) the Law Society of Kenya and
  - the Director General of the Authority who shall serve as an ex-officio member.
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