Quartet CONSULTING

Finance Bill 2025 Overview

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Introduction

The Finance Bill, 2025 has been submitted to the National Assembly and formulates proposals relating to revenue raising measures, including liability to and collection of taxes. The Bill proposes to amend the Income Tax Act (Cap. 470), the Value Added Tax Act (Cap. 476), the Excise Duty Act (Cap. 472), the Tax Procedures Act (Cap. 469B), and the Miscellaneous Fees and Levies Act (Cap. 469C).

Notably, the government has departed from the traditional three-tiered approach to commencement dates. The Bill does not contain any provisions set to take effect on 1st September. Instead, only 2 out of the Clauses are scheduled to come into operation on 1st January, 2026, while the remaining provisions will take effect on 1st July, 2025.

Income Tax Act

a. Income Tax Act

Expansion of the Definition of Royalty

The Bill proposes to expand the definition of royalty to include payments made for the distribution of software, where recurring payments are made for the use of such software through a distributor.

Implications

This marks a departure from international best practice on the taxation of software payments, particularly as articulated under Article 12 of the OECD Model Tax Convention. Under the Convention, withholding tax (WHT) generally applies only where payments are made in consideration for rights to exploit the underlying intellectual property (IP) of the software.

Historically, certain software-related payments such as licence fees paid to software providers under distribution and end-user licence agreements have not been subject to WHT in Kenya, on the basis that they do not grant the payer any IP rights in the software. This is consistent with both international standards and the High Court's ruling in Seven Seas Technologies Limited v Commissioner of Domestic Taxes (Income Tax Appeal No. 8 of 2017), which affirmed that such payments should not attract WHT absent a transfer of IP rights.

Definition of "Related Person"

A single, uniform definition of "related person" is proposed to replace the multiple definitions. The proposed definition is

1. In the case of two persons, who participate directly or indirectly in the management, control or capital of the business of the other person; and in the case of more than the two persons.

2. Any other person who participates directly or indirectly in the management, control or capital of the business of the two persons: or

3. An individual who –
   - participates directly or indirectly in the management, control or capital of the business of the two persons.
   - is associated with the two persons by marriage, consanguinity or affinity.
   - the two persons participate in the management, control or capital of the business of the individual.

Implications

The multiplicity of definitions in existing law has led to inter-pretive inconsistencies and audit disputes. This proposal should streamline related-party analysis.

Increase in Tax-Free Per Diem Threshold

The tax-free per diem ceiling is to be increased from KES 2,000 to KES 10,000 per day.

Implications

A long-awaited inflationary adjustment that aligns tax treatment of travel reimbursements with modern business realities.

Taxation of Emoluments

The Bill proposes to amend the Income Tax Act to require employers to apply all applicable deductions, reliefs, and exemptions when computing the tax deductible from an employee's emoluments.

Implications

This amendment aligns with the reforms introduced under the Tax Laws (Amendment) Act, 2024, and is aimed at ensuring that employees benefit from available tax reliefs and exemptions at the point of payroll processing. It eliminates the need for employees to seek refunds through post-filing claims, thereby improving cash flow and administrative efficiency.

Withholding Taxes

The Bill proposes to amend Section 10 of the Income Tax Act to include:

i. The supply of goods to a public entity
ii. The sale of scrap

Implications

This proposal aligns with the reforms introduced under the Tax Laws (Amendment) Act, 2024, and seeks to harmonize the treatment of income from such transactions with the withholding tax (WHT) provisions under Sections 35(1) and 35(3) of the Income Tax Act. By doing so, the Bill clarifies that income arising from the supply of goods to public entities and the sale of scrap is subject to WHT, whether earned by residents or non-residents. The intended outcome is to enhance tax compliance and reduce ambiguity regarding the taxability of such income streams.

Clarified Due Date for Minimum Top-Up Tax (MTT)

The Bill proposes that minimum top-up tax be payable by the end of the fourth month after the end of the year of income.

Implications

The Finance Bill 2025 proposes to amend the Income Tax Act to clarify that, for covered persons, multinational entities with an annual consolidated group revenue exceeding EUR 750 million, the due date for payment of the Minimum Top-Up Tax shall be four months after the end of the financial year.

Limitation of carryover of tax losses

The Bill proposes to limit carryover of tax losses to five years.

Implications

Currently, the Income Tax Act permits taxpayers to carry forward tax losses indefinitely. The proposed amendment would significantly impact taxpayers particularly those in capital-intensive or long-gestation industries who typically take longer to recover initial investments and generate taxable profits.

By capping the carryforward period at five years, affected entities may be unable to fully utilize accumulated tax losses, potentially increasing their effective tax burden and discouraging investment.

Tax on Dividends Paid from Untaxed Profits

Companies must self-assess and declare dividends distributed out of untaxed profits, with tax payable concurrently with the return.

Implications

This proposal seeks to ensure that dividends distributed from profits not previously taxed are subject to taxation at the point of distribution.

Companies will now be required to account for and remit the tax liability on such dividends at the time of filing, increasing administrative responsibility.

This change aims to prevent tax avoidance by ensuring that profits retained without tax are not later distributed without appropriate tax treatment.

Advance Pricing Agreements (APAs)

The Bill proposes to introduce a provision allowing non-resident persons who carry out business with related resident persons or through a permanent establishment in Kenya, or resident persons who carry on business with related persons operating in a preferential regime, to enter into Advance Pricing Agreements (APA).

The APA will be valid for a period not exceeding **five consecutive years.**

Implications

APAs will provide greater certainty in the pricing of controlled transactions. By allowing taxpayers to agree in advance on the transfer pricing methodology, the introduction of APAs will help avoid potential tax audits and litigation.

Once the Bill is enacted into law, it is anticipated that the Cabinet Secretary will issue Regulations or guidelines outlining the practical implementation of the APA provisions. This move is expected to enhance transparency and reduce disputes over transfer pricing matters.

100% Deduction for Implements and Utensils (Non-Plant Assets)

A 100% deduction is introduced for the diminution in value of utensils and implements used in business, excluding plant and machinery.

Implications

Currently, the provision allows deductions based on the Commissioner's discretion, which determines what is considered "just and reasonable," without specifying a set rate. The proposed amendment establishes a clear rate of 100% for such deductions in the year of income, removing any ambiguity in the deduction process.

Repeal of investment deductions

A 100% deduction is introduced for the diminution in value of utensils and implements used in business, excluding plant and machinery.

Implications

This change could significantly impact large-scale investments in regions outside Nairobi and Mombasa. By eliminating these preferential investment deductions, the Bill may reduce the attractiveness of investing in other parts of the country.

KRA Exemption Certificate Timelines Extended

The Finance Bill 2025 proposes to amend the Income Tax Act by extending the statutory timeline within which the KRA is required to process applications for exemption certificates.

The current period of sixty (60) days is proposed to be extended to ninety (90) days from the date of receipt of a duly completed application.

Implications

While the extension may provide KRA with additional time to clear this backlog, there is a need for greater administrative accountability.

It would be beneficial for Parliament to include a provision that deems an exemption application to be automatically approved if not processed within the stipulated timeline, ensuring that taxpayers are not unduly delayed in receiving their exemption status and providing greater certainty and fairness in the process.

Provision on tax rate applicable on fringe benefit

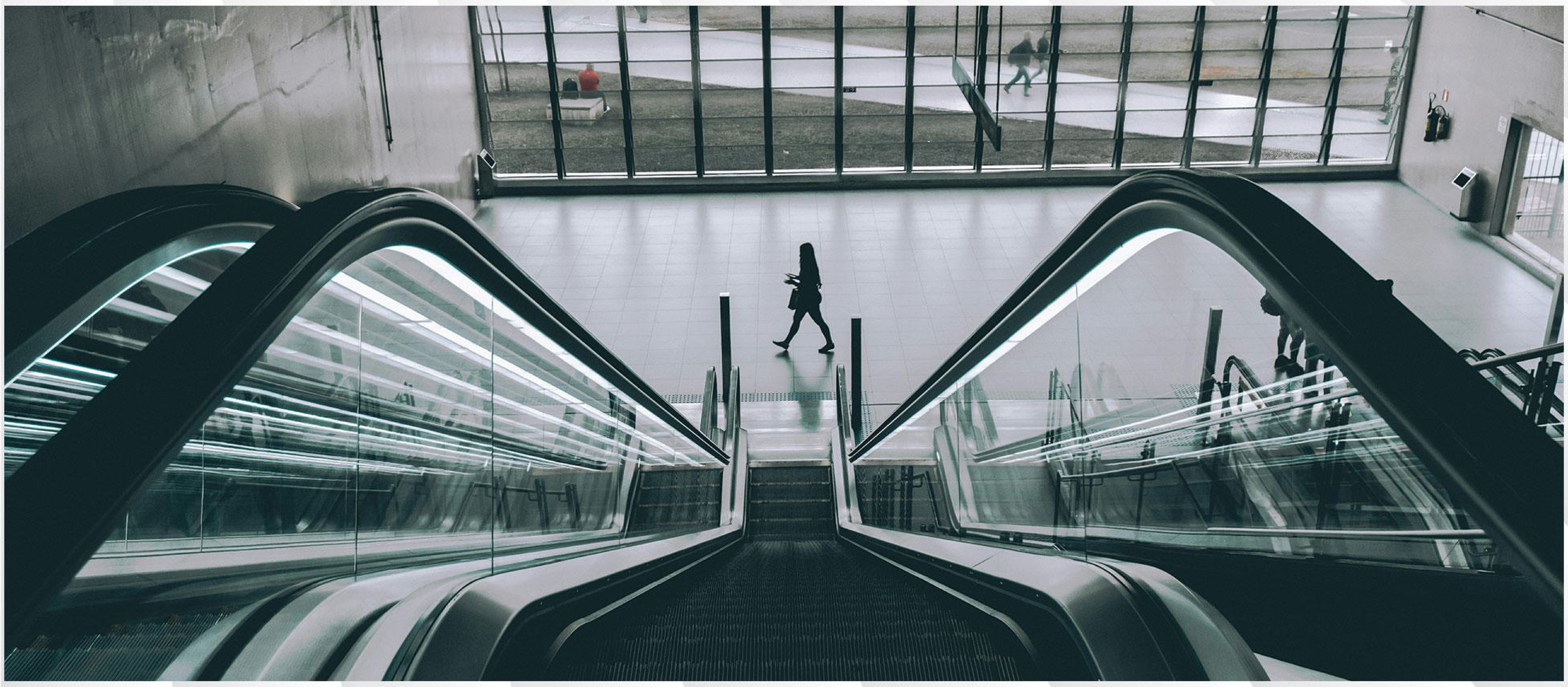
The Bill clarifies that the corporate tax rate, 30%, applies to fringe benefit tax.

Exempt Income

The Finance Bill 2025 proposes to exempt the following categories of income from taxation:

1. Gains accruing from the transfer of securities traded on any securities exchange licensed by the Capital Markets Authority.

2. Dividends paid by a company certified by the Nairobi International Financial Centre Authority shall be exempt from tax where such a company reinvests at least Kenya Shillings two hundred and fifty million (KShs 250 million) in Kenya during the relevant year of income.



Reduced CIT for entities certified by NIFCA

Corporate income tax ("CIT") rate for companies certified by the Nairobi International Financial Centre Authority ("NIFCA") to be 15% for the first 10 years and 20% for the subsequent 10 years subject to other conditions set out in the Bill.

The Bill also proposes a reduced CIT rate of 15% for the first 3 years and 20% for the succeeding 4 years for start-ups certified by NIFCA.

Implications

This proposal is designed to incentivize investment in Kenya by offering competitive tax rates to both established companies and start-ups operating within the Nairobi International Financial Centre (NIFC).

For established businesses, the reduced CIT rate in the initial 10 years could significantly enhance cash flow and capital retention, potentially fostering expansion and attracting international financial services firms to Kenya.

Similarly, for start-ups, the tax relief could stimulate innovation and entrepreneurship within the financial sector.

Taxation of sports initiatives

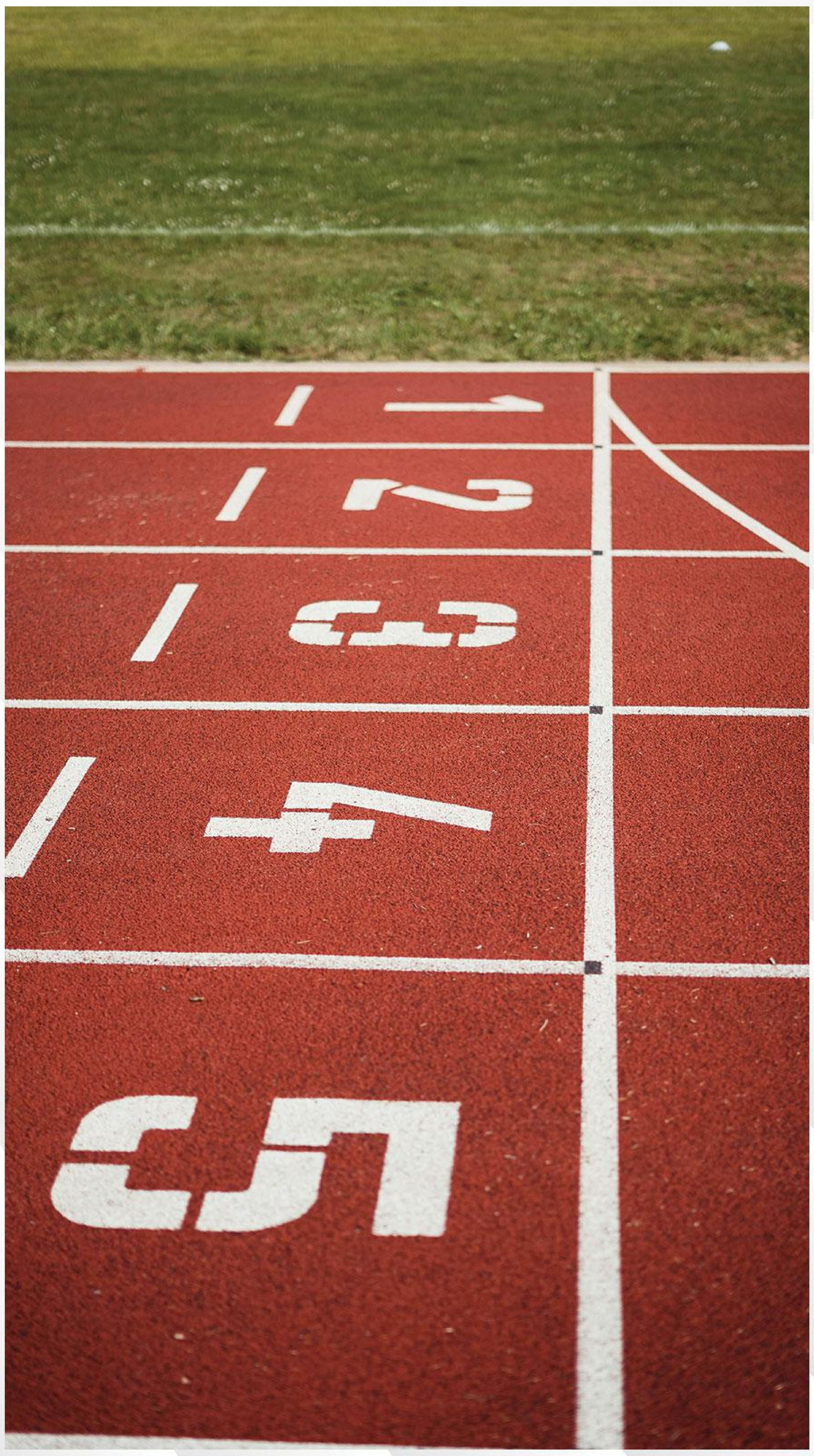
The Bill seeks to include any donation made towards the construction of a public sports facility as an allowable deduction.
The Bill also proposes to delete the provision allowing expenditure incurred in sport sponsorship, with prior approval from the cabinet secretary responsible for sports as an allowable deduction.

Implications

If the proposal is passed, it may have a negative impact on sports initiatives in Kenya.

The deletion of the provision for tax-deductible sponsorships could discourage businesses and organizations from sponsoring sports activities, leading to reduced funding for sporting events, teams, and infrastructure.

Without the tax incentives, companies may be less inclined to invest in sports sponsorship, which could hinder the development and promotion of sports at various levels



Removal of Housing 15% Corporate Tax Rebate

The Bill proposes to scrap the 15% tax rebate for companies constructing 400+ residential units.

Implications

The preferential tax treatment for expenditure related to sports sponsorships and investments in residential housing was designed to encourage large-scale investments, particularly in the government's affordable housing agenda.

Removing or restricting these tax incentives could undermine the government's efforts to stimulate private sector participation in the housing sector.

Specifically, the tax reliefs were intended to attract investment in residential housing development, helping to meet the growing demand for affordable housing.

Without these incentives, developers may be less inclined to invest in housing projects, potentially slowing progress on the affordable housing goals and reducing the availability of affordable homes for the public.

Clarification That Qualifying Dividends and Qualifying Interest Are Final Taxes

The Finance Bill 2025 proposes to amend the Income Tax Act to expressly provide that tax paid on qualifying dividends and qualifying interest shall be treated as a final tax.

Implications

This clarification affirms that no further tax shall be payable by the recipient on such income. taxpayers will have greater certainty regarding their tax obligations.

Digital Asset Tax Rate Halved from 3% to 1.5%

Implications

By reducing the tax rate to 1.5%, the Bill alleviates the tax burden on individuals and entities disposing of digital assets especially because the tax is on the value and not the gain.

This proposal if passed into law may encouraging greater participation in the digital asset market.

CGT Exemption for Transfers from an Individual to a Company where the Individual is the sole- shareholder

The Finance Bill 2025 proposes to exempt from CGT the transfer of property from an individual to a company in which the individual is the sole shareholder.

Implications

This exemption encourages the incorporation of personal assets into corporate entities, which can be particularly beneficial for estate planning, business restructuring, and asset protection purposes.

Since the beneficial ownership remains unchanged, the exemption simplifies the process and eliminates the tax burden typically associated with transferring assets.

Application for Change of Accounting Period

Where a taxpayer wishes to change their accounting year end, they are required to make an application to the Commissioner at least 6 months prior to the year end.

The Bill proposes to automatically allow such applications where the Commissioner has failed to make a determination within 6 months from the date the application was lodged.

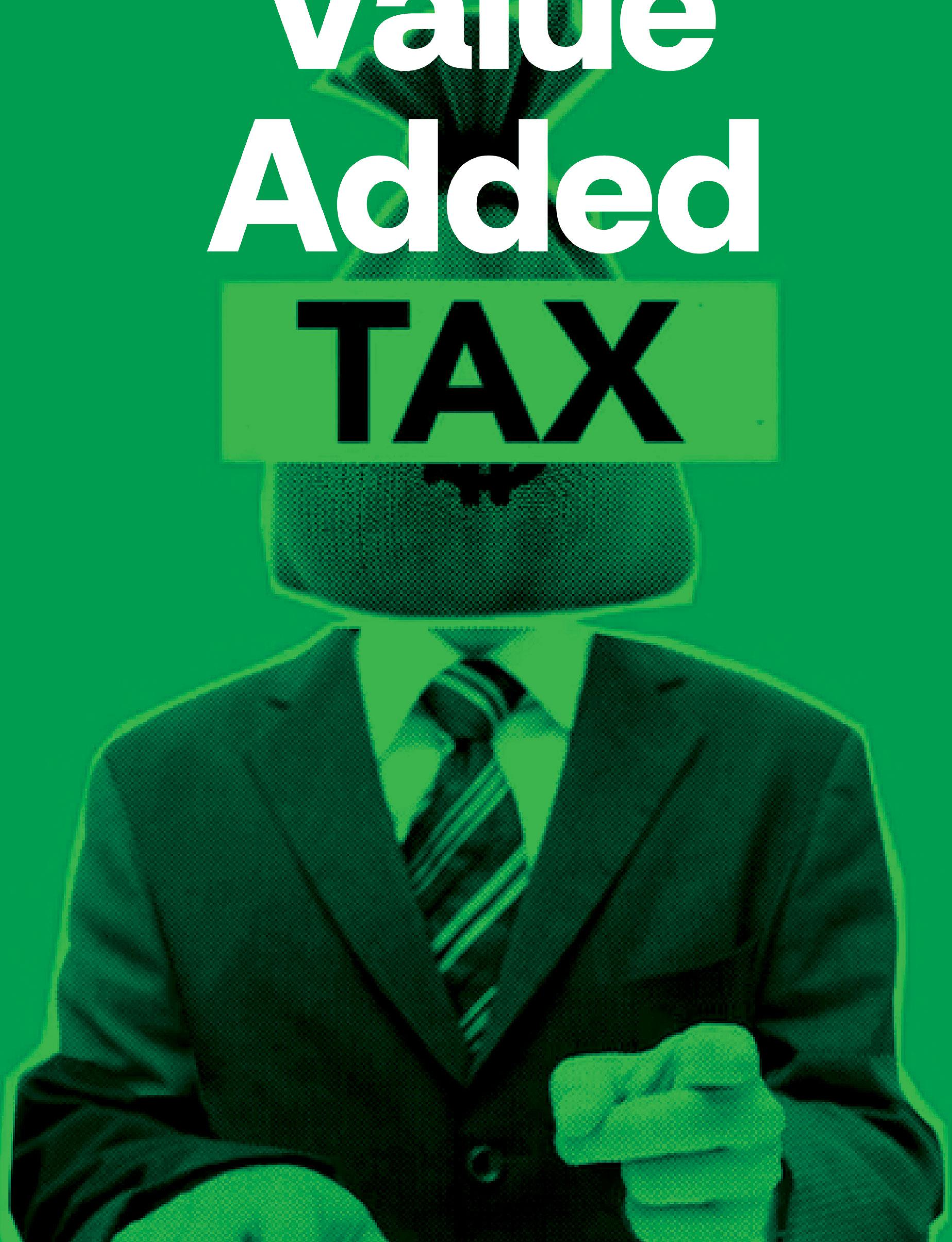
Implications

This amendment introduces a statutory consequence for the inaction of the Commissioner, ensuring that taxpayers are not penalized by administrative delays.

It incentivizes timely decision-making by the Commissioner and provides greater certainty for taxpayers, preventing them from being unfairly impacted by prolonged waiting periods.

By automatically allowing the application if no determination is made within the specified timeline, the Bill promotes efficiency in the tax administration process and protects taxpayers' rights to timely responses.

Value Added TAX



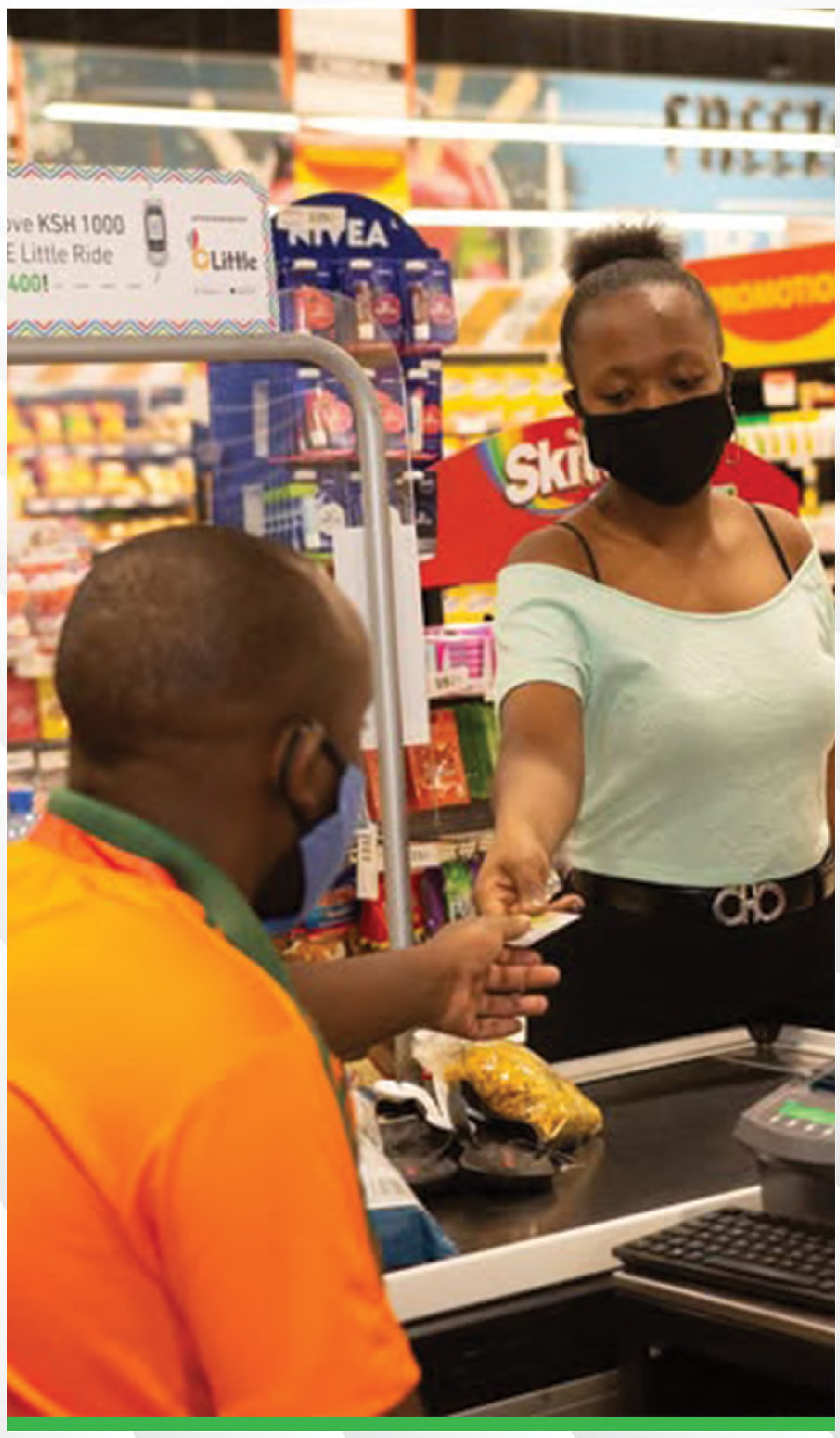
VAT Refunds

The Bill proposes to reduce the timeline to lodge Value Added Tax ("VAT") refunds from 24 months to 12 months.

It further proposes to amend the threshold for lodging VAT refund on bad debts from 3 to 2 years on any outstanding amount from the date of supply

Implications

Reducing the statutory period from 24 months to 12 months will encourage quicker resolution of VAT refunds, potentially improving cash flow for businesses.



The amendment to the bad debts provision by reducing the time frame from 3 years to 2 years is significant for businesses with outstanding debts, ensuring that they can claim VAT refunds sooner when debts are unlikely to be paid which may improve cash flow for businesses that suffer bad debts.

Introduction of VAT Clawback for Misuse of Exempt/Zero-Rated Inputs

Where a person imports or purchases goods or services which are exempt or zero rated and the person subsequently disposes of, or uses, the goods or services supplied in a manner inconsistent with the purpose for which the goods or services were exempted or zero rated, the person shall be liable to pay tax on the goods and services at the applicable rate at the time of disposal or inconsistent use.

Implications

This amendment emphasizes that VAT exemptions and zero-rating are not absolute and are contingent upon the continued compliance with the intended use of the goods or services.

It ensures that businesses or individuals cannot take advantage of these tax benefits and then misuse or divert the goods or services for purposes other than those originally intended

Reclassification of Exempt Goods to Standard-Rated

The following goods are to be reclassified as Standard Rated goods under the proposed Amendment-Standard Rate(16%):

- Other medicaments, containing alkaloids or derivatives thereof, put up in measured doses in form of packings for retail sale

- Weighing Machinery (excluding balances of a sensitivity of 5cg or better), or tariff number 8423.10.00 purchased or imported by registered hospitals upon approval by the Cabinet Secretary responsible for matters relating to health

- Inputs and raw materials used in the manufacture of passenger motor vehicles

- Specially designed locally assembled motor vehicles for transportation of tourists, purchased before clearance through customs by tour operators upon recommendation by the competent authority responsible for tourism promotion provided the vehicle meet the following conditions
    i. The vehicle shall at all times be registered and operated by a company that is licensed under the Tourism Vehicle Regime

Reclassification of Exempt Goods to Standard-Rated (cont'd.)

ii. The vehicle shall be used for the exclusive transportation of tourists

iii. The vehicles shall have provisions for camping, rescue and first aid equipment, luggage compartments and communication fittings and

iv. Any other condition the Commissioner might impose

Provided that tax shall become payable upon change of use or disposal of the vehicle for other use

- Taxable goods for the direct and exclusive use for the construction of tourism facilities, recreational parks of fifty acres or more, convention and conference facilities upon recommendation by the cabinet secretary responsible for matters relating to recreational parks

- Aviation Sector (All goods and parts thereof of chapter 88)

- Direction finding compasses, instruments and appliances for aircraft

- Locally manufactured passenger motor vehicles

- Taxable goods, excluding motor vehicles imported or purchased for direct and exclusive use in geothermal, oil or mining prospecting or exploration by a company granted a prospecting or exploration license

Reclassification of Exempt Goods to Standard-Rated (cont'd.)

- Goods imported or purchased locally for the direct and exclusive use in construction of houses under an affordable housing Scheme

Reclassification of Zero Rated (0%) to Exempt

The following goods are to be reclassified from Zero Rated to Exempt:

- Inputs or raw materials (either produced locally or imported) supplied to pharmaceutical manufacturers in Kenya for manufacturing medicaments as approved from time to time by the cabinet secretary

- Inputs or raw materials locally purchased or imported for the manufacture of animal feeds upon recommendation by the Cabinet Secretary for agriculture

- Supply of motorcycles tariff heading 8711.60.00

- Supply of electric bicycles & buses

- Transportation of sugarcane from farms to milling factories

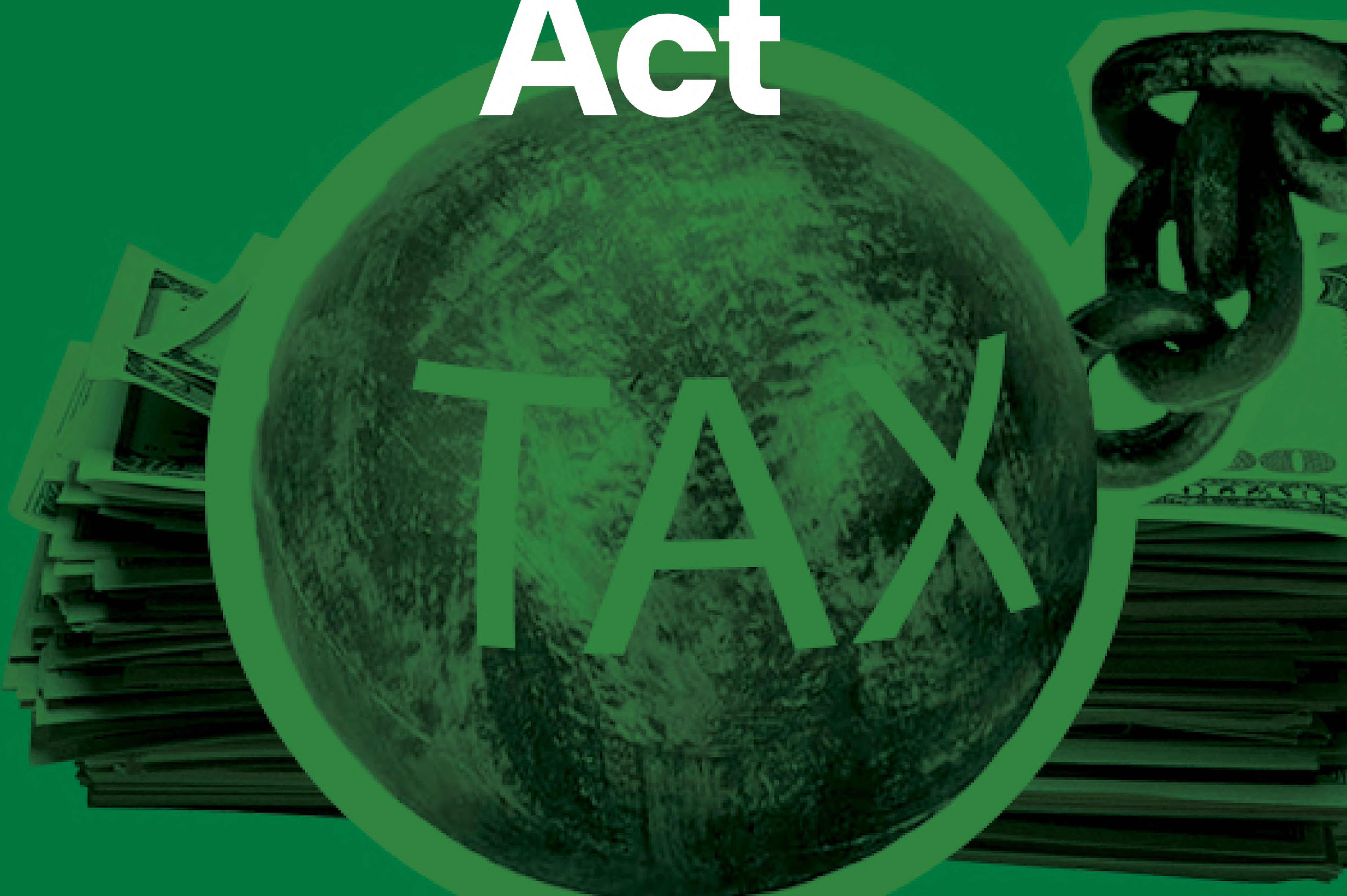
Reclassification of Zero Rated to Exempt (cont'd.)

- Supply of solar and lithium-ion batteries

- Bioethanol vapor (BEV) stoves classified under HS Code 7321.12.900 (cooking appliances and plate warmers for liquid fuel)

- The supply of locally assembled and manufactured mobile phones

Excise Duty Act



c. Excise Duty Act

Definition of digital lender expounded

The Finance Bill, 2025 proposes to revise the definition of a “digital lender” to include any person extending credit through an electronic medium.

The new definition excludes banks licensed under the Banking Act, Sacco societies registered under the Co-operative Societies Act, and microfinance institutions licensed under the Microfinance Act.

Implications

This expanded definition removes the previous requirement for licensing by the Central Bank of Kenya (CBK), signaling the government’s intention to bring more unregulated or non-traditional lenders into the tax framework, specifically for excise duty on loan fees and interest.

Classification of Goods by EAC Tariff Code

The Bill proposes a provision stating that goods should be classified according to the tariff codes set out in Annex 1 to the East African Community (EAC) Customs Union Protocol. The general rules of interpretation outlined in this annex will apply when classifying goods for excise duty purposes.

Implications

This amendment creates a direct link between Kenya's excise duty classification system and the EAC Common External Tariff (CET), ensuring consistency in product classification across customs, import duties, and excise taxation.

Introduction of "Digital Marketplace" definition

The Bill seeks to introduce the definition of a digital marketplace to include an online platform which enables users to sell goods or provide services to other users.

Introduction of "Digital Marketplace" definition

Implications

This aligns with the definition established in the VAT Act, reinforcing the government's strategy to uniformly tax the digital economy and platform-based services across various tax laws.
For purposes of this provision, a non-resident person means a person outside Kenya.

Place of supply of excisable services

The Bill seeks to clarify that if the place of business of the supplier is outside Kenya, the supply of services shall be deemed to be made in Kenya if the services are consumed by a person in Kenya through the internet, an electronic network or a digital marketplace.

Implications

This aligns with a destination-based taxation principle, where excise duty is imposed based on where the service is consumed, rather than where it is provided.

Timelines for issuance of licences

The Bill proposes to introduce a statutory 14-day timeline for the Commissioner to consider the licence application.

This proposed amendment, seeks to establish a clear timeline for the issuance (or refusal) of excise licences, which previously had no specified timeframe.

Implications

This is a welcome move as it helps avoid administrative delays and supports ease of doing business for local manufacturers and importers.

Tax Procedures Act

Exemption from Stamp Duty on Property Registered as Security for Unpaid Tax

The Bill proposes to amend the Tax Procedures Act, 2015, to exempt from stamp duty the registration of a commissioner's notification.

Implications

Currently, when a taxpayer with property in Kenya fails to settle their tax liability by the due date, the Commissioner is empowered to notify the Land Registrar in writing to have the taxpayer's interest in the property registered as security for the outstanding tax.

The Registrar must then register this notification in a manner equivalent to an instrument restricting disposal of the property.

The proposed amendment seeks to waive the stamp duty typically applicable to such registrations, thereby removing a cost barrier in enforcing tax recovery mechanisms and enhancing administrative efficiency.

Extension of Agency Notices to Non-Residents

The Bill proposes to amend the Tax Procedures Act, 2015, to exempt from stamp duty the registration of a commissioner's notification.

Implications

The proposed change ensures that non-resident persons who are liable to tax in Kenya are also subject to the same enforcement mechanisms as resident taxpayers.

Deletion of Provision Protecting Trade Secrets and Customer Data from Mandatory Sharing

The Bill also proposes to delete an existing provision that restricts the Commissioner from compelling taxpayers to integrate or share data relating to:

(a) trade secrets; and
(b) private or personal data held on behalf of customers or collected in the course of business

Implications

The proposed deletion raises serious data privacy and confidentiality concerns, as it would potentially allow the tax authority to compel access to sensitive commercial information and customer-specific personal data.

This could place businesses in conflict with existing data protection laws, such as the Data Protection Act, 2019, and may expose them to legal and reputational risks

Computation of Time Following the Commissioner's Approval for Late Objection Filing

The Finance Bill 2025 proposes that where the Commissioner grants a taxpayer leave to file an objection out of time, the period within which the Commissioner may make an objection decision shall commence from the date the objection is lodged

Implications

This amendment eliminates existing ambiguity around the computation of time in late objection cases. It ensures that both the Kenya Revenue Authority (KRA) and taxpayers have a shared and predictable timeline, thereby promoting procedural clarity, fairness, and administrative efficiency in the handling of tax disputes.

Deletion of Working Days Computation Rule

The Finance Bill 2025 proposes to delete the provision introduced less than a year ago that excluded Saturdays, Sundays, and public holidays from the computation of time for lodging an objection with the Commissioner (section 51), and for filing appeals with the Tax Appeals Tribunal (section 52), the High Court (section 53), and the Court of Appeal (section 54).

Implications

If enacted, this amendment will revert the law to its earlier position, where time is computed based on calendar days, and if a deadline falls on a weekend or public holiday, the relevant action must be taken on the preceding working day.

This effectively shortens the period available for taxpayers to respond or take action compared to the current position.

Penalty for failure to deduct or withhold tax

The Finance Bill 2025 proposes to amend the law to provide that, notwithstanding the general rule that a person who fails to deduct, withhold, or remit tax is liable for the principal tax, penalties, and interest as if the tax were due and payable by that person, such liability for the principal tax shall not arise where the recipient of the payment has duly paid and accounted for the full amount of tax due.

This proposed provision seeks to limit the exposure of withholding agents to the principal tax in instances where the ultimate tax liability has already been discharged by the payee.

Implications

This is a positive and pragmatic change that aligns tax enforcement with actual revenue outcomes.

It prevents the duplication of liability and protects the payee from being penalised for technical lapses where the underlying tax obligation has already been met by the recipient.

However, the payee will still be liable for any penalties and interest arising from non-compliance with withholding obligations.

Power to Waive Penalties and Interest

The Bill proposes to give the Cabinet secretary the power to, on the recommendation of the Commissioner, waive the whole or part of any penalty or interest imposed under this Act where the liability to pay the penalty or interest was due to:

a) an error generated by an electronic tax system;

b) a delay in the updating of an electronic tax system;

c) a duplication of a penalty or interest due to a malfunction of an electronic tax system; or

d) the incorrect registration of the tax obligations of a taxpayer.

Implications

This is a welcome move which aims to ensure that taxpayers are not unfairly penalized for system-related issues beyond their control.

Conclusion

It is vital to underscore that the current draft remains subject to refinement through the constitutionally mandated public participation process. The Departmental Committee on Finance and National Planning will be responsible for facilitating this engagement, offering Kenyans and stakeholders an invaluable opportunity to provide input through written and oral submissions.

The Committee will thereafter table a report before Parliament, where Members of the National Assembly may propose further amendments before passage. If approved, the Bill will be forwarded to the President for assent and formal enactment into law.

We therefore urge all stakeholders to engage actively in the consultation process. Meaningful participation will be key to ensuring that the final legislation is responsive, equitable, and supportive of Kenya's long-term economic growth.

Let's Work Together

Quartet Consulting are a dedicated team of seasoned tax professionals committed to providing comprehensive and personalized tax services to meet your unique financial needs.
We're excited to connect and collaborate with you on innovative strategies that will shape the future of your business.

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