

MEMO

Date: Monday, 12th July 2021
Subject: KENYA FINANCE ACT, 2021

The Finance Act, 2021 has amended the definition of other fees by deleting **fees or commissions earned in respect of a loan**.

We understand that the intended objective of the deletion is to bring **fees or commissions earned in respect of a loan** under the ambit of excise duty, however, we consider this a gray area for the reasons set out below.

The Finance Act, 2012 (assented on 27 April, 2012) introduced excise duty on **other fees** charged by financial institutions, however, it did not provide a definition of the term **other fees** upon which excise duty was to be imposed.

To clear the ambiguity, the Finance Act, 2013 (assented on 24 October, 2013) introduced a definition for **other fees** to mean *any fees, charges or commissions charged by financial institutions, but does not include interest*.

Following the enactment of the Excise Duty Act, 2015 which repealed the C&E Act, **other fees** was defined to include *any fees, charges or commissions charged by financial institutions relating to their licensed financial institutions, but does not include interest on loan or return on loan or an insurance premium or premium based or related commissions*.

The Excise Duty Act failed to define interest which resulted in differing interpretations of what constitutes interest, with majority of the financial institutions deeming **loan related fees** as interest and therefore not chargeable to excise duty. The exclusion of loan related fees from excise duty plunged the financial institutions in legal battles with the Kenya Revenue Authority (KRA) with most of the cases ending at the Tax Appeals Tribunal (TAT).

In the case of **National Bank of Kenya Limited versus Commissioner of Domestic Taxes**, the TAT ruled that excise duty was not applicable on loan commitment and loan appraisal fees, pre-2013 Finance Act & post July 2013 when the Finance Act amendments came into force. In both periods, the TAT held that loan related fees fall within the ambit of interest and therefore not subject to excise duty.

In reaching its finding in the aforementioned case for the excise duty assessment in the pre-2013 Finance Act period, the TAT held that the Finance Act, 2012 failed to provide a definition for the term **other fees** and therefore left room for differing interpretations. Accordingly, the TAT held that the ambiguity that resulted from the amendment introduced by the Finance Act, 2012 must be interpreted in favour of the Appellant. The TAT therefore found that the KRA erred in applying excise duty on interest and interest related fees prior to the introduction of the Finance Act, 2013.

In its ruling for the excise duty for the assessment on interest and interest related fees post July 2013, the TAT cited the case of **Co-operative Bank of Kenya versus Commissioner of Domestic Taxes in the Tax Appeal No. 45 of 2017** where it was held that in the absence of a definition of the term 'interest' under the Excise Duty Act, inference of an operational definition is found in the Income Tax Act (ITA). The ITA defines interest to mean "*interest payable in any manner in respect of a loan, deposit, debt, claim, or other right or obligation, and includes premium or discount by way of interest and any commitment or service fee paid in respect of any loan.*"

In relation to the above case and the TAT's finding on KRA's assessment of excise duty on interest & interest related fees post July 2013, the Appellant submitted that the definition of **other fees** introduced through the Finance Act, 2013 excluded interest from the ambit of excise duty. The Finance Act, 2013 did not define however, what constitutes interest.

The Appellant further submitted that it was necessary to define interest so as to determine the nature of payments that are not subject to excise duty. The Appellant offered various definitions of interest based on case law and ordinary meaning of the word, some of which we reproduce below:

(a) Black's Law definition

"...interest is the compensation allowed by law or fixed by the parties for the use or forbearance of borrowed money. Basic cost of borrowing money or buying an instalment contract. Payments abura peas are Linda for the use of money. Cost of using credit of funds of another.

(b) Case laws definitions

- (i) **Deputy, Administratrix v. Du Pont [1940] USSC 7** where interest was defined as *"...compensation for the use or forbearance of money"*.
- (ii) **Skeen v. Slavik, 555S.W.2n 516** *"...where a charge is admittedly compensation for the use, forbearance, or detention of money, it is, by definition, interest regardless of the label placed upon it or the artfulness with which it is concealed"*.

Based on the Appellant's submissions as highlighted above, and the TAT ruling on the matter, fees or commissions earned in respect of a loan could be deemed as interest as per the definitions highlighted above.

In a latest bid to bring clarity and certainty to what constitutes '**other fees**' chargeable to Excise Duty, the Finance Act, 2019 amended the definition of the term '**other fees**' to mean *any fees, charges or commissions charged by financial institutions relating to their licensed financial institutions licensed activities, but does not include interest on loan or return on loan or an insurance premium or premium based or related commissions or fees or commissions earned in respect of a loan or any share of profit or an insurance premium or premium based or related commissions specified in the Insurance Act or regulations made thereunder or specified in the Insurance Act or Regulations"*.

The Finance Act, 2019 excluded from the purview of excise duty fees or commissions earned in respect of a loan.

The deletion of the phrase **fees or commissions earned in respect of a loan** by the Finance Act, 2021 could be interpreted to mean that they are now chargeable to excise duty. This interpretation is in line with the KRA's position on the matter. The deletion, however, has reintroduced the ambiguity that the Finance Act, 2019 sought to correct and it now leaves room for differing interpretations where **fees or commissions earned in respect of a loan** can be interpreted as interest as defined in Section 2 of the ITA, hence exempt from excise duty.

Our view is that the industry needs to take a combined position on the change and get a joint clarification on this matter.

Caveat

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