ABRIDGED MEMORANDUM SUBMITTED BY THE KENYA PRIVATE SECTOR ALLIANCE (KEPSA) ON THE FINANCE BILL, 2023, TO THE NATIONAL ASSEMBLY DEPARTMENTAL COMMITTEE ON FINANCE AND NATIONAL PLANNING

Critical clauses to be relooked at to enhance the competitiveness of Kenyan Businesses

1. *Promoting Business Certainty through appropriate Tax Dispute Resolution Mechanisms*
   - The Finance Bill's Clause 36 (a) and (b) pertain to the Tax Appeal Tribunal Act. The suggestion is that before appealing a disputed tax decision, parties must deposit an amount equal to twenty per cent of the disputed tax or security with the Commissioner. However, we propose removing these proposed clauses. These clauses infringe on the right to justice enshrined in Kenya's Constitution and will significantly affect taxpayers' cash flows. Tax disputes can take years to resolve, even before the High Court, and the proposal also places additional responsibilities on the Commissioner.
   - We recommend deleting Clauses 59, 61, and 62 from the Finance Bill due to their adverse impact on the Tax Dispute resolution mechanism. Clause 59 removes the Court's discretion to consider additional grounds and doesn't account for new information. We propose the penalty in Clause 61 be equal to the tax shortfall, resulting in a 25% revenue increase while still considering innocent errors.

2. *Promotion of Kenya as a Services Hub*
   - Clause 33 proposes the amendment of the VAT Act to put exported services as exempt from VAT as opposed to zero-rated. The proposal would affect the deductibility of input tax incurred by the suppliers of such services. This has an adverse ripple effect on the country's price competitiveness in the supply of cross-border services. We propose that exported services be zero-rated.

3. *Export Promotion Levy*
   - Clause 68 of the Finance Bill proposes to amend The Miscellaneous Fees and Levies Act to introduce export and investment promotion levies. The East Africa Customs Control Management Act provides for import duty which addresses the intention of this new proposal. The introduction of additional levies puts Kenya at a disadvantage as a preferred location for investment, especially compared to EAC and COMESA.
   - We propose to limit the levy to instances where the items sought to be imported can be sufficiently sourced locally.
   - Kenya imported 14,074 tonnes of corrugated paper and paperboard worth Ksh 1.2 billion, and 129,700 tonnes of uncoated kraft paper worth Ksh 10.7 billion in 2021. The proposed tax may harm Kenya's production of end products due to lack of raw material.

4. *Affordable petroleum products to cushion the ordinary Kenyan and reduce the living cost*

- Clause 28 (a) of the Finance Bill proposes to amend the VAT Act by putting petroleum products into the standard VAT category. The increase of 8% will lead to a corresponding increase in the cost of fuel by Kes 12.56 and 12.76 per litre for Diesel and Petrol, respectively, on the current Nairobi pump price of Kshs 168.4 and 182.7. Further, Oil Marketing Companies (OMCs) will need additional capital to sustain their margins. In 2019 OMCs enjoyed margins of 0.1% with an investment of Ksh. 1 million. In July 2023, if the proposal passes, OMC margins will drop to 0.05% with an investment of Ksh. 2 million. This additional cashflow financing will reduce the OMC margins and profitability hence a reduction in corporate taxes paid to the Government. Therefore, we propose deleting the proposal to retain VAT at 8%.

5. *Improving compliance for increased revenue collection*
    - Clause 20 (c) of the Finance Bill proposes to amend the Income Tax Act, Clause 41 proposes amends to the Excise Duty Act, and Clause 54 (b) proposes to amend the Tax Procedures. The clauses all speak to reducing the time for tax remitting for the different industry players, with timelines from 24 hours to 3 days.
    - Proposals may harm cash flows, create admin and compliance issues, and increase costs due to tight tax payment deadlines. Our suggestion is to set the due date on the 9th day of the following month, which would enable the smooth collection of taxes while ensuring maximum convenience for both taxpayers and the Government.
    - Clause 30 (a) proposes an amendment of the Value Added Tax Act, 2013, in subsection (2), by deleting the word **"or"** appearing in paragraph (a) and substituting, therefore, the word **"and".** The amendment is against the Tax principle of simplicity. Making it mandatory for a purchaser to have proper documentation, including invoices, will make it easier for taxpayers claiming input VAT as they need visibility of the supplier's return. We propose deleting this proposal to retain the word '**or.**'
    - Clause 30(b) proposes an amendment of the Value Added Tax Act, 2013, to disallow expenditure or loss incurred where the invoices of transactions are not generated from an electronic tax invoice system under income tax computation. The proposal will limit the participation of Micro and Small Enterprises that are not eligible for VAT registration (Not within the 5 million thresholds under the Act) from conducting business with bigger enterprises.

6. *National Housing Development Fund*
    - Clause 76 amends the Employment Act to provide for the contribution of an employee and employer towards the National Housing Development Fund. Our proposal is to implement a voluntary contribution system starting in January 2024, with employer matching. This approach avoids any challenge to private property rights and ensures constitutionality. Regulations for fund accountability should be developed in the Finance Bill.

7. *Stability in the taxation regime in the Gaming sector.*
    - Clause 2a of the Finance Bill proposes to amend the Income Tax Act by expanding the definition of winnings to include the amount staked and the gains. The courts put this definition in the following decisions: Tax Appeal No. 304 of 2019 Pevans East Africa Limited vs The Commissioner of Domestic Taxes and Others, and Tax Appeal No. 169 of 2020 Resort Kenya Limited vs Commissioner of Domestic Taxes. In the above decisions, the Tribunal determined the methodology used in calculating winnings by ruling that winnings refer to payouts by the licensee but do not include the amount staked by the punter. Accordingly, we propose that the proposal is deleted to retain the original definition of 'winnings', which indicates winnings as 'gains'.
    - Clause 43 b (v) & (vii) propose to amend the first schedule of the Excise Tax referring to Part II – (v) and (vii), which do not exist as the Court has nullified it after their introduction in the Finance Act 2021. The reference case is *Constitutional Petition No. E406 of 2021.*

8. *Excise Duty on Sugar and advertisement*
    - Clause 43(a)(vi) proposes the amendment of the First Schedule to the Excise Duty Act to introduce an excise rate of Shs 5 per kg on imported sugar. The proposal doesn't specify which tariff codes will be affected, leading to excise duty on industrial sugar. This puts sugar-based products in Kenya at a disadvantage, compared to other EAC countries without the duty. Uganda is the only country in the region with industrial sugar, and local demand exceeds the supply. Therefore, we propose excluding industrial sugar from the proposal.
    - Clause 43 (b) (x) proposes the amendment of the Excise Duty Act to have duty on fees charged on advertisements across different mediums. The proposed excise tax increase could harm the media industry, affecting 21.1% of its advertising income and reducing tax contributions. We recommend removing the clause to prevent such negative impacts.

9. *Promotion of the local Motor Vehicle Manufacturing Industry.*
    - The Finance Bill's Clause 24(b) (iv) aims to introduce a new definition of local content in Head B of the Third Schedule to the Income Tax Act. Unfortunately, the industry is currently not benefiting from the incentives outlined in the Act as it still requires higher assembly volume.
    - To address this issue, the amendment should take into account the definitions and incentives outlined in the National Automotive Policy, which considers various levels of assembly.

10. *Promotion of best practices to support agriculture and the pharmaceutical industry*

- The proposed amendment to Clause 34 (a) (i) (ii) (iii) of the VAT Act aims to eliminate the zero-rated status of input and raw materials supplied to pharmaceutical manufacturers in Kenya for producing medicaments. Likewise, inputs and raw materials for producing agricultural pest control products, whether locally produced or imported, will no longer be exempted.
- The counterfeiting and illegal trade of pesticides in Kenya amount to Ksh. 11.3 billion, resulting in significant losses in investment, this would increase if the proposals go through.
- This move may further increase pesticide costs, leading to higher prices of food products. Moreover, Kenya's competitiveness in the global horticultural market may decline as it has already lost 13% of the market share to emerging players like Ethiopia, Rwanda, and some South American countries.