



IPF

INSTITUTE OF PUBLIC FINANCE



UNIVERSITY

**PUBLIC FINANCE MANAGEMENT
(PFM) BOOT CAMP PROGRAM**

TAXATION MODULE





COPYRIGHT

This Training Manual is a publication of the Institute of Public Finance (IPF), designed specifically for use in the University PFM Boot Camp Training Program.

IPF retains the copyright of this material. To use this material, or any part thereof, in any other publication or on a website, please obtain the permission of IPF's Communications department.

To use or adapt these materials, or any part thereof, for running non-profit educational programmes led by other organizations, please consult with IPF's Communications department. To contact IPF, please send an email to communications@ipfglobal.or.ke.

OVERVIEW

This Training Manual has been developed to serve as a guide for Trainers of Trainers in IPF's University PFM Boot Camp Program. Specifically, it focuses on policy, legal and regulatory aspects of taxation at the international, national and subnational levels; opportunities for public participation; analysis of tax policy; as well as evidence-informed advocacy skills, including the development of submissions like memoranda on taxation to government agencies. ToTs are encouraged to use participatory methods, techniques, and tools, such as group discussions, brainstorming, case studies, exercises, video shows, and role-plays.

Purpose

This manual aims to equip university students with relevant PFM knowledge and skills for effective

participation in governance and tax policy-making processes.

Overall Objective

To provide a standard training tool that enhances the capacity of the trainees to be efficient and effective in participating in governance and tax policy-making processes at the national and subnational levels.

Training Modules

The training sessions comprise eight (8) modules which cover cross-cutting issues in policy, legal and regulatory aspects of taxation at the international, national, and subnational level.

For questions or clarifications, please contact communications@ipfglobal.or.ke.



Table of Contents

COPYRIGHT	iii
OVERVIEW	iv
Purpose	iv
Overall Objective	iv
Training Modules	iv
1. Introduction to the Fundamentals of Taxation	xi
1.1 Definition, historical evolution and purpose of taxation	1
1.1.1 What is Taxation?	1
1.1.2 How did the concept of taxation develop historically?	2
1.1.3 What is the Purpose of Taxation?	2
1.2 Core Principles of Taxation	4
1.2.1 Worldwide Principles of Taxation	4
1.2.2 Constitutional Underpinning of Principles of Taxation in Kenya	4
1.3 Understanding Direct and Indirect Taxes	6
1.4 Key Institutions and their Role in Taxation	7
1.4.1 The National Treasury	7
1.4.2 Kenya Revenue Authority (KRA)	7
1.4.3 Parliament	7
1.5 Tax Policy Framework and the Medium-Term Revenue Strategy (MTRS) in Kenya	7
1.6 Understanding Tax Laws: Why is Tax Law Different?	8
1.6.1 Yearly Change of Law	9
1.6.2 Uniformity under Tax Law	9
1.6.3 Prescription of Time	9
1.6.4 Multiplicity of Statutes	9

2. Direct Taxes Taxation of Income in Kenya 11

2.1 The Income Tax Act 14

2.1.1 What is Income and why do we tax income? 14

2.1.2 Types of income subject to income tax in Kenya: 14

2.1.3 Allowable deductions..... 16

2.1.4 Instalment Tax..... 17

2.1.5 Pay As You Earn (PAYE) 18

2.1.6 Withholding Tax (WHT)..... 20

2.1.7 Advance Tax..... 22

2.1.8 Rental Income Tax..... 22

2.1.9 Turnover tax (ToT)..... 23

2.1.10 Significant Economic Presence (formerly Digital Service Tax) 24

2.1.11 Minimum Top-up Tax..... 25

3. Indirect Taxes 26

Definition of Key Terms 27

3.1 The Value Added Tax Act, 2013— General Principles of VAT 28

3.1.1 VAT Compliance in Kenya 28

3.1.2 The Concept of Taxing Value in the Chain of Production 28

3.1.3 Stages of the VAT Chain 28

3.1.4 Accounting for VAT: input & output mechanism 30

3.1.5 How VAT Works: Zero-Rated, Vatable and Exempt 30

3.1.6 Withholding VAT 30

3.1.7 VAT records and returns – Etims 31

3.1.8 VAT & International Trade 31

3.1.9 VAT Refunds 32

3.2 Excise Duty 32

3.2.1 History of Excise Duty 33

3.2.2 Types of Excise Duty..... 33

3.2.3 Rationale for Excise Duty 33

3.2.4 Excisable goods and services..... 33

3.2.5 Overview of the Excise Duty Act, 2015..... 34

3.3 The East African Community Customs Management Act, 2004 36

3.4 Miscellaneous Fees and Levies Act, 2016.....	37
3.4.1 Objectives of the Act.....	37
3.4.2 Provisions.....	37
3.4.3 Amendments to the Act	38
4. Non Tax Revenues	39
4.1 What are Non-Tax Revenues	40
4.1.1 Kenya's non-tax revenue Compared to the Region's	40
4.1.2 Examples of Non-Tax Revenues	41
4.1.3 Role of Non-Tax Revenues in government financing.....	41
4.1.4 Why is Kenya's Non-Tax Revenue So Low?	42
4.2 ARE NON-TAX REVENUES A GOOD ALTERNATIVE TO TAX REVENUES?	42
4.2.1 Advantages of Non-Tax Revenues	42
4.2.2 Limitations of Non-Tax Revenues	42
4.2.3 Equity In Non-Tax Revenue	43
4.2.4 Recommendations for Enhancing Non-Tax Revenue in Kenya	43
5. Taxation at the Sub-National Level Own Source Revenue	45
5.1 Taxes	47
5.1.1 Property tax	47
5.2 Charges and fees	47
5.3 Levies	49
6. Contemporary Issues in Taxation	51
6.1 Tax Expenditures	52
6.1.1 What are tax expenditures?	52
6.1.2 How are tax expenditures calculated	53
6.1.3 What is the size of tax expenditure in Kenya?.....	53
6.2 International Taxation Frameworks.....	55
6.2.1 OECD INCLUSIVE FRAMEWORK	55
6.2.2 What is the OECD Inclusive Framework?	57
6.2.3 The Development of OECD Inclusive Framework in Kenya	57
6.3 Environmental Taxes and their Role in Climate Change and Revenue Generation..	58

6.3.1 What Are Environmental Taxes?	58
6.3.2 What different forms of environmental tax exist?	60
6.3.3 What is the Core Objective of Environmental Taxes? Climate Change or Revenue Generation	60
6.3.4 Do we have Environmental Taxes in Kenya?	60
6.3.5 What Other Climate Finance Initiatives Exist in Kenya	62

7. Decoding The Finance Bill **64**

7.1 The Central Role of the Finance Bill in Public Finance Management (PFM) **66**

7.1.1 Background to the Finance Bill **66**

7.1.2 What is the Finance Bill? **66**

7.3 The legislative process of a Financial Bill **67**

7.3.1 Pre-Legislative stage (Formulation & drafting) **67**

7.3.2 Committee Stage (Clause-by-Clause Review)

7.3.3 Senate Consideration (If applicable) **71**

7.3.4 Presidential Assent & Enactment **71**

7.3.5 Implementation & Monitoring **71**

7.3.6 Strengths and Weaknesses of the Finance Bill **71**

7.3.7 The Impact of the Finance Bill on Taxation **72**

7.4 Analysis and Participation in the Finance Bill Process: How to Develop and Submit an Effective Memorandum **72**

7.4.1 Key steps in developing an effective memorandum **73**

7.4.2 Step 3: Submit Memorandum and implement advocacy strategies **74**

8. Revenue in Numbers **75**

8.1 Revenue performance **76**

8.1.1 National Government- Ordinary revenue and Appropriation in Aid **76**

8.1.2 County Governments **77**

8.2 Credibility of revenue targets in Kenya **77**

8.2.1 National Governments **77**

8.2.2 County Governments **78**

List of Tables

Table 1: Preferential CIT rates	15
Table 2: Installment tax due dates and percentages	18
Table 3: Individual Tax Bands and Rates, with effect from 1st July, 2023	18
Table 4: PAYE calculation for someone earning Ksh 50,000	20
Table 5 : Withholding Tax Rates	20
Table 6: Difference between DST and SEPT	24
Table 7:Example of VAT application.....	29
Table 8:Excise duty exemptions contained in the Second Schedule	34
Table 9:Key Differences Between Tax and Non-Tax Revenues	41
Table 10: Opportunities for public participation	73

List of Figures

Figure 1: A snippet of the Income Tax Act (Section 3)	15
Figure 2: A snippet of Safaricom's financial report	17
Figure 3: A snippet of the Income Tax Act (Section 3)	22
Figure 4: Example of application of VAT	29
Figure 5: A snippet of the Tax Law (Amendment) Act, 2024	35
Figure 6: A snippet of the Excise Duty, Act 2015	35
Figure 7: Total Tax expenditures (Ksh billion)	54
Figure 8: Total tax expenditures (% of GDP)	54
Figure 9: TE's shares by revenue head	55
Figure 10: Snapshot of the Legislative Stages of a Bill to a Law	70
Figure 11: Tax heads contribution to the total revenue	76
Figure 12: Sources of County Revenue	77
Figure 13: Revenue Target and Outturn	78
Figure 14: Revenue Targets vs Actuals	78



1. Introduction to the Fundamentals of Taxation



Session Objectives

- i. Develop a foundational understanding of taxation, including its definition, historical origins, and fundamental purpose.
- ii. Explore key debates on taxation, including moral arguments, points of contention, and areas of disagreement.
- iii. Examine the core principles of taxation as established in the Constitution of Kenya 2010 and their significance in fiscal policy.
- iv. Gain insight into the fundamentals of taxation, including who is taxed, what is taxed, and the concepts of tax impact and tax incidence.

- v. Identify and analyze the different types of taxes in Kenya, as outlined in the Constitution, and their role in revenue generation.
- vi. Understand the characteristics of taxation laws, including their structure, application, and legal implications.

Resources Needed

- The Constitution of Kenya 2010
- The Tax Laws in Kenya: The Income Tax Act, The Value Added Tax Act and the Excise Duty Act
- The National Tax Policy
- The Medium-Term Revenue Strategy

How to Run the Session

Icebreaker Activity: The Taxation Challenge

Instructions:

- Divide participants into small groups and give each group a balloon.
- Ask them to form a circle and hold hands, ensuring they maintain this connection throughout the activity.
- As a team, they must keep the balloon in the air, preventing it from touching the ground—all while keeping their hands linked.
- **Reflection:**
After the activity, facilitate a discussion on how this exercise relates to the purpose of taxation:
 - Just like the balloon represents essential public services, taxation ensures they remain supported.
 - Keeping the balloon afloat requires teamwork and shared responsibility, much like how taxes function when everyone contributes fairly.
 - If one group member fails to participate effectively, the balloon may drop—just as inadequate taxation can weaken public systems.

1.1 Definition, historical evolution and purpose of taxation.

1.1.1 What is Taxation?

Taxation can be understood from **three** key perspectives:

- **Taxation as the Price of Civilization:** As **Oliver Wendell Holmes Jr.** famously stated, “Taxes are what we pay for civilized society.” From this perspective, taxation is a financial obligation levied on individuals and businesses to fund essential public services, maintain infrastructure, and uphold societal well-being.ⁱ

- **Taxation as a Shared Sacrifice:** Reflecting on the inevitability of taxation, **Benjamin Franklin** remarked, “In this world, nothing can be said to be certain, except death and taxes.” This view frames taxation as an unavoidable yet essential contribution from all members of society.
- **Taxation as a Burden or a Necessity:** A more critical perspective is offered by **Chief Justice John Marshall**, who in *McCulloch v. Maryland* cautioned that “The power to tax involves the power to destroy.”ⁱⁱ This view acknowledges taxation as a legal tool

for revenue collection but also highlights the risks of excessive or mismanaged taxation.

1.1.2 How did the concept of taxation develop historically?

1.1.2.1 The Ancient and Medieval Origins of Taxation

Throughout history, governments have relied on taxation to fund public services, infrastructure, and, in some cases, to sustain the lifestyles of ruling elites. In ancient societies, taxes were primarily tied to agriculture, the backbone of most economies. Before colonial rule, taxation in African societies was largely informal. It took the form of tribute, labor contributions, and agricultural levies, which supported local governance and community welfare. Chiefs and kings-imposed taxes in kind (e.g., livestock, grain, or services) to sustain their courts, military, and infrastructure projects.ⁱⁱⁱ

Key colonial taxes in Kenya included:^{iv}

- **Hut Tax (1901):** A direct tax on African households, pushing men into wage labor.
- **Poll Tax (1910s):** Levied on adult males, ensuring African participation in colonial industries.
- **Land Tax:** Aimed at discouraging indigenous farming in favor of European settlers.

After independence in 1963, Kenya restructured its tax system to fund national development. The government introduced:

- **Progressive income taxes**, ensuring higher earners contributed more.
- **Value Added Tax (VAT)** in 1990, broadening revenue collection.
- **Excise duties** on goods like alcohol and fuel.

Today, Kenya's taxation is governed by the Kenya Revenue Authority (KRA), with frameworks outlined in various Acts such as Income Tax Act, Value Added Tax and Excise Duty Act.

1.1.3 What is the Purpose of Taxation?

Taxation plays a crucial role in shaping the economic, social, and political landscape of a country. Its purposes include:^v

- **Raising revenue for public services:** Governments rely on taxes to finance essential services such as defense, law enforcement, education, healthcare, infrastructure development, pensions, and social welfare programs. These services are critical to maintaining a functioning society, ensuring that citizens have access to basic needs and protection.
- **Economic regulation and stability:** Taxation is an important instrument for economic regulation and stability. By adjusting tax policies, governments can control inflation, stimulate economic growth, and mitigate the effects of economic downturns.
- **Reducing inequality:** Another key function of taxation is reducing income inequality through progressive tax systems. Progressive taxation ensures that high-income earners contribute a larger portion of their income, while lower-income individuals benefit from reduced tax burdens and social programs.
- **Influencing consumer behavior:** Taxation is also used as a policy tool to influence consumer behavior, encouraging responsible choices and discouraging harmful activities. Governments impose higher taxes on goods such as alcohol, tobacco, and sugary beverages to reduce consumption and promote public health.
- **Taxation for political and strategic interests:** Although taxation is generally implemented for the public good, it can sometimes be manipulated for political and strategic interests. Governments may use tax policies to favor certain social groups, protect domestic industries from foreign competition, or even suppress political opposition.
- **Redistribution of wealth:** Lastly, taxation plays a significant role in redistributing wealth to promote economic fairness. This principle

is based on the concept of diminishing marginal utility, which suggests that additional income is less valuable to high earners than to lower-income individuals. By imposing higher taxes on the wealthy, governments can fund social programs such as healthcare, education, and unemployment benefits, ensuring a more equitable distribution of resources. For example, in Kenya, taxation supports the National Hospital Insurance Fund (NHIF), making healthcare more accessible to low-income households.

• **1.1.4 Criticisms of the Purpose of Taxation^{vi}**

The moral dilemma of coercion in taxation: One of the primary criticisms of taxation is that it is inherently coercive. Unlike voluntary transactions, taxes are imposed through legal mandates, with non-compliance leading to penalties, fines, or even imprisonment.

- **Taxation and individual autonomy:** Another critique revolves around taxation's impact on individual freedom. Taxes reduce people's ability to use their earnings as they see fit, limiting their capacity to provide for their families, invest in personal aspirations, or support charitable causes of their choosing.
- **Crowding out of charitable giving:** In high-tax environments, individuals and businesses have fewer disposable resources to contribute to philanthropy, social enterprises, and voluntary initiatives.
- **Government inefficiency and conflicts of interest:** Critics argue that government spending is often wasteful, bureaucratic, and prone to corruption. Unlike private individuals or businesses, governments lack direct accountability for financial efficiency, leading to overspending, mismanagement, and the funding of ineffective programs. Additionally, taxation often serves political interests rather than public necessity. Public funds may be allocated not based on need or efficiency, but rather on political alliances, election strategies, and lobbying pressures.
- **Taxation and economic distortions:** Excessive taxation can discourage work, savings, investment,

and entrepreneurship. When tax rates are too high, individuals may work less, retire earlier, or move their wealth to lower-tax jurisdictions—leading to reduced productivity and economic stagnation.

Milton Friedman explained this inefficiency by categorizing spending into four types:^{vii}

- **Spending your own money on yourself** – You are careful about both cost and quality.
- **Spending your own money on others** – You focus on cost but less on quality (e.g., buying gifts).
- **Spending other people's money on yourself** – You focus on quality but not on cost (e.g., company expense accounts).
- **Spending other people's money on others** – You are careless about both cost and quality (e.g., government spending).

Since government taxation falls into the fourth category, critics argue that public funds are often spent inefficiently, without the incentives for innovation, accountability, or cost-effectiveness that exist in the private sector.

- **Taxation and Social Division:** As taxation increases, different interest groups begin competing for government funding, leading to political conflicts and social divisions. The more revenue that flows through the political process, the more opportunities arise for favoritism, corruption, and power struggles. Additionally, when taxes are used for redistribution, some groups may feel unfairly burdened, while others may become overly dependent on state support.

1.1.4.1 The Question of Whether Taxation is Justified

At its core, taxation raises a profound ethical question: **Is taxation a form of theft?** While the term is contentious, critics argue that taxation is fundamentally different from voluntary exchange, as it involves the forced transfer of wealth under the threat of punishment. Unlike theft, taxation is legally sanctioned and (in democratic societies) determined

by elected representatives. However, critics question whether the consent of a majority is sufficient to justify the forced expropriation of a minority's wealth. As Calvin Coolidge put it, **"Collecting more taxes than is absolutely necessary is legalized robbery."**^{viii}

1.2 Core Principles of Taxation

1.2.1 Worldwide Principles of Taxation

To ensure that taxes acquire acceptance by the people, and foster compliance with taxes imposed, governments in the world seek to base their tax measures on various principles. The Kenyan constitution 2010 has recognized some of these principles such as equity and the need for taxation to be grounded on sound legal framework. In addition to these, other taxation principles that guide the government include:^{ix}

- **Certainty and simplicity**–Tax rules should be clear and simple to understand, so that taxpayers know where they stand. A simple tax system makes it easier for individuals and businesses to understand their obligations, making it more likely for business to make informed decisions and respond to policy choices.
- **Efficiency**– The compliance costs for business and administration costs for government should be as minimal as possible. For instance, the government should not use a higher proportion of its revenue generated to collect taxes enough to meet fiscal targets.
- **Flexibility** – Tax systems should be flexible and responsive enough to ensure that they keep pace with technological and commercial developments.
- **Human Rights Compliance** – Taxation should not lead to violation of human rights. Tax policies should ensure that they adopt a human rights-based approach in the imposition of tax measures

by adhering to the principles of tax law.

- **Transparency** – taxpayers must have information regarding the design and implementation of taxes.
- **Accountability** – the State must manage the tax system responsibly and ensure that affected parties can raise their concerns and seek redress.
- **Participation** – there must be proactive participation of the public before, during and after the designing and implementation of taxation

1.2.2 Constitutional Underpinning of Principles of Taxation in Kenya

The Constitution of Kenya 2010 establishes various essential elements that are crucial towards the imposition of taxes in Kenya.

- **Equity in taxation:** Through article 201(b)(i) the government is bound to ensure that taxation promotes equity by ensuring that **the burden of taxation is shared fairly**. The principle can be understood through two main concepts: horizontal and vertical equity. Horizontal equity implies that taxpayers in similar circumstances should bear a similar tax burden. Vertical equity, on the other hand, suggests that taxpayers with higher incomes should pay a greater proportion of their incomes in taxes.
- **Authority to levy taxes at the national and county Levels:** To avoid any conflicts in the imposition of taxes between the national and county governments, article 209 outlines various taxes which the respective governments may impose. The national government is empowered to levy income tax, value added tax, custom duties and other duties on import and exported goods, and excise taxes. Conversely, county governments are authorized to impose property taxes, entertainment taxes and any other taxes, outlined by an Act of Parliament.
- **Taxation Based on a Legal Framework** – Article 210 of the Constitution emphasizes that all taxes must be grounded in a clear legal framework, ensuring that the power to tax is not imposed arbitrarily or abused. It also provides that waivers and exemptions to those taxes must be based on a sound legal framework.



1.3 Understanding Direct and Indirect Tax

Taxation is broadly classified into direct and indirect taxes, each with distinct implications for taxpayers and economic policy. Direct taxes are imposed directly on individuals or businesses and cannot be transferred to another party. These include income tax, corporate tax, property tax, inheritance tax, and capital gains tax. They are often progressive, meaning higher earners pay a larger share, aligning with the principle of taxation based on the ability to pay. Indirect taxes, on the other hand, are levied on goods and services and are ultimately borne by consumers. These include Value Added Tax (VAT), excise duties on alcohol and tobacco, import tariffs, and sales taxes. Unlike direct taxes, indirect taxes can be shifted from businesses to consumers through price adjustments.

Activity: Exciting Trivia Challenge to Enhance Understanding of Direct and Indirect Taxation. Through the division of groups, the trainees will be divided into groups where they will each participate in answering interesting questions on direct and indirect taxes. It will contain three rounds: round one on general classification of taxes as direct or indirect; Round two which will look into certain life problems and ascertain whether the tax applied shall be direct or indirect and Round Three a Tax Auction Challenge which will help participants understand how tax revenue is allocated, the impact of tax evasion, and the importance of strategic fiscal planning.



1.4 Key Institutions and their Role in Taxation

The taxation system in Kenya is governed by several key institutions, each playing a critical role in the development, administration, enforcement, and oversight of tax policies. These institutions ensure that tax laws are effectively implemented, revenue collection is efficient, and fiscal policies align with Kenya's economic goals. The primary institutions involved in taxation include The National Treasury, Kenya Revenue Authority (KRA), and Parliament.

1.4.1 The National Treasury

The National Treasury is the central government body responsible for formulating fiscal policies, managing public finances, and overseeing tax administration in Kenya. Its role in taxation includes:

- **Tax policy formulation:** It develops and reviews tax policies to align them with Kenya's economic objectives and revenue needs.
- **Budget preparation:** It prepares the Annual Budget Statement, outlining revenue collection strategies, tax amendments, and fiscal priorities.
- **Tax legislation & amendments:** It drafts tax-related laws, such as the Finance Act, which introduces changes to existing tax laws and creates new tax measures.
- **Revenue allocation:** Distributes tax revenue to various levels of government, including county governments under the devolved system.

1.4.2 Kenya Revenue Authority (KRA)

The Kenya Revenue Authority (KRA) is the primary tax collection agency, responsible for ensuring compliance with Kenya's tax laws. Established under the Kenya Revenue Authority Act (1995), KRA operates under the supervision of the National Treasury. KRA's core functions include:

- **Tax collection & enforcement:** KRA administers taxes such as Income Tax, VAT, Excise Duty, and Customs Duties to meet revenue targets.
- **Taxpayer education & support:** It provides

taxpayers with guidance on compliance, filing returns, and understanding tax obligations.

- **Audits & compliance monitoring:** KRA conducts tax audits and investigations to detect tax evasion and ensure compliance.
- **Dispute Resolution:** It handles tax disputes through internal reviews and refers unresolved cases to the Tax Appeals Tribunal (TAT).
- **Customs & Border Control:** KRA manages import and export taxes, ensuring compliance with trade regulations.

1.4.3 Parliament

Parliament plays a legislative and oversight role in taxation, ensuring that tax policies are fair, transparent, and aligned with Kenya's economic goals. Parliament's role in taxation includes:

- **Approval of Tax Laws:** Parliament reviews and passes tax-related bills, including the Finance Act, which sets out tax rates and policies for the fiscal year.
- **Oversight of KRA & National Treasury:** Through committees such as the Public Accounts Committee (PAC) and Finance and Planning Committee, Parliament monitors the efficiency of tax collection and expenditure.
- **Revenue Allocation to Counties:** The Senate and National Assembly determine revenue distribution between the national and county governments.

1.5 Tax Policy Framework and the Medium-Term Revenue Strategy (MTRS) in Kenya

A well-defined tax policy framework is essential for ensuring predictability, stability, and efficiency in revenue collection. In Kenya, taxation policies are guided by the National Tax Policy (NTP) and the Medium-Term Revenue Strategy (MTRS), both of which play a crucial role in shaping tax laws, enhancing compliance, and driving economic growth. NTP provides the overarching principles of taxation, while the MTRS outlines structured revenue mobilization strategies over a specific period.

Together, they contribute to a fair, transparent, and predictable tax system, essential for business confidence and economic planning.

The National Tax Policy (NTP) establishes clear guidelines for tax administration, aiming to mobilize revenue, promote equity, and reduce tax complexity. It ensures that taxation is progressive, stable, and aligned with economic objectives such as wealth distribution, investment incentives, and social welfare. The policy also emphasizes broadening the tax base, minimizing distortions, and addressing challenges of compliance to reduce the tax gap.

Complementing the NTP, the Medium-Term Revenue Strategy (MTRS) 2022/2023 – 2026/2027 provides a structured roadmap for revenue mobilization, enhancing predictability in tax administration. The MTRS focuses on expanding the tax base, improving compliance, and **leveraging technology** to modernize tax collection. Under this strategy, Kenya has implemented digital tax solutions like iTax and eTIMS, expanded VAT coverage, and strengthened measures against tax evasion and illicit financial flows. Additionally, the MTRS aligns Kenya's tax policies with international best practices, such as the OECD's Base Erosion and Profit Shifting (BEPS) framework, ensuring that multinational corporations contribute their fair share of taxes.

By integrating the NTP and MTRS, Kenya ensures that its tax policies are stable, predictable, and responsive to economic changes. Businesses and investors benefit from long-term tax certainty, while the government secures sustainable revenue streams for national development. This structured approach fosters a transparent and equitable taxation system, balancing economic growth with fiscal responsibility.

The Ninth Corporate Plan (2024/25 – 2028/29) serves as Kenya Revenue Authority's (KRA) strategic roadmap for tax planning and revenue

mobilization over the next five years. It aligns tax administration with Kenya's national development goals, including Vision 2030, the Fourth Medium-Term Plan (MTP IV), and the Bottom-Up Economic Transformation Agenda (BETA). The plan focuses on expanding the tax base, enhancing compliance, and leveraging technology for efficient tax collection, ensuring a fair contribution from all sectors.

Key strategic priorities include simplifying tax processes, improving taxpayer education, digitizing tax administration, and strengthening enforcement against evasion. It emphasizes broadening VAT coverage, optimizing income tax collection, and modernizing customs and border management to enhance revenue sustainability. Additionally, the plan incorporates a monitoring and evaluation framework to track progress, ensuring tax policy reforms contribute to national fiscal stability while balancing economic growth and taxpayer burden. By setting annual revenue targets and integrating digital tax systems, the plan shapes Kenya's tax policy by driving reforms that enhance voluntary compliance, reduce administrative inefficiencies, and improve overall tax fairness and efficiency.

1.6 Understanding Tax Laws: Why is Tax Law Different?

Tax law is a distinct and complex area of legal regulation that differs from other branches of law due to its fluid nature, broad applicability, time-sensitive enforcement, multiple governing statutes, and intricate administrative procedures. Unlike criminal or civil law, tax law is highly dynamic, constantly evolving to align with economic policies, government revenue needs, and international tax obligations. Additionally, tax law must balance equity, efficiency, and enforceability, ensuring compliance while minimizing loopholes that could lead to tax evasion or avoidance. Below are the key reasons tax law stands apart from other legal frameworks.

1.6.1 Yearly Change of Law

One of the defining characteristics of tax law is its frequent amendments, often through annual finance laws, budget statements, or tax reforms. Unlike other legal domains that remain largely stable over time, tax legislation is regularly updated to address new economic realities, close loopholes, and enhance revenue collection. Changes may include adjustments to tax rates, new deductions and exemptions, expansion of tax bases, or introduction of entirely new tax regimes.

For instance, in Kenya, the Finance Act is passed every year, bringing revisions to income tax, VAT, excise duties, and corporate taxation. Similarly, global trends such as the OECD's Base Erosion and Profit Shifting (BEPS) initiative have led to international tax law reforms, requiring multinational corporations to comply with new taxation standards. These annual changes increase the complexity of compliance for taxpayers and professionals, necessitating continuous legal and financial education to stay updated.

1.6.2 Uniformity under Tax Law

Unlike other legal frameworks that distinguish between individuals and corporations in terms of rights and obligations, tax law applies uniformly across diverse taxpayers, including individuals, businesses, partnerships, trusts, and multinational corporations. Regardless of economic status or sector, taxpayers are bound by the same fundamental tax obligations—filing returns, reporting income, and paying taxes due.

However, uniformity does not always mean equality in taxation. Tax systems often implement progressive, proportional, or regressive tax structures that differentiate obligations based on income levels or transaction types. Additionally, tax authorities ensure compliance through uniform enforcement mechanisms, such as audits, penalties, and legal proceedings for non-compliance. The principle of uniformity in tax law ensures fairness, predictability, and neutrality, preventing

preferential treatment or discrimination between different taxpayers.

1.6.3 Prescription of Time

Tax law is heavily governed by strict timelines for assessment, filing, and dispute resolution, ensuring legal certainty for both taxpayers and tax authorities. The prescription of time, or statute of limitations in tax matters, defines how long tax authorities can assess or audit a taxpayer's liability and how long taxpayers can challenge tax assessments or claim refunds.

For example, in Kenya, the Tax Procedures Act stipulates a five-year limit for the Kenya Revenue Authority (KRA) to review tax returns and issue additional assessments. Beyond this period, tax authorities generally lose the right to demand unpaid taxes, unless fraud or misrepresentation is involved. Similarly, taxpayers must adhere to strict filing deadlines—such as 30th June for annual individual tax returns—failing which they face penalties and interest on overdue taxes. Strict time limits promote efficiency, prevent indefinite liability, and safeguard taxpayers from retrospective enforcement, ensuring that tax disputes are resolved within a reasonable timeframe.

1.6.4 Multiplicity of Statutes

Tax law is not confined to a single legal document but is instead regulated through multiple statutes, subsidiary regulations, and international treaties. This complexity arises because taxation intersects various economic sectors, revenue streams, and international obligations, necessitating separate legal frameworks.

In Kenya, tax law is governed by several key statutes, including:

- Income Tax Act – Governs personal and corporate income taxation.
- Value Added Tax (VAT) Act – Regulates consumption taxes on goods and services.
- Excise Duty Act – Imposes taxes on specific goods such as alcohol, tobacco, and fuel.

- Tax Procedures Act – Establishes the framework for tax administration, compliance, and enforcement.
- East African Community Customs Management Act – Regulates cross-border taxation within the EAC region.

Additionally, Kenya is a signatory to international tax treaties and agreements, such as Double Taxation Agreements (DTAs) and OECD BEPS measures, which further influence its tax landscape. The multiplicity of statutes means taxpayers must navigate different regulatory frameworks based on the nature of their income, transactions, and international operations.

1.6.5 Administrative Procedures

Unlike other areas of law that rely solely on judicial processes for enforcement, tax law is heavily administrative, meaning tax authorities play a central role in assessment, collection, compliance enforcement, and dispute resolution. These procedures are designed to ensure efficient tax collection while reducing the need for lengthy court proceedings.

Key administrative procedures include:

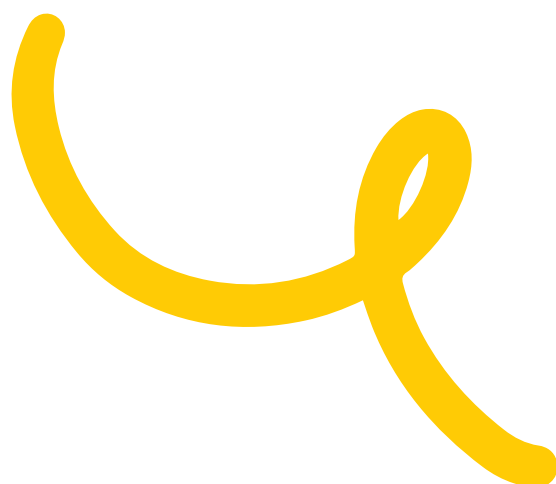
- Self-Assessment and Tax Filing – Taxpayers are required to calculate and declare their tax liability, ensuring voluntary compliance.
- Audits and Investigations – Tax authorities conduct random or targeted audits to verify taxpayer accuracy and detect non-compliance.
- Penalties and Interest – Late payments, under-declaration, or misreporting of taxes attract fines, interest, and legal enforcement actions.
- Dispute Resolution Mechanisms – Taxpayers can challenge tax assessments through administrative appeals, tribunals, or courts.

In Kenya, the Tax Appeals Tribunal (TAT) serves as the primary forum for resolving disputes between taxpayers and the Kenya Revenue Authority (KRA) before cases escalate to higher courts. Furthermore, alternative dispute resolution (ADR) mechanisms, such as negotiations and settlements, are encouraged to reduce litigation and expedite tax resolution.

The administrative nature of tax law not only ensures that compliance is managed efficiently and systematically, but it also places a significant burden on taxpayers to understand, file, and pay taxes accurately.

Key Takeaway:

- Taxation remains a central pillar of governance, yet its moral implications warrant ongoing scrutiny.
- While taxation may be necessary for maintaining order, security, and essential services, governments must be cautious not to overstep ethical boundaries.
- Coercion, inefficiency, political favoritism, and economic distortions must be minimized through fair and transparent tax policies.
- Ultimately, the challenge lies in striking a balance- ensuring that taxation serves the public good without undermining personal freedom, economic incentives, or social harmony.
- Governments must acknowledge that taxation is not merely an economic tool, but a moral issue that requires careful, principled, and responsible application.



2. Direct Taxes: Taxation of Income in Kenya



Objectives of the session

- Understand the concept of income taxation and the governing legal framework in Kenya
- Understand the different forms of income taxation in Kenya

- Relate the concept of income taxation to the broader concept of taxation and principles of taxation

Resources needed

- The National Tax Policy
- The Medium-Term Revenue Strategy (MTRS)
- Income Tax Act Cap 470, 1974

How to run the session

- Prepare a PowerPoint presentation on the overview of income taxation in Kenya, governing legal framework, different forms of income taxation.
- Deliver the presentation to the trainees in 45 minutes while linking income taxation to principles of taxation.
- Instruct the trainees to log in to the Kenya Law Reforms Commission website and access the Income Tax Act, 1974.
- Engage the trainees in a 20-minute group discussion during which they will discuss distribution of the tax burden and identify different forms of taxation of income guided by case studies.
- Give each group 5 minutes to present their findings in plenary
- Conclude the session by recapping the key takeaways, emphasizing the importance of understanding income taxation and how it relates to principles of taxation.

Definition of key terms

a. Income

Income refers to the monetary gain or financial benefit received by an individual, business, or entity over a specified period, usually as a result of work, investments, or business activities.

b. Person

"Person" includes a company, association or other body of persons whether incorporated or unincorporated.



c. Resident

Companies incorporated in Kenya are treated as Kenyan tax residents. Additionally, companies incorporated overseas are also treated as Kenya resident if their 'management and control is exercised in Kenya in a particular year of income under consideration'. A company may also be declared a tax resident in Kenya pursuant to a declaration in a legal notice by the Cabinet Secretary for the National Treasury.

d. Non-resident

A non-resident is an individual or entity that does not meet the residency criteria for tax purposes as defined under the Income Tax Act (Cap 470)^{xi} of Kenya. Legal Definition Under the Income Tax Act (Cap 470), Section 2.

A non-resident is:

- An individual who is present in Kenya for less than 183 days in a tax year (January to December).
- A company incorporated outside Kenya and managed from another country.
- A trust or partnership that is not domiciled in Kenya.

e. Permanent establishment (PE)

A fixed place of business through which business is wholly or partly carried on and includes a place of management, a branch, an office, a factory, a workshop, a mine, an oil or gas well, a quarry or any other place of extraction or exploitation of natural resources, a warehouse in relation to

a person whose business is providing storage facilities to others, a farm, plantation or other place where agricultural, forestry plantation or related activities are carried on and a sales outlet;

A business carried on in Kenya through a fixed place of business gives rise to a PE, as does a building site, or a construction or assembly project, that has existed for six months or more. The definition of PE is extended to include a dependent agent that habitually concludes contracts on behalf of others. The Finance Act, 2023^{xii} expanded the definition of PE to include a service PE concept. The new definition also excludes certain activities that are preparatory and auxiliary in nature from creating a PE. In addition, the new definition of the fixed place of business PE lacks a threshold as to how long a business must be operating in Kenya to create a PE.

f. Tax relief

Tax relief refers to a reduction in the amount of tax payable by an individual or business, granted by the government to support taxpayers and encourage specific economic activities. It lowers the overall tax burden by deducting a specified amount from taxable income or directly from tax liability.

Under Section 30 of the Income Tax Act (Cap 470) of Kenya, tax reliefs are deductions granted to eligible taxpayers to reduce their final income tax liability.

Group Activity 1: Are Kenyans Overtaxed? (15 mins)

Instructions:

Form 2-3 groups

Debate the question: "Do you think Kenyans are overtaxed?"

Each group presents their argument (2 mins each)

Group Activity 2: Case study

Divide the participants into 3-4 groups in breakout rooms.

Give each group a short case study- It could be of someone like a salaried worker, a landlord, a small business, etc.

Let them discuss the case study for about 15 mins

- What type of tax applies to this person or business?
- (Is it PAYE, Rental Income Tax, Turnover Tax, or Digital Services Tax?)
- How much tax should they pay? Do a simple calculation using the information

Each group will explain their case and answer in 5 minutes.

2.1 The Income Tax Act

2.1.1 What is Income and why do we tax income?

Income refers to the financial gain received by individuals or entities, typically in the form of wages, salaries, profits, interest, rent, and dividends. Some reasons for taxing income include:

Revenue Generation: The primary reason is to generate revenue for the government, which is then used to fund public goods and services such as education, healthcare, infrastructure, and defense.

Redistribution of Wealth: Income taxes can help reduce economic inequality by redistributing wealth. Those with higher incomes typically pay a higher percentage in taxes, which can then be used to support social programs.

Economic Stability: Taxes can help manage economic cycles by adjusting the amount of money circulating in the economy. During inflation, higher

taxes can reduce spending; during recessions, lower taxes can stimulate spending.

Encouraging certain behavior: Certain tax policies can encourage or discourage specific behaviors. For example, insurance and mortgage relief

2.1.2 Types of income subject to income tax in Kenya:

Income tax is a tax charged for each year of income, upon all the income of a person whether resident or non-resident, which is accrued in or was derived from Kenya. Income Tax is imposed on: (Section 3)

- Business income from any trade or profession
- Employment income
- Rent income
- Dividend and Interests
- Pension income
- Income from a Digital Marketplace
- Natural resource income among others

Figure 1: A snippet of the Income Tax Act (Section 3)**3. Charge of tax**

(1) Subject to, and in accordance with, this Act, a tax to be known as income tax shall be charged for each year of income upon all the income of a person, whether resident or non-resident, which accrued in or was derived from Kenya

(2) Subject to this Act, income upon which tax is chargeable under this Act is income in respect of-

(a) gains or profits from-

(i) any business, for whatever period of time carried on;

(ii) any employment or services rendered;

(iii) any right granted to any other person for use or occupation of property;

(b) dividends or interest;**(c) (I) a pension, charge or annuity; and**

(ii) any withdrawals from, or payments out of, a registered pension fund or a registered provident fund or a registered individual retirement fund; and

(iii) any withdrawals from a registered home ownership savings plan;

(ca) income accruing from a business carried out over the internet or an electronic network including through a digital marketplace

(d) deleted by Act No. 14 of 1982, s. 17;

(e) An amount deemed to be the income of any person under this Act or by rules made under this Act;

(f) gains accruing in the circumstances prescribed in, and computed in accordance with, the Eighth Schedule;

(g) subject to section 15(5A), the net gain derived on the disposal of an interest in a person, if the interest derives twenty per cent or more of its value, directly or indirectly, from immovable property in Kenya;

(h) a natural resource income; and

(i) gains from financial derivatives, excluding financial derivatives traded at the Nairobi Securities Exchange.

A company is considered resident in Kenya if it is incorporated under Kenyan Law or if the management and control of its affairs are exercised in Kenya for any given year of income. It is also considered resident if the Cabinet Secretary, National Treasury & Planning declares the company to be tax resident, for a particular year of income in a notice published in the Kenya Gazette. Resident companies are taxable in Kenya on income accrued or derived from Kenya. Where a business

is carried on or exercised partly within and partly outside Kenya by a resident person, the whole of the gains or profits from such business shall be deemed to have accrued in or to have been derived from Kenya; therefore, taxable in Kenya. Non-resident companies are subject to Kenya corporate income tax (CIT) only on the trading profits attributable to a Kenyan PE. There are special rates for certain resident and non-resident companies as set out in table 2.

Table 1: Preferential CIT rates

Entity	CIT rate (%)
Export processing zone (EPZ) enterprises:	
First ten years	0
Next ten years	25
Thereafter	30
Registered unit trusts/Collective investment schemes	Exempt (subject to conditions)
Companies listed on securities exchange	25 (first five years)
Special economic zone (SEZ) enterprises, developers, and operators	10 (first ten years); 15 (succeeding ten years)
Local motor vehicle assembly companies	15 (first five years); 15 (succeeding five years, subject to conditions)
Company operating a carbon market exchange or emission trading system that is certified by the Nairobi International Financial Centre Authority	15 (first ten years from the year of commencement of its operations)
Company operating shipping businesses	15 (first ten years from the year of commencement of its operations)
Rates on gross income of non-residents derived from Kenya:	
Transmission of messages	5
Ownership or operation of ships and aircraft	2.5
Demurrage charges	2.5

2.1.3 Allowable Deductions

Under Section 15 of the Income Tax Act (Cap 470) of Kenya, corporations are permitted to deduct specific expenses from their gross income to determine their taxable income. These allowable deductions include:

- Expenditure Wholly and Exclusively Incurred in Production of Income: Expenses directly related to the generation of taxable income.
- Capital Allowances: Depreciation of qualifying assets, such as industrial buildings, machinery, and equipment, as specified in the Second Schedule of the Act.
- Bad Debts: Debts that have become uncollectible, provided they were previously included as taxable income and all reasonable steps to recover them have been taken.
- Donations: Contributions to charitable organizations, subject to conditions outlined in the Act.
- Interest Expenses: Interest on borrowed funds used in the production of income, within prescribed limits.
- Rent and Rates: Payments for property used in the business operations.
- Repairs and Maintenance: Costs incurred for the repair and maintenance of property, machinery, or plant used in the business.
- Research and Development: Expenditure on scientific research related to business.
- Legal and Professional Fees: Fees for services directly related to the business operations.
- Employee Remuneration: Salaries, wages, and benefits paid to employees.

Figure 2: A snippet of Safaricom's financial report

2(A) INCOME TAX EXPENSE	GROUP		COMPANY	
	2023 KShs'm	2022 KShs' m	2023 KShs'm	2022 KShs'm
Current income tax	(41,113.5)	(39,146.8)	(39,422.7)	(38,706.8)
Adjustments in respect of current income tax of previous year	(177.1)	(12.1)	(177.1)	(12.1)
Deferred income tax (Note 17)	5,194.6	4,472.0	5,195.6	4,473.4
Adjustments in respect of deferred income tax of previous year	233.6	(30.4)	233.6	(30.5)
Income tax expense	(35,862.4)	(34,717.3)	(34,170.6)	(34,276.0)
Profit before income tax	87,500.9	102,213.4	109,110.2	106,065.3
Tax calculated at the applicable income tax rate of 30%	(26,250.3)	(30,664.0)	(32,733.1)	(31,819.6)
Tax effect of:				
- Income not subject to tax	2,174.2	283.2	3,424.6	1,635.0
- Expenses not deductible for tax purposes	(4,984.1)	(4,112.6)	(4,918.6)	(4,048.8)
Adjustments in respect of deferred income tax of previous year	233.6	(30.4)	233.6	(30.5)
Adjustments in respect of current income tax of previous year	(177.1)	(12.1)	(177.1)	(12.1)
Deferred tax not recognised in the year	(6,858.7)	(181.4)	-	-
Income tax expense				
Income tax expense	(35,862.4)	(34,717.3)	(34,170.6)	(34,276.0)

2.1.3.1 Deductions not allowed

Under Section 16 of the Income Tax Act (Cap 470) of Kenya, certain expenses are disallowed as deductions when calculating taxable income for corporations. These include:

- **Non-Production Expenditure:** Expenses not wholly and exclusively incurred in the production of taxable income.
- **Capital Expenditure:** Costs related to the acquisition, improvement, or restoration of capital assets.
- **Personal Expenses:** Expenditures of a private or domestic nature.
- **Income Tax Payments:** Taxes on income or profits paid or payable under the Act.
- **Unapproved Pension Contributions:** Contributions to pension, provident, savings, or similar funds not approved by the Commissioner.
- **Fines and Penalties:** Payments for legal infractions, including fines and penalties.
- **Entertainment Expenses:** Unless incurred wholly and exclusively in the production of income.
- **Donations:** Except those made to approved charitable organizations or causes.
- **Club Membership Fees:** Subscriptions to

clubs, unless related to the business's income production.

- **Depreciation:** Accounting depreciation is disallowed; instead, capital allowances as specified in the Act are deductible.
- **Reserve Funds:** Allocations to reserves or provisions, except as allowed by the Act.
- **Dividends:** Distributed profits to shareholders are not deductible.
- **General Provisions for Bad Debts:** Only specific bad debts that have become uncollectible are deductible.
- **Excessive Interest Payments:** Interest paid on loans exceeding the prescribed limits, especially in cases of thin capitalization.
- **Expenses Recoverable Under Insurance or Contract:** Costs for which reimbursement is receivable.

2.1.4 Instalment Tax

Installment Tax is a form of advance tax payment made by taxpayers whose income is not subjected to Pay As You Earn (PAYE) or withholding tax. It is required under Section 12 of the Income Tax Act (Cap 470) and applies to businesses, self-employed individuals, and corporations to ensure tax

compliance before the end of the financial year.
Installment tax is applicable to:

- Businesses and companies that expect to pay income tax of KSh 40,000 or more per year.
- Self-employed individuals whose income is not subject to PAYE.
- Professionals, consultants, and landlords earning taxable income.

2.1.4.1 How is Instalment Tax Calculated?

The tax is computed using either of the following methods:

Prior-Year Basis:

Taxpayers estimate 110% of the previous year's tax liability and pay it in equal installments.

Current-Year Basis:

Taxpayers estimate their current year's taxable income, apply the tax rate, and pay in equal installments.

2.1.4.2 Instalment Tax Payment Schedule

The Kenya Revenue Authority (KRA) requires installment tax to be paid in four equal installments during the year, based on the financial year-end:

Table 2: Installment tax due dates and percentages

Due Date	Percentage of Total Tax Due
20th April	25%
20th June	25%
20th September	25%
20th December	25%

Table 3: Individual Tax Bands and Rates, with effect from 1st July, 2023

Tax Bands	Annual	Monthly	Rates
On the first	Shs. 288,000	Shs. 24,000	10%
On the next	Shs. 100,000	Shs. 8,333	25%
On the next	Shs. 5,612,000	Shs. 467,667	30%
On the next	Shs. 3,600,000	Shs. 300,000	32.5%
On all income in excess of	Shs. 9,600,000	Shs. 800,000	35%

For businesses with accounting years different from the calendar year, payments are made on the 4th, 6th, 9th, and 12th month of their financial year.

2.1.4.3 Exemptions from Installment Tax

- Individuals whose employment income is fully taxed under PAYE.
- Businesses with a tax liability below Ksh 40,000 per year.
- Persons taxed under Turnover Tax (TOT) instead of corporate tax.

2.1.5 Pay As You Earn (PAYE)^{xiii}

PAYE is a method of collecting tax at source from individuals in gainful employment. Gains or Profits includes wages, casual wages, salary, leave pay, sick pay, payment in lieu of leave, fees, commission, bonus, gratuity, or subsistence, travelling, entertainment or other allowance received in respect of employment or services rendered. Companies and Partnerships with employees are required to deduct tax according to the prevailing tax rates from their employees' salaries or wages on each payday for a month and remit the same to KRA on or before the 9th of the following month.

Individual Income Tax is charged for each year of income on all the income of a person, whether resident or non-resident, which accrued in or was derived from Kenya. Individual Tax Bands and Rates, with effect from 1st July, 2023.

2.1.5.1 Tax Relief under PIT

Tax relief is an incentive that reduces the amount of tax that a person has to pay. Every resident individual is entitled to a personal relief of Ksh. 28,800 per year (Ksh. 2,400 per month) effective from 25 April 2020. In addition, resident individuals are entitled to an insurance relief equal to 15 percent of the premiums paid for themselves, their spouse, or their child, subject to a maximum of Ksh. 60,000 per year. This insurance relief applies to life insurance policies, education policies with a maturity period of at least ten years, and health insurance policies.

2.1.5.2 Employment Income not subject to PAYE

- Meals provided by the employer up to a maximum of Ksh 5000 per month or Ksh. 60,000 per year.
- Night-out of Ksh.2,000 per day
- Medical Cover by employer
- In the case of non-Kenyan citizens who are in Kenya solely to serve the employer, expenditure on passages between Kenya and any place outside Kenya borne by the employer.
- Pension contribution made by an employer, who is a person chargeable to tax, to a registered or unregistered scheme that is within the allowable limit of Ksh. 30,000 per month or Ksh 360,000 per year.
- Gratuity or similar payment paid by an employer in respect of employment or services rendered which is paid under a public pension scheme not exceeding Ksh. 360,000 for each year of service.

2.1.5.3 Allowable deductions

These are the amounts deducted from an employee's emoluments in order to arrive at the amount which will be subjected to tax. Amounts deductible in determining the taxable employment income shall include:

- Amount deducted as Affordable Housing Levy pursuant to the Affordable Housing Act, 2024.^{xiv}
- Contribution to a post-retirement medical fund subject to a limit of Ksh. 15,000 per month.
- Contributions made to the Social Health Insurance Fund (SHIF).
- Mortgage interest, not exceeding Ksh. 360,000 per year (Ksh. 30,000 per month), upon money borrowed by a person from one of the first six financial institutions specified in the Fourth Schedule to the Income Tax Act, to purchase or improve premises occupied by the person for residential purposes.
- Contribution made to a registered pension or provident fund or a registered individual retirement fund up to a limit of Ksh. 360,000 per year (Ksh. 30,000 per month).

2.1.5.4 Exemption from PIT

The Persons with Disabilities Act 2003^{xv} and the Persons with Disabilities (Income Tax Deductions and Exemptions) Order 2010 provide for income tax exemption for persons with disabilities, allowing those who meet set criteria—such as having a disability assessment report from a gazetted hospital, registration with the NCPWD, receipt of taxable income, and successful vetting by a designated committee—to apply to the Cabinet Secretary for Finance for exemption on the first Ksh.150,000 per month or Ksh.1.8 million annually. In addition, diplomats and consular staff from foreign countries are exempt from paying income tax on their official earnings in Kenya, while employees of certain international organizations may also enjoy tax exemption based on agreements between the Kenyan government and the respective organizations.

Table 4: PAYE calculation for someone earning Ksh 50,000

Description	Amount (Ksh)
Gross Pay	50,000
NSSF Contribution	- 2160
SHIF	-1375
Housing Levy	750
Taxable income	45,715
PAYE (less personal relief of Ksh 2400)	6097.85
Total deductions	10382.85
Net Pay	39617.15

2.1.6 Withholding Tax (WHT)

This is a method of tax collection whereby a payer of certain incomes deducts tax upon payments of certain incomes to payees and then remits the tax deducted to the Commissioner of Domestic Taxes Department within 5 working days after the deduction is made. The percentage deducted varies between incomes and is dependent on whether you are a **resident or non- resident**. WHT is deducted at source from the following sources of income: Interest, dividends, royalties, management or professional fees (including consultancy, agency or contractual fees), commissions, pensions, rent received by non-residents, and other specified payments.



Table 5: Withholding Tax Rates

Type of incomes	Resident	Non Resident
Artists and entertainers	-	20%
Management fees	5%	20%
Professional fees	5%	20%
Training fees (inclusive of incidental costs)	5%	20%
Winnings from betting, gaming, prize competition, gambling)	20%	20%
Royalties or natural resource income	5%	20%
Dividends (nil for resident companies with shareholding >12.5%), (5% resident qualifying dividend and citizens of EAC)	10%	15%
Equipment (movable) Leasing	N/A	5%
Interest (Bank)	15%	15%
Interest (Housing Bond HBI)	10%	15%
Interest on at least two year government bearer bonds, (issued outside KE- 7.5%)	15%	15%
Other bearer bonds interest	25%	25%
Bearer bonds with maturity of ten years or more	10%	
Rent – buildings (immovable)	10%	30%
Rent – others (except aircraft)	N/A	15%
Pensions/provident schemes (withdrawal)	10 – 30%	5%
Insurance Commissions – brokers	5%	20%
Insurance Commissions – Others	10%	
Consultancy and agency (from 1 July (consultancy fees to EAC citizen – 15%)	5%	20%
Contractual (from 1 July 2003)	3%	20%
Telecommunication services/Message transmission	-	5%
Natural Resource Income (w.e.f 1 st January 2015)	5%	20%
Digital content monetization (w.e.f 1 st July 2023)	5%	20%
Sales promotion, marketing and advertising services	5%	20%
Withholding on rental income tax by tax agents (w.e.f 1 st January 2024)	7.5%	N/A
Gains from financial derivatives	N/A	15%

Going forward, owners/operators of digital marketplaces or platforms (both resident and non-resident) will need to **withhold on payments for digital content monetization, property or services made/facilitated through their platform**. "Platform" has been defined as a digital platform or website that facilitates the exchange of short-term engagement, freelance or provision of a service, between a service providers who is an independent contractor or freelancer, and a client or customer. **The WHT rate shall be 5% for residents and 20% for non-residents. This affects the likes of Uber, Netflix etc.**

2.1.6.1 Withholding Tax Exemptions

- Dividends received by a company resident in Kenya from a local subsidiary or associated company in which it controls (directly or indirectly) 12.5% or more of the voting power.
- Royalties, interest, management fees, professional fees, training fees, consultancy fees, agency or contractual fees paid by a Special Economic Zone developer, operator or enterprise in the first ten (10) years of its establishment, to a non-resident person with

effect from 1st July, 2023.

- Marketing commissions and residue audit fees paid to non-resident agents in respect of export of flowers, fruits and vegetables.
- Interest payments to financial institutions stated in the fourth schedule of the Income Tax Act.
- Payments made to tax-exempt bodies.
- Resident management, professional, training and contractual fees whose aggregate value is Ksh 24,000 and below in a month.
- Air travel commissions paid by local air operators to non-resident agents.

2.1.6.2 Is withholding tax a final tax?

There are a few instances where withholding tax is the final tax. Withholding tax is final when deducted in relation to a payment made to a non-resident person with no permanent establishment in Kenya. Regarding payments to resident persons, withholding tax is a final tax when it relates to winnings, qualifying interest, qualifying dividend and pension. In every other case, withholding tax is NOT a final tax. The taxpayer is required to declare their income(s) and withholding tax details when filing their annual tax returns and to pay any balance of tax due.

2.1.7 Advance Tax

This is a tax paid in advance before a public service vehicle, or a commercial vehicle goes for the annual inspection. This is a tax paid in advance before

a public service vehicle or commercial vehicle is licensed at the applicable rates. Advance tax is not a final tax. Individuals who have paid any advance tax are required to declare the same in their individual income tax returns submitted yearly and pay any additional tax due.

2.1.7.1 What are the tax rates for advance tax?

- For vans, pick-ups, trucks, prime movers, trailers and lorries; Ksh. 1,500 per ton of load capacity subject to a minimum of Ksh. 2,400 per year of income;
- For saloons, station-wagons, mini-buses, buses and coaches; Ksh. 60 per passenger capacity per month subject to a minimum of Ksh. 2,400 per year of income.

2.1.7.2 Is advance tax a final tax?

Advance tax is not a final tax. Taxpayers who have paid any advance tax are required to declare the same in their income tax returns submitted yearly and pay any additional tax due.

2.1.7.3 When is it due?

It is due on 20th of January or before transfer of ownership of vehicle.

2.1.8 Rental Income Tax

Rent means payments received from a right granted to another person for use or occupation of immovable property which includes premium or similar consideration received for the use or occupation of property.

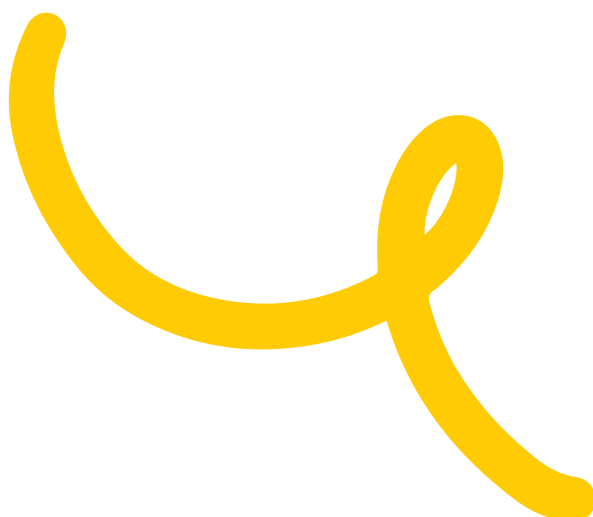


Figure 3: A snippet of the Income Tax Act (Section 3)**6A. Imposition of residential rental Income Tax**

(1) Notwithstanding any other provision of this Act, a tax to be known as residential rental income tax shall be payable with effect from 1st January, 2016 by any resident person from income which is accrued in or derived from Kenya for the use or occupation of residential property, and which is in excess of two hundred and eighty-eight thousand shillings but does not exceed fifteen million shillings during any year of income.

Provided that this section shall not apply where a person who would otherwise pay tax under this section, by notice in writing addressed to the Commissioner, elects not to be subject to residential rental income tax, in which case the other provisions of this Act shall apply to such a person.

(2) The Cabinet Secretary may, by notice in the Gazette, prescribe regulations for the better carrying out of the provisions of this section.

A simplified tax regime on residential rental income known as Residential Rental Income Tax (popularly known as Monthly Rental Income or MRI) was introduced through the Finance Act 2015^{xvi} and came into effect on 1st Jan 2016. MRI is payable by a resident person (individual or company) on rental income accrued or derived in Kenya for the use or occupation of residential property. The rate of tax is 7.5%, effective 1st January 2024, on the gross rent received and is a final tax. No expenses, losses or capital deductions are allowed for deduction from the gross rent.

Following the enactment of the Finance Act 2020,^{xvii} MRI is applicable to persons earning rental income which is in excess of two hundred and eighty thousand shillings but does not exceed fifteen million shillings during any year of income with effect from 1st January 2021. Property owners with rental income above Ksh. 15 million per year are required to declare the rental income together with incomes from other sources (if any) while filing their annual income tax returns.

Exemptions from MRI include:

- Rental income from commercial property
- Non-resident landlords
- Landlords who earn rental income in excess of 15,000,000 per year.

The Finance 2023 Act^{xviii} has introduced a provision for appointment of rental income tax agents for

the purposes of collection and remittance of rental income tax to the Commissioner (effective 1st July 2023.) The tax shall be charged at 7.5% effective 1st January 2024 and remitted by the fifth working day after the deduction was made. Further, the Commissioner may revoke this appointment at any time.

2.1.9 Turnover tax (ToT)

Turnover Tax is a tax charged on businesses whose gross turnover is more than Ksh. 1,000,000 but does not exceed or is not expected to exceed Ksh. 25,000,000 during any year of Income. TOT is chargeable under Section 12 (C) of the Income Tax Act (CAP 470). It is a simplified regime for small businesses, because it is difficult for them to comply with the standard CIT regime. It is payable at the rate of 3% on gross sales effective 19th March 2024.

Turn over Tax is charged on the gross sales and is a final tax. A Turnover Tax registered taxpayer dealing in vatable supplies and has a turnover of Ksh. 5,000,000 and above is required to register for VAT as well.

A person eligible for Turnover Tax (ToT) can choose to opt out by notifying the Commissioner in writing (Section 12C (2)). If they opt out, they will be taxed under the normal income tax regime. This option benefits businesses with low profit margins or high-deductible expenses. The following incomes are exempt from ToT

- Rental income
- Management or professional or training fees; and
- Any income which is subject to a final withholding tax under the Income Tax Act such as qualifying dividends or qualifying interests

Note: No expenses are allowed for deduction.

2.1.10 Significant Economic Presence (formerly Digital Service Tax)

The Tax Laws (Amendment) Act, (TLAA) 2024.^{xix}

repealed the Digital Services Tax (DST) which was applicable at the rate of 1.5% and replaced it with Significant Economic Presence ("SEP") tax whose effective rate is 3%. Further, whilst the Act exempts non-residents with an annual turnover of less than 5million Kenya shillings (KES) from SEP tax, it does not anticipate significant economic presence to arise from either the number of users in Kenya or the level of sales in Kenya and as such the SEP tax appears to be very similar to the DST. Below is an overview of the key differences between DST and the now applicable SEP:

Table 6: Difference between DST and SEPT

Item	Digital Service Tax (DST)	Significant Economic Presence Tax (SEP)
Tax rate	1.5% on gross turnover, without taking into account expenses or profits.	10% of the gross turnover is considered taxable profit for SEP purposes. The tax rate is 30% of the taxable profit. Effectively the tax rate is 3% of gross turnover.
Due date	DST was payable monthly, on or before the 20th day of the month following the month in which the service was offered.	Similarly, SEP is payable monthly, on or before the 20th day of the month following the month in which the service was offered.
Revenue Threshold	No threshold.	SEP does not apply where the annual turnover is less than 5 million shillings.

2.1.10.1 Significant Economic Presence Tax Exemptions

SEP tax shall not apply to the following:

- non-resident persons who offer digital services through a permanent establishment in Kenya
- non-resident persons who carry on the business of transmitting messages by cables, radio, optical fiber, television, broadcasting, internet, satellite, or other similar methods of communication
- income subject to withholding tax
- non-resident persons providing digital services to an airline in which the Government of Kenya has at least forty-five per cent (45%) shareholding
- non-resident persons with an annual turnover of less than Kenya shillings five (5) million

2.1.10.2 Significant Economic Presence Tax Implications

- The tax burden for non-residents under the SEP tax will be significantly higher at the rate of 3% gross revenue as opposed to the DST which was applicable at the rate of 1.5% of the gross revenue.
- The DST regime did not have exemptions which have now been introduced under the SEP regime. For instance, the five million threshold cushions entities that do not carry out significant activities in the country.
- Other developments in the digital space

Note: We expect the KRA to issue comprehensive guidelines on the implementation of SEP.

2.1.11 Minimum Top-up Tax

The Tax Laws (Amendment) Act, (TLAA) 2024, introduced a domestic minimum top-up tax, allowing Kenya to impose an additional amount of tax on the profits of entities that are part of an in-scope multinational group. This ensures the effective tax rate on those profits is 15%. The proposed domestic minimum top up tax is derived from the Organisation for Economic Co-operation and Development's (OECD) Pillar Two framework, which seeks to ensure an effective tax rate of at least 15% in every jurisdiction where an in-scope multinational group operates.

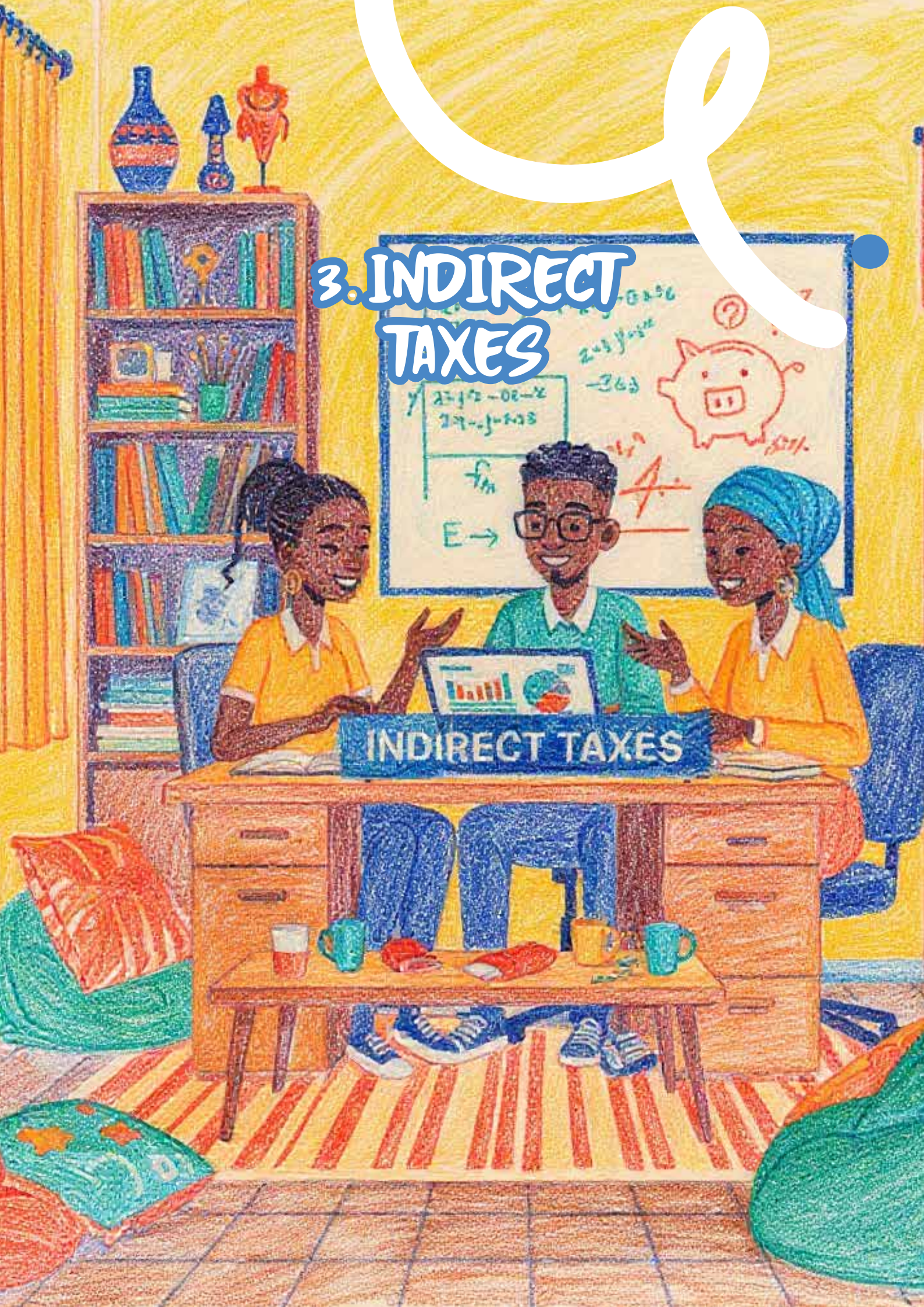
For the purposes of the Kenya Income Tax Act, an in-scope multinational is defined as a member of a multinational group with a consolidated annual turnover of at least EUR 750 million in the consolidated financial statements of the ultimate parent entity in at least two of the four years immediately preceding the tested year of income.

¹The tax is applicable on deemed taxable profit which is deemed to be 10% of the gross turnover.

Key takeaways

- Legal Framework & Taxable Income – **Income tax is governed by the Income Tax Act (Cap 470) and applies to** business income, employment income, rental income, investment income, and digital marketplace earnings.
- Resident vs. Non-Resident Taxation – Resident companies **are taxed at 30% on income accrued in Kenya, while** non-resident companies **are taxed at 30% on income derived from a Permanent Establishment (PE) in Kenya.**
- Tax relief and exemptions – **Personal relief of Ksh 2400/month for everyone;** PWDs (up to KSh 1.8M), diplomatic staff, and certain international organizations **enjoy tax exemptions. Preferential rates for EPZs, SEZs**
- Tax Collection Methods – **Includes** Corporate Income Tax (CIT), PAYE (employment tax), Installment Tax (advance business tax), Withholding Tax (WHT) on professional fees & dividends, and Turnover Tax (ToT) for small businesses.
- Recent Tax Reforms – SEP Tax (3%) replaces DST, **introduction of the** Affordable Housing Levy, **and** Minimum Top-Up Tax (15%) for multinationals.

3. INDIRECT TAXES



Session Objectives

- Understand the fundamental principles of VAT.
- Identify the three VAT rates in Kenya.
- Understand the VAT treatment of imports, exports, and services, including the reverse charge mechanism for foreign services and the impact on businesses involved in international trade.

Resources Needed

- The Constitution of Kenya 2010
- The Tax Laws in Kenya: The Value Added Tax Act

How to Run the session

1. Prepare a PowerPoint presentation on the overview of VAT in Kenya, covering the types of VAT, registration process, filing requirements, and key regulations.
2. Deliver the presentation to the trainees in 30 minutes.
3. Instruct the trainees to log in to the Kenya Revenue Authority (KRA) website and access the VAT Act, 2013 for reference.
4. Illustrate how VAT is applied in various scenarios, including standard rate VAT, zero-rated VAT, and VAT exemptions, providing examples of each type.
5. Engage the trainees in a 20-minute group discussion during which they will identify the practical applications of different VAT types and the importance of VAT compliance in business operations.
6. Give each group 5 minutes to present their findings in plenary, ensuring all trainees contribute their ideas on how VAT applies to their industries.
7. Conclude the session by recapping the key takeaways, emphasizing the importance of understanding VAT registration, filing, and the role of eTIMS for tax compliance.

Definition of Key Terms

- **Value Added Tax (VAT):** A consumption tax levied on goods and services at each stage of the supply chain, administered by the Kenya Revenue

Authority (KRA) under the VAT Act, 2013.

- **Kenya Revenue Authority (KRA):** The government agency responsible for tax collection and enforcement of tax laws in Kenya, including VAT compliance.
- **Electronic Tax Invoice Management System (eTIMS):** time reporting of transactions. eTIMS is mandatory for VAT-registered businesses to generate valid tax invoices.
- **Taxable Supplies:** Goods and services subject to VAT at either 16% (Standard rated) or 0% (Zero-Rated).
- **Zero-Rated Supplies:** Supplies taxed at 0%, allowing businesses to claim input VAT. Examples: exports and some agricultural products.
- **Exempt Supplies:** Supplies that are not subject to VAT, meaning businesses cannot claim input VAT. Examples: financial and educational services.
- **Input VAT:** The VAT paid on business purchases, which can be deducted from output VAT if the purchases relate to taxable supplies.
- **Output VAT:** The VAT charged on sales of taxable goods and services.
- **Net VAT Payable:** The difference between output VAT and input VAT, which must be remitted to KRA.
- Formula: **Net VAT** = Output VAT - Input VAT
- **Time of Supply:** The point at which VAT is due, determined by the earliest of:
 - When goods/services are delivered
 - When an invoice is issued
 - When payment is received
- **Value of Supply:** The price on which VAT is charged, including related costs like transport and commissions.
- **Input Tax Apportionment:** The method used to calculate the portion of input VAT that can be claimed when a business deals in both taxable and exempt supplies.
- Formula: $(\text{Taxable Turnover} / \text{Total Turnover}) \times 100 = \text{Deductible VAT Percentage}$
- **VAT Compliance via eTIMS:** Businesses must use eTIMS to issue valid electronic tax invoices, ensuring real-time transaction reporting to KRA. Non-compliance can result in penalties.

3.1 The Value Added Tax Act, 2013— General Principles of VAT

VAT is a tax levied on the supply of products and services at various stages of production and distribution. Businesses collect this tax on behalf of the government, but the final consumer bears the cost.

Kenya's VAT is governed by the VAT Act of 2013, as well as later revisions and regulations. The Kenya Revenue Authority (KRA) is in charge of ensuring VAT compliance and administration.

VAT is charged by the VAT Act, Cap 476, and the VAT Regulations of 2017. It is determined using an input-output tax system that takes into account the value added at each stage of production. Currently, Kenya has three VAT rates.^{xx}

- **Standard Rate (16%)**– applicable to most taxable goods and services.
- **Zero-rated (0%)**– applies to exports and essential supplies, allowing businesses to claim input tax deductions.
- **Exempt supplies**– not subject to VAT, and input tax is non-deductible

3.1.1 VAT Compliance in Kenya

Kenyan businesses must comply with VAT regulations as per the Value Added Tax Act, 2013, with recent updates under the Tax Laws (Amendment) Act, 2024.

a. VAT Registration

Businesses that make or expect to make taxable supplies totaling more than KES 5 million in a 12-month period must register for VAT. This threshold calculation excludes the sale of capital assets. Businesses below this threshold can choose voluntary VAT registration if they meet the requirements. Non-residents who provide services to Kenyan consumers via electronic networks, the internet, or digital markets must

register, regardless of their turnover. Mandatory for businesses with an annual turnover of KES 5 million or more. Voluntary registration is allowed for businesses below this threshold if they meet KRA's requirements. Filing & Payment VAT returns must be filed monthly through iTax by the 20th of the following month.

b. Electronic Tax Invoices

Businesses must use TIMS-compliant Electronic Tax Registers (ETRs) to generate invoices.

3.1.2 The Concept of Taxing Value in the Chain of Production

VAT is designed to charge the incremental value added during each stage of manufacturing and distribution. This ensures that tax is only imposed on the added value, not the overall value of the product at each stage. The principle works as follows:

3.1.3 Stages of the VAT Chain

- a. **Raw Material Supplier**– Supplier sells raw materials to manufacturers and charges VAT for the transaction. The provider collects and remits the VAT to KRA.
- b. **Manufacturer**– Transforms raw ingredients into finished products. When selling items to a wholesaler, the producer charges VAT on the entire price while claiming a credit for VAT paid on raw materials.
- c. **Wholesalers** buy items and add a margin before selling to retailers– VAT is charged on the new selling price, and the wholesaler deducts the VAT paid to the manufacturer.
- d. **The retailer** purchases items from the wholesaler and sells them to the end consumer– VAT is applied to the retail price, and the retailer deducts the VAT paid to the wholesaler.
- e. **The consumer** bears the final tax burden, as they cannot claim input VAT.

Note:

- VAT is collected at every stage, but businesses only remit VAT on the value added at their stage.
- The consumer bears the full tax burden, as they cannot claim any input VAT.
- Businesses registered for VAT offset input VAT against output VAT, ensuring tax is only paid on the added value they create.

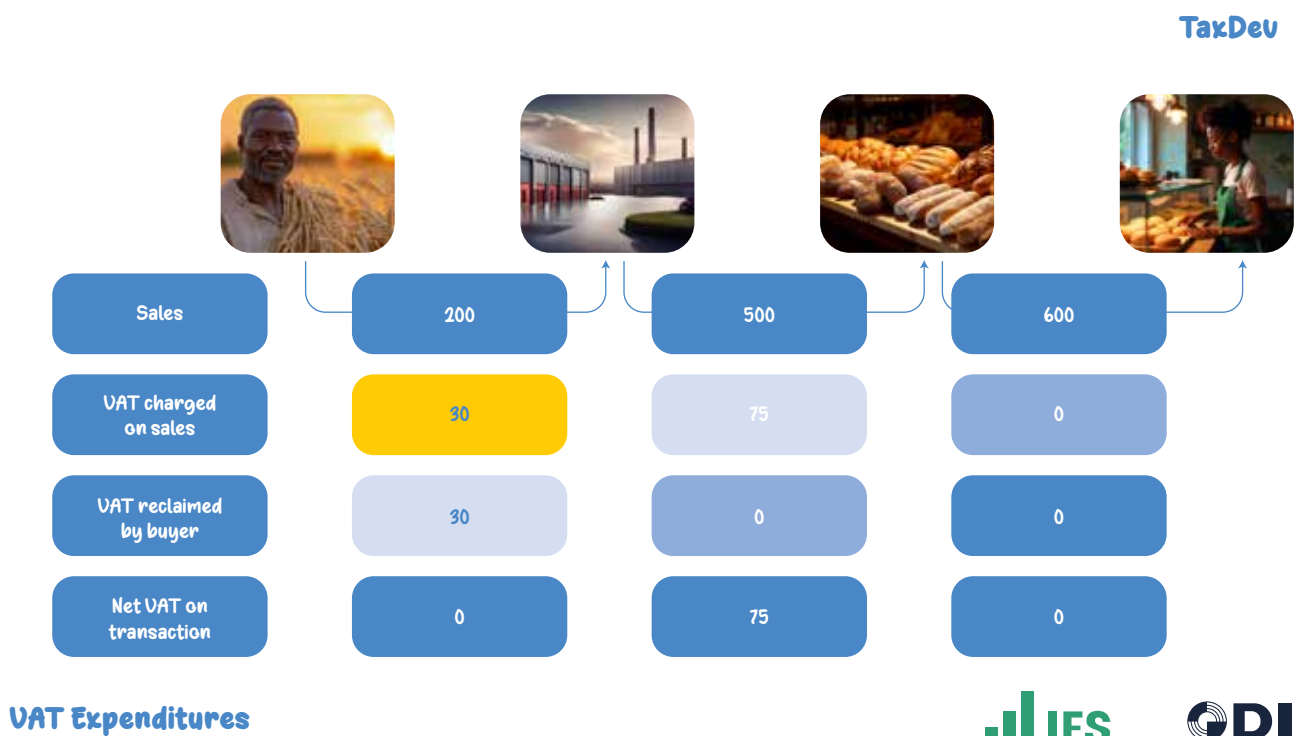
- Zero-rated items (e.g., exports) allow full VAT refund claims, while exempt items (e.g., education services) do not allow input VAT recovery.

Example: Bread Production in Kenya

Let us examine how VAT is applied at each stage in the bread production process (assuming VAT rate = 16%).

Table 7: Example of VAT application

Stage	Transaction	Price (Ksh.)	VAT (16%)	Total Price	VAT Payable to KRA
Farmer	Sells wheat to miller	10,000	1,600	11,600	=1,600
Miller	Grinds wheat, sells flour to baker	20,000	3,200	23,200	(3,200-1,600) =1,600
Baker	Produces bread, sells to market	30,000	4,800	34,800	(4,800-3,200) =1,600
Supermarket	Sell bread to final consumer	40,000	6,400	46,400	(6,400-4,800) =1,600
Consumer	Buy bread at closing price (including VAT)	46,400	Final tax paid by consumer	-	-

Figure 4: Example of application of VAT

3.1.4 Accounting for VAT: input & output mechanism

3.1.4.1 Input VAT (Recoverable VAT)

VAT paid by a business when purchasing taxable goods and services for business use. It can be deducted from output VAT. A retailer purchases goods worth Ksh. 1,000,000 and pays 16% VAT (Ksh. 160,000). The retailer can claim Ksh. 160,000 as input VAT.

3.1.4.2 Output VAT (Collected VAT)

VAT charged on sales of taxable goods and services. The collected amount must be remitted to KRA.

Example The retailer sells goods worth Ksh. 2,000,000 and charges 16% VAT (KES 320,000). The Ksh. 320,000 output is VAT that must be reported to KRA.

3.1.4.3 VAT Payable Calculation

Transaction, Amount (Ksh), VAT (16%)
Purchases 1,000,000 (VAT 16%) = 160,000
Sales 2,000,000 (VAT 16%) = 320,000
VAT Payable to KRA, (320,000 - 160,000) = 160,000
The business must remit Ksh 160,000 to KRA.

3.1.5 How VAT Works: Zero-Rated, Vatable and Exempt

3.1.5.1 Zero-Rated Supplies (0% VAT)

Zero-rated goods and services are taxed at 0%, allowing businesses to claim input VAT refunds.

Amendments introduced through the Finance Act, 2023, expanded the list of zero-rated items to include Exported services, Locally manufactured goods, and Exempt supplies (No VAT added) to the zero rated goods.^{xxi}

3.1.5.2 VAT Exemptions

- **Exempt Supplies:** Supplies that are not subject to VAT, meaning businesses cannot claim input VAT. Examples: financial and educational services.
- **Agricultural Inputs:** Micronutrient foliar feeds and bio-stimulants, tea packaging materials, mosquito repellents

- **Textile Industry:** Woven fabrics and worn clothing imported as raw materials for manufacturing textiles.
- **Aviation & Defense:** Aircraft spare parts, Goods, inputs, and raw materials for companies under Special Operating Framework Agreements (SOFA), Equipment, machinery, and motor vehicles for the Kenya Defence Forces and National Police Service. Exempt supplies do not attract VAT, and businesses dealing only in exempt supplies cannot claim input VAT deductions.
- When payment is received (partial or full)
- When the service is performed
- a. Special Cases
 - Imports: VAT is due at the time of importation. Continuous Supplies (e.g., rent, utilities)
 - VAT is due when an invoice is issued, or payment is made.
 - Hire Purchase Sales: VAT is due at the point of sale, even if payments are made in instalments.

3.1.5.3 Key Amendments from the Tax Laws (Amendment) Act, 2024 (Effective 27th December 2024)

- Change in the time of supply for exports- VAT is now applied when export certificates or supporting documents are available.
- Removal of the 90:10 input tax apportionment rule- Previously, businesses with exempt supplies below 10% could claim full input VAT; this is no longer allowed.
- New VAT exemption- The transfer of a business as a going concern is now VAT-exempt.

3.1.6 Withholding VAT

A process in which, for certain transactions, the buyer (or recipient of the services) must retain a part of the VAT owed and directly pay it to the tax authority instead of sending the entire sum to the supplier.

This method is commonly implemented in areas where there is a greater risk of non-compliance.

3.1.6.1 Why is Withholding VAT used?

To guarantee tax collection from suppliers who might otherwise under-report or fail to pay the complete VAT amount collected.

3.1.6.2 What is the operational process?

Step 1- The buyer determines the VAT amount based on the invoice.

Step 2- Two percent (as required by tax authorities) is withheld.

Step 3- The supplier receives the adjusted amount, while the withheld VAT is paid directly by the buyer to the government.

3.1.6.3 Who remits withholding VAT?

Appointed Withholding VAT agents on or before the twentieth day of the month following the month in which the deduction is made.

3.1.6.4 How does withholding VAT work?

When the appointed agents make payments to their suppliers, they are required to deduct 2% the value of the taxable supplies and remit it to the Commissioner. The balance of the payment, including the balance/remaining 14% VAT, is paid to the supplier. A withholding VAT certificate is issued to the supplier, via their registered email, once the VAT withheld has been remitted to the Commissioner through iTax.

3.1.7 VAT records and returns – Etims

The Electronic Tax Invoice Management System (eTIMS) portal is an integral tool used by the Kenya Revenue Authority (KRA) to streamline tax administration, particularly for VAT record keeping and returns.

• VAT Records:

Businesses are required to maintain detailed records of their sales (output VAT) and purchases (input VAT). These records include invoices, receipts, and other supporting documents.

• VAT Returns:

VAT returns are periodic declarations (usually monthly or quarterly) that summarize the output

VAT collected and the input VAT paid. The difference (VAT payable or refundable) is then settled with the KRA.

- Sales (Output VAT)- VAT charged on sales.
- Purchases (Input VAT)- VAT paid on purchases.
- Net VAT- The difference, which is either remitted to or refunded by the tax authority.

3.1.7.1 Efficiency of e-Tims Taxpayers Portal

Centralized Digital Records:

- Transaction Data- Businesses are required to record all their sales and purchase transactions on e-TIMS. This includes details like invoice numbers, dates, amounts, and applicable VAT.
- Input and Output VAT- The portal categorizes transactions into output VAT (tax charged on sales) and input VAT (tax paid on purchases). This helps businesses maintain clear records that are essential for VAT reconciliation.
- Audit Trail- By digitizing all records, eTIMS creates an audit trail that makes it easier for both businesses and tax authorities to review historical data, ensuring transparency and reducing the risk of errors.

3.1.8 VAT & International Trade

When services are provided in Kenya but involve international elements, the VAT treatment may differ.

3.1.8.1 International aspects– goods

This involves a 16 percent VAT charge on the cost of the goods plus any customs duties and shipping charges. It applies to both goods brought into Kenya from outside the East African Community (EAC) and from other EAC countries.

3.1.8.2 International aspects– services

Services that are exported (i.e., provided to a non-resident client outside Kenya) are typically zero-rated. This means that although the service provider charges 0% VAT, they are still required to file a VAT return.

Example: A Kenyan software development company provides IT support to a client in the United States. The service is zero-rated, so no VAT is charged, but the company must still report on the sales.

3.1.8.3 Imported services reverse charge mechanism

When a non-resident service provider supplies services in Kenya (for example, consulting services), the local recipient (often a Kenyan business) might be required to account for VAT using the reverse charge mechanism. This means the Kenyan business calculates the VAT as if it were the supplier and remits it to KRA.

Example: A foreign consulting firm provides advisory services to a Kenyan company. Instead of the firm charging VAT, the Kenyan company self-assesses VAT on the cost of the service and remits it via its VAT return.

3.1.9 VAT Refunds

The two most common types of Value Added Tax (VAT) refunds are made pursuant to the provisions of Section 17(5) of the VAT Act 2013 which allow payment of excess input tax to a registered person where.

1. Refund arising from making zero rated supplies –Registered VAT taxpayers deal with taxable supplies listed under the second schedule of the VAT Act. However, the claim should be on the inputs that are solely used in the making of the zero rated supplies and should be made within 12 months from the date of the supplies.
2. Refund arising from tax withheld by appointed tax withholding agents and the registered person lodges the claim for the refund of the excess tax within twenty-four months from the date the tax becomes due and payable. For example, where a contractor supplies goods or services to an appointed withholding VAT agent, the agent withholds the tax at 2%. Due to the claim of input tax from the output tax while filing,

the already withheld tax puts the contractor at a refund position.

3. Tax paid in error – For example, a withholding VAT agent withholds tax for the wrong taxpayer, the taxpayer then can apply for the refund for the tax paid in error. Claim should be within 12 months from the date of payment.
4. Bad Debts – Claim is made when a supplier is not paid by the buyer for goods they have supplied and it should be made after 3 years, on the basis that the buyer has been declared insolvent by the court. The seller has to prove that all avenues have been sought in claiming the debt including seeking redress from the court have been unsuccessful. This claim on bad debts has to be made within 5 years

3.2 Excise Duty

Session objectives

At the end of the session, the students will have:

- Understood the concept of excise duty, including its history and definition.
- Gained knowledge on the various types of excise duties applicable in Kenya.
- Understood why excise duty is imposed and its significance in the broader tax system.
- Understood what qualifies as excisable goods and services and how they are categorized.
- Gained a comprehensive understanding of the Excise Duty Act, 2015, including its structure and provisions.

Resources needed

- The Excise Duty Act, 2015.
- The Finance Act, 2018, and 2023.
- The Tax (Amendment) Act, 2024.
- The M-shwari App.

How to run the session

- Prepare a power point presentation on the overview of excise duty, types of excise duty and excisable good and services in Kenya.
- Deliver the presentation to the trainees in 30 minutes.

- Instruct trainees to log in to the Kenya Law website and access Excise Duty Act, 2015 for reference.
- Illustrate amendments made to the Excise Duty Act, 2015 using examples 1.2 and 3.
- Engage the trainees in 20-minute group discussion during which they will identify amendments made to the Excise Duty Act, 2015.
- Give each group 5 minutes to present their findings in plenary.
- Conclude the session by recapping the key takeaways.

3.2.1 History of Excise Duty

Excise duty is one of the oldest taxes levied worldwide on selected products. The earliest products to be levied excise duty included alcohol and tobacco. In Kenya, excise duty was introduced during colonial times and was initially charged on beer, wine, spirits and tobacco. Ever since, so many amendments have been made to take care of modern business practices and technology. In 2015, the Excise Duty Act, 2015 was enacted and it repealed the Customs and Excise Act subject to certain conditions set out therein. The Excise Duty Act, 2015 came into effect on 1st December 2015. It was intended to achieve international best practices: simplicity, certainty, revenue mobilization, leverage on technology.

3.2.2 Types of Excise Duty

- Specific duty rate**– This is where specific amount of tax is charged per unit of measure on an excisable product. An example is the excise duty imposed on cigarette with filters (hinge lid and soft cap) at Ksh 4100 per mile.
- Ad valorem duty rate**– This is where a percentage rate of duty charged on the value of an excisable product. An example is the imports tax charged on the total Cost, Insurance and Freight (CIF).

3.2.3 Rationale for Excise Duty

Initially, excise duty was referred to as “sin” or “luxury”, tax as it was imposed on specific goods and services to regulate their consumption. However, over time, the government has expanded the

scope of excise duty, imposing it on various goods and services for a broader range of reasons as discussed below:

- To raise government revenue
- For health reasons
- To correct negative externalities arising from the consumption of products
- For environmental concerns
- To improve the vertical equity of the tax system/ reallocation of resources from the rich to the poor (Distributive)
- For restitution of society
- To punish

3.2.4 Excisable goods and services

3.2.4.1 Excisable goods

Domestic excise duty is a tax levied on the production or sale of specific goods and services within Kenya. This applies to both locally manufactured and imported items as outlined in **part I of the First Schedule** of the Excise Duty Act, 2015. It primarily applies to:

- Luxurious goods
- Goods with negative desired effects
- Addictive products
- Goods with low price elasticity

Excisable goods include alcoholic beverages, tobacco products, sugar- sweetened beverages and energy drinks, cosmetic and beauty products, petroleum products and plastics and environmentally harmful materials.

Manufacturers and importers of excisable goods must register with **Kenya Revenue Authority (KRA)** and file returns by the **20th of the following month**. Licensed manufacturers and importers are required to submit their excise returns through iTax system.

For certain excisable goods, **excise stamps** must be affixed as proof that the required excise duty has been paid by the manufacturer. Legal Notice No.

30 of 2023 titled: The Excise Duty (Excisable Goods Management System) (Amendment) Regulations, 2023 has amended, among other provisions, the price of excise stamps effective 31st March 2023.

Imported goods are subject to excise duty and must comply with the **East African Community Common External Tariff** (EAC CET).

3.2.4.2 Excisable services

Excise duty is also levied on certain services as outlined in **part II of the first schedule** of the Excise Duty Act, 2015.

These services include:

- Telephone and internet data services
- Fees charged for money transfer services by

financial institutions.

- Fees charged for money transfer services by cellular phone service providers
- Fees charged on digital services such as online streaming, advertising and other digital transactions.
- Betting, gaming, price competition and lottery services

3.2.5 Overview of the Excise Duty Act, 2015

The Excise Duty Act has 46 sections and two schedules. The First Schedule has three parts which contain a list of the Excisable Goods and Services and the corresponding rates. The Second Schedule contains the exemptions from Excise Taxation for both goods and services.

Table 8: Excise duty exemptions contained in the Second Schedule

Part	Section	Content
I	1- 4	Preliminary
II	5- 14	Liability for Excise Duty
III	15- 23	Licensing
IV	24- 27	Excise Control
V	28	Excise stamps
VI	29- 32	Refunds
VII	33- 37	Excise Duty Procedure
VIII	38- 41	Offences and Penalties
IX	42- 46	Miscellaneous Provisions
	First Schedule	Excisable Goods and Services
	Second Schedule	Exempt Excisable Goods and Services

Source: The Excise Duty Act, 2015

Traditionally, the Excise Duty Act, 2015 has been amended annually through the **Finance Act**, which is enacted by **30th June every year**. These amendments specify changes to excise duty including adjustments to tax rates and the inclusion or exclusion of specific goods and services from the list of excisable items. However, amendments can also be made through other

laws. For example, in December 2024, amendments were made to the Excise Duty Act, 2015 through the Tax Laws (Amendment) Act, 2024.

Example 1: An amendment through the Tax Law (Amendment) Act, 2024. The Tax Law (Amendment) Act, 2024 amends part III of the Excise Duty Act, 2015 by inserting new definitions as shown below. (Fig.9)

Figure 5: A snippet of the Tax Law (Amendment) Act, 2024

(c) in Part III by inserting the following new definitions in the proper alphabetical sequence —

"fees charged by digital lenders" includes any fees, charges or commissions charged by digital lenders relating to their licensed activities but does not include interest, pre-loan interest, post-loan interest, return on 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;

"small independent brewer"

means

manufacturers of beer, cider, perry, mead, opaque beer, wine and fortified wines and mixtures of fermented beverages with nonalcoholic beverages manufactured whose production volume does not exceed 150,000

litres per month.

To track these changes, refer to the Excise Duty, Act 2015 as shown below. (Fig.10)

The Excise Duty, Act 2015 effectively amended the paragraph as shown below.

Figure 6: A snippet of the Excise Duty, Act 2015.

"fees charged by digital lenders" includes any fees, charges or commissions charged by digital lenders relating to their licensed activities but does not include interest, pre-loan interest, post-loan interest, return on 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;

Probable reason for amendment: The government provides clarity on the fees chargeable to excise duty in relation to digital lenders.

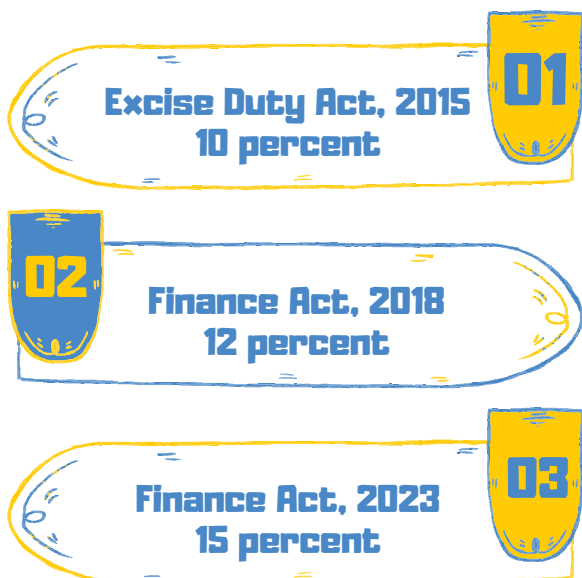
Example 2: Excise Duty imposed on fees charged by digital lenders

The Excise Duty, Act 2015 imposes an excise duty rate of 20 per cent on fees charged by digital lenders. An example of this excise duty is the one imposed on facility fee on m-shwari –a savings and loan service that enables M-PESA customers to save as little as Ksh. 1, and access credit from Ksh. 1,000. The screenshot shows that a facility fee of Ksh. 37.5 percent charged for borrowing a loan of Ksh. 500. A 20 percent excise duty is imposed on the facility fee which translates to Ksh. 7.50.^{xxiv}

The screenshot displays the M-PESA interface for a loan transaction. At the top, there are buttons for 'DEPOSIT FROM M-PESA', 'WITHDRAW TO M-PESA', 'DEPOSIT', 'LOCK SAVINGS', and 'LOAN'. Below these, a transaction history for the date 2025-03-07 is shown. The transactions include an excise duty repayment, an excise duty charge, a facility fee, and a loan disbursement.

Date	Description	Amount (KSH)	Reference
2025-03-07	EXCISE DUTY REPAYMENT	KSH. 7.50	TC78QEYTUA
2025-03-07	EXCISE DUTY	KSH. 7.50	TC78QEYTUA
2025-03-07	FACILITY FEE	KSH. 37.5	TC78QEYTUA
2025-03-07	LOAN DISBURSEMENT	KSH. 500	TC78QEYTUA

Example 3: Amendments to excise duty on fees charged for money transfer services



3.3 The East African Community Customs Management Act, 2004

The East African Community is mandated to advance economic, social, and political integration among Partner States. The key economic goal is establishing a fully functional Customs Union, implemented by the Directorate of Customs under the EAC Treaty.

The **EAC Customs Management Act (CMA) 2004** was enacted to facilitate customs integration. The act was founded on input from governments and businesses, which is critical to shaping an effective law. Some of the key areas that the Act focuses on include digital trade, anti-counterfeit measures, and dispute resolution. The Act applies to all EAC Partner States (Burundi, DRC, Kenya, Rwanda, South Sudan, Tanzania, and Uganda).^{xv}

Administration

The Directorate of Customs was established under the EAC Treaty (Article 75(3)) to:

- Initiate and coordinate customs policies across Partner States.

- Oversee the implementation of the Common External Tariff (CET) and trade facilitation.

The Directorate is also responsible for:

- **Policy Coordination:** Harmonizing customs laws and procedures.
- **Trade Facilitation:** Implementing the EAC Protocol on Customs Union.
- **Enforcement:** Monitoring compliance with customs laws.
- **Capacity Building:** Training and standardizing customs operations.
- **Dispute Resolution:** Addressing inconsistencies in customs administration.

Each Partner State appoints a Commissioner of Customs to:

- Manage national customs operations.
- Collect and account for customs revenue.
- Delegating powers to officers (e.g., inspections, seizures).

Notable Customs Powers and Duties (Sections 6–10) contained in the Act comprise:

- **Customs Seal and Flag (Section 6):** Official symbols to identify customs authority.
- **Police Powers for Officers (Section 7):** Customs officers have **full police powers** (arrest, search, seizure) within their jurisdiction.
- **Exchange of Information (Section 10):** Partner States must share data on cross-border trade and smuggling.

The administration also comes with operational provisions (Sections 11–17) such as:

- **Appointment of Ports/Customs Areas (Sections 11–12):** Designates approved ports, airports, and border posts for customs control.
- **Offences by Officers (Section 9):** Penalties for corruption (e.g., bribes, disclosure of confidential information) include fines (up to \$2,500) and imprisonment (up to 3 years).
- **Liability for Negligence (Section 17):** Officers/Commissioners may be sued for **willful negligence** causing loss/damage to goods.

Importation

The EAC Act governs the importation of goods into the East African Community (EAC), and outlines prohibitions, procedures, and customs controls.

Some of the key provisions under importation include:

1. Prohibited & Restricted Imports (Sections 18–20)

- **Prohibited Goods (Section 18):**
 - Listed in Part A of the Second Schedule (e.g., counterfeit goods, hazardous materials).
 - Absolute ban on importation.
- **Restricted Goods (Section 18):**
 - Listed in Part B of the Second Schedule (e.g., firearms, certain pharmaceuticals).
 - Require special permits/licenses for import.
- **Council's Authority (Section 19):**
 - The EAC Council can amend restrictions via Gazette notices.

2. Arrival & Reporting Procedures (Sections 21–32)

- **Vessels/Aircraft (Sections 21–28):**
 - They must report cargo to Customs 24 hours before arrival (vessels) or immediately after takeoff (aircraft).
 - The master/Agent must submit a cargo manifest and answer Customs queries.
- **Overland Imports (Sections 29–31):**
 - Vehicles/persons must enter through designated border points.
 - Must declare goods and present supporting documents (e.g., invoices, permits).
- **Penalties:**
 - Failure to report = **finest + forfeiture of goods**.

3. Unloading & Customs Control (Sections 33–43)

- **Approved Places (Section 33):**
 - Goods must be unloaded at **Customs-designated areas** (ports, airports, bonded warehouses).
- **Examination & Entry (Sections 34–38):**
 - Goods must be entered for clearance within **21 days** (options: home use, warehousing,

transit).

- Provisional assessment allowed if documents are incomplete (with duty deposit).
- **Special Cases (Sections 39–43):**
 - Temporary removal for testing/repairs (with security bond).
 - Perishable/abandoned goods may be sold/destroyed by Customs.
- **4. Passenger Clearance (Sections 44–46)**
- **Dual-Channel System (Section 45):**
 - Green Channel: For passengers with no dutiable goods.
 - Red Channel: For passengers carrying dutiable/restricted items.
- **Baggage Declaration (Section 46):**
 - Travelers must declare all goods upon entry.

3.4 Miscellaneous Fees and Levies Act, 2016

The Miscellaneous Fees and Levies Act of 2016 was enacted to improve the administration of different fees and levies on imports and exports in Kenya. The law intends to improve tax collection, encourage industrial expansion, and properly control trade-related fees.^{xxvi}

3.4.1 Objectives of the Act

- Simplify fee and levies management.
- Implement export charges to benefit local industries.
- Ensure compliance with tax requirements.
- Generate revenue for infrastructure development.

3.4.2 Provisions.

- **Import Declaration Fee (IDF)**– 3.5% of customs value imported products. Certain exemptions apply, including government imports and vital products.
- **Railway Development Levy (RDL)**– Imported products are charged at 2% of their customs value. The revenue collected goes towards railway infrastructure projects.
- **Export levy**– Applied to select exported

commodities to promote local value addition. Levy rates differ depending on the type of items.

Exemptions include supplies for diplomatic missions, goods imported through government contracts and required raw materials and industrial inputs.

3.4.3 Amendments to the Act

The Act has been amended multiple times to reflect changing economic policies and trade rules

Notable revisions include:

- 2017: levy rate adjustments.
- 2018: the taxed goods list was expanded.
- 2019-2021: changes to exemptions and levy rates
- 2022-2024: implementation of new compliance measures and rate modifications.

3.4.4 Compliance requirements

- Importers and exporters must provide exact amounts and pay duties on time.
- Noncompliance may result in penalties and interest costs.

- Monitor regular updates from the Kenya revenue authority (KRA) and National Treasury to ensure compliance.

Importers should ensure items are appropriately classified and tariffs are paid before clearing.

Exporters must verify and comply with relevant export duties.

The Miscellaneous Fees and Levies Act of 2016 is critical for both trade regulation and revenue mobilization. Compliance with this Act promotes seamless business operations and helps to avoid legal issues.

Key takeaways

1. Excise Duty is an indirect tax that is imposed by the government on certain products with negative externalities to discourage their consumption.
2. The scope of excisable goods and services has been expanded over the years.
3. Excise Duty is amended through the Finance Act and other laws such Tax (Amendment) Act.



4. NON TAX REVENUES.



Objectives of the Session

By the end of this training session, participants will have:

- Gained a clear understanding of what non-tax revenues are, including how they are generated and how they fundamentally differ from tax revenues.
- Identified and categorized the main types of non-tax revenue sources in Kenya
- Examined Kenya's performance in mobilizing non-tax revenue compared to regional peers.
- Analyzed systemic challenges affecting the effectiveness of non-tax revenue, the equity and fairness of non-tax revenue systems.
- Discussed the limitations of non-tax revenues as an alternative to taxes and recommend practical strategies for improving non-tax revenue mobilization in Kenya.

How to run the Session

1. Prepare a power point presentation to be delivered in 30 minutes.
2. Brief the participants on the topic and the session objectives.
3. Introduce the topic, the definitions and the difference between the tax and non-tax revenues.

Icebreaker

- **Option A – Story-based activity:**
Present a short story involving multiple

government payments (e.g., someone paying a parking fee, renewing their driver's license, getting a passport, and paying VAT at a supermarket). Then ask participants: "Which of these do you think are tax revenues, and which are non-tax revenues?"

- **Option B – Personal reflection activity:**
"Can you name a government service you've recently paid for that wasn't a tax?" Invite a few participants to share, then clarify the classification.
4. Present the rest of the slides
 5. Before discussing limitations, pose this question to the group:
"Do you think non-tax revenues could be a strong alternative to taxes?" Allow 2–3 participants to share their views. Use their input to transition into the next section.

4.1 What are Non-Tax Revenues

Non-tax revenues are government earnings that originate from sources other than taxes. They are generated through the government's regulatory, commercial, or administrative functions, rather than through tax collection.^{xxvii} The sources include fees, fines, investments, and income from government-owned properties or services. Non-tax revenue is an important but often under-tapped source of public revenue.

4.1.1 Kenya's non-tax revenue Compared to the Region's

While Kenya has a wide range of NTRs on its books, it collects relatively little revenue by regional standards: only 2.3 percent of GDP in 2021, compared to nearly 6 percent of GDP for the region.

The below average performance is also evident in specific sources of non-tax revenues. Just 0.8 percent of GDP is generated from government property income and about 0.2 percent of GDP from administrative fees for government services. Comparatively, the continent's average collection is 2.4 percent and 1 percent of GDP for property income and administrative fees respectively. Kenya received grants amounting to just 0.3 percent of GDP in 2021, compared to the regional average of 1.4 percent. Cape Verde, Egypt, Ghana, Morocco and Seychelles generated more than 1 percent of GDP in non-tax revenues from sales of goods and services and administrative fees. Kenya on the other hand generated less than 0.5 percent of GDP from the same sources.

Table 9: Key Differences Between Tax and Non-Tax Revenues

Difference	Tax Revenue	Non-Tax Revenue
Source	Collected through mandatory levies on income, goods, and service, without direct service or benefit in return.	Earned from government services, fines, return on investments, use of public resources etc.
Predictability	More stable and predictable, as it is collected regularly based on established tax laws and economic activity. Governments can forecast these revenues with greater confidence during budget planning.	Often unpredictable and volatile as it depends on factors such as fines, investment returns, or resource royalties which can fluctuate due to market conditions, policy changes, or irregular demand.
Legal Requirement	Citizens are legally required to pay.	Usually based on voluntary actions (e.g., park entry fees).
Collection Process	Requires complex structures like KRA for collection.	Often simpler and direct (e.g., public office fees).
Revenue Size	Typically contributes to most government income.	Usually a smaller percentage of total revenue.

4.1.2 Examples of Non-Tax Revenues

Fees and Charges: Payments made by individuals or businesses for accessing government services. Examples include passport fees, court filing fees, driving license charges, game park fees, parking fees, etc.^{xviii}

Fines and Penalties: Payments imposed as punishment for violating laws or regulations. These aims to deter unlawful behavior. Examples include traffic fines, environmental violation penalties, and tax evasion/late payment fines.

Interest and Dividends: Income earned from government loans or profits distributed by state-owned enterprises (SOEs). Examples include interest from government-issued loans to parastatals and dividends from companies like KenGen or Safaricom.

Rent and Leasing: Revenue generated from renting or leasing government-owned properties and assets. Examples include rent collected from public markets, stadiums, or office spaces.

Licenses and Permits: Fees paid for official authorization to conduct specific activities or businesses. Examples include business permits, liquor licenses, and construction permits.

Royalties: Payments made to the government for extracting natural resources or using state-owned intellectual property. Examples include royalties

from mining activities, oil and gas among others.

Sales of Assets: Revenue from the disposal of public properties, often done through auctions or sales. Examples include the auction of government vehicles, sale of underutilized land, or disposal of obsolete equipment.

Donations and Grants: Financial contributions from development partners, foreign governments, or organizations to support public projects. Examples include grants for education, health, or climate-related initiatives.

4.1.3 Role of Non-Tax Revenues in government financing

Supplementing Tax Revenues: They provide an additional income stream, reducing reliance on traditional taxes.

Funding Specific Services: Revenue from fees, fines, and royalties is often reinvested into related services, improving service delivery.

Enhancing Budget Flexibility: Since non-tax revenues are less tied to economic cycles than certain taxes, they can offer financial stability.

Supporting Local Governments: In Kenya, Own Source Revenue (OSR) collected by counties (e.g., parking fees, market levies) boosts local development.

Encouraging Compliance and Behavior Change: Fines and penalties discourage unlawful activities.

while environmental levies promote sustainable practices.

4.1.4 Why is Kenya's Non-Tax Revenue So Low?

Underreporting: Kenya's non-tax revenue figures may be underestimated due to varying reporting across government agencies. Different entities categorize non-tax revenues inconsistently, making it difficult to track and analyze revenue streams.

Limited Sources: Kenya's non-tax revenue base is narrow, relying heavily on a few key streams like dividends and fees.

Inefficiencies in SOEs: State-owned enterprises have underperformed in recent years, reducing dividend contributions to the government.

Poor Reporting Practices: Non-tax revenue data in budget documents lacks clarity and detail, making it challenging to interpret.

Weak Administration: Kenya's non-tax revenue system faces administrative challenges, with semi-automated processes and delays in reviewing fees and charges.

According to a research by the Institute of Public Finance ([link](#)), the government could collect as much as Ksh 140 billion more from non-tax sources by exploring additional non-tax revenue streams, automating collection, enhancing profitability of state-owned enterprises, and standardizing the process of imposing fees, charges and rates.

4.2 ARE NON-TAX REVENUES A GOOD ALTERNATIVE TO TAX REVENUES?

Non-tax revenues are not a strong alternative to tax revenues in Kenya due to their relatively small contribution to the Gross Domestic Product (GDP). The tax revenues significantly outweigh non-tax revenues in their contribution to GDP. For instance, in 2022, Kenya's tax-to-GDP ratio was approximately 16.8%. In contrast, non-tax revenues accounted for about 0.5% of GDP in that fiscal year.^{xxix}

4.2.1 Advantages of Non-Tax Revenues

a. Diversification of Income Sources: Relying

solely on tax revenues exposes governments to economic shocks. Non-tax revenues provide an alternative stream that can help stabilize budgets.

- b. Revenue linked to Specific Sectors: Non-tax sources like user fees, environmental levies, and royalties target specific activities or industries, allowing the government to earn directly from resource use or services.
- c. Promotes Accountability: Non-tax revenues often come from direct payments for services (e.g., park fees, licenses), which can improve public perception if citizens see value in what they pay for.
- d. Encourages Behavioral Change: Charges like environmental levies or congestion fees can discourage harmful practices while generating revenue.

4.2.2 Limitations of Non-Tax Revenues

- i. Unpredictable and Volatile: Non-tax revenues, particularly those tied to resources (e.g., oil royalties or tourism fees), can fluctuate due to market conditions or seasonal changes.
- ii. Limited Growth Potential: Unlike tax revenues, which naturally increase as the economy grows through higher incomes, business profits, and consumption, non-tax revenues often have a limit.
- iii. Expanding non-tax revenues significantly may require introducing new fees, fines, or charges, which can place an extra financial burden on citizens and businesses.
- iv. Equity Concerns: Fees and charges can disproportionately impact low-income groups, especially if applied to essential services like healthcare or education.
- v. Administrative Complexity: Managing diverse non-tax revenue streams may require specialized systems and capacity, particularly at the county level.

4.2.3 Equity In Non-Tax Revenue

Non-tax revenues can become punitive if they are poorly designed or implemented without considering fairness and equity. While these revenues are intended to generate income, they can unintentionally burden certain groups or hinder access to essential services through:

Disproportionate Impact on Vulnerable Groups:

Fixed fees for services like healthcare, education, or water may place a heavier financial burden on low-income individuals.

Excessive Charges on Essential Services:

Overpricing permits, licenses, or utilities can limit access to basic services.

Ambiguous or Non-Transparent Fees:

Unclear or hidden charges can create confusion and frustration. Some government agencies may impose multiple layered fees, making services costly and inaccessible.

Overburdening Specific Sectors:

Imposing excessive fees on industries like tourism, mining, or transport may discourage investment and growth in those sectors.

Environmental Levies Without Alternatives:

While environmental charges are often justified, they can feel punitive if no affordable, eco-friendly alternatives are available.

4.2.3.1 How to Ensure Equity in Non-Tax Revenues

Equity-Based Fee Design: Introduce progressive charges where higher-income individuals pay more (e.g. wealth-based healthcare fees).

Transparency: Clear communication of fee structures, the rationale behind charges, and how revenues are used helps prevent undue burdens on vulnerable or low-income groups.

Public Participation: Engage citizens in discussions on new fees to ensure they are reasonable and

justified.

Exemptions for Essential Services: Spare critical services like healthcare, education, and basic utilities from excessive fees.

4.2.4 Recommendations for Enhancing Non-Tax Revenue in Kenya

Enhancing collections through full automation is key.

The government should expedite digital payment systems for services. On August 4, 2023, the president directed that all government service payments be made via a single National Treasury-managed platform, expected to generate an additional Ksh 10 billion. In FY 2022/23, non-tax revenue exceeded its target by Ksh 16.4 billion, driven by increased digitization, parastatal fund mop-ups, and higher dividends from firms.

Diversify and Target Non-Tax Revenues:

Kenya should explore alternative revenue streams aligned with its economic strengths. The creative industry, which contributed Ksh 121 billion in 2022, can grow further through better protection and commercialization of intellectual property. Expanding tourism services and commercializing government assets, such as leasing public properties, also present revenue opportunities.

Improve Non-Tax Revenue Reporting:

Kenya should adopt standardized reporting frameworks across agencies, provide detailed revenue breakdowns, and expand digital systems like e-Citizen to capture all non-tax revenues. Regular audits would enhance accountability and address revenue gaps.

Devolving Non-Tax Revenue Collection in Counties:

Allowing counties to manage some non-tax revenues, such as market fees and community tourism charges, can improve efficiency. This requires clear legal frameworks, county staff training, revenue-sharing agreements, and local innovation to maximize collections.

Strengthening State-Owned Enterprises (SOEs):

Improving the financial performance and management of SOEs can boost dividend income. This may involve strengthening governance structures, enhancing oversight, and promoting profitability.

Key Takeaways

- Non-Tax Revenues are government earnings from sources like fees, fines, licenses, and dividends
- Distinct from taxes as they are linked to services or penalties, not mandatory levies.

- Kenya's non-tax revenue contributes less than 1% of GDP due to limited sources, poor reporting, and inefficiencies in SOEs and collection systems.
- Non-tax revenues can be regressive and unpredictable. Poorly designed charges may burden low-income groups or discourage business activity.
- Kenya should automate payments, standardize reporting, expand revenue streams (e.g. tourism), strengthen SOEs, and allow counties to manage localized collections.



- 5. Taxation at the Sub-National Level Own Source Revenue



Objectives of the session

By the end of this session, participants will be able to:

- Understand the legal and institutional framework governing own source revenue (OSR) in Kenya's county governments.
- Identify key sources of own revenue for counties and assess their performance trends.
- Evaluate the challenges and constraints affecting OSR mobilization and administration at the county level.

- Discuss best practices and reforms to enhance OSR collection, efficiency, and accountability.
- Appreciate the role of OSR in strengthening county fiscal autonomy and service delivery.

Resources needed

- Public Finance Management Act (PFMA), 2012
- County Governments Act, 2012
- Commission of Revenue Allocation Reports, especially the model of Tariffs and Pricing policy
- Office of the Controller of Budget's Budget Implementation Report reports
- County Finance Acts
- Constitution of Kenya, 2010
- Enhancing Revenue Generation and Progressivity of Property Taxation in Kenya

How to run the session

- Start warm up session through interactive questioning
- Deliver a 30 minutes power point presentation
- Guide participants to access the said legal requirements guiding taxation at the sub nationals.
- Divide participants into small groups for a 20 minute session on what challenges counties are facing in the collection of own source revenue and how can counties enhance its collection.
- Ask each group to present for 2-3 minutes on the same
- Wrap up the session by giving the overview of the whole session

For county governments to effectively deliver their mandates, they require adequate financial resources. While they receive allocations from nationally raised revenue, fiscal decentralization necessitates that counties also generate their own revenue. Article 209 of the Constitution^{xxx} therefore grants county governments the authority to impose taxes and charges, including property taxes, entertainment taxes, and other revenue measures permitted by an Act of Parliament. However, Article 209(5) imposes restrictions to ensure that county taxation does not hinder national economic policies.



disrupt economic activities across county borders, or impede the free movement of goods, services, capital, and labor.

The Own source revenue falls into three main categories

5.1 Taxes

5.1.1 Property tax

Property rates are taxes levied on the value of property including land. They are assessed by a rating authority with the assistance of the valuer. In Kenya property rates were governed by: Valuation for Rating Act (Cap 266) (1956), which guides the preparation of valuation rolls, and Rating Act (Cap 267) (1963), which identifies the rating authority and provides for the imposition of rates and applicable forms of rating.

Following the 2010 Constitution, particularly Article 209(3), county governments are required to enact property rating and valuation laws. Due to revenue underperformance, the National Rating Act 2024^{xxxix} was introduced to provide a uniform legislative framework to impose property rates in conjunction with the following two important laws that impact property taxation. They include:

- The Land Act (2012): Implements Article 68 of the Constitution by revising, consolidating, and rationalizing land laws for better administration and management of land resources.
- The Land Registration Act (2012)^{xxxix} Provides for the registration of land titles in line with devolved governance.

The National Rating Act, 2024 outlines provisions on the valuation of rateable property, preparation and approval of valuation rolls, duty to levy rates, definitions of a rateable owner, forms of rating, public participation requirements, rate setting and collection, remission, discounts and waivers, enforcement measures, exemptions, contributions in lieu of rates, and entertainment tax regulation.

5.2 Charges and fees

Part II of the Fourth Schedule of the Constitution outlines the functions of county governments, which give rise to various public services that attract fees and charges. Section 120 of the County Governments Act ^{xxxix}, 2012, mandates county governments to develop a Tariffs and Pricing Policy for all user fees and charges. However, to date, no county government has complied with this legal requirement by formulating such a policy to guide the determination of fees and charges.

Below are examples of fees and charges imposed by county governments:

a). Outdoor Advertising licensing

Outdoor advertising plays a crucial role in supporting vibrant industries and fostering a competitive economy. However, while businesses seek to maximize their advertising reach, it is essential to balance this with the need to protect public spaces, maintain aesthetic appeal, and ensure public safety. To achieve this balance, outdoor advertising is regulated primarily through licensing.

Before devolution, the now-defunct local authorities (LAs) had significant powers to regulate outdoor advertising. These powers, granted under the Local Government Act ^{xxxix} (Cap. 265, Section 162), allowed LAs to:

- i. Control the display of advertisements, ensuring they adhered to public decency, safety, and urban planning guidelines.
- ii. Regulate the use of mobile advertising, such as advertising vans, banners, flags, and digital screens.
- iii. Govern the distribution of handbills in public places to prevent littering and unauthorized advertising.
- iv. Manage street decorations to ensure harmony with urban planning objectives.

With the enactment of the 2010 Constitution^{xxxvi} the responsibility for regulating outdoor advertising was transferred to county governments under the Fourth Schedule, which designates county governments as the primary authorities responsible for outdoor advertising regulations.

The legal basis for licensing

The **County Outdoor Advertising Control Act, 2015**^{xxxvii} establishes the legal framework for outdoor advertising licensing. Under this Act, any individual or business intending to engage in outdoor advertising must obtain a license from the respective county government. The licensing process ensures that advertisements are safe, do not obstruct public spaces or road users, and align with the aesthetic and environmental standards of the area.

The application for an outdoor advertising license requires compliance with specific conditions, including:

1. Submission of an application in the prescribed form, accompanied by the required fee.
2. Provision of a site plan detailing the exact location, dimensions, and type of advertisement.
3. Written consent from the site owner or any other party with a vested interest in the property.
4. An artistic impression or diagram illustrating the proposed advertisement's design, scale, and positioning.
5. Consideration of the advertisement's impact on road safety, visual clutter, and public amenities.

The county executive committee member responsible for outdoor advertising evaluates applications based on these criteria. If the application meets all regulatory requirements, a license is issued, specifying the duration and conditions of display.

Once a license is granted, the advertisement must be installed within six months, failure to which the approval lapses. Additionally, a licensee:

- Cannot alter, remove, or upgrade an advertisement without prior approval, except for routine maintenance.
- Must renew the license before expiry, following the same application process.
- Must remove an advertisement within seven days of license expiry or revocation.

Revocation of the license

A license may be revoked if the advertisement:

- Becomes a safety hazard or obstructs visibility.
- Violates urban planning or historical preservation guidelines.
- Causes excessive light pollution or distracts road users.

Before revocation, the county must issue a 21-day notice to the licensee and allow them an opportunity to respond. If dissatisfied with the decision, the licensee has the right to seek judicial review within 14 days of the decision.

b) Parking fees

Parking fees are charges imposed on vehicles for the use of public parking spaces provided by the county government. These charges are reviewed annually through the **Finance Act** to align with policy objectives, infrastructure maintenance needs, and urban mobility strategies.

The primary objectives of parking fees include managing traffic flow and reducing congestion in urban centers and localities, regulating the conduct of motorists, and generating revenue to support the maintenance and provision of parking facilities. By implementing structured parking fees, counties can promote efficient land use, encourage the use of alternative transport modes, and enhance urban planning.

The **Traffic Act (Cap 403)**^{xxxviii} provides the legal framework for traffic regulation, including parking management. Sections **73A and 73B** empower local authorities to enact by-laws governing designated parking places, including the determination of

applicable charges. This ensures that parking regulations are legally enforceable and aligned with broader transportation policies.

c). Business Licensing Fee

A business licensing fee is a levy imposed by the county government as a prerequisite for conducting business within its jurisdiction. Upon payment of the required fee, a trader is issued a trade license, granting them legal authorization to operate.

The cost of a business license varies depending on several factors, including the size of the business, its location, and the type of activity it engages in. Businesses in prime urban areas or those classified as high-risk operations may attract higher fees compared to smaller enterprises or those in less strategic locations. In addition to revenue generation, business licensing serves as a regulatory tool, allowing counties to monitor commercial activities, enforce health and safety standards, and promote fair competition within their economies.

Counties periodically review business licensing fees to align with economic conditions and policy objectives. Some counties have also adopted digital platforms to facilitate online applications and payments, improving efficiency and reducing bureaucratic delays in the licensing process.

d). Liquor Licensing Fee

Liquor Licensing Fee refers to the cost of obtaining a license to legally sell or serve alcoholic beverages in an establishment.

Before 2010, liquor licensing in Kenya was governed by the Liquor Licensing Act (Cap 121) of 1957, which placed regulatory authority under the Minister of State for Provincial Administration and Internal Security. The Act divided the country into licensing areas, such as Nairobi licensing area and multiple district-based areas in regions like Nyanza Province. The minister had the power to declare

these areas and determine the liquor fees payable within them.

In 2010, this Act was repealed and replaced by the Alcoholic Drinks Control Act No. 4 of 2010^{xxxix}. The new law created Alcoholic Drinks Regulation Committees in each district, responsible for issuing liquor licenses for brewing, wholesale, and retail sale of alcoholic beverages. It also established the National Authority for the Campaign Against Alcohol and Drug Abuse (NACADA), which took on the role of regulating alcohol-related issues at the national level. Additionally, the law created the Alcoholic Drinks Control Fund, which consists of revenue generated from license fees and other related charges.

The Alcoholic Drinks Control Fund is primarily used to finance programs and activities related to alcohol regulation, research, and rehabilitation. The Fund supports research, documentation, and dissemination of information on alcoholic drinks, contributing to informed policymaking and public awareness.

5.3 Levies

1. Agriculture produces cess

The Agricultural Produce Cess (APC) is a tax levied on tradable commodities by county governments to raise revenue for the origin counties where the crops are grown. It applies to agricultural and fishing products that are commercially produced or supplied, such as maize, milk, cattle, vegetables, fish, fruits, coffee, tea, and flowers.

The funds generated from the cess are intended to improve physical infrastructure, such as roads and other assets that enhance agricultural production services and facilitate the marketing and distribution of these commodities. Before devolution, cess collection was reinforced through agricultural sector policies, such as the Kenya National Livestock Policy (2008) and the Kenya Meat Commission (Amendment) Act (1966), which outlined

cess rates and collection procedures.

The legal framework for cess collection changed after the introduction of devolution. The 2013 Agriculture, Fisheries, and Food Authority (AFFA) Act repealed the Agriculture Act, removing the legal basis for cess imposition. There is a lack of precise alignment regarding cess, leading to inconsistencies in its application. The absence of harmonized legislation has resulted in high and multiple charges, numerous collection points, and increased costs for producers and traders, which ultimately hurts the competitiveness of the agricultural sector. Additionally, different counties use varying units of measurement, such as tonnage, package size, vehicle type, or the number of trips, creating trade barriers within the country.

In Kenya, county financial bills, where agricultural cess and market levies are domiciled, have become the primary means of introducing new charges rather than addressing agricultural taxation through structured and harmonized laws. Each county has the discretion to determine the rate and computational formula for the fees based on prevailing laws and regulations. The rates may be in the form of a numeric value or percentage, with no clear justification for how they are determined. Regardless of the rate structure, the final amount payable is based on the volume and/or value of the tradable commodity.

2. Market access fee

This is a fee charged to traders of goods, animals, or any other products to enable them to transact their business within the county markets.

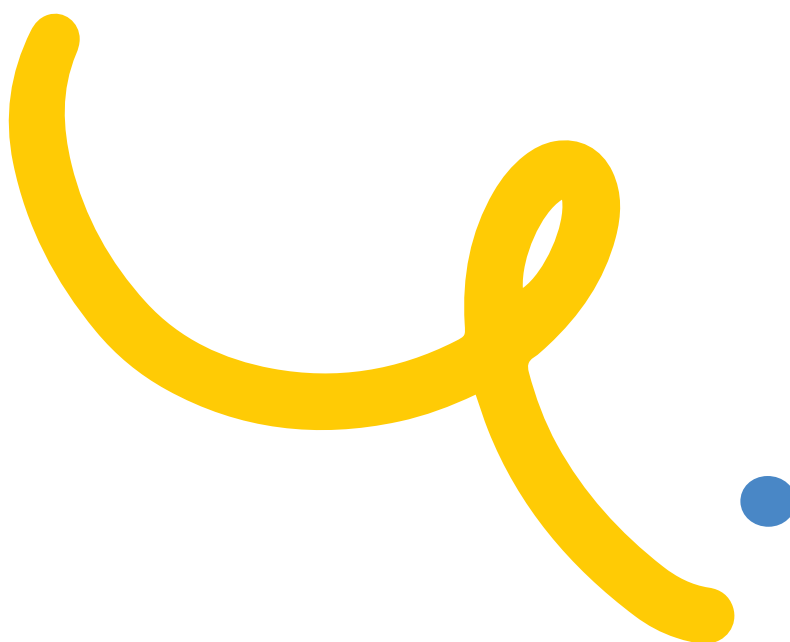
The specific objectives of levying market fees are to:

- i. Mobilize resources for providing services at the market.
- ii. Develop and maintain market infrastructure.

Market access fees vary depending on factors such as the type of goods being sold, the size of the trading space occupied, and whether the trader operates in a formal market structure or an open-air market.

Key Takeaways

- ODS empowers county fiscal autonomy and service delivery under Article 209.
- Key revenue streams: Taxes (like property), fees/charges (e.g., business permits, parking), and levies (e.g., cess, market fees).
- Main challenges include weak legal frameworks, outdated systems, multiple/higher charges, and poor enforcement.
- We need to harmonize laws, digitize systems, strengthen transparency, and adopt fair/efficient collection practices.



6. Contemporary Issues in Taxation





6.1 Tax Expenditures

Objectives of the session

- Understand what tax expenditures are and how they work.
- Understand how tax expenditures are calculated.
- Know how to interpret tax expenditure numbers.

Resources needed

- Government of Kenya Tax expenditure reports
- A Review of Kenya's 2022 Tax Expenditures Report (a publication by IPF)

How to run the session

- Prepare a PowerPoint presentation on tax expenditures covering definition of tax expenditures, how tax expenditures are calculated and an overview of tax expenditures numbers in Kenya
- Instruct the trainees to log into the Global Tax Expenditures Database and Global Tax Expenditures Transparency Index websites
- Engage the trainees in a 20-minute group discussion during which they will discuss tax expenditure transparency gaps
- Give each group 5 minutes to present their findings in plenary, ensuring all trainees contribute their ideas on how to improve transparency in the use of tax expenditures
- Conclude the session by recapping the key takeaways, emphasizing the importance of understanding the policy implications of tax expenditures

6.1.1 What are tax expenditures?

Tax expenditures are the government's estimated revenue loss that results from giving tax concessions or preferences to a particular class of taxpayer or activity. They can take many forms, including **tax exemptions, tax deductions, tax offsets (or credits), and concessional tax rates or timing rules, such as accelerated depreciation of capital assets, that either reduce or defer a taxpayer's tax liability.**^{xli} A typical example: personal tax relief that every

person who pays Personal Income Tax enjoys in Kenya.

6.1.1.1 Why do tax expenditures matter?

Tax expenditures are functionally the same as government spending; they cost money through lost revenue. It is important to assess their value in policy terms, just as we do with other parts of the budget so that they are effective, efficient and equitable.

6.1.2 How are tax expenditures calculated

Unlike a spending budget, where every expenditure item is an act of will to spend money, **a tax expenditure is a decision not to collect a tax.**^{xlii}

But to define this, we need some standard against which to measure our decisions; otherwise, there is no logical limit to what might count as a tax expenditure. For example, the government does not tax the air we breathe. Does that mean that there is a tax expenditure on air? Obviously, not. Tax expenditures must be relative to what we take to be "normal" taxation. The way that this is usually determined, is to decide on what the "benchmark" tax system is, and then look for deviations from it.

There are three approaches to defining tax expenditures and the benchmark tax system:

- **The reference tax law** takes a country's tax system as the starting point of defining the benchmark and defines a tax expenditure as an explicit concession that departs from the applicable tax provision.

- **The conceptual approach** defines a normative benchmark tax system guided by a theoretical concept of comprehensive income or consumption that provides guidance on how policy should be defined, irrespective of whether the benchmark corresponds to the existing tax law.
- **Expenditure subsidy approach** where the government only costs tax incentives that are clearly analogous to an expenditure subsidy. What are the policy implications of tax expenditures?

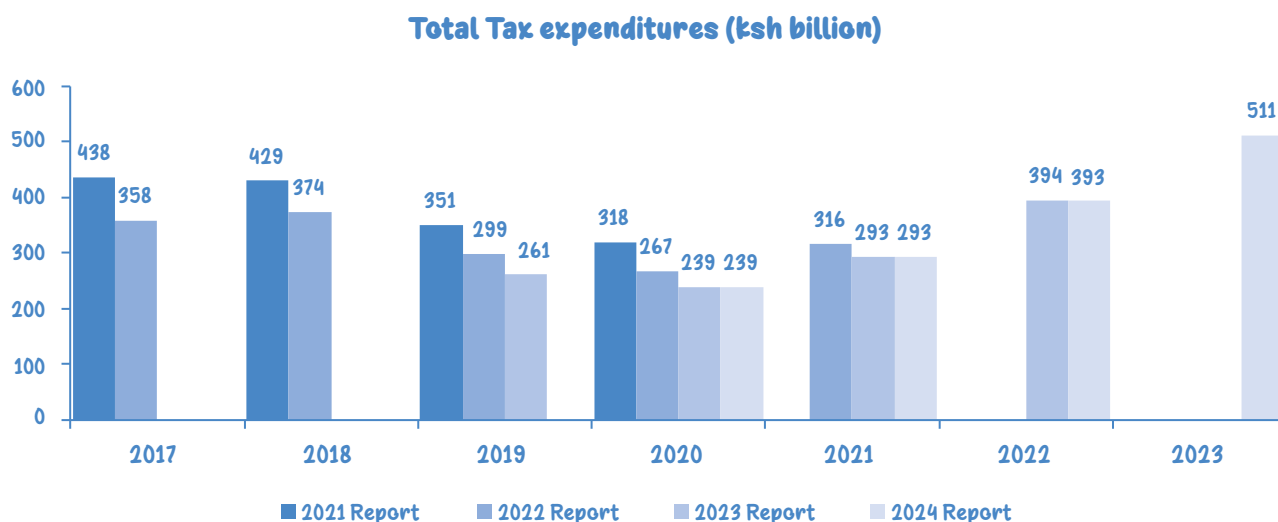
Refer to Annex III in the 2024 Tax Expenditure Report for preferential measures that are not tax expenditures.

The government of Kenya uses the tax law approach to define tax expenditures and the benchmark tax system. It defines tax expenditures as **"tax foregone due to explicit concession that departs from what is considered as a generally applicable tax provision under the existing tax law and is meant to achieve a specific socio-economic outcome"** and a benchmark as **"a baseline against which a tax expenditure is recognized as a standard tax treatment at international standard or in Kenya and not conferring preferential treatment to particular group of taxpayers."**

6.1.3 What is the size of tax expenditure in Kenya?

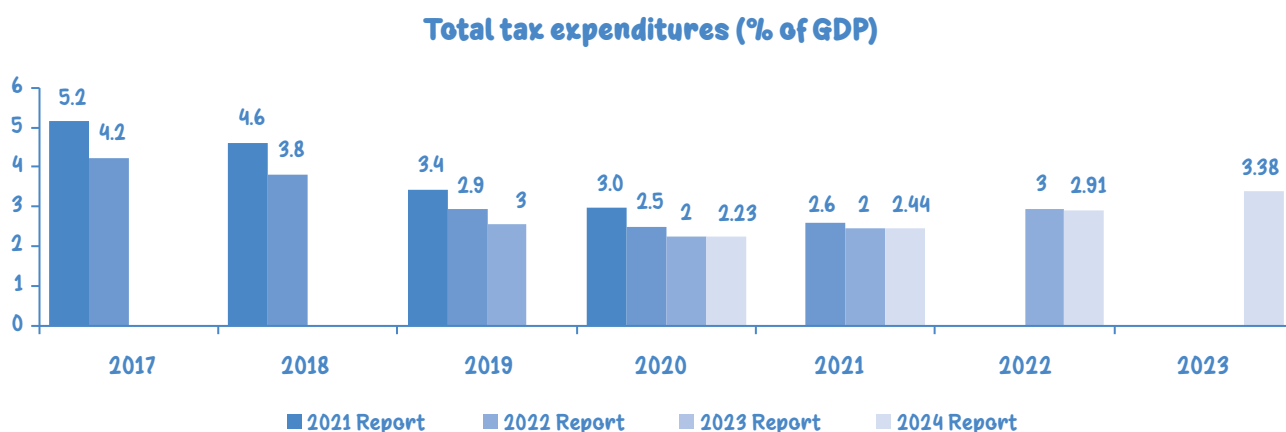
Tax expenditures increased between 2020 and 2023, both in nominal terms and as a percent of GDP, from Ksh 239 billion (2.3 percent of GDP) to Ksh 511 billion (3.4 percent of GDP) (Figure 11 and Figure 12).^{xliii}

Figure 7: Total Tax expenditures (Ksh billion)



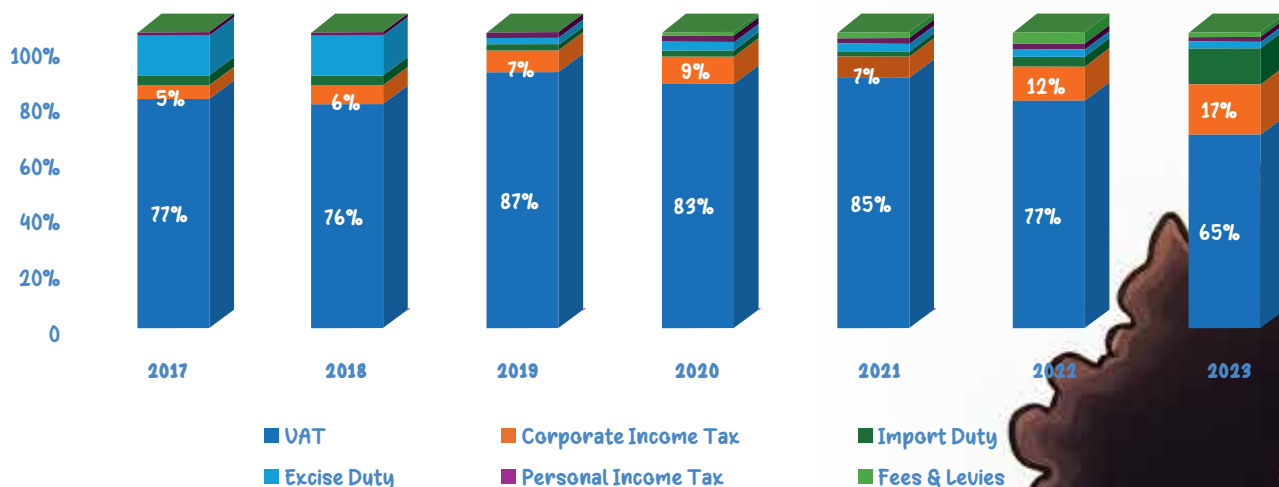
Comparing numbers from different years and from different reports, it is evident that changes in the benchmark has caused changes in these numbers. However, from the reported numbers we cannot tell what component was caused by change in benchmark or by policy changes.

Figure 8: Total tax expenditures (% of GDP)



In terms of composition, VAT TEs account for more than 65% of TEs in Kenya



Figure 9: TE's shares by revenue head**Key takeaways**

- Tax expenditures are government revenue losses from tax concessions; they are a policy choice to not collect revenue. They are akin to direct government spending and should be assessed for efficiency, effectiveness, and equity.
- Tax expenditures are measured against a benchmark tax system, with Kenya using the tax law approach to define and calculate them.
- Kenya's tax expenditures rose from Ksh 239 billion (2.3% of GDP) in 2020 to Ksh 511 billion (3.4% of GDP) in 2023, with VAT accounting for over 65%.
- Transparency, clear policy objectives, and regular evaluation are essential to ensure tax expenditure contributes effectively to economic growth.

6.2 International Taxation Frameworks**6.2.1 Oecd Inclusive Framework****6.2.1.1 What/Who is the OECD?**

The Organization for Economic Co-operation and Development (OECD) is an international organization that works to build better policies for better lives.^{xliiv} It draws on more than 60 years of experience and insights to shape policies that foster prosperity and opportunity, underpinned by equality and well-being. The OECD has 38 members.



The OECD, through data analysis:

- Aims at improving economic performance
- Aims at fighting international tax evasion and tax avoidance.

Tax evasion is the deliberate attempt not to pay tax where it is due, while **tax avoidance** is taking advantage of legally available tax planning opportunities to minimize one's tax liability.

6.2.1.2 Who/What is the G20?

Group Twenty (G20) is the premier forum for international economic cooperation. It plays an important role in shaping and strengthening global architecture and governance on all major international economic issues. The G20 members represent around 85% of the global GDP, over 75% of global trade, and about two-thirds of the world population. The G20 has 21 members: 19 countries and 2 International Organizations (the European Union and African Union). The G20 discusses:

- Economic and financial coordination
- Climate Change
- Global Healthcare.

6.2.2 What is the OECD Inclusive Framework?

The **OECD Inclusive Framework on Base Erosion and Profit Shifting (BEPS)** (when companies avoid taxes by exploiting gaps in the international tax rules)

This global initiative that brings together over **140 countries and jurisdictions** to:

- Tackle tax avoidance by multinational enterprises.
- Improve the coherence of international tax rules.
- Ensure a more **fair and transparent** international tax system.

It is called 'inclusive' because developing and developed countries alike can work together on an equal footing, unlike traditional OECD initiatives. Members work in unison to implement measures to curb Base Erosion and Profit Shifting.

6.2.3 The Development of OECD Inclusive Framework in Kenya

Digitalization and globalization have had a significant impact on commerce and livelihoods across the world. This has come with complex challenges to the tax structures and rules especially with the rise of global Multinational companies which are highly digitized. These entities operate and derive profits from jurisdictions where they don't necessarily have a physical presence. This has made it difficult for governments especially developing and underdeveloped countries to obtain tax revenues from these Multinational entities.

The OECD in an effort to strengthen international tax systems, to make it more responsive to current trade practices and tackle tax avoidance came up with the Base Erosion and Profit Shifting initiative, an inclusive framework that welcomed the participation of multiple countries including Kenya that were not members of the OECD in an effort to ensure participation on an equal footing for all countries to ensure a more transparent environment.^{xlv} Kenya joined the Inclusive Framework in 2017.

The OECD Inclusive Framework initiative-The Statement came up with a two-pillar proposal that included:

- Pillar one rules create a new taxing right in market jurisdictions like Kenya that go beyond the current physical presence rules currently embodied in domestic laws.
- Pillar two introduces a global minimum tax which would ensure multinational corporations pay a minimum amount of tax with respect to their global profits.

Many developing countries, Kenya included did not join, the primary concern being these countries already had in place unilateral regimes such as the digital service tax which worked and helped expand the revenue base. Other concerns raised by Kenya included:

- The OECD proposed a global minimum tax rate

of 15% which Multinationals must pay. Kenya considered this rate to be too low and proposed a higher rate of 20%.

- Joining the consensus of the two-pillar solution, Kenya would have to forgo the digital service tax they had already implemented, although pillar one of the Inclusive Framework would mean allocation of 100 billion dollars it is uncertain how much of that money Kenya would receive, if any.

Amidst these concerns Kenya acknowledges the need to remove unilateral measures to realize flexibility in tax administration, simplicity in tax administration and cooperation in assertion of tax sovereignty.

Kenya is yet to sign on the OECD two pillar framework and has made proposals to the OECD which include the following:

- To bring more companies within the scope of the jurisdiction.
- Developing countries to retain taxing rights on Digital service Tax for out-of-scope companies.
- Allow for a non-binding arbitration process.

Kenya is committed to international cooperation in taxation matters, a key part of the country's tax diplomacy profile over the years. Continuous stakeholder engagement is part and parcel of this endeavor. The future is brighter, and Kenya is looking forward to being part of the deal sooner than expected.

6.3 Environmental Taxes and their Role in Climate Change and Revenue Generation

Objectives

- Define environmental taxes and explain their purpose.
- Analyze the core objectives of environmental taxes: climate change mitigation versus revenue generation.
- Discuss existing environmental taxes and climate finance initiatives in Kenya.
- Engage in interactive discussions and policy

simulations on environmental taxation.

Resources needed

- ATAF environmental taxation handbook
- Climate change Act
- The Climate Change (Carbon markets) Regulations, 2024
- Excise duty Act
- Finance bill 2024
- Carbon trading Blog. [link](#)

How to run the session

- Start with warm-up questions. Perhaps using a poll to collect answers to gauge the level of understanding among the participants.
- Deliver a 30-minute PowerPoint presentation on environmental taxes: definition, types, global and Kenyan examples, and objectives (climate vs. revenue).
- Instruct trainees to visit the Kenya law website to search for references to environmental or green taxes.
- Illustrate practical examples of how environmental taxes (e.g., fuel levy, plastic ban) are applied or could be improved in Kenya.
- Divide participants into small groups for a 20-minute discussion on how environmental taxes could work in Kenya and how it can navigate the political economy and give 2-3 mins for presentation.

6.3.1 What Are Environmental Taxes?

Environmental taxes are fiscal tools designed to encourage sustainable practices by imposing costs on environmentally harmful activities.^{xlvii} These taxes aim to reduce pollution, conserve resources, and generate revenue that can be reinvested in environmental and social programs. Environmental taxes follow the "polluter pays" principle, ensuring that those who cause environmental harm bear the cost. Examples include import tariffs on plastic material, charges on traffic congestion, excises on fertilizers, fishing levies, deforestation taxes, and carbon taxes. These taxes are widely promoted to reduce environmental damage while raising

revenue from polluters.

6.3.1.1 Key Characteristics

- Target activities that contribute to pollution and resource depletion.
- Aim to change behaviour rather than just raise revenue.
- Encourage investment in clean energy and sustainable practices.

6.3.1.2 Examples of Environmental Taxes around the World

- **Carbon Taxes:** A carbon tax is a fee on carbon emissions from burning fossil fuels, aimed at reducing greenhouse gas emissions. It creates economic incentives for cleaner energy use and generates revenue for environmental and social programs. Many countries, including South Africa, Sweden, Norway, and Canada, impose taxes on carbon emissions to reduce greenhouse gas emissions. These taxes are applied to fossil fuels based on their carbon content.
- **Plastic Bag Taxes:** Nations like Ireland have introduced taxes on plastic bags to reduce plastic waste and encourage the use of reusable bags.
- **Vehicle Emission Taxes:** Countries such as Germany and the UK levy taxes on vehicles based on their emissions, promoting the use of cleaner and more efficient vehicles.
- **Waste Disposal Taxes:** In countries like the Netherlands, taxes are imposed on waste sent to landfills to encourage recycling and waste reduction. On the other hand, Norway has a waste Incineration tax intended to internalize the cost of environmental pollution.
- **Energy Taxes:** Denmark and Finland tax energy consumption, including electricity and heating fuels, to promote energy efficiency and renewable energy sources. Similarly, South Africa introduced a carbon tax in 2019 to discourage excessive carbon emissions and encourage businesses to adopt cleaner energy alternatives.

6.3.1.3 Purpose of Environmental Taxes

- **Mitigate Environmental Damage** – These policies discourage pollution and promote sustainability by imposing taxes on activities that harm the environment.
- **Generate Government Revenue** – Environmental taxes provide funds that can be reinvested in green initiatives, infrastructure, and social programs.
- **Encourage Sustainable Practices** – They incentivize businesses and individuals to adopt eco-friendly alternatives, such as renewable energy and efficient resource use.
- **Implement the Polluter Pays Principle** – Ensuring that those responsible for environmental harm bear the cost of their actions.
- **Address Market Failures** – By internalizing the external costs of pollution, environmental taxes help correct market inefficiencies.

6.3.1.4 Challenges and Criticisms of Environmental Taxes

- **Economic Burden on Lower-Income Groups:** Higher energy and fuel costs can disproportionately affect vulnerable populations, making essential goods and services more expensive.
- **Impact on Industries:** Sectors heavily reliant on fossil fuels may face high compliance costs, which could potentially affect economic growth.
- **Effectiveness Concerns:** Some taxes primarily serve as revenue-generating tools rather than direct disincentives for pollution.
- **Elasticity of Demand:** In cases where alternatives are costly or unavailable, behavior change may be limited.
- **Regulatory and Enforcement Issues:** Weak institutional frameworks and poor monitoring can lead to tax evasion and limited compliance.
- **Compliance Costs:** Businesses may face higher operational expenses due to regulatory requirements, which can affect competitiveness, especially for small and medium-sized enterprises (SMEs).

6.3.2 What different forms of environmental tax

exist?

Environmental taxes can be categorized into four main dimensions: energy, transport, pollution and resources.^{xlviii} These taxes play a crucial role in promoting sustainability by aligning economic activities with environmental goals.

Energy Taxes

- Carbon taxes on fossil fuels
- Electricity consumption taxes.
- Transport Taxes
- Vehicle emission taxes
- Congestion charges
- Fuel taxes.

Pollution Taxes

- Waste disposal taxes
- Industrial emission charges

Resource Taxes

- Timber extraction fees
- Waste usage charges
- Mining levies

6.3.3 What is the Core Objective of Environmental Taxes? Climate Change or Revenue Generation

The foremost aim of environmental taxes is to reduce environmental harm by internalizing the costs of pollution and resource depletion. These taxes ensure that those who contribute to environmental degradation bear the financial responsibility for their actions, thereby encouraging cleaner production and consumption practices.

While revenue generation is not the primary goal of environmental taxation, it is a significant byproduct. The funds collected from these taxes can be used to finance climate adaptation and mitigation projects, such as renewable energy investments and environmental conservation programs. Support vulnerable populations affected by climate policies, ensuring a just transition to greener economies as well as offset other taxes, such as reducing income or labor taxes, to maintain economic balance and competitiveness.

A well-designed environmental tax system

should prioritize climate change mitigation and environmental sustainability while ensuring that revenue generation supports long-term ecological and economic goals.^{xlviii} Ideally, as these taxes succeed in reducing pollution and resource depletion, their revenue may decline over time, indicating a positive shift toward a cleaner economy. The success of these taxes is ultimately measured not by the revenue they generate but by their effectiveness in fostering a low-carbon, resource-efficient, and environmentally responsible economy.

Case Study Reviews: Review Norway's, Sweden's and South Africa on environmental taxation

Activity

Discussion Questions:

Which approach should Kenya prioritize, climate change or revenue generation?

How can Kenya balance the two objectives effectively?

6.3.4 Do we have Environmental Taxes in Kenya?

Kenya does not have direct environmental taxes but has tried to implement several interventions to address climate concerns. Key measures include:

- **Excise Duty on Plastic Bags:** Despite Kenya's 2017 ban on plastic bags, an excise duty on plastic packaging materials remains in place to further discourage plastic use and promote sustainability. Manufacturers and importers are required to pay a levy of 25% or KSh 200 per kilogram, whichever is higher, on imported self-adhesive plastic materials and plastic plates. This tax increases the cost of plastic production, pushing businesses toward eco-friendly alternatives like biodegradable packaging.
- **Excise Duty on Carbonated Drinks and Plastics:** In Kenya, beverages packaged in plastic bottles, such as carbonated drinks, are subject to excise duty to reduce plastic waste and promote sustainable packaging alternatives. According to the Excise Duty Act, fruit and vegetable juices attract a levy of KSh. 14.14 per litre, while bottled

water and other non-alcoholic beverages (excluding juices) are taxed at KSh. 6.41 per litre.

^{xlix} This tax measure discourages plastic use while encouraging manufacturers to adopt eco-friendly packaging solutions.

- **Excise Duty on Motor Vehicles:** In Kenya, excise duty on motor vehicles is based on engine capacity to discourage fuel-inefficient and high-emission vehicles. According to the Kenya Revenue Authority (KRA), vehicles with engine capacities exceeding 1,500 cc but not exceeding 3,000 cc are taxed at 25% of the Customs Value plus Import Duty, while those exceeding 3,000 cc attract a 35% excise duty. This tiered taxation system aims to promote environmental sustainability by encouraging the use of smaller, fuel-efficient vehicles to reduce emissions and fuel consumption.
- **Excise Duty on Fossil Fuels:** Taxes are levied on petroleum products to discourage excessive use and promote cleaner energy alternatives. The Petroleum Development Levy (PDL) and the Road Maintenance Levy (RML) function as indirect environmental taxes by influencing fuel consumption and emissions. The PDL, established under the Petroleum Development Fund Act of 1991, is primarily used to stabilize fuel prices, but it also supports energy projects that promote cleaner and more sustainable fuel use. The RML, governed by the Kenya Roads Act, 2007, funds road maintenance while indirectly discouraging excessive fuel consumption by increasing fuel costs, thus reducing emissions and promoting environmental sustainability.
- **Waste Management Fees:** County governments impose fees for waste collection and disposal to encourage proper waste management practices.
- **E-Waste and Hazardous Waste Management Fees:** The National Environment Management Authority (NEMA) enforces regulations for the responsible management of electronic and hazardous waste. Companies involved in producing or importing electrical and electronic equipment must register with NEMA and pay prescribed fees. According to the Draft E-Waste

Regulations, the application for registration requires payment of a prescribed fee as set out in Schedule 13. Additionally, businesses handling hazardous waste must obtain licenses from NEMA, with fees specified in the Waste Management Regulations, 2006. These measures aim to promote environmentally sound practices in waste management.

- **Environmental Impact Assessment (EIA) Fees:** The National Environment Management Authority (NEMA) requires project proponents to conduct an Environmental Impact Assessment (EIA) before initiating projects. The fee for obtaining an EIA license is 0.1% of the total project cost, with a minimum charge of KSh. 10,000 and no upper limit.
- **Environmental Management and Coordination (EMCA) Regulations:** Under the Environmental Management and Coordination Act (EMCA) of 1999, NEMA has established various regulations that may include fees and charges to ensure environmental compliance.
- **Green Energy Tax Incentives:** Kenya promotes renewable energy investments through various tax incentives and policies aimed at reducing reliance on fossil fuels. Under the Investment Allowance provisions, businesses can claim capital expenditure deductions for renewable energy projects, with an initial deduction of 50% in the first year, followed by 25% per year on a reducing balance basis. Additionally, the government has implemented a Feed-in-Tariff (FiT) policy to encourage renewable energy generation by guaranteeing fixed payments for electricity produced from sources like wind and solar, ensuring stable returns for investors. These measures aim to foster a conducive environment for clean energy investments and promote environmental sustainability.

6.3.4.1 Proposed environmental taxes

Eco Levy (Proposed in Finance Bill 2024): The Finance Bill 2024 planned to introduce an Eco Levy targeting manufacturers and importers of products such as diapers, rubber tires, and electronics.

The levy aimed to fund waste management infrastructure and promote eco-friendly practices. It was among the contentious issues that led to the withdrawal of the 2024 Finance Bill.

Environmental Restoration Levy (Proposed):

In 2024, the Ministry of Environment proposed an Environmental Restoration Levy on all imported finished products to fund environmental restoration efforts.

6.3.5 What Other Climate Finance Initiatives Exist in Kenya

Beyond environmental taxes, Kenya has implemented climate finance initiatives to support sustainability.

1. Carbon Trading & Offsets

The Climate Change Regulations, 2024, establish a legal framework for the development and management of carbon projects, thereby governing carbon trading and offset mechanisms in Kenya¹. These regulations outline the procedures for registering and implementing carbon offset projects, ensuring they adhere to national standards and contribute to sustainable development. By participating in carbon markets, companies can invest in emission reduction initiatives, effectively offsetting their carbon footprint and supporting Kenya's climate change mitigation efforts. The regulations also provide for the establishment of a carbon registry to record all carbon projects, enhancing transparency and accountability in the carbon market.

2. Green Bonds

Green bonds are financial instruments issued to raise capital exclusively for projects that generate environmental benefits, such as renewable energy and sustainable infrastructure. Kenya achieved a significant milestone in 2019 in sustainable finance with the issuance of its inaugural green bond by Acorn Holdings Limited. This KES 5 billion Medium-Term Note (MTN) programme was designed to finance environmentally friendly student housing projects in Nairobi.¹¹ The first tranche, issued in

October 2019, raised KES 4.262 billion, surpassing the KES 2 billion minimum target. The bond had a 5-year term with a 12.25% coupon rate, maturing in October 2024. In October 2024, following the successful early redemption of the outstanding KSh. 2.6888 billion, the bond was delisted from the Nairobi Securities Exchange (NSE). The initiative addressed the student housing shortage and set a precedent for sustainable financing in Kenya's capital markets.

3. Climate Bonds

Climate bonds are fixed-income instruments designed to fund projects that mitigate or adapt to climate change, such as renewable energy, sustainable transport, and climate-resilient infrastructure. Climate bonds finance projects that actively cut carbon emissions or help mitigate climate change impacts, while green bonds support environmentally sustainable and socially responsible projects, aiming for positive environmental outcomes. Issued by governments, corporations, or financial institutions, they function like traditional bonds but are dedicated to environmentally sustainable initiatives. Often certified under international standards like the Climate Bonds Initiative (CBI), these bonds ensure transparency and credibility. By attracting private and institutional investment, climate bonds help bridge the climate finance gap and support the transition to a low-carbon economy.

4. Climate Adaptation Fund

Kenya supports vulnerable communities through climate adaptation initiatives such as the Integrated Programme to Build Resilience to Climate Change, implemented by NEMA, which enhances climate-resilient agriculture, water management, and disaster risk reduction. Additionally, the County Climate Change Fund (CCCF) facilitates access to climate finance for locally led adaptation projects, integrating climate resilience into county development plans.

5. Public-Private Partnerships (PPPs)

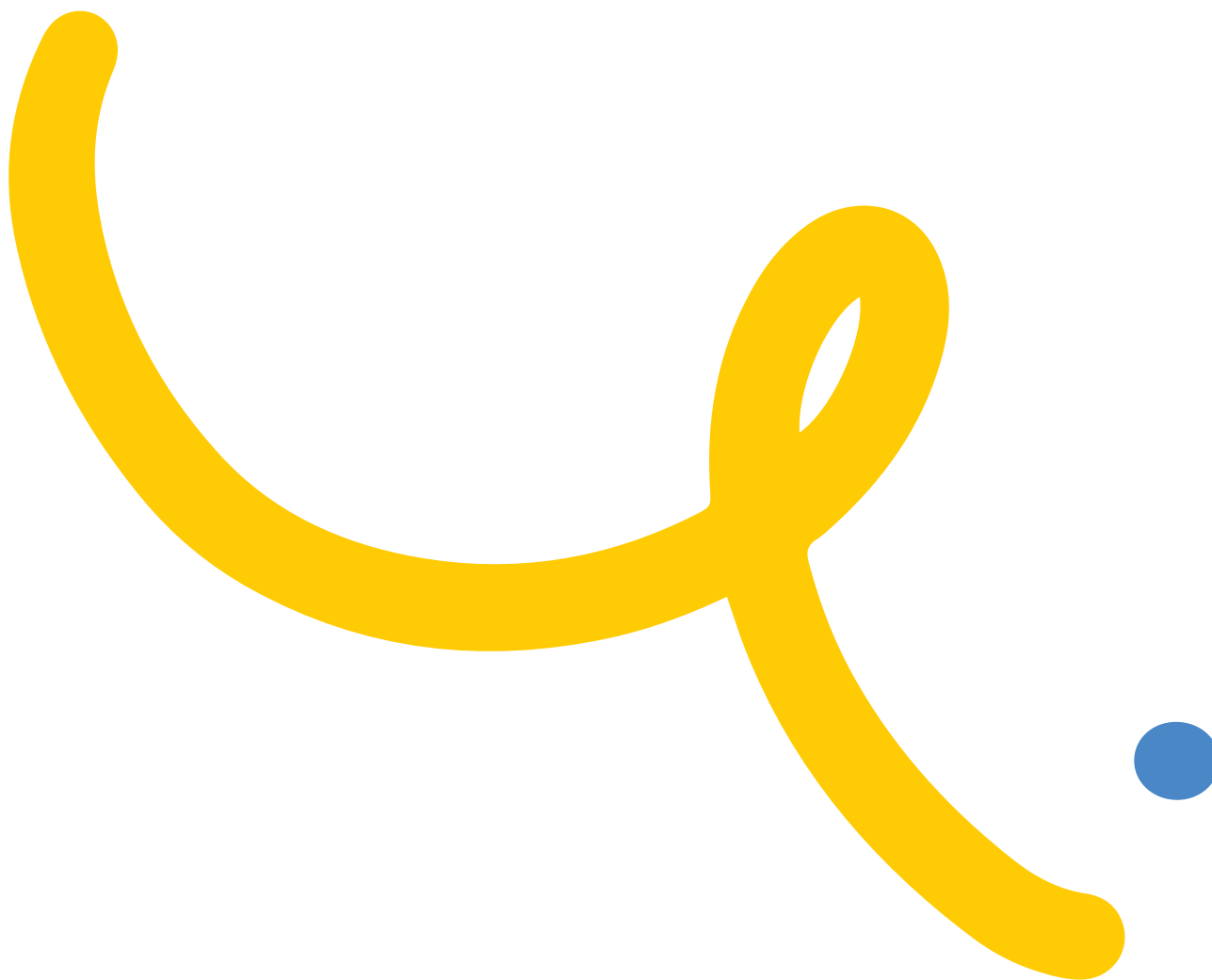
Kenya has leveraged Public-Private Partnerships (PPPs) to promote renewable energy and reduce reliance on fossil fuels. A key example is the Lake Turkana Wind Power Project (LTWP), Africa's largest wind farm, generating 310 MW of clean energy, approximately 14% of Kenya's electricity supply, powering 1.2 million homes.^{lii} Developed through a KSh 52.1 billion PPP agreement, LTWP significantly reduces carbon emissions by replacing thermal power generation. Such

initiatives demonstrate how PPPs drive large-scale renewable energy investments, enhancing environmental sustainability and mitigating climate change.

Summary of Key Points

Environmental taxes discourage pollution and generate revenue.

Kenya has implemented various forms of indirect environmental taxes and climate finance initiatives. A balance is needed between revenue generation and climate action.



7. Decoding The Finance Bill



Session objectives

At the end of the session, the students will have:

- Learned the central role of the Finance Bill (FB) in Kenya's public finance.
- Clarified misconceptions about the Finance Bill.
- Understood the Finance Bill process and its impact on tax laws and policies.
- Identified key tax changes introduced by the Finance Bill and assessed their impact on different economic sectors and demographics.
- Developed skills in analyzing and drafting a memorandum for public participation.

Resources needed

To run this session, you will need:

- Facilitation Plan
- Pre and post-surveys
- The Constitution of Kenya 2010
- Finance Act 2023
- Finance Bill 2024
- Relevant articles for advanced and post-session reading: IEA, ICPAK and others.
- Sample memorandum submitted to Parliament

- Links to Parliamentary website for tracking Finance Bill debates and public hearings

How to run the session

1. Pre and post-surveys (10 mins)

- Administer pre-survey to assess participants' understanding of the Finance Bill.
- Conduct post-survey to measure knowledge gain.

2. Presentation with Slides (20 mins)

- The Central Role of FB in PFM: How the Finance Bill influences revenue collection and fiscal policy.
- Countering Misinformation and Disinformation in the Finance Bill Process: Clarifying what the Finance Bill is and is not.

The Process of Enacting the Finance Bill: Step-by-step breakdown from drafting to enactment.

The Impact of the Finance Bill on Taxation: How proposed changes affect key taxes laws with reference to: Income Tax, VAT, and Excise Duty.

Analysis and Participation in the Finance Bill Process: How to develop and submit an effective memorandum.

Exercises

1. Breakout Session 1 – How to Read and Analyze your National and County Finance Bill (40 mins)

- Divide participants into groups 8–10.
- Assign each group either the Finance Bill 2023 or 2024.
- Use a predetermined guide to assess the Nation Government Finance Act 2023

o Identify the fundamentals of the Finance Act

o Substantive review of the Finance Act 2023

- Plenary presentations and feedback (20 mins): Each group presents a 5-minute summary.

2. Breakout Session 1 – Reviewing tax changes (40 mins)

- In the same groups as Breakout 1:
- Assign each group either the Finance Bill 2023 or 2024.
- Discuss the top three changes the Finance Bill introduced to:

o Income Tax Act

o Value Added Tax Act

o Excise Duty Act

- Identify the intended policy outcomes of these changes

- Plenary presentations and feedback (20 mins): Each group presents a 5-minute summary.

3. Breakout Session 2 – Assessing impact & drafting a Memorandum (30 mins)

- In the same groups as Breakout 1:

o Assess the impact of the tax changes on different economic sectors, including SMEs, low-income earners, and the informal sector.

o Discuss who benefits and who loses from these changes.

o Propose alternative recommendations for tax policy.

o Suggestion key consideration to include in drafting of a brief memorandum for submission.

- Plenary presentations and feedback (20 mins): Each group presents a 5-minute summary.

Handouts (Copies)

- Finance Bill 2023 or 2024
- The Constitution of Kenya 2010
- Sample memorandum submitted to Parliament
- Relevant articles for advanced and post-session reading
- Template for drafting a memorandum.

7.1 The Central Role of the Finance Bill in Public Finance Management (PFM)

7.1.1 Background to the Finance Bill

The Finance Bill plays a crucial role in shaping Kenya's tax framework, directly influencing the business environment, investment decisions, and financial obligations of citizens. It is a legal requirement under the Public Finance Management Act (PFMA), 2012, serving as the primary tool for implementing the government's revenue-raising measures.

Under Section 39A of the PFMA, the Cabinet Secretary for the National Treasury must make a public pronouncement on budget policy highlights and **propose revenue-raising measures** for the national government. The Cabinet Secretary must also consider any regional or international agreements ratified by Kenya, including the East African Community Treaty. Where such agreements specify a date for budget policy pronouncements, the Cabinet Secretary must ensure that the measures are announced on the designated date.

Following this, the Cabinet Secretary is required to submit the Finance Bill to Parliament for consideration.

Parliament then has up to 90 days (as stipulated in Section 40 of the PFMA) to scrutinize, debate, and approve the Bill, with or without amendments. This process ensures that taxation and fiscal policies are subjected to:

- Legislative oversight
- Public participation
- Alignment with national economic priorities

7.1.2 What is the Finance Bill?

The Finance Bill is a legislative proposal that introduces changes to tax and revenue-related laws to implement the government's fiscal policies.^{liii} It provides the legal framework for raising revenue to finance the national budget for the upcoming fiscal year. To achieve this, the Finance Bill proposes amendments to existing tax laws, including:

- Income Tax Act (Cap. 470)
- Value Added Tax (VAT) Act, 2013
- Excise Duty Act, 2015
- Tax Procedures Act, 2015

These amendments may involve:

- Adjustments to tax rates and brackets
- Introduction of new taxes or levies
- Modifications to deductions, exemptions, and tax credits
- Changes to tax administration and enforcement procedures

Additionally, the Finance Bill may outline **measures by the Kenya Revenue Authority (KRA)** to enhance revenue collection, such as:

- Strengthening tax enforcement mechanisms
- Introducing new compliance requirements
- Streamlining tax payment processes



1.1 Important!

The Finance Bill is not a standalone tax law but rather an omnibus legislation that amends multiple existing tax laws governing taxation and revenue administration.¹⁰ It serves as an annual legislative tool through which the government adjusts tax policies, rates, exemptions, and compliance measures to align with its fiscal objectives.

Understanding the role of the Finance Bill

1. Collection of amendments: The Finance Bill introduces modifications to various tax laws, including the Income Tax Act (Cap. 470), the Value Added Tax (VAT) Act, the Excise Duty Act, and the Tax Procedures Act. These amendments can adjust tax rates, introduce new levies, or revise administrative procedures.
2. Not a law until passed: The Finance Bill only becomes law once it has been debated, approved by Parliament, and assented to by the President, at which point it is enacted as the Finance Act. Until this happens, existing tax laws remain in force.

Does the government stop collecting taxes without a Finance Bill?

To explain the omnibus nature of the, even in the absence of a new Finance Bill, tax collection continues under the existing tax laws. For instance:

- Income tax: Salaries, business profits, and corporate earnings will still be taxed as per the existing Income Tax Act (Cap. 470).
- VAT: Goods and services will continue to attract VAT at the rates established in the VAT Act, 2013 unless amended.
- Excise Duty: Taxes on alcohol, fuel, and other excisable goods will still apply under the Excise Duty Act, 2015.
- Tax administration: The Kenya Revenue Authority (KRA) will continue enforcing tax compliance under the Tax Procedures Act, 2015.

Why is the Finance Bill important?

- While tax collection does not depend on the Finance Bill, this legislation is critical because it:
- Adjusts tax policies to respond to economic needs
- Introduces new revenue measures to meet budgetary requirements
- Provides tax incentives or exemptions to stimulate economic growth
- Ensures alignment with regional and global tax standards

Thus, the Finance Bill is not the foundation of tax collection but rather a key instrument for fiscal policy adjustments each year.

7.3 The legislative process of a Financial Bill

The legislative process of the Finance Bill in Kenya follows a structured parliamentary process,¹¹ typically involving seven key stages, from introduction to enactment. This process ensures thorough parliamentary scrutiny, public participation, and potential amendments before implementation. The stages align with the **Constitution of Kenya (2010)** and parliamentary procedures, promoting transparency, fiscal responsibility, and legal compliance. In some cases, two additional stages apply: if the Bill affects county governments, it proceeds to the Senate (**eight stages**); if the President refers it back to Parliament, reconsideration introduces another step (**nine stages**).

Here's a breakdown of the key legislative stages:

7.3.1 Pre-Legislative stage (Formulation & drafting)

The National Treasury develops the Finance Bill based on fiscal policy proposals outlined in the Budget Policy Statement (BPS) and Annual Budget Estimates. This stage may involve stakeholder consultations, including engagements with business groups, civil society organizations, and the public to gather input on proposed tax and revenue measures. Once the draft Finance Bill is finalized, it is submitted to the Cabinet for approval before being tabled in Parliament for legislative consideration.

First reading (Introduction in Parliament)

The Cabinet Secretary for the National Treasury formally submits the Finance Bill to the National Assembly, where it is read for the first time. This marks its official introduction to Parliament. At this stage, there is no debate or discussion—the Bill is simply tabled and made available for consideration.

in subsequent stages.

Second reading (General debate)

In the Second Reading stage of the Finance Bill, Members of Parliament (MPs) debate the broad policy issues rather than specific clauses. During this stage, MPs provide general opinions and recommendations before moving to the Committee stage, where specific clauses of the Finance Bill are scrutinized in detail. These broad policy issues typically include:

- 1. Revenue generation strategy** – How the proposed taxes align with the government's revenue targets and whether they will be sufficient to fund national and county budgets.
- 2. Economic growth and investment impact** – The effect of tax proposals on key economic drivers such as Small and Medium Enterprises (SMEs), Foreign Direct Investment (FDI), and industrial growth.
- 3. Tax burden and equity** – Whether the Finance Bill fairly distributes tax responsibilities across different income groups, ensuring progressivity and protecting vulnerable populations.
- 4. Inflation and cost of living** – How changes in Value Added Tax (VAT), excise duty, or income tax rates impact the cost of essential goods and services, affecting household disposable income.
- 5. Sector-specific impacts** – The implications for agriculture, manufacturing, services, and digital businesses, particularly in terms of taxation incentives or new levies.
- 6. Compliance and Tax administration** – The practicality of enforcing new tax measures, the efficiency of revenue collection agencies like the Kenya Revenue Authority (KRA), and potential risks of tax evasion.
- 7. Debt Sustainability and fiscal deficit** – Whether the proposed revenue measures help reduce reliance on public borrowing and support long-term fiscal stability.
- 8. Alignment with national development goals** – How the Bill aligns with Vision 2030, the Bottom-Up Economic Transformation Agenda (BETA), and other policy frameworks.

9. Public participation and stakeholder concerns

– Whether the Bill incorporates feedback from citizens, businesses, and civil society organizations.

10. Environmental and social considerations

– The impact of new taxes on environmental sustainability, such as green tax incentives or penalties for pollution.

7.3.2 Committee Stage (Clause-by-Clause Review)

At this stage, the Finance Bill is referred to the Departmental Committee on Finance and Planning, which undertakes a detailed review of its provisions. The Committee:

- Conducts public consultations, allowing citizens, businesses, civil society organizations, and other stakeholders to submit their views, often through memoranda and public hearings.
- Engages with government agencies such as the Kenya Revenue Authority (KRA) and the National Treasury to assess the technical and fiscal implications of proposed tax measures.
- Compiles a Committee Report, incorporating stakeholder feedback and policy recommendations.
- Presents the Committee Report to the National Assembly for consideration.

After this, the National Assembly sits as the Committee of the Whole House, where MPs:

- Scrutinize the Finance Bill clause by clause, debating each provision in detail.
- Consider and vote on proposed amendments based on the Committee's recommendations or MPs' submissions.
- Ensure that the Bill aligns with fiscal objectives, economic realities, and public concerns.

Once the clause-by-clause review is completed, the amended Finance Bill proceeds to the Third Reading for final approval.

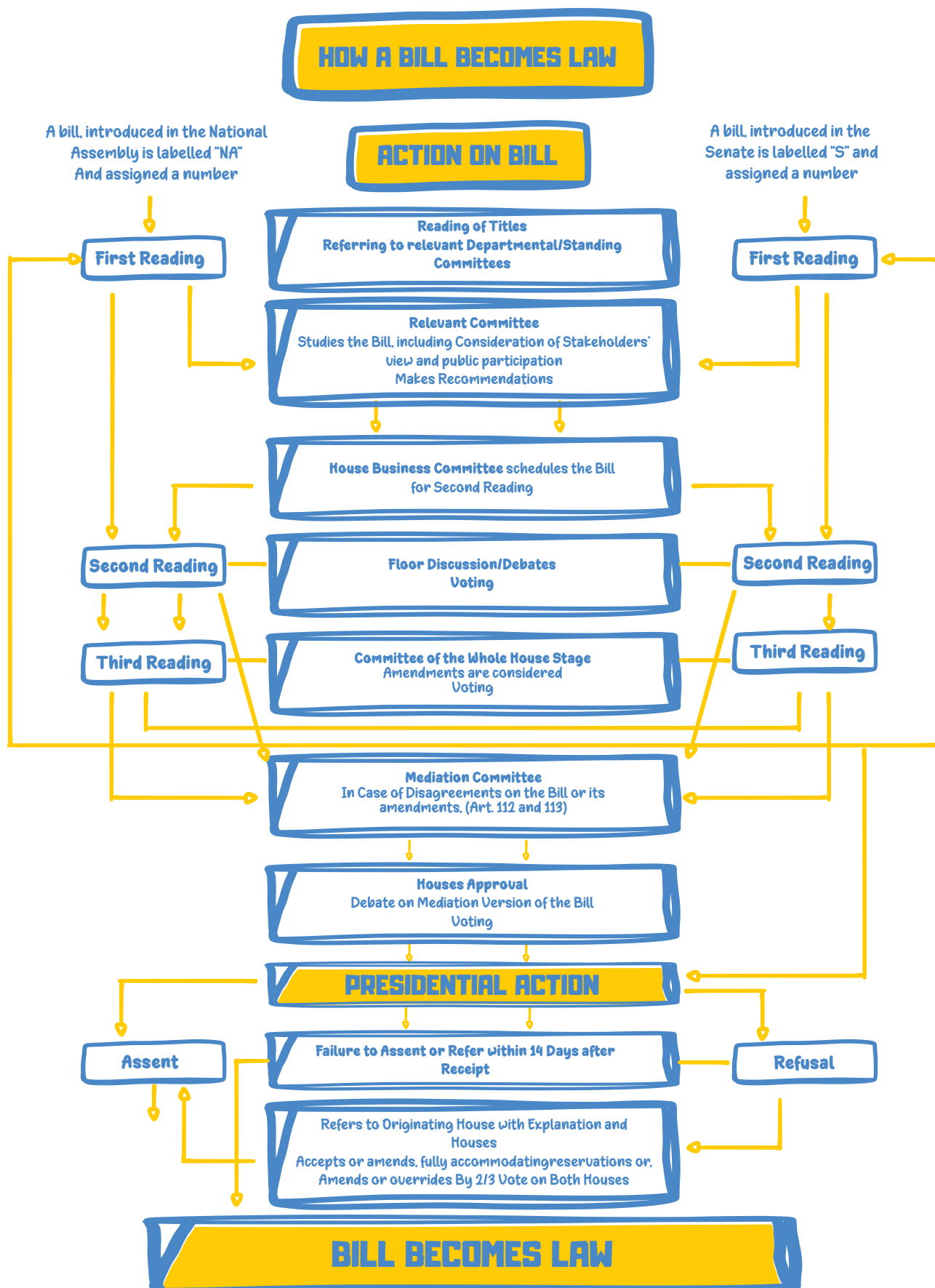
Third reading (Final approval by Parliament)

At this stage, the Finance Bill, as amended during the Committee Stage, is presented to the National Assembly for final approval. Members of Parliament (MPs) debate the refined version of the Bill, but only minor, non-substantive amendments (such as technical or drafting corrections) are permitted—no major policy changes can be introduced at this point.

If the Finance Bill contains provisions affecting county governments, it is referred to the Senate for consideration.

If the Bill does not affect counties, the Senate has **no legislative role** in its passage, and the Bill proceeds directly to the **Presidential Assent stage**.

Figure 10: Snapshot of the Legislative Stages of a Bill to a Law



Once approved by the National Assembly, the Finance Bill moves to the next step in the legislative process.

7.3.3 Senate Consideration (If applicable)

- If the Finance Bill has provisions affecting county finances, it is referred to the Senate for review.
- The Senate may approve, reject, or amend the Bill.
- If the Senate makes amendments, the Bill returns to the National Assembly for concurrence.

7.3.4 Presidential Assent & Enactment

Once Parliament approves the Finance Bill, it is submitted to the President for assent within 14 days. The President has two options:

1. Assent to the Bill, making it law—at which point it becomes the Finance Act.
2. Refer the Bill back to Parliament with reservations and proposed amendments.

If the Bill is referred, Parliament can:

- Incorporate the President's recommendations and pass the amended Bill.
- Reject the recommendations and override the President's reservations with a two-third majority vote, after which the Bill must be assented to.

In case of an Assent by the President the Bill, it is gazette, officially becoming law as the Finance Act, and its provisions take effect as stipulated.

7.3.5 Implementation & Monitoring

Once the Finance Bill is passed, the Kenya Revenue Authority (KRA) and other relevant government agencies take over the implementation process, enforcing the newly enacted tax measures.

Key steps in this phase include:

- Implementation of tax provisions as outlined in the Finance Act.
- Issuance of compliance guidelines and regulations to provide clarity on enforcement and adherence.
- Public awareness and stakeholder engagement,

including sensitization of businesses, taxpayers, and industry players on the new tax changes.

- Ongoing monitoring and assessment by stakeholders—including businesses, civil society, and economists—to evaluate the impact on businesses, individuals, and the broader economy.

Adjustments or clarifications may follow based on implementation feedback and emerging challenges.

7.3.5.1 Judicial interpretation or constitutional challenges

If certain provisions of the Finance Act are challenged in court and declared unconstitutional, Parliament may be required to amend the law to align with judicial rulings. One of the most common sources of such challenges is litigation, which can delay tax implementation, creating uncertainty for businesses and government revenue collection. The Affordable Housing Levy is an example here.

^(vi) The levy was initially declared unconstitutional by the High Court of Kenya in November 2023. The court ruled that the levy was improperly introduced through the Finance Act, 2023 and violated principles of taxation and public participation. However, the government later reintroduced the levy through the Affordable Housing Act, 2024, which provided a legal framework specifically for the levy and the housing program.

7.3.6 Strengths and Weaknesses of the Finance Bill

The annual nature of the Finance Bill has been criticized for contributing to an unpredictable taxation system in Kenya. Frequent changes to tax policies create uncertainty for businesses and investors, making long-term financial planning difficult.^(vii) This volatility undermines the principles of an efficient and optimal tax system by reducing stability and consistency in revenue collection.

Additionally, the omnibus nature of the Finance Bill makes it challenging to meet the stringent public participation requirements outlined in the

Constitution of Kenya (2010).^{lviii} As a result, courts have nullified Finance Bills in the past due to inadequate stakeholder consultation.

A notable example is the Finance Bill 2024, which was entirely withdrawn following widespread public protests rejecting its proposals.

7.3.7 The Impact of the Finance Bill on Taxation

In the previous sessions, we learned about taxation and the different laws that govern taxation in Kenya, and how they are affected by the Finance Bill. In these sessions, we will discuss the impact of the amendments to these laws.

The Finance Bill plays a pivotal role in shaping Kenya's taxation landscape by amending existing tax laws. These changes directly affect businesses, individuals, and the broader economy by altering tax rates, compliance requirements, and exemptions. In doing so, the Finance Bill influences government revenue generation, business competitiveness, and

consumer purchasing power. Understanding its impact is crucial for stakeholders to anticipate and adapt to evolving fiscal policies.

7.4 Analysis and Participation in the Finance Bill Process: How to Develop and Submit an Effective Memorandum

Public participation in the Finance Bill process is a constitutional right and a critical tool for shaping tax policies and fiscal decisions. Stakeholders—including individuals, businesses, civil society organizations, and professional bodies—play a key role in analyzing proposed amendments and submitting well-reasoned memoranda with recommendations.

Active engagement throughout the Finance Bill process ensures that tax policies are fair, transparent, and responsive to public needs. By participating strategically, stakeholders can influence legislation, promote accountability, and help shape a more inclusive fiscal system.



Table 10: Opportunities for public participation

Stage	Opportunities for Participation	Who Can Engage
Pre-Budget Consultations	• Engage in consultations with National Treasury, Parliament, and County Governments. • Submit recommendations based on sectoral needs and policy priorities (e.g., business). • Participate in public forums organized by the National Treasury on fiscal policy. • Conduct advocacy and mobilize stakeholders to shape proposals before inclusion in the Finance Bill.	Civil society organizations, business associations, professional bodies, and the public.
Publication & Tabling in Parliament	• Review the Finance Bill once published. • Conduct stakeholder meetings to analyze proposed tax changes. • Prepare draft memoranda with initial concerns and recommendations.	Tax experts, economic analysts, businesses, advocacy groups, legal professionals.
Public Participation Stage	• Submit a memorandum to the Finance & Planning Committee or relevant County Assembly Committee. • Attend public hearings organized by Parliament or County Assemblies. • Use media, social platforms, and policy briefs to highlight concerns. • Engage with MPs and MCAs to advocate for favorable changes.	Citizens, private sector, professional associations, industry groups, and civil society.
Parliamentary Review & Amendments	• Track committee proceedings and monitor debates. • Use advocacy networks to engage MPs or committee members. • Issue policy briefs to legislators to support key arguments. • Participate in stakeholder roundtables hosted by Parliament or think tanks.	Policy experts, research institutions, business leaders, advocacy groups.
Presidential Assent & Implementation	• Challenge unconstitutional or unfair provisions through legal action (if needed). • Monitor implementation by KRA and County Governments. • Continue advocacy to amend unfavorable tax policies in future Finance Bills. • Educate businesses and citizens on compliance requirements under the new Finance Act.	Tax professionals, legal experts, advocacy organizations, and media.

7.4.1 Key steps in developing an effective memorandum

• Step 1: Review and analyze the Finance Bill

Identify proposed amendments to **tax laws** (Income Tax Act, VAT Act, Excise Duty Act, etc.).

Assess the **potential impact** of these changes on businesses, consumers, and the economy.

Compare with previous Finance Acts to understand policy trends.

• Step 2: Develop a Memorandum

A well-organized memorandum should include:

Title & reference:

- "Memorandum on the Finance Bill [Year]"

- Reference the relevant Bill sections being addressed.

Introduction:

- Briefly introduce your organization or background.
- State the purpose of the memorandum.

Key issues & analysis:

For each tax law amendment:

- What is being changed? (Quote the section of the Bill)
- What is the impact? (Economic, business, social, or legal implications)
- What is your recommendation? (Retain, amend,

or remove the proposal, with justification)

Conclusion:

- Summarize key concerns and recommendations.
- Call for deeper public engagement or additional reviews.

7.4.2 Step 3: Submit Memorandum and implement advocacy strategies

Where to Submit: Memoranda should be sent to **Parliamentary Committees (Finance & Planning Committee, Budget Committee)** through email or physical submission.

Engagement: Participate in public hearings, stakeholder consultations, and advocacy meetings.

Follow-up: Track committee deliberations and build coalitions to amplify advocacy efforts.

Breakout session – Reviewing tax changes (40 mins)

Participants will analyze key amendments in the Finance Bill 2023 or 2024 and assess their intended policy outcomes.

Session structure:

1. Group formation (5 mins)

- Divide participants into groups of 8–10 members.
- Assign each group either the Finance Bill 2023 or Finance Bill 2024 for review.

2. Group discussion (30 mins)

Each group will:

- Identify and discuss** the top three changes introduced by the Finance Bill in the following tax laws:
 - Income Tax Act** – What specific provisions were amended?
 - Value Added Tax (VAT) Act** – Which goods/services were reclassified, exempted, or subjected to new VAT rates?
 - Excise Duty Act** – How were excise rates adjusted, and which products were affected?
- Analyze the intended policy outcomes** of these changes:
 - What was the government's objective in implementing these amendments?
 - How do these changes impact businesses, consumers, and government revenue?

3. Plenary presentations and feedback (20 mins)

- Each group will present a **5-minute summary** of their findings.

Key takeaways

- The Finance Bill is a powerful fiscal tool used annually by the government to amend existing tax laws and introduce new revenue measures. It is not a tax law by itself but modifies several tax statutes to align with national budget goals.
- Legislative oversight and public participation are essential in the Finance Bill process. Citizens, civil society, and the private sector have constitutionally guaranteed rights to engage at every stage—from pre-publication consultations to post-enactment advocacy.
- Tax amendments in the Finance Bill affect everyone from small businesses to large corporations, and from low-income earners to investors. These changes influence prices, business decisions, consumer behavior, and overall economic growth.
- A well-drafted memorandum is a critical advocacy tool. Through clear, evidence-based submissions, stakeholders can recommend alternatives, raise concerns, and influence Parliament's decision-making.
- Participation does not end with submission. Effective follow-up, coalition-building, and monitoring implementation are key to ensuring that public input leads to tangible policy outcomes.

8.

**REVENUE
IN NUMBERS**



8.1 Revenue performance

8.1.1 National Government- Ordinary revenue and Appropriation in Aid

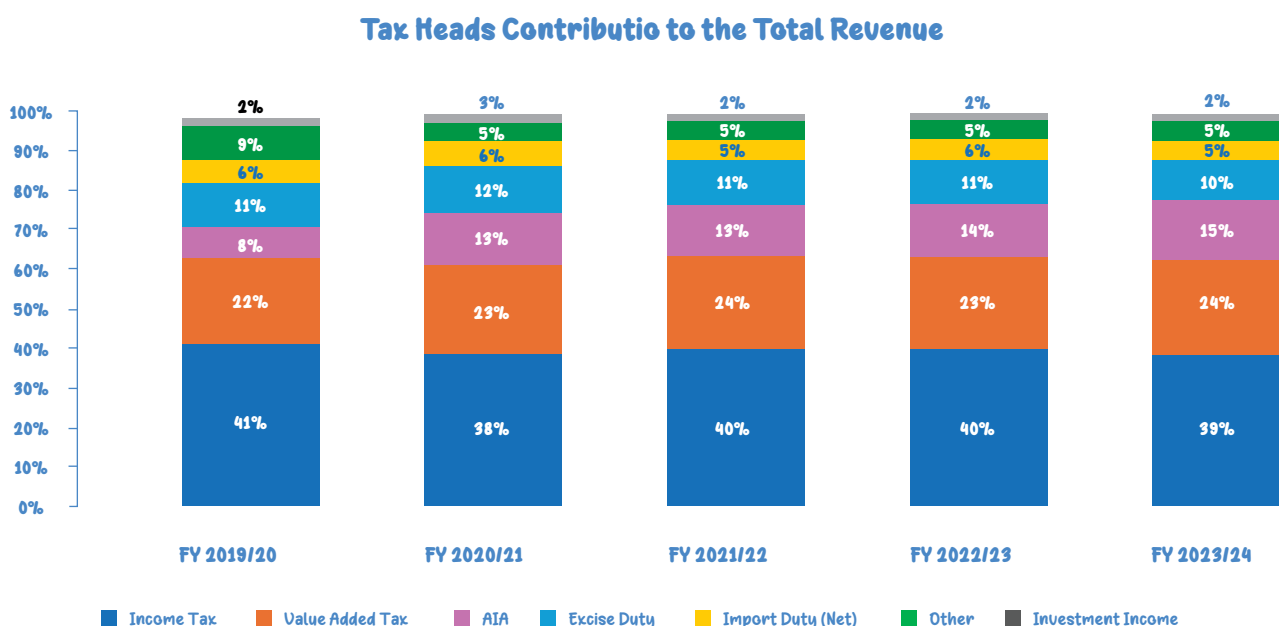
In Kenya, revenues are categorized into ordinary revenue and Ministerial Appropriation in Aid (A-i-A). Ordinary revenue is composed of all taxes and non-tax revenues that are paid into the Consolidated Fund. Tax revenues include personal income tax, corporate income tax, value added tax, excise duty, import duty, stamp duty, and capital gain tax. Non-tax revenues include immigration revenues, mining royalties, fines and forfeitures, traffic revenue, land revenue, and investment income. Ministerial A-i-A are revenues collected by various Government Ministries, Departments and Agencies (MDAs) and spent at source after appropriation. These include Railway Development Levy, Road Maintenance Levy, Petroleum Development Levy, Housing Levy, and University Fees, among others.

Kenya's total revenue collection has grown modestly by 15 percent from Ksh 1,734 billion in FY 2019/20 to Ksh. 2.7 trillion in FY 2023/24^{ix}. Ordinary

revenue accounts for an average of 90 percent of the total Government revenue with taxes on income constituting the largest share of 39 percent in FY 2023/24. However, this revenue collection has consistently been below target.

Income tax remains Kenya's top revenue stream, dipping in FY 2020/21 due to COVID-19 impacts, then rebounding in FY 2021/22 and FY 2022/23 with economic recovery and stronger KRA audits. VAT has grown steadily, driven by a strong rebound in household consumption after 2020 and policy reforms, particularly the 2021 Finance Act, which extended VAT to digital platforms and imported services. A-i-A rose to Kenya's third-largest revenue stream, boosted by IFMIS and eCitizen automation, which sealed leakages and improved collections from regulatory fees like hospital charges, land rent, and business licenses. Excise duty remained stable until FY 2020/21, then declined by FY 2023/24 due to lower excise rates on petrol and diesel. Import duty followed a similar trend, primarily due to a general decline in the volume of imported products.

Figure 11: Tax heads contribution to the total revenue



Source: Budget Review and Outlook Paper, National Treasury

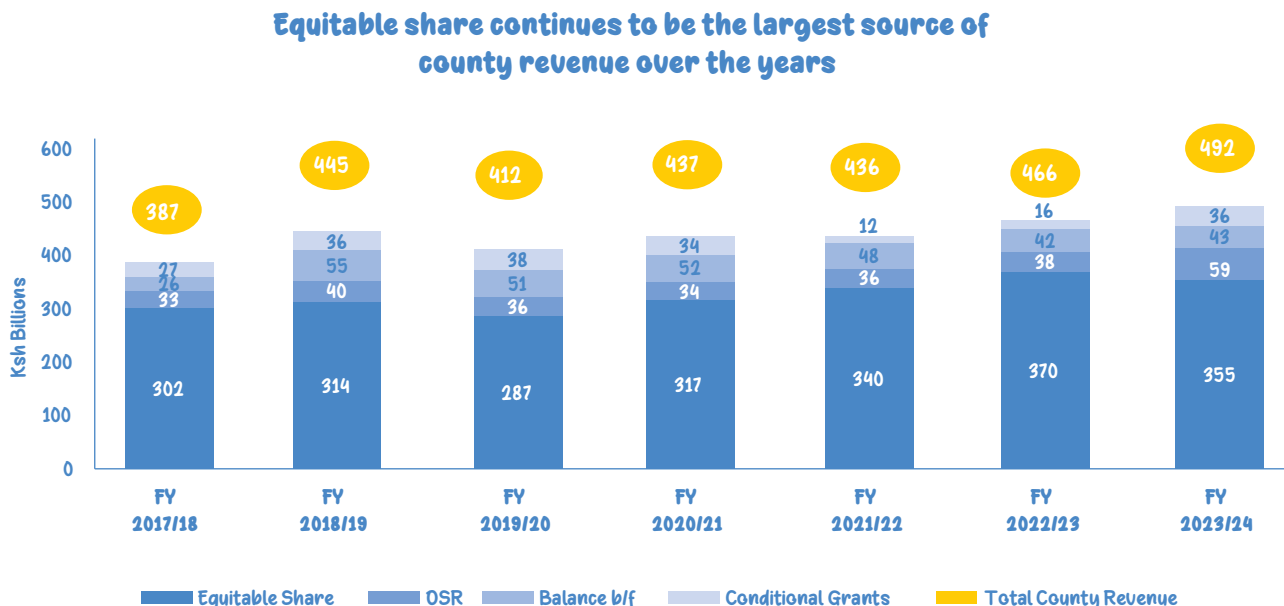
8.1.2 County Governments

More than 70% of the total county revenue comes from the National's equitable share each year, revealing counties' heavy dependence on national

funding and their exposure to financial management shocks.

And despite the growth in OSR, it only accounts for between 8% to 12% of total revenue, emphasizing that counties lack financial independence.

Figure 12: Sources of County Revenue



8.2 Credibility of revenue targets in Kenya

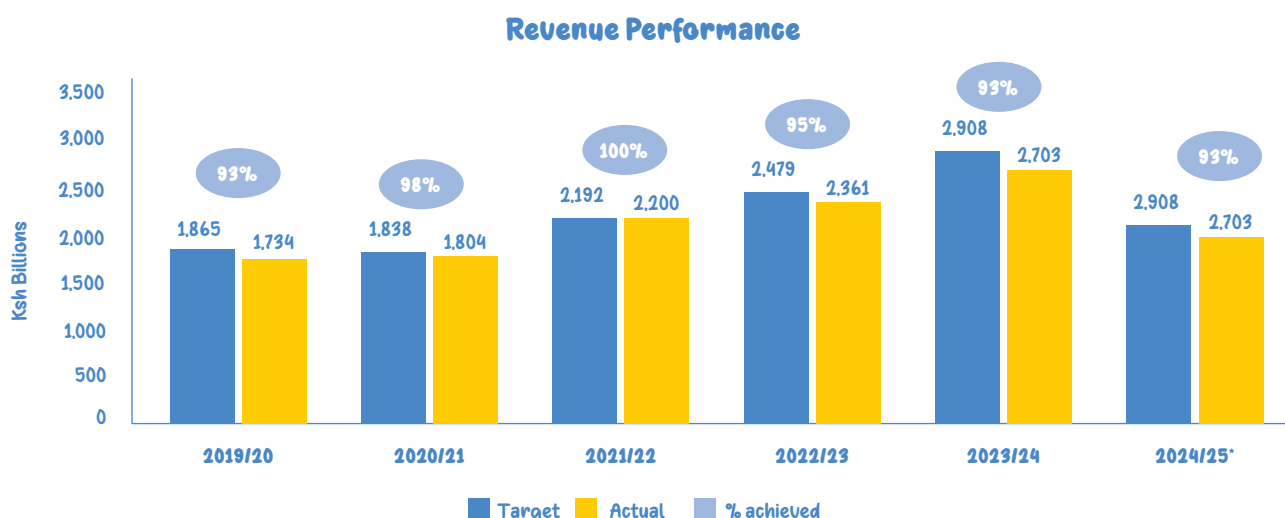
8.2.1 National Governments

Historically, Kenya has struggled to meet its revenue targets which are frequently set at ambitious levels that exceed actual collections. Kenya's revenue targets lack credibility due to the persistent pattern of underperformance, despite occasional successes like the KSh 8 billion surplus achieved in 2021/2022. Revenue performance in

2023/24 was below target, maintaining a long-term trend of underperformance against projections.

External shocks—such as global economic downturns or natural disasters—can unpredictably hinder revenue collection, but unrealistic projections are also rooted in internal flaws, including inaccurate forecasting and, at times, deliberate attempts to inflate or deflate revenue expectations.

Figure 13: Revenue Target and Outturn



Source: Budget Review and Outlook Paper, National Treasury

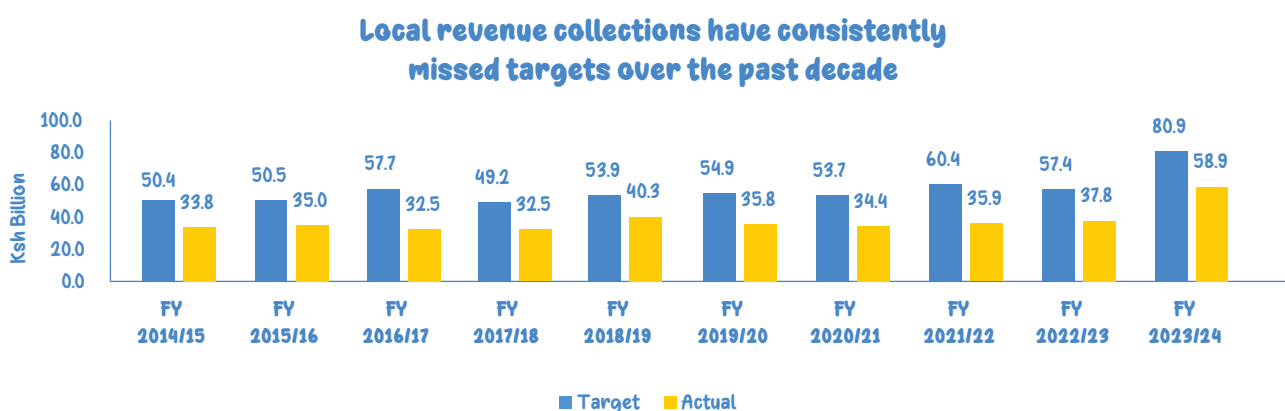
8.2.2 County Governments

Local revenue collections have fallen short over the years, with counties consistently underperforming against their targets. From FY 2014/15 to FY 2022/23, actual collections ranged between KSh 32 to 41 Billion, while targets remained significantly higher averaging above KSh 50 Billion¹⁶

unrealistic revenue projections and administrative challenges such as weak enforcement mechanisms and continued reliance on manual systems in many counties. For instance, in FY 2023/24, counties recorded the highest OSR collection at KSh 59 billion but still fell short of the KSh 80 billion target, highlighting ongoing challenges in setting realistic targets and sustaining reforms

This persistent shortfall has been attributed to

Figure 14: Revenue Targets vs Actuals



Endnotes



Endnotes

- i. Compania General de Tabacos de Filipinas v. Collector of Internal Revenue, 275 U.S. 87, 100 (1927) [Link](#)
- ii. McCulloch v The State of Maryland et al 17 U.S.
- iii. Eamonn Butler, "Introduction to Taxation" (2024) IEA [Link](#)
- iv. Atiya Warris, "Taxation Without Principles: A Historical Analysis of the Kenyan Taxation System" (2007) [Link](#)
- v. Eamonn Butler, "Introduction to Taxation" (2024) IEA [Link](#)
- vi. Eamonn Butler, "Introduction to Taxation" (2024) IEA [Link](#)
- vii. Eamonn Butler, "Introduction to Taxation" (2024) IEA [Link](#)
- viii. Eamonn Butler, "Introduction to Taxation" (2024) IEA [Link](#)
- ix. M Kabinga, "Principles of Taxation" (2016) [Link](#)
- x. The National Treasury and Economic Planning, "National Tax Policy" (2024) [Link](#); Th National Treasury and Economic Planning, "The Medium-Term Revenue Strategy: An Approach for Enhancing Domestic Revenue" (FY 2024/25-2026/27) [Link](#)
- xi. Income Tax Act Cap 470. [Link](#)
- xii. Finance Act 2023. [Link](#)
- xiii. PAYE. [Link](#)
- xiv. Affordable Housing Act. [Link](#)
- xv. Persons with disabilities Act. [Link](#)
- xvi. Finance Act 2015. [Link](#)
- xvii. Finance Act 2020. [Link](#)
- xviii. Finance Act 2023. [Link](#)
- xix. Tax Laws Amendment Act. [Link](#)
- xx. VAT Act. [Link](#)
- xxi. What is VAT. [Link](#)
- xxii. The Etrms and how it works. [Link](#)
- xxiii. The Tax Laws (Amendment Act), 2024. [Link](#)
- xxiv. The Finance Act 2023. [Link](#)
- xxv. EACCMA. [Link](#)

- xxvi. [The Miscellaneous Fees and Levies Act. Link](#)
- xxvii. [Non-Tax Revenues for Financing Sustainable Development. link](#)
- xxviii. [The OECD classification of non-tax revenues and interpretative guide. link](#)
- xxix. [Harnessing Non-Tax Revenue Potential. link](#)
- xxx. [Article 209 of the Constitution. Link](#)
- xxxi. [National Rating Act 2024. Link](#)
- xxxii. [Land Act 2012. Link](#)
- xxxiii. [Land Registration Act 2012. Link](#)
- xxxiv. [County Governments Act. Link](#)
- xxxv. [Local Government Act. Link](#)
- xxxvi. [2010 Constitution. Link](#)
- xxxvii. [County Outdoor Advertising Act. Link](#)
- xxxviii. [Traffic Act \(Cap 403\). Link](#)
- xxxix. [Alcoholic Drinks Control Act. Link](#)
- xl. [Agriculture, Fisheries and Food Authority Act. Link](#)
- xli. [What are Tax Expenditures and how are they structured. link](#)
- xlii. [Tax Expenditures. link](#)
- xliii. [Kenya 2022 Tax Expenditures Report. link](#)
- xliv. [The OECD: Better Policies for better lives. link](#)
- xlv. [OECD/G20 Inclusive Framework on BEPS. link](#)
- xlvi. [Environmental Tax. link](#)
- xlvii. [Green Taxation- in support of a more sustainable future. link](#)
- xlviii. [Global Tax Program. link](#)
- xlix. [Excise Duty Act. link](#)
- l. [The Climate Change \(Carbon Markets\) Regulations, 2024. link](#)
- li. [Kenya Closes its First ever Green Bond. link](#)
- lii. [Lake Turkana Wind Power Project. link](#)

lii. Tax 101: Misconceptions on the Withdrawal of the Finance Bill and Its Implications on Kenya's Appropriations. [Link](#)

lii. Tax 101: Misconceptions on the Withdrawal of the Finance Bill and Its Implications on Kenya's Appropriations. [Link](#)

lv. A Guide To The Legislative Process In Kenya Second Edition. [Link](#)

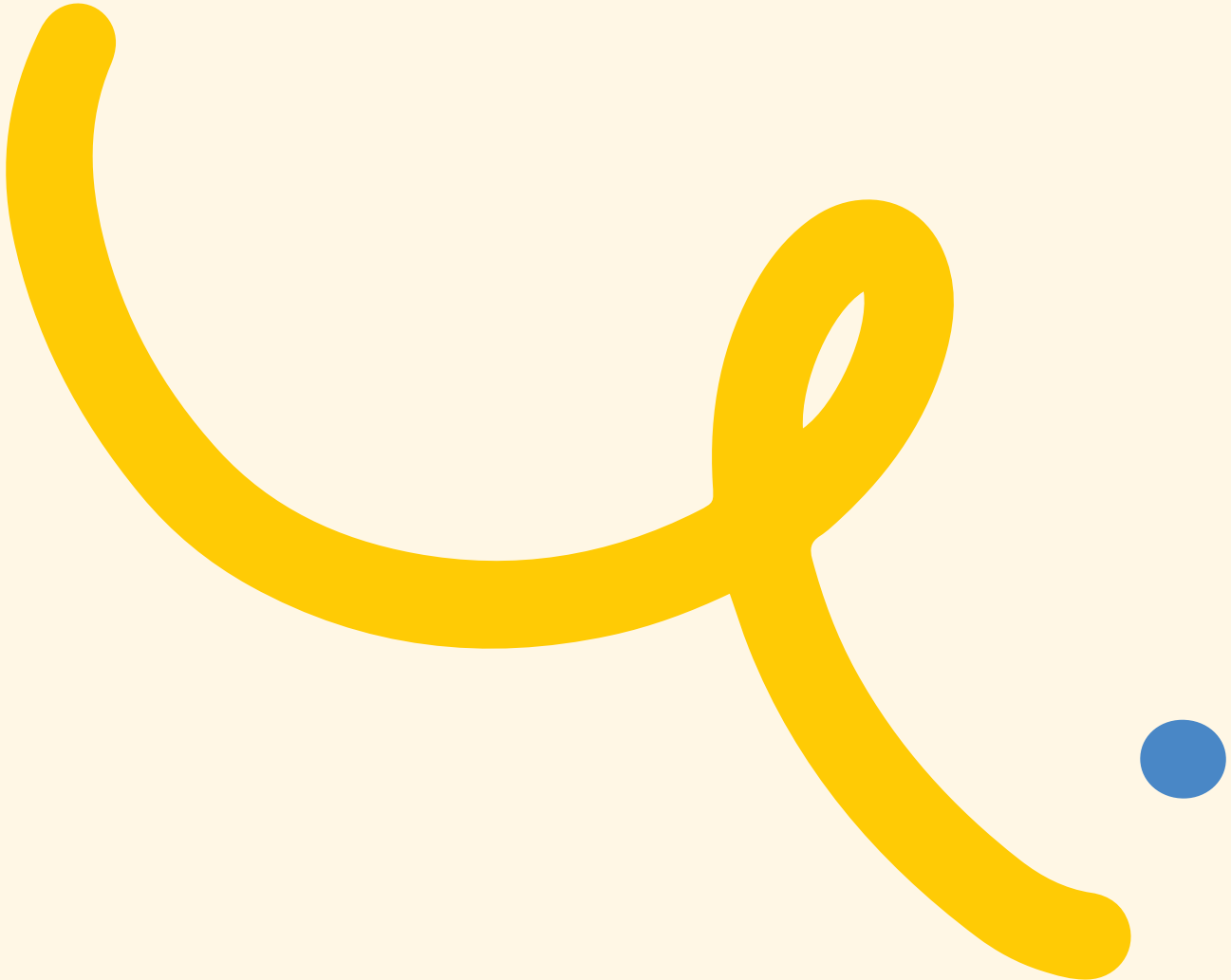
lvi. Court of Appeal Maintains Housing Levy Suspension by the High Court. [Link](#)

lvii. Do Away with Perennial Revisions of The Tax Laws for a Predictable Tax System. [Link](#)

lviii. Trust Takes Years To Build: How Can The Government Mend The Broken Public Confidence Post-Finance Bill 2024 Protests?. [Link](#)

lix. Budget Review and Outlook Paper. [Link](#)

lx. OCOB Reports. [link](#)





CONTACT OR VISIT US TODAY!
INSTITUTE OF PUBLIC FINANCE (IPF)
FOURTH FLOOR, ROSAMI COURT, MURINGA ROAD, KILIMANI
E-MAIL: INFO@IPFGLOBAL.ORG.KE
P.O. BOX 21753-00100, NAIROBI, KENYA
TEL: +254 758 728 882 WWW.IPFGLOBAL.ORG.KE
©2025