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INSTITUTE OF PUBLIC FINANCE

Kenya Women Parliamentary Association
KEWOPA

PRESENTATION TO THE NATIONAL ASSEMBLY DEPARTMENTAL COMMITTEE ON FINANCE AND NATIONAL PLANNING ON THE FINANCE BILL, 2026

A. INTRODUCTION

This memorandum has been prepared by the Institute of Public Finance (IPF) in partnership with the Kenya Women Parliamentary Association (KEWOPA). We begin by commending the Departmental Committee on Finance and National Planning of the National Assembly for providing the public with an opportunity to present views on the Finance Bill, 2026, a Bill that carries significant implications for Kenya's fiscal framework, economic stability, investment environment, and taxpayer welfare. Our submissions are guided by the need to promote a tax system that is predictable, equitable, efficient, constitutionally compliant, and capable of supporting sustainable economic growth while safeguarding taxpayer rights and enhancing voluntary compliance.

At the outset, we wish to emphasize several broader policy concerns that continue to emerge within Kenya's taxation framework.

- First, there remains an urgent need for greater predictability, certainty, and stability within the tax system, particularly in light of the frequent amendments, reversals, and policy shifts introduced through successive Finance Acts, which continue to undermine investor confidence, increase compliance costs, and disrupt long-term planning.
- Secondly, there is need for stronger alignment between annual Finance Bills, the Medium-Term Revenue Strategy (MTRS), and the National Tax Policy to ensure consistency in implementation and policy coherence. In particular we are concerned that:
  - Several key commitments highlighted within the MTRS implementation matrix remain outstanding, including the review of Personal Income Tax bands, the reduction of Corporate Income Tax from 30% to 25%, and the downward revision of VAT rates, yet the National Treasury has continuously reduced the number or exempt/zero rated supplies.
- Thirdly, as discussions on equitable taxation continue to evolve, there is increasing need for a more coherent approach towards the taxation of wealth and high-value capital accumulation while limiting broad exemptions that may disproportionately benefit sophisticated investment structures. As IPF we have produced a paper highlighting how Kenya can introduce a wealth tax on 7,200-dollar millionaires (those with assets exceeding

Ksh 129 million) and 16 centi-millionaires (those with net assets exceeding Kshs 12.915 billion).

- Additionally, tax policy must increasingly align with Kenya's broader climate change and green industrialization commitments, particularly within sectors such as e-mobility and renewable energy, where inconsistent fiscal measures risk undermining long-term sustainable investment. Ethiopia provides an illustrative example of how a country can reduce its dependence on fossil fuel and transition to e-mobility.
- Finally, while the Finance Bill, 2026 contains several progressive proposals aimed at improving tax administration and strengthening compliance, certain provisions continue to raise concerns relating to taxpayer rights, proportionality of penalties, legal certainty, and the overall ease of doing business. It is against this background that we present our submissions and recommendations on the specific clauses contained in the Bill.

PART I: INCOME TAX ACT

1. PAY AS YOU EARN (PAYE) AND PERSONAL INCOME TAX RELIEF

Chairperson and Honourable Members, the continued rise in the cost of living and the growing tax burden on salaried employees has intensified public concern regarding the current PAYE framework. PAYE remains one of the most efficiently enforced tax heads and, as a result, salaried employees continue to bear a disproportionate share of the direct tax burden due to the ease of collection and the limited opportunities for tax planning available to employees compared to other sectors of the economy.

Over the last several years, there have been repeated policy pronouncements under the Medium-Term Revenue Strategy and various public statements indicating Government intention to reduce or eliminate PAYE for persons earning KSh 30,000 and below and to lower the burden for persons earning up to KSh 50,000. However, these reforms have not been reflected in the Finance Bill, 2026.

While the National Treasury has indicated concern regarding a potential revenue shortfall estimated at KSh 35 billion, we respectfully submit that reducing the PAYE burden would significantly increase disposable income, enhance household purchasing power, stimulate consumer spending, and support economic activity during a period characterised by rising fuel

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prices and increased economic hardship. Any resulting revenue gap can instead be addressed through more progressive taxation measures targeting accumulated wealth, luxury assets, and aggressive tax avoidance structures rather than continued overreliance on salaried income taxation. **We therefore urge the Committee to recommend a review of PAYE bands and rates with a view to easing the burden on lower and middle-income earners.**

2. CLAUSE 2: DEFINITION OF ROYALTIES

Clause 2 of the Bill proposes to expand the definition of royalties to include payments arising from software distribution arrangements and payments relating to the use of proprietary digital platforms, payment systems, switching systems, clearing systems, settlement systems, and related digital infrastructure.

Chairperson and Honourable Members, we respectfully oppose this proposal for several reasons.

First, this is now the third consecutive attempt to introduce into law the classification of software distribution payments as royalties despite clear judicial pronouncements to the contrary. In Seven Seas Technologies Limited v Commissioner of Domestic Taxes, the High Court expressly distinguished between payments made for the use of copyrighted intellectual property and payments arising in the ordinary course of distributing software products. The Court rejected the blanket characterization of software distribution arrangements as royalty payments merely because software is involved. The continued reintroduction of this proposal despite ongoing appellate proceedings undermines legal certainty, predictability in tax administration, and respect for judicial authority.

Secondly, the proposed inclusion of proprietary digital platforms and payment systems within the definition of royalties is excessively broad and ambiguous. As currently drafted, the amendment appears capable of classifying ordinary operational and transactional fees as royalty payments simply because they relate to digital infrastructure or payment systems. This creates significant uncertainty regarding service fees, processing fees, transaction fees, network fees, and other ordinary commercial charges that are generally understood as payments for services rather than consideration for intellectual property rights.

If adopted, the proposal is likely to increase disputes, create uncertainty within the financial and digital economy sectors, discourage innovation, and expose ordinary commercial transactions to unintended withholding tax obligations. We therefore urge the Committee to reject Clause 2.

3. CLAUSE 19: CHANGE OF TIMELINES FOR FILING TAX RETURNS

Clause 19 proposes to amend Section 52B of the Income Tax Act by moving the filing deadline for tax returns from June to April for taxpayers whose accounting year ends in December. The Bill further proposes that nil returns be filed within one month following the end of the year of income.

While KRA has indicated that the proposal seeks to enhance efficiency in tax administration and improve reconciliation processes, we respectfully submit that the proposed timelines are impractical, particularly for corporate taxpayers. Corporate taxpayers require sufficient time to prepare audited financial statements, complete internal approvals, and finalise accurate tax computations before filing returns. Reducing the filing period from six months to four months is likely to compromise the quality and accuracy of compliance and may increase disputes arising from errors and omissions.

Further, taxpayers continue to experience instability and downtimes within KRA systems. Shortening compliance timelines without first addressing these technological challenges risks unfairly locking taxpayers out of compliance systems and exposing them to unnecessary penalties despite genuine efforts to comply. The proposal relating to nil returns is equally restrictive and may disproportionately burden small taxpayers and individuals. We therefore urge the Committee to reject Clause 19.

4. CLAUSE 20: EXEMPTION OF CAPITAL GAINS TAX ON TRANSFERS TO REITS

Chairperson and Honorable Members, we respectfully oppose the proposed blanket exemption of Capital Gains Tax on transfers of property to Real Estate Investment Trusts. While the intention may be to encourage investment within the real estate sector and deepen the REIT market in Kenya, the proposal risks disproportionately benefiting high-net-worth individuals and large property owners who may restructure assets into REITs primarily for tax planning purposes.

The amendment may therefore undermine progressive taxation principles by reducing the ability of the tax system to effectively tax substantial gains arising from high-value property transactions.

We therefore urge the Committee to reject the proposed CGT exemption relating to transfers to REITs. (Emphasize on the PAYE)

B. VAT ACT Amendments

Amendments in the VAT Act are the epitome on unpredictability of Kenya's system with routine reclassification of goods and services.

5. Clause 26: Definition of taxable value of supply in hire purchase transactions

The amendment restricts the exclusion of financing charges from taxable value to suppliers licensed under the Hire Purchase Act. Previously, any supplier could claim this exclusion.

6. Clause 28: Increase of the time frame VAT refunds on bad debt

The Bill introduces a new Section 17A requiring registered persons to account for input VAT previously deducted where taxable supplies subsequently become exempt and remain unsold. The amendment reverses an amendment passed in Finance Act 2025, reflecting unpredictability created by frequent tax changes.

The proposal effectively extends waiting time for VAT tax refunds on unpaid supplies, which will affect cashflow for businesses and thus should be rejected. It is also to be remembered that this provision has been revised multiple times over the past few years, creating uncertainty.

7. Clause 29: Tax invoice requirements

- The proposal delinks issuance of invoices from VAT registration status of a person.
- This proposal may possibly close a compliance gap where suppliers have historically justified non-issuance of tax invoices on the basis that they are not VAT registered, even where their transactions are taxable supplies.
- The proposal also aligns with Section 23A of TPA

8. Clause 31: VAT Reclassification

Routine reclassifications are back which reflects policy uncertainty contrary to the objectives of the National Tax Policy and the Medium-Term Revenue Strategy. In addition, some items are proposed to benefit from extended exemptions, defeating the goal of reducing tax expenditure and promoting equity in taxation.

For example, the proposed exemptions of all aircraft parts should be rejected. The proposal extends the exemption to all aircraft parts imported by aircraft operators or persons engaged in

the business of aircraft maintenance to counteract deletion of Article 88 supplies from the list of zero-rated goods

This committee has justified this exemption with the need to protect Kenya's aviation sector; however, this exemption benefits the high-income earners who are more likely to operate such businesses or use aircrafts and have the ability to pay taxes.

The proposed reclassification from vatable to exempt for the supply of goods and services for direct and exclusive use in the implementation of infrastructure projects undertaken under a Public Private Partnership framework is good because, the exemption is likely to reduce the cost of PPP projects but the government must address transparency concerns around approval and costing of PPP projects.

Other items proposed to be exempt include Dialyzers; Scrap metal and worn clothing and other worn articles upon importation

Reclassification from exempt to vatable at 16 percent

The affected supplies include: Chapter 88 goods (Aircraft, spacecraft, and parts); Direction-finding compasses, instruments and appliances for aircraft; Taxable goods and services for direct and exclusive use for the construction of tourism facilities, recreational park; Goods imported or purchased locally for direct and exclusive use in the construction of houses under an affordable housing scheme; denatured ethanol of tariff number 2207.20.00

Reclassification from zero-rated to exempt

Reclassification from zero-rated to exempt broadly aligns with the government's intention to limit zero rating to export and reduce VAT refunds; but will result in price increases for the affected commodities including:

- Inputs or raw materials locally purchased or imported for the manufacture of animal feeds
- Inputs or raw materials (either produced locally or imported) supplied to pharmaceutical manufacturers in Kenya.
- Transportation of sugarcane from farms to milling factories.
- The supply of imported or locally purchased telephones for cellular networks and other wireless networks.
- The supply of electric motorcycles
- The supply of electric bicycles
- The supply of solar and lithium-ion batteries
- The supply of electric buses of tariff heading
- Bioethanol vapour (BEV) Stoves

The proposal to move several items from zero-rated to exempt status is in line with the Government's policy of limiting zero-rating to exports. While this approach may reduce the burden of VAT refunds on the Kenya Revenue Authority (KRA) and improve administrative efficiency, it has important implications for businesses. Under an exempt regime, firms cannot claim VAT input, which effectively increases production costs and may lead to higher consumer prices, particularly in sectors such as pharmaceuticals, agriculture, and clean energy inputs. IPF therefore recommends that, where such reclassifications are adopted, consideration should be given to extending exemptions to final products or targeting relief to mitigate price increases and protect consumers.

C. EXCISE DUTY ACT

Clause 36: Amendment to the first schedule. Excisable goods

Clause 36 proposes amendment by deletion of a proviso that exempts excise across a number of goods that are imported into the country that originate from the East African Community.

Chairperson and Honourable Members, we oppose this proposal due to this key reason, The East African Community Customs Union Protocol, to which Kenya is a founding signatory, establishes a customs union area within which goods meeting the EAC Rules of Origin are to circulate freely without the imposition of customs duties or charges of equivalent effect. The deletion of the EAC Rules of Origin exclusion from these excise duty descriptions raises a direct and serious question of compliance with this protocol. Enacting this amendment exposes Kenya to legal challenge by affected Partner States, with the consequent risk of diplomatic friction and reputational damage as a reliable EAC partner. We therefore urge the committee to reject this amenndment.

Clause 36 (iv) Amendment of the first schedule by deletion of a proviso relating to products manufactured by licensed small independent brewers.

Clause 36 proposes the deletion of the proviso that products manufactured by licensed small independent brewers are subject to a preferential excise duty rate of KSh 10 per centilitre of pure alcohol.

Chairperson and Honourable Members, we respectfully oppose this proposal for the following reason: The proposed deletion of the preferential excise duty treatment for licensed small independent brewers is likely to undermine the growth and sustainability of small-scale alcoholic beverage manufacturers, weaken competition within the beverage industry, and disproportionately benefit dominant market players. We therefore urge the committee to reject this amendment.

Clause 36 (ix) Amendment of the first schedule by deleting the description "imported articles of plastic and the corresponding rate of excise duty.

Chairperson and Honourable members, we respectfully oppose this proposal for this key reason: Kenya has over the past years built one of the most progressive anti-plastic regulatory frameworks in Africa including the ban on plastic bags in 2017. The complete deletion of excise duty on imported plastic is a move in the opposite direction to this established environmental policy trajectory that needs justification that the current proposed amendment does not provide. We therefore urge the committee to reject this amendment.

D. TAX PROCEDURES ACT

CLAUSE 45: REMOVAL OF PROTECTION AGAINST AGENCY NOTICES DURING PENDENCY OF APPEALS

Clause 45 proposes to delete Section 45(14)(e) of the Tax Procedures Act, which currently prevents the Commissioner from issuing agency notices where a taxpayer has appealed an assessment before the Tax Appeals Tribunal or the Courts. We reject this proposal.

Chairperson and Honourable Members, this proposal raises serious constitutional and administrative justice concerns. The current provision serves as an important safeguard by ensuring that taxpayers are not subjected to enforcement action before disputes are conclusively determined. Allowing KRA to issue agency notices during the pendency of an appeal effectively prejudges disputes before determination and exposes taxpayers to significant financial hardship even where the disputed assessment may later be overturned or varied by the Tribunal or the Courts. Such enforcement measures may severely disrupt business operations, interfere with cash flow, and undermine confidence in the tax dispute resolution framework. Further, the proposal risks discouraging taxpayers from exercising their statutory right of appeal due to fear of immediate enforcement action. This creates a coercive environment where taxpayers may feel compelled to settle disputed taxes regardless of the merits of their case. We therefore urge the Committee to reject Clause 45.

CLAUSE 49: COMPUTATION OF TIME FOR OBJECTIONS AND APPEALS

Clause 49 proposes to delete Section 77(2) of the Tax Procedures Act, thereby removing the exclusion of weekends and public holidays in calculating timelines for objections and appeals. We reject this proposal.

Chairperson and Honourable Members, the current framework ensures that taxpayers and their advisers are afforded meaningful working days to prepare objections, gather documentation, seek professional advice, and properly formulate legally sound appeals. Removing this safeguard would mean that weekends and public holidays are counted within already strict statutory timelines, effectively reducing the actual working time available to taxpayers. This increases the risk of inadvertent non-compliance and may result in valid disputes being dismissed on procedural technicalities rather than being heard on their merits. The proposal is likely to disproportionately affect small and medium-sized taxpayers who may not have immediate access to legal or tax

advisory support. It may also lead to increased applications for extension of time and additional litigation over procedural defaults, thereby placing unnecessary strain on the dispute resolution system. We therefore respectfully urge the Committee to reject Clause 49.

CLAUSE 50: REPEAL AND REPLACEMENT OF SECTION 86

Clause 50 proposes to repeal and replace Section 86 of the Tax Procedures Act relating to penalties for non-compliance with electronic tax obligations, including the issuance of electronic tax invoices, electronic filing of returns, and electronic payment of taxes. We reject this proposal and propose the following.

We acknowledge that the proposed amendment introduces procedural safeguards by requiring the Commissioner to first issue a notice to the taxpayer and consider whether the non-compliance resulted from circumstances beyond the taxpayer's control before imposing penalties. These are positive developments that improve procedural fairness and recognize the importance of allowing taxpayers an opportunity to be heard.

However, notwithstanding these improvements, the proposal should still be rejected in its current form because the penalties remain excessively punitive and disproportionate.

The retention of a penalty amounting to two times the tax due is particularly concerning. In cases involving substantial tax liabilities, the penalties may become excessive and go beyond what is reasonably necessary to encourage compliance.

Further, although the amendment introduces a reduced penalty of KES 10,000 for individuals, the wording of the provision means that individuals may still be exposed to penalties of two times the tax due or KES 100,000 where those amounts exceed KES 10,000. This undermines the intended relief for individual taxpayers. These concerns are particularly significant given the practical challenges taxpayers continue to face with eTIMS, including system downtimes, integration difficulties, technical failures, and inadequate support. Many of these challenges are outside the taxpayer's control and may make full compliance difficult despite genuine efforts to comply.

For small businesses especially, the proposed penalties may be financially devastating and may discourage formalization and voluntary compliance. A more proportionate approach would involve the adoption of percentage-based penalties linked to the severity of the non-compliance while limiting individual taxpayers strictly to the KES 10,000 fixed penalty. We therefore urge the Committee to reject Clause 50 in its current form and recommend a more balanced and proportionate framework.