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The road to recovery: Building economic resilience

National budget bulletin

June 2021

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Economy

Economy: Is recovery possible in FY 2021/2022?

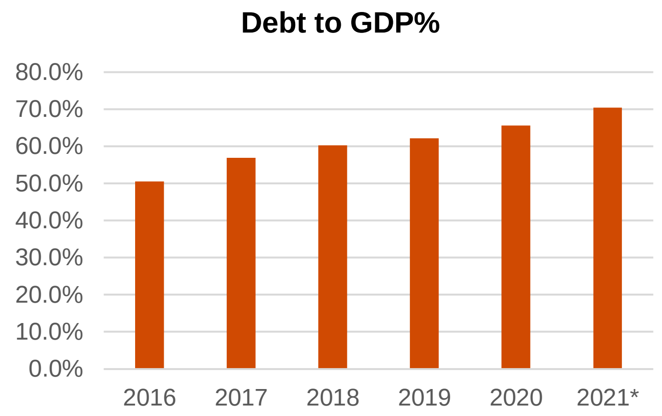
Kenya's FY2021/22 budget is being presented at a time when the global economy is emerging from recession due to the pandemic. In Kenya, economic recovery emerges in the context of limited resources, significant expenditure demands (post COVID-19 economy recovery, debt repayments, political expenditure, etc.) and a reduction in achievable revenue.

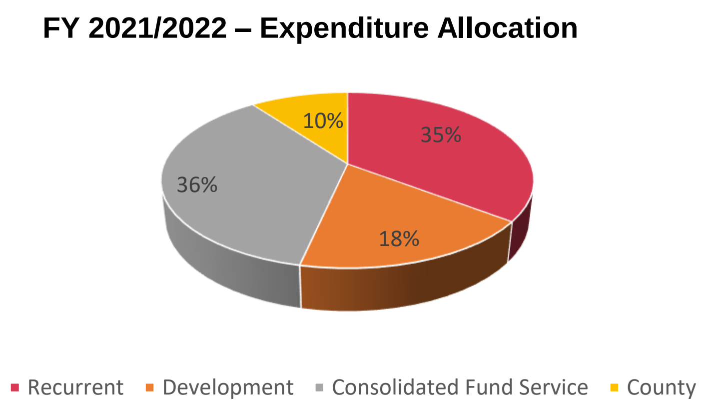
The Government is keen to reduce the budget deficit to GDP ratio from 8.7% currently to 3.6% by FY 2024/2025. Economic growth of 6.6% in FY 2021/22 from 0.6% in FY 2020/2021 is also projected.

Reducing the budget deficit is key to economic recovery, and is going to be pegged on raising revenue collection, reducing wastage and inefficiencies and ring-fencing economic developments.

The estimated ordinary revenues in FY 2021/22 amounted to KES 1,775.6 billion which is marginally higher than the FY 2020/21 estimate of KES 1,594 billion.

The projected performance is premised on broadening of the tax base and tax reforms through introduction of digital tax, voluntary tax disclosure programme, enhancing rental tax among others. Revenue performance may also result from a resurgent performance in KRA collections in Q1 of 2021, in which the targets were surpassed.





6.6%

Projected economic growth in FY 2021/22

Economy (continued)

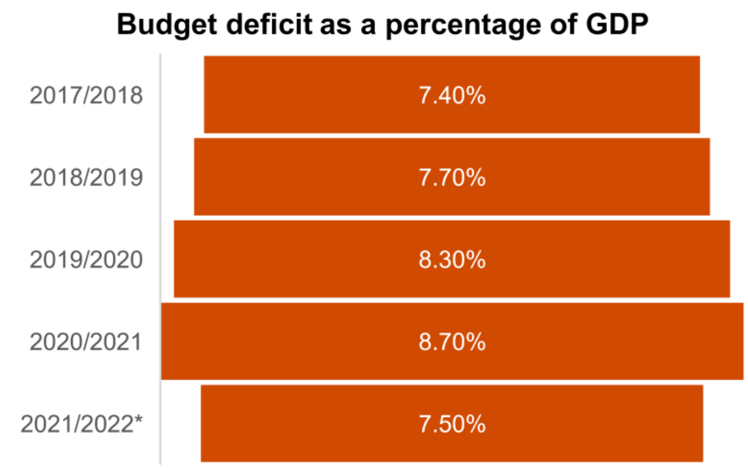
This performance may prove challenging to achieve given the outcome of similar reforms and the fact that the tax revenue to GDP ratio has been on a steady decline for the last few years having peaked at 19% in FY 2013/14. The latest projected ratio for 2020/21 is 14.3% with a similar projected ratio for FY 2021/22. These ratios are now below the desirable 15% (OECD) threshold needed to finance sustainable economic growth.

The government is projecting to progressively reduce expenditure as a share of GDP from 25.6% in FY 2020/21 to 24.3% in FY 2021/2022. This may be challenging due to legacy projects the government has to carry out, fulfillment of the Big Four agenda, payment of pending bills, post COVID-19 interventions among others. Also no initiative to address the public wage bill has been highlighted.

The gradual development expenditure shrinkage in relation to the total annual expenditure budget should also be of concern. In the budget estimates for FY 2021/22 it represents 18% (KES 655 billion) of total government expenditure, against the requirement of the PFM Act of 30%.

Debt continues to weigh significantly on revenues collected with loan payments being on the upward growth as the Government seeks more loans to fulfil its short term and long-term commitments.

To fund the budget deficit, the government is going to source KES 662 billion from the domestic market and KES 271 billion from foreign markets. Domestic borrowing has the effect of locking out SMEs and private business, slowing economic growth.



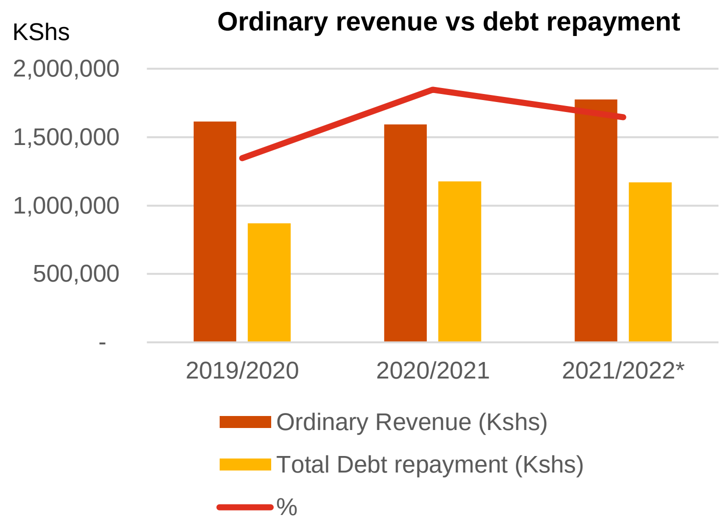
Economy (continued)

Kenya's total debt to GDP ratio has seen an increase from 50.5% in 2016 to 65.6% in 2020 according to the World Bank. With the projected budget deficit of KES 930 billion in FY 2021/22, more borrowing is expected to take this ratio to above 70%. The current total loan level is estimated at KES 8.4 trillion and to cover the projected deficit, the debt ceiling set at KES 9 trillion is also expected to be raised.

The debt repayment ratio to ordinary revenue collected has seen an increase from 54% in FY 2019/2020 to a projected 66% in FY 2021/22 which was a slight reduction compared to FY 2020/21 (74%). When paying loans and recurrent expenditure is not possible from revenues, government runs into the problem of needing to borrow from one source to pay another.

An economic stimulus programme in FY 2021/22 amounting to KES 23.1 billion which targets to cushion vulnerable citizens and business affected by COVID-19 has been highlighted. Given the possibility of the economy being affected by the on-and-off closures due to COVID-19, particularly with rates of vaccination still low, and with an increasing population of vulnerable citizens, the amount set aside may not be sufficiently impactful although the stimulus is still a welcome move.

The Government continues on its quest to achieve the Big Four agenda as noted by the budgetary allocations amounting to KES 142 billion. The allocations cover universal healthcare, affordable housing, manufacturing for job creation and food and nutrition security.



The government aims to clear KES 13.1 billion of pending bills by the end of the financial year, a laudable effort that will bring liquidity to the market and jumpstart economic activities. The process of paying such bills within such a short time can encourage certain abuses and anomalies, however.

Overall the economic and fiscal reforms should continue to create an enabling business environment, enhancing job creation and minimize inflationary pressure and the cost of living.

Economy (continued)

Conclusion

- The projected growth of 6.6% in FY 2021/22 will be a challenge to achieve in an economy that might still face disruptions due to the COVID-19 pandemic and a growing budget deficit. Vaccination should be prioritized.

- The government’s efforts to reduce inefficiencies and wastage are applauded. However, more scrutiny should be applied to ministerial, department and agency budgets; re-appraisal of development projects should be completed; an empowered project management unit instituted; and the adoption of public private partnerships expanded, amongst other initiatives.

- Re-negotiation of the current terms of existing loans is key, as is seeking more concessionary financing.

- A clear fiscal policy that aims to reduce the growing budget deficit should be pursued.

- Economic reforms spurring the economy should be encouraged, such as a Bill to mandate payment of rendered works or services to government entities.

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Tax

A balanced scorecard for the Government from a tax perspective

The National Budget for Fiscal Year ("FY") 2021/ 22 is the penultimate budget for the current Government. In 2013 a new governance structure in Kenya in the form of devolved government was ushered in resulting in the need for increased revenue through increased tax collections. Over the last seven years, the government has doubled the tax revenue collected from KES 759 billion to KES 1,475 billion as shown in the table below.

19%

Kenya's tax to GDP ratio in FY2013/14

Table[1]

Year	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19
Tax revenue in Billions	**KES**	**KES**	**KES**	**KES**	**KES**	**KES**	**KES**
Direct taxes	393	454	506	561	628	642	689
Indirect taxes	329	406	454	515	587	619	711
Tax revenue	**722**	**860**	**960**	**1,076**	**1,215**	**1,261**	**1,400**
Other	37	60	62	61	58	79	75
Total Exchequer Revenue	**759**	**920**	**1,022**	**1137**	**1,273**	**1,340**	**1,475**

However, despite the increased tax collections, the tax revenue collected as a percentage of GDP has shrunk over the same period. In FY2013/14, Kenya's tax to GDP ratio was at 19% while in FY2018/19 it stood at 16.7%.

The mismatch between GDP growth and tax collections may be attributable to several reasons including GDP growth being fuelled by public infrastructure investment that may not necessarily generate immediate tax revenue or growth in sectors that are exempt from tax or have contributed very little to tax collections. It is however noted that the current tax to GDP ratio is still within the International Monetary Fund ("IMF") prescribed rate for developing countries of 15%.

[1]Kenya Revenue Authority 2018/2019 Annual Revenue Performance Report

A balanced scorecard for the Government from a tax perspective (continued)

Probably as a result of the low tax to GDP ratio, there has been a trend under the current Government to introduce new taxes. In the Finance Act 2014, the Government reintroduced capital gains tax on sale of property at a rate of 5% which had been suspended for over 29 years. In the subsequent Finance Act, the Government introduced the rental income tax after which was followed in 2019 with a Turnover Tax targeted at Small and Medium Enterprises ("SMEs").

In 2020, in a bid to mobilise tax revenue after the COVID-19 pandemic, the Government introduced a minimum tax and the digital service tax ("DST"). The introduction of new taxes within a short period of time can create an element of uncertainty and confusion for taxpayers. In extreme circumstances, it can deter foreign investors when the tax environment is perceived as unpredictable.

We have seen over the years a focus on tax procedures which are primarily geared towards increasing the scope of authority of the Kenya Revenue Authority ("KRA") and providing more powers to the Commissioner. These amendments under the Tax Procedures Act appear to be overly biased towards the KRA without considering the taxpayer's perspective. In some instances, these provisions may be in conflict with other sections of the Tax Procedures Act and procedural rules contained in other statutes.

Over the last decade, KRA has worked to become more open and available for interactions with taxpayers. Any new powers being granted to KRA should be used judiciously to avoid sacrificing the gains developed from the constructive relationships built with taxpayers.

The introduction of new taxes within a short period of time can create an element of uncertainty and confusion for taxpayers.

A balanced scorecard for the Government from a tax perspective (continued)

One of KRA's most important transformations over the last decade has been its adoption and use of technology. This has led to a better customer experience by taxpayers and has managed the cost of revenue collection. The ease of paying taxes has resulted in an increase in tax collections.

Another trend witnessed is the modernisation of the tax laws in Kenya. In 2013, the Value Added Tax (VAT) Act was replaced with a new Act. In 2015, the Excise Duty and the Tax Procedures Acts were enacted.

The only legislation pending reform is the Income Tax Act. Where modernisation of the tax legislation results in the simplification of the tax laws, such simplified laws can lead to lower compliance costs.

Finally, it is noted that a number of regional and international trade agreements have been signed in the last decade e.g. AfCFTA, COMESA, AGOA. However, Kenya has been slow in adopting the tax policies they have signed under the regional and international trade agreements into the domestic tax legislation. In some instances, Kenya has passed laws in the domestic legislation that run counter to such agreements such as the limitation of treaty benefits in the Income Tax Act.

We see the same trends witnessed over the last seven years continuing in this year's Finance Bill, particularly in relation to increasing the powers of the Commissioner and increasing the scope of taxation. More details relating to these changes are in our tax alert which you can read here.

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Customs Duty

Protecting local enterprises

The Cabinet Secretary highlighted the following proposals by the East African Community ("EAC") Partner States:

Stays of application of import duty rates per the East African Community Common External Tariff ("EACCET")

The following duty rates will be applicable on importation of the following items for one year:

- Iron and steel products – 25% and corresponding specific rates;
- Vegetable products, e.g. potatoes, peas, tomatoes, etc. – 30% pending finalization of the review of the EACCET;
- Products for manufacture of leather and footwear products – 25% and a further specific duty rate to deter undervaluation; and
- Furniture – 35%.

Duty remissions

Duty remissions will apply for one year on importation of raw materials and inputs for manufacture of:

- Masks, sanitizers, ventilators and personal protective equipment ("PPE");
- Baby diapers; and
- Roofing tiles.

Proposed changes will become effective 1 July 2021 following publication of the East African Community Gazette Notice.

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Legislative updates

The majority of the legislative reforms proposed in the FY2021/22 budget are covered in the Finance Bill, 2021 and summarized in our previous alert. Other legislative changes that have been proposed by the Government and are pending in Parliament are as follows:

The Public Procurement and Asset Disposal (Amendment) Bill, 2020 proposes changes to the contracting framework to ensure greater participation of local contractors by allowing contracts to be awarded to multiple bidders.

The Central Bank of Kenya (Amendment) Bill, 2021 seeks to license digital credit service providers. See our previous alert for more details.

Amendments have been proposed to the **Retirement Benefits (Mortgage Loans) (Amendment) Regulations, 2020** to allow members of retirement benefits schemes to utilize up to 40% or a maximum of KES 7M of their accrued benefits to purchase a house under a tenant purchase basis.

Amendments have also been proposed to the **Insurance Regulations** to provide for the maximum permitted management expenditure for each class of long-term insurance business.

The Disaster Risk Management Bill, 2021 which is aimed at coordinating disaster response, mitigation and recovery.

The Public Private Partnership Bill, 2021 that intends to revise the legal, operational and institutional structures in the PPP framework with the aim of expediting financial closure of PPP projects.

The following policy initiatives have also been proposed by the Government:

- Introduction of further measures as part of the ongoing reforms in the coffee and tea sectors, to enhance competitiveness of these sub-sectors.
- Finalisation of a comprehensive policy and administrative reforms to fully entrench local assembly of motor vehicles and motorcycles.
- Publication of a National Retirement Policy to harmonise the various existing pension schemes and laws with the aim of securing the interests of beneficiaries and rights of pension contributors.
- Strengthening of the National and County Governments' capacities to manage climate risk through the development of climate change laws.

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Devolution at the center stage of economic revival

Devolution at the center stage of economic revival

The path to transition and stimulating more own source revenue

The transition to the next planning cycle

- Devolution is at the core of stimulating economic growth within the current context.
- The country is at a crossroads, since this is the last budget before the next election cycle. In addition, this is the last allocation before the next five year county integrated planning cycle.

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Own Source Revenue (OSR)

- The pressure on revenue collections at the national level and has put more pressure on counties to enhance their own source revenues (OSR) collection efforts.
- With increased equitable share allocation, counties are expected to sustain efforts towards identifying new revenue streams, automating revenue collection through deployment of one integrated county revenue management system and expanding the revenue base for existing revenue streams.

Devolution - The Highlights from FY 2021/22 budget

Key budget highlights

Equitable allocation

The County Governments allocated KES 370.0 billion as equitable share. This is an increase of KES 53.5 billion from allocation of KES 316.5 billion in FY 2020/21.

17%

The increase in equitable share allocation from FY 2020/21.

- The equitable share allocation is based on the Third Basis formula applicable for the allocation from FY 2020/21 to FY 2024/25 which has following key parameters; (i) Population (18%); (ii) Health Index (17%); (iii) Agriculture Index (10%); (iii) Urban Index (5%); (iv) Poverty Index (14%); (v) Land Area Index (8%); (vi) Roads Index (8%), and; (vii) Basic Share index (20%).
- KES 7.5 billion as conditional allocations from the National Government's share of revenue and KES 32.3 billion from development partners.
- To facilitate performance of the transferred functions, the Nairobi Metropolitan Services (NMS), allocated KES 27.2 billion made up of KES 18.0 billion for recurrent expenditure and KES 9.2 billion for development expenditure.
- KES 7.5 billion as conditional allocations from the National Government share of revenue and KES 32.3 billion from development partners.
- To facilitate performance of the transferred functions, the Nairobi Metropolitan Services (NMS), allocated KES 27.2 billion made up of KES 18.0 billion for recurrent expenditure and KES 9.2 billion for development expenditure.
- In order to provide basic services to previously marginalized areas as envisaged under the Constitution of Kenya, the concerned County Governments have been allocated KES 6.8 billion under the Equalization Fund in the financial year 2021/22. This Fund will be used to finance development programmes that aim at reducing regional disparities among beneficiary counties.
- The National Treasury has developed the Public Finance Management (Equalization Fund) Regulations, 2021, for National Assembly consideration and approval.
- The increased allocation of funds to counties will need to be supported by timely disbursements. This will enhance the counties' ability to fund their operations and provide service delivery to the citizens.

Devolution at the centre stage of economic revival

Other key initiatives in the budget speech

- To ensure that the process of transfer of functions between County and National Governments is fully re-enforced in law, the National Treasury is developing legislation to guide Transfer of Functions and Cooperation between the National and the County Governments.
- To support County Governments' capacities to enhance their own source revenue and reduce over-reliance on equitable share, the National Treasury will rolled out a nation-wide capacity building exercise for the County Governments on interventions contained in the National Policy to Support Enhancement of County Governments' Own-Source Revenue.
- Scaling up of the implementation of Universal Health Coverage to all counties due to the COVID-19 pandemic. In addition there are plans to recruitment of 5000 diploma and certificate level health care workers.
- In order to stimulate youth employment, there shall be creation of over 100,000 job opportunities for the youth under the Kazi Mtaani initiative and 5,500 community scouts in wildlife conservation areas across the 47 counties.
- In order to resolve pending bills issue, a directive has been issued to Government Ministries, Departments and Agencies and the County Governments to clear all their pending bills by 30 June 2021. The PFM Regulation have put in place measures to ensure that procurement of goods and services is only initiated when the budget has been set for that procurement. Delays in payment of pending bills to businesses who provide services to both National and County Governments has affected liquidity and operations of these entities. While we acknowledge that the directive is in the right direction, considering limited left to 30 June 2021, it shall require a massive effort to ensure 100% settlement of all pending bills at the county level by the set deadline. In addition, the CS appealed to Parliament to back the Government's proposal to temporarily stop transfers to County Governments that persistently fail to comply with the directive to clear pending bills.
- In order to manage climate risks, the Government has partnered with development partners in the implementation of the proposed Financing Locally Led Climate Action Program and has already mobilized funding of over KES 18 billion to support the initiative for the next five years. The purpose of the program is to assist the National and county governments to manage climate risk, establish a county climate change fund and develop climate change laws.

4

Sectoral analysis

Financial Services

Banks' importance to the post pandemic recovery phase

The Cabinet Secretary acknowledged the important role played by banks in cushioning Kenyans from the adverse impact of the COVID-19 pandemic. He further stated that the sector is key to the post-pandemic recovery phase.

Protecting borrowers

The Cabinet Secretary noted that the government had, through the Central Bank of Kenya (Amendment) Bill 2021, proposed to license digital credit service providers. The Bill, which was submitted to Parliament in April 2021, is seen as a measure to protect Kenyans from high charges and other unfair practices. Currently, there is no legal framework governing the digital borrowing platforms.

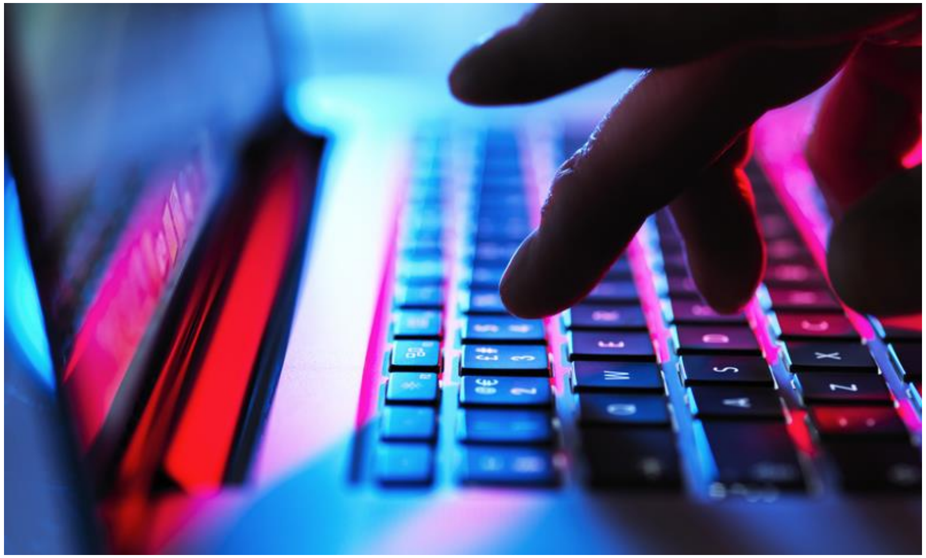
Enhancing access to affordable credit and housing

The Cabinet Secretary noted that the government had operationalized the Credit Guarantee Scheme by providing KES 3 billion seed capital. He stated that the capital will be progressively raised to KES 10 billion, with KES 2 billion being allocated to the scheme in the current budget.

The scheme is aimed at making lending to micro, small & medium enterprises (MSMEs) less risky and therefore encouraging lending to the subsector. It remains to be seen whether the scheme will have a significant impact on the subsector.

Under the affordable housing program of the Government's Big Four agenda, the Cabinet Secretary proposed to allocate KES 3.5 billion to the Kenya Mortgage Refinance Company (KMRC). KMRC offers fixed rate long term loans at concessional rates to mortgage providers.

In addition, he announced that the KMRC is set to issue an infrastructure bond by October 2021 and will issue green bonds in future to finance climate friendly housing projects.



Tax measures contained in the Finance Bill 2021

i. Excise duty on fees and commissions on loans

The Cabinet Secretary has proposed to amend the definition of "other fees" as contained in the Excise Duty Act, 2015 by deleting the words "fees or commission earned in respect of a loan". The proposal appears to be a departure from the amendment in the Finance Act 2019 which clarified that 'fees and commissions earned in respect of a loan or any share of profit' are not subject to excise duty. Excise duty on 'other fees' has in the past been a contentious issue between the Kenya Revenue Authority (KRA) and banks due to lack of clarity on whether or not fees and commissions earned in respect of loans constitute 'other fees' subject to excise duty. This proposal is likely to lead to the re-emergence of tax disputes between KRA and financial institutions.

ii. Interest restriction

The Cabinet Secretary has proposed to limit the deduction of interest expense to a maximum of 30% of EBITDA. The proposed restriction will also apply to payments that are economically equivalent to interest and expenses incurred in connection with raising finance. Interest restrictions based on interest to EBITDA ratios are in line with recommended best practices by the OECD of protecting the tax base by minimising excessive deductions of interest. As currently drafted, the proposal is a significant divergence from the established practice of excluding financial institutions from such interest restrictions. This is on the basis that interest expense is akin to a financial institution's 'cost of sales'.

Strengthening Nairobi's position as a regional financial hub

Following enactment of the Nairobi International Financial Centre (NIFC) Act in 2017, the Cabinet Secretary directed the Authority to publish a framework for attracting investments and innovative financial services by December 2021. The Government has moved slowly over the years in establishing and operationalising the NIFC, and it remains to be seen how much progress will be made in the year.

Extension of common reporting standards

Following ratification of the Convention on Mutual Administrative Assistance in tax matters, the Cabinet Secretary seeks to introduce Common Reporting Standards (CRS) which will require financial institutions to identify reportable accounts, collate information in a standard format and provide this information to the KRA. The KRA would systematically and periodically exchange such taxpayer information with authorities of countries that are signatories to the CRS convention or a tax authority that is the subject of bilateral agreement.

This will introduce onerous compliance obligations for banks and attract penalties for non-compliance.

Financial Services (continued)

Amendments to the Insurance Act

The Cabinet Secretary proposed amendments to the Insurance Act:

- to provide for the regulation of foreign insurance brokers. This will safeguard the interests of insurers and policyholders, and
- to align the maximum permitted management expenditure with the classification of long-term insurance business lines that had been implemented in 2009. The amendment is expected to improve compliance and reduce the tax burden on the long term insurance business.

Enhancing accessibility and efficiency of capital markets

The Cabinet Secretary proposed to amend the Central Depositories Act to allow opening of investment accounts by persons investing on behalf of others. This is expected to increase inclusivity by allowing collective investments by groups.

An amendment to the Capital Markets Act has been proposed to introduce a time limit of 90 days to the tribunal for hearing and determining appeals. The faster resolution of issues is expected to enhance efficiency in the capital markets.

The Government intends to operationalise an electronic, over-the-counter secondary market platform for Government securities by June 2022. This is expected to improve pricing efficiency, increase transparency in trading of securities and grow the domestic debt market.

Financial Services (continued)

Enhancing retirement benefits services and coverage

The Cabinet Secretary has proposed the following measures aimed at improving the provision of retirement benefits in the country:

- the National Treasury will implement a pensions information management system to help in clearing the pension liability backlog. This will enable the beneficiaries to receive payments promptly;
- development of a National Retirement Benefits policy to harmonize all pensions laws. The policy will cover both the formal and informal sector and will seek to protect beneficiaries and pension holders; and
- roll out a national informal sector pension scheme in the next financial year. The scheme will target 15 million informal sector workers thus enhancing inclusivity

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40%

Increase in cumulative pension payments

Regulation Amendments

Amendment of the Retirement Benefit Act to allow for registration and regulation of corporate trustees. This is expected to allow for professional management of pension schemes and improve governance.

Treasury has developed post-retirement medical regulations which will allow members to make contributions to a medical fund that can be accessed at retirement or transferred to a medical insurer. This is expected to increase access to health care by retired citizens.

An amendment to the Retirement Benefits Act has also been proposed to regulate stand-alone post retirement medical funds, which is expected to safeguard the members.

Infrastructure highlights

Introduction

Infrastructure is generally regarded as the main enabler of an economy. In keeping with that trend, infrastructure has received generous allocation in this Budget. Being President Kenyatta's final term, it appears that several projects and developments are planned to showcase his legacy.

These cut across the country and focus on roads, rail, energy, ports and airports. The activity generated from the investment should help reinvigorate the economy following the depressed growth during the COVID-19 pandemic.

Furthermore, the Cabinet Secretary has forwarded to Parliament proposed amendments to the PPP Act intended to hasten the time to financially close projects, and encourage the private sector to partner in infrastructure development.

Rail, road, airports and airstrips

In a bid to boost regional connectivity, improve rural accessibility and ensure continuous urban decongestion, especially within the Nairobi central business district, the government has singled out rail as a key enabler. It will benefit from the following allocations:

- KES 27.2 billion for phase II of the SGR
- KES 2 billion for the Naivasha ICD
- KES 1.3 billion for the railways metro line
- KES 1.1 billion for the Nairobi-Nanyuki meter gauge rail; and
- KES 700 million for rehabilitation of the Nakuru-Kisumu meter gauge rail.

These investments, coupled with those in other intermodal and last mile solutions, will continue to enhance efficiency of Kenya's critical transport and logistics sector.

KES 603M

The CS has also allocated an additional KES 603 million for the construction and expansion of airports and airstrips. While the CS did not directly highlight specific amounts allocated to roads construction or rehabilitation, all these infrastructural developments will lead to improved road networks.

The ripple effect is then expected to drive economic development in the rural areas, improve regional trade and act as a business incentive for potential investors.

Energy: Power Transmission and Distribution

Background

The COVID-19 pandemic has not only affected economic growth but also slowed down activities such as power generation capacity development and implementation of transmission and distribution lines.

Reduced demand has exacerbated the systemic challenges of stranded power as a result of supply-demand mismatch and transmission system constraints for over-generated capacity.

In order to cushion the sector and shore up financing for investment into power infrastructure, the Treasury has set aside KES 71.9 billion to support the reliable and affordable energy agenda.

KES 11.3B

has been allocated for the development of geothermal energy

Included in this allocation is KES 50.1 billion directed towards constructing additional transmission and distribution lines and establishing new substations to extend power supply in rural areas.

On the generation side, KES 11.3 billion has been allocated for the development of geothermal energy, further cementing geothermal as the preferred generation technology to supply Kenya's base load demand.

This allocation is broadly in line with Kenya's long term energy sector plan which entails running geothermal and hydro technologies exhaustively before turning to other technologies such as nuclear plants.

Nuclear energy and coal exploration were collectively allocated KES 1.3 billion, which can be viewed as a strategy to prime the pump for generation mix diversification in the long term.

Solar and wind generation investors will receive reinstated tax exemptions on VAT for equipment while power producers that have signed Power Purchase Agreements (PPAs) before April 2020 will continue benefiting from VAT exemption in respect of taxable goods until the projects run their full lifecycle. This is a welcome relief for investors who recently had these incentives withdrawn.

Energy: Power Transmission and Distribution

Alignment with other policy instruments and long term sector plans

Under the revised FiT Policy, all solar and wind power projects, as well as other RE projects larger than 20MW, will be procured under the Renewable Energy Auction Policy.

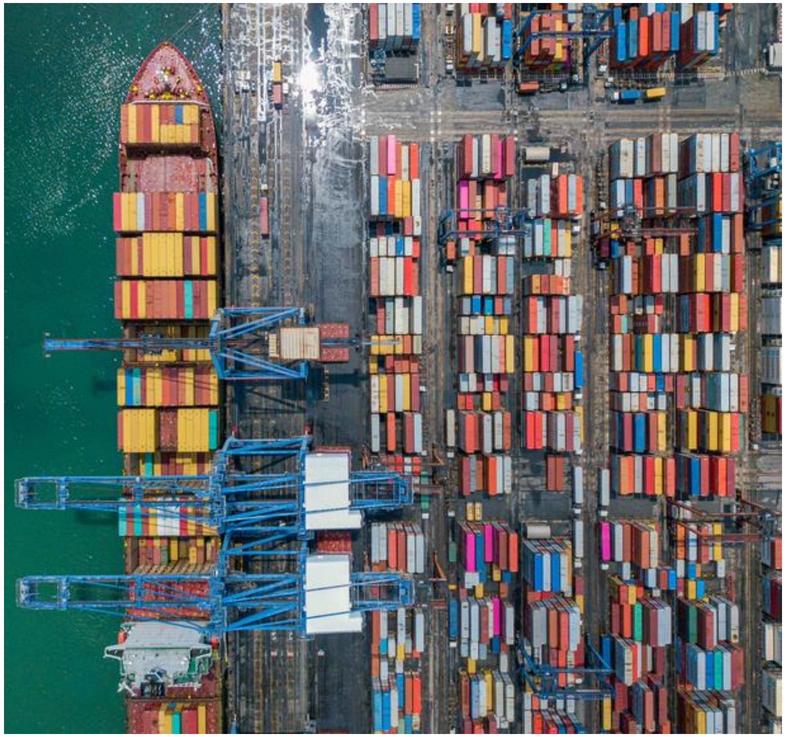
Geothermal projects, on the other hand, will be procured under the Policy on Licensing of Geothermal Greenfields.

The end goal for the allocations into the energy sector is to attain universal access while supporting ongoing projects and programs aimed at reducing system losses and improving system reliability.

Anticipated new demand from heavy consumption is expected from projects such as the electrification of public facilities such as the Standard Gauge Railway (SGR) as well as Special Economic Zones and industrial park investments. These electrification initiatives have received an allocation of KES 6.4 billion.

Ports Infrastructure and Economic Zones

Enhancing local manufacturing and regional trade



Sea ports, being the key entry gateway into the country and the region, remain an area of infrastructure investment focus for the government. In particular, additional budgetary allocations have been made for the development of the LAPSSET project. With the recent launch of the first berth at the Lamu Port, a number of investment initiatives seek to enhance the utilisation of the Lamu port and attract more ships to the port. These include:

- KES 3. 0 billion Free Disease Holding Ground for livestock exports through the port;
- KES 1.0 billion for construction of a Fish Processing Plant in Lamu; and
- Allowing refuelling of ships at the port by other ships and bulk fuel storage facilities to be established.

Specific allocations to the development of the support infrastructure of the LAPSSET corridor, including roads and railway lines, remain to be seen to actualise the plans for improved interconnected and interregional trade through the movement of labour and cargo.

Additionally, the government has also proposed allocations of KES 7.5 billion to the Mombasa Port Development Project.

Special economic zones and industrial parks

As part of realising and implementing the the Big Four agenda and Economic Recovery Strategy, the government also plans to facilitate industrial investments in the country through the operationalisation of special economic zones in Dongo Kundu (KES 8.5 billion), Naivasha (KES 350 million), and Kisumu and additional investments in industrial parks, specifically the Kenanie Leather Industrial Park and Athi River Textile Hub.

Other proposed allocations relate to improving existing infrastructure such as the KES 130.2 million modernisation of the RIVATEX and KES 800 million budgeted for improving access roads into industrial parks.

These investments may address the relatively lower levels of value addition in the country. However, the investments will need to be coupled with added measures to address investor concerns on appropriate incentive structures and policy stability.

This will help to achieve the desired increase in economic contribution by the manufacturing sector and broader economic development.

Conclusion

The significant allocation to infrastructure in this year's budget reflects the importance of the sector in promoting local manufacturing and improving regional trade and connectivity.

The government intends to invest in the energy sector with the application of measures to increase and improve access to electricity and stabilise the grid, as well as through encouraging and facilitating investments into economic zones to develop a robust manufacturing base, which will also absorb current and planned power generation capacity.

Regional trade and connectivity continues to be a priority as the government seeks to reduce the trade deficit and increase foreign exchange earnings, as access to regional markets continues to be a key growth driver for manufacturers and trading businesses.

Overall, to realise its ambitious infrastructure targets, the government will need to define a clear and sustainable deployment mechanism. This will involve adopting a prudent balance between government-funded efforts and various private sector participation models, especially in the context of increased budgetary deficit and reduced debt carrying capacity.

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Manufacturing

Despite the adverse impact of the COVID-19 pandemic, the government remains committed to supporting Manufacturing as a key pillar of the Big Four Agenda

COVID-19 disruptions

The government has reaffirmed its commitment to support and fast track the growth of the manufacturing sector as part of the Big Four agenda, in the wake of a difficult operating year on account of the COVID-19 pandemic.

The Cabinet Secretary indicated the government will promote local industries with an allocation of KES 20.5 billion under various implementing Ministries, Departments and Agencies.

Micro, Small and Medium Enterprises are set to play a significant role in boosting the manufacturing sector with various support initiatives including; KES 2.0 billion to the Credit Guarantee Scheme and KES 600 million for provision of finances through Kenya Industrial Estate.

Continued investment into Special Economic Zones

The government is banking on special economic zones to spur growth of industries in the counties to help the manufacturing sector recover from a difficult operating year.

KES 8.3 billion has been allocated for Dongo Kundu Special Economic Zone, a significant increase from the 3.0 billion allocated in last year's budget. Other areas that received cash injections include;

- KES 350 million for the development of the Special Economic Zone Textile Park in Naivasha;
- KES 90 million for the Freeport and Industrial Park Special Economic Zone in Mombasa and;
- KES 130.2 million for the modernization of 63 RIVATEX.

The government is looking to local manufacturers to boost opportunities for employment and save in foreign exchange

Local assembly

The Government continued to support local assembly of motor vehicles and motor cycles by providing various tax incentives including removal of excise duty on locally assembled motor

vehicles, duty-free importation of Completely Knocked Down kits and reduced corporate tax from 30 to 15

percent for the first five years of operation. The Cabinet Secretary indicated that the industry responded well to these incentives with licences awarded to 13 motor vehicle and 17 motorcycle assemblers.

With these local assemblers, the government will have created employment opportunities and saved the country in foreign exchange.

Local manufacturing

The Cabinet Secretary indicated that there has been an increase in capacity of the metal and allied subsector. However, the local manufacturers in this sub-sector continue to face stiff competition from cheaper imports.

In order to continue protecting this sub sector, the EAC Partner States agreed that imported iron and steel products shall continue attracting a duty rate of 25 percent with the corresponding specific rates for a further one year.

EAC partner states have also agreed to extend the duty-free importation window for raw materials and inputs for production of masks, sanitisers, ventilators and personal protective equipment for a further one year to help the ongoing fight against the Covid-19 pandemic.

Imported iron and steel products shall continue attracting a duty rate of 25%

Tourism and Hospitality Sector

The government plans to use targeted interventions to stimulate an industry that has been significantly hit by the COVID-19 pandemic

Industry contraction

Restrictions on travel to combat COVID-19 have reduced airline travel and accelerated cancellations of hotel reservations. The result has been reduced foreign exchange inflows and severely impacted service sector-related employment across the country.

According to KNBS, Kenya received 439,487 tourists in 2020 through Jomo Kenyatta and Moi International Airports, a significant decline from 1.54 million tourists received in 2019.

The sector is expected to recover gradually in 2021, following the relaxation of travel restrictions, the opening of international travel and the implementation of restaurant management protocols and travel health and safety protocols.

Tourism sector allocations

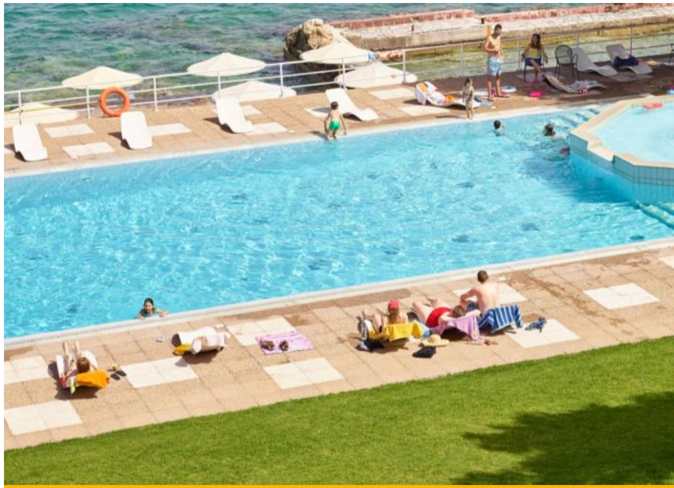
The government plans to stimulate the recovery of the tourism and hospitality sector as part of its targeted strategic interventions.

The Cabinet Secretary acknowledged that the COVID-19 pandemic and the subsequent containment measures have greatly affected the tourism sector.

As such, the government has allocated KES 1.7 billion for the tourism fund and KES 643 million for the Tourism Promotion Fund to support the recovery of the Tourism and Hospitality Sector. These figures are a significant decrease from the KES 9.3 billion allocated to tourism recovery in the 2020/21 national budget.

439,487

Tourists visited Kenya in 2020



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Health

At least 18.9% of the national health sector budget goes to COVID-19 response: A key pillar to rebuilding the economy

Highlights of the health sector budget

- Implementation of the big four agenda remains a priority in this budget with KES 121.1B being allocated to the health sector.
- To bolster the fight against COVID-19, the government has introduced some tax relief measures on various pharmaceuticals and medical equipment.
- An amount of KES 14.3B has been allocated for the purchase of COVID-19 vaccines.
- Universal Health Care (UHC) still remains relevant with KES 47.7B allocated.
- To enhance the capacity of the healthcare system, an mount of KES 1.2B has be allocated for the recruitment of 5,000 healthcare workers.

Focus on COVID- 19

- The COVID-19 pandemic overstretched Kenya's health care system and hence the country's response to it is key to rebuilding the economy.
- Since 13 March 2020 when the first case was confirmed in Kenya, a total of 173,000 COVID-19 confirmed cases have been detected as of 9 June 2021. All counties are affected (Nairobi, Kiambu and Mombasa are the top 3 counties).
- So far, over one million Kenyans have received the first dose of the vaccine. There remain challenges to the vaccine roll-out. To address this, KES 14.3B has been allocated for COVID-19 vaccines.
- As a preventive measure, KES 8.7B has been allocated to mitigate against emergence of new COVID-19 variants.

KES 14.3B

allocated for COVID-19 vaccine

KES 121.1B

allocated to health sector in this year.

Health

Where the money goes

Key budgetary allocation to other sector priorities

- To enhance early diagnosis and management options for cancer and reduce the burden of treatment among Kenyans, an allocation of KES 800M for procurement of Cyberknife Radiotherapy Equipment and the establishment of two cancer centres in Meru and Kakamega
- An allocation of KES 5.8B to support and manage fight against HIV/AIDS, Malaria and tuberculosis in the country.
- To enhance vaccines and immunizations programme, we have set aside KES 3.9B.
- KES 4.1B for Free Maternity Health Care;
- KES 7.2B for the Managed Equipment Services (MES) as well as KES 1.8B to provide medical cover for the elderly and severely disabled persons in our society.

KES 38.1B allocated for the improvement of health service delivery to:

- Kenyatta National Hospital
- Moi Teaching and Referral Hospital
- Kenya Medical Training Centres
- Kenya Medical Research Institute
- Kenya National Hospital Burns and Paediatrics Centre

18.9% of the health sector budget has been allocated to bolster COVID-19 responses, and whereas this is necessary to support the rebuilding of the economy, the pandemic continues to compete for scarce resources in the health and economy sectors.

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Agriculture

The quest for attaining food and nutrition security:

Value addition and diversification in the agriculture sector

The agricultural sector is the economy's backbone, with enormous growth and transformation potential. The sector's contribution to GDP has stagnated at around 32-33% with relative decline in the last few years. With more than 60% of Kenya's exports attributable to agriculture, and through its links to other sectors including manufacturing, distribution, and services, agriculture contributes an extra 27% to GDP. Furthermore, the sector's contribution to labour participation is significant; 40% of the population – and 70% of the rural population – is employed in agriculture.

Agricultural output and value addition comprise 80% crops, 15% livestock, 2% fish and aquaculture and 3% others, such as forestry and support services. The sector experienced resurgent growth of slightly over 1% in the third quarter of 2020 mainly attributable to tea, fruits and sugarcane. While this indicates optimism, the challenges of COVID-19 continued to suppress activity within this sector.

KES 60B allocated to Kenya's agriculture sector in this year's budget

Through the budget lens

The FY 2021/22 agricultural sector allocation is KES 60 billion compared to KES 52.8 billion in FY 2020/21, representing a 5% increase. In addition, a number of initiatives within the Economic Stimulus Programme and Economic Recovery Strategy were proposed and are poised to contribute to food and nutrition security and improve household income in line with the Big Four agenda and the Agriculture Sector Transformation and Growth Strategy.

Agriculture (continued)

Focus areas in the FY 2021/22 budget

- allocation to the livestock sector targeting smallholder farming and pastoral communities in Kenya, while enhancing value chains;
- blue economy resources aimed at increasing fish production by refurbishing Liwatoni Fishing complex and setting up a new fish processing plant in Lamu. This will promote exports and increase incomes for the local fishermen;
- cash crops allocation proposed for the revitalization of the coffee industry, modernization of cooperative cotton ginneries as subsidy and extension support; and
- continued funding of the existing projects including an allocation for the emergency locust response and irrigation projects.

In our view, the measures and interventions proposed within the agriculture sector will enhance diversification. It remains to be seen, however, whether they are extensive enough to spur the requisite economic growth, increasing employment and thus disposable income for aggregate demand creation.

Aside from the increased allocation in the FY 2021/22 budget, we note the following were not sufficiently addressed:

- Allocation to deal with external shocks with regard to the recurrent droughts and floods as well as adverse weather conditions;
- Ring-fencing county allocations through conditional grants to secure investment in agriculture given that it is a devolved function;
- Initiatives to deal with management of farm produce thus reducing middlemen, post-harvest losses and improve post-harvest handling;
- Digitising agriculture to enhance agricultural extension services and agricultural innovations to promote access to market for produce; and
- Establishment of large-scale agro and food processing hubs across the country through a rapid Public-Private-Partnership (PPP) process targeting both domestic and export markets.

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Technology

Digitization of the economy set to catalyze economic recovery, create jobs and improve lives and livelihoods of Kenyans

Digitization of the economy

The government remains focused on developing a digital economy, viewing it as a key contributor to the socio-economic development of the country. In his budget remarks the Cabinet Secretary indicated that the government will upscale investment in ICT and digital infrastructure in order to facilitate e-commerce and efficient delivery of public services.

The Government will continue to leverage on digitization of the economy as a way to catalyze economic recovery, create jobs and improve lives and livelihoods of Kenyans.

To leverage on technological gains, the budget allocates KES 20.9 billion to fund initiatives in the Information, Communication and Technology sector. Specifically, this allocation includes;

- KES 1.0 billion for Government Shared Services;
- KES 1.2 billion for maintenance and rehabilitation of the National Optic Fibre Backbone Phase II Expansion Cable;
- KES 1.1 billion for installation and commissioning of Eldoret-Nadapal Fibre Optic Cable;
- KES 463.0 million for maintenance and rehabilitation of Last Mile County Connectivity Network.

KES 463.0 million

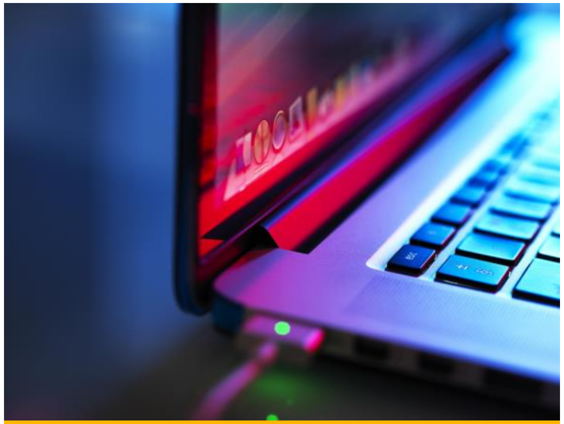
for maintenance and rehabilitation of Last Mile County Connectivity Network

The government will continue to invest in its flagship programs with the aim of transforming Kenya into a digital economy

Konza still a flagship program

Despite having stalled over the past several years, the Konza Technopolis remains a key investment area as part of the government's technology agenda. The smart city will take up an estimated 70% of the Information and Communication Ministry's budget. To fast track development, the following allocations were made to Konza:

- KES 12 billion for Horizontal Infrastructure Phase I;
- KES 3.6 billion for Konza Data Centre and Smart City Facilities;
- KES 400 million for construction of Konza Complex Phase 1 B and; KES 200 million for development of Konza Technopolis Masterplan.



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E-Government Procurement

The government looks to continue last year's plan to automate public procurement. A deadline has been set for 31 December 2021 for the roll out of an end-to-end procurement system.

Anticipated benefits include: savings as a result of greater efficiency, reduced operational costs and enhanced transparency and accountability through increased bidder participation.

Digitization of land records

To support the affordable housing agenda, the Cabinet Secretary indicated that significant progress has been made to enhance efficiency, transparency and certainty in land matters by re-engineering the land registration processes and the digitization of land records.

Workforce

Creating employment at the centre

The theme of this year's budget is *"Building Back Better: Strategy for Resilient and Sustainable Economic Recovery and Inclusive Growth".* Key workforce initiatives to enable employment opportunities include:

Equity, poverty reduction, women and youth empowerment

- KES 3 billion proposed under the *Kazi Mtaani* Initiative for youth empowerment and empowerment. The program in FY21/22 aims at creating over 100,000 job opportunities.
- KES 1 billion allocated Kenya Wildlife Services to engage 5,500 community scouts in wildlife conservation areas across the 47 counties.
- To empower the youth and support businesses owned by youth, women and persons living with disabilities, KES 10 billion proposed for the National Youth Service; KES 4.2 billion for the Kenya Youth Empowerment and Opportunities Project; KES 454.1 million allocated for the Youth Enterprise Development Fund; KES 120.0 million for the Women Enterprise Fund; and KES 62 million for the Youth Employment and Enterprise Fund.

Health

- For the enhancement of healthcare system capacity, KES 1.2 billion has been allocated for the recruitment of 5,000 diploma and certificate level healthcare workers for one year under the Universal Health Coverage.

Education Outcomes

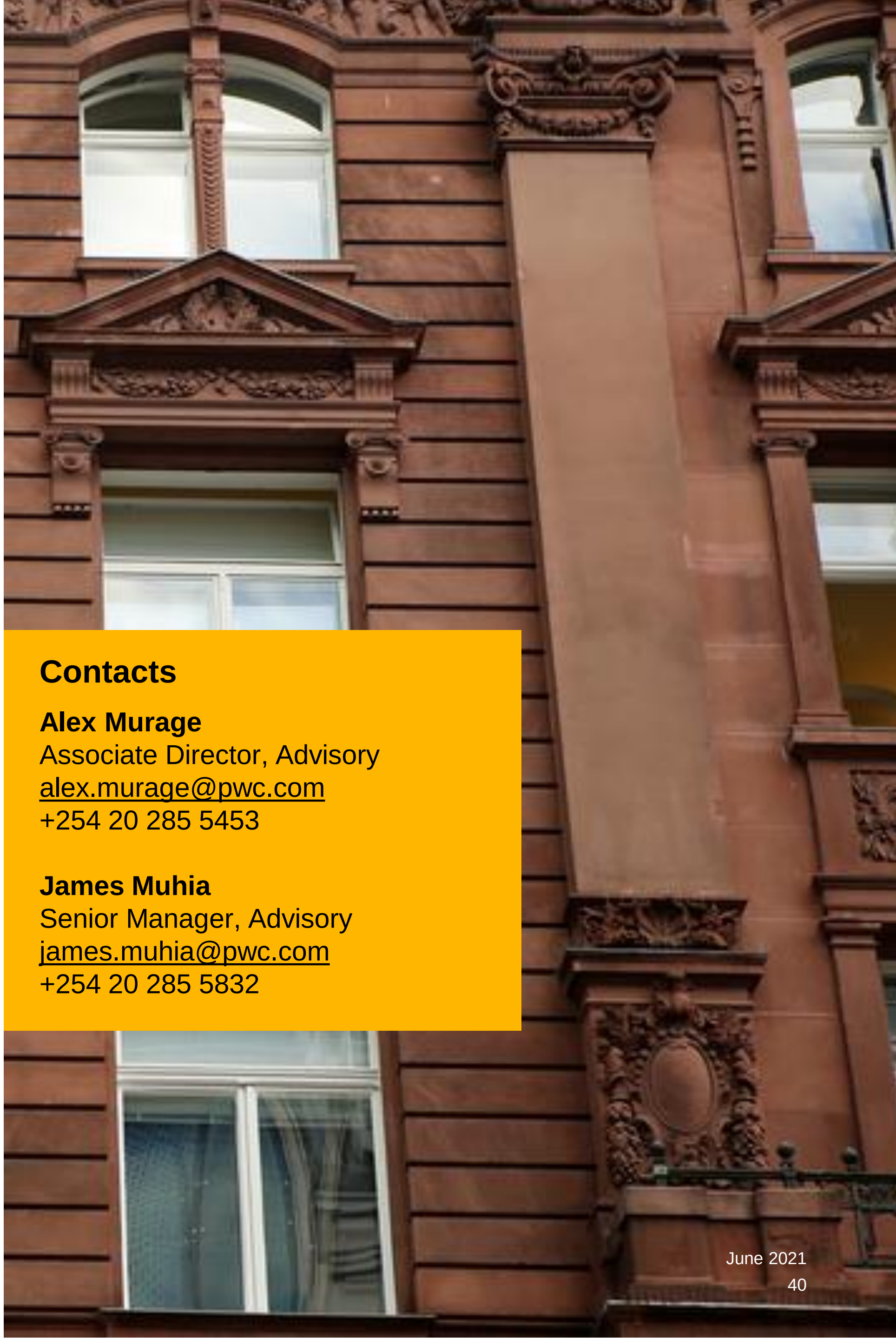
- KES 2.5 billion proposed for the recruitment of teachers.
- Improvement of education outcomes to be realized through the construction of additional classrooms in secondary schools, procurement of locally fabricated desks for both primary and secondary schools and recruitment of 4,000 and 8,000 primary and secondary school intern teachers, respectively.
- KES 1.0 billion planned for the Competency Based Curriculum and KES 420.0 million for the Digital Literacy Programme and ICT Integration in Secondary Schools.
- Under the Economic Stimulus Programme, KES 6.4 billion set aside for improving education outcomes and KES 633.0 million for promotion of Youth Employment and Vocational Training.
- To equip the youth with essential training and internship opportunities; KES 1.4 billion proposed for the Kenya Industry and Entrepreneurship Project; KES 800 million for the Kenya Youth Employment and Opportunities Project; KES 448 million for Industrial Research Laboratories; and KES 199.5 million for Constituency Industrial Development Centers.

Big Four agenda

- Implementation of priority programs under the Big Four agenda has been cited as a critical path to supporting sustainable economic recovery and accelerating employment creation.
- Approximately KES 9.6 billion has been allocated for special economic zones, textile parks and industrial park facilities to unlock additional employment opportunities.
- The government has approved 13 motor vehicle and 17 motorcycle assemblers. These local assemblers have created employment opportunities while also saving the country substantial foreign exchange.

“Our rallying call in this year’s budget is therefore job creation through continued and sustained economic growth. To strengthen this position, we shall implement a comprehensive Economic Recovery Strategy that will expand economic activities and address these challenges.”

HON. (AMB.) Ukur Yatani, EGH,
Cabinet Secretary for the National Treasury and Planning,
Republic of Kenya



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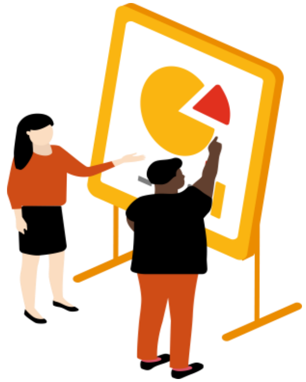
4

East Africa highlights

East Africa highlights

Kenya



Summary of growth in 2020/21

- In 2020 the Kenyan economy grew by 0.6% compared to 5.4% in 2019. This decline is mainly attributed to the outbreak of COVID – 19 pandemic.
- The service sector experienced a significant activity drop in growth compared to 2020.
- The Agricultural sector experienced a modesty growth in 2021 providing a much needed cushion to the economy from declining further. While the second quarter of 2020 registered a reasonable growth many other sectors of the economy experienced contraction.
- The CS painted a 6.6% ambitious overall economy growth projection with 6.1% growth expected in the medium term.

2021 Economic constraints

The economic growth rate declined due to the following:

- COVID–19 pandemic – The pandemic caused a devastating effects in all sectors of the economy hence reducing the GDP growth
- Invasion of desert locusts and floods – causing food security risk, undermining economic growth and loss of livelihoods.

However, towards the end of 2020, there was adequate rainfall received which cushioned the economy's performance from further shrinking. This boosted Agriculture sector which grew by 6.3% in quarter 3 of 2020 compared to 3.6% growth in 2019.

Government priorities

The government is trying to take deliberate measures to strike a balance both in stimulating economic recovery and responding to the health challenges and effects of COVID-19 pandemic.

- Implementing the Economic Stimulus Programme (ESP) focusing on the vulnerable, particularly the emerging urban vulnerable by cash-transfer programs, health workers recruitment and implementing interventions under the post COVID-19 Economic Recovery Strategy; and
- Implementation of the "Big Four Agenda" i.e. universal healthcare, food security and nutrition, manufacturing and affordable housing.

East Africa highlights: **Kenya**

Key tax highlights

Value Added Tax

- Widened scope of the VAT on digital economy by expanding the definition of the digital marketplace on the VAT Act to include all online platforms that enable users to sell or provide services, goods or other property to other users.
- Prohibition from deducting input tax incurred on hiring or leasing of passenger cars or minibuses.
- Elimination of group VAT registration option as one person for VAT purpose.
- Regulations under the VAT Act to take effect after publication without having to be tabled before the National Assembly;
- Change in status of exported services from zero rate to exempt.

The following are now VAT exempt:

- Medicaments used in our health facilities including decongestants and food supplements.
- Diagnostic and laboratory reagents, artificial respirators including therapeutic respiration apparatus, breathing appliances, gas masks as well as medical equipment and technologies used in the provision of medical services.
- Inputs used in the manufacture of medical ventilators and breathing appliances.
- Goods for exclusive use in geothermal or oil exploration and mining prospecting.
- Equipment for generation of solar and wind energy.
- Asset transfer into the Real Estate Investment Trusts and Asset Backed Securities.

Income Tax

- Requirement by entities with operations outside Kenya to file returns on activities in other jurisdictions.
- Digital service tax to also be charged on business carried out over the internet or an electronic network, in addition to business over a digital market place.
- Definition of permanent establishment in attempt to align the Income Tax Act to the International best practice.
- Tax losses can be carried forward indefinitely, from the previous 10 years restriction.
- Replacement of the current thin capitalization provisions based on debt to equity ratio with a new requirement that interest can only be deducted to a maximum of 30% of Earnings Before Interest Tax, Depreciation and Amortization (“EBITDA”).

East Africa highlights: **Kenya**

Income Tax cont'd…

- A tax rebate of 50% for employers who offer internship to at least 10 apprentices from technical, vocational institutions in addition to the existing rebate on university graduates.
- A proposal to change the basis used for calculating investment allowances from a reducing balance basis to a straight-line methodology.
- Alignment of the withholding tax rates applicable to payments made to subcontractors for services rendered in respect of mining and petroleum operations and other management fees not falling within the definition of service fees to 10%.

Excise duty

- Relief from excise duty paid on internet data services purchased in bulk for resale.
- Sugar confectionary and chocolate manufactured locally to be subject to excise duty.
- Imported glass bottles have been excluded from the purview of excise duty.
- Change from 'specific rate regime' to 'ad valorem rate regime for motorcycles of tariff 87.11.
- Introduction of excise duty on jewelry and nicotine products.
- Reintroduction of excise duty on betting activities at the rate of 20% of the amount wagered or staked.
- Fees or commissions earned in respect of a loan to be subject to excise duty.

Employment taxes

- Proposed introduction of a15% National Hospital Insurance Fund (NHIF) insurance tax relief on premiums.

Miscellaneous fees and levies

- Taxpayers' eligibility to apply for a refund of overpaid fees and levies or fees and levies paid in error.
- Introduction of exemption from Import Declaration Fee("IDF") and Railway Development Levy("RDL") on imported goods valued at KES five (5) billion or more where goods are imported for the interest of the public or to promote investment.

East Africa highlights: **Kenya**

Custom duty

- Duty-free importation window for the following items has been extended for one year:
    - raw materials and inputs for manufacture of masks, sanitizers, ventilators and personal protective equipment remission;
    - inputs for manufacture of roofing tiles for use in affordable housing scheme;
    - input for manufacture of baby diapers;
- Import duty at 25% on iron and steel products is extended for one year to protect the local industry.
- To protect local farmers, vegetable products including potatoes, peas and tomatoes will be subject to import duty of 30%.
- In order to protect the local leather and footwear products manufacturers, the 25% import duty will continue to apply on these products. A further specific duty rate has been introduced to guard against undervaluation of products imported.
- To guard against cheap and low quality imports and also protect the Jua Kali sector, the 35 import duty on furniture has been extended for a further one year.

Tax administrative changes

- Introduction of a 90 days time limit for the hearing and determination of appeals at the Capital Markets Tribunal from the date of filing of the appeal.
- Introduction of common reporting standard obligations for automatic exchange.
- There is a proposal to enhance the reward payable under the Kenya Revenue Authority Act for persons who provide information leading to the identification or recovery of unassessed taxes or duties.
- The Bill proposes to increase the period within which assessments can be amended by the Commissioner from five years to seven years.
- Increase of the statutory document retention period from the current five years to seven years.

East Africa highlights

Uganda

Summary of growth in FY21

- Uganda's economic growth for 2020/21 is projected at 3.3%, rising slightly from 3.0% for the prior year. This is significantly below the average growth of 6.5% for the preceding two years, largely due to the impact of the Covid-19 pandemic.
- Headline inflation is projected at 4.7%, within the government's 5% target but above the prior year rate of 2.9%.

Economic drivers in FY21

Economic drivers for the year as identified by the government include:

- Peace, security, good governance and an efficient and effective judicial system.
- Scientific research and innovation, transforming Uganda's industrial base.
- The steady growth of the mining industry continues to be a major contributor to Uganda's economy with its contribution to GDP increasing from 1.1% in 2016/17 to 2.3% in 2020/21.
- Increased access to electricity which now stands at 51% of which 24% is on-grid and 27% off-grid.

Government priorities for FY22

The main government focus is to strike a balance between stimulating economic recovery through the following interventions:

- Boosting business activity through financing private sector growth as well as investment promotion.
- Promoting agro-industrialisation in order to address challenges resulting from low production and productivity of primary agriculture, poor post-harvest handling and storage, limited value addition and insufficient market access.
- Establishment of infrastructure for economic growth and development including transport infrastructure and power infrastructure.
- Digital transformation in order to enhance socio-economic transformation and improve efficiency and productivity especially under restricted movements presented by the Covid-19 pandemic.

Key tax highlights

Value Added Tax

- Input tax credits must be claimed within six months (previously no time limit).
- New quarterly return filing requirement for certain taxpayers making supplies to non-taxable persons (e.g. non-residents supplying electronic services).
- A refund of 5% of the VAT incurred by non-taxable persons on purchases above UGX 5 million per month where supported by electronic invoices.
- New exemptions for LPG and denatured ethanol made from cassava.
- New exemption for imported services used to make exempt supplies.
- Removal of exemption for clinker and inputs to limestone mining.
- Potential imposition of an automatic 200% penalty for errors in VAT returns.

Excise duty

- Remission of excise duty paid on plastic packaging for exported goods, medicaments or plastic bags manufactured from recycled plastics.
- Introduction of a 12% excise duty on internet data (previously nil). This rate will now apply uniformly to all telecom services.
- In conjunction with the above, repeal of the Over the Top ("OTT") social media tax of UGX 200 per day.

- Introduction of excise duty on fermented beverages including cider, perry, mead, spears or near beer at the higher of 60% or Ushs.950 per litre.
- Increase of UGX 100 per litre on petrol and diesel.

Income Tax

- Removal of concurrent deduction of initial and normal depreciation allowances on new assets in the first year.
- Change in asset classification for motor vehicles and other automobiles resulting in a reduced tax depreciation rate of 20% (compared to the current 30% or 35%).

East Africa highlights: **Uganda**

Income Tax cont'd…

- All landlords (both corporate and individual) to pay rental tax at the same rate of 30% and be allowed a fixed deduction of 75% of rental income (giving an effective tax rate of 7.5% on gross rents).
- Support for automatic exchange of information where such is provided for in an international agreement.
- CPI indexation in the calculation of capital gains for assets held more than 12 months.

Tax administration changes

- New requirement for an applicant to have a Tax Identification Number (TIN) before a government authority can issue any form of business licence.
- Introduction of an Alternative Dispute Resolution procedure to assist in resolving tax disputes.

East Africa highlights

Tanzania

Summary of growth in 2020

Tanzania recorded GDP growth rate in 2021 of 4.8%, lower than projection of 5.5% and 7% in 2020. The decline was due to the impact of COVID-19 in Tanzania's trading partners and floods which damaged transport infrastructure and delayed implementation of some development projects.
Inflation remained stable at 3.3% as compared to 3.4% in 2020.

Revenue policies

The Government seeks to increase domestic revenue collections through a number of measures including:

- improving business and investment environment by harmonising, abolishing and reducing tax rates, levies and nuisance fees.
- Widening the tax base and creating a friendly environment for taxpayers.
- Emphasising the use of ICT systems.
- improving the Government's electronic Payment Gateway (GePG) system and maximise its usage by all Government institutions.
- Strengthening monitoring systems in public institutions for timely submission of dividends and contributions.
- Strengthening enforcement of tax laws in order to address tax evasion challenges and minimise revenue leakages.
- Transferring the role for verification of quality of imported fuel from private contractors to the Tanzania Bureau of Standards (TBS) in order to control tax evasion due to fuel adulteration.
- Prioritisation of implementation of strategies and projects to increase revenue generation.

Government priorities

The main priority for the Government is to ensure effective implementation of the 2021/2022 Annual Development Plan. In implementing this initiative, the Government plans to:

- Maintain discipline and increase efficiency in the use of public funds.
- Ensure fiscal deficit does not exceed 3% of the GDP in line with EAC macroeconomic convergence criteria.
- Allocate funds to priority areas which stimulate economic growth.
- Ensure ongoing projects are given priority prior to committing to new ones;
- Control accumulation of arrears.
- Enhance the use of ICT in transactions and in the Government operations to increase efficiency and enhance local capacity on systems security.

East Africa highlights: **Tanzania**

Income Tax

Proposed changes include:

- Exemption from income tax on interest derived from all Government bonds.
- Introduction of a 2% withholding tax on payments for agro-products, livestock and fisheries supplied to processing industries, millers and Government agencies with an exception of (i) small farmers and (ii) sales to Agriculture Marketing Cooperatives Societies (AMCOS).
- Introduction of 5% depreciation allowance on cost of assets under the East African Crude Oil Pipeline (EACOP).
- The Minister for Finance to be given sole powers to grant income tax exemption on specific development projects funded by the Government i.e. without Cabinet approval.
- Introduction of a 3% income tax rate on the sale value of minerals, payable at the time of sale of minerals (only applicable to small scale mining).
- Introduction of deemed PAYE, payable by an employer engaged in small scale mining (on behalf of the employees) calculated at 0.6% of the sale value of minerals, payable at the time of sale of minerals.

Employment taxes

- Reduction of PAYE rate to 8% (from 9%) for the lowest individual tax band.
- Increase in the employee threshold for skills and development levy (SDL) to apply from 4 to 10.
- Exemption of SDL for religious health institutions.
- Introduction of a 0.4% levy to employers engaged in small scale mining, payable at the time of sale of minerals.
- Reduction of rate for contributions to Workers Compensation Fund from 1% to 0.6% for the private sector.

Tax administration

Proposed changes include:

- Reinstatement of Commissioner’s power to remit interest and penalties without limitations set in the Regulations.
- Removal of the 100% penalty for a transfer pricing adjustments.
- Court of law to be given powers to collect fines and penalties relating to tax offences.

East Africa highlights: **Tanzania**

Value added tax

Exemptions

- Imports and local purchases for EACOP.
- Crude oil of HS Code 2709.00.00.
- Specified data devices including smartphones (HS Code 8517.12.00), tablets (HS Code 8471.30.00 or 8517.12.00) and modems (8517.62.00 or 8517.69.00).
- Imported precious metals and raw materials.
- Insurance of livestock farming.
- Specified cold rooms (HS Code 9406.10.10 and 9406.90.10).
- Broadening exemption to both aluminium and stainless-steel milk cans with HS Code 7310.29.90, 7310.10.00 and 7612.90.90.
- Return of VAT exemption to NGOs, approval to be provided by the Commissioner of TRA.
- Specified importations by the National Identification Authority (NIDA) of contactless smart cards (HS Code 3921.11.90) and card consumables (HS Code 3921.11.90).
- Exemption on grass used for football pitches in city councils subject to approval by the Tanzania Football Federation (TFF).
- Abolishment of exemption on (i) cans intended for preserving milk with HS Code 7310.29.20 and (ii) on specified solar lights (HS Code 85.13 and 94.05).

Others

- Zero rate on the EACOP crude oil transportation and related services
- VAT deferment on capital goods limited to goods under chapters 84, 85 and 90 of the EAC CET.
- Reciprocity of VAT refunds for transferred goods purchased in Tanzania Mainland or Zanzibar.

Excise duty

- Reduction of excise duty rate for beer made from locally grown and malted barley from TZS 765/ ltr to TZS 620/ ltr.
- Increase excise duty by 30% on spirits.
- Introduction of 10% excise duty on imported and locally produced synthetic (plastic) fibres (Heading 55.11and 56.07) except fishing twine (HS Code 5607.50.00) and imported used motorcycles aged more than 3 years (HS Code 8711).

East Africa highlights: **Tanzania**

Customs

- Removal of the requirement of 15% refundable additional import duty on sugar for industrial use.
- Valuation of imported printed fabrics (Vitenge) to be re-vested in the Commissioner General.
- The EAC Ministers agreed to adopt USD 50 as de minimis value where customs duties shall not be collected.

Other levies and taxes

- Reduction of outdoor advertising fees;
- Stamp duty rates updated in line with the current economy.
- Produce cess may not apply to companies liable for service levy.
- Increment of road and fuel tolls by TZS 100/ltr of petrol and diesel.
- Introduction of 10% gaming tax on gross gaming revenue (GGR) from: (i) virtual games; and (ii) gaming products licenced under pilot study.
- Reduction of winning tax from all sports betting from 20% to 15%.
- Increase of gaming tax on sports betting from 25% of GGR to 30%; Additional 5% to be allocated to the sports development fund.
- Increment of fuel levy from TZS 150 to TZS 250.
- Imposition of levy on mobile money transactions upon sending or withdrawing money, depending on the transaction value.
- Imposition of a levy of between TZS 10 to TZS 200 per day per SIM card depending on the ability of the user to recharge the balance.
- Reduction of premium rate from 2.5% to 0.5% for new land occupancy and from 1% to 0.5% on regularizing land.
- Several amendments on fees paid to the Registrar of Societies.
- Amendments of various fees and levies imposed by ministries, agencies, regulatory authorities, regions and independent departments.

The Non Citizen (Employment Regulation) Act, 2015

- Imposition of a penalty of TZS 500,000 per month for failure to submit monthly returns to the Labour Commissioner.
- Imposition of 12 months imprisonment or a fine of TZS 10,000,000 as a sanction for failure to submit monthly return.
- Abolition of student visa/ pass fee for higher learning institutions students in Tanzania-Mozambique exchange Programme (TAMOSE).
- Visa fees to be retained by the union party which collected that fee (as opposed to the current practice where visa fees are collected by both Union parties).

East Africa highlights

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Thank you

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