KENYA BUDGET 2023-2024 HIGHLIGHTS

Aligning your business with tax trends in Kenya

This commentary is based on the Budget Statement FY 2023-2024

June 2023

BDO

SUMMARY OF KENYA'S 2023-2024 BUDGET POLICY STATEMENT

ECONOMIC OUTLOOK	• Global uncertainties such as geopolitical tensions and financial instability may lead to slower economic growth for Kenya. • Economic growth for 2022 slowed down to 4.8 per cent from 7.6 per cent in 2021 due to the adverse impact of the multiple shocks that affected the economy. • Services industry grew in 2022, but drought caused the agricultural sector to contract for the second year, impacting manufacturing, wholesale, and retail trade. • The Government predicts the economy to grow by 5.5% in 2023, fueled by private sector growth and better weather conditions for agriculture during the March-May rain season. This growth is expected to continue in the medium term. • Kenya's inflation rate has surpassed the 7.5% target due to high food and energy prices influenced by weather conditions and global oil prices. The Central Bank raised the CBR rate to 9.5% in March 2023 to address this. • The Government is implementing a fertilizer subsidy program and duty-free importation of essential food items to improve agricultural production and reduce domestic prices. • The Central Bank of Kenya aims to maintain stable inflation rates by implementing reforms like better forecasting, more robust interbank markets, and improved communication of policy decisions.

POLICY PRIORITIES

- The five priority sectors are: Agricultural Transformation, Micro Small and Medium Enterprises (MSME) Economy, Housing & Settlement, Healthcare, Digital Superhighway and Creative Industry.
- The Government aims to implement interventions in infrastructure, manufacturing, blue economy, services economy, environment, education, women's agenda, youth development, social protection, sports, culture, and governance.
- With the help of IMF, the Government aims to establish a new Resilience and Sustainability Facility arrangement that parallels the Extended Fund Facility(EFF)/ Extended Credit Facility(ECF) arrangements.
- Kenya will access Special Drawing Right (SDR) 306.7 million through the ECF/EFF in July 2023, increasing the total IMF financial support to SDR 1,509 million.
- Kenya will receive an additional SDR 407.1 million through the 20-month Resilience and Sustainability Facility (RSF) agreement, bringing the total IMF support to approximately US$3.52 billion by April 2025.
- Kenya has implemented a new Government-to-Government (G2G) program for fuel importation to ease the strain on local petroleum supply and currency due to the global US dollar shortage. The private sector can import petroleum through the Open Tender System (OTS).
- Each month, 740,000 metric tons of petroleum products are imported. 60% are used domestically, while 40% are used for regional transit. Procurement in US dollars can create foreign exchange challenges and unstable rates.
- The Government partnered with oil companies to stabilize the exchange rate, restructure fuel prices, and promote market growth. The agreements ensure extended credit periods, longer supply contracts, cost savings, and uninterrupted supply. This move aims to discourage speculation and stimulate the foreign exchange market.
- The Government is implementing programs to attract resources and manage climate risks with county governments and partners.
- The e-Government Procurement system will launch by December 2023, streamlining public procurement and asset disposal processes for increased efficiency, transparency, and cost savings. It will also monitor all related activities.
- State corporations will downsize staff and enforce a 70:30 technical-to-support staff ratio. Hiring budgets will require approval and funding confirmation from multiple commissions.
- The Cabinet approved the Privatization Bill 2023 to simplify processes and restructure State Corporations. The goal is to decrease reliance on exchequer funding.
- There is a program to improve KPLC and Kenya Airways by reducing their loan balances, payables, and receivables. For KPLC there will be transfer of all transmission assets/lines to KETRACO, settling of the Rural Electrification Schemes operations and maintenance cost deficit, reducing system losses, and establishing fair representation for private shareholders.
- Treasury plans to implement Pending Bills Verification Committee to analyze and settle the bills, which now amount to over Kes 537.2 billion.

POLICY PRIORITIES

- In 2022, banks had a strong performance with a 12.3% deposit growth and a 22.0% pre-tax profit increase. Non-performing loans decreased from 14.7% to 13.3%. Banks are consolidating and expanding regionally via acquisitions to enhance their resilience and capitalize on available opportunities. The sector is expected to remain stable and robust in 2023.

- The Central Bank of Kenya has regulated Digital Credit Providers (DCPs) to protect consumers. 32 DCPs have been licensed so far, with more awaiting approval. Collaboration with other regulators aims to ensure proper regulation and consumer safety.

- Central Bank of Kenya is launching "DhowCSD," an upgraded securities depository to boost financial markets. The system aims to enhance liquidity, efficiency, growth, and digital access while positioning Kenya as an economic hub. Investors will enjoy a seamless experience with scalable digital solutions.

- The bank is improving digital payments and reducing money laundering risks with mobile money interoperability, new payment provider licensing, and strengthened KYC/CDD processes. Payment laws are being reviewed, and oversight is enhanced for better AML/CFT/PF risk-based supervision.

- Kenya Deposit Insurance Corporation may raise coverage limit for MSMEs. They have an Alternative Dispute Resolution framework and capital markets are developing.

- New regulations to be rolled out to help MSMEs access financing through the Nairobi Securities Exchange and allow start-ups to raise funds from local and global investors.

- LAPTRUST IMARA's Real Estate Investment Trusts are now listed on Nairobi Securities Exchange, offering investors the opportunity to invest in diversified real estate assets that generate income.

- The National Treasury will use digital solutions to improve public service pensions. User-friendly online platforms will allow pensioners to access statements, update information, and make inquiries. The goal is to make pension payments easier through the Public Service Superannuation Scheme.

FISCAL MEASURES

- Plans to ensure debt sustainability by broadening the tax base, controlling expenditures, and prioritizing social and high-impact investment expenditures.
- Revenues are targeted to increase by 17.9% of GDP in FY 2023/24 and by over 18.3% of GDP in the medium term. The KRA plans to collect Kes 4.0 trillion in the medium term through administrative measures and policy reforms.
- The Government is working on a new tax policy to improve the tax system and increase revenue. The policy aims to ensure consistency in tax regulations and monitor tax spending.
- Kenya Revenue Authority to rely on technology and processes to monitor revenue by connecting to business systems to stem tax evasion.
- The Government aims to make public spending more efficient and cost-effective by cutting non-essential expenses, phasing out unsustainable subsidies, reducing tax exemptions, utilizing Public Private Partnerships, and implementing an e-procurement system.
- The revenue target for FY 2023/24 budget is Kes 2.96 trillion in total revenue, with 15.8% of GDP coming from ordinary revenue, Kes 348.7 billion from Ministerial Appropriation-In-Aid, and Kes 42.2 billion from grants.
- The 2023/24 budget is projected to be Kes 3.7 trillion, with recurrent expenses at Kes 2.53 trillion and development expenses at Kes 743.5 billion. County Governments will receive Kes 385.4 billion in equitable shares.
- The fiscal deficit is expected to decrease to Kes 718.0 billion (4.4% of GDP) in 2023/24, down from Kes 840.9 billion (5.8% of GDP) in 2022/23. It will be covered by net external financing of Kes 131.5 billion (0.8% of GDP) and net domestic financing of Kes 586.5 billion (3.6% of GDP).
- The Government may use a debt-to-GDP ratio to manage the debt and has proposed a bill to establish a debt ceiling. Approval is needed from the House.
- The Government and private sector are working together through an improved Public Private Partnership(PPP) framework to prioritize sustainability and address climate change. The Project Facilitation Fund provides funding and support for PPP projects, resulting in Kes 15 billion raised for urban road and renewable energy projects.
- High-impact PPP projects for bulk water supply and food security have also been approved, increasing production and potable water supply. A Water Purchase Agreement has been established to promote sustainable private sector development.
- The National Treasury is in the process of developing a 10-year infrastructure plan that will be cross-cutting across various Ministries to support the delivery and prioritization of projects.
- The National Treasury targets Kes 100 billion from private sector investment in key sectors such as airports, seaports, water, agriculture, energy, and digitalization to stimulate economic growth and attract private capital.
- To boost local investment in PPP projects, the Government prioritizes using local goods and services. Also encourage more local financing of these projects and include climate resilience strategies. To attract private sector capital, seek support from key institutions like capital markets and commercial banks.
- BETA Economic Agenda targets five key sectors: Agriculture, Small Business, Housing, Healthcare, and Digital Industry.

TAXATION MEASURES

PERSONAL TAX

Review of Income Tax Rate for Resident Individuals

- The Cabinet Secretary (CS) proposes an amendment of the Income Tax Act with regard to the resident individuals tax rates by adding two extra tax bands.
- With the current tax bands , the taxation of the employed population is more regressive creating a gap in the taxation of high income and lower income earners.
- The change in Pay-As-You-Earn (PAYE) tax structure makes taxation of individuals more progressive in sharing the tax burden more uniformly across income groups. The proposed change results to increased revenue to the government from the additional individual tax bands.

Current Individual Tax rates

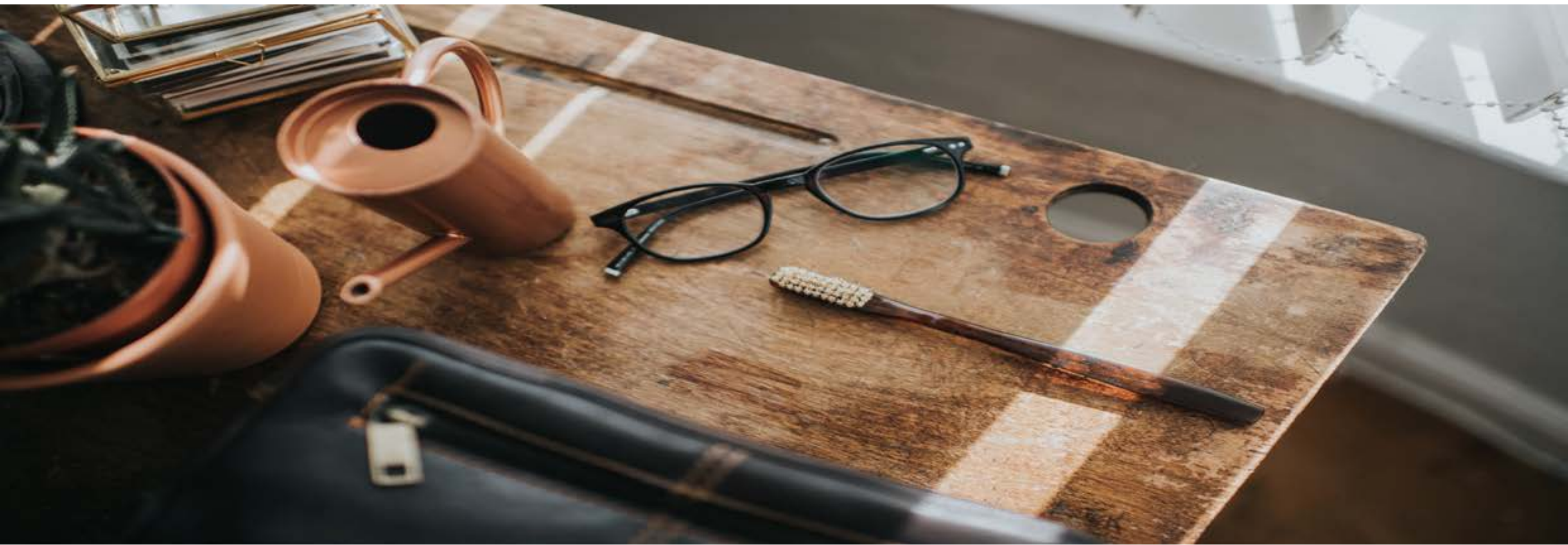
Tax Bands	Proposed Tax Rates
1 - 24,000	10%
24,001 - 32,333	25%
Above 32,333	30%
Personal Relief	**KES 2,400**

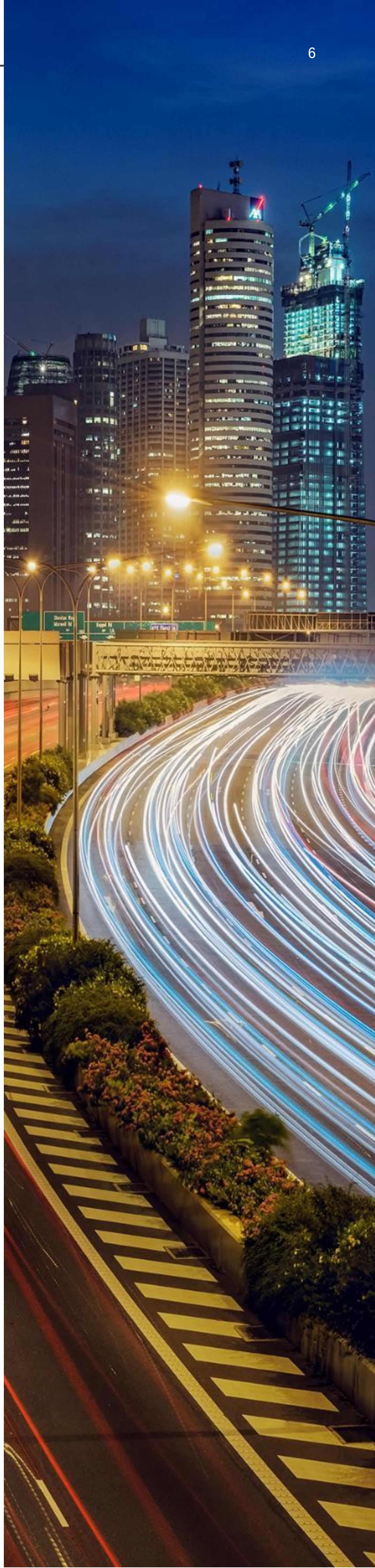
Proposed Individual Tax rates

Tax Bands	Proposed Tax Rates
1 - 24,000	10%
24,001 - 32,333	25%
32,334 - 500,000	30%
500,001 - 800,000	32.5%
Above 800,000	35%
Personal Relief	**KES 2,400**

Affordable Housing Levy

- The CS proposes to allocate a budget of KES 35.2 Billion to the housing programme in the governments efforts to make cost of housing affordable to majority of Kenyans.
- Further, the CS proposes an amendment of the Employment Act, of 2007 to include an affordable housing levy of 1.5% deducted from employee's gross monthly salary from the previously proposed 3%.
- There has been an increase of informal settlements in the country due to the high cost of housing resulting from unemployment and other economic challenges.
- Through the allocation, the government anticipates to make housing affordable to Kenyans and creating quality jobs for TVET graduates with expertise in the construction sector.





CORPORATE TAX

Introduction

The CS proposes to amend several provisions included in the Finance Bill 2023 as we previously discussed in the BDO Finance Bill 2023 tax alert.

The proposals in the Finance Bill 2023 have occasioned a heated debate due to the tax measures intended to revise the tax rates such as turnover tax and introduction of new streams of income tax such as tax on repatriated profits.

Interest Deduction Restriction

- Interest deduction restriction based on EBITDA introduced in 2021 was aimed at discouraging tax planning opportunities. This is currently applicable to both local and foreign financial institutions and interest expenses exceeding 30% of EBITDA are not tax deductible and foreign exchange losses are deferred.

- The CS proposes to exclude this interest deduction restriction on local loans to facilitate access to credit. Also, the CS proposes the extension of the disallowed expenses on non-resident loans for the next five years and not three years as proposed in the Finance Bill of May 2023.

Review of the Turnover Tax Threshold

- The Finance Bill 2023 proposed an amendment of the current threshold for Turnover tax on revenues from KES 1 Million to KES 50 Million. The new threshold band is KES 1 million to KES 15 Million.
- The CS proposes to retain the lower threshold at KES 1 Million and cap the upper threshold at KES 25 Million.
- This is aimed at excluding small traders with less than KES 1 million turnover from taxation while those exceeding KES 25 million will pay tax under the normal tax regime.

Introduction of Tax Rate on Repatriated Profits

- The Finance Bill 2023 introduced tax on repatriated profits by Permanent Establishments. However, the Bill did not clarify the applicable tax rate.
- The CS proposes a tax rate of 15% on the repatriated profits which is a rate similar to withholding tax paid on dividends to non-resident shareholders.

Reduction of Withholding Tax Rate on payments to Digital Content Creators

- The Finance Bill 2023 proposed to subject Withholding Tax (WHT) on payments to digital content creators at a tax rate of 15%.
- This elicited public anger considering that majority of the players are the youth and the rate proposed is significantly higher. The CS proposes to subject WHT on such payments at a tax rate of 5%.
- Strong opposition to this proposal resulted in reduction of the rate to 5% to align it to the Withholding tax rate applicable other payments like professional and management fees.

VALUE ADDED TAX

The CS retained most of the proposed changes in the Finance Bill 2023 under the Valued Added Tax (VAT). Some of the revise proposals are as highlighted below.

Tax Rate on Liquified Petroleum Gas (LPG)

- The Finance Bill proposed to exempt LPG from VAT under the First Schedule of the VAT Act 2013.
- The CS proposes to have the LPG Zero Rated to ease the burden on the suppliers with hidden costs resulting from non-deduction of the related input VAT.
- Further, the CS proposes to the removal of import declaration fees (IDF) and Railway Development levy on LPG.

VAT exemption on machinery and equipment for use in Pharmaceutical companies

- Currently, the VAT Act exempts only plant and machinery imported for use in pharmaceutical companies.
- To promote the local manufacture of the machines and the equipment and ensure a level playing field, the CS proposes to extend the VAT exemption to locally purchased machines and equipment.

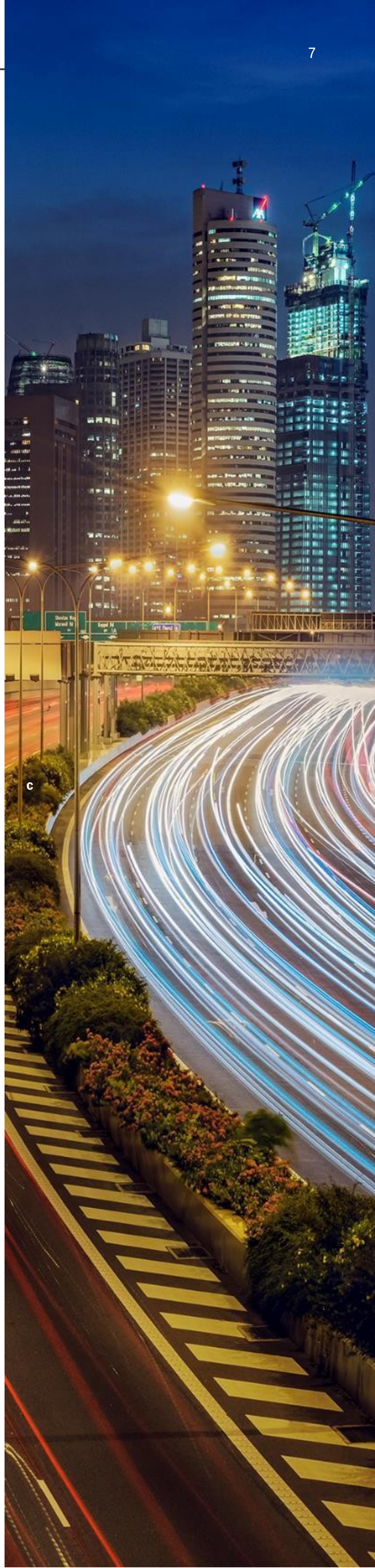
Removal of VAT on Exported Services

- Currently, the VAT on exported services is applicable at 16%.
- The Finance Bill 2023 proposed that the exported services to be exempt from VAT.
- The CS in his address to the National Assembly proposes to remove VAT on exported services.
- What is not clear is whether this service will be exempt or zero rated as the word “remove” used by the CS does not place the service in either category. The Finance Act 2023 once enacted into law will provide clarity.

TAX PROCEDURES ACT

Tax Administration

The CS proposed an amendment to the Tax Procedures Act (TPA) requiring the commissioner General to provide data management and reporting system that taxpayers would use to electronically submit standardized transactional data in real time.



EXCISE DUTY ACT

Excise duty has been tremendously revised to increase the tax base and raise revenue for the government. While the CS has retained most of the proposal in the Finance Bill, 2023, a few changes have been proposed as outlined in the table below:

Details	Current Tax Provision	Finance Bill 2023	CS Proposals
Remittance of excise duty on betting and gaming activities.	20th day of the following month	Retained	Within 24 hours after closure of transactions by betting and gaming companies.
Excise duty rate on Betting, gaming, price competition and lotteries	7.5%	20%	12.5%
Excise duty on imported fish	N/A	20%	KES 100,000 per metric tone or 10% of the excisable value whichever is higher.
Excise duty on powdered Juice	N/A	Retained	KES 25 per kilogram
Repeal of annual Inflation adjustments	Inflation adjustment done annually.	Retained	Repeal of the provision
Excise duty on imported sugar	N/A	Retained	KES. 5 per kilogram except that imported by registered pharmaceutical manufacturers for use in the manufacture pharmaceutical products.
Excise duty on advertisements by television, print media, billboards and radio stations in promotion of alcohol, betting, gaming, price competition and lotteries	N/A	Retained	15% on excisable value of the fees charged.
Excise duty on telephone and internet data services	20%	Retained	15%
Excise duty on money transfer services by banks, money transfer agencies and other financial service providers	20%	Retained	15%
Excise duty on fees charged for money transfer by cellular providers or payment service providers licensed under National payment system	12%	15%	10%
Excise duty on imported cement	N/A	Retained	10% Of the excisable value or KES 1.50 per kilogram whichever is higher
Excise duty on imported furniture	N/A	Retained	30% of the customs value excluding those originating from EAC countries.
Excise duty on imported paints varnishes and lacquers	N/A	Retained	15% of the excisable value

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