Rationalizing Tax Expenditures in Kenya

The 2021 Tax Expenditure report is the first report to be prepared by the National Treasury with an aim of enhancing government budget and fiscal transparency. To find out more on the impact of the tax expenditure report we spoke with team from National Treasury Macro & Fiscal Affairs Department

What are tax expenditures? Why should taxpayers care about tax expenditures? (How does it affect them?

Basically, we look at tax expenditures as the revenue forgone by the government. This means revenue that the government was to receive or collect is now either a deduction or a credit or even could be an exemption. By this I mean tax that would have been paid to the government you are now exempted from paying it.

A good example is during COVID-19 pandemic , we received tax relief from our income. It was actually a form of revenue forgone by the government, because what government was actually supposed to receive, or rather collect, they never collected.

On the other hand, tax expenditure is also an incentive to a particular sector either to promote that sector to boost it to grow either in manufacturing, MSME, agriculture and even special economic zones.

The common Kenyan should care about the tax expenditures because they reduce the revenue that's going to the government and the government collects these taxes for infrastructure development, hospital, education and the social sectors that the government supports. So, you as a taxpayer, should be concerned when there are many tax expenditures by the government because it is reducing what Wanjiku should be enjoying.

Of importance to note is tax expenditures are targeted. Not everyone enjoys this relief.

Based on the 2021 Tax expenditure report, what informed the guidelines for tax exemptions, waiver, variations and remission?

Tax exemptions, waivers, reliefs, remissions and variations are processed based on legal provisions contained in the Kenyan tax laws. These tax laws are generally categorized as either indirect or direct tax laws. The tax laws are operationalized through policies and Treasury Circulars. For income tax related deductions, the governing tax law is Income Tax Act and not "permit".

How does the National Treasury ensure the incentives, exceptions do meet their objectives?

Actually Treasury circular number 9 of 2018 has all the framework, and one of the things that we are supposed to ensure is to do a monitoring and evaluation exercise, like for the projects, we are actually supposed to go and monitor whether those goods that were procured are going directly into the project. We don't only do it as National Treasury, we do it with the implementing ministry and with Kenya Revenue Authority.

What plans does the National Treasury have to sensitize the public about Tax expenditure?

In order to sensitize the public on tax expenditure, the National Treasury has already uploaded the 2021 and 2022 Tax Expenditure Reports on its website with the aim of enhancing transparency and accessibility in regard to tax expenditure.

When developing the tax expenditure reports, is there an element of public participation?

For sure there is an element of public participation but it's not carried out physically. We usually upload the document on the National treasury website for people to give their views and comments.

Based on the 2021-2022 Tax Expenditure report, how would you describe the impact of tax exemptions to the economy?

Basically, I would say that one of the strategic objective is the encouragement of investments.Actually by offering tax incentives, the government aims to attract investment in specific sectors of the economy, such as manufacturing, agriculture or tourism.

The other thing would be the stimulation of economic growth. This is by reducing the tax burden to the businesses. Just like I mentioned, the micro and small enterprises, you are exempt from paying corporation tax if your turn over value is less than Ksh. 1 million per annum. So, by that the government expects these businesses to stimulate the growth of the economy.

The other impact would be job creation. Once an investor establishes a business courtesy of tax reliefs accorded by the government, this creates employment for the people.

We have promotion of the economic diversification by offering the tax incentive. We are saying these specific sectors that are targeted are going to reduce the dependence on some sectors.

The other thing is also to encourage research and development. You realize that if you are engaged in research and development, you also enjoy some tax incentives. It will also boost the innovation of our young people in different sectors.

When looking at the agricultural sector, if we give companies in this sector deduction for the equipment and machinery, it will also help boost mechanization in agriculture, and this equally applies to ICT, innovation and creativity.

Looking at the draft National Tax policy, what are some of the highlights touching on Tax expenditures?

The tax policy is currently at stakeholder stage.

There is need to streamline how we manage incentives. For example, what is the optimal level of incentives, the type of incentives, the criteria for developing the incentives, how they are reviewed and even tracking to ensure they achieve the targeted purpose. At some point some incentives are rendered redundant after the government targeted to do something. There has to be a framework that guides on how we can measure performance, whether the objective was really met.

The policy will therefore give us a clear framework on managing the incentives.

National Treasury worked with KRA to review existing tax exemptions through the tax laws (amendment) act 2020, briefly highlight some of the exemptions that were removed and the expected impact?

Following the amendment of tax law in 2020, some of the things that were removed were exemption towards investment income. In this, we refer to bonds and treasury bills which were previously exempt from taxes. This has resulted in increased tax simply because, when you have tax on the interest that you earn on treasury bills, it is also a revenue for the government.

So, broadly saying , when you remove those incentives or rather exemptions, you're looking at growing the revenue for government. The broader perspective is the growth of revenue, and then eliminating the tax evasion issue.

The 2021 Tax expenditure report assesses the trend of tax expenditure for the period 2017-2021 , What are some of these trends and what do they mean going forward ?

Here the focus is more on infrastructure, the growth of micro and small enterprises, and then the expansion of tax incentives for foreign investments.

What role does parliament have as far as Tax expenditure/exemptions is concerned?

Parliament is a key player because of their legislative and law making role. All tax incentives and tax exemption are supported by Law. Lawmakers have the powers to make laws and regulations touching on tax incentives.

The other thing is oversight. The Cabinet Secretary (National Treasury) is expected to table a report of tax expenditures to parliament and the reason why the wavers were given.

Then of course I would say, the representation of the people. Parliament represents and acts as the voice of Wanjiku's when it comes to tax maters.

Parliament equally has a role in reviewing tax policies.. This includes the powers to amend and to repeal the various acts.

Do counties do their own form of tax exemptions?

Counties can only pass their own county revenue bill, but the national taxes, this I mean income tax, value-added tax, customs duties and other duties on import and export of goods; and excise tax these ones are managed at the national level even for them they request for exemptions through the National Treasury.

What are some of the tax incentives, or exemptions in place that the common mwananchi should be aware of?

What Wanjiku should be interested in, we have tax deduction for insurance premiums. The Kenyan citizen who pay health insurance, they can claim a tax deduction of up to Ksh. 60,000 per annum, it's important for them to know.

Pension contribution is the next agenda. If you invest in a pension scheme and you contribute per annum, one can claim up to. 240,000 per annum.

Then of importance is the mortgage investment. When you have a mortgage, you are allowed to claim a tax deduction up to ksh30,000 per annum for interest paid on that mortgage.

Are there countries you would like to benchmark against as far as tax expenditures is concerned?

Mauritius and Rwanda were the first African countries that developed tax expenditure reports and would be good if we benchmarked with either of them, they are countries we can learn from.

What are the International Best Practice when it comes to Tax Expenditures?

Publishing of tax expenditures is an international best practice which we are doing, with the aim of improving transparency.

Public participation is another area that requires enhancement from our end. We need a more participatory approach when it comes to public participation, because our engagement with the public is mostly through the media, and we may not be reaching the real wanjiku who doesn't see it on the website.

The next area of support that we require is developing the framework of tracking and monitoring tax expenditures. There's need to develop a mechanism to try and evaluate impact of tax reliefs, whether they really achieved the intended objective or purpose. This will greatly improve transparency and the government can even know whether to continue pursuing the tax expenditures or re-think on their design.