

Tax & Legal Alert  
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## Tax Alert

### Excise duty and export levy rates inflation adjustment

The Commissioner General (“CG”) of the Kenya Revenue Authority (“KRA”) has adjusted excise duty on excisable goods with specific rates by the average inflation for the last financial year of 6.3% pursuant to Section 10 of the Excise Duty Act 2015. Further, the CG has adjusted the export levy on raw hides and skins by the inflation rate of 6.3% in accordance with Section 5(4) of the Miscellaneous Fees and Levies Act (“MFLA”).

The new excise duty and export levy rates were published on 3 October 2022 in Legal Notice No 176 and 177 respectively and took effect on 1 October 2022.

## Inflation adjustment of excise duty rates

### Background

Section 10 of the Excise Duty Act provides that the CG, subject to approval by the Cabinet Secretary for the National Treasury (CS), may adjust specific rates of excise duty to take into account inflation through a notice in the Gazette.

The inflation adjustment is calculated as the average rate of monthly inflation of the preceding financial year. In this financial year, the specific rates have been adjusted by the average inflation rate for the financial year 2021/2022 of 6.3%. According to the First Schedule of the Excise Duty Act, specific excise duty rates should be adjusted annually and should take effect on 1 October of every year.

The Finance Act 2022 amended Section 10 of the Excise Duty Act to allow the CG, with the approval of the CS to exempt specified products from inflation adjustment after considering the circumstances prevailing in the economy in that year in respect of such products. In this year's inflation adjustment, the CG has exempted petroleum products from inflation adjustment in light of the high pump prices attributed to high global prices of petroleum products. The CG has also excluded sim cards and liquid nicotine from the list perhaps because excise duty on these products was introduced on 1 July 2022.

The CG invited members of the public and stakeholders to provide their views on the inflation adjustment through a public notice dated 1 September 2022 in accordance with the Statutory Instruments Act.

The list of products published in Legal Notice 176 is as outlined in the table below:

	Tariff Description	Current Rate of Excise Duty (Ksh.)	New Excise Duty (Ksh.)
1.	Fruit juices (including must) and vegetable juices, unfermented and not containing added spirit, whether or not containing added sugar or other sweetening matter	Sh. 13.30 per litre	Sh. 14.14 per litre
2.	Bottled or similarly packaged waters and other non-alcoholic beverages, not including fruit juices or vegetable juices	Sh. 6.03 per litre	Sh. 6.41 per litre
3.	Beer, cider, perry, mead, opaque beer and mixtures of fermented beverages with non-alcoholic beverages and spiritous beverages of alcoholic strength not exceeding 6%	Sh. 134.00 per litre	Sh. 142.44 per litre
4.	Powdered beer	Sh. 121.85 per kg	Sh. 129.53 per kg
5.	Wines including fortified wines and other alcoholic beverages obtained by fermentation of fruits	Sh. 229.00 per litre	Sh. 243.43 per litre
6.	Spirits of undenatured ethyl alcohol, spirits liqueurs and other spiritous beverages of alcoholic strength exceeding 6%	Sh. 335.30 per litre	Sh. 356.42 per litre
7.	Cigars, cheroots, cigarillos, containing tobacco or tobacco substitutes	Sh. 15,296.60 per kg	Sh. 16,260.29 per kg
8.	Cigarette with filters (hinge lid and soft cap)	Sh. 3,825.99 per mille	Sh. 4,067.03 per mille
9.	Cigarettes without filters (plain cigarettes)	Sh. 2,752.97 per mille	Sh. 2,926.41 per mille
10.	Other manufactured tobacco and manufactured tobacco substitutes, "homogenous" and "reconstituted" tobacco, tobacco extracts and essences	Sh. 10,707.88 per kg	Sh. 11,382.48 per kg
11.	Motorcycles of Tariff Heading 8711 other than motorcycle ambulances and locally assembled motorcycles	Sh. 12,185.16 per unit	Sh. 12,952.83 per unit
12.	Imported sugar confectionary or Tariff Heading 1704	Sh. 40.37 per kg	Sh. 42.91 per kg
13.	Imported white chocolate including chocolate in blocks, slabs or bars or Tariff Codes 1806.31.00, 1806.32.00 and 1806.90.00	Sh. 242.99 per kg	Sh. 257.55 per kg
14.	Products containing nicotine or nicotine substitutes intended for inhalation without combustion or oral application but excluding medicinal products approved by the Cabinet Secretary responsible for matters relating to health, and other manufactured tobacco and manufactured tobacco substitutes that have been homogenized and reconstituted tobacco, tobacco extracts and essences	Sh. 1,500.00 per kg	Sh. 1,595.00 per kg

## Our view

On 1 July 2022, the Government increased excise duty on most excisable products considered as “harmful products” and “luxurious products” by an average rate of 10% through the Finance Act 2022 in a bid to generate additional revenue.

Subsequently, on 3 October 2022 the CG increased excise duty on most of the foregoing products by a further 6.3% bringing aggregate increment of excise duty to about 16.9%.

The objective of adjusting specific excise duty rates for inflation is to ensure that excise duty revenue generated from these products grows in proportion with economic growth. However, the Government needs to take into consideration that an increase of excise duty beyond a certain rate is likely to have adverse effects on the welfare of the population and the economy at large. Although the demand for most excisable goods is largely inelastic, the increase of excise duty beyond a certain optimal rate will discourage consumption of these products and ultimately reduce Government revenue, discourage investment in the affected industries, and increase unemployment. High excise rates will continue to encourage consumption of cheaper illicit alternatives and promote cross border smuggling.

During the public participation on the inflation adjustment there was consensus from the affected stakeholders that the CG should consider exemption of various products from the inflation adjustment particularly considering the excise duty rates had already been increased in July 2022. According to most manufacturers and importers of excisable products, any further increment in excise duty on the products would suppress the demand of the goods and ultimately reduce Government revenue.

In our view, the Government should consider investing in research and data analysis tools to evaluate the effect of increase in excise duty on the affected businesses and on consumption patterns of the excisable products which will also help identify the overall impact on revenue collection. The data will be relevant in establishing optimal rates of excise duty on the various products to enable the CG make an informed decision while adjusting excise duty rates for inflation.

The exemption of petroleum products from inflation adjustment is a welcome move that will provide the much-needed relief, albeit minimal, to majority of Kenyans who are directly or indirectly impacted by the price of fuel. This is particularly crucial at a time when the international prices of petroleum products have soared to an all time high. Petroleum products play an important role in almost every sector of the Kenyan economy and changes in the price of petroleum products generally increases the cost of living.

We note that whereas the new rates were published on 3 October 2022, the commencement date as per the Legal Notice is 1 October 2022.

Although the Excise Duty Act provides that the adjusted prices should take effect on 1 October of every year, Legal Notice 176 was published on 3 October 2022, therefore, a commencement date of 1 October 2021 would result in retrospective application of the law. This is likely to cause confusion amongst taxpayers and the revenue authority particularly where the revenue authority takes a contrary view.



## Inflation adjustment of export levy rates

### Background

Section 5(4) of the MFLA provides that the CG, through a notice in the *gazette*, may adjust specific export levy rates annually considering inflation. The inflation-adjustment is calculated as the average rate of monthly inflation of the preceding financial year.

The Finance Act 2022 amended the commencement date of adjusted rates to 1 October of every year from 1 July of every year to align with similar provisions in the Excise Duty Act.

The CG has adjusted the export levy on raw hides and skins of various tariff codes from 80% or USD 0.52 per Kg to 80% or USD 0.55 per kg.

### Our view

Inflation adjustment on export levy was introduced on enactment of the MFLA in 2016. However, this is the first time that the CG is adjusting the export levies for inflation.

The Government imposes export levy on raw hides and skins to discourage exportation of this product

and encourage local value addition. The Government had attempted to reduce the export levy on raw hides and skins through the Finance Bill 2022 to 50% or USD 0.32 per Kg but the proposal was not adopted by the National Assembly.

In our view, the Government should provide an enabling environment and policies to encourage local investment in tanneries such as provision of financial support to pastoralists, tax incentives on inputs and equipment required to facilitate further processing of raw hides and skins among others. Increasing the export levy may deter exports but does not provide a sustainable solution to the challenges facing the development and modernization of the leather sector.

Further, for local pastoralists to benefit from the raw hides and skins business, the Government should put in place measures to ensure that raw hides and skins fetch competitive prices in the local market to discourage exportation. It is therefore important that the Government prioritizes addressing the challenges facing the sector or risk reduced investment in the raw hides and skins business.



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