#NationalBudget2025

# Kenya Budget Highlights 2025/26

## *On the edge: Navigating Kenya's fiscal tightrope*

June 2025

***"While the budget aims to increase revenue through expanded tax measures, there is apprehension about the potential impact on consumer spending and business investment."***

Kenya has navigated a complex economic landscape over the past year, marked by resilience and strategic adaptation to global and domestic challenges. In 2024, Kenya's economy grew by 4.7% compared to 2023, driven by improved productivity in the agriculture sector and strong resilience in the services sector. The agricultural sector, a cornerstone of the Kenyan economy, benefited from favourable weather conditions, contributing about 17% of the GDP growth in 2024. Meanwhile, the technology sector flourished, supported by innovation and an increasingly skilled workforce.

Other positive highlights of 2024 include the reduction of interest rates, the improved stability of the Kenya Shilling to US dollar exchange rate, and the reduction of inflation. In April 2025, the Monetary Policy Committee reduced the benchmark interest rate to 10% from 13% in July 2024. Inflation reduced to 4.2% in the same period compared to the previous year. At the same time, the US dollar to Kenya Shilling exchange rate has been relatively stable throughout the year, ranging between KES 128 and 130 to the US dollar.

The Finance Bill 2025 reflects a commitment to fiscal discipline and strategic resource allocation, emphasising infrastructure development, healthcare, and education. These investments are crucial for fostering inclusive growth and enhancing the nation's global competitiveness. This commitment to fiscal discipline is a direct response to the sentiments raised by Kenyans in 2024 for the government to "live within its means".

However, concerns have been raised regarding the balance between taxation and economic stimulation. While the budget aims to increase revenue through expanded tax measures, there is apprehension about the potential impact on consumer spending and business investment. It is imperative that the government carefully calibrates these measures to ensure they do not stifle economic momentum.

Overall, the outlook for Kenya's economy in 2025 is optimistic, with a forecast growth of 5%. Kenya is well-positioned to leverage its strengths and address its challenges through collaborative efforts between the public and private sectors. By fostering an environment conducive to innovation, investment, and sustainable development, Kenya can continue to advance towards a prosperous future.

Beyond the figures and policies, this budget presents an opportunity for the government to rebuild and reinforce the public's trust in its ability to steward our nation's resources wisely. I encourage all stakeholders, from citizens to businesses and government agencies, to actively engage in the discussions that follow, contributing your insights and perspectives as we work together to achieve a sustainable fiscal environment that will not only ensure the responsible management of our public finances but also foster economic growth that benefits all.

Anne Muraya
CEO
Deloitte East Africa

*“This year’s Budget proposals reflect an aversion to introduce new taxes, likely informed by the adverse public reaction to the new taxes proposed by the Finance Bill, 2024”*

The FY2025/2026 budget comes against the backdrop of less-than-optimal revenue performance in the current financial year, which, coupled with increased spending pressure contributes to a growing fiscal deficit. Specifically, ordinary revenue collection at the end pf the March 2025 stood at KES 1.697 Trn against a target of KES 1.840 Trn representing a shortfall of KES 142.8 Bn. According to the Government, the underperformance was mainly on account of withdrawal of the Finance Bill, 2024 and the related protests that led to a slowdown of economic activities.

To counter these revenue collection shortfalls, the Government proposes to implement various revenue mobilisation efforts to shore up collections by the Kenya Revenue Authority (KRA) to over KES 4.0 trillion in the medium term. These efforts, which are anchored in the National Tax Policy and Medium-Term Revenue Strategy(MTRS), include strengthening tax administration for enhanced compliance, expansion of the tax base and minimizing tax expenditures.

These initiatives are broadly similar to previous policy statements but specific measures being implemented vary from enhanced digitalisation in the indirect tax space to new tax measures targeting the gig economy and non-residents among others. However, revenue collection continues to perform below target despite implementation of the above measures. This could be an indicator that the tax base is not growing as much as anticipated, which is a factor of overall economic performance as well as overreliance on the same tax base.

Although the Government has made tax base expansion a key focus in the recent past, the efforts may not yet have borne much fruit and there is still more work to be done.

**Proposed tax measures**

For FY2025/2026, the Government aims to collect revenues totalling KES 3.328 trillion, against a total budget of KES 4.24 trillion. Noting that the Government is presently unlikely to meet the FY2024/2025 revenue target of KES 3.067 trillion (KES 2.580 trillion being ordinary revenue), these revenue and expenditure estimates could, arguably, be viewed as ambitious taking into account the global and local economic environment.

In view of the above estimates, the Finance Bill, 2025 (Bill) proposes to implement several tax measures aimed at expanding the tax base, minimising tax expenditures, and enhancing compliance. Some of the measures geared towards tax base expansion include the expansion of the scope of significant economic presence tax (SEPT) and value added tax (VAT) on digital marketplace supplies as well as excise duty on supplies by non-resident persons.

To minimise tax expenditures, the Government plans to limit the period to carry forward tax losses to 5 years, to repeal accelerated investment allowances and preferential tax rates, and to rationalise the exemption and zero-rating of goods and services for VAT. To seal revenue loopholes and enhance compliance, the Bill proposes various measures, including empowering the Commissioner to issue agency notices to agents of non-resident persons subject to tax in Kenya.

Fred Omondi
Tax & Legal Leader
Deloitte East Africa

The Bill has some welcome measures to alleviate the tax burden including an increase in the tax-exempt limit for per diems, extension of mortgage interest deduction to cover construction of residential houses, exemption of gratuity payments and a reduction in the export and investment promotion levy on certain steel products. On the flipside, the Bill also has various proposals which could hurt taxpayers, such as the enhancement of the Commissioner's powers to issue agency notices even where there is an ongoing tax dispute and the requirement for taxpayers to share sensitive trade or personal data upon integration of their systems with the KRA. We hope that such measures will be relooked at prior to the Bill's assent into law.

**Conclusion**

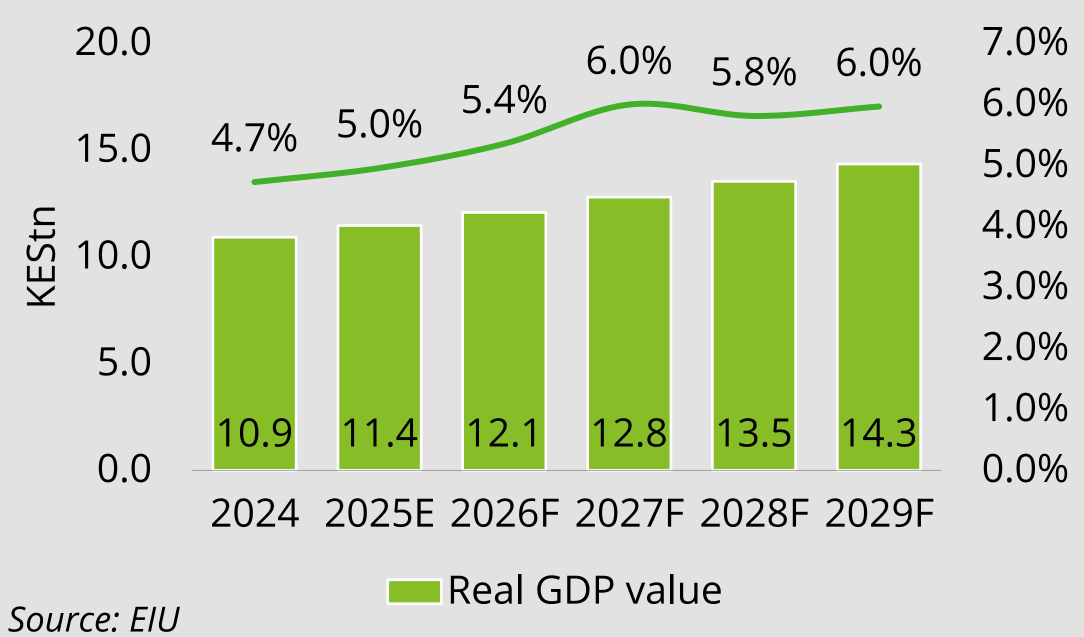
Overall, this year's Budget proposals reflect an aversion to introduce new taxes, likely informed by the adverse public reaction to the new taxes proposed by the Finance Bill, 2024. However, it remains to be seen whether enhanced administrative measures will result into more revenue collection to avoid widening the deficit. The one area that calls for attention is the need for stability in tax policy. Notably, the frequent tax changes and policy reversals should be avoided. One would hope that revenue growth would be predicated more on increased economic activity and tax base expansion rather than tax increases.

*"The one area that calls for attention is the need for stability in tax policy. Notably, the frequent tax changes and policy reversals should be avoided"*

# Economic Outlook

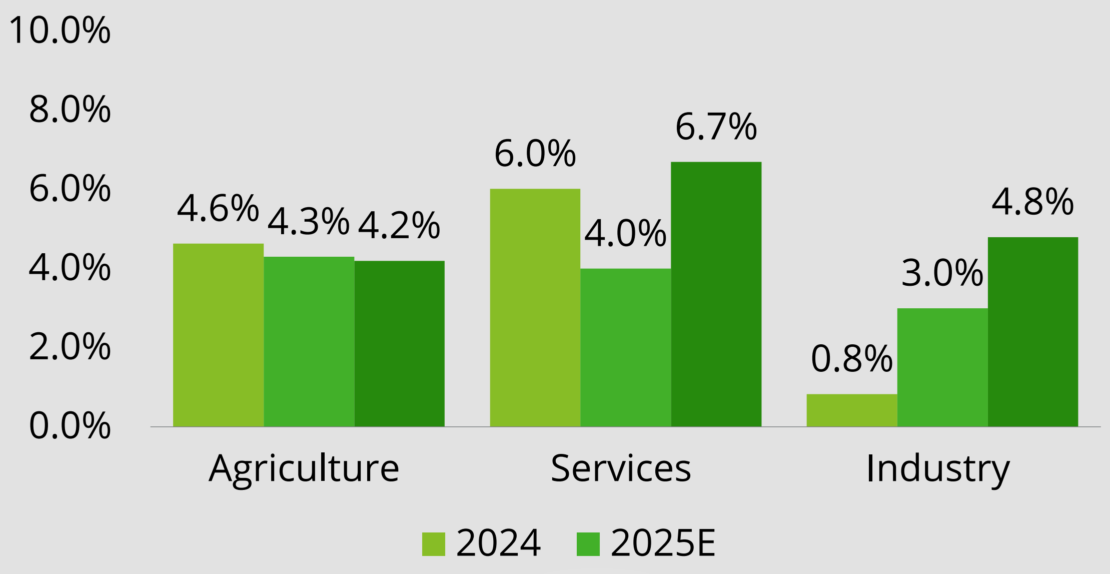
# Economy at a Glance

**Real GDP and Real GDP growth**




*Source: EIU*

**Sectoral Growth**




*Source: EIU*

## GDP Growth

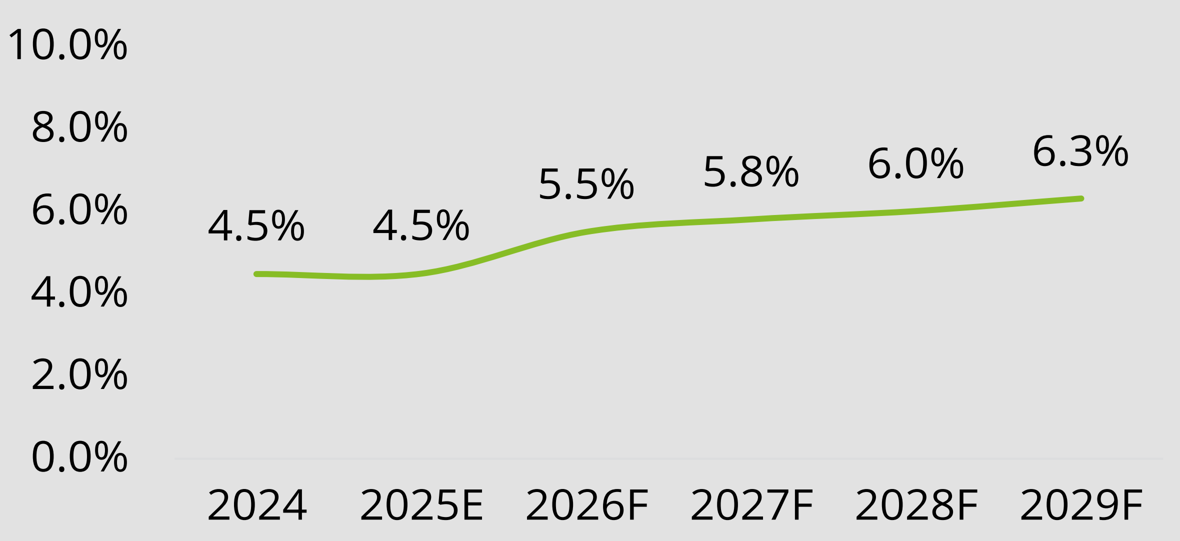
- Kenya's GDP growth is projected to accelerate to 5.0% in 2025 from 4.7% in 2024, primarily driven by increased household spending. This expansion is hinged on the Central Bank of Kenya's (CBK) gradual interest rate reductions, stimulating borrowing, investment, and consumption.
- Between 2026 and 2029, real GDP growth is forecasted to average 5.8%, primarily driven by expected growth in the services sector and continued recovery of the consumer spending power.
- The country is expected to benefit from lower interest rates, cheaper oil imports, a sustained tourism recovery, broad-based digitalisation, deeper regional integration and rising intra-regional trade, aided by infrastructure investment. However, Kenya's economy still faces downside risks from climate related shocks and political instability linked to the high cost of living and unemployment.

## Sectoral Growth Rate

- Agriculture: The sector is expected to grow by 4.3% in 2025, a slight decline from 4.6% in 2024. The expected growth is dependent on adequate rainfall and continued access to cheaper fertiliser supplied under the National Fertiliser Subsidy Program.
- Industry: The sector is expected to grow by 3.0% in 2025 compared to 0.8% in 2023, primarily supported by improved performance in the construction subsector. This is hinged on continued reductions in interest rates supporting increased investments, and a stable shilling.
- Services: The sector is expected to grow by 4.0% in 2025 supported by increased consumption on the back of reduced interest rates in the country.

# Economy at a Glance

## Inflation



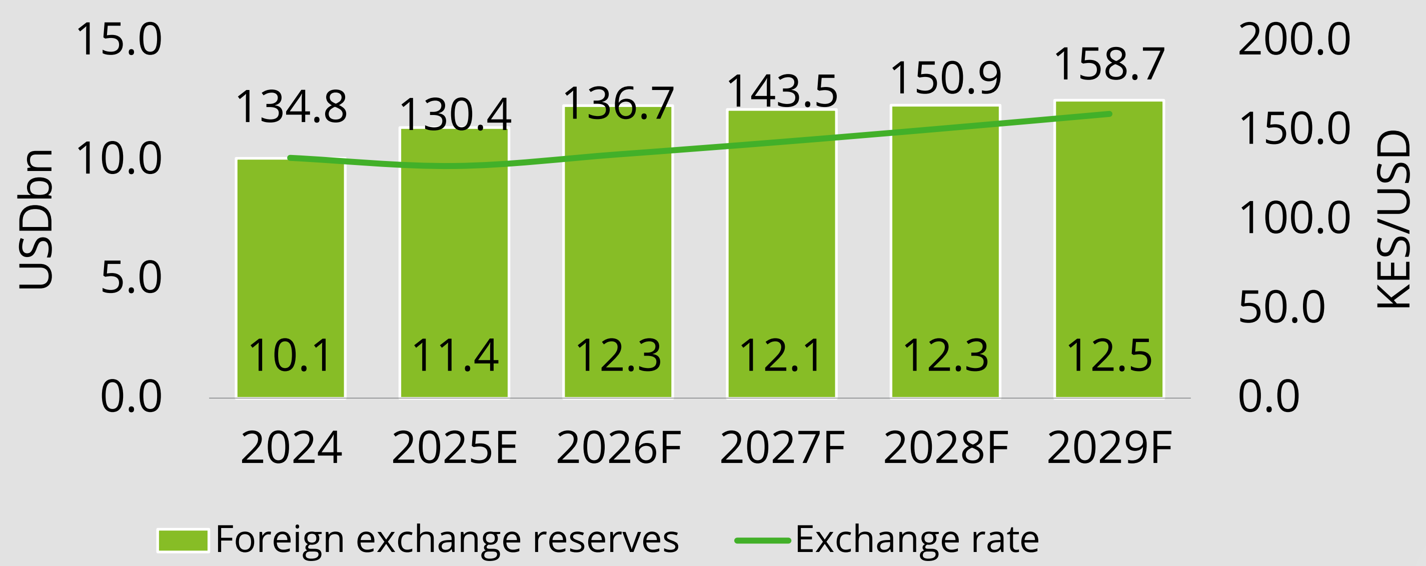

*Source: EIU*

Between June 2024 and May 2025, the country's inflation has averaged 3.6%, supported by lower food and fuel inflation, and effective monetary tightening measures by the Central Bank. Furthermore, the stabilisation of the Kenya Shilling against major currencies has helped curtail imported inflation, particularly for fuel.

Inflation is projected to accelerate to average 4.5% by the end of 2025, primarily due to increased consumer spending, as the CBK continues its monetary easing. Nonetheless, inflation is expected to fall within the CBK target band of 5+/- 2.5%.

Between 2026 and 2029, inflation is projected to average 5.9%, mainly attributable to the gradually weakening Shilling along with the country's sustained current account deficit.

## Foreign exchange reserves and exchange rate




*Source: EIU*

After a significant depreciation to KES 156.5/USD in 2023, the Kenyan Shilling (KES) recovered, strengthening to KES 134.8/USD in 2024.This was largely due to the positive market responses to the country's Eurobond issuance of USD 1.5bn and new loans from major development finance institutions.

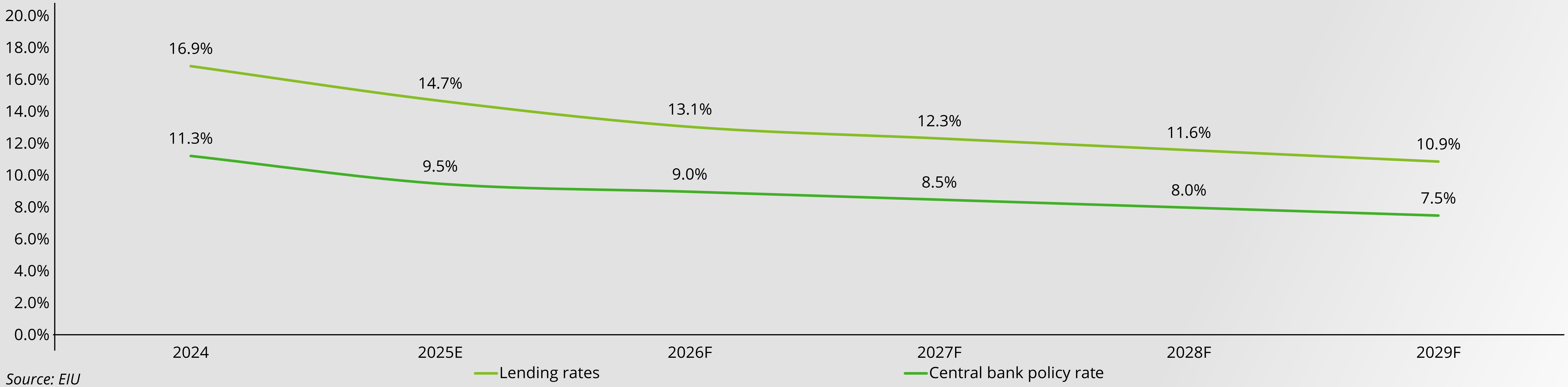
The Kenya Shilling has since remained stable averaging KES 129.4/USD between June 2024 and May 2025 and is projected to average KES 130.4/USD by year end 2025. This robust performance is attributed to declining global commodity prices, increased Foreign Direct Investments (FDI), and growing exports.

However, the Kenya Shilling is projected to depreciate by an average of 5.0% between 2026 and 2029, reaching KES 158.7/USD by 2029. This anticipated depreciation stems from Kenya's status as a significant net importer, which fuels demand for foreign currencies and contributes to a widening current account deficit.

The country's foreign reserves stock is expected to average USD 11.4bn in 2025 equivalent to 5.3 months worth of import cover and well above CBK's four months target.

# Economy at a Glance

**Policy interest and commercial lending rates**



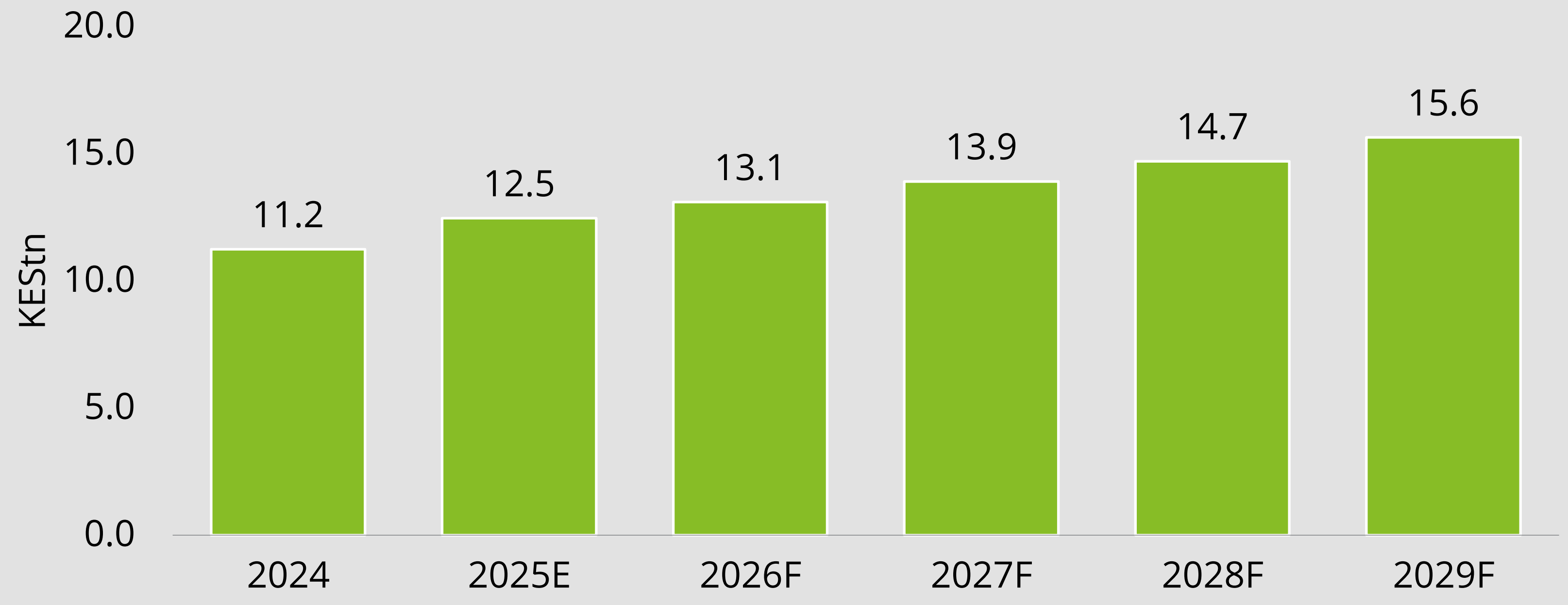

*Source: EIU*

## Interest rate

- Kenya's lending rate increased to16.9% in 2024, the highest since 2014. This was occasioned by the CBK's decision to raise the policy rate to 12.5% in February 2024, with the aim of curbing inflation. By the close of 2024, the CBK reduced the rate to 11.3% with the goal of lowering lending rates, thereby encouraging private sector borrowing and economic growth.
- Since December 2024, the CBK has consistently lowered the policy rate, from 11.3% to 10.6% in February 2025, 10.0% in April, and 9.6% by June 2025. These reductions aim to prompt banks to lower commercial lending rates. The CBK is expected to further reduce the policy rate to 9.5% by the end of 2025, with lending rates projected to decrease to 14.7%.
- Reduced lending rates will support lower borrowing costs for investors, enhancing investment appeal, and simultaneously make it more affordable for consumers to finance purchases. This increased consumer spending on goods and services will ultimately accelerate Kenya's economic growth.

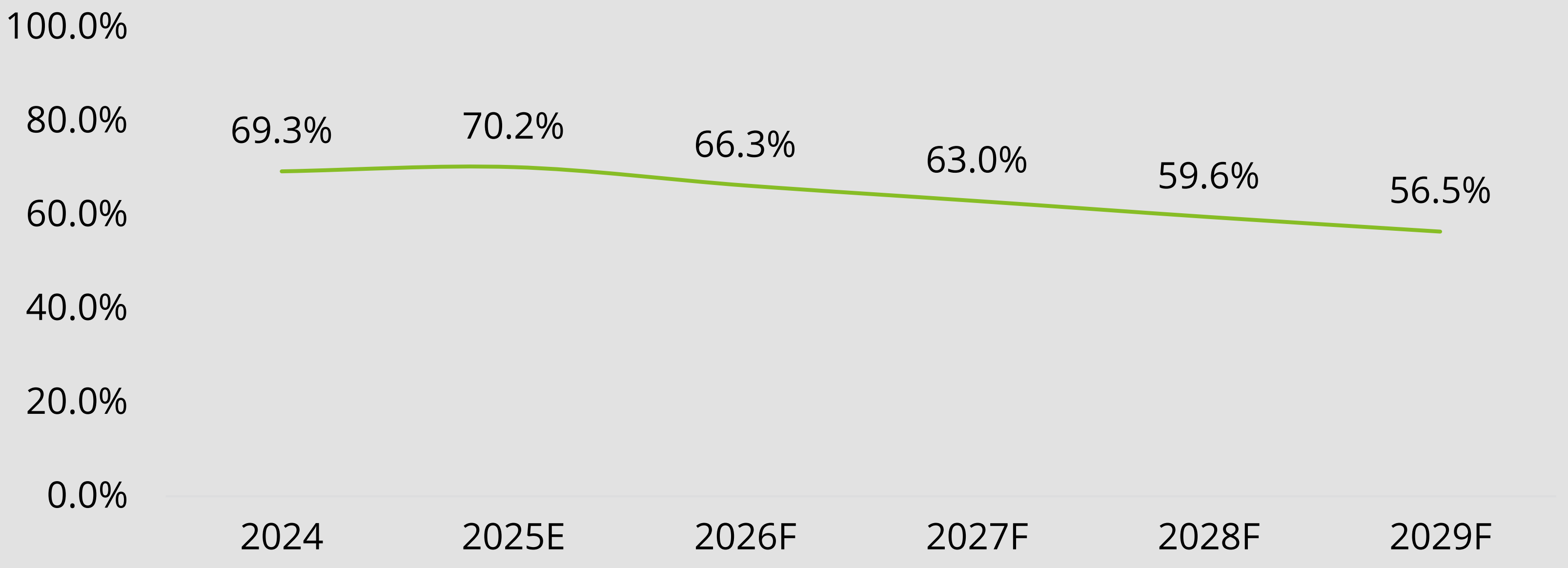
# Economy at a Glance

### Public Debt




*Source: EIU*

### Public debt as % of GDP




*Source: EIU*

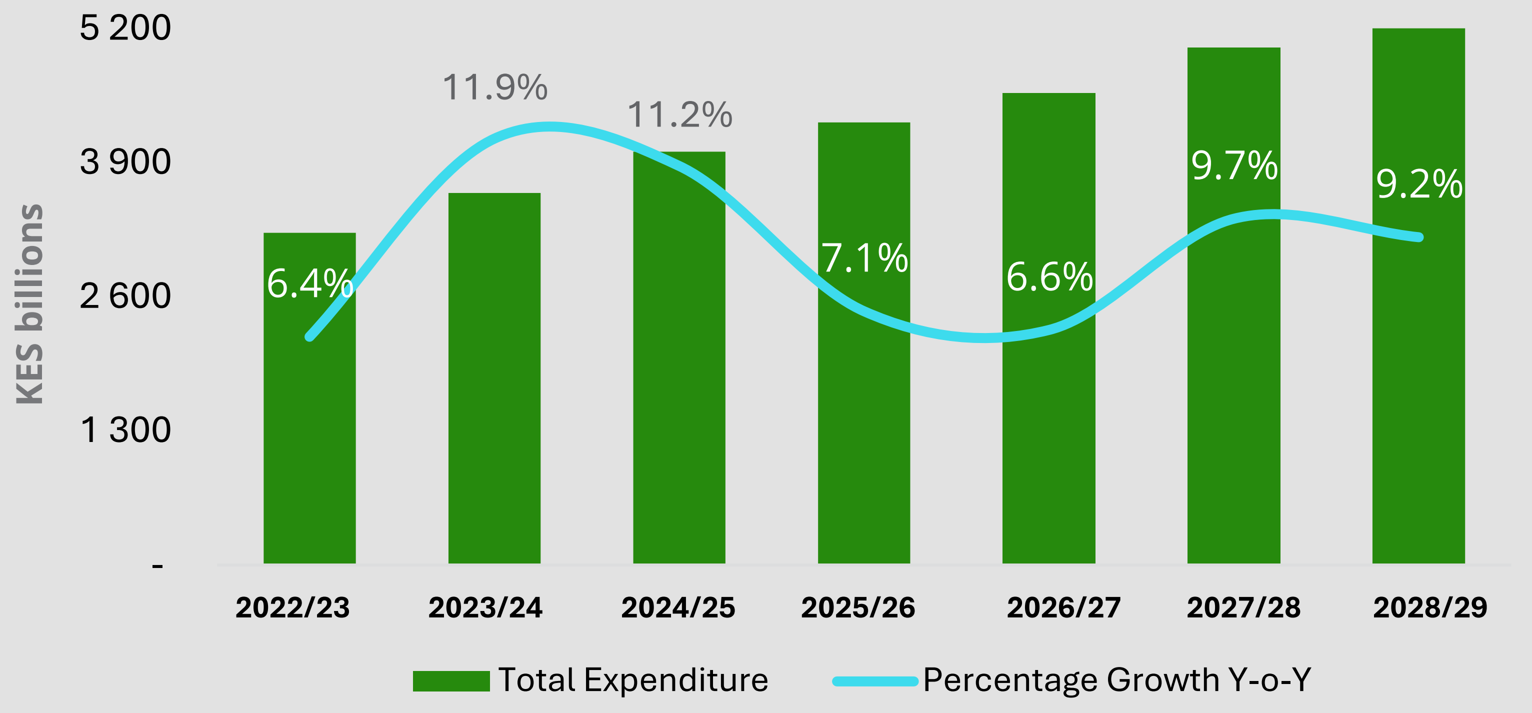
## Debt

- Due to the annulment of the Finance Bill 2024, the government is seeking alternative financing to plug the tax revenue shortfall. As a result, public debt is expected to rise to KES 12.5tn in 2025 from KES 11.2tn in 2024, as the government focuses on increasing tax revenue through implementation of the revised Finance Bill 2025.
- The bill seeks to amend key tax statutes including the Income Tax Act, VAT Act, and Excise Duty Act with the aim of enhancing the average revenue to GDP ratio. This will help mitigate the reliance on borrowing and contribute to fiscal deficit reduction, which is crucial for effective debt management.
- Kenya's public debt (as a % of GDP) is projected to average at 70.2% in 2025 and will remain a concern with debt servicing expenses consuming over 60% of tax revenue in 2025. The country faces the risk of crowding out spending on development if the trend persists into the medium term. Furthermore, higher debt burden could impact FDI and expose the country to foreign currency exchange risk.

# Tax Measures

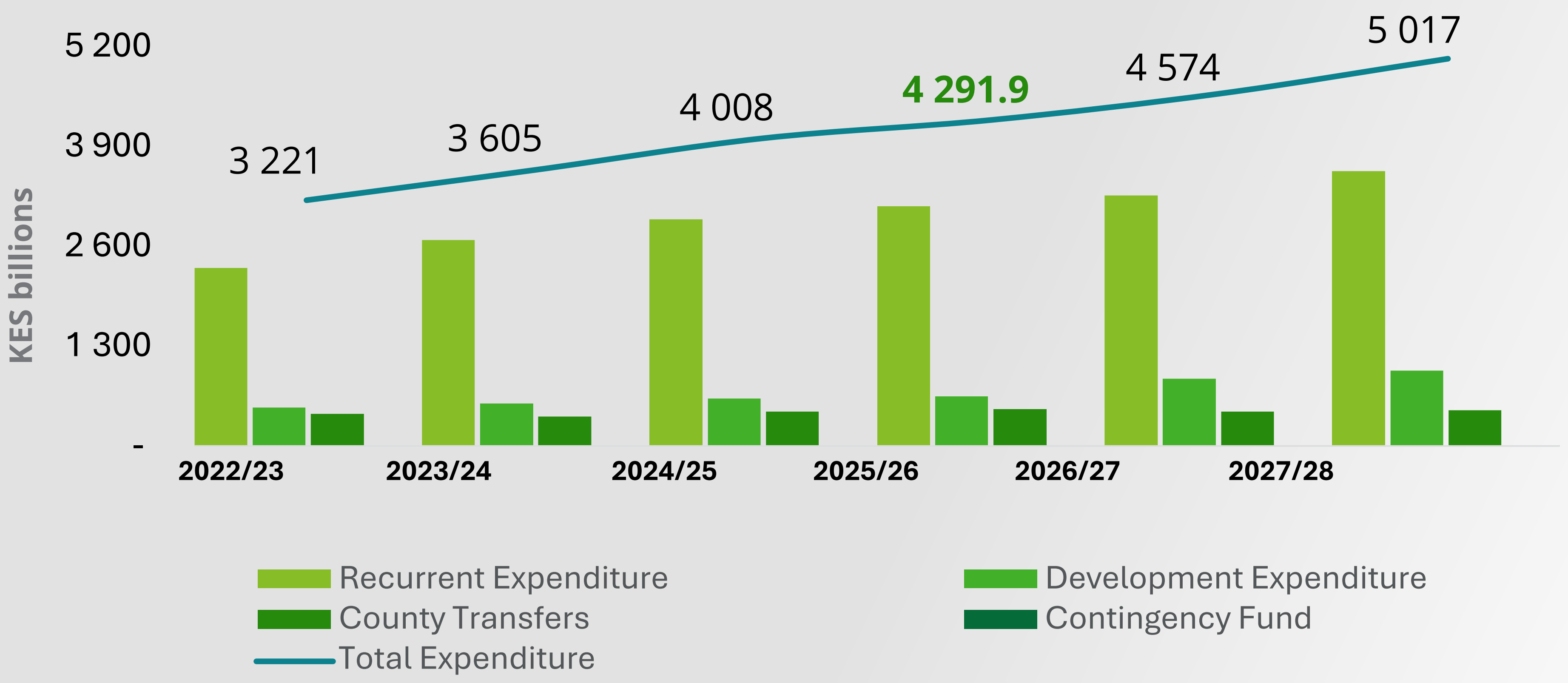
# Budget Overview

## Budget Growth




*Source: The National Treasury's Budget Summary for the Fiscal Year 25/26*

## Budget Trends




*Source: The National Treasury's Budget Summary for the Fiscal Year 25/26*

The Government has presented a budget of KES 4.292 Trn for the FY 25/26 representing a 7.1% increase from the FY 24/25 budget of KES 4.007 Trn.

Recurrent expenditure consumes the lions' share of the projected budget at KES 3.134 Trn (73%) while development expenditure is projected at KES 693.2 Bn (16%) in FY 25/26. Allocations to County Governments are projected at KES 474.9 Bn (11%).

The FY 25/26 budget represents 22.3% of the country's GDP for the period down from 22.9% in FY 24/25 speaking toward fiscal consolidation.

The FY 25/26 budget represents a 7.1% year on year growth as compared to the 11.2% growth evidenced between the FY 23/24 and FY 24/25 fiscal cycles.

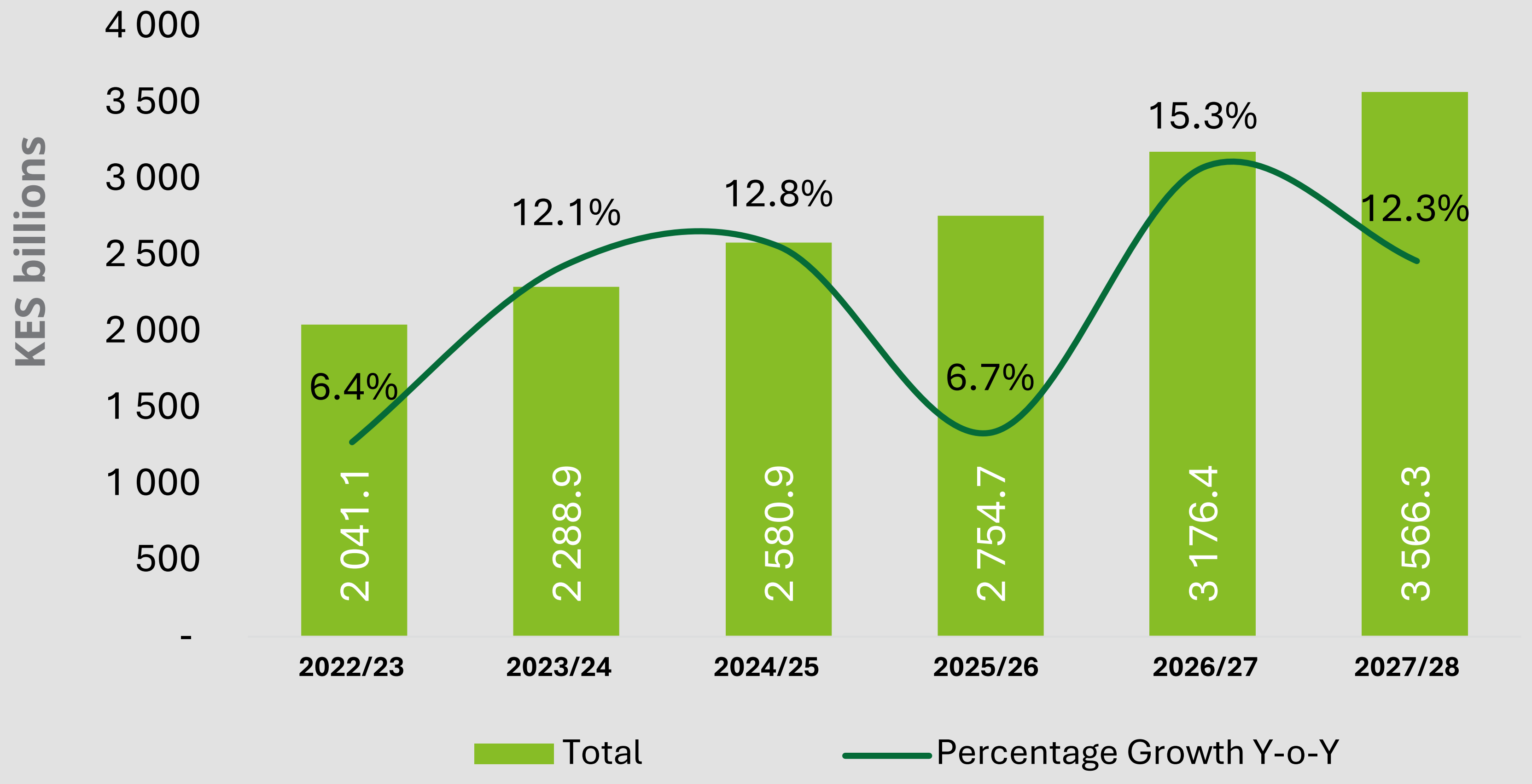
The reduced growth in the budget illustrates efforts toward containing expenditure pressures, particularly in light of significant debt obligations.

Resultant of these efforts, the projected fiscal deficit for FY 25/26 is expected to reduce from KES 997.5 Bn to KES 923.2 Bn representing a 7.5% decline.

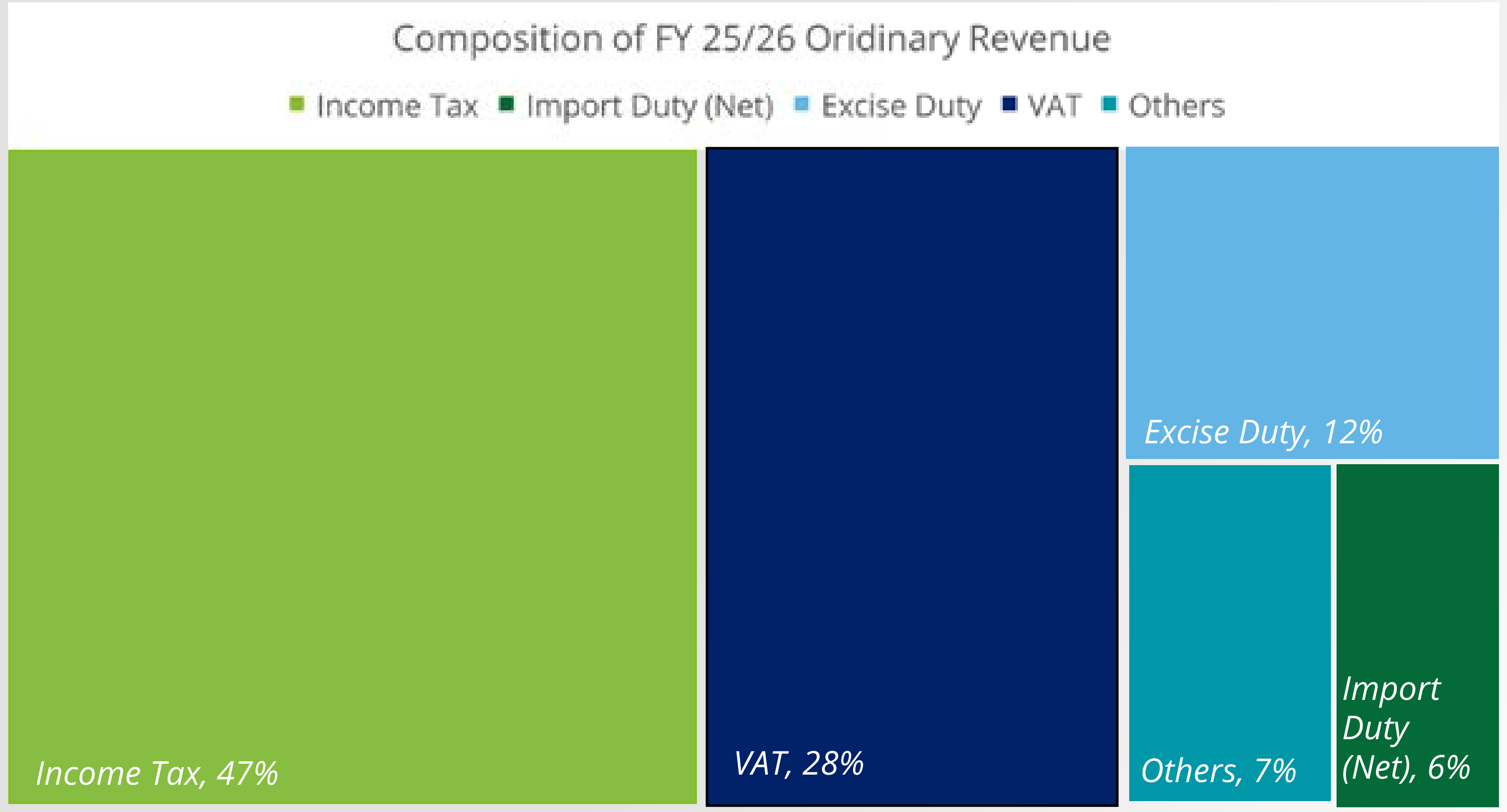
*Source: The National Treasury's Budget Summary for the Fiscal Year 25/26*

# Trend in actual revenue collections

## Trends in Ordinary Revenue




*Source: The National Treasury's Budget Summary for the Fiscal Year 25/26*




*Source: The National Treasury's Budget Summary for the Fiscal Year 25/26*

The Government projects to collect ordinary revenue to the tune of KES 2.755 Trn in FY 25/26 from the projected KES 2.581 Trn in FY24/25, representing a growth of 6.7%.

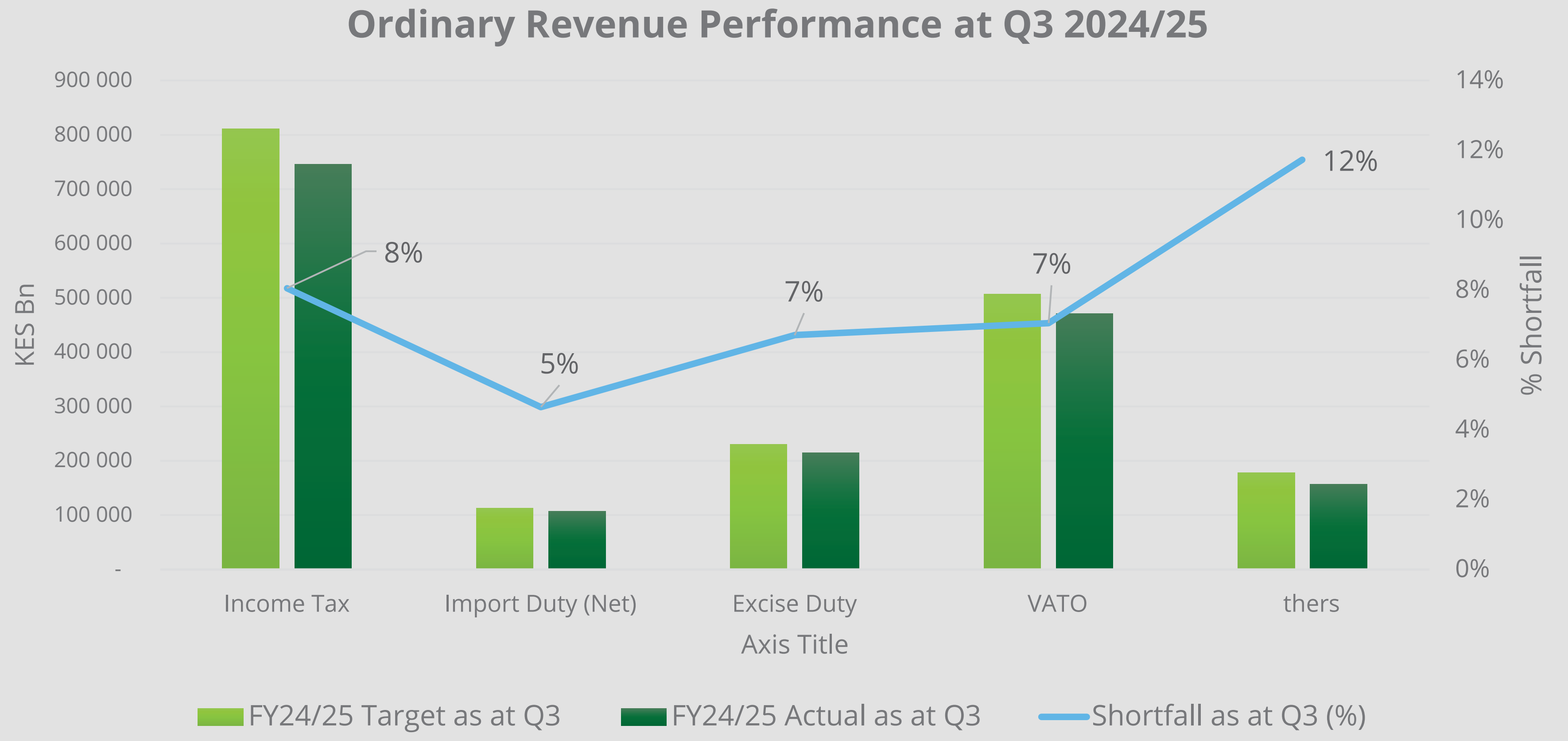
The projected year on year growth in ordinary revenues of 6.7% may be viewed as conservative keeping in mind that growth is ordinarily projected to be in double digit percentage points.

This largely considers the country's low appetite to increased taxation together with fewer revenue raising measures contained in the Finance Bill, 2025.

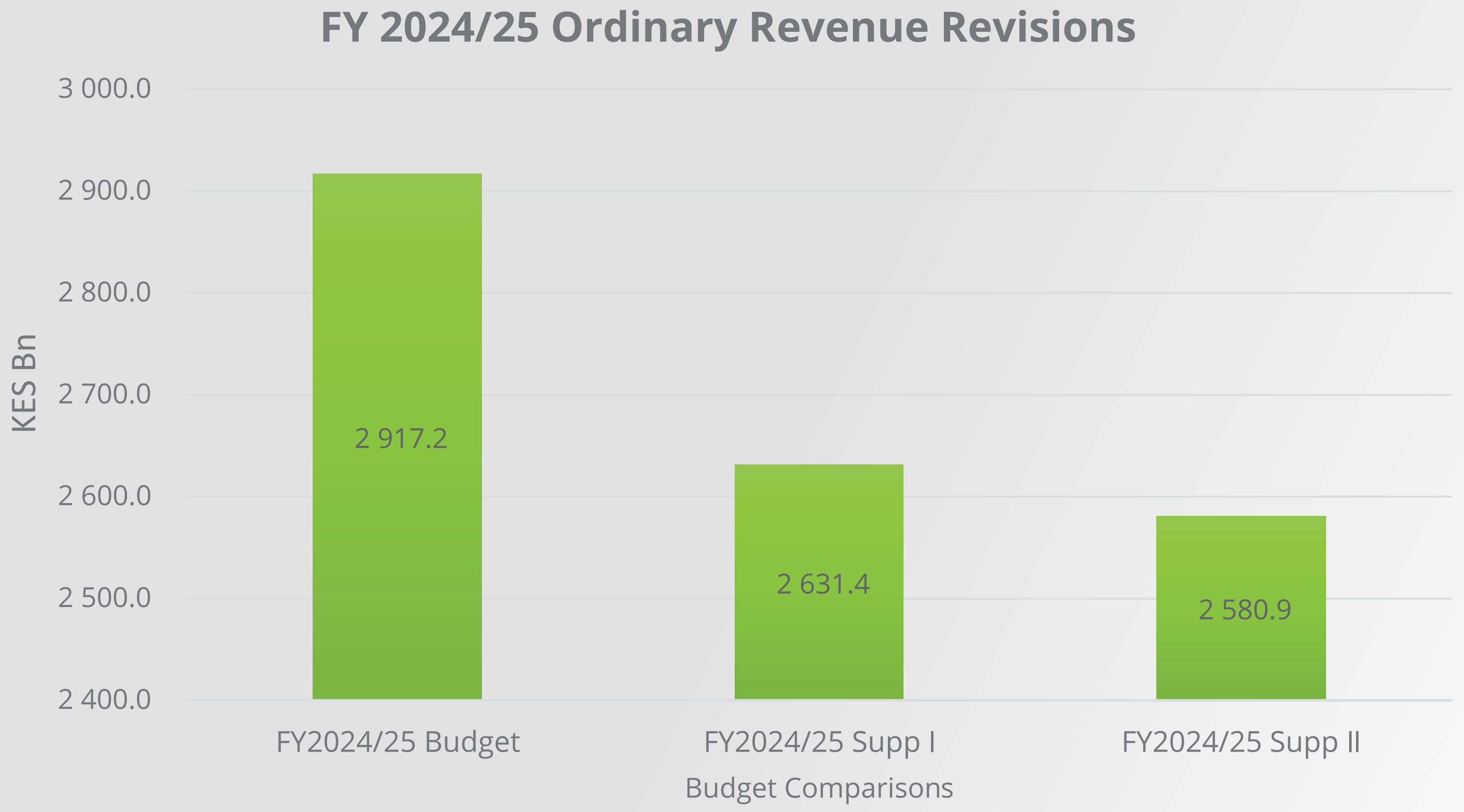
Of the projected ordinary revenue of KES 2.755 Trn in FY 25/26, income taxes are expected to contribute the lion's share at KES 1.285 Trn being 47% of the projected ordinary revenues.

On the other hand, VAT is projected to rake in KES 772 Bn, being 28% of the ordinary revenue projections while excise duty collections are estimated to be KES 336 Bn, being 12%.

# Trend in actual revenue collections




*Source: The National Treasury's Budget Summary for the Fiscal Year 25/26*




*Source: The National Treasury's Budget Summary for the Fiscal Year 25/26*

**As at 31 March 2025, ordinary revenue collections have evidenced an overall shortfall of 8%. The Government has raised ordinary revenues of KES 1.697 Trn against a target of KES 1.840 Trn representing a shortfall of KES 142.8 Bn.**

**Should revenue performance remain constant in Q4 FY 24/25, a similar shortfall may be evidenced at the close of the financial year.**

**Where collection shortfalls persist into FY 25/26, this may diminish the Government's fiscal space to cater for significant debt servicing obligations arising in the year.**

**Due to the withdrawal of the Finance Bill 2024, revenue projections as at 01 June 2024 were revised downward twice via the FY 24/25 supplementary budget I and II.**

**Overall, the FY 24/25 projected ordinary revenue of KES 2.580 Trn is 11.5% (337B) lower than the initial budget of KES 2.917 Trn.**

# Trend in actual revenue collections

Not commenced
Proposed / Ongoing
Implemented
Scheduled

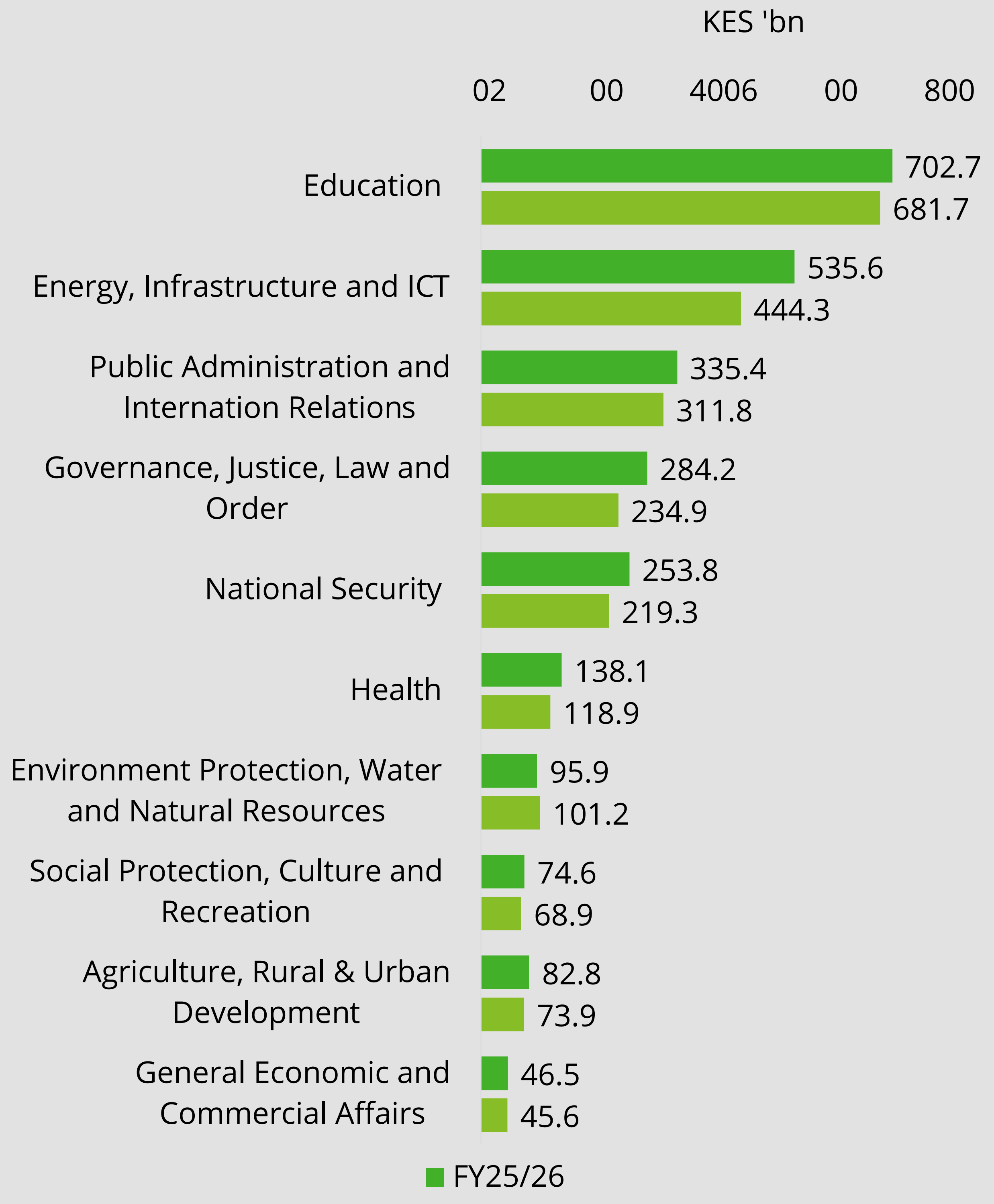
## Medium Term Revenue Strategy Implementation Matrix (Key highlights)

| | FY 24/25 | FY 25/26 | FY 26/27 | Status |
|---|---|---|---|---|
| Reduction of CIT rate from 30% to 28% | | | | Not commenced |
| Review and harmonization of non-resident WHT with resident rates | | | | Not commenced |
| Review the mechanisms underpinning taxation on repatriated profits | | | | Implemented via the Finance Act, 2023. Further review expected in FY 26/27 |
| Introduction of WHT on goods supplied to public entities | | | | Implemented via the TLAA, 24. Further proposal in the Finance Bill, 2025. |
| Review personal income tax bands to enhance progressivity | | | | Not commenced |
| Implementation of exempt pension regime | | | | Proposed under the Finance Bill, 2025. |
| Adjust the VAT registration threshold to KES 8M | | | | Proposed under the Finance Bill, 2024. Withdrawn |
| Reduce the VAT standard rate (By 1% in FY 24/25 and a further 1% in FY 26/27) | | | | Not commenced |
| Rationalising VAT exemption and zero-rating regime | | | | Ongoing |
| Implementation of cardon tax incl. motor vehicle circulation tax | | | | Proposed under the Finance Bill, 2024. Withdrawn |

# Sectoral Highlights

# Sectoral Allocations

**Summary of sector allocation**




*Source: Kenya Budget Speech*

***The largest winners in the 2025/2026 budgetary allocation include:***

### Education

The education sector has been allocated KES 702.7bn in FY25/26 a 3.1% increase from KES 681.7bn in FY24/25. The sector received 27.6% of the total sectoral allocation, aimed at promoting quality and inclusive education for sustainable socio-economic development.

The government is keen on building capacity to ensure smooth student transitions to junior secondary schools under the competency-based-curriculum (CBC) system and to facilitate increased student intake in technical and vocational education and training institutes.

### Energy, infrastructure, and ICT

The Energy, Infrastructure, and ICT sector has been allocated KES 535.6bn in FY25/26, a 20.6% increase from KES 444.3bn in FY24/25, making up 21.0% of the total sectoral allocation.
The sectoral allocation will be critical for creating employment opportunities, especially within the affordable housing program, and enhancing the transport sector through the construction and maintenance of roads and ports.

### Public administration and international relations

This sector has been allocated KES 335.4bn in FY25/26, an 7.6% increase from KES 311.8bn in FY24/25, representing 13.2% of the total allocation.
The funding will support 44 programmes and 120 subprograms aimed at achieving the Bottom-Up Economic Transformation Agenda.

# Sectoral Allocations

## Education

- The government recognises education as a key sector and has increased sectorial allocation by 3.1% in FY25/26 to KES 702.7bn. Education is a key driver in promoting political, social, and economic development through education and training to create a knowledge-based economy.
- Key priorities for FY25/26 include;
    - Prioritise funding for tertiary and higher education to ensure that Kenyans receive the knowledge and skills they need to satisfy labor market demands and encourage entrepreneurship;
    - To expand digital learning programs and the provision of ICT infrastructure, to empower learners with the knowledge and digital skills required to thrive in a fast-evolving global marketplace;
    - Investing in teacher welfare and capacity development prioritising professional development, recruitment, and enhanced teacher support, particularly in underserved regions; and
    - Awarding student loans (HELB) to university and TVET students.
- These initiatives aim to build a knowledge-based economy and promote sustainable political, social, and economic development.

3.1%

KES. 702.7bn

## Energy, Infrastructure, and ICT

- The energy, infrastructure, and ICT sector has received the second highest allocation in FY25/26 budget reiterating its crucial role in Kenya's socio-economic progress. Allocation increased by 20.6% from KES 444.3bn in FY24/25 to KES 535.6bn in FY25/26.
- The sector functions as a driver and enabler to the other sectors of the economy.
- Key priorities for FY25/26 include:
    - Construction and maintenance of roads, bridges, railways, and ports;
    - Construction of transmission lines, transmission substations, distribution lines and distribution substations;
    - Building affordable housing units and social housing units;
    - Connecting additional customers to electricity;
    - Installing on-grid and off-grid standalone solar home systems to enhance electricity access;
    - Laying kilometres of fibre cables; and
    - Providing internet connectivity to public institutions.

20.6%

KES. 535.6bn

# Sectoral Allocations

**Health**

- The government increased the budgetary allocation to the healthcare sector by 16.2% from KES 118.9bn to KES 138.1bn. The government recognises the healthcare sector as an important contributor to the national economic growth through ensuring that all Kenyans are productive and live a healthy life.
- Priority programs for FY25/26 include:
  - Expanding primary healthcare infrastructure, focusing on maternal and child health, and improving supply chains for essential health products;
  - Investing in digital health infrastructure to connect healthcare facilities with the National Optic Fibre Backbone Infrastructure (NOFBI); and
  - Implementation of the Electronic Community Health Information System (eCHIS).
  - The sector aims to expand the Universal Health Coverage (UHC) and strengthening the health system's resilience.

↑16.2%

KES. 138.1bn

**Public Administration and International Relations**

- The government recognises that Public Administration and International Relations (PAIR) is key in coordinating, managing, and overseeing the planning, administrative, public finance, and legislative functions of the government, and in promoting Kenya's international relations. The budget's allocation to PAIR increased by 7.6% from KES 311.8bn in FY24/25 to KES 286.8bn in FY25/26.
- Key priorities for FY25/26 include;
  - Implement 44 programmes and 120 sub-programmes designed to address citizen's needs, enhancing service delivery; and
  - Promote comprehensive public financial management, intensify resource mobilization, and strengthen monitoring and evaluation.

↑7.6%

KES. 286.8bn

# Proposed Tax Measures

# Overview of Income Taxes

***"Kenya stands a chance to be on the strategic roadmap to be prosperous as a middle-income economy."***

Walter Mutwiri
Partner,Tax & Legal
Deloitte East Africa

The Bill predominantly mirrors the fiscal policy measures set out in the 2025 Budget Policy Statement ("BPS"). The foremost objectives include, inter-alia, strengthening tax administration to enhance compliance, expansion of the tax base, minimization of tax expenditure, sealing of tax leakage loopholes and invocation of technology to remodel and transform tax management processes. In essence, the Bill is a blend of tax administration and fiscal policy measures aimed at boosting revenue collection.

The BPS has projected a total revenue of KES 3.385 trillion made up of ordinary revenue (tax collections), Appropriation in Aid ("A in A"), which is revenue from Government fees and levies, and grants for the year 2024/25. Thus far, the KRA has reported a decline in revenue collections when juxtaposed to the intended target for the fiscal year. This is evident in the total revenue for the period from July 2024 to March 2025, which amounted to KES 1.697 trillion against a target of KES 2.475 trillion from ordinary revenue. The actual total revenue for the same period is KES 2.013 trillion, which represents a 59% yield against the projected annual revenue (KES 3.385 trillion).

Considering that the fiscal year is nearing the end, it is highly unlikely that the KRA will meet the projected revenue target, hence the anchorage of the Bill towards sealing of loopholes for acceleration of revenue collection in the coming financial year. This is indeed a delicate balancing act especially in the wake of widespread hue and cry occasioned by the recent focus on personal taxes where the general feel has been that the salaried population within the formal ecosystem is overburdened with taxes amidst tough economic times.

In addition, the cost of doing business is excessive on account of high taxes, high cost of borrowing and high cost of energy when compared to peers within the region. However, the base lending rates continue to reduce by dint of interventions by the CBK and the expectation is that this will give businesses the much-needed impetus for growth in the coming days.

Against the backdrop of tough economic times and reduced disposable income, it is arguable that imposition of further taxes on employment income would have been untenable particularly in the wake of public uproar that culminated in protests against incremental taxes contained in the Finance Bill, 2024. Besides, the trickle-down effect of incremental taxes would be detrimental to the economy at large and consequently minimize the impact of the intended economic stimulation.

The Bill was expected to be guided broadly by provisions of the MTRS, whose mission is to enhance domestic revenue collection and thus its pivotal impact in the Bill. On the premise that the MTRS aims to reduce tax disputes, the Bill discharges this by proposing to introduce Advance Pricing Agreements on transactions between related parties subject to Transfer Pricing ("TP") rules where taxpayers will be allowed to agree with the KRA on an appropriate criterion for the determination of the arm's length outcome for future related party transactions. In effect, potential disputes with regards to TP will be averted in the nascent stages. Similarly, in line with the MTRS, the Bill seeks to expand the tax base through a raft proposals such as expansion of the scoping for royalty to include payments for distribution of software in instances where there are regular payments for the use of the software through the distributor; the scoping for SEPT, to include any income that is accrued in or derived from Kenya by non – residents through a business carried out over the internet or electronic network including through a digital marketplace.

# Overview of Income Taxes

Additionally, the Bill seeks to minimize tax expenditure which is equally in line with the MTRS. Key proposals that are reflective of this intent include; the limitation of period to carry forward of tax losses to five years; a repeal of accelerated investment allowance in the first year of use for investments made outside Nairobi and Mombasa counties relating to buildings used for manufacture; hotel buildings and machinery used for manufacture and also investment in SEZs and a repeal of preferential tax rates applicable to companies engaged in the construction of at least 100 residential units in a year as well as those engaged in the local assembly of motor vehicles.

Notably, some of the proposals in the Bill constitute retractions of very recent legislative tax provisions. For instance, the proposal to share data with the Commissioner relating to trade secrets and personal data and exclusion of weekends and public holidays within the timeframe for consideration for purposes of lodgment of objections and appeals to tax disputes, were both enactments in the Tax Laws Amendment Act, 2024 which took effect from 27 December 2024 and aimed at achieving the converse of the Bill. Whilst it is worthwhile to take cognizance that some of the retractions are in harmony with the MRTS, aggressive tax measures coupled with frequent changes serve to suppress economic growth and deter both domestic and foreign direct investments. This is because some investment decisions are influenced by tax incentives contained in prevailing tax legislative provisions. Therefore, recurrent changes to those provisions serve to erode investor confidence as well as shunning away potential investors. Holistically, frequent changes to tax legislative provisions create uncertainty and anxiety to taxpayers while at the same time disrupting businesses' operating environment. In effect, the intended steadiness with respect to tax operating framework as envisaged in the National Tax Policy ("NTP") is rescinded.

It is worth mentioning that the country's economic landscape has been marred by huge expenditure that is channeled towards recurrent bills, with an insignificant portion going towards development. Therefore, there is need to invoke radical measures that will address the expenditure problem at hand right away including dealing firmly with rampant corruption, illicit trade and pilferage. Further, in order to build a robust, stable and predictable tax system that supports sustainable economic growth, proposed fiscal measures should always seek to align with the NTP, which is a prime policy framework that when effectively implemented and utilized can stimulate economic growth both in the short and long runs.

In conclusion, the National Budget for the fiscal year 2025/26 presents an opportunity for Kenya to address its fiscal challenges, its ballooning public debt while at the same time creating an environment fit for purpose as an engine for spurring growth. By invocation of ways to deal with revenue challenges and fixing the expenditure gaps, Kenya stands a chance to be on the strategic roadmap to be prosperous as a middle-income economy.

***"The National Budget for the fiscal year 2025/26 presents an opportunity for Kenya to address its fiscal challenges, its ballooning public debt while at the same time creating an environment fit for purpose as an engine for spurring growth."***

# Income Tax Measures

## *Corporate Income Tax*

- The carry-forward period for tax losses to be capped at 5 years.
- The accelerated investment allowance rates of 100% and 150% for investments made outside Nairobi and Mombasa Counties to be scrapped. These rates apply to machinery and buildings used for manufacture, and hotel buildings.
- The reduced corporate tax rate of 15% for companies that construct at least 100 residential units a year, and those whose business is local assembly of motor vehicles to be repealed.
- Companies certified by the Nairobi International Financial Centre Authority (NIFCA) to be taxed at 15% in the first 10 years of operation and 20% for the next 10 years where the company invests at least KES 3 billion in the first 3 years of operation, is a holding company with at least 75% of its top management being Kenyans, and the regional headquarters of the company are in Kenya with at least 60% of its top management being Kenyan citizens.
- Startup companies certified by the NIFCA to be taxed at 15% in their first 3 years and 20% for the next 4 years.
- Dividends paid by companies certified by the NIFCA to be exempt from tax if the companies reinvest at least KES 250 million in the year.
- Payments into and out of the Social Health Insurance Fund (SHIF) to be exempted from tax.
- Taxpayers to claim deductions in respect of expenditure incurred in the construction of a public sports facility.
- The cost of any implement, utensil or similar article to be allowable as a deduction in full.
- Deductions in respect of expenditure incurred by a person sponsoring sports, with the prior approval of the Cabinet Secretary responsible for sports, to be repealed.
- APAs which will allow taxpayers to enter into transfer pricing agreements with the Commissioner, to be introduced. APAs will be valid for up to 5 years.
- A single entity within a Multinational Entity resident in Kenya, can be designated by the ultimate parent entity, to file a Country – by – Country report on behalf of other resident entities within the same group with the Commissioner.
- The Fringe Benefit Tax (FBT) rate, which was erroneously deleted by the Tax Laws Amendment Act, 2024 is to be reinstated. As was the case before the accidental deletion, FBT shall apply at the resident corporate tax rate (currently 30%) to any loan advanced by an employer to its employees or directors at lower interest rates than the Commissioner's prescribed rates.
- The Domestic Minimum Top-up Tax (DMTT), which was introduced through the Tax Laws Amendment Act 2024, to be payable within 4 months after year end. DMTT is the additional top-up tax that is payable by covered persons whose combined effective tax rate falls below 15% in a given year of income.
- Applications for change of the accounting year-end to be deemed allowed if the Commissioner does not respond within 6 months from the date the application is made.
- The period within which the Commissioner should issue a tax exemption certificate to an applicant to be increased from 60 days to 90 days.
- The instalment tax underpayment penalty of 20% stipulated in the Income Tax Act to be repealed. The 5% penalty stipulated in the Tax Procedures Act shall therefore be expected to apply.

# Income Tax Measures

## *Personal Income Tax*

- The daily tax-free Per-Diem rates increased from KES 2,000 to KES 10,000.
- The deduction of mortgage interest for owner-occupied property, which currently applies to interest on loans taken for the improvement or purchase of residential property, to be extended to also cover interest on loans taken out for the construction of residential premises.
- All gratuities paid upon attainment of retirement age, including gratuity paid from private schemes, to be exempt from income tax. Currently, only gratuities and allowances paid under a public pension scheme are exempt.
- Withholding tax on qualifying interest to be final tax. The Tax Laws (Amendment) Act 2024 had introduced a confusion regarding this.
- Provisions which spell out tax-exempt thresholds for taxable withdrawals from pensions, provident funds and home ownership savings plans to be repealed. Tax exemptions shall only apply to withdrawals made upon attainment of the retirement age, early retirement due to ill-health, or on completion of at least twenty years from the date of registration as a member of the fund.
- The deduction of one-thirds of the employment income of individuals who are not citizens of Kenya and who are in Kenya solely for performance of their duties in relation to the employer's regional office is to be repealed.

## *Withholding Tax*

- The definition of royalty to be expanded to include payments made in respect of the distribution of software where regular payments are made for the use of software through the distributor. Such payments shall therefore attract withholding tax.
- Section 10 of the Income Tax Act is to be amended to deem payments in respect of the supply of goods to a public entity and the sale of scrap to be income accrued in or derived from Kenya. This is aimed at enforcing the withholding tax obligation introduced through the Tax Laws Amendment Act, 2024 on such payments.
- Tax on the income of non-resident ship owners and charterers to be collected through the withholding tax regime. The tax is currently collected through the self assessment regime.
- Withholding tax shall not be recovered from the payer where tax will have been accounted by the recipient of the payment.

## *Capital Gains Tax*

- The Capital Gains Tax (CGT) exemption on property transfers within a special economic zone to be limited to transfers where the transferor is a licensed special economic zone developer, enterprise or operator.
- Transfer of property to a company where the individual, spouses, spouse or immediate family members hold 100% shares to be CGT exempt. Immediate family means the children of the spouse or former spouse.
- The CGT exemption for securities traded on a licensed securities exchange to be extended to individuals. The exemption currently applies to companies only.
- The provision that allows a person to claim a deduction of capital losses is to be repealed.

## *Taxation of the Digital Economy*

- The scope of SEPT to be expanded to cover any income that is accrued in or derived from Kenya by a non-resident through a business carried out over the internet or an electronic network including through a digital marketplace. The current provision only captures income accruing to a non-resident from the provision of services through a digital marketplace.
- The minimum threshold of KES 5 million for SEPT to be scrapped.
- The rate for Digital Asset Tax to be reduced from 3% to 1.5%.

# Overview of Indirect Taxes

## *"Indirect taxes continue to contribute heavily to the government's ordinary revenue..."*

According to the 2025 Budget Policy Statement, all broad-based categories of ordinary revenue did not meet the half year to December 2024 revenue target. The government reported a shortfall of KES 93.2 billion. Of this amount, KES 56.3 billion related to indirect taxes with VAT, Excise Duty and Import Duty reporting shortfalls of KES 36.5 billion, KES 13.7 billion and KES 6.1 billion respectively. As a result, the government revised its expected ordinary revenue collections for the fiscal year 2024/2025 from KES 2,631.4 billion to KES 2,580.9 billion. This is despite the recent changes to tax laws that were introduced through the Tax Laws (Amendment) Act 2024 that aimed, in part, to boost revenue collection for the second part of the fiscal year.

Nevertheless, indirect taxes continue to contribute heavily to the government's ordinary revenue with the budget estimates for the year 2024/2025 suggesting a targeted collection of close to 49% of the government's planned ordinary revenue of KES 2,917.2 billion. In addition, there is an expected growth of the targeted revenue from indirect taxes from the short term to the medium term with the government forecasting collection of KES 1,871.8 billion from indirect taxes by the year 2028/2029.

To this end, for the coming fiscal year, the Bill has suggested several changes to the VAT, excise duty and miscellaneous fees and levies regimes that aim to shore up revenue collection and perhaps seal revenue leakages.

From a VAT standpoint, some of the revenue enhancing measures that the Bill proposes include the introduction of internet, radio, and television broadcasting services within the ambit of electronic services and the subjecting of these services to VAT at 16%. The Bill further proposes the removal of certain products from the exemption schedule, thus effectively also rendering them subject to VAT at 16%. These include items such as aircrafts of Chapter 88(except heavy aircraft weighing more than 2000Kgs), input for the manufacture of passenger vehicles locally, locally manufactured passenger and special tour vehicles as well as certain medicaments.

In addition, the Bill has proposed to move certain supplies from zero-rating to exemption. It has also addressed revenue leakage and tax expenditure by, among others, deleting provisions of the VAT law that permit refunds relating to official aid funded projects. The changes further include streamlining measures that seek to align the procedure for VAT refunds largely to what is prescribed under the Tax Procedures Act.

Further, proposed changes to the Excise Duty law generally seek to provide clarity to existing provisions through definition of certain terms and cleanup of certain drafting errors introduced through the Tax Laws Amendment Act, 2024. Some of the clarifications provided include definition of the scope of excisable services offered by non-resident to include services offered over electronic, internet or digital platforms, definition of digital lenders, changes to the tax base for coal, and imported float glass. The Bill also proposes to reduce excise duty on neutral spirts purchased by licensed manufacturers of spiritous beverages from KES 10 per centilitre of pure alcohol (approx. KES 964 per litre for spirits of 96.4% alcoholic strength) to KES 500 per Litre. Unlike the recent years, the Bill has not introduced excise duty on new products or increased excise duty on existing products.

In terms of miscellaneous fees and levies, one notable change is the reduction of the Export and Investment Promotion Levy ("EIPL") rate on certain products of iron and non-alloy steel, a move that is perhaps aimed at boosting the construction and manufacturing industries.

In conclusion, it must be noted that indirect taxes are mainly premised on consumption. Their main trigger is the availability of disposable income in the economy. Inevitably, a growth in the collection of VAT, excise duty, import duties and other miscellaneous fees and levies hinges on the growth of the earning capacity of most Kenyans and the creation of employment and entrepreneurial opportunities for the emerging higher percentage of young people. It is therefore paramount that the government invests in creating an enabling environment that will enable businesses to thrive if it's going to realize its medium term to long term revenue collection ambition.

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# Indirect Tax Measures

## *Value Added Tax (VAT)*

- Change of the definition of tax invoice to mean an electronic tax invoice issued in accordance with the Tax Procedures Act.
- Expansion of the requirement to issue tax invoice to cover all supplies, irrespective of their VAT status. Current requirement only covers taxable supplies.
- Change of the statutory timelines within which one may apply for refund of VAT paid on bad debts from three years to two years.
- Clean-up of the provisions requiring a registered person to refund tax to the Commissioner if bad debts occasioning a refund are subsequently recovered from the recipient. Proposal deletes the timeline of sixty days and retains thirty days. Similar clean-up on the provisions relating to interest on late refunds.
- Expansion of the scope of VAT on digital marketplace supplies to include internet, radio or television broadcasting services within the scope of VAT.
- Deletion of the provision of the VAT law allowing taxpayers to offset excess withholding VAT credits against other tax liabilities. However, provisions permitting offsets under the TPA remain.
- Removal of exemptions on key sectors such as tourism, housing, energy, mining, and local vehicle manufacturing, widening the VAT base.
- Restriction of exemptions on official aid funded projects (to exclude fuels, lubricants, tyres) and deletion of exemptions for certain aircraft parts and tourism vehicles.
- Move from zero-rate to exempt status for, among others, inputs for local manufacture of medicaments and animal feeds, supply of electric buses, bicycles, solar/lithium batteries, BEV stoves, motorcycles, packaging for tea and coffee, and transport of sugarcane from the farm to the mill.
- Several other inclusions, deletions and changes to clean-up both the zero-rating and exemption schedules.
- Introduction of VAT where exempt or zero-rated goods or services are used inconsistently with their intended purpose. If such goods are later used or disposed of otherwise. Aimed to curb misuse of tax incentives by entities in preferential tax zones.

# Indirect Tax Measures

## *Excise Duty*

- Amendment of the definition of a digital lender to mean a person extending credit through an electronic medium but excludes a bank licensed under the Banking Act, a SACCO society registered under the Co-operative Societies Act, or a microfinance institution licensed under the Microfinance Act.
- Expansion of the scope of excisable services offered by non-resident persons to include excisable services offered over the internet, an electronic network, or through a digital marketplace.
- Definition of a digital marketplace to mean an online platform which enables users to sell goods or provide services to other users.
- Classification of excisable goods in the Excise Duty Act will be in accordance with the East African Community Common External Tariff (EACCET).
- Excisable services offered by a non resident outside Kenya will be deemed to be made in Kenya if consumed in Kenya through the internet, an electronic network, or a digital marketplace.
- Introduction of a 14-day timeline for the Commissioner to review and reply to excise duty license applications upon receipt of all valid documents.
- Reduction of excise duty on neutral spirits of alcoholic strength exceeding 90% purchased by licensed manufacturers from KES 10 per centiliter of pure alcohol to KES 500 per litre.
- Excise duty on specific self adhesive and other plates, sheets, film, foil and strip, of plastics will be 25% of the excisable value or KES 200 per Kilogramme whichever is higher.

## *Customs*

- Stay of application of the Common External Tariff (CET) rates has been extended for a further period of one year on the following products:
  - Rice at 35% or USD200/MT instead of 75% or USD345/MT.
  - Leather products at 35%.
- Duty remission is to be extended on the following products for a further period of one year:
  - Wheat at 10% instead of 35% provided the millers enjoying the remission first purchase locally produced wheat.
  - Inputs for assembly of telecommunication devices including mobile phones, laptops and tablets.
  - Inputs for manufacture of animal feeds at 0%.
- Grant of duty remission on inputs for assembly of cranes.
- Tariff split on transformers to distinguish between fully built and unassembled transformers.
- Kenya will not seek stay of application of CET on paper used for manufacture of packaging material. The paper will therefore attract the CET rate of 10%.

## *Miscellaneous Fees and Levies*

- Restriction of Import Declaration Fee (IDF) and Railway Development Levy (RDL) exemption on aircraft and aircraft parts to heavy aircrafts weighing above 2,000 kg.
- Reduction of Export and Investment Promotion Levy on billets and wire rods from 17.5% to 10%.

# Overview of Tax Administration

***"It is paramount that tax administration reforms be carefully balanced with principles that promote administrative fairness and strengthen procedural safeguards"***

Globally, there has been a growing trend among countries to implement significant reforms in tax administration. These reforms generally revolve around three key objectives: First, the enactment of tax laws aimed at enhancing compliance through robust enforcement mechanisms. Second, there is a concerted effort to improve the efficiency and effectiveness of tax administration in order to boost revenue collection. Finally, many jurisdictions are introducing measures to promote high level of voluntary compliance by simplifying tax system's and fostering greater trust between the revenue authorities and taxpayers.

Amidst this wave of reforms, it is essential that tax authorities are equipped with adequate powers for information gathering and tax collection – both to deter non-compliance and facilitate timely revenue collection. Nevertheless, any steps towards reforming tax administration should aim to provide greater certainty to taxpayers while enhancing the legitimacy of the tax authority.

## Proposals in the Finance Bill 2025

If enacted as is, the Finance Bill 2025 ("the Bill") will empower the Commissioner to issue tax agency notices to taxpayers who have appealed against a Tax Appeals Tribunal (TAT) decision. This will compel taxpayers to pay the disputed tax before the appeal process is fully exhausted. Such a provision is punitive especially in instances where the underlying assessments lacks merit. Further, the absence of clear guidance on tax refund in the event of a favourable outcome for the taxpayer increases the risk of administrative inefficiency and potential financial strain in taxpayers.

Further, the Bill proposes to reduce the time available to a taxpayer to file an objection or appeal by disregarding the weekends and public holidays when calculating the response timeline- a departure from the provision introduced under the Tax Laws Amendment Act 2024. This abrupt change, coming just five months after the earlier enactment, introduces uncertainty in the tax administration and may undermine predictability in the application of the tax procedures.

In a bid to enforce collection of taxes from non-residents with no taxable presence in Kenya, the Bill proposes to empower the Commissioner to issue agency notices to the agents of non- compliant non-resident with no tax presence in Kenya. While this measure may strengthen the collection of taxes such as Digital Asset Tax and Significant Economic Presence Tax (SEPT), the proposal raises a concern on due process. Specifically, issuance of an agency notice to the agents does not afford the affected taxpayers an opportunity to present their case before enforcement measures are taken thus undermining the procedural fairness.

The Bill also proposes several measures aimed at streamlining existing legislation and reducing ambiguity. For instance, the Bill proposes to remove withholding tax payments from the list of items exempt from electronic tax invoice management system (e-TIMS). This proposal provides clarity by explicitly stating that withholding tax payments are not subject to e-Tims thus aligning the legalisation with practical treatment of such payments – this may have been a drafting error from the onset.

## Conclusion

Overall, the proposals set out in the Bill reflect a broader global trend towards strengthening tax administration through enhanced enforcement to increase revenue collection. Measure such as empowering the Commissioner to issue agency notices and extending the enforcing mechanism to non-residents are clearly aimed at boosting compliance and expanding the tax base. At the same time, efforts to streamline the legislation by cleaning up ambiguous provisions are a step in the right direction towards building a coherent tax framework.

While the proposed administrative reforms may enhance revenue mobilisation, abrupt legislative changes and limited opportunities for taxpayer recourse could undermine trust in the tax systems. To this end, it is paramount that tax administration reforms be carefully balanced with principles that promote administrative fairness and strengthen procedural safeguards for taxpayers.

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# Tax Administration Measures

## *Tax Procedures*

- Payments whose withholding tax is final to be exempt from the eTIMS invoicing requirements.
- The Commissioner to include reasons for amending an assessment in the written assessment notice sent to taxpayers.
- Un-deducted withholding tax will not be recovered from the payer where the recipient of the payment will have accounted for the full principal tax on the payment.
- Property sold by the Commissioner to recover unpaid tax to be exempt from stamp duty.
- Agency notices to be issued to agents of non-resident persons subject to tax in Kenya.
- Increase of the timeline for the Commissioner to determine a refund or offset application from 90 days to 120 days (180 days where there is an audit of the refund application).
- Where a taxpayer is allowed to lodge a late objection, the timeline for issuance of the objection decision would start from the day the objection is lodged .
- Taxpayers will be compelled to share trade secrets, private and personal data with the Commissioner.
- The computation of time required for taxpayers to lodge appeals to the TAT or courts of law, or to object against a tax decision, to include Saturday, Sunday and public holidays (non-working days).
- Penalties and interest arising from system errors to be waived.

## *Other Measures*

Stamp duty exemption to apply on the transfer of property by a company to its shareholders as part of an internal reorganization, provided that:

a.) The property is transferred to shareholders in proportion to their shareholding immediately before the transfer; and

b.) Where the property is shares, such shares should be in a subsidiary of the company undertaking the transfer.

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