NATIONAL ASSEMBLY

OFFICIAL REPORT

Tuesday, 18th June, 1996

The House met at 2.30 p.m.

[Mr. Speaker in the Chair]

PRAYERS

ARRIVAL OF HIS EXCELLENCY THE PRESIDENT

(Mr. Speaker announced the arrival of His Excellency the President, the hon. Daniel Toroitich arap Moi, M.P.)

(Hon. Members rose in their places while His Excellency the President took his seat in the Chair of State)

COMMITTEE OF WAYS AND MEANS

MOTION

THAT MR. SPEAKER DO NOW LEAVE THE CHAIR

The Minister for Finance: (Mr. Mudavadi): Mr. Speaker, Sir, I beg to move that Mr. Speaker do now leave the Chair.

PAPERS LAID

1996/97 Estimates of Revenue of the Government of Kenya for the year ending 30th June, 1997.

1996/97 Financial Statement.

(By the Minister for Finance)

While efforts are being made to improve revenue collection, we need also to be vigilant in the monitoring of public expenditure to minimize the Budget deficit. I am determined to ensure that all Government expenditure is strictly limited to the provisions approved by this House. On the other hand, to accelerate the issuance of development funds to Ministries within the fiscal limits, I am now considering the modalities for the transfer of ordinary revenue to the Development Exchequer Account. As an expression of my determination to eliminate and not to raise expenditure, I intend to publish as from October, the preliminary Budget out-turn on a quarterly basis so that Kenyans can assure themselves that our physical targets are being met. In addition, I tabling today amendments to the Civil Contingencies Fund Act to increase the capital limit of the fund from K£1.5 million to K£100 million.

I now turn to a more detailed review of fiscal policy. As hon. Members are able to refer to the copies of the Printed Estimates, I will limit myself to the areas of the particular concern for growth and fiscal stringency.

Mr. Speaker, Sir, 143 public enterprises have now been disposed of or brought to the point of sale. And to date, this has yielded K£374 million to the Treasury and the public sector holding companies. A further K£100 million is already expected to accrue to the Treasury in the immediate future from privatization that are at an advanced stage of preparation.

We intend to eliminate or substantially reduce Government shareholdings in all the remaining 64 designated parastatals by the end of 1997. We will encourage the participation of Kenyans in the new ownership both by reserving some of the shares and by ensuring transparency in the bidding process. We have successfully sold more than 76 per cent of the Government stock in Kenya Airways and its subsidiaries, and other divestitures and public floatations planned in the coming months include the Nyayo Bus Corporation, the National Bank of Kenya, the Kenya Commercial Bank, the Chemelil and Mumias Sugar Companies and Kenya Reinsurance Corporation.

Furthermore, the Kenya Tourist Development Corporation is already divesting its holdings in several lodges and hotels including African Tours and Hotels and the Serena Properties and Lodges. We will ensure that those parastatals which are being retained in public ownership because of their strategic significance are rationalised so as to enhance their productivity and quality of service delivery while at the same time reducing their drain on our fiscal resources.

As the list of such initiatives is long, I will
refer, briefly, to the more important among them. The assessment of pararastals close debts and tax arrears is now complete and process of settlement is underway. Performance contracts have been developed or are at an advanced stage of preparation while new or improved maintenance agreements have been negotiated with private contractors. Agreed operational restriction activities include the separation of functional units into profit centres and autonomous companies and we are also introducing legislation to provide for the clear-cut or regulatory and commercial functions and to eliminate monopolies which it makes economic sense to do so. To facilitate these reforms most of the agencies concerned have been exempted from the provisions of the State Corporations' Act.

Mr. Speaker, Sir, all Ministries are now committed to relaxing their restrictions on private sector provision of services relating to marketing, training, extension work, research, auditing, inspection, computerisation, publishing and so on.

In the coming year, I intend to use my powers under the Stamp Duty Act to contract out the selling of revenue stamps so as to improve their distribution throughout the country and thereby minimise the loss of revenue from unpaid stamp duty.

Mr. Speaker, Sir, the Commission of Inquiry on Local Authorities has established that the inability of the Local Authorities to fund their services and redeem their debts is not simply a matter of the limited scope of their revenue sources. It is much more the case that these sources are now exploited inefficiently and that some councillors and civic officials have betrayed their trust and exerted pressure to favour their personal and political ends. The present situation is most unsatisfactory, but remedial measures are now being taken under the Local Government Reform Programme and Urban Transport Infrastructure Project. These reform measures focus on upgrading financial and project planning management, reducing excessive licensing and reforming agricultural cessage and improving revenue assessment and collection.

Mr. Speaker, Sir, the Civil Service Reform Programme has resulted in 20 per cent reduction in staffing number since June 1993. Contrary to misrepresentations in some quarters, the objective is not to reduce of the provision of essential Government service, but actually to improve services through a more rational use of scarce resources. We have taken special care to safeguard the viability of key cadres in priority staffing areas and a skilled retention programme is being implemented emphasising training and performance related paying.

Retrenchment expenditure on directly related pension, terminal grants and retraining course has now amounted to some K£279 million. And these measures have already yielded annually net savings in salaries and allowances of the order of K£72 million which implies that the present payback period of well under four years. I propose to set aside some K£50 million for this purpose in 1996/97 which should reduce payback period even more.

Mr. Speaker, Sir, the Government will ensure that the structure of its expenditure is in conformity with its developmental priorities as set out in the public expenditure review. The share development expenditure will be increased, 75 per cent of which is committed for core projects.

Mr. Speaker, Sir, the progress achieved so far in poverty alleviation still remains unsatisfactory, especially as this is the United Nations Year for the reduction of absolute poverty whose objective we fully support. Nonetheless, I am confident that the programmes we initiated last year will soon yield more tangible and positive results.

In the coming year, I am proposing to make special allocation of K£160 million for particular poverty targeted programmes as well as increasing the general provisions for the social services. In the rural areas, increased funding is being provided to rehabilitate minor roads and stock routes to increase the availability of local crop storage facilities, to improve access to unpolluted water for human and livestock use, to expand the school feeding and immunisation programme, to enhance district and locational health care and to encourage workshops for artisans especially for women groups. In the urban areas, I propose to fund great public efforts relating to the installation of water treatment plants and water kiosks, the co-operative societies and other institutions will be encouraged to finance local housing development, financial technical assistance will also be provided to alleviate the education and other problems of street children, *Jua Kali* enterprises and women groups.

While these measures are of critical importance, to be fully effective, they must take place in the context of fast and sustained economic growth. Thus, we have been careful to maximise employment and training opportunities in our poverty alleviation programmes so as to increase their contribution to GDP growth through sustainable self-help groups.

Mr. Speaker, Sir, the private sector continues to lead in employment generation while public sector employment is being contained. The existing employment generating programmes include measures to improve geographical and occupational mobility in general through enhanced communications, employment focused technical and management training together with a special credit and extension schemes oriented towards the development of club based women groups, *Jua Kali* operators and youth. To build on their success, I am making increased provision for all these programmes next year. In particular, I propose to set aside K£10 million to supplement the Head of State efforts towards the establishment of the National Youth Development Fund whose objective is to promote employment for the youth through the self-help groups. This Fund will be made operational through the DDC mechanism. I would also like to retaliate here that this programme does not bear the face of any political party.

Mr. Speaker, Sir, it has been noted on many occasions, and with truth, that investment in education is the most important single factor underpinning growth. It is for this reason that the Government has always made generous budgetary provision for this sector. In 1996/97, I am proposing to increase the overall education budget by 10 per cent. The numbers and subject range of text books being supplied to schools from public funds will be increased while further efforts will be made to moderate cost of books and other school items paid for by the parents. Funding for the school milk and feeding programmes is being increased in the ASAL areas and a school bursary programme for secondary education is being doubled.

As part of the on-going process of decentralising financial responsibility, the governing boards of schools, polytechnics and institutes of technology will have complete authority over their fees. However, the Government will continue to monitor the situation carefully and intervene whenever there is evidence of exploitation especially in the poorer areas. Expenditure decisions are also being decentralised in the tertiary education sector and the University Councils will soon have complete autonomy on the determination of their tuition, accommodation and catering fees. To enforce financial discipline, the Higher Education Loans Board (HELB) has been given adequate powers to step up its loan recovery rate and the commercial banks are invited to participate in student financing.

Mr. Speaker, Sir, the Government has been progressively increasing the budgetary provision in the health sector to improve both facilities and the proportion of critical medical staff in the population. In 1996/97, I propose to increase the health budget by 19 per cent. We intend to keep the growth of this expenditure within realistic bounds through increased fiscal rationalisation. To that end, we are introducing greater financial autonomy at district level and self financing through user charges. Moreover, we are re-orientating funding priorities towards preventive rather than curative care and targeting a much higher rate of treatment cost recovery for the National Hospital Insurance Fund (NHIF). Arrangements are also in hand to improve the cost effectiveness of hospitals, especially referral hospitals, where re-structuring programmes will allow them to concentrate more cost effectively on their referral functions rather than on the provision of general health services. We are also committed to the encouragement of improved insurance cover, provision for curative care, both for the NHIF and through private insurers. The operational autonomy of the NHIF is being increased and amendments to the Act will shortly be tabled to extend its coverage to the self-employed and to the *Jua Kali* workers. To encourage the wider utilisation of private insurance companies, particularly in the hospitalisation, I am now directing the Commissioner for Insurance to ensure that the health and medical organisations concerned operate under the provisions of the Insurance Act.

During the coming financial year, I propose to increase the funding for all agricultural activities, by a further seven per cent. Over the years, the Government has subsidized the provision of seeds and other inputs in line with the pursuit of fiscal efficiency. It is our intention to gradually phase out these subsidised elements and to organise research and extension work increasingly on a cost sharing basis. The first steps in this direction have been taken already and I expect to offset agricultural support costs in 1996/97 by savings from cost sharing arrangements. Hon. Members should be re-assured, however, that these measures will take fully into account the ability to pay, and they will not be implemented in Arid and Semi Arid Lands (ASAL) and other disadvantaged regions.

Mr. Speaker, Sir, we have been consistently prudent in containing the expansion of our debt to levels supportable within our means while meeting all our repayment obligations in time. At the end of the 1995/96 financial year, our total public sector debt stood at K£24.8 billion and of this, K£18.5 billion or 75 per cent, represented foreign debt. To put things in another perspective, the foreign debt amounted to nearly four times our entire export earnings in 1995, and around 23 per cent of these earnings, were committed in advance for prompt settlement of our external debt interest charges. Over the last three years, we have expanded the economy, while at the same time reducing our external debt burden from over 91 per cent of GDP in 1993 to 76 per cent now. Moreover, the measures now in force are expected to bring about further reductions in this ratio. The reduction in our domestic debt has the higher priority as we seek to release more of the nation's resources for private sector use. During 1995/96, we succeeded in reducing the domestic debt to GDP ratio by 1.5 percentage points with the resultant savings on interest and costs. Monetary considerations permitting, I intend to make further reductions to the domestic debt-to-GDP ratio next year.

Mr. Speaker, Sir, since their incorporation under the Kenya Revenue Authority, the Tax Departments, have not only enhanced collections, but are developing more cost efficient collection and refunding methods. The Personal Identification Number (PIN) system is now in operation and has led to the introduction of the income tax self assessment system, which will minimise the assessment difficulties faced by the taxpayer. The PIN system also facilitates the fast administration of tax sequence, particularly by the Value Added Tax (VAT) Department, where the backlog of the past is being reduced to moderate limits and where additional funding is being earmarked to permit further reductions this coming year.

The verification services of the Export Promotion Programmes Office (EPPO) have been contracted out to a trade survey company to enhance the collection of residual revenues, eliminate economic sabotage and accelerate the cancellation of security bonds taken out by exporters. This exercise is being pursued urgently on a crash programme basis. There are now some 350 companies regularly using the various EPPO duty/VAT remission programmes and they benefitted from our remission of taxes to the order of K£200 million last year.

Hon. Members will be aware of the steps taken in February, 1996 to impose increased fines on imports without proper pre-shipment inspection documents. These measures have had a dramatic impact on the congestion levels while increasing revenue collections and improving the detection of corruption. To further enhance the effectiveness of the Preshipment Inspection Programme (PSI) system, computerised procedures are now being implemented to improve the reconciliation between the PSI and Customs valuations and make it even harder to defraud the revenue.

Mr. Speaker, Sir, the tight fiscal policies which I intend to maintain will be complimented by an equally tight monetary policy focused as before on the control of inflation within single digits. In the higher growth economy which I now predict, the maintenance of these low inflation rates will be no mean feat, but in my view, it is an achievable one. To monitor monetary policy more effectively, the Central Bank of Kenya (CBK) will utilise various bench marks, particularly its own net domestic asset level which will be further reduced, reflecting the tighter controls on the use by Ministries of the CBK overdraft facility.

Mr. Speaker, Sir, the CBK is the principal agency charged with maintaining the soundness of our currency, price stability and the integrity of the financial system. To assure investors and the general public that our anti-inflationary policies will continue with unremitting vigour, I will be tabling amendments to the Central Bank Act, which will increase its statutory powers in these areas. I have expressed my concern many times about the failure of the commercial banks to bring down interest rates to acceptable levels and to narrow the large gap of interest rates between overdraft and savings. To encourage competition in this area, and provide saving opportunities for the general public, the CBK is encouraging the development of new financial instruments. It has relaxed the minimum purchase values of Treasury Bills and it will soon take steps to allow their trading on the Nairobi Stock Exchange (NSE). To further widen the range of short term instruments available during 1996/97, the Central Bank of Kenya will introduce re-purchase agreement facilities for Government securities. To further strengthen the financial soundness of the insurance industry, I am raising the bank guarantee required from insurers by the Commissioner of Insurance on initial registration to K£25,000 and the minimum balance kept by general insurers at the CBK to K£200,000. The value of the professional indemnity policy taken out by Brokers is also being increased to K£200,000 and their minimum bank guarantee to K£25,000. On the other hand, I am proposing to reduce the compulsory levy for the College of Insurers to 0.2 per cent of Gross Premium Income which can now be passed on to Policy holders. At the same time, I am arranging for the College to provide courses for the compulsory certification of insurance agents, which will be introduced during 1997. The Government is also considering proposals for the introduction of a compensation scheme for injuries resulting from motor accidents. The new arrangements will necessitate major amendments to the Insurance Act, which will be tabled as a matter of urgency. I am also tabling an amendment to Section 67(c) of the Insurance Act to give adequate powers to statutory managers to declare a moratorium on companies in financial difficulties and also to safeguard the interests of policy holders. In this regard, I have today authorised the Commissioner of

Insurance to appoint a Statutory Manager to take over immediately the Kenya National Assurance Company, which is wholly owned by the Government. This decision should now remove any uncertainty over the status of the company. Mr. Speaker, Sir, the pension sector is a major component of the financial system and to prevent exploitation, it is appropriate now to tighten up the minimum standards of our pension schemes. I will shortly table a Pensions Scheme Regulation Bill to specify structural and performance conditions for registered pension plans and also provide for the administration of this Act under an Authority. As part of the general reform of this sector, I will shortly be tabling amendments to the NSSF and Income Tax Acts to convert the NSSF into an autonomous tax-exempt agency. Until this is done, it will be obliged to invest its revenue mainly in Government securities.

The capital market sector continues to develop at a rapid pace. Plans for the introduction of a central depository for the clearing and settlement of securities are advanced and other developments which are now being reviewed include competition in brokerage activities and the use of brokers to trade in Treasury Bills. I am also giving consideration to the promotion of venture capital funds.

Mr. Speaker, Sir, the Structural Adjustment Programme has already improved the cost-efficiency and export competitiveness throughout the economy particularly in manufacturing industries. Nevertheless, industrial productivity remains low and the share of manufacturing in the economy has remained stagnant for some years at under 14 per cent. It is clear that much more needs to be done if the sector is to be relied on to underpin our targeted GDP growth rates on a sustainable basis. The programme for achieving this is now being elaborated in a Sessional Paper which will be presented in due course. The Government is sometimes accused of neglecting infra-structural improvement. In fact, nothing could be further from the truth and I would like to take a little time to demonstrate the seriousness of our commitment here.

During the 1996/97 financial year, over K£1.1 billion is to be spent on new infra-structural development, in education, health, water, development, agriculture, road building and other public works which constitute nearly 60 per cent of the entire development budget. Moreover, this sum does not include the first sums to be spent on the maintenance of the existing infra-structural facilities by the strategic parastatals and other agencies. In 1996/97, expenditure on routine road maintenance will be increased by some 20 per cent and major improvements will also be undertaken on the main Nairobi-Mombasa highway and other trunk roads while funding will be restored for all the new roads which were suspended last year. A strategic plan for the road sector has now been prepared which will fully finance routine and periodic maintenance by the turn of the century, improved funding and priority setting the immediate term and involve a greater use of the private sector in both road maintenance and construction.

I have also budgeted K£15 million to support the contracting out of locomotive maintenance by Kenya Railways. International expertise is being acquired for the improved management of the container terminal at Mombasa Port. Moi Airport has just been rehabilitated and modernised and upgrading of facilities is being undertaken at Jomo Kenyatta International airport while the completion of the new airport at Eldoret will open up Western Kenya to international trade and tourism. The new 75 Mega Watt diesel power station at Kipevu will soon be brought into operation. Plans are also at an advanced stage to contract an independent power producer to supply an additional 50 Mega Watts as a stop-gap measure while bids have been invited for the construction of the Olkaria and Kipevu power stations with a combined capacity of some 140 Mega Watts.

Major developments are also taking place in the petroleum sector. Among other developments, are the proposed facility for importing LPG, the Product Testing Laboratory and the extension of the Mombasa Eldoret pipeline to Malaba and on to Kampala in line with the original corporation. With the de-control of oil prices now well established, I am proposing amendments to the Petroleum Development Fund Act. First, since the National Oil Corporation of Kenya is now a marketing company, it is no longer appropriate for it to collect the petroleum development levy from its competitors. Effective from 1st July, 1996, this levy will be collected by the Kenya Revenue Authority. Secondly, the objective of the Petroleum Development Fund will be changed to reflect the new market realities. Funds will be restricted to support activities that do not compete, but rather, support the private sector.

Major allocations are being made for major improvement in Nairobi and the Coast among others. And our target in respect of water development is to make sure that at least 75 per cent of our people have easier access to organised clean water points by the end of the century.

Mr. Speaker, Sir, we are co-operating actively with our two East African partner countries in the exchange of information for policy co-ordination. We are making progress in the harmonization of tariff structures and rates for the preparation for the early elimination and standardization of country of origin criteria in the regulation of transit trade and the prevention export fraud. We are also moving together in the preparation of double taxation treaties. I am pleased to announce that an agreement has been reached on full regional convertibility and this will be implemented from 1st July, this year so that trade and other transactions among the three countries can be settled from that date in national currencies.

The Central Banks of the three countries will announce the modalities. We are committed to maximum co-operation with our COMESA partners. Kenya has fully implemented the programme of COMESA tariff references and further reductions in these duties will be introduced.

Mr. Speaker, Sir, because of the undoubted importance of the tourism sector in our economy, we have consistently devoted substantial sums to its advancement. The establishment of the Tourism Promotion Board, represents a major step forward and you can now look to a much more effective focus of our promotional efforts under its professional guidance.

Mr. Speaker, Sir, the Government also attaches great importance to the harmonization of rapid growth and industrialisation with environmental protection. Moreover, the viability of our tourism industry, which is our largest single earner of foreign exchange is completely dependent on the prevention of environmental degradation. As the details of the environmental programmes are set out elsewhere, I will limit myself today to confirming that I propose to set aside substantial funds for projects specifically related to environment. To make the taxpayers contributions to stretch as far as possible, I expect to recover a higher proportion of these funds than in the past from increased tourist charges and more effectively targeted cost-sharing measures.

Mr. Speaker, Sir, I expect the economy to perform even better in the current year as the implications of the present policy incorporates the work with the system. There are now signs of significant recovery in both domestic and foreign investment particularly in export oriented manufacturing industries.

Over the 1996 calender year, the GDP growth rate is now expected to reach 5.5 per cent while in the 1996/97 financial year, it is focused to be even higher at 6 per cent.

During the 1995/96 financial year, the total gross revenue collections increased by some 16 per cent to K£7.3 billion. This outturn reflects both the upturn in economic activity, the wider tax base and the increased collections.

Total recurrent expenditure in the 1995/96 financial year is now expected to come to K£6.1 billion and the development expenditure to K£1.7 billion. Accordingly, I now anticipate that the deficits for the financial year, 1995/96, on a commitment basis but excluding grants will amount to some K£414 million. This is substantially lower than anticipated in last year's Printed Estimates and it represents a significant reduction in the deficit to GDP ratio to 1.9 per cent from the 2.6 per cent prevailing in the previous year. Inclusive of grants, the deficit is expected to amount to K£68 million. The net domestic finance requirement will allow a reduction in domestic debt of K£284.

Total revenues in the 1996/97 financial year are targeted to increase by a further 4 per cent to K£7.6 billion. This represents some 28.1 per cent of GDP, a significant reduction from the total revenue ratio of 29.8 per cent in 1995/96.

Privatisation proceeds accruing during the 1996/97 financial year are expected to amount to some K£150 million, which will be used for debts redemption.

With the strengthening of donor support, I expect a substantial increase in grant income to K£430 million. The disbursement of programme loans should amount to a further K£173 million. By way of contrast, total external repayments in 1996/97 are budgeted at K£1.1 billion.

Mr. Speaker, Sir, total gross expenditure in 1996/97 financial year will be limited to K£7.9 billion or 29.5 per cent of GDP, proportionately less than in the previous year. Of this, recurrent and development expenditures will be limited to K£6 billion and K£1.9 billion respectively, representing increases under 2 per cent for the former and 10 per cent for the latter.

Mr. Speaker, Sir, recurrent expenditure estimates include domestic interests payments of K£900 million, and foreign interest payments of K£510 million. Wage and salary costs are expected to increase by some 7 per cent over last year's level to some K£2.5 billion, based on the target Civil Service Staffing of 212,400 by June, 1997, and taking into account normal drift and the reform of the pay structure to incorporate performance related elements. Allocation for pensions at K£185 million are estimated to be 42 per cent higher. Hon. Members will be happy to hear that I will shortly be tabling the Pensions (Increase) Amendment Bill, 1996, to effect these changes.

(b) Development Expenditure

The estimates for Development Expenditure GDP during 1996/97 are in line with our commitment in the Policy Framework Paper. Full funding will be provided for all core projects.

We are now aiming at an even smaller deficit on a commitment basis and excluding grants of K£389 million or 1.7 per cent of GDP. Including grants, the 1996/97 Budget will have a small surplus of K£42 million, even after settling some K£169 million of Pending Bills accumulated in the previous years. This should allow a further reduction on domestic financing by K£12 million.

(c) Residual Financing

Mr. Speaker, Sir, to achieve my total revenue and deficit target, I will have a residual gap of some K£128 million, which I will finance by additional measures next year. I will now describe how I propose this.

9. Taxation Proposals

Mr. Speaker, Sir, before I present my taxation proposals, I wish to make some observations about the performance of the revenue system. Prior to 1993/94, ordinary revenue collections were typically below 23 per cent of GDP. However, for three years now, including 1995/96, ordinary revenues have been around 28 per cent of GDP. This high burden has been necessary to bring the deficit under control.

Now that we have been successful in stabilising the economy, I am pleased to inform the hon. Members that I am able to ease the planned ordinary burden for 1996/97 to about 26 per cent of GDP. This should provide the Private Sector with more resources to invest and create jobs. This is consistent with my Budget theme.

Despite the successes and revenue raising, the modernisation process of the tax system will continue. To improve the efficiency and fairness, it is still necessary to continue the process of lowering and rationalising tax rates and expanding the base. Particular emphasis will continue to be put on strengthening the administration in order to bring those who have managed to evade taxes in the past into the net.

Mr. Speaker, Sir, the financial resources for the Kenya Revenue Authority (KRA) are being brought closer to their target level of 1.5 per cent of the estimated revenue collections. The organisational structure of the Authority is being put in place. New professional and technical staff are being hired. I am expecting, indeed, I am demanding on behalf of all Kenyan taxpayers, that the KRA raise the efficiency and effectiveness of tax collection, and also improve the service provided to taxpayers in order to make compliance to the tax laws simpler and cheaper. At the same time, while the KRA is responsible for administration of the tax law, the Ministry of Finance remains responsible for tax policy and, in fact, the overall revenue system.

In the context of the Civil Service Reform Programme, the strengthening and rationalising of the Ministry of Finance, is an urgent and important goal that would receive priority attention in the course of next year in order to support the Tax Policy and other economic management responsibilities of the Ministry.

Mr. Speaker, Sir, following convention, I will now ask the remainder of my speech be regarded as a Notice of Motion to be moved before the Committee of Ways and Means. I will first present proposals that affect Customs procedures and other technical matters, then I will turn to proposals with direct revenue consequences.

Customs Measures

First, the KRA is now working in close co-operation with the Kenya Ports Authority (KPA) to introduce a new cargo-controlled system at the Port of Mombasa to facilitate the movement of cargo, to increase cargo security and to prevent cargo from leaving the Port area without the payment of proper duties and taxes. As part of this system, shipping agents shall be required to supply all bills of lading in addition to ships' manifests to Customs and Ports Authority. Customs shall be applying the penalties already in the Law for failure to supply complete documentation head of cargo being off-loaded. Secondly, as an extension of this cargo control system and to encourage rapid clearance of imports, I am proposing to tighten the control of goods not entered for clearance with 21 days of discharge after arrival at the Port. Two public notices would be made of certain entered goods in place of the current single Gazette Notice. The first will be a notice in the Press warning importers to clear their goods within 21 days of this notification. Any goods still remaining unentered after this warning period will no longer be available to the importer, but will be gazetted for auction with the proceeds going to duties, taxes, sale expenses, Port charges and the general Customs revenues. Provisions are also being made for the contracting out by the KPA of the auctions of such unentered, abandoned and seized goods to professional private auctioneers to increase the revenue yield. In addition, customs warehouse rents at the Port will be raised to discourage unnecessary delays in entering and clearing goods.

Third, I propose to introduce new legal provisions explicitly covering the pre-shipment inspection programme. In so doing, I am also introducing some changes to the PSI Programme effective on 1st July, 1996, the two per cent fee charged for processing the Import Declaration Form will no longer be collected by commercial banks. Instead the KRA will be responsible for fee collection when the goods are entered and the fee will be charged on the full customs value at that time. In addition, the import declaration form will be sent directly by the importer to the pre-shipment inspection company to initiate inspection. IDFs will be required and the fee payable on all types of imports requiring pre-shipment inspection. The PSI companies, however, will only inspect shipments above a minimum value. This minimum inspection limit will be raised from an f.o.b. value of $500 to $1,000. These measures will speed up the processing of import documents and improve the collection of the IDF fee and making a separate fresh list that would explain these changes in more detailed. Further more, the Treasury, KRA and the PSI companies will work jointly over the next year to enhance the reconciliation of all PSI documents with Customs entry documents to ensure full compliance of the programme.

Fourth, Mr. Speaker, Sir, the bonded warehouse provisions for imports have been abused and have contributed to speculation on imports. While the KRA will continue to improve its controls on warehousing, I am proposing to expand the restrictions on the types of goods allowed into bonded warehouses. Goods that are not identifiable by marks such as serial or model numbers and cannot be readily accounted for, would not be entered into bonded warehouses. Items that are inflammable, corrosive, explosive or perishable are also excluded. In addition to this general principles, I am also amending the regulations to explicitly exclude goods such as vehicles and dry cell batteries, tyres, used motor vehicles, office supplies (including stationery) and food products (including maize, wheat, powdered milk, rice and sugar).

Fifth, the efforts to tighten controls on duty exemption that has been on-going since 1992 will continue. This year the focus is in official aid-funded projects to ensure that duty free equipment is being used as intended on the aid-funded projects. The bonding of equipments will now be followed up by investigation and verification on site before the bond is released. Where motor vehicles or earth-moving equipments are purchased, duty-free with aid-funds, this would no longer be permitted to be registered in the contractor's name. They can only be registered in the name of a project funded by an aid agency or the Government or a non-profit organisation specified in a Gazette order. In addition, auto-motor fuel and lubricants will only be exempted where a specific provision is made in the Legal Notice covering the project.

Mr. Speaker, Sir, early this year I made an announcement that donated motor vehicles will no longer receive duty exemption unless after rigorous examination, it could be determined that these vehicles are truly intended to serve strictly charitable purposes. This policy will be followed even more vigorous in future and to ensure that vehicles used are for intended purpose, the KRA will follow up with investigations. Sixth, to improve controls on imported vehicles, the Certificate of Clearance issued by the Customs Department is being re-designed to strengthen controls on the registration of motor vehicles that have cleared customs.

Seventh, to prevent leakage of goods imported for the Navy, Army and Air Force Institutions (NAAFI) and the Armed Forces Canteen Organisation (AFCO), all such goods shall be required to bear the mark of NAAFI or AFCO to identify the importing organisation. Hence forth, only AFCO shall be allowed to clear goods imported for AFCO use. Eight, to improve controls on transit traffic, licensed customs agents clearing goods in transit will be required to have an additional licence. Ninth, in international trade, certain containers are used repetitively and hence are allowed to move duty free. I propose to allow specially designed containers supplied by foreign buyers such as those used for flower export to enter duty free. I am also proposing to allow containers designed for transporting semen for artificial insemination to be imported free of duty subject to the approval of the Director of Veterinary Services.

Tenth, to widen the range of agencies in addition to the Family Planning Association that are approved to import contraceptives duty free, I propose to also include the Ministry of Health and other agencies approved by the Treasury. Eleventh, I am proposing to allow spouses of returning diplomats to import a motor vehicle duty free under the same conditions as the diplomatic officer.

Finally, to provide greater competition in cargo handling services, I am now proposing to allow transit sheds to be allocated outside of the traditional air-site and port areas provided that the Commissioner is satisfied that sufficient security arrangements are in place to protect revenues.I now turn to my customs proposals that have direct revenue consequences. First the rationalisation of import duties will be continued to improve the effectiveness of customs collections and to make domestic businesses more competitive. I am proposing to lower the top rate of 40 per cent to 35 per cent. In addition, the 10 per cent band will be lowered and merged with the 5 per cent band. Items in the 10 per cent band are mainly capital goods items and primary raw materials. A few items in the 10 per cent band that are not capital goods or primary raw materials will be shifted to the 15 per cent band. This cost-saving measures should give a significant boost to local industry.

Second, Mr. Speaker, in line with the broad rationalisation changes just announced, I am proposing that the import tariffs on certain capital equipment items still remaining in the 25 per cent band be reduced to 15 per cent. These include items such as hand tools and wheelbarrows widely used in the rural and informal sectors. The tariff, on a number of primary raw materials used mainly in the plastics and the spinning and weaving sectors will be reduced from 15 per cent to 5 per cent. In addition, where goods in the 25 per cent band are generally exported or do not require import protection, I propose to lower their rates to 15 per cent.

Third, I propose to increase the protection offered to some specific sectors to provide transitional assistance to improve their efficiency to face international competition in future. Import duties on some lines of paper and paper board will be raised while the import duties will be lowered on the lead mix used in making motor vehicle batteries and on plastic bottles for the cosmetic sector.

Fourth, Mr. Speaker, Kenya is a sports loving nation. I propose to lower the tariffs on sporting equipment to 15 per cent where the rates are currently higher in tariff bands.

Fifth, to improve customs compliance on used clothing imports, I am proposing to drop the alternative specific duty rates. Only the *ad valorem* customs and VAT rates will apply.

Sixth, to allow local manufacturers to compete with imports, I am proposing to allow local makers of shading nettings and import plastic sheeting for agricultural or horticultural use to apply under EPPO for duty-free importation of their raw materials. To further facilitate EPPO operations I am reducing the minimum amount of raw material imports per application under the Essential Goods Production provisions from Kshs 1 million to Kshs 200,000.

Seven, I am proposing to set the tariff rates on major agricultural commodities at the following *ad valorem* rates. The import duty rates on maize and wheat will be 15 per cent; on powdered milk, 25 per cent; and on sugar and rice, be 35 per cent. In addition, alternative specific duties will be retained but at lower effective rates to protect against under-valuation. As already announced, these commodities will no longer be allowed into bonded warehouses in order to limit speculative hoarding.

Eighth, with the lower import rates now applicable and significant lower prices of jet fuel prevailing since the de-control of oil product prices, Mr. Speaker, I am proposing that the value of custom duty for air freight again include one half of the freight charge as was the case prior to 1991.

Finally, Mr. Speaker, kerosene has been free of duty for the last few years. While the duty free status of kerosene has been beneficial to the poor, it has also resulted into a diversion of kerosene into industrial uses, into mixing with diesel or petrol as an automotive fuel and into smuggling into neighbouring countries. Honourable Members will be interested to note that Tanzania charges a total of about 16 per cent in duty and taxes while Uganda charges a duty of 115 per cent on kerosene. The expansion of alternative uses of kerosene have resulted in an enormous increase in kerosene sales at the expense of an alternative dutiable petroleum products with a huge loss of revenue and increased pollution of the atmosphere. I am therefore proposing to charge an import duty of Kshs 3 per litre which is an effective duty rate of 18 per cent on kerosene.

Mr. Speaker, the import duty rate changes that I have just announced will become effective from midnight tonight. These custom measures on a net basis will reduce revenue to the Exchequer by K£ 1.8 million in 1995/1996.

Mr. Speaker, since the introduction of the Value Added Tax in 1990, the VAT has undergone a systematic expansion of its base and rationalisation of its laid structure. I am proposing to take a few further steps in the development of the VAT. First, to continue the rationalisation of the VAT and move towards a more uniform rate structure, I propose to lower the top rate from 25 per cent to the standard rate of 15 per cent, and at the same time to raise the lower rate from 6 per cent to 8 per cent. This will remarkably simplify VAT administration.

Second, I am proposing only minor expansions to the VAT base. Taxable services will now include actuarial services and material testing services, but excluding testing for medical, dental and agricultural purposes. To harmonise the taxation at the retail level, certain additional types of juices will become designated goods so that they are also taxed at the retail level like other beverages. Third, I am proposing to raise the VAT rates on hard fats from the lower rates to the centre rate of 15 per cent. At the same time the VAT rates on vegetable oils will remain at the lower rate in order to encourage the consumption and production of vegetable oils.

Fourth, I propose to charge the lower rate of VAT on oil cake which will allow input taxes arising in producing oil cake to be deducted which should help lower the cost of animal feeds made from oil cake.

Fifth, to ease VAT administration problems, I am proposing to exempt from VAT a number of basic commodities including wheat, wheat flour, bread, maize, maize flour, rice and milk.

Sixth, to help combat malaria, I propose to zero rate mosquito chips and coils.

Seventh, Mr. Speaker, from time to time, groups of professionals in the travel and tour business visit

Kenya to learn about the tourist attractions of our country so that they can promote tourism to Kenya. To encourage this valuable tourism promotion, I am proposing to zero rate the hotel and restaurant services provided to such visiting groups where their tours have been organised with local associations and approved by the Director of Tourism.

Eighth, to speed up tax collections, I propose to bring forward the monthly VAT payments date from the 27th to the 20th day of the month following tax collection by a registered business. Similarly, excise duties will be payable on the 20th instead of the 21st day of the month following collection.

Ninth, when a business that is registered for VAT is sold but continues its operations, the VAT Act allows its stock to be transferred without incurring VAT. I am proposing to extend this provision to the transfer of other assets of the business to simplify the sale of ongoing registered businesses.

Finally, Mr. Speaker, a major concern for may businesses, particularly exporters and makers of zero rated goods such as pharmaceutical, has been the backlog of VAT refunds that has built up over the past year. This backlog arose following a temporary suspension of VAT refund payments to deal with some fraudulent dealings uncovered in the refund system. The Kenya Revenue Authority is now working to strengthen the VAT verification and audit capacity for both refund and regular VAT traders. I have made provision of K£ 600 million in the VAT revenue estimates to reduce the backlog in VAT refund payments during fiscal 1996/97.

I, therefore, want to assure the export and other businesses affected that they should invest and conduct business in the confidence that these refund payments will be met over the coming year. At the same time, I would warn any intended evader of VAT that the chances of being caught and penalised are rising by the day as the Kenya Revenue Authority strengthens its audit and enforcement capacity.

Mr. Speaker, Sir, the changes in the rates of VAT that I have just announced will take effect from mid-night tonight. The measures that I have introduced into VAT and excise duties will raise to an additional K£51.2 million in revenues. Fairness and efficiency are two hallmarks of a good income tax. An important way of achieving this is minimizing the number of low income earners directly involved in the income tax. My first new measure, therefore, is to increase and simplify tax reliefs offered to individuals. I propose to replace the family, single, and insurance reliefs with a one personal relief of Kshs7,200. That will be available to all individual tax payers. Men and women will now receive equal reliefs for equal income. Income tax is finally becoming gender sensitive! Individuals with monthly incomes up to Kshs6,000 will be free of income tax. This will remove about 140,000 low income workers from tax paying status next year. It will also significantly simplify the Pay-As-You-Earn system, as it will no longer be necessary for the employers to certify the marital status of their workers.

Secondly, to protect against inflation-induced bracket creep, I propose to expand the tax brackets by 5 per cent from K£3,900 to K£4,104. In addition, a new 30 per cent bracket will be inserted to reduce the number of middle-income earners falling into the top marginal tax rate bracket.

Thirdly, I am proposing to lower the final withholding tax rate on qualifying dividends paid to residents from 7.5 per cent to 5 per cent, in order to reduce the double taxation on income derived from equity investments.

Fourthly, interest income has not been effectively taxed, especially that earned by individuals. To rectify this, and simplify the administration, I am proposing to raise withholding tax on interest income from 10 per cent to 15 per cent. At the same time, however, interest earned by individuals will become qualifying interest such that the 15 per cent tax will be a final tax where interest is earned from a financial institution. The tax rates on housing bonds will remain at 10 per cent to encourage investments in those instruments.

In addition, it has come to my attention that large sums of money are being held in bearer certificates of deposit by high income earners. To ensure that they pay their fair share of tax, the withholding tax on this bearer instruments will be set at 20 per cent. Again, this will be a final tax where individuals earn interest on those instruments from financial institutions.

Fifth, to encourage the development of equipment leasing market, I propose to lower the withholding tax on equipment supplied by non-residents from 30 per cent to 15 per cent. The withholding rate on immovable property such as land and buildings, however, will remain at 30 per cent.

Sixth, to throw the tax net wider, I am proposing to introduce a withholding tax of 5 per cent on royalty payments to residents. This withholding tax can be offset against the tax assessed on the annual return of the recipient of the royalty.

Seventh, with the increasing value of employer-provided motor vehicles now required, to be recognised as employee benefits, I am proposing to raise the limits on the capital expenditures on passenger cars qualifying for wear-and-tear allowances from Kshs100,000 to Kshs500,000 in 1997, and then further to Kshs1 million in 1998.

Eighth, to speed up tax collections and to harmonise with the payment dates for VAT and excise duty announced earlier, I propose to move forward the payment date for quarterly instalment payments from the end of the month to the 20th day for instalment payments in the 6th, 9th and the 12th months of the current year. The payments in the 4th month will remain at the end of the month to coincide with the final self-assessment tax payment for the year. In addition, to simplify the payment of instalment tax, which is now well institutionalised, I am proposing that the instalment tax returns will no longer be required. Pay-in slips will be used and instalment tax payment will be reconciled at the time of submission of end-of-year self-assessment-return.

Ninth, over the recent years, new specific fines and penalties have been introduced to cover the new procedures such as self-assessment and instalment payments. But a general fine for offenses under the Income-Tax Act has remained unchanged. I am, therefore, proposing to increase the maximum fine from Kshs4,000, a level unchanged since 1974, to Kshs100,000.

Finally, Mr. Speaker, I am proposing a number of measures affecting the pension sector. As promised last year, I am proposing to raise the deductible contribution limits for registered pension and provident funds and registered individual retirement funds from Kshs60,000 per year to Kshs 90,000 per year. In addition, to remove the double taxation of unregistered pensions, I am proposing amendments to make unregistered pension payments free of tax where they are paid by non-exempt companies and where no deductions were taken for the contribution and the income earned by the fund has been subject to tax. As already announced, the National Social Security Fund (NSSF) will undergo reform. In the light of this, I am proposing to change the tax treatment of NSSF effective from 1st January, 1997. First, both employer an employee contributions will become tax deductible under the limits for defined contribution registered pension funds. Second, lump-sum benefits will qualify for an exemption on the first Kshs360,000 of the payments to bring them in line with other registered pension funds and any pensions that NSSF may pay in future would also qualify under the annual Kshs150,000 limit for registered pensions.

Third, the income earned by NSSF will be tax free as long as NSSF complies with rules relating to the publication of its audited accounts and full allocation of the income to the accounts of its members.

Mr. Speaker, the measures I have just announced will raise and addition of K£15.1 million in revenues.

Mr. Speaker, Sir, road maintenance is a clear priority of the Government. To bring the state of the road system back to a satisfactory level demanded by Kenyans requires increasing amounts to be allocated to road maintenance. Expenditures have risen each year: In 1994/95, K£102 million was spent, this year, K£181 million is expected to be spent, and next year, K£215 million is budgeted. These higher expenditures, unfortunately, requires corresponding increases in the Road Maintenance Levy. To raise 74 per cent of the total revenues required for road maintenance expenditures, or K£159 million through the Road Maintenance Levy, requires that I raise the levy by Kshs0.7 per litre. Therefore, the levy on petrol will be Kshs2.7 per litre and on automotive diesel, Kshs2.2 per litre.

Mr. Speaker, Sir, the various fees for the registration and licensing of motor vehicles, for drivers' licences, and those relating to sale and transfer of motor vehicles have remained unchanged for a number of years. I propose, therefore, to increase the fees under the Traffic Act and Transport Licensing Act, and to bring amendments to raise taxes under the Second-Hand Motor Vehicles Purchase Tax Act.

Finally, to ensure that our nation gets better returns from the employment of expatriates, I am proposing to increase the fees charged for entry permits under the Immigration Act as well as fees charged for issuing identity cards under the Aliens Registration Act.

Mr. Speaker, Sir, these miscellaneous measures will raise an additional K£63.5 million in revenues.

Mr. Speaker, in reviewing the measures I have outlined, hon. Members would be aware that these reflect a consistent pattern of policy dating back to mid-80s. I am gratified with the positive reaction of the donors to my presentation of our policies to the Consultative Group in March this year. I now renew my call to the donors to further support our development efforts. While we recognise that the last few years have been difficult ones for our investors these are now behind us. Accordingly, I call on all Kenyan enterprises to shake off the past and exploit the new opportunities to the full, and I warmly extend this call to foreign investors to join with us in wealth creation.

In this context, I call on the financial institutions of all types to underpin investments and savings by developing innovative and customised financial packages especially for exporters and the expanding jual kali. I also call on our East African partners to join wholeheartedly with us in the development of our region through the harmonisation of policies on trade, investment and movement of peoples.

The budget I am presenting to this House is a sober and realistic basis for maintaining economic stability and encouraging the investment which all of us desire. I am confident that it will command all party support. The coming financial year should be one when the economic seedlings we have so carefully nurtured will grow into fruit bearing trees- a whole forest of them! Thus, I call on all hon. Members to make their personal contributions to this husbandry so that the nation can reap an abundant harvest.

Mr. Speaker, Sir, I beg to move.

(Question proposed)

DEPARTURE OF HIS EXCELLENCY THE PRESIDENT

Mr. Speaker: It is now the pleasure of His Excellency the President to take his leave.

ADJOURNMENT

Mr. Speaker: Hon. Members, it is now time to adjourn the House. The House is adjourned until tomorrow, Wednesday, 19th June, 1996, at 9.00 a.m.

The House rose at 4.10 p.m.