

PRESS RELEASE*Immediate release**7th January 2009***Revenue Performance Report****1. Introduction**

This is the revenue performance report for the Kenya Revenue Authority (KRA) covering the second quarter of 2008/09 Fiscal Year, October to December 2008 and cumulative performance during the first half of the fiscal year 2008/09.

In the Financial Year 2008/09, the Authority is expected to collect an ambitious target of **Kshs. 492.9 billion** representing a growth of **13.6%** over the Kshs. 433.9 billion collected in 2007/08 Fiscal Year.

2. Operating Economic Environment

Economic performance leading up to the 2nd quarter has been poor contributing to the underperformance in the 1st quarter of 2008/09 and the beginning of 2nd quarter.

Economic growth: The *Kenya National Bureau of Statistics* (KNBS) has released its 1st, 2nd and 3rd quarter 2008 (calendar year) GDP growth estimates.

Following the decline in 1st quarter GDP occasioned by the post election violence, with GDP declining by 1%, second quarter GDP rebounded to grow at 3.2%. However, this growth acceleration was not sustained with 3rd quarter GDP growing by an estimated 2.1%. Kenya is therefore unlikely to achieve the growth rates forecast for 2008 in the Government's Budget Strategy Paper,

Inflation: The country continued to experience high levels of inflation in the period leading to the second quarter of the financial year. Inflation accelerated in 2008/09 with the 18.2% average inflation rate achieved over 2007/08 rising to 27.6% in September 2008,

Exchange rates: In January 2008 the shilling was exchanging at a rate of Kshs. 70.6 to the US dollar. There was then a period of appreciation leading to a rate of Kshs. 63.8 by June 2008. At the start of the 2nd quarter 2008/09, (i.e., at the end of September 2008) the shilling had depreciated and was trading at Kshs. 71.4 to the dollar. Hence, there has been considerable volatility in the exchange rate,

Interest rates: In June 2008 the Treasury Bill interest rate averaged 7.7% It remained close to this level for most of the 1st quarter, being the only macro economic variable that remained fairly stable.

The economic environment for the first 3 quarters of the calendar year and the first quarter of the fiscal year was thus not conducive to the achievement of extremely ambitious revenue targets and to a large extent determined the poor outcome in the 1st quarter 2008/09.

During the 2nd quarter of the financial year 2008/09, the key elements of the operating environment were as follows:

Inflation: the overall inflation rate decelerated from 28.4 percent in October to 27.7 percent in December 2008. The decrease was due to decline in prices of fuel and power. However, the overall rate of inflation remained high,

Interest rate: The 91-day Treasury bill rate rose from 7.75 percent in October to 8.39 percent in November 2008 and further to 8.59 percent by the end of December 2008, implying a rising trend,

Exchange rate: The Kenyan Shilling exchanged at Kshs. 76.66 to the US dollar in October, 78.18 in November and 77.71 in December 2008. Thus, by December it had depreciated by 8% compared to its September level,

NSE index: the index declined from 3,387 points in October 2008 to 3,341 points in November and then closed at 3,521 points at the end of December 2008. Hence, there was a slight improvement over the quarter.

3. Revenue performance in the 2nd quarter (October-December 2008)

Despite the less than promising economic environment leading into the second quarter and the absence of significant improvement in macro economic variables during the quarter, KRA has been able to achieve significant revenue growth and thus meet the revenue target for the quarter.

Table 1 below summarizes the revenue performance during the 2nd quarter.

Table 1: Second Quarter (October-December 2008) Revenue Performance (Kshs million)

| Department | Percentage of Forecast Revenues | Target 2 nd quarter | Actual 2 nd quarter | Variance | Performance Rate | Actual 2 nd quarter 2007/08 | Growth over 2 nd quarter 2007/08 (%) |
|------------------|---------------------------------|--------------------------------|--------------------------------|--------------|------------------|--|---|
| Domestic Taxes | 62.9% | 75,813 | 72,093 | (3,719) | 95.1 | 63,562 | 13.4 |
| Customs Services | 36.3% | 43,678 | 49,093 | 5,415 | 112.4 | 40,510 | 21.2 |
| Road Transport | 0.8% | 945 | 616 | (329) | 65.2 | 626 | (1.6) |
| Total | 100.0 | 120,436 | 121,803 | 1,367 | 101.1 | 104,698 | 16.3 |

During the 2nd quarter of 2008/09 (i.e. October to Dec 2008), KRA collected **Kshs 121.8 billion** against a target of **Kshs 120.4 billion**. A surplus of **Kshs 1.4 billion** was realized, driven primarily by the strong performance in December 2008. In the month of December 2008, the Authority collected **Kshs 48.0 billion** against a set target of **Kshs 44.1 billion** thereby surpassing the target by **Kshs 3.9 billion**.

In the 2nd quarter, Customs Services department surpassed the set revenue target by **Kshs 5.4 billion** while Domestic Taxes and Road Transport departments fell short of their respective targets during the quarter by **Kshs 3.8 billion** and **Kshs 0.3 billion** respectively.

KRA recorded revenue growth of 16.3% in the 2nd quarter of 2008/09 compared to the same period in 2007/08 with Customs Services Department recording revenue growth of 21.2% while Domestic Taxes Department

recorded revenue growth of 13.4%. Road Transport Department recorded a revenue decline of 1.6% during the second quarter.

3.1 Administrative Measures

To a large extent, the turnaround in revenue performance during the 2nd quarter was the result of administrative measures put in place by the Authority. The main measures were the following:

3.1.1 Domestic Taxes Department

Taxpayer Audits: Audits are being assessed on the basis of case coverage as opposed to revenue yield. In addition, audit selection is based on a risk profiling framework. During the quarter, Kshs 819.7 million was collected from audits.

Taxpayer Recruitment: During the quarter, 35,125 new taxpayers were recruited leading to revenue collection of Kshs. 362 million.

Debt Management: During the quarter under review, a total of Kshs 2,020 million of debt was collected.

3.1.2 Customs Services Department

The implementation of a 24 hours a day operation at Mombasa and border points:

The implementation of 24 hours, 7 days a week service delivery was implemented at the port of Mombasa and at land border entry points at Lunga Lunga, Taveta, Namanga, Isebenia, Busia and Malaba. The Port of Mombasa previously closed for 12 hours at night and throughout the weekend. The new move, which came into effect on 18th August 2008, has improved the clearance of cargo at the port of Mombasa from 48

to at least 24 hours. Congestion at the port has been a major cause of concern in Kenya as well as neighbouring countries including Rwanda, Uganda and Tanzania. Since implementation of the 24 hour operation, 72,120 containers have so far been cleared.

Port Decongestion: KRA has continued to hold auctions to dispose of over due containers. Additionally, the destruction of sub standard motor vehicles will continue till all overstayed vehicles are disposed of.

Post clearance audits and other recoveries: during the 2nd quarter the department collected a total of Kshs. 760 million from post clearance audits, auctions and related initiatives.

3.1.3 Road Transport

Mobile licensing and TLB meetings: The department conducted mobile licensing in several regions during the quarter. In addition TLB meetings were also conducted.

Security printed logbooks: The department continued with replacement of old log books with new security printed logbooks.

4. Challenges faced during the second quarter

In spite of the exemplary performance during the second quarter, KRA faced a number of challenges. These include the following:

PAYE: During the 2008/09 budget estimates, PAYE from the salaries and allowances for Members of Parliament and Constitutional Office holders was factored in. However, KRA has not been able to collect the adjusted PAYE from these categories of taxpayers given that the proposal to tax their salaries and allowances was rejected by parliament,

VAT: The recent reduction in the VAT rate on power from 16% to 12% will create substantial refunds as the inputs are taxed at 16%. Hence some of the companies in the energy sector may benefit and find themselves in a refund position.

Corporation Tax: Instalment tax in the months of September and October 2008 was affected as companies made lower instalment payments by taking into account the effect of reduced higher profitability projections due to post election violence. In addition, as companies took advantage of the wide range of available investment incentives including Import Duty Set-offs and investment deduction, the instalment tax collections were reduced. This will be a continuing problem,

Excise duty: The measures in the budget proposals for 2008/09 that were introduced for the spirits industry are yet to be implemented by the taxpayers in the industry since some taxpayers have shifted to manufacturing non-malt lager which attracts a lower tax rate of Kshs. 36 per litre from Kshs. 50 per litre. This has subsequently been normalised at the Committee stage.

5. Cumulative Revenue Performance (July-December 2008)

5.1 Revenue performance in the first half of 2008/09 (July-December 2008)

Table 2 below summarizes the revenue performance during the first half of 2008/09 (i.e. July-December 2008).

Revenue collection in the period July-December 2008 totalled **Kshs. 230.7 billion** against a target of **Kshs. 239.5 billion**. This represents a performance rate of **96.3 percent**.

Compared to July-December 2007 when **Kshs 204.5 billion** was collected, revenue grew by **Kshs. 35.0 billion** or **12.8 percent**. Customs Services Department recorded the highest revenue growth of 13.9% followed by Domestic Taxes Department at 12.2%. Road Transport recorded a revenue decline of 1.5%.

Table 2: Cumulative Revenue Performance in the period July-Dec 2008 (Kshs million)

| Department | Percentage of Forecast Revenues | Target July - Dec 2008 | Actual July - Dec 2008 | Variance | Performance Rate (%) | Actual Jul-Dec 2007 | Growth over July-Dec 2007 (%) |
|------------------|---------------------------------|------------------------|------------------------|----------------|----------------------|---------------------|-------------------------------|
| Domestic Taxes | 38.0% | 146,795 | 138,080 | (8,715) | 94.1 | 123,048 | 12.2 |
| Customs Services | 61.3% | 90,937 | 91,350 | 413 | 100.5 | 80,214 | 13.9 |
| Road Transport | 0.7% | 1,806 | 1,221 | (585) | 67.6 | 1,239 | (1.5) |
| Total | 100.0% | 239,538 | 230,651 | (8,887) | 96.3 | 204,501 | 12.8 |

6. Implementation of Reforms

The Authority will continue to implement the initiatives under the modernization process through the Revenue Administration Reform and Modernization Programme (RARMP) and exploit the gains of the reforms implemented so far. Some of the reforms implemented/ongoing during the first half of 2008/09 are as follows:

Customs Services Department

(i) Implementation of the Authorized Economic Operator (AEO) concept

The process of expanding the AEO scheme commenced in August 2008 and was geared at expediting service for the compliant importers and thus rewarding compliant behaviour. Such clients are given preferential treatment in dealing with transaction where they have proven track record of compliance with customs operations.

(ii) Implementation of the Electronic Cargo Tracking System.

Piloting commenced on 18th August with 28 trucks destined to Rwanda and Uganda. Emerging challenges from the pilot exercise are being addressed. However, by and large, the project is a success and would improve revenue collection in the future.

(iii) Implementation of the Cargo Management Information System (CAMIS)

KRA introduced the web-based Cargo Management System (CAMIS) on 24th June 2008. CAMIS is a centralized system for monitoring and accounting for un-entered cargo, from the time Customs Officers board the vessels to confirm the cargo quantities, to the places of cargo discharge where declarations are made. The system is currently operational in Mombasa only and easily identifies goods to be moved to the Customs Warehouse after the 21 day declaration period has expired and is useful for calculating Customs Warehouse Rent and supports transparency in the auction process.

Domestic Taxes Department

Integrated Tax Management System (ITMS)

In December 2008, the Authority implemented (on pilot basis) the e-tax registration and e-tax filing components of the ITMS. These are the first modules under the Integrated Tax Management System. Once fully implemented, the system will revolutionize the domestic taxes administration and enhance revenue collection.

7. Conclusion

Despite the cumulative underperformance in the first half of 2008/09, KRA has achieved revenue growth of 12.8% compared to similar period in 2007/08. The stronger performance recorded in the second quarter and the economic fundamentals behind it –including a lower price for oil and a weaker currency– are likely to prevail. In addition, the operationalization of additional reform projects such as the Integrated Tax Management System (ITMS) will further enhance the capacity of the Authority to collect revenue. We are therefore confident that we will be able to make good the revenue shortfall in subsequent quarters.

Kenya Revenue Authority remains appreciative of the support it has always received from tax payers and in particular the support of the political leadership at the highest level that has enabled the Authority to stay the course even when this meant implementing unpopular decisions. This support will need to continue if 2008/09 revenue targets are to be met. Only by meeting these targets will the Government have the resources to achieve its objectives. It

is therefore imperative that for the rest of the year the tax paying public co operates with the Authority to ensure the targets are met.

M. G. WAWERU, EBS
COMMISSIONER GENERAL