REPUBLIC OF KENYA

Budget Speech

for the

Fiscal Year 1979/80
(1st July—30th June)

by

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Vice-President and Minister for Finance

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REPUBLIC OF KENYA

Speech delivered to the National Assembly on 7th June, 1979, by the Hon. Mwai Kibaki, Vice-President and Minister For Finance, Republic of Kenya, when presenting the Budget for the Fiscal Year 1979/80 (1st July to 30th June).

Mr. Speaker, Sir,

I beg to move that Mr. Speaker do now leave the Chair.

STATE OF THE ECONOMY

I wish to draw the attention of Hon. Members to the Statements made by H.E. the President at the time of launching the Fourth Development Plan and in the Speech at the State Opening of Parliament. His Excellency warned the nation that the economy faced many problems and that the coming months were going to be very difficult. These difficulties are now already here with us and we have to face them.

I hope that Hon. Members have read this year's Economic Survey which contains a full and up-to-date analysis of the current economic situation. I also hope that Hon. Members have studied in detail the new Development Plan for 1979-1983 as well as the Printed Estimates of Revenue and Expenditure for 1979/1980 which are before us today.

In my Budget Speech last year, I reported on the very encouraging performance of the economy arising from the boom in commodity prices of 1977/78. I was then able to state that our main problem was that of internally generated inflation resulting from excessive liquidity in the system. I warned of the dangers of relaxing the grip on money supply since this would only add to the flames of inflation.

For many reasons, the performance of the economy in 1978 was not as good as had been anticipated. The severe drop in commodity prices in the latter part of the year had a most dramatic effect on our terms of trade. The impact of certain payments related to national security became more pronounced. The relaxation on import contracts early in 1978 also resulted in many foreign commitments being entered into and the result of this was experienced in the following months.

At the same time, the Government's own foreign expenditures were raised considerably by increased investments in infrastructure and manufacturing, particularly in the Corporations inherited from the East African Community and in the sugar industry. Thus, as I had already forecast, the balance of payments became, once again, the major constraint to economic growth.

Looking at individual economic sectors, GDP generated in *agriculture, forestry and fishing* has been substantially reduced in 1978 when measured at current prices. At constant prices a small fall seems likely. The rains in 1978 were too heavy for a good coffee harvest to be reaped in 1978/79 but most other crops appear to have done fairly well and the livestock industry has benefitted from the good pastures. The rise in prices of domestically consumed crops and livestock products was more than outweighed by the slump in prices of export crops, resulting in an overall decline of 1.8 per cent in the index of items sold by the agricultural sector in 1978. The index of prices of inputs purchased by the sector on the other hand rose by 7.5 per cent in 1978. Thus, this combined effect of a rise in the prices paid and a fall in the prices received brought about an 8.5 per cent fall in the sector's terms of trade in 1978. *Manufacturing* industry has recorded another substantial advance in 1978 although not at the level of 1977 because of some adverse influences including the lack of substantial growth in exports. The effects of import controls on the supplies of raw materials to industry were not felt materially in 1978. *Wholesale and retail trade* appears to have had a good year in 1978 and sales on imports and local production were at high levels. The tourist industry earned the country record foreign earnings even though there was only a small increase in tourist arrivals from overseas countries.

The *transport* sector showed some improvement on 1977 with the better functioning of the domestic corporations established to take over from the defunct E.A. Corporations. However, there is still room for better performance and greater profitability in this sector. The *construction* industry was working nearer its capacity in 1978, but the improvement over 1977 was not as great as might have been indicated by the figures on building plans passed by local authorities in 1977 and 1978.

Services, including the Government's own employment, continued to grow reflecting an increase in the numbers in employment. Elsewhere private sector services benefitted from the high level of 1977 incomes which were being spent in 1978.

Thus, apart from the need to contain imports and domestic credit expansion, 1978 was in general a reasonably successful year though the overall GDP growth rate, at about 5.7 per cent, was below what had been forecast and below the annual average expected in the new Plan period.

In the 1978/79 Financial Year, Government revenues were below expectations partly because of the decline in incomes as well as because of the import controls imposed in 1978. On the other hand, recurrent expenditure has risen more rapidly than anticipated. This has reduced the recurrent surplus considerably, making it necessary to fill the gap in the resources required for the development budget by increasing the total of Treasury Bills on issue. This form of deficit financing may have raised inflationary pressures in the economy but its impact has been limited by the substantial reduction in the country's net foreign assets.

The major feature in the monetary scene in 1978 was the large reduction in net foreign assets by K£77.6 million. The impact of this reduction on the money supply was more than by the rise in domestic credit of K£159.3 million so that the total of money and quasi-money rose by K£85.2 million or by 13.7 per cent. Since October, 1978, there has been little change in the monetary aggregates and inflationary pressures had temporarily abated from October, 1978 to February, 1979.

Preliminary data on employment and earnings show that the numbers in wage employment probably rose by only about 1 per cent in 1978, while real wages, after adjusting for consumer price increases averaging 12.5 per cent, fell by about 1.4 per cent. The squeeze on real earnings of the wage employed was affected by the rise in rental payments as well as by increases in prices of a whole range of products including foodstuffs.

A particularly important subject in the economic scene in Kenya is the net cost of petroleum imports. Since 1973 the price of crude petroleum has soared and while Kenya benefits from the external sales of petroleum products from the Mombasa refinery, the gains from these sales at higher prices have not been sufficient to offset the higher cost of the crude oil and oil product imports. Thus the *net cost* of petroleum imports has been risen from K£1.1 million in 1973 to K£47.3 million in 1978. The continuation of this trend will have particularly unfavourable implications on the economy as a whole.

Balance of Payments

During the year 1978, total export earnings declined by 21.1 per cent as compared with 1977. At the same time payments for our imports increased rapidly to a total of K£661.2 million which was 24.4 per cent higher than in 1977. The large visible trade gap of K£265.5 million could not be covered by net receipts from invisible transactions and capital inflows. The country's balance of payments recorded a deficit of K£77.6 million at the end of 1978 compared to a surplus of K£112.7 million in 1977.

In view of this, the Government found it necessary to introduce urgent measures in December to reduce the level of importation as well as to control domestic credit. The import pre-payment and deposit scheme introduced on December 22nd is aimed at making it possible for importers to be more selective and cautious in the use of our foreign exchange, while also making consumers more oriented towards purchasing locally manufactured goods. In its modified form, the scheme provides for progressive penalty on luxury items of import while exempting those essential items required for our development projects, particularly in agriculture and manufacturing. Also exempted are those essential items of social use such as drugs. The scheme is under constant review and adjustments are made as and when it becomes necessary. In this connection, most of the criticism levelled against the scheme has been from misinformed and ill-intentioned self-interests.

The scheme was a necessary short term measure to regulate and control imports so that essential supplies which are not locally available may be given priority in the use of our limited foreign reserves. This approach is also within our general policy of reducing import dependency.

Implications on Fiscal and Monetary Policy of Present Outlook for 1979

The adverse trend in the balance of payments experienced in 1978 is expected to continue in 1979 and 1980. With the already announced increase of 14.5 per cent in the price of crude oil for 1979, our import bill will rise substantially. At the same time, the global increase in crude oil prices will automatically lead to increases in other essential imports. The commitments already made on defence, the former Community Corporations and the recent capital investment commitments in the private sector, will continue to demand the use of a substantial portion of our reduced foreign reserves. On the other hand, our exports receipts, for reasons already explained, cannot be expected to increase—if anything they will fall below the 1978 level. It is, therefore, forecast that the balance of payments will record a deficit which will deplete our reserves to unacceptably low level. We shall, therefore, have to seek international resources to enable us to continue paying for our most essential imports.

As already mentioned earlier, the coffee boom which had a significant impact on Kenya's GDP growth rate in 1977 came to an end in 1978, resulting in a drop in the rate of growth of GDP from 7.3 per cent in 1977 to 5.7 per cent in 1978. For 1979, due to the combined effect of reduced coffee crop and slowing down in economic activity arising from the need to contain the deficit in the balance of payments, GDP growth rate seems unlikely to exceed 4 per cent at constant prices. In fact, it may be as low as 3 per cent.

Figures for the first few months of 1979 show that the country's foreign reserves are no longer falling but this is a somewhat misleading picture in view of the substantial import applications and authorization which have not been paid for.

The anticipated balance of payments deficit is such that it cannot be met purely by import controls and minor reductions in foreign reserve holdings. I therefore propose to meet part of this resource gap by limited use of commercial borrowing. Hon. Members will be aware that the Government has always strongly resisted pressures that we should increase our overseas borrowing and particularly through commercial banks. We have always maintained that such borrowing does not solve problems of long-term investment requirements and development needs. Indeed, such borrowing if used only to finance consumer items of imports would tend to compound our problems by providing short-term cover for fundamental structural problems—a clear case of sweeping the dirt under the carpet.

In the present circumstances, however, we have to provide limited cover for the import requirements of the new Development Plan, particularly for those projects and programmes which depend on imported inputs. For this purpose, and in order to cover any budgetary deficit which may not be fully covered by other measures, I have arranged with a consortium of major banks in London to provide a Euro-currency loan of $200 million to finance the import content requirements of some projects in the new Development Plan. This facility, which will be repayable in six years, with an eighteen months grace period, need not be used in full and for the coming financial year, I hope to use only K£25 million, for budgetary support.

At the same time, I have had most fruitful discussions with the International Monetary Fund and the World Bank with a view to getting their support to meet some of our foreign exchange requirements through IMF facilities and an IBRD programme loan. Similarly, I have been able to convince our major bilateral assistance donors of the need to convert some of their project aid funds to balance of payments support. If the necessary negotiations are concluded urgently, it will perhaps not be necessary for us to draw down on the full amount of the commercial loan I have just referred to. Since this would also be one way of reducing the pressure on Government borrowing from the local banking system, everything is being done to ensure speedy conclusions of these arrangements. I would like to express our utmost appreciation to the agencies and governments who have, once again, proved to be so understanding of our problems in these difficult times.

All these measures will take some time to imprement and perhaps even longer to show a definite improvement in our reserve position.

The import controls now in operation will therefore be continued in the short run. However, these controls cannot be continued for too long because of the danger of causing reduction in economic activity in manufacturing and commerce, followed by ripple effects on the rest of the economy. The consequences of this, as Hon. Members are aware, would be stagnation of the economy, resulting in our inability to achieve the principal policy objectives outlined in the Plan.

Alternative measures must therefore be found to prevent the economy from stagnating in the face of the deterioration in the country's terms of trade. These measures will, to a large extent, include borrowing of international resources for balance of payments support, increased use of bilateral assistance for import financing, and possible reduction in foreign reserves holding to facilitate the easing of import and credit controls. But the amount of foreign resources estimated to be received will not solve this problem overnight. Even if it were in such quantities as would put our balance of payments into a healthy position, it would still require us to reorganize our priorities to ensure that available resources are utilized on the most essential developments.

Accordingly, Mr. Speaker, we shall be forced to make some domestic adjustment particularly in monetary policy and Government expenditures. This is the price we have to pay for over-reliance on a few export commodities whose prices fluctuate widely and a structure of industrial production developed mainly to service the domestic market, but based on a high proportion of imported raw materials.

The monetary policy pursued over the last two years has been geared towards the reduction of growth in money supply and domestic credit. The effects of this tight money situation on the economy have also been reflected in the domestic prices. Thus, the increases in consumer prices in 1978 were lower than in 1977. In 1978, consumer prices in Nairobi rose by 13.7, 8.1 and 8.3 per cent for lower, middle and upper income groups compared to 21.0, 13.5 and 14.5 per cent respectively in 1977. Thus, the tight money situation has considerably reduced the rate of inflation in the past year. But, while domestic credit needs to be controlled to prevent inflationary pressures from rapidly rising money supply, it must also be realized that domestic credit is crucial in determining the revival or slump in economic activity. However, faced as we are by a deteriorating balance of payments, it would be imprudent economic management for us to wholly relax the credit squeeze now in force. I have, however, directed the Governor of the Central Bank to reduce the liquidity ratio to 16 per cent to enable commercial banks lend a little more to the economy. I shall, therefore, expect domestic credit to be maintained at a slightly higher level in 1979 than last year.

With regard to Government expenditures, we have had, regrettably, to curtail both the recurrent and development budget slightly next year in order to reduce Government demand on domestic credit. Consequently, Hon. Members will already have noticed from their copies of the Printed Estimates that the 1979/80 Estimates are lower than the projections contained in the Development Plan. I should like to emphasize that the decision to reduce development spending has been taken most reluctantly and only in the light of the limited options open to us under the prevailing balance of payments position.

As I said earlier, I estimate the growth of GDP at current prices in 1979 to be no more than 4 per cent. This percentage increase in GDP would mean that Government revenues might rise by a similar percentage without changes in the present levels of taxation. But the import controls in operation will eliminate any possible rise in duties and sales tax collected on imports. In addition, they will result in decline in profits thus reducing growth of Corporation Tax at current rates. So the rise in total revenue should be below the 4 per cent.

However, it is unlikely that we shall be able to contain price increases to less than ten per cent in the coming year and this in itself should result in some increase in revenue. It is safe, therefore, to forecast that Government revenue at existing rates is likely to rise by about 5 per cent in 1979/80 over the level to be attained this year. This rate of increase will bring the level of revenue far below our targets in the Plan. Alternative methods of taxation must therefore be considered to ensure that revenue receipts can be increased to meet more of the Government's extended commitments.

FINANCIAL OUTTURN 1978/79

In the last Budget Speech, I estimated a total recurrent revenue of K£504.85 million. Of this, £158 million was to come from Customs and Excise, K£120 million from Sales Tax and K£172 million was to be raised through Income Tax. The balance of K£54.85 million was to be generated by various other sources of revenue. These estimates were based on the assumption that the economy would continue experiencing the buoyancy which was evident throughout 1977 and in early 1978. In the event, these economic conditions did not sustain. The rapid deterioration in the terms of trade and the reduction in availability of domestic credit, coupled with lower returns in agriculture and commerce have all led to a serious shortfall in revenue receipts. The lower level of imports had a dramatic adverse effect on monthly customs duty and sales tax collections. Due, however, to somewhat better receipts in the early part of the year, it is expected that customs revenue will barely meet the target of K£158 million. Sales Tax receipts are expected to drop by K£20 million to only K£100 million for the year. On Income Tax, the picture is not very rosy either. Of the K£172 million estimated for the year, only K£133 million had been collected by the end of April and I expect only a further K£14 million to be collected in May and June. I therefore anticipate a shortfall of K£25 million from this source.

Fortunately, there has been a marked improvement in the revenue receipts from items of Other Revenue and I wish to draw your attention particularly to the increase in Investment Revenue. I hope this arises from my warning last year to Parastatals that they must show a better return on the public funds entrusted to them for investment. All in all, however, the revised revenue estimate of K£465 million reflects a shortfall of K£40 million. The gross estimates of revenue including Appropriations-in-Aid of K£38.77 million will therefore be K£503.77 million.

This lack of growth in current revenue comes at a time when the country needs a major injection of resources through Government spending. This consideration has led to continued reliance by the Exchequer on borrowing from the banking system and the domestic financial institutions to an extent which is not only undesirable, but also obviously unsustainable. In the first six months of 1978/79, Government's short-term borrowing from the banking system increased to over K£75 million as against the level of K£27 million indicated in the 1979/83 Plan. At the same time, credit to the private sector grew by only 1 per cent per month. If this situation were to continue for long it would lead to severe dislocation and a stifling of the growth of the private sector.

Turning now to Expenditure, I would remaind Hon. Members that the 1978/79 Printed Estimates indicated Recurrent Expenditure including Appropriations-in-Aid of K£339 million. The Consolidated Fund Services took up another K£75 million, making a total Recurrent Expenditure Budget of K£414 million. Due to various changes and unforeseen commitments, Parliament has authorized additional expenditure in Supplementary Estimates No. 1 of K£34 million. On the basis of the current rate of spending, it is estimated that a total amount of K£480 million will have been issued by the end of June. This figure includes Excess Votes approved by Parliament during the year as well as payment of an Advance to the Cereals and Sugar Finance Corporation. Thus, from the Current Revenue of K£504 million, only K£24 million will be available for transferring to the Development Exchequer.

The 1978/79 Printed Development Estimates projected an expenditure of K£258 million including K£34 million in Appropriations-in-Aid. As at the end of May only K£137 million had been issued, leaving an amount of K£87 million to be issued in the month of June. It is obvious that this large amount cannot be spent in one month and once again, I wish to express my concern at the slow rate of implementation of development projects which is indicated by this figure. It is expected that by the end of June, only another K£34 million will have been issued thus reflecting an under-expenditure of K£53 million as compared with K£37 million surrendered in the previous year.

EXPENDITURE 1979/80

Now we come to the year 1979/80 when, as I have already indicated, the balance of payments will be the major bottleneck to our economic performance and consequently to Government expenditure.

Recurrent Expenditure of Ministries is estimated at K£467 million, excluding K£42 million Appropriations-in-Aid. This figure, however, includes provisions of K£86 million for Consolidated Fund Services, and Excess

Votes from previous years. This represents an increase of 6 per cent over what I expect Ministries to draw this year. Considering that the salaries of employees under various Ministries will receive the normal annual incremental credit averaging between four and five per cent, and that there are additional commitments relating to the 10 per cent additional employment, adult literacy, free milk for primary school children, population census and general elections, next year's Recurrent Budget is very tight. Ministries will, therefore, have to undertake the same services with no real increase in budgetary provisions despite the inflationary effects.

A significant point to note is that Consolidated Fund Services Expenditure will increase to K£86 million. This is mainly due to increased debt repayments arising out of quick maturing commercial loans which were necessary in safeguarding the territorial integrity of this country. The repayments are indeed expected to accelerate in the next few years and will therefore continue to put pressure on the rest of recurrent expenditure.

As I said earlier, I anticipate that normal revenue will register an increase of about K£20 million over the actual receipts for 1978/79, taking into account a level of inflation of about 10 per cent. This would bring the projected current revenue for 1979/80 to K£485 million, or approximately K£20 million below the original estimate of K£505 million for 1978/79. Thus, the Recurrent Account reflects a surplus of only K£18 million which, as usual, I intend to transfer to the Development Exchequer and I would ask the House to accept this Statement as notice of my intention to do so. I must, however, call the attention of Hon. Members to this very seriously reduced Recurrent Surplus which means that we shall have to depend more on external resources for our development programmes.

The Development Estimates for 1979/80 call for an expenditure of K£232 million excluding Appropriations-in-Aid of K£20 million but including Excess Votes and Under Issues from last financial year. Although this figure is less than the amount voted in the current year, it is nevertheless 13 per cent higher than the amount which I expect Ministries to spend this year.

I do not intend to dwell further on the details of either recurrent or development spending for now. Suffice it to say that I intend to finance total expenditure of some K£762 million. The rest of my Speech will outline how I intend to do this.

External Revenue 1979/80

As I have already indicated, some friendly donor countries which have given us aid in the past are now prepared to increase substantially their grants and loans to Kenya. I estimate that we shall draw K£123 million during the coming year. Of this, some K£22 million is receivable as grants, K£67 million as concessionary loans tied to particular projects and K£34 million will come from IMF facilities and part of the commercial loan intended to ease our balance of payments problem. Recently, several governments have agreed to convert their previous development loans to Kenya into grants and I would like to take this opportunity to express the appreciation and gratitude of the Government and this House for this generous action.

Thus, I expect to use external revenue totalling K£123 million or 15 per cent of the total Expenditure of K£762 million. I am therefore left to raise K£639 million locally.

Internal Revenue 1979/80

I estimate that ordinary revenue, including local Appropriations-in-Aid, should provide some K£528 million at existing rates of taxation. Government stock issues should provide another K£45 million from the non-bank sector, making a total of K£573 million.

I have, therefore, a gap of K£66 million. When I talked about the balance of payments earlier on, I pointed out that it would be imprudent for me to rely too heavily on the banking system if the twin objectives of reducing inflation and relaxing the credit squeeze to the private sector are to be realized. I shall, therefore, have to rely more heavily on increased taxation to close this gap.

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NEW TAXATION PROPOSALS

Mr. Speaker, the remaining part of my Speech will therefore be concerned with how I propose to close that gap of K£66 million. As usual, I ask that this part shall be regarded as being notice of a Motion to be moved before the Committee of Ways and Means.

CUSTOMS AND EXCISE

The House will be aware that over the last few years we have been carrying out a reform of the customs tariff to make it a more suitable instrument of furthering our development objectives. In view of present-day circumstances and in order to give ourselves a bit of respite to consolidate what has been done, I do not propose to pursue that programme this year. There are, however, a few anomalies which I propose to put right and these are covered in the Finance Bill which has been published today. I shall only draw the attention of the House to the more significant of these changes.

The Finance Bill includes an amendment covering a very large number of items in the Customs Tariff for the purpose of harmonizing the numbering, nomenclature and description of items in order to come in line with the new system introduced by the International Customs Co-operation Council. As these have no revenue implications and are also clearly listed in the appendix, I do not need to recite them here. Similar amendments are also proposed under the Sales Tax and the Local Manufactures Export Compensation Act. These are purely technical amendments with no revenue implications.

Similarly, a small amendment is included which would enable the Minister to authorize in writing a person to allow the release of goods where an adequate bond is paid to cover the customs due.

The period during which goods may remain in a warehouse before clearance is now only six months with provision for re-warehousing only twice. Some

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manufacturers have found this period to be inadequate for clearing raw materials imported in bulk, and I propose to increase the warehousing period to one year with provision for re-warehousing once. Several amendments are also proposed in order to clarify the definition of a "coasting vessel" and avoid use of the current definition for tax evasion.

The Commissioner is at the moment allowed to give certain rewards to persons who assist in arresting persons, seizing goods and conviction of persons involved in offences under the Act. Under the existing provisions, the reward may be anything up to the value of the goods involved. I propose to put a limit of Sh. 20,000 to this in order to minimize the possibility of collusion between the offender and the person assisting in his apprehension.

The Commissioner is also authorized by the Act to exempt from duty certain goods which are declared as personal baggage of a person who is genuinely changing his residence to Kenya. In order to avoid the misuse of this provision by Kenyan residents returning from short trips abroad, the provision will be amended to require that such returning residents must have lived outside Kenya for a period of, at least, two years immediately preceding the date of such "bona fide" change of residence.

I would now like to refer more specifically to those amendments which have revenue implications. In our concern to ensure that the prices of basic food items are kept as low as possible, we have always avoided putting taxation on food items, including those imported from outside Kenya. However, in view of successful Government programmes over the years, Kenya has now become largely self-supporting in basic foods and I can no longer see any justification for the continued protection of imported foods which compete with and discourage our own production. With effect from today, therefore, I am imposing a higher rate of duty on a small range of such items which include various types of imported fish, milk and dairy products, maize and maize products and fruit juices. Most of these items which have in the past attracted a rate of duty of between 25 per cent and 30 per cent will now be subject to duty at 50 per cent.

In the area of textiles and related items, the House will be aware of the continuous problems we have from the importation of various made and unmade items which compete unfairly with our own production. This is particularly unfair in view of the very good quality of the textiles now being manufactured in Kenya. I, therefore, propose to increase the duty on fabrics of mainly synthetic as well as cotton materials from Sh. 3 to Sh. 5 per sq. metre and on undergarments from Sh. 4 to Sh. 7/50 each. The *advalorem* duty on knitted fabrics goes up from 55 per cent to 70 per cent while on imported linen, the duty goes up from 65 per cent to 100 per cent. Similar rates of duty will be imposed on all made garments.

At the same time, I propose to reduce the duty on a number of imported parts of certain items which are now manufactured or assembled locally, such as microphones, television sets, radios, bicycle parts and liquid meters. Many of these items are of interest to the majority of citizens of this country who should be able to enjoy them at a reasonable price.

I estimate that these measures, taken together, will provide the Exchequer with additional revenue amounting to K£2 million.

Excise

I propose to make two changes in the excise tariff. Firstly, tobacco. I do not propose to change the rates of excise duty on cigarettes and tobacco but I do propose to raise, by ten per cent, the levels at which current rates of duty become effective. Allowing a small increase for the manufacturer, this measure will have the effect of increasing the price of some of the popular cigarettes such as Sportsman by Sh. 0.50 per packet, Embassy by Sh. 1/50 per packet and the more expensive brands of "555" and Rex by Sh. 1/50.

Secondly, I propose also to increase the rate of duty on locally manufactured spirits by Sh. 2/50 per proof litre.

Taken together, these measures on excise duty will provide an additional K£5.2 million in revenue.

Income Tax Act

The Income Tax Act has been amended frequently in the recent years both for revenue purposes and to make its operations easier. The tax levels under the Act are generally high and compare well with those levied in other countries. In recognition of this fact and of the need to continue providing adequate incentive for more investment and higher productivity, I propose this year not to change the rates of taxation under the Act. In return, however, I must seek the co-operation of all taxpayers in making sure both timely and adequate meeting of their obligation. The Income Tax Department has now been instructed to move to those areas, including the rural and urban areas where new farmers and businessmen are not meeting their tax obligations fully. I am sure that staff of the Department will have the support of all Hon. Members and other law-abiding citizens in their efforts.

However, as a small token to remind taxpayers of their obligation to pay tax on time, I propose, once again to amend section 94 of the Act to provide that the penalty for the late payment of tax shall be increased from the present 5 per cent, with 10 per cent every other five months, to a single penalty of 15 per cent.

Two small amendments are proposed in section 5 (3) of the Act. The first will remove an anomally under which the director of a company would be liable to be taxed twice on the same income arising from premises provided to him by the employer.

The second will allow the whole-time director of a farm company who is required to live in a house on the farm to be treated in the same manner as other employees of the farm who, under measures introduced last year, are assessed to tax on the house at the rate of 10 per cent instead of 15 per cent of their total emoluments.

A new measure is introduced to require that companies which make payments which are liable to tax under section 35 shall deduct the amount of tax in the same way as individuals are required to do today.

In order to encourage taxpayers to make their return on time, I am providing that the penalty charged for non-submission of returns under section 72 (i) shall be increased from 2 per cent to 3 per cent.

Under the existing provisions of section 92, a taxpayer who receives his assessment prior to 31st May is required to pay one half of the amount assessed by 30th June and the other half by 30th September. The tendency has been for most taxpayers to pay all their tax by 30th September even where penalties are incurred between 30th June and 30th September. I propose to amend this section in order to provide that a taxpayer may meet his full obligations at any time not later than 30th September on any assessment made up to 31st August.

Finally, under Income Tax, a small amendment to the Second Schedule will enable the inclusion of losses on the sale of assets in the calculation of a trading loss in the same way that a profit on sale of assets is included in the trading profit.

I propose that these measures should become effective as from 1st January, 1980, except for the amendment to sections 5 and 35 which will come into effect immediately.

SALES TAX

I now propose to deal at some length with the question of Sales Tax. Since its introduction in 1973, this form of tax has increasingly played an important role in our fiscal and economic policy. Today, with a yield of over K£100 million in 1978/79, it forms the third largest source of revenue, after Income Tax and Customs and Excise. In addition, it has become significant in the management and regulation of prices in the economy. In the new Development Plan, it is clearly stated that indirect taxation shall be a more important source of Government revenue for further development financing. It is this instrument therefore that I propose to utilize more in the efforts to raise more revenue this year and to allocate more fairly and equitably, the new burdens of which I spoke earlier.

First, I propose to raise, with effect from midnight to-night, the general rate of Sales Tax from 10 per cent to 15 per cent. This will therefore be the minimum level of tax paid for all items, both imported and locally manufactured, on which the general Sales Tax rate is applicable.

Hon. Members will recall that last year, I raised the rate applicable to certain items which are not of general household use and for which specific rates are provided. These are the items listed in Part II of the First Schedule. In order to retain the same general price and tax relationship between these items and those under Part I, I propose to again increase the rate on these items from 20 per cent to 25 per cent of taxable value. The list concerned includes such items as mineral waters, toilet waters, perfumery and cosmetics, matches, films, ornaments, leather goods, travel goods, furs, articles of personal adornment, precious and semi-precious stones, domestic refrigerators, elevators, lifts, washing machines, domestic appliances, passenger motor cars and buses of 14 passengers and below, pleasure boats, cameras, watches and clocks and television sets.

However, in order to encourage the growth of indigenous artistic talent, I am removing from this Schedule the sales tax imposed last year on locally produced gramophone records. At the same time, I am imposing the higher rate of sales tax on all imported cassettes which have been threatening the growth of the local music recording industry.

At this point, I wish to wish to issue a strong warning to our manufacturers and traders with respect to the price implications of the measures. The House will recall that when we first introduced a general sales tax of 10 per cent, we calculated that the retail price increase should not have exceeded 6 per cent. Many traders, however, took the opportunity to increase their prices by as much as 15 per cent. We now envisage that the new level of sales tax should cause a retail price increase of only about 3 per cent. I must, therefore, state most emphatically that any trader who increases his price by more than this margin is breaking the law and I have instructed the Price Controller to ensure that any such trader should be dealt with most severely when caught.

Mr. Speaker, I now turn to one of our favourite subjects—beer. Last year, I proposed an increase in taxation of 40 cts. per bottle of Tusker or Whitecap and *pro-rata* increase in the prices of other beers and stouts. Although there was a reduction in consumption of beer, the reasons for this are more to be found in the general social conditions during the year. The breweries were therefore unable to go ahead with projected expansion of capacity and revenue during the first part of the year was not as buoyant as expected. I am now confident that this trend will change. With the general clamp down on local beer-halls and the higher producer prices for some commodities, the consumption has already started picking up. This trend will no doubt accelerate as we get nearer to election time. In view of this and of the need to proceed with the scheduled expansion of capacity by construction of a new brewery at Kisumu, I propose to increase the price of beer by another 40 cts. per bottle of Tusker/Whitecap, with *pro-rata* increases on other brands and on stout. Of this, the breweries will be allowed to retain 16 cts. while the balance of 24 cts. will go to the Exchequer.

From this measure, I expect to raise K£4.5 million additional revenue.

As I have indicated earlier, our use of petroleum products needs careful consideration. A very major part of our problems arises from the very high cost of imports of crude petroleum and petroleum products. With the ever-increasing prices now being set by the oil exporting countries, Kenya must make substantial changes in its overall dependence on imported petroleum and petroleum products. This will take some time and will involve heavy capital expenditure. In the meantime, the wanton and careless use of expensive fuel must be reduced by fiscal as well as physical measures. Among the measures I shall propose today, there will be several whose main objective is to make luxury motorists pay more for the use of such an extremely costly energy resource.

In addition, therefore, to passing on the full increase in crude oil and product prices as dictated by the oil exporters, I have no alternative but to increase taxation on petroleum products. In order to discourage luxury use of petrol and encourage utilization of other products, I propose to load the whole of this on premium and regular gasoline while other products remain as they are. The increase in premium and regular gasoline prices will be 30 cts. and 20 cts. respectively throughout the country.

These prices become effective as from midnight to-night and should add an estimated K£4.5 million to revenue in the next year.

I wish to make it very clear, Mr. Speaker, that this is still a very lenient approach when compared to measures taken in other countries where the prices are much higher and availability of products is restricted. If further increases in basic crude prices are effected by the OPEC countries, we shall have no option but to pass these to the consumers. In the meantime, the Government is giving urgent consideration to other physical measures for greater conservation and optimum use of petroleum energy, and these will be announced in due course.

Wines and Spirits

Mr. Speaker, the next item on my list today is Wines and Spirits. The main consumers of these items are those people both local as well as foreigners, who have the means to afford and enjoy a good dinner. The items do not, therefore, have much relationship to the cost of living of the majority of citizens of this country. At the same time, they place a substantial burden on our foreign reserves especially during difficult times as at present. For this reason, I recently considered it appropriate to remove them from price controls so that their prices can be dictated by supply and demand forces. Since then, the prices of wines and spirits have gone up. It seems to me only reasonable that the Exchequer should benefit from the increase in prices by retaining the existing ratio between retail price and tax. I have therefore increased the rate of sales tax on wines and spirits to 30 per cent. I have also increased the rate of import duty on wines by an average of 15 per cent and the specific rate on spirits has been raised from Sh. 65 per proof litre to Sh. 75 per proof litre. In addition, I have imposed higher excise on locally produced spirits from Sh. 42/50 to Sh. 45 per proof litre as mentioned earlier.

From all the measures I have taken under Sales Tax Act, I expect to raise a total of K£23 million as additional revenue.

Second-hand Motor Vehicle Purchase Tax

I have previously referred to the need to reduce the consumption of the more expensive grades of petroleum products. Towards this end, we must discourage, as much as possible, not only importation but the purchase and use of large passenger cars which use greater quantities of the more expensive petroleum products. I therefore propose to introduce a number of measures deliberately aimed at the users of such large passenger cars. The first of such measure relates to the Second-hand Motor Vehicle Purchase Tax.

With immediate effect, therefore, the following rates of tax shall apply:—

	Sh.
For a motor vehicle with less than four wheels	100
For a motor vehicle with four wheels and with an engine capacity—	
(i) not exceeding 1200 c.c.	500
(ii) exceeding 1200 c.c. but not exceeding 1500 c.c.	600
(iii) exceeding 1500 c.c. but not exceeding 1750 c.c.	700
(iv) exceeding 1750 c.c. but not exceeding 2000 c.c.	900
(v) exceeding 2000 c.c. but not exceeding 2250 c.c.	1,000
(vi) exceeding 2250 c.c.	2,000

Considering the very high values that Second-hand Motor Vehicles are fetching today, I do not consider this rate of taxation to be high.

I expect to raise an additional K£800,000 of revenue from this change.

Fees Under the Traffic Act

There is a wide range of fees under the Traffic Act which have not been revised for some time. They have, therefore, remained very low in relation to the current prices of vehicles and petroleum products as well as the costs of road maintenance. In consultation with the Minister for Power and Communications, it has been decided that these fees shall be revised with immediate effect.

The most important of these fees is that relating to Road Licences for passenger cars on which a major change is now introduced. Until now, this fee has been based on the tare weight of the vehicle licensed. This method of licensing gives an undue advantage to the owner of a light vehicle which may have a large engine capacity and therefore favours the users of the faster passenger cars. Under regulations passed today by the Minister for Power and Communications, a revised system is introduced based on the cubic capacity of the engine. The progressive rates used in the new system will ensure that the owners of larger-engined passenger cars will pay a heavier licence fee. Thus the licence for a 1200 c.c. car will cost Sh. 300 per year, while for a 2000 c.c. car, the licence will cost Sh. 800. For a 3000 c.c. car, the road licence will cost

Sh. 1,400 while anybody wishing to drive a car with a 5000 c.c. engine will have to pay Sh. 3,500 per year. Beyond that, the fee will increase by one shilling for every additional cubic centimeter. These fees become effective on the next date of renewal of the licence.

COMMERCIAL VEHICLES ROAD LICENCES

As regards commercial vehicles, Road Licence fees are currently based on whether a vehicle is petrol or diesel propelled. The fee for a diesel propelled vehicle is twice that of a petrol propelled vehicle of equal tare weight. This seems obviously wrong since petrol is more expensive than diesel.

Our oil refinery produces adequate diesel fuel for our needs while we have to import certain grades of petrol at greater cost to our foreign reserves. In order to encourage more use of diesel for commercial transportation, it is proposed to remove the existing discrimination and to raise the licence fee for petrol propelled commercial vehicles to the same level as the diesel propelled vehicles.

OTHER TRAFFIC LICENCES

Other licences under the Traffic Act are also too low and needs to be raised to be in line with current costs. The details of these fees are laid out in the new regulations under the Act and I shall not itemize them here. They, however, include fees for the issue and renewal of driving licences, issue of documents and duplicates thereof, special carrier licences as well as dealers general licences and special identification plates. In case anybody should think it is cheaper to drive without licences, I have asked the Minister for Power and Communications to propose revised penalties for breach of the relevant regulations.

The above measures under the Traffic Act are expected to bring an additional K£2.5 million to the Exchequer.

AIR PASSENGER TAX

Mr. Speaker, we are all aware that the Government has just completed the construction of two magnificent Airports at Nairobi and Mombasa. I am sure we are all very proud of such modern facilities. But such developments cost a lot of money. I do not, therefore, think it unreasonable to ask those who use these facilities to pay a little more for the privilege. I am therefore increasing, from midnight to-night, the Air Passenger Tax from Sh. 40 to Sh. 80. This should provide the Exchequer with an additional K£900,000 of revenue.

HOTEL ACCOMMODATION TAX

Another area to which a lot of public funds have been directed is in providing facilities such as hotels and roads for the comfort of visitors to this country. While holidays in Kenya may not appear to be cheap as compared with those in other tourist resorts, I am sure that we have much more to offer for every shilling spent on holiday in this country. It is therefore, not too much to ask that the tourists and owners of hotel establishments pay a little more for the maintenance of the conditions which makes Kenya such an attractive holiday resort. I therefore propose to increase, with immediate effect, the Hotel Accommodation Tax from 10 per cent to 15 per cent on bed and breakfast charges and from 7½ per cent to 10 per cent for all other accommodation charges.

I expect to raise additional revenue of K£680,000 from this measure.

ENTERTAINMENT TAX

Entertainment taxes have not been revised over the last eight years. During this time, the standard of entertainment has improved and the establishments concerned have also raised their charges. I am therefore asking them to provide a little more help to the Exchequer by raising the tax on entertainment as listed in the Schedule to the Finance Bill. While there is very little change on the cheaper entertainment ticket, those paying more than Sh. 5 will contribute an average of about 15 per cent in tax. I do not consider this onerous and particularly for those who will pay a little more at the higher ticket values.

I hope to raise an additional K£150,000 of revenue from these changes.

MISCELLANEOUS FEES

I now turn to other general licences issued under different Acts of Parliament. Most of these have not been reviewed for over five years and the fees have remained very low, some dating back to 1971. In order to bring them in line with the general increase in costs, I propose to raise them as follows:—

Liquor Licensing Act

The fees issued under the Liquor Licensing Act are very low in relation to the level of profits in the business. Since many businessmen in this trade have not yet been brought within the income tax network, I propose that the fees should be increased and a Legal Notice to this effect has been published this afternoon.

Trade Licences

Trade licence fees have also remained low for a long time. Many of the businessmen concerned have done reasonably well and can afford to pay higher licence fees. The increases are detailed in the relevant part of the Finance Bill, but to cite a few cases, the fee for a wholesale trader increases from Sh. 200 to Sh. 400 per year, for catering in urban areas the fee will rise from Sh. 30 to Sh. 60, while for general trade the fee rises from Sh. 100 to Sh. 200 with the fee in rural areas rising from Sh. 40 to Sh. 80. Although the increases may appear large on a percentage basis, the new rates are still very low compared to the annual turnovers of the business enterprises concerned.

Mr. Speaker, I now turn to a different category of fees, those dealing with banking and financial institutions.

UNIVERSITY OF NAIROBI LIBRARY

BANKING ACT

Under the Banking Act, banks are required to pay an annual fee of Sh. 5,000 for a licence which enables the bank to operate all its branches. I consider this fee to be too low in relation to the profits made by banks and I propose to raise it to Sh. 10,000 per year. In addition, I propose that in order to encourage banks to increase their operations in the rural areas, an additional fee of Sh. 2,000 shall be paid for every branch operated by a bank within a Municipality. No fees will be raised for bank branches operated in rural areas and other urban centres.

Financial Institutions

Also under the Banking Act, provisions are made for licensing of Financial Institutions. There has been a recent trend towards rapid increase in these institutions, possibly because of the easy profits to be made through them and also due to the more flexible rules under which they operate. I feel that the good profits will not be much affected if we increase the fees a bit, and I propose to raise these from Sh. 5,000 to Sh. 15,000 per annum, with Sh. 5,000 being payable for every additional branch of a financial institution.

These changes should provide the Exchequer with additional revenue of K£50,000.

Finally, in this area, I refer to insurance companies licences. Following the changes which have been introduced in insurance legislation and the streamlining of the industry by the Government, I expect that insurance companies will continue to improve on the very good profits which they have always made in this country. On the other hand, the licence to operate an insurance company still remains at the very low level of Sh. 2,000 per annum. I am sure they can afford a little increase and I propose to raise the fee to Sh. 10,000 per annum.

Let me state here, Mr. Speaker, that I do not expect insurance companies to increase their premium because of this higher fee. The Government has just carried out a review of the insurance business and is currently studying the Report prepared for it by an expert in this field. I hope, as a result of this, to be able to present to this House revisions to the Insurance Act which will make it more relevant to the needs of the Kenya economy.

After all these new taxation measures I am still left with a gap of K£30 million. I propose to finance this remaining part by way of Treasury Bills and a decrease in Exchequer Cash Balances.

Mr. Speaker, I am aware that the taxation measures I have just proposed are indeed onerous. But I have warned many times in the past that the responsibility of developing this nation must ultimately rest with Kenyans themselves. Last year, I also drew the attention of the House to the fact that we could not strengthen the security of this country without foregoing some of our development targets especially in social services, or alternatively making greater sacrifices.

I am pleased to note that most Ministries have worked well within their provisions without much sacrifice to the development effort. With the recently announced measures for increased employment, accelerated adult education and supply of milk to primary school children, Ministries will, once again, be called upon to resort to maximum efficiency and economies in order to maintain a satisfactory level of services.

There are, however, two other exercises to be undertaken this year and to which I must refer. The first is the Population Census which we are committed to undertake once every decade and which is essential for proper planning. The second, which is of obvious interest to Hon. Members, is the General Election. I take this opportunity to wish all Hon. Members the best of luck in their efforts to retain their Seats.

In conclusion, I wish to express once again my confidence in the ability of the people of Kenya to overcome their difficulties. If we heed to the call by His Excellency, the President, on Madaraka Day, for every citizen to pay his taxes in time, we shall make our burden lighter. Guided by the indomitable energy and dynamic statesmanship of our President, and backed by the commitment of all Kenyans to our Harambee motto, we can still march forward briskly in the true spirit of "Nyayo".

Mr. Speaker, I beg to move.

GPK 1027—3,500—6/79