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POLICY BRIEF

Eliminating Business Unfriendly Policies on Multiple Inter-county Taxation Affecting Micro, Small and Medium Enterprises

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Executive Summary

This policy brief seeks to highlight challenges facing the Micro,Small and Medium Enterprises (MSMEs) sector in relation to multiple licenses or fees levied by county governments when goods or services move across county borders.The purpose of the policy brief is to facilitate public-private dialogue in eliminating restrictive trade policies resulting multiple licenses that hinder free movement of goods and services throughout the country.This policy brief focuses on 3 categories of fees,licenses or levies applied by counties on goods and services moving across different county jurisdictions i.e. cess or infrastructure maintenance fees, motor vehicle branding and distribution licenses. Our research identified the following key challenges faced by the businesses related to multiple fees and licensing requirements across the counties:

The policy brief identifies the following key challenges faced by the businesses related to multiple fees and licensing requirements across the counties–

- Double taxation;
- Levying of cess on national trunk roads when goods are passing through a county;
- Payment for multiple distribution licenses in each county where a distributor or manufacturer supplies goods or products to business customers;
- Payment of multiple vehicle branding fees in each county where a branded vehicle passes through;
- Payment of inter-county fees and licenses based on different unit of measurements applied by different counties.
- Payment of inter-county fees and licenses based on different unit of measurements applied by different counties

And proposes the following recommendations for consideration:

- **The National Treasury, Ministries of Trade and Transport** should set up an inter-ministerial taskforce with representation from the **State Law Office and county governments and private sector** to review inter-county taxation in relation to each county and draft the proposed policy measures into policy and legislative changes.

- **The National Treasury** should prepare for adoption and enactment national policy and legislation in accordance with Art. 191 of the Constitution to provide for:

  - Uniformity in establishing norms, standards and national policy on cess and infrastructure maintenance fees, motor vehicle branding fees, and the distribution of licenses. Policy changes should protect the common market with respect to mobility of goods, service, capital, and labor across the country.

  - For cess specifically, the tax should only be levied once, in the county of origin.The imposition and collection of cess on any goods being transported through a county or on a national trunk road should be prohibited, and cess designated for maintenance of county roads should only be collected on a country road, not a national trunk road.

- **The National Treasury and Ministry of Trade** should prepare, adopt, and enact national policy and legislation for the national recognition of permits issued at the county level, of vehicle branding licenses and fees, as well as the recognition and distribution of licenses to enable the free movement of goods across the country.

- **County governments** should adopt a modern automated tax collection system for cess.

- **The Ministry of Trade** should prepare for adoption and enactment a national policy and legislation on uniform standards and norms on units of measurement.

- Vehicle branding should be defined and clarified in the national legislation so as to differentiate different forms of branding for purposes of taxes.The National Treasury should initiate preparation and adoption of national policy and law on vehicle branding

- Distribution licenses should only be acquired and paid once in the county where the business has commercial establishment.

By adopting the above proposed policy measures it is anticipated that the cost of doing business will be reduced, the free movement of goods throughout the country will increase, and businesses will benefit from improved sustainability and predictability.

Overview: Multiple Inter-County Taxes

Section 2 of the Fourth Schedule to the Constitution assigns functions to counties, sets the basis for the provision of county public services . County governments have two main sources of revenue, equitable transfers from national government or their own sources revenue. County's own sources revenue consists of fees related county licenses, user charges for county services and permits, levies, property rates and entertainment taxes among others.Art 209 (2) of the Constitution of Kenya grants county governments powers to levy property rates, entertainment taxes or any other tax as authorized by an Act of Parliament.

Whereas county taxes, levies, fees and charges should target local residents, businesses or any use of county services and resources, county governments have levied some fees, taxes and levies that target nonresidents or businesses which do not have interaction with county services. County governments have imposed fees and charges without due regard to their impact on national economic policy and common market in the country. Businesses have faced the challenge of multiple taxation when moving goods and services across the country.Three of such taxes are Cess or infrastructure development levies, distribution licenses and motor vehicle branding.

1. Republic of Kenya (2010)The Constitution of Kenya. Government Printers, Nairobi

Cess- Infrastructure Maintenance Fees

Cess (which in some counties such as Kiambu is referred to as infrastructure maintenance fee[2]) is levied on[3]:

a) Agricultural and fishing products produced or supplied for commercial purposes such as maize, milk, cattle, vegetables, fish, fruits, coffee, tea and flowers and forestry products such as wood and wood products (e.g. timber and charcoal);

b) Extractives such as quarry products (stones, ballast, sand, quarry chips, murram) and other minerals).

Cess is one of the sources of counties' own revenue. The table below summarizes a sample of percentage of cess contribution to counties own source revenue for select counties.

Sample cess contribution to county revenue in select counties

County	Percent of Cess Contribution to County Own Source Revenue
1. Embu[4]	7
2. Nakuru[5]	1.2
3. Kiambu[6]	3.9
4. Kisii[7]	2.7

The unit of measurement for purposes of levying the cess is the weight of the product, package/container (e.g. per sack of the product) or carrying capacity of the motor vehicle. Cess is collected at source or during transportation of the products at designated county or national government roads . Ordinarily, counties levy cess fees on products or goods produced or extracted from the county. Where cess for goods (especially agricultural products) has been paid for in a county, some counties do not charge cess for the goods to be transported through the county. A transporter is only required to produce evidence of paying cess in the county of origin. For example, a transporter ferrying vegetables from Nyandarua county, which are destined for sale/distribution in Kitui, is only required to pay cess in Nyandarua county and does not pay cess when transporting goods through Kiambu, Machakos, Nakuru or Nairobi depending on the route used. However, the transporter or trader has to pay market fees to access or sell the goods in the destination market.

2. County Government of Kiambu (2018) The Kiambu County Finance Bill, 2018. Government Printers, Nairobi. Available at www.kiambu.go.ke.
3. See Note 3 and 4.
4. Embu county government (2018). Embu County Budget Review and Outlook Paper. Available at www.embu.go.ke.
5. Nakuru county government (2018). Nakuru County Budget Review and Outlook Paper. Available at www.nakuru.go.ke .
6. Kiambu county government (2018). Kiambu County Budget Review and Outloo Paper. Available at www.kiambu.go.ke.
7. Kisii county government (2018). Kisii County Fiscal Strategy Paper, 2018. Available at www.kisii.go.ke.
8. See County Government of Kisii (2017). Kisii County Finance Act, 2017. Available at www.kisii.go.ke.

However, transporters of extractives such as stone, sand and ballast are required to pay cess in each county where they pass through in addition for the cess paid in the county of extraction. In this case, cess is levied by county governments irrespective of whether transportation through the county takes place on county roads or national government roads such as trunk roads. The table below highlights some of the cess fees payable in select counties for extractives. The fees demonstrate that counties adopt different standards of measurements when levying cess. In addition, a trader moving products across such counties with different units of measurement faces the challenges of complexity of different units of measurement.

Sample cess fees in select Counties

County	Cess fees range (Kshs)
1. Embu[9]	100 - 1200 per ton
2. Nakuru[10]	1% of gross turnover
3. Kiambu[11]	400 - 1000 per trip (infrastructure maintenance fee)
4. Kisii[12]	50 – 500 per trip & 20,000 per container

Motor vehicle branding

Outdoor advertising is a county function. County governments levy fees for external branding of motor vehicle, which ranges between of Ksh. 5,000 – 8,500 per year per motor vehicle. Counties seek to levy the fees from any branded vehicle whose business the commercial presence is based in the county, as well as any branded vehicle driving in or through the county. Ordinarily, vehicle branding entails use or corporate colours, identity or images as part of the external identity of a motor vehicle. The table below highlights some of the motor vehicle branding fees payable in select counties.

Sample motor vehicle branding fees in select counties

County	Fees (Ksh)
1. Embu[17]	4,000 – 10,000 per motor vehicle
2. Nakuru[18]	6.000 – 10,000 per motor vehicle
3. Kiambu[19]	5,000 per motor vehicle
4. Kisii[20]	5,000 – 20,000 per motor vehicle

Distribution Licenses

Counties issue trade licenses for the diverse economic activities. One is the economic activity is the distribution services. However, counties also demand that any person distributing of goods or services, for example from a manufacturer or supplier to a wholesaler or retailer, must have a distributor's license issued by the county. The table below highlights some of the distribution fees payable in select counties.The distribution of fees is representative of the range of fees charged by the counties across the country.The sample distribution fees are an indicator of the range of fees that businesses are subjected to by different counties, which increase when a trader distributes goods from one county to another. Currently, there is no national standard or policy on how distribution fees should be applied or levied by counties.

9. Embu county government (2018). Embu County Finance Ac, 2017.Available at www.embu.go.ke.
10. Nakuru county government (2018). Nakuru County Finance Act, 2018.Available at www.nakuru.go.ke.
11. Kiambu county government (2018). Kiambu County Finance Act, 2018.Available at www.kiambu.go.ke.
12. Kisii county government (2017). Kisii County Finance Act, 2017.Available at www.kisii.go.ke.
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14. Nakuru county government (2018). Nakuru County Finance Act, 2018.Available at www.nakuru.go.ke.
15. Kiambu county government (2018). Kiambu County Finance Act, 2018.Available at www.kiambu.go.ke.
16. Kisii county government (2017). Kisii County Finance Act, 2017.Available at www.kisii.go.ke.

Sample distribution fees in select counties

County	Fees (Ksh)
1. Embu[12]	15,000 – 30,000
2. Nakuru[13]	31,500 – 135,000
3. Kiambu[14]	2,000 - 5,000
4. Kisii[15]	15,000 – 30,000

Challenges Facing MSME Sector on Multiple Inter-County Taxation

Whereas the county governments levy the taxes or fees for own source revenue generation, the levying of the fees to businesses trading across counties results in several challenges.As observed by Kenya National bureau of Statistics (2016), 16% of MSMEs indicated payment of licenses and associated constraints as one of the key challenges they face in business. Specifically, the challenges below have been observed in relation to the 3 categories of licenses:

Cess or infrastructure maintenance fees

From the context describe above, MSMEs face the following challenges in relation to payment of cess across counties:

a) a) Businesses are subjected to multiple taxation by being obligated to pay cess in each county where they transport their goods into or through the county where a county does not recognize that the business has paid cess in the county of origin. A business transporting goods through different counties has to pay cess in each of those counties especially for extractives.

b) Counties have poor cess administration processes and collection systems.They mainly erect barriers on highways and have to stop each vehicle for inspection and determination of amount payable.This has resulted in cumbersome process in transport and logistics and has resulted in loss of business especially where perishable goods such as flowers,fruits and vegetables are subjected to delays while in transit.

c) Counties collect the cess from roads classified under national government (especially Class A, B and C. Even where a transporter has not transported goods on any county road, the counties still impose and collect the fees.There is therefore no policy justification for a county to levy cess fees for goods transported on national government roads without any use of the county roads.

d) Different counties adopt different unit measures for purposes of levying fees e.g. tonnage, per package (e.g.sack) size of motor vehicle and number of trips.This creates trade barriers in relation to free movement of goods across the country

17. Embu county government (2018). Embu County Finance Ac, 2017. Available at www.embu.go.ke.
18. Nakuru county government (2018). Nakuru County Finance Act, 2018. Available at www.nakuru.go.ke.
19. Kiambu county government (2018). Kiambu County Finance Act, 2018. Available at www.kiambu.go.ke.
20. Kisii county government (2017). Kisii County Finance Act, 2017. Available at www.kisii.go.ke.

Motor vehicle branding fees

Motor vehicle branding is deemed to be outdoor advertisement by counties hence the imposition of vehicle branding fees.The following challenges are experienced by businesses on multiple taxation related to vehicle branding:

a) Businesses are subjected to multiple taxation by being obligated to pay fees for each branded vehicle that drives into each county where the business enterprises supplies goods or services.The charges apply to any branded vehicle irrespective of the purpose of driving into the county and duration of stay within the county.

b) Counties impose vehicle branding fees to motor vehicles whose business operators do not have commercial establishment in the county.

c) County governments often impound branded vehicles driving into or through the counties and demand that the operators must pay for the motor vehicle branding fees.

Distribution Licenses

Counties have a class of licenses related to distribution of goods.The following are the challenges related to distribution license and multiple taxation-

a) Businesses (especially manufacturers and distributors) are subjected to multiple taxation by being obligated to pay for distribution licenses in each county where they distribute, offload or supply goods to business customers (Business to Business transactions) with commercial establishment in the respective destination counties.

b) A manufacturer or distributor with coverage of more than one county has to apply for licenses in each of those counties irrespective of whether they have commercial establishment in those counties or not.

Impact of Multiple Inter-county Taxation on MSME Sector

The following is the impact of multiple taxation in the above 3 areas:

a) The multiple fees paid in each county increase the cost of distributing goods and services.

b) Multiple fees increase the cost of doing business for manufacturers,distributors,and wholesalers. This has resulted in increase in product prices and consequently reduction in sales. On average, a manufacturer or distributor supplying or distributing goods or service provider to a region of 8 counties grouped as a geographical market segmentation region using branded vehicles pays an average of ***Ksh. 240,000*** (using an average of ***Ksh. 30,000*** per year) to distribute the products in the counties and additional ***Ksh. 800,000*** for using branded vehicles (including sales and marketing vehicles at an average of 10 vehicles visiting each county in the course of the year paying an average of ***Ksh 10,000***).This would amount to an average of ***Ksh. 1,040,000*** per year. This cost would be in addition to other regulatory fees and licenses that an enterprise pays for in the county that it has commercial establishment.

c) High cost of doing business has the potential to reduce investments in sectors that attract high license fees, which in the end reduces opportunities for job creation and economic growth.

d) Due to high distribution costs associated with distribution of goods and services across the counties,distributors and manufacturers have opted not to directly supply the goods directly to business customers. Instead, they have to have the business buyers collect the goods purchased from the main facilities since a business enterprises does not pay distribution fees for bringing in goods from outside the county.This has increased the cost of doing business for local businesses since they do not have the economies of scale that would be enjoyed by a manufacturer or distributor.

e) Levying inter-county fees for goods being transported into or through the counties restricts free movement of goods and services across the country and act as a barrier to trade within the common market in the country.

Policy gaps on Multiple Inter-county Taxation

The following are the policy gaps that have contributed to existence of county policies and practices that hinder free movement of goods and services across counties and inhibited business and investment friendly climate:

a) **Lack of a national uniform policy on standard** on the unit of measure for purposes of levying cess and related fees by all counties;

b) **Lack of national policy and standard for promoting free movement of goods and services** across the country for purposes of implementing Article 191 of the Constitution;

c) **Lack of policy on mutual recognition of county licenses, fees and charges among counties;**

d) **Lack of national recognition and application of a county license** throughout Kenya for activities such as motor vehicle branding and distribution licensing which would see businesses move across county borders;

e) **Lack of policy regulating with powers of county governments to impose and collect taxes, fees and charges** for goods passing through the county even where those goods are transported through county or national trunk roads.

Policy Recommendations for Reforming County Policies Resulting to Inter-county multiple taxation

Cess - Infrastructure Maintenance Fees

The following policy interventions should be adopted in order to address the challenges associated with cess or infrastructure development fees:

a) **The national treasury should prepare for adoption and enactment national policy and legislation in accordance with Art. 191** of the Constitution so as to provide for –
   - Uniformity in establishing norms, standards and national policy on cess and infrastructure maintenance fees;
   - Protection of the common market in respect of mobility of goods, services, capital and labour across the country;
   - Cess to be levied only once in the county of origin and not while the goods are in transit to other destination markets;
   - Prohibition of imposition and collection of cess on any goods being transported through a county or on a national trunk road (class A, B or C roads) where those goods are destined to sale or consumption in another county. Further, cess which is designated for maintenance of county roads should only be collected in a county road and not in a national trunk road.

b) **County governments should adopt a modern automated tax collection system** where cess should be paid for through online payment systems to avoid delays occasioned by collection of the levy on the roads.

c) **The National Treasury and ministry of trade should prepare for adoption and enactment national policy and legislation for the national recognition of permits** issued in a county throughout the country to enable the free movement of goods across the country especially where the goods pass through a county in transit to other counties.

d) **The ministry of trade should prepare for adoption and enactment a national policy and legislation on uniform standards and norms on units of measurement** for purposes of taxation or levying of county fees and charges on all agricultural goods, products and extractives.

Motor Vehicle Branding Fees

The following policy interventions should be adopted in order to address the challenges associated with vehicle branding fees:

a) The National Treasury should prepare for adoption and enactment national policy and legislation in accordance with Art. 191 of the Constitution so as to provide for –

- Uniformity in establishing norms, standards and national policy on motor vehicle branding fees; and
- Protection of the common market in respect of mobility of goods, services, capital and labour.

b) The National Treasury and ministry of transport should prepare for adoption and enactment national policy and legislation for for purposes of enabling free movement of goods across counties.

- Motor vehicle branding fees should only be paid once in the county where the business has commercial establishment or where the vehicles will ordinarily be utilized for business operations in case of national corporate entities operating businesses nationally: Provided that a business entity operating branded vehicles in more than one county shall be responsible for ensuring that appropriate licenses are acquired for the respective vehicles in the counties where the vehicles would operate in.
- A vehicle branding permit/fees issued in a county should be recognized as a universal license applicable in all counties for purposes of supplying goods or services to business customers.

c) Vehicle branding should be defined and clarified in the national legislation so as to differentiate different forms of branding for purposes of taxes.

Distribution Licenses

The following policy interventions should be adopted in order to address the challenges associated with distribution licenses–

a) The National Treasury should prepare for adoption and enactment national policy and legislation in accordance with Art. 191 of the Constitution so as to provide for –

- Uniformity in establishing norms, standards and national policy on distribution licenses; and
- Protection of the common market in respect of mobility of goods, services, capital and labour

b) The National Treasury and ministry of trade should prepare for adoption and enactment national policy and legislation for national recognition of distribution licenses issued in a county throughout the country for purposes of enabling free movement of goods across counties. A distribution license (which is issued as a business license) issued in a county should be recognized as a universal license applicable in all counties for purposes of supplying goods to business customers

c) Distribution licenses should only be acquired and paid once in the county where the business has commercial establishment. But where a distributor or supplier establishes a commercial outlet in another county other than the main county where commercial establishment is located, the distributor shall acquire a distributorship license or depot license and may be appropriate.

General policy recommendation covering the 3 areas

The National Treasury, Ministries of Trade and Transport, should set up an inter-ministerial taskforce with representation from the State Law Office and county governments and private sector to review inter-county taxation in relation to each county and draft the proposed policy measures into policy and legislative changes.

Best Practice: Regulation on Interstate Commerce in United States

United States' has a federal system of governance. States has powers to enact laws to govern the functions assigned to the states provided those laws do not contradict the federal laws. States levy taxes such as payroll, property, sales, estate and gifts and excise taxes and user fees.

States do not regulate (including tax) interstate commerce, which refers to the purchase, sale or exchange of commodities, transportation or people, money or goods and navigation of waters between States .This is left to the federal government. Only businesses established or located and doing business in a State are subject to State taxation. Consequently, interstate commerce does not constitute doing business in a respective state, (CSC, 2018) . In addition, isolated transactions by a business in another State other than State where it ordinarily does business does not constitute doing business.

In relation to the multiple taxation aspects discussed in this brief and borrowing from US example, motor vehicle branding, distribution of goods from one county to another and transporting goods through a county would not amount to doing business in a county. Consequently, they would not be subject to county taxation.

Conclusion

In conclusion, businesses in Kenya that trade in goods or services across counties are subjected to multiple taxation in relation to cess, distribution and branding of vehicles.The multiple taxation has resulted in increased cost of doing business resulting in reduced business growth and employment creation.The policy brief has identified the policy gaps and proposed measures to be adopted in order to mitigate the policy gaps.Adopting the proposed policy measures will significantly to result in improved business and investment climate.

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