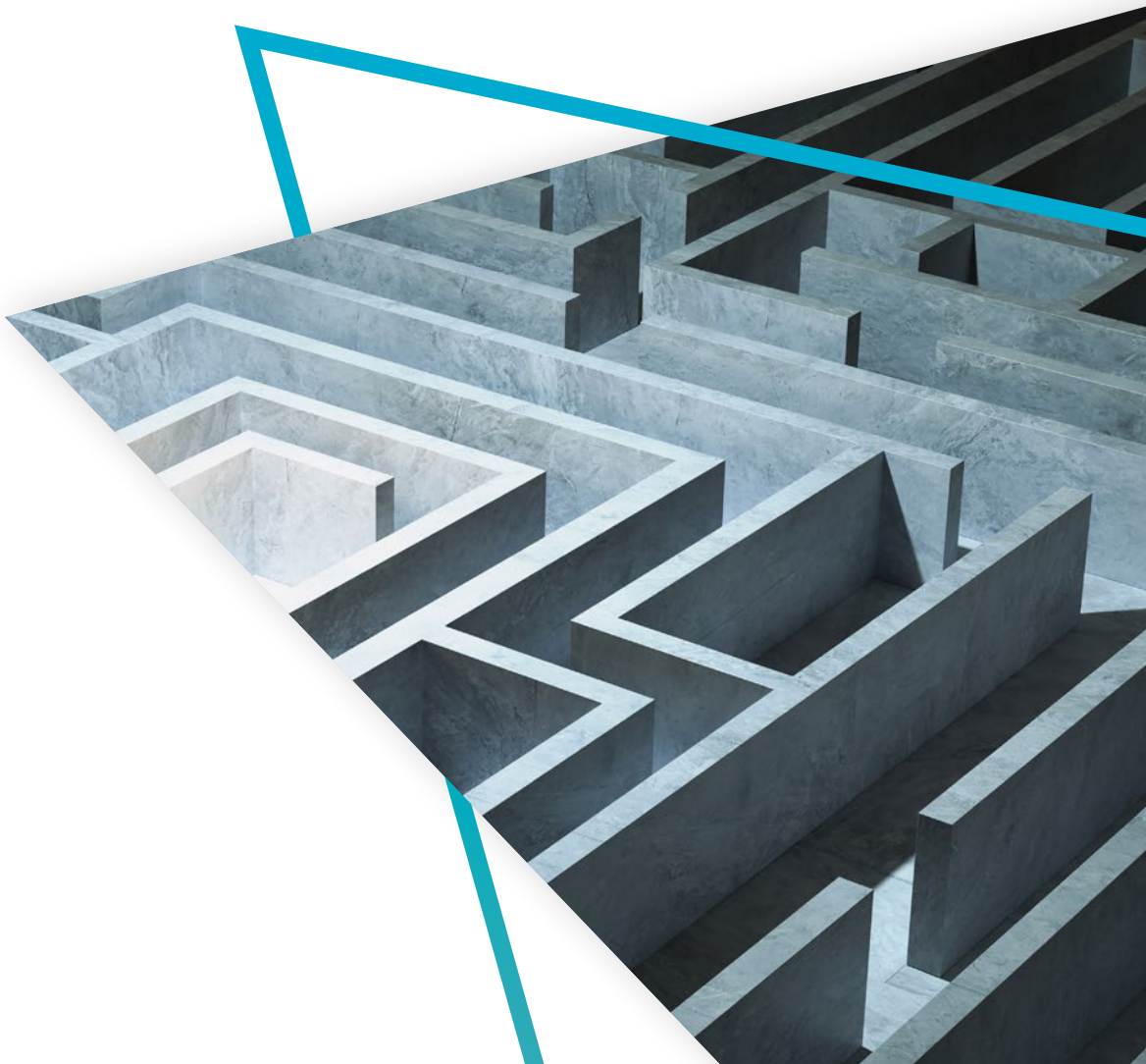
Tax & Exchange Control

ALERT | 25 January 2024

CDH INCORPORATED



In this issue

KENYA

For more insight into our expertise and services

Analysis of the Court of Appeal's ruling on implementation of the Social Health Insurance Act, 2023

On 21 November 2023, the Cabinet Secretary for Health (Health CS) officially set 22 November 2023 as the commencement date for the Social Health Insurance Act, 2023 (SHIA).

The SHIA abolishes the National Health Insurance Fund (NHIF) and establishes three new funds: (i) the Primary Healthcare Fund (PHF), (ii) the Social Health Insurance Fund (SHIF), and (iii) the Emergency, Chronic and Critical Illness Fund (ECCIF).

The draft Social Health Insurance (General) Regulations, 2024 (Regulations) which are currently undergoing public participation indicate that households with income from salaried employment will pay a monthly contribution to SHIF at a rate of 2,75% of their gross salary each month. They further stipulate that the minimum amount payable in this regard shall not be less than KES 300.

Our alert of 5 December 2023 which you can find here discusses additional features of the SHIA in detail.

High Court's ruling that suspended implementation of the SHIA

On 24 November 2023, Mr Enock Aura filed a petition at the High Court seeking various declarations, orders of prohibition and injunctions in relation to the SHIA and two other statutes. He claimed that they were invalid because their enactment did not comply with the constitutional requirement of public participation. Aura further contended that some of the sections of the SHIA were inconsistent with the Constitution.

Justice Mwita heard the petition and accompanying notice of motion ex-parte on 27 November 2023. He subsequently issued conservatory orders restraining the implementation of the SHIA until 7 February 2024.

In response, the Health CS filed a notice of motion application seeking a stay or suspension of the conservatory orders. She argued that the High Court's orders would have a significant impact on over 17 million former NHIF members, who could no longer access pre-treatment authorisation on account of the repeal of the National Hospital Insurance Fund Act, and this could potentially cause a monumental crisis within the health sector.

The court maintained its position in the earlier ruling, directing parties to comply with the orders issued therein.

The appeal

Dissatisfied with the High Court's determination, the Health CS approached the Court of Appeal (CoA). She sought a stay of implementation of the orders pending the hearing and determination of the intended appeal.

It was her case that the High Court had misdirected itself by issuing ex-parte orders against her, without giving her an opportunity to be heard. She also urged the CoA to consider the plight of patients who faced the potential suspension of their treatment till 7 February 2024.

Aura contended that the appeal was incompetent and amounted to an abuse of the court process. He argued that no evidence of a potential health crisis had been tendered. He maintained that no harm or loss would accrue as the regulations operationalising the implementation of the SHIA had not been enacted.

Analysis of the Court of Appeal's ruling on implementation of the Social Health Insurance Act, 2023

CONTINUED

The Court of Appeal's ruling

The CoA found the appeal to be arguable as the conservatory orders that the High Court had issued were too wide in scope and final in effect. The High Court had suspended three statutes ex-parte and failed to accord the respondents an opportunity to be heard contrary to their constitutional right to fair trial, and the principle of natural justice.

As to whether the intended appeal would be rendered irrelevant, the CoA considered the existence of an imminent danger to the health of millions of Kenyans who stood the chance of being denied treatment. Through its orders, the High Court had created a regulatory vacuum that would result in the inability to grant pre-treatment authorisation to former members of the NHIF.

The CoA suspended the orders of the High Court restraining implementation of the SHIA, with the exception of the following sections which remain suspended pending hearing and determination of the main appeal:

i. Section 26(5), which makes registration and contribution a precondition for dealing with or accessing public services from the national and county Governments or their entities.

ii. Section 27(4), which provides that a person shall only access healthcare services where their contributions to the SHIF are up-to-date and active.

iii. Section 47(3), which obligates every Kenyan to be uniquely identified for purposes of the provision of health services.

Conclusion

The impact of the CoA's ruling is that households with income from salaried employment will begin to part with a portion of their income each month, at a rate to be determined once enactment of the Regulations is finalised. The draft Regulations currently provide for a rate of 2,75% of an employee's monthly gross salary with no cap.

Analysis of the Court of Appeal's ruling on implementation of the Social Health Insurance Act, 2023

CONTINUED

The table below compares the amounts that will be deductible under the 2,75% rate provided for in the draft Regulations, versus the amounts that employees were contributing under NHIF:

Gross pay (KES)	NHIF deduction (KES)	SHIF deduction (KES)
20,000	750	550
50,000	1,200	1,375
100,000	1,700	2,750
200,000	1,700	5,500
500,000	1,700	13,750
1,000,000	1,700	27,500

The Ministry of Health is currently receiving comments in relation to the draft Regulations and this will continue until 9 February 2024. Thereafter, it should be clear whether the 2,75% will be the applicable rate for deductions.

Overall, we are of the view that proper implementation of the SHIA will potentially transform Kenya's health sector by ensuring equitable access to quality healthcare for all. It is noteworthy, however, that the SHIF rates appear to disproportionately focus on employed Kenyans in comparison to those in other sectors of the economy.

Alex Kanyi and Judith Jepkorir

Analysis of the Court of Appeal's ruling regarding income tax waivers issued via Gazette Notices

On 17 February 2023, the High Court declared section 13(2) of the Income Tax Act (ITA), which grants the Cabinet Secretary power to exempt certain income from tax, to be unconstitutional. The section provides that the Minister may, by notice in the Kenya Gazette, exempt from tax any income or class of income which accrued in or was derived from Kenya. Our alert of 26 April 2023 accessible here discusses the High Court's judgment in detail.

The judgment arose from a petition filed by Eliud Matindi who argued that tax waivers granted to Japanese employees, consultants, and companies on account of section 13(2) of the ITA violated the principles of equality and non-discrimination. Matindi also contended that Legal Notice No. 15 of 2021, which gave effect to the exemptions, had not been subjected to public participation contrary to Article 10(2) read with Article 118(1) of the Constitution.

Among the projects that benefitted from this tax exemption were the infrastructure developments at the Mombasa Special Economic Zone, power distribution systems in Nakuru and Mombasa, and the Olkaria 1 Unit 1, 2 and 3 plant rehabilitation projects, among others.

The appeal

Aggrieved by the decision of the High Court, the National Assembly together with its speaker (applicants) appealed to the Court of Appeal (CoA). They sought conservatory orders or a stay of execution of the entirety of the High Court's judgment and decree pending the hearing and determination of their intended appeal.

The applicants argued that the High Court's judgment would have the effect of treating every application for tax exemption to the Kenya Revenue Authority (KRA) as a money bill, to be submitted to the National Assembly for consideration and public participation. Such a situation would create a crisis at the KRA, considering the number of applications of this nature received by it each day.

The respondents' case

Matindi, the first respondent, contended that the applicants' memorandum of appeal did not disclose arguable points with a prospect of success. Further, the absence of an order staying the judgment would not render the appeal irrelevant were it to succeed.

Matindi also argued that the KRA had not recorded any difficulties in complying with the High Court's judgment. In the event that the appeal succeeded, then the taxes collected from that date would be refundable to the affected named and known Japanese companies, consultants and individuals.

Analysis of the Court of Appeal's ruling regarding income tax waivers issued via Gazette Notices

CONTINUED

The Cabinet Secretary for Treasury and the Attorney General supported the position and submissions of the applicants, while there was no appearance from the KRA, the fourth respondent.

The Court of Appeal's ruling

The CoA granted the orders of stay sought. It considered the following issues:

1. The applicants would face significant inconvenience against the public interest. This is because mechanisms would need to be put in place to effect the recovery of taxes that had been exempt for a period of over 10 years.
2. Declaring section 13(1) of the Income Tax Act unconstitutional would create challenges in obtaining tax waivers. It would necessitate the presentation of all applications for exemption before Parliament for consideration as money bills, with the associated constitutional obligations such as public participation. The CoA agreed with the applicants that Parliament was not adequately equipped to handle such a responsibility.
3. Finally, the CoA was of the view that the declarations and orders of the High Court were far-reaching and necessitated a stay.

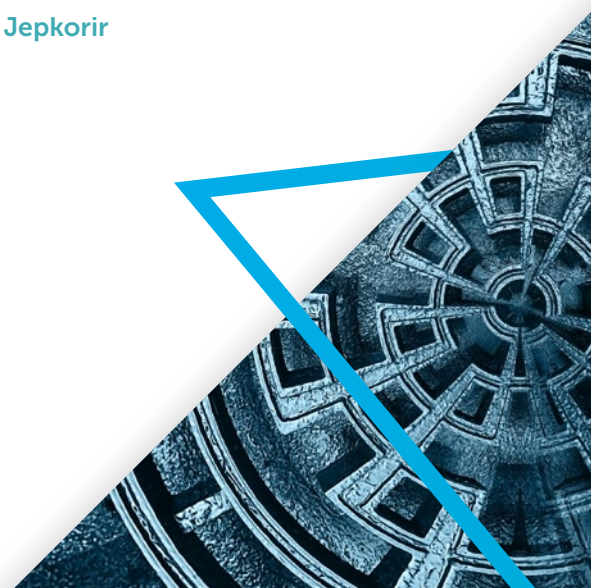
The CoA also suspended the coming into force of the High Court's declarations for a period of six months, pending hearing and determination of the main appeal.

Commentary and conclusion

The effect of the CoA's ruling is that section 13(2) of the ITA continues to operate. Exemptions that were issued to Japanese companies through gazette notices pursuant to section 13(2) of the ITA remain valid for the next six months, pending the determination of the main appeal.

It is crucial to highlight that through the Finance Act 2023, the ITA was amended to exempt from tax non-resident contractors, subcontractors, consultants, or employees involved in the execution of a project entirely financed through a 100% grant under an agreement between the development partner and the Government of Kenya. The amendment in our view does not cure the issues at the CoA because some of the projects that benefitted from the impugned tax waivers were financed through concessionary loans, not grants. We await the CoA's decision in this case.

Alex Kanyi and Judith Jepkorir



OUR TEAM

For more information about our Tax & Exchange Control practice and services in South Africa and Kenya, please contact:

Emil Brincker
Practice Head & Director:
Tax & Exchange Control
T +27 (0)11 562 1063
E emil.brincker@cdhlegal.com

Gerhard Badenhorst
Director:
Tax & Exchange Control
T +27 (0)11 562 1870
E gerhard.badenhorst@cdhlegal.com

Jerome Brink
Director:
Tax & Exchange Control
T +27 (0)11 562 1484
E jerome.brink@cdhlegal.com

Petr Erasmus
Director:
Tax & Exchange Control
T +27 (0)11 562 1450
E petr.erasmus@cdhlegal.com

Dries Hoek
Director:
Tax & Exchange Control
T +27 (0)11 562 1425
E dries.hoek@cdhlegal.com

Alex Kanyi
Partner | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E alex.kanyi@cdhlegal.com

Heinrich Louw
Director:
Tax & Exchange Control
T +27 (0)11 562 1187
E heinrich.louw@cdhlegal.com

Howmera Parak
Director:
Tax & Exchange Control
T +27 (0)11 562 1467
E howmera.parak@cdhlegal.com

Stephan Spamer
Director:
Tax & Exchange Control
T +27 (0)11 562 1294
E stephan.spamer@cdhlegal.com

Tersia van Schalkwyk
Tax Consultant:
Tax & Exchange Control
T +27 (0)21 481 6404
E tersia.vanschalkwyk@cdhlegal.com

Louis Botha
Senior Associate:
Tax & Exchange Control
T +27 (0)11 562 1408
E louis.botha@cdhlegal.com

Varusha Moodaley
Senior Associate:
Tax & Exchange Control
T +27 (0)21 481 6392
E varusha.moodaley@cdhlegal.com

Abednego Mutie
Senior Associate | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E abednego.mutie@cdhlegal.com

Nicholas Carroll
Associate:
Tax & Exchange Control
T +27 (0)21 481 6433
E nicholas.carroll@cdhlegal.com

Puleng Mothabeng
Associate:
Tax & Exchange Control
T +27 (0)11 562 1355
E puleng.mothabeng@cdhlegal.com

Brandon Otieno
Associate | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E brandon.otieno@cdhlegal.com

BBBEE STATUS: LEVEL ONE CONTRIBUTOR
Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

PLEASE NOTE
This information is published for general information purposes and is not intended to constitute legal advice. Specialist legal advice should always be sought in relation to any particular situation. Cliffe Dekker Hofmeyr will accept no responsibility for any actions taken or not taken on the basis of this publication.

JOHANNESBURG
1 Protea Place, Sandton, Johannesburg, 2196. Private Bag X40, Benmore, 2010, South Africa.
Dx 154 Randburg and Dx 42 Johannesburg.
T +27 (0)11 562 1000 F +27 (0)11 562 1111 E jhb@cdhlegal.com

CAPE TOWN
11 Buitengracht Street, Cape Town, 8001. PO Box 695, Cape Town, 8000, South Africa. Dx 5 Cape Town.
T +27 (0)21 481 6300 F +27 (0)21 481 6388 E ctn@cdhlegal.com

NAIROBI
Merchant Square, 3rd floor, Block D, Riverside Drive, Nairobi, Kenya. P.O. Box 22602-00505, Nairobi, Kenya.
T +254 731 086 649 | +254 204 409 918 | +254 710 560 114
E cdhkenya@cdhlegal.com

STELLENBOSCH
14 Louw Street, Stellenbosch Central, Stellenbosch, 7600.
T +27 (0)21 481 6400 E cdhstellenbosch@cdhlegal.com

CDH INCORPORATED