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Impact of Covid-19 Pandemic on Kenyan Tax Revenue

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Abstract

The first case of Coronavirus-19 was detected in the Wuhan city in China in December 2019. The virus first spread across the world leading to the declaration by the World Health Organization (WHO) of the disease as a Public Health Emergency of international concern on 30th January 2020, and as a pandemic on 11th March 2020. In response to the pandemic, the governments instituted various measures to either contain the spread of the virus or ameliorate its effect on the citizenry. The government of Kenya put in place three different measures to in response: fiscal policy measures, monetary measures and containment measures. Various institutions within the government including the Kenya Revenue Authority (KRA) also put in place additional measures to ensure continued service delivery. This study has investigated the effects of fiscal policy measures, containment measures and KRA's approaches to tax collection on tax revenue. The theories that underpin this study are demand and supply theory, technology acceptance theory (tam model) and Keynesian theory. The study employed a descriptive cross-sectional study design, which employs mixed methods. The study population were business entities. A questionnaire comprising of closed and open-ended questions was developed and administered to the respondents. Generally, the study found that the fiscal measures although had positive effect on the taxpayers, they had a negative effect on tax revenue. The containment measures had negative effect on the business entities and by extension tax revenue. With respect to the KRA's approaches to tax collection during Covid-19, they had mixed results. Recommendation have also been given including need for further research in the area..

Keywords: Covid-19, Tax revenue

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1. Background

Kenya has seen tremendous growth in the use of technology with internet penetration at 89.5% of the population as at December 2019. Intense reliance on technology has been noted hence causing a huge transformation in the business environment. Finance Act 2019 (the "FA 2019") amended the Income Tax Act to provide for taxation of income accruing through the digital market place. The Act defined the "digital marketplace as a platform that enables direct interaction between buyers and sellers of goods and services through electronic means.

Through the enactment of the law, Kenya joined countries such as Japan, India, Turkey and Angola, which have adopted unilateral digital tax laws. Organisation for Economic Co-operation and Development (OECD) and Group of Twenty (G20) countries have been engaging on how to effectively tax the digital economy. European Union (EU) countries such as UK and Spain have adopted Digital Service Tax (DST) of 3% on revenue earned by Multinational Corporations (MNC's) in certain digital economy sectors from activities linked to the user-based activity of their residents.

Majority of the EU countries including the United Kingdom (UK) and Spain are however awaiting conclusion on the OECD deliberations on taxing the digital economy, which will assist them in determining adequate digital presence of MNC's. Different countries and intergovernmental organizations have tried or proposed modifying definitions and interpretations of permanent establishment rules to include "digital presence" criteria.

The Kenya Finance Act 2020 ("FA 2020") inter alia introduced a Digital Services Tax (DST) with effect from 1 January 2021 payable by persons whose income from the provision of services is derived from or accrues in Kenya through a digital market place. The DST is chargeable at the rate of one point five percent (1.5%) of the gross transaction value of the service payable at the time of the payment transfer for the service to the service provider.

Through the DST, the exchequer by Finance Committee of the National Assembly anticipated to raise Kes 2 Billion in tax. DST targets both resident persons and non-resident persons with permanent Establishment (PE) in Kenya and a final tax for non-residents with no PE in Kenya. Bilateral tax treaties dictates specific criteria for what constitutes a permanent establishment (PE), but they often require a fixed, physical presence (Digital presence) within the country. PE is also defined in section 2 of the Income Tax Act and the UN and OECD Tax Convention which is universally understood to mean a non-resident person with a fixed place of business in Kenya that has existed for a period of 6 months or more or as determined under the Double Tax Agreement (DTA).

In addressing the issue of digital presence, the Kenya DST has provided a definition on user location as follows "that a person shall be subject to DST if the person provides or facilitates provision of a service to a user who is located in Kenya."

The regulations on the implementation mechanism for the tax on digital services, Digital Service Tax, 2020 (the "DST Regulations") highlight the salient features such as applicable digital chargeable services, user location, gross transaction value, tax liability, the return process, registration process and offences/penalties applicable. The DST will achieve the constitutional principle of equity by subjecting foreign players in the digital sector that have long taken advantage of the inadequacy of the traditional tax framework by paying zero or nominal tax on income derived from Kenya.

1.1 Research Focus

The greatest share of the Kenya digital economy at 85% is shared by non-PE MNC's i.e., Facebook, Amazon, Google, Netflix, E-bay, AnB among others. Policymakers argue that MNCs in the digital economy are "undertaxed" or are not paying a "fair share" of taxes in their jurisdictions of operation. Two issues that often underlie these sentiments are:

The ability of digital economy MNCs to provide services without establishing a physical presence (or "permanent establishment") in the country in which their customers reside.

The ability of digital economy MNCs to shift their profits away from countries where they conduct real economy activity (e.g., sales, development, production) toward low-tax jurisdictions where the MNCs are conducting little to no real economic activity.

Other concerns possibility of reducing tax via transfer pricing, especially where, if a country can establish the right to tax an MNC's profits in the digital economy via permanent establishment rules.

The lack of universal body that oversees administration of non-PE in the country envisages challenges in DST compliance. Despite the challenges in enforcement due to the lack of visibility by KRA on tracking digital transactions related to digital services and the inadequacy of punitive measures for non-residents without a PE in Kenya – any additional revenue collected by the exchequer is a positive step as Kenya. In addition, the DST achieves the constitutional principle of equity by subjecting foreign players in the digital sector that have long taken advantage of the inadequacy of the traditional tax framework by paying zero or nominal tax on income derived from Kenya.

Based on the above review, little empirical inquiry has been undertaken on the enforcement of the digital service tax. This study therefore sought to fill the gap by assessing measures through which digital service tax may be enforced in the Kenyan economy.

1.2 Research Objective

1.2.1 General Objectives

The overall objective of the study was to establish enforcement measures of taxation of the digital economy.

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1.2.2 Specific Objectives

To outline the gaps in enforcement of taxation of digital services in Kenya

To propose enforcement measures that will facilitate implementation of taxation of digital services in Kenya.

To identify ways of addressing challenges in taxation of digital services in Kenya

To propose regulations on taxation of digital services in Kenya based on existing Laws.

1.2.3 Research Questions

What are the gaps in enforcement of taxation of digital services in Kenya?

What enforcement measures can be implemented to facilitate taxation of digital services in Kenya?

How can Kenya address the challenges around taxation of digital services?

What regulations on taxation of digital services can be put in place based on the existing laws?

1.3 Value of the research

While several researchers have carried out elaborate studies on taxation of the digital economy and the associated challenges, no studies have been done on the enforcement of DST. It is on the basis of this, that we proposed to interrogate and establish the effective measures required in the enforcement of taxation of the digital economy.

The research established that taxation of digital economy has imposed new enforcement challenges to tax policymakers, tax authorities and governments. The challenges are attributed to complex nature of transactions carried out in the digital economy. The study identified major gaps such as difficulty in determining transactional value on income accrued or received in Kenya as harboured by jurisdiction issues in which value creation occurred. The gap can be addressed by review and amendment of Kenya's double tax treaties, mapping of IP addresses by KRA and Communication Authority of Kenya. Additionally, it is important to frame the DST around various revenue streams.

Further, considering the legal perspective, the current Kenyan concept of permanent establishment especially regarding digital tax, does not establish a taxable presence. This is because it is mainly based on an entity as being physically present or having a physical representative in the country. Therefore, it will be necessary to come up with parameters defining what amounts to a digital permanent establishment (PE) or circumstances that will trigger a digital PE in Kenya. Without a nexus, KRA runs the risk of countless challenges in addressing DST enforcement.

2. The Taxation of Digital Economy

The government of Kenya introduced the Digital Service Tax (DST) in 2021 to broaden its tax base. This move has however been graced by several challenges touching on the principle of nexus, data and characterization of transactions and income. While it is appreciated that Kenya is one of the earliest economies to embrace digital taxation, the generalizability of much published research on this issue is limited and the question still lingers that the digital service taxation needs more better strategies for addressing specific challenges in Kenya.

According to (Katz, 2015) Digital Economy can be defined as value chain comprising firms operating within an eco-system delivering content and applications to consumers and enterprises. The definition has however evolved and simplified further, currently the sector is argued to comprise of both market providers and service providers. (Katz, 2015), emphasized taxation of the Digital economy as one of the most important policy issues in today's environment. The first meeting on taxation of the digital economy held on November 1997, resolved to have OECD lead the taxation framework of the e-commerce, forming the basis of formulating ways on how to tax the digital economy (OECD, 2001). The meeting brought together government and business representatives for informal discussions on the challenges posed by global e-commerce to tax systems.

The (OECD, 2001) emphasized on the importance of Ottawa deliberations as it covers the cannons of good taxation in e-commerce among them neutrality, efficiency, flexibility, certainty, simplicity, effectiveness & fairness, however, fair challenges exist in enforcing the measures. (Katz, 2015), identified two opposing trends in digital taxation policy among them maximization of collections based on exponentially growing digital flows while the second one recognizes that lowering taxation benefits consumers and businesses, and consequently, economic growth. (Katz, 2015), maintains that the dialogue with the business community and non-members, as part of the post-Ottawa process, has proved valuable, particularly in identifying current and emerging business models and practices.

The growth in cross border e-commerce has seen easier movement of goods and services however, (OECD, 2001), argues that this new trend presents new international challenges for indirect tax authorities, therefore, underlining the need for substantially greater levels of international administrative co-operation. Recently the OECD and European Union (EU) have been spearheading engagements on universal taxation guidelines for all countries; this however has seen unexpected delays resulting to several countries adopting unilateral Digital Service Tax (DST) policies.

In his research on the digitalization of the global economy and taxation of multinational digital service suppliers (Google, Amazon, Facebook, and Apple (GAFA)), (Chris Noonan, 2020) focused on Base Erosion and Profit Shifting (BEPS) and failed to provide enforcement measures. (Chris Noonan, 2020), raises concerns on popular and political disquiet witnessed on these multinationals where they have continued to pay minimal income tax notwithstanding their enormous profits derived from doing business in other

countries. (Chris Noonan, 2020), argues that Apple and Google, earn more than half their profits outside of the USA, but pay very little income tax in the so-called market jurisdictions or market states. The market states for digital services naturally wish to expand their national tax bases to get their 'fair share' of tax revenue from non-resident digital service suppliers (Chris Noonan, 2020).

2.1 Gaps in Enforcing Digital Service Taxation in Kenya

A number of reports from audit firms in Kenya have depicted negative perception on the newly implemented DST. Delloite and KPMG have opined that the new amendments are rudimentary and have equivalent double taxation for those using the digital platform. They believe that new tax laws will be burdensome to consumers and operators of the platform; particularly where VAT is placed in online supplies (Guyu, 2019) with this in mind, the Act poses several challenges, as highlighted below.

First, there were no clear guidelines on how the new changes to the Income Tax Act and VAT Act will be subsequently applied as argued by (Sigadah, 2018). The amendments have not ascertained who between the buyers and the seller in the digital platform bears that tax burden. For example, should the new VAT provisions place the consumers' tax incidence, it will inevitably stifle innovation and take away the same incentive to operate in the digital marketplace. It should be noted that the digital market space has been a more cost-effective way of carrying on business operations for a long time.

Second, huge population of Kenyan youth, due to unemployment, have turned to the digital market space to reduce the operating costs of their start-up business. The new tax amendments will cause flight from the digital market space, which will in a huge way affect the growth of start-ups, including small and mid-size enterprises in the country. The new tax amendments could endanger cross-border trade and investment. The new provisions do not speak to the effect of corresponding to the international tax regime. This poses a great challenge to foreign investors who will ultimately face double taxation on the same income. If not addressed, this could stifle cross-border trade and thus there is need to update existing tax treaties.

Third, Lack of defined territorial boundaries for digital players will pose a challenge in collecting or implementing these new provisions. Digital players are constantly evolving. This poses a significant challenge to legislators, who now have to think along the international tax agreement lines.

Fourth gap is on administration. For Value Added Tax (VAT), the amendment states that the tax will be chargeable on goods and services sold to Kenyan resident customers in the digital market space. The reasoning behind the provision is that the supply of the good or service has taken place within its jurisdiction and the equally consumed locally. Besides, the amendments state that income earned on goods or services sold and provided by non-residents to Kenyans is income derived in Kenya, and therefore, the same should be declared and taxed in Kenya. Implementation of these provisions will be difficult because of the lack of presence of these non-resident suppliers in Kenya. According to (Sigadah, 2018) Administrative challenges arise for the Authority in enforcing and collecting of tax from such transactions.

Firth, the amendments made by the Finance Act also did not consider the intangible nature of transactions conducted through the digital platform. The new provisions place a massive burden on Kenya Revenue Authority to monitor all transactions taking place in the platform and equally difficult task to identify Kenyan entities ideal for appointment as digital tax agents. Should the Authority choose to bring non-residents to compliance for goods and services sold, several challenges need to be addressed through withholding tax. It should be noted that transactions within the platform are online. Therefore, a consumer in Kenya cannot withhold tax on payments for goods or services received online when in the real sense, the price displayed on the good or service has not factored in Kenya local taxes and the goods and services are delivered upon confirmation of full payment by the customer.

Sixth, enforcement of these new tax provisions on consumers and providers of goods and services in the digital marketplace will be difficult. In his report on digital taxation (Ngeno, 2020) Argues that Revenue Authorities have no power whatsoever to compel non-resident suppliers to charge VAT on their goods or services to Kenya's consumers. He (Ngeno, 2020) further alluded that this would pose, and for countries who have tried, it has posed diplomatic wrangles. Another challenge posed is that goods sold by non-residents are imports, which follows that non-resident suppliers cannot charge VAT on exports. Should they take this route, they will be an incomplete breach of the "destination principle" adopted as the best practice by the OECD VAT Guideline.

Revenue Authorities can only compel residents into paying VAT on imported goods. This shift the tax burden from the targeted non-residents. The tax burden shifted to resident consumers becomes burdensome because they cannot negotiate on commodities purchased online. Prices are, in most cases, fixed. On the other hand, such an action will in a huge way increase the cost of goods or services to the end consumer in Kenya. (Ngeno, 2020) Further, explicates a possibility of posing a challenge of over-taxing non-residents suppliers who could potentially have customers across the globe. This will stifle foreign trade if all jurisdictions decide to tax the non-resident suppliers (Ngeno, 2020).

Seventh, non-resident persons without a permanent establishment in Kenya, registers for the DST obligation, files but fails to remit the taxes to the Revenue Authority and is out of the jurisdiction. According to research by (Delloite, 2020), there are currently no measures in place to enforce compliance in payment. The auditing firm argues that being a new form of

taxation in Kenya and, indeed, in many parts of the world, it is expected that the implementation and enforcement of DST is likely to face some challenges but with continuous refinement and aligning to best practices, the hurdles should be overcome in the long run (Deloitte, 2020).

2.2 Challenges on Digital Economy Taxation

The Organization for Economic Co-operation and Development (OECD) developed a report on Action 1 Base Erosion and Profit Shifting (BEPS), this was used to develop and identify the tax challenges of the digital economy. In contrast to the findings, OECD failed to establish a feasible approach for addressing the challenges in the digital economy's broader problems. Further (OECD, 2015), committed to reconsidering digital economy taxation in 2020 and proposed that countries adopt the proposed solutions while still respecting any existing treaty obligations. In order to address the possibility of broader tax issues raised by digitalization, a reasonable approach was led by the Task Force of the Digital Economy (TFDE) in developing a framework on potential options addressing the tax challenges of the digital economy.

Similarly, the European Union (Athanasaki, 2018), proposed implementation of two directives focusing on Digital Presence Directive and the Digital Services Tax Directive, and recommendation focusing on the Digital Presence Directive. This mainly aimed at restoring taxation to both business and residency jurisdictions (thereby minimizing stateless income).

The (OECD-iLibrary, 2018) published an Interim report on potential options analysed by the Task Force on the Digital Economy (TFDE) including taxing nexus in the context of significant economic presence for instance a virtual Permanent Establishment; a withholding tax on some forms of digital transactions; an equalization levy and specific rules targeting large multinational companies.

Further, the OECD/G20 Inclusive Framework on BEPS adopted a Work Program in May 2019, laying out a framework for reaching a global consensus on how to resolve the arising tax challenges posed by digitalization (OECD, 2019). The OECD released a policy note that divided potential solutions into two complementary pillars (OECD, 2020), followed by a public consultation paper. The policy note highlighted that Pillar one focused in addressing the broader challenges of the digitalization of the economy and allocation of taxing rights having a new nexus rule independent of physical presence; to go beyond the ALP, while Pillar Two addresses remaining BEPS concerns by introducing a minimum tax rule.

2.2.1 Measures of Addressing Challenges in Digital Taxation

The OECD has been on the forefront in providing guidelines and thus providing recommendations to mitigate the challenges of the digital taxation. The Task Force (OECD-ilibrary, 2014) considered Ottawa convention framework principles such as Neutrality, Efficiency, Certainty and simplicity, Effectiveness and fairness and Flexibility. As previously stated, pursuant to (OECD, 2015) the criterion on unilateral measures discussed by the Task Force on the Digital Economy (TFDE) are divided into different categories.

First criteria are based on introduction of a new nexus based on significant digital presence. This provision provides for countries to create an alternate nexus to resolve circumstances where certain business operations are performed entirely digitally with no Permanent Establishment (PE) in country of jurisdiction. In addition, (OECD-ilibrary, 2014) argued that PE should cover an enterprise engaged in “fully dematerialized digital activities” deemed as only if they exceeded certain thresholds which could include digital footprints such as the number of active accounts/users for social platforms and number of visitors to respective websites among others.

Additionally, companies engaging in completely dematerialized digital activities should be considered to have a Permanent Establishment if they meet certain revenue thresholds, which will entirely affect the business country's digital economy. A number of experts agree that the focus should be on the extent of the thresholds rather than whether economic presence is a fair norm based on factors such as number of contacts, number of visitors to websites, and the existence of a user base in the subject market country to resolve administrative concerns. In this regard, certain countries have incorporated digital or online factors into permanent establishment threshold, for example, Slovakia Republic in the year 2018 expanded definition of permanent establishment to include certain online platforms.

The Second criteria focuses on replacing Permanent Establishment with significant presence. Potential option proposed in OECD public comments reports indicated the need to replace the existing Permanent Establishment concept with a “significant presence” test. Theoretically, views of scholars have argued that the existing PE concept needs systemic changes to meet the emerging digital economy business models. For instance, Nigeria’s Finance Bill 2020 signed into law the principle of significant economic presence to the basis of taxation of non-resident companies operating in the digital services and e-commerce sectors.

Third criteria focuses on broadening the scope of withholding tax which includes expanding the definition of Royalties among other exception to the Permanent Establishment rule under which the taxing right is allocated to the source rule to include digital products and services. Countries like Greece, Philippines, Malaysia (active from 2016, 2003 and 2017 respectively) have relooked into the recognition of payments for the right to use software virtual images, or sound transmission as Royalties.

Proposing withholding tax on all base-eroding payments made by citizens of a country for digital products or services rendered by a foreign provider, serving as an option will only be effective when consideration of withholding on payments by residents depending on the taxpayer's position, the jurisdiction where the asset is used, or where the service is given from non-resident providers. In addition, adoption of Withholding tax on technical service fee as outlined by (Alessi, 2018) noted increasing number of countries, adopting exceptions to the Permanent Establishment threshold for certain service fee in their domestic law and/or double tax treaties. This outlines a provision of allowing a withholding tax on a gross basis in the source country when the payer is resident in that country.

Studies done by (Rukundo, 2020) points to the facts that for African countries to address digital taxation challenges there is need for an equitable approach that targets digital MNEs while not impeding the growth of local businesses such as setting high thresholds that only foreign digital Multinational Enterprises are likely to reach. Some countries have adopted recommendation including turnover taxes by introducing an equalization levy. The levy is intended to address disparity in tax treatment between foreign and domestic businesses where foreign business have sufficient economic presence in the jurisdiction as outlined by (OECD, 2018). This implies the equalization levy applies only when a Kenyan resident advertiser (including a taxable Permanent Establishment held by a non-resident) makes a payment to a non-Kenyan resident supplier for an online advertisement, the provision of digital advertising space, or any other service or facility that enables online advertising. Countries such as India in year 2016 amended its domestic tax law to introduce an "equalization levy" as a gross-based tax or equivalently a turnover tax limited to revenue from online advertising supplied by non-residents as efforts to address the tax challenges of the digital economy.

Fourth criteria, focuses on specific regimes targeting a unified approach, the OECD Secretariat published a proposal (OECD Secretariat, 2019) restoring a balance of power in advance international negotiations between tax authorities and highly profitable multinational enterprises (MNEs), including digital companies, to pay tax wherever they have significant consumer-facing activities while generating their profits. Multinational enterprises exist in large part because these interactions generate more income than separate domestic firms interacting at arm's length. While it is appreciated in other countries multinational and other associated companies are required, at least for tax purposes, to match their transfer prices for cross-border internal transactions with market prices under the ALP.

Further (Rukundo, 2020) argues that African countries compliance on MNE's can be addressed through collective action by having a single registration point, return filing hence payment may be easier for digital Multinational Enterprises (MNE's) rather than them having to do this separately in each of the 54 countries in Africa. Some countries have enacted new regulations or introduced specific anti-abuse rules to address excessive use of base eroding payments aimed directly at multinational corporations in order to ensure taxes are collected where revenue is generated and profit shifting is avoided. In the case of Australia's multinational anti-avoidance law (MAAL), adopted in December 2015, Permanent Establishment anti-avoidance rule is limited to non-resident companies belonging to large Multinational Enterprises. Studies done by (OECD-iLibrary, 2018) revealed U.S. base erosion and anti-abuse tax (BEAT) adopted in 2017 which looks at domestic companies or permanent establishments members of a Multinational Enterprise group whose activities in the United States exceed a high revenue threshold over a three-year period. In addition, the tax payer is entitled to make "base eroding payments" under the legislation this includes any amount paid or accrued by the taxpayer to foreign related parties for which a "deduction is allowable" (OECD-iLibrary, 2018).

Critically analysis identifies the nexus aspect of tax should not be understated or either overstated. Nonetheless, large amounts of sales can be generated without a taxable presence being understated or raising pertinent questions. This is because, until now there has been no consensus on a multilateral approach to address the challenges in digital taxation however some countries have taken uncoordinated and unilateral measures. The OECD member countries' aim is to address the political and technical issues surrounding these tax challenges by mid-2021, and to bring the process to a successful conclusion (Ernst & Young, 2021).

(Rukundo, 2020) contends that African countries will need to investigate and develop ways to address challenges of taxation of the digital economy in their unique way because the administrative challenges that African countries tax administrations face vary from those of the more developed OECD countries. The study offers a holistic review that encouraged African countries to develop its own multilateral approach and to participate in the multilateral discussions on the reform of international taxation needed to address the challenges of the digital economy.

2.3 Digital Service Tax Enforcement Measures

In 2018, (Bird and Bird LLP, 2020) due to slow progress at OECD level, the European Union (EU) proposed two directives for taxing the digital economy, short-term measure that would impose a tax on revenues for companies with worldwide revenues over €750m and EU revenues over €50m (Simmons & Simmons, 2018). The second proposal was a long-term measure that sought to introduce the concept of 'significant digital presence' to determine EU tax requirements. (Bird and Bird LLP, 2020), envisaged that the first short term measure would be a filler initiative before the

longer term and more 'contentious' proposal was agreed among Member States. Despite various attempts to reach agreement, EU Member States were unable to reach a compromise on either the short or the long-term proposals.

A number of EU members came up with different Unilateral Digital Service Tax (DST). The UK Government however introduced its DST in the year 2020, but on the other hand committed itself to finding a solution at international level. However, the Act does not include a specific 'sunset clause' that would automatically withdraw the legislation. Rather, it gave some flexibility by stating that it will dis-apply the DST 'once an appropriate international solution is in place' and carry out a review in 2025. Spain DST provides an indirect tax that would not fall within the scope of Double Taxation Treaties signed and entities which meet the following requirements: (i) net revenues during the prior calendar year exceeding €750 million, and (ii) the total value of revenue derived from the development of the activities will be subject to DST in Spain exceeds €3 million. However, there is scanty information on the enforcement measures taken by Spain.

The challenges facing OECD are opined on the political will and number of outstanding issues including double taxation where concerns on whether there will be a need to revise the double tax treaties and its feasibility? Other issues include tax refund mechanism and the role of the tax authorities, if the rules will fit together (Controlled Foreign Corporations (CFCs) and Global Intangible Low-Taxed Income (GILTI) and the mechanism to replace the unilateral measures.

On the issue the lifespan of the unilateral tax measures, several countries have given different conflicting answers (TMF Group, 2020). While some countries like the France, Spain and Italy confirmed that the unilateral measures are intermediary and will be replaced by OECD regulations once consensus has been reached. The UK on the other hand only confirmed to review its DST measures by the year 2025. However, the DST measures have received wide objections from the US government particularly threatening tough measures on products France.

The OECD October 2020 as outlined by (TMF Group, 2020) proposed specific revenue threshold to be applied for country-by-country reporting. However, some countries have implemented DST deviating from this rule Revenue thresholds. (TMF Group, 2020), further argues, the more different thresholds are used for the various reporting requirements, the more challenging it will be for companies to keep track of them and to be compliant.

Some of the enforcement measures taking shape around the world include disclosure obligations, enhanced information sharing and increasingly aggressive enforcement strategies (Cleary Gottlieb, 2021). The EU and the UK introduced mandatory disclosure regime, known as DAC6, which require intermediaries (including tax advisers, accountants, lawyers and banks) that establish or advice on certain kinds of "cross-border arrangements" to provide extensive information about those arrangements to local tax authorities. Germany, Austria and Finland compliance approach as outlined by (Cleary Gottlieb, 2021) relies on intermediaries' reports and taxpayers for enhanced information sharing among tax authorities and wide-ranging follow-up information requests.

In order to enforce DST compliance France adopted alignment of impacted business, the administrative reporting and compliance framework of the DST tax with the existing VAT framework. In Italy, (Maisto, 2021) the enforcement measures are that non-resident entities, which in the course of a calendar year fall within the scope of DST, but lack a permanent establishment in Italy or a VAT number will have to request a DST identification number from the Italian Revenue Agency. Further, (Maisto, 2021) if a non-resident has an affiliate company in Italy, the affiliate will be jointly responsible for compliance with the group's DST obligations. Further, DST is not, in principle, deductible from income.

However, several countries have adopted the OECD recommendation on threshold concept they have set different values as follows (KPMG, 2020); United Kingdom 25M Pounds for UK revenue and 500 M pounds for worldwide revenues, Australia has set the bar at AU$75,000 ($53,500), while India talks about 500,000 rupees ($6,750). In Italy and France, revenue is measured at both local level and group level, with different thresholds for each; 5.5 million euros ($6.5 million) for revenues incurred in Italy, 25 million euros for revenues incurred in France and 750 million euros revenue for the total worldwide amount. Hungary goes as low as 344,000 euros.

2.3.1 Digital Service Tax Compliance Measures –Kenyan Perspective

Kenya has made strides towards large-scale technological and digital developments over the last two decades, and it now ranks third in Africa. Study done by (Ng'eno, 2020) indicates Kenya's population as having high inclination to online services, including betting, borrowing, and online purchases. The government's intention cited to Kenyans through a declaration by the Kenya Revenue Authority way back in 2018 at its annual summit. The Government of Kenya introduced taxation of the digital market space through the Finance Act of 2019. The Act amended provisions of the Income Tax Act and Value Added Tax Act to enable the government tax goods and services supplied in Kenya's digital market place with effect from 7 November 2019. (Latif, 2019) Argues that, although the government's decision is a step forward to increasing revenue, there need to be legislative and the administrative framework changes to implement the law effectively.

Kenyan Digital Service Tax (DST) set out several raft measures aimed at ensuring players in the digital economy

observes. Some of the measures despite having fair challenges include defining both permanent and non-permanent establishment, providing registration process, providing a clear and simple DST system. (TMF Group, 2020), maintains that the unilateral measures enforce a revenue tax rather than an income tax, therefore companies cannot benefit from the tax losses and cannot benefit from tax credits. The Kenyan DST regulations further stipulates that double tax treaties apply only to income tax and the DST will not be in scope. However, (KPMG, 2020) observed that digital services payments to countries that have income tax treaties with Kenya will not be subject to digital services tax, given the reliance on the concepts of residency and permanent establishment as a basis for determining the jurisdiction with the taxing rights (KPMG, 2020).

Further (KPMG, 2020), raised concerns on the lack of a turnover threshold for the Kenyan DST, alluding to significant administrative burdens for companies with “low value” transactions. The OECD (TMF Group, 2020) in its digital economy taxation perspective argued that provision of turnover threshold, as basis for taxation will bring equity amongst players in the sector. On the issue of tax base, (KPMG, 2020) argues that there are debates around the accounting standards to be applied and around the way in which losses are going to be allocated and accounted for. This further is asserted by (Bloomberg, 2020) who argues that the discussion is around whether to apply the accounting standards of the parent company or the local one.

According to Kenyan DST regulations 2021, user of digital services will be deemed to be located in Kenya, if; they pay for the service from a financial institution in Kenya, they access the service from an IP address in Kenya, they access the service using a device in Kenya and their billing or residential or business address is in Kenya. If a user meets any of the four proxies, (CIO, 2021) then the income derived from the service provided to that user will be subject to DST in Kenya. (Cleary Gottlieb, 2021) in October 2020 (OECD) introduced new proposed nexus and profit allocation rules to ensure that multinational companies (including digital companies) pay tax wherever they have significant profit-making consumer-facing activities.

In determining the right place for paying the right tax (TMF Group, 2020) alludes the debate is not whether companies pay the right amount of tax but whether they pay it in the right jurisdiction. The approach is to tax the income in the country where consumers or users are located, rather than the country of residence. While (Cleary Gottlieb, 2021) clarifies the need for a different taxation of the digital economy and the need to move away from the “physical” nexus. (Bloomberg, 2020), claims the definition of the new taxation world is still under debate because it needs to ensure tax neutrality, to facilitate a fair trade and to avoid the implementation of discriminatory taxes.

2.3.2 Transfer pricing in the digital economy

While analysing business trends in relation to taxation (Katz, 2015) noted that Facebook and Google employ similar strategy of a centralized processing operation. The operation model involve deploying offices around the world with staff in charge of selling advertising and providing technical consulting to its customers (Katz, 2015). The sales are not logged locally but remotely in subsidiaries such as Google Ireland in the case of Google. If you consider the permanent establishment rule, the operator will not pay taxes in the local country where the acquisition of digital ads is conducted. The rationale is that the sale actually occurs in the remote subsidiary where the purchase is logged.

(Katz, 2015) further argues that remote subsidiary does not necessarily pay taxes at the local tax office; the revenues received from customers located in each country are transferred in the form of royalty fees for intellectual property to another subsidiary, which in turn is transferred to tax haven. The resulting arrangement minimizes the income tax paid by the local office. According to (Katz, 2015), Google revenues from France, Germany, and the United Kingdom in 2012 were estimated at approximately $9B generated by digital advertising sold to local customers. Of this amount, the three country subsidiaries reported $1.28B in revenues and $33M in income tax.

In the year 2014, (Katz, 2015) Netflix had 53 million worldwide subscribers, of which 66% are located outside the United States. The company objective is to generate 80 per cent of revenues from international subscribers, which compels aggressive expand in all continents (Katz, 2015). The city of Buenos Aires imposed a 3% gross income tax on all foreign online subscription services, including video, music and games (Katz, 2015). This target streaming services and relies on credit card companies acting as tax withholding agents for the purpose of tax enforcement. Rather than taxing consumers (Multiples Group, 2018) maintains that, the objective is to collect taxes from digital content distributors that do not pay any corporate taxes in Argentina. The law also stipulates the tax cannot be passed to consumers.

In order to reduce tax liabilities, (OECD, 2001) global players tend to segregate taxable income from the activities that generate it. The approaches to reduce taxation include avoiding taxable presence in certain markets by shifting gross profits from the market where the good is being offered to subsidiaries located in tax havens or low tax environments, keeping withholding tax low or nil at the source, by shifting profits in the form of royalties or interest to a lower tax jurisdiction. Lastly by avoiding taxation of low-tax profits at the level of the parent by searching for preferential domestic tax regimes.

In dealing with this situation, (Katz, 2015) suggests that governments need to consider three trade-offs. The first issue is to assess from a cost/benefit standpoint the fact that the

resulting low taxation enhances adoption of digital goods and services against the fact that by shifting liabilities away from income producing locations (Katz, 2015) other taxpayers need to bear the burden. The second issue to deal with is unfair competition (Katz, 2015). Local digital players according to (OECD, 2015) when paying the corresponding taxes based on their location will have to compete with global players offering the service at an economic advantage. The third issue to consider is taxation asymmetry in regards to other firms of the digital eco-system (Katz, 2015).

The limited availability of information on who has consumed a specific digital good or service becomes an obstacle to collect taxes in an effective manner as observed by (Katz, 2015). Further (Katz, 2015) argues that globalization exacerbates this problem insofar that it is difficult to locate information of who are the consumers that have purchased a good stored in a server beyond the frontiers of a given country. (Katz, 2015), maintains that in the City of Buenos Aires; Netflix, Apple TV, Spotify and others had no operation offices in Argentina with servers capturing information on subscribers. In this case, the biggest challenge was on collection of information for administering the tax collection activities this was resolved by relying on credit card issuers. The purchase of subscriptions was paid through credit card therefore; it was easier for the government to make these companies key point of information gathering.

This option however, solved the information-gathering hurdle, but did not address the tax collection obstacle as further highlighted by (Katz, 2015). In the purchase of physical goods, collection of sales taxes becomes the responsibility of the place of purchase. In the Argentina, case (Katz, 2015) the provider of the service was located beyond its borders. Therefore, (Katz, 2015) a system dependent on streaming service providers for collection and remitting taxes and levies was not cost effective hence opting to rely on credit card issuers. When a consumer pays for a subscription on his or her credit card (Katz, 2015) notes that the digital operator collects the tax and delivers the amount collected to the authority hence addressing the collection barrier.

This however, raised consumer privacy violation. According to (Katz, 2015), cluster consumer advocates argued that the act of collecting, storing and delivering information of digital good purchases private of a citizens is an infringement of their privacy. In the identification of country of residence, companies rely on either the IP address or the location of the consumer's computer, or the address of the credit card used to purchase the subscription.

Large Corporation have billing systems and therefore, (Katz, 2015) ability to track information and collect taxes. Furthermore, (Katz, 2015) argues that large corporation do not like exposure to reputational conflict especially on tax avoidance. The emergence of small and medium firms offering Internet-based services such as electronic commerce, social networking, matching platforms, etc.). According to (Delloite, 2020) this leads to the emergence of an informal economy where the government faces more difficulties in collecting taxes. If the informal sector of the economy represents around 50 per cent of the GDP, as is the case in many countries in the world of emerging market economies, tax revenues coming from small digital operators tends to be limited.

Chapter Three: Research Design and Methodology

This chapter will be structured to provide a detailed review of the research design, the area of study covered, data sources and methodology relied in the research.

3. Research Design

This research employed a mixed type of methods. The first part of the study consisted of a series of well-structured questionnaires (for tax experts, digital service/market place providers, consumers, KRA staff, and technician of different industries affected) and semi-structured interviews with key stakeholders (DST Project team, Auditing firms and industry providers) in participating organizations. The other design was use of interview of willing consumers, ICT practitioners and tax auditors to know how they feel about digital service tax enforcement in Kenya.

This study employed a descriptive research design to agree on the gaps in the Digital Service Tax Act, challenges facing digital economy taxation and effective enforcement measures applicable. (Saunders, 2012) Descriptive research portrays an accurate profile of persons, events, or situations. This design offers to the researchers a profile of described relevant aspects of the phenomena of interest from an individual, organizational, and industry-oriented perspective. The research design enabled the researchers to gather data from a wide range of respondents on digital service tax enforcement in Kenya. This will help in analysing the response obtained.

To address the key research objectives, this research used both qualitative and quantitative methods and combination of primary and secondary sources. The qualitative data supports the quantitative data analysis and results. The result obtained was triangulated since the research utilized qualitative and quantitative data types in the data analysis. The study area, data sources, and sampling techniques are as discussed below.

3.1 The study area

According to (Fraenkel, 2000) studies, population refers to the complete set of individuals (subjects or events) having common characteristics in which the researcher is interested. The population of the study was determined based on random sampling system. This data collection conducted from April 07, 2021 to May 15, 2021, from selected tax experts, digital service/market place providers, consumers, KRA staff, and industries affected. The digital service and market place providers were selected based on their geographical coverage, employee number, established year, and the industry type even though all criterions were difficult to satisfy.

3.2 Data sources

3.2.1 Primary data sources

It was obtained from the original source of information. The primary data is more reliable and have more confidence level of decision-making with the trusted analysis having direct intact with occurrence of the events. The primary data sources are industries' perception on DST enforcement measures (through observation, pictures, and photograph) and industry employees (management and bottom workers) (interview, questionnaires and discussions).

3.2.2 Secondary data

Desk review was conducted to collect data from various secondary sources. This includes reports and project documents at various digital service providers. Secondary data sources have been obtained from literatures regarding digital economy taxation, and the remaining data from the companies' manuals, reports, and some management documents. Reputable journals, books, different articles, periodicals, proceedings, magazines, newsletters, newspapers, websites, and other sources were considered on the digital economy taxation. The data also obtained from the existing working documents, manuals, procedures, reports, statistical data, policies, regulations, and standards were be considered for the review.

3.3 Analysis Methodology

The quantitative approach was used in this study. In this study a combination of random and purposive sampling was utilized. Data was collected using questionnaires. Data analysis was conducted after collection of data. Quantitative data collected was captured in Microsoft Excel format and cleaned. The cleaned data was then exported to statistical analysis software, SPSS, for an in-depth analysis. Data presentation went beyond basic descriptive statistics, but showed the relationship between variables, present data in form of frequency tables, graphs and pie charts which was used in the presentation of findings.

4.1 Demographic Characteristics

Demographic characteristics of respondents that participated are presented in Figure 1. The majority (87.7%) of respondents are Kenyan resident, (5.1%) are Kenyan resident not living in Kenya, (2.6%) are Non Resident with no Permanent Establishment in Kenya and 0.5% are Non Resident with a Permanent Establishment in Kenya.

Figure 1: Taxation Residency

In terms of qualification and occupation, the majority (37.9%) are in tax profession, (34.4%) indicated that they are public servants, (3.6%) business person, (2.1%) civil society, (5.6%) private sector employee, (5.6%) Tax professionals and civil servant, (1%) business person and tax profession, others are 3.1% and missing responses accounted for 6.7% of the total responses. It was also observed that majority of the respondents representing all fields under study had the requisite qualifications to give a credible opinion This indicates that conclusions drawn from these sectors represent fair opinion regarding perspectives in digital taxation as indicated in Figure 2 below.

Figure 2: Respondents Professionals

Regarding the respondents' space in the digital economy, the majority (63.1%) of respondents were tax profession, 4.1%, 4.6% and 1.5% are digital market place provider, digital service provider and digital and digital service providers respectively. Whereas 9.2% of the respondents are users of digital services as shown in figure 3 below.

Figure 3: Respondents space in digital economy

This question was asked to assess respondents' knowledge about DST. Regarding the respondents' awareness of the introduction of Digital Service Tax (DST) through the Finance Act 2020 (FA 2020). The majority (91.8%) of respondents are aware of the enactment of the digital service tax in Kenya, 6.7% are unaware and 1.5% did not answer. This indicates that conclusions drawn from this study is reliable given that more than 90% of total respondents are aware of the introduction of DST as shown in figure 4 below.

Figure 4: Respondents Knowledge/awareness of DST

On the question of, if the Kenyan Unilateral Digital Services Tax (DST) is a good tax policy?

The first objective of the study focused on assessing respondents' views regarding Kenyan Unilateral Digital Services Tax (DST) as being a good tax policy or not. The majority 81% view Kenyan unilateral digital service tax as being a good tax policy whereas 16.4% viewed it as being not a good policy and 2.6% did not respond to this question as shown in figure 5 below.

Figure 5: awareness of the introduction of DST

4.2 Gaps in the enforcement of DST in Kenya and measures to address.

On gaps existing in the digital economy taxation, 22.4% of the respondents' view determining the actual transaction amount as the biggest gap, 15.27%, accounting of DST, 13.85% of respondents agreed that determination of taxation point is gap. Additionally, 13% of respondent agree that DST does not address transfer pricing/profit shifting while 10.39% agree on mandatory registration of digital service/market providers as a good measure in enforcing revenue collection in the sector. Whereas 8.9% of respondents' view that Gross Transaction Value negates apportionment of income where the digital service is offered to users located both in Kenya and outside Kenya, 8.9% of respondents agree that the flat rate tax of 1.5% does not create equity in taxation, 0.2% stands abused due to treaty shopping by multinational corporations. All respondents agreed that there are gaps in DST and no one respondent to the No gap category. The proportionate respondents are as shown in figure 6 below.

Figure 6: Gaps existing in the enforcement of DST

Regarding enforcement measures in taxation of the digital economy, the respondents were asked what are the most

important factors to consider in the enforcement of digital tax. 23.22% of the respondents indicated that it is important that avoiding of double taxation be considered in enforcement measures, 21.17% of respondents viewed that creating a clear and simple system should be considered. Additionally, 20.7% of the respondents expressed that taxpayer education and sensitization as an important factor to consider in the enforcement of taxation of digital economy and 15.17% of respondents called for creation of a level playing field between traditional and digital companies as a factor to be considered in the enforcement of digital taxation. The proportionate percentage responses are as shown in figure 7 below.

Figure 7: Measures to be considerations in the enforcement of DST

In regards to tax avoidance majorly by multinationals the respondents deemed it necessary to be addressed for effective enforcement of the digital economy taxation. Various ways in addressing this tax avoidance were assessed by respondents. 23.22% of respondents agreed that there is need to avoid double taxation, 21.17% view that there is need of creating a clear and simple system, 20.7% view taxpayer education as key and 15.17% agreed that there is need to create a level playing field between traditional and digital companies.

Figure 8: Addressing Tax Avoidance challenges

The research sought also to find ways and means of addressing challenges in digital taxation in Kenya. The responses were as follows: the majority 30.5% of respondents indicated that Improved stakeholder engagement as important in achieving compliance while 26.4% recommended the use of technologies such as Artificial Intelligence (AI). Consequently, 25% of respondents recommended Strengthening of the current DST to bring more digital services on-board, particularly it was noted the cryptocurrency trading and e-cigarettes among others have not been captured in the current DST scope. 13.1% of respondents recommended changes to the corporate tax rules, keeping the arm's-length principle.

Figure 9: Addressing tax avoidance in DST

4.3 Regulations changes in the enforcement of DST

Regarding Multilateral approaches to taxation of the digital economy, targeting Multinational Corporations (MNEs) the majority 35% of respondents indicated that using of tax representatives/ agents as the best enforcement measure. 34.07% indicated the Use of 'user IP address mapping', 29.3% recommended using special registration numbers for entities outside Kenya and 1% of respondents recommended taxation at source for multinational cooperation's as shown in figure 10 below.

Figure 10: Taxation of multinationals without permanent establishment in Kenya

Regarding addressing determination of the user location in digital tax in Kenya. The majority 41.13% of respondents indicated that using of user IP addresses as the most appropriate enforcement tool in addressing determination of user location, 33.58% of respondents recommended the use of point of payment approach. 23.77% of respondents recommended an approach of using Place of supply or recipient approach and only 1.5% of respondents suggested the use of payment gateway (tax at source) as shown in figure 11 below.

Figure 11: Determination of user location in DST

On the issue of Kenya's description of permanent and non-permanent establishment in the enforcement of DST. 37.6% of respondents agreed to the statement that an entity qualifies for permanent establishment if it has physical presence or a physical representative in Kenya. Additionally, 26.1% agreed to the statement that the use of 'user IP address mapping' will address the issue of tax point between jurisdictions while 23.3% agreed the use of revenue threshold (Amount earned) be used in determination of if an entity has generated taxable income within a jurisdiction. The rest 13% agreed to the statement that the Kenyan definition of permanent establishment will not establish taxable presence as shown in the figure 12 below.

Figure 12: Description of permanent and non-permanent establishment in Kenya reference to DST.

4.4 Challenges in operationalisation of the DST regulations

The research also sought to identify challenges likely to occur in the operationalization of DST regulations. In this section we focused on identifying challenges likely to occur in the operationalization of draft regulations once ratified. An open- ended questions was asked. A vast majority of the respondents were not aware of the draft regulations and therefore the number of no responses was high representing 36.04%. Key issues raised by respondents in response to this question include:

- Lack of enforcement framework – 25.23%
- Lack of awareness/ need for sensitization -19.82%
- Determination of user location – 9%
- Tax avoidance/evasion – 9%

Figure 13: challenges likely to occur in the operationalization of DST regulations

4.5 Recommendations to improve regulations

This section focused on identifying recommendations to address the current DST draft regulations before ratification. This question received a significant number of no responses representing 29.82%, however key recommendations raised include:

- Conduct awareness – 32.46%
- Improve compliance/enforcement measures – 14.04%
- Determination of user location – 2.63%
- Others i.e. –change of law, double taxation etc. – 21.05%

Figure 14: Recommendations to improve draft regulation

5. Conclusion and Recommendations

This chapter covers an account of the study summary findings, discussions as well as the conclusions drawn from the findings. In line with the study findings and conclusion, the chapter also suggests policy recommendations and areas for further research.

5.1 Summary Findings

5.1.1 Gaps in digital tax Enforcement

From the study, we establish that taxation of digital economy has imposed new enforcement challenges to tax policymakers, tax authorities and governments. This is mainly due to the complex nature of transactions carried out in the digital economy. The study reveals that the following as the main gaps in the enforcement of digital tax in Kenya.

5.1.1.1 Determination of the actual transaction amount and tax jurisdiction

There is difficulty in determining transactional value on income accrued or received in Kenya this mainly due to the challenges of determining the jurisdiction in which value creation occurred. The problems this tension causes are particularly evident in the case of profits generated by internet-related activities. The difficult question then is to determine where that place is. You could say that it is where the company carries out its business activities, i.e. where it has an economic presence, or 'nexus'. As a point of reference, however, that is not exactly very specific.

5.1.1.2 DST does not address profit shifting

There is need for DST to minimise the potential for tax evasion and avoidance by putting in place measures to address challenges posed by multinationals who practised aggressive profit shifting. This may however, require international consensus, currently spearheaded by OECD and G20 countries.

5.1.1.3 Digital services tax is therefore applicable to a narrow range of entities

The Income Tax Act, states that the digital services taxes will apply to a digital marketplace which in turn is defined in the same Act as a platform that enables the direct interaction between buyers and sellers of goods and services through electronic means. Therefore, DST only applicable to a narrow range of entities. DST holds that a business that is selling its own goods on a digital platform that is not providing a platform for sellers and buyers to interact but is selling its own products is not a digital market place provider. For instance, ride-hailing apps that connect drivers and riders would be considered a digital marketplace while an ecommerce venture that sells its own product online would not be a digital marketplace.

5.1.1.4 No Turnover Threshold to cushion informal industries

Kenya has a large informal sector that covers mainly semi-organized and unregulated activities. There is need of protecting emerging industries with small margins.

5.1.1.5 The Proposed regulations overruling the scope of the act

If the draft legislation is adopted it will illegally charge to tax businesses not defined in the act. This is because, DST regulations appears to extend the application of the digital services tax to a host of activities that do not qualify as a digital marketplace or platform providers as per the definition in the main part of the Income Tax Act. The proposed legislation leaves a very large room for further determination on a case-by-case basis. This represents a wide application of the law.

5.2 Enforcement measures & Policy Recommendations

From the results of the study, a number of enforcement measures and recommendations suggested including: -

5.2.1 Taxpayer Education & Sensitization

The study findings affirmed that taxpayers would readily comply if they have ample knowledge to understand the new digital service tax introduced. Thus, the taxpayer education through education programs organized by the Revenue authority or other public education institutions is necessary to increase public awareness especially in areas concerning digital regulation & taxation laws and especially to explain how and where the government spends the money collected.

5.2.2 Regular Stakeholders Engagement

Stakeholders with regards to DST can be explained as those individuals or entities that share a common interest in engaging with and influence the application of DST. Engagement of stakeholders is key especially in the legislations and enforcement of DST tax given that resistance to change is an inevitable part of any change in reforms. Any tax policy formulated through a process of consultation is usually regarded legitimate, assuming its outcome meets the preferences of a majority of interest groups who are affected by the decision. In addition, such a process adds transparency and accountability to the policy making process.

5.2.3 Policy Recommendations regarding Multinational corporations

5.2.3.1 Redefining what constitutes a permanent establishment

On legal perspective, the current Kenyan concept of permanent establishment especially regarding digital tax, does not establish a taxable presence. This is because it is mainly based on an entity being physically present or having a physical representative in the country. It will be necessary to come up with parameters defining what amounts to a digital permanent establishment (PE) or circumstances that will trigger a digital PE in Kenya. Without a nexus, KRA runs the risk of countless tax evasion in DST.

Therefore, there is need to redefine permanent establishment to include digital companies that have no

physical presence within a jurisdiction. These virtual or digital permanent establishments are usually defined using specific criteria including engagement with the local market.

5.2.3.2 Subject withholding tax to digital service

Intermediaries such as financial institutions have a role to play in the withholding of digital tax of multinationals. The tax withheld at source would be credited against taxes due in the residence country, in this case Kenya. This would bring multinational corporations to tax bracket.

5.2.3.3 Review and amendment of Kenya's double tax treaties

Double tax treaties need to be reviewed, this is because, existing tax treaties could lead to revenue loss through tax avoidance schemes. The study revealed that multinational corporations would tend to go for treaty shopping in other jurisdictions in order to avoid taxes.

It is also observed that digital service payments to countries that have income tax treaties with Kenya will not be subject to digital services tax, given the reliance on the concepts of residency and permanent establishment as a basis for determining the jurisdiction with the taxing rights.

This review of treaties can be done with a multilateral instrument such as OECD and ATAF that will automatically amend the existing treaties (of countries that sign up for it) and save everyone the trouble of renegotiating their treaties one by one.

5.2.4 Domestic Policies recommendations

5.2.4.1 Activate the use of user IP address in determining tax point

There is need for KRA and Communication Authority of Kenya to liaise in mapping of IP addresses. This means that, a user located in the Kenyan territory, confirmed via the IP address of the user's device used for enjoying the digital service shall be deemed located in the Kenyan territory in a tax period.

5.2.4.2 Frame unilateral digital tax around various revenue streams

Due to the complexity of the sector, Kenya can look to apply unilateral digital tax around three revenue streams: advertising revenue; commission income generated by online marketplaces when facilitating transactions between users; and income from the resale of user data for advertising purposes. This will help ensuring businesses pay their fair share of tax. If the digital services tax is applicable to a narrow range of entities, extend the application of the digital services tax to a host of activities. How the current DST and the proposed legislation is currently applied leaves out many entities who ought to be included in the tax brackets.

5.2.4.3 Introduction of turnover threshold for DST purposes in Kenya

Government of Kenya should have considered setting a minimum threshold for applicability of DST and exempting some businesses with low margins. A big percentage of Kenyan sector is made up informal businesses which creates a whopping 82.7% of employment in Kenya. There is need of protecting such emerging industries. Therefore, the government of Kenya should have considered setting a minimum threshold for applicability of DST and exempting some businesses with low margins.

6.0 Recommendation and Further Research

There was time constraints hence the study did not extensively cover some sectors within the digital economy. Notably, more elaborate engagement and targeted interview with Multinationals is necessary. The other area of interest where we did not get enough audience to make concreate findings was on crypto-currency trading. Therefore, we recommend further studies on multinational and crypto-currency trading. Future studies should widen the research period in order to have a longer time series data, which can give results that are more reliable. This will enable the authority to assess the certainty, convenience, and simplicity in revenue collection by the authority.

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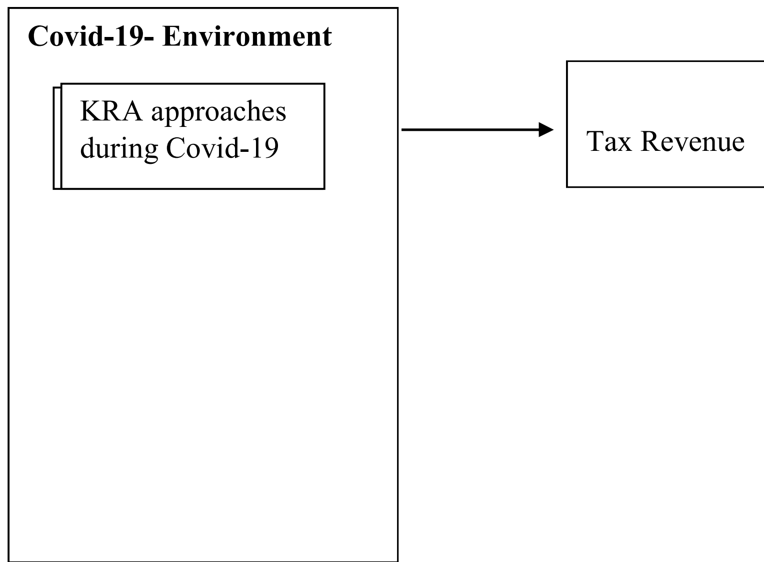
Annex

Figure 2.1: The conceptual framework



Variable	constructs	Reference
Fiscal policies	VAT, IT, Excise, Corporate	Likert scale of 1-5
Restrictions measures	Curfew, Intercountry movement, Social distancing	Likert scale of 1-5
KRA approach	Tax relief for person earning gross monthly income of up to Ksh 24,000 Reversion of personal income tax (PAYE) rate (bands) from 25% to 30% Reversion of resident corporation income tax (CIT) rates from 25% to 30% Retention of the turnover tax rate from the current 3% to 1% Reversion of the VAT from 14% to 16% effective 1st January, 2021	Likert scale of 1-5
Tax collection	VAT collection. IT1 Collection, Excise collection	Secondary data collection from KRA records.

County	Population per county	Distribution Ratio	Sample Size
North Rift Region	1,163,186	0.16	70
South Rift Region	2,162,202	0.31	129
Western Region	1,155,574	0.16	69
Southern Region	1,208,333	0.17	72
Northern Region	608,599	0.09	36
Central Region	759,164	0.11	45
Total	**7,057,058**		**422**

(Kenya National Bureau of Statistics, 2019)