Trade mispricing costing Kenya billions every year

KRA top official says practice by importers and exporters is having significant negative consequence for country's revenue collection

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Kenya School of Revenue Administration says trade misinvoicing has been ongoing for years now and a favourite tool for money launderers.

Kenya is losing hundreds of billions of shillings in illicit financial flows each year, with much of the damage rooted in trade misinvoicing, according to experts.

Trade misinvoicing involves the deliberate manipulation of commercial invoices in order to misreport the value of a transaction, thus shifting money across international borders without detection.

It is a common practice, Kenya School of Revenue Administration (KESRA) says has been ongoing for years now and a favourite tool for money launderers. It is a vice which the institution says is a direct revenue loss for the government.

Custom duties, import tariffs, and value-added taxes (VAT) are typically calculated based on the declared value of goods. When this value is manipulated, the government through Kenya Revenue Authority (KRA) receives less revenue than it should.

"This practice is having a significant negative consequence for our country's revenue collection. It is a challenge the exchequer continues to address," said Doreen Mbingi, Deputy Commissioner, Academic Affairs, at the KRA's training school specialising in tax and customs administration, fiscal policy and management.

Increasing tax evasion through trade misinvoicing, she noted, was deteriorating the already vulnerable local tax system and "halts positive progress in the restructuring attempts of the government to improve tax collection."

Mbingi was speaking during an ongoing forum on tax administration by the Tax Justice Network Africa in Nairobi. Indeed, KRA collected Sh2.17 trillion in tax revenue in the financial year ended June 2023, translating to a 6.7 per cent growth compared to the previous financial year.

However, it missed its revenue target for the financial year 2022/23 by Sh107.0 billion, mainly on vices like tax avoidance, misinvoicing and other illicit tax loopholes. Further, the 2022 figures by the Africa Tax Network Africa and Oxfam, and the Global Financial Integrity, show that Kenya losses close to $43 billion every year or over Sh5 trillion every year through tax evasion and illicit financial flows (IFFS). Africa loses about $88.6 billion annually as a result of the vice.

Financial transfers

IFFs deprive countries like Kenya of the much-needed resources for their development, and while definitions may vary, IFFs are broadly accepted as cross-border financial transfers with illegal origin or destination. "This is money that is illegally earned, used or moved and which crosses an international border" and, as such, represent an important obstacle to international development efforts," notes the report.

Tax expert, Norah Kawiche, however noted that there needs to be clear tax laws and policies as well as transparency to encourage compliance. "Without that, we will continue facing the same challenges," she said. Kenya's financial sector is among the most secretive globally and is also the second most rigid in Africa after Algeria and among the top 30 in the world, according to the Financial Secrecy Index of 2020 by the TJNA.

Countries like Dubai and Mauritius among others have acted as magnet destinations for tainted money for most moneyed Kenyans – with their property markets built to attract foreign buyers, with the Dubai emirate for instance, dominated by towers of upscale flats and man-made islands studded with luxury villas.

Kenya was also out in the watch list of notorious countries helping individuals hide money from the rule of law, according to a 2020 EU Commission report which commenced legal actions against Luxembourg over laws to prevent money laundering and tax avoidance.

Those reports found that Kenya was among the notorious countries assisting well-placed personalities in siphoning public funds and moving them to offshore countries like Mauritius and Luxembourg with the help of western consulting firms.

The European Union said it was stepping up scrutiny of financial assets controlled by politicians and company owners in an effort to clamp down on money laundering.