MONTHLY LEGAL UPDATE

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TSEGAMLAK SOLOMON & ASSOCIATES

January, 2025

Top Update

ESX Officially Launched with a Bell-Ringing Ceremony

The ESX will provide a regulated marketplace for the listing and trading of securities, opening up new opportunities for businesses and investors alike.

What's Covered this Month?

Welcome to the January 2025 edition of the TSA Legal Update! This newsletter brings you key legal developments to help you stay informed and navigate the evolving legal landscape.

In this issue, we cover:

1. Launch of the Ethiopian Securities Exchange (ESX)
2. Amendment to the Investment Incentives Regulation (No. 517/2022)
3. Customs Valuation Update for Manufacturers and Investors
4. Enactment of the Property Tax Proclamation
5. Enactment of the Asset Recovery Proclamation
6. Federal High Court Rules in Favor of Enat Party in Property Tax Directive Case

1. Launch of the Ethiopian Securities Exchange (ESX)

ESX was officially launched on January 10, 2025 with a traditional bell ringing event, marking a significant milestone in the development of Ethiopia's capital markets. This achievement followed a series of strategic and regulatory developments aimed at creating a robust and transparent financial ecosystem. The establishment of the ESX was enabled by Capital Market Proclamation No. 1248/201, which provided the legal framework for its formation under a public-private partnership model, with the government's ownership capped at 25% of the total capital. This structure was designed under Article 31 of the Capital Market Proclamation to ensure private sector participation and foster investor confidence.

Following the enactment of the Proclamation, the establishment of the ESX followed a multi-year process that began with the formation of a project office. This office later transitioned into a legally recognized share company in 2023, enabling it to raise capital from both domestic and foreign investors. The capital-raising process was essential for ensuring the exchange's operational readiness and financial sustainability. Key milestones included the development of market infrastructure, such as trading platforms, clearing and settlement systems, and regulatory frameworks to ensure compliance and investor protection.

Prior to its launch, the Ethiopian Capital Markets Authority (ECMA) enacted the Exchange and Exchange Licensing Directive No. 1009/2024 on July 16, 2024. This directive provided the legal framework for the licensing, operation, and supervision of securities exchanges, derivatives exchanges, and over-the-counter (OTC) markets. The ESX successfully obtained licenses to operate as a securities exchange and an OTC market, fulfilling the regulatory requirements necessary for its launch.

The launch of the ESX was accompanied by the listing of Wegagen Bank, one of Ethiopia's prominent banking institutions, as the first entity on the exchange. This listing symbolized the beginning of a new era for Ethiopia's financial sector, providing companies with access to capital markets and offering investors opportunities to participate.

2. Amendment to the Investment Incentives Regulation (No. 517/2022)

The Council of Ministers has introduced amendments to the Investment Incentives Regulation (No. 517/2022), which included significant changes to income tax exemptions, customs duty exemptions for motor vehicles, and incentives for strategic mining and petroleum operations. The amendments aim to align the regulation with current economic priorities and address specific challenges faced by investors in key sectors.

Key Amendments

1. Income Tax Exemption Incentives (Article 4, Sub-Article 4)

The amendment revises the thresholds for income tax exemptions granted to investors who provide employment opportunities outside Ethiopia to Ethiopians with recognized qualification certificates. The updated thresholds are as follows:

- 1-year income tax exemption: Employing 2,000–3,000 Ethiopians.
- 2-year income tax exemption: Employing 3,001–5,000 Ethiopians.
- 3-year income tax exemption: Employing more than 5,000 Ethiopians.

This change represents a significant increase from the previous thresholds, which were set at 100–300 employees for a 1-year exemption, 301–500 employees for a 2-year exemption, and more than 501 employees for a 3-year exemption.

2. Exemption of Motor Vehicles from Customs Duties (Article 13)

The amendment maintains the general framework for customs duty exemptions on motor vehicles used for investment purposes, as determined by directives issued by the Ministry of Finance. However, it introduces an exception for companies operating in mining, petroleum, agriculture, tourism, and construction sectors.

- **New Provision:** Companies in these sectors may import pickup and station wagon vehicles duty-free for use in remote areas, subject to approval by the Ethiopian Investment Board.
- **Exclusion:** Pickup and station wagon vehicles remain excluded from customs duty exemptions under normal circumstances.

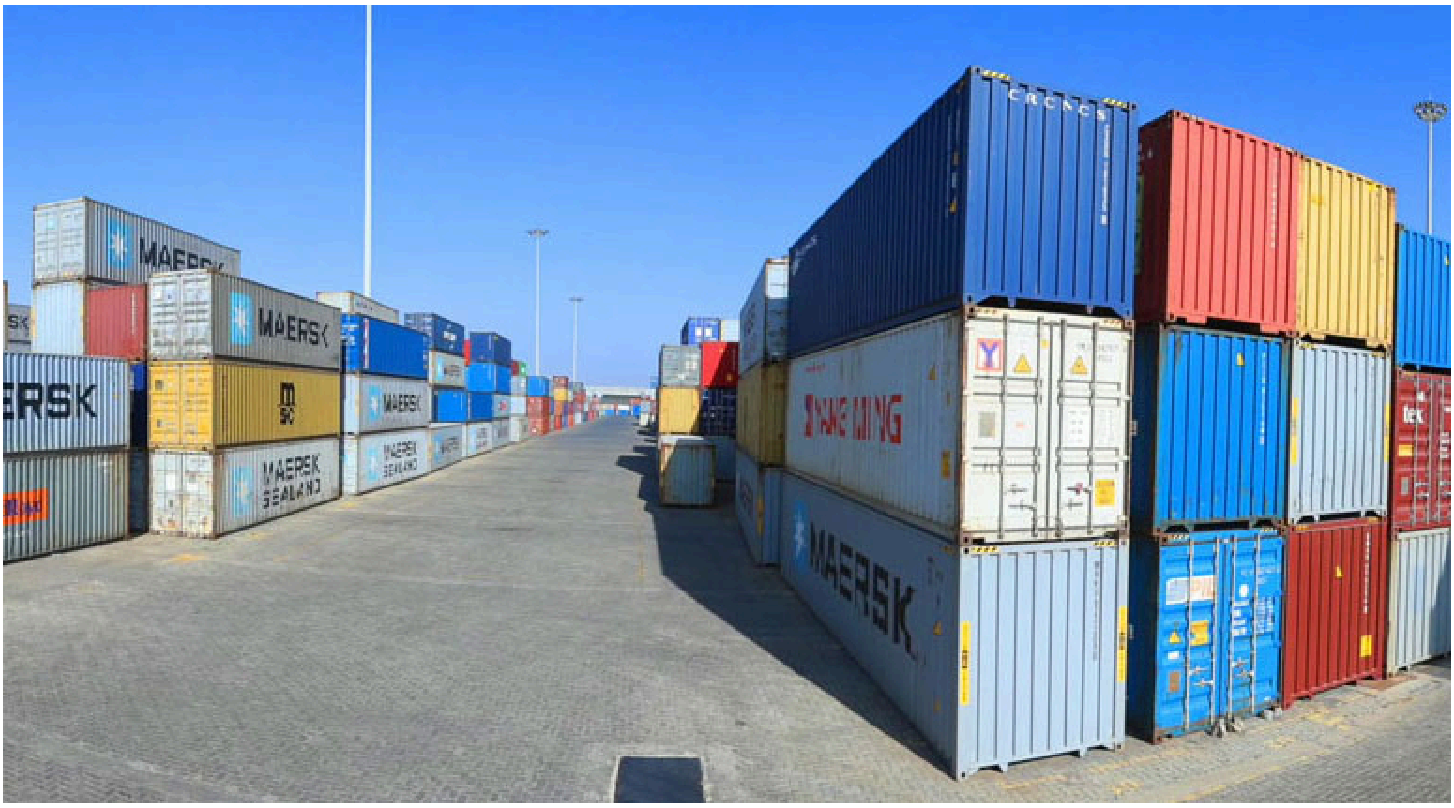
3. Incentives for Mining Investment (Article 16)

A new sub-article (Sub-Article 4) has been added to Article 16, granting the Ethiopian Investment Board the authority to provide additional incentives to companies engaged in strategic mining and petroleum operations. This provision allows for flexibility in offering tailored incentives to support high-priority projects in these sectors.

4. Transitional Provision (Article 27)

A new sub-article (Sub-Article 3) has been added to Article 27, ensuring that customs duty and tax exemptions granted under mining and petroleum agreements signed prior to the entry into force of these regulations remain valid. These exemptions, which were approved by the Council of Ministers, will not be affected by the new amendments.

3. Customs Valuation System Revised for Manufacturers and Investors



On January 22, 2025, the Ethiopian Customs Commission issued Circular No. 4/1352/17, introducing temporary measures to address challenges related to customs valuation for businesses in the manufacturing sector. The circular was issued in response to longstanding complaints from the business community, particularly manufacturers, regarding inefficiencies and inconsistencies in the customs valuation process under the existing Customs Tariff and Tax Valuation Directive No. 158/2011.

The primary issues included:

I. Exaggerated Valuation of Goods: The Customs Commission's valuation of imported items often is much higher than the invoice value of the items resulting in significantly higher duty and tax payments, creating financial burdens for importers.

II. Delays in Valuation Process: The lengthy time taken by the Customs Commission to determine the value of imported goods led to increased warehouse fees and project delays, particularly for manufacturers importing capital goods, raw materials, and construction materials essential for their operations.

To address these challenges, the circular introduced temporary measures for investors and businesses in the manufacturing sector, among others. Until Directive No. 158/2011 is amendment, importers in this sector—including manufacturers, investors importing capital goods for investment projects, those engaged in government projects, state-owned enterprises, and federal and regional governments—will be assessed based on the value declared in their official invoices. This measure aims to streamline the customs process, reduce delays, and alleviate the financial burden on businesses critical to Ethiopia's industrial and economic development.

Other businesses outside the above listed sectors will continue to be subject to the existing customs valuation process under Directive No. 158/2011. The circular represents a targeted effort to support investors and the manufacturing sector, which plays a vital role in Ethiopia's economic growth, while broader reforms to the customs valuation framework are being developed.

4. Enactment of the Property Tax Proclamation

The House of People's Representatives passed a new Property Tax Proclamation in January 2025, marking a significant step in the Ethiopian government's efforts to expand the tax base and enhance municipal revenue generation. The proclamation introduces a comprehensive tax policy that imposes levies on urban land, buildings, and land improvements. This initiative is part of the government's broader strategy to strengthen local governance, finance infrastructure development, and promote equitable taxation.

Key Provisions

I. Taxable Amount:

The taxable amount for any property is set at 25% of its market value or replacement value, whichever is applicable. This provision ensures that the tax base reflects the current economic value of properties while accounting for variations in property conditions and locations.

II.Tax Rates:

- **Land Usage Rights:** Tax rates range from 0.2% to 1% of the annual taxable amount, depending on the location, size, and usage of the land.

- **Buildings and Land Improvements:** Tax rates range from 0.1% to 1% of the taxable value, with variations based on the type and purpose of the property (e.g., residential, commercial, or industrial).

III. Municipal Revenue Collection:

Municipalities are authorized to collect property taxes directly, granting them increased financial autonomy. This decentralization of revenue collection is expected to enable local governments to fund essential services, such as infrastructure development, public utilities, and urban planning projects, more effectively.

IV. Implementation and Compliance:

The proclamation establishes guidelines for property valuation, tax assessment, and collection processes. Property owners are required to declare the value of their properties, and municipalities are tasked with verifying these declarations to ensure accuracy and fairness.

Non-compliance with the proclamation, including underreporting property values or failing to pay taxes, may result in penalties.

5. Enactment of the Asset Recovery Proclamation

The parliament approved the Asset Recovery Proclamation, which introduces significant changes to the legal framework governing the recovery of assets obtained through crime or unexplained wealth. The proclamation aims to strengthen the government's ability to combat economic crimes, enhance transparency, and align with international standards on asset recovery.

Key Changes Introduced by the Proclamation

I. Introduction of Non-Conviction-Based Confiscation:

- The proclamation introduces non-conviction-based confiscation, allowing the state to confiscate assets even if the accused is not convicted of a crime. This is particularly aimed at addressing unexplained wealth where individuals cannot justify the source of their assets.
- A 10-year look-back period is established for unexplained assets, with a threshold of 10 million Birr for claims.

II. Expansion of Scope to Legal Persons and Virtual Assets:

- The new law applies to legal persons (e.g., corporations) involved in criminal activities, not just public servants or government employees.
- Virtual assets (e.g., cryptocurrencies) are explicitly included within the definition of assets subject to recovery.

III. Enhanced Investigation Powers:

- Investigators and prosecutors are granted broad powers to use special investigation techniques, including monitoring bank accounts, intercepting communications, and conducting undercover operations.
- Freezing and seizure of assets can be ordered by the court or, in urgent cases, by the Minister of Justice for up to three working days.

IV. Asset Management Framework:

- Courts can appoint asset managers to oversee seized or frozen assets, ensuring their economic value is preserved.
- Asset managers have the authority to collect rents and profits but cannot transfer or mortgage assets without court approval.

V. International Cooperation:

- Ethiopia will cooperate with foreign states in mutual legal assistance for asset recovery, including freezing, seizure, and confiscation of assets.
- Confiscated assets can be repatriated to requesting states based on bilateral agreements or international conventions.

VI. Whistleblower Rewards:

- Individuals who provide information leading to asset recovery may receive rewards, excluding those who access such information professionally (e.g., investigators, prosecutors).

VII. Criminal Liability:

- Penalties for non-compliance include imprisonment for failing to disclose evidence, destroying evidence, or violating freezing/seizure orders.
- Legal persons (e.g., corporations) face fines of 20-30% of the damage caused or advantage obtained for violating court orders.

6. Federal High Court Rules in Favor of Enat Party in Property Tax Directive Case

In an unprecedented turn of events, the Administrative Bench of the Federal High Court has ruled in favor of Enat Party in its lawsuit against the Addis Ababa City Administration Finance Bureau regarding an illegal property tax directive. The Court's decision, delivered on January 17, 2025, declared that the directive lacks a legal basis and should not be implemented.

Background of the Legal Battle

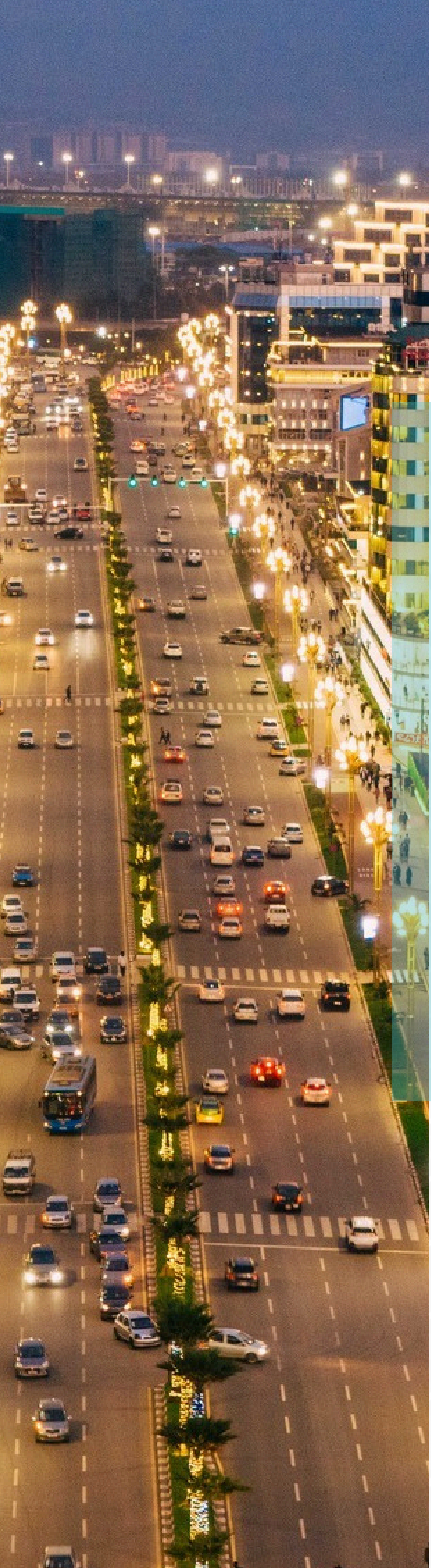
The legal dispute stems from a directive introduced by the Addis Ababa City Administration nearly two years ago, which enabled the Finance Bureau to begin collecting property taxes from residents. Enat Party challenged the directive, arguing that the City Administration lacked the legal authority to impose such a tax. The Party contended that directives must derive from regulations, which in turn must be based on proclamations. At the time the directive was introduced, no such proclamation enabling the collection of property taxes existed.

Court's Ruling and Immediate Aftermath

The Court's decision was announced following a session on January 17, 2025, during which it was determined that the Addis Ababa City Administration Finance Bureau had overstepped its authority by introducing a property tax directive without a supporting legal framework. The Court ruled that the directive was not derived from a valid proclamation or regulation.

The City Administration immediately appealed the decision on the same day, requesting the Court to issue an injunction preventing Enat Party from disclosing the verdict to the media or the public. The Court granted the injunction, stating that the disclosure of the decision could cause "irreversible damage" to the City Administration. The Court ordered that the decision should not be disclosed to the media until the City Administration files its appeal within the next 15 days.

Despite the injunction, both the City Administration's Justice Bureau and Enat Party posted summaries of the verdict on their respective social media pages, effectively making the Court's decision public. This unprecedented action by both parties highlights the contentious nature of the case and the high stakes involved.



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