MONTHLY LEGAL UPDATE

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This month's legal update marks May 1st, International Workers' Day, a moment to reflect on the critical role that labor laws play in protecting workers' rights and promoting fair employment practices.

Top Update

Ethiopia Approves Regulation to Implement AfCFTA Tariff Liberalization Commitments

The Government of Ethiopia has approved a regulation to implement its AfCFTA tariff reduction commitments, marking a key step toward facilitating duty-free trade with other African member states.

What's Covered this Month?

Welcome to the May 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:

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1. Understanding the New Ministry of Finance Directive on Tax Audits and Assessments

On May 29, 2025, Ethiopia's Ministry of Finance issued a new Directive titled "Directive on the Conduct of Tax Audits and Issuance of Tax Assessment." This Directive, authorized under Proclamation No. 983/2016, sets out a standardized approach for how the Ministry of Revenue conducts tax audits. The goal is to bring greater transparency, consistency, and legal certainty to the audit and tax assessment process.

Who This Directive Applies To

The Directive applies to all businesses subject to federal taxes in Ethiopia, regardless of size or sector. It governs the full range of tax audits conducted by the Ministry of Revenue, from the moment an audit is initiated to the issuance of a final amended tax assessment. The rules are binding on both the tax authority and taxpayers, meaning all parties must follow the same procedures and timelines. Whether your business is undergoing a full audit or simply responding to a desk review, this Directive now forms the legal framework for that process.

Types of Tax Audits You May Face

Under the Directive, there are six main types of audits. A Comprehensive Audit is the most detailed, covering all tax obligations and records for a specific period, usually triggered by risk indicators or signs of widespread non-compliance. A Desk Audit is less intrusive, conducted remotely by reviewing submitted documents, often in routine or low-risk cases.

A Transfer Pricing Audit focuses on whether transactions between related companies, especially international ones, are conducted at fair market value. A Refund Audit happens when a business claims a tax refund; the authority reviews the claim and supporting documents. A Fraud Investigation Audit is launched when there is suspicion of intentional evasion or misrepresentation, and may involve more serious enforcement actions. Lastly, an Issue-Oriented Audit focuses on a specific tax concern, often prompted by data mismatches or third-party information.

How the Audit Process Works

The audit process begins when the tax authority formally notifies your business about the audit. The notice will state the type of audit, the tax period under review, and the documents required. Once notified, you must prepare all relevant records and comply with the instructions provided.

The audit itself involves a review of your records, declarations, and business activities. Afterward, the authority issues a Preliminary Amended Assessment, which outlines their findings and any changes to your tax liabilities. You'll then have ten working days to respond. If you object, you must submit a written explanation and supporting documents. If you do not respond, the assessment is considered accepted. After reviewing your response (or lack thereof) the tax authority issues the Final Amended Assessment, which becomes enforceable.

Your Responsibilities as a Taxpayer

During the audit, you are required to provide full and accurate records, respond to notices within deadlines, and cooperate in good faith with the audit process. Deliberate concealment, falsification, or destruction of information is strictly prohibited. You must also maintain a professional environment for the auditors and comply with all procedural requirements as set out in the Directive.

What Happens If You Don't Comply

The Directive itself doesn't create new penalties, but any failure to meet its obligations can trigger enforcement actions under the Tax Administration Proclamation. This includes financial penalties, legal sanctions, and administrative measures depending on the nature and seriousness of the non-compliance.

2. Ethiopia Approves Regulation to Implement AfCFTA Tariff Liberalization Commitments

The Government of Ethiopia has taken a significant step toward fulfilling its obligations under the African Continental Free Trade Area (AfCFTA) by approving a regulation that operationalizes Ethiopia's tariff reduction commitments under the agreement. The decision was made at the Council of Ministers meeting held on Miyazia 23, 2017 E.C. (May 1, 2025 G.C.).

The regulation enables the progressive elimination of customs duties on goods traded between AfCFTA member states, as part of Ethiopia's phased implementation of the AfCFTA Tariff Concession Schedule. This aligns with the broader objectives of the AfCFTA to increase intra-African trade, promote regional economic integration, and strengthen cross-border value chains.

Key Features of the Regulation:

- Tariff Reductions for Intra-Africa Trade: Duties will be reduced or eliminated in accordance with Ethiopia's schedule of tariff concessions submitted to the AfCFTA Secretariat.

- Trade Facilitation: The regulation mandates streamlined customs procedures and encourages efficient cross-border trade among member states.

- Non-Tariff Barrier Mitigation: In addition to tariff liberalization, the regulation supports measures to ensure that administrative and procedural barriers do not undermine the benefits of the duty reductions.

- Support for Industrialization and Transformation: The regulation aims to position Ethiopia more competitively within regional value chains and to stimulate domestic production by opening access to larger African markets.

The regulation enters into force upon publication in the Federal Negarit Gazette and will be binding on all relevant customs, trade, and border management authorities.

This marks a milestone in Ethiopia's AfCFTA implementation journey, reinforcing the government's commitment to creating a predictable, rules-based trading environment and unlocking the economic potential of regional trade integration.

3. MoF Issues Directive on Investment Incentives: What Investors Need to Know

In May 2025, Ethiopia's Ministry of Finance issued Directive No. 1064/2025 to operationalize the Investment Incentives Regulation No. 517/2022. This new framework aims to tighten compliance, clarify eligibility, and improve how tax and customs incentives are granted and monitored. It introduces new rules tailored for specific sectors and geographies, while preserving the integrity of past arrangements.

Directive No. 1064/2025 marks a shift toward a more rules-based and transparent incentive regime. By tightening controls and linking tax benefits to compliance and local economic impact, it aims to protect public revenue while still encouraging strategic investment.

1. Eligibility Criteria for Accessing Incentives

To access income tax holidays and customs exemptions, investors must operate in eligible sectors, possess valid licenses, and present a confirmation letter from the relevant investment authority confirming project completion. Expansion or upgrading projects are governed by Directive No. 941/2023, which sets additional performance and documentation standards. These requirements seek to ensure only qualified and operational investors benefit from public revenue foregone through incentives.

2. Reporting Duties and Incentive Revocation

The Directive introduces a stricter compliance regime. Investors must timely submit audited financial statements and income declarations. Delays or failures may trigger penalties under the Tax Administration Proclamation. More seriously, tax holidays can be revoked if obtained via false documentation, if the investment is abandoned, or if the investor fails to meet reporting or operational duties.

Before cancellation, investors have 10 working days to respond to a notice from the Ministry and 30 days to file an appeal. Once revoked, all previously exempted taxes become payable, along with interest and penalties. This accountability mechanism aims to prevent abuse and ensure incentives serve their intended purpose.

3. Customs Duty Relief and Local Sourcing Rules

Duty-free importation of construction materials and capital goods is subject to phased import schedules (typically in 30%, 30%, and 40% tranches) verified against project milestones. To import in larger volumes upfront, investors must submit a cash or bank guarantee.

Incentives are conditional on the absence of equivalent domestic alternatives. Where suitable local substitutes exist, the Ministry of Industry may deny import requests and require local sourcing. If input materials are purchased locally, duties may be refunded through the Customs Commission, based on industry-specific input-output formulas. This ensures protection for domestic industries while keeping investor costs predictable.

4. Sector-Specific Carve-Outs and Special Economic Zones

Enterprises in Special Economic Zones (SEZs), including developers, sub-developers, and operators, remain eligible for special incentives detailed in an annex to the Directive. However, certain sectors and activities are excluded. For instance, manufacturing of nails or iron sheets qualifies only if starting from raw materials, and food processing incentives exclude traditional products like enjera, dabo, and baltena. Similarly, gymnasiums offering body-building services are not eligible under training incentive schemes.

5. Continuity of Prior Incentives and Extractive Sector Exceptions

The Directive preserves incentive entitlements previously granted under repealed regimes such as Regulation No. 270/2005, maintaining investor confidence and legal continuity. It also recognizes that mining and petroleum investments remain governed by specific sector laws or contractual arrangements. This ensures Ethiopia's extractive industries, often subject to bespoke fiscal regimes, retain their regulatory autonomy.

4. NBE Amended Licensing Directive for Payment Instrument Issuers

The National Bank of Ethiopia (NBE) issued Directive No. ONPS/10/2025 on May 12, 2025, replacing the previous Directive No. ONPS/01/2020. This amendment, based on the National Payment Systems Proclamation No. 718/2011 as amended by Proclamation No. 1282/2023, marks a significant regulatory shift for Payment Instrument Issuers (PIIs), including mobile money and wallet-based platforms. The reform is a continuation of NBE's efforts to modernize the digital financial sector.

Stronger Institutional Requirements and Phased Capital Compliance

The Directive doubles the minimum paid-up capital requirement from ETB 50 million to ETB 100 million or its foreign currency equivalent. This change aims to enhance financial stability and operational resilience in a fast-evolving sector. Existing license holders are granted a transitional period until June 2027 to meet the new capital threshold, while new entrants must comply within two years from the date of licensing. The capital hike is in line with the NBE's shift to a risk-based supervision model and sends a clear signal that robust financial footing is a prerequisite for digital financial service providers operating at scale.

Governance and Ownership Restrictions

To mitigate concentration risk and promote competitive fairness, the Directive introduces new limits on ownership. No person may directly own more than 40 percent of a PII's subscribed capital, while total direct and indirect holdings are capped at 60 percent. Notably, government institutions, telecom operators, and already-licensed financial entities are exempt from this restriction, recognizing their systemic roles. Alongside these shareholding caps, the Directive updates executive eligibility standards by reducing experience requirements for CEOs and senior executives to seven years of work, with a minimum of three years in managerial roles. This offers companies more flexibility in talent acquisition without sacrificing oversight integrity.

Interoperability and Integration to Enhance Platform Cohesion

To eliminate silos in the digital payments space, the Directive mandates full interoperability among PIIs. All mobile money providers are now required to support wallet-to-wallet transactions and integrate with the Ethiopian Instant Payment System (EIPS) operated by EthSwitch. This rule is pivotal for enabling seamless real-time payments across different platforms and ensuring that users are not restricted by service boundaries. The integration mandate reflects NBE's strategic priority to build a cohesive and inclusive payment infrastructure that can scale nationally and serve as a backbone for financial innovation.

Updated Consumer Protections and Usage Limits

The Directive lowers the threshold for mandatory two-factor authentication (2FA) from ETB 15,000 to ETB 5,000, reinforcing safeguards against fraud amid growing digital transaction volumes. In parallel, the daily transaction and balance limits for Level 2 accounts have been significantly raised to better accommodate high-volume business users. These now include a maximum daily transaction limit of ETB 300,000, an account balance cap of ETB 150,000, and person-to-person transfer limits of ETB 75,000. QR-based merchant payments are permitted up to ETB 250,000 per day. These adjustments reflect the increasing importance of digital wallets for enterprise-level and merchant-driven transactions.

Compliance, Monitoring, and System Integrity

New operational obligations emphasize real-time Know Your Customer (KYC) processes and the deployment of risk-based transaction monitoring systems. PIIs are also required to conduct comprehensive security audits every six months and submit the findings to NBE. These compliance measures reinforce the broader goals of anti-money laundering (AML), cybersecurity, and financial transparency. Additionally, the Directive introduces formal definitions, such as those for interoperability and instant payment systems, to ensure regulatory clarity. While the Directive takes immediate effect, defined compliance windows exist for key changes like capital adequacy and interoperability to support a smooth transition.

5. NBE Introduces Reforms to Enhance Foreign Exchange Market Functionality

Continuing its foreign exchange liberalization efforts launched in July 2024, the National Bank of Ethiopia (NBE) has issued an amendment to Foreign Exchange Directive No. FXD/1/2024. The new measures, outlined in both the directive and an accompanying press release, aim to increase flexibility for importers and travelers, improve market transparency, and align Ethiopia's foreign exchange (FX) framework with international best practices. These reforms complement earlier initiatives like bi-weekly FX auctions and respond to improved FX reserves, a stronger balance of payments, and rising foreign capital inflows.

Increased Advance Payment Threshold for Imports

The Directive raises the advance payment cap for imports from USD 5,000 to USD 50,000 per transaction per foreign supplier without requiring bank guarantees. For amounts exceeding USD 50,000, importers must submit a foreign bank guarantee confirmed by a local authorized bank. This adjustment eases upfront capital restrictions for many legitimate importers, particularly SMEs previously constrained by the lower threshold. It reflects the improved FX liquidity due to increased inflows from exports, remittances, and development partners. While this new threshold aligns with regional liberalization trends and enhances procurement flexibility, the bank guarantee requirement for larger payments may pose challenges for smaller businesses without established international banking relationships.

Expanded Foreign Exchange Access for Travelers

The Directive significantly increases FX entitlements for both personal and business travelers, differentiating access based on foreign currency (FCY) account status and travel purpose. Personal travelers can now access up to USD 10,000 in cash or via debit card. FCY account holders additionally may use 20% of their account balance, though only through debit card transactions, doubling the previous 10% allowance. Business travelers are entitled to USD 10,000 plus 20% of their FCY balance under similar debit card restrictions. Non-account holders and institutions such as trade associations, event organizers, and religious organizations may purchase up to USD 15,000, split between USD 10,000 in cash or debit card and USD 5,000 debit card only. These changes respond to growing legitimate FX needs for trade, tourism, religious events, and international business, while encouraging digital transactions to reduce cash dependence.

Caps on FX Service Charges and Transparency Measures

To protect consumers and promote market discipline, the NBE has capped FX-related banking service fees at 4% of the transaction value. This applies to import payments, travel allowances, and other foreign transactions. Additional minor or supplementary fees, often inconsistently applied by banks, are now prohibited. Starting June 2025, banks must publish their FX service charges on the NBE website for real-time public access. This transparency initiative addresses long-standing concerns about opaque pricing, curtails excessive fee accumulation on high-volume FX transactions, and harmonizes cost structures across institutions. Banks will need to revise fee schedules, eliminate ad hoc charges, and regularly report to the NBE to ensure compliance.

Procedural Clarity and Compliance Requirements

The Directive reiterates standard documentation requirements for FX buyers and travelers, extending eligibility to a broader range of entities. Necessary documents include passports, valid air tickets, and business licenses where applicable. All FX disbursements are subject to KYC and AML controls conducted by authorized forex bureaus and banks. While documentation requirements remain largely unchanged, the Directive enhances compliance by conditioning higher FX access on complete and verifiable submissions. Forex bureaus and banks retain discretion to reject incomplete applications, with oversight provided by regulatory audits.

Enforcement and Outlook

Though the Directive does not introduce new penalties, the NBE has emphasized a zero-tolerance approach to misuse of the revised FX privileges. Banks are expected to implement the increased thresholds and fee caps fully by June 2025. Non-compliance with the 4% service charge limit or failure to publish fees online may result in regulatory sanctions under existing prudential frameworks.

6. NBE Issues Directive on Bank Recovery Plans No. SBB/93/2025

The National Bank of Ethiopia (NBE) has introduced Directive No. SBB/93/2025, titled Recovery Plan of Banks Directive, effective May 23, 2025. This marks the first standalone regulation requiring banks to develop comprehensive Recovery Plans (RPs) designed to restore financial stability during periods of significant stress. Drawing from international frameworks such as those established by the Basel Committee on Banking Supervision (BCBS) and the Financial Stability Board (FSB), the Directive represents a major step toward proactive crisis management and enhanced institutional resilience within Ethiopia's banking sector.

Scope, Applicability, and Strategic Objective

The Directive applies to all licensed commercial banks regardless of their ownership or systemic importance. Each bank must prepare a tailored recovery plan that identifies credible options to address severe financial distress while sustaining critical operations. Notably, the Directive clarifies that the goal is not to guarantee prevention of bank failure, but to equip banks with forward-looking, internally driven strategies that can help avoid resolution processes, capital depletion, or regulatory intervention.

Core Components of the Recovery Plan

Banks are required to develop and regularly update Recovery Plans that incorporate key elements:

- A governance framework clearly defining responsibilities for preparing, approving, and activating the plan, with oversight at the Board level and accountability by senior management.
- A strategic analysis that identifies core business lines and critical functions, along with an assessment of vulnerabilities and operational interdependencies.
- Recovery indicators comprising qualitative and quantitative triggers, such as capital adequacy ratios, liquidity metrics, and asset quality thresholds, that signal distress and prompt recovery actions.
- Concrete recovery options including asset disposals, capital raising initiatives, cost-cutting measures, business model adjustments, and liquidity sourcing strategies.
- A communication plan outlining protocols for internal coordination and external engagement with regulators, counterparties, and the public during a recovery phase.

Additionally, plans must include scenario analyses and stress testing to validate the feasibility of recovery options under various adverse conditions.

Board Accountability and Supervisory Review

Responsibility for the Recovery Plan rests primarily with the Board of Directors, which must approve the plan and oversee its regular review. The Board is also tasked with ensuring the plan's integration within the bank's overall risk management and capital planning frameworks.

The NBE will conduct supervisory reviews of submitted plans as part of its Supervisory Review and Evaluation Process (SREP). Identified deficiencies may lead to mandated revisions, resubmissions, or corrective actions. Failure to comply with the Directive, including non-submission or ineffective implementation, could result in penalties and other regulatory measures.

Submission Timelines and Update Requirements

Banks are required to submit their initial Recovery Plan within eight months of the Directive's effective date. Subsequent updates must occur at least annually, or more frequently if there are material changes in the bank's structure, risk profile, or the macro-financial environment. Banks must also maintain thorough documentation and decision logs related to recovery planning for supervisory inspection.

7. Coffee Export Licensing Returns to Single Window System

In a regulatory notice issued in September 2025, the National Bank of Ethiopia (NBE) announced a structural shift in the administration of coffee export licensing. As part of a long-awaited systems integration effort, the responsibility for registering coffee export contracts and issuing export permits, temporarily assumed by the NBE, has officially been returned to the Coffee and Tea Authority (CTA).

This transition follows the full integration of the CTA into Ethiopia's Customs Single Window System, a digital platform designed to streamline inter-agency coordination and enhance trade facilitation. The NBE confirmed that, as of May 1, 2025, its interim role in contract registration and permit issuance has ended. Banks are now instructed to process all foreign exchange transactions related to coffee exports in accordance with the applicable export proceeds directive currently in force.

For previously submitted export contracts that have not yet been fully registered, the NBE will continue issuing export permits on a transitional basis. However, the Bank will no longer accept new contract registrations or issue permits for new transactions. Going forward, all new coffee export approvals must be processed directly through the CTA's digital portal.

8. Tax Clearance Now Mandatory for Property and Vehicle Transfers in Addis Ababa

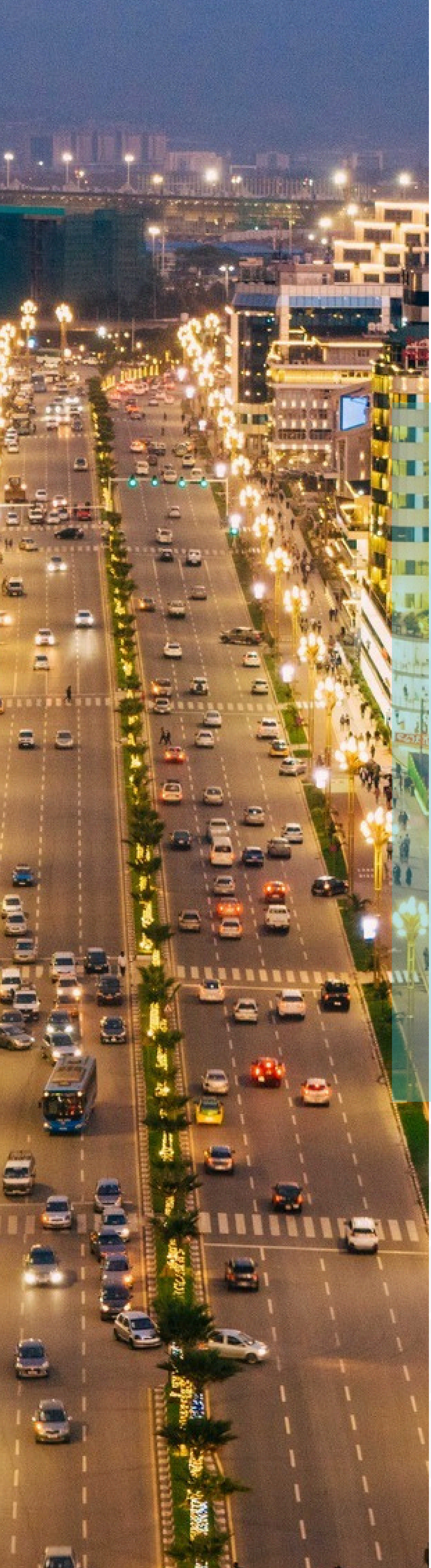
In a recent directive issued to the Addis Ababa Land Development and Management Bureau, the Addis Ababa Land Holding Registration and Information Agency, and the Addis Ababa Transport Bureau, the Addis Ababa City Government Revenue Bureau has introduced stricter compliance measures governing the transfer of immovable property and vehicles, including code-designated automobiles. Under the new enforcement regime, no transfer shall proceed without the presentation of a valid tax clearance certificate.

The Revenue Bureau emphasized that municipal services and development initiatives rely heavily on tax revenue. Accordingly, it has made tax compliance a precondition for asset transfers, positioning the directive as part of a broader strategy to enhance domestic resource mobilization and improve fiscal integrity within the city.

Citing Article 39(4) of the Federal Tax Administration Proclamation No. 983/2016, the Bureau reiterated that immovable property and vehicles may be subject to seizure to satisfy outstanding tax obligations. The directive reflects a shift toward coordinated enforcement among municipal institutions to close compliance gaps and combat tax evasion.

Effective immediately, all concerned institutions have been instructed to fully implement this requirement. No transfer of title, registration, or related transaction may be processed in the absence of documentary evidence confirming that all applicable tax liabilities have been settled.

This development signals a growing emphasis on the integration of tax compliance into public service delivery, with the aim of fostering accountability and ensuring that the fiscal obligations attached to property and vehicle ownership are met in full.



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