



Finance Bill, 2021 and TP: What should taxpayers expect?

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Presentation outline



- Introduction
- Definition of Control
- Permanent Establishment
- Thin Capitalization provisions
- Country by Country (CbyC) Reporting



Definition of Control

Control Definition



“Control” has been defined to include:

- Direct or indirect ownership of $\leq 20\%$ of the voting rights in a company
- Advancing a loan to another person and that constitutes $\leq 70\%$ of the BV of the borrower’s total assets
- A guarantee that constitutes $\leq 70\%$ of the total indebtedness

Control Definition



- Power to appoint more than half of the board of directors or at least one director or executive member of the governing board
- Ownership or exclusive rights over intellectual property
- Supplying $\leq 90\%$ of the purchases of the other person or influences pricing or other conditions relating to such supply

Control Definition



- Purchasing $\leq 90\%$ of the sales of another or influences pricing or conditions related to the sales
- A person dealing or relating with another in a way which the commissioner deems to constitute control

Implications?



- Reduced control threshold
- Broadened definition of control
- Rectifies the omission by Tax Laws Amendment Act, 2020
- An appreciation of other forms of control
- Increased TP compliance burden for taxpayers



What constitutes a Permanent Establishment?

PE Definition



- A fixed place of business
- A building site, construction, assembly or installation project or any supervisory activity > 183 days
- Provision of services including consultancy services through employees or other personnel > 91 days

PE Definition



- An installation or structure used for exploration of natural resources ≥ 91 days
- Dependent agent - habitually concluding contracts or playing a material role in the conclusion of contracts
- Does not apply where the activities are of a preparatory or auxiliary character

Implications



- Clarity on covered activities and qualifying durations
- The exception in line with the OECD Model Tax Convention on Income and Capital
- Halving of the relevant qualifying periods for consultants providing services
- Expanded definition - a warehouse, farm, plantation and a sales outlet

Implications



- Seeks to counter the artificial avoidance of PE status through the splitting of contracts - BEPS 7
- Increased risk of crystallizing a PE
- Taxpayers to ensure that transfer pricing outcomes are aligned with value creation
- PEs subject to TP compliance



Additional reporting by MNEs

- Ultimate parent entity (UPE) of a multinational enterprises group (MNE) to submit a return
- The return to contain the group's financial activities in and outside Kenya
- Should be submitted not later than 12 months from the last day of the group's financial year

An “Ultimate Parent Entity” is defined as an entity that:

- ✓ Is resident in Kenya for tax purposes
- ✓ Is not controlled by another entity
- ✓ Owns and controls an MNE group



- Multinational Enterprise Group - defined as a group that includes two or more enterprises that carries on business through a PE or through any other entity in another jurisdiction

CbyC Reporting - Key metrics



The return should contain the following:

- Total revenue
- Profit or loss before tax, income tax paid, income tax accrued
- Stated capital
- Accumulated earnings
- Number of employees and tangible assets

CbyC Implications



- Align with the OECD Base Erosion and Profit Shifting (BEPS) Action 13
- Only applies where UPE is based in Kenya
- Enhanced transparency and scrutiny of MNEs tax matters
- Greater information sharing-The Multilateral Convention on Mutual Administrative Assistance in Tax Matters (MAAC)



Overhaul of the Thin Capitalization provisions

Thin capitalization



- New provisions governing non-deductible interest payments
- Gross interest paid or payable to related persons and third parties in excess of thirty per cent (30%) of EBITDA
- Any income exempt from tax shall be excluded in the calculation of EBITDA (Tax sheltered income)

Thin capitalization



- Will apply to:
 - ✓ Interest on all loans
 - ✓ Payments that are economically equivalent to interest
 - ✓ Expenses incurred in connection with raising the finance

Implications



- Significant overhaul of the current provisions
- Aligns to international best practice - BEPS 4 - excessive interest/financing exempt income?
- Highly geared entities will be adversely affected due to the low threshold (30%)
- Potential impact on selected sectors eg financial institutions and power generation
- Tax EBITDA? Capitalized interest? Interest income?

Questions & Answers



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