



PERMANENT ESTABLISHMENTS IN KENYA

Where a non-resident operates or does business in Kenya without incorporating or setting up a business vehicle in Kenya, it would be important for such a person to review their Permanent Establishment ("P.E") status in light of the Kenya Income Tax Act provisions and such other relevant laws as may be applicable.

Globally, countries either operate under an income-based or a source-based tax regime. In many instances, countries would borrow from both extremes. Kenya essentially operates a source-based tax regime and effectively taxes all income accrued in or derived from Kenya. In essence therefore, Kenya would tax all residents and non-residents. Non-residents can either have a permanent establishment in Kenya or have absolutely no fiscal presence. Non-residents with no fiscal presence are taxed through the withholding tax system, where withholding tax is applicable, whilst those with a permanent establishment are taxed through the corporate tax system. There are very minor differences in the taxation of Kenyan residents and that of non-residents who have permanent establishments. These include:-

Tax	Resident company	Non-resident with a permanent establishment
Corporation tax	30% plus withholding tax on dividend distribution.	37.5% of the net income attributable to the P.E which is a final tax.
Deductibility of expenses	All expenses wholly and exclusively incurred for the generation of taxable income	All expenses wholly and exclusively incurred for the generation of taxable income are fully deductible save for interest,

	are fully deductible, subject to the ITA provisions.	management fees, royalties paid by the P.E to its non-resident head office. In addition, exchange losses incurred by the P.E on transactions with its non-resident head office not deductible.
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Prior to 2014, a Permanent Establishment was defined in the Income Tax Act as a fixed place of business in which a person carries on business and which has existed for six months or more. The Finance Act 2014 expanded this definition to include a person's dependent agent as a P.E. Specifically, a dependent agent is defined as a person with the authority to conclude contracts in the name another person. Even with the expansion, the definition is still not as wide as the OECD definition which is also based on the fixed place of business test and dependent agent test. Under the OECD, the concept of "fixed" extends to include any place of business with a certain degree of permanence.

Under the Kenyan laws, the possible tax exposures/risks that would arise where a non-resident person is deemed to have a P.E (assuming the P.E is not formalized) include the following:-

- i. The Kenya Revenue Authority is likely to establish the total turnover/revenue earned by the P.E from its Kenyan operations and effectively impose income tax on such income i.e. corporation tax at 37.5%. This tax is likely to be applied to the net income attributable to the P.E and it is also likely that the KRA would reject any expenses/costs that are attributable to the generation of such income effectively taxing the total net income; and
- ii. Where a P.E exists, a non-resident person would essentially move from doing business with Kenya to doing business in Kenya. In effect, the Kenyan tax laws including Value Added Tax would be applicable. As such, the treatment of any supply of goods or services would be subject to the provisions of the Kenyan VAT Act.

In view of the above, we highly recommend that all non-residents doing business in Kenya, review their operations in light of the above provisions. In the event that a P.E exists, all such persons should formalize the P.E in Kenya, either through incorporation of a business vehicle or registration of a branch in Kenya. This would mitigate against the adverse tax implications that are likely to ensue where a P.E is deemed to be in existence.



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For any further information regarding Permanent Establishments in Kenya, please contact Faith Muia on FMuia@vivaafriallp.com or contact us on info@vivaafriallp.com

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