CORPORATE STRUCTURING

Local and Foreign New Entrants

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Corporate Structuring for Local and Foreign New Entrants

- **Limited Liability Company**

An LLC is a common entity considered by promoters looking for a chance to minimise exposure to liability as promoters. It needs at least one member, and a maximum of 50 - other than an employee who is a shareholder, a member does not include an employee, cannot invite members of the public to subscribe to its shares, and shares held jointly are considered owned by one member. While an LLC cannot invite the public to subscribe to its shares, it is allowed to invite private offers to a maximum of one hundred persons in Kenya as per the guiding legislation.

- **Public Limited Company**

A company may become a public company by registering as a plc, going against the private offers' limitation provided for under the law, converting to a plc or when intending to seek authorization to be listed. Companies falling under this category have an intense level of statutory compliance.

- **Unlimited Liability Company**

Companies Act, 2015 (Act) provides that Unlimited Liability Company has no limit on matters liability of its members. The Act provides exemptions to ULC to lodge financial statements with the Registrar of companies upon meeting a certain set of conditions. If the ULC allots shares that are not uniform from previously allotted shares, it must lodge documents with the Registrar of Companies to have the shares registered.

- **Limited Liability Guarantee**

Companies Act, 2015 (Act) provides that companies limited by guarantee do not have shares. The liability of members is limited to the amount the members undertake as per the Articles of Association to contribute in the event of a liquidation. However, the Act does not restrict companies limited by guarantee that existed before the Act to have share capital.

s 5 of the Act provides that a company is a limited company if it is limited by shares or guarantees. Further, a person who is not a member of the LLG does not have the right to participate in profits.

The registration process is a bit slow due to the background check conducted by the National Intelligent Services (NIS).

- **Limited Liability Partnership**

LLPs, which are regulated by the Limited Liability Partnership Act, provide protections similar to an LLC; however, it is considered a transparent financial structure. However, considering the maximum income tax applicable is the graduated 30%, it provides a better room for reducing tax burden compared to the LLC that attracts 30% Corporate Tax and 5% WHT towards residents having control of at least 12.5% and 15% WHT towards non-residents. LLPs have less statutory compliance requirements, equal tax deductions as an LLC, and easy to dissolve/close.

- **Community-Based Organisations**

CBOs are registered through the Ministry of East African Community (EAC), Labour and Social Protection. There are limited activities that a CBO can be used for, which includes business, community projects, crop farming, cultural or traditional activities, environmental conservation, financial services, fishery, health care, livestock rearing, poultry keeping, skills development, tourism, youth empowerment, merry-go-round, and table baking.

The registration requirements include minutes authorising the need to be registered, a list of members with identifications, the by-laws/constitutions/rules, and payment of the registration fee.

- **Branch**

A foreign company can set its presence in Kenya as a subsidiary or Branch. The liabilities of a Branch extend to the Parent Company (PCo.), hold the same name as the PCo., offer the same products or services as the PCo., and file accounts for the Branch and PCo.

A Branch's Corporate Income Tax (CIT) is 37.5% and does not apply tax deductions available for a subsidiary.

- **Sole Proprietorship**

Sole Proprietorship has no distinction with the business owner - which is mainly considered the trading name. As a result, when sued, the owner will equally be liable. For instance, if the sole proprietor's business name is "Future Example" and the owner is John Doe, when suing or getting sued, the court documents will indicate ***John Doe t/a Future Example*** and signs legal documents by his/her name.

However, the applicable taxes include the income tax and minimum tax. However, depending on the business model and performance, there are appropriate licenses and other indirect taxes.

- **Non-Governmental Organisations**

The registration process is a bit slow due to the background check conducted by the National Intelligent Services (NIS). However, LLG has proven beneficial for those interested in flexibility and unprecedented limitation to operate.

- **Trusts**

Trusts are regulated through various legislations such as the Trustee Act, Trustees (Perpetual Succession) Act, Public Trustee Act, Law of Succession Act, and their respective subsidiary legislations. Trusts are created for various reasons, and the most common one is the protection of assets or eases the succession process in favour of the Trust's beneficiaries. For purposes of registering a perpetual trust, the Trustees (Perpetual Succession) Act and Trustees (Perpetual Succession) Regulations are the applicable legislations.

- **Societies**

Societies Act regulates the formation of entities within the said legislation - some of the organisations falling under this group may include foundations (which can also be registered under LLG) and associations. However, Savings and Credit Co-operatives (SACCOs) are regulated through the Co-operative Societies Act, SACCO Societies Act, and subsidiary legislation.

General Information on Corporate Structures

For purposes of consistency, the term "undertaking" will be used to refer to all the above, while a specific entity will be referred by its legislatively acknowledged terminology like LLC, LLP, among others.

The promoters of a business need to understand the available undertaking about their respective operation models. Certain undertakings are not viable based on certain Government Agencies Licenses; for instance, certain activities cannot be licensed under certain undertakings.

Shareholding

The Companies Act, 2015 of Kenya's Laws allows sole shareholder and directorship of various sets of company models

Shareholding of an undertaking is likely to be affected where the undertaking is owned by a foreigner and requires licenses from Sector-Specific Government Agencies. Sector Specific Government Agencies such as the Capital Markets Authority, Communication Authority, Energy and Petroleum Regulatory Authority. These Government Agencies will require that specific percentage of the shares be allocated to a Kenyan Citizen.

Tax

Corporate Tax & Dividends Tax

Kenya's taxing system is developing to a Limited Partial Territorial Tax System (LPTTS), and it is also a member of the Organisation for Economic Co-operation and Development (OECD). As a result, Kenya develops its tax structures independently based on its generally assumed Territorial Tax System (TTS) and the OECD Guidelines' reliance. For instance, the Employee Stock Ownership Plan (ESOP) assessment under unquoted entities is guided by the OECD when submitted to the Kenya Revenue Authority (KRA) for consideration.

Tax is an essential factor for various types of promoters. These concerns are influenced by reasons of being local or foreign investors. In reference to serious local investors, corporate structuring or restructuring is essential to view the various implications and advantages the undertaking can harness to minimize its tax obligations.

Serious foreign investors will consider whether their primary country and Kenya have a Double Tax Treaty or Agreement (DTT/DTA), which provides a pleasant environment when effecting tax laws. Kenya has 11 effective DTTs with: Canada, Denmark, France, India, Iran, Norway, Sweden, United Kingdom, Zambia, and South Africa.

The mere fact that Kenya has no DTT with other countries does not make Kenya a hostile environment on matters tax since Kenya's taxing system lingers on LPTTS and TTS. This is advantageous to a foreign investor since the tax is based on source, which must have arisen from Kenya. However, the foreign investor's country may have an Extensive PTTS that results in double taxation, and it may make it harsher if the foreign investor's country does not provide tax credits in reference to tax already paid in Kenya.

As a result, it is always advisable for the foreign investor to register another company in a country with a low corporate tax or, essentially, one with a TTS that will act as the shareholder in the Kenyan-based undertaking. To enhance an undertaking's corporate profile and rating, it is advisable to register the undertaking in a country not classified as a tax haven.

Indirect Taxes

In most instances, the promoters tend to focus on Corporate Tax and Withholding Tax on the Dividends. However, other indirect taxes affect the operation of a business. Some of the indirect taxes include minimum tax, V.A.T., excise tax, customs taxes, among others. An undertaking's business model will always attract certain indirect taxes while others remain consistent across the market.

Holding Company Structures

Tax structures attract the use of a Holding Company (HCo.). It is vital that while considering a country with a TTS, one should also consider the question of whether that country provides for a better HCo. regime that is suitable to the intended corporate structure.

Internal Financial Relationships

A group of foreign investors will develop Internal Financial Relationships (IFRs) with the subsidiary or branch. Depending on the adopted undertaking structure, tax laws will apply differently when it comes to effecting deductions. Some of the deductions in question result from the IFRs, hence, the need to consider the structures put in place.

IFRs can be due to financial facilities, Intellectual Property Licenses, and partnership projects. The Transfer Pricing Regulations guide these IFRs to avoid creating loopholes that an undertaking would use in tax evasion. The simple concept behind the Transfer Pricing Rules under IFRs is to encourage arms-length relationships between related or associated undertakings.

Licenses, Permits, and Approvals

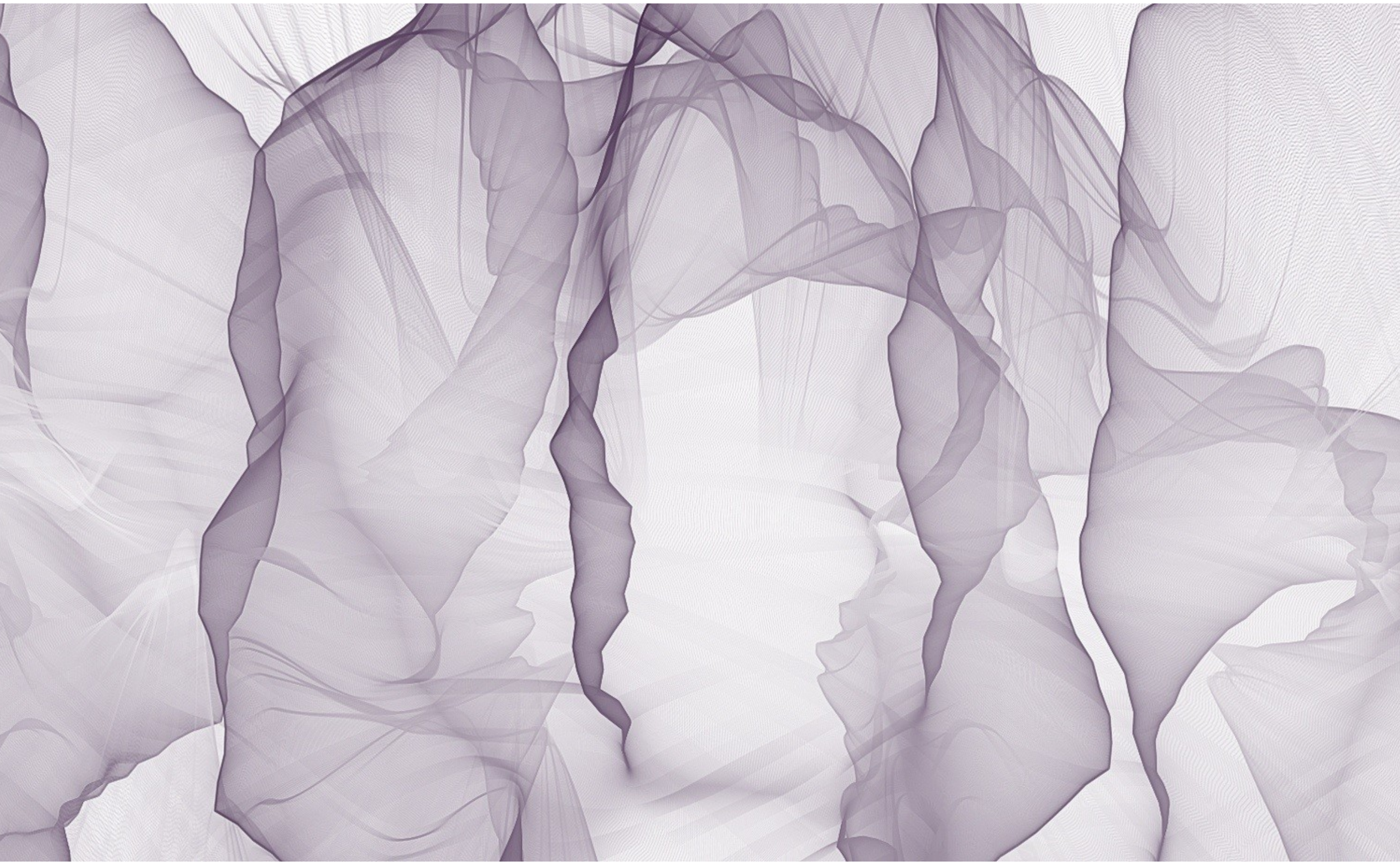
The formation of an undertaking results in securing licenses, permits, and approvals that will enable the undertaking to operate with ease within a given market. Detailed analysis must be provided on the intended undertaking prior to formation and the market it is targeting.

Foreign Direct Investment

The Foreign Investment Protection Act (FIPA) provides room for Kenya and other countries or groups of countries to formalise a favourable investment environment for their respective nationals. Currently, the Kenyan Government has established relationships with the French Republic, Republic of Finland, Swiss Confederation, Islamic Republic of Iran, Republic of Burundi, OPEC Fund for International Development, State of Kuwait, Slovak Republic, Republic of Mauritius, and the Republic of Korea.

The DTTs enhance a cordial FDA for foreign new entrants that can maximize on the DTTs or network of companies within the DTTs countries.

In a recent judicial jurisprudence, companies have invoked the Constitution on matters discrimination. The companies invoked Kenya's FIPA and Constitution's provisions to establish that certain laws were discriminative towards foreign-owned companies to a certain degree of practice, formulation of legislation, or policies.



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