



CHOOSING BETWEEN A BRANCH AND A SUBSIDIARY IN KENYA: *Key Tax Considerations*

Foreign entities wishing to establish a presence in Kenya largely have a choice between registration of a Subsidiary or a Branch. The main difference between the two entities is that a Subsidiary is considered a separate legal entity from the Parent Company whereas a Branch is not a separate entity, but an extension of the Parent Company. The choice between the two depends on the business approach one wishes to take.

INCORPORATION

A Subsidiary in Kenya is registered as a local company under Part II of the Companies Act, 2015 and is considered a separate legal entity distinct from its parent company notwithstanding that it is controlled by the parent company.

Incorporation of a Subsidiary would include providing a memorandum and articles of association, details of directors and shareholders, a statement of nominal capital and obtaining any of the necessary licences and permits. Subsidiaries would also be required to file annual returns with the Registrar of Companies as well as file annual returns.

As a general principle a parent company is not liable for the actions and liabilities of a subsidiary. A Subsidiary is considered resident for tax purposes.

A Branch on the other hand, is registered as a foreign company under Part XXXVII of the Companies Act, 2015 and is not a separate legal entity but an extension of the parent company. The parent company is fully liable for its actions and liabilities. Branches in Kenya are considered non-resident for the purpose of taxation.

Incorporation of a Branch involves providing the foreign company's Certificate of Incorporation, constitution and the details of directors and shareholders. Compliance requirements include maintenance of a registered office, annual filings with Registrar of Companies as well as tax filings with the KRA.

TAX IMPLICATIONS:

Income Tax

Corporation tax in a subsidiary will be similar to that of a resident company where the rate is 30%. A subsidiary will also be entitled to any local tax benefits available to resident companies.

Payments made by a Subsidiary entity to its Holding company are subject to Withholding Tax (**WHT**), since they are seen to be payments in different legal entities. Withholding Tax rate is 15% on dividends made to the holding company.

On the other hand, Branches in Kenya are taxed at 30% with additional tax on repatriated income using a prescribed formula to be used to compute

the repatriated income.

Section 7B of the Income Tax Act (ITA), states that:

*7B. (1) A non-resident person who carries on business in Kenya through a permanent establishment shall pay tax on **repatriated income** for the year of income.*

(2) The repatriated income under subsection (1) shall be computed using the following formula—
 $R = A1 + (P - T) - A2$

Where— R is the repatriated profit;

A1 is the net assets at the beginning of the year;

P is the net profit for the year of income calculated in accordance with generally accepted accounting principles;

T is the tax payable on the chargeable income; and

A2 is the net assets at the end of the year.

(3) The tax imposed under this section shall be in addition to tax chargeable on the income of the permanent establishment under section 4.

(4) For the purposes this section, “net assets” means the total book value of assets less total liabilities for the year of income and shall not include revaluation of assets.’

Repatriated profits refer to foreign-earned profits or financial assets that are sent back to a foreign company's / Branch's country of establishment, after deduction of any tax obligations in the Branch's country of residency.

Section 10 (3) of the ITA further states that:

(3) Where a payment has been made to a non-resident person, withholding tax paid thereon shall not be refundable or available for deduction against the income where an audit adjustment has been made in respect of such payment.’

Following the above, the ITA prescribes a tax rate of 15% equivalent to the withholding tax rate applicable on dividends paid by a resident company to a non-resident shareholder. This tax measure places the tax rates for Branches at par with resident companies operating in Kenya.

Value Added Tax (VAT)

An Entity is required to register for VAT if it is making or expecting to make taxable supplies of

over KES 5 million in a 12-month period. Supplies which are exempt from VAT are provided for under the First Schedule of the VAT Act.

A Branch or Subsidiary dealing in supplies attracting VAT will be liable for VAT payment where the taxable supplies are made for the consumption of Kenyan consumers. The taxable value for payment of VAT is the consideration for the supply which includes any taxes, duties, levies, fees, and charges paid or payable on or by reason of the supply.

Excise Duty

Excise duty is not a direct tax, it is an indirect tax charged on the importation, local manufacture of certain products, and supply of excisable services. The tax is levied on the producer or supplier, who passes the tax onto the consumer by including it in the product's price.

An entity, whether a Branch or Subsidiary, will only pay Excise Duty if it deals in excisable goods or services in Kenya. Excisable commodities include items such as bottled water, soft drinks, cigarettes, alcohol, fuels, and motor vehicles, while excisable services include services such as telephone and Internet data services, fees charged for money transfer services, and other fees charged by financial institutions. Under the Excise Duty Act, there are different rates of excise duty charged on different goods or services in Kenya.

Employment Taxes

Where an employer is determined to be a Kenyan incorporated entity, being either a Branch or Subsidiary, it will be required to account for tax on behalf of its employees, through the PAYE mechanism. The general position in Kenya is that emoluments provided by an employer to an employee are taxable under the PAYE system.

Employers (whether a Branch or Subsidiary) are also required to make statutory deductions and contributions in relation to the following:

1. National Social Security Fund (NSSF)
2. Social Health Insurance Fund (SHIF)
3. Affordable Housing Levy (AHL)
4. National Industrial Training Authority (NITA) Levy

Late payment/failure by an employer to account for income tax or any statutory contribution will lead to exposure to liabilities in the form of penalties and interests.

TRANSFER PRICING CONSIDERATIONS

Transactions between a Kenyan resident person and non-resident parties are required to be undertaken on arm's length basis pursuant to the Income Tax (Transfer Pricing) Rules, 2006 (TP Rules). The Commissioner is empowered to adjust the profits accruing to a resident person to reflect such profit as would have accrued if independent persons dealing at arm's length had been involved in a transaction.

Essentially, in Kenya, all companies that belong to a group of companies, whether local or foreign, are treated independently. TP Rules became effective from 1st July 2006 and borrowed significantly from the Organisation for Economic Co-operation and Development (OECD) Transfer Pricing Guidelines. The TP Rules apply to:

- Transactions between associated enterprises within a multinational company, where one enterprise is located in, and is subject to tax in, Kenya, and the other is located outside Kenya [**Subsidiary**]; and
- Transactions between a permanent establishment and its head office or other related branches, in which case the permanent establishment shall be treated as a distinct and separate enterprise from its head office and related branches [**Branch**].

What this means is that any Branch or Subsidiary present in Kenya must comply with these transfer pricing rules in Kenya. A Branch or Subsidiary that seeks to prove that the transactions between the entity and its non-resident Head Office or Parent Company are carried out on arm's length basis, will be required to:

1. Develop an appropriate transfer pricing policy;
2. Determine the arm's length price as prescribed under the guidelines provided under the Transfer Pricing Rules; and
3. Avail documentation to evidence their analysis upon request by the Commissioner.

SUMMARY

A summary of the above is captured in the table below:

Aspect	Subsidiary	Branch
Legal Status	Separate legal entity, incorporated under Part II of the Companies Act, 2015	Not a separate entity, but an extension of the parent company, registered under Part XXXVII of the Companies Act, 2015
Liability	Parent company not liable for actions and liabilities of the subsidiary	Parent company fully liable for branch's actions and liabilities
Tax Residency	Considered resident for tax purposes	Considered non-resident for tax purposes
Income Tax	Corporate tax at 30%	Tax at 30% on profits + 15% Branch Repatriation Tax on repatriated profits

Profit Repatriation	N/A	Repatriated income subject to 15% tax (equivalent to dividend WHT)
Withholding Tax	Dividends paid to parent subject to 15% WHT	Dividends paid from the Kenyan Branch to the foreign entity subject to 15% WHT
Value Added Tax (VAT)	Must register if taxable supplies exceed KES 5M in 12 months; charge 16% on taxable supplies (unless exempt/zero-rated)	Same requirement — must register for VAT if taxable supplies exceed KES 5M
Excise Duty	Payable only if dealing in excisable goods/services (e.g., alcohol, fuel, telecoms, financial services)	Same as subsidiary — applies only if branch supplies excisable goods/services
Employment Taxes	As an employer, required to account for PAYE, NSSF, SHIF, NITA and AHL	As an employer, required to account for PAYE, NSSF, SHIF, NITA and AHL
Transfer Pricing	Transactions with non-resident parent subject to Transfer Pricing Rules, 2006	Transactions with head office or related branches also subject to Transfer Pricing Rules; branch treated as a distinct entity for TP purposes
Compliance Requirements	Local board of directors, annual filings with Registrar of Companies, tax filings with KRA	Maintain registered office, annual filings with Registrar, tax filings with KRA

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