Who we are

At EY, we are 230,000 people based in 728 offices in 150 countries, organized into 28 Regions and four Areas.

All of our people work in one of our service lines – Assurance, Advisory, Tax, and Transaction Advisory Services (TAS) – or in Core Business Services (CBS) which provides internal operational support such as HR and IT services.

EY is committed to doing its part in building a better working world. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY Eastern Africa Tax Services

EY has been in Eastern Africa for over 87 years and has acquired a unique perspective and experience on the region’s business practice. This experience, pooled with our global resources, adds immense value to our clients.

EY’s tax professionals in the Eastern Africa region provide you with deep technical knowledge, global and local, combined with practical, commercial and industry experience. The firm has a network of six (6) offices in the region: Kenya, Uganda, Rwanda, Tanzania, Ethiopia and South Sudan with over 500 professionals. The South Sudan practice has an office in Juba, Tong Ping area. Clients in Somalia and Djibouti are served from Nairobi while clients in Burundi are served from Kigali, Rwanda.

Our talented people, consistent methodologies and unwavering commitment to doing our part in building a better working world, help you to build the strong compliance and reporting foundations and sustainable tax strategies that help your business achieve its ambitions.
In Tax, we have more than 50,000 people globally who help our clients understand and manage their tax compliance and reporting obligations responsibly and proactively. We help them assess, improve and monitor their tax function’s processes, controls and risk management and maintain effective relationships with the tax authorities.

Tax has six sub-service lines which cover a wide range of issues: Business Tax Services, Global Compliance and Reporting, Indirect Tax, International Tax Services, People Advisory Services and Transaction Tax.

What we stand for

Our positioning, the difference to which we aspire, is to be known for having the highest performing teams, and delivering exceptional client services, worldwide.

Our positioning

What we stand for

- At EY we are committed to helping our people our clients, and our wider communities achieve their potential. It’s how we make a difference.
- It’s about 230,000 people working together to help each other develop and succeed professionally and personally. It’s about helping our clients deliver on their promises to their markets and shareholders. And it’s about making a difference in the communities.

Our values

Who we are

- People who demonstrate integrity, respect and teaming.
- People with energy, enthusiasm and the courage to lead.
- People who build relationships based on doing the right thing.

Quality as a constant

Building a better working world

- Every day, every EY person is part of building a better working world - for their clients, their families, their communities and themselves. Everything they do - every audit, every tax return, every interaction with a client or colleague - contributes to making the working world better than it was. But, we aspire to do more. And we believe, that through a shared agenda with our clients and stakeholders, we can achieve more together.
Insurance sector in Kenya

In Kenya there are a total of 49 insurance companies, 5 reinsurance companies and 198 insurance brokers. There are a total of 5,155 insurance agents in Kenya. The Insurance Regulatory Authority (IRA) is the regulator of all insurance companies in Kenya, with a mandate to regulate, supervise and develop the insurance industry in Kenya.

The minimum paid-up capital has been set at Kshs 600M, Kshs 400M, Kshs 1B and Kshs 500M for the general, long term, general business reinsurance and long term business reinsurance. The overall insurance penetration (gross premiums as a percentage of GDP) has been estimated to be around 3.1%.

Kenya’s ratio of insurance companies to total population stands at 1.1x, with 49 insurers serving approximately over 44M people, compared to South Africa’s 171 insurance companies for 54M, Ghana’s for 52 insurance companies for 26M and Nigeria’s 60 insurance companies for 181M.

Our promise to our clients:

◊◊ We believe that through collaboration with clients and stakeholders we can more effectively address the challenges the working world faces and together be part of the solutions ◊◊
Recent developments in the sector

Mergers, Acquisitions and Restructuring:
There has been several mergers and acquisitions affecting the insurance sector in a bid to take advantage of synergies and also as a way of the larger companies diversifying into both general and life businesses.

Notable acquisitions in 2015 included the acquisition of Real Insurance by Britam, Pan Africa insurance acquiring a 51% stake into Gateway insurance to grow its general business line, the UAP-Old Mutual merger and Jubilee Holdings partnering with DRC's State-owned insurance company Sonas to offer medical and life cover products.

Entry of Global Brands:
Given the low penetration rates in the country, global brands have ventured into the region with Saham Group acquiring Mercantile Insurance, Prudential Financial Company (UK) acquiring Shield Assurance Company and Swiss Re buying a stake into Apollo Group. The entry targeted at one of the fastest growing regions in the world.

Adoption of the Risk Based Supervision (RBS):
The IRA is planning to introduce new capital requirements based on the nature of business carried out by the insurers to try and match the risk activities of organizations to their core-capital.

Diversification of Investments:
Insurance companies in Kenya have actively ventured into the real estate segment particularly in the office space segment with the Britam and UAP towers coming up during the year. The adoption of asset management by CIC and Pan Africa insurance has also seen the sector further diversify revenue streams aiming to grow their investment incomes.

Launch of Mobile Insurance Products:
New products have also come into the market to improve the process of premium collection with partnerships like the Orange Bima from a partnership by CIC, and Airtel also partnering with Pan Africa Life Assurance Limited and MicroEnsure to create an insurance product covering Airtel customers in Kenya offering access to free life, accident and hospitalization insurance based simply on how much they spend on the network.

Innovative Channels of Distribution:
Insurance companies have come up with alternative channels of distributing their products, including partnering with banks through bancassurance and the introduction of premium payments through mobile channels.

Lower Investments Returns:
Given Insurance companies in Kenya hold at least 8% of total government bills and bonds, volatility of interest rates and subsequently yields on government bonds adversely affect mark to market investment returns. The poor performance of the equities markets in 2015 also adversely affected the sectors.

Introduction of Islamic Finance:
The finance bill 2017 introduced the definition of what constitutes Islamic Finance. The bill amended section 2 of the Income Tax Act to recognize this definition which was put as “Islamic finance arrangement” means all financial arrangements, including transactions, instruments, products or related activities that are structured in accordance with Islamic law; while “Islamic finance return” was defined to mean any amount received or paid in relation to Sukuk or an Islamic finance arrangement; we believe the main aim of this is to recognize the rapid growing Islamic financial institutions and products in the market.
Tax issues in the Insurance sector in Kenya

Excise duty
The Finance Act 2012 introduced a 10% excise duty on fees charged for money transfer services by cellular phone service providers, banks, money transfer agencies, other financial service providers and other fees charged by financial institutions. Through the Finance Bill 2013, insurance companies have now been included in the definition of “financial institutions” which is the term that has replaced “financial service providers”. The Bill also defined the term “other fees” as “fees, charges or commissions charged by financial institutions but does not include interest”.

In light of the above, all persons licensed under the Insurance Act are now required to start collecting from their customers a 10% excise duty on any fees, charges or commissions and remitting the same to the KRA. The effective date of this amendment was 18 June 2013 with the first return expected to have been submitted to the KRA on or before the 19th of July 2013.

Revenue recognition
Unquestionably, what IFRS 9 Financial Instruments means for financial institutions in terms of new challenges and complexities, the new IFRS 15 Revenue from Contracts with Customers means for corporate institutions. Although financial institutions’ reporting is currently focusing on IFRS 9, IFRS 15 will not bypass the financial services industry without tangible effect because of its potential impact on the amount and timing of revenue recognition. The IASB (International Accounting Standards Board) recently revised the effective date of the standard to 1 January 2018 from its original 1 January 2017, giving companies more time to prepare for this change.

IFRS 15 applies to various revenues generated by banks or insurance companies, such as fees, commissions and other income that may result from servicing loans, asset management, custody services, pension administration, insurance broking or claims handling, but are not limited to those.

Financial institutions will need to evaluate the challenges when planning their transition to IFRS 15. The new standard will require the allocation of transferred prices more often to separate performance obligations that also tend to be at a later point of time than required under the current revenue recognition standard. Moreover, the amortization of costs generated to obtain a contract will require judgment of users of the standard. Presented below are some of the taxes that an insurance company would be exposed to:
Presented below are some of the taxes that an insurance company would be exposed to:

1. Corporation tax
   1.1. Introduction
   Insurance companies are recognized as Financial Institutions - 4th Schedule of Income Tax Act (ITA). Insurance companies include a mutual or proprietary company deemed to be an insurance company. Taxation is governed by Section 19 of the ITA - which covers both resident and non-resident insurance companies. The taxation basis of life business is distinct from general business. When an insurance company carries on life and general business (composite), the life insurance is treated as a separate business for taxation purposes.

   Taxation of Residents - Section 19(5) & (5A)
   • “Actuarial surplus” - Difference between the market value of the life fund assets and the actuarial liability plus a defined margin.
   • “Excess expenditure” - Difference between total management expenditure during the year and permitted expenditure.
   • “Permitted expenditure” - Amount prescribed by the Insurance Act regulations and it is a percentage of the amount of premiums received during the financial year, depending on the class of business written. Outlined in the Insurance form 70-1.
   • The amount of the actuarial surplus transferable is limited to a maximum of 30% of the total surplus at year end (S46(5) of Insurance Act).
   • The actuarial valuation basis is a very important element of taxation of the life insurers because it determines the quantum of surplus and hence the quantum of inter-fund transfers.
   • The valuation basis should have the following qualities;
     • Should be prescribed, reasonably stable and realistic.
     • The Insurance Act provides for this basis and has since been updated to be more realistic by changing the mortality tables used (Finance Act 2011).

1.2 Life Business
   Key terms
   • The components of taxable income of a life business are;
     • Actuarial surplus recommended for transfer for the benefit of shareholders.
     • 30% of excess expenditure (management expenses and commissions).
     • Other transfer from the life fund for the benefit of shareholders.
     • When the actuarial valuation of a life fund results to a deficit, the shareholders are required to inject money into the life fund.
     • Deficit treated as a negative transfer for tax purposes.
     • Limited to the amount of actuarial surplus recommended to be transferred by the actuary in previous years of income.
Taxation of Non-Resident - Section 19(6)

• The taxable income of a non-resident insurer consists of the same proportion of:
  • the recommended actuarial surplus transfer as the actuarial liability in respect of its long
term insurance business in Kenya bears to the actuarial liability in respect of its total life
business.
  • other transferable amounts from the life fund for the benefit of the shareholders as the
actuarial liability in respect of its long term insurance business in Kenya bears to the
actuarial liability in respect of its total life business.
  • 30% of the excess expenditure.

Illustration on Taxation of Non-Resident

Let:
• a - Actuarial liability in respect of business in Kenya
• b - Actuarial liability in respect of total long term business
• Thus Proportion = a/b

Therefore taxable income is sum of:
• a/b* actuarial surplus transferred
• a/b* Other amounts transferred
• a/b* 30% of excess expenditure

Taxation of Non-Resident - Section 19(6A)

• When the actuarial valuation of a life fund results to a deficit, the shareholders are
required to inject money into the life fund.
• The proportionate amount of the money so transferred is treated as a negative transfer
for tax purposes.
• Limited to the amount of actuarial surplus recommended to be transferred by the
actuary in the previous years of income.
• The proportionate amount transferred is;
• a/b * money injected (money transferred)
1.3. General Business

Key tax concepts

- “Expense apportionment” = \( \frac{c}{a} \times b \)
- where:
  - a - Investment income
  - b - Management Expense
  - c - Exempt Investment Income
- “Exempt income” - dividends from equity investments and income from disposal of investment shares traded in any securities exchange operating in Kenya.

- Taxation of Residents – Section 19(3)
  - Taxed like any other ordinary business
  - Taxable income include:
    - Net premiums; and
    - Any income derived from investments held in connection with that business.
    - Expenses are deductible excluding costs and expenses attributable to earning exempt income.
  - Basis of apportionment - Section 19(3)(c)(iii).
  - Taxable income adjusted in accordance to the provisions of Sections 15 and 16 of the Income Tax Act.

- Taxation of Non-Residents – Section 19(4)
  - The taxable income is calculated as:
    - Net earned premiums received or receivable in Kenya; plus
    - Any premiums paid on reinsurance to the head office of the company.

Additions:

- Other income received or receivable in Kenya including commission or expense allowance received from reinsurance, other than from the head office.

- Investment income as the Commissioner determines to be just & reasonable.

Deductions:

- Claims admitted and agency expenses incurred.
- A proportion as the Commissioner may determine to be just and reasonable of those expenses of the head office, as would have been allowable if the company was a resident company.
1.4. Composite Insurance Company
Taxable Income - Section 19(8)

The amount of gains or profits from insurance business, both from life insurance and from other classes of insurance, is taken into account together with any other income of the company charged to tax in ascertaining the total taxable income.

Tax Computation Format

<table>
<thead>
<tr>
<th></th>
<th>KShs</th>
<th>KShs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit as per Income statement</td>
<td></td>
<td>XX</td>
</tr>
<tr>
<td>Add: Disallowable deductions including expense relating to exempt investment income (Apportionment)</td>
<td>XX</td>
<td></td>
</tr>
<tr>
<td>Less: Allowable deductions</td>
<td>(XX)</td>
<td></td>
</tr>
<tr>
<td>Adjusted taxable income (loss)</td>
<td></td>
<td>XX</td>
</tr>
</tbody>
</table>

LC Ruling: Losses arising from either business can be offset against profit from either business to arrive at the ultimate taxable income / (loss)
Taxation of Insurance Holding Companies (Non-operating)

A holding company, whether Insurance or any other business’ core business is investments and holding of subsidiaries. The companies will therefore earn income mainly from Dividends from equity investment and from the subsidiaries, Interest income from both loans advanced to subsidiaries and those from funds invested in fixed deposits and management fees.

Dividends and interest income earned by a holding company is therefore business income and is taxable as such as provided for under section 3 (2) (i) of the Income Tax Act (ITA) and not under section 3 (2) (b) of the Act. These streams of income should therefore not be treated as exempt income unless the holding company receiving the dividend owning more than 12.5% of the shares of the company paying the dividend as provided for under section 7 (2) of the ITA.

1.5. Controversies on taxation of Life Business

a) Actuarial Surplus

KRA contends that 30% of transfer of surplus to the statutory reserve account is presumed to benefit shareholders

The above presumption is allegedly based on the provisions of Section 46 (5) of the Insurance Act;

“Notwithstanding subsection (1), an insurer may, for the purpose of declaring or paying a dividend to shareholders or a bonus to policy holders, utilize the surplus disclosed in the valuation balance sheet of a statutory fund set out in the actuary's abstract relating to an investigation made in pursuance of section 57 and accepted by the Commissioner, subject to the condition that the amount allocated or paid to the shareholders out of a statutory fund shall not exceed thirty per cent of the surplus disclosed therein after making the necessary adjustments to the surplus.”

Professional view

There is no presumption under Section 46(5) of the Insurance Act that 30% of the transfer to the reserve funds would automatically benefit shareholders. The 30% cap is aimed at protecting the interest of the policy holders.

Indeed, the determination of what constitutes benefit to the shareholders is subject to approval by the Commissioner of Insurance. The benefit to the shareholders from such transfer(s) could thus range from zero to 30%.

b) Taxable income under Section 19 (9)

Prior to year 2009, the total taxable income of an insurance company was determinable in accordance to the provisions under Section 19(9) of the Income Tax Act. The aforementioned section, which was deleted with effect from 1 January 2009, stipulated that;

“Where an insurance company conducts life insurance business, the gains or profits from insurance business for a year of income shall be the greater of - (a) the gains or profits of such a company as determined under section 19(8); or (b) the profits reported by such a company in its accounts required to be furnished in its return of income under section 54, provided the provisions of section 15(4) shall not apply in respect of a loss arising out of life insurance business.”

Professional view

According to Section 19(9), given a situation where the income determined under section 19(8) is lower than the accounting profit reported in the financial statements, the profit reported in the financial statements would constitute the taxable income for the entire insurance business without making any distinction between the general and life business profits. In this regard, the profit referred to under section 19(9)(b) is the total accounting profit before tax from both the general and life businesses reported in the company's accounts.
c) Transfers for the Shareholders’ benefit

Local Committee (LC) Ruling
KRA v Local insurance company: LC ruled that any transfer from the General fund to the Shareholders’ benefit are taxable (One sentence ruling).

Contentious Issue
What should be the treatment where the transfers relate to funds already taxed? For instance, funds could have been transferred from the retained earnings at the point when “statutory reserve” or “General reserve” was created.

Professional View
Transfers relating to funds / reserves already taxed should not be taxed since this would amount to double taxation.

Challenge
The ITA has not made specification on whether the transfer of already taxed funds should be exempt from tax.
2. Withholding Tax (WHT)

Withholding tax is deducted on specific payments made to both resident and non-resident persons in accordance with the provisions of the ITA. The payer acts as an agent for Kenya Revenue Authority (KRA).

The main payments that are subject to withholding tax include: agency fee, management or professional fee, consultancy fee, contractual fee, royalties, interests, dividend, among others. With effect from 1 July 2003 payments to a resident person of over KShs. 24,000 per month are subject to WHT. This applies to training, management & professional fees only.

Whether or not the payments are subject to withholding tax depends on the nature of the payment and whether they would fall under the above classification. The withholding tax rates applicable are detailed under the Third Schedule to the ITA. Lower rates for withholding tax are applicable on some payments to residents of countries that have a double tax agreement with Kenya. Kenya has double tax treaties with Canada, Denmark, Germany, India, Norway, Sweden, United Kingdom, Zambia, South Africa and France. The treaty provisions are automatically applicable and no consent or approval is required from KRA in order to use the rates.

Every company has an obligation to remit to the tax authority any taxes withheld by the 20th of the month following the deduction. Failure to comply with withholding tax rules exposes the company to principal tax that ought to have been paid by the service provider. Further the company would be subject to penalty of 10% of the amount of tax involved subject to a maximum of one (1) million Kenya Shillings and interest at a rate of 1% per month.

3. Excise Duty

Excise duty, commonly referred to as “sin tax” is a tax on the importation or local manufacture of certain products and the supply of excisable services.

All manufacturers, providers and importers of excisable goods and services should collect and account for excise duty. Excisable goods and services are listed in the 1st Schedule to Excise Duty Act, 2015. Excisable services include mobile and wireless phone services, fees charged for money transfer services and other fees charged by financial institutions.

Introduction of Excise duty on financial services

Excise duty on financial services was introduced in Kenya in 2012 through the amendment to the now repealed Customs & Excise Duty Act (Cap 472) of the Laws of Kenya. The amendment introduced excise duty on, inter alia, ‘other fees’ charged by financial institutions. Some contentious issues that came with the introduction of this duty were lack of clarity on who qualified as a financial institution, what constituted ‘other charges and thereby the commencement date.

These issues were addressed by the Finance Act 2013, where ‘financial institutions’ were defined to include ‘persons registered under the Insurance Act’ and ‘other fees’ were defined to include fees, charges or commissions charged by financial institutions but not including interest.

With the enactment of Excise Duty Act, 2015, further amendment were made where other fees were defined to includes any fees, charges or commissions charged by financial institutions relating to their licensed financial institutions, but excludes interest on loan or return on loan or an insurance premium or premium based or related commissions.
**Tax Point**

For excisable services, the tax is due when the services are rendered (earlier of the date services are performed, issuance of invoice or when payment is received in whole or part). The return for the same should be submitted on or before the 20th of the subsequent month following that of the tax point. Fines and penalties for non-compliance.

<table>
<thead>
<tr>
<th>Item</th>
<th>Fine/Penalty</th>
</tr>
</thead>
<tbody>
<tr>
<td>A person who undertakes an activity which requires a license without being licensed</td>
<td>Double the excise duty that would have been payable</td>
</tr>
<tr>
<td>Late filing of return</td>
<td>The higher of Kshs.20,000 and 5% of unpaid tax</td>
</tr>
<tr>
<td>Late payment</td>
<td>Simple interest @ 1% monthly rate on amount due</td>
</tr>
</tbody>
</table>
4. Customs Duty

Customs duties are charged on imported and some exported goods. Goods are imported in the country either for home consumption, warehousing, transit, temporary importation, Export processing Zone or re-export. If the goods are entered for home consumption, all applicable import taxes will be paid at the Customs Service Department. The duties applicable are categorised into:

- Import Duty
- Excise Duty
- VAT on imports
- Import Declaration fee (IDF)
- Railway Development Levy (RDL)

Import duty on goods originating outside EAC is charged at varying rates as per EAC Common External Tariff, 2012. The bases of charging duties are ad valorem (on price of the goods so declared) and specific units (on quantity, weight, number of measurement). Generally, customs duty rates range from 0% to 25%. However, for goods regarded as sensitive including sugar, wheat flour, rice, milk among others, the duty rates are higher than the normal 25% ranging from 35% to 100%.

Reduced rates are applicable on imports from countries in the COMESA region ranging from 0% to 1%. It is important to have a certificate of origin for the reduced rates to apply. The value of imported goods is determined in accordance with the General Agreement on Trade and Tariffs (GAAT) Valuation rules adopted in Kenya from January 2000. The value is based on Cost, Insurance and Freight (excluding air freight).

Goods liable to import duty may on first importation be warehoused without payment of duty in a government warehouse or a bonded warehouse, after which they may be entered for home consumption, exportation, removal to another warehouse, as stores for aircraft/vessel, re-warehousing, removal to an EPZ or removal to a free port.

Several goods are exempt from customs duty. These are as listed under Part A and B of the Fifth Schedule of the EACCMA.

Marine Insurance

Insurance Regulatory Authority (IRA) issued a public notice on 13 January, 2017, which provided guidance on the implementation of the local marine cargo insurance directive by the Cabinet Secretary for National Treasury (“CS”) in his fiscal year 2016/2017 National Budget presentation. The Public Notice inter alia confirms the effective date of the CS’s directive as 1 January, 2017. All importers are now required to insure their cargo using a local insurance entity as follows:

- The importer or the importer’s appointed clearing agent (“agent”) is required to purchase a local marine cover from a registered insurance company and obtain a certificate. This can be done through an insurance agent, broker or directly through the insurance company;
- The importer or agent should thereafter access the Kenya Trade Network Agency (“Kentrade”) system using their login credentials (user name and password) and create a Unique Consignment Reference (“UCR”) number;
- The importer or agent shall access the module for Marine Cargo Insurance (“MCI”) registration on Kentrade and link an application for marine cargo insurance with the UCR created above; and
- The application for marine cargo cover is then submitted online to one of the listed insurance companies (as per the importer’s choice).
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About EY

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