REPUBLIC OF KENYA
THE NATIONAL TREASURY AND PLANNING

EXPLANATORY MEMORANDUM TO THE AGREEMENT BETWEEN THE GOVERNMENT OF THE REPUBLIC OF KENYA AND THE GOVERNMENT OF THE REPUBLIC OF MAURITIUS FOR THE AVOIDANCE OF DOUBLE TAXATION WITH RESPECT TO TAXES ON INCOME

LEGAL NOTICE NO. 114 of 2020

PART I

Name of the Statutory Instrument:	Agreement between the Government of the Republic of Kenya and the Government of the Republic of Mauritius for the Avoidance of Double Taxation with respect to taxes on income
Name of the Parent Act:	The Income Tax Act (Cap. 470)
Enacted Pursuant to:	Section 41 of the Income Tax Act (Cap. 470)
Name of the Ministry/ Department:	The National Treasury and Planning
Gazetted on:	30th June, 2020

PART II

1. Purpose of the Statutory Instrument

To provide a legal framework for the elimination of double taxation of the residents of Kenya and Mauritius with respect to taxes on their income, without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance.

2. Legislative Context

The Agreement between the Government of the Republic of Kenya and the Government of the Republic of Mauritius creates a legal framework for use by the Revenue Authorities of the two countries for the avoidance of double taxation with respect to taxes on income.

3. Policy Background

The primary purpose of tax treaties is mainly 'for the avoidance of double taxation' of income arising from cross-border transactions. Double taxation stifles trade and investment between countries as it penalises businesses that trade between such two countries. Tax treaties also address other issues such as the prevention of tax evasion and non-discrimination. This ensures that businesses do not avoid taxation in the two contracting States. It also provides for the non-discrimination of businesses trading in the two countries.

Currently, there is no Agreement on the Avoidance of Double Taxation between Kenya and Mauritius. The Agreement between the two countries was therefore negotiated as a result of the need to have a legal framework for the administration of avoidance of double taxation with respect to taxes on income between the two countries.

4. Consultations Outcome

In the preparation and negotiation of the Agreement on the Avoidance of Double Taxation between Kenya and Mauritius, consultations were held with key stakeholders and the public. Consultative meetings were convened with the Kenya Revenue Authority, the Ministry of Foreign Affairs and the Office of the Attorney General to synchronize the underlying policy and legal matters. A Public Notice was also issued and uploaded on the National Treasury and Planning website soliciting views of the public by 18th May, 2020.

The consultations yielded useful feedback which was used to negotiate the final Agreement. The comments received included:

i) That Article 1 on "Personal Scope" needed to be beefed up to enhance clarity of the scope/circumstances under which the residents of the two countries will be taxed. This was done by adding Paragraphs 2 and 3 of Article 1.

ii) That clarity needed to be made on Article 4 on "Resident" to enhance the definition of "Place of Effective Management" to clarify on the treatment of a person other than an individual who is a resident of both Contracting States. This was addressed by adding paragraph 4 in Article 4.

iii) That Article 5 on "Permanent Establishment" should use the United Nations (UN) Model Double Taxation Agreement text to provide a more comprehensive definition of the term "Permanent Establishment" (PE). This was considered and the text used provides a comprehensive definition of "what constitutes" and "what does not constitute" a PE.

iv) That the proposed taxation rate of 5 percent for dividends under Article 10 on "Dividends" should be reviewed upwards. In addition, a provision should be made to allow for taxation (in accordance with the laws) of profits earned by a company which is a resident of a contracting State and has a PE in the other contracting State. The taxation rate was renegotiated and raised from 5 percent to 8 percent (paragraph 2 of Article 10). Paragraph 6 of Article 10 was introduced to provide for taxation (of profits earned by a company which is a resident of a contracting State and has a PE.

v) That the proposed rate of 10 percent for taxation of royalties under Article 12 on "Royalties" should be reviewed upwards. This was addressed by enhancing the taxation rate for royalties to 12 percent (Paragraph 2 of Article 12).

vi) That the Agreement should introduce an Article on "Technical Fees" to enable the country tax income earned by persons who come to offer technical services, such as consultancies. This was addressed by introducing Article 12A.

vii) That a provision should be made in Article 20 on "Students and Apprentices" to cover grants, scholarships and remuneration for employment by students and business apprentices. This was addressed by introducing Paragraph 2 of Article 20.

viii) That there was need to make a provision in Article 21 on "Other Income" to cover any other items of income of a resident of a Contracting State not dealt with in the other Articles of the Agreement. This was addressed by introducing Paragraph 3 of Article 21.

ix) That there was need to cover "stateless persons" in Article 23 on "Non-Discrimination". This was addressed by introducing Paragraph 1A in Article 23 which provides that stateless persons who are residents of a Contracting State shall not be subjected in either Contracting State to any taxation or any requirement connected therewith, which is otherwise or more burdensome than the taxation and the connected requirements to which nationals of the State concerned in the same circumstances, in particular with respect to residence, are or may be subjected.

x) That the Agreement should introduce an Article on "Entitlement of Benefits" to guide how benefit under the Agreement shall would be treated. This was addressed by introducing Article 27A.

5. Highlights of the Agreement

The Agreement provides the intention of the Government of the Republic of Kenya and the Government of the Republic of Mauritius desiring to conclude an agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income.

Article 1: Provides that the Agreement shall apply to persons who are residents of one or both of the Contracting States.

Article 2: Provides the scope of the taxes to be covered by the Agreement. The Agreement shall apply to taxes on income imposed on behalf of a Contracting State or its political subdivisions, irrespective of the manner in which they are levied. These will include all taxes imposed on total income or on elements of income

Article 3: The Article provides the general definitions of the terms used in the Agreement.

Article 4: Provides the meaning of the term “resident of a Contracting State”.

Article 5: Provides the meaning of the term "permanent establishment".

Article 6: Provides the meaning of the term "immovable property" and how income derived from Immovable Property shall be taxed.

Article 7: The Article provides how profits from business shall be taxed.

Article 8: Provides how profits of an enterprise from the operation or rental of ships or aircraft in international traffic shall be taxed.

Article 9: The Article provides how profits accruing to enterprises associated with the main enterprise shall be taxed.

Article 10: Provides how dividends shall be taxed. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State. However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of that State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed: (a) 5 per cent of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) which holds directly at least 10 per cent of the capital of the company paying the dividends; (b) 10 per cent of the gross amount of the dividends in all other cases.

Article 11: Provides how Interest shall be taxed. Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. However, such interest may also be taxed in the Contracting State in which it arises and according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 10 per cent of the gross amount of the interest. Interest arising in a Contracting State shall be exempt from tax in that State if it is derived and beneficially owned by: (a) the Government, a political subdivision or a local authority of the other Contracting State; or (b) any institution, body or board which is wholly owned by the Government, a political subdivision or a local authority of the other Contracting State.

Article 12: The Article provides how Royalties shall be taxed. Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. However, such royalties may also be taxed in the Contracting State in which they arise, and according to the laws of that State, but if the beneficial owner is a resident of the other Contracting State, the tax so charged shall not exceed 10 per cent of the gross amount of the royalties.

Article 12A: Provides how fees for technical services will be taxed. Fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other Contracting State in accordance with its laws. However, subject to the provisions of Articles 8, 15 and 16, fees for technical services arising in a Contracting State may also be taxed in the Contracting State in which they arise and subject to the laws of that Contracting State, but if the beneficial owner of the fees is a resident of the other Contracting State, the tax so charged shall not exceed 10% of the gross amount of the fees.

Article 13: Provides how Capital Gains shall be taxed. Capital Gains derived by a resident of a Contracting State from the alienation of immovable property situated in the other Contracting State may be taxed in that other State. Capital Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State including such gains from the alienation of such a permanent establishment (alone or with the whole enterprise), may be taxed in that other State. Gains from the alienation of ships or aircraft operated in international traffic or movable property pertaining to the operation of such ships or aircraft shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.

Article 14: Provides how salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment in the other Contracting State shall be taxed.

Article 15: The Article provides how Directors' Fees and Remuneration of Top-Level Managerial Officials derived by a resident of a Contracting State in his capacity as a member of the board of directors of a company which is a resident of the other Contracting State shall be taxed.

Article 16: Provides how income derived by a resident of a Contracting State as an entertainer or as a sportsperson, from his personal activities exercised in the other Contracting State shall be taxed.

Article 17: Provides how pensions and other similar payments arising in a Contracting State and paid in consideration of past employment to a resident of the other Contracting State shall be taxed.

Article 18: Provides how salaries, wages, and other similar remuneration, other than a pension, paid by a Contracting State or a political subdivision, local authority or statutory body thereof to an individual in respect of services rendered to that State or subdivision, authority or body shall be taxed.

Article 19: Provides that a professor or teacher who makes a temporary visit to one of the Contracting States for a period not exceeding two years for the purpose of teaching or carrying out research at a university, college, school or other educational institution in that State and who is, or immediately before such visit was, a resident of the other Contracting State shall, in respect of remuneration for such teaching or research, be exempt from tax in the first-mentioned State, provided that such remuneration is derived by him from outside that State.

Article 20: Provides that a student or business apprentice who is present in a Contracting State solely for the purpose of his education or training and who is, or immediately before being so present was, a resident of the other Contracting State, shall be exempt from tax in the first-mentioned State on payments received from outside that first-mentioned State for the purposes of his maintenance, education or training.

Article 21: Provides for how other income (not dealt with in the foregoing Articles of the Agreement) shall be taxed.

Article 22: The Article provides the procedure of how each of the two Contracting States will ensure that double taxation is eliminated. Both Contracting Parties will use the method of allowing a tax credit against the tax on income of that resident an amount equal to the tax paid in the respective Country. Such credit, however, shall not exceed that portion of the tax as computed before the credit is given, which is attributable, to the income, which may be taxed in the respective Country. In the case of Kenya, where, in accordance with the provisions of the Agreement, income derived by a resident of Kenya is exempt from tax in Kenya, Kenya may nevertheless, in calculating the amount of tax on the remaining income of such resident, take into account the exempted income.

Article 23: The Article provides for the non-discrimination of the nationals of a Contracting State, that such national shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances may be subjected.

Article 24: Provides for a Mutual Agreement Procedure which shall be followed where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of the Agreement.

Article 25: The Article provides how the competent authorities of the Contracting States shall exchange such information as is foreseeably relevant for carrying out the provisions of the Agreement or to the administration or enforcement of the domestic laws concerning taxes of every kind and description, insofar as the taxation thereunder is not contrary to the Agreement.

Article 26: Provides that nothing in the Agreement shall affect the fiscal privileges of members of diplomatic missions or consular posts under the general rules of international law or under the provisions of special agreements.

Article 27: Provides for the kind of assistance that the Contracting States shall lend to each other in the collection of revenue claims.

Article 27A: The Article provides how benefits under the Agreement will be treated. A benefit under the Agreement shall not be granted in respect of an item of income if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the Agreement. Where a benefit under the Agreement is denied to a person, the competent authority of the Contracting State that would otherwise have granted this benefit shall nevertheless treat that person as being entitled to this benefit, or to different benefits with respect to a specific item of income, if such competent authority, upon request from that person and after consideration of the relevant facts and circumstances, determines that such benefits would have been granted to that person in the absence of the transaction or arrangement. The competent authority of the Contracting State to which a request has been made under this paragraph by a resident of the other Contracting State shall consult with the competent authority of the other Contracting State before rejecting the request.

Article 28: Provides the procedures that shall be followed by each Contracting State in bringing the Agreement into force.

Article 29: The Article provides for the procedure to be followed by either of the Contracting States in terminating the Agreement.

6. Impact

The Agreement is expected to foster economic benefits to the two countries, including enhanced investment by residents of the two countries, removing or reducing double taxation on investment and removing tax discrimination on investors. The Agreement is also expected to foster greater diplomatic and political ties between Kenya and Mauritius.

7. Monitoring and Review

The Agreement will be implemented by the Kenya Revenue Authority and will be reviewed from time to time on need basis to assess its effectiveness.

8. Contact

The Principal Secretary, National Treasury.

THE NATIONAL TREASURY AND PLANNING

6TH JULY, 2020