KPMG

Tax alert

Declaration of Related Party or Controlled Transactions in the Income Tax Company Return

Overview

The Kenya Revenue Authority has through a public notice, made changes to the Income Tax Corporation Tax (IT2C) return to include a form for declaration of related party transactions. When filing their income tax returns, all taxpayers with related party transactions are required to answer, "Yes", to the question, under the basic information sheet of the IT2C return, on whether or not they have related parties outside Kenya or controlled transactions.

Revenue authorities around the world have recognised a potential tax base erosion through related party transactions that occur within Multinational Entities (MNEs). This has led to the implementation of measures across many jurisdictions to enhance tax transparency and prevent harmful tax practices, such as the introduction of specific disclosure requirements for related party transactions in tax returns.

Scope of related party or controlled transactions declaration

Taxpayers with related parties outside Kenya and/or any controlled transactions will be required to disclose their transactions annually in the IT2C return.

The requirement will apply in relation to related persons where;

a) Either person participates directly or indirectly in the management, control or capital of the business of the other; or

b) A third person participates directly or indirectly in the management, control or capital of the business or both.

c) An individual, who participates in the management, control or capital of the business of one, is associated by marriage, consanguinity or affinity to an individual who participates in the management, control or capital of the business of the other.

Additionally, the rules will also apply to resident entities which carry on business with related and unrelated persons operating in a preferential tax regime.

According to section 18A(2) of the Income Tax Act, preferential tax regimes include;

a) any Kenyan legislation, regulation or administrative practice which provides a preferential rate of tax to such income or profit, including reductions in the tax rate or the tax base; or

b) a foreign jurisdiction which :

   i. Does not tax income;

   ii. Taxes income at a rate that is less than twenty per cent;

   iii. Does not have a framework for the exchange of information;

   iv. Does not allow access to banking information; or

   v. Lacks transparency on corporate structure, ownership of legal entities located therein, beneficial owners of income or capital, financial disclosure, or regulatory supervision.

Content of related party or controlled transactions declaration

The declaration will contain the following information:

a) Details of related party transactions including; names of related persons, jurisdiction of incorporation, nature of relationship, description of transactions, mode of consideration and aggregate value of the transaction;

b) Comparative financial performance of the local entity/branch and the Ultimate Parent Entity/Head Office;

c) Category of related party transactions, description of the same, transaction values for the categorised transactions, transfer pricing adjustments if any and transfer pricing methods;

d) A separate disclosure for related party transactions of a capital nature indicating similar disclosures to c above;

e) A section showing the amounts due to or due from related parties from borrowings or current account balances at year end.

Our opinion

Due to the international push for transparency and exchange of information for tax purposes, MNEs must ensure that the information shared with tax authorities is uniform across all jurisdictions to avoid unnecessary sanctions and penalties.

Additionally, MNEs with related persons operating in preferential tax regimes including low tax jurisdictions may be required to disclose such transactions in their tax returns.

Local entities are required to maintain transfer pricing documentation, contracts and service level agreements and any other documentation to justify an arm's length standard in relation to related party or controlled transactions. We expect the Commissioner to continuously enhance transfer pricing disclosures to enhance transfer pricing compliance.

Penalty for non-compliance

Any person who fails to comply with the regulations shall be liable to a fine not exceeding one million shillings and to imprisonment for a term not exceeding three years, or to both, as prescribed under section 94 read together with section 104 of the Tax Procedures Act, 2015.

Please reach out to us for assistance in filing your transfer pricing declaration in the IT2C return and evaluation of your transfer pricing compliance status.

Stephen Ng'ang'a
Partner/Director
Tax & Regulatory Services
KPMG Advisory Services Limited
E: swnganga@kpmg.co.ke

Teresia Muli
Senior Manager
Tax & Regulatory Services
KPMG Advisory Services Limited
E: tmuli@kpmg.co.ke

home.kpmg/ke/en/home