

Place of Effective Management



Introduction

Tax Appeals Tribunal (TAT) rendered judgement in the case of M-Kopa LLCC/O M-Kopa Kenya Limited versus Commissioner of Domestic Taxes about the determination of the place of effective management (POEM) for taxation purposes. The Tribunal while allowing the Appeal, held that, POEM is where the company is actually managed. It is where the key management and commercial decisions that are necessary for the conduct of the entity's business are in substance made.

Background

The Appellant (M-Kopa LLC) in this case, is a limited liability company registered in the State of Delaware in the United States of America (USA). It is the holding company of M-kopa Kenya Ltd. The KRA undertook an audit of the Appellant's operations for the year 2017 and communicated its tax assessment of Kshs 368,507,926.00 concerning Corporation tax, Pay as You Earn (PAYE) and Withholding Tax (WTH). Aggrieved by this decision, the Appellant filed this appeal.

Appellant's argument:

The Appellant argued that it was not tax resident in Kenya for the 2017 year of income. That the Appellant's control of affairs was not exercised in Kenya contrary to KRA's assertion that 19 out of 27 meetings of the Appellant were held in Kenya, thus Kenya was the POEM of the Appellant. The Appellant reiterated that only 1 full board of managers meetings was held in Kenya.

That the concept of control has always been used to determine the tax residency of a company, and this level of control as demonstrated in many tax cases is found at the level of the company's board of managers. That the POEM in this case should be where the board met and made key strategic commercial decisions.

Consequently, the fact that only 1 out of the 4 board meetings were held in Kenya, majority of directors were non-Kenyan in essence demonstrated that the company's board meeting were regularly held and key decisions made from a location outside Kenya.

Respondent's argument;

That in determining the tax residency of the Appellant, it considered provisions of Article 4 of the Organisation for Economic Cooperation and Development Model Tax Convention on Income and on Capital (OECD NTC) which provides that; The place of effective management is the place where key management and commercial decisions that are necessary for the conduct of the entity's business are in substance made. The place of effective management will ordinarily be the place where the most senior person or group of persons (for example a board of directors) makes its decisions, the place where the actions to be taken by the entity as a whole are determined.

That from the above Article 4 of the OECD, the Appellant's meets all the requirements to be deemed a tax resident in Kenya as follows; CEO and senior executives of the Appellant carried out day to day management of the company from Kenya. Majority of board meetings were held in Kenya. Senior managers in leading positions, setting strategic goals and making decisions on M-Kopa operations are permanent employees in Kenya.

The Respondent reiterated that from the foregoing it concluded that the Appellant's Central Management and Control/place of effective management (POEM) was in Kenya for the year 2017. Appellant was a tax resident in Kenya and therefore, deemed the whole of its gains or profits in 2017 to have accrued in or have been derived from Kenya.

Tribunal Determination

The Tribunal while relying on Article 4 of the OECD held that the Appellant (M-Kopa LLC) was not tax resident in Kenya in the year 2017 year of income. According to the Tribunal, that determination of POEM has not been defined in the Income Tax Act (ITA), hence reliance on case laws and international legal instruments. That from OECD Guidelines, POEM is the pivot that determines the tax residency of a corporation like the Appellant.

That POEM is where a corporate entity is actually managed, that is where the management and control of the corporate body was exercised. That it was factual that only one board of director's, meetings was held in Kenya and decisions made by board committees had to be approved by board of directors. That from the Appellant's Operating Agreement, board of directors were the one with authority to manage and make decisions on behalf of the Appellant. This meant that POEM of the Appellant was where the Appellant's board met and made key decisions, thus the POEM of the Appellant was not in Kenya.

The Tribunal further added that, determination of POEM is a legal issue which require a wholesome analysis of the facts and circumstances of the case.

Implications of this ruling on taxpayers.

This judgement by TAT has reiterated and offered clarity on what is place of effective management (POEM) for purposes of determining if an entity is a tax resident in Kenya. It demonstrates that determination of place management is relevant for tax purposes especially in a case where a company has offshore subsidiaries. The primary issue in determining whether a foreign entity is tax resident in Kenya is whether the key strategy decisions were substantially made in Kenya in the relevant year of income. Taxpayers, especially multinational companies with offshore subsidiaries, need to critically consider how the location of the directors of the offshore subsidiaries is structured, and how this will impact on determination of the POEM of these subsidiaries for purposes of consideration of residency.



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