#3/2023

WTS Africa Quarterly Newsletter

Editorial

Recent tax developments in Africa

Dear Madam/Sir,

We hope you may find interesting our third edition of the WTS Africa Regional Quarterly Newsletter where we collate and present taxation related news from six countries on the continent.

The following participants in the WTS Global network have contributed with a diverse range of international tax topics. These contributors are from the following countries:

- Angola – Vieira de Almeida (VdA)
- Kenya – Viva Africa Consulting LLP
- Mauritius – WTS Mauritius
- Nigeria - WTS Blackwoodstone
- Senegal - FACE Africa Tax & Legal
- South Africa - WTS Renmere

Our experts will be happy to answer any questions you may have.

We thank you for your interest.

Yours sincerely,

WTS Africa Team

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Please find the complete list of contacts at the end of the newsletter.

Angola

Angola tax measures for 2024

In 2023, with the conflict involving Russian Federation and Ukraine, the global economy has been volatile, and several countries have been facing economic difficulties, inter alia, inflation especially in Europe and in the USA.

In this regard, Angola is not an exception, as there have been significant social and economic impacts in the Angolan economy landscape (despite the hike on oil barrel prices [USD 90] higher than the USD 75 initially predicted by the Angolan Government in the State Budget for 2023), namely, the local currency depreciation (the Kwanza is one of the worst performing African currencies this year), inflation pressure (which was also driven higher by a Government decision of lowering the fuel subsidy, which has led to a steep increase in gasoline prices) and the escalation of the cost of living, in particular, in the acquisition of foodstuffs.

As a result, the Angolan Government through the Council of Ministers has announced earlier this year in July, a package of measures that aim to ease the cost of living and boost the economy.

The tax relief measures, include the following:

- A reduction of the applicable VAT rate on foodstuffs, from 14% to 7% (the list of goods has not been made public yet), for the financial year of 2024;
- Extension of the scope of the VAT simplified regime to cover exempt operations;
- A mechanism allowing on the import of industrial equipment to support the local production, that the VAT settlement may be completed in twelve (12) monthly instalments;
- Regarding Real Estate Tax, and in order to make mortgage loans more affordable, it is foreseen an exemption applicable to the transfer of properties with a valuation of AOA 40,000,000.00 (approx. EUR 42,000) and a 50% tax reduction for transfer of properties with a valuation between AOA 40,000,000.00 and AOA 100,000,000.00 (approx. EUR 106,000.00)
- The elimination of Stamp Duty on real estate development, as well as on the registration of the share capital of companies;
- The allowance of accounting monetary updates relating to investments in fixed assets to their fair value without any tax implications (a sort of year zero for companies to update their balance sheets);
- Clarifying certain exemptions relating to medical goods, books, assimilated operations, special customs arrangements, and those arising from international agreements.

Nonetheless, despite the announcement by the Angolan Government, these measures are still under discussion and approval of the Parliament and further publication in the Angolan Official Gazette is required.

Additionally, with regard to tax measures, the Angolan Tax Authorities have announced that the taxpayers may benefit from a reduction of interest and penalties (30% and 50% respectively) if they regularize pending tax debts until 31 December 2023, benefiting from the regime already set forth under the General Tax Code.

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Kenya

Corporate Tax Residency in Kenya: The Management and Control Test

Recently, the issue of the corporate tax residency of companies incorporated outside Kenya has arisen, especially for multi-national enterprises with a business presence or related entities in Kenya.

Kenya's Income Tax Act defines residency in relation to a body of persons under three parameters:

- Incorporation in Kenya;
- The place of management and control of the affairs of the body is in Kenya; and
- Declaration by way of a Gazette Notice by the Cabinet Secretary responsible for the National Treasury that the body is resident in Kenya.

The question of management and control therefore arises where the other two parameters do not apply. Notably, management and control is not defined under the Income Tax Act, necessitating the adoption of the common law interpretation in the determination of corporate residency.

Central Management and Control (CMC) Test

The common law position is enunciated in the case of De Beers Consolidated Mines Ltd v Howe [1906] AC, 455. The Court explained that a company resides, for purposes of income tax, where its real business is carried out. The Court elaborated that real business is carried out where its central management and control is carried out.

The CMC test considers the factual and legal management and control of a company. Residency is a question of fact. Courts will therefore consider where the key decisions of an entity are made, e.g., the acquisition or disposal of assets, approval of budgets, significant capital expenditure, major operational decisions, approval of contracts and significant borrowings. This is distinguished from decisions of a more day-to-day operational nature.

The Tax Appeals Tribunal (TAT) in Kenya has applied the CMC test in its recent decisions on the issue of corporate residency of offshore companies. The TAT has taken a practical approach to the CMC test, which entails a consideration of the following: -

a) The types of decisions that are made by the central management of the company. (What)
b) The individuals responsible for the decisions. (Who)
c) The mode of making decisions, such as meetings and resolutions. (How)
d) The place where the decisions are made, and by extension, the place where the

decision-makers reside. (Where)

Place of Effective Management (POEM) Test

The Kenya Revenue Authority has also considered the POEM test to determine corporate residency of offshore companies in Kenya. The POEM test is provided for under the OECD Model Tax Convention on Income and Capital, which involves the consideration of several factors, including: -

a) Where meetings of the board of directors or equivalent body are held;
b) Where senior executives carry on their activities, senior day-to-day management is carried on and accounting records are kept;
c) Where the entity is headquartered; and
d) Which country's laws govern the legal status of the person.

The POEM test is applied where an entity is considered a resident of two contracting states.

In the wake of virtual board meetings, as opposed to physical meetings, it will be interesting to see the interpretation of the CMC and POEM tests on the issue of management and control by the Kenyan courts.

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Mauritius

Taxation of Interest Derived by a Collective Investment Scheme or a Closed-End Fund

Mauritius is increasingly popular as a platform for Fund Managers to structure investment funds, including Collective Investment Scheme("CIS") and Closed-End Fund ("CEF") vehicles, targeting Africa and Asia. Nonetheless, the Fund structures have traditionally been skewed towards equity investments while the use of Mauritius for structuring Debt Funds has remained fairly low. With public and private debt levels soaring across the globe, Mauritius has implemented legislations, through the Finance Act 2023, to give an impetus to the Debt Fund offering within its International Financial Centre.

The Securities Act 2005 has been amended to provide for CIS and CEF to be explicitly authorised to invest in "*money market instruments or debt instruments including loans, debt obligations or similar instruments*". This extension explicitly broadens the investment horizon of CIS and CEF to cater for debt funds and is welcome by industry players as it brings Mauritius at par with most sophisticated financial centres from a regulatory perspective.

In addition, in order to render Debt Funds more attractive from a tax perspective, the Income Tax Act 1995 has also been amended. While the standard tax rate applicable to a CIS or CEF on its chargeable income is 15%, with the amendments brought to the Finance Act 2023, a CIS or CEF earning interest income may claim either:

(a) An exemption of 95% of the interest income earned, subject to satisfaction of prescribed economic substance requirements; or
(b) credit for actual tax suffered on the interest income,

whichever was more beneficial.

The application of the 95% exemption leads to an effective tax rate of 0.75% on the interest income earned by a CIS or CEF.

The economic substance conditions, which mirror the requirements under OECD BEPS Action Plan 5, require that the CIS or CEF:

(i) carries out its core income generating activities in Mauritius;
(ii) employs, directly or indirectly, an adequate number of suitably qualified persons to conduct its core income generating activities; and
(iii) incurs a minimum expenditure proportionate to its level of activities.

The core income generating activities to be carried out in Mauritius with respect to a CIS or CEF is defined in the legislation as follows:

CIS	Investment of funds in portfolios of securities, or other financial assets, real property or nonfinancial assets; diversification of risks; redemption on the request of the holder
CEF	Investment of funds collected from sophisticated investors, in portfolios of securities, or in other financial or non-financial assets, or real property

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Nigeria

VAT Privileges for Diplomatic Missions and International Organisations

The Federal Inland Revenue Service (FIRS) recently published Guidelines for the Refund of Value Added Tax (VAT) paid by Diplomats, Missions and International Organisations (Qualified Persons) on Goods and Services purchased to provide such qualified persons with a framework for processing such requests for VAT refunds.

Based on the above, where diplomats or diplomatic missions and international organisations pay VAT on goods purchased or services rendered, such diplomats and organisations will be entitled to a refund of the VAT paid at the point of purchase. This is premised on the established principle that goods and services purchased by Diplomats are zero-rated.

Qualified Parties and transactions for refund

The transactions that qualify for refund under the Guidelines are as follows - VAT paid on goods and services purchased or imported by Diplomats, Diplomatic Missions and International Organisations. Persons or Organisations eligible to apply for refund of VAT are Diplomats (foreign employees of embassies/missions not below the rank of third secretary), Diplomatic Mission (Embassies and High Commissions), International Organisations conferred with diplomatic immunities and privileges by the Honourable Minister of Foreign Affairs by an Order published in a Federal Gazette pursuant to the Diplomatic Immunities and Privileges Act.

Refund Process

The Ministry of Foreign Affairs conducts all interactions with qualified Diplomats and Diplomatic Missions and collaborates with FIRS during refund process to ensure efficiency and transparency.

International Organisations

The process for refunds under this sub head is different as all applications for refunds on goods purchased by International Organisations (conferred with diplomatic immunities and privileges by the Honourable Minister of Foreign Affairs by an Order published in a Federal Gazette) are to be made to the Executive Chairman, Federal Inland Revenue Service (FIRS) and to ensure seamless refunds, the application must be accompanied with proper documentation.

Conclusion

The Guidelines on VAT refund is a welcome development that has created opportuities for diplomats and qualified international organisations to exercise some of the priviledges granted them as a result of their status. It will be interesting to see the implementation of the Guidelines in the months ahead.

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Senegal

Arm's length principle in transfer pricing: Senegalese tax authorities favor local comparable

Senegalese tax legislation references the arm's length principle since the 2018 Finance Act, particularly in Article 17, paragraph 1 of the General Tax Code (CGI), and provides for related party notion (article 17.4 of the CGI).

However, the instruction specifying the suitable transfer pricing method in Senegal is under process (Cf. Senegal - Transfer pricing country sheet, February 2022). Meanwhile, doctrinal opinion No. 4907/MEFP/CAB/CT/JK of July 17th, 2019 by the General Directorate of Taxes and Domains (DGID) and published in October 2022, suggests that Senegalese tax authorities prefer a method based on local comparable for determining transfer prices.

This opinion emerged post a general accounting audit for the 2013 fiscal year concerning crude groundnut oil sales prices charged with a related entity. The taxpayer opposed the tax authorities' accusations of non-adherence to the arm's length principle, as the price was based on "quoted" prices in Cost-Assurance-Freight (CIF) Rotterdam values using the "MUNDI" index, instead of the "Free On Board (FOB)" value used by auditors.

Responding to the appeal, tax authorities noted the OECD's 2015 recommendation of "quoted" price for commodities like crude groundnut oil, but believed such comparable are only viable in absence of a relevant local comparable, which they considered better reflects company profitability. In the said opinion, tax auditors' preference for relevant local comparable over the quoted price in detecting indirect profit transfer was deemed correct.

From this, two conclusions arise:

- Transfer pricing is an international and a local issue. Tax authorities remain sovereign in applying OECD principles as long as they have not been incorporated into domestic law.
- Though the arm's length principle is recognized in Senegalese law, application conditions aren't yet clear in Senegal's tax system, posing tax security issues for multinationals here. Open, pragmatic, and educative interactions with Senegalese tax authorities are crucial to evade tax reassessments.

A primary defense against tax reassessment risk is establishing thorough transfer pricing documentation to justify the group's pricing policy. Beyond documentation, forging advance pricing agreements with tax authorities is essential to mitigate the mentioned tax risk.

In our view, the first line of defense against the risk of tax reassessment of the company's pricing policy is to put in place relevant transfer pricing documentation that is sufficiently detailed to justify the group's pricing policy. Over and above this documentation, the use of advance pricing agreements with the tax authorities is now necessary to reduce the level of exposure to the above-mentioned tax risk.

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South Africa

The Coronation judgement and the foreign business establishment ("FBE")

In terms of section 9D of the Income Tax Act 58 of 1962 ("ITA"), income tax is imposed on South African shareholders of 'controlled foreign companies' ("CFC") on the income earned by the CFC in certain circumstances. However, where a CFC has a FBE in the jurisdiction from where it operates, the income of that CFC may fall outside of section 9D.

Section 9D(1) defines a FBE as a fixed place of business which is conducted through one or more physical structures (e.g. office), which is suitably staffed and equipped and has suitable facilities— all to such a degree that it allows the CFC to conduct the primary operations of its business.

The supreme court of appeal ("**SCA**") recently considered the definition of FBE in *Commissioner for the South African Revenue Service v Coronation Investment Management SA (Pty) Ltd* [2023] 2 All SA 44 (SCA). The somewhat controversial judgement caused significant uncertainty and concern amongst South African multinational enterprises which operate *via* subsidiaries in foreign countries.

The case dealt with the question of whether the operations of an Irish subsidiary ("**the CFC**") of the respondent constitutes a FBE as defined. In applying this definition, the SCA was required to identify the primary business operations of the CFC. The CFC held a licence issued by the Central Bank of Ireland authorising it to conduct collective investment management (including investment management, administration and marketing). The CFC opted to outsource the management of collective investment schemes to service providers outside of Ireland and therefore had no staff in Ireland to perform the outsourced functions. The respondent argued that the primary business operations of the CFC were that of fund manager (as distinct from investment manager) and maintaining its business licence in Ireland.

The SCA noted that the CFC's Memorandum of Association and its business licence entitled it to conduct the wider business of fund management and investment management and the fact that it decided to outsource its investment management functions implied that it did not conduct its primary business via the office in Ireland. The SCA rejected the notion that the primary business is determined with reference to how the CFC chooses to operate. The SCA acknowledged that there are many functions which a company may choose to legitimately outsource, but it cannot outsource its primary business. The court found that the FBE exemption did not apply to the income of the CFC.

While the Tax Court and the SCA reached different factual conclusions, the judgments both shine a sharp light on the requirement for a FBE not only to involve having substance abroad but also that the relevant CFC's primary operations need to be exercised through that infrastructure, especially where the CFC outsources to a third party that is not based in the same jurisdiction.

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