Narrative Report on Kenya

PART 1: NARRATIVE REPORT

Kenya: Africa's newest international financial centre

Kenya's financial sector is highly secretive. The country scored 80 out of 100 in terms of secrecy, which explains its high ranking of 27 in the Financial Secrecy Index of 2018. Though the country's share of the offshore world is not large, this may be set to increase as the government positions Nairobi as the latest African International Financial Centre.

Kenya lies on the east coast of Africa with a population of 48.46 million as of 2016. In 2016, Kenya was identified as one of the fastest growing economies in Sub-Saharan Africa with GDP per capita over 1445 US$[1] and GDP growth improving by 6% in 2016, up from 5.6% in 2015, driven by construction, manufacturing, finance and insurance, rebound in the tourism industry, strong remittance inflows, information and communication technology, and wholesale and retail trade.[2]

Kenya also takes the lead in East Africa on Foreign Direct Investment (FDI) with a majority of inflows being attributed to extractives and infrastructure projects.[3] The key economic goal set out in Kenya's Vision 2030 is to sustain high levels of economic growth.[4] However, key development challenges remain, including inequality, healthcare, education and climate change.

According to a study done by Oxfam Kenya, less than 0.1% of the population own more wealth than the bottom 99.9%.[5] The rising inequality in Kenya cannot be ignored. In the recently published Paradise Papers, a former minister was identified as having London based assets owned through a Mauritius based company.[6]

In 2016, the Panama Papers implicated several Kenyans hiding their wealth in offshore jurisdictions, with a number of politically exposed persons being identified.[7] The use of secrecy jurisdictions is not unknown in Kenya.

Introducing the Nairobi International Financial Centre

In an effort to achieve a 'well-functioning financial system in order to accelerate economic growth by encouraging FDI, safeguarding the economy from external shocks, and establishing Kenya as a leading financial centre in Eastern and Southern Africa',[8] the Government of Kenya included the Nairobi International Financial Centre as one of the commitments for Vision 2030.

As a result, in September 2017, the Nairobi International Financial Centre (NIFC) Act, No. 25 of 2017, entered into force to provide a legal framework for the development of the NIFC and the NIFC Authority. According to the National Treasury,[9] the purpose of the NIFC is to establish a 'stable, efficient and globally competitive financial services sector in Kenya' with the ultimate objective of encouraging domestic and foreign investment, generating saving opportunities and contributing to overall economic growth.

To achieve this, the NIFC Authority will improve the transparency and ease of doing business by reforming the existing regulatory and institutional

Rank: 27

Chart 1 - How Secretive?

80
Secrecy Score

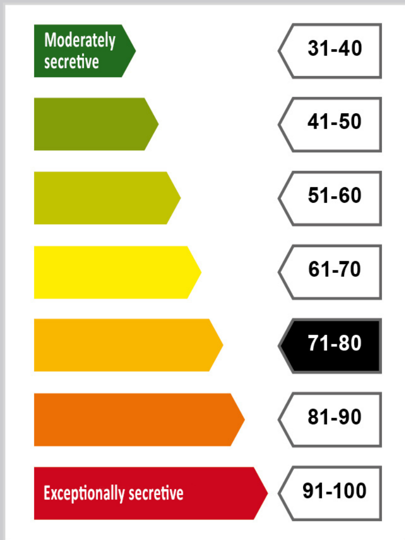
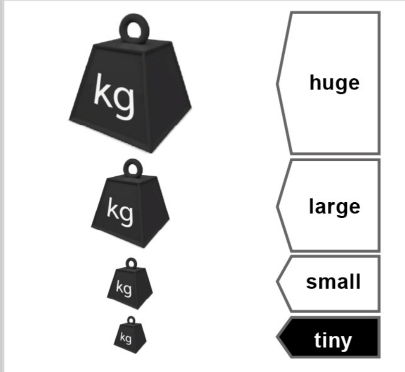


Chart 2 - How Big?



Kenya accounts for less than 0,1 per cent of the global market for offshore financial services, making it a tiny player compared with other secrecy juridictions.

The ranking is based on a combination of its secrecy score and scale weighting.

Full data on Kenya is available here: www.financialsecrecyindex.com/database

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If you have any feedback or comments on this report, contact us at **info@taxjustice.net** framework, establish a one-stop shop for financial services and related firms, and offer incentives and opportunities to attract global firms to establish a presence in Nairobi.[10] The National Treasury is set on adopting an integrated model similar to that of the City of London.

The International Monetary Fund (IMF) defines an IFC as a centre (usually a city) where the bulk of financial sector activity is offshore, the transactions are initiated elsewhere, and the majority of institutions involved are controlled by non-residents.[11] IFCs typically have large numbers of financial institutions engaged, primarily, in business with non-residents; financial systems with external assets and liabilities out of proportion to domestic economies; and, more popularly, centres which provide low or zero taxation, moderate or light financial regulation, banking secrecy and anonymity.[12]

The NIFC Authority has yet to publish their strategy and framework or widely consult the public, despite the threat that the tax concessions and banking secrecy may facilitate unhealthy tax competition, aggressive tax avoidance, and illicit financial flows.

Alongside the establishment of the NIFC, Kenya continues to expand its tax treaty network. Kenya currently has 15 double taxation agreements (DTAs) in force, seven that are signed and not yet in force, seven concluded and not signed, five under negotiation and 15 under consideration.[13] Most recently, Kenya has operationalized DTAs with China, the United Arab Emirates, and the Netherlands. A number of these DTAs have been identified as being unfavourable to Kenya.[14]

In tandem with these developments, the Kenya Revenue Authority (KRA) and other regulatory bodies have been actively pursuing and committed to meeting the standards set out by the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) and the Organisation for Economic Co-operation and Development (OECD) Base Erosion and Profit Shifting project. Some of the efforts include signing the convention on Mutual Administrative Assistance in Tax Matters (MAATM) and taking steps to meet the international standards set out in the Global Forum's Terms of Reference to Monitor and Review Progress Towards Transparency and Exchange of Information.

Additionally, in 2015, Kenya rolled out the overhaul of the regulatory framework for business and taxation that set a solid foundation for financial transparency regarding the availability of ownership information and reporting on beneficial ownership.

Financial sector requirements

The Kenyan banking sector is regulated by the Central Bank of Kenya (CBK) and has 43 banking institutions, eight representative offices of foreign banks, 12 microfinance institutions, and three credit reference bureaus.[15]

Kenya's Vision 2030 includes broad objectives relating to consumer protection through the increase of transparency, fairness and affordability of banking and other financial products and services.[16]

The Proceeds of Crime and Anti-Money Laundering Act (PCAML Act), No. 9 of 2009 became effective in June 2010 to provide a framework for identifying, tracing, freezing, seizing and confiscating any proceeds of crime. The provisions of the PCAML Act override any obligations relating to secrecy or other restrictions on disclosure of information imposed by any other law or otherwise.[17]

The PCAML Act established the Financial Reporting Centre (FRC) for purposes of assisting in the identification of proceeds of crime and combating money laundering. The FRC is also tasked with the fight against financing of terrorism under the Prevention of Terrorism Act 2012. The centre maintains a register of reporting institutions, receives reports on suspicious activities or transactions from reporting institutions, receives cash transaction reports above a certain threshold, and receives reports on cross-border conveyancing of monetary instruments.

The PCAML Regulations 2013 have been effective since March 2013 and set out the obligations of reporting institutions. Reporting institutions include financial institutions and designated non-financial businesses and professions. All institutions are required to carry out Money Laundering Risk Assessments to identify, assess, monitor, manage and mitigate risks. In this regard, reporting institutions are required to carry out a customer due diligence to determine the following:

- Verified customer's identity using reliable, independent source documents (tax registration and identification documents);
- The verified identity of the beneficial owner[18] and develop an understanding of the ownership and control structure of the customer;
- Purpose and nature of the business relationship; and

- On going due diligence on the business relationship and scrutiny of transactions carried out to ensure consistency with the reporting institution's knowledge of the customer, their business and risk profile, including the source of funds.

The PCAMLA Regulations also apply to any persons (including directors and senior management) who know or ought to reasonably know that property forms part of the proceeds of crime or who fails to comply with monitoring and reporting obligations. Failure to report a restricted activity constitutes a crime.

In 2016, CBK adopted a Risk Based Supervisory Framework for Anti-Money Laundering and Countering Financing of Terrorism (AML/CFT). The framework was designed to further complement prudential supervisions and legal compliance.

Regulation of business conduct on transparency and accountability

Various types of entities are permitted in Kenya including companies, partnerships, limited liability partnerships (LLP), sole proprietorships, trusts, societies, and co-operative societies.

In 2015, the President of Kenya assented several bills relating to the regulatory framework for business and taxation that were targeted at improving the ease of business. Some of these regulations include the Companies Act, the Insolvency Act, Special Economic Zones Act, the Business Registration Act 2015, the Companies and Insolvency Legislation (Consequential Amendments) Act 2015 and the Finance Act Amendments 2015.

As of 2015, any individual attempting to register an entity is required to hold and provide a Personal Identification Number (registration for tax purposes), a copy of their identity card and photographs of the directors or partners in the case of a company or partnership. Companies and co-operative societies are required to maintain a register of members that should be open and shared with the Registrar of Companies in the case of a company. On registration, LLPs are required to provide the name, identification document, nationality and the place of residence of each partner and manager of the partnership.

The Business Registration Act established the Business Registration Services to administer incorporation, registration, operation and management of companies, partnerships and other entities. The body is responsible for monitoring these entities and supporting the functions of the Registrar of Companies including in maintaining updated ownership information.

Information about companies incorporated in Kenya is available online via the *e-citizen* portal.[19] The Register of Companies is required to include the shareholders, beneficial owners, directors and address of the company. This information is only accessible through payment of an administrative fee. Information on the beneficial ownership is limited to the name and address of the identified persons; no verification of this information is required. In relation to Trusts, Section 54B of the Income Tax Act, Chapter 470 of the Laws of Kenya (ITA), requires that the full identities and addresses of trustees, settlors and beneficiaries of the trust be disclosed to the KRA.

To support the operationalization of the MAATM Convention, the Mutual Legal Assistance Act (MLA Act) sets out the procedure for responding to foreign jurisdiction requests for information and identifies KRA as a Competent Authority.

Beneficial ownership transparency

In 2017, Transparency International Kenya (TIK) published a report highlighting the state of beneficial ownership transparency in Kenya.[20] TIK assessed the beneficial ownership transparency legal framework against the ten beneficial ownership transparency principles covering several areas including the definition of a beneficial owner, availability and access to information on legal entities including trusts, roles and responsibility of financial institutions, business and professionals, and bearer shares and nominees.

The assessment determined that the AML laws in Kenya adequately defined beneficial ownership, however, minor shortcomings in the requirements of legal entities to maintain information on all natural persons who exercise ownership or control of the legal entity were identified.[21] In addition, the ability of enforcement bodies, the tax authority and the FRC to access beneficial ownership information requires improvement particularly where the scope information included in the Register of Companies is limited and no proof of verification is provided.[22]

In particular, access to beneficial ownership information relating to private companies is limited. In relation to trusts, significant improvement is required in the access of competent authorities to beneficial ownership information.[23] Further, advocates have no obligation to identify the beneficial owners of their clients.[24] This can, arguably, be extended to other professionals.

As identified above, Kenya has ratified the MAATM Convention, which is considered to be a positive step in supporting exchange of information and transparency.

Kenya does not prohibit the use of nominee shareholders and directors; however, the on-going legislative reform is expected to remedy this weakness.[25] The Companies Act 2015 prohibits the use of bearer shares.[26]

Global Forum on Transparency and Exchange of Information: Key findings

The Global Forum's Phase 2 review of Kenya, carried out in 2016,[27] analysed the practical implementation and effectiveness of the legal framework and was based on the laws, regulations and exchange of information mechanisms in force or effect as at 18 December 2015.

Based on a review of the regulatory framework as set out above, the Global Forum staff determined that Kenya's overall rating was largely compliant. Some of the justifications included the introduction of Section 54B of the ITA, the prohibition on bearer shares,

The Global Forum team did, however, identify that the AML regime is limited, the Registrar of Companies did not have a system of oversight to monitor compliance with ownership obligations and sanctions for non-compliance were not enforced in practice and trustees of Kenyan trusts are only required to maintain accounting records where the trust derives income subject to tax in Kenya.

What does the Nairobi International Financial Centre mean for the future of transparency in Kenya?

The Lord Mayor of the City of London Corporation and one of the City Corporation's main lobbying bodies, the City UK, have strongly influenced and participated in the design and implementation of the NIFC.[28]

Despite the progress in transparency and exchange of information, the establishment of the NIFC will be a drastic move in the wrong direction. IFCs thrive on secrecy and incentives, and it has been demonstrated[29] that the proposed NIFC could lead to profit shifting and base erosion.

In particular, Section 17 of the NIFC Act stipulates that any person connected to the NIFC Authority or who has access to any information relating to the affairs of the Authority shall not divulge any of that information unless disclosure is required by law or by a Court of law. Disclosure in contravention of this section constitutes an offence liable to a fine not exceeding approximately USD 2,000 or an imprisonment term not exceeding three years or both.

A strong secrecy regime combined with a corruption-ridden economy is certainly a recipe for disaster with the potential to facilitate illicit financial activity without the need of accessing offshore jurisdictions. The majority of tax havens tend to powerful rich countries or dependencies of such countries, which attract money because people trust that their money is safe in a legal system backed by a stable democracy.[30]

As a result, less obviously trustworthy locations will typically find their 'competitive edge' in going downmarket, accepting dirtier money than other jurisdictions.[31] The NIFC is expected to permit selected local investors access on par with foreign investors.[32]

Already, Kenya's beneficial ownership transparency and AML regime require significant strengthening, although the secrecy element of the NIFC is not as intense as that of some well-known offshore jurisdictions. Due to a lack of consultancy on the framework thus far, it is unknown which direction the Authority will be taking, but progress should be expected in the coming year.

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Endnotes

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Kenya

PART 2: KENYA'S SECRECY SCORE

OWNERSHIP REGISTRATION

- 63% 1. Banking Secrecy
- 50% 2. Trust and Foundations Register
- 100% 3. Recorded Company Ownership
- 100% 4. Other Wealth Ownership
- 100% 5. Limited Partnership Transparency

LEGAL ENTITY TRANSPARENCY

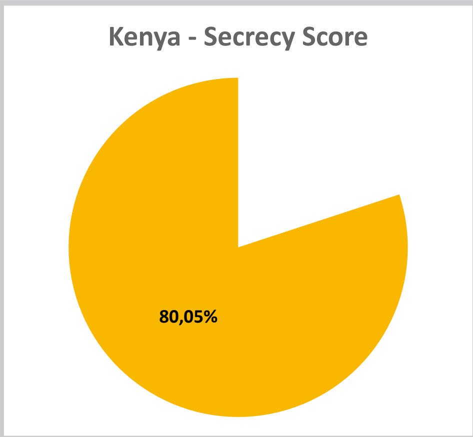
- 100% 6. Public Company Ownership
- 100% 7. Public Company Accounts
- 100% 8. Country-by-Country Reporting
- 50% 9. Corporate Tax Disclosure
- 100% 10. Legal Entity Identifier

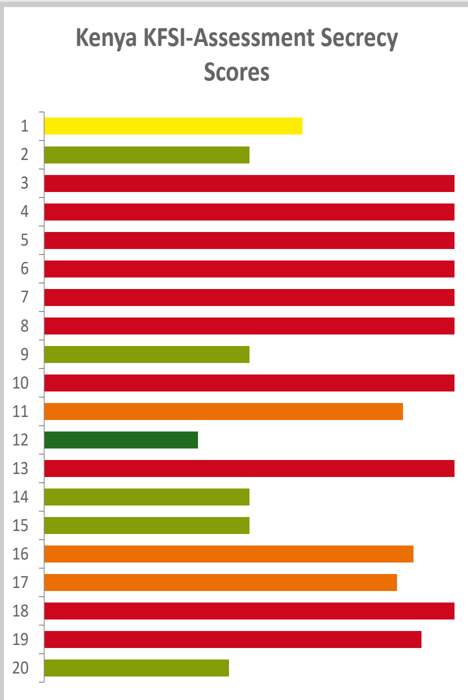
INTEGRITY OF TAX AND FINANCIAL REGULATION

- 88% 11. Tax Administration Capacity
- 38% 12. Consistent Personal Income Tax
- 100% 13. Avoids Promoting Tax Evasion
- 50% 14. Tax Court Secrecy
- 50% 15. Harmful Structures
- 90% 16. Public Statistics

INTERNATIONAL STANDARDS AND COOPERATION

- 86% 17. Anti-Money Laundering
- 100% 18. Automatic Information Exchange
- 92% 19. Bilateral Treaties
- 45% 20. International Legal Cooperation





Notes and Sources

The ranking is based on a combination of its secrecy score and scale weighting (click here to see our full methodology).

The secrecy score of 80 per cent has been computed as the average score of 20 Key Financial Secrecy Indicators (KFSI), listed on the left. Each KFSI is explained in more detail by clicking on the name of the indicators.

A grey tick indicates full compliance with the relevant indicator, meaning least secrecy; red indicates non-compliance (most secrecy); colours in between partial compliance.

This paper draws on data sources including regulatory reports, legislation, regulation and news available as of 30.09.2017.

Full data on Kenya is available here: www.financialsecrecyindex.com/database.

To find out more about the Financial Secrecy Index, please visit www.financialsecrecyindex.com.