THE INCOME TAX (MINIMUM TOP UP TAX) REGULATIONS, 2025

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The Kenya Revenue Authority (KRA) released draft regulations for the operationalization of the Minimum Top up Tax under Section 12G of the Income Tax Act.

Minimum top-up tax is a tax payable by a "covered" person where the combined effective tax rate in respect of that person for a year of Income is less than 15%.

In this article we discuss the regulations and key issues to note.

What is Minimum Top-up Tax?

Globalization has transformed the global economy leading to enhanced innovation and access to capital. However, it has also resulted in challenges, especially in taxation.

A major concern has been multinational groups' ability for leveraging the benefits of globalization to structure operations in a way that allows them to shift profit and achieve lower tax rates on some or all of their income.

These structures have put pressure on countries to lower their corporate income tax rates and/or offer incentives to compete for capital and investment from the multinationals.

This measure has created a collective action problem that has led to the so-called race to the bottom.

To mitigate the race to the bottom, the Inclusive Framework members agreed to a co-ordinated system of Global anti-Base Erosion (GloBE) rules that are designed to ensure large multinationals pay a minimum effective tax rate of 15% on the income arising in each jurisdiction where they operate.

The GLoBE rules consist of a set of interlocking rules that ensure that the minimum tax is collected by the low-tax jurisdiction itself, under Qualified Domestic Minimum Top-up Tax (QDMTT), what has been introduced by Kenya, or, where no QDMTT applies, by another implementing jurisdiction through the imposition of either:

I. an Income Inclusion Rule (IIR) which imposes top-up tax on a parent entity in respect of the low taxed income of a constituent entity; or

II. an Undertaxed Profits Rule (UTPR) which denies deductions or requires an equivalent adjustment in a subsidiary jurisdiction in order to produce an equivalent incremental increase on the taxes paid by the MNE Group.

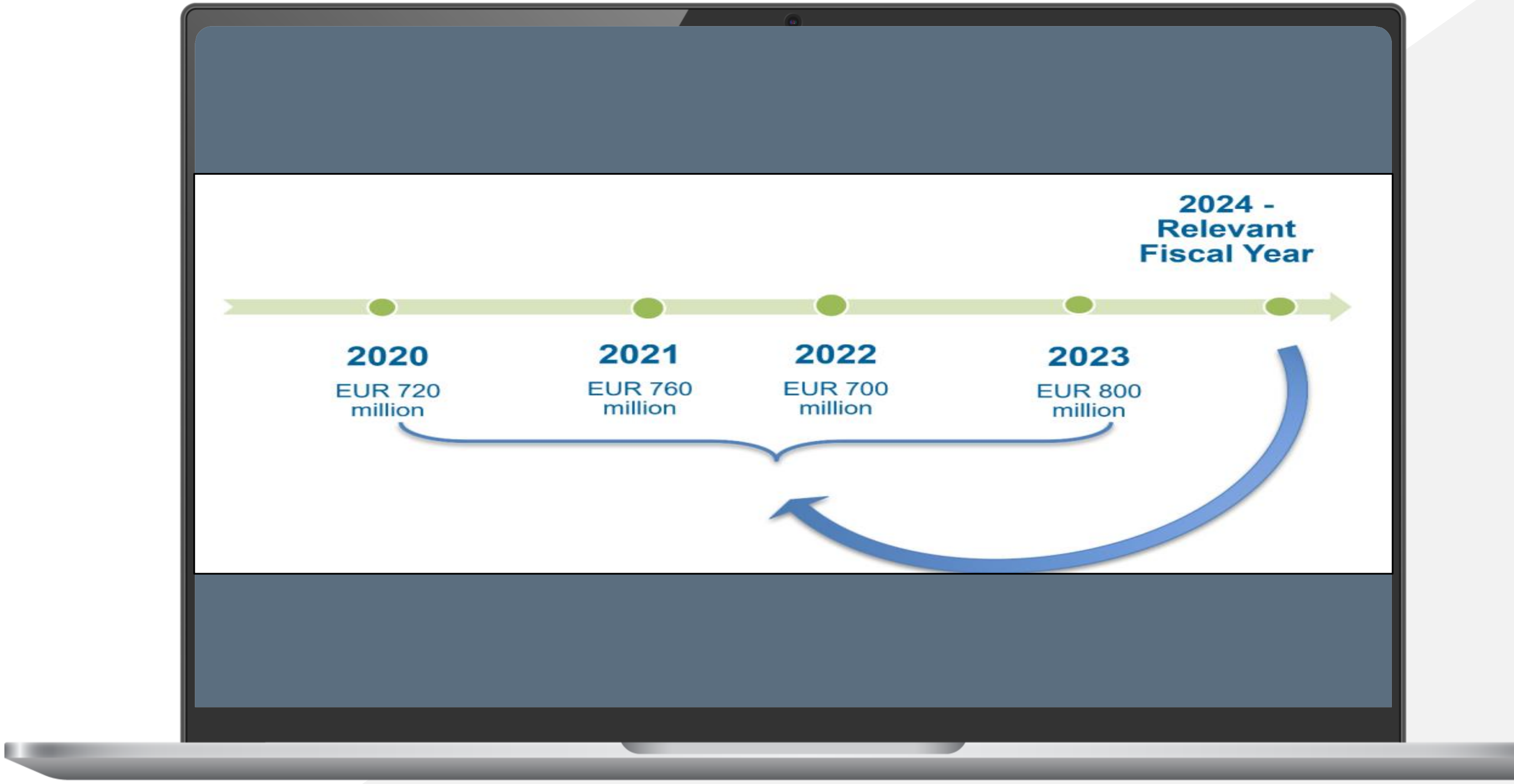
In-Scope Entities

The minimum top-up tax will apply to entities that are part of MNE groups with consolidated annual turnovers at or above EUR 750 million.

The threshold amount is similar to the one used for Country-by-Country Reporting (CbCR). However, unlike CbCR which is based on an annual calculation, the revenue threshold for the minimum top-up tax is based on a four-year test.

The MNE Group should have attained the threshold in at least two of the four years of income immediately preceding the tested year of income as demonstrated below.

However, there are several entities that will be excluded from the rules including public entities that are not engaged in business, pension funds, non-operating investment holding companies and sovereign wealth funds, among others.



How will it work?

- Once an entity is in scope (meets the 750 Million Euro threshold), it should determine its effective tax rate (ETR):

$$\textit{Effective Tax Rate (ETR)} = \frac{sum\ of\ all\ the\ adjusted\ covered\ taxes}{sum\ of\ all\ net\ income\ or\ loss} \times 100$$

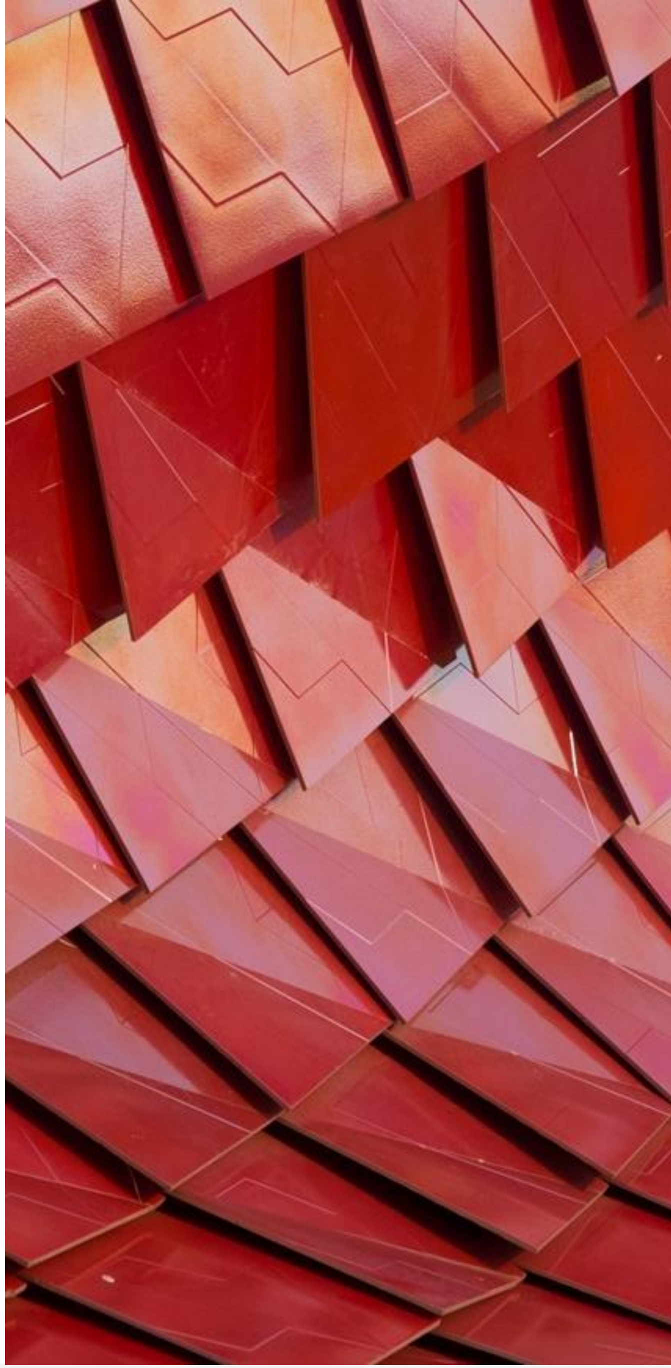
- If the ETR is less than 15%, say 9%, then the entity is liable to pay an additional tax (top-up tax).

- The additional tax is imposed on the entity's excess profits which is the income attributable to the entity after applying a substance-based income exclusion allocation key as shown below:

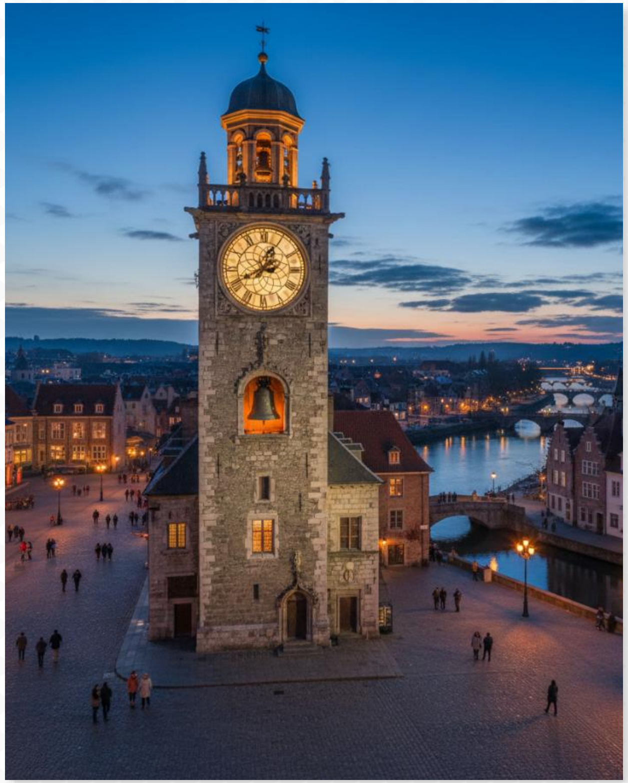
$$Excess\ profits = Net\ Income - 10\%\ of\ employee\ costs - 8\%\ of\ net\ book\ value\ of\ tangible\ assets$$

- Using the example of an ETR of 9%, the top-up tax will be computed as:

$$Top\ up\ tax = 6\% \times Excess\ profits\ ,\ \textit{where } 6\% = 15\%\ \textit{(Minimum tax)} - 9\%\ \textit{(ETR)}$$



Important Timelines



1. Notification to KRA – An entity that will be in scope of these rules shall issue the first notification to the commissioner within the first 60 days these regulations come into effect and shall do similar notifications by the 6th month of each year;
2. Payment of Minimum top-up Tax – in-scope entities shall pay the minimum top up tax by the fourth month of the following financial year, i.e., payable when you pay the Balance of Tax (by April for December year ends);
3. Filing of the Top-up Tax Return – the top up tax return shall be filed by the 6th Month of the following financial year (i.e., when filling your annual return – e.g., by June for December year end); and
4. Filing of GloBe information return (GIR) – GIR provides general information about the MNE Group as a whole by providing a high-level overview of the application of the GloBE Rules in respect of every jurisdiction where the MNE Group is operating. The GloBe return shall be filed by the 18 Months after the end of the first year of income an entity becomes subject to these rules and 15 months after the financial year end in the subsequent years.

We anticipate that the Minimum Top-Up Tax Regulations will come into force in early this year. Given the complexity of the rules, the extensive data requirements, and the strict compliance timelines, multinational groups that may fall within scope should begin assessing their exposure without delay.

Entities that are part of an MNE Group are encouraged to engage early for a risk assessment, impact modelling, and implementation support, to ensure timely compliance and to mitigate potential tax and reporting risks under the new regime.

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