Franchising in Kenya

According to the World Bank, Kenya is considered a low income nation with a population of 42 Million. It averages 5% GDP growth, largely because of expansions in tourism, telecommunications, transport, construction and a recovery in agriculture. Kenya’s population is relatively young and is becoming increasingly urbanized. There is a high level of computer literacy, especially among the youth. The government, generally perceived as investment friendly, has enacted several regulatory reforms to simplify both foreign and local investment. One of those reforms is constitutional and has created 47 new counties in Kenya similar to U.S. states. Until recently, the franchise business model has been slow to take hold in Kenya because local investors know little or nothing about its potential rewards, industry insiders say; however, American franchises such as KFC and Naked Pizza have begun to pop up in Nairobi. Given the establishment of the counties, investment prospects outside of Nairobi are likely to emerge in the coming years.

Market and Prospects

The franchising market in Kenya is steadily growing and evolving from single-unit owners to multi-unit operators employing professional staff of field and unit managers, while they focus on strategy and growth. There are several franchise companies in Kenya that cover almost every industry, from well-known national brands to smaller and local opportunities but is most common in the Hospitality industry. Other common franchising industries in Kenya include the clothing industry and fuel industry. Franchise businesses seem to exhibit the pattern of establishing franchising outlets within major shopping malls around the country.

Consumer Lifestyle Reports in Kenya have reported increased consumer expenditure, on eating, drinking habits and shopping especially among the urban population, as a result of growing disposable income. Kenya’s evolving lifestyle trends can be seen in more shopping malls and recreational facilities coming up across Nairobi and other leading Kenyan cities including: Eldoret, Kisumu, Mombasa, Nyeri, Nakuru and Machakos. This is a key pointer to investors wishing to set up shop in various locations in Kenya.
Franchises in the food, restaurant and beverages industries are the most successful - ranking them by growth, branch and demand. Kenyans are spending more time and money eating out or ordering in especially during work hours and the fast food industry has benefited greatly as a result.

Some of the popular food franchises in Kenya include: Wimpy, Debonairs, Pizza Inn, and Steers. Franchising is also now beginning to take hold because investment in services that meet basic needs is lucrative. For example, recently the American-backed Wananchi group invested US$43m in acquiring the coffee and restaurant chain Java. Leisure and recreational facilities are also a good investment decision. Franchising has not yet taken off in banking and sports.

Requirements and Legal Framework

There are no specific franchise laws in Kenya; therefore, investors must rely heavily on existing commercial laws and various applicable business laws, which include:

- Common Law
- Copyright Act of 2011

The Trade Marks Act (Cap. 506) which makes specific provisions in section 31 for the “recognition of license user agreements” and most franchisors have exploited this legal avenue. The registered user (licensee) would be the franchisee while the franchisor is actually the legal owner or proprietor of the trade mark.
The primary hurdle involves formalizing remittance procedures for fees and royalties to the
franchisor or licensor. Legal forms of the business are governed by the Companies Act of 2009.
Immigration laws and work permits governing foreign investors also apply. Additionally, there
are licensing requirements that are peculiar to particular businesses. It would therefore be wise
for the franchisor to protect his intellectual property by registering the patent, trademark or trade
name or any other intellectual property of the franchise.

There are significant guarantees against expropriation of private property under the Constitution
of Kenya, which require due process along with full and adequate compensation in the event of
expropriation. The 1995 abolition of the Exchange Control Act and the guarantees against
expropriation except with due process and compensation have encouraged many local and
foreign investors as well as franchisors to invest in the Kenyan market.

A Franchisor should first evaluate whether his/her business has a ready market in Kenya and
what the prospects of getting potential franchisees are. The market forces in Kenya in relation to
the franchisor’s products since these will determine the possibility of getting willing franchisees.
U.S. Franchisors seeking market entry in Kenya are strongly advised to consult with the US
Commercial Service at the US Embassy in Kenya (CS Kenya), and to seek legal counsel from
local attorneys and business associations such as The Kenya National Chamber of Commerce.

The average startup investment in money and time for a franchise will depend on the nature of
the industry as franchising in some industries will require a higher upfront investment capital and
time while others may require less. The averages in some selected industries in Kenya are as
follows:
(i) In Food/Restaurant industry, the average start up cost is US$100,000;
(ii) In Accounting and Finance US$50,000;
(iii) In Advertising and Marketing US$10,000;
(iv) Business services franchise US$25,000;

Taxes

In the case of franchising, it is the franchisee that is using the property of the franchisor in return
for the royalty paid by the franchisee to the franchisor. Under Kenya tax law and practice, the
franchisee withholds and remits to the Kenya Revenue Authority the tax on the royalty.

Taxation in the context of franchising might also arise in the context of the payment of any
royalties, management or professional fees, commissions, consultancy or agency fees and
contractual fees that arise under the franchising agreement.
The franchisor needs to be aware of the corporate tax applicable to the foreign companies which is *37.5 %* of the taxable profit.

**Basis**
Resident and nonresident corporate entities are subject to tax on all income accruing in or derived from Kenya.

**Taxation of dividends**
Dividends from a Kenyan company are not subject to additional tax other than what is deducted at source (see "Withholding tax", below). Attributable expenses are disallowed as deductions. Dividends from a foreign company are not taxable in Kenya.

**Capital gains**
Capital gains are not taxable in Kenya (while there is capital gains legislation, it has been suspended since 1985).

**Losses**
Business income, investment income (other than for financial institutions, for which investment income is considered business income), rental income and income from agriculture are assessed separately and losses only may be utilized against taxable income from the same source. As from 12 June 2009, tax losses may be deducted in the year in which they arise and the 4 following years of income (previously, an indefinite carry forward was allowed). Losses may not be carried back and capital losses are not deductible.

**Foreign tax credit**
Foreign taxes paid are treated as an allowable expense, except where a tax treaty applies, in which case a tax credit is granted.

**Tax Incentives**
Kenya provides for a 100% investment deduction on hotels, as well as buildings and machinery used in manufacturing. Manufacturing investment in buildings and machinery situated within satellite towns adjoining Nairobi, Mombasa or Kisumu attract an investment allowance of 150%. Enterprises in export Processing Zones enjoy a 10-year tax holiday.

<table>
<thead>
<tr>
<th>Royalties (%)</th>
<th>Management and Professional Fees (%)</th>
<th>Consultancy, Agency Fees (%)</th>
<th>Contractual Fees (%)</th>
<th>Training (including incidental costs) (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>20</td>
<td>20</td>
<td>15</td>
<td>20</td>
<td>20</td>
</tr>
</tbody>
</table>

Non-Residents
Withholding tax:
Dividends – No withholding tax is imposed if the recipient is a qualifying Kenyan financial institution or the resident recipient company controls 12.5% or more of the capital of the payer. Otherwise, the rate is 5% for dividends paid to residents of Kenya and on listed shares for citizens of the East African Community, and 10% for other nonresidents.
Interest – The general rate on interest paid to residents and nonresidents is 15%.
Royalties – Royalties paid to residents are subject to a 5% withholding tax; the rate is 20% for royalties paid to non-residents.

Branches of non-resident companies are taxable on all income derived from or accrued in Kenya. In determining the profits of a permanent establishment in Kenya, the gains or profits shall be ascertained without any deduction in respect of interest, royalties, management or professional fees paid or purported to be paid by the permanent establishment to the non-resident, and by disregarding any foreign exchange loss or gain with respect to the net assets or liabilities purportedly established between the permanent establishment in Kenya and the foreign head office or other offices of a non-resident person.

Other Issues

The introduction of the new county system of government will definitely boost the need for foreign investments in Kenya as different counties strive for sustainability. This shall subsequently oversee efforts by county governments to undertake regulatory reforms that shall enhance their business environments in terms of making them friendly for foreign investments.

Please be advised that the above information should be seen as a general guideline only. We strongly recommend that U.S. franchisors seek professional counsel from tax experts with in-depth knowledge of Kenya tax law. CS Kenya is happy to facilitate those connections.

For More Information
The U.S. Commercial Service in Kenya can be contacted via e-mail at: office.nairobi@trade.gov; Phone: +254 20 363 6424; Fax: +254 20 363 6722; or visit our website: www.buyusa.gov/kenya

The U.S. Commercial Service — Your Global Business Partner
With its network of offices across the United States and in more than 80 countries, the U.S. Commercial Service of the U.S. Department of Commerce utilizes its global presence and international marketing expertise to help U.S. companies sell their products and services worldwide. Locate the U.S. Commercial Service trade specialist in the U.S. nearest you by visiting http://www.export.gov/eac.