Strathmore UNIVERSITY

STRATHMORE LAW SCHOOL
MASTER OF LAWS (LL.M)
SUPPLEMENTARY EXAMINATION
LLM 8315: TAXATION OF FINANCIAL INSTITUTIONS

DATE: Friday, 15th May 2026 Time: 3 Hours

Instructions

1. This examination consists of FIVE questions.
2. Answer any THREE questions.
3. This examination is open book.
4. You should spend a fair amount of time organising your thoughts before starting to write.
5. Careful organisation and clarity will be highly valued.
6. Please start each question on a new page.

QUESTION 1

Taifa Wealth Management Ltd (TWML), a licensed fund manager, is reviewing whether its existing product structures remain tax-efficient and legally compliant. TWML currently administers three product lines:

- **Umbrella Unit Trust Scheme:** A single trust vehicle housing five sub-funds with different investment mandates (equities, fixed income, money market, balanced, and a newly proposed ESG fund). Investors may switch between sub-funds without exiting the scheme.
- **Captive Insurance Subsidiary:** Taifa Re Ltd, a wholly owned insurance subsidiary incorporated in Nairobi that underwrites risks exclusively for group entities and related-party clients.

- **Diaspora Bond Fund:** A closed-ended fund marketed exclusively to Kenyan nationals resident abroad, investing in Kenya Government infrastructure bonds and listed real estate securities.

You have been retained as TWML's external tax and legal counsel. Advise on the following:

i. Analyse the tax treatment of each of TWML's three product lines from the perspective of both the fund vehicle and the end investor. In your analysis, identify any structural weaknesses that expose TWML or its investors to unnecessary tax liability. **(10 marks)**

ii. The Kenya Revenue Authority (KRA) has queried whether the sub-fund switching facility within the Umbrella Unit Trust Scheme constitutes a taxable disposal for capital gains tax purposes. Advise TWML on the legal merits of this position and, if the switching facility does trigger a tax liability, propose a lawful restructuring that eliminates or defers the charge. **(10 marks)**

<u>QUESTION 2</u>

You are a tax policy consultant advising the Treasury of a developing African country that is reviewing its international tax treaty network. The country currently has double taxation agreements (DTAs) with ten countries, including several major capital-exporting nations. However, recent analysis shows that MNEs are exploiting treaty provisions through treaty shopping and other BEPS-related strategies, resulting in significant revenue leakage.

a) Explain the concept of treaty shopping and discuss at least three methods through which MNEs exploit tax treaties to achieve unintended tax benefits, citing relevant examples where applicable. **(8 marks)**

b) Assess the role of the OECD Multilateral Instrument (MLI) as a mechanism for modifying existing bilateral tax treaties to address treaty abuse. In your answer, evaluate both the strengths and the practical limitations of the MLI, particularly from the perspective of developing countries. **(7 marks)**

c) The country is considering introducing a domestic Principal Purpose Test (PPT) into its Income Tax Act as a standalone anti-avoidance measure. Critically analyse the legal and administrative challenges of implementing a PPT in a developing country context and suggest how these challenges may be mitigated. **(5 marks)**

Question 3

Micheal Yaxon Ltd. is a Kenyan multinational enterprise engaged in agro-processing and fast-moving consumer goods. Michael Yaxon operates through wholly-owned subsidiaries in Ethiopia, Rwanda, and Mozambique. The group is considering a comprehensive restructuring of its corporate and tax structure to improve profitability and optimise its regional tax position. Its current structure is as follows:

i. Michael Yaxon Kenya is the ultimate parent and holds all intellectual property (IP), including trademarks and proprietary processing technology.
ii. Each subsidiary pays royalties to Michael Yaxon Kenya for use of the IP under existing intercompany agreements.
iii. Financing for subsidiary expansion has been provided through intercompany loans from Michael Yaxon Kenya at fixed interest rates.

a) Identify and analyse the key transfer pricing risks Michael Yaxon faces under its current structure with respect to both the royalty arrangements and the intercompany loan pricing. Explain how the KRA may challenge these arrangements and the potential consequences for Michael Yaxon. **(10 marks).**

b) Propose three alternative restructuring options for Michael Yaxon that would improve tax efficiency across the group, address the identified transfer pricing risks, and align with the OECD's arm's length principle. For each option, outline its key features and primary tax advantage. **(10 marks).**

QUESTION 4

Kenya has recently discovered significant lithium deposits. A consortium of three multinational mining enterprises incorporated in Australia (AustraliaCo), Canada (CanadaCo), and the United Arab Emirates (DubaiCo), respectively, has established a joint venture to extract and export lithium. The joint venture is structured as follows:

i. A holding company, LithiumCo Holdings, is incorporated in Mauritius and holds 100% of the shares in the operating subsidiary in Kenya.

ii. LithiumCo Holdings is in turn wholly owned by the three companies (AustraliaCo, CanadaCo and Dubai Co).

iii. All project financing has been arranged through a related-party lender incorporated in the Netherlands, charging market-rate interest on a USD-denominated facility.

iv. The lithium ore is sold exclusively to a related-party trading company incorporated in Singapore, which then sells to unrelated end-buyers in Asia.

a) Identify and critically assess at least four distinct BEPS risks embedded in the joint venture structure described above, explaining the mechanism by which each risk results in a reduction of tax revenue for Kenya. **(10 marks)**

b) Advise Kenya on three immediate legislative or administrative measures it could adopt to protect its tax base from the identified BEPS risks, drawing on the OECD/G20 Inclusive Framework recommendations and any relevant African regional tax initiatives. **(10 marks)**

<u>QUESTION 5</u>

Kenya has, in recent years, introduced several tax policy measures aimed at broadening the tax base and increasing revenue from the financial sector, including the introduction of a Significant Economic Presence Tax (SEPT), amendments to thin capitalisation rules, and enhanced transfer pricing documentation requirements. Critics argue, however, that Kenya's tax policy framework for financial institutions remains fragmented, reactive, and insufficiently aligned with the principles of fairness, neutrality, and efficiency.

You have been invited to present a policy paper to the National Treasury on reforms to Kenya's taxation framework for financial institutions. Your paper should address the following:

a) Drawing on established principles of tax policy, critically evaluate Kenya's current approach to taxing collective investment schemes, with specific reference to the treatment of unit trusts, REITs, and pension funds under the Income Tax Act. Identify at least three structural inconsistencies or inequities in the current regime that your proposed reforms should address. **(10 marks)**

b) Assess the adequacy of Kenya's existing legislative framework in addressing the tax challenges posed by the digitalisation of the financial sector, with particular reference to the Digital Service Tax and its application to digital lending, digital insurance distribution, and mobile-based payment platforms. Discuss whether the DST as currently structured is consistent with internationally agreed principles on the taxation of the digital economy. **(10 marks)**