Tax Training for Non - Governmental Organizations

Painting a clear picture

Deloitte Place

April 2015

Course Contents

- Financial Reporting for NGOs & PBO Act Briefs
- International Public Sector Accounting Standards (IPSAs)
- Withholding Tax
- Corporate Tax
- Pay As You Earn

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Financial Reporting for NGOs PBO Act Briefs

Refined summary

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NGO Act requirements

- The NGO Act is being replaced by the PBO Act
- Filling of returns with the NGO Board 3 months after the end of the financial year using the statutory Form 14 (F-14)
- NGOs with receipts > 1M KES should submit audit accounts to the Board
- Audits Should be conducted by ICPAK practicing members
- Accounts Must be in KES
- Accounts must be in compliant with relevant reporting framework

? What determine the framework which the entity will adopt

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Reporting Frameworks

- International Financial Reporting Standards (IFRS)
- International Financial reporting Standards for Small and Medium Enterprises (IFRS for SMES)
- International Public Sector Accounting Standards (IPSAS) – Accrual
- International Public Sector Accounting Standards (IPSAS) Cash Basis
- Generally Acceptable Accounting Standards

All for the organizational reporting

- For Projects/Specific Donor funded Financial Statements special purpose framework should be used for reporting
- Including other reports such as reports on Compliance, Internal Controls and other requirements

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Financial Statements Components

For Organizational financial statements the basics should be (depending on the requirement of the financial reporting framework)

- Statement of Income and expenditure
- Statement of financial position
- Statement of changes in reserves/funds
- Statement of cashflows
- Statement of comparative between actual and budget
- Notes to the FS – Significant Accounting Policies and detailed notes

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Key Balances and Transactions and accounting Treatment

Income Statement Items

1. Income – Restricted and Unrestricted Funds

   – Different reporting frameworks requires different accounting of restricted and unrestricted funds

2. Expenditure – Advances or when accounted for by the implementing partners

3. Other income

4. Donations in Kind and in cash

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Key Balances and Transactions and accounting Treatment

Statement of financial position/Balance sheet items

- Property and Equipment
  - Organizational
  - Projects Assets
  - Donated assets
- Intangible assets
- Investments
- Bank and cash balances
- Receivables
- Unexpended grants/funds – represented by Cash and advances
- Deferred income
- Payables

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Key Balances and Transactions and accounting Treatment

Statement of changes in reserves/Funds

- Accumulated fund balances
- Any special fund maintained by the entity
- Assets replacement reserve

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Other Requirements

Depending on how the NGO is registered, relevant compliance is necessary:

- If registered under the Companies Act – Limited by shares or Guarantee
- Should file returns with the Registrar of companies annually
- Any change of directors should also be filed with the registrar of companies

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Where can we assist

- Review of financial statements to confirm compliance with the appropriate reporting framework
- Assist in preparation of financial statements that are in accordance with the applicable reporting framework
- Review organization’s compliance with agreement terms and conditions with the development partners
- Review internal controls to confirm effectiveness of the design and whether operating effectively
- Assist the organization’s with conversion from one reporting framework to another

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Where can we assist

- Develop finance manuals that are compatible with the applicable reporting framework
- For entities with Sub grantees – we can assist in assessing the capacity of the implementing partners as well as pre-disbursements assessment
- Manage disbursement of funds to implementing partners
- Train on key donors requirements such as EU, USAID, DANIDA etc.

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PBO Act

Objective of the PBO Act: To advance a new legal, regulatory and institutional framework for Public Benefit Organisations (PBOs) in Kenya.

- Presidential assent – 14th January, 2013
- Commencement date - by notice
- Repeals NGO Coordination Act of 1990
- Applies to all PBO operating in Kenya
- Administrative and regulatory framework for public benefits organizations to be placed under the Ministry of Planning and Devolution
- PBO Act not yet operational

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PBO Act – Current Status

Task Force was formed By the Ministry of Planning & Devolution to look at potential amendments through Public Participation country wide

- The Task Force is supposed to submit its report and make recommendations to CS by end of April 2015 who will give way forward on the same
- Meant to Repeal the NGO Act with transitional provisions
- Gazetted but to be sent back to parliament after public consultations on some amendments
- Organizations whose objectives include the direct benefit of members shall not be PBOs

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PBO Act - Benefits

Benefits to be enjoyed by registered NGOs i.e.

- Tax exemptions on members' subscriptions,income from economic activities,interest on dividend income, sale of assets,stamp duty(including on purchase of property)
- Waiver of court fees
- Preferential treatment under the VAT Act
- Incentives for donations by legal and natural persons

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PBO Act - Benefits

- Employment tax preferences
- Special tax incentives for donations from endowments, etc
- Direct government financing via subsidies,grantsfor specific purposes and contracts to perform certain work
- Preferential treatment in public procurement procedures
- Provision of information for policy making
- Access to training courses offered by Government Institutions

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PBO Act – Other Issues

- Previous registrations null and void
- NGOs registered under the repealed law deemed to be registered under the new law and have up to 1 year to seek registration as a PBO under the new law
- Former NGO Co-ordination Board to be transformed into PBO Authority
- An NGO registered under the repealed Act shall be bound by the provisions of the new Act

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PBO Act – Other Issues

- NGOs exempted from registration under the repealed law must seek registration under the Act within 3 months of the commencement of the Act
- For international NGOs, proof of registration in another country required
- International NGOs to have at least one third of governing body comprising Kenyans who reside in Kenya ---- no longer 1 Kenyan
- Filing of annual reports with the Authority within 6 months after the end of financial year

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PBO Act – Other issues

- PBOs expressly allowed to engage in lawful economic activities provided the income is applied solely to the PBO's public benefit purposes (e.g. investment in real estate for not-for-profit purposes)

- Until such time as the Tax statutes are amended to bring them in line with the PBO Act; the Kenya Revenue Authority (KRA) will continue to apply the existing exemption framework

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New Tax Exemption Applications under the PBO Act

- Firstly, an applicant would first have to qualify for registration and register as a PBO
- The Tax benefits would not be automatic, we expect there to be a process through which the tax exemptions are sought and confirmed
- Specific guidelines have not been issued and the challenge is that the Tax Acts have not been amended to incorporate the changes in the PBO Act
- Until such time as the Tax statutes are amended to bring them in line with the PBO Act; the Kenya Revenue Authority (KRA) will continue to apply the existing exemption framework

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PBO tax incentives compared to existing tax incentives

- PBO tax incentives are broader e.g. inclusion of employment tax aspect
- The tax incentives apply to a wider list of organizations i.e. not just for relief of distress or advance of religion or education
- They are contained in the same piece of legislation. It would be neater if the Tax Acts then referred to the PBO Act so that all PBO exemption information is available in a single Act
- However, successful implementation will be driven by the processes at KRA level

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Key messages

- The PBO Act has been passed into law and needs to be complied with and benefitted from ***when it becomes operational***
- Please seek professional support to understand the specific nature of your obligations under the PBO Act given your activities in Kenya
- Further guidance expected on a number of issues e.g. Tax exemption procedures so keep checking with us for an update

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How we can support PBOs

PBO specific support:

- More detailed legal review to assess requirements, risks and benefits of registration as a PBO
- Registration as a PBO
- Tax exemption applications
- Tax review to identify non- compliance as well as any tax planning opportunities

Other services:

- Regulatory review to ascertain compliance with Kenyan regulatory regime
- Labour law advice including drafting compliant employment contracts
- Litigation services in respect of any suits brought on the basis of Kenyan law
- Commercial services such as review of contracts with suppliers, service providers, landlords etc
- Tax compliance services including Payroll processing

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International Public Sector Accounting Standards (IPSAs)

Back to Basics

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Introduction to International Public Sector Accounting Standards (IPSAS)

Introduction

•The International Public Sector Accounting Standards Board (IPSASB) focuses on the accounting and financial reporting needs of national, regional and local governments, related governmental agencies, and the constituencies they serve

•It addresses these needs by issuing and promoting benchmark guidance and facilitating the exchange of information among accountants and those who work in the public sector or rely on its work. IPSASB is responsible for the issue of IPSAS

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Types of IPSAS

There are two types of **IPSAS;**

- ***Cash basis***: Allows for transparent financial reporting of cash receipts, payments and balances, under the cash basis of accounting

- ***Accrual Accounting:*** Focuses on revenue, cost, assets, liability and equity, instead of cash flow only. Most IPSAS are on accrual basis which is in line with IFRS

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IPSAS

•Compliance with the IPSAS guarantees that the financial reporting of public bodies conveys what is termed a “true and fair view” of the financial status of an organisation as is. IPSAS are modeled around the International Financial Reporting Standards (IFRS.) The use of IPSAS also ensures that financial statements are comparable for organizations that adopt them

•IPSAS take account of the characteristic features of the public sector. They are high quality global financial reporting standards for the application by public sector entities other than Government Business Enterprises. (GBEs)

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Why IPSAS are being introduced

1) The application of the IPSAS gives the financial reporting by bodies incorporated under public law greater significance through comparability with internationally recognised regulations for submitting financial statements. The greater transparency raises the quality of financial management, facilitates dealings with financiers and simplifies communication with the general public

2) In Kenya, there is increasing demand for public accountability and transparency by all stakeholders in the Public Sector. Current revelations during the Public Accounts Committee (PAC) hearing on the Auditor General's reports raise issues of financial accountability and transparency. The preparation of transparent and understandable financial statements is an important way for Government bodies to demonstrate their accountability to their taxpaying stakeholders and development partners. This communication is an important part of building trust

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Why IPSAS are being introduced (Continued)

Quality and comparability

The adoption of IPSASs by governments will improve both the quality and comparability of financial information reported by public sector entities around the world. It will improve the comparability of reports between various government agencies, parastatals, donor funded projects etc. Reports prepared in accordance with IPSASs provide for comparability between different financial periods, even within the same institutions, hence facilitating management decisions

Transparency

Disclosure information requirements of various reports will facilitate transparency in the financial dealings of public institutions. These disclosures will enable users of financial information interpret the reports in the right context and better decision making processes

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Why IPSAS are being introduced (Continued)

Consistency

IPSASs will also improve consistency in preparation and reporting of financial information. This will in turn enable users to draw consistent conclusions given similar sets of financial statements

Accountability

Adoption of IPSASs will improve accountability and ease the audits of public institutions. This will translate into timely audit reports, better information to donors and countries providing external assistance, better quality and credibility of financial reports

Governance

IPSASs will result in stronger governance procedures and a framework for the accounting practice in the public sector. This will strengthen the financial management of public institutions

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Challenges in adoption of IPSAS

There are a number of challenges envisioned in the adoption of IPSAS. These include;

- The IPSASs concept needs to be ***embraced by stakeholders*** such as Parliament, National Audit Office, Treasury, Government departments, Development Partners as well as Non – Governmental Organizations (NGOs)
- It is essential to have a ***legislative backing*** for the adoption of IPSASs among the public sector entities
- There are ***varying levels of national regulations relating to auditors*** and preparers of financial statements, as well as a history of developing ethics codes to meet local requirements

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Challenges in adoption of IPSAS (Continued)

- There are ***cost to be incurred in the implementations of IPSASs***. Statutory bodies responsible for enforcing accounting regulations require ***funding*** to roll out implementation of IPSAS. These costs include research, training, technology and consultancy costs
- There is ***call for political goodwill*** in the implementation of better accountability in the Public Sector due to divergent views on accountability

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SCOPE of IPSAS

- Applied to all general purpose financial statements prepared and presented under the accrual basis of accounting in accordance with IPSASs
- ***Does not*** apply to condensed interim financial information
- Applies to ***all public sector entities other than Government Business Enterprises (GBEs)***

Government Business Enterprise means an entity that has **all** the following characteristics:

a) Is an entity with the power to contract in its own name;

b) Has been assigned the financial and operational authority to carry on a business;

c) Sells goods and services, in the normal course of its business, to other entities at a profit or full cost recovery;

d) Is not reliant on continuing government funding to be a going concern (other than purchases of outputs at arm's length); and

e) Is controlled by a public sector entity.

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IPSASs in summary

Cash Basis IPSAS

Objective:

•To prescribe the manner in which general purpose financial statements should be presented ***under the cash basis of accounting***

•Compliance with the requirements and encouragements of this Standard will enhance ***comprehensive and transparent financial reporting*** of the cash receipts, cash payments and cash balances of the entity

•It will also enhance ***comparability*** with the ***entity's own*** financial statements of previous periods and with the financial statements of **other entities** which adopt the cash basis of accounting

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Cash-basis IPSAS

- The IPSASB has developed standards specifically for jurisdictions that continue to prepare financial statements on a cash basis. IPSAS Financial Reporting Under the Cash Basis of Accounting is in two parts: Part 1 addresses mandatory reporting requirements, and Part 2 sets out encouraged disclosures to support information reported under Part 1

- The standard encourages an entity to voluntarily disclose accrual-based information. An entity in the process of moving from cash accounting to accrual accounting may wish to include particular accrual-based disclosures in the process of transition

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IPSAS summary

In this guide, we summarize the provisions of all IPSAS outstanding at February 1, 2012. These standards are based on accrual accounting. This summary is intended as general information and is not a substitute for reading the entire standard

IPSAS	Standard	Based on
IPSAS 1	Presentation of Financial Statements	IAS 1
IPSAS 2	Cash Flow Statements	IAS 7
IPSAS 3	Accounting Policies, Changes in Accounting Estimates and Errors	IAS 8
IPSAS 4	The Effects of Changes in Foreign Exchange Rates	IAS 21
IPSAS 5	Borrowing Costs	IAS 23
IPSAS 6	Consolidated and Separate Financial Statements	IAS 27
IPSAS 7	Investments in Associates	IAS 28
IPSAS 8	Interests in Joint Ventures	IAS 31
IPSAS 9	Revenue from Exchange Transactions	IAS 18
IPSAS 10	Financial Reporting in Hyperinflationary Economies	IAS 29
IPSAS 11	Construction Contracts	IAS 11
IPSAS 12	Inventories	IAS 2

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IPSAS summary

IPSAS	Standard	Based on
IPSAS 13	Leases	IAS 17
IPSAS 14	Events After the Reporting Date	IAS 10
IPSAS 15	Financial Instruments: Disclosure and Presentation — superseded by IPSAS 28 and IPSAS 30	N/A
IPSAS 16	Investment Property	IAS 40
IPSAS 17	Property, Plant and Equipment	IAS 16
IPSAS 18	Segment Reporting	IAS 14
IPSAS 19	Provisions, Contingent Liabilities and Contingent Assets	IAS 37
IPSAS 20	Related Party Disclosures	IAS 24
IPSAS 21	Impairment of Non-Cash-Generating Assets	IAS 36
IPSAS 22	Disclosure of Financial Information About the General Government Sector	N/A
IPSAS 23	Revenue from Non-Exchange Transactions (Taxes and Transfers)	N/A
IPSAS 24	Presentation of Budget Information in Financial Statement	N/A
IPSAS 25	Employee Benefits	IAS 19

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IPSAS summary

IPSAS	Standard	Based on
IPSAS 26	Impairment of Cash-Generating Assets	IAS 36
IPSAS 27	Agriculture	IAS 41
IPSAS 28	Financial Instruments: Presentation	IAS 32
IPSAS 29	Investment Property	IAS 40
IPSAS 30	Financial Instruments: Recognition and Measurement	IAS 39 as amended by IFRS 9
IPSAS 31	Financial Instruments: Disclosures	IFRS 7
IPSAS 32	Service Concession Arrangements: Grantor	IFRIC 12

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IPSAS not based on IFRS

The five IPSAS not based on IFRS

- IPSAS 21: Impairment of Non-cash-generating Assets
- IPSAS 22: Disclosure of Financial Information about the General Government Sector
- IPSAS 23: Revenue from Non-Exchange Transactions (Taxes and Transfers)
- IPSAS 24: Presentation of Budget Information in Financial Statements
- Cash Basis IPSAS

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Main differences with IFRS

IPSAS have generally been based on IFRSs which are adopted to address the needs of the public sector. Some of the key differences between the two sets of accounting standards include:

- Basis of accounting: Many governments and their agencies (other than GBEs) continue to prepare financial statements on a cash basis, in line with their fiscal budgeting
- Recognition and measurement differences to address the absence of a profit driver for many public services where public policy objectives result in services being provided at no charge or an amount less than cost recovery. For example, non exchange transactions are common in the public sector (e.g., transfer payments), which have no equivalent in the for-profit sector. Similarly, for the purposes of impairment, a broader notion of service potential is considered for the public sector than just considering future cash flows generated
- Presentation and disclosures: The nature of government activities and the broader concept of accountability for outcomes demands a greater emphasis on information that is typically not found in for-profit financial statements prepared under IFRS. For example, information about the general government sector (GGS), revenue from non exchange transactions, and the presentation of budget information

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Trends in adoption of IPSAS worldwide

•The UN Group made the decision to adopt IPSASs in 2005. A number of other ***supranational organizations*** are also using IPSASs for their financial reporting. These include the European Commission and the OECD, NATO, IFAC and INTERPOL

•More than 70 countries have ***agreed processes or have a project in place*** to adopt IPSASs or align with IPSASs as part of wider reforms to adopt accrual accounting e.g. **Rwanda, Uganda**, Algeria, South Africa, Ghana, Brazil, Switzerland, Russia, India, China, Britain, USA, etc.

•ICPAK is leading in creating awareness of the need for IPSAS

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How can Deloitte assist?

•Deloitte has the ***technical skill and capacity to help the Public sector adopt IPSAS in Kenya***. Having practiced in the Kenyan Arena for many years, we have in depth understanding of the Public Sector needs in respect to financial reporting

•We have a network of global firms with whom we can leverage on to assist the IPSAS implementation in Kenya and Africa in general

•In 1999, Deloitte in Kenya worked with the private sector to assist them in the adoption of IFRS. We still hold seminars and workshops for business leaders and accounting practitioners to consult on implementation of IFRS and provide updates on recent changes. We can also assist the Public sector achieve the same

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Questions & Answers

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Withholding Tax

Giving you direction

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Withholding Tax training objectives

Learn/refresh on principles of withholding Tax so as to increase general withholding Tax awareness

Contents

1. Principles of withholding Tax obligations
2. Payments attracting withholding Tax
3. Definition of key terms for WHT
4. Withholding Tax Rates
5. Withholding Tax procedures & penalties
6. KRA Audits
7. Withholding Tax planning

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What is Withholding Tax?

- It is a system under which income Tax is collected on agency basis on behalf of the KRA
- The agency relationship is imposed by the law
- Agent making certain payments is required to withhold an amount (representing income Tax) and remit such amount to the revenue authority
- **Note: The income Tax collected under this system is Tax for payee of the specified payments, while the payer is only an agent for the Tax authorities**

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Basis of Withholding Tax in Kenya

The key Income Tax Act (ITA) provisions governing WHT are as follows:

- **Section 3**:- Income Tax chargeable on income which accrued in or was derived from Kenya or deemed to have been accrued in or derived from Kenya
- **Section 10**:- Certain payments by residents or Permanent Establishment (PE) deemed to be income which accrued in or was derived from Kenya
- **Section 35**:- Places the obligation on the payer to deduct Tax from certain payments to both residents and non-residents
- **Section 39 (1)**:- Allows WHT to be set off against the income Tax
- **Section 130**:- Gives the Minister of Finance powers to make rules with respect to the administration of Tax

Income Tax (Withholding Tax) Rules, 2001:- Pursuant to the powers conferred under Section 130, the Minister has issued these rules to prescribe the WHT administration procedures

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Section 35 of the ITA Specifies Following Payments as Subject to Withholding Tax

Payments to Residents and PE

- Management or professional fee whose value exceeds KES 24,000
- Training
- Dividend
- Interest
- Royalty
- Winnings from betting and gaming

Payments to Non - Residents

- Management or professional fee
- Training
- Royalty
- Rent for use or occupation of property
- Dividend
- Interest
- Payment to sportsmen or entertainers
- Winnings from betting and gaming

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Management or professional fees defined

- **ITA definition (Section 2)** - Payment made to a person, other than payment made to an employee by his employer, as consideration for managerial, technical, agency, contractual, professional or consultancy services however calculated
- **Contractual fee** - payment for work done in respect of building, civil or engineering works - See Section 35(3)(f) of the ITA
- **Consultancy fees** - payment made to any person for acting in an advisory capacity or providing services on an consultancy basis
- **Agency fees** – payment made to a person for acting on behalf of any other person or group of persons, or on behalf of the government, but excludes any payments made by an agent on behalf of the principal when such payments are recoverable
- **Professional** – not defined but recognized professions set out in Fifth

  Schedule to the ITA - Examples of payments covered here include medical fees, advocates fees, dental fees, payments to a land surveyor, veterinary surgeons, Architects or quantity surveyors, Engineers, auditors, consultancy fees and certified public secretaries etc

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Training fees

- **Section 2 of ITA Definition –** “payment made in respect of a business or user training services designed to improve work practices and efficiency of an organization, and includes any payment in respect of incidental costs associated with the provision of such services”
- An example is Tax training fees including any accommodation and travel incurred in the process

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Royalty

Section 2 of the ITA definition - payment made as a consideration for the use of or the right to use:

- The copyright of a literary, artistic or scientific work
- Patent, trade mark, design or model, plan, formula or process or
- Any industrial, commercial or scientific equipment

Examples

- Payments in respect of trade marks/brands, Intellectual property fees

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Withholding Tax rates

Income	Resident %	Non-resident %
Dividend > 12.5% voting power Dividend < 12.5% voting power	Exempt 5	10 10
Interest: Bearer instruments (>10 years) Financial institutions and Government 2 year bearer bonds	 10 15	 15 15
Qualifying interest: Housing bonds Bearer instruments	10 25	15 25
Royalties	5	20
Rent: Immovable property	N/A	30
Management or professional fees	5	20
Contractual fees	3	20
Consultancy and agency fees *EAC residents consultancy fee is 15%. EAC DTA awaiting conclusion	5	20
Insurance Commissions	10	20

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Rates applicable on payments to countries with which Kenya has a Double Tax Agreement in force

	UK	Germany & Canada	Denmark, Norway, Sweden, Zambia	India	France
	%	%	%	%	%
Management or professional fees * This does not include agency fees	12.5	15	20	17.5	20
Royalties	15	15	20	20	10
Rent					
• Immovable Property	30	30	30	30	30
• Other than immovable property	15	15	15	15	15
Dividends	10	10	10	10	10
Interest	15	15	15	15	12
Pension and retirement annuities	5	5	5	5	5
Entertainment and sporting events	20	20	20	20	20
Promoting entertainment or sporting events	20	20	20	20	20

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How withholding Tax is calculated

- Simply multiply the invoice amount relating to the services provided by the relevant withholding Tax rate
- Assume a management fee invoice is KES 1,000. This will also attract VAT at 16%. The total invoice amount will be KES 1,160
- Management fee payment to a resident person attracts withholding Tax at the rate of 5%. Withholding Tax will be KES 50

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How withholding Tax is calculated

The cheque payable to the supplier will be determined as follows.

	KES
Fee invoice	1,000
Add: VAT at 16%	160
	1,160
Less: Withholding Tax 5%	(50)
Less: Withholding VAT 6%	(60)
	1,050

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Withholding administration

- WHT is due by the 20th day of the month following the month of deduction
- Upon deduction and payment of WHT, a person is required to keep a record of the name of payee, PIN no, gross amount paid, nature of payment and amount of Tax deducted
- The Tax remitted is to be accompanied by an appropriate return (W8F) showing name of payee, gross amount paid and amount of Tax deducted
- The person making the WHT payment is required to furnish the payee with a certificate (W9F) showing gross amount and Tax deducted. The payee uses this certificate to claim Tax credit against corporation Tax
- End of year procedure – Within 2 months after the end of the year, to submit to the KRA a statement (W10F) and declaration showing particulars of the payees, withholding Tax deducted and gross amounts

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Withholding Tax forms

Returns and Forms:

- W1-Dividends
- W2-Interest
- W3-Royalties, management fees
- W8F-Tax deduction card (For consultancy, agency and contractual fees)
- W8A – (For interest)
- W9-Tax certificate
- W10F-End of year

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Withholding Tax penalties and interest

- For purposes of recovery of Tax, withholding Tax is demanded from the payer as though it were its Tax (recall WHT belongs to PAYEE and not PAYER)
- A penalty of 10% applies for late payment of withholding Tax (subject to a maximum of KES 1 Million)
- Up until 10 June 2010, any penalty levied was deemed to be Tax due and therefore attracted late payment interest
- Late payment interest of 2% per month is chargeable on any Tax remaining unpaid after the due date (but subject to the *In Duplum Rule)*
- Failure to file the annual return attracts a penalty of KES100,000 or 6 Months in jail or both

NB: The famous Section 72D penalty of 20% does not apply to WHT but KRA still challenges periods prior to 11 June 2010

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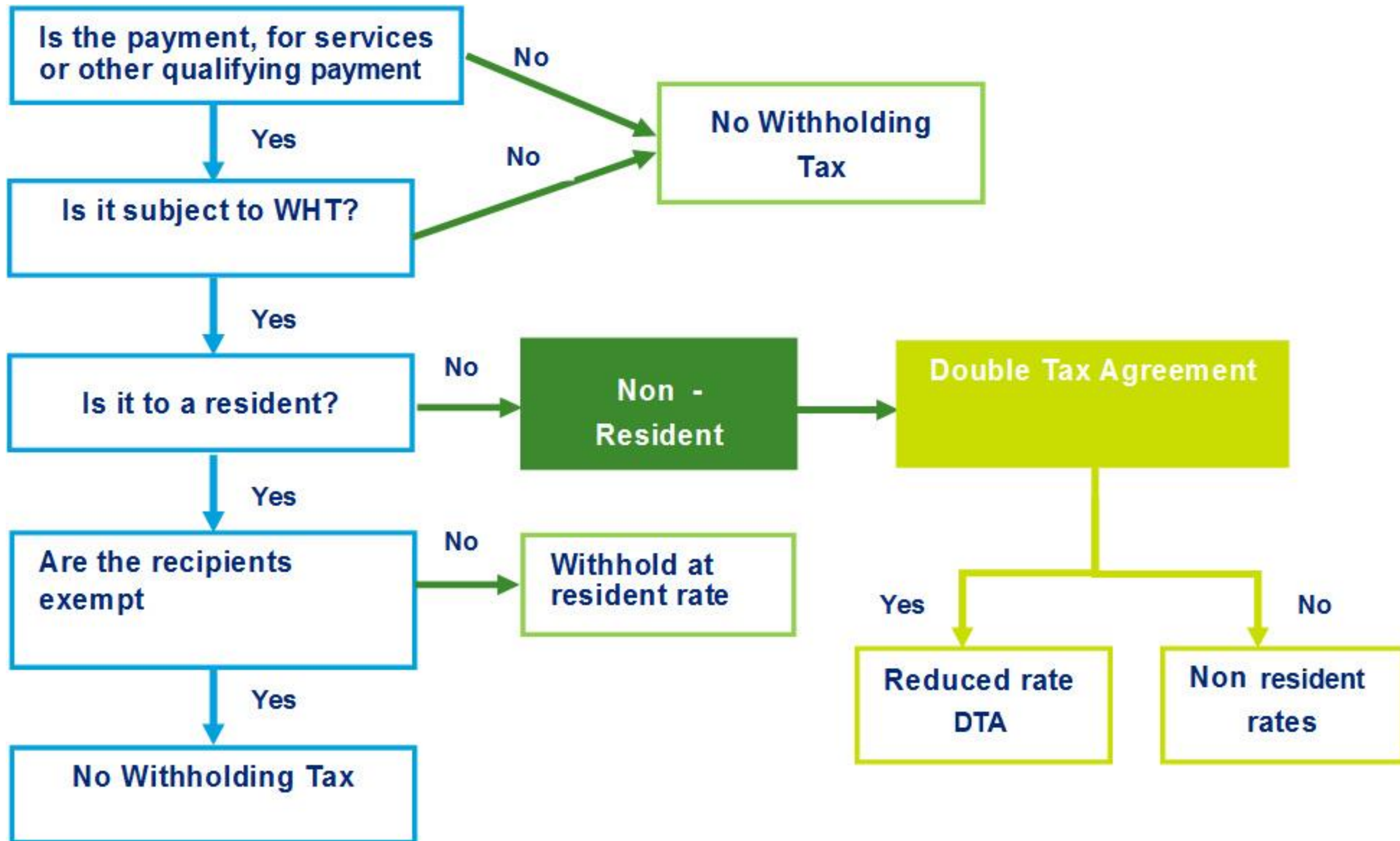
In a nutshell…



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KRA audits

Complex Withholding Tax issues

1. **Definitions** – It is usually difficult to determine which heading the payment falls under. Getting it wrong here means getting it wrong on rates
2. **The Tax point** – The Income Tax Act defines 'paid' to include distributed, credited, dealt with or deemed to have been paid. How do you deal with accruals that are subsequently reversed
3. **Mixed supplies** – WHT applies only to services. What happens where fees to be paid under a contract relate to both goods and services
4. **Double Tax Treaty environment** – Where there is a DTT, careful review and application is required. DTTs have delicate provisions that must be carefully applied
5. **Disbursements** – Are these part of the fees or not? The law is not clear and KRA insists forms part of fees and has won some cases
6. **Gross up problem** – Where the payee insists on receiving its full payment, the payer has to gross up. But the law says its not payer's Tax

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Withholding Tax planning

- Compliance to avoid fines and penalties
- Payment timing
- Direct disbursements payments
- Obtaining all certificates and claiming the Tax
- Double Tax Treaties – signed but not yet in force: EAC Countries, South Africa, Mauritius, Kuwait, Iran, UAE
- Contractual provisions
- Year-end crediting as opposed to monthly or quarterly

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Questions & Answers

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Corporation Tax

Showing you the way

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Outline

- Introduction
- Implications of Corporate Income Tax
- Exemptions from Corporate Income Tax
  - Circumstances to be considered tax exempt
  - Tax exemption certificates
  - Procedures for applying for tax exemption
  - KRA requirements
- PBOs – Tax Provisions
- Returns
- Assessments, Objections and Appeals
- Penalties and offences
- KRA in-depth Audits

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Income Tax in Kenya

Administration

- The National Treasury (Formerly Ministry of Finance)
- Kenya Revenue Authority (KRA)
- Domestic Taxes Department deals with Income Tax, VAT and Excise duty. Domestic Revenue Department that includes Medium Taxpayer Office and Large Taxpayers Office (LTO)-which is a separate department

Applicable law

- Income Tax Act (ITA)
- Subsidiary legislation - Schedules, Income Tax Rules
- Income Tax Departmental / Administrative instructions
- Case Law

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Basis of charge to Tax

- Tax is charged on the basis of source and/or residence
- Income Tax is charged on all income of a person whether resident or non-resident which accrues in or is derived from Kenya
- For business carried on partly within and partly outside Kenya, the whole of the profit from that business is Taxable in Kenya, e.g. transporters

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Non-Taxable income

- Exempt income under 1st Schedule; e.g.:
  - Income of Govt. Ministries, exempt NGOs
  - Income of County Governments
  - Income of a registered pension and provident scheme/fund
  - Interest on post office savings accounts
  - Interest income from all listed bonds (3-year maturity or more) used to raise funds for infrastructure & social services
  - Dividend received by a resident company from a company where it controls 12.5% or more of the voting shares

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Exemption from Corporate Tax

- Section 13 (2) of the ITA states that the Cabinet Secretary in charge of National Treasury may by notice in the Kenya Gazette exempt certain income from tax in respect of income not listed in the First Schedule (of the ITA)
- Paragraph 10 of the First Schedule of the Income Tax Act provides that:

  the income of an institution, body of persons, or irrevocable trust, of a public character established solely for the purposes of the relief of the poverty or distress of the public, or for the advancement of religion or education:-

  (a) established in Kenya; or

  (b) whose regional headquarters is situated in Kenya

  in so far as the Commissioner is satisfied that the income is to be expended either in Kenya or in circumstances in which the expenditure of that income is for purposes which result in the benefit of the residents of Kenya
- Bilateral Agreements and Double Tax Agreements

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Exemption from Corporate Tax

- Gains or profits from a business shall be exempt from tax where:
  - the gains or profits are put to use solely for the mentioned purposes and either -
  - the business is carried on in the course of the actual execution of those purposes; or
  - the work in connection with the business is mainly carried on by beneficiaries under those purposes; or
  - the gains or profits consist of rents (including premiums or similar consideration in the nature of rent) received from the leasing or letting of land and chattels leased or let therewith

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Exemption from Corporate Tax

- KRA issued a public notice on 16 February 2010 stating that all exemption certificates issued under Paragraph 10 of the First Schedule in the ITA that did not have expiry dates were rendered effectively invalid immediately
- The public notice stipulated that interested parties should apply for exemption certificates a new and that these shall be valid for a period of 3 years. However, the Finance Bill 2013 increased the validity period to 5 years
- Where an applicant has complied with all the requirements he will be issued with an exemption within sixty days of the lodging of the application
- Prior exemptions covered investment incomes i.e. interest and dividend income however the new legislation is silent in this area

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Procedures to apply for a tax exemption certificate

1. Review of Bilateral or Double Tax Agreements to ensure qualification for exemption
2. Review for qualification for exemption under Paragraph 10 of the Income Tax Act
3. Where one qualifies under option 1 above – no requirement to make the application as one automatically qualifies
4. Where you fall under category 2 above – you are required to make a formal application for exemption to the relevant KRA policy unit station
5. The KRA to conduct a comprehensive tax audit to ensure that the organization complies with all relevant legislation i.e. PAYE, Withholding Tax
6. Where KRA is satisfied that the organization is fully complaint with all tax heads they will then issue the exemption certificate
7. Application for renewal of this certificate to be done every 5 years. In practice this application must be made 6 months prior to the expiry

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KRA requirements

The KRA requirements for an Income Tax exemption are as follows:

- A brief outline of the activities of each organization;
- A letter from the relevant government agency dealing with the activities of each organization, confirming the nature of the activities carried out by the organization;
- The constitution, trust deed or the articles and memoranda of the organization;
- The management accounts of the organization for at least the last six (6) months;
- The bank statements of the organization for at least the last six (6) months;
- Evidence of the projects carried on for the last three (3)

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PBOs Act – tax provisions

PBOs receive benefits of registration as set out in the Second Schedule, namely:-

- Tax exemptions from:

  a) Income tax on sums received as membership subscription, donations and grants;

  b) Income tax on the PBOs income generating activities if the income is wholly used to support the purposes of which the PBO was established;

  c) Income tax on interest and dividends on investments and gains earned on assets or the sale of assets; and

  d) Stamp duty.

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PBO Act – tax provisions (Cont.)

- Preferential treatment under the VAT and customs duties legislation in relation to the importation of goods and services.

- Incentives for donations by legal and natural persons.

- Employment tax preferences.

- Special tax incentives for donations to form endowments, prudent investment policies, etc.

NB: Agency tax obligations remain as that is the 'other person's tax'.

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PBO Act – tax provisions (Cont.)

Challenges:

- Provisions are vague – it refers to “preferential treatment”, “preferences”, “incentives” etc. What do these terms mean since they have been used instead of “exemption”?
- Process is not provided for – tax exemptions usually require a vetting process with the Tax Commissioner or Finance Minister having the power to confirm or deny the exemption
- Conflict between existing provisions and new ones
- PBOs Act 2013 not yet in force

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Tax Risks for PBOs

Exemptions: not understanding scope of tax exemptions or not adhering to the requirements or required processes, especially as regards KRA. Failure to lodge correct paperwork could invalidate the exemption

Compliance: organisation failing to submit returns where required e.g. Corporate Income Tax returns required, even if there is no taxable income to report. VAT returns also required if you are VAT registered, even if VAT registration is done in error

Agency taxes: Withholding Taxes and PAYE obligations typically not covered by exemptions, unless there is a specific provision in ITA or government agreement. Tax not withheld becomes responsibility of withholding 'agent'. Examples of such cases:

- Not withholding tax on payments to research consultants based in Kenya or outside Kenya.
- Not withholding PAYE on benefits provided to staff e.g. unaccounted for per diems, unregistered pension schemes etc.

Penalty regime: the penalties and interest charges are onerous, even where a genuine mistake has been made. Waiver applications to the Cabinet Secretary for the National Treasury take a long time to resolve

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Managing your tax risks

- Make sure you know ALL about your various tax obligations – it is not enough to do what others are doing. Remember items like NHIF, NITA, NSSF etc. Please obtain specific advice based on your circumstances.
- Meet all tax compliance deadlines – the penalties are harsh.
- Regarding prior year activities, carry out a tax health checks to identify non-compliance issues that you may not be aware of. Consider options for dealing with the tax exposure. The earlier the problem is identified, the better!
- Keep up to date on tax matters and changes to legislation that impact you e.g. on pension, schooling benefit etc.

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Tax returns

- *Where the entity is dormant or tax exempt for a particular accounting period, it is still required to file its annual return, in this case referred to as a nil return as the entity did not trade or is exempted from tax.*
- Annual self assessment returns from 1992 plus:
  - Financial statements;
  - Tax Computation;
  - Auditors' certificate; and
  - Other support documents – withholding Tax certificates, etc.
- Due date for return is six months following the end of the income year/ accounting year.

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Assessments, objections & appeals

Assessments

- Self-assessment-Self-declared Tax
- Additional assessments are issued by Commissioner of Income Tax after audit
- Amended assessment after objection/appeals
- Estimated assessments issued for non-filers

Objections

- Taxpayer may object against an assessment issued by Commissioner within 30 days
- A late objection may be lodged after the specified time on grounds of absence from the country, sickness or other reasonable cause

Appeals

- There is a new Tax Appeals Act which was passed in December 2013 to replace all the appeals provisions in the various Tax Acts
- Tax Appeals Act was declared operational from 1 April 2015 through Legal Notice No 32
- Once in place, Tax Appeals Tribunal will replace Income Tax Local Committee that presides over income tax disputes
- Once can appeal against any decision of the Tax Authority by giving 30 days notice from the date of decision
- Appeal documents need to be served within 14 days of giving notice of intention to appeal

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Tax offences and penalties

Offences	Penalties
1. Late submission of the self assessment return	5% of Tax outstanding at the self assessment date-minimum KES.10,000 & 1,000 for companies & individuals respectively
2. Omission of income or fraud in a return	Additional Tax equal to maximum of double the difference between the Tax per the return submitted and the correct Tax per the correct income
4. Late payment	20% of Tax due

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Income Tax in-depth audit

- KRA selects Taxpayers for in-depth examination
- Enforce Tax compliance, full income disclosure, enhance collection and Taxpayer education
- Taxpayer Charter has provided for procedure for audit and rights of a Taxpayer

Procedure

- Letter from KRA for in-depth examination
- Mutually agreed date for commencement
- Tax agent to review/be involved
- Limit of time of audit specified in the Charter
- Audit to cover two years plus current

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Income Tax in-depth audit

Tips:

- Don’t give the KRA more than they ask for
- Skeletons in cupboard- advance planning required
- Cultivate mutually beneficial relationship
- Check the accuracy of KRA findings
- Discuss risk/potential liability with Tax consultants

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Questions & Answers

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PAYE

Back to Basics

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Objective

- Participants will be able to understand the basic underlying concepts covering Pay As You Earn (PAYE)

Areas covered

1. Understanding basic PAYE concepts
2. What constitutes Taxable income
3. Non-Taxable benefits
4. Allowable deductions
5. Tax reliefs
6. Other employment payments
7. PAYE forms and returns
8. Penalties and offences
9. Objections and appeals
10. Gray areas
11. Tax Planning ideas

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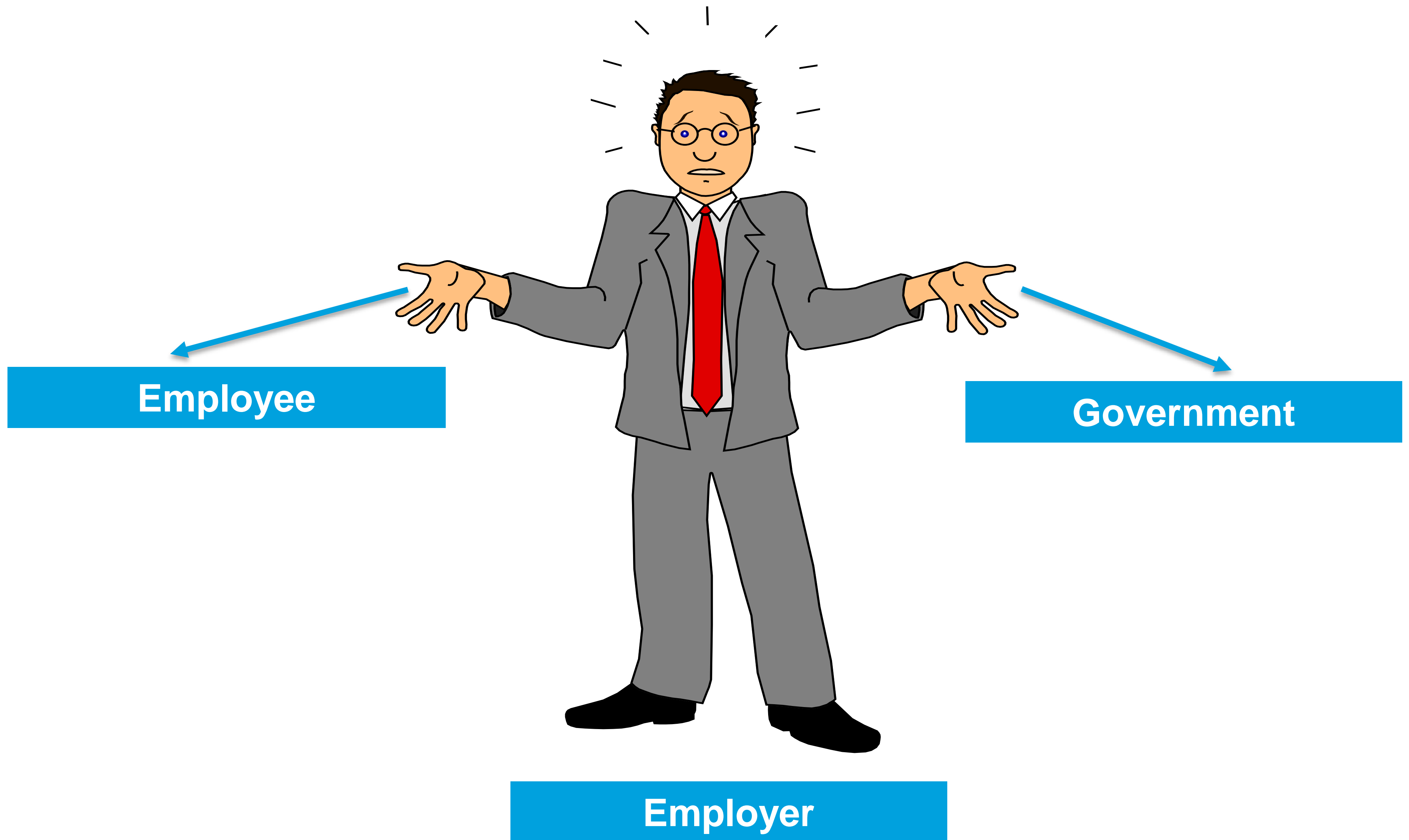
P.A.Y.E.



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Different parties

Employee

- Any holder of an office for which remuneration is payable
- Includes an individual receiving emoluments in respect of any employment, office, appointment or past employment

Casual employee

- One who is engaged for a period less than one month and emoluments are calculated in reference to the period of the engagement
- Regular casual employees are not considered as casuals

Employer

- Any person paying remunerations
- Any agent, manager or representative of employer who is outside Kenya
- Any trust, insurance or body of persons paying pension

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The agency burden

- PAYE is the employers responsibility
- The normal PAYE year runs from 1st January to 31st December

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Employment income

Chargeability to Tax

- Non-residents - income paid by a resident employer or permanent establishment of a non resident employer
- Resident individuals – Kenya and worldwide employment income

Residence rules for individuals

- Permanent home and presence in Kenya in that year of income
- No permanent home, but:
  - 183 days presence in Kenya in that year of income
  - 122 days or more in that year and each of the two preceding years

For citizens

- Set off of foreign Taxes paid on the same income

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Taxable income

- All emoluments in cash
- Non cash benefits exceeding KES 36,000 p.a. in the aggregate, with a few exceptions
- Club Subscriptions
- Per diems in excess of KES 2,000 per day

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Fringe Benefit Tax (FBT)

- Loans at concessionary interest rates
- Loans from unregistered pension or provident fund
- FBT applies even after an employee leaves employment as long as the loan remains un-paid
- Calculated using the 91 day treasury bill rates(market rates of interest)
- Benefit Taxed on employer at corporation rate of Tax

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Housing benefit

- Director and a whole time service director:
  - Higher of:
    - 15% of total income;
    - Fair market rental value; and
    - Actual rent paid by employer.
- Other employees: 15% of gains or profits from employment or rent paid by the employer (at arm's length), whichever is higher
- Where premises are provided by a third party under an agreement at arm's length, Taxable value is as above
- Where premises are provided by a third party under an agreement which is not at arm's length: Taxable value is the higher of fair market value & rent paid by the employer
- Where premises are owned by the employer: Housing benefit is the fair market rental value of the premises
- Occupied for part of the year: to be reduced proportionately
- Occupied part of premises: value to be reduced proportionately
- Rent contribution: to reduce value by amount of contribution

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Car benefit

- Chargeable benefit for private use shall be the higher of the rate determined by the Commissioner and the prescribed rate of benefit (2% p.m. of the initial cost of the vehicle)
- Where the vehicle is leased or hired from a third party, the benefit will be equal to the cost of hiring or leasing

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Other Taxable benefits

- Other benefits subject to higher of cost to employer or fair market value
- Benefits Taxed at prescribed rate only – by concession of CIT where the cost or fair market value cannot be determined
- Furniture – 1% of original cost p.m.
- Communal water supply – KES.500 p.m.
- Telephone (landline & mobile) – 30% of bills p.m.
- Communal electricity supply – KES.1,500 p.m.

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Non – Taxable benefits

- Leave passages: expatriate employees
- Medical services
- Employer's contribution to pension funds
- *Exception: Contributions by non Taxable employers:*
  - to unregistered schemes
  - excess contribution to registered schemes
- Education fees Taxed on the employer
- Reimbursement of expenses incurred by employee wholly and exclusively in production of income

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Allowable deductions

(Against Taxable income)

- Pension contribution – maximum KES20,000 p.m.
- Home ownership savings plan – maximum KES 4,000 p.m.
- Owner occupied interest – Maximum KES 12,500 p.m.

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Tax reliefs
(Against Tax payable)

- Personal relief, KES 1,162 per month.
- Life insurance and education policy – 15% of premium, maximum KES 5,000 p.m.

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Lump sum payments

- The income is spread backwards for five years and Taxed together with income earned in the prior years, balance Taxed in the fifth year
- Tax is recomputed using the prior year rate
- Service gratuity pay: Includes gratuity, bonuses, salary arrears etc relating to current and past years service-usually applies to retirees
- Compensation for loss of office: Relates to severance pay, retrenchment/redundancy

Spread forward

- Notice pay assessable in the period immediately after the date of termination of employment
- Leave pay assessed in the year to which it relates
- Ex-gratia assessed in the year of receipt

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PAYE forms/returns

- Remittance of monthly PAYE is before the 9th of the following month
- Form P11 - Remittance of monthly PAYE through banks, or Nil return submission to the Commissioner of Domestic Taxes
- Quarterly PAYE return to be filed before the 10th day of the month following the end of each quarter. (e.g. quarter ending September, return is due by 10th October)
- should be accompanied by
  - FormP9A – employees Tax deduction card detailing amount and details of all payments from which Tax was deducted;
  - Form P10 – Employers summary of monthly PAYE remittances including dates when payments were made to the bank;
  - P10A – Details of Tax deducted for each employee per P9A; and
  - P10B – FBT return.
- If return is filed monthly online, there is no requirement to file the quarterly returns

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National Security Social Fund (NSSF)

- Objective is to provide retirement benefit to members
- Rate of Contribution -10% of the employee's wages subject to a maximum of KES 400 per month of which half is contributed by the member
- Special contributions (casual workers)-KES 1 for each complete KES 20 of wages. Contribution is by employer only
- With effect from 1 May 2014, the New NHIF Act 2013 will take effect
- Under the new Act, each employer must pay to the Pension Fund in respect of each of his employees:
  - \- employer's contribution at 6% of the employee's monthly pensionable earnings; and
  - \- employee's contribution at 6% of the employee's monthly pensionable earnings.
- Objective is to provide health insurance coverage for members and their dependents
- Rate of Contributions vary from a minimum of KES 30 to a maximum of KES 320 per month with respect to salaried employees. (New rates suspended)
- Informal sector - Voluntary contributions
- Contribution is by the employee only. The employer only acts as an agent to collect and remit

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Suspended NHIF rates

Gross Income (KES)	Contributions (KES)
< 5,999	150
6,000 to 7,999	300
8,000 to 11,999	400
12,000 to 14,999	500
15,000 to 19,999	600
20,000 to 24,999	750
25,000 to 29,999	850
30,000 to 49,999	1,000
50,000 to 99,999	1,500
Over 100,000	2,000
Self-employed (special)	500
Indigents (voluntary)	300

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Penalties and offences

- Tax recovered from employer
- Failure to operate PAYE system satisfactorily: 25%, minimum 10,000
- Interest thereon, 2% per month on the principal Tax underpaid
- General penalty, where no other penalty is prescribed: KES 100,000, six months imprisonment

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Objections & appeals

- An employer can object against a PAYE Tax computation to the Commissioner for Domestic Taxes (CDT)
- An employer has right of appeal to the Local Committee against imposition of penalty or any other decision taken by the Commissioner under SECTION 37 (i.e. section dealing with PAYE) of the Income Tax Act
- Appellant required to pay all Tax due and the penalty prior to making the appeal

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Gray areas - general

- Shared benefits
- Servants
- Housing
- Sales vans/cars
- Benefits provided and used within the employer's premises
- Alarm
- Electricity - shared among employees & between employees and employers
- Mobile Phones
- Sale of products to staff at cost
- Benefit value is the cost or market price ?
- Employer guaranteed loans
- Employees charged at lower interest rate
- Passages to destinations other than home country
- Entertainment
- Consultancy vs. employment

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Tax planning ideas

- Maximize reliefs and deductions such as mortgage interest and insurance relief
- Mileage claim vs. car allowance
- Car loan vs. company car
- Telephone benefit (scratch cards) – only 30% Taxable
- Benefits below threshold
- Per Diems up to 2,000 per day. Excess to be on reimbursement basis or accounted for.

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Questions & Answers

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