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Direct Tax and Employee Tax Bootcamp

Deloitte Place, Nairobi

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Contents

- Corporation Tax
- Withholding Tax
- Pay As You Earn

Corporation Tax

Outline

- Introduction
- Imposition of Income Tax
- Exemption from Income tax
- Ascertainment of Total Income-Deductions allowed and deductions not allowed;
- Capital deductions
- Persons assessable & assessments
- Returns and record-keeping
- Communications & Electronic System
- Leasing
- Administrative Penalties
- Finance Act 2016 - changes affecting business tax.

Income Tax in Kenya

Administration

- The National Treasury-parent ministry and deals with policy issues
- Kenya Revenue Authority (KRA)-Tax administration aspect and has various departments
- Domestic Taxes Department deals with Income Tax, Value Added Tax and Excise duty
- Domestic Taxes Department further split into Medium and Small Taxpayers (MST) Office and Large Taxpayers Office (LTO)
- Other departments that cut across all taxes include Investigations & Enforcement department

Income Tax in Kenya

Applicable laws

- Income Tax Act (ITA)
- Tax Procedures Act (TPA)
- Tax Appeals Tribunal Act
- Subsidiary legislation - Schedules, Income Tax Rules
- Income Tax Departmental / Administrative instructions
- Case Laws

Kenya Tax structure

Direct Taxes

- Income Tax-Corporate & Individual

Indirect Taxes

- Value Added Tax
- Excise duty
- Customs Duty

Other Taxes/levies

- Stamp duty
- Airport Tax
- Tourism levy
- Road maintenance levy
- Import Declaration fees
- Export levies
- Second hand motor vehicle purchase tax

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

Charge to tax

Resident companies

A company is resident for any year of income if:

- It is incorporated under a Law in Kenya
- Management and control is exercised in Kenya
- It has been declared resident by a notice in the Kenya Gazette by the Cabinet Secretary for the National Treasury

Non-resident companies

Non-resident company with a permanent establishment in Kenya:

- A permanent establishment is a fixed place of business e.g. a branch or a Liaison office. A building site, a construction or assembly project which has existed for six months or more is deemed to be a fixed place of business
- Tax on income of such an entity will be determined at the prevailing non-resident tax rate

Charge to tax – source

When is income accrued in or derived from Kenya?

- Contracts signed in Kenya
- Passengers and cargo embarked in Kenya
- Communication apparatus established in Kenya
- Farming, mining, manufacturing operation in Kenya
- Property located in Kenya
- Funds collected in Kenya by banks

What constitutes taxable income

Gains or profits from:

- Any business
- Use or occupation of property – rent
- Capital gains
- Dividends
- Interest

Sundry Income:

- Insurance claims
- Releases from provisions
- Trading receipts
- Balancing charges (business ceased)
- Any other deemed taxable income

Non-Taxable income

Exempt income under 1st Schedule of Income Tax Act (ITA); 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
- Interest income on bonds issued by the East African Development Bank

Dividend received by a resident company from a company where it controls 12.5% or more of the voting shares

The Cabinet Secretary can exempt from tax an income or class of income through a notice, which notice has to be laid before the National Assembly for approval.

General rules on allowability of expenses

Wholly and exclusively incurred in the production of chargeable income - allowable business expenses

Revenue expenditure – allowable

Capital expenditure – not allowable

Allowable deductions

- Bad and doubtful debts (specific)
- Advertisements costs
- Losses of business income brought forward from prior years (carry forward limited to 4 years from 2010)
- The period for carrying forward tax losses now extended to ten years from the current five years. Taxpayers with huge capital investment had faced a risk of losing the benefit due to the short period of tax loss utilization

Allowable deductions

- Bad and doubtful debts (specific)
  - This has been a controversial one for some time
  - There has been disputes between KRA and banks on what is allowable
  - Law provided in 2007 that KRA may prescribe the appropriate guidelines for determining bad debts
  - The guidelines took long to be issued while the disputes between the parties continued
  - Arguments that Banks follow accounting standards and CBK prudential guidelines to provide for bad debts or write-off
  - The above arguments led to KRA losing cases at the tax arbitration body

Allowable deductions

- Bad and doubtful debts (specific)
  - KRA got to issue the guidelines in 2011 but this did not help the situation as it did not address the issue of specific provision for doubtful debt
  - KRA currently reviewing Bank's 2015 financials following spike in bad debt provision
  - It has already started issuing assessments running into hundreds of millions

Allowable deductions

- Pre-trading expenses
- Repairs and maintenance
- Entrance fee or annual subscription to trade association that elects to be taxed on the receipts from members
- Lease rentals
- Diminution in value of implement, utensil or similar article employed in production of gains or profits (plant and machinery not included)
- Legal costs & incidental expenses for purposes of listing in NSE without raising additional capital
- capital expenditure incurred on rating for purpose of listing on securities exchange operating in Kenya;
- Club subscriptions paid by employer on behalf of an employee.

Allowable deductions

- Contributions to a national provident fund or similar scheme established for employees through out Kenya
- Legal and incidental costs relating to authorization and issue of shares and securities to the public
- Legal costs and stamp duty relating to leases for premises if the lease does not exceed 99 years
- Non-resident branch taxes where the income is taxable in the hands of the Kenyan parent company
- Cash donations to registered charitable organizations whose income is exempt from tax or any project approved by the Cabinet Secretary for the National Treasury
- Capital expenditure on the construction of public schools, hospitals, roads or any similar social infrastructure (CS's prior approval required)

Capital deductions

- There are various capital deductions that are based on the nature of business apart from the general wear and tear deductions that apply across businesses
- One that could be relevant to your industry is Commercial building deductions
- Initially introduced in 2009 to take effect from January 2010 but there was lack of clarity
- To qualify, one should have constructed and used for business by him or his lessee and provided road, power, water, sewer and other social infrastructure
- A clarification that came in 2012 to take effect from January 2013 provided that a commercial building is one in use as an office, shop or showroom but the building should be one that does not qualify for other deductions under the schedule dealing with capital deductions
- The rate is 25% per annum meaning the cost can be written off over 4 year period

Capital deductions

Wear & Tear Deductions

Capital Deductions on machinery. Machinery includes:

- Vehicles
- Ship
- Aircraft
- Plant & machinery
- Software
- Furniture and fittings
- Office equipment

Capital deductions

Classes of machinery	Rates (%)
1) Tractors, combine harvesters, heavy earth moving equipment, other self-propelling machines of similar nature (including buses and lorries)	37.5
II) Computer and related hardware, calculators, copiers and duplicating and fax machines	30
III) Other vehicles and aircrafts	25
IV) All other machinery, including ships	12.5

Software

- Prior to 2009 there was uncertainty on claiming capital deductions on software
- Finance Bill 2009 introduced a rate of 5% period between 12 June 2009 and 31 December 2009
- Finance Act 2009 set the rate to 20% but effective from 1 January 2010

Deductions not allowed

- Capital Expenditure including software purchase
- Provisions
- Expenses for personal use
- Depreciation and amortization
- Contributions to unregistered pension schemes or funds
- Income tax or tax of similar nature on income

Persons assessable

- Persons include entities and individuals
- Persons whose income is accrued or is derived from Kenya
- Resident persons
- Non-resident persons which include a Branch and a Permanent Establishment
- Income of married women living deemed to be income of the husband but this would not apply if the married women opts to file separate Return
- Income of incapacitated person assessed in the name of trustee, guardian or receiver appointed by a court

Persons assessable

- Income of non-resident person assessed in his name or the name of his trustee, guardian, attorney, factor, agent, receiver or manager
- Income of deceased person deemed to be income of his executors or administrators and assessed on them
- Joint trustees are liable for an assessment on the trustees jointly and severally
- Agent responsible for payment of tax on behalf of a person is indemnified against any claim for all payments made by him

Tax assessments

- Self –assessment include payment return, NIL Return and credit return as well as electronic return with pre-entered information or tax being computed electronically as the information is being entered into the form
- Default assessment are made on taxpayers who fail to submit returns
- Advance assessment can be made before the due date on which the return is due
- Amended assessment arises where a tax audit results in change in the self-assessment or the taxpayer applied for correction of error or mistake
- Application for correction of error or mistake should be made within 5 years from the date of filing the self-assessment return
- The Act limits the period open for tax assessment by the KRA to 5 years from end of the reporting period to which it relates
- However, there is no time limit for assessment in case of gross or willful neglect, evasion or fraud by a taxpayer

Tax Returns

- Annual self assessment returns from 1992 plus:
  - Financial statements
  - Tax Computation
  - Auditors' certificate, and
  - Other support documents – withholding Tax certificates, etc.

The above scenario prevailed before introduction of iTax

Under iTax, data relating to the above are populated in a excel sheet and uploaded into the system

Manual withholding tax certificates no longer required as they are no generated once payment is made

Tax Returns

Due date for return is six months following the end of the income year/ accounting year

- The Tax Procedures Act provides for extension of time to submit tax returns
- The application for extension should be done before the original due date of the return and the Commissioner shall respond in writing
- The Commissioner has to be satisfied with the reasons for the delay in order to grant the application for extension
- However, the extension of time to submit a tax return does not extend to payment of tax associated with the return
- The Act empowers the Commissioner, by notice, to require a taxpayer to submit a tax return at any time during a reporting period and pay any tax due in relation to the return

Record-Keeping

- Records should be kept in either of the two official languages and retained for 5 years from the end of the reporting period to which it relates unless a shorter period is specified in a tax law
- The period may be extended where filed returns are amended by the taxpayer or Commissioner; or where there are proceedings that commenced before the end of the 5 year period
- The prescribed unit of currency in books of accounts, records, tax returns or tax invoices is the Kenya Shilling
- The Act permits Regulations to be published that may provide for a simplified system of record-keeping for small business enterprises

Communications & Electronic System

- The TPA gives Commissioner powers to demand that a certain tax return, application, document, payment of tax or act be done through electronic or mobile communication
- A statement contained in a document in electronic form shall be admissible as evidence of any fact stated in that document
- Submission of returns or payments of tax can done electronically on any day even where the due date falls on a weekend or public holiday in Kenya provided the deadline stipulated in a tax law is met
- Before this change, tax legislation requires filing of tax returns and payment of tax to be done on the previous working day if the due date falls on a weekend or public holiday in Kenya
- The Commissioner may issue a Tax Compliance Certificate valid for a specified period and may revoke it where a person fails to honor a tax demand or has violated provisions of a tax law

Leasing rules

- The Income Tax (Leasing) Rules introduced in 2002
- "Lessee" – person who leases from the owner or lessor of the asset and pays periodic payments
- "Lessor" – person who leases an asset to a lessee
- "Finance lease" – a contract which the lessor agrees to lease assets to the lessee for a specified period of time where the risks and rewards associated with ownership of the assets are substantially transferred from the lessor to the lessee, but with the title to the asset always remaining with the lessor
- "Operating lease" – a contract under which the lessor agrees to lease the assets to the lessee for specified periodical payments where the title to the assets and the risks and rewards associated with ownership substantially remain with the lessor
- "Hire purchase" – a contract under which the lessor agrees to lease the assets to the lessee for a specified period of time, with the intention of transferring ownership on the expiry of the lease
- No distinction between operating & finance leases for tax purposes

Chargeable income

- All income accruing to a lessor from payments made in respect of an operating or finance lease is taxable
- Lessor can claim a deduction for wear & tear
- Lessor can claim deduction of all other expenditure incurred wholly and exclusively in the production of income
- Lessee can claim deduction on full amount of lease payments made to the lessor

Capitalization of Assets

- Assets shall be capitalized in the books of the lessor
- Assets leased shall NOT be capitalized in the books of the lessee
- The lessor shall maintain a separate register for all leased assets

Termination of lease: "claw-back"

- **Commissioner has powers to recover any deductions enjoyed by the lessee where the lessee is deemed to have acquired the asset if lease is terminated:**
  a. without payment of any consideration
  b. on payment of nominal consideration in relation to fair market value of the asset, and
  c. upon transfer for an amount less than market value
- **The lessee will however be able to claim capital allowances on the claw-back amount**
- **Similarly the lessor's claims of capital allowances are claw-backed and the transaction recorded as a sale for tax purposes**

Cross-border lease

- Where a lessor in Kenya enters a cross-border lease, the gross lease payments made to the lessor shall be deemed to be income chargeable to tax
- Where a lessee in Kenya enters a cross-border lease, the gross lease payments made by such lessee shall be deemed to be income derived from Kenya and shall be subject to withholding tax

Administrative penalties

Offense	Provisions in the Tax Procedures Act
Failure to register or de-register for tax purposes where required to do so by a tax law	Penalty of KES 100,000 per month or part thereof subject to a cap of KES 1 million
Failure to keep, retain or maintain proper documents as required by a tax legislation	Penalty equal to 10% of the amount of tax payable subject to a minimum of KES 100,000
Late submission of PAYE returns	Penalty equal to 25% of the tax due or KES 10,000; whichever is higher
Late filing of any other tax return	Penalty of 5% of the amount of tax payable under the return subject to a minimum of KES 20,000 This penalty applies equally to both corporate entities and individuals KES 5,000 for turnover tax
Failure to file any other document, other than a tax return	Penalty of KES 1,000 per day subject to a maximum penalty of KES 50,000

Administrative penalties

Offense	Provisions in the Tax Procedures Act
Penalty for failure to submit a tax return online or pay a tax electronically when required to do so within 14 days of being asked	Penalty of KES 100,000
Tax shortfall attributable to deliberate provision of false or misleading statement or omission	Penalty of 75% on tax shortfall attributable to fraudulent tax filing 20% penalty applicable on tax shortfall not attributable to fraud Penalty on tax shortfall increased by up to 25% for repeat offenders (i.e. up to 100% on tax shortfall) Penalty reduced by 10% when a person discloses tax shortfall voluntarily to the KRA before audit starts

Administrative penalties

Offense	Provisions in the Tax Procedures Act
Tax avoidance	Penalty equal to 200% of the amount avoided by a taxpayer This penalty is not eligible for waiver by the Commissioner or the Cabinet Secretary
Fraudulent claim for a refund of tax	Penalty of 200% the amount of the claim under all tax laws
Offenses committed by KRA officers or persons required to act on Commissioner instructions	Fine not exceeding KES 2 million or to imprisonment for a term not exceeding 5 years or to both

Administrative penalties

Offense	Provisions in the Tax Procedures Act
Offenses committed by tax agents such as participating in creation of tax avoidance or evasion schemes; acting as a tax agent illegally	Fine equal to 200% of the amount of tax evaded or a fine of KES 5 million whichever is higher or to imprisonment for a term not exceeding 5 years, or to both
Fraudulent act of omission and commission in respect of a tax period	Fine not exceeding KES 10 Million or 200% of the amount of tax evaded, whichever is higher, or imprisonment for a term not exceeding 10 years or both
Failure to appear before the commissioner when required when the Commissioner is satisfied that the person committed an offense	KES 10,000 in the case of an individual and KES 100,000 in any other case.

Finance Act 2016-Changes affecting corporation tax

- The Cabinet Secretary for the National Treasury has now gazetted the Regulations for the graduate apprenticeship scheme through the Income Tax (Set-off Tax Rebate for Graduate Apprenticeships) Regulations, 2016
- Interest income on bonds issued by the East African Development Bank have been included under the First Schedule to the Income Tax Act that specifies income exempt from tax

2016 Changes

- Amendment of Eighth Schedule to the ITA to provide that the following transfer of assets is not subject to CGT:
  - between spouses
  - between former spouses as part of a divorce settlement or a *bona fide* separation agreement
  - to immediate family including a divorce or a *bona fide* separation agreement, or
  - to a company wholly owned by spouses or a spouse and immediate family

Questions & Answers

Withholding Tax (WHT)

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- The legislation
- Payments/services subject to WHT
- Rates-residents
- Obligations to deduct
- WHT administration
- WHT penalties and interest
- Complex issues/KRA audit issues
- WHT Planning
- Finance Act 2016 changes affecting WHT

Introduction – Principles of withholding tax

- Is an agency form of tax where a person making certain types of payments which are income subject to tax in Kenya is required to deduct tax therefrom and remit/transmit the tax deducted directly to the KRA
- The person who is required to withhold tax on a payment is called a **payer** while the person who is entitled to receive a payment which is income subject to withholding tax is the **payee**
- W/tax is not an additional tax. Rather, it is a payment of tax in advance on the income of the payee
- Where w/tax is not final tax, the tax should be claimable by the payee if the payee is resident in Kenya or is a PE of a non-resident person
- W/tax achieves the following:
  1. Curbs tax evasion
  2. Reduces tax administration costs, and
  3. Manages a country's cash flow

The Legislation

The following are the key provisions that govern the operation of WHT in Kenya:

- **Section 3 of the Income Tax Act (ITA)**:- stipulates that income tax should be chargeable on the income which accrued in or was derived from Kenya or on the income deemed to have been accrued in or derived from Kenya
- **Section 10 of the ITA**:- Deems the payments liable to w/tax to be income accrued in or derived from Kenya
- **Section 34** & the **Third Schedule** to the **ITA** - Provides the income tax rates
- **Section 35 of the ITA**:- Lists the payments that are subject to w/tax
- **Section 39 (1) of the ITA**:- Allows w/tax to be set off against income tax
- **Section 72D of the ITA** – Stipulates the penalty for late payment of tax
- **Section 38 of the Tax Procedures Act** – stipulates the late payment interest
- **Income Tax (Withholding Tax) Rules, 2001**:- Issued by the National Treasury CS (then Minister for Finance) pursuant to the powers conferred to the CS under Section 130 of the ITA. The rules prescribe the WHT administration procedures

Payments/services subject to withholding tax

Payments to Residents and PE

- Management or professional fee whose value exceeds KES 24,000
- Training fee
- Dividend
- Interest
- Royalty and natural resource income
- Rent on commercial property
- Winnings payable by bookmakers to punters
- Pension/retirement annuities

Payments to Non - Residents

- Management or professional fee
- Training fee
- Royalty and natural resource income
- Rent for use or occupation of property
- Dividend
- Interest
- Payment to sportsmen or entertainers
- Winnings payable by bookmakers to punters
- Telecommunication service fees
- Pension/retirement annuities

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 fees** – not defined but recognized professions set out in the **Fifth Schedule to the ITA** – Based on the professions listed under the Fifth Schedule, professional fees should therefore include fees charged by medical practitioners, dentists, advocates, surveyors and land surveyors, architects and quantity surveyors, engineers, accountants and certified public secretaries

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 of training fees includes payment for this tax training
- Incidental costs in connection with training can include **accommodation**, **travel** expenses etc. incurred on behalf of facilitators/trainers

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 e.g.. Franchise fees, intellectual property fees including software licenses etc.

Natural resource income

- Defined under Section 2 of the ITA to mean:
- An amount including a premium or such other like amount paid as consideration for the right to take minerals or a living or non living resource from land or sea, or
- an amount calculated in whole or in part by reference to the quantity or value of minerals or a living or non-living resource taken from land or sea

Examples

- Payments for quarrying
- Payments in respect of mining minerals
- Payments for the right to obtain timber
- Payments for the right to fish

Withholding Tax Rates

Description	Resident rate (%)	Non - residents rate (%)
Dividends > 12.5% voting power	Exempt	10
< 12.5% voting power	5	10
Interest - Housing Bonds	10	15
- Government bearer bonds 2 years and more	15	15
- Other interest	15	15
Insurance commission		
- Brokers	5	20
- Others	10	20
Royalties and natural resource income	5	20
Sporting or entertainment income	-	20
Pension/retirement annuities	0 to 30	5
Telecommunication service fees	-	5

Withholding Tax Rates

Description	Residents (%)	Non-residents (%)
Rent / leasing – Immovable property	10 (a)	30
- Others	-	15
Management, professional (other than contractual) & training fees	5	20 (b)
Contractual fees	3	20

a) Rent payable to resident persons for use of immovable commercial property to be liable to **10%** w/tax w.e.f. 1 January 2017. Withholders of such tax to be appointed by KRA

b) Payment of consultancy fees to **individuals** of the EAC partner states liable to w/tax at 15% and not 20%

Rates applicable on payments to persons resident in countries that have double tax treaties with Kenya

Residency country	Dividends	Interest	Royalties	Management fees
Canada	10	15	15	15
Denmark	10	20	20	20
France	10	12	10	0 or 20% (a)
Germany	10	15	15	15
Mauritius	5 or 10 (b)	10	10	0 or 20% (a)
India	10	15	15	17.5
Norway	10	15	20	20
Sweden	10	15	20	20
South Africa	10	10	10	0 or 20% (a)
United Kingdom	10	15	10	12.5
Zambia	0 or 10 (c)	15	15	15

a) The DTT between Kenya and France/South Africa and Mauritius do not have an article on management fess. Still not very clear whether rate should be 20% or 0%
b) Where dividends are paid to persons resident in Zambia, no dividend w/tax should be applied if the dividends are subject to tax in Zambia
c) If the beneficial owner is a company that holds at least 10% of the paying company's capital, w/tax should apply at 5%

Obligation to deduct

- Section 35 of the ITA provides an obligation to the payer to deduct tax on eligible payments for remission to KRA directly
- Failure to deduct tax on an eligible payment and remittance of the same to KRA is an offence under the ITA and attracts penalties and interest

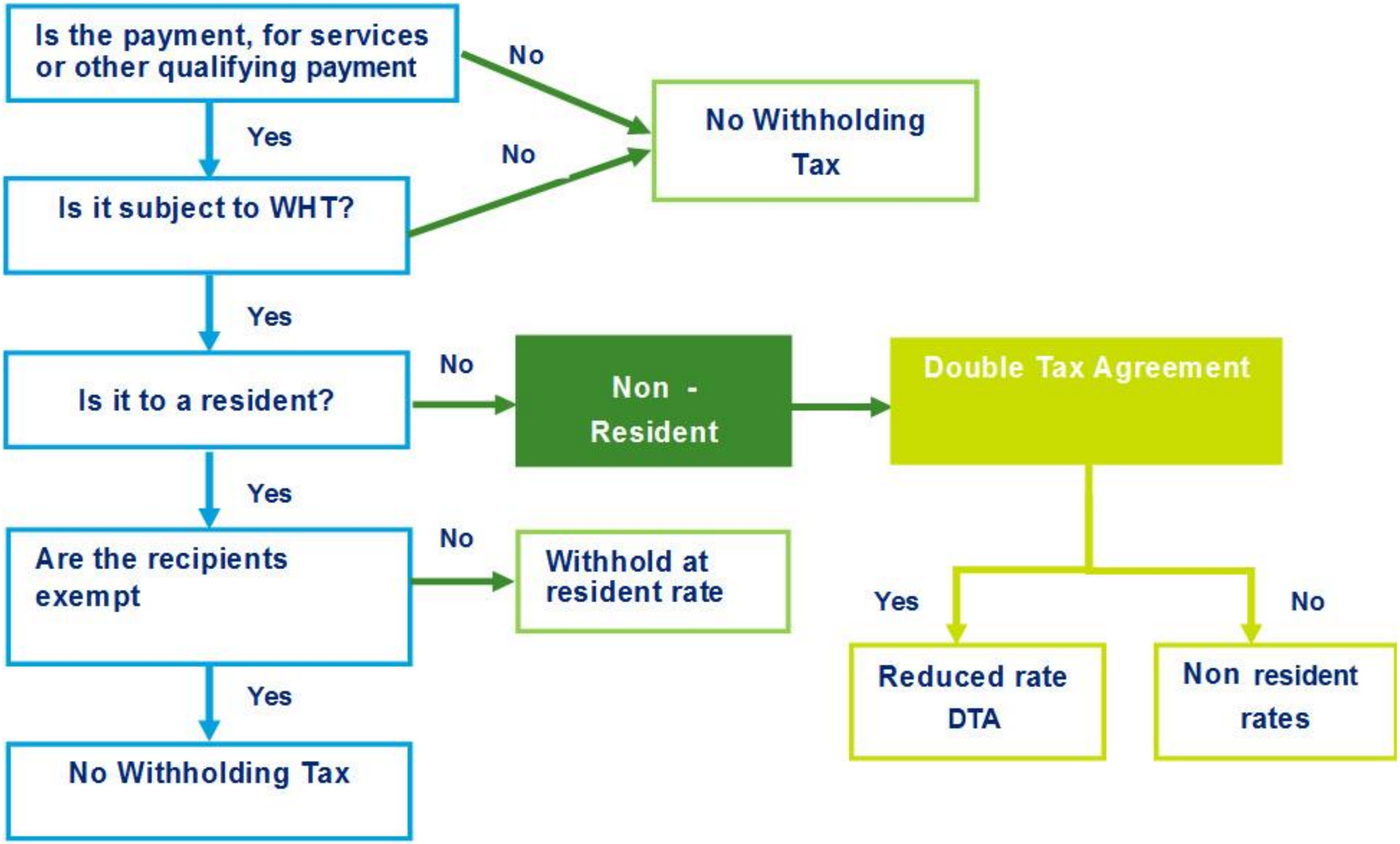
Withholding tax administration

- 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, gross amount paid, nature of payment and amount of tax deducted
- Withholding tax accounting is now fully supposed to be done through iTax
- Upon paying the tax, the iTax platform should generate a certificate that should be sent to the payee to enable the payee claim credit against income tax
- Annual w/tax return – A withholding tax return needs to be filed with KRA by the end of February of the following year. The return summarizes all payments made in the prior year

Penalties and interest for non-compliance

- For purposes of recovery of tax, withholding tax is demanded from the payer as though it were the tax of the payer (recall WHT belongs to PAYEE and not PAYER)
- A penalty of 20% should apply for late payment of withholding tax – up until 9 June 2016, the penalty used to be 10% but capped to KES 1 million
- Late payment interest of 1% per month is chargeable on any tax remaining unpaid after the due date – the late payment interest charged is capped to the principal tax involved (*Induplum rule*)
- Failure to file the annual return attracts a penalty of KES 100,000 or imprisonment for 6 months or less

In a Nutshell…



Complex issues/ KRA audit issues

1. **Definitions** – It is important to determine whether a payment falls under the ambit of withholding tax based on the highlighted definitions. For instance, should payments to body builders be liable to w/tax?
2. **The tax point (actual payment vs accrual)** – Should w/tax be based on actual payment or accrual?
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. **Treaty provisions** – Where there is a DTT, careful review and application is required. DTTs have delicate provisions that must be carefully applied. The South African, French and the Mauritian treaty are important examples
5. **Disbursements and reimbursements** – should w/tax be based on disbursements and reimbursements? What is the difference between the two
6. **Gross up problem** – where a contract is negotiated net of tax, should w/tax be based on the contract fee or should it be grossed up?
7. **Payment in kind** – How should w/tax be accounted if payment is made in kind? For instance on winnings

Withholding Tax Planning

- Compliance to avoid fines and penalties
- Payment timing
- Direct disbursements payments
- Obtaining all certificates and claiming the tax
- Double Tax Treaties
- Contractual provisions, and
- Year-end crediting as opposed to monthly or quarterly

Finance Act 2016 changes

- Deletion of the 10% penalty (that was capped at KES 1 million) – effective 9 June 2016
- W/tax in respect of commercial property rent paid to resident persons clarified – rate to be 10% and not 12% as per the Finance Act 2015. In addition, enabling provisions now introduced – effective 1 January 2017
- Non-resident and resident tax rates applicable to winnings from betting and gaming deleted
- Withholding tax agents for residential rental income to be appointed

Questions & Answers

PAYE

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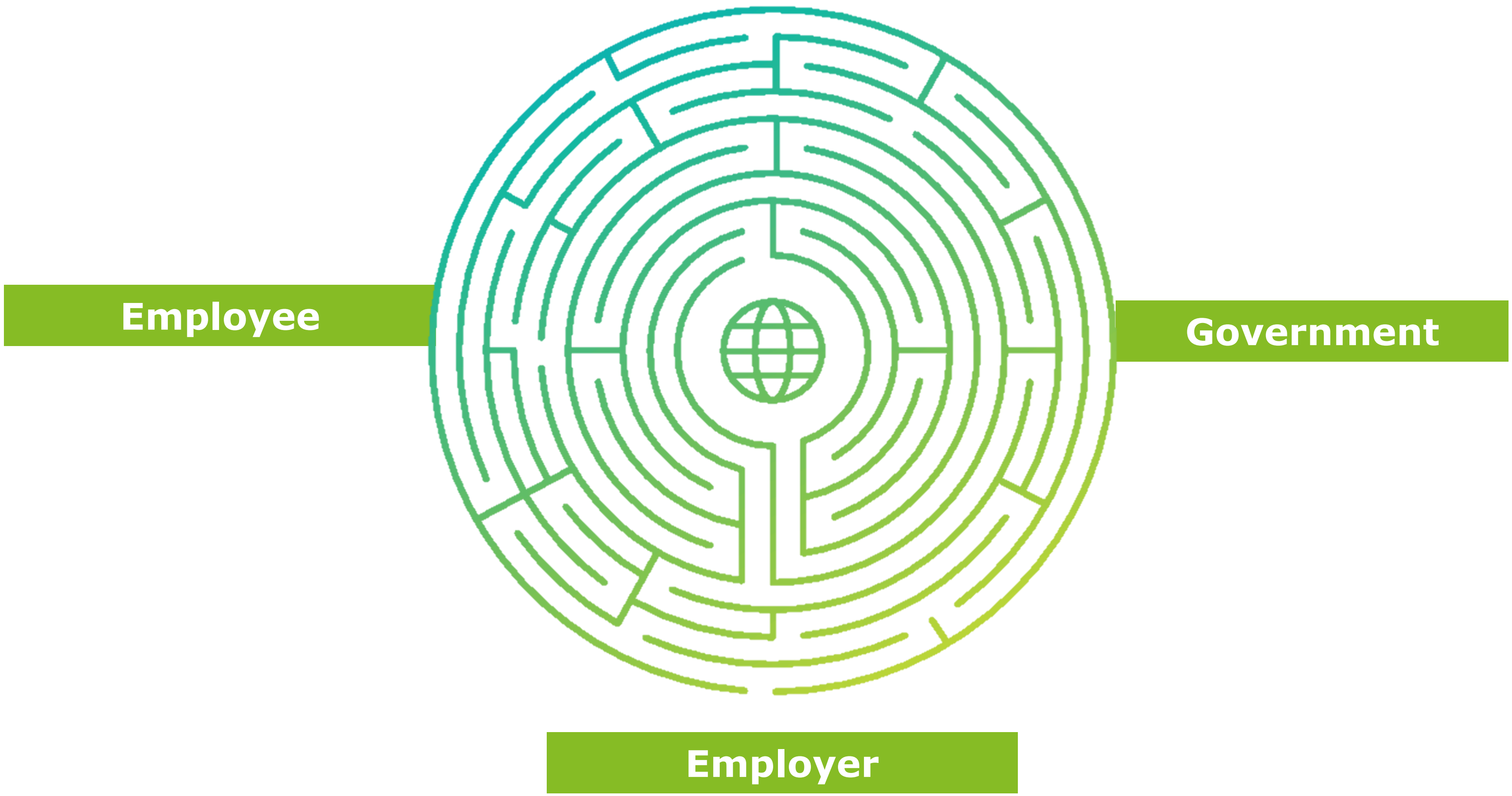
P.A.Y.E.



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
- **Appointments**
- Directors – executive and non-executive
- Directors allowances and benefits – PAYE or WHT?
- **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 to be 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

The agency burden

- PAYE is the employers responsibility
- Employee is an agent of the government
- The normal PAYE year runs from 1st January to 31st December

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

Taxable income

- All cash emoluments except bonus, overtime and retirement benefits to employees in the lowest tax bracket i.e. 10,164/11,180
- Non cash benefits exceeding KShs 36,000 p.a. in the aggregate, with a few exceptions such as lunch benefit
- Club Subscriptions
- Private expenditure paid by employer e.g. utility bills
- Per diems in excess of Kshs. 2,000 per day

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

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

Housing benefit

- 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

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.

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 – Kshs.500 p.m.
- Telephone (landline & mobile) – 30% of bills p.m.
- Communal electricity supply – Kshs.1,500 p.m.

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
- Lunch benefit subject to a maximum value of KES 4,000 per month

Allowable deductions
(Against taxable income)

- Pension contribution – maximum Kshs. 20,000 p.m.
- Home ownership savings plan – maximum Shs.4,000 p.m.
- Owner occupied interest – Maximum Shs.12,500 p.m (Shs 25,000 p.m. w.e.f. 1 January 2017)

Tax reliefs
(Against tax payable)

- Personal relief, KShs 1,162 per month (KES 1,280 w.e.f 1 Jan 2017)
- Life insurance and education policy – 15% of premiums, maximum KShs 5,000 p.m.

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

Lump sum payments

- 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
- Bonus assessed in the month of receipt

PAYE forms/returns

- Remittance of monthly PAYE is before the 9th of the following month
- Online filing of monthly PAYE or Nil return submission to the Commissioner of Domestic Taxes via iTax
- Quarterly returns no longer required due to online filing

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 KShs 400 per month of which half is contributed by the member
- Special contributions (casual workers)-KShs 1 for each complete KShs 20 of wages. Contribution is by employer only
- Under the NSSF Act 2013, 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
- The value of the pensionable earnings has a lower limit and an upper limit, both of which will gradually increase over a 5 year period. The new rates are yet to be effected due to ongoing litigation

National Hospital Insurance Fund (NHIF)

- Objective is to provide health insurance coverage for members and their dependents
- Rate of Contributions vary from a minimum of KES 150 to a maximum of KES 1,700 per month with respect to salaried employees
- Informal sector - Voluntary contributions
- Contribution is by the employee only. The employer only acts as an agent to collect and remit

NHIF Rates

Gross income (KES)	Monthly premium (KES)
0-5,999	150
6,000 - 7,999	300
8,000 - 11,999	400
12,000 - 14,999	500
15,000 - 19,999	600
20,000 - 24,999	750
25,000 - 29,999	850
30,000 - 34,999	900
35,000 - 39,999	950
40,000 - 44,999	1,000
45,000 - 49,999	1,100
50,000 - 59,999	1,200
60,000 - 69,999	1,300
70,000 - 79,999	1,400
80,000 - 89,999	1,500
90,000 - 99,999	1,600
100,000 and above	1,700
Self employed (special)	500

National Industrial Training Authority (NITA)

- Subject to approval by NITA, employers who are registered with NITA and are up to date on levy payments can get a reimbursement of training costs if:
  - The employer makes an application to NITA two weeks before the training i.e. for local training and one month for overseas training
  - The training provider is registered with the NITA and is up to date with the annual registration renewal
  - The employer can prove that the training is relevant to the employees' duties/work, and
  - The reimbursement claim must be supported with receipts of payment of training costs and the approval letter from NITA

Penalties for non-compliance

Failure to pay the training levy attracts a penalty of 5% on the amount of levy due to the authority

PAYE penalties and offences

- Tax recovered from employer
- Failure to operate PAYE system satisfactorily: 25%, minimum 10,000
- Interest thereon, 1% per month on the principal tax underpaid
- General penalty, where no other penalty is prescribed: KES 100,000, six months imprisonment

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 Tax Appeals Tribunal against imposition of penalty or any other decision taken by the Commissioner under the provisions of the Tax Procedures Act
- Appellant required to pay all tax due and the penalty prior to making the appeal

KRA in-depth tax audit

- KRA selects taxpayers for in-depth examination
- Purpose is to 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

KRA in-depth tax 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

Tax Returns

- Annual self assessment returns from 1992 plus:
  - P9
  - Mortgage certificate
  - Insurance relief certificate, and
  - Other support documents – withholding tax certificates, etc.
- Due date for return is six months following the end of the income year
- Issues:
  - Kenyan citizens working abroad
  - Expats
  - Tax credits

Grey areas - general

- Shared benefits e.g.
  - Servants
  - Housing
- Sales vans/cars
- Benefits provided and used within the employer's premises
  - Alarm
  - Electricity - shared among employees & between employees and employers

Grey areas

- 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

Finance Act 2016 -changes affecting individuals

- Exemption of bonuses, overtime and retirement benefits made to low income employees whose income falls in the lowest tax band (KES 10,164) effective 1 July 2016
- Increase of personal relief to KES 1,280 per month (15,360 per annum) effective 1 January 2017
- Individual tax bands have been increased by 10% as summarized below effective 1 January 2017:

Rate in each shilling	%
On the first 134,164	10
Next 126,403	15
Next 126,403	20
Next 126,403	25
Over 513,373	30

Tax planning ideas

- Maximize reliefs and deductions such as mortgage interest and insurance relief
- Mileage claim vs. car allowance
- Car loan vs. company car
- Reduced rate or motor vehicle benefit – ITA provides for a lower rate of benefit where restricted use of the vehicle can be proved. The Commissioner has also issued guidelines on the supporting information required
- 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

Questions & Answers