Presented by CPA Wycliffe Kibisu
Venue: Sarova White Sands Mombasa
Date: 6th November 2014
Topic: Tax Compliance and Efficiency for NPOs

Tax Compliance and efficiency for NPOs is essential as ever

Presented by:

Taxworld Africa

The agenda

- Tax planning basics/Definations
- Relationship of Tax compliance and efficiency and organization tax policy
- Tax affecting NPOs
- Exemption/Benefits of taxes
- Overview of other tax matters

TAX WORLD AFRICA

TAX PLANNING BASICS

- **To save or defer tax, think about timing.**

Smart timing can reduce your tax liability — poor timing can unnecessarily increase it

Definations

- There are various types of not-for-profit organizations ("NPOs"):
- Non-Governmental Organizations (NGOs) (New PBO Act 2013 to be Public Benefit Organizations (PBOs)).Companies Limited by Guarantee; Societies; and Trusts.
- Other not-for-profit legal forms include churches, political parties, and trade unions.

Definations

Tax efficiency From Business Entity Perspective- Businessdisctionery.com

- Feature of a financial instrument which permits its holder to establish or modify an investment position such that it **attracts lower tax liability than other such instruments**. Tax efficient instruments include tax-free bonds, tax-free money market accounts, and stocks (shares) which are held for more than a year (thus paying long-term, and not short-term, capital gains tax).

TAX WORLD AFRICA

Definations

Tax Planning

- Basic level of tax planning is tax compliance ie being able to pay the correct tax, within the set deadline and filing the right documents within the set deadline.
- The advanced level of tax planning involves designing your transaction to optimize tax and tax related costs in the organization value chain.

- As part of Corporate Governance Code, the Management board must disclose in annual report its business risks (strategic, operational, financial and compliance risks).

- Taxes fall under the business risks of compliance and may involve either the below the line taxes or transactional taxes.

- Tax risks management entails the risks associated with non-compliance with tax legislation, risks of wrong reporting or risks of missed opportunity to save tax cash outflow.

- The big picture is that taxes can curtail corporate strategy and company **reputation**.

- **The following are identified as risks that are inherent in an organization tax system:-**
- Valuation risks-The risks that the tax amount disclosed in Financial Statements are wrong. This may include both corporate taxes, differed taxes and transaction taxes as VAT and other levies
- Reputation risk-The risk that failure to pay taxes may have a negative impact on a company after a revenue authority audit that may disclose additional taxes that are well above its cash flow ability.
- Operation risk-We have some taxes that are outside the scope of the tax department but may curtail business performance. E.g payroll taxes, VAT and information reporting
- The above can only be managed by a change in human factor and changes of cultural aspects (correct **"Tone at the top"**).

- In contrast to popular believes, tax risks mainly arise from issues related to **poor** or lack of communication between departments and people, instead of factual or technical analysis of tax issues.
- Insight-**Communication**
- Follow-up-**Communication**
- **Facts Analysis-Communication**
- Technical Analysis-**Knowledge**

- From the above, it is clear that communication is critical to a tax risk management. 85% of mistakes in taxes are arising from communication.
- Making sure that the relevant persons understand the tax issue, the essential facts and what is needed to resolve the issue and most importantly: **Who takes ownership** requires an organization to have a tax role and responsibility matrix

WHY TAX POLICY?

1. **Planning and general approach**
   The organization aims for certainty on tax positions it adopts but where tax law is unclear or subject to interpretation, written advice or confirmation will be sought as appropriate to ensure, on the balance of probabilities, that the position adopted would, <u>more likely than not, be settled in our favour.</u>

2. Compliance and Tax Authority relationship

The organization should comply with all tax regulations in all countries in which it operates. It should submit all returns by their due dates and in line with local tax law.

OUR TAX POLICY

3. **Reputation**

It is not appropriate for the Group’s tax affairs to appear in the public domain or for a tax decision to have any adverse effect on shareholder value. The Group is only prepared to enter into transactions which could appear in the public domain where they have an underlying commercial rationale or have become common practice. Where this is a risk, the CFO, Media Relations and appropriate parties must be informed before the risk is taken. The tax function will manage its compliance affairs to minimise the risk of any adverse public comment.

Exemption of Taxes

- Kenya exempts NPOs from the following taxes:
  - corporate income tax the income of certain NPOs that carry out specific types of activities.
  - Unrelated business income is subject to tax under certain circumstances.
  - Kenya also subjects certain sales of goods and services to VAT, with a fairly broad range of exempt activities.
  - The tax laws confer only limited tax benefits on corporate donors and on individual donors.

Exemption of Taxes Incomes

- For its income to be exempt from income tax, an organization must have been established solely to relieve poverty or distress of the public, or to advance religion or education. In addition, the Commissioner of Income Tax must conclude that the income is expended either wholly within Kenya or in ways that benefit the residents of Kenya (Income Tax Act First Schedule, Cap 470, Para. 10 as amended by Legal Notice No. 6 of 2001].
- Income consisting of profits from a business is subject to an additional restriction: Such income is exempt from tax only if it meets the criteria set in the paragraph.

Exemption -VAT

- Under the PBO Act, there shall be preferential treatment under VAT and customs duties for imported goods or services that are used to further an organization's public benefit purposes (PBO Act Second Schedule Para.
- Under Regulation 30 of the NGO Coordination Regulations 1992, if an organization requires exemption from VAT on goods and services required to meet its objectives and on income-generating activities (or income for expatriate employees), it must make an application through the NGO's Board to the Cabinet Secretary of Finance.

Exemption of Taxes-DUTY

- The East African Customs Union, which came into force on 1st January 2005, introduced new changes to the Duty on imported items for charitable organization.
- Prior to coming into force of the EACU, NGOs and charitable organizations were exempted from customs duties and other charges of equivalent effect under the customs law of the individual member state.
- It is important to note that NGOs and charitable organizations (globally) enjoy duty exempt status since the services they provide are directed towards alleviating poverty and providing basic needs to the marginalized and underserved members of our society.
- Governments have an obligation to extend duty concessions to NGOs and charitable organizations to supplement their efforts.

Exemption of Taxes

- The East African Customs Management Act 2004 (EACMA), which spells out the customs law of the community, phased out the duty exemptions previously extended to NGOs and charitable organizations under the national regime effective 1st January 2005.
- This implies that the charitable organizations operating in the East African Community (EAC) region are now stripped of their duty exempt status and are required to account for customs duties like any one else.

Exemption of Taxes

- However, the EAC Council of Ministers extended a window through which charitable organizations can access the duty exempt status.
- The window provides that individual partner states can, through a budgetary allocation, provide funds to cater for duty on imported goods.
- For this program to work, the Ministries of Finance in the respective member states are required (though not mandatory by law) to avail funds through a budgetary allocation to pay for the duties applicable on goods imported by NGOs and Charitable organizations.
- To access this pool, charitable organizations are required to obtain an exemption authority from the respective Ministries of Finance. The exemption authority will essentially give an undertaking to the Customs that all duties payable on goods being imported by a particular charitable organization will be paid by the Ministry of Finance.

PBO Act 2013-NEW

- **SECOND SCHEDULE (s.6)**
- **BENEFITS OF REGISTRATION**
- **1. Indirect government support in the form of—**
- (a) exemptions from—
- (i) income tax on income received from membership subscriptions and any donations or grants;
- (ii) income tax on income acquired from the active conduct of income producing activities if the income is wholly used to support the public benefit purposes for which the organization was established;
- (iii) tax on interest and dividends on investments and gains earned on assets or the sale of assets;

PBO Act 2013-NEW

- (iv) stamp duty; and
- (v) court fees.
- (b) preferential treatment under value added tax (VAT), and customs duties in relation to imported goods or services that are used to further their public benefit purposes;
- (c) incentives for donations by legal and natural persons;
- (d) employment tax preferences and;
- (e) special tax incentives for donations to form endowments, prudent investment policies, etc.

PBO Act 2013-NEW

- 2. Provision of direct government financing for public benefit organizations that partner with the government, via budget subsidies, grants for specific purposes, and contracts to perform certain work.
- 3. Preferential treatment in public procurement procedures and bidding for contracts.
- 4. Provision of information to enable public benefit organizations to contribute effectively to the policy processes.
- 5. Access to training courses that are relevant to public benefit organizations and offered by government institutions.

NPOs-POINT TO NOTE

- The Finance Act 2012 introduced limits on the validity period of income tax exemption certificates.
- A tax exemption certificate shall be renewed where an application is made to the Cabinet Secretary of Finance, through the Commissioner, at least six months before the expiry period.
- The Cabinet Secretary may also revoke an exemption on the basis of any just cause (Finance Act 2012 First Schedule, Para. 10).
- This affects trusts, NGOs, churches and other charitable organizations involved in relief, education, and religious activities.

OTHER TAX MATTERS

- PAYE-Tax payment and returns
- Reverse VAT exposures
- Withholding tax on services or interest
- NHIF and returns
- NSSF and returns
- Industrial training levies and returns
- KBS levy and returns
- Annual income tax returns requirements

EXAMPLE

- SAFE STAY International is a global NPO that operate in 42 countries in Africa. Due to the growing agitations by labor Unions in South Sudan and the need to keep employment related costs optimal, the Africa head of human resources has presented a draft contract to outsource the employee related activities in South Sudan at USD 25 million per month.
- Currently the NPO is spending USD 25.5 million on employee related activities.
- The HHR has indicated a saving of USD 6 million per year by the project excluding labor related cases.
- As a member of the board, What will be your position? Approve/Not approve

EXAMPLE-EFFECT OF TAXES

- After 10 years, the Revenue Authority of Kenya has declared the payments to be consultancy fees which should have attracted reverse VAT at 16% and withholding tax of 20% as we do not have a DDT with Southern Sudan.
- Effective cost of the changes:

Amount Paid in 10 Years	USD 3,000 Million
Reverse VAT 16%	480 Million
Withholding tax	600 Million
Total	USD 4,080Million
Initial costs	USD 3,060 Million

Additional tax related costs USD 1,020 Million. This excludes interest and penalties.

Contact for Support

Email:wkibisu@taxcredit.co.ke

+254738882299

CPA Wycliffe Kibisu Majengo
TAX DIRECTOR
TAXWORLD AFRICA LTD
BCOM (Accounting-UON) , MBA(Deakin-Australia) Chartered Global Management Accountant(CGMA),(ACMA-UK)

Questions

Thank you!

Wycliffe Kibisu

Email: wkibisu@taxcredit.co.ke

+254738882299

Website:www.taxworldafrica.co.ke