

# INCOME TAX WORKSHOP

## Taxation of Individuals

Friday, 7<sup>th</sup> April 2017

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Building a better  
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# Employee taxes

## Chargeable income

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- ▶ For the purposes of section 3(2)(a)(ii), an amount paid to-
  - ▶ a person who is, or was at the time of the employment or when the services were rendered, a resident person in respect of any employment or services rendered by him in Kenya or outside Kenya; or; **S.5 (1) (a)**
  - ▶ a non-resident person in respect of any employment with or services rendered to an employer who is resident in Kenya or the permanent establishment in Kenya of an employer who is not resident, shall be deemed to have accrued in or to have been derived from Kenya. **S.5 (1) (b)**

# Employee taxes

## Chargeable income

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- ▶ **Employment can be cash or non-cash.**
- ▶ **All cash emoluments are taxable e.g. basic salary, allowances, bonus.**
- ▶ **Non-cash benefits – some are taxable others are not.**

# Employee taxes

## Non cash benefits

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- ▶ Save as otherwise expressly provided, the value of a benefit, advantage, or facility of whatsoever nature above **Kshs.36,000** granted in respect of employment or services rendered is taxable. **s.5 (2) (b)**
- ▶ All non cash benefits are taxed at the higher of actual cost to the employer and the market value e.g. utilities, domestic help, watchmen, alarms, gifts, equity compensation, company products.
- ▶ The Commissioner may, from time to time, prescribe the value where the cost or the fair market value of a benefit cannot be determined.
  - ▶ Provision of furniture – 1% of the cost of furniture to employer.
  - ▶ Telephone (landline and mobile phone) – 30% of bills.
  - ▶ Electricity (communal or from generator) – KShs. 1,500 p.m
  - ▶ Water (communal or from borehole) – KShs. 500 p.m

# Employee taxes

## Non – cash benefits cont..

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- ▶ School fees for dependants is taxable. **s.5 (4) (d)**. However, if tax is borne by the employer – not taxable.
  - ▶ What about **exempt employers**?
- ▶ Value of meals served to employees in a canteen or cafeteria operated or established by the employer or provided by a third party who is a registered taxpayer (whether meals are in the employer's or third party premises) where the value of the meals does not exceed KShs, 48,000 p.a per employee – not taxable **s.5 (4) (f)**.

# Employee taxes

## Motor vehicle benefit

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- ▶ Provision of a 'company' car is taxable at the higher of:-
  - ▶ 2% p.m. of the initial cost of the car (W.e.f 1.1.1998) or
  - ▶ Commissioner's prescribed rates. **S. 5 (2B)**
- ▶ However, w.e.f.1.1.2008, for employees who have restricted use of motor vehicles, the Commissioner may determine a lower rate of the benefit depending on the usage of the vehicle upon proof. **S.5 (2B)**. See guidelines on restricted use of motor vehicle([Appendix 1](#))
- ▶ W.e.f. 16.06.2006, where the car is hired or leased, the taxable benefit is the lease or hiring cost. **S.5 (2B) (a) (ii)**

# Employee taxes

## Motor vehicle benefit cont'd

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- ▶ KRA has been of the view that employees having access to pool vehicles shall be deemed to have received transport benefit chargeable to tax provided the aggregate value of the benefits exceeds KShs. 3,000 p.m.
  - ▶ Is that right?
- ▶ Such benefit shall be calculated based on the cost of maintenance of such motor vehicles.

# Employee taxes

## Housing benefit – S. 5 (3)

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- ▶ If the employer pays rent under an agreement **at arm's length**, value of the benefit is the higher of:-
  - ▶ **15%** of gross emoluments (excluding the value of the house), or
  - ▶ actual cost to the employer.
- ▶ However, if the employer pays rent under an agreement **not at arm's length**, value of the benefit is the higher of the fair market value of the premises for that year or rent paid by employer.
- ▶ Where premises are **owned by the employer**, the value of the benefit is the fair market rental value.
- ▶ Housing provided to agricultural employees - **10%** of gains from employment.

# Employee taxes

## Housing benefit {S. 5 (3)}

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### ► Points to note:-

- If the premises are occupied for part of the year only, the value is reduced relative to the period of occupation.
- If the employee pays rent to his employer for the premises the benefit is reduced by the amount of rent paid
- Where only part of the premises is provided, the Commissioner may reduce the value to an amount he considers just and reasonable.

# Employee taxes

## Medical benefit

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- ▶ Where an employer provides free medical services to his employees, the value of such medical services is a non-taxable benefit on full time employees and whole time service directors.
- ▶ This was expanded to include the following with an allowed maximum limit of KShs. 1 million:
  - ▶ Directors other than whole time
  - ▶ Partners in a partnership
  - ▶ Sole proprietors
- ▶ W.e.f. 1.1.2008, medical insurance provided by an insurance provider approved by the Commissioner of Insurance and paid by the employer on behalf of a fulltime employee is not taxable. **S.5 (4) (b)**
- ▶ W.e.f. 9.6.2011: Medical Insurance/ Medical expense for employee dependants, are not taxable. **S.5 (4) (b)**

# Employee taxes

## Employees' Group Life Cover

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- ▶ If an employer pays a premium for an insurance on the life of his employee and for the benefit of the employee or his dependants it is considered a taxable benefit from employment unless;
  - ▶ The amount is paid to a registered or unregistered pension scheme, pension fund, provident fund or individual retirement fund;
  - ▶ The cover confers a benefit to the employer.

# Employee taxes

## Per diem

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- ▶ Given for upkeep of staff when on official travel away from their normal work station.
- ▶ Where the Commissioner is satisfied that the costs are a reimbursement of amounts utilized wholly and exclusively in production of income for the employer.
- ▶ W.e.f. 16 June 2006 the first KShs 2,000 per day is considered a reimbursement and is not taxable. **S.5 (2) (a) (ii)**
- ▶ Amounts exceeding KShs. 2,000 should ideally be supported with vouchers from an arms-length source.
- ▶ Where these are not available, supporting workings acknowledged by the third party supplier should be attached.

# Employee taxes

## Tax free remuneration

Where employer bears tax on behalf of employees, the tax paid by the employer is considered a benefit chargeable to tax. Gross up factors to be applied are as follows:-

<b>Taxable Income Range (a)</b>	<b>Tax on Taxable Income (b)</b>	<b>Marginal Tax Rate (c)</b>	<b><u>Factor Without Housing</u> (d)</b>	<b><u>Factor With Housing</u> (e)</b>
0 - 11,180	1,118	10%	1.111	1.130
11,181 - 21,715	2,698	15%	1.176	1.208
21,716 - 32,249	4,805	20%	1.250	1.299
32,250 - 42,784	7,438	25%	1.333	1.404
Over 42,785		30%	1.429	1.527

# Common PAYE Issues

## Interest free or low interest loan

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- ▶ Relates to loans which interest charged is below the commissioner's prescribed rate, which are published quarterly (half yearly) for low interest on loans taken before 11.6.1998.
- ▶ For old loans (taken before 11.6.1998), Low Interest Benefit (LIB) applies – the interest is taxed on employee at graduated scale rates. **s.12B**
- ▶ For loans advanced after 11.6.1998: Fringe Benefit Tax (FBT) is 30% of the difference between the commissioner's interest rate and that actually charged – payable by employer. **s.12B**

# Taxation of expatriates

## Focus areas:-

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1. Pension – employer contribution to offshore schemes, where is the cost borne?
2. Medical Insurance – is it approved by the Commissioner of Insurance?
3. Net incomes – Are they grossed up and which factor is applied?
4. Group life cover – who does it confer a benefit to?
5. Split payroll – is full income being taxed in Kenya?
6. Equity income – which is the tax point and what portion is taxable in Kenya when assignment end date
7. Housing – is it a housing benefit or allowance and how is the taxable benefit determined?

# Taxation of terminal dues

## Lump sum payment

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- ▶ An amount received in respect of employment in a year of income different from the year of accrual, such income is deemed to be income of the year of accrual.
- ▶ If the year of accrual is earlier than 4 years prior to the year of receipt, the income is spread back over 5 years prior to the year in which the income is received or employment ceased.
- ▶ The service gratuity amount is to be spread backwards and taxed together with income earned in the relevant years.
- ▶ Notice pay is assessable in the period immediately after date of leaving employment.
- ▶ Pay in lieu of leave should be taxed in the year to which the leave days relate.

# Taxation of terminal dues

## Compensation for the termination of a contract of employment

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- ▶ Where there is a specified term contract, the amount of the compensation will be spread over the unexpired period at equal amounts and taxed accordingly.
- ▶ Where the contract is for unspecified term and provides for terminal payment, then the compensation will be spread forward and assessed at the rate of the employee's remuneration p.a. immediately before termination.
- ▶ Where the contract is for unspecified term and does not provide for terminal payment, the compensation is to be spread forward in equal amounts for three years following the termination.

# Tax planning insights

## Home Ownership Savings Plan (HOSP)

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- ▶ An employee is eligible to a deduction of a maximum of **KShs. 48,000** p.a. up to a maximum of 10 years in respect of funds deposited in approved institutions, provided;
  - ▶ The employer has evidence to confirm that the approved Institution is registered by the Commissioner.
  - ▶ The employer will be the one to deduct and remit the amount to the Institution on behalf of the employee.
  - ▶ Employer will attach to form P9A (HOSP) a declaration duly signed by the eligible employee.
  - ▶ “Approved Institution” – means a licensed financial institution or a licensed Insurance Company.
- ▶ W.e.f. 1.1.2007, interest earned on deposits to HOSP up to a maximum of **KShs. 3,000,000** is tax exempt.

# Tax planning insights

## Mortgage interest deduction

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- ▶ Available to owners of residential houses who occupy them; no claim for more than **1 residence**'
- ▶ Applies to purchase or improvement of premises.
- ▶ Deduction of up to **KShs. 300,000** p.a. (**effective 01 Jan 2017**)
- ▶ Deduction given on interest from banks, insurance companies, building societies and National Housing Corporation only. **S.15(3)(b)**
- ▶ **Saccos** have been left out among the qualifying financial institutions.

# Tax planning Insights

## Contributions to pension scheme

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- ▶ Contributions to registered pension, provident and individual retirement schemes – Up to a maximum of KShs. 240,000 p.a. is tax allowable. **S.22A**
- ▶ However, contributions by employers who are not taxable to unregistered schemes or excess contributions to registered schemes are a taxable benefit on employee. **S.5 (4) (c)**
- ▶ Allowable amount is determined per individual employee & summed. Hence for each member, amount should be the lesser of ;
  - ▶ 30% of pensionable pay;
  - ▶ KShs.240,000 or proportion for the year; or
  - ▶ Actual contributions.

# Tax planning insights

## Reliefs

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### Insurance relief

- ▶ 15% of premiums paid up to a maximum of KShs 60,000 p.a. (W.e.f. 1.1.2007).
- ▶ Shall apply only to life or education policies whose term commences on or after the 1.1.2003. Education policy: maturity period of at least 10 years.
- ▶ Health insurance w.e.f. 1.1.07. **S.31**

### Personal relief

- ▶ KShs. 1,280 per month with effect from 01 January 2017.
  - ▶ KShs 1,408 (wef 1 Jan 2018)
- ▶ Individuals serving several employers qualify for personal relief from only one employer.

# Tax planning insights

## Disabled persons

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- ▶ **L/N 36** – Exemption for persons with disabilities registered with the National Council for Persons with disabilities
  - ▶ First KShs. 150,000 per month exempted.
  - ▶ Non reimbursable home care and hospital costs are allowed.
  - ▶ Cost of devices allowable. Maximum costs of KShs. 50,000 allowable per month.

See Legal Notice 36 (2010) on taxation of disabled persons (**Appendix 3**)

# Tax planning insights

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**Group life insurance covers** - Policy document should confer a benefit to the employer

**Medical Insurance** - Provided through approved Insurer

**Meals** - Restrict cost to Kshs. 48,000 p.a. and ensure service provider is a registered tax payer

**Housing** - Employee should sign the lease agreement

**Passages** – provide actual air ticket, or employee should pay and claim a reimbursement with supporting documents

# Employee taxes and statutory deductions

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## Employer's responsibilities

- ▶ Ensure employee has a PIN, deduct, remit PAYE and fringe benefit tax to the KRA and file PAYE monthly return by 9<sup>th</sup> of month following the month of deduction. Furnish employee with tax deduction card (P9) after the end of the year.
- ▶ Ensure employees are registered with NSSF and NHIF and remit contributions by the due dates.

## Employee's responsibilities

- ▶ Register with KRA, NSSF and NHIF.
- ▶ Complete own taxes and pay the KRA especially on change of jobs or where they have other sources of income. Complete and file tax return by due date.

# Penalties for Non-compliance

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- ▶ Failure to deduct and account for tax from employment emoluments.
  - ▶ 25% non compliance penalty.
  - ▶ 1% interest per month.
- ▶ Failure to apply for registration or deregistration - Kshs.100,000 for every month or part of a month subject to a maximum of KShs.1,000,000
- ▶ Failure to file an individual self assessment return (SAR) by 30 June of the subsequent year - penalty of 5% of the tax balance subject to a minimum of KShs. 20,000 (iTax is still issuing penalty orders of KShs.1,000).
- ▶ Failure to pay a tax balance on an individual SAR by 30 April – penalty of 20% and interest at 1% per month or part thereof.

# Employee taxes

## Current PAYE bands (Para 1, Head B of 3<sup>rd</sup> Schedule)

Income per month (KShs.)			%	Cumulative
0	-	11,180	10	1,118
11,181	-	21,715	15	2,698
21,716	-	32,249	20	4,805
32,250	-	42,783	25	7,438
Over		42,783	30	

Income per annum (KShs.)			%	Cumulative
0	-	134,164	10	13,416
134,165	-	260,567	15	32,377
260,568	-	386,970	20	57,657
386,971	-	513,373	25	89,258
Over		513,373	30	

# Recent changes – Finance Act 2016

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- ▶ Exemption from tax of income from employment paid in the form of bonuses, overtime and retirement benefits to employees employment income before these benefits is taxed at the lowest tax band. **Effective 01 July 2016**
- ▶ Increase in owner occupier mortgage deduction from KShs. 150,000 p.a to KShs. 300,000 p.a. **Effective 01 January 2017**
- ▶ As per the regulations, an employer who engage at least ten university graduates holding bachelor's degree for a period of at least six to twelve months in any year of income would be entitled to a rebate equal to 50% of the amount of the salaries and wages paid to the apprentices, in addition to the normal salaries and wages deductible for tax. The incentive is allowable within a period of three years.

# Recent changes – Finance Bill 2017

- Increase the PAYE tax bands by 10%. **Effective 01 January 2018**

From (KShs)	To (KShs)	Tax Rate (%)
On the first 134,164	On the first 147,580	10
On the next 126,403	On the next 139,043	15
On the next 126,403	On the next 139,043	20
On the next 126,403	On the next 139,043	25
All income over 513,373	All income over 564,709	30

- Increase in personal relief from KShs. 15,360 p.a to KShs. 16,896 p.a. **Effective 01 January 2018**

# Recent changes – Finance Bill 2017

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## Tax Amnesty for investors in diaspora

- ▶ Period to file returns for the tax amnesty extended from 31 December 2017 to 30 June 2018
- ▶ The investors should also repatriate the funds declared under the amnesty to Kenya
- ▶ From an individual perspective, this would apply to individual tax resident who were subject to tax on worldwide employment income but failed to declare and pay tax on this income.

# Questions/Comments

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*THANK YOU!*