TAXATION OF PBOs

Employment Taxes - PAYE

Presentation by:

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26th July 2018

Content

- Residency status
- Employee & employer responsibility
- Chargeable income
- Interest free and low interest loans
- Allowable deductions and Reliefs
- Current changes (draft Income Tax Bill)
- General penalty
- Statutory deductions

Residency Status

Residency rules

Residency when applied to an individual means:

- that one has a permanent home in Kenya and was present in Kenya for any period in a particular year of income under consideration; or
- that one has no permanent home in Kenya but was present in Kenya:
  - For a period amounting in aggregate to 183 days or more in that year of income; or,
  - Average period (s) exceeding 122 days in a year of income and in each of the 2 preceding years

Employer & Employee responsibility

Employer responsibility

- Ensure all employees have a KRA PIN;
- Compute, deduct and remit PAYE and Fringe benefit tax to KRA by the 9^{th} of the month following the month of the deduction;
- Furnish employees with tax deduction cards (P9) at the end of the year; and,
- Ensure that all employees are registered with NHIF & NSSF;
- Deduct and remit NHIF & NSSF by due dates (9^{th} and 15^{th} of the month following the month of the deduction)

Employee responsibility

- Register with KRA, NHIF and NSSF
- File own returns and pay KRA any tax due especially in the case where they have other revenue sources

Chargeable Income
Section 3(2)(a)(ii) & Sec 5(2)

Chargeable income

Section 3(2)(a)(ii) **of the Income Tax Act (ITA) provides that:**

- …income in respect of gains or profits from employment or services rendered should be subjected to tax

For the purposes of the above section, 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 *Sec 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 *Sec 5(1)(b)*

Chargeable income cont'd

Taxable employment income include:

- wages, salary, leave pay, sick pay, payment in lieu of leave, fees, commission, bonus, gratuity, or subsistence, traveling, entertainment or other allowance received in respect of employment or services rendered *Sec 5 (2) (a)*

- any amount so received in respect of employment or services rendered in a year of income other than the year of income in which it is received *Sec 5 (2) (a)*

Chargeable income cont'd

In general

- All types of remuneration and benefits received by an employee for services rendered constitute taxable income *Sec 5 (2)*

- Types of emoluments subject to tax are:
  - Cash emoluments: and
  - Non – cash benefits

Chargeable income cont'd

Examples of cash emoluments

- salary, leave pay, sick pay, commission, bonus, service charge, other allowance etc.

Examples of non - cash benefits

- Meals benefit
- Housing benefit
- Motor vehicle benefit
- Telephone benefit
- Furniture
- School fees etc.

Individual taxation - Per diems

Sec 5 (2)(a)(iii)

- Per diem is normally given to employees in respect of time spent outside his/her place of work while on official duties

- The first KES 2,000 is deemed to be a reimbursement of the amount so expended and shall be excluded in the calculations of his/her gains from employment

- However, per diem amounts exceeding KES 2,000 should be supported preferably with receipts/vouchers from an arms-length source

- No special per diem rates are provided for overseas travels

Individual taxation – Tax free remuneration

- Where an employer wishes to pay employees net of tax, the tax paid by the employer on behalf of employees is in itself a benefit chargeable to tax
- The Commissioner has given a formula on how to compute the tax-on-tax effect as below
- The gross up factor applied where a housing benefit is provided is higher than where a housing benefit is not provided

Monthly taxable pay (KES)	Rate %	Multiplier factor without housing benefit	Multiplier factor with housing benefit
on the first 12,298	10%	1.111	1.13
On the next 11,587	15%	1.176	1.208
On the next 11,587	20%	1.25	1.299
On the next 11,587	25%	1.333	1.404
Over 47,059	30%	1.429	1.527

Individual taxation – Tax free remuneration example

	Without Housing benefit	With Housing benefit
	KES	KES
Monthly cash income	26,000	50,000
Less: Pension contribution	(800)	(950)
Monthly cash income after deductions	25,200	49,050
Monthly benefits	15,000	20,000
Total income including benefits	40,200	69,050
Housing benefit	-	25,000
Taxable income	40,200	94,050
Gross tax	6,464	22,279
Less: Relief	(1,408)	(1,408)
Tax net of relief	5,056	20,871
Factor	1.333	1.53
Montly tax payable	6,740	31,870
Chargeable income/Basic pay	32,740	81,870

Normally the employer pays an employee a gross salary out of which tax is deducted. When an employer pays an employee net of tax, then tax has to be paid by the employer on top of the net salary paid to employee

Individual taxation – Lump sum payment (Gratuity, service pay)

- 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 to

Individual taxation-compensation for termination of contract

Sec 5 (2)(c)

- Compensation received is taxable, whether or not provision was made in the contract for the payment of that compensation
- Where there is a specified term contract, the amount of compensation will be spread over the unexpired period at equal amounts and taxed accordingly
- Where the contract is unspecified term and provides for terminal payment, then the compensation will be spread forward and assessed at the rate of the employees remuneration p.a. immediately before termination
- Example: assuming A is terminated in 2018 while earning KES 500,000 p.a. and the contract provides for compensation of KES 1,200,000, then the compensation will be spread forward in multiples of KES 500k i.e. 2019 – KES 500,000 2020 – KES 500,000 2021 – 200,000

Individual taxation-compensation for termination of contract

Sec 5 (2)(c)

- 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

Taxation of Non-Cash Benefits

Sec 5 (2)(b)

- The value of all benefits, advantages or facilities of whatsoever nature whose **aggregate value** is higher than **KES 36,000** per annum is taxable on the employee. However, where the value is lower, it is not taxable on the employee

- All non cash benefits are taxed at the **higher** of **actual cost** to the employer and the **fair market value**

- The Commissioner may, from time to time, prescribe the value where the cost or the fair market value of a benefit cannot be determined

Taxation of Non-Cash Benefits Meals

Sec 5 (4)(f)

- 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 **KES. 48,000** per year per employee should not be subject to tax

Taxation of Non-Cash Benefits
Housing benefit

Sec 5 (3)

- Free housing is taxed at the higher of:
  - actual cost to the employer, or
  - 15% of gross emoluments, excluding value of the house, (15% of total income for a director), or
  - the market rental value
- If the employer pays rent under an agreement at arm's length, value of the benefit will be higher of:
  - 15% of gross emoluments (excluding 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

Taxation of Non-Cash Benefits Housing benefit cont'd

Sec 5 (3)(d)(ii)

Take away

- 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
- Where only part of the premises is provided, the Commissioner may reduce the value to an amount he considers just and reasonable
- Where the gains from employment exceed KES 600k in a year, the value of the premises determined shall be subject to the limit of:
    - The higher of the rent paid by the employer or the fair market value (agreement with a 3rd party not at arms length); or
    - The fair market rental value of the premises owned by the employer

Taxation of Non-Cash Benefits Housing benefit cont'd

Sample workings

- A earns a basic salary of KES 30,000 per month. A has other benefits amounting to KES 15,000 per month. A is housed and the employer pays to the landlord KES 20,000 per month under an agreement made at arms length with the 3rd party. What is the total taxable salary of A?

- Basic salary.. KES 30,000
- Add: benefits......................................KES 15,000
- Total...KES 45,000
- Housing benefit...................................KES 20,000

(higher of 15%*45,000 = 6,750) or KES 20,000

- Total taxable salary.............................KES 65,000

Taxation of Non-Cash Benefits Motor vehicle benefit

Sec 5 (2B)

- Provision of a company car is taxable at the higher of:
  - 2% p.m. of the initial cost of the car or
  - Commissioner's prescribed rates (cc rates)
- W.E.F 2008, where employees have restricted use of a car, the Commissioner may if satisfied, determine a lower rate of the benefit depending on the usage of the vehicle
- Where vehicle is hired or leased, the taxable benefit is the cost of leasing or hiring
- Pool car - benefit is calculated based on the cost of maintenance of such motor vehicles. Considered in the KES 3,000 threshold.

Taxation of Non-Cash Benefits Motor vehicle benefit cont'd

Motor vehicle benefit taxation guidelines – restricted use

- The employer shall maintain a documented policy entailing:

  - The cadre of employees entitled to be provided with vehicles
  - The permitted usage to which the vehicle may be put
  - The nature of expenses to be met by the employees or the employer in respect of the vehicles
  - Evidence of how usage is monitored and controlled
  - Whether the vehicle is self or chauffer driven

- In such a case and based on the commissioners satisfaction, a lower rate of benefit shall be determined depending on the usage of the vehicle

Taxation of Non-Cash Benefits Medical benefit

Sec 5 (4)(b)

- 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.
- 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
- W.E.F June 2011, Medical insurance/medical expense for employee dependants, shall not be subject to tax
- However, medical insurance is taxable if it is provided by an insurance company that is not approved by the Commissioner of Insurance
- In this case the premiums paid are taxed

Taxation of Non-Cash Benefits Passages

Sec 5 (4)(a)

- Gains or profit from employment does not include the expenditure on passages between Kenya and any place outside Kenya borne by the employer where:
  - The employee is recruited outside Kenya and who is in Kenya solely for the purpose of serving his employer; and,
  - He is not a citizen

- However, where the employee receives cash some periodically which he is free to spend as he chooses and does not have to account to the employer, the amount received is a taxable cash allowance

Taxation of Non-Cash Benefits School fees benefit

Sec 5 (4)(d)

- Education fees paid by the employer for employee's dependants' are taxable on the employees

- However, where the tax is borne by the employer, through add back in the tax computation, the benefit will not be taxable on the employee

- What is the case for PBO's?

Taxation of Non-Cash Benefits commissioner's prescribed rates

Benefit	Prescribed rate per month (KES)
Telephone (Landline or mobile)	30% of monthly bills
Electricity	1,500
Furniture	Higher of amount paid per month if hired or 1% of actual cost

Interest free or low interest loan

Sec 12B

- This relates to loans given by the employer whose interest rate is below the commissioner's prescribed rate published on quarterly basis for low interest loans
- Fringe benefit tax is applicable at the rate of 30% on the difference between the commissioner's interest rate and the interest actually charged
- FBT is payable by the employer

Allowable deductions and reliefs

Contribution to a pension scheme

Sec 22A

- Contributions to registered pension, provident and individual retirement schemes – Up to a maximum of KES 240,000 p.a. (KES 20,000 p.m.) is tax allowable.
- However, contributions by employers to unregistered schemes or excess contributions to registered schemes are a taxable benefit on employee.
- Allowable amount is determined per individual employee & summed. Hence for each member, amount should be the lesser of ;
  - 30% of pensionable pay;
  - KES 240,000 or proportion for the year; or
  - Actual contributions.

Contribution to a pension scheme - Example

Staff	E'er Cont	E'er NSSF	E'ee Cont	E'ee NSSF	Total	Tax E'ee	Tax E'er
U	8,000	200	8,000	200	16,400	Nil	Nil
V	9,800	200	9,800	200	20,000	Nil	Nil
W	19,800	200	19,800	200	40,000	Nil	20,000
X	25,000	200	25,000	200	50,400	5,200	25,200
Y	30,000	200	30,000	200	60,400	10,200	30,200
Total	**92,600**	**1,000**	**92,600**	**1,000**	**187,200**	**15,400**	**75,400**

Where:

- E’er Cont.......Employer’s pension contribution
- E’er NSSF......Employer’s NSSF contribution
- E’ee Cont.......Employee’s pension contribution
- E’ee NSSF......Employee’s NSSF contribution
- Tax E’ee..........Employee taxable pension contribution
- Tax E’er..........Employer taxable pension contribution

Home Ownership Savings Plan (HOSP)

Sec 22C

- "Registered home ownership savings plan" means a savings plan established by an approved institution and registered with the Commissioner for receiving and holding funds in trust for depositors for the purpose of enabling individual depositors to purchase a permanent house
- "Approved institution" means a bank or financial institution registered under the Banking Act, an insurance company licensed under the Insurance Act or a building society registered under the Building Societies Act.
- "Permanent house" means a residential house that a financial institution would accept as collateral for a mortgage, and includes any part or portion of a building, used or constructed, adapted or designed to be used for human habitation as a separate tenancy for one family only, whether detached, semi-detached or separated by party walls or floors from adjoining buildings or part or portion of such building

Home Ownership Savings Plan (HOSP)

Sec 22C

- An employee is eligible to a deduction of a maximum of KES 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
- Interest earned on deposits to a registered HOSP up to a max of KES 3m is exempt from tax

Persons with disability

- Sec 35 of the Persons with disabilities Act 2003, was amended vide Finance Act 2009

- L/N 36 – Exemption for persons with disabilities registered with the National Council for Persons with disabilities

  - First KES 150,000 per month exempted
  - Non reimbursable home care and hospital costs are allowed
  - Cost of devices allowable. Maximum costs of KES 50,000 allowable per month

- Must have an exemption certificate from KRA which is renewable after every 3 years

Mortgage interest relief

- 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 KES 300,000 p.a.
- Deduction given on interest from banks, insurance companies, building societies, National Housing Corporation and Cooperative Society Sec 15(3) (b)

Insurance relief

- Relief given of 15% of premiums paid up to a maximum of KES 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. Sec 31

Personal relief

- Rates applicable are as follows:
  - Relief prior to 01 January 2017 – KES 1,162 p.m.
  - Relief effective 01 January 2017 – KES 1,280 p.m.
  - Relief effective 01 January 2018 – KES 1,408 p.m.

- Individuals serving several employers qualify for personal relief from only one employer

Low income earners

- Employee whose total gross earnings do not exceed the amounts below are not taxable
  - KES 11,135 p.m. prior to 2017
  - KES 12,260 p.m. in 2017
  - KES 13,484 p.m. from January 2018

- Employees in the lowest tax band are exempt from tax on employment income paid in the form of bonuses, overtime and retirement benefits effective 01 July 2016

How do you handle casual workers from a tax perspective?

PAYE tax bands 2018

Effective 01 January, 2018

Monthly taxable pay (KES)	Rates of tax %	Cumulative (KES)
On the first 12,298	10	1,230
On the next 11,587	15	1,738
On the next 11,587	20	2,317
On the next 11,587	25	2,897
Excess over 47,059	30	
Personal relief	1,408	
Insurance relief	5,000	

Annual taxable pay (KES)	Rates of tax %	Cumulative (KES)
On the first 147,580	10	14,758
On the next 139,043	15	20,856
On the next 139,043	20	27,809
On the next 139,043	25	34,761
Excess over 564,710	30	
Personal relief	16,896	
Insurance relief	60,000	

Current changes (Draft Income Tax Bill & Finance Bill, 2018)

Proposed changes by the draft Income Tax Bill

Increase in individual tax bands effective January 2018

Monthly taxable pay (KES)	Rates of tax %	Cumulative (KES)
On the first 12,298	10	1,230
On the next 11,587	15	1,738
On the next 11,587	20	2,317
On the next 11,587	25	2,897
Excess over 47,059	30	
Personal relief	1,408	

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On the next 139,043	20	27,809
On the next 139,043	25	34,761
Excess over 564,710	30	
Personal relief	16,896	

Proposed changes by the draft Income Tax Bill

- Per diems – The ITB seeks to align per diem rate to the public service prescribed rates
- ESOP – The ITB clarifies that taxable benefits for Employee Share Options will accrue at the date of exercising the option, currently is at the end of vesting period
- Taxation of non-resident individuals pension or retirement annuities increased from 5% to 10%
- Termination compensation to be spread evenly over the unexpired period of the contract whether or not this is provided for in the contract
- The ITB proposes to tax all non-cash benefits without any threshold by removing the provision under Sec 5 (2)(b) which provides for a threshold of KES 3,000 p.m.

Proposed changes by the draft Income Tax Bill

- The ITB proposes to cap exempt bonuses and overtime to individuals earnings before the incorporation of bonuses and overtime

- The ITB proposes to exempt medical benefits under cover by non-resident insurance schemes not registered by Insurance Regulatory Authority (IRA)

- HOSP – the ITB proposes to remove this tax incentive

General Penalty

General penalty

- Failure to deduct and account for tax from employment emoluments.
  - 25% non compliance penalty Sec 83 of the Tax Procedures Act (TPA)
  - 2% interest per month effective 1 July, 2018
  - Failure to have a PIN KES 100,000
- 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 KES 20,000
- Failure to pay a tax balance on an individual SAR by 30 April – penalty of 20% and interest at 2% per month or part thereof
- Knowingly making false statement or misleading information leading to a lower tax liability attracts a tax shortfall penalty of 75% of the tax shortfall

Statutory Deductions

Statutory deductions
National Social Security Fund (NSSF)

- Every employer is required to register with NSSF. Both an employee and employer are required to contribute 5% of the basic salary to the Fund up to a maximum of KES 200 per month. Special contributions are also payable in respect of casual employees, who are not registered. Such contributions should be based on 5% of the wages *Sec 5 & 10 NSSF Act*

- On 24 December 2013, the Government of Kenya enacted the NSSF Act No. 45 to replace the NSSF Act (Cap. 258). Implementation of the new Act is however pending a court decision

- Payable by 15th of the month following the month of deduction

- General Penalty of 5% per month or part thereof *Sec 14 NSSF Act*

Statutory deductions National Health Insurance Fund (NHIF)

- Employers and employees are required to be registered with NHIF. However, it is only the employee who contributes to the Fund
- With effect from 1st April 2015 monthly contributions are on a graduated scale rate depending on the monthly income and ranges from KES 150 to KES 1,700
- Expatriates are also required to contribute.
- NHIF is payable by the 9th of every month following the month of deduction
- Late payment of any contribution attracts a penalty equal to two times the amount of the unpaid contribution

Statutory deductions
National Health Insurance Fund (NHIF)

NHIF rates

Gross Income (KES)	Proposed Premiums (KES)
0 – 5,999	150
6,000 – 7,999	300
8,000 – 11,799	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 over	1,700
*Self-employed (Special)	500

Interactive Session

TAXATION OF PBOs

Corporate Income Tax Exemption

Presentation by:

CPA Willy Siundu
26th July 2018

Content

- Provisions of the PBO Act
- Tax exemption of PBO’s as per the Income Tax Act
- Tax risks for PBOs
- Tax due dates & Penalty
- Managing your tax risks

Provisions of the PBO Act, 2013

Definition of terms

- **Public benefit activity** - means an activity that supports or promotes public benefit by enhancing or promoting the economic, environmental, social or cultural development or protecting the environment or lobbying or advocating on issues of general public interest or the interest or well-being of the general public or a category of individuals or organizations

- **Public Benefit Organization** – means a voluntary membership or non-membership grouping of individuals or organizations, which is autonomous, non-partisan, non-profit making and which is:
  - organized and operated locally, nationally or internationally
  - engages in public benefit activities in any of the areas set out in the Sixth Schedule; and
  - is registered as such by the Authority *Sec 5 PBO Act*

Definition of terms cont’d

- **A Public Benefit Organization does not include:**
  - a religious organization which is primarily devoted to religious teaching or worship
  - a society within the meaning of the Societies Act
  - a public body established by or under any written law
  - a community based organization whose objective include the direct benefit of its members

Financial management of PBOs

Sec 29, 30 &31

- PBOs should implement internal accounting procedures to ensure transparency and proper use of its financial and other resources
- PBOs should utilize financial and other resources for the attainment of its purpose
- PBOs should keep proper books of account in relation to its operations
- PBOs should prepare annual statement of accounts which conform to the generally accepted accounting practice applicable
- PBOs should submit annual reports to PBOA within 6 months after the end of the financial year
- This should include a report dealing generally with the programme of activities of the PBO during that financial year

Provisions of the PBO Act – Tax incentives

Second schedule of PBO Act

- Tax exemptions and preferential tax treatments

Corporate Income Tax exemption on member subscriptions, donations, grants income acquired to be wholly used in support of the PBO purposes

Preferential treatment under VAT & Custom duties in relation to goods imported to be used in furtherance of the PBO purposes

Tax Exemptions

Preferential employment tax (PAYE) treatment

WHT exemption on interest & dividends on investments and gains earned on assets or sale of assets

Provisions of the Income Tax Act

Tax Exemptions - PBOs

First Schedule of the Income Tax Act (ITA) - Paragraph 10

- Exempts from tax the income of an institution of a public character established solely for the purpose of the relief of poverty or distress of the public, or for the advancement of religion or education

1. Established in Kenya
2. Whose regional H/Q is situated in Kenya
3. Satisfy the Commissioner that it is for benefit of Kenyan residents

Tax Exemptions - PBOs

Conditions to be fulfilled for exemptions during operations

Paragraph 10 (b)…any such income which consists of gains or profits from a business shall not be exempt from tax unless those gains or profits are applied solely to those 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 received from the leasing or letting of land and chattels leased or let therewith.

Exemption application process

1

Application to the Commissioner

- The constitution of the PBO
- Copy of PIN certificate
- Registration certificate
- Income tax returns & financial statements
- List of projects undertaken for the past 3 years
- List of assets including registered names and bank statements for the last 3 years
- Introduction letter from the County Government – to inform KRA of the existence and activities of the PBO
- Any other documents

Exemption application process

2

Processing of the application by the Commissioner

- The Commissioner acknowledges the receipt of the application
- The Commissioner may institute compliance check for the prior period
- Request for additional information if need be
- Confirmation of the compliance with the requirements for exemption is done

Exemption application process

3

Issuance of the Exemption certificate

- The certificate is issued within 60 days if all documents are in order
- The validity of the exemption certificate is 5 years
- However, the Commissioner may revoke it before the lapse of the 5 years for any just cause
- On expiration of the 5 years, the PBO should make a fresh application

Other Exemptions

Sec 13

- The income specified in Part 1 of the First Schedule which accrued in or was derived from Kenya shall be exempt from tax to the extent so specified
- The Minister may, by notice in the Gazette, provide:
  - that income or a class of income which accrued in or was derived from Kenya shall be exempt from tax to the extent specified in the notice;
  - that an exemption above shall cease to have effect either generally or to the extent specified in the notice

Tax Risks for PBOs

Tax risks for PBOs

Exemptions

- Failure to understand the 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 tax exemption

Tax Compliance issues

- Most PBOs fail to submit tax returns where they are required to e.g. Corporate Income Tax return – NIL return and returns for other tax obligations

Agency taxes – WHT, PAYE

- Most PBOs assume that they are exempted from the agency taxes on receipt of an exemption certificate. This has led to PBOs being penalized for non-compliance

Tax due date & Penalty

Tax due date & Penalty

Return filing due date

- Tax return filing due date is on the last day of the 6th month following year end

Late filing penalty

- KES 20,000 (Sec 83 of the TPA)

Managing your taxes

Managing your taxes

Know your taxes

- As a PBO, ensure you are aware of your tax obligations. You can seek specific tax advice for your situation

Deadlines

- File all tax returns by due dates to avoid unnecessary penalties and interest

Carry out frequent tax reviews/health checks

- This helps the PBO identify any tax risks that it may not be aware of

Interactive Session

TAXATION OF PBOs

Case Study: PBO vs KRA Case Laws

Presentation by:

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27th July 2018

Content

- Sample Case Laws between the KRA & the PBOs

Diakonie Emergency Aid vs KRA Appeal No.46 of 2015

Case background

- The Appellant (DEA) is an NGO registered in Kenya and was assessed by KRA for the period 2006-2010
- KRA demanded PAYE in arrears from employees of DEA Primary Health Care (DEA PHC) South Sudan & Daryeel Bulsho Guud (DBG) in Somalia
- This was based on the fact that DEA was considered a permanent establishment for DEA PHC & DBG due to its role in the disbursement of funds to employees in the respective countries
- DEA however argued that it acted as a receiving office for funds of the respective countries due to the volatile political & economic environment

Diakonie Emergency Aid vs KRA Appeal No.46 of 2015

ICPAK
Uphold Public Interest

KRA position

- KRA contended that DEA is a PE and therefore the funds disbursed to employees for the respective DEA PHC &DBG ought to have been subjected to PAYE
- DEA disputed KRA findings at the Tribunal

Tribunal ruling

- DEA did not create a PE by virtue of receiving and disbursing funds to DEA PHC & DBG as the control and approval was made in Germany
- DEA PHS & DBG employees had signed agreements for co-operation with Germany and therefore income of those employees cannot be deemed to have been derived from Kenya as per the provisions of Sec 5 (1) of the Income Tax Act

Diakonie Emergency Aid vs KRA Appeal No.46 of 2015

Sec 5 (1)

- Provides that " *amount paid to a non- resident 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 so resident, shall be deemed to have accrued in or to have been derived from Kenya*"
- The Tribunal ruled in favour of the Appellant (DEA)

HelpAge International vs KRA Petition No.372 of 2014

Key dispute

- Whether KRA was justified to demand PAYE on non-cash benefits enjoyed by expatriate employees while working in Kenya

Case background

- The petitioner (HelpAge International) engaged services of 3 expatriates employees who were paid from UK, however, while in Kenya the expatriate employees enjoyed some non-cash benefits which were footed by the petitioner
- KRA assessed the petitioner and demanded PAYE on the non-cash benefits
- The petitioner paid a portion of the amount demanded then later disputed the assessment on grounds that KRA was not justified to demand the PAYE

HelpAge International vs KRA Petition No.372 of 2014

- According to KRA and as per Sec 5 (2) of the Income Tax Act, the expatriate employees were obligated to pay taxes on those benefits whether or not they were residents in Kenya as long as the income was generated for services rendered or benefit received while in Kenya

High Court ruling

- The High Court held that despite the Petitioners commendable work of caring for the elderly, it had an obligation to pay relevant taxes

KWS vs KRA Appeal No.116 of 2015

Tax exemption

- One of the ruling was in relation to KWS tax exemption status and whether the tax exemption amounted to an automatic reprieve from payment of tax on other tax heads

Tribunal ruling

- Tax exemption only relates to Income Tax
- Exemptions are tax head specific and entity specific and not analogous

Everret Aviation Ltd vs KRA Appeal No.2 of 2009

Distinction between an employee and a consultant

- The dispute was whether resident freelance pilots should be considered as employees for PAYE purposes

Aspect for consideration included

- Differentiating between a contract for service and a contract of service

Everret Aviation Ltd vs KRA Appeal No.2 of 2009

Contract of service as per the Income Tax Act

- means an agreement, whether oral or in writing, whether expressed or implied, to employ or to serve as an employee for any period of time and includes a contract of apprenticeship or indentured leadership under which the employer has the power of selection and dismissal of the employee, pays his wages or salary and exercises general or specific control over work done by him; and for the purpose of this definition an officer in the public service shall be deemed to be employed under a contract of service

Everret Aviation Ltd vs KRA Appeal No.2 of 2009

Distinction between contract for service and contract of service in simple terms

- In a contract for service – the master can order or require what is to be done
- - an individuals work, even though done for the business, it is not integrated into it but is only an accessory to it

- In a contract of service – the master can order, require what is to be done and how it shall be done
- - a person is employed as part of the business and his work is done as an integral part of business

Everret Aviation Ltd vs KRA Appeal No.2 of 2009

Ruling

Relevant factors considered cont'd

- Control and integration – the method of payment, any obligation to work only for that employer, stipulates time (hours, overtime, holidays)
- Entitlement to social welfare benefits
- Who provides the tools of work
- Whether the individual can delegate work or not - independence
- Economic reality – who bears the risk of loss and the chance of profit

KRA won the case

Interactive Session