

Withholding Tax

Presentation by:

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Presentation Outline

- 1 Overview of Withholding Tax (WHT)
- 2 Payments Subject to WHT
- 3 Legal provisions on WHT
- 4 Withholding Tax Rates
- 5 Pension and Provident Schemes
- 6 Consequences of Non-Compliance
- 7 Examples and Recent Case Law
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Overview of WHT



What is Withholding Tax (WHT)?

- ✓ Tax deducted at source on payments to both resident and non-resident persons on income from various sources.



Depending on the **income source**,
WHT can either be a **final tax (F)** or
an **advance tax (A)** payment

- ✓ Interest, agency fees, royalties, management, professional and training fees for resident companies; (A)
- ✓ Interest, agency fees, royalties, management, professional and training fees for non-resident companies; (F)
- ✓ Interest payments to an individual; (F)
- ✓ Commissions; (A)
- ✓ Amounts withdrawn from registered pension fund; (F)
- ✓ Payments to non-residents for the use or occupation of property; (F)
- ✓ Winnings from betting and gaming; (F)

- ✓ Qualifying Dividends - dividends chargeable to tax with the exception of dividends from Co-operative societies (F)
- ✓ Non-qualifying dividends – from co-operative society dividend (A)

Why withholding tax?

- ✓ Cash flow to the government
- ✓ An advance payment of tax hence providing an additional compliance measure
- ✓ Cost effective collection measure through the use of other taxpayers
- ✓ Provides a manageable avenue for taxation of non-residents deriving income from Kenya

- ✓ **Section 3(2), Section 10, Section 35, Paragraph 3 and 5 of the Third Schedule to the ITA and WHT Rules 2001**
- ✓ Section 10 provides that any payment paid by a resident person or a person having a permanent establishment in Kenya in respect of:
 - Management or professional fee or training fee;
 - A royalty or natural resource income;
 - Interest and deemed interest;
 - The use of property;

Shall be deemed to be income accrued or derived in Kenya

- ✓ **Section 35** of ITA provides for payments subject to WHT both to resident and non-resident persons. These include:
- Interest, agency fees, dividends, royalties, management, professional and training fees;
 - Commissions;
 - Amounts withdrawn from registered pension or provident fund;
 - Payments to residents/non-residents for the use or occupation of property.

Income Tax Act (ITA)

- ✓ Paragraph 3 and 5 of the Third Schedule to the ITA detail the rates applicable for WHT
- ✓ The WHT Rules 2001 provide further clarification on the administration of WHT
- ✓ “Paid” is defined in Section 2 to include distributed, credited, dealt with or deemed to have been paid.
- ✓ In Fintel v KRA the judge clarified the definition of paid includes accrual

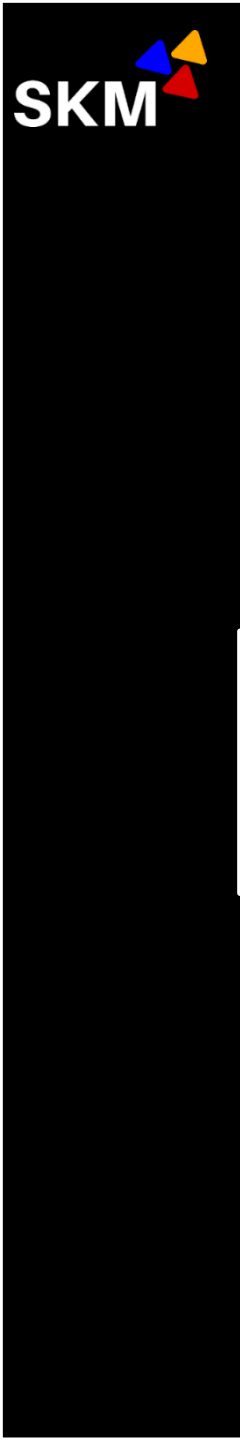
Obligations under the WHT regime

It is the **Responsibility** of the person making payment of income subject to WHT to:

- **Compute and deduct** the tax at the relevant rate;
- **Remit the tax** so deducted by the 20th day of the month following that in which tax is deducted

Incase of dispute between the payer and payee:

- payer should furnish the payee with a written statement showing the WHT deducted;
- Payee may give a notice of objection in writing to the Commissioner within 30 days after receiving the written statement showing the WHT deducted



Withholding tax rates

WHT rates for payments made to residents

Nature of payment	Rate
Management or professional fees: (> 24,000) - Managerial, technical, agency, consultancy fees and Training fees	5%
Contractual fees: (>24,000) - Building, civil and engineering works	3%
Royalties - Software license	5%
Interest*:	
Bank interest and other sources	15%
Bearer instruments	
- 2 years;	25%
- Beyond 10 years w.e.f 12.06.09	10%
Dividends: EA citizens (Uganda and Tanzania) are now considered Kenyan residents for purposes of WHT on dividends	5%

*Interest paid to financial institutions is exempt from WHT as per Sec 35(3)(b) of the ITA


WHT rates for payments made to non-residents

Nature of payment	Rate (%)
Management or professional fees:	20
Royalties - e.g. software licenses	20
Dividends	15
Contractual fees (building /civil/engineering)	20
Rents: Real estate	30
Lease of equipment	15
Interest	15
Interest on bearer instrument	25
Commissions - brokers	20
Commissions – agents and others	20

Double taxation agreements(DTAs)

DTA Country	Dividends (%)	Interest (%)	Royalties (%)	Management & Professional (%)
Canada	15	15	15	15
Denmark	15	15	20	20
France	10	12	10	20
Germany	15	15	15	15
India	10	10	10	10
Iran	5	10	10	20
Norway	15	15	20	20
Qatar	5/10	10	10	20
Seychelles	5	10	10	10
South Africa	10	10	10	20
South Korea	8/10	12	10	20
Sweden	15	15	20	20
UAE	5	10	10	20
United Kingdom	15	15	15	12.5
Zambia	0	15	20	20

Limitation of Benefit Clause



What is the LOB clause?

- ❖ Business profits - Amount is taxed as business profit in the contracting state.
- ❖ Effective from 1 January 2015.
- ❖ Purpose? To prevent companies from treaty shopping for countries with favorable tax rates.
- ❖ The parent company of the recipient must be a resident of the receiving country and own at least 50% of the company receiving the service subject to WHT.
- ❖ Underlying ownership? Includes direct and indirect ownership by individuals through interposed companies.

Payments by pension and provident schemes

Unregistered schemes:

- ✓ No further tax is deductible on withdrawals


Registered schemes:

- ✓ Withdrawals are taxable
- ✓ WHT ordinarily deductible at PAYE rates
- ✓ Wider brackets apply



Special withdrawals (KShs)	Ordinary withdrawals (KShs)	Rate
First KShs 300,000		Exempt
First 400,000 after the exemption	First KES 288,000	10%
Next 400,000	-	15%
Next 400,000	-	20%
Next 400,000	Next KES 100,000	25%
Over 1.6 M	Above 388,000	30%

Special withdrawals	Ordinary withdrawals
Payment made after the expiry of fifteen years after joining the fund	Before expiry of 15 years after joining the fund
Attainment of the age of 55 years	
Early retirement on grounds of sickness	



Is it worthy
deferring
withdrawal?

Annuity or
lumpsum on
retirement?

Example of taxation of pension withdrawal

Take an example of pension withdrawal of KES 1,000,000 by pensioners under the ordinary and special withdrawals. Under both instances, KES 300,000 shall be exempt for tax purposes.

The taxable amount shall be KES 700,000 as follows:

Special withdrawals (KShs)	Tax due (KShs)	Ordinary withdrawals (KShs)	Tax due (KES)
First 400,000 after the exemption	40,000	First KES 288,000	28,800
Next 400,000	45,000	-	-
Next 400,000	-	-	-
Next 400,000	-	Next KES 100,000	25,000
Over 1.6 M	-	Above 388,000	93,600
Total tax payable	85,000		147,400
Net payable to pensioner	915,000		852,600

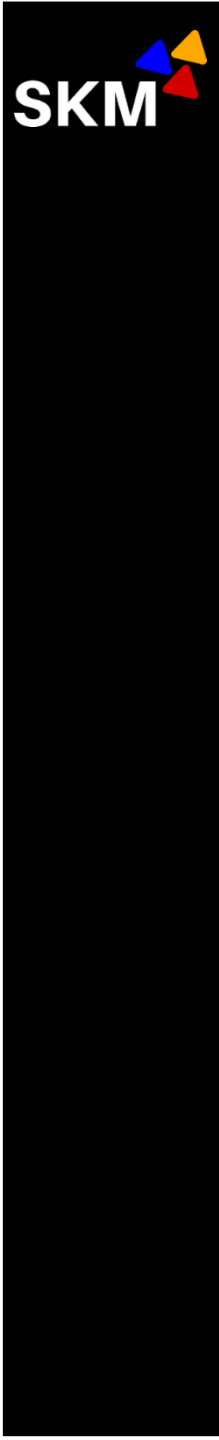
- ✓ Where payment is to be made net of tax, the payer is required to gross up the WHT base amounts against the foreign suppliers' invoices when paying WHT
- ✓ The WHT is calculated on the grossed up amount
- ✓ Alternatively, the payer could include the element of tax when negotiating its contracts





Non-compliance with WHT rules and obligations

- ✓ Late payment penalty of **5%**;
- ✓ Interest at **1%** per month on the outstanding tax, until payment in full;
- ✓ W.E.F 13 June 2008 - In duplum rule applies to interest on tax



Case laws and recent court rulings



Local Committee Ruling on Tsavo Power Company Limited Vs Kenya Revenue Authority

THE FACTS

- ✓ KRA Audit conducted established that Tsavo was not charging WHT on miscellaneous expenses (hotel accommodation, travel and transport)
- ✓ It was held that disbursements are subject to WHT unless tax payer can prove there is no margin on the disbursement
- ✓ Definition of management and professional fees “however calculated” to include disbursements

Definition of paid for WHT

Fintel Limited Vs Kenya Revenue Authority **A High Court case challenged the definition of “paid” under** **Section 2 of the ITA**

THE FACTS

- ✓ Fintel entered into a contract for the construction of a rental building and experienced difficulties in settling outstanding fees
- ✓ KRA conducted an audit and demanded WHT on interest liability accrued for failure to settle fees
- ✓ Accrual of an expense in the audited accounts amount to the same expense being “paid” as defined under Section 2 of the ITA

Fintel Limited Vs Kenya Revenue Authority **A High Court case challenged the definition of “paid” under** **Section 2 of the ITA**

THE FACTS

- ✓ As a result, WHT was applicable on the interests accrued in the audited accounts by Fintel as it had claimed an expense/deduction

A company is being provided with the following services. Identify which ones are subject to WHT:

Service	Service
Installation of operating software	Rent paid to a non-resident person
Supply of mobile phones to Base Titanium	Construction services
Subscription fees for Oracle software	Rent paid to a resident person
Tax advisory fees	Dividends paid to shareholders
Monthly salary to employee	Safaricom telephone bills

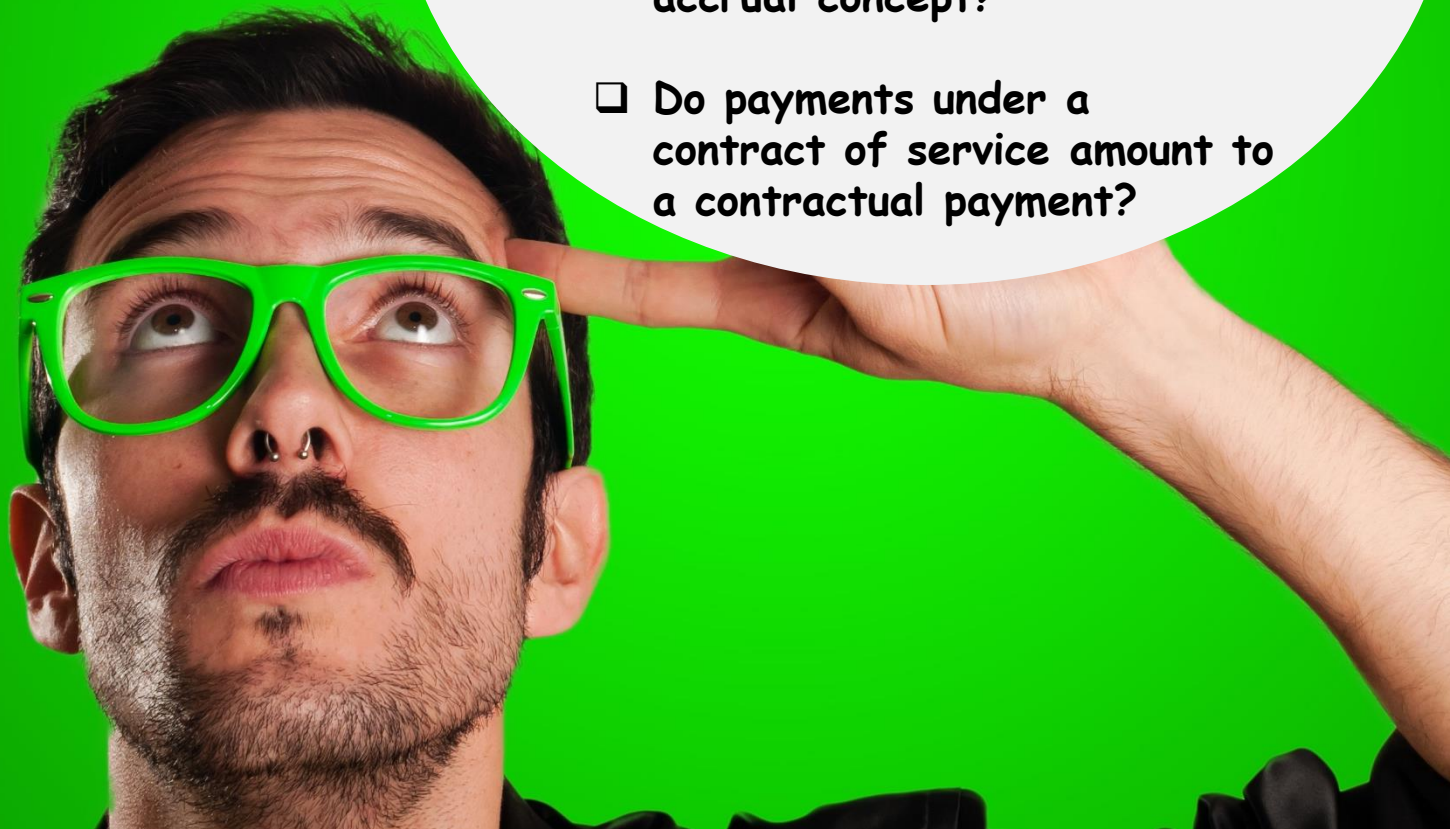
Services that are subject to WHT upon making payment

Service		Service	
Installation of operating software	✓	Rent paid to a non-resident person	✓
Supply of mobile phones to your organisation	x	Construction services	✓
Subscription fees for Oracle software	✓	Rent paid to a resident person	x/✓
Tax advisory fees	✓	Dividends paid to shareholders	✓
Monthly salary to employee	x	Safaricom telephone bills	x

Think

About it...

- ☐ If you are paying tax on behalf of the other party, why should KRA treat it as your tax and still demand the tax and penalties on non-payment?
- ☐ What happens in case you overpay WHT based on the accrual concept?
- ☐ Do payments under a contract of service amount to a contractual payment?



Q & A Session





Contact details



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