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Tax Matters

(A tax newsletter for charitable organisations operating in East Africa)

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In this issue

Welcome to this first issue of Tax matters. In Tax matters we plan to update you on tax developments in East Africa, in particular any changes in legislation applicable to charitable organisations and current trends or agreements reached with the tax authorities. We have decided to include a section on frequently asked questions, this month focusing on Kenya. We hope you will find this first issue of Tax matters useful and welcome any comments for future issues

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Feature Articles

Duty Exemptions for Charitable Organisations

Joseph Kimote 

Kenya

The East African Customs Union (EACU), which came into force on 1st January 2005, introduced profound changes in regional trade policy and related customs legislation.

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. Generally, 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.

Joseph Kimote is a tax manager and economist specialising in Customs and Excise Duties and international trade. He joined the East African firm in 2000.

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. Technically, 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.

However, the EAC Council of Ministers extended a window through which charitable organisations 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. The scheme works as follows: 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 organisation will be paid by the Ministry of Finance. The undertaking issued to Customs will subsequently be utilized in having the goods released on a duty free basis. Treasury will thereafter make a direct payment to Customs for the duties payable. In the event that the resources provided by Treasury for this purpose are exhausted, then the goods would be cleared on a duty paid basis unless additional funds are allocated for this purpose.

From the above, it is quite clear that the above arrangement only provides for a temporary reprieve on duties as it is purely dependent on the Ministry allocating funds. In recognition of the important and crucial role played by NGOs in alleviating poverty, it would have been a good idea if the duty exemption for charitable organisations was expressly provided for in the EACMA. The current arrangement is highly vulnerable to abuse and no doubt will be monitored closely by the donor agencies.

VAT procedures for charitable organisations in Tanzania

Edward Mwachinga 

Tanzania

Edward Mwachinga is a Tax Manager with the Tanzanian firm. He holds a Bachelor of Laws degree from the University of Nairobi; he is also a member of the Law society of Kenya and the East African Law Society.

Edward joined Deloitte & Touche in Nairobi in 2003 and transferred to the Dar es Salaam office in May 2004. He has extensive experience in providing advice on indirect tax issues for a variety of clients serviced by the firm in East Africa including mining, communication, manufacturing, civil engineering and power generation industries.

The Value Added Tax Act (the "Act") in Tanzania provides relief from VAT on the purchase or importation of taxable supplies by persons and organizations referred in the third schedule to the Act as "Relieved Persons". This relief may be granted subject to the limits and conditions prescribed in the Act and in accordance with procedures determined by the Minister (responsible for Finance).

Relief from VAT is only available on a transaction by transaction basis upon application for relief from VAT in respect of the particular transaction for which relief is sought.

In order to enjoy relief from VAT, the Relieved Person is required to make an application using the prescribed forms 220 or 223 depending on whether the Relieved Person is a diplomat/diplomatic mission or not. These forms are available from the VAT regional revenue offices. Once the forms have been completed they are

required to be submitted to the Regional Manager of the region in which the person or organization is based for consideration and/or approval.

With the application the Relieved Person is required to attach a pro forma invoice showing the value and quantity of the goods and/or services that the Relieved Person wishes to purchase. Additional documentation may be required to provide evidence that the person or organization qualifies for relief under the Act. For example a non – profit community based organization may be required to provide a copy of a valid certificate of registration, a description of the project it is undertaking and a certificate issued by the Permanent Secretary of the Ministry of Finance that the Relieved Person qualifies for relief from VAT on its purchases.

If the application is approved by the Regional Manager, the applicant is issued with an authority to procure taxable supplies free of VAT in a prescribed form VAT 222 or VAT 224 depending on whether the Relieved Person is a diplomat/diplomatic mission or not. The authority to procure taxable supplies free of VAT is usually valid for a specific period and is limited to the specific supply and value reflected in the pro forma invoice attached to the application.

It is important to note that relief from VAT is only valid provided the tax point for VAT purposes has not occurred. That is to say the authority to procure taxable supplies free of VAT must be obtained before the goods or services are received, payment is made or a tax invoice issued. If any of these conditions precede the issue of the authority to procure taxable supplies free of VAT, the authority is (using the words of the Tanzania Revenue Authority) "useless".

Frequently Asked Questions

If you have any specific questions you would like us to handle in the next issue, please feel free to send your questions to taxmatters@deloitte.co.ke.

From your experience as tax practitioners, please let me know how willing and expedient the government is in granting tax exemptions or remissions.

It would be correct to say that the granting of tax exemption (of any kind) has become more difficult in the recent past. This is not restricted to just NGO's but to other tax payers as well. This is partly due to abuses of exemptions to NGO's and partly due to the pressure to collect revenue.

I have noted the provisions of the 1st Schedule to and section 13 (i) of the Income Tax Act relating to the power of the Minister to grant exemptions from payment of income tax of income in certain circumstances. In addition to public interest, are you aware of other considerations that the Minister would take into account in deciding whether to grant such exemptions?

All exemptions are normally given in interest of the public. This can be to promote a particular industry or sector (which then benefit the public directly or indirectly) or for welfare of the public (e.g. health, education, religious activities etc).

Are there any special provisions relating to taxation of NGOs and can NGOs claim the normal deductions such as wear and tear allowances on equipment?

There are no special taxation provisions for NGO's. If the NGO is not exempted from tax then it will be required to account for tax and claim relief and allowances just as any other tax paying entity.

Would income earned by an NGO be exempt from income tax if such income was to be repatriated to another country?

No. In Kenya, unless specifically exempted, any income that is accrued in or derived from Kenya is subject to tax in Kenya.

What tax breaks are available to expatriate staff employed by an NGO?

Unless the agreement between the Kenya government and the NGO specifically exempts NGO's expatriate staff from paying taxes, such expatriate staff are required to account for taxes (if they become resident for tax purposes or are paid by a Kenyan employer).

I have noted the provisions of section 23(1) of the Value Added Tax Act, which empower the Minister to grant remissions on the ground of public interest, in your experience what criteria does the Minister normally apply to determine public interest?

The remission under Section 23 (1) is granted where the goods or services will be used to alleviate special needs of the public (including distribution to the poor and needy) such as medical, educational, religious or rehabilitation. A remission could

also be granted where there is a calamity such as drought, an epidemic etc. It is such special circumstances that are deemed to be in the public interest.

Is exemption or remission granted under the VAT Act blanket or limited to certain transactions?

8th Schedule would grant zero-rating for all supplies to the listed person (unless provided otherwise). However, in order to get zero-rating (whether under the 8th schedule or not) for goods and services, specific transactional exemption certificates have to be applied for and supplied to the supplier.

Remember...

An NGO is not automatically exempt from income tax and Customs duties. In all East African countries an NGO must apply to obtain relief as a charitable organisation, and until relief is granted in writing, the NGO is a taxable organisation and eligible to payment of customs duties. The relief on customs duties which was provided for in the national customs legislations was eroded by the enactment of the East African Customs Management Act in January 2005

A charitable organisation which is exempted from certain taxes under a memorandum of understanding with the Kenyan government must still apply to the Kenya Revenue Authority for income tax, VAT and Customs Duty exemption.

Even where a charitable organisation obtains relief from income tax, it does not relieve the organisation from its obligation to deduct tax from its employees or from acting as a withholding tax agent.

An NGO which is granted charitable status for income tax purposes must still lodge income tax returns every year.

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