Understanding key legislations on the law on direct taxes on income law No. 16/2005
UNDERSTANDING KEY LEGISLATIONS ON THE LAW ON DIRECT TAXES ON INCOME LAW No. 16/2005
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1. GENERAL PROVISIONS

Definitions of terms

1. **Taxpayer**: Every person subject to tax.

2. **First employer**: Employer who gives the greatest amount of income to the employee.

3. **Person**: Any individual, legal person or association of persons.

4. **Related person**:
   - An individual and his spouse, lineal ascendants or lineal descendents;
   - Any person who owns 50% or more of the shares of a company either in value or number.

5. **Casual Labourer**:
   - Unskilled – does not need special skills to use equipment;
   - Engaged for less than 30 days in a tax period (year).

6. **Small business**: turnover of less than 20 mil. RWF

7. **Residence**: The following are the conditions for residence
   - Has a permanent residence in Rwanda;
   - Has a habitual place of abode in Rwanda;
   - Is a Rwandan representing Rwanda abroad;
   - An individual who stays in Rwanda for more than 183 days in any 12-month period – intermittently or continuously;
• A company or association established according to Rwandan Law;
• Has its effective place of management in Rwanda at any time during a tax period;
• A Rwandan government owned company.

8. **Permanent establishment**
A fixed place of business where business is wholly or partially carried on; including:
  • An administrative branch;
  • Factory;
  • Workshop;
  • Mine, quarry or any other place for the exploitation of natural resources;
  • A building site or a place where construction or assembly works are carried out.

9. **Following elements are not considered as a permanent establishment while considered alone:**
  • Facilities used solely for storage or display;
  • Stock kept for storage or display only;
  • Stock of goods kept for processing by another person;
  • Place used solely for purchasing goods or collecting information;
  • Place used solely for making preparations of the persons activities.

**Through an agent in Rwanda**

• A person may have a Permanent Establishment through an agent acting on his/her behalf with a capacity to enter into contracts on his/her behalf.
A person is not Permanent Establishment if:

a. The person carries on business through a general commission agent, broker or other private agent who operates in the ordinary course of business;

b. A company that controls or is controlled by another company is not a Permanent Establishment of the other.

10. **Foreign tax credit**

   • A resident of Rwanda generates income from abroad;
   • Pays tax to a foreign country on that income;
   • The tax paid abroad is deductible from the tax due in Rwanda;
   • The deduction can not exceed the amount of tax to be paid in Rwanda on the foreign earned income;
   • Must be supported by evidence of payment abroad.

11. **Tax period**

   • Normally it is the calendar year
   • The Minister has the power to allow a different tax year if it:
      ✓ Is an entity;
      ✓ Is required to keep books of account;
      ✓ Has a compelling reason for a different tax year;
   • Period from start of the period the change occurs to the date of the change becomes a special tax period.
II. PERSONAL INCOME TAX

1. General provisions
2. Employment income
3. Business profits
4. Investment income

1. GENERAL PROVISIONS

The Base of personal income tax
There is hereby established an annual “personal income tax” levied on income received by an individual.

Obligations of the concerned taxpayers of income tax
- Residents on their domestic and foreign sources.
- Non-residents on income earned/ sourced in Rwanda

Composition of taxable income
- Employment income;
- Business profit;
- Investment income

Tax rate
- Taxable income is rounded to the nearest 1,000 RWF;
- Personal income is taxed at: 0%, 20% & 30%;
- Small businesses pay tax at 4% of turnover in case of no detailed accounting;
- An individual who receives taxable income prepares annual declarations and presents it to the Tax Administration not later than;
- 31st March of the following tax period.
Exempted persons from annual declaration are those who only receive:

- Income subject to PAYE withholding.
- Investment income subject to withholding tax of 15%.
- Employees seeking refund of > FRW 5,000 must make annual declaration.
- An Individual who carry profit-oriented business activities, files an annual declaration with balance sheet, profit & loss and annexes therewith.
- Taxpayers with annual turnover to be determined by the Minister may be required to have their declarations and financial statements certified by a qualified professional.

GENERAL PROVISIONS – DETERMINATION OF TAX LIABILITY

Calculate and pay the tax on the day of the annual declaration

- Deduct the following from the annual tax payable
  - Tax withheld as per article 51 of this law (interest, dividend,)
  - Tax withheld according to Article 52 (5% at customs and 3%)
  - Quarterly prepayments

- Credit balance to taxpayer may be used to:
  - Discharge other debts
  - Discharge future debts
  - Refund to taxpayer within 30 days of request
2. EMPLOYMENT INCOME

INCOME FROM EMPLOYMENT ACTIVITIES

- Wages, salaries, bonuses, leave pay, sick pay, medical allowances etc;
- All kinds of allowances, including any cost of living, subsistence, rent, and entertainment or travel allowance;
- Reimbursement of expenses the employee or his/her associate incurs;
- payments to the employee for to his or her acceptance to work in any conditions of employment;
- Redundancy or termination pay;
- Pension payments;
- Other payments made in respect of current, previous or future employment.

EMPLOYMENT INCOME – EXEMPTIONS

- EXEMPT EMPLOYMENT INCOME
  - Reimbursement of expenses the employee incurs for the business of the employer;
  - Reimbursement of expenses the employee incurs that are deductible from his/her business profits;
  - Retirement contributions by the employer for state pension;
  - Pension payments under the state social security system;
  - Any foreigner who represents his or her country in Rwanda;
• Any other individual employed in any Mission of a foreign state performing state affairs, who is a national of that state and a bearer of a diplomatic passport; or
• Any non-citizen individual employed by an international organization formed under International Law.

EMPLOYMENT INCOME – BENEFITS IN KIND

Benefits in kind included in employment income:

• Use of employer’s vehicle at 10% of total employment income excluding benefits in kind;
• Interest saved by an employee from loan (including advance of more than 3 months salary) provided by the employer (calculated at interest rate offered to commercial banks by BNR);
• Use of employer’s housing, furniture and equipment valued at 20% of the total employment income excluding benefits in kind;
• Benefits provided to a person related to an employee;
• Benefits provided by an entity to a member of that entity.

3. PROFIT ON BUSINESS ACTIVITIES

PRINCIPAL ELEMENTS

• Income from business activities;
• Accounting for small businesses;
• Exemptions for agricultural activities;
• Income on assets in foreign currency;
• Long-term contracts;
• Deductible expenses, including thin capitalization;
• Non-deductibles;
• Trading stock;
• Depreciation rules;
• Investment allowance;
• Training & research;
• Bad debts;
• Loss carried forward;
• Transfer pricing;
• Quarterly prepayments.

INCOME ON COMMERCIAL ACTIVITIES

Determination of business profit

• Income from all business activities reduced by all business expenses;
• Determined per tax period of the bases of profit and loss account drawn in accordance with the NAP, subject to this law;
• The Commissioner General may use any other accounting method or source of information as appropriate subject to this law to ensure accuracy of the taxpayer’s profit;
• Income tax exemption: Income accruing to registered collective investment schemes and employees “shares scheme are exempted from income tax”;
PROFIT ON COMMERCIAL ACTIVITIES

- **Small business: special arrangement**
  - Has the Option to declare and pay based on accounting books
  - Minister determines the rules of accounting
  - Once opted no return to lump sum taxation for 3 years

- **Income from agriculture**
  Exempted if turnover is less than FRW 12 million in a tax period.

INCOME ON ASSETS IN FOREIGN CURRENCY

Assets in foreign currency valued at the exchange rate of the RWF on the last day of the tax period.

Profit or loss on those assets is included in the profits or loss of that period.

LONG-TERM CONTRACTS

- Cover all contracts which are not completed within the tax period in which work commenced – excluding those which are estimated to be completed within 12 months of commencement of contract;
- Based on percentage completed during a tax period;
- Percentage determined by dividing the cost incurred during a tax period into the estimated total contract cost;
- The percentage applied to the contract value to determine revenue for the each tax period;
- Loss in a tax period in which a contract is completed is carried back and offset against a previously taxed business profit;
DEDUCTIBLE EXPENSES

Must fulfil the following:

- Direct purpose of and in the normal course of the business;
- Are real expenses substantiated with proper documents;
- Result in decrease in net assets; Example from attendees
- Are included in the expenses for the period in which they are incurred.

NON-DEDUCTIBLES

1. Bonuses and fees to Board;
2. Dividends paid out;
3. Interest paid on loans in foreign currency in excess of the London inter-
   bank offered; rate at the beginning of tax period increased by 1% point;
4. Contributions to reserves or other special funds;
5. Fines and penalties;
6. Gifts or donations in excess of 1% of turnover to non profit making
   persons;
7. Donations given to profit making persons;
8. Income tax;
9. Personal consumption expenses;
10. Entertainment expenses.
THIN CAPITALISATION

- Objective is to protect revenue from heavy charges of interest;
  - Taxpayers tend to borrow more instead of financing by equity;
- **Rule**: Loan financing does not exceed 4 times the amount of equity;
  - Equity excluding reserves and provisions;
- Interest in excess of this will be disallowed;
- This rule does not apply to banks and insurance companies.
- **EXAMPLE**: Attendees

TRADING STOCK VALUATION

- Lower of market or cost on last day of tax period
- Example: attendees

DEPRECIATION RULES

- Non-wearing assets not depreciated – land, fine arts, jewellery, etc;
- Buildings, machinery and built-in heavy equipment at 5% a year on straight line basis;
- Intangible assets such as goodwill and research & development at 10% a year;
- Pooling system for the following:
  - Computers, software and related – 50% a year;
  - Other business assets – 25% a year - example.
BASIC VALUE RATES & DEPRECIATION

- Base is cost or book value of asset:
  - Increased by cost of assets acquired, improved, renewed or reconstructed;
  - Decreased by the sale price of assets disposed of or compensation received for loss of asset;
- If the depreciable value is less than FRW 500,000, expense the entire amount.

INVESTMENT ALLOWANCE

- 0% of invested amount deducted in year 1;
- 50% outside Kigali (is this defined?) or for priority sectors;
- Conditions:
  - Excludes vehicles that carry less than 8 persons (Except those in tourist business);
  - Investor must be registered as a taxpayer;
  - Investment amount must be = 30 million;
  - Asset must be held for at least 3 tax periods (year or month needs definition) after period in which the investment allowance was considered;
  - Disposal (except under natural calamities or other involuntary conversion) will result in payment:
    - Of the reduction in tax because of the allowance obtained;
    - Interest on the reduced tax for every full calendar month elapsed after end of the calendar month in which the investment allowance has been granted.
TRAINING AND RESEARCH EXPENSES

- All are expensed during the period they are incurred;
- Do not include the purchase of land, buildings, other immovable properties, including refining, rehabilitation and reconstruction as well as exploration expenses or other assets (what are other assets).

BAD DEBT

Bad debts are deductible if:

- An amount corresponding to the debt was included in taxable income previously;
- The debt is written off from the books of accounts;
- There is proof that the debtor is insolvent;
- Exception:
  - Commercial banks for any increase in the mandatory reserves on non-performing loans as required by BNR;
  - Bad debts recovered are added back to taxable profit.

LOSS CARRIED FORWARD

- Losses sustained in a tax period deducted from profits of the next 5 tax periods;
- Earlier losses are settled first;
- Foreign sourced losses are not allowed to be carried forward;
• Loss sustained by a taxpayer whose share are not traded in the stock market, is not allowed to be carried forward when changes of ownership occur by more than 25%. This applies to losses incurred in the tax period the change of ownership happened and the previous tax period.

TRANSFER PRICING

• When transactions between related persons result in less taxable profits than would have been had the transactions occurred between unrelated persons, the tax administration may adjust the profit of either party to redeem the correct taxes;

• Minister issues regulations

  ✓ Commissioner General may make arrangements in advance with the taxpayer regarding the price to be used for a transaction.

QUARTERLY PREPAYMENTS (Art 31)

• Payment is 25% of tax declared in previous period;
• Due on 30 September, 31 December of the year of tax and 31 March and 30 June of the year that follows;
• The quarterly prepayments are reduced by the tax withheld;
• If taxpayer started during previous period, the quarterly prepayment = 25% of the amount of tax in previous period divided by the number months the taxpayer carried on the business times 12.
4. INVESTMENT INCOME

- Includes payments of interest, dividends, service fees, royalties, and rent which has not been taxed as business income;

- Interest income:
  - subject to a flat rate of 15%;
  - If subject to withholding, it is final tax;

- Dividend income:
  - subject to a flat rate of 15%;
  - If subject to withholding, it is final tax;

- Royalty income:
  - subject to a flat rate of 15%;
  - If subject to withholding, it is final tax;

- Rent income:
  - Includes rent of machinery and other equipment, land and livestock;
  - Revenue is reduced by:
    - 10% of revenue for expenses;
    - Interest on loans, and
    - Depreciation

- Apply the personal income tax rate for individuals;
- Apply corporate rate for companies, which are exempt from rental income tax.
III. CORPORATE INCOME TAX

GENERAL PROVISIONS

- Corporate income tax is levied on business profits of entities;
- The following are the taxpayers:
  - Companies legally incorporated either in Rwanda or abroad;
  - Cooperative societies and their unions;
  - Public enterprises;
  - Partnerships;
  - Entities established by Provinces, Districts, the City of Kigali, and towns, to the extent that these entities conduct a business;
  - De facto companies, associations and all other entities that either by form, by goal, or by result are established to realize benefits.

EXEMPT ENTITIES

- The Rwanda Government, Provinces, Districts, the City of Kigali, and towns;
- The National Bank of Rwanda;
- Entities that carry on only activities of a religious, humanitarian, charitable, scientific or educational character, unless and to the extent that they conduct a business;
- International organizations, agencies of technical cooperation and their representatives, if provided by international agreement;
- Qualified pension funds;
- The State Social Security Fund (Caisse Sociale du Rwanda);
- Rwanda Development Bank (B R D).
EXTENT OF LIABILITY

- Resident entities are liable to tax from both domestic and foreign sources of income;
- Non-residents from sources in Rwanda only.

TAX RATE

- Business profit rounded down to nearest 1,000 RWF and levied at 30%;
- A registered investment entity that operates in a Free Economic Zone and foreign companies that have their headquarters in Rwanda that fulfil the requirements stipulated in the Rwandan Investment Code is entitled to:
  ✓ Corporate income tax at the rate of zero percent (0%);
  ✓ exemption from withholding tax;
  ✓ Tax free repatriation of profit.

RATE INCENTIVE FOR INVESTMENT

- A registered investor is entitled to a profit tax discount;
- 2%, if the investor employs between 100 & 200 Rwandans;
- 5%, if the investor employs between 201 and 400 Rwandans;
- 6% if the investor employs between 401 and 900 Rwandans;
- 7%, if the investor employs more than 900 Rwandans;
- To benefit from the above must maintain employees for at least 6 months during the tax period, and should not be employees with incomes that fall within the 0% tax rate.
TAX INCENTIVES FOR EXPORTERS

- If a taxpayer exports commodities or services that bring to the country between 3,000,000 and 5,000,000 USD in a tax period, is entitled to a tax discount of 3%.

- If a taxpayer exports commodities or services that bring to the country more than 5,000,000 USD in a tax period, is entitled to a tax discount of 5%.

- Micro-finance companies engaged in activities approved by competent authorities pay corporate income tax at the rate of 0% for a period 5 years from the time of the approval of the activity. Could be renewed by order of the Minister.

TAX DECLARATION

- A taxpayer who receives business profit is required to submit declaration with statements and annexes to the Tax Administration, not later than the 30th day of the sixth month of the following tax period.

- The amount of tax to be paid is calculated on the basis of the annual declaration, reduced by:
  - The tax withheld from payments included in taxable income;
  - The withholding taxes;
  - The prepayments made during the tax period.
• The tax is paid to the Tax Administration on the same day as the presentation of the annual declaration;

• If withholding and prepayments exceed the liability as per the annual declaration, the excess is offset against arrears or future liability. If no arrears refunded within 30 days of request by taxpayer.

BUSINESS PROFIT

• Corporate profit is calculated like in individual businesses;

• Inter-company dividends received from a resident company or partnership are exempt in the determination of taxable profit.

Corporate (resident) reorganization

• Reorganisation includes:
  ✓ merger of 2 or more resident companies;
  ✓ acquisition or takeover of 50% or more shares by value or number;
  ✓ Acquisition of 50% or more of the assets and liabilities of one resident company by another, solely in exchange of shares in the purchasing company;
  ✓ one resident company splits into two resident companies

• Transferring company is exempt from tax on capital gains;
• Receiving company takes assets at book value;
• Receiving company entitled to take reserves and provisions; created by transferring company subject to conditions that have applied to
transferring company without the reorganisation.

MERGERS – EXAMPLES

- Company A had a total of 1,000 shares distributed as follows among three owners:
  - Share holder 1 = 500 shares;
  - Shareholder 2 = 200 shares;
  - Shareholder 3 = 300 shares;
  - Company B acquires the shares of shareholder 1 and 3 by issuing 100 shares of B, which has a total of 1,000 shares;
  - In this case B has acquired 80% of the ownership of A;
  - Instead of acquiring the shares B acquired 500 of the total assets of 1,000 and 200 of the total liabilities of 400. The acquisition is 50% in this case. The agreement could be for B to receive 50% of dividends declared each period and to have 50% of voting rights.

LIQUIDATION

- All liquidation receipts are considered as dividends on shares.
IV. WITHHOLDING TAXES

• PAYE
  ✓ Employers;
  ✓ Agencies paying pensions except for pensions paid according to the state social security;
  ✓ Tax exempt income is exempt from withholding;
  ✓ An employer who is not the first employer must withhold the tax at the top rate of 30%;
  ✓ If employer is not obliged to withhold the PAYE, the employees has to declare and pay within 15 days;

PAYE RATE

• 0 – 30,000 RWF = 0%;
• 30,001 – 100,000 RWF = 20%;
• Greater than 100,000 RWF = 30%;
• Casual labourers = 15% on all earnings exceeding RWF 30,000 on which rate is zero;
• Details are in PAYE Guide.

WITHHOLDING TAX ON OTHER PAYMENTS

• Withholding tax of 15% levied on:
  ✓ Dividends;
  ✓ Interest;
  ✓ Royalties;
  ✓ Service fees;
  ✓ Performance payments;
  ✓ Lottery & other gambling;
• Withholding agent to submit declaration and pay within 15 days tax is withheld (every month);

• Applies to non-resident individuals and entities for payments allocated to Permanent Establishment that person maintains in Rwanda.

WITHHOLDING TAX ON IMPORTS AND PUBLIC TENDERS

• 5% on imports for commercial use is paid at customs;
• 3% on payments for public tenders net of VAT;
• Exempts:
  ✓ Those exempted from business profit tax;
  ✓ Those with tax clearance certificate.

FAILURE TO WITHHOLD TAX

• Obligation to withhold and pay is on:
  ✓ The agent is personally liable for the tax with penalties and interest when failing to withhold the tax;
  ✓ The agent may recover the principal tax from the payee;
  ✓ The payer must declare and pay within 15 days after end of month in which the tax was withheld.

RECORDS OF PAYMENTS AND TAX WITHHELD

• A withholding agent maintains and makes available to the Tax Administration records showing:
  ✓ Payments made to taxpayer;
  ✓ Amount withheld and paid;
• The above records must be kept for 10 years after the end of the tax period to which the records relate.