CPA

Certified Public Accountant Examination

Stage: Advanced A2.3

Subject Title: Advanced Taxation

Study Manual

iCPAR
INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS OF RWANDA
Driving Sustainable Performance

INSIDE COVER – BLANK

INSTITUTE OF
CERTIFIED PUBLIC ACCOUNTANTS
OF
RWANDA

Advanced 2

A2.3 TAXATION

First Edition 2012

This study manual has been fully revised and updated

in accordance with the current syllabus.

It has been developed in consultation with experienced lecturers.

© iCPAR

All rights reserved.

The text of this publication, or any part thereof, may not be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopying, recording, storage in an information retrieval system, or otherwise, without prior permission of the publisher.

Whilst every effort has been made to ensure that the contents of this book are accurate, no responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication can be accepted by the publisher or authors. In addition to this, the authors and publishers accept no legal responsibility or liability for any errors or omissions in relation to the contents of this book.

Contents

BLANK

Chapter 1
Taxation of Businesses operated by Individuals who are not employees

Contents

A Taxpayers concerned

1) Individuals who are not employees: There are taxpayers required to pay income tax on business benefits who are physical people and who carry on activities involving financial remuneration on a purely personal basis. In other words, such taxpayers are not employees contracted to an employer or a corporate or business entity. These latter situations are assessed for employment or corporate income tax respectively.

Examples of the former taxpayers would include generally tradesmen or ‘liberal professions’ such as lawyers, doctors and consultants.
Like “employees”, these taxpayers are assessed according to Chapter II of Law 16/2005 of 18/08/2005 on Direct Taxes on Income … **(the DTI)**

2) Corporate or business entities are covered by Chapter III of the DTI.

But much in Chapter II of DTI also applies to businesses which fall into the categories covered by Chapter III

Taxes are assessed on the profits made by a business. As covered in the first course, profits are Income less expenses. But not all items of expenditure can be deducted from profits for tax purposes.

B Deductible items

a. General
Any expenditure which complies with Art 21 of the DTI may be offset against taxable income or business profits:

- Such expenditure must be committed for the direct need and the normal requirements of the company;
- They must be supported by appropriate documentation to confirm that they have been incurred;
- They must involve a reduction of the net assets of the company;
- They must be included for tax purposes in the expenditure of the period during which they are committed.

But some types of expense are not “tax-deductible”. These include in particular:

- Cash bonuses, attendance fees and other similar payments allocated to the members of the Board of directors;
- Declared dividends and participations in profits;
- The surplus of interest paid on loans made out in a foreign currency, compared to the interbank rate offered in London or "*London Inter-Bank Offered Rate* " (LIBOR) at the beginning of the fiscal year increased by one percent (1%); *(Law No. 73/2008 Article 2 para 3)*

- Contributions to reserves, provisions and other funds with specific purposes, others than those envisaged by the tax law.
- Fines and other penalties;
- The proportion of any gift (donations in cash or the equivalent value of gifts in kind) which exceeds one percent (1%) of sales turnover. However if these gifts are granted by persons or entities carrying on a gainful employment, the gifts will not be entirely non-deductible;
- Income tax of businesses that is paid abroad and value-added tax (VAT);

Indeed, tax paid abroad is not deductible from the tax base under consideration - it instead constitutes a foreign tax credit. Also the VAT cannot be deductible expenditure since it is offset against output VAT. However, all other taxes are deductible from the tax base, as the law only specifically prohibits the deduction of the two taxes discussed above;

- Personal consumer expenditure and any entertainment expenditure provided that this expenditure was not already included on income tax of employment (EIT).

Special attention should be given to Art 22 DTI but see also *Law No. 73/2008 of 31/12/2008* which modifies the DTI.
Those reserves, provisions and funds which are mentioned by the tax law, and which consequently are accepted as deductible, include in particular qualifying pension funds (art.14 4º DTI) and investment provisions (Article 26 DTI);

b. Depreciation

Depreciation is an annual charge against the profits of a company to take account of the reduction in value resulting from the use of fixed assets belonging to the organisation. It therefore forms deductible expenditure for the fiscal year under consideration. However, some assets that are not subject to physical deterioration and associated depreciation in the same way are not allowable. These include in particular land, works of art and heritage assets (art 24 paragraph 2 DTI).

The law outlines four (4) categories of acceptable charges relating to depreciation (article 24 para. 3, 4 and 5 DTI) which have their own specific allowable rates as follows:

1. Construction of, or the costs of acquisition of, costs of improvement, restoration or rebuilding of tangible assets. The annual allowable rate of depreciation is 5% of the cost price. Examples: of such assets include industrial buildings themselves plus equipment which forms part of the building such as elevators, light fittings, air-conditioning and conveyors where these are built into the fabric;
2. Development or costs of acquisition, costs of improvement, restoration or rebuilding of the intangible assets, which includes goodwill acquired from a third party. Annual rate of depreciation is 10% of the cost price. The assets thus will be entirely depreciated in ten (10) years. Example: Goodwill, concessions, patents, licences, etc.;
3. Computers and their accessories, information systems and communication. Annual rate of depreciation: 50% of the carried forward balance of the asset net of depreciation. An IT system costing Rwf20m will be valued at 2% of its cost price by year 6
4. Other assets of the company: 25% of the carried forward balance of the asset net of depreciation. Examples: machine tools, work benches, seed cleaners etc. motor

vehicles, furniture, etc. That is the assets are depreciated on a reducing balance basis; by year 9 the WDV will be 2.5% of cost – cf IT equipment

Not only is depreciation is calculated in two different ways according to whether the asset falls into the first two, or the last two, categories described but:

- For the first two categories (depreciation of 5% and 10% of the cost price), depreciation is calculated individually, asset by asset, and is based on the original cost i.e. straight-line basis. Additions are simply treated at cost and sales are set against the relevant individual asset.
- For the second two categories (50% and 25% rates of depreciation), depreciation is not calculated by individual asset, but by total pool category *(article 24 of DTI)*; And the depreciation is calculated on the depreciated value at the beginning of the year (NBV – *net book value* or WDV – *written down value*) brought forward i.e. on a Reducing Balance basis.
- For the "pooled" assets, additions are added to or sales are subtracted from the pool value at the beginning of the year – Art 25 DTI).
- For all categories, due allowance must be made where due to abnormal occurrences, assets are damaged or devalued.

However, for the four (4) categories of allowable assets, when a used and depreciated asset (either completely or partially depreciated) forms part of a business acquired by a taxpayer, then annual instalments of depreciation are calculated on the price at acquisition (if in the first two categories) or on the depreciated value ('net book value') of the asset at the date of acquisition if in the last two categories.

It is important to categorise the assets correctly and ensure that the depreciation is correctly calculated.

It should be noted that if the depreciated value of the assets at the beginning of a year (the depreciation base) does not exceed 500,000 Rwf, the full amount constitutes a deductible running cost (art.25 of the DTI).

Finally, if the net book value is negative (as would be the case for example if the selling price of certain assets of the category are higher than the cost price of all the assets in the category of costs), this net amount is treated as a gain and is added to profits and the assets base valuation amount becomes nil (art 25 al.2 DTI).

Example:
Joe starts a business manufacturing chairs. The factory cost Rwf 270 million, the 2 lathes cost Rwf45 million each and are supported by a Computer Aided Design (CAD) computer which cost Rwf50,000,000 including cabling and equipment to link the CAD computer to the Computer Numerically Controlled (CNC) lathes.
The rest of the factory equipment – benches and other tools - cost 45,000,000 and there is a small admin team and their computers and printer cost 50,000,000 including software and their office furniture cost 20,000,000.
Total investment cost Rwf 525 m
Company policy is to depreciate an asset over its useful life using the straight-line method:
Factory – 20 years

Lathes – 10 years
Computers and associated equipment - CAD and office – 3 years
Benches and all other tools - 10 years
Office furniture – 10 years

		Factory	Lathes	CAD	Benches etc	Office Computers	Office furniture
Cost	Rwf '000	270,000	90,000	50,000	45,000	50,000	20,000
Life years		20	10	3	10	3	10
Annual Depreciation per company Straight line basis		13,500	9,000	16,667	4,500	16,667	2,000
Rate % per RRA		0.05	0.25	0.5	0.25	0.5	0.25
Depreciation in first year		13,500	22,500	25,000	11,250	25,000	5,000
Value to which Depreciation is to be applied next year							
Per company policy straight-line basis uses		270,000	90,000	50,000	45,000	50,000	20,000
Per RRA Cat 1 Dep'n based on Cost		270,000					
Cat 2 - computer equipment WDV				25,000		25,000	
Cat 3 all other tools and equipment WDV			81,000		40,500		18,000
Difference RRA minus Company policy		0	13,500	8,333	6,750	8,333	3,000
Adjustment to be deducted from Business Profits							39,917

The total business depreciation in year 1 is Rwf62,333 thousands, whereas the RRA would calculate taxable profits where depreciation summed to Rwf102,250 thousands. The adjustment to Line 75 of CIT Real Regime Calculator *(see Appendix 1)* would be +39,917,000

For the pooled assets, the RRA method uses the WDV approach and so the life of an asset is not fixed as the straight-line method is. 10% per year straight-line = 10 years
25% per year of WDV means that pooled assets costing 2,000,000 new are written down to 1,500,000 at the start of year 2 and Rwf1,125,000 at the start of year 3 and so on. In fact in year 6 the opening valuation is less than Rwf500,000 and so the whole pool would be expensed to SoCI

c. Investment allowance

Where the business is a registered investor and is able to take advantage of the investment allowance, the profits in year 1 would be dramatically different. But this is also the year when start-up costs are expected to be greatest and so the chances of profits slimmer.

According to paragraph 26 of the DTI, an investment allowance of forty percent (40%) of the amount invested in new or used assets may be depreciated excluding motor vehicles that carry less than eight (8) persons, except those exclusively used in a tourist business. This amount is deductible for a registered investor in the first tax period following the purchase and/or of use of such assets if:

1. the amount of business assets invested is equal to thirty million (30,000,000) Rwandan francs; and
2. the business assets are retained for at least three (3) tax periods after the tax period in which the investment allowance was taken into consideration.

The investment allowance becomes fifty per cent (50%) if the registered business is located outside Kigali or falls within the priority sectors as described by the Investment Code of Rwanda.

The investment allowance effectively increases the depreciation charge to business profits and for pooled assets, reduces the value of these assets carried in subsequent years. – next year's depreciation for pooled assets is calculated against the written down value as at the 1st of the period plus the cost of any acquisitions made in the period.

If the business asset that is granted an investment allowance is disposed of before the end of the period mentioned in the above point 2, the reduction of income tax stemming from the investment allowance must be paid back to the Tax Administration unless such an asset is destroyed by natural calamities or other involuntary conversion. The repayment amount is calculated back to the acquisition date of the relevant asset.

To be eligible for the Investment Allowance, the following conditions must be fulfilled:

- It is necessary to be a recognised and registered investor;
- The acquired asset cannot be a vehicle capable of transporting less than eight (8) passengers unless it is used solely for tourist business;
- The amount invested must be at least 30 million francs;
- The assets must be held for at least three (3) fiscal years from the time that the provision for investment was taken into account;

For ease of book-keeping and to make year-end work much easier perhaps the entity should adopt the RRA depreciation rates and then there would be no need to make adjustments.

But, and this is a big BUT, the business profits for management Account purposes in any one period could be markedly affected and thus the ratios such as Return on Capital Employed, RoI, ratios which are most important for the investor, would be affected. Calculations such as WACC could become invalid and these inaccuracies could in turn lead to incorrect investment decisions.

When making decisions to select asset lives and how to depreciate assets, the implications must be carefully assessed before going ahead. Once a specific accounting policy has been properly adopted, changes in later years can affect the accounts and reports for "prior" years.

d. Expenses for training and research

Art. 27 DTI prescribes that expenses of training and research during a fiscal year are deductible expenses.

All Training and Research expenses incurred which promote business activities during a tax period are considered as deductible from taxable profits in accordance with provisions of Article 21 of this law.

Such expenses, when they are incurred as part of process to purchase of land, buildings and other immovable properties including renovation or reconstruction as well as exploration expenses and other assets, are considered as part of the capital cost and will be added to the cost of the asset.

To understand this concept more clearly, it is necessary to refer to relevant "*International Accounting Standards"* (IAS). In IAS 9 regarding "activities of research and development" (August 1991), the IAS established a distinction between:

- *Research*: this relates to original research undertaken in order to acquire original scientific and technical knowledge;
- *Development*: this relates to the translation of the results of research into a plan of production of materials, apparatus, products, processes, systems and services new or substantially new before the commencement of production or commercial exploitation.

Commentators have opined that, by expenses of research, the law wanted also to include the expenses of development because the two expenditures are often part of the same aim or project. See IAS on R&D and the way these costs are treated in the books of accounts

e. Bad debts

The deduction of bad debts is allowed for tax purposes but a bad debt is regarded as irrecoverable only if the loss has acquired a final and irreversible nature during the fiscal period. Exactly when a bad debt becomes irrecoverable is an issue of fact and the final decision lies with the tax department, but the business must have good evidence that the debt is not recoverable.

To be considered irrecoverable the bad debt must meet certain conditions in order to be fiscally deductible (article 28DTI):

- This bad debt has been previously included before in the income of the taxpayer;
- The bad debt has then been cancelled for accountancy purposes;
- The taxpayer has taken all reasonable steps to recover the debt and has conclusive evidence confirming the insolvency of their debtor or other proof of inability to pay.

f. Recoverable losses

As its name indicates, income tax relates to profits earned by a taxpayer. However a taxpayer may not generate profits during a fiscal year. He/she can also incur losses. In this case, not only does the taxpayer avoid a tax liability during the fiscal year, he/she also has the right to carry forward this loss to the next year, so that profits in year 2 can be reduced by the loss incurred in the year before – up to five years before.

Article 29: Loss Carried Forward
If the determination of business profit results in a loss in a tax period, the loss may be deducted from the business profit in the next five (5) tax periods, earlier losses being deducted before later losses.

However: per Article 20 of Law 16/2005 (DTI) "A loss in tax period in which a long-term contract is completed may be carried back and offset against previously taxed business profit from that contract to the extent it cannot be absorbed by business profit in the tax period of completion

However, losses incurred overseas cannot be offset against any profits of Rwandan origin during the same fiscal year, or against any future or previous profits of Rwandan origin.

Article 29 Para 3 (DTI) If during a tax period, the direct and indirect ownership of the share capital or the voting rights of a company, whose shares are not traded on a recognized stock exchange changes more than twenty five per cent (25%) by value or by number, paragraph one of this Article ceases to apply to losses incurred by that company in the tax period and previous tax periods.

Article 20: Long-term contract
The timing of inclusion in and deduction from business profit relating to a long-term contract is accounted for on the basis of the percentage of the contract completed during any tax period.

The percentage of completion is determined by comparing the total expenses allocated to the contract and incurred before the end of the tax period with the estimated total contract expenses including any variations of fluctuations.

a. Long-term contracts

Within the meaning of the law, a long-term contract is a contract for manufacture, installation or construction, or the provision of services relating to these activities, which is not completed during the fiscal year in which it began. This excludes any contracts whose completion was at the outset envisaged to be within twelve (12) months of commencement (art.20 DTI).

For these contracts, the following rules apply:

- Business profit relating to a long-term contract is accounted for on the basis of the percentage of the contract completed during any tax period. As per ISA standard IAS 11, the percentage of profit is calculated from the percentage of completed and takes into account estimation future costs. Effectively, if the estimated final cost is expected to be greater than the sale value, then 100% of the loss to date is taken to the SoCI.
- Para 3 allows that where a long term contract subsequently makes a loss where previously a profit was anticipated and duly assessed, the realised loss can be offset against the previously taxed profit of that contract. Where the overall

business profit is insufficient to cover the loss, the loss can be set against the profits attributed to that contract in previous years.

A is performing a long-term contract which started in Jan 2010 and expected to last until 2012. At the end of 2010, completion so far was calculated as 25% and the final sale at Rwf1,000,000,000 and expected profit was 10%, Rwf100,000,000. Rwf25,000,000 would have been assessed at 30% payable to RRA.
At the end of 2011 the valuations were 70% complete and profit was expected to be 7.5% of the sale value which was now 1,200,000,000.
Profit assessable for tax = 7.5% x 1,200,000,000 x 70% = 63,000,000
at 30% = 18,900,000 less 30% x 25,000,000 charged in 2010.
If in 2012 the contract is completed as forecast in 2011, the tax charge for 2012 would be:
7.5% x 1,200m x 30% = Rwf27m less tax charged in 2010 and 2011

But suppose the contract finally made a loss of Rwf20,000,000 and the remaining business profits were not sufficient to cover this sum, the profits of the previous years could be adjusted by readjusting the profit of the long-term contract from Rwf63m to Rwf 43m. In this way tax due in respect of the previous year could be adjusted downwards and a refund added to the calculation for the current year.

Readjusted tax for 2011: 30% of Rwf43m = Rwf12.9.
Tax paid in 2011 was Rwf 11.4 m. Tax refund = Rwf1.5m

b. Agricultural and breeding activities

The tax law exempts from tax the income arising from agricultural and breeding activities if annual turnover does not exceed twelve million (12.000.000 Rwf) Rwandan francs during a fiscal year (Article 18 DTI).

This measure is intended to take into account the significance of these activities in the Rwandan economy reality where more than 90% of the population relies on subsistence agriculture with the sale to local markets of any surplus from their harvests. However, when the value of such sales exceeds the amount indicated, the law takes the view that the related agricultural activity is no longer one of subsistence. Therefore, the income of these activities will be taxed.
If the business profits are less than 20,000,000 francs i.e. the business is “small” (Article 2 of DTI) then the tax assessed could be a lump sum of 4% of turnover.

The law is not specific regarding produce taken from the farm into the home, but the wording refers to turnover and so it might be assumed that the turnover is that portion of output which is sold in a market and not used in the home.

C Assessment of tax

1. Business size = i.e. Turnover

Where a business falls within the category described in Article 2 section 6º DTI) and the annual turnover is less than 20,000,000 francs business tax can be levied at 4% of turnover (Article 11 – 2 of DTI). It also applies to other taxpayers who may have elected to adopt this mode of taxation.

However, these small businesses can choose to be taxed on their actual profits according to a simplified accounting method determined by Ministerial decree (Article 17 DTI).

Suppose that your turnover is 19,000,000, and you elected not to prepare accounts or complete a tax return you would declare and pay tax at 4% of Rwf19 million. This would be Rwf760,000

Grossed up at 30% this would be equivalent to a taxable profit of Rwf2,533,333 or a profits to sales ratio of 13.3%

If your profits were say 10% it might pay to do the accounting:

Example:

Fred runs a business. He is the sole "employee":

	SoCI	SoCI	SoCI
	Rwf	Rwf	Rwf
Sales (T/O)	19,500,000	19,500,000	19,500,000
Cost of sales	17,550,000	16,900,000	15,000,000
Profit assessable to tax	1,950,000	2,600,000	4,500,000
Tax at 30%	585,000	780,000	1,350,000
Profits available for distribution	1,365,000	1,820,000	3,150,000
Profit % sales	10.00	13.33	23.08
Tax at 4% of turnover	780,000	780,000	780,000
Advantage of 4% tax	(195,000)	-	570,000
i.e. + means more to spend			

A profit of 13.3% of sales is the point at which the 4% on T/O is the same as 30% on profits.

A return on sales of less than this means that doing the accounts and preparing a proper return might pay off – how much will be spent doing the accounts?

On the other hand, greater profits would make the 4% turnover tax more attractive.

In the example above, Fred's business at 4% would attract tax of Rwf780,000 and this is much lower the 30% tax bill if his assessable profits were Rwf4,500,000

If a business is profitable, and the turnover is less than Rwf20 million per year, it is unlikely that the 4% tax on turnover would be disadvantageous.

An after tax profit of Rwf780,000 is really not very much for a business and not one to aim for simply to justify preparing accounts to reduce one's tax bill.

Also, you have to bear in mind that the business is operated by Fred alone and if he paid himself a salary of Rwf 8,000,000 (included in the costs above) then PAYE income tax would be payable:

			Rwf
0 –	360,000	Nil	
next	840,000	20%	168,000
balance	6,800,000	30%	2,040,000
			2,208,000

So in the end, Fred has 8,942,000 to spend in the year assuming PBIT of Rwf 4,500,000

and he has paid a combined tax bill of 3,556,500 or tax at 18% of turnover.

2. Tax on actual profits

This type of taxation automatically applies to taxpayers whose annual sales turnover is equal to, or higher than, 20 million Rwandan francs per fiscal year. The taxable amount is not in this instance the sales turnover but the profit earned.
As is the case for income tax on employment, the assessed income is rounded down to the nearest thousand RwF (Article 41 DTI). Whilst Article 11 says "rounded to the nearest thousand", Article 41 says "rounded down to the nearest thousand"

Declaration and payment of tax

Whilst an annual return must be completed and filed with the tax authorities before the 30th day of the March after the end of a fiscal period (or the 30th day of the 3rd month where the fiscal period does not end 31 December) it is also important to remember that a business either as an individual or company must pay each quarter a 25% portion of what was paid in tax for the previous year. This will become the prepayment for the current year.

If the taxpayer began his activities during the preceding fiscal year, the quarterly instalment is equal to twenty five percent (25%) of the amount of the tax due arising in the preceding fiscal year, adjusted by dividing by the number of months during which the taxpayer undertook his activities during this preceding period and multiplying by twelve (12).

Suppose Fred's business is being considered:
He made taxable income from his business of Rwf4,500,000 last year and so his quarterly payments this year will be ¼ of 30% of Rwf1,350,000 i.e.Rwf337,500.

His salary was Rwf8m and suppose the business pays him the same this year, his monthly salary will be Rwf666,667 and he will pay by the 15th of the month following the tax due plus the CSR(RSSB) payments.

Monthly salary	666,667
PAYE income tax	184,000
CSR - employer's contribution at 5%	33,333
CSR employee's contribution at 3%	20,000

	Salary	Tax due
Taxed at nil	30,000	-
Taxed at 20%	70,000	14,000
Taxed at 30% - all above 100,000	566,667	170,000
	666,667	184,000

By the 15th day of each month Fred's business will remit to RRA, Rwf237,333 being the tax due plus both the CSR contributions.

Of course the net monthly salary that Fred actual receives will be after tax and the CSR 3% deduction namely Rwf462,667. The 5% contribution is an expense to the business.

D. Import Duties and withholding tax

The table from RRA shows:

Product	**Rwanda**	**EAC**
Raw Materials	0%	0%
Capital	0%	0%
Intermediate	15%	10%
Finished	30%	25%

The RRA Customs tariff also states that some food product intermediaries are variable at 0% or 5%. The EAC tariff is not yet finalised. Certain items are subject to

Vehicles are subject to more specific rates depending on engine size, and certain beverages and other items such as tobacco ready for consumption are subject to consumption tax as well.

Certain importations require that the importing agent in Rwanda pay to RRA 15% of the value of the item before it is released to the buyer. In addition to the above, certain operations are the subject to a deduction at source – withholding tax. These are imports and payments by public institutions in relation to public tender/service contracts. (Article 52 para. 1 and 2 DTI):

- An advance calculated as five percent (5%) of the cost of the imported goods, including Cost Insurance and Freight (known as CIF) when regular commercial practices are applied to transactions involving these goods. A withholding tax of three percent (3%) on the sum of invoice, excluding value added tax, is retained on payments by public institutions to the winner of public tenders

.

However such deductions at source do not apply to the taxpayers who are in one of the two (2) following categories (article 52 para. 3 DTI):

- Taxpayers whose business profits are exempt from taxation;
- The taxpayers who have a tax clearance certificate and this is granted annually by the Commissioner General of the RRA. This final tax scheme applies only to "good taxpayers" i.e. those with a good tax track record such as timely submission of tax declarations, prompt payments of tax liabilities and those who do not have tax arrears.

E Tax on investment incomes

Tax base

As far as investment income is concerned, the tax law aims to tax any payment received in cash or in kind by an individual in the form of interest, dividends, royalties or rent and which was not taxed as a business profit (art.32 DTI – *Income from Investments*). In other words, any income from investments received by commercial companies will not be subject to withholding tax if the quarterly tax calculations include this income. (Section 3 Article 31 DTI).

Income in the form of interest includes any income arising from loans, deposits, guarantees and current accounts. It also includes income from government securities, income from bonds, and negotiable securities issued by public and private companies and income from cash bonds

Dividend income, as mentioned in the Law No 16/2005 on Direct Taxes on Income, is subject to a flat tax of fifteen percent (15%).
If dividend distribution was subjected to withholding tax as stipulated in the law, the taxpayer does not pay tax on income.
Dividend income includes income from shares and similar income distributed by companies and other entities.
In the determination of business profits of a resident company, dividends and other profit-shares received from a resident entity are exempt.
The profits which pay dividends have been taxed at 30% before the dividend is deducted. One could thus argue that the dividends have already been subjected to tax.

Income in the form of dividends includes income arising from shares and participation in the profits in any type of company as well as similar incomes distributed by any entity enumerated by article 38 of the law. Withholding tax is 15%

The term "**royalty income’** includes all payments of any kind received as a payment for the use of, or the right to use, any copyright of literary, craftsmanship or scientific work including cinematograph films, films, or tapes used for radio or television broadcasting. The term also includes any payment received from using a trademark, design or model, computer application secret formula or process. It also includes the price of using, or of the right to use, industrial, commercial or scientific equipment or for information concerning industrial, commercial or scientific knowledge. Royalty income also includes payments for natural resource payments. Again tax is 15% flat rate

Rental income: All revenues derived from rent of machinery and other equipment and land including livestock in Rwanda, are included in taxable income, reduced by:

a) ten per cent (10%) of gross revenue as deemed expense;
b) interest paid on loans;

c) depreciation expenses as determined according to Article 24of the DTI. Income derived from the rent of buildings or houses incorporated as assets mentioned in Article 38 of this law is subject to corporate income tax and is exempted from rental income tax.

Rental incomes arising from houses and buildings incorporate as assets of qualifying entities (Art 38) are subject to corporation income tax and are exempted from rental income tax. (Article 36 DTI).

Finally, it should be noted that some incomes can be compared to investment income as they are deducted at source using a rate identical to that used on investment income. These incomes include any profits from the lottery or any another games of chance (art. 51 DTI).
And yet more finally, lottery and gambling winnings are also subject to withholding tax at 15% and this deducted at source.
All withholding tax agents must complete returns and payments within 15 days of the period end,.

F Payment of tax

The rate of income tax applied to investments is not applied on a progressive basis as is the case for the majority of income tax payments described above. They are instead applied using a proportional rate which is fixed at fifteen percent (15%) of the assessed incomes (Article 33 parag.1 DTI).

“A withholding tax of fifteen percent (15%) is levied on the following payments made by resident individuals or resident entities including tax-exempt entities:

These incomes are any dividends, except those paid between companies, any interest paid on deposits, royalties, payments for performance by musicians, artist sportsperson and the profits of lotteries and other games of chance which have a monetary value (Article 51 DTI). The payments are subject to tax even when paid by or through an entity not resident in Rwanda
For other investment incomes (interest other than that paid on money deposits, or rental incomes, other than those on houses and buildings and received by physical persons) the recipient will have to submit an annual declaration and to pay tax at a proportional rate of 15% by, at the latest, the 30th day of the sixth month of the following fiscal year (Article 12 DTI).

Chapter 2
Income Tax on Companies

Contents

A. TAXPAYERS CONCERNED

The tax law which applies to Business Entities and individuals who are not employees also applies to companies. But companies and similar organisations as described in Article 38 DTI are subject to additional regulations.:
According to article 38, the following entities shall be subject to corporate income tax:

1. Companies established in accordance with Rwandan or foreign law;
2. Cooperative societies and their branches;
3. Public business enterprises;
4. Partnerships;
5. Entities established by Districts and the City of Kigali, to the extent that these entities are involved in business activities;
6. De facto companies or associations and any other entities that perform business activities, and are established for the purpose of making profits.

.

But much of what applies to companies is also defined in Articles 1 to 36 which apply to companies as well as individuals who are tradesmen or members of the professions.
Articles 37 et seq apply to businesses registered as companies or who are covered by Article 38 – referred above

Tax residence

Unless specifically stated otherwise (see above), a commercial company is taxable in Rwanda only if it has a tax residence here. Such an entity is regarded as resident in Rwanda if, during a fiscal year (Article 3 para. 3 DTI):

- If it is established in accordance with Rwandan legislation even if the company does not have its effective management in Rwanda;
- The entity is effectively directed from Rwanda at any time during the fiscal year even if it is established in accordance with foreign legislation;
- The entity is a state-owned Rwandan company.

However, commercial companies which do not meet these conditions will be liable to tax only on their profits arising from a permanent establishment in Rwanda (Article 40 para. 2 DTI). A double taxation situation is avoided by a system of tax credits and double taxation relief agreements (see above). It is important to remember that even where an official Double Taxation Agreement does not exist, tax paid in another country should be taken into account when assessing tax due in Rwanda. Where tax paid in the other country is higher than paid in Rwanda does not mean that an allowance will be given iN Rwanda. The same would happen to a Rwandan business operating in the UK.

B. TAX BASE

Principles

All income less deductible expenses is subject to Corporate Income Tax.
Article 37 establishes the Corporate income tax and Article 41 of DTI establishes the rate to be 30%.

Exemptions

Dividends paid between companies

Art. 45 DTI exempts taxable profits, any dividends or participations in the received profits of a resident company. The reason for this measure is that, as far as the company making the distribution is concerned, dividends have already been taxed in the form of income tax collected from the entity as they are not deductible expenses.

Gains arising on the reorganizations of companies

As far as a reorganization is concerned, the law aims to address several situations (Article 46 DTI):

- The amalgamation of at least two resident companies;
- The acquisition of at least fifty percent (50%) of the shares or voting rights, by number or value, of a resident company, in exchange for shares in the acquiring company;
- The division ("scission") of a resident company into at least two resident companies.

In case of reorganization of companies, the transferring company is exempt from tax in respect of capital gains or losses realized on reorganization. The receiving company values the assets and liabilities involved at their book value as stated by the transferring company at the time of reorganization. The receiving company depreciates the business assets according to the rules that would have applied to the transferring company as if the reorganization had not taken place.
In case of reorganization, the receiving company is entitled to carry over the reserves and provisions in the books of the transferring company, subject to the conditions that would have applied to the transferring company as if the reorganization had not taken place. The receiving company assumes the rights and obligations of the transferring company in respect of such reserves and provisions.

C. ASSESSMENT AND ALLOWANCES

1. Principle

Once the taxable profit is established by the taxpayer, it must be rounded down to the nearest thousand Rwf (Article 41 DTI).

The rate of the tax is fixed at thirty percent (30%) of taxable profit.

2. Reduction of the rate of the tax through investment promotion and incentives.

a) Companies with large numbers of employees

In order to promote investment and to encourage the companies to engage employees, the tax law has outlined tax incentives but only for approved investors. In practice, this takes the form of a discount of the rate of tax applied as the number of employees increases (Article 41 para. 3 DTI).

- If the company employs between one hundred (100) and two hundred (200) Rwandans, the rate of tax will be reduced by two percent (2%);
- If the company employs between two hundred and one (201) and four hundred (400) Rwandans, the rate of tax will be reduced by five percent (5%);
- If the company employs between four hundred and one (401) and nine hundred (900) Rwandans, the rate of tax will be reduced by six percent (6%);
- If the company employs beyond nine hundred (900) Rwandans, the rate of tax will be reduced by seven percent (7%).

However, the employees to be taken into account are those where:

- the business is their prime employer – i.e. the tax deducted is not simply 30% withholding tax which would happen where the person works for several employers (see Articles 48 and 50 DTI)
- the employees are paying income tax – their pay is greater than Rwf 30,000 per month
- the employees are employed for at least 6 months during the fiscal year (art. 41 *in fine* DTI).

This provision obviously aims at encouraging companies to hire better-paid Rwandan employees.

b) Exporting companies

A discount in the rate of the tax is also in place for companies which operate in export fields in order to encourage them to continue to play a positive role for the growth and development of the Rwandan economy. This exemption is based on sales turnover generated by export activities (art.42 para. 1 and 2 DTI):

- If export activities generate between three million US dollars ($3,000,000) and five million dollars ($5,000,000) for Rwanda, the rate of the tax will be discounted by three percent (3%);

- If export activities generate more than five million dollars (5 000 000 $) for Rwanda, the rate of tax discount will be five percent (5%).

At an exchange rate of Rwf 600 to 1 USD, 3 million USD are the same as Rwf1.8 billion

It should be noted that the reductions in the rate of tax for exports cumulate with the reductions of the rate of tax for occupation of workers.

c) Declaration and payment of the tax

Art. 43 DTI which regulates the tax declaration and the modes of payment of the tax on the profits of companies are almost identical to article 12DTI, its counterpart for income tax.
Therefore, the applicable rules for the declaration and the payment of the income tax apply *mutatis-mutandis* for the declaration and the payment of the income tax of companies.

BLANK

Chapter 3
Value Added Tax

Contents

A. CHARACTERISTICS AND MECHANISM

Characteristics of VAT

The characteristics of VAT are as follows:

- VAT is a tax on Sales which constitutes a tax on the expenditure paid by the ultimate consumer since it concerns a general tax on products and services. Value Added Tax is calculated on the costs excluding VAT (input VAT). The “added” element comes from the fact that a purchaser who also sells, pays to the RRA the tax invoiced out (output tax) less the input tax. I.e he pays only VAT which relates to the difference between the sales less the goods purchased to start with.
- VAT is *a tax collected by split payments* which is received each time a chargeable commercial transaction is made. It is not a tax on production which would be due from just one intermediary in the chain;
- VAT is *a neutral tax*. Except in some rare cases, a person who is not the ultimate consumer recovers the whole of the VAT which has been invoiced to him by suppliers. The tax is consequently not an element of the cost price and the length of the chain of production does not impact on the amount of the tax due. This tax is supported entirely by the ultimate consumer;
- VAT is *a transparent tax.* It is possible, at each stage of the marketing of a product, to determine the amount excluding VAT and the amount of the VAT included. Indeed, if one knows the price excluding VAT of a good or of a service (PEVAT) one can calculate the amount of the VAT included as well as the VAT inclusive price (PVATI) by the following formula: PVATI = PEVAT + (PEVAT x VAT rate).
- VAT is embodied in the Law No. 06/2001 of 20/01/2001 and in referred to here as LVAT

Mechanisms of VAT

The taxable person, unless exempted (for this concept, see above), effectively plays the role of *tax collector*, i.e. they invoice the tax to their customer and they pay it to the tax administration after deduction of the VAT which is paid by them to their own suppliers.

Example: Working hypothesis: single rate of VAT with 10%.

Operations	PHTVA	VAT	VAT paid to the RRA
A producer sells sugar to a wholesaler	100	100x10% = 10	**10**
The wholesaler resells them with a local wholesale dealer.	200	200 X 10% = 20	20-10 = **10**
The local wholesale dealer resells sugar with a retailer	300	300 X 10% = 30	30-20=**10**
The retailer sells to a consumer	400 plus VAT	400X10%=40	40-30=**10**
TOTAL VAT PAID			40

Let us take again an example with the same producer price (100) and the same price to the end consumer (400 plus VAT) but with fewer intermediaries:

Operations	PHTVA	VAT	VAT paid to RRA
A producer sells sugar to a wholesaler	100	100x10% = 10	**10**
The wholesaler resells them with a retailer	300	300 X 10% = 30	30-10=20
The retailer sells to a consumer	400 plus VAT	400 X 10% = 40	40-30=10
TOTAL VAT PAID			40

It will be noted that the number of transactions has no impact on the amount of tax finally paid to the Tax Administration since in the two examples, the VAT to be paid to RRA (40) corresponds exactly to the rate of the VAT (10%) applied on the price paid by the ultimate consumer (400), even though the number of intermediaries is different in each case.

B. CSUMMARY OF LAW(S)

Concepts

Art 12. 1 of Law Number 06/2001 (dated 20th January 2001) relating to the introduction of VAT states that supplies of goods and provisions of services carried out subject to payment by a taxable person acting in that capacity are regarded as being chargeable.

This article was supplemented by the provisions of article 10 of the Ministerial Order Number 001 (dated 13th January 2003), relating to procedures concerning the imposition of VAT. These specify that a taxable person is: "anybody who carries on a chargeable activity in Rwanda…".

However, it is necessary to distinguish two (2) categories of taxable people (art.10 of Law Number 25/2005 (dated 4th December 2005) which deals with the creation of tax procedures, namely;

Any person who undertook a chargeable activity in the preceding fiscal year exceeding twenty million francs (20.000.000 RwF), or five million Rwandan francs (5.000.000 RwF) in the previous quarter, is required to register and submit a VAT return to the Tax authorities within seven (7) days of the end of the period.

Any person who is not required to register for VAT can do so voluntarily. The law here aims at any supplier who does not meet any of the two conditions mentioned above. §2. Consequences of the constraint.

A person who does not need to register and is not registered will invoice his customers with no VAT added; but he cannot reclaim the VAT which his suppliers invoice to him. The advantage of a lower sales price must be offset against the non-recoverable input tax.

<u>Example - All sellers are registered</u>

	Sugar producer	Processor	Wholesaler	Retailer
Inputs = Costs of production	50	118	236	354
Recoverable Input VAT		18	36	54
Margin	50	100	100	100
Sale	100	200	300	400
VAT %	18%	18%	18%	18%
Output VAT	18	36	54	72
Total invoice	118	236	354	472
Paid to RRA	18	18	18	18
Margin	50	100	100	100

The final consumer pays Rwf472 and unless he sells on and is registered he cannot reclaim the “input” VAT.

Example - All sellers are registered except the final

				Not registered
Inputs = Costs of production	50	118	236	354
Recoverable Input VAT		18	36	
Margin	50	100	100	100
Sale	**100**	**200**	**300**	**454**
VAT %	18%	18%	18%	
Output VAT	18	36	54	-
Total invoice	118	236	354	454
Paid to RRA	18	18	18	
Margin	50	100	100	100

The final consumer pays Rwf454

To obtain the same margin as in the example (1) where all the businesses are registered, the last in the chain in example 2 has to charge not quite as much as the final registered supplier, but considerably more than the Rwf400 before VAT.

Example - The final supply is **zero rated** - supply to in-flight stores or export

	Food producer	Processor	Wholesaler / Distributor	Supplier to Airline / Overseas customer
Inputs = Costs of production	50	118	236	354
Recoverable Input VAT		18	36	54
Margin	50	100	100	100
Sale	**100**	**200**	**300**	**400**
VAT %	18%	18%	18%	0%
Output VAT	18	36	54	-
Total invoice	118	236	354	400
Paid to / (Reclaimed from) RRA	18	18	18	(54)
Margin	50	100	100	100

Note that as the final supply is zero rated, the Input VAT can be reclaimed, but there is no Output VAT.

In the situation where some supplies are exempt and some subject to VAT, the supplier must relate input VAT to one or other category. Input VAT related to exempt supplies cannot be offset against any output VAT.

Suppose the registered business is selling transport and only a proportion of the services involve public transport in “bus or coach licensed …and having a seating capacity for fourteen or more adult persons” (Article 86 5 (b) LVAT). These are exempt supplies and the supply invoice carries no VAT where the inputs may well carry VAT., The other transport services will be subject to VAT.
Only the input VAT relating to non-exempt supplies can be reclaimed from RRA.
In circumstances of mixed supply and where the inputs cannot be easily allocated to either exempt or non-exempt outputs, the un-attributable supply is apportioned usually on the basis of sales of exempt supply as a percentage of total supplies. It is important that any such apportionment should be agreed with Commissioner General of RRA – see Article 42 (b) LVAT

C Responsibilities and obligations

Any registered person who carries out deliveries of goods or provisions of services must invoice the price with the VAT added and showing the VAT. And insofar as its operations are subject to VAT, the taxable person can deduct from the payment to the RRA the VAT for which they have been invoiced. Moreover, it is required to pay the tax charged to the public treasury.

In addition the taxable person also has a series of obligations concerning accounting for VAT: these include rules on bookkeeping, retention of invoices etc. (Article 14 25/2005 on Tax procedures).

LVAT refers to Law 06/2001 of 20/01/2001 on the code of Value Added tax

Taxable operations

1. Supply of goods

"Consideration" in relation to a supply or import, means the total amount in money or its equivalent paid or payable for the supply or import by any person, directly or indirectly. It includes any duties, levies, fees, or charges paid or payable on, or by reason of, the supply or import, other than value added tax, reduced by any price discounts or rebates for prompt payment, allowed and accounted for at the time of supply or import (Article 85.6 LVAT).

"Goods" means tangible movable property, buildings and other real property developments, and items treated as goods under this Law, but does not include money; (art 85.8 LVAT).
For purposes of the application of the VAT, intangible goods such as a service, gas or electricity are treated in the same way as tangible or movable property.

2. Provision of services

Provisions of services may be defined as all the operations which do not require a transfer of property but which are made with a counterpart including leases, hire or the transfer of a right or interest. It should nevertheless be specified that the provisions of services made by an employed person or a government official are not taxable operations as far as VAT is concerned.

3. Imports

Imports can be either a supply of goods or a provision of services. The import of goods refers to goods coming into Rwanda from a foreign country. It relates to a provision of services if it is carried out under one of the following two (2) conditions (Article 85.10 of the LVAT):

- The service provider is a non-resident;
- The person receiving benefits of the services is a resident in the ordinary sense of a business carried on outside Rwanda but the services are supplied for use or consumption in Rwanda.

D Exempted and Zero rated businesses

VAT Exemption

Art. 86 of the LVAT describes a series of operations which are exempted from VAT. These operations give place neither to VAT invoicing, nor VAT declaration or recording for the taxable people who carry them out. However, by the same token they do not have the right to deduct any VAT that they pay on the goods and services that they purchase.

As modified and completed by article one of Law Number 29/2010 (dated 30th June 2010), "Notwithstanding the powers vested in the Minister by the provisions of Article 15 of this Law, the following goods and services are exempted from Value Added Tax":

1 Water supply services:
   a) the main supply of clean water;
   b) sewerage treatment services to protect the environment for non-profit motives.

2 Goods and services for health purposes:
   a) the supply of health and medical services;
   b) articles designed for persons with disabilities;
   c) the supply of equipment and drugs to hospitals and health centres;
   d) the supply or importation of drugs and medical equipment made by authorized persons for medical use, to patients and persons with disabilities

Bodies eligible for exemption under point 2 (b) shall be those recognised by the laws of Rwanda as public institutions, social organisations and any other form of voluntary or charitable institution.

3 Educational materials and services:
   a) educational services provided to pre-primary, primary and secondary students;

b) educational services provided by social organizations to students and other youths, with the aim of promoting the social, intellectual and spiritual development of the members for non-profit purposes;
c) educational services provided to vocational and other higher learning institutions;
d) educational materials supplied directly to learning institutions.

Eligible bodies for the purposes of this exemption shall be those recognised by the laws as public institutions, not for profit social organisations and any other form of voluntary or charitable institutions.

4 Books, newspapers, journals and other electronic equipment used as educational materials.

5 Transport services:

a) transportation of persons by road in busses and coaches licensed under the law governing the transport vehicles with a seating capacity for fourteen (14) persons or more;
b) transportation of persons by air;
c) transportation of persons by railway;
d) transportation of persons or goods by boat;
e) transport of goods by road**.**

6 Lending, lease and sale :

a) the sale or lease of an interest in land;
b) the sale of a building or part of a building, flat or tenement meant for residential purposes;
c) the renting of, or other grant of the right to use, accommodation in a building used-predominantly as a place of residence of any person and his family, if the period of accommodation for a continuous term exceeds 90 days, unless the building is meant for accommodation.

7 Financial and Insurance Services:

a) the premiums charged on the provision of life and medical insurance services;
b) fees charged on the operation of current accounts;
c) transfer of shares;
d) capital market transactions for listed securities.

8 Precious metals

a) The supply of gold to a Bank in bullion form.

9 Funeral services:

a) The supply of any goods or services in the course of a person's burial or cremation, including the provision of any connected licence or certificate.

10 Energy supplies:

a) energy saving lamps;
b) solar water-heaters;
c) wind energy systems;
d) liquefied petroleum gas, cylinders and invertors;
e) equipment used in the supply of biogas energy;
f) kerosene intended for domestic use, premium and gasoil.

11 Trade Union subscriptions.

12 Leasing of exempted goods.

13 All Agricultural and Livestock products, except for those which are subsequently processed, are exempted from VAT. However, milk which is processed by local industries is exempted from this tax.

14 Agricultural inputs and equipment.

15 The following goods and services imported by persons with the appropriate investment certificates are exempted from Value Added Tax:

a) machinery for industries;
b) raw materials for industries;
c) building and finishing materials imported by an investor fulfilling the requirements determined by an order of the Minister in charge of finance;
d) refrigerating vehicles, tourist vehicles, ambulances, fire-extinguishing vehicles, hearses;
e) vehicles and movable property and equipment for foreign and Rwandan diaspora investors and their expatriate staff;
f) equipment for tourism and the hotel industry and relaxation sites defined on the list determined by the Minister in charge of finance;
g) goods and services meant for free economic zones;
h) medical equipment, medicinal products, agricultural, livestock, fishing equipment and agricultural inputs;
i) equipment in education field;
j) tourist chartered aeroplanes.

The exemptions referred to under points a), h) and i) concern all investors, even those not possessing the investment certificate.

16 Equipment for information, communication and technology as they appear on the annex to this law are exempted from the value added tax.

17 Mobile handsets and the subscriber identification module (SIM card) connected to them.

The Minister of Finance has prepared a list of the exempted products which was annexed to the LVAT.

Operations imposed at a zero rate
In contrast to VAT-exempt transactions, the input tax for zero rated supplies is reclaimable. Therefore, the taxable person must be record, invoice and declare VAT. The chargeable operations which are treated as zero rate are exports and certain operations undertaken by various categories of people (Article 87 of the LVAT). They include in particular the following situations:

- Goods imported by a diplomatic mission accredited in Rwanda for uses inherent to the mission but subject to reciprocity in the country concerned in the country concerned;
- Goods or services provided under a convention between the Rwandan Government and of financial backers within the framework of finances projects.

A Ministerial order determines the conditions and the procedures concerning taxation at zero rate for these categories.

Deductions and restitutions

1. Notions of the deduction

The mechanism of deductions plays an essential role in the adoption of VAT, because it is this that allows the system to be "neutral and transparent".
In VAT, the deduction is made "tax from tax": the taxable person deducts the tax it can deduct from expenditure that it has made from the tax that it owes to the Treasury. The mechanism is significantly different from direct taxation where the deduction is made "base to base"; i.e. where deductible expenditure is offset against the taxable amount.

2. Characteristics of the deduction

As regards VAT, the deduction has the following characteristics:

- The deduction is **immediate** in the sense that the taxable person is not required to immediately make payments of the price of his supplies to his supplier or sell or use all the stock;
- The deduction is **total**, i.e. the tax paid to a supplier is deductible for the taxpayer's total amount due and also the fact that the tax on a supply is deducted at once, whatever its value or its lifespan;
- The deduction is **inclusive**, in the sense that all the deductions relating to one declaration period (usually annual) is added together in the declaration.

3. Conditions of deduction

Basic conditions
The principles of deduction are defined in art. 41 of the LVAT.
Three (3) conditions must be necessarily met in order to be able to profit from the right of deduction:

- It is necessary to be *a registered taxable person*. The right of deduction is not available either to consumers nor to taxpayers carrying out exempted operations;
- The operations must be *chargeable,* whether it is at the normal rate of the VAT or the zero rate;
- The tax must be *due*. VAT is due at the moment that the goods are delivered or at the moment when the supply of the services is made (Article 20 of the LVAT). The issue of when payments are actually made to the supplier therefore does not impact on the right to deduction. The tax nevertheless must be legally due. Just because tax is mentioned on the invoice, it does not necessarily mean that this is the case. This is particularly important as far as tax evasion is concerned.

2. Formal requirements

From Law No, 25 of 04/12/2005 on Tax procedures
Article 14: Value Added Tax invoice

A Value Added Tax invoice is an accounting document prepared in the form determined by the Tax Administration and which shows the following information:

1. names of the taxpayer and the client, and the taxpayer's trade name, if different from the personal name;
2. taxpayer identification number and the purchaser's if necessary;
3. number and date of the value added tax registration certificate;
4. description of goods sold or services rendered;
5. value of taxable goods or services;
6. sum of Value Added Tax due on the given taxable transaction;
7. date on which the Value Added Tax invoice was issued;
8. serial number of the Value Added Tax invoice.

In case the sale of goods or services is carried out at retail to clients who are not value added tax registered taxpayers, a simplified cash receipt determined by the Tax Administration may be issued instead of a value added tax invoice.

b. Periodical declarations
In order to be able to reclaim a refund for the input tax, the registered person must submit a declaration in the office of the RRA (Article 37 LVAT). This Declaration must be deposited within fifteen (15) days following the accounting period concerned. If the declaration is not made within this time, the taxpayer may be required to pay interest.

According to art. 38 LVAT, the first accounting period corresponds to the month which follows that of registration. From then on, the accountable period will equate to one month except when amended by the Commissioner General of the RRA who can determine another accounting period (generally three months) in its place.

c. Repayments

When the periodic declaration of the taxable person reveals a balance in his favour, the Commissioner General may repay to the taxpayer the amount that remains in credit due to the surplus. This should be repaid within thirty (30) day from either the end of the period relating to the declaration or from the receipt of the last declaration of tax due.

Localization of operations

It is important to locate the chargeable operations involved because, under the terms of the principle of the territoriality VAT, they are taxable in Rwanda only if they took place in Rwanda. But in theory, the place of delivery of goods is regarded as the place where the goods involved are placed at the disposal of the purchaser. If this location is in Rwanda, then the delivery of the goods is presumed to take place in Rwanda.

With regard to the character of the provision of services, the criteria used to locate them will be, by necessity, more abstract than for the deliveries of the goods. The system outlines a series of presumptions, which gives guidance as to where the service is deemed to have taken place.

According to article 9 LVAT, services shall be regarded as supplied in Rwanda if the supplier of the services:

a) has a place of business in Rwanda and no place of business elsewhere;
b) has no place of business in Rwanda or elsewhere but his usual place of residence is in Rwanda,
c) has places of business in Rwanda and elsewhere but the place of business most directly concerned with the supply of the services in question is the one in Rwanda; or
d)has no place of business in Rwanda and has place of business elsewhere but the recipient of the services uses or obtains the benefit of the services in Rwanda

Determination of VAT

1. Base of the VAT

In theory, the tax due is based on payments received or those paid to obtain goods or services (Article 16 LVAT). This may be in monetary or non-monetary terms. When the payment is in a monetary form, the taxable amount is the price paid for the transaction. In this case, any discounts and the rebates are taken into account unless the payment is carried out in instalments (art.19 LVAT).

However, in cases where part of the payment is in non-monetary terms or when the price is below what would normally be expected for the goods and services concerned, the open market value is taken into account. This measure is introduced to guard against tax evasion or tax avoidance which would occur if the taxable amount below that normally obtainable on the open market, or by fixing part of the silver price and the other in delivered well or service rendered. What would be not easily appraisable for the tax department?

The open market value is defined as the price for which the goods and the services concerned could be delivered or rendered in the ordinary course of businesses to a person independent of the supplier or the person receiving the benefits (Article 17 LVAT).

2. Rate of VAT

The rate of the VAT is applied at a proportional rate currently fixed at eighteen percent (18%) of the taxable amount (Article 34 LVAT). Rwanda does not have reduced rates on some items as exists in some other countries. However, Rwandan legislation provides that certain supplies of goods or provisions of services either are exempt from VAT or taxed at a zero rate, as discussed above.

BLANK

CHAPTER 4
DECENTRALIZED TAX - FIXED ASSET TAX

Contents

A. Purpose of the Law 59/2001 of 31/12/2011 Establishing the sources of Revenue and property of decentralized entities and governing their management

Article One : Purpose of this Law

The purpose of this Law is to describe and establish the sources of revenue and property of decentralized entities in Rwanda and to govern their management.

In this Law (Article 2), the following terms shall have the following meanings:

1. **“market value**”: amount of money for which a property should be sold on the date of its valuation in the open market by a willing buyer;
2. **“market value of an usufruct right”:** amount of money paid to acquire such an usufruct right;
3. **“improvements”:** immovable structures or amenities that are not buildings but increase the actual value of a parcel of land or a building;
4. **“title deed”:** a written legal document confirming a person’s right to a property, which is delivered according to the law by the competent authority;
5. **“assessment cycle”:** a period of four (4) years that commences on January 1st of the first year after the commencement of this Law as well as each period of four (4) consecutive years thereafter;
6. **“parcel of land”:** a plot of land with clear boundaries which is wholly owned by one person or several persons in divisible shares;
7. **“public institution”:** an legal personality managed in accordance with laws governing public service, to which the State allocates funds in order for it to carry out specialized activities for public;
8. **“building**”: an immovable and stable construction which protects humans and properties, animals or machineries permanently, or in the long term, from the disaster. Buildings include also houses;
9. “**decentralized entities”:** local administrative entities with legal personality and administrative and financial autonomy;
10. **“date of valuation”:** the date of reference for an assessment of value conducted during an assessment cycle;
11. **“owner”:** a person who is registered as a holder of a property or who is deemed to be the holder thereof in accordance with Rwandan law;
12. **“tax prescription period”:** a period after which an administration has no right to recover tax due from the taxpayer;
13. **“person”:** an individual, a legal entity or an association of individuals;
14. **“taxpayer”**: any person who is subject to tax in accordance with this Law;
15. **“fixed asset tax”**: a tax levied on immovable property;
16. **“ rental income tax”** : a tax imposed on individuals who earn income from rented immovable property;
17. **“trading license tax”** is a tax levied on profit-oriented activities;
18. **“residential property”:** a building exclusively intended for being occupied as a residence without any profit-oriented activity being carried out therein or in the plot of land on which it is erected;

19. **“fixed asset”:** a property that has a fixed location and cannot be moved elsewhere and includes parcels of land, buildings and improvements thereto.

Article 3: Income taxable year

The income taxable year starts on January 1st and ends on December 31st of the same year except for rental income tax

Article 4: Revenue and property of decentralized entities

The revenue and property of decentralized entities shall come from the following sources:

1. taxes and fees paid in accordance with this Law;
2. funds obtained from issuance of certificates by decentralized entities and their extension;
3. profits from investment by decentralized entities and interests from their own shares and income-generating activities;
4. fines;
5. loans;
6. Government subsidies;
7. donations and bequests;
8. fees from the value of immovable property sold by auction;
9. funds obtained from rent and sale of land of decentralized entities;
10. all other fees and penalties that may be collected by decentralized entities according to any other Rwandan law.

All revenue projections of decentralized entities shall be included in their annual budget.

Article 5: Local taxes

Taxes which are assessed and collected by decentralized entities are the following:

1° Fixed asset tax;
2° Trading licence tax;
3° Rental income tax.

This chapter deals in detail with Fixed Tax. F2.4 covers the other decentralised taxes.

B. Fixed Asset Tax

Fixed asset tax base - *Article 6*

Fixed asset tax shall be levied on the following:

1. the market value of parcels of land;
2. the market value of buildings and all improvements thereto registered with the Land Registration Centre and for which the owner has obtained a title deed from the time the building is inhabited or used for other activities;
3. the value of land exploited for quarry purposes;
4. the market value of a usufruct with a title deed.

The date of valuation is January 1st of the first income taxable year in a four (4) -yearly assessment cycle and all fixed assets must be valued and, may be reassessed before the end of the duration of the relevant assessment cycle, with reference to that date.

Obligations for taxpayers

The fixed asset tax shall be assessed and paid by the owner or deemed owner.

The local decentralised entity is not responsible in the first place for valuing the property. The owner will obtain valuation from the purchase price if it a new acquisition – *(see Article 17)* or by employing the expert assistance of a valuer.

Effectively, this is **Self-Assessment.**

For the purposes of the application of this Law, the following persons shall be deemed to be owners:

1. the holder of a fixed asset where the title deed has not yet been registered in the name of the owner;
2. a person who occupies or deals with an asset for a period of at least two (2) years as if he/she is the owner and as long as the identity of the legally recognized owner of such asset is not known;
3. a proxy who represents an owner who lives abroad;
4. a usufructuary.

The owner of a fixed asset who lives abroad may have a proxy in Rwanda. The proxy shall have to fulfil all obligations this Law requires from the owner. Misrepresentation by a proxy is deemed to be a misrepresentation by the owner.

Tax liability shall not be terminated or deferred by the disappearance of an owner of a fixed asset, where that owner has disappeared without leaving behind a proxy or other person to manage that asset on his or her behalf. If, after all reasonable steps have been taken to locate the owner, a competent court has ruled that the owner of that fixed asset cannot be found, the asset shall be forfeited to the decentralized entity where it is located in accordance with the law relating to management of abandoned property.

Usufruct

When a person has a usufruct on a parcel of land, a building or improvements thereto, the holder of such a right shall be deemed to be the owner. The tax liability for the usufructuary shall start from the date of commencement of the usufruct.

A usufruct is where a person does not own the property but has the use of it as if he/she did

Co-ownership of fixed asset

When a fixed asset is owned by more than one person, the co-owners shall appoint and authorize one of them or any other person as a proxy to represent them collectively as a group.

When co-owners have not appointed a co-owner or a proxy to represent them collectively as a group, the decentralized entity shall reserve the right to select any of them as a proxy who will then act for the group.

Self-assessment

Every taxpayer must, not later than March 31st in the first tax year, file a tax declaration to the decentralized entity where the asset is located .

Fixed asset tax declaration

Decentralized entities shall make available tax declaration forms no later than the January 31st of every year and on January 31st of the years which follow general revisions as provided for in Article 15 of this Law.

The tax declaration shall be signed personally by the taxpayer, his/her proxy or the usufructuary and thereafter transmitted to the decentralized entity where the asset is located.

Non-receipt of a fixed asset tax declaration form shall not relieve the taxpayer of his/her obligation to pay the tax.

Late submission, or incomplete or misleading tax declaration:

Apart from collecting the actual amount of the tax due, the decentralized entity shall levy a fine not exceeding 40% of the tax due where:

1. the fixed asset tax declaration form is not submitted;
2. the fixed asset tax declaration form is submitted late;
3. the fixed asset tax declaration form is substantially incomplete;
4. the fixed asset tax declaration form contains incorrect or fraudulent information with an intent to evade tax.

Review and re-assessment of tax by the decentralized entity

The tax declaration shall be reviewed by the decentralized entity within a period of six (6) months starting from April 1st of the year the tax declaration was filed. If the tax declaration was filed late, the six (6) months period shall start on the date the concerned decentralized entity receives it. The review shall be based on the nature and general state of the fixed asset, its location and its actual or zoned use.

Tax assessment notice – *Art.14*

The tax assessment notice shall contain at least the following details:

1. tax base calculation outline;
2. calculation of the market value of the concerned fixed asset;
3. calculation of the tax in Rwandan francs;
4. names of the owner or his/her proxy;
5. address of the owner, the proxy or the usufructuary;
6. the due date for the tax payment;
7. mode of payment;
8. consequences of late payment or non-payment;
9. reference to the taxpayer’s right to complain and appeal.

Article 15: **Assessment cycles and general revision**

The assessment cycle is every 4 years. At the commencement of each cycle, a new general revision of market value shall take place in accordance with Articles 10, 11, 12, 13 and 14 of the Law 59/2011.

A new fixed asset tax declaration shall be filed by not later than March 31st of the first year of each tax assessment cycle.

The new self-assessed tax amount must be paid for four (4) consecutive years without filing a new tax declaration or assessment notice.

Appreciation and depreciation

If, due to changes to a fixed asset, the value of that asset increases or decreases by more than twenty percent (20%) within an assessment cycle, the taxpayer shall submit a new tax declaration with all details within a period of one (1) month after the value has so changed.

Upon receipt of the tax declaration, the decentralized entity shall review the new tax declaration, and where applicable, issue a new assessment as provided for in Article 13 of this Law.

Reasons for an increase in value shall include the upgrading of a building or the adding of additional floors to a building, general renovation or extension or improvement of a building. Reasons for a decrease in value shall include the demolition of a building, in whole or in part, after a natural disaster. A global fluctuation of the market value between two general revisions shall not be a reason for a new assessment.

Article 17: Valuation of fixed asset

It is the responsibility for the owner (or deemed owner) to value the asset or have the property valued.

Undeveloped land: If the fixed asset constitutes a parcel of land that has not been developed or built upon, the market value shall constitute a per square metre value times the size of that parcel of land.

Developed property: Where the fixed asset consists of a parcel of land and a building and improvements, the aggregate value of the land, the building and improvements constitute the market value of such fixed asset.

In the first instance, unless it is patently clear that the purchase price is below the market value, the purchase price will be the valuation of the property. The taxable value should be rounded up to the next full one thousand Rwandan francs.

Tax exemption *Article 18*

The following fixed assets shall be exempted from the fixed asset tax:

1. fixed assets used exclusively for **medical purposes**, or caring for vulnerable groups, and those meant for **educational and sporting activities**, where **no profit-making activity** takes place;
2. fixed assets exclusively intended **for research activities** which are **not** meant **for profit-**making;
3. fixed assets belonging to the Government, Provinces, decentralized entities, as well as public institutions except where they are used for profit-making activities;
4. fixed assets used primarily **for religious activities** in accordance with the laws with exception of those fixed assets used for profit-making activities;
5. fixed assets used primarily **for charitable activities** as determined by the Minister in charge Social Affairs;
6. fixed assets belonging to **foreign diplomatic missions** in Rwanda if their countries do not levy tax on fixed assets of Rwanda's Diplomatic Missions;
7. land in use for agriculture, livestock or forestry, if the taxpayer owns less than two (2) hectares. If he/she owns more than two (2) hectares, the first two (2) hectares shall be exempt and tax shall be levied only on the excess land;
8. fixed assets and usufructs used primarily for residential purposes, if the assessed value does not exceed three million (3,000,000) Rwandan francs. If the assessed value exceeds such an amount, only the excess value shall be taxed.

Article 19: Tax rate

The tax rate is fixed at a thousandth (1/1000 or 0.1%) of the taxable value per year.

The tax rate for lands exploited for quarry purposes is fixed at a thousandth (1/1000) of the taxable value per year.

Objection to a calculated value

Objections must be filed with the local entity within one (1) month after receipt of the assessment. For an objection to be considered, it must be in writing, justified, clear and signed by the taxpayer, his/her proxy or the usufructuary.

Within a period of two (2) months after receiving the letter of objection, the concerned decentralized entity must notify its decision. If it is satisfied that the objection was justified, the concerned decentralized entity must pay back the overpaid tax with interest in accordance with the provision of Article 23 of this Law within one (1) month after notifying the decision. If the decentralized entity does not notify its decision within two (2) months, the objection of the taxpayer shall be deemed to be founded.

Appeal before a competent court

If the taxpayer is not satisfied with the decision of the decentralized entity, he/she can lodge an appeal with the competent court.

If the court finds that the appeal of the taxpayer is justified and the decision was unfairly imposed against him/her, the concerned decentralized entity must pay back the overpaid tax within one (1) month after the decision has been taken. Interests accrued thereon must be paid to the taxpayer in accordance with the provisions of Article 23 of this Law.

Tax payment

The tax, as assessed by the taxpayer must be paid to the decentralized entity where the fixed asset is located not later than March 31st of the tax year.

As long as there is no general revision or an assessment notice issued by the concerned decentralized entity, the same amount shall be paid annually by the taxpayer for four (4) consecutive tax years.

The self-assessed tax must be paid not later than March 31st, even if the revision of fixed asset tax or fixed asset tax declaration has not yet been concluded.

Article 23: Due date for tax payment

The tax payment must be paid not later than March 31st of the tax year. Additional tax resulting from a tax assessment notice of the concerned decentralized entity shall be paid within one (1) month from the day the tax assessment notice is issued to the taxpayer.

When the owner of a fixed asset, his/her proxy or usufructuary has disappeared without having appointed a proxy, tax collection documents shall be sent through the post office for a period of at least three (3) months and shall be posted in all administrative buildings within the decentralized entity where the fixed asset is located. If the tax due is not paid within the prescribed period, the concerned decentralized entity shall apply procedures provided under this Law.

The objection or appeal against the assessed tax shall not relieve the taxpayer of his/her obligation to pay the tax assessed. When the taxpayer exercises his/her right to object or appeal, the total amount of assessed tax must be paid by the due date provided under Paragraph One of this Article. If the taxpayer's objection is justified, the overpaid tax must be refunded within one (1) month after the decision is made. In this case, the concerned decentralized entity must pay to the taxpayer interests accruing on the overpaid tax in accordance with this Law.

Change of ownership of fixed asset and payment of tax

When fixed assets already exist or are purchased between January 1st to March 31st, the fixed asset tax shall be paid by the (new) owner thereof in a single instalment for the entire year.

Where the fixed assets change ownership after March 31st, the former owner must pay the tax as should have been done (as provided under the Law). When the person who sells the asset fails to meet his/her obligations as a taxpayer, fines and late interests shall be calculated and paid by him.

No transfer of ownership of fixed asset shall take place without a tax clearance certificate issued by the concerned decentralized entity.

Fines for late tax payments

A tax not paid when it is due shall bear interest. The interest rate is fixed at one point five percent (1.5 %). Interest is calculated on a monthly basis, non-compounding, counting from the first day after the tax should have been paid until the day of payment, which is included. Every month started will count for a complete month.

Apart from the interest payable, a surcharge equivalent to ten percent (10 %) of the tax due must be paid. However, such a surcharge shall not exceed an amount of one hundred thousand (100,000) Rwandan francs.

Deferral of tax payment

If, due to special circumstances the taxpayer is temporarily unable to pay the tax due, the Council of the concerned decentralized entity may, upon request by the taxpayer or his/her proxy, grant a deferral of payment for up to six (6) months without any fine. In this case, interest shall be paid as described in Article 25 of this Law.

The taxpayer must request a deferral of tax payment in writing at least one (1) month before the due date, after tax review or tax re-assessment. The Council of the decentralized entity must respond to the request of the taxpayer before the due date.

Tax payment in instalments

The taxpayer may request the concerned decentralized entity to authorize him/her to pay tax in instalments. The payment in instalments shall not exceed a period of twelve (12) months. The taxpayer must submit to the concerned decentralized entity a tax instalment payment plan which indicates an immediate payment of at least 25% of the tax due. The failure by the taxpayer to pay under the conditions of the tax instalment payment plan shall result in an immediate obligation to pay the total remaining amount of tax due.

Article 28 of Law 59/2011 forbids any one should interfere with the activities and responsibilities of the decentralized entity. Anybody who does so alone or conspires with others to do so can be fined an administrative fine of twenty thousand (20,000) but not exceeding one hundred thousand (100,000) Rwandan francs without prejudice to other penalties provided under criminal law.

Procedures for the enforcement of this Law

Articles 29 -

If by the due date, the taxpayer has not yet filed a tax declaration, and paid the tax or has not applied for tax deferral, or the tax deferral was not granted, the concerned decentralized entity shall have the right to start procedures to identify and recover unpaid taxes.

Before starting the tax recovery procedures, a written warning must be sent to the owner(s) with all the details of the unpaid taxes and actions planned to enforce the law. The taxpayer shall be afforded the opportunity to pay the taxes but with interest.

If the tax is not paid within one (1) month of dispatch of the warning letter, the concerned decentralized entity has the right to start enforcement procedures.

Fixed asset tax which remains unpaid is a debt which can be claimed before competent courts.

The decentralized entity where the fixed asset is located shall have the right to attach:

1. rent owed by a tenant to the taxpayer up to the amount of rent owed *Article 32,*
2. money owed to or held on behalf of the taxpayer by third parties – *Article 33,*
3. movable assets belonging to the taxpayer, - *Article 35*
4. fixed assets belonging to the taxpayer – *Article 35* .

Also part of article 33- Once the official request for the payment of taxes has been sent, no money shall be used by the third parties without authorization by the concerned decentralized entity. If the third parties did not notify the substantive reason for non-payment within thirty (30) days as from the date the notification in writing was received, they are assumed fully liable for the debt to the concerned decentralized entity in the amount equal to the amount of money they owe the defaulting taxpayer.

In respect of unpaid taxes, precedence shall be given to the payment of fixed asset tax debt – *Article 34.*
In case of conflict of interests over this right between the Central Government and decentralized entities or between decentralized entities themselves, such right shall be reserved to the Government entity that has first initiated proceedings against the taxpayer in respect of his/her fixed assets.
As for all other creditors of the taxpayer, the right of the Central Government and decentralized entities shall still have precedence.

Seizure and sale of movable and fixed assets

In respect of the seizure and sale of movable and fixed assets, the decentralized entities must comply with the law on civil and commercial procedures. Seized assets shall only be sold by public auction. In respect of fixed assets, a public auction must be arranged and directed by the public notary or by a competent bailiff.

The right to seize and sell the taxable fixed asset by public auction shall only be exercised after other enforcement mechanisms have been reasonably exhausted and not before a period of three (3) years from the due date of payment has lapsed.

The local decentralised entity can postpone an auction but can do this only once – *Article 36.*

The proceeds from the public auction shall first be used to set off the tax, interests accruing thereto, surcharges and penalties owed to the concerned decentralized entity.

The remaining amount shall be returned to the taxpayer.

In the case of the taxpayer's absence, the remaining amount shall be kept in the state treasury for a period not exceeding five (5) years. If the taxpayer has not claimed this amount within this period, the law relating to management of abandoned property shall be applicable.

Insolvency and bankruptcy

In case of insolvency or bankruptcy, the decentralized entity where the taxable asset is located has the right to start a forced sale of the concerned asset according to the specific law on public auction.

Amount of tax

Taxes on undeveloped sites are fixed by District Councils but must be within the limits determined by the law (art 17 LFD):

1. In the town of Kigali, the tax must be between 20 and 50 RwF per m^2;
2. In other urban districts, the tax must be between 10 and 20 RwF per m^2;
3. In trade centres, the tax must be between 1 and 10 RwF per m^2;
4. In rural areas, the tax on undeveloped sites must not be more than 1000 RwF per hectare. When the area is more than twenty hectares (20ha), the tax on the area above the first 20 hectares must be between one thousand and one (1001) RwF and two thousand (2000) RwF per hectare.

If the sites without construction are touristic locations, the tax is increased by ten percent (10%) of the ordinary annual tax. For the purposes of calculating the tax, fractions of square metres (m^2) and fractions of hectares are ignored.

In conclusion, art 28 LFD, as modified by the law of 1st October 2003, provides that the tax due must, at the latest, be declared and paid to the receiver of the taxes of the district by March 31st of the following fiscal year.

CHAPTER 5
TAXATION OF CROSS BORDER ACTIVITIES

Contents

A. <u>Distinction between trading in and trading with a country</u>

When an individual, or a business, is trading there are two possibilities:
Either the trade is carried out within their own country:

i.e. both supplier and customer are in the same country – "domestic" trade

Or the trade is carried out with another country:

i.e. the supplier is in one country, and the customer is in another – "international" trade.

When the goods or services are supplied to a customer in another country, the supplier **<u>exports</u>** to that country. When goods or services are bought from a supplier in another country, the customer **<u>imports</u>** from that country.
Both goods and services can be exported and imported. Goods are self-evident – food, minerals, raw materials etc. Examples of the export of services are a designer in country A producing designs for a customer in country B, or an accountant in one country advising a client in another.
Every trading transaction gives rise to tax issues, but the tax issues will differ depending on whether the trade is domestic or international.
A key feature of international trade is import taxes. This is where a country decides to impose import taxes (also known as custom duties) on various products on arrival into a country. The duties will vary depending on the actual product. So, for example, a country which has a vibrant steel business may impose relatively high import duties on steel in order to protect the domestic steel industry from cheap imports.
The duties will also depend on the origin of the imports. Thus imports from Country A may carry higher import duties than those from Country B.

In Appendix I is an extract from the East African Community legislation –
The East African Community Customs Management Act, 2004 incorporating all amendments up to 8th December, 2008

An additional feature of international trade is the emergence of trading blocs of countries such as the EAC.
These typically involve groups of countries coming together and agreeing to cooperate closely on trade. The degree of cooperation can vary, and the countries involved are usually ones that have close links with each other for geographic, historical or cultural reasons.
A good example of a bloc with geographic links is the East African Community (EAC) Common Market. Another good example is the European Union (formerly the European Common Market) – which was formed for historical and geographic reasons.

Generally speaking such blocs evolve over time. They can start with an agreement to simplify trade administration between two or more countries and to reduce tariffs, customs duties etc on goods and services traded between the countries.

The ultimate aim of such partnerships is to abolish commercial borders between member states, thus pushing the commercial borders to the periphery of a trading bloc. Thus, goods imported into country A of a trading bloc are deemed to be imported into all the countries.

So, in the case of the EU, when goods are imported into Belgium, they are also deemed to be imported into France. This means if the goods are subsequently sold from Belgium into France, they are not classified as either a Belgian export or a French import. Neither are there any tariffs, duties etc. payable. Such a transaction is in essence a trading bloc domestic transaction, and is known formally as "intra-community trade".

B. Double Taxation Agreements

International Taxation involves taxation which is cross border. It can arise from an individual having taxable income or assets in two countries, or a business operating in two (or more) countries. Due to increased globalisation, the growing level of businesses trading internationally around the globe, and increased personal mobility, international taxation is becoming more and more prevalent. Travel restrictions are less onerous, and it is no longer difficult for people to move from one state to another to carry out businesses or to seek employment opportunities. Capital is more mobile and with advances in e commerce and e banking it moves more swiftly than ever before. Such activities are all likely to attract tax liabilities.

To take a simple example. Joe is a citizen of and lives in Country A. He has a home there, and lives there with his wife and family. Thus, in the normal scheme of things, Joe would be taxed on his income in Country A, in common with all other residents and citizens who live there, and who use the roads, sanitation systems and other public services there.

However Joe is slightly unusual. Every Tuesday morning Joe flies to Country B, works there until Thursday afternoon and then flies home again. He gets paid in Country B.

The dilemma however, is – in what country does the tax liability fall, and how is that decided? And a further issue that may arise is that if an individual or a business is taxed in

Country A **and** in Country B, then that person or entity has effectively been taxed twice on the same income or transaction. If such a situation were to prevail, it could materially inhibit the development of international trade.

So, for example, Country A will argue that Joe is a citizen and a resident, he lives with his wife and family there, and every citizen is expected to make their contribution to the various public services they enjoy. Thus, they will argue, Joe should be taxed on his income in Country A, according to the rules that prevail there.

But Country B will argue that Joe should pay his income tax in their country, because the income originated there, and their rules state that anyone earning an income in their country should be taxed there.

The dilemma for Joe is that he could end up being taxed in both countries on the same income – which is a bit unfair on Joe. The dilemma for both Countries is that they could end up not taxing Joe in either country. And if it is to be only one – which one, and how is that decided?

So a system of double taxation agreements has evolved to deal with this type of situation. The taxpayer does not have to be an individual – it could be a company, or a business operating in both countries.

There are two principal scenarios to be considered:

(A) Where there is a double taxation agreement in place

(B) Where there is not

Scenario (A)

In scenario (A) (where there is a tax treaty, on avoidance of double tax and prevention of fiscal evasion), between Country A and Country B, the treaty generally will specify in a clear wording that the right to tax is with state Country B, because this is the country in which the income arises – i.e. the "source" country. Country A, which taxes on worldwide incomes, i.e. income arising from Country A **and** Country B, will then compute tax payable. Country A will provide credit for the tax paid to Country B i.e. the country where the incomes were sourced. It is thus, through this arrangement that double taxation is avoided.

Scenario (B)

In Scenario (B) (where there is no existing tax treaty on avoidance of double tax and prevention of fiscal evasion) country B will to tax Joe on incomes arising from country B, because that is the source of the incomes. When he goes back to country A, country A may give Joe credit for the tax paid in country B. However, country A may only do this on a unilateral basis, and is not obliged to do so. Thus the certainty created for Joe, and other taxpayers in Scenario a is absent here.

Under Rwanda's income tax law (Law No.16/2005 OF 18/08/2005, On Direct Taxes on Incomes as modified and complemented to date), this is indicated in article 6, regarding foreign tax credit. Note: foreign tax credit provision exists in almost all tax laws(Acts).

It is desirable, and indeed necessary, in the field of international taxation, that there are rules agreed between different countries as to which tax jurisdiction takes what portion of tax, and why a given tax jurisdiction should forego in whole or in part what it considers to be its revenues. Having such agreements creates taxation certainty for businesses and individuals who operate internationally. Also, such agreements can include provision for cooperation and sharing of information which can assist in tackling tax evasion.

Various countries have concluded and ratified tax treaties with other countries. Typically these tend to start with a country's major trading partners. Rwanda has signed and ratified tax treaties with Mauritius, South Africa and Belgium. The East African Tax Treaty on Avoidance of Double Tax and Prevention of Fiscal Evasion, is also on the horizon and it is likely that, in time Rwanda will adopt and ratify this. Key to all such treaties is that the business community (and other taxpayers) will be provided with certainty in cross border taxation issues.

A typical Double Taxation Agreement (DTA) will address key issues. Each agreement may differ depending on the prevailing circumstances, and the participating countries. However, a typical DTA would be likely to include provisions for some or all of the following:

PERSONS COVERED

This provision defines who the treaty will apply to, and specifically if it will apply to persons who are residents of either State or both. This is a central concept in all double taxation treaties. Benefits are only extended by one State to "residents" of the other State.

TAXES COVERED

This provision article sets out the taxes to which the treaty will apply. In some cases this may apply only to taxes on income, (personal and corporate); in other cases it may also apply to Capital taxes.

It is very important that there is clarity around precisely what taxes are included in the treaty, and which are not included.

RESIDENT

This provision sets out the rules for determining whether a person is a resident of of one State or a resident of the other State for the purposes of the treaty. Only residents of the Contracting States can claim the benefits of the treaty. A resident of a Contracting State is a person who is subject to comprehensive taxation in that State.

The provision can contain tie-breaker provisions to resolve cases where an individual would be regarded as a resident of both Contracting States.

A treaty will also normally contain a tie-breaker test for corporate entities. Where the entity is a resident of both States it will normally be deemed to be a resident of the State in which it is effectively managed.

PERMANENT ESTABLISHMENT

This provision defines the term “permanent establishment”. The concept of a permanent establishment is important generally but is of primary importance for the purposes of Business Profits. Only when an enterprise of one of the Contracting States carries on business through a permanent establishment in the other State is its presence regarded as sufficiently substantial to allow that State to tax the business profits attributable to the permanent establishment.

A “permanent establishment” is defined as a fixed place of business through which the business of an enterprise is wholly or partly carried on.

INCOME FROM IMMOVABLE PROPERTY

This provision defines the rules relating to taxation of income from immovable property, including income from agriculture or forestry.

The term “immovable property” is defined by reference to the domestic law of the Contracting State in which the property is situated.

BUSINESS PROFITS

Under this provision, each Contracting State agrees to rules for the taxation of Business Profits. The rules tend to revolve around whether an enterprise has a permanent establishment in a State. The provision can also set out the rules by which the profits of a permanent establishment are to be attributed.

.

ASSOCIATED ENTERPRISES

This provision deals with transfer pricing.

Generally such a provision determines that the profits made by an enterprise from dealings with an associated enterprise in the other Contracting State may be increased to the level they would have been if the enterprises had been independent and dealing at arms-length. This is known as the “arm’s length” principle.

It may also provide for the adjustment of profits of the associated enterprise in the other State as a consequence of an adjustment in the first State.

DIVIDENDS

This provision is concerned with the taxation of dividends paid by a distributing company resident in one Contracting State to a shareholder resident in the other State.

The term “dividends” will be defined in the article.

INTEREST

This provision provides rules for the taxation of interest arising in one Contracting State and paid to a resident of the other State.

The provision normally provides that the interest may be taxed in the State in which it arises but if the beneficial owner of the interest is a resident of the other State the rate of tax is limited to a specified percentage of the gross interest payment. This will normally be lower than the tax rate that would otherwise apply.

The provision will also include a comprehensive definition of the term “interest”.

ROYALTIES

This provision provides rules for the taxation of royalties. It may limit the taxation in the source State of royalties paid to a resident of the other State.

The term “royalties” is defined and can covers payments in respect of copyright of literary, artistic or scientific work as well as patents and trademarks. Some treaties also cover leasing payments – “payments for the use of, or the right to use, industrial, commercial or scientific equipment” – which would otherwise normally come under Business Profits.

.

INCOME FROM EMPLOYMENT

This provides for the taxation of income from employment.

It generally provides that remuneration in respect of an employment derived by an individual who is a resident of a Contracting State may be taxed only in that State unless the employment is exercised in the other Contracting State. In that event, the other State may tax the remuneration derived from the exercise of the employment in it.

ARTISTES AND SPORTSPERSONS

This deals with the taxation of entertainers and sportspersons resident in one of the Contracting States and performing services in the other State.

PENSIONS and ANNUITIES

This provides a general rule for the taxation of pensions and annuities.

It normally provides that a pension arising in a Contracting State and paid in consideration of past employment to a resident of the other Contracting State will be taxed only in that other State. In some treaties, the source country retains the right to tax pensions.

,

ELIMINATION OF DOUBLE TAXATION

This provision is relevant where both Contracting States retain taxing rights on items of income or gains. Double taxation is relieved in such cases by the State of residence of the taxpayer either exempting the income or gains from further taxation or granting credit for the tax paid in the other State.

.

EXCHANGE OF INFORMATION

This provides for the exchange of information that is relevant for the carrying out of the provisions of the treaty or of the domestic laws of the Contracting States concerning taxes covered by the treaty. All information so exchanged is to be treated as secret and disclosed only to persons concerned with the administration of the taxes to which the treaty applies. There is no obligation to act or supply information other than in accordance with domestic law or normal administrative practice, or to supply information which would disclose trade secrets or would be contrary to public policy.

C. <u>Regional Perspective</u>

In East Africa, the EAC Partner States commenced implementing the EAC Common Market Protocol in July 2009. This means that Rwanda, Uganda, Kenya, Tanzania and Burundi entered into a single market with free movement of factors of production based on the principles of non discrimination, most favoured nation and transparency.

Some of these rights include free movement of goods, persons and labour.

The EAC citizens also have the rights of establishment (i.e. a Ugandan citizen can set up a business in Rwanda, and vice versa) as well as rights of residence. There is also provision for free movement of services and capital.

It is important to note that taxes on international trade will remain as is, except for import duty which will be at 0% on imports from the EAC that comply with the rules of origin criteria.

If a trader for example imports juice or biscuits that are manufactured in Uganda (an EAC member state) and have a valid certificate of origin, the Rwandan Revenue Authorities (RRA) will not collect import duty (a tax levied on goods imported into the country) on such goods as long as it is proved the goods are originating from the region.

In Rwanda, issuance of certificates of origin has been decentralized to the RRA Gikondo Customs department and at all border posts including, Gatuna (Rwanda-Uganda border) and

Rusumo (Rwanda-Tanzania border). It is intended that this service will be introduced at the Rwanda-Burundi border.

While import duty was abolished for such trade, traders will continue to pay other domestic taxes due on goods including Value Added Tax (VAT) of 18 percent, consumption tax (excise duty) as well as withholding tax of 5 percent.

However, the withholding tax mentioned above is exempt for people who have a tax clearance certificate (Quitus Fiscale).

Free movement of goods under the Common Market is provided for under the protocol (Article 39).

On 1st July, 2009, Rwanda commenced the implementation of the EAC Customs Union and started levying zero percent import duty tariff on goods originating from the Partner States, applying the Common External Tariff and the East African Customs Management Act and Regulations.

Implementation of the Customs Union is progressive. For example, the internal tariff elimination on intra regional trade took 5 years.

Removal of VAT, Consumption tax (excise duty) and Withholding tax will be implemented when a fully fledged customs union is established.

Such a union will also include the following:

- Shifting of borders between Partner States to the peripheral
- Collection of duties and taxes at the point of entry into the Customs Union Territory
- Agreeing on the revenue sharing mechanism;
- Establishment of a regional authority to administer the Customs Union
- Elimination of rules of origin on intra regional trade. In a fully fledged Customs Union, goods from Nairobi to Kigali will not attract any duties and taxes will be considered just as goods coming from Huye, Southern Province or Musanze, Northern Province.

Harmonization of tax policies and laws

The EAC Common Market Protocol provides that the Partner States will progressively harmonize their tax policies and laws to remove tax distortions. This will be done to facilitate the free movement of goods, services and capital and to promote investment within the Community.

It is important to note that the implementation of the EAC Common Market has not changed the existing fiscal regime and the anticipated changes will progressively be realized as Rwanda enters into a fully fledged Customs Union and the harmonization of tax policies and laws finalized.

Harmonization of domestic taxes is being handled under EAC Framework by the Fiscal Affairs Committee(Technical Committee on tax harmonization) and Fiscal Affairs Committee has established Technical Working Groups on Value Added Tax, Excise Tax and Income Tax develop a harmonized legal framework on tax laws and a roadmap for the harmonization process.

It should also be noted that the double taxation and the prevention of fiscal evasion with respect to taxes on income (DTA) was agreed upon by the Partner States and is awaiting legal input from the Attorney Generals Before approval by Council.

This will all take time to achieve. It may be further complicated by the admission of new member states to the Common Market. And it is possible that there may be a deeper strengthening of trade ties. For example in the EU, the arrangements have moved on from being a pure trading bloc to a group of countries who have some common laws, and in some cases a common currency.

Countries can also involve themselves in wider, but looser associations for international cooperation. Such an example is COMESA (the Common Market for Eastern and Southern Africa). The benefits of COMESA are:

1. A wider, harmonised and more competitive market
2. Greater industrial productivity and competitiveness
3. Increased agricultural production and food security
4. A more rational exploitation of natural resources
5. More harmonised monetary, banking and financial policies
6. More reliable transport and communications infrastructure

19 countries – including Rwanda - are members of COMESA, and the agreed activities cover more than just taxation issues.

D. <u>Most Favoured Nation</u>

Most Favoured Nation (MFN) is a status or level of treatment accorded by one state to another in international trade. This means that the country which is the recipient of this treatment must, nominally, receive equal trade advantages as the "most favoured nation" by the country granting such treatment.

Such advantages would include such things as low tariffs or high import quotas. It effectively means that a country that has been accorded MFN status may not be treated less advantageously than any other country with MFN status by the country granting MFN status.

MFN status is accorded by members of the World Trade Organization (WTO) to each other.

Preferential treatment of developing countries, regional free trade areas and customs unions is permitted by exception.

Some of the benefits conferred by MFN status are:

- As a consequence of MFN, smaller countries can participate in the advantages that larger countries often grant to each other. In the absence of an MFN, smaller countries would often not be powerful enough to negotiate such advantages by themselves.

- MFN provides domestic benefits: Administration is simplified. By having one set of tariffs for all countries the rules are simplified and made more transparent. It also lessens the frustrating problem of having to establish rules of origin to determine which country a product (that may contain parts from all over the world) must be attributed to for customs purposes.

- MFN restrains domestic special interests from obtaining protectionist measures. For example, butter producers in country A may not be able to lobby for high tariffs on butter to prevent cheap imports from developing country B, because, as the higher tariffs would apply to every country, the interests of A's principal ally C might get impaired.
- As MFN clauses promote non-discrimination among countries, they also tend to promote the objective of free trade in general.

There is, however, a recognition that the MFN rule should be relaxed to accommodate the needs of developing countries.

The emergence of powerful trade blocs (e.g the EU, or the North American Free trade Agreement (NAFTA) has presented challenges to the MFN concept. In these blocs, tarriffs have been lowered or eliminated among the members while maintaining tariff walls between member nations and the rest of the world.

E. Withholding Tax Provisions

Withholding tax, also called **retention tax**, is where a government requires the payer of an item of income to withhold or deduct tax from the payment, and pay that tax directly to the government.

In most jurisdictions, withholding tax applies to employment income. Thus employers deduct the appropriate tax, pay the employee the net amount, and pay the balance (i.e. tax) over to the government.

Rwanda operates a PAYE (pay as you earn) withholding tax system:

Rwandan tax law requires that when an employer makes available employment income to an employee the employer must withhold, declare, and pay the PAYE tax to the Rwanda Revenue Authority within 15 days following the end of the month for which the tax was due.

In the case of engaging a casual labourer for less than 30 days during a particular tax year, the employer shall withhold 15% of the taxable employment income of the casual labourer.

The employer is personally responsible for the correct withholding, declaration and the timely payment to the Rwanda Revenue Authority.

The employer is personally responsible for keeping proper books of account to prove that the tax has been correctly withheld, paid, and accounted for. Under those circumstances where, the employer is not required to withhold and pay the tax, the employee is responsible for registering, declaring, accounting, and paying the tax.

Many jurisdictions also require withholding tax on payments of interest or dividends. In most jurisdictions, there are additional withholding tax obligations if the recipient of the income is resident in a different jurisdiction, and in those circumstances withholding tax sometimes applies to royalties, rent or sale of property. Withholding tax enables Governments to combat tax evasion, and sometimes impose additional withholding tax requirements if the recipient has been delinquent in filing tax returns, or in industries where tax evasion is perceived to be common.

Withholding Tax on other payments in Rwanda

A withholding tax of 15% is levied on the following payments made by resident individuals or resident entities including tax-exempt entities:

Dividends, except those governed by Article 45 of this law;
Interest payments;
Royalties;
Service fees including management and technical service fees;
Performance payments made to an artist, a musician or an athlete irrespective of whether paid directly or through an entity that is not resident in Rwanda;
Lottery and other gambling proceeds.

Withholding Tax on Imports and Public Tenders

A withholding tax of five percent (5%) of the value of goods imported for commercial use shall be paid at custom on the CIF (cost insurance and freight value) value before the goods are released by customs.

A withholding tax of three percent (3%) on the sum of invoice, excluding the value added tax, is retained on payments Or by public institutions to those who supply goods and services based on public tenders.

Typically the withholding tax is treated as a payment on account of the recipient's final tax liability. It may be refunded if it is determined, when a tax return is filed, that the recipient's tax liability to the government which received the withholding tax is less than the tax withheld, or additional tax may be due if it is determined that the recipient's tax liability is more than the withholding tax. In some cases the withholding tax is treated as discharging the recipient's tax liability, and no tax return or additional tax is required.

The amount of withholding tax on income payments other than employment income is usually a fixed percentage. In the case of employment income the amount of withholding tax is often based on an estimate of the employee's final tax liability, determined either by the employee or by the government.

Some governments have written laws which require taxes to be paid before the money can be spent for any other purpose. This ensures the taxes will be paid first, and will be paid on time as the government needs the funding to meet its obligations.

Most countries require that payers of certain amounts, especially interest, dividends, and royalties, to foreign payees withhold income tax from such payment and pay it to the government. Payments of rent may be subject to withholding tax or may be taxed as business income. The amounts may vary by type of income. A few jurisdictions treat fees paid for technical consulting services as royalties subject to withholding of tax. Tax treaties may reduce the amount of tax for particular types of income paid from one country to residents of the other country.

Some countries require withholding by the purchaser of real property.

Taxes withheld may be eligible for a foreign tax credit in the payee's home country.

F Transfer Pricing

Other issues may also arise in international taxation – and a key issue is the issue of **transfer pricing**.

Take for example, the case of Business A being headquartered in Country A, and has a subsidiary in Country B. It makes widgets in Country B which it exports back to its parent in Country A. Let us assume that Country A has a corporate tax rate of, say 15%, and Country B has a corporate tax rate of say 35%.

Business B makes 500,000 widgets, at a unit cost of 1 franc. It decides it needs a gross profit of a further 1 franc, and so decides to sell the widgets at 2 francs each back to its own business in Country A.

Therefore;

Sales: (To country A)	1,000,000
Cost of sales	500,000
Profit	500,000
Taxed @ 35%	175,000

The business in Country A sells the widgets locally, for 4f each. They incur distribution costs of 1f each.

Therefore

Sales (In Country A)	2,000,000
Cost of goods sold	(1,000,000)
Distribution costs	(500,000)
Profit	500,000
Taxed @ 15%	75,000

Therefore total tax

In country B	175,000
In country A	75,000
Total	250,000

However, to reduce the tax liability, the company could decide to make no profit in Country B, and all the profit in Country A.

Thus, if the sales are all to their own business in Country A, the company could decide to charge their own company Rwf 1 per unit. The following therefore would be the case:

<u>Country B</u>

Sales: (To country A)	500,000
Cost of sales	500,000
Profit	0
Taxed @ 35%	0

<u>Country A</u>

Sales	2,000,000
Cost of goods	(500,000)
Distribution costs	(500,000)
Profit	1,000,000
Tax @ 15%	150,000

Therefore we can see that the overall tax liabilities are reduced from 250,000 to 150,000. This has been achieved by the simple mechanism of transferring the original profits from Country B to Country A, where there is a lower tax rate.

This in turn has been achieved by reducing the price of the goods sold into Country A. Thus no profits are made in Country B, and all the profits are made in Country A. The pricing mechanism used between different parts of the same business is known as "transfer pricing", and as can be seen from the above examples can be used to manipulate the profits in various countries. Because this means that the tax can also be manipulated the authorities in various countries are very interested in this.

Double taxation agreements are increasingly concerned with this issue and seek to mitigate the effects of artificially created pricing structures.

Transfer pricing refers to:

- the setting,
- analysis,
- documentation,
- and adjustment

of charges made **between related parties** for goods, services, or use of property. Transfer prices among components of an enterprise may be used to reflect allocation of resources among such components, or for other purposes.
OECD Transfer Pricing Guidelines state,

"***Transfer prices are significant for both taxpayers and tax administrations because they determine in large part the income and expenses, and therefore taxable profits, of associated enterprises in different tax jurisdictions."***

Over 60 governments have adopted transfer pricing rules.

Transfer pricing rules in most countries are based on what is referred to as the "arm's length principle" – that is to establish transfer prices based on analysis of pricing in comparable transactions between two or more unrelated parties dealing at arm's length. The OECD has published guidelines based on the arm's length principle, which are followed, in whole or in part, by many of its member countries in adopting rules. The United States and Canadian rules are similar in many respects to the OECD guidelines, with certain points of material difference. A few countries, such as Brazil and Kazakhstan, follow rules that are materially different overall.

The rules of nearly all countries permit related parties to set prices in any manner, but permit the tax authorities to adjust those prices where the prices charged are outside an arm's length range. Rules are generally provided for determining what constitutes such arm's length prices.

Prices actually charged are compared to prices or measures of profitability for unrelated transactions and parties. The rules generally require that market level, functions, risks, and terms of sale of unrelated party transactions or activities be reasonably comparable to such items with respect to the related party transactions or profitability being tested.

Most tax treaties and many tax systems provide mechanisms for resolving disputes among taxpayers and governments in a manner designed to reduce the potential for double taxation. Many systems also permit advance agreement between taxpayers and one or more governments regarding mechanisms for setting related party prices.

Many systems impose penalties where the tax authority has adjusted related party prices. Some tax systems provide that taxpayers may avoid such penalties by preparing documentation in advance regarding prices charged between the taxpayer and related parties. Some systems require that such documentation be prepared in advance in all cases.

The OECD system provides that prices may be set by the component members of an enterprise in any manner, but may be adjusted to conform to an **arm's length standard**. The system provides for several approved methods of testing prices, and allows the government to adjust prices to the midpoint of an arm's length range. Both systems provide for standards for comparing third party transactions or other measures to tested prices, based on comparability and reliability criteria. Significant exceptions are noted below.

Most governments have granted authorization to their tax authorities to adjust prices charged between related parties. Some authorizations, (e.g. the United States, United Kingdom, Canada, and Rwanda – Law 16/2005 DTI), allow domestic as well as international adjustments. Some authorizations apply only internationally. Most, if not all, governments permit adjustments by the tax authority even where there is no intent to avoid or evade tax. Adjustment of prices is generally made by adjusting taxable income of all involved related parties within the jurisdiction, as well as adjusting any withholding or other taxes imposed on parties outside the jurisdiction. Such adjustments generally are made after filing of tax returns

Nearly all systems require that prices be tested using an "**arm's length**" standard. Under this approach, a price is considered appropriate if it is within a range of prices that would be charged by independent parties dealing at arm's length. This is generally defined as a price that an independent buyer would pay an independent seller for an identical item under identical terms and conditions, where neither is under any compulsion to act.

There are clear practical difficulties in implementing the arm's length standard. For items other than goods, there are rarely identical items. Terms of sale may vary from transaction to transaction. Market and other conditions may vary geographically or over time. Some systems give a preference to certain transactional methods over other methods for testing prices.

In addition, most systems recognize that an arm's length price may not be a particular price point but rather a range of prices.

The OECD rules require that reliable adjustments must be made for all differences (if any) between related party items and purported comparatives that could materially affect the condition being examined.

Transactions not undertaken in the ordinary course of business generally are not considered to be comparable to those taken in the ordinary course of business. Among the factors that must be considered in determining comparability are:

- the nature of the property or services provided between the parties,
- functional analysis of the transactions and parties,
- comparison of contractual terms (whether written, verbal, or implied from conduct of the parties),and
- comparison of significant economic conditions that could affect prices, including the effects of different market levels and geographic markets.

Comparability is best achieved where identical items are compared. However, in some cases it is possible to make reliable adjustments for differences in the particular items, such as differences in features or quality.

Buyers and sellers may perform different functions related to the exchange and undertake different risks. For example, a seller of a machine may or may not provide a warranty. The price a buyer would pay will be affected by this difference. Among the functions and risks that may impact prices are:

- Product development
- Manufacturing and assembly
- Marketing and advertising
- Transportation and warehousing
- Credit risk
- Product obsolescence risk
- Market and entrepreneurial risks

- Collection risk
- Financial and currency risks
- Company- or industry-specific items

Manner and terms of sale may have a material impact on price. For example, buyers will pay more if they can defer payment and buy in smaller quantities. Terms that may impact price include payment timing, warranty, volume discounts, duration of rights to use of the product, form of consideration, etc.

Goods, services, or property may be provided to different levels of buyers or users: producer to wholesaler, wholesaler to wholesaler, wholesaler to retailer, or for ultimate consumption. Market conditions, and thus prices, vary greatly at these levels. In addition, prices may vary greatly between different economies or geographies.

Most systems provide variations of the basic rules for characteristics unique to particular types of transactions. The potentially tested transactions include:

- Sale of goods. Identical or nearly identical goods may be available. Product-related differences are often covered by patents.
- Provision of services. Identical services, other than routine services, often do not exist.
- License of intangibles. The basic nature precludes a claim that another product is identical. However, licenses may be granted to independent licensees for the same product in different markets.
- Use of money. Comparable interest rates may be readily available. Some systems provide safe haven rates based on published indices.
- Use of tangible property. Independent comparatives may or may not exist, but reliable data may not be available.

Tax authorities generally examine prices actually charged between related parties to determine whether adjustments are appropriate. Such examination is by comparison (testing) of such prices to comparable prices charged among unrelated parties. Such testing may occur only on examination of tax returns by the tax authority, or taxpayers may be required to conduct such testing themselves in advance or filing tax returns. Such testing requires a determination of how the testing must be conducted, referred to as a transfer pricing method.

Most systems consider a third party price for identical goods, services, or property under identical conditions, called a comparable uncontrolled price (CUP), to be the most reliable indicator of an arm's length price. All systems permit testing using this method, but it is not always applicable.

Among other methods relying on actual transactions (generally between one tested party and third parties) and not indices, aggregates, or market surveys are:

- Cost plus (C+) method: goods or services provided to unrelated parties are consistently priced at actual cost plus a fixed mark-up. Testing is by comparison of the mark-up percentages.

- Resale price method (RPM): goods are regularly offered by a seller or purchased by a retailer to/from unrelated parties at a standard "list" price less a fixed discount. Testing is by comparison of the discount percentages.
- Gross margin method: similar to resale price method, recognised in a few systems.

Some methods of testing prices do not rely on actual transactions. Use of these methods may be necessary due to the lack of reliable data for transactional methods. In some cases, non-transactional methods may be more reliable than transactional methods because market and economic adjustments to transactions may not be reliable.

These methods may include:

- Comparable profits method (CPM): profit levels of similarly situated companies in similarly industries may be compared to an appropriate tested party.
- Transactional net margin method (TNMM): while called a transactional method, the testing is based on profitability of similar businesses.
- Profit split method: total enterprise profits are split in a formulary manner based on econometric analyses.
- CPM and TNMM have a practical advantage in ease of implementation. Both methods rely on microeconomic analysis of data rather than specific transactions. These methods are discussed further with respect to the U.S. and OECD systems.

Two methods are often provided for splitting profits:[1] comparable profit split and residual profit split. The former requires that profit split be derived from the combined operating profit of uncontrolled taxpayers whose transactions and activities are comparable to the transactions and activities being tested. The residual profit split method requires a two step process: first profits are allocated to routine operations, then the residual profit is allocated based on non-routine contributions of the parties. The residual allocation may be based on external market benchmarks or estimation based on capitalised costs.

Where testing of prices occurs on other than a purely transactional basis, such as CPM or TNMM, it may be necessary to determine which of the two related parties should be tested. Testing is to be done of that party testing of which will produce the most reliable results. Generally, this means that the tested party is that party with the most easily compared functions and risks. Comparing the tested party's results to those of comparable parties may require adjustments to results of the tested party or the comparatives for such items as levels of inventory or receivables.

Testing requires determination of what indication of profitability should be used. This may be net profit on the transaction, return on assets employed, or some other measure. Reliability is generally improved for TNMM and CPM by using a range of results and multiple year data.

Valuable intangible property tends to be unique. Often there are no comparable items. The value added by use of intangibles may be represented in prices of goods or services, or by payment of fees (royalties) for use of the intangible property. Licensing of intangibles thus presents difficulties in identifying comparable items for testing. However, where the same property is licensed to independent parties, such license may provide comparable transactional prices. The profit split method specifically attempts to take value of intangibles into account.

Enterprises may engage related or unrelated parties to provide services they need. Where the required services are available within a multinational group, there may be significant advantages to the enterprise as a whole for components of the group to perform those services. Two issues exist with respect to charges between related parties for services: whether services were actually performed which warrant payment, and the price charged for such services. Tax authorities in most major countries have, either formally or in practice, incorporated these queries into their examination of related party services transactions.

There may be tax advantages obtained for the group if one member charges another member for services, even where the member bearing the charge derives no benefit. To combat this, the rules of most systems allow the tax authorities to challenge whether the services allegedly performed actually benefit the member charged. The inquiry may focus on whether services were indeed performed as well as who benefited from the services. For this purpose, some rules differentiate stewardship services from other services. Stewardship services are generally those that an investor would incur for its own benefit in managing its investments. Charges to the investee for such services are generally inappropriate. Where services were not performed or where the related party bearing the charge derived no direct benefit, tax authorities may disallow the charge altogether.

Some jurisdictions impose significant penalties relating to transfer pricing adjustments by tax authorities. These penalties may have thresholds for the basic imposition of penalty, and the penalty may be increased at other thresholds. For example, U.S. rules impose a 20% penalty where the adjustment exceeds USD 5 million, increased to 40% of the additional tax where the adjustment exceeds USD 20 million.[

The rules of many countries require taxpayers to document that prices charged are within the prices permitted under the transfer pricing rules. Where such documentation is not timely prepared, penalties may be imposed, as above. Documentation may be required to be in place prior to filing a tax return in order to avoid these penalties. Documentation by a taxpayer need not be relied upon by the tax authority in any jurisdiction permitting adjustment of prices. Some systems allow the tax authority to disregard information not timely provided by taxpayers, including such advance documentation. India requires that documentation not only be in place prior to filing a return, but also that the documentation be certified by the chartered accountant preparing a company return.

Results of the tested party or comparable enterprises may require adjustment to achieve comparability. Such adjustments may include effective interest adjustments for customer financing or debt levels, inventory adjustments, etc.

[

Tax authorities of most major countries have entered into unilateral or multilateral agreements between taxpayers and other governments regarding the setting or testing of related party prices. These agreements are referred to as **advance pricing agreements** or **advance pricing arrangements** (APAs). Under an APA, the taxpayer and one or more governments agree on the methodology used to test prices. APAs are generally based on transfer pricing documentation prepared by the taxpayer and presented to the government(s).

Multilateral agreements require negotiations between the governments, conducted through their designated **competent authority** groups. The agreements are generally for some period of years, and may have retroactive effect. Most such agreements are not subject to public disclosure rules. Rules controlling how and when a taxpayer or tax authority may commence APA proceedings vary by jurisdiction.

CHAPTER 6
EMERGING TRENDS IN TAXATION

Contents

A Avoidance and Evasion

Evasion of paying tax is a simple breaking of the law whether it be a tax law or any other law.

Avoidance is a means of reducing one's tax liabilities but within the law. Transfer pricing whether it be done within a country or as a cross-border exercise has been used as a means of reducing a tax liability.

Off-shore loans and deposits/bonds are also used as a means of reducing tax. Interest paid on a loan is tax deductible.

A Ltd a resident of R could borrow money from A2 Ltd which is situated in another country, LLY, where the tax laws are more lenient. The Loan from A2 Ltd attracts interest and the income is taxed in LLY. The interest charged to A in R reduces the taxable income of A.

The RRA and the EAC are developing ways and means or reducing avoidance:

- By encouraging tax payers to be good citizens and help pay their dues for the benefit of Rwanda and ultimately themselves.
- By writing and passing laws to make constructive avoidance illegal. This is where an entity takes positive steps to reduce tax liabilities by means of accounting exercises and using "off-shore" entities and transfer pricing as tools.

See Appendix II which is an extract from the RRA Business Plan 2010-2012 and details aims and targets regarding progress on taxation.

RRA see Threats to include

- Smuggling and tax evasion on the increase;
- Tax planning activities by some taxpayers to avoid payment of taxes;
- Continued low level of compliance by taxpayers to pay tax arrears;
- Loopholes existing in taxation laws;

By showing these in such detail indicates that these points will be tackled by RRA officers and by the writing, passing and implementation of Law(s).

B Transfer pricing

Transfer prising has been covered within the Cross-border trading section. But the concept is as valid within a group within one country as it is across borders.

For many years now, Transfer Pricing has not only used as a legitimate means of pricing goods sold between related parties or members within a group, but also for "transferring" profit to/from an otherwise loss making operation – to reduce the tax bill of the profitable operation and as the loss-maker will be making a smaller loss; but a loss carries no tax bill. Where the group companies reside in different locations with different tax regimes, transfer pricing has been used as a means of taking advantage of the differences.

So if A Ltd in Kigali also owned a business in the Republic of Ireland where corporate tax rates are 12%, by selling goods to Ireland at an inflated price, profits could be transferred to Ireland where they could be subjected to lower tax rates. Obviously, in reality, the plan is quite a simple as that, but the principle is there.

The Article 24 of DTI addresses this situation.

First 'related persons' are defined. They include the following categories (Article 24 DTI):

- An individual and his/ her spouse, his/her direct ascendants and descendants
- A company and any person who holds directly or indirectly fifty per cent (50%) or above, in value or by number, of the shares or voting rights in the companies.

In this case, if such parties apply transaction terms other than those which would be employed between independent parties, the Commissioner General of Rwanda Revenue, in conformance with the directives of the Minister of Finance, may direct that the income of one or more of those related persons is to include profits which he/she or they would have made if he/she or they operated as independent persons.

Article 30: Transfer Pricing
Where conditions are made or imposed between related persons carrying out business in their commercial or financial relations which differ from those which would be made between independent persons, the Commissioner General, in accordance with regulations issued by the Minister, may direct that the income of one or more of those related persons is to include profits which he/she of they would have made if he/she or they operated as independent persons.
In order to ensure efficient application of this Article, the Commissioner General may make arrangements in advance with persons carrying out business including money trading, subject to conditions if necessary, that related persons conclude their business in the same way as would be the case between independent persons.

This particular rule is of course an anti-tax-avoidance measure designed to ensure that certain interconnected economic operators do not fix abnormally low or high prices in their business transactions, as this could result in a reduction in assessed incomes and, consequently the tax collected as a result.

The following example is Z Ltd who makes hide skins for drums. Z sells to Y Ltd a member of the consortium as well as to other drum manufacturers.

As with all groups, the internal price is different from the external price. But suppose in example 1 the price is the same. At this price Y Ltd makes a loss of Rwf 150m

	Rwf k/SqM	Metres sold	Rwf K	Rwf k / Drum	Drums	Rwf k
Outside group	12	100,000	1,200,000	45	50,000	2,250,000
Sale to Y Ltd	12	200,000	2,400,000			
		300,000	3,600,000			2,250,000
Hides	4		1,200,000	12	200,000	2,400,000
all other costs	4		1,200,000	20		1,000,000
Costs per unit	8		2,400,000			3,400,000
Taxable profits			1,200,000			-1,150,000
Tax payable			360,000			0

Z pays tax on its profits but Y Ltd pays no tax.

Suppose Z Ltd were to reduce the price charged to Y Ltd to Rwfk 7 per square metre, Y Ltd's loss would reduce to Rwfk -150 but Z Ltd sales would drop to Rwfk 2,600 and profits to Rwfk 200,000.

The tax advantage to the "consortium" would be Rwf 300,000,000

	Rwf k / SqM	Metres sold	Rwf K	Rwf k / Drum	Drums	Rwf k
Outside group	12	100,000	1,200,000	45	50,000	2,250,000
Sale to Y Ltd	7.0	200,000	1,400,000			
		300,000	2,600,000			2,250,000
Hides	4		1,200,000	7.0	200,000	1,400,000
all other costs	4		1,200,000	20		1,000,000
Costs per unit	8		2,400,000			2,400,000
Taxable profits			200,000			-150,000
Tax payable			60,000			0
Group tax bill						60,000
Tax saving on example 1						300,000

But the RRA would question the sale to Y Ltd at a price at lower than cost.

An arm's length price would be considered to be at least cost plus a % markup.

Even so a tax advantage can be gained:

	Rwf k / SqM	Metres sold	Rwf K	Rwf k / Drum	Drums	Rwf k
Outside group	12	100,000	1,200,000	45	50,000	2,250,000
Sale to Y Ltd	9	200,000	1,800,000			
		300,000	3,000,000			2,250,000
Hides	4		1,200,000	9	200,000	1,800,000
all other costs	4		1,200,000	20		1,000,000
Costs per unit	8		2,400,000			2,800,000
Taxable profits			600,000			-550,000
Tax payable			180,000			0
Group tax bill						180,000
Tax saving on example 1						180,000

Even at a "reasonable" price, there can be a tax advantage to the joint venture and more for the shareholders in the way of dividends which are paid out of profits after tax

C Online Taxation

With the increasing use of the internet, tax returns filing and payment are two activities which lend themselves to automation. The use of online filing and payment is at various stages of development around the world.

There are advantages for both taxpayers and the revenue authorities in this.

For the taxpayer the key benefits are:

1. Convenience - they can do their tax returns at a time, and in a place that suits them.
2. Efficiency – they do not have to write out forms, post them, or take them personally to an office.
3. Speed – they can complete their transactions quickly.
4. Audit trail – there is always an electronic record of what has been submitted without the need to keep paper files etc
5. Errors in transcription or electronic reading of forms is reduced

For the tax authorities the key benefits are:

1. Cost of tax collection is reduced. Once the online system is set up, the staff savings can be considerable, as will the savings on paper, postage etc.
2. Compliance Monitoring - with a properly functioning online system the authorities can very quickly focus on non-compliant taxpayers, and with the staff resources freed up from administration can focus more on the high risk areas.
3. Efficiency – the streamlining of tax returns and payments will lead to a more efficient operation.

4. Probable increased compliance – by making it easier for citizens to file and pay returns it is likely that compliance rates will increase.

The Rwanda Revenue Authority has rolled out an electronic tax filing and payment system that allows taxpayers to file and pay for their taxes online. The self-declaration service is available for VAT, PAYE, withholding (lto), consumption (lto) and iqp (lto) tax.

With this new e-tax system, taxpayers no longer need to travel to Rwanda Revenue Authority offices or stand in long queues. A call centre has also been established to provide customer care to taxpayers through telephone enquiries, further reducing the need for customers to travel to the Rwanda Revenue Authority offices for information.

As a result, the processing time for VAT returns, Income Tax returns and PAYE returns has been reduced from 23.5 days to just 1 day. Commercial Banks have also seen the value of this system and are now enrolling to provide e-tax payment services, further promoting the use of the system.

The Investment Climate Facility for Africa has worked with the Rwanda Revenue Authority to develop the e-tax system as part of the drive to modernise Rwanda’s tax administration.

CHAPTER 7.
THE FISCAL REGIME UNDER THE EAC LAW

Tax and EAC

Under EAC Law, business people will continue to pay VAT, Consumption Tax and Withholding Tax on goods originating from EAC Partner States. East African Community (EAC) Member states have begun implementing the Common Market Protocol. This means that Rwanda, Uganda, Kenya, Tanzania and Burundi have entered into a single market with free movement of factors of production based on the principles of non-discrimination, most favoured nation status and transparency.

These rights include the free movement of goods, persons and labour.

EAC citizens also have rights of establishment and residence as well as the free movement of services and capital.

There has been some misconception among the public that under the Common Market regulations, all goods imported into Rwanda or other member states are exempted from taxes. This is not the case however, as taxes on international trade will remain safe from import duty which remains at 0% on all goods from the community that comply with the rules of origin criteria.

If a trader for example imports iron sheets or soap that are manufactured in Kenya (an EAC member state) and has a valid certificate of origin, the RRA will not collect import duty (a tax levied on goods imported into the country) on such goods as long as it is proved the goods are originating from that region.

In Rwanda, the issuance of certificates of origin has been decentralized to the RRA Gikondo Customs department and all border posts including those at Gatuna (on the Rwanda-Uganda border) and Rusumo (on the Rwanda-Tanzania border). While import duty is abolished for qualifying goods, traders will continue to pay other domestic taxes due on goods including Value Added Tax (VAT) of 18 percent, consumption tax (excise duty) as well as a withholding tax of 5 percent.

However, the withholding tax mentioned above is exempt for those who have a tax clearance certificate (“Quitus Fiscale” – this is a certificate widely used within the French legal system which has now been incorporated into Rwandan law).

Free movement of goods under the Common Market rules

The Common Market Protocol stipulates that “The free movement of goods between the Partner States shall be governed by the Customs Law of the Community as specified in Article 39 of the Protocol on the Establishment of the East African Community Customs Union”.

On 1st July, 2009, Rwanda commenced the implementation of the EAC Customs Union rules and began levying zero percent import duty tariffs on goods originating from the Partner States, applying the Common External Tariff and the East African Customs Management Act and Regulations. This was part of a progressive implementation process. Internal tariff elimination on intra-regional trade was introduced progressively between 1st January 2005 and 31st December 2009.

The removal of VAT, Consumption tax (excise duty) and Withholding tax will be effected upon realization of a fully fledged customs union which is yet to materialize. If such a union were to come about, the following might be envisaged; The shifting of borders between Partner States to the periphery of the EAC;

- The collection of duties and taxes at the point of entry into the Customs Union Territory;
- Agreements on the revenue sharing mechanisms to be adopted;
- Establishment of a regional authority to administer the Customs Union
- The elimination of rules of origin on intra-regional trade. In a fully-fledged Customs Union, goods shipped from Nairobi to Kigali for example will not attract any duties and taxes will be considered in the same way as if the goods were between Huye, Southern Province and Musanze, Northern Province for example.

Harmonization of tax policies and laws

The EAC Common Market Protocol provides that "The Partner States undertake to progressively harmonize their tax policies and laws to remove tax distortions in order to facilitate the free movement of goods, services and capital and to promote investment within the Community".

Harmonization of domestic taxes is being handled under the EAC Framework by the Fiscal Affairs Committee (in particular the Technical Committee on tax harmonization) and the Fiscal Affairs Committee has established Technical Working Groups on Value Added Tax, Excise Tax and Income Tax with the aim of developing a harmonized legal framework on tax laws and a roadmap for the harmonization process.

It should also be noted that double taxation agreements and the prevention of fiscal evasion with respect to taxes on income (DTA) was agreed upon by the Partner States and is awaiting legal input from the Attorney Generals before approval by the (The Customs Co-operation Council).

RRA emphasizes that the implementation of the EAC Common Market has not changed the existing fiscal regime and the anticipated changes will progressively be realised as partner states enter into a fully-fledged Customs Union and the harmonisation of tax policies and laws is finalised.

Appendix I

EAST AFRICAN COMMUNITY

The East African Community Customs Management Act, 2004

This Edition of the East African Community Customs Management Act, 2004 *incorporates all amendments up to* 8*th December,* 2008 *and is printed under the authority of Section* 12 *of the Acts of the East African Community Act,* 2004

The student is encouraged to read this act plus amendments and especial reference should be made to:
Part 1 defines terms and develops the valuation of goods being transferred across borders and is quoted below..

The second schedule sub-sections (ss. 18, 19, and 20) Prohibited and restricted imports generally

Third schedule (ss. 70, 71, and 72) prohibited and restricted exports generally – a table of prohibited and restricted goods is tabled.

Fourth schedule (ss. 37 and 122.) Determination of value of imported goods liable to *Ad valorem* import duty

Extracts from the Act amended and published in 2008

PART I

INTERPRETATION:

1. (1) In this Schedule—

"customs value of imported goods" means the value of goods for the purposes of levying *ad valorem* duties of customs on imported goods;

"identical goods" means goods which are same in all respects, including physical characteristics, quality and reputation. Minor differences in appearance shall not preclude goods otherwise conforming to the definition from being regarded as identical;

"similar goods" means goods which, although not alike in all respects, have like characteristics and like component materials which enable them to perform the same functions and to be commercially interchangeable. The quality of the goods, their reputation and the existence of a trademark are among the factors to be considered in determining whether goods are similar.

"identical goods" and "similar goods" do not include, as the case may be, goods which incorporate or reflect engineering, development, artwork, design work, and plans and sketches for which no adjustment has been made under subparagraph (1) (*b*) (iv) or paragraph 9 because such elements were undertaken in the Partner States;

"produced" includes grown, manufactured and mined.

(2) For the purposes of this Schedule—

(a) goods shall not be regarded as "identical goods" or "similar goods" unless they were produced in the same country as the goods being valued;

(b) goods produced by different persons shall be taken into account only when there are no identical goods or similar goods, as the case may be, produced by the same person as the goods being valued.

(3) For the purpose of this Schedule, persons shall be deemed to be related only if:

(a) they are officers or directors of one another's businesses;

(b) they are legally recognised partners in business;

(b) they have an employer and employee relationship;

(c) any person directly or indirectly owns, controls or holds five percent or more of the outstanding voting stock or shares of both of them;

(d) one of them directly or indirectly controls the other;

(e) both of them are directly or indirectly controlled by a third person;

(f) together they directly control a third person; or

(g) they are members of the same family.

(4) A person who associates with another person in business, such that one is the sole agent, distributor or sole concessionaire, however described, of the other shall be deemed to be related for the purposes of this Schedule if they fall within the criteria of sub-paragraph 3.

TRANSACTION VALUE

2. (1) The customs value of imported goods shall be the transaction value, which is the price actually paid or payable for the goods when sold for export to the Partner State adjusted in accordance with the provisions of Paragraph 9, but where—

(a) there are no restrictions as to the disposition or use of the goods by the buyer other than restrictions which:

(i) are imposed or required by law or by the public authorities in the Partner State;

(ii) limit the geographical area in which the goods may be resold; or

(iii) do not substantially affect the value of the goods;

(b) the sale or price is not subject to some condition or consideration for which a value cannot be determined with respect to the goods being valued;

(c) no part of the proceeds of any subsequent resale, disposal or use of the goods by the buyer will accrue directly or indirectly to the seller, unless an appropriate adjustment can be made in accordance with the provisions of Paragraph 9; and

(d) the buyer and seller are not related, or where the buyer and seller are related, that the transaction value is acceptable for customs purposes under the provisions of subparagraph (2).

(2) (*a*) In determining whether the transaction value is acceptable for the purposes of subparagraph (1), the fact that the buyer and the seller are related within the meaning of Paragraph (1) shall not in itself be a ground for regarding the transaction value as unacceptable. In such case the circumstances surrounding the sale shall be examined and transaction value shall be accepted provided that the relationship did not influence the price. If, in light of information provided by the importer or otherwise, the proper officer has grounds for considering that the relationship influenced the price, he shall communicate his grounds to the importer and such importer shall be given reasonable opportunity to respond and where the importer so requests, the communication of the grounds shall be in writing;

(*b*) In the sale between related persons, the transaction value shall be accepted and the goods valued in accordance with the provisions of subparagraph (1) whenever the importer demonstrates that such value closely approximates to one of the following accruing at or about the same time.

(i) the transaction value in sales to unrelated buyers of identical or similar goods for export to the Partner State;

(ii) the customs value of identical or similar goods as determined under the provisions of Paragraph 6;

(iii) the customs value of identical or similar goods as determined under the provisions of Paragraph 7.

Provided that, in applying the provisions under subparagraph (2) (*a*) and (*b*) of this Paragraph, due account shall be taken of demonstrated differences in commercial levels, quantity levels, the elements enumerated in paragraph 9 and costs incurred by the seller in sales in which the seller and the buyer are not related that are not incurred by the seller in sales in which the seller and the buyer are related.

The tests set forth in subparagraph (2) (*b*) are to be used at the initiative of the importer and only for comparison purposes. Substitute values may not be established under the provisions of subparagraph (2) (b).

TRANSACTION VALUE OF IDENTICAL GOODS

3. (1) (*a*) Where the customs value of the imported goods cannot be determined under the provisions of paragraph 2, the customs value shall be the transaction value of identical goods sold for export to the Partner State and exported at or about the same time as the goods being valued:

(*b*) In applying the provisions of this paragraph, the transaction value of identical goods in a sale at the same commercial level and in substantially the same quantity as the goods being valued shall be used to determine the customs value and where no such sale is found, the transaction value of identical goods sold at the different commercial level or in different quantities, adjusted to take account of differences attributable to commercial level or to quantity, shall be used, provided that such adjustments can be made on the basis of demonstrated evidence which clearly establishes the reasonableness and accuracy of the adjustment, whether the adjustment leads to an increase or decrease in the value;

(2) Where the costs and charges referred to in Paragraph 9 (2) are included in the transaction

value, an adjustment shall be made to take account of significant differences in such costs and charges between the imported goods and the identical goods in question arising from differences in distances and modes of transport.

(3) Where in applying the provisions of this paragraph, more than one transaction value of identical goods is found, the lowest such value shall be used to determine the customs value of the imported goods.

TRANSACTION VALUE OF SIMILAR GOODS

4. (1) (*a*) Where the customs value of the imported goods cannot be determined under the provisions of Paragraph 2 and 3, the customs value shall be the transaction value of similar goods sold for export to the Partner State and exported at or about the same time as the goods being valued;

(*b*) In applying this Paragraph, the transaction value of similar goods in a sale at the same commercial level and in substantially the same quantity as the goods being valued shall be used to determine the customs value. Where no such sale is found, the transaction value of similar goods sold at a different commercial level and/or in different quantities, adjusted to take account of differences attributable to commercial level and/or to quantity, shall be used, provided that such adjustments can be made on the basis of demonstrated evidence which clearly establishes the reasonableness and accuracy of the adjustment, whether the adjustment leads to an increase or a decrease in the value.

(2) Where the costs and charges referred to in subparagraph (2) of Paragraph 9 are included in the transaction value, an adjustment shall be made to take account of significant differences in such costs and charges between the imported goods and the similar goods in question arising from differences in distances and modes of transport.

(3) Where, in applying the provisions of this paragraph, more than one transaction value of similar goods is found, the lowest such value shall be used to determine the customs value of the imported goods.

REVERSAL OF ORDER OF APPLICATION OF DEDUCTIVE VALUE AND COMPUTED VALUES

5. Where the customs value of the imported goods cannot be determined under the provisions of paragraphs 2, 3 and 4, the customs value shall be determined under the provisions of paragraph 6 or, when the customs value cannot be determined under that paragraph, under the provisions of paragraph 7 save that, at the request of the importer, the order of application of paragraphs 6 and 7 shall be reversed.

DEDUCTIVE VALUE

6. (1) (a) Where the imported goods or identical or similar imported goods are sold in the Partner State in the condition as imported, the customs value of the imported goods under the provisions of this paragraph shall be based on the unit price at which the imported goods or identical or similar imported goods are so sold in the greatest aggregate quantity, at or about the time of the importation of the goods being valued, to persons who are not related to the persons from whom they buy such goods, subject to deductions for the following:

(i) either the commissions usually paid or agreed to be paid or the additions usually made for profit and general expenses in connection with the sales in such country of imported goods of the same class or kind;

(ii) the usual costs of transport and insurance and associated costs incurred within the Partner State;

(iii) where appropriate, the costs and charges referred to in Paragraph 9 (2); and

(iv) the customs duties and other national taxes payable in the Partner State by reason of importation or sale of the goods.

(b) Where neither the imported goods nor identical nor similar imported goods are sold at or about the time of importation of the goods being valued, the customs value shall, subject to the provisions of subparagraph (1) (a), be based on the unit price at which the imported goods or identical or similar imported goods are sold in the Partner State in the condition as imported at the earliest date after the importation of the goods being valued but before the expiration of 90 days after such importation.

(2) Where neither the imported goods nor identical nor similar imported are sold in the Partner State in the condition as imported, then, if the importer so requests, the customs value shall be based on the unit price at which the imported goods, after further processing, are sold in the greatest aggregate quantity to persons in the Partner State who are not related to the persons from whom they buy such goods, due allowance being made for the value added by such processing and the deductions provided for in subparagraph (1) (a).

COMPUTED VALUE

7. (1) The customs value of imported goods under the provisions of this Paragraph shall be based on a computed value which shall consist of the sum of:

(a) the cost or value of materials and fabrication or other processing employed in producing the imported goods;

(b) an amount for profit and general expenses equal to that usually reflected in sales of goods of the same class or kind as the goods being valued which are made by producers in the country of exportation for export to the Partner State;

(c) the cost or value of all other expenses necessary to reflect the costs added under Paragraph 9 (2).

(2) A person who is not resident in the Partner State may be required to, or compelled to produce for examination, or to allow access to, any account or other record for the purposes of determining a computed value. However, information supplied by the producer of the goods for the purposes of determining the customs value under the provisions of this Paragraph may be verified in another country by a proper officer with the agreement of the producer and provided sufficient advance notice is given to the government of the country in question and the latter does not object to the investigation.

FALL BACK VALUE

8. (1) Where the customs value of the imported goods cannot be determined under the provisions of Paragraphs 2, 3, 4, 5, 6 and 7, inclusive, the customs value shall be determined using reasonable means consistent with the principles and general provisions of this Schedule and on the basis of data available in the Partner State.

(2) Customs value shall not be determined under the provisions of this paragraph on the basis of:

(a) the selling price in the Partner State of goods produced in the Partner State;

(b) a system which provides for the acceptance for customs purposes of the higher of two alternative values;

(c) the price of goods on the domestic market of the country of exportation;

(d) the cost of production other than computed values which have been deter- mined for identical or similar goods in accordance with the provisions of Paragraph 7;

(e) the price of the goods for export to a country other than the Partner State;

(f) minimum customs values; or

(g) arbitrary or fictitious values.

(3) Where the importer so requests, he or she shall be informed in writing of the customs value determined under the provisions of this paragraph and the method used to determine such value.

ADJUSTMENTS TO VALUE

9. (1) In determining the customs value under the provisions of Paragraph 2, there shall be added to the price actually paid or payable for the imported goods as follows:

(a) to the extent that they are incurred by the buyer but are not included in the price actually paid or payable for the goods:

(i) the commissions and brokerage, except buying commissions;

(ii) the cost of containers which are treated as being one for customs purposes with the goods in question;

(iii) the cost of packing whether for labour or materials;

(b) the value, apportioned as appropriate, of the goods and services where supplied directly or indirectly by the buyer free of charge or at reduced cost for use in connection with the production and sale for export of the imported goods, to the extent that such value has not been included in the price actually paid or payable as follows:

(i) materials, components, parts and similar items incorporated in the imported goods;

(ii) tools, dies, moulds and similar items used in the production of the imported goods;

(iii) materials consumed in the production of the imported goods;

(iv) engineering, development, artwork, design work, and plans and sketches undertaken elsewhere than in the Partner State and necessary for the production of the imported goods;

(c) royalties and licence fees related to the goods being valued that the buyer must pay, either directly or indirectly, as a condition of sale of the goods being valued, to the extent that such royalties and fees are not included in the price actually paid or payable;

(d) the value of any part of the proceeds of any subsequent resale, disposal or use of the imported goods that accrues directly or indirectly to the seller.

(2) In determining the value for duty purposes of any imported goods, there shall be added to the price actually paid or payable for the goods:-

(a) the cost of transport of the imported goods to the port or place of importation into the Partner State; provided that in case of imports by air no freight costs shall be added to the price paid or payable;

(b) loading, unloading and handling charges associated with the transport of the imported goods to the port or place of importation into the Partner State; and

(c) the cost of insurance.

(3) Additions to the price actually paid or payable shall be made under this paragraph only on the basis of objective and quantifiable data.

(4) Additions shall not be made to the price actually paid or payable in determining the customs value except as provided in this paragraph.

Following this schedule is a Section headed “Interpretative Notes”. The student is encouraged to read these notes.

Appendix II

Extract from Rwanda revenue Authority Business Plan 2011-2012

RRA Business Plan 2011-2012

2 INTRODUCTION

The current RRA medium-term strategy covers the period from July 2010 to June 2013. Major activities to be performed by the authority remain aligned to the three year period strategy. RRA s strategic directions for the said period are as follows:

a) Maximisation of revenue mobilisation;
b) Service delivery;
c) Encourage voluntary compliance and broaden tax base;
d) Further strengthen the capacity of the organisation.

This however, means that every year, a business plan must be prepared, that is in line with this medium term strategy**.**

The 2011/2012 RRA business plan sets out the major activities and strategies to achieve those activities and indicators upon which success will be measured. This plan is embedded in the 2010/2013 RRA's Medium Term Strategy framework.

Part one of the 2011/2012 business plan reflects RRA's major Corporate Statements that include: the overall mission, vision, core values and SWOT analysis. Part two of the plan deals with the priorities as well as key indicators by which performance against objectives and planned activities during the year 2011/2012 will be monitored.

3 CORPORATE STATEMENTS

RRA s corporate statements remain unchanged for the 2011/2012 business plan; priorities are aligned to the following **RRA s vision**, **mission and core values:**

Mission is:

"*Mobilise revenue for national development through efficient and equitable services that promote business growth*."

RRA s Vision is:

To become a world-class efficient and modern revenue agency, fully financing national needs.

Core values:

- *Integrity;*
- *Customer focus;*
- *Transparency;*
- *Professional Service delivery;*
- *Teamwork.*

4 RRA SWOT ANALYSIS

4.1 Strengths

- Strong commitment of RRA staff;
- Improved planning processes;
- Taxpayers education strategy;
- Computerization of core business functions and availability of good IT
- infrastructure leading to efficient service delivery and enhanced revenue collection;
- Operational block management system in every district of Kigali City;
- Collection of National Social Security Fund contributions with associated benefits for PAYE compliance;
- Licensing of tax advisors that streamlines tax profession and increases taxpayer s compliance;
- Effective implementation of EAC Customs Union Management Act and Common Market Protocols;
- Enhanced trade facilitation in domestic and cross border operations;
- Existence of sophisticated equipment to detect and prevent smuggling;
- ISO 9001 2008 certified;
- Existence of a fully fledged in house training institute;
- Flexible management of financial resources;
- Decentralized services.

4.2 Weaknesses

- Slowness to adopt change management;
- Some cases of poor customer care and service delivery;
- Inadequate skills in ICT among staff and limited integration of IT systems;
- Limited skills in some technical areas (e.g. risk management, transfer pricing, mining taxation, e-commerce and cross border transactions);
- Lack of proper management of tax expenditures;
- Staff shortage as a result of more responsibilities to RRA and continued staff turnover due to comparatively better remuneration by the private sector;
- Low response levels and ineffective communication;
- Weak audit function and refund processes;
- Delays in revenue data reconciliation exercise;
- Low quality data from the point of data capture up to dissemination point;
- Poor document and data management;
- Corruption practices amongst some RRA officers;
- Lack of a sound welfare scheme;
- Lack of an effective monitoring and evaluation mechanism for monitoring corporate priorities and projects;
- Poor reading and research culture among RRA staff;
- Slow payment process of suppliers;
- Failure to implement procurement plan well;
- Poor working environment for some RRA offices.

4.3 Opportunities

- Strong government support;
- Strong partnership with both internal and external stakeholders;
- Stable political and economic environment;

- Certification of taxpayers financial statements;
- Existing forum and good relations with the private sector;
- Planned new initiatives to facilitate trade and improve service delivery e.g. etax, electronic cargo tracking equipment, construction of more One-Stop- Border posts;
- Introduction of electronic tax registry to manage VAT;
- Regional and international cooperation agreements (EARAs[1], HMRC[2], and SARS[3]);
- Membership to African Tax Administration Forum (ATAF);
- All-inclusive national ICT strategy

4.4 Threats

- Low level of record-keeping and accounting skills within business community;
- Illiteracy of majority of small taxpayers negatively impacts on the accuracy of tax returns filed;
- Tax base erosion due to increasing tax-incentives and exemptions demands;
- Informal sector growth;
- Smuggling and tax evasion on the increase;
- Tax planning activities by some taxpayers to avoid payment of taxes;
- Continued low level of compliance by taxpayers to pay tax arrears;
- Globalization challenges petroleum prices, food prices, e-commerce & trade facilitation demands.
- Low commitment of some stakeholders towards the implementation of shared projects leading to failure of these projects kicking off;
- Failure by some suppliers to honour the provision of services causing unnecessary delays in projects implementation;
- Loopholes existing in taxation laws;
- IT security threats;
- Network failures that negatively affect service delivery and work productivity;

5. PRIORITIES FOR 2011/2012

Having examined the environment in which we work and our organisational capabilities, we have set the following priorities with the corresponding activities to orient the organisation towards realising the strategic objectives over the period of this plan.

5.1 Maximization of revenue mobilisation

- Achieve revenue targets Rwf 515.5 billion.
- Furnish operational functions with appropriate resources to handle tasks before them.
- Identify measures to cover loopholes in the process of granting incentives.
- Analyse different options to improve efficiency of major tax heads (PAYE, VAT).
- Prepare a proposal to retake some decentralised taxes.

5.2 Service delivery

- Establish more revenue collection and service centres.
- Upgrade the CSR system to streamline its administration.
- Implement electronic services to improve delivery.

---

[1] East African Revenue Authorities
[2] Her Majesties Revenue and Customs of UK
[3] South African Revenue Service

- Commence construction of One Stop Border Posts.
- Initiate pre-arrival request for exemptions.
- Implement Authorised Economic Operator Program.
- Implement Regional Customs Transit Bond Guarantee Scheme.
- Conduct EAC regional time release study.
- Extend simplified trade regime at borders with Burundi, Tanzania and DRC.
- Carry out a feasibility study to increase border posts threshold.
- Test and implement RADDEX interconnectivity with TRA and OBR.
- Conduct focused taxpayers training programs by sector of activities and by category of taxpayers.

5.3 Encourage voluntary compliance and broaden the tax base

- Develop a simplified tax declaration and accounting system for SMEs, translated in Kinyarwanda language.
- Draft a new tax regime for the identified SME category.
- Identify loopholes existing in tax laws and administrative procedures and recommend amendments.
- Introduce electronic transaction devices (ETD) to improve VAT productivity.
- Integrate CSR software with the tax system and harmonise PAYE and CSR declaration forms.
- Acquire and implement electronic cargo tracking system.
- Establish and implement a name and shame mechanism for non-compliant taxpayers.
- Enhance SIGTAS to deliver a single view taxpayer account.
- Waive off/suspend old and enforce recoverable tax arrears.
- Participate in a study aimed at widening the tax base.
- Connect RRA system to national ID registry office.

5.4 Further strengthen the capacity of the organization

- Carry out a study on current RRA performance and propose reform initiatives to improve efficiency.
- Train staff in areas that will impact revenue mobilization, customer service and management functions.
- Streamline customs process and procedures as well as customs work environment for the acquisition of CSD ISO certification.
- Organise benchmarking and attachment programs for staff in revenue collection operations in best performing revenue administrations.
- Conduct a study on establishing electronic filing and archive management system.
- Carry out a study for the expansion of RRA Training Institute.
- Replace RRA servers and install new ones to ensure business continuity.
- Enhance RRA networking system.
- Upgrade SAGE to include document management modules.
- Acquire and use new HR management software.
- Connect RRA to RITA Government network.
- Prepare RRA s data by sector of activity.

6. CASCADING KEY OBJECTIVES PROCESS

The above key activities set out what the organisation will do to achieve the set strategic objectives and how these will be measured. In order to ensure that we remain on course and ensure that RRA staff perform activities aligned to the corporate goals, a cascading process

that involves further breaking down of the corporate level activities was done at the departmental level.
Each department has developed a detailed business plan indicating schedule of activities and timeline guided by the corporate level priorities as reflected in this plan.
Each activity to be performed shows the responsible department as well as the timeline. This will help in ensuring effective implementation of this business plan and making reviews to avoid any possible slippages. This will keep the entire organisation focused towards achieving the vision.

Appendix III a

CIT Real Regime Tax Calculator

5	Business income	(annual turnover)
10	Cost of goods sold	(line 170 of annex A)
15	Gross Profit	(Line 5-line10)
20	Expenses	(line 285 of annex A)
25	Depreciation	line599 of annex A):
30	Total expenses and depreciation	(add lines 20 through 25):
35	Net operating income	(subtract line 30 from line 15):
40	Investment income	(line15 of annex B):
45	Non operating & Extraordinary income	(sum of Line 25 through 40
50	Total income	(addline35 through 45):
55	Non operating & extraordinary expenses	
60	Investment expenses	(line35 of annex B):
65	Net income	(line50-line55-line60):
70	Reintegration of non-deductible expenses	
75	Depreciation adjustment	(+/-)
80	Loss of carried forward from previous five tax periods	
85	Taxable income	(add line65 through line75)-line80:
90	Corporate income tax	(line85 * 30%)
95	Tax discounts	(brought forward from line 160):
100	Foreign tax credit	(line65 of annex C):
105	Corporate income tax payable	
110	Quarterly prepayments	(line70 of annex D):
115	Withholding on imports	
120	Withholding on public tenders	
125	Withholding on other payments	(investments, service fees):
130	Total credits	(sum line 110 through 125):
135	Overpayment from previous periods	
140	Net tax due/credit (subtract line140+line145 from line110):	
145	Refund claimed	
150	Balance	

Appendix III b

PIT Real Regime Calculator

5	Self-employment income (line 135 of annex B)			
10	Cost of goods sold	(line 170 of annex B)		
15	Gross Profit	(Line 5-line10)		
20	Expenses	(line 290 of annex B)		
25	Net operating income	Deduct line 20 from 15		
30	Employment Income	Line 25 of Annex A		
35	Investment income	Line 15 of annex C		
40	Non operating and extraordinary income			
45	Total Income	(sum of Line 25 through 40		
50	Employment deductions	Line 25 of Annex A		
55	Investment expenses	Line 35 of annex C		
60	Non operating & Extra-ordinary expenses			
65	Total expenses	sum of line 50 through 60		
70	Net income	subtract line 65 from line 45		
75	Reintegration of non deductible expenses			
80	Depreciation adjustment			
85	Loss carried forward from previous tax periods			
90	Taxable income (add line 70 and line 75 and +/- line80)-line85			
95	Personal income tax			
100	Tax discounts	(brought forward from line 175)		
105	Foreign tax credit	Line 65 of annex E		
110	Personal income tax payable	(line 95 -(line 100+line 105)		
115	Quarterly prepayments (line 70 of annex F)			
120	Withholding on imports			
125	Withholding on public tenders			
130	Withholding on other payments (investments, service, fees			
135	Withholding on payments (PAYE)			
140	Total of credits	(sum line 115 through 135)		
145	Overpayment from previous periods			
150	Net tax due/credit (Subtract line 140 + line 145 from line 110			
155	Tax refund claim			
160	Balance			