TAXATION

Senior **4** Student Book

ACCOUNTING PROFESSION OPTION

Experimental Version

FOREWORD

Dear Student,

Rwanda Basic Education Board (REB) is honoured to present Senior 4 Taxation book for the students of Accounting Profession Option which serves as a guide to competence-based teaching and learning to ensure consistency and coherence in the learning of the Taxation. The Rwandan educational philosophy is to ensure that you achieve full potential at every level of education which will prepare you to be well integrated in society and exploit employment opportunities.

The government of Rwanda emphasizes the importance of aligning teaching and learning materials with the syllabus to facilitate your learning process. Many factors influence what you learn, how well you learn and the competences you acquire. Those factors include the relevance of the specific content, the quality of teachers' pedagogical approaches, the assessment strategies and the instructional materials available. In this book, we paid special attention to the activities that facilitate the learning process in which you can develop your ideas and make new discoveries during concrete activities carried out individually or in groups.

In competence-based curriculum, learning is considered as a process of active building and developing knowledge and meanings by the student where concepts are mainly introduced by an activity, situation or scenario that helps the student to construct knowledge, develop skills and acquire positive attitudes and values.

For efficiency use of this textbook, your role is to:

- Work on given activities which lead to the development of skills;
- Share relevant information with other students through presentations, discussions, group work and other active learning techniques such as role play, case studies, investigation and research in the library, on internet or outside; Participate and take responsibility for your own learning;
- Draw conclusions based on the findings from the learning activities.

To facilitate you in doing activities, the content of this book is self-explanatory so that you can easily use it yourself, acquire and assess your competences. The book is made of units as presented in the syllabus. Each unit has the following structure: the unit title and key unit competence are given and they are followed by the introductory activity before the development of taxation concepts that are connected to real world of economic environment.

The development of each concept has the following points:

- Learning activity which is a well set and simple activity to be done by students in order to generate the concept to be learnt;
- Main elements of the content to be emphasized;
- Worked examples; and
- Application activities to be done by the user to consolidate competences or to assess the achievement of objectives.

Even though the book has some worked examples, you will succeed on the application activities depending on your ways of reading, questioning, thinking and handling calculations problems not by searching for similar-looking worked out examples.

Furthermore, to succeed in Taxation, you are asked to keep trying; sometimes you will find concepts that need to be worked at before you completely understand. The only way to really grasp such a concept is to think about it and work-related problems found in other reference books.

I wish to sincerely express my appreciation to the people who contributed towards the development of this book, particularly, REB staff, RRA Officers, development partners, Universities Lecturers and Secondary school Teachers for their technical support. A word of gratitude goes to Secondary Schools Head Teachers, Administration of different Universities (Public and Private Universities) and development partners who availed their staff for various activities.

Any comment or contribution for the improvement of this textbook for the next edition is welcome.

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ACRONYMS AND ABBREVIATIONS

BNR : National Bank of Rwanda

CBHI : Community Based Health Insurance

CIT : Corporate Income Tax

FDA : Food and Drug Authority

FDAR : Food and Drug Authority Rwanda

FRW : Rwandan Francs

IRS : Internal Revenue Service

MDR : Middle Daily Remuneration

MMI : Military Medical Insurance

MMR : Middle Monthly Remuneration

PAYE : Pay As You Earn

PIT : Personal Income Tax

RAMA: La Rwandaise d'Assurance Maladie

RDB : Rwanda Development Board

RRA : Rwanda Revenue Authority

RSB : Rwanda Standards Board

RSSB : Rwanda Social Security Board

RURA : Rwanda Utilities Regulatory Authority

SEZ : Special Economic Zone

TWDV : Tax Written Down Value

VAT : Value Added Tax

VUP : Vision Umurenge Programme

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UNIT 1

INTRODUCTION TO RWANDAN TAX SYSTEM

Key unit competence: Describe various Rwandan tax system legislation

Introductory activity: A case study

Every year around, before and after June 15, everybody especially business people will be discussing about tax changes in the national budget. This is because tax reforms and new taxes introduced are announced on that day. However, have you ever wondered why you and businesses need to pay taxes?

In Rwanda, there are arms of the government (ruling bodies) from the Village, Cell, Sector, and District, Provincial and National levels. These bodies comprise: legislature (who make laws), executives (who enforce laws) and judiciary (who exercise laws). Paying taxes is a civic duty, although doing so is also a requirement of the law.

Taxes take many forms too. When you work at a job to make money, you pay income taxes. Depending on how much money you earn, a certain percentage (part) of the money you make is withheld (kept out of your pay check and sent to the government).

- When you buy things at a store, you also usually pay sales tax, which is a percentage of the cost of the item charged by the store. If you own property, you also pay property taxes on the value of your property.

If you do not pay your taxes, the government agency that oversees taxes the Rwanda Revenue Authority (RRA) - will require you to pay your taxes or else face penalties, such as fines or going to jail.

The money you pay in taxes goes to many places. In addition to paying the salaries of government workers, your tax also helps to support common resources, such as police and fire fighters.

- Tax money helps to ensure the roads you travel on are safe and well-maintained. Taxes fund health facilities such as health centers and hospitals, education, public libraries, parks and ensuring security in the country and many other public utilities. Taxes are also used to fund many types of government programs that help the poor and less fortunate, as well as many schools!

Each year as the "Tax Day" rolls in, adults of all ages and businesses must report their income to the RRA, using special tax forms. There are many laws that set forth complicated rules about how much tax is owed and what kinds of special expenses can be used ("written off") to lower the amount of taxes you need to pay

For the average worker, tax money has been withheld from pay checks throughout the year. On "tax day," each worker reports his or her income and expenses to the RRA.

Employers also report to the RRA how much they paid each worker. The RRA compares all these numbers to make sure that each person pays the correct amount of taxes.

If you have not had enough tax money withheld from your checks throughout the year to cover the amount of tax you owe, you will have to send more money ("pay in") to the government. If, however, too much tax money was withheld from your pay checks, you will receive a check (get a "refund") from the government.

Referring to the passage answer the following questions:

- What are the major changes expected by people especially business people on June 15, every year?
- What makes the business people so anxious to know the changes mentioned above in question1?
- Why do you think it is important for businesses to pay taxes to the government?

- How do the following benefit from taxes?
  i. Entrepreneur.
  ii. Government.
  iii. Society.
- Identify and briefly explain at least two types of taxes paid in Rwanda?
- What happens to businesses or people who do not pay taxes?
- What is the difference between tax and taxation?

1.1. Meaning of taxation, tax and duty

Activity 1.1

Q1. Assume, your parents have restaurant in Kigali city; -help them to understand that compulsory imposed to them and its contribution for public purposes.

Q2. What do you think is the purpose of taxation?

1.1.1. Meaning of a taxation

Taxation is a term for when a taxing authority, usually a government, levies or imposes a tax. The term "taxation" applies to all types of involuntary levies, from income to capital gains to estate taxes. Thus, taxation is a system being used by Government to serve general public interest.

Taxation is a system of raising money or revenues by the government from individuals/business and companies by law through taxes.

1.1.2. Tax

A tax is generally referred to as a compulsory levy imposed by the government upon assessment. Tax is fees charged (levied) by government on product, income or activity. Tax is also defined as a compulsory levy or charge by the state to its citizens and non-citizens that are usually payable in monetary form. The collected fund is then used to fund different public expenditure programs. The main types of taxes are direct tax and indirect tax.

1.1.3. Duty

In general, duty refers to the tax imposed on goods when they are transported across international borders. In simple terms, it is the tax that is levied on import and export of goods. The government uses this duty to raise its revenues, safeguard domestic industries, and regulate movement of goods.

Application activity 1.1

1. What do you think for the meaning of taxation?
2. In your own words, explain why the institution called “Rwanda Revenue Authority (RRA) “has been given the mandate of collecting tax.

1.2. Current legislation relating to taxation and tax periods

Activity 1.2

Referring to the activities in the previous lesson 1.1, do you think it is important to know taxation for business operations, what is the final resting place of a tax or the person or company that actually pays the tax?

1.2.1. Current legislation relating to taxation

The basis of taxation in Rwanda is derived from article 164 of the constitution of Rwanda (2003), which states “No taxation can be imposed, modified or removed except by law”.

It also states: “No exemption from or reduction in tax may be granted unless authorized by law”.

Thus, laws are required to impose taxes, or to exempt a person or a transaction from tax.

This is put into action by income tax law as organic law. Further ministerial orders and commissioner general rules assist in the implementation of the law once approved, these are gazette (published) and become law.

The taxation background in Rwanda is very dynamic. This is evidenced by different changes introduced in tax legislation:

- Taxations in Rwanda dates way back in 1912 when property tax was introduced.
- After independence, taxes were formally introduced in Rwanda by the law of the 2nd June 1964 concerning Profit tax.
- Recently in April 2018, Law N° 016/2018 of 13/04/2018 establishing Taxes on income repealed the law n° 16/2005 of 18/08/2005 was introduced.
- Customs and excise duties were also introduced by the law of 17th July 1968.
- The East African Community Customs Management act 2004.
- Law N° 34/2015 of 30/06/2015 establishing the infrastructure development levy on imported goods.
- Law N° 19/2017 of 28th/04/2017 establishing the levy on imported goods financing African Union activities.
- Law N° 35/2015 of 30th/06/2015 establishing the levy on petrol and gas oil for road maintenance.
- In 2001 VAT law was introduced requiring taxpayers to start paying Value Added Tax.
- The current VAT law is Law 40/2016 of 15th/10/2016 modifying and complementing Law N° 37/2012 of 09th/11/2012.
- Law N° 75/2018 of 07th/09/2018, law determining the sources of revenue and property of decentralized entities.
- Law N° 025/2019 of 13th/09/2019 establishing the Excise Duty.
- Law N° 29/2012 of 27th/07/2012 establishing tax on gaming activities.
- Law N° 55/2013 of 02th/08/2013 on minerals tax.
- Law N° 14/2009 of 30th/06/2009 determining motor vehicle registration fees.

All the above laws are related either to direct taxes or indirect taxes. Besides Law No 026/2019 of 18th/09/2019 on Tax procedures, the main law on direct taxation in Rwanda is law 016th/2018 of 13th/04/2018.

1.2.2. Types of taxes, their advantages and disadvantages

There are two main types of taxes, direct tax and indirect tax

a) **A Direct tax** is a tax on the income or wealth of a person. It is recovered generally from that person under previously enacted legislation; an example would be income tax.

Advantages of direct tax

- Cheap to collect
- Convenient to pay because they are spread over a long period
- Direct taxes are flexible and are easily increased and decreased
- They are simple to understand
- Most direct taxes are progressive since the rich people pay taxes at higher rate than the rates at which the poor people pay.
- Direct taxes are very effective at redistributing national income among the population.

Disadvantages of direct tax

- In the developing countries with high levels of unemployment income are very low and so the revenue that is generated from direct taxes is always very low.
- Costs of assessment and collection are high when the tax payers are scattered in different locations.
- It is difficult to measure the taxable capacity of the people to determine how much income tax they have to pay. This leads to either over taxation or under taxation.
- Direct taxes are easy to evade as people cannot conceal their income. Others get income from many sources and are not resident in a single place. This makes assessment and collection very complicated as a consequence, people evade the taxes.

b) An **indirect tax** is a tax on production, exchange or consumption of goods or services. It is charged at the time a taxable operation is carried out. This is the case for VAT and excise duty.

Advantages of indirect tax

- Convenient to pay as they are paid together with the price of commodities in installment.
- There is less tax evasion since they are included in the price of commodities.
- Indirect taxes cover a wide range of taxable items and therefore raise more revenue.
- A tool to control the production and the consumption of harmful goods like cigarettes, alcohol, etc…

- Tool to protect domestic industries against competition from foreign producers and dumping.
- Indirect taxes are the most important sources of government revenues since they are based on consumption of goods and services and yet the consumer has got full control and decision power to spend or not.

Disadvantages of indirect tax

- Indirect taxes are regressive in nature and therefore don't satisfy the principle of equity since the rich and the poor pay the same amount of taxes on the same essential goods consumed.
- Indirect taxes are inflationary in nature as they increase prices of goods and services hence increasing costs of production, costs of living, therefore leading to demand for higher wages.
- Being consumption tax, indirect taxes are unavoidable.

1.2.3. Tax period

There is no way somebody can understand the concept of tax period without making the difference between tax period itself, fiscal year and budget year.

Fiscal Year is a period of twelve (12) months that begins on January 1 and ends on December 31 the same year.

Budget year is a period of twelve (12) months that begins on July 1 and ends on June 30 of the following year.

"Tax period" means the period of time at the end of which the tax liability accrues. In some documentation, tax period is referred as fiscal year.

1. Tax period for individuals

A tax period is the period for which tax is calculated and paid.

An individual, whether they are in business or employed, will calculate their tax in relation to the calendar year (from 1 January to 31st December) is known as the tax period.

2. Tax period for companies

The default tax period for a company is also the calendar year. However; companies may apply in writing to the minister of finance to use a different

12 – month period, under the following conditions:

- The company is required to prepare its accounts under Generally Accepted Accounting Principles (GAAP); and

- The company presents a sound reason for using an alternative tax period (for example, aligning their accounting date with a head office or parent company)

Once a company has been granted approval to change the date, it must approach the Rwanda Revenue Authority (RRA) so that they configure the new dates in their tax system. Failure to do so may result in penalties.

All in all, the tax period may be different from the fiscal year depending on the type of tax:

- **For CIT**, tax period is always annual.
- **For PIT**, tax period is annual.
- **For PAYE**, tax period is monthly but may be quarterly on request,
- **For VAT**, tax period is monthly but may be quarterly on request for those who have a turnover which is less than FRW 200,000,000.
- For excise duty, tax period is every 10 days starting with the beginning of each month.

Application activity 1.2

- Using examples differentiate direct taxes from indirect taxes.
- The government of Rwanda introduced the local industry promotion named as “Made in Rwanda”. Explain how the government could use the taxes in order to protect domestic industries.

1.3. The Residence and the Permanent Establishment (PE)

Activity1.3

Analyze the photos above and answer the questions that follow.

1. What is the residence?
2. Discuss on the permanent establishment.

1.3.1. Meaning of residence

A person or a company's residence position determines their liability to pay Rwandan tax, especially on overseas income source.

An individual is considered to be a resident in Rwanda if he/she fulfils one of the following conditions:

- He/she has a permanent residence in Rwanda
- He/she has a habitual abode in Rwanda
- He/she is a Rwandan representing Rwanda abroad
- An individual, who stays in Rwanda for more than 183 days in 12-month period, either continuously or intermittently, is considered to be a resident in Rwanda for the tax period in which the 12-month period has ended.

A person other than a natural person may be also considered as a resident in Rwanda during a tax period if:

- It is a company established under Rwandan law
- It has a place of effective management in Rwanda
- It is a Rwanda Government company.

If any entity has a business in Rwanda, its effective management is determined by looking at factors such as:

- The day-to-day control and management
- Where shareholder's meeting is held
- Where the accounting records are kept
- The residence of the main shareholders and directors
- The existence of a business in Rwanda carried on through technological means (eg a trading website)

1.3.2. The impact of residence

A Rwandan resident person is generally liable to Rwandan income tax on their worldwide taxable income. Whereas non-resident persons are only liable to income tax on income generated in Rwanda the same principle applies to Rwandan resident companies. They are liable to Rwandan corporate income tax on their worldwide profits, whereas a non-resident company is only liable to Rwanda corporate income tax on a profit generated through Rwandan permanent establishments.

1.3.3. The Permanent Establishment (PE)

The Permanent Establishment (PE) definition.

Permanent establishment is defined by the law n° 026/2019 of 18/09/2019 on tax procedures, chapter one called general provisions in article 3 as a fixed place of business through which an income generating business wholly or partially conducted.

a) Activities considered permanent establishments

The following are considered permanent establishments according to Rwandan law:

- A place of management
- A branch
- A factory or workshop
- A mine, an oil or any other place for an exploitation of natural resources
- A site set of construction, construction site, or a place where supervision or assembly work are carried out
- A place for the provision of services, including consulting services, carried on by a person, with the support of employees or other personnel, for more than 90 days in a 12 –month period either continuously or intermittently.

b) Activities not considered permanent establishments

The following shall not be deemed to be operations through permanent establishments:

- The use of facility solely for the purpose of storage or display of goods or merchandise belonging to the enterprise
- The maintenance of goods belonging to the enterprise for the purpose of display or storage
- Maintenance of stock of goods for the purpose of processing
- Maintenance of fixed place of business solely for the purpose of purchasing goods for the enterprise

Maintenance of a fixed place of business solely for the purpose of carrying on for enterprises any other activities.

Application activity 1.3

- Explain the determinants the residence of natural persons
- Describe the activities considered permanent establishments

1.4. List the rights and obligations of the taxpayer according to Rwandan tax system

Activity 1.4

Kabera and her mother want to start a shop in Musanze district of selling clothes in Musanze shop. Her mother is suggesting that before starting they should meet all taxpayer requirements but Kabera doesn't understand why he should do that. He wants to start without wasting time. Help Kabera to understand the five (5) requirements that any taxpayer needs to start a shop.

1.4.1. The rights of the taxpayer according to Rwandan tax system

i. The right to be informed, assisted and heard

Taxpayer is entitled to have up-to-date information on the operation of the tax system and the way in which their tax is assessed.

ii. The right of appeal

The right of appeal against any decision of the tax authorities applies to all taxpayers and to almost all decisions made by the tax authorities, whether as regards the application of the law or of administrative ruling, provided the taxpayer is directly concerned.

iii. The right to pay no more than the correct amount of tax

Taxpayers should pay no more tax than is required by the tax legislation, taking into account their person circumstances and income.

iv. The rights to confidentiality and secrecy

Another basic taxpayers' right is that the information available to the tax authorities in the records of a taxpayer is confidential and will only be used for the purposes specified in tax legislation. Tax legislation usually imposes very heavy penalties on tax officials who misuse confidential information. The confidentiality rules that apply to tax authorities are far stricter than those applying to other government departments.

1.4.2. The obligations of the taxpayer according to Rwandan tax system

i. Relevant legislation

Taxpayer obligations are mainly governed by law No 026/2019 on Tax procedures.

ii. Registration of a business

Articles 11 and 12 of law 026/2019 specify that an individual must register with the Rwandan Revenue Authority within seven days (7days) of setting up a business or company, or starting to generate taxable income. The tax administration will then issue the taxpayer with the tax identification number (TIN), which they will use when communicating with the tax authorities and submitting their tax returns. In particular, the taxpayer should quote their TIN on all returns and backing documentation submitted to the tax administration.

iii. Record-keeping

Taxpayers are obliged to keep records to support the information contained within their tax declaration.

This rule applies to:

- All companies
- Individuals engaged in business, professional or vocational occupations, except where their turnover is less than FRW 1,200,000 per tax period

The types of records that are required to be kept depend on the size of the business. All businesses (except individuals exempted under the rule above) are required to keep the following books and records:

- Calculations of tax liability

- Documentation of withholding taxes charged
- Documentation showing the obligation to file declaration of a tax withheld, such as the residence details of the recipient of a payment subject to withholding tax.

In addition to this, businesses with turnover in excess of FRW 20,000,000 per year are obliged to keep the following records:

- Business assets and liabilities
- Daily records of income and expenditures
- Purchases and sales of goods and services related to the business
- Records of closing trading stock

Lastly, companies only are required to follow a double entry bookkeeping system and to accompany their tax declaration with a full set of accounts prepared to the date of the tax period.

The records must be kept for a period of ten years (10years) following the end of the tax period. They must be at the taxpayer's premises.

iv. Tax declarations

Articles 13 and 50 of law 16/2018 deal with tax declarations for individual and companies respectively.

Taxpayers must usually file tax declaration to the tax administration by 31 March following the end of tax period (this is the case of profit tax using tax period from 1st January to 31st December). The tax declaration for taxpayers in business will include the accounts (a balance sheet, profit and loss account and other notes prepared under local GAAP), and other documents as required by tax administration. Individuals can be exempted from filling a tax declaration if their only income is employment income that has suffered withholding tax.

1.5. Categories of direct and indirect tax

Activity 1.5

Purity has got an individual business besides being a shareholder in Purity Manufacturing Co which is a foreign investor installed here in Rwanda, Gasabo District, Remera sector from January 2018, produce the Juice for local market and export. Base on facilities created by Government of Rwanda and international leaving standard, The board of directors appoints Mrs Kayitesi as Managing director of the company. Her benefit in contract is FRW 45,000,000. The Managing director is provided with furnished accommodation and a fueled car. Outline four Categories of taxation according to the Rwanda tax system legislation

1.5.1. Direct taxes

In general, direct taxes are levied on profit and income.

a) Personal Income Tax

Personal tax on income is levied on income received by an individual. It may comprise the following elements:

- Employment;
- Business activities;
- Investment;
- Capital gain;
- Use, sale, lease or free transfer of an immovable property allocated to the business;
- Use, sale, lease or free transfer of movable property allocated to the business.

The following income types are liable to income tax. They can be broadly categorized as employment income, business activity income, investment income and capital gain.

For Rwanda resident individuals, the source of income is worldwide while for non-resident, only income arising in Rwanda is subject to tax. Broadly, among the sources of income, we may consider:

- Income generated from performing services (including employment)
- Activities of a craft person, singer, artist or player
- Sports, cultural or leisure activities
- Income of Rwanda permanent establishment
- Income from the use, lease and disposal of movable assets by Rwandan business
- Sale, lease and free transfer of immovable Rwandan business assets
- Farming, fishing and forestry
- Usufruct (right of use of asset) and other rights attached to Rwandan Business assets
- Income from investment in share (i.e., dividends)
- Sales or transfer of shares and debentures (capital gains tax)
- Change of partnership profit into shares, such that a partner's interest increases
- Distributions of partnership profits to partners
- Income from lending and deposits(interest)
- Transfer, sales and lease of intellectual property

- Other income generating activities that are not classified as exempt

According to Rwanda legislation, all income types raised are subject to tax. They can be categorized as follow:

- Personal Income Tax (PIT)
  - ✓ PIT real regime
  - ✓ PIT flat
  - ✓ PIT lump sum
  - ✓ Rates of income tax for vehicles transporting persons
  - ✓ Rates of income tax for vehicles transporting goods
- Pay As You Earn (PAYE)
- Investment income tax
  - ✓ Interest income
  - ✓ Dividend income
  - ✓ Royalty income
- Capital gain
- Rental income (here ignore housing which is decentralized)
- Tax on minerals
- Taxes on gaming activities
- Different types of withholding taxes
- Quarterly payment

b) Corporate Income Tax (CIT)

Rwandan resident companies, if not exempt bodies, pay corporate income tax on all of their taxable income sources. The principles of what is taxable, and which expenses are tax deductible, are similar to those for Personal Income Tax (PIT) but different tax rates are applied. For CIT, a fixed rate of 30 % is applied on the nearest thousand profits while for PIT we use the following progressive tax rate:

Annual Taxable income (FRW)		Tax rate
From	To	
0	360,000	0 %
360,001	1,200,000	20 %
1,200,001	And greater than	30 %

1.5.2. Indirect taxes

In general, indirect taxes are applied on consumption of goods and services.

a) VAT

- VAT is an acronym for the term Value Added Tax
- It is an indirect tax on "taxable supplies" made by a "taxable person"
- Subject to all taxable goods and services
- Two tax rates in force:
  - ✓ Standard rate of 18%
  - ✓ Zero rate (0%)

A taxpayer must register for VAT if his turnover is above FRW 20,000,000 for any twelve-month period or above FRW 5,000,000 for three consecutive quarters. In addition, any taxpayer may choose to register voluntarily for VAT if he doesn't meet the threshold.

b) Excise tax

- Excise tax is imposed on specified goods /service produced locally or imported to be consumed in the country.
- Excise tax was established in Rwanda in 1960 and is levied on locally produced beers, lemonades, mineral water, juices, liquors, wines, fuel, vehicles, powdered milk, as well as on cigarettes, etc… and their imported counterparts if appearing on the list published in the consumption tax law.
- Excise tax is also levied on telephone communication since year 2007.

Application activity 1.5

1. Explain the following fiscal terms:

- Personal income tax
- Corporate income tax
- Withholding tax

2. Outline main Source of income liable to personal income tax

1.6. Definition of terminologies used in taxation

Activity 1.6

Analyze the following scenario and answer questions that follow: Marc is a prominent trader in one of the growing centres of Eastern Province. He normally buys his goods from the neighbouring country of Uganda. In the previous budget, the minister announced that in order for the government to be able to fund its activities such as providing free education, road construction, all people will pay a certain amount of money to the government but charged on the goods sold and bought in form of taxes. Marc realized that this might reduce his profits. Therefore, he decided that in order to continue getting the same profits, he would:

- Decisions 1 pay some boys to get for him some goods from Uganda by crossing the river without going to customs to pay taxes.
- Decision 2 for goods on which he would pay taxes, he would increase the prices charged to the customers.
- Decision 3 or stop buying some of the goods on which the tax had been increased.

Questions:

Q1. From the scenario, what do you think is the meaning of the following:
- Tax.
- Taxation.
- Tax avoidance.
- Tax evasion.
- Tax shifting.

Q2. From the decisions Ruth made, which of them is:
- Tax avoidance.
- Tax evasion.
- Tax shifting.

Q3. Among the three actions, which one (s) do you think he can be penalized for? And why?

1.6.1. Terminologies used in taxation

Tax burden: Tax burden this is the effect of a tax on the taxpayers.

Tax incidence: Tax incidence (or incidence of tax) is an economic term for understanding the division of a tax burden between stakeholders, such as buyers and sellers or producers and consumers.

A tax incidence is effectively the burden that a party, either an individual or business, ultimately bears, even if they're not the ones directly paying a tax. For example, a sales tax on clothing would be paid directly by consumers at the time of purchase.

Tax impact: The impact of a tax is the first point of contact with the taxpayers. The term impact is used to express the immediate result of or original imposition of the tax. The impact of a tax is on the person on whom it is imposed first. Thus, the person who is Habile to pay the tax to the government bears its impact.

Tax base: Tax base refers to the items /activities or value on which tax can be imposed to raise tax revenue or activities/incomes covered by the tax system in an economy.

The tax base is the total amount of income, property, assets, consumption, transactions, or other economic activity subject to taxation by a tax authority. A narrow tax base is inefficient. A broad tax base reduces tax administration costs and allows more revenue to be raised at lower rates.

Taxable capacity: Taxable Capacity refers to the maximum capacity that a country can contribute by the way of taxation both in ordinary and extra ordinary circumstances. In other words, it refers to the maximum capacity of the people of a country to bear the burden of taxation without much hardship.

Determinants of Taxable Capacity

The taxable capacity of a country is determined by a number of factors. The main factors are:

1. Size of income and wealth: generally, the larger wealth and income of the country, greater is its taxable capacity. Hence rich nations have a higher taxable capacity than poor nations.
2. Stability and Growth of income: basically, if the economy operates smoothly and progresses well, and ensures a stable and growing income, the taxable capacity of the community will be higher. But it here is fluctuations with serious ups and downs, and especially during a depression, taxable capacity will obviously be lower.
3. Standard of living of the people the standard of living determines the consumption pattern and habit of the community. A community accustomed to greater needs as satisfaction on account of living, cannot bear great sacrifice in paying taxes, hence its taxable capacity will be less. But if the standard of living is low, there is a greater surplus available for taxation, so that taxable capacity will be high.

4. Price level: if the price level is reasonably low and stable, a high income means greater taxable capacity. But, if prices are rising fast, a very high income may also pose a low capacity in real terms.
5. Characteristics of the tax system: a multiple tax system has a greater advantage of enlarging the overall taxable capacity than a single tax system.
6. Nature and purpose public expenditure: public expenditure is largely for developmental schemes the productivity power of the country improves and order is very essential for improving taxable capacity enlarges. Further taxation intended for financing capital formation is therefore quite justified as it raises the taxable capacity in effect.
7. Political condition: Generally, when people appreciate the government, they will be willing to undergo many hardships and bear heavier taxes to in order to enable the government to undertake welfare measures beneficial to the common people, hence the taxable potential automatically expands.

Tax evasion: Tax evasion occurs when a person or business illegally avoids paying their tax liability, which is a criminal charge that's subject to penalties and fines.

Tax avoidance: Tax avoidance is where the taxpayer carries out his or her business in such a way that he will be required to pay less tax by exploiting the loopholes in the tax law/system. Tax avoidance is when an individual or company legally exploits the tax system to reduce tax liabilities, such as, establishing an offshore company in a tax haven. It means paying as little tax as possible while still staying on the right side of the law.

Tax exemption: Tax exemption is exoneration from paying tax granted by Tax Administration. A tax exemption is the right to exclude all or some income from taxation by governments.

Tax shifting: Tax shifting this is the transfer of either part or the whole amount of the tax imposed on a tax payer to another party. It is the transfer of the tax burden to another party. This is mainly with indirect taxes where the producers or sellers usually shift the burden to the consumers by increasing prices of commodities on which they are charged.

Backward shifting occurs when the price of the article taxed remains the same but the cost of the tax is borne by those engaged in producing it.

Taxpayer: Taxpayer is any person who is subject to tax according to the tax laws of Rwanda.

Budget year: Budget year is a period of twelve (12) months that begins on July 1 and ends on June 30 of the following year.

Tax Administration: In Rwanda, Tax administration is represented by Rwanda Revenue Authority.

Fiscal Year: Fiscal Year is a period of twelve (12) months that begins on January 1 and ends on December 31.

Authorized officer

Authorized officer as an officer of the tax administration empowered by the competent organ to conduct audit, investigations, negotiate with the taxpayer, make adjustments, prepares and issues tax assessment notices of assessment, drafts affidavits and who is responsible for any other act necessary to ensure the enforcement of the law on tax procedures and other laws in relation to collection of tax, and who is issued with means of identification to possess such powers.

1.6.2. Characteristics of a Tax.

The definitions point out four main characteristics:

– **There is no quid-pro- quo in tax:**

Tax is not levied for a return for a specific service rendered by government to taxpayers. An individual cannot ask for any special benefit from the government in return for the tax paid.

– **It is a compulsory contribution:**

It is imposed by the government on individuals, households, or companies. Because of its compulsory nature, those who do not pay it are reliable to being punished but it is to be paid by those who come under its jurisdiction.

– **It involves a sacrifice:**

It is a payment by taxpayers which is used to benefit all the citizens whereby the government uses the collected revenues to establish infrastructures such as hospitals, schools as well as other public utility services.

– **It is paid out of total wealth:**

Meaning tax is computed based on a certain specific percentage of the total income.

Application activity 1.6

– Differentiate tax incidence from tax impact
– Discus the characteristics of tax
– With examples, differentiate Tax avoidance and Tax evasion

1.7. The canons/principles of taxation

Activity 1.7

Analyze the Photos below and answer the questions that follow.

Refer to the picture above and state the Canons / Principles of Taxation

1.7.1. The Canons / Principles of Taxation

Canon of Equity

The principle aims at providing economic and social justice to the people. According to this principle, every person should pay tax to the government according to his ability and not the same amount. The rich class people should pay higher taxes to the government, because without the protection of government authorities (Police, Defense, etc.) they could not have earned and enjoyed their income. Adam Smith argued that the taxes should be proportional to income, i.e., citizens should pay the taxes in proportion to the revenue which they respectively enjoy under the protection of the state.

The progressive rates of taxation are adopted in most countries to satisfy this principle.

Canon of Certainty

According to Adam Smith, the tax which an individual has to pay should be certain, not arbitrary. The taxpayer should know in advance how much tax he has to pay, at what time he has to pay the tax, and in what form the tax is to be paid to the government.

In other words, every tax should satisfy the canon of certainty. At the same time a good tax system also ensures that the state/government also be certain about the amount of revenue and the time when it is expected to flow to the treasury.

Canon of Convenience

The mode and timing of tax payment should be as far as possible, convenient to the tax payers. By this principle, Adam smith means that the tax should be levied at the time and the manner which is most convenient for the contributor to pay it. Every tax ought to be levied at the time or the manner in which it is more convenient for the taxpayer to pay. E.g.; payment of VAT, the consumer is convenient because one pays it when he/she buys the goods and at the time which he has the means to buy.

This principle lay down that both the time and manner of payment should be convenient to the taxpayer. In the Words of Adam Smith: “Every tax ought to be levied at the time or in the manner in which it is most likely to be convenient for the contributor to pay it”.

Canon of Economy

Tax system should be economical for the state to collect the tax, i.e. the cost of collection should not exceed the amount of tax to be received. The tax should also be economical to the taxpayer i.e. the tax payer should have sufficient money left with him after payment of tax. A very heavy tax will discourage savings and investment and thus adversely affect the productivity of the economy.

The canon of economy implies that the expenses of collection of taxes should not be excessive. This principles state that the cost of tax collection should be lower than the amount of tax collected. Every tax should satisfy the economy in two ways.

Canon of Productivity

The principle of productivity indicates that a tax when levied should produce sufficient revenue to the government. A system that generates small revenue for the government is normally discouraged. This is a good principle to follow in a developing economy.

Canon of Elasticity

According to this principle, every tax imposed by the government should be elastic in nature. In other words, the income from tax should be capable of increasing or decreasing according to the requirement of the country. For example, if the government needs more income at time of crisis, the tax should be capable of yielding more income through increase in its rate.

Canon of Flexibility

It should be easily possible for the authorities to revise the tax structure both with respect to its coverage and rates, to suit the changing requirements of the economy. With changing time and conditions, the tax system needs to be changed without much difficulty. The tax system must be flexible and not rigid.

Canon of Simplicity

Canon of simplicity implies that the tax system should be fairly simple, plain and intelligible to the tax payer. It should not be complicated; if it is complicated and difficult to understand, then it will lead to oppression and corruption.

Canon of Diversity

This principles state that the government should collect taxes from different sources rather than concentrating on a single source of tax. It is not advisable for the government to depend upon a single source of tax, it may result in inequity to the certain section of the society; uncertainty for the government to raise funds. The government should collect revenue from its citizens by levying direct and indirect taxes. Variety in taxation is desirable from the point of view of equity.

Application activity 1.7

1. Why is it important to have principles of taxation?

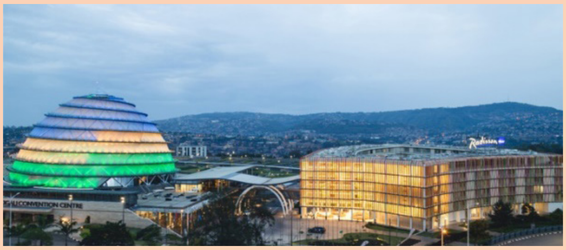
2. Referring to the principles (characteristics) of a good taxation system you know, briefly explain why each is important to the taxpayer and tax authority (RRA).

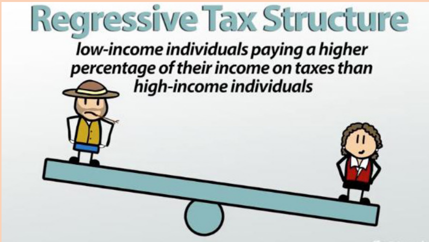
3. In your community, you have probably heard people and business people complaining about the taxes they pay or charged to different or similar items. Identify any 5 things you have heard normally people complain about.

1.8. The importance of tax and the Classification of taxes

Activity 1.8

Analyse the Photos below and answer the questions that follow.





1. With examples from your community or Rwandan community at large, why do you think people and business enterprises need to pay taxes to the government?

2. The Government of Rwanda had introduced the local industry promotion named as Made in Rwanda. Explain how the Government could use the taxes in order to protect domestic industries.

1.8.1. Importance of paying taxes

a) Importance of paying taxes to the government

- Source of government revenue. Taxes are the main source of government revenue to finance its public expenditure. Thus, taxes enable the government to pay its workers, construct roads, maintain security, and provide health care, education among others.
- Taxes benefit the Rwandan government to meet its objectives and goals such constructing affordable houses to the citizens which helps improve the standards of living.
- Taxes help the government to finance its policies especially on poverty alleviation through programs such as “GIRINKA”, “VUP”, and “UBUDEHE” among others.

- Taxes enable the government to regulate the prices of goods and services in the country hence ensuring a low cost of living and maintaining the standards of living of the citizens.
- Taxes enable the government to maintain a balance between the poor and rich. The government uses the taxes from business people to provide services needed by the poor, which otherwise the rich could not provide
- Taxes enable the government to promote its policy industrialization through reducing products from other countries that would otherwise out compete the home industries.
- Taxes enable the government to ensure that the citizens have enough products. This can be through taxes charged to reduce products moving out of the country or removing taxes on goods needed in the country. This helps maintain a high standard of living.

b) Importance of paying taxes to Society

- There are reduced rates of poverty among the community due to a significantly equal distribution of income through various activities and projects set by the government.
- Improved wellbeing among the vulnerable and elderly as they benefit from the different government programs financed through taxes.
- Reduced infant mortality rates and increased life expectancy due to improved access to health facilities and services.
- Increase in the percentage of the population that completes secondary and TVET education, reducing the literacy levels, improving on the peoples' skills through programs such as 12YBE.
    - Increased community/social solidarity, general happiness, life satisfaction, and a significant more trust among the community members and for public institutions.
- Taxes are charged on some products to discourage their production and usage hence controlling over-exploitation of resources as well as protecting the environment which is vital for the existence of the society.

1.8.2. Classification of taxes

Taxes can be classified in the following ways:

a) According to its nature

- Personal, poll or capitation tax: It is a tax of a fixed amount on individuals residing within a specified territory, without regard to their property, occupation or business. Ex. Community tax (basic)
- Property- imposed on property, real or personal, in proportion to its value, or in accordance with some reasonable method or apportionment. Ex. Real estate Tax

b) According to who bears the burden of the tax?

- Direct- the tax is imposed on the person who also bears the burden thereof Ex. Income tax, corporate tax etc.
- Indirect –imposed on the taxpayer who shifts the burden of the tax to another, Ex. VAT

c) According to the method of determination of amount of tax

- Specific –imposed and based on a physical unit of measurement as by head number, weight, length or volume. Example: fermented liquors, cigars.
- Ad Valorem of a fixed proportion of the value of the property with respect to which the tax is assessed. Ex, Real estate tax, excises tax on cars.

d) According to purpose

- **General, fiscal, or revenue** - imposed for the general purpose of supporting the government. Example: Income tax, percentage tax.
- **Special or regulatory** - imposed for a special purpose, to achieve some social or economic objective. Ex. Protective tariffs or custom duties on imported goods intended to protect local industries.

e) According to scope or authority imposing the tax

- **Centralized** - imposed by the national government ex; CIT, PIT
- **Decentralized** - imposed by municipal corporations or local Governments ex. property tax, rental tax and other fees

f) According to graduated scale of rates.

- **Progressive taxes:** a tax is progressive if the tax rate increases as the income increases. Example: Pay As You Earn (PAYE), the rate increases as the income increases where from FRW 0 - 30,000 the rate is 0%, from 30,001 - 100,000 the rate become 20% and from FRW 100,001 and above the rate become 30%.
- **Regressive taxes**: a tax is regressive if the tax rate reduces with the increase in levels of income. As income increase the tax rate decreases. Example, a person earning FRW 100,000 = pays 10% of his income and a person earning FRW 200,000 = pays 5%.
- **Proportional taxes**: proportional taxes are also called flat taxes. The tax rate is constant for all levels of income. People of low income and people of high income pay taxes at the same rate. Example:Value Added Tax (VAT), the rate is fixed to 18% irrespective the taxable value. This means that the even if the rate is fixed but the taxpayer pays the different amount depends on his/her taxable value.

All tax payers irrespective of their income levels pay 20% of their income as a tax. This does not mean that they pay the same amount but rather they pay the same rate.

Application activity 1.8

- By giving specific examples from your community, how does your society benefit from taxes?
- What do you think would happen in the country if taxes were not paid?

Source of Taxable Income

According to Article 5 of Law 16/2018, income taxable in Rwanda includes the following activities performed in Rwanda by any person and activities performed abroad by a resident of Rwanda:

i. Services and employment;
ii. Activities of a crafts person, singer, artist and a player;
iii. Sports, cultural and leisure activities;
iv. Activities carried on by a non-resident through a permanent establishment in Rwanda;
v. Use, sale, lease and free transfer of business movable assets;
vi. Sale, lease and free transfer of immovable assets allocated to the business;
vii. Crop farming, animal farming, fishing and forestry activities;
viii. Usufruct and other rights attached to immovable assets and their sale if such rights are allocated to the business;
ix. nvestments in shares of companies;
x. Direct or indirect sale or transfer of shares or debentures;
xi. Change of profits into shares that increases the capital of partners;
xii. Distribution of profits among partners;
xiii. Lending, deposits and other similar income generating activities;
xiv. ransfer, sale and lease of intellectual property;
xv. Any other income generating activities.

Skills Lab 1

Through internet or after a field visit to RRA office, students are required to prepare a written report on taxes administered in Rwanda.

End of unit assessment 1

Q1. It is said that “tax is the free money to central or local authorities from taxpayers” do you agree with this statement. Justify your answer

Q2. Describe any four characteristics of a good tax.

Q3. Discuss the classification of taxes

Q4. Which one of the following circumstances would be the minister permit a tax period other than 31 December?

p) Claude Karera, an individual in business, whose trade is seasonal; he is very busy at the time when the tax return is required to be filed

q) Musoni ltd, a small enterprise not required to prepare accounts under GAAP

r) AB Ltd, a large company preparing its accounts under GAAP, which wishes to prepare accounts to 30 June for commercial reasons

s) CD LTD, a large company preparing its accounts under GAAP, which wishes to prepare accounts to 30 June in order to delay its tax liabilities

Q5. Which two of the following individuals would be treated as resident in Rwanda in the tax period 2019?

- Solange Mukandanga, an individual whose habitual abode in Rwanda but who is currently travelling around the world and will be away for the whole of 2019
- Harry James, UK citizen who been seconded to Rwanda by his employer for the period 1 September 2019 to 30 April 2020 – he is staying in hotels while in Rwanda, and he has never visited Rwanda prior to his secondment
- Sophie smith, a colleague of Harry James, who was seconded to Rwanda for the periods 1 December 2018 to 31 January 2019 and 15 April 2019 to 31 august 2019, but has now returned to the UK (her usual home)
- Hank Azarea, a US citizen who owns a hotel as a business in Rwanda but has only visited Rwanda for two weeks in 2019; he does not have a Rwandan home

a. 1 and 2

b. 1 and 3

c. 2 and 3

d. 3 and 4

Q6. Which of the following tax principle require to have multiple taxes in order to ha have a good tax system?

A. Simplicity
B. Economy
C. Convenience
D. Diversity

Q7. According to …… principle, a good tax system should yield enough revenue for the government activity

A. Economy
B. Productivity
C. Equity
D. Simplicity

Q8. Tax evasion is illegal while tax avoidance is legal

A. True
B. False

Q9. Which of the following does not explain a resident individual?

A. An individual with permanent resident is Rwanda
B. An individual with habitual abode in Rwanda
C. A Rwandan ambassador in USA
D. A foreigner who has stayed in Rwanda for 167 days

Q10. Which of the following is considered as a permanent establishment as per the Rwandan tax Law?

i. A factory or a workshop;

ii. A mine, a quarry or any other place for an exploitation of natural resources;

iii. Maintains a stock of goods or merchandise belonging to him/her solely for the purpose of storage;

iv. A site set for construction, construction site or a place where supervision or assembly works are carried out;

v. Maintains a stock of goods or merchandise belonging to him/her solely for the purpose of processing by another person;

A. I and II
B. I, ii, iii
C. I, ii, iv
D. All the above

Q11. A tax which increases as the income increases is

A. Progressive tax
B. Proportion tax
C. Regressive tax
D. Digressive tax

Q12. Which of the following is not a source of income for tax in Rwanda

A. Activities of a crafts person, singer, artist and a player;
B. Sports, cultural and leisure activities;
C. Activities carried on by a non-resident through a permanent establishment in Rwanda;
D. Loan and grants

Q13. Which of the following taxes is classified as a direct tax

A. Capital Gain tax
B. VAT
C. Import duty
D. Excise tax

Q14. All duties are taxes but not all taxes are duty

A. True
B. False

UNIT 2 LAWS RELATED TO BUSINESS ACTIVITIES

Key unit competence: To be able to identify laws related to business activities

Introductory activity: A case study

Looking at the situation above in photo and talk about the activities carried out there.

In Rwanda today we have many businesses having different organization according to their activities. These organizations may be public or private. As a result of liberal economy Rwanda is currently adopting, any legal entity or person is allowed to carry out business activities. For instance, a business organization can be a company which is traditionally a business organization, a cooperative or individual him/ herself. These kind of business activities need order, standards, right protection in order to clear some disputes that may happen. What is the solution to these challenges in business?

2.1. Law and Business Law

Activity 2.1

A community made up of people who concerned to pursue their own self-interest, needs regulation because there are situations where everyone pursues their own self-interest, everyone will be worse off than they would have been if they acted differently.

Through the situation at school and in your home community, what can govern relationships between individuals and their society?

2.1.1. Meaning of law

The word "law" is difficult to define, particularly as it is used in different ways. It contains, however, the concepts of orderliness, universality and objectivity. Nonetheless, one may define it as a set of binding rules established and enforced by competent authorities in order to govern relationships between persons in a given community. The binding aspect of a legal rule is very meaningful as it differentiates it from other norms such as moral rules, ethical or religious rules which are deprived of immediate sanctions once they are violated.

Law is defined as a body of enforceable rules governing relationships between individuals and their society (Miller & Jentz, 2008).

Law is a social phenomenon; as the roman maxim says, there is no society without rules: "Ubisocietasibi jus". In the middle Age, law was considered to have been dictated by Divine Will, and revealed to wise men. This was known as natural law deriving from God and transcending personal will of any individual.

From the time of ancient Greek empire to the contemporary world, law has been and remains a human phenomenon.

Philosophers, writers and politicians have always demonstrated the importance of legal norms meant to regulate relationships within communities. However, the way it is perceived, its interpretation and its sources have undergone several mutations.

The term" law" can be defined in different ways by different scholars. More commonly, when people speak of law, they refer to the rules themselves. The law says that you" must ...", a phrase we use and hear. This is the sense in which the law will be generally used.

Therefore, the law can be defined as follows: Law is a set of principles; rules and standards of conduct that have general application to the society, have been developed by an authority for that society and for which the violation imposes a sanction.

2.1.2. Business law

This covers business related activities like law of insurance, law of bankruptcy, agency relationship, sale of goods, negotiable instruments, company law, carriage law, banking law and labour law.

Business law is a section of code that is involved in protecting liberties and rights, maintaining orders, resolving disputes, and establishing standards for the business concerns and their dealings with government agencies and individuals.

Application activity 2.1

a) What do you understand by law?
b) Explain what you understand by law governing relationships. Mention your opinion.
c) Why do you think that law is set of principles; rules and standards of conduct?
d) Do you think law is necessary in society?

2.2. Important terms used in law

Activity 2.2

Looking at the photo above, think about the activities being carried out. Then discuss some terms used during these activities.

2.2.1. Claimant/Plaintiff:

This is the person who sues another in a court of law. Or a plaintiff is the person or entity initiating a lawsuit by filing a complaint in a court of law.

2.2.2. Defendant:

This is the one against whom a law suit is brought.

2.2.3. Appellant:

A person who appeals to a higher court against a decision of a lower court and requests that that decision be set aside.

2.2.4. Law suit:

Accusation in the court of law

2.2.5. Remedy:

This is the relief given to the innocent party to enforce a right or to compensate for violation of a right.

2.2.6. Counsel:

Legal advice given in a case; also means a lawyer or attorney in a case.

2.2.7. Damages:

Money that a defendant pays to the plaintiff in a civil case if the plaintiff has won the case.

2.2.8. Fine:

Money paid by the defendant to the public or government

Application activity 2.2

Discussion in groups on the meaning of the following terms used in law:

Plaintiff: this is the person who sues another in a court of law. Or a plaintiff is the person or entity initiating a lawsuit by filing a complaint in a court of law.

Defendant: this is the one against whom a law suit is brought.

Appellant: a person appealing to a higher court against a decision made by a lower court, seeking reversal of that decision.

Damages: money that a defendant pays to the plaintiff in a civil case if the plaintiff has won the case.

Fine: Money paid by the defendant to the public or government

2.3. Importance of business law in business operations

Activity 2.3

One of the most frequently debated topics is business. Business is the effort of individuals to produce and sell, for a profit, the goods and services that satisfy society's needs. The goals of the business will vary based on the type of business and the business strategy being used. The money raised from business supports the government and allows it to fund in public expenditures.

As a business to be or referring to business activities in your community, what are benefit of law in the businesses?

With examples from your community or Rwandan community at large, why do you think people and business enterprises need law?

Business law refers to a set of laws that govern the dealings regarding commercial matters, namely business organizations. It encompasses all laws that guide on how to set up a business and then how to run it. This includes all the laws that govern on how to set up, start, manage, run, close or sell a business. It includes contracts, laws of corporations, other business organizations, commercial papers, income tax, secured transactions, intellectual properties, and other transactions and dealings related to the business.

2.3.1. The prime purpose of business law

The prime purpose of business law is to maintain order, resolve disputes, establish generally accepted standards, protect rights and liberties when it comes to business and its relation to other businesses, government authorities, and the customers.

2.3.2. The importance of business law

- **Set of standards**: Earlier, the customer had to suffer a lot due to the absence of a proper law that could safeguard their interests and money invested in a particular business. As there was no such law regarding maintenance of order, rights, and liabilities, etc., the business owners made their own standards and made the customers suffer just because of the greed to make more money. With the establishment of business law, many standards have been established which have to be followed by businesses.
- **Maintain Equilibrium**: This creates a sense of satisfaction among customers. In the absence of the law, different countries had different laws regarding the business dealings which made it difficult for the customers as well as the seller to establish a deal. But now every country has the same

standards, and the deal between buyer and seller is easily established. This brings ease in business dealings and transactions all across the globe.

- **Decrease chances of frauds:** Business law helps the owners themselves to get aware of the laws against other businesses and individuals. It also helps the individuals, to be aware of the rights against the businesses so that they can use them in case they fall prey to the frauds and misery of the business.
- **Presence of Ethical conduct:** With the help of business law, business owners may make better decisions, and also know when to seek legal help. Every business has to maintain an ethical conduct but most businesses, in the greed to earn more profits; do not follow such conducts. Business law makes it mandatory for all the businesses to maintain an ethical conduct which in turn pleases the buyers and they form a good image of the business.

Application activity 2.3

1. Determine why the business law is important to business.
2. Identify how the business law protects people from harmful business practices

2.4. Laws related to business

Activity 2.4

Today in Rwanda we have many businesses having different organization according to their activities. In Rwanda, there are arms of the government (ruling bodies) from the village, sector, district, provincial and national levels. These bodies comprise: Legislature (who make laws), Executives (who enforce laws) and Judiciary (exercise laws).

With examples from your community or Rwandan community at large, why do you think people and business need different laws to govern their activities?

2.4.1. Land act:

An Act to provide for the tenure, ownership and management of land, to amend and consolidate the law relating to tenure, ownership and management of land; and to provide for other related or incidental matters.

2.4.2. Food and drugs law:

The Food and Drug Act prohibited interstate commerce in misbranded and adulterated foods, drinks, and drugs. While it has since been repealed, new laws regulate a wide range of consumer products. This Law establishes Rwanda Food and Drugs Authority and determines its mission, organization and functioning.

2.4.3. Consumer protection law:

Consumer protection laws offer an important part of a reliable market economy. While "buyer beware" was once the motto of the free market, these regulations help keep sellers honest, with no threat of unpleasant surprises.

2.4.4. National environmental law:

This Law determines modalities for protecting, conserving and promoting the environment against climate change. Environmental law refers to a variety of protections which share the goal of protecting the environment.

Application activity 2.4

Discuss on the role of laws related to business in Rwanda

2.5. Legal institutions related to businesses in Rwanda

Activity 2.5

In Rwanda today we are living in society where there are many government institutions whose mandate is to accelerate Rwanda's economic development, introduced to facilitate the wellbeing of the society as well as the business.

As a business to be or referring to business activities in your community, which government institutions do you think businesses need?

2.5.1. Commercial Courts:

Figure: 2.5.1

The commercial court system, established in 2008, is made up of three commercial courts based in the three major urban areas in Rwanda, that is: Kigali, Musanze and Huye and the Commercial High Court located in Kigali.

These courts were introduced to handle commercial matters in order to deal with a big backlog of commercial cases, speed up the resolution of business disputes and thus play a part in the promotion of investment in the country.

2.5.2. Rwanda Revenue Authority (RRA):

Figure: 2.5.2

The Rwanda Revenue Authority is a government revenue collection agency established by the Parliament of Rwanda. The RRA is charged with enforcing, assessing, collecting, and accounting for the various taxes imposed in Rwanda.

2.5.3. Rwanda Development Boards (RDB):

Figure: 2.5.3

Rwanda Development Board (RDB) is a government institution whose mandate is to accelerate Rwanda's economic development by enabling private sector growth.

The Rwanda Development Board is under the supervision of the Office of the President and is governed by a Board of Directors made up of global entrepreneurs and experts.

RDB was established in 2008 out of a merger of 8 Government institutions, primarily to create a One Stop Shop for business and investments. RDB has been built with global expertise and modelled on international best practice.

Currently, RDB's key services are; Investment Promotion, Export & Special Economic Zone (SEZ) Development, Investment Deals Negotiation, Tourism and Conservation, Skills Development and One Stop Center services (business and investment registration, visa facilitation, tax incentives management, etc.)

RDB is here to provide support throughout the entire investment journey and to ensure that Rwanda remains one of the best places to do business in Africa and the World.

2.5.4. Rwanda Utilities Regulatory Authority (RURA):

Figure: 2.5.4

Rwanda Utilities Regulatory Authority (RURA) was initially created by the Law n° 39/2001 of 13 September 2001 with the mission to regulate certain public utilities, namely: telecommunications network and/or Telecommunications services, electricity, water, removal of waste products from residential or business premises, extraction and distribution of gas and transport of goods and persons.

2.5.5. Food and Drug Authority (FDA):

Figure: 2.5.5

The FDAR Department protects and promotes human and veterinary public health through conducting assessment and evaluations of application dossiers for processed foods/ drinks, food additives, food supplements, both human and veterinary medicines, vaccines and other biologics, medicated cosmetics, medical devices, chemicals and pesticides, and tobacco and tobacco products. The FDAR Department also recommends for registration and/or marketing authorization (MA) to products that comply with Rwanda FDA regulatory requirements for registration

2.5.6. Rwanda Standards Boards (RSB):

Figure: 2.5.6

Rwanda Standards Board (RSB) is a public institution established by Rwanda Government Legislation N° 50/2013 of 28/06/2013 determining the mission, organization and functioning of the Rwanda Standards Board to undertake all activities pertaining to the development of Standards, Conformity Assessment and Metrology services in the country.

It is the only body with powers to define and possess national standards. Public services and public or private firms must present their standards to RSB for adoption at national level. RSB is governed by the Board of Directors composed of major stakeholders from government, industry and academic institutions, as well as consumer associations.

Application activity 2.5

Discuss the role of institutions governing business in Rwanda.

2.6. Business registration according to forms of business

Activity 2.6

Registering a business can be one of the best ways you can expand your business and help ensure its success. Rwanda has the fewest procedures and fastest processes to register and start a business.

Search and share the information of registering some businesses in Rwanda.

As a business to be in your community and in Rwanda at large, what kind of business do you think need to be registered.

2.6.1. Registering a sole trade business or Individual Enterprises:

Business registration operates as a single point integrated service. Once you complete your business registration, you have also completed tax registration with the Rwanda Revenue Authority, employer registration with the Social Security Fund of Rwanda and notification of business activities to the National Institute of Statistics of Rwanda. This integrated registration is achieved through the filling of a consolidated application form covering all the information required for registration and notification with the relevant agencies.

Business Registration is concluded by the issuance of a business registration certificate which has a unique enterprise code that acts as a unique identifier of the business in relation to any public agency. The Enterprise/Company code is also the Tax Identification Number (TIN).

The business registration services cover all businesses determined by the Company Law No 07/2009 of 27/04/2009 and/or the Ministerial Order N° 02/09/MINICOM of 08/05/2009.

2.6.2. Registering a company:

Rwanda has the fewest procedures and fastest processes to register and start a business. Below are the steps followed to register a business in Rwanda. You can register your business online at http://org.rdb.rw/ or at the Office of the Registrar General which is a department within the Rwanda Development Board located in Kigali, the capital city (see links below for full address).

What are some of the important documents needed before I can register my business in Rwanda?

Domestic Company Registration

- Copy of ID/Passport
- Complete two copies of Memorandum of Association Art 14 (downloaded on our website here).

Opening a branch/ Foreign company

- Power of attorney to present the company in Rwanda. (Notarized)
- A duly authenticated copy of the memorandum Articles of Association. (Notarized)
- Certificate of Registration/Incorporation issued by the registration authority in the country of incorporation. (Notarized)
- Notarized resolution from the authorized agency authorizing to open a branch.
- Passport copies of the shareholders/directors.
- List of directors residing in Rwanda (at least One)

2.6.3. Registering a partnership:

A partnership company is a type of business where two or more individuals pool together their resources to achieve a common goal through business. This type of business is usually helpful when an individual does not have enough resources to start a venture.

You can register your partnership business online at http://org.rdb.rw/ or at the Office of the Registrar General which is located in Kigali.

2.6.4. Registering a cooperative:

Registration of a Cooperative is the action or process of registering a cooperative by attributing a registration number or of being registered in registration book for Cooperatives.

When, How and where to register a Cooperative?

A cooperative is registered when it fulfils all legal requirements. The exercise is done online by the applicant him/herself through the Cooperative Management Information System (CMIS) (to be soon open).

Requirements for a cooperative to be granted legal personality:

- to have Internal regulations
- to define its domain of activity and objectives;
- to have the required number of founder members;
- to have a certificate issued by the Sector in which it will operate indicating that the cooperative meets the requirements;
- to have a business plan indicating:

a) the intended business model;
b) a clear outline of the economic and social benefits the cooperative provides to its members
c) an action plan for at least the first three (3) years;
d) to present its working capital to finance its activities.

Detailed steps to register a Cooperative:

1. Cooperative applies for legal personality through the CMIS
2. Sector Cooperative Officer (SCO) assesses the application and may decide to visit the cooperative. The sector has 5 days to approve the application.
3. Once approved, the application is moved to the district. The District Cooperative Officer (DCO) assesses (review) and approves or rejects. He / She has to approve or reject the application the application.
4. After district approval, the application is moved to RCA.
5. RCA requests approval from BNR in case of SACCO's application
6. If RCA approves, legal personality is granted within two (2) working days.
7. If application is rejected, it is sent back with comments for rectification

Requirements for membership in a primary cooperative:

A person who wishes to be a member of a primary cooperative must:

1. be at least sixteen (16) years of age;
2. Submit a written application for membership;
3. Not be engaged, either directly or indirectly, in any business likely to jeopardize that of the cooperative he or she intends to join;
4. Pay his or her share in accordance with the bylaws of the cooperative;
5. Be committed to work with the cooperative in all or part of its operations as provided for under the bylaws;

Application activity 2.6

1. How can register a business in Rwanda?
2. Registering a business is one way of ensuring its success. Discuss?

2.7. Benefits of registering a business

Activity 2.7

In Rwanda we have many businesses ensure economic development of country. One of those businesses are registered and another one is not registered.

Look at the situation of business at home and around the country then shows if registering business is necessary or not.

As a business to be or referring to business activities in your community, why do you think businesses need to be registered?

2.7.1. Reputation from customer

Registering your business gives your potential customers confidence that they are dealing with a reputable organization. Building reputation especially from customers and clients if you've never done business before is very difficult.

2.7.2. You get legal liability protection

When you register your business as Limited Liability Company, you are a different entity from your company. If you incorporate, you will not be held personally responsible for certain accidents and other liabilities.

If you obtained loan and you defaulted in payment, your bank will not seize your property except the company asset because you are protected from such incidence.

2.7.3. Branding and Legitimacy

To prove that you have a legitimate business, legally in Rwanda, you will be required to provide proof of business registration. A registered business helps in building reputation with your suppliers, customers, and employees.

2.7.4. Loan facility

When your company is registered, accessing loan becomes very easy compare to personal loan application. With your documents, you are going to have to prove that you're actually a business. This gives credibility and trust and also ensures confidence. Your investors or lenders will see that they are dealing with a company and will be willing to do lend you money if other terms and conditions are made.

2.7.5. Create employment

A registered business can employ full-time employees and pay them salaries and other benefits.

Application activity 2.7

Discuss on the benefice of registering business in Rwanda.

2.8. Consequences of not registering a business

Activity 2.8

In Rwanda we have many businesses ensure economic development of country. One of those businesses are registered and another one is not registered.

As a business to be or referring to business activities in your community, show consequences of not registering business.

2.8.1. Pay Fines and Penalties

If business fails to comply with business license requirements and you operate your business without a valid license, you should expect to have to pay a fine or penalty.

2.8.2. Lawsuits

Not having the proper business licensure opens your company up to lawsuits. There are several ways that this can occur. A customer that is unhappy with the goods or services you provided could take you to small claims court and cite your lack of business licensure as fraudulent activity.

2.8.3. Closing business

Failing to obtain or renew a business license can cause to close business.

2.8.4. Arrests business responsible

You could even be arrested for not having a business license. Operating a business without a license can be considered to be fraudulent activity, so some jurisdictions might decide to arrest the parties responsible.

2.8.5. Inability to bid

Another consequence of operating without a business license could be the inability to bid on specific projects or opportunities. Sometimes, to win a bid, you have to show proof that you're licensed.

2.8.6. Loss of reputation

If you do get fined or sued as a result of not having a business license, the resulting negative press can be more cost than any penalty, because your reputation is everything. When a customer is informed that your business is not operating legally, it could call into question the quality of your work and the trustworthiness of your business, which can be devastating and difficult to rebuild.

2.8.7. Difficulty to Obtain Financing:

Having a business license is one of requirement for loan agreements and financing

Application activity 2.8

1. Give the reason why not having a business license can cause business to be closed?
2. Explain the reason why not registering business can be result of losing reputation for business?

Skills Lab2

Via internet search, visit the RDB website and write a note on the following aspects:

1. Requirements for starting a business
2. How to register a business
3. Institutions that are involved with starting and developing a business

End of unit assessment 2

1. Determine the scope of law in business.
2. Identify how the rule of law protects people from harmful business practices.
3. Imagine that you have businesses. What types of permits are required to conduct your business and which government entities had jurisdiction over your business?
4. Registering a business is legal requirement. Is this statement true or false? Give reasons to justify your response.
5. What would business be like in a land without any rule of law system? Be specific

UNIT 3

TAXATION OF EMPLOYMENT INCOME

Key unit competence: To be able to compute employment income tax

Introductory activity

Analyze the photo below and answer the question:

Refer to the picture above, which activities are being conducted?

3.1. Components of employment income

Activity 3.1

Assume that at the conclusion of your studies, you have been chosen to be a member of the personnel (staff) at your institution. Do you believe you will be compensated at the end of the month? If so, what kind of remuneration do you expect? If not, what is the reason?

An individual's employment income is calculated as the sum of all taxable cash components and taxable benefits in kind less any applicable reliefs.

Employment income includes all payments paid to an employee by his/her employer in cash or in-kind in relation to the work performed. Those payments are composed of the following:

- Wages, salary, leave pay, sick pay and medical allowance, payment in lieu of leave for an employee who stops working before benefiting from his/her annual leave, sitting allowances, commissions, bonuses, and gratuity;
- Allowances relating to the cost of living, subsistence allowances, housing allowances, and entertainment or travel allowances;
- Any discharge or reimbursement of expenses incurred by the employee or an associate;
- Payments to the employee working in exceptional conditions of employment;
- Payments for redundancy or loss or termination of the contract;
- Pension payments;
- Other payments made in respect of previous, current, or future employment.

Application activity 3.1

PAYE is a tax on income derived from employment. The profession tax on remuneration is collected by means of monthly deductions from salaries by employers. In your opinion, what are the main categories of income subject to PAYE? List at least 4 examples per category.

3.2. Payments and persons exempted from employment income tax

Activity 3.2

1) Do you think that a provision on exemptions is necessary for PAYE in Rwanda while source of income is worldwide?
2) On which condition the income of a foreigner who represents his or her country in Rwanda should be exempted?
3) Given international conventions and as far as PAYE is concerned, what is commendable when the employer is not obliged to withhold taxes due?

3.2.1. Payments exempted from employment income tax

The following payments are not included in the calculation of taxable employment income:

- The discharge or reimbursement of expenses incurred by the employee or his/her associate:

a) Wholly for business activities of the employer;

b) Those that are deducted or would be deductible in calculating the employee's income from all his/her business activities;

- Contributions made by the employer for the employee to the public institution in charge of social security;
- Pension payment from the public institution in charge of social security or from a qualified pension fund;
- Payments made to non-Rwandan citizens in return for aid services under agreements signed by the Rwanda government; and
- Payments made to non-residents performing duties in Rwanda by a non-resident employer.

3.2.2. Persons exempted from employment income tax

The following individuals are free from Rwanda's employment income tax, as allowed for by international agreements alluded to in Article 16 of the income tax law No. 016-2018, for services rendered in the performance of their official duties:

- A foreigner who represents his/her country in Rwanda;
- Any other individual employed in any Embassy, Legation, Consulate or Mission of a foreign state performing State affairs, who is a national of that State and who owns a diplomatic passport;
- A non-citizen individual employed by an international organization that has signed an agreement with the Government of Rwanda in accordance with Rwandan laws.

Application activity 3.2

Explain the logic behind the fact that any non-citizen individual employed by an international organization formed under international law is exempted from PAYE in Rwanda?

3.3. Benefits in kind

Activity 3.3

Benefits in kind can be more difficult to value than regular employment income. In which way this statement is true? What are the possible shortcuts used by Rwanda Taxation System to overcome this barrier?

Benefits in kind received by an employee are included in taxable employment income in consideration of market value as follows:

3.3.1. Motor vehicle benefit in kind

The benefit of the provision of a motor vehicle for either official or private use, with or without a driver during a tax period, is calculated as **10%** of the employee's total emoluments minus benefits in kind.

If the car is rented by the employer, rather than owned, . The amount is considered as any other allowance an employee has received as per article 15 of Law 16/2018

Illustration 1: Computation of Motor vehicle benefits

Rukundo has a basic salary of FRW 400,000 per month, he also receives a communication allowance of FRW 100,000 per month, housing allowance of FRW 200,000 per month and he also uses a company vehicle for both private and official use.

Required: Compute the car benefit and taxable employment income

Particulars	**Amount FRW**
Basic salary	400,000
Add other cash benefits	
Communication allowance	100,000
Housing allowance	200,000
Gross salary/Total cash benefits	700,000
Add benefits in Kind	
Company car (10%*700,000)	70,000
Taxable employment income	770,000

3.3.2. Loan interest benefit in kind

Loan and salary advances

There shall be added to the taxable income, benefits on a loan including advance on a salary exceeding a three (3) months' salary given to an employee valued at a difference between:

a) The interest on loan, which would have been paid by the employee during the month in which the loan was received, calculated at a rate of interest offered to Rwanda;

b) And the actual interest paid by the employee in that month;

Illustration 2: Computation of Loan benefits

Rukundo has a basic salary of FRW 400,000 per month, he also receives a communication allowance of FRW 100,000 per month, housing allowance of FRW 200,000 per month and he also uses a company vehicle for both private and official use. During the period, the employer gave him a loan of FRW 10,000,000 at an interest rate of 12%, per year when the interbank interest rate is 15%.

Required: Compute the taxable employment income of Rukundo

Solution

Particulars	**Amount FRW**
Basic salary	400,000
Add other cash benefits	
Communication allowance	100,000
Housing allowance	200,000
Gross salary/Total cash benefits	700,000
Add benefits in Kind	
Company car (10%*700,000)	70,000
Loan benefits (15% -12%)*10,000,000}/12	25,000
Taxable employment income	795,000

Illustration 3: Computation of salary advance benefits

Uwimana received a salary advance of FRW 8,000,000 from his employer which must be paid within one year. The basic salary of Uwimana is FRW 1,500,000 per month. She was not charged with any interest. The interbank interest rate is 8%. Compute his taxable benefit.

As said above, the three months' salary is exempted 1,500,000 x 3 = 4, 500,000

The taxable benefit will be [8,000,000 – 4,500,000] x 8%

3.3.3. Accommodation benefits in kind

An employer may provide free residential accommodation to an employee. The benefit of the provision of free accommodation, whether furnished or unfurnished, is calculated as **20%** of the employee's total emoluments excluding benefits in kind.

If an employer rents a house rather than owning it, the amount paid is considered as any other allowance as per article 15 of law 16/2018.

Illustration 4: Valuation of house benefits

Rukundo has a basic salary of FRW 400,000 per month, he also receives a communication allowance of FRW 100,000 per month, housing allowance of FRW 200,000 per month and he also uses a company vehicle for both private and official use. During the period, the employer gave him a loan of 10,000,000FRW at an interest rate of 12%, per year when the interbank interest rate is 15%. Rukundo also stays in a company house in Kabuga.

Required: Compute his taxable employment income

Solution

Particulars	**Amount FRW**
Basic salary	400,000
Add other cash benefits	
Communication allowance	100,000
Housing allowance	200,000
Gross salary/Total cash benefits	700,000
Add benefits in Kind	
Company car (10%*700,000)	70,000
Loan benefits (15% -12%)*10,000,000}/12	25,000
Company House (20%*700,000)	140,000
Taxable Employment income	935,000

Illustration 5: Valuation of benefits in kind:

Kirabo has a gross salary of FRW 620,000 she stays in the company house and uses a company car for both private and official use. The employer also gave her a loan of FRW 2,400,000 free of interest during the month. Also, assume that the BNR interbank rate is 10%. The benefits and the taxable income are determined as follows:

a) Housing = 20% of FRW 620,000 = FRW 124,000

b) Vehicle use = 10% pf FRW 620,000 = FRW 62,000

c) Interest = 10% of 2,400,000 times 1/12 = 20,000

d) Taxable income = FRW 620,000 + 124,000 + 62,000 + 20,000 = FRW 826,000

In taxation, whatever kind of donation moving from the employer to the employee is considered as a benefit in kind. Any other benefit which an employee receives because of job or any assistance made to the family member of the employees is considered as a benefit and therefore should be added to the employment income. This is the case of domestic employee and school fees:

Domestic employees:

If the employer has domestic employees and those employees are paid by the employer, the salary paid to the domestic employees is considered as a benefit to the employee and therefore should be added to the employment income of the employee.

School fees:

If the employer pays the school fees for the children of the employees, the school fees paid should be considered as a benefit to the employee and added to the employment income.

Illustration 6

Muvandimwe has a basic salary of FRW 300,000; he stays in a company house and also uses a company car for both private and official use. His taxable employment income will be

A. FRW 300,000
B. FRW 330,000
C. FRW 360,000
D. FRW 390,000

Answer is D

Application activity 3.3

1. Robert Ngabonziza is provided with the use of a car owned by his employer and a driver as a perk of his job. The driver is employed separately by the employer and taxed under PAYE. Robert receives a cash salary of FRW 4,200,000 per month. Compute Robert's benefit in kind.

2. Nancy Umulisa borrowed FRW 5,000,000 from her company to pay for her house's repair. She is required to pay an annual interest rate of 1%. The National Bank of Rwanda is now lending money to commercial banks at a 6.5% annual interest rate. Calculate Nancy's benefit in kind.

3. Octave Murenzi obtains FRW 54,000,000 annual salary and FRW 700,000 bonus this tax period. In addition, his employer provides him with a furnished house to live in. Compute Octave's benefit in kind.

3.4. Categories of employee

Activity 3.4

In PAYE concerns, Rwanda Tax Legislation distinguishes three types of employees. List them and discuss their definitions.

There are three categories of employees:

(a) "**Permanent employees**" – this is everyone who does not fall into either casual labourers or employee with more than one employer.

The following rates of income tax apply to monthly employment income for permanent employees:

Monthly taxable income (in FRW)

From	To	Taxable income	Tax rate
0	30,000	30,000	0%
30,001	100,000	70,000	20%
100,001	And greater than		30%

The following working is suggested for your income tax calculations for permanent employees (based on monthly taxable employment income of FRW 270,000):

FRW				FRW
30,000	X	0%		**0**
70,000	X	20%		**14,000**
170,000	X	30%	(balancing figure)	**51,000**
270,000				
Total income taxe payable on employment income				**51,000**

(b) “Casual labourers” –this is an employee who fulfill the following conditions at the same time:

- Performs unskilled labouring activities;
- Does not use machinery or any equipment requiring special skills; and
- Is engaged by an employer for a maximum of 30 days during a tax period.

The following rates of income tax apply to monthly employment income for casual labourers:

Bands of taxable income	Taxable income	Tax rate
FRW	FRW	%
0 – 30,000	30,000	0
30,001 +		15

In brief, the tax law defines a casual labour as an employee who does not use special skills on the job and does not exceed 30 days in a tax period. Casual labour is taxed at a rate of 15% and the first FRW 30,000 is exempted

E.g. Jane was employed as a cleaner for four weeks. She is paid FRW 30,000per week. Compute her taxable income and tax payable:

- Basic pay (30,000*4) 120,000
- Exempt (30,000)
- Taxable income 90,000
- Tax payable (90,000*15%) 13,500

(c) “Employee with more than one employer” – this is an employee who is employed by more than one employer at the same time:

- The employer who pays them the highest taxable income is referred to as the ‘first employer’;
- The first employer declares them as a ‘permanent employee’ and taxes them as such;

- Any additional employers treat them differently (any additional employers must withhold tax at 30% of their taxable income
- Here there is the concept of second employer. The law defines a second employer as the one where the employee spends little time in the period. Income from the second employment is taxed at a rate of 30%

Illustration 1: Computation of taxable income and PAYE

Mujane is employed by KTB Musanze branch as the branch manager on the following terms:

A monthly salary of FRW 1,200,000, Residential house where she contributes FRW 2 00,000 per month, a company vehicle which she uses both private and office, the company pays two house girls for her each FRW 50,000, transport allowance of FRW 300,000 per month. During the month she went to Kigali to attend the board meeting and she used FRW 120,000 on transport; she has not yet received a reimbursement

Determine the monthly and annual taxable income and tax liability of Mujane

Computation of taxable employment income and tax liability

	Monthly	Annually
Salary	1,200,000	14,400,000
Add allowances		
Transport allowance	300,000	3,600,000
Employment income/gross salary	1,500,000	18,000,000
House Benefit (20%x1500 -200)	100,000	1,200,000
Motor vehicle benefit (10%x1, 500,000)	150,000	1,800,000
House girls	100,000	1,200,000
Taxable Income	1,850,000	22,200,000
Monthly Tax Liability		
0-30,000 tax rate 0%	0	
30,000 – 100,000 tax rate 20%	14,000	
100,000-1,850,000 tax rate 30%	525,000	
Tax liability	539,000	
Annual Tax Liability		
0-360,000 tax rate 0%		0
360,000-1,200,000 tax rate 20%		168,000

1,200,000 – 22,200,000 tax 30%		6,300,000
Tax liability		6,468,000

Illustration 2: Computation of taxable income and PAYE

Kayitesi is employed by Eco bank as the financial manager on the following terms: Monthly salary of FRW 2,000,000 per month, a company house and vehicle. Kayitesi uses the vehicle both private and business purpose. In addition she also receives FRW 100,000 per month as transport allowance. The company contributes for her FRW 50,000 per month in a licensed medical provider. However, the general policy of medical insurance is FRW 20,000 to all employees paid to RAMA. The bank also gave her an interest free loan of FRW 3,000,000. Kayitesi employs one house girl paid by the company at FRW 60,000 per month. During the month she contributed FRW 95,000 as pay as you earn (PAYE). Determine the monthly and annual taxable income and her tax liability. The interbank interest rate is 15%:

	Monthly	**Annually**
Salary	2,000,000	24,000,000
Transport allowance	100,000	1,200,000
Gross salary	2,100,000	25,200,000
Housing benefit (2,100,000 x20%)	420,000	5,040,000
Motor vehicle benefit (2,100,000x10%)	210,000	2,520,000
Medical allowance (50,000-20,000)	30,000	360,000
Interest (3,000,000x15%)/12	37,500	450,000
House girl benefit	60,000	720,000
Taxable Income	2,857,500	34,290,000

Monthly tax liability

0-30,000 tax 0%	0
30,000 – 100,000 tax 20%	14,000
100,000 – 2,857,500 tax 30%	827,250
Tax liability	841,250
Less PAYE	(95,000)
Tax payable	746,250

Annual Tax Liability

0 – 360,000 Tax 0%	0
360,000 – 1,200,000 tax 20%	168,000
1,200,000 – 34,290,000 tax 30%	9,927,000
Tax liability	10,095,000
Less PAYE	(1,140,000)
Tax Payable	8,955,000

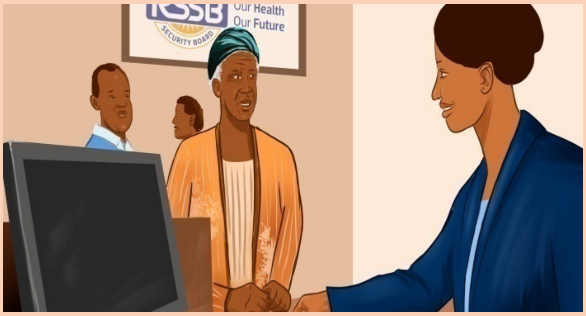
Application activity 3.4

1. Dukore Company employs Muneza in an unskilled role on a temporary basis. Muneza works for 20 days and Dukore Company pays him FRW 50,000. Compute Muneza's income tax payable

3.5. RSSB contributions and reliefs for employment income

Activity 3.5

Observe the picture here below of the Rwanda Social Security Board (RSSB) Headquarters and answer the question:



Refer to the picture above, which comment do you have on PAYE and Pension Contribution management

Employee contributions to the Rwanda Social Security Board (RSSB) are deducted from an employee's paycheck in a similar manner to PAYE. Employer contributions are also required and are deductible for tax purposes for the employer.

These are withheld by the employer and paid to the Rwanda Revenue Authority (RRA) along with PAYE. Then the RRA passes them to the RSSB.

3.5.1. RSSB Contributions

RSSB contributions are paid by all employees and employers and these funds the social security schemes run by the government.

The following schemes are worth looking into:

i. Pension and maternity leave schemes – mandatory for all employers

The rates of contributions required are:

	Employee Contribution	Employer Contribution	Total	Based on:
Pension	3%	5%	8%	All employment income except transport allowances and car benefits
Maternity leave	0.3%	0.3%	0.6%	Same as above

Tax base = Cash benefits + benefits in kind – Transport allowance/car benefit

ii. Medical scheme

This scheme is compulsory for public sector employers but optional for employers in the private sector. It provides extra benefits to employees

	Employee Contribution	*Employer Contribution*	*Total*	*Based on:*
Medical	7.5%	7.5%	15%	Basic salary only

iii.Community-Based Health Insurance Scheme

This scheme is compulsory for employees and is deducted from the employee's net salary and remitted by the employer.

All employers must collect and remit these subsidies to the Rwanda Social Security Board (RSSB) on a monthly basis not later than the 15th day of the following month.

	Employee Contribution	*Employer Contribution*	*Total*	*Based on:*
CBHI	0.5%		0.5%	Net salary

Illustration on computation of Pension and medical contribution

Lydia is employed by Kam investment Limited as the accountant on the following terms

a) Basic salary per month FRW 350,000
b) Communication allowances FRW 20,000 per month
c) Housing allowance FRW 100,000 per month
d) Transport allowance FRW 50,000 per month

Required: Compute the taxable income, PAYE, Pension contribution and Medical contribution

Answer:

Particulars	**Amount FRW**
Basic salary	350,000
Add other cash benefits	
Communication allowance	20,000
Housing allowance	100,000
Transport allowance	50,000
Taxable income	520,000
PAYE	
(0 – 30,000) @ 0%	0
(30,001 - 100,000) @20%	14,000
(100,001 – 520,000) @ 30%	126,000
Tax payable	140,000
Pension contribution by Employer	
Pension (520,000 – 50,000) *5%	23,500
Maternity (520,000 – 50,000) *0.3%	1,410
	24,910
Pension Contribution by Employee	
Pension (520,000 – 50,000) *3%	14,100
Maternity (520,000 – 50,000) *0.3%	1,410
	15,510
Medical contribution	
Employer (350,000*7.5%)	26,250

Employee (350,000*7.5%)	26,250
Community Health Based Insurance (CBHI)	
Total income	570,000
Less: PAYE	(140,000)
Less pension employee	(15,510)
Less Medical employee	(26,250)
Tax base	338,240
CBHI 0.5%	1,691.2

3.5.2. Employee contributions

If the scheme applies, the employer withholds these contributions and pays them to the RSSB on the employee's behalf. They are not a tax-deductible employment expense because PAYE is applied to gross taxable employment income before RSSB contributions are deducted.

3.5.3. Employer contributions

These are not subject to employee taxation. When calculating taxable business profits, they are allowed as an expense for the employer.

3.5.4. Pension relief

As per the law of 2018, an employee can contribute any amount. Thus, the threshold of 10 % of salary not exceeding FRW1,200,000 is no longer binding

Application activity 3.5

Marcel Manzi is employed by Bahoneza Ltd. He receives a monthly basic salary of FRW 950,000 and a cash allowance for living accommodation of FRW 470,000 and is provided with a car giving rise to a benefit-in-kind of FRW 142,000. Bahoneza Ltd has not elected to use the medical scheme. Calculate the amounts which Bahoneza will pay over to the RRA in employer and employee contributions to the applicable RSSB schemes.

3.6. Declaration and Payment

Activity 3.6

Observe the picture here below of Rwanda Revenue Authority (RRA) Headquarters and answer the question:

Refer to the picture above, who pay PAYE and RSSB Contributions to respective offices

3.6.1. Payment deadlines

The standard tax period for PAYE and RSSB is one month. This means that PAYE is declared and paid on a monthly basis.

However, if an employer has an annual turnover of or below FRW 200,000,000 then they may choose to pay on a quarterly basis (although the RSSB contributions must still be declared and paid on a monthly basis).

Taxpayers who declare PAYE on a quarterly basis have four quarters: the end of May, August, November, and February.

The declaration and payment must be made by the 15th of the month after the end of the tax period, whether monthly or quarterly.

For example, the tax for the:

- Month of March must be declared and paid by 15th April
- Quarter March to May must be declared and paid by 15th June

If the deadline falls during the weekend or on a public holiday, the next working day will be considered as the deadline.

3.6.2. Declarations

Previously, PAYE and RSSB contributions were declared separately; however, a **unified declaration** has been introduced and all newly-registered employers must use it. It is definitely advised that current employers use it.

Each employee's information, as well as their taxable pay and perks for which PAYE is due, will be included in the declarations. To arrive at the overall liability, a tax calculation for each employee will be performed. On different tabs of the declaration, details of casual laborers and those for whom this employer is their "second" employer is noted.

Depending on the circumstances, some employers may be excluded from paying PAYE. If this is the case, an individual must calculate PAYE on their own and remit it to the tax administration on a monthly basis.

3.6.3. Statement to employee

Employers are required to provide each employee with a statement each tax period showing:

- The employee's name
- The amount and type(s) of income received
- The amount of PAYE and RSSB contributions that have been withheld and paid on their behalf.

Application activity 3.6

Tracy Mwiza has just accepted a job working for Nziza as a shop assistant for Nziza's retail business, which has a turnover of FRW 30,000,000 per year. Nziza has never previously employed anyone, and this is Tracy's first job since leaving school.

Explain briefly to Tracy how her tax liability on her employment income will be paid.

Skills Lab 3

Through internet or after RRA officer presentation, students are required to prepare written report on PAYE and RSSB contributions in Rwanda.

End of unit assessment 3

1) Thierry Ngabo has an annual salary of FRW 75,000,000. He is provided with unfurnished accommodation and a car for his private use, which are both owned by his employer. Thierry Ngabo has three children attending school and his employer provides an annual education allowance of FRW 3,000,000 per child. Thierry Ngabo contributes FRW 50,000 per month to a privately qualified pension fund.

Calculate Thierry Ngabo's monthly income tax payable and PAYE.

2) Other sources of government revenue include "Rates," which are voluntary payments made to the government for specific services such as medical insurance, pension funds, and so on. Let's pretend that an employee was owed the following monthly remuneration during a certain month: Basic salary: FRW 885,000, responsibility allowance: FRW 796,000, performance pay increase: FRW 190,500, transport allowance: FRW 250,000, and post incentives: FRW 305,000 This employee was also provided housing in kind for the month.

Required:

a) Calculate the employee and employer contributions to the pension fund.
b) Calculate the contribution of maternity leave on both sides as described above.
c) As before, calculate the medical scheme (old RAMA) on both sides.
d) Determine the employment tax (P.A.Y.E.)
e) Determine the NET SALARY
f) Calculate the contribution to the Community-Based Health Insurance Scheme
g) Compute his take-home pay.

3) Karebu was employed as a cleaner in KY Limited for a period 6 months and is being paid FRW 80,000 per month. Karebu will be taxed as:

A. Casual Labour
B. Permanent employee
C. Second employment
D. None of the above

4) Kamisi was employed as a casual labour for 3 weeks and is paid FRW 50,000 per week. His tax liability will be

   A. FRW 45,000
   B. FRW 22,500
   C. FRW 18,000
   D. FRW 20,000

5) Mugisha gets a basic salary of FRW 100,000, transport allowance of FRW 50,000 and stays in the company house. His taxable income will be

   A. FRW 150,000
   B. FRW 180,000
   C. FRW 165,000
   D. FRW 170,000

6) The gross salary of Harelimana is FRW 500,000, he uses a company car and stays in the company house. His tax liability will be

   A. FRW 134,000
   B. FRW 179,000
   C. FRW 195,000
   D. FRW 75,000

UNIT 4 TAX DEPRECIATION

Key unit competence: Apply tax depreciation to produce a tax liability

Introductory activity

The main causes of depreciation are the natural wear and tear of fixed assets through use, which causes the value of fixed assets to decrease every year, for example, a typewriter is replaced by a computer, an asset is no longer used due to the change in enterprise size, and some assets have wastefulness due to the extraction of raw materials from them.

Referring to the section above, answer the following questions:

1) What is depreciation?
2) Using research, outline the assets that are depreciated in a pool system based on interest rates.
3) With research, the machines were bought in 2015 for FRW 40,000,000. Find the value of the depreciation using the fixed rate according to the Income Tax law No. 16/2018.

4.1. Definition, Nature of tax depreciation and its availability

Activity 4.1

If our school spend FRW 25,000,000 on a delivery vehicle, then the truck is projected to be used for four years. Advise the school administration on what they can do to ensure that it is replaced at the end of the planned usage period.

Depreciation is an accounting word that refers to a way of allocating the cost of a tangible or physical asset over its useful life. Depreciation is a term used to describe how much of an asset's worth has been used. It lets businesses generate revenue from the assets they possess by paying for them over time

Depreciation of fixed asset is defined as the allocation of the costs of the asset to the years in which benefits is expected from its use resulting in the loss of value of the asset due to physical deterioration or obsolescence.

Depreciation is an annual charge against the profits of a company to take account of the theoretical reduction in value resulting from the use of fixed assets belonging to the organization. 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, the works of art, and heritage assets.

a) Definition of tax depreciation

Tax depreciation is a method of accounting for the decrease in the value of an investment property's assets over time.

A tax depreciation allowance is available to individuals or corporations who own depreciable assets at the end of the tax period and use those assets to generate revenue.

b) Nature of tax depreciation and its availability

Tax depreciation is a form of tax relief given for capital expenditure. It replaces accounting depreciation because it is given in a standard manner according to tax legislation.

Accounting depreciation, capital purchases costing over FRW 500,000, and acquisition costs of fixed assets were all disallowed expenses.

All enterprises can claim tax depreciation on most fixed assets that will be used for business purposes. If a trader leases rather than owns an asset, the trader can only claim tax depreciation if the lease is classified as a finance lease (i.e. the asset is recognized on the trader's balance sheet). The lessor (the legal owner) is entitled to claim tax depreciation for operating leases.

Not all forms of capital expenditures are eligible for tax depreciation. The categories of capital expenditures for which tax depreciation can be claimed are listed in Article 28 of the income tax law No. 016/2018. Expenditure on the following items qualifies as a qualifying expense:

- Buildings, heavy industrial equipment, and fixed machinery – the eligible expenditure includes the costs of acquisition, construction, improvement, renovation, and reconstruction of such assets
- Purchased intangible assets, including purchased goodwill.
- Information and communication systems – there are different rates of allowances for these assets depending on whether their estimated useful life is more than or less than 10 years.
- Other qualifying business assets.

Land, Antiques, and Jewelry are examples of assets that do not qualify for tax depreciation because they are not susceptible to wear and tear or obsolescence. Internally generated intangible fixed assets, such as customer loyalty, are not eligible for tax depreciation.

Application activity 4.1

Goodwill was purchased by KBM Ltd, a Rwandan resident company, for a price of FRW 150,000,000.

Which of the following statements is true in relation to the tax relief available on this purchase?

a) KBM Ltd must have obtained a valid investment certificate in order to claim 10% tax depreciation.
b) No tax depreciation is available as this is an intangible asset.
c) The tax depreciation rate is 10% on a reducing balance method basis.
d) An investment allowance of FRW 75,000,000 could be available to KBM Ltd.

4.2. Difference between tax depreciation and accounting depreciation

Activity 4.2

Before we talk about accounting depreciation and tax depreciation, what is initial depreciation itself?

Depreciation is a way of accounting for the decrease in the useful life of tangible assets owing to obsolescence, wear and tear, and other factors. Accounting and tax depreciation are frequently different due to two key factors: computation method and accounting for asset useful life (they are calculated according to different procedures and assumptions).

a) What is Accounting Depreciation?

Accounting depreciation (also known as book depreciation) is the cost of a tangible asset allocated by a company over the useful life of the asset. The recognition of accounting depreciation is driven by accounting standards and principles such as GAAP. Remember that depreciation is a non-cash item. In other words, depreciation expense does not represent an actual cash flow for a business.

Despite its non-cash nature, depreciation expense still appears on the company's financial statements. A company records its depreciation expenses on the income statement. Thus, this non-cash item ultimately reduces the net income reported by a company.

In addition, most accounting standards require companies to disclose their accumulated depreciation on the balance sheet. The accumulated depreciation reveals the impact of the depreciation on the value of the company's fixed assets recorded on the balance sheet.

Accounting depreciation can be calculated in numerous ways. The two most common ways to determine depreciation are straight-line and accelerated methods.

The straight-line depreciation is the easiest and most frequently used depreciation method. It distributes depreciation expenses equally over all periods of the asset's useful life.

Conversely, accelerated depreciation methods allow deducting greater depreciation expenses in the earlier periods of the asset's useful life and smaller depreciation expenses in the subsequent periods. One of the examples of the accelerated depreciation methods is the double declining depreciation method.

b) What is Tax Depreciation?

Tax depreciation is the depreciation expense claimed by a taxpayer on a tax return for a tax period to compensate for the loss in the value of the tangible assets used in income-generating activities. Similar to accounting depreciation, tax depreciation allocates depreciation expenses over multiple periods. Thus, the tax values of depreciable assets gradually decrease over their useful lives. By deducting depreciation, tax authorities allow individuals and businesses to reduce their taxable income.

A taxpayer cannot claim depreciation for all assets. Only some assets that meet the specific requirements in the given tax jurisdictions may be eligible for the depreciation claim. Although the requirements generally vary among the tax jurisdictions, the most common criteria for depreciable assets are:

- The asset is the property owned by a taxpayer
- A taxpayer uses the asset in the income-generating activities
- The asset possesses a determinable useful life
- The asset's useful life is more than one year.

Tax authorities treat depreciation expenses as tax deductions. In other words, taxpayers can claim depreciation expenses for eligible tangible assets to reduce their taxable income and the tax amount owed.

Therefore, tax depreciation is calculated for the purpose of income tax. The main purpose of this calculation is to reduce taxable income. This is based on the Internal Revenue Service's (IRS) rules. For example, the IRS may state that a certain asset's useful life is ten years, hence tax depreciation calculations should be done for a ten-year period.

The IRS rules also allow a company to accelerate the depreciation expense. This means charging more depreciation in the first few years and less depreciation in the later years of the asset's life. This saves income tax payments in the first few years of the asset's life but will result in more taxes in the later years. Companies that are profitable find accelerated depreciation to be more attractive. Due to this reason, the company has to maintain two types of records for depreciation: one for the financial reporting purpose and the other for income tax purposes.

Furthermore, various businesses may have different depreciation policies, and tax depreciation may be considered differently as a result. For example:

- Full year's depreciation will be charged in the year of purchase
- No depreciation will be charged for the year if the asset is purchased in the middle or near the end of the year.
- No depreciation will be charged on the year of disposing of the asset

The key difference between Accounting Depreciation and Tax Depreciation is that while the accounting depreciation is prepared by the company for accounting purposes based on accounting principles, the tax depreciation is prepared in accordance with Internal Revenue Service's rules (IRS).

Application activity 4.2

1. What is Accounting Depreciation?
2. Brainstorm common criteria for depreciable assets.

4.3. Tax depreciation applied to individual assets and to pools of assets

Activity 4.3

Businesses can claim most of their labor costs on their tax returns as they incur the cost, but typically have to deduct their investment costs over many years. Due to inflation and the time value of money, the protracted amortization of capital expenditures is forcing companies to understate their capital expenditures in present values, thereby overstating their true revenues.

Tax on consumed income or personal expenses would have investment costs deducted as they are incurred, which is the optimal treatment for achieving the most economically efficient level of capital formation. Capital costs would only be amortized if investments lost economic value over time. Economic depreciation has two problems. First, it is impossible to measure because similar assets in different uses wear out or become obsolete at different rates. Second, the concept ignores the cost of locking money into an asset from the date of its purchase, reducing investment.

Answer the following questions with reference to the section above:

With research outline reasons for providing amortization

4.3.1. Tax depreciation applied to individual assets

The following assets are each treated independently for the calculation of the applicable tax depreciation, from the types of qualified assets listed in lesson 4.1 above:

- **Buil**dings, heavy industrial equipment, and
- **Heavy industrial machinery** – these are depreciated annually each on its own, on the basis of the rate of depreciation equivalent to **five percent (5%)** on a straight-line basis, so the relevant cost is multiplied by 5% and this remains constant until the asset is fully depreciated (20 years) or sold.

- **Intangible** assets including goodwill that is purchased from a third party are depreciated annually each on its own, on a straight-line basis, each on its own, on the basis of the rate of depreciation of ten percent (10%) of the relevant cost of the asset.
- Information and communication systems with an expected life of over 10 years – are depreciated annually on a straight-line basis of the rate of depreciation of **ten percent (10%)** of the relevant cost of the asset.

4.3.2. Tax depreciation applied to pools of assets

The remaining items of qualifying expenditure will be grouped, or 'pooled', and tax depreciation applied to the group of assets rather than to each asset individually.

The rates applicable are:

- **Computers** and accessories, and information and communication systems with a life of no more than 10 years: fifty per cent (50%) on a reducing balance basis
- Other qualifying business assets (Motor vehicle, Furniture, equipment and simple machines): twenty-five percent (25%) on a reducing balance basis

Keep in mind that the calculation of the tax depreciation on a pool is on a reducing balance basis; it is a percentage of the brought forward eligible expenditure (known as the 'tax written down value' (TWDV)) as adjusted for acquisitions and disposals that have taken place in the year.

Application activity 4.3

a) What rates of tax depreciation, if any, apply to the following items of expenditure?

   A. Production line machinery built into a factory

   B. A piece of telephone equipment with an expected life of 15 years, acquired under an operating lease

   C. The extension of a residential home

   D. The purchase of patent rights

4.4. Computing tax depreciation

Activity 4.4

Analyze the picture above and answer the following question:

With research, the machines were purchased at a cost of FRW 45,000,000. Find the value of the depreciation using the fixed rate according to the Income Tax Law No. 16/ 2018

4.4.1. Calculation of tax depreciation on individual assets

The principle of calculating tax depreciation for a single item is straightforward: simply apply the proper percentage to the asset's qualifying cost. Remember that assets that receive straight-line depreciation are treated individually, not collectively. As a result, each asset's computation must be prepared separately.

In the tax period in which the asset is acquired, a full year's worth of tax depreciation is given (irrespective of when in the period the purchase took place). There is no tax depreciation available during the time when an asset is sold.

When an asset is sold (disposed of), the sale proceeds are included in the trader's taxable income calculation (under Article 5 of Income Tax Law No. 16/2018, items 5 and 6). The asset's remaining balance must then be written off as a separate deduction in the year of sale.

4.4.2. Calculation of tax depreciation on asset pools

Computers, accessories, and information and communication systems having a 10-year life expectancy, and other qualifying assets, are given tax depreciation via 'pools' of expenditure. The balance of expenditure brought forward is increased for items purchased during the year (net of the investment allowance if applicable) and reduced by the proceeds of any relevant items sold. After that, the remaining balance is multiplied by the appropriate percentage (50 percent or 25 percent for computer equipment and other assets respectively).

The following preform should be used when computing these allowances:

Tax period to XX.XX.XXXX	*Computer equipment pool*	*Other business assets pool*	*Tax depreciation claimed*
	FRW'000	FRW'000	FRW'000
TWDV brought forward	A	B	
Add acquisitions (net of			
investment allowance)	C	D	
Less proceeds on disposal	(E)	(F)	
Balance to depreciate	G	H	XX
Tax depreciation	(G x 50%)	(H x 25%)	
TWDV carried forward	X	X	

Notes

- If either G or H above are negative (due to the sale proceeds on assets sold in the year being greater than the balance in the pool), a 'balancing charge' arises: the negative balance increases taxable profit for the year and the pool becomes zero.
- If either G or H are a positive value of less than FRW 500,000, the entire balance is deducted from profits as a balancing allowance (rather than multiplying by 50% or 25%). Again, the pool will be reset to zero.

Application Example

The TWDV brought forward on a computer equipment pool at the beginning of a tax period is FRW 1,000,000. There are no new acquisitions of computer equipment during the period.

- If computer equipment is sold during the year for FRW 1,200,000 the pool would stand at a negative balance of FRW (200,000). This FRW 200,000 would be added to taxable profit:

	FRW	FRW
TWDV b/f	1,000,000	
Proceeds	(1,200,000)	
Balance	(200,000)	
Balancing charge	200,000	(200,000)

- If computer equipment was sold for FRW 600,000 the pool would stand at FRW 400,000. Instead of a 50% allowance, the full FRW 400,000 would be deducted from taxable profit.

	Computer equipment	*Tax depreciation*
	FRW	FRW
TWDV b/f	1,000,000	
Proceeds	(600,000)	
Balance	400,000	
Balancing allowance	(400,000)	400,000
Pool c/f	NIL	

Application activity 4.4

Nkuvugishe Plc acquired a piece of telecommunication equipment at a cost of FRW 20,000,000 on July 01st, 2018. The expected life of the equipment was 20 years. The equipment was then disposed of on March 01st, 2020 for FRW 9,000,000.

Nkuvugishe Plc did not purchase any other assets in the tax period to December 31st, 2018.

Calculate the tax depreciation available on this asset for the three years to 31st, December 2020.

4.5. Investment allowance and Private use of assets by business owners

Activity 4.5

Analyze the images above and answer the following questions.

a) With research outline the rate of investment allowance

b) Discuss on investment allowance

4.5.1. Accelerated Depreciation

Rwanda encourages investment by providing a greater rate of tax relief (capital allowance) during the year of acquisition.

a) Conditions for the Accelerated Depreciation to apply

- For the Accelerated Depreciation to be claimed, the following conditions need to be met (Law No. 06/2015 relating to investment promotion and facilitation):
- The taxpayer must have applied for, and hold, a valid investment certificate issued by the Rwanda Development Board, specifying the incentives to which the taxpayer is entitled
- The taxpayer has invested at least US$ 50,000 in each new asset or used asset in the tax period
- Must Operate in at least one of the sectors below and meet the requirements:

    i. Export projects;

    ii. Manufacturing;

    iii. Telecommunications;

    iv. Agro processing;

    v. Education;

    vi. Health

    vii. Transport excluding passenger vehicles with less than nine (9) people seating capacity;

    viii. Tourism investments worth at least one million eight hundred thousand United States Dollars (USD 1, 800, 000);

    ix. Construction projects worth at least one million eight hundred thousand United States dollars (USD 1,800,000);

    x. Any other sectors provided the investment is worth at least one hundred thousand United States dollars (USD 100,000);

    xi. Any other priority sector as may be determined by an Order of the Minister in charge of finance;

- The assets must be retained by the business for at least three tax periods following the period of the claim; and

b) The rate of investment allowance

TheAccelerated depreciation is 50% of the acquisition cost of the asset.

c) The impact on tax depreciation

If the Accelerated depreciation is claimed on an asset, this will reduce the cost that is eligible for standard tax depreciation. Depending on the type of asset purchased, the remaining amount of qualifying expenditure will be given tax depreciation on a straight-line basis or allocated to a pool after computing and deducting the capital allowance.

d) Assets sold within three years

The investment allowance is revoked if a taxpayer claims the investment allowance on an asset but then sells it within three years. The reduction in tax obtained by claiming the investment allowance must be repaid to the tax administration, along with the applicable interest and penalties for the underpayment of tax.

4.5.2. Private use of assets by business owners

Private usage of a business asset by the owner or any employee limits the amount of tax depreciation that may be claimed.

If an item qualifies for tax depreciation, but the **owner uses it for personal reasons**, the tax depreciation deductible from cost is given in full at the usual rate, depending on the type of asset, while the tax depreciation claimable is limited to the proportion of business use only.

This arises when an asset is **used partly for business and partly for private purposes by the trader**, or any employee of the trader.

Keep in mind that, where an asset has divided use, then the tax administration should determine the amount of tax depreciation to be given based on the proportion of business use of the asset. Tax depreciation should be **calculated in full** at an appropriate rate and then the deductible tax depreciation will be that tax depreciation **multiplied by the percentage of business use** of the asset. Currently, the assumption is that 20% is for private use.

Application activity 4.5

A building is constructed in Musanze for use in the trade of MwizaPlc, a Rwandan resident trading company. The building cost FRW 200,000,000 and was paid for on 30th November 2019. MwizaPlc has a tax period to 31st December each year. MwizaPlc holds a valid investment certificate for this expenditure.

Which of the following statements is correct concerning the tax relief available for MwizaPlc on the cost of the building?

a) The investment allowance will be FRW 100,000,000 and the balance of FRW 100,000,000 will qualify for straight-line depreciation at 5% per year.

b) The investment allowance will be FRW 100,000,000 and the remaining FRW 100,000,000 will qualify for straight-line depreciation at 10% per year.

c) The investment allowance will be FRW 100,000,000 and the FRW 200,000,000 will also qualify for straight-line depreciation at 5% per year.

d) The building will only be eligible for standard tax depreciation at 5% per year.

End of unit assessment 4

1. Gasabo Plc, a Rwandan resident company, has the following brought forward balances on its assets that qualify for tax depreciation:

	Information	TWDV b/f (FRW)
Business premises	Cost FRW 100,000,000 investment allowance at 50% claimed on acquisition	40,000,000
Computer server equipment	Useful life 12 years, original cost FRW 6,000,000	4,200,000
Computer equipment pool	All assets life under 10 years	3,500,000
Other assets pool		8,600,000
Car (used privately by a company employee)		3,000,000

During the year, the following transactions took place:

Purchases

Office furniture costing FRW 600,000

Disposals

Computer equipment – proceeds FRW 3,100,000

Calculate the total tax depreciation available to Gasabo Plc in the tax period. Show clearly the balances to carry forward for each pool or individual asset.

2. Ineza Company purchased a building during the tax period for a price of FRW 50,000,000. No investment certificate was applied for by Ineza Company. The building is mainly used as retail premises by Ineza Company, but there is living accommodation above the shop which is used by one of the directors. Compute the maximum annual tax depreciation that can be claimed by Ineza Company in relation to this building.

UNIT 5 THE TAXATION OF INVESTMENT INCOME

Key unit competence: To be able to use and interpret the taxation of investment income

Introductory activity

Looking at the situation above in photos and talk about the activities carried out there.

In Rwanda everybody especially business people discussing about tax. This is because of wondering why you and businesses need to pay taxes. In Rwanda, there are ruling bodies from the village, sector, district, provincial and national levels. These bodies comprise: Legislature (who make laws), Executives (who enforce laws) and Judiciary (who exercise laws). The salaries that public servants receive to do their jobs come from taxes. Paying taxes is considered as civic duty, doing so is also a requirement of the law.

Paying your taxes is requirement of the law. If you do not pay your taxes, the government agency that oversees taxes (the Rwanda Revenue Authority or RRA) will require you to pay your taxes or else face penalties, such as fines or going to jail.

The Taxes have many forms depend on the tax base and taxpayer. When you work at a job to make money, you pay income taxes. Depending on how much money you earn.

When you buy things at a store, you also usually pay sales tax, which is a percentage of the cost of the item charged by the store. If you own property, you also pay property taxes on the value of your property.

As a business to be or referring to your community, what taxes can be paid to investment?

With examples from your community or Rwandan community at large, why do you think people and business need to pay tax on investment?

5.1. Legislative features or components of investment income

Activity 5.1

In Rwandan economy taxes are the most important source of government revenue.

Taxes differ from other sources of revenue in that they are compulsory levies and are not paid in exchange for some specific thing, but for welfare of taxpayers as a whole.

The Taxes have many forms depending on the tax base and taxpayer. When you generate income, you pay income taxes depending on how much money you earn. If you own property, you also pay property taxes on the value of your property.

As a business to be or referring to your community, look at income an individual may receive from investments and identify the elements this tax can have?

Investment income tax: Includes payments of interest, dividends, service fees, royalties, and rent which has not been taxed as business income in accordance with law No 016/2018.

5.1.1. Legislative features

Investment income includes all payments in cash or in kind in the form of interest, dividends or royalties. In the majority of cases, this will already have been paid as a withholding tax, but must still be declared, and then claimed back.

a) Financial interest

According to Article 40 of Law 16/2018, financial income includes:

i. Income from loans;

ii. Income from deposits;

iii. Income from guarantees;

iv. Income from government securities, income from bonds, negotiable securities issued by the Government, securities issued by public and private companies, as well as income from cash negotiable securities.

According to Article 60 of Law 16/2018, interest income is subject to a withholding tax of 15% on the value exclusive of VAT.

However:

- The interest income derived from the Treasury bond with a maturity period of three years and above, the withholding tax is 5%.
- Interests on deposits in financial institutions for more than one year is exempted;
- Interests on deposits/ savings made in Rwanda national investment trust (RNIT Iterambere Fund) is also exempted
- Interests on loans granted by a foreign development financial institution exempted from income tax under applicable law in the country of origin is also exempted;
- Interests paid by banks operating in Rwanda to banks or other foreign financial institutions is also exempted.

b) Dividend income

According to Article 41 of Law 16/2018, Dividend income is the payment of profits to shareholders, and is derived from the owing of shares in any societies. Because the profits of Rwandan resident companies suffer corporate income tax, the only further tax that may be payable by a Rwandan taxpayer on dividends received from a Rwandan company is withholding tax. This is applied on the outstanding balance of profit after taxation.

Like interest income, dividend income is also subject to a withholding tax of 15%. However, for shares that are listed at the Rwanda stock exchange and owned by a taxpayer from East Africa, it is subject to a withholding tax of 5%.

c) Royalties

Royalty income as per article 42 of law 16/2018, royalty income includes:

i. All payments of any kind received as a prize for the use of, or the right to use, any copyright of literacy, craftsmanship or scientific work including cinematograph films, films, or tapes used for radio or television broadcasting;

ii. Any payment received from using a trademark, design or model, computer application and invention patent;

iii. The price of using, or of the right to use industrial, commercial or scientific equipment or for using information concerning industrial, commercial or scientific knowledge;

iv. Payments from natural resource use.

The royalty income is taxed at a rate of 15% flat

Declaration period

Finance income, capital gain on shares, dividend income and royalty income are declared within 15 days after the month of withholding. For example if the month of withholding is April 2022, the tax should be declared and paid not later than 15th May 2022

d) Rental income

Rental income includes income from the rental of machinery and other equipment, including agriculture and livestock equipment. For the purpose of this lesson, rental income includes rent of machinery and other equipment only.

Application activity 5.1

1. Compare dividend and royalties as components of investment income
2. What kind of rental income is included in investment income?

5.2. Exemption from investment income

Activity 5.2

Paying taxes is requirement of the law. If you do not pay your taxes, the government agency that oversees taxes (the Rwanda Revenue Authority or RRA) will require you to pay your taxes or else face penalties, such as fines or going to jail. But there are some of incomes which are not chargeable to income tax on the individual.

- In Rwanda, not all goods and services pay taxes.
- Do you agree with this statement? Support your choice.
- Can you give some examples of goods and services you think should not pay taxes in Rwanda?

Exemption income is any income which is not chargeable to income tax on the individual.

1. Income accruing from savings in collective investment schemes and employees' shares scheme within a company are exempted from income tax.

2. Income earned by an agriculturalist or a pastoralist on agricultural or livestock activities is exempt if the turnover from agricultural or livestock activities do not exceed twelve million Rwanda francs (FRW 12,000,000) in a tax period. In case the turnover exceeds twelve million Rwandan francs (FRW 12,000,000), the latter amount is excluded from the taxable income.

3. Capital gain from the sale or transfer of shares on the capital market and capital gain from the sale or transfer of units of the collective investment schemes, is exempted from capital gain tax.

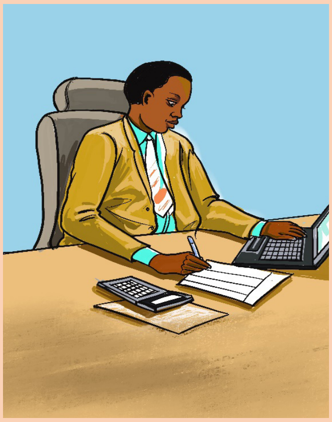
4) Interest income is exempted from the withholding tax:
   - Interests on deposits in financial institutions for at least a period of one year;
   - interests on loans granted by a foreign development financial institution exempted from income tax under applicable law in the country of origin;
   - interests paid by banks operating in Rwanda to banks or other foreign financial institutions;

Application activity 5.2

Through the examples of Rwandan community, describe the exemptions on investment income

5.3. Computation of tax on investment income

Activity 5.3



- Do you think it is important for businesses to know how to compute the amount of tax they are supposed to pay? Give reasons.

5.3.1. Financial interest:

Example:

Muhirwa has a current account with Mountain Bank ltd. Mountain Bank ltd pays him a gross interest of FRW 55,000 on his savings. As the source of this income, Mountain Bank ltd must declare and pay withholding tax on this interest of:

FRW 55,000 × 15%= FRW 8,250

This FRW 8,250 is declared and paid to RRA by Mountain Bank ltd. Therefore, the net amount that is transmitted by Mountain Bank ltd to Muhirwa is:

FRW 55,000- FRW 8,250= FRW 46,750

FRW 8,250 withholding tax was withheld by Mountain Bank ltd on behalf of Muhirwa. Therefore, Muhirwa can claim back this amount in income tax declarations.

5.3.2. Dividend income

Example one:

BCM ltd pays a gross dividend of FRW 100,000 to its shareholder, MUKUNZI. As the source of this income, BCM Ltd must declare and pay withholding tax on this dividend of:

FRW 100,000 × 15% = FRW 15,000

This FRW 15,000 is declared and paid to RRA by BCM Ltd. Therefore, the net amount that is transmitted by BCM Ltd to MUKUNZI is:

FRW 100,000 – FRW 15,000 = **FRW 85,000**

FRW 15,000 withholding tax was withheld by BCM Ltd on behalf of MUKUNZI. Therefore, MUKUNZI can claim back this amount in Income Tax declarations.

Example two:

HIMBAZA owns shares in MUHABURA limited a private company that is listed at Rwanda Stock Exchange (RSE). During the year ended, he received a dividend income of FRW 1,000,000

Dividend income: 1,000,000 x100/95 (since shares are listed at RSE the WHT tax is 5%) 1,052,632 x 5%=52,632

5.3.3. Royalties:

Example:

In order to promote your sales, XY Enterprise decides to use the mark of Inyange for a period of one year. In exchange XY Enterprise pays to Inyange Industries twenty-four million (FRW 24,000,000).

a) How do you call this type of income?
b) Calculate the related tax if any.

Possible Answer:

a) The term named for that income is Investment income/ royalty income
b) Tax to be paid = FRW 24,000,000 × 15% = FRW 3,600,000

Application activity 5.3

1. MUKUNZI received FRW 10,000 from his saving from the bank. Determine the gross amount to be included in his taxable income.

2. Modern Ltd company has received ten million (FRW 10,000,000) for allowing Millenium company to use its brand of soft drinks for two years. Calculate tax to be paid

5.4. Rental income from machinery and equipment

Activity 5.4

Basing on your knowledge on civic education, standards in business and other knowledge related to taxes, answer the following questions:

1. What do you understand by "machinery"?
2. What do you understand by "equipment"?
3. If people have Machinery and equipment for rent, do you think they have an obligation to pay their taxes? Give reasons to support your response.
4. If your response is yes in 3 above, mention some of the responsibilities you think taxpayers should have.

5.4.1. Rental income from machinery and equipment

Article 43 of law 16/2018 states that all revenues derived from rent of machinery and other equipment including agriculture and livestock equipment in Rwanda, are included in taxable income, reduced by:

1) Ten percent (10%) of gross revenue as deemed expense
2) Depreciation expenses
3) Interests paid on loans if the asset was financed by the loan

1. Example:

Mizero owns machineries which he rents to various entrepreneurs. During the year ended 31/12/2021, he received a gross income of FRW 15,000,000. The machineries were purchased at a cost of FRW 30,000,000 of which FRW 10,000,000 was a loan from the bank and he pays an interest rate of 19% annually. Mizero pays a quarterly installment of FRW 150,000 on the rental income.

Required: Compute his taxable income

Solution:

Since Mizero is an individual, tax liability is calculated using PIT formula.

Income from Rent of Machineries			
Gross income			FRW 15,000,000
Less allowable expenses		10% x 15,000,000	-1,500,000
			FRW 13,500,000
Less depreciation	25% ×30,000,000	7,500,000	
Less interest expenses (19% x 10,000,000)		1,900,000	FRW 9,400,000
Rental income			FRW 4,100,000

Tax liability

Tax band	Tax rate	Tax
0 – 360, 000	0%	0
360,001 – 1,200,000	20%	168,000
1,200,0001 – 4,100,000	30%	870,000
Tax liability		1,038,000
Less quarterly payments	150,000 × 3	450,000
Tax payable		**588,000**

If Mizero is a company, then apply corporate rate of 30% for companies, which are exempt from rental income tax.

Application activity 5.4

HIRWA owns some heavy industrial machinery which cost him FRW 20,000,000. He has rented the machinery out this year for FRW 2,400,000. HIRWA borrowed money to buy the machinery and has paid interest of FRW 100,000 this year. The relevant tax depreciation rate is 5% on cost.

Calculate his taxable rental income.

5.5. Capital gains tax on shares

Activity 5.5

In Rwanda, the taxes have many forms depend on the tax base and taxpayer. When you work at a job to make money, you pay income tax. Depending on how much money you earn.

When you buy things at a store, you also usually pay sales tax, which is a percentage of the cost of the item charged by the store. If you own shares and immovable property used for business purpose, you also pay tax referring to the income you earn.

Basing on your knowledge on civic education, standards in business and other knowledge related to taxes, what tax can be paid on income from shares.

5.5.1. Capital Gains Tax

According to Article 36 of Law 16/2018, capital gain tax is charged on the sale or transfer of shares. The capital gain on sale or transfer of shares is the difference between the acquisition value of shares and their selling price or transfer price.

5.5.2. Who must register for Capital Gains Tax?

The tax on profit from the sale of shares is withheld, declared and paid by the company whose shares were sold.

5.5.3. Tax rate of Capital Gains Tax

Article 37 of the same Law provides that capital gain tax is taxed at a rate of 5%, applied to the profit from the sale of shares, where profit equals sale price minus purchase price. i.e the difference between the acquisition price and selling prices.

5.5.4. Tax periods and deadlines of Capital Gains

Capital Gains tax must be declared and paid by the 15th of the month after the transaction was made. The tax is paid by the entity disposing of the shares (having recovered this tax from the seller of the shares).

Sale of shares on the capital markets, and the sale of units in collective investment schemes, are exempted from this tax. This exemption only applies to secondary market transactions for listed shares and securities.

5.5.5. Computation of capital gain tax

Example:

Madam KANAKUZE purchased 150,000 shares from Bank of Kigali at FRW 249 per share, a private limited company in 2012. In 2021, KANAKUZE sold 70,000 shares to Mark at FRW 350 per share.

Compute the capital gain and the capital gain tax

Possible Answer:

Particulars	FRW	FRW
Sales proceeds	70,000 x 350	24,500,000
Cost of the shares sold	70,000 x 249	(17,430,000)
Capital gain		**7,070,000**
Capital gain tax	5% x 7,070,000	**353,500**

5.5.6. Withholding and Declaration of Capital Gain Tax

According to Article 38 of the Law 16/2018, the capital gain tax on the sale or transfer of shares shall be withheld by the company within which the transaction occurred. This company shall declare and pay the capital gain tax to the Tax Administration within fifteen (15) days following the month in which the sale or transfer of shares occurred.

However, Article 39 of the same Law stipulates that capital gain from the sale or transfer of shares on the capital market and capital gain from the sale or transfer of units of the collective investment schemes, is exempted from capital gain tax.

Application activity 5.5

KANYARUTOKI owned 900,000 shares at Mobile Telephone Network (MTN) Rwanda, a private company. The share was purchased in 2015 at a price of FRW 180 per share. In 2021, he transferred 350,000 shares to MANZI. The market price of the shares at the date of the transfer is FRW 200 per share.

Required: Compute his capital gain and the capital gain tax.

5.6. Capital gains tax on immovable property

Activity 5.6

In Rwanda we have many businesses ensuring economic development of country. Some of those businesses are purchasing and selling immovable properties. The Taxes have many forms depending on the tax base and taxpayer.

Basing on your knowledge related to taxes, what tax can be paid on income of immovable property.

5.6.1. Capital gains tax on immovable property

Capital gains tax on immovable business property is paid at a rate of 30% of the selling value of the property (net of selling expenses and any unrelieved tax base) and can be declared as income as part of an individual's income tax assessment, or by a company as part of their corporate income tax. Alternatively, it can be declared separately. The capital gains tax is usual due by 31 March following the end of the tax period of the disposal; however, if a company uses a tax period that is not 31 December, the tax will be due by the last day of the third month following the end of the tax period.

5.6.2. Declaration of Capital Gains Tax:

Capital gains, refers to the sale or transfer of commercial immovable property, or profit from the sale of shares.

If a taxpayer receives taxable capital gains, and is registered for Income Tax, the taxpayer must declare these as income within the Income Tax declarations.

If a taxpayer receives taxable capital gains and is not registered for Income Tax, nor required to register for Income Tax, the taxpayer must register and declare Capital Gains Tax at RRA offices.

The only domestic tax type which cannot be declared online is Capital Gains Tax. This can only be declared with the help of RRA staff at RRA offices.

5.6.3. Exemption of Capital Gains Tax

1. A registered investor shall not pay capital gains tax. However, income derived from the sale of a commercial immovable property shall be included in the taxable income of the investor.
2. Capital gain on shares that are listed in Rwanda stock exchange and they are under secondary market
3. Capital gain on shares that are under a collective investment scheme

5.6.4. The penalties and fines

for Capital Gains Tax are similar to other domestic taxes.

This includes penalties and fines for:

- Late declaration
- Late payment
- Declaring less than the correct tax due
- Paying less than the tax due declared. There are no additional penalties or fines specifically applicable to Capital Gains Tax. The only difference compared to other domestic taxes is that as Capital Gains Tax is declared and paid on a case-by-case basis, there is no need to submit regular Capital Gains Tax declarations if no taxable capital gain has been received.

Example:

SEMUHUNGU purchase house in 2010 of FRW 40,000,000, SEMUHUNGU who is not registered as investor, sold this house in 2020 FRW 50,000,000 to KAYUKI. Compute taxable liability of SEMUHUNGU after sales.

Answer:

Taxable income for SEMUHUNGU is:

FRW 50,000,000 - 40,000,000 = FRW 10,000,000

Tax liability: FRW 10,000,000 × 30% = FRW 3,000,000

Application activity 5.6

1. What will happen when taxpayer receives taxable capital gains but registered in income tax?
2. What about penalties and fines for not paying capital gains tax?

End of unit assessment 5

1) Article 35 on law 16/2018 states that investment income includes any payment in cash or in kind in the form of the following types of income?

    A. Interest, Dividends, Trading and Rent

    B. Interest, Dividends, Royalties and Rent

    C. Dividends, Royalties, Trading and Rent

    D. Interest, Employment, Royalties and Rent

2) Which of the following types of income is chargeable to income tax on immovable business property?

    A. Pension payments from the state social security system

    B. Income accruing to employee share schemes

    C. Capital gain tax

    D. Capital gains from secondary market transactions in listed securities

3) SEBANANI has a current account with KIVU Bank ltd. KIVU Bank ltd pays him a gross interest of FRW 100,000 on his savings. As the source of this income, KIVU Bank ltd must declare and pay tax on this interest. Calculate taxable income

    A. FRW 100,000

    B. FRW 5,000

    C. FRW 15,000

    D. FRW 30,000

4) MUKAMANA owns some IT equipment which she let out for FRW 2,500,000 this year. It had cost her FRW 11,500,000, and the relevant tax depreciation rate is 10% on cost. MUKAMANA had to borrow money to fund the purchase of the equipment and pays interest of FRW 100,000 each year. MUKAMANA's taxable rental income for the year will be:

    A. FRW 2,500,000

    B. FRW 11,500,000

    C. FRW 1,000,000

    D. FRW 100,000

UNIT 6 TAXATION OF INDIVIDUAL BUSINESS PROFITS

Key unit competence: To be able to apply and compute the taxation of individual business profits (PIT).

Introductory activity

Observe the picture above and make an analysis of what is happening

The criteria for determining what is taxable and non-taxable business income, as well as what expenses may and cannot be deducted from turnover for tax purposes, are relatively similar for sole traders, partnerships, and corporations, and are all covered in this unit.

6.1. Definition of the concept

Activity 6.1

Because business owners and entrepreneurs work at the top of a company, their ability to make financial decisions can make a company more profitable and achieve financial success. However, it all starts with funding. But here, too, you can perform well in your company and the income tax law exempts you from income tax. Brainstorming.

Certain forms of business profits are tax-free; however, the majority of commercial activities are taxable.

a) What is a business?

In Rwandan tax law, there is no definition of a business. It might be viewed as a liberal trade, career, or profession.

A liberal profession is defined in Article 3 of the income tax law No. 16/2018 as: "a profession exercised on the basis of special skills, in an independent manner, in offering services to clients".

Business is an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, members or participants.

The following considerations should be in establishing whether a trade is being carried on, according to case law from other jurisdictions:

- The subject matter – are the goods being sold normally held as trading stock?
- The length of the period of ownership – the shorter this is, the more likely activity will be treated as a trade.
- The frequency of similar transactions – a single transaction is unlikely to be treated as a trade whereas multiple similar transactions suggest trading.
- Supplementary work and marketing activities.
- The existence of a profit motive.

Meaning of business Profit

Article 19 of section 3 of Law 16/2018 provides guidelines on the computation of business profits. According to Article 19 of Law 16/2018 business profits are determined as the income from all business activities reduced by all business expenses. Business profit also includes proceeds of sale of any business asset and proceeds from asset sharing received during the tax period. Business profits are determined per tax period on the basis of the profit or loss account drawn up in accordance with Generally Accepted Accounting Principles, subject to the provisions of this Law. The Tax Administration may use any other accounting method or other source of information in accordance with the law, to ensure the accuracy of the taxpayer's profit.

Tax exemption for profit on agricultural and livestock activities

Article 21 of Law 16/2018 also provides that income earned by an agriculturalist or a pastoralist on agricultural or livestock activities is exempt if the turnover from agricultural or livestock activities do not exceed twelve million Rwanda francs (FRW 12,000,000) in a tax period. In case the turnover exceeds twelve million Rwandan francs (FRW 12,000,000), the latter amount is excluded from the taxable income.

E.g., Jaden owns a farm in Bugesera where he practices agriculture and livestock farming.

During the year ended 31/12/2018 he received the following incomes

Item	**Turnover in amount FRW**
Sale of milk	8,120,000
Sale of bananas	5,000,000
Sale of beans	7,500,000
Sale of Irish potato	4,200,000

Required: Compute his taxable income and tax liability

Answer:

Taxable income 24,820,000 – 12,000,000 = 12,820,000

Tax Liability since the turnover is below 50,000,000, Jaden can opt to be taxed in the lump sum regime. And since the turnover is above 20,000,000FRW, the tax rate will be 3%Tax liability 3% x 12,820,000 = 384,600

Application activity 6.1

Mutunzi Gashumba owns a piece of land reserved for agricultural and livestock activities then during the year 2020 he sold 20 tons of beans which brought him a total income of FRW 15,870,350.

Required: Compute his taxable income.

6.2. The taxation of small businesses

Activity 6.2

Small and medium-sized enterprises (SMEs) make a significant contribution to the economy in terms of employment, innovation and growth. This applies to both industrialized and developing countries. Small and medium-sized enterprises, or SMEs, are playing an increasingly important role in the global economy, particularly in job creation. Micro and small businesses are a response to the needs of people, communities and society. Brainstorm on the important contributions of small businesses to economic development

Small businesses and micro-enterprises have a simplified method for calculating the income tax due. They are, however, allowed to opt-out of the simplified method and use the 'real regime'

6.2.1. Micro-enterprises – "Flat tax" regime

A **micro-enterprise** is one whose business activities generate turnover equal to or less than twelve million Rwandan francs (FRW 12,000,000) per tax period.

A micro-enterprise pays a flat tax. Turnover, rounded down to the nearest one thousand figure (FRW 1,000), is used to determine the flat tax due as below:

Annual turnover (FRW)	Annual flat tax due (FRW)
Up to 2,000,000	Nil
From 2,000,000 to 4,000,000	60,000
From 4,000,001 to 7,000,000	120,000
From 7,000,001 to 10,000,000	210,000
From 10,000,001 to 12,000,000	300,000

6.2.2. Small businesses – "Turnover" regime

A small business is one whose business activities result in a turnover ranging between twelve million and one Rwandan francs (FRW 12,000,001) and twenty million Rwandan francs (FRW 20,000,000) per tax period;

A turnover tax, commonly known as the "lump sum" regime, is the default tax structure for small businesses. The year's income tax due is based on 3% of total turnover, with no deductions for expenses or asset allowances.

Any small business may choose to opt-out of the turnover tax and into the 'real regime' (i.e., taxation of trading profit as adjusted for tax purposes, as discussed later in this chapter); this necessitates the preparation of financial statements in compliance with local GAAP. They must notify the tax administration of their decision, which is then irrevocable for three years from the date of making this notification.

If a small firm chooses not to pay the turnover tax, it may apply to the finance minister for a simplified method of accounting to calculate income taxable profit (Ministerial Order 5/19/10/TC dated 29/04/2019). Only daily cash and credit sales and purchases, as well as a record of all cash transactions, are needed of taxpayers. Full GAAP accounting is no longer required.

Keep in mind that, in the case of agricultural and livestock activities, only the excess (taxable) turnover is considered for calculating the tax due under either the flat tax or turnover tax regimes.

6.2.3. Liberal professions

The turnover tax and flat tax systems do not apply to businesses carrying on liberal professions; they must use the real regime.

Small and medium-sized enterprises (SMEs) make a significant contribution to the economy in terms of employment, innovation and growth. This applies to both industrialized and developing countries. Small and medium-sized enterprises, or SMEs, are playing an increasingly important role in the global economy, particularly in job creation. Micro and small businesses are a response to the needs of people, communities and society. Brainstorm on the important contributions of small businesses to economic development

Application activity 6.2

Calculate the amount of flat tax or turnover tax that the following businesses would pay, assuming that they had not opted out of the small business regime. If a flat tax or turnover tax is not applicable, state why.

a) Clement Gatete, a clothing manufacturer with an annual turnover of FRW 18,000,000 and expenses of FRW 4,000,000 per tax year.

b) Henriette Uwiragiye, a lawyer with an annual turnover of FRW 15,000,000 per tax year.

c) Dutembere Plc, a company specializing in the tourist industry, with a turnover of FRW 25,000,000 and expenses of FRW 6,000,000 per tax year.

d) Claude Mukamire, a crop farmer with an annual turnover of FRW 17,000,000.

6.3. Adjustment of profit for tax

Activity 6.3

The starting point in determining whether an item of income is business income is to determine whether the activity giving rise to the income is properly characterized as a business. With this in mind, what is adjusted profit for tax purposes?

For those businesses within the real regime, the amount of tax is determined by taxable profits. The taxable profit is the profit on which the tax is imposed. This is not the same as accounting profits; these must be adjusted for tax rules.

Accounting standards frequently clash with tax legislation. The taxable business profit is calculated by making multiple adjustments to the accounting net profit figure in order to bring the profit into compliance with tax laws.

6.3.1. The need to adjust profits

The Rwanda Revenue Authority (RRA) will normally accept profits that are determined in accordance with accounting principles provided that there is no conflict between the accounting principles and tax legislation. However, there is often a conflict, and the accounting profits may require several **adjustments** to be made to them in order to determine the taxable profits. Taxable profits are required to be determined in accordance with the requirements of tax legislation. Expenses that are allowed for tax purposes do not require any adjustment if accounts have already been prepared to reflect such expenses.

Some expenses which are charged in the accounts are not recognized as expenses for tax purposes. Expenses that are not allowed for the purposes of taxation should be added back to the net profit figure. Most expenses are specifically non-deductible per the requirements of tax legislation while other expenses are non-deductible because they do not meet the general criteria for allowing them as expenses for tax purposes. Similarly, some income which is credited to the profits is not taxable as business receipts or is entirely exempt from income tax.

6.3.2. Computation of taxable business profits

	FRW'000	FRW'000
Net profit as per accounts (A/Cs)		X
Add:		
a) Expenses charged in the A/Cs but not deductible for tax purposes	X	
b) Taxable income not credited to A/Cs	X	X
Less:		
c) Income credited to A/Cs but not taxable		X
d) Expenses for tax purposes not deducted in the A/Cs	(X)	X
Adjusted business profits		X
Less tax depreciation (unit 4)		(X)
Taxable business profits		X

6.3.3. General rule for the deduction of expenses

Article 25 of the Income Tax Law No. 16/2018 sets out the conditions for an expense to be deductible for tax purposes.

Expenses must fulfil the following conditions:

i. They are incurred directly for the purpose of the business and are directly attributable to the income generated.

ii. They represent a real expense incurred, and the taxpayer can substantiate the expense with a proper purchase document or receipt.

iii. The expense results in a decrease in the net assets of the business: either cash has actually been spent in the period, or an invoice exists to substantiate any accrued expenses.

iv. They relate to activities carried out in the tax period in which they were incurred (i.e they are deductible on the accrual basis). An expense incurred in a tax period must be claimed in that tax period – it cannot be deducted in a later year.

If expenses that do not meet all of these criteria have been charged to the profit and loss account, they must be added back in arriving at taxable profits. There are also some specific expenses that are not deductible from trading income and must be disallowed.

6.3.4. Expenses that are not deductible from taxable income (Disallowed expenses)

According to Article 26 of the income tax law No. 16/2018, the following categories of expenditure are not eligible for tax relief and must be excluded from the calculation of taxable trade profits:

i. Dividends paid by a company, or profits paid out of a business to its owner;

ii. Reserve allowances, savings, and other special-purpose funds, unless otherwise provided for by income tax law No. 16/2018;

iii. Fines and similar penalties;

iv. Donations, except if they total less than 1% of turnover and are made to non-profit making organizations (for example charities); if total donations to non-profit-making entities exceed 1% of turnover, the amount in excess of 1% of turnover is disallowed.

v. Tax paid, including Rwandan income tax, overseas income tax, and recoverable Value Added Tax (VAT);

vi. Personal expenses of the business owner;

vii. Entertaining expenses, except for expenses on general sporting activities for all employees;

viii. Twenty percent (20%) of expenses paid on business overheads that have both business and private elements which are not practically separable, such as telephone, water, electricity, and fuel;

ix. Management fees, technical services fees, and royalties paid to non-resident persons, where they exceed two percent (2%) of the turnover of the taxpayer – where such fees exceed 2% of turnover, the excess is disallowed;

x. Board sitting allowances, and any other amounts that should be taxed as employment, where tax has not been deducted under PAYE

xi. Interest arising from loans between related persons either paid or due on a total loan that is greater than four (4) times the amount of equity. This equity should not include provisions or reserves according to the balance sheet, which is drawn up in accordance with the Generally Accepted Accounting Principles.

The provisions under item (xi) above do not apply to commercial banks, financial institutions, and insurance companies.

Application Example

Categorize the following expenses as either allowable or disallowable in the tax computation for Gasabo Ltd, a Rwandan corporate business with turnover of FRW 150,000,000 in the tax period. If an expense is partially disallowed, state the amount would be added back to profit.

Expense	Allow in full	Disallow in full	Disallow part	Amount to add back (FRW'000)
Accounting depreciation of FRW 2,000,000		X		
Charitable donation of FRW 2,000,000			X	500,000 (>1% of turnover)
Staff bonuses of FRW 20,000 each (20 staff)	X			
A bad debt with a value of FRW 1,000,000 where the sale was recognized in income in the immediately preceding year and the amount written off in the books in the current year		X (debt <FRW 3,000,000; not yet three years old)		

Illustration 1: on computation of taxable and tax payable for individual

Mbonimpa is a medium business man in Kaciru. During the year ended 31/12/2021, he reported a loss of 4,700,000FRW. He provides the following information in support of this figure.

Purchases	**150,800,000**	**Sales**	**208,000,000**
Opening stock	12,450,000	Closing stock	1,680,500
Salaries	20,300,000		
Rent	9,600,000		
Marketing	1,500,000		
Electricity	4,000,000		
Depreciation	1,800,000		
Bad debt	950,000		
Purchase of furniture	3,280,000		
Repair and maintenance	2,200,500		
Donations	1,790,000		
Accounting fees	2,500,000		
Fines and penalties	2,650,000		
Entertainment	560,000		
Loss	4,700,000		

Additional Information

i. Mbonimpa lives in a flat above his shop. 30% of the rent and Electricity relates to the flat.

ii. During the year ended Mbonimpa took goods costing 800,000FRW to his home. The goods had a selling price of 1,600,000FRW.

iii. 300,000FRW of the bad debt expenses relates to debtor that has been declared bankrupt by the court. The remaining amount is a provision that was made at the end of the period.

iv. iThe donation was made to a charitable organisation

v. The fines and penalties relates to failure to withhold and paying taxes on time.

vi. Allowable capital allowance for tax purpose is 3,520,500FRW

vii. Mbonimpa pays 150,000 every quarter to Rwandan revenue authority as income tax

Required

i. Compute the taxable income, the tax liability and tax payable of Mbonimpa for the year ended 31/12/2021

ii. When should Mbonimpa declare and pay taxes.

Answer:

i. Computation of taxable income of Mbonimpa for the year ended 31/12/2021

Figures in Rwandan Francs

Particulars	Workings	Amount (FRW)	Amount (FRW)
Loss			(4,700,000)
Add back non allowable expenses:			
Rent	(30% x 9,600,00)	2,880,000	
Electricity	(30% x 4,000,000)	1,200,000	
Depreciation		1,800,000	
Bad debt	(950,000-300,000)	650,000	
Purchase of furniture		3,280,000	
Donation	W1	0	
Fines and penalties		2,650,000	
Entertainment		560,000	
Personal consumption	(1,600,000 – 800,000)	800,000	13,820,000
Business profit			9,120,000
Less capital allowance			(3,520,500)
Taxable income			5,599,500
Tax liability and tax payable	Tax rate		Tax
0 – 360,000	0%		0
360,001 – 1,200,000	20%		168,000
1,200,001 – 5,599,500	30%		1,319,850
Total tax liability			1,487,850

Less income tax paid	(150,000 x 3)		(450,000)
Tax payable			1,037,850

Workings

W1 Allowable donation 1% x 208,000,000 = 2,080,000

Donation made during the period 1,790,000

Since the donation was made to allowable charitable organisation and it is below one 1% of the turnover, it is all allowed

ii. Nzaboninka should make his declaration by 31/03/2018

Illustration2: Computation of taxable income and tax payable for individual

With examples differentiate between deductible and non-deductible expenses for income tax purposes

a) Nzamurambaho owns a supermarket in Kigali town. He submitted the following information to RRA for the income tax assessment purpose for the year ended 31/12/2021

Items	**Amount (000) FRW**	**Amount (000) FRW**	
Sales		250,000	
Cost of sales		(180,000)	
Gross profit		70,000	
Operating expenses			
Salaries	12,000		
Rent	8,000		
Electricity	4,000		
Bad debt	3,000		
Depreciation	15,000		
Income tax	7,000		
Transfers to reserves	2,500		
Audit fees	1,500		
Legal fees	8,000		
Advertising	4,000		

Repair and maintenance	10,000		
Donation	5,000		
Communication	2,500	(86,500)	
Operating loss		16,500	

Relevant information

i. FRW4,000,000 related to salaries accrued and not considered in the income statement

ii. 40% of the rent will expire in 2017

iii. Of the bad debt FRW1,000,000 relates to the customer that was declared bankrupt at the end of the year

iv. Capital allowances have been agreed by the tax administrators as FRW4,500,000

v. Legal fees relate to settling the divorce case

vi. Of the repair and maintenance, FRW3,000,000 was used to partition an office of the internal auditor.

vii. The donation was made to church

viii. Communication is the money loaded on the mobile phone of Nzamurambaho He uses it for both private and business

Required: Compute the taxable income and tax liability of Nzamurambaho

Answer:

Computation of taxable income and tax payable of Nzamurambaho for the year ended 31/12/2021

Items	**Workings**	**amount (000) FRW**	**Amounts (000)FRW**
operating Loss			(16,500)
Add non allowable deductions			
Rent	40% x 8000	3,200	
bad debts	(3,000 - 1000)	2,000	
depreciation		15,000	

income tax		7,000	
transfer to reserve		2,500	
legal fees		8,000	
repair and maintenance		3,000	
donation	(5000 -1% x 250000)	2,500	
communication	20% x 2500	500	43,700
less un recorded salaries			(4,000)
			23,200
less capital allowance			(4,500)
			18,700
taxable business income			
Tax liability			
0 - 360,000	0%		-
360,001 - 1,200,000	20%		168,000
1,200,000-18,700,000	30%		5,250,000
Tax liability			5,418,000

Application activity 6.3

The management of DUHAHE Ltd presented the following information for different accounts for the year ended 31st, December 2020:

ACCOUNTS	FRW
Sales	55,000,000
Cost of goods sold	12,000,000
Administration expenses	2,000,000
Operating expenses	1,500,000
Fines and penalties paid	500,000
Rent	3,000,000
Receivables	400,000
Bank and cash balances	2,500,000
Provisions for bad debt	5,000,000
Transport &insurance	1,500,000
Depreciation expenses	400,000

Communication expenses (telephone)	500,000
Interest paid to Bank of Kigali	400,000
Electricity and water expenses	400,000
Fuel expenses	600,000

Additional information:

- 25% of the rent is to be considered as personal expenses for Mr.Kagabo, one of the directors of the company.
- Overheads expenses (Telephone & Electricity), because the shop and the family's residence were in the same building, it was difficult to separate such expenses.
- Investment allowance, allowable for the year is FRW 1,500,000

Required:

a) Calculate the profit for the company for the year ended 31st Dec 2020.

b) Determine the adjusted taxable income for the year ended 31st Dec 2020.

The management of DUHAHE Ltd presented the following information for different accounts for the year ended 31st, December 2020:

ACCOUNTS	FRW
Sales	55,000,000
Cost of goods sold	12,000,000
Administration expenses	2,000,000
Operating expenses	1,500,000
Fines and penalties paid	500,000
Rent	3,000,000
Receivables	400,000
Bank and cash balances	2,500,000
Provisions for bad debt	5,000,000
Transport &insurance	1,500,000
Depreciation expenses	400,000
Communication expenses (telephone)	500,000
Interest paid to Bank of Kigali	400,000
Electricity and water expenses	400,000
Fuel expenses	600,000

6.4. Capital and revenue expenditure

Activity 6.4

Since you've covered some lessons in general ledger, you need to distinguish between capital expenditures and revenue expenditures.

Expenditure that is capital in nature (i.eg; a fixed asset) does not qualify for tax relief in the period it is incurred. While revenue expenditures are those expenditures of the government that do not lead to the creation of fixed assets. The government spends money under various accounting heads, such as paying interest on loans, salaries, pensions, subsidies, spending on different ministries and departments, etc.

Law regulating capital and revenue expenditure.

The third requirement of Article 25 (income tax law no. 16/2018) stipulates that an expense must diminish the business's net assets in order to qualify for tax relief. This implies that it must be revenue rather than capital in nature. The following are the primary factors to consider when calculating taxable profits:

i. **Expenditure** incurred on the acquisition or improvement of fixed assets, including any associated legal and professional fees, **cannot be deducted** unless the asset cost is less than FRW 500,000. Items costing FRW 500,000 or less may be deducted immediately.

ii. Accounting depreciation of fixed assets and losses on the disposal of fixed assets are **non-deductible expenses.**

iii. Accounting **profits** on disposals of fixed assets are **not taxable income.** The proceeds on the sale of an asset will be charged to income tax (or capital gains tax).

When expenditure is made once and for all with a view to bringing into existence an asset or advantage for the enduring benefit of a business, that expenditure will reasonably be treated as capital expenditure.

Problems arise when dealing with repairs and renewals. Repair is restoration by renewal or replacement of subsidiary parts of the whole. For example, replacing a chimney in a factory would be a replacement of a part of an asset (the building), and therefore is revenue expenditure and will qualify for immediate tax relief, but if the asset itself was a chimney (for example at a power station), replacing it would be capital, and therefore considered a fixed asset - this would not be deductible immediately but would qualify for tax depreciation.

When an asset is purchased that requires significant investment before it can be utilized in commerce, this investment is typically capital - for example, making a ship seaworthy before it can be used.

However, expenditure on newly purchased assets to repair natural wear and tear, on the other hand, represents revenue and is allowed.

Application activity 6.4

Which **TWO** of the following items would be considered capital, and therefore not deductible from business profits?

1. Repair of a large piece of machinery following a breakdown – the repair cost FRW 600,000
2. A computer upgrade costing FRW 300,000
3. A building extension costing FRW 15,000,000
4. The purchase of a second-hand delivery van costing FRW 1,000,000

a) 1 and 3
b) 2 and 3
c) 3 and 4
d) 1 and 4

6.5. Transactions in foreign currencies

Activity 6.5

Brainstorm what is a foreign currency and what foreign currency transaction is.

Gains or losses on translation of assets are reflected as part of taxable income.

6.5.1. How exchange differences arise

The conversion of the values of assets and liabilities held in a foreign currency may be required while preparing accounts (and taxable income) in Rwandan francs. Here are some examples:

i. A sale to an overseas customer (where invoiced in a currency other than Rwandan francs) which is an outstanding debtor at the end of the tax period
ii. Any asset, such as stock or a machine, that was purchased in a currency other than the Rwandan franc
iii. An outstanding creditor that will be repaid in a foreign currency

The item must be re-translated using the closing exchange rate if the exchange rate at the time of the original transaction differs from the exchange rate at the end of the tax period. There will be an exchange gain or loss as a result of this. The relevant exchange rates to use will be those published by the National Bank of Rwanda.

6.5.2. Tax treatment of exchange differences

If the accounts were prepared in accordance with GAAP, the differences would have already been estimated and accounted for in the period's profit or loss. There will be no need to modify profits because taxing exchange gains and deducting exchange losses as part of taxable company income is proper. If these entries aren't made in the books, an adjustment to taxable income will be made to reflect the entire exchange discrepancies.

Application Example

Robert Kamanzi, a Rwandan resident exporter of goods, makes a sale to Jacob Walton, a US customer, on 14 September 2021. Kamanzi agrees with Jacob that he will pay for the goods in US dollars ($). Kamanzi invoices for a total of $2,300. Payment terms are agreed at 60 days, and Jacob had not settled the invoice by 30 September 2021.

Relevant exchange rates are as follows (FRW per USD):

14th September 2021: 994.8804 / 30th September 2021: 997.5315

Calculate the exchange difference that would be taxable or deductible for Kamanzi.

Solution

At the date of the sale, the original invoice was worth ($2,300 x 994.8804) = FRW 2,288,225. The Rwandan franc has strengthened, and so if Jacob were to have paid the invoice on 31st September, it would now be worth ($2,300 x 997.5315) = FRW 2,294,322. The exchange gain of FRW 6,097 will be treated as part of taxable business income. Conversely, any exchange losses are a deductible business expense.

Application activity 6.5

Jackson Habimana, a sole trader, has purchased some goods from a Finnish supplier and has received an invoice for € 5,000. He has not settled this invoice at the end of the tax period.

Relevant exchange rates are as follows (FRW per €):

Date of purchase: 1,020.85

End of tax period: 1,051.25

Complete the following sentence:

Jackson will record an exchange (gain/loss) of FRW __________ in the tax year, and this will be treated as (taxable income/a deductible expense).

6.6. Long-term contracts and stock

Activity 6.6

Accrual accounting is commonly used as the basic financial reporting system for businesses. The idea behind the system is to reconcile the costs with the income for specific activities, so that a true picture of the profitability of the activities can be obtained. The results of accrual accounting are manifested in the balance sheet, income statement, and a variety of other historical business reports. The cost and revenue information required to perform all optimizations is different than that required for accrual accounting, and the requirements for tax analysis are in turn different.

Answer the following questions based on the above scenario:

1. What is the definition of a long-term contract?
2. Discuss the accrual concept.

Long-term contracts must be taxed according to the accruals concept. Losses on long-term contracts are treated in a special way. Stock must be appropriately valued and accounted for in arriving at taxable profits.

6.6.1. What is a long-term contract?

A long-term contract is a contract for manufacture, installation, construction, or "Long term contract" means a contract for work, manufacture, installation of construction, the performance of related services, which is not completed in the tax period in which work under the contract commenced, or other than a contract estimated to be completed within the twelve months as of the date on which work under the contract commenced. 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 or comparing the value of the work certified and the contract price.

Percentage of completion = expenses of the work certified

Estimated contract cost: 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

Example:

On 1st/1/2021 Akandi Limited started the construction of road from Nyagatare to Kayonza. The agreed contract price was FRW 30,000,000,000. The cost accountant of Akandi Limited estimated a cost of FRW 27,000,000,000 to the complete the road. By 31st/12/2021, the road was only complete up to Kabarore and the following costs were incurred up to that point: salaries and wages FRW 350,000,000, Materials FRW 4,500,000,000, Administration and General Expenses FRW 800,000,000 and other miscellaneous expenses FRW 200,000,000.

Required:

a) Compute the Taxable income for Akandi limited for the year ended 31st/12/2021.

b) Differentiate between accounting period and period of accounts

Solution:

Computation of taxable income for Akandi Limited for the year ended 31/12/2021.

Particulars	Workings	Amount (FRW)	Amount (FRW)
Contract price			30,000,000,000
Estimated cost			27,000,000,000
Costs incurred during the period			
Salaries	350,000,000		
Materials	4,500,000,000		
Administration	800,000,000		

Miscellaneous	200,000,000	5,850,000,000	
Percentage of completion	$\frac{\text{Cost incurred}}{\text{Estimated cost}}$	$\frac{5,850,000,000}{27,000,000,000}$	21.67%
Revenues accruing to the period	Percentage of completion x contract price	21.67% x 30,000,000,000	6,501,000,000
Less cost during the period			(5,850,000,000)
Taxable Income for the period			651,000,000
Total			

Example: If a contract with an agreed price of FRW 2,000,000 is estimated to cost FRW 1,500,000 to fulfil, there is an estimated overall profit of FRW 500,000. If, at the end of the tax period, the contract is still in progress and the costs incurred to date total FRW 1,050,000:

i. The percentage complete is estimated at (FRW1,050,000/FRW1,500,000) = 70%

ii. Hence the income that should be reflected in business profits will be (70% x FRW 2,000,000) = FRW 1,400,000.

iii. The amount of profit to tax in the current tax period will be FRW 350,000 (FRW 1,400,000 –FRW 1,050,000) or (70% x (FRW 2,000,000 – FRW 1,500,000)). If this is not the amount of profit that has been recognized in the accounts, an appropriate adjustment must be made.

6.6.2. Losses on long-term contracts

If in the subsequent period where a long-term contract is completed, there are unexpected costs incurred by the business in order to complete the contract, this may result in a loss being incurred, whereas in previous tax periods the taxpayer may have paid income tax based on anticipated contract profits.

This loss will reduce the taxable profit of the subsequent period (as the expenses recognized in the profit and loss account will be higher than the associated income). If a loss cannot be offset by other profits in the period in which the contract is concluded, the excess loss might be ‘carried back’ and used for profits already recognized on that contract.

6.6.3. Stock

The majority of retail and manufacturing companies will maintain a level of trading stock. As you may recall from your accounting studies, cost of sales identifies closing stock as a company asset that is 'matched' with sales revenue when the item is sold using the accruals concept.

The same principle applies to taxable income: a stock tax deduction is only available after the accompanying income is recognized. Closing stock is valued at the lower cost and market price on the last day of the tax period, according to Article 27 of the income tax law No. 16/2018.This means that stock losses would be recognized right away, however, gains (profits) would not be recorded until the asset was sold. However, before the taxpayer may claim compensation, the RRA must inspect the stock and agree on the loss to expense. Losses cannot be expensed without RRA clearance.

If the trader provides a service rather than commodities, the work in progress may be valued at cost at the conclusion of the tax period.

Application activity 6.6

Which TWO of the following statements are TRUE in relation to the taxation of long-term contracts and stock?

1) The tax treatment of long-term contracts generally follows GAAP.
2) Income to be taxed will depend on the amount invoiced to a customer in the year.
3) The percentage of a contract that was completed during the year will determine the level of profit to be taxed.
4) Stock is always valued for tax purposes at its market value at the end of the tax period.

a) 1 and 4 b) 2 and 3

c) 1 and 3 d) 2 and 4

6.7. Bad debts

Activity 6.7

In the determination of business profit, a deduction is allowed for bad debts if the following conditions are fulfilled:

- if an amount corresponding to the debt was previously included in the income of the taxpayer;
- if the debt is written off in the books of accounts of the taxpayer; and
- if the taxpayer has taken all possible steps in pursuing payment and has shown concrete proofs that the debtor is insolvent

But there is an exception: bad debts recovered are added back to taxable profit.

Given the above statements, you are required to prepare a presentation on the following questions:

a) What is a bad debt?
b) Any simple example of bad debt?
c) What causes bad debts?
d) What are the effects of bad debts?
e) Why bad debts recovered are added back to taxable profit?

Bad debts: These are amounts outstanding in the personal accounts of debtors which have proved will not be paid.

Bad debt is an expense that a business incurs once the repayment of credit previously extended to a customer is estimated to be uncollectible and is thus recorded as a charge off.

Bad debts will usually be charged as an expense to the profit and loss account. They represent income that has been recognized but will never be received by the seller.

To be eligible for tax relief for bad debt, the seller must meet all of the following requirements:

i. The amount has previously been included in the taxable income of the taxpayer;
ii. The debt has been written off in the books of accounts of the taxpayer;
iii. The taxpayer has taken all reasonable steps to recover the debt and the debtor has been declared insolvent by a court decision.

However, for an individual whose debt is less than three million Rwandan francs (FRW 3,000,000) in addition to the conditions referred to in points 1° and 2° above, the taxpayer must provide proof that he has taken all reasonable steps over a period of three (3) years to recover the debt.

Thus, no court insolvency decision needs to have been made for such debts, but there will be a significant delay between the debt becoming bad and the tax relief becoming available.

If the aforementioned requirements are not completed, the bad debt will not be eligible for tax relief. As a result, if the bad debt is charged to the profit and loss account, it must be put back into the calculation of taxable profit before a deduction can be taken in a later tax period provided the circumstances are met.

Note that licensed financial institutions and leasing businesses are exempt from meeting the aforementioned standards and may deduct any rise in their mandatory reserves for non-performing loans.

Any provisions made for doubtful debts, whether general or specific in nature, are not allowable expenses. They fail to satisfy neither the above conditions nor the general conditions for deductibility set out in lesson 6.3.3. A reduction in a provision may be subtracted from the accounting profit; on the other hand, an increase in a provision must be added back in the adjustment of profit.

Application activity 6.7

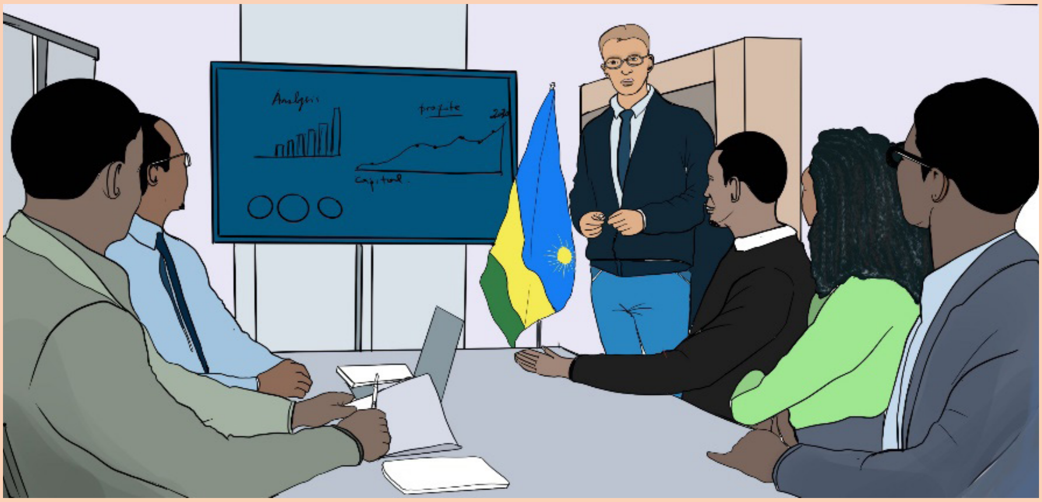
Nancy Keza, a business owner, is owed the sum of FRW 2,700,000 by Kelly Umuhoza, a customer. The original sale was recorded in Nancy's books on 31st July 2018, with credit terms of 60 days, and declared as part of business profits in Nancy's tax declaration for that year. Nancy has been trying to recover this amount from Kelly since then. She wrote the debt off as a bad debt in the 2020 accounts. Nancy has regularly tried to contact Kelly and has employed debt collectors, but has as yet been unsuccessful in recovering the money.

What is the correct treatment of this debt in Nancy's tax declaration for the tax period to 31st December 2021?

a) Add back a disallowed expense of FRW 2,700,000
b) Deduct bad debt relief of FRW 2,700,000
c) Do nothing

6.8. Transfer pricing

Activity 6.8



Businesses rely on transfer pricing to ensure transaction prices between related parties are comparable to fair market value. This process, conducted in accordance with Organization for Economic Co-operation and Development (OECD) guidelines, requires that the governing entity of this transaction choose a pricing methodology that provides the best estimate of that fair market value. Why do countries choose a transfer pricing methods?

Adjustments to taxable income and deductible expenses may be required when transactions between related parties are not at arm's length.

6.8.1. Transfer pricing principles

Multinational groups of companies will typically trade with each other in goods and services. The price at which such transactions occur is called the transfer price. While the trading of goods between Rwanda and other countries is governed by Article VII of GATT (the General Agreement on Tariffs and Trade), and must not take place at an artificial or contrived value, this rule does not apply to the transfer price for services. An overseas parent company could therefore charge management fees, and **manipulate the transfer price** so that profits arise in a country where the **rates of taxation are lower** so that the **overall tax liability of the group is minimized.**

The transfer pricing rules mean that the purchase price of goods and services paid for by Rwandan businesses to related parties should not exceed the amount that would have been paid to an independent third party.

6.8.2. Definition of related persons

Article 3 of the income tax law N°. 16/2018 defines related persons as “any person who acts, or is likely to act, in accordance with the directives, opinion or wishes of another person when such directives, opinion or wishes are communicated or not communicated to them”.

The following are specifically deemed related persons:

i. An individual and their spouse, lineal ancestors, and descendants until at least the third degree

ii. A person who participates directly or indirectly in the management, control or capital of the other person,

iii. A third person who participates directly or indirectly in the management, control or capital, or both control and capital, of another person (for example two companies that are controlled by the same parent company are related),

iv. Any of the above persons who participate directly or indirectly in the management, control or capital of an enterprise

A common example of related persons is a company and its shareholders and directors; the shareholders meet the definition in (ii) above as persons who participate in the capital of the company (which is a legal person in its own right), and the directors participate in management.

6.8.3. Impact of transfer pricing rules

Related persons must retain documents that justify that the prices charged on transactions between themselves were carried out on an arm’s-length basis.

If a taxpayer fails to retain such documentation, the tax administration has the power to adjust taxable profits accordingly. For example, if the price paid for a management service by a Rwandan business to its overseas parent company was above an arm’s-length price, the tax administration would increase taxable income by the difference between the actual price and the arm’s-length price.

Arm’s length prices

If a person enters into a controlled transaction, he or she must determine the price and margin resulting from the transaction, in a manner that complies with the arm’s length principle. In determining whether the result of a controlled transaction complies with the arm’s length Principe

Methods of determining arm's length prices

Comparable uncontrolled price method

The comparable uncontrolled price method consists in comparing the price charged on property, goods or services transferred or supplied in a controlled transaction to the price charged on property, goods or services transferred or supplied in a comparable uncontrolled transaction and done in comparable circumstances.

Resale price method

The resale price method begins with the price at which a product that has been purchased from a related person is resold to an independent person

Cost plus method

The cost-plus method begins with the costs incurred by the supplier of property, goods or services in a controlled transaction. An appropriate cost-plus markup is added to the costs incurred to make an appropriate profit, taking into account the functions performed and the market conditions. The result is considered as an arm's length price of the original controlled transaction

Transactional net margin method

The transactional net margin method consists of comparing the net profit margin related to the appropriate base such as costs, sales or assets that a person achieves in a controlled transaction with the net profit margin achieved in a comparable uncontrolled transaction.

Transactional profit split method

The transactional profit. If it is possible to determine arm's length profits for some of the functions performed by related persons in connection with the transaction using one of the approved transfer pricing methods, the transactional profit split method is applied based on the common residual profit that results once such functions are so remunerated

6.8.4. Thin capitalisation

Internationally, most tax jurisdictions (including Rwanda) provide that taxable income may be reduced by amounts paid as interest on loans to related parties. By contrast, most do not provide tax relief for distributions to owners made to shareholders by way of dividends. As a result, multinational enterprises are motivated to finance their foreign subsidiary companies through loans rather than share capital. When the subsidiary is financed heavily by debt finance, its taxable profits would be substantially reduced by interest payments.

To prevent huge reductions of taxable profits by way of interest deductions, thin capitalization rules apply. These rules limit the amount of interest that would be allowed as a deduction when computing taxable business profits. This is done by not allowing as an expense the amount of interest paid on related party loans when the company's debt to equity ratio exceeds a certain limit.

In Rwanda, this limit is a ratio of four to one: where debt is more than four times equity (share capital on the balance sheet), a company is said to be "thinly capitalized" and interest payable on loans to related persons will not be given tax relief (and must therefore be added back).

Example

YC Plc, a Rwandan company, has the following capital structure:

Share capital FRW 50,000,000

Reserves FRW 150,000,000

Debt FRW 300,000,000 (of which FRW 100,000,000 is an intra-group loan)

The company is thinly capitalized, as debt (FRW 300,000,000) is six times the equity shares capital (FRW 50,000,000).

The implications of this are that the interest on the intra-group loan would be disallowed in full.

Application activity 6.8

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.

Required: Demonstrate the transfer pricing process in this case.

End of unit assessment 6

Q1. Here is the statement of profit or loss of Diane, sole trader, for the tax period ended 31 Dec.

	FRW'000	FRW'000
Gross profit (turnover less cost of sales)		90,000
Other income		
Profit on sale of a fixed asset		860
		90,860
Expenses		
Wages and salaries	59,000	
Electricity and fuel	5,000	
Depreciation	1,500	
Bad debts	3,150	
Entertainment expenses for customers	350	
Patent royalties paid (to third parties)	3,200	
Legal expenses on acquisition of new office premises	650	
		(72,850)
Finance costs		
Bank interest paid		(300)
Net profit		<u>17,710</u>

Additional information

Salaries include FRW 15,000,000 paid to Diane to cover her personal expenses.

Electricity costs include the cost of lighting and heating Diane's home (where she regularly carried on her business before acquiring a purpose-built office during the year).

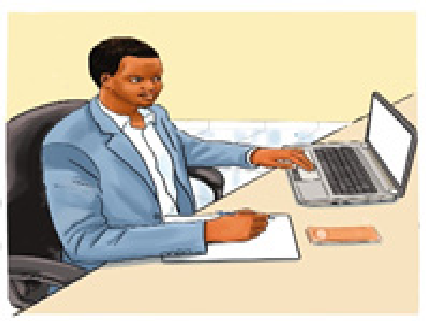
The bad debt cost was written off due to the court insolvency of a customer during the year; this income was recorded in the accounts in the immediately preceding tax period, and Diane spent considerable effort attempting to recover the debt prior to the insolvency.

Compute the adjusted taxable trade profit (before tax depreciation). You should start with the net profit figure of FRW 17,710,000.

UNIT 7 ESTABLISH PAYROLL REQUIREMENTS AND PAYROLL PREPARATION

Key unit competence: To be able to prepare payroll according to organizational policy

Introductory activity



Case study:

Ineza company is located at Gisenyi sector, Rubavu district, western province. The core value of Ineza is to provide better services to its customers and achieving its goals. INEZA company is in competition with different local companies. INEZA company is encountering challenges of paying staff salaries on time, secondly complains on discrepancies of wrong computation, wrong deduction, missing allowances are often raised by staff. This is due to lack of qualified and competent accountant. In other words INEZA company has a challenge of performing those issues.

From the passage above answer the following questions:

1. What is the name of document required to prepare for the above case study?
2. Give the difference between salary and wage.

7.1. Employment contract

Activity 7.1

Analyze the photos below and answer the questions that follow.

Q1. After defining the term "contract" differentiates the object from the purpose.

7.1.1. Definition of employment contract

Employment contract is an agreement between an employer and an employee whereby an employee undertakes to work under the authority of the employer in return for remuneration.

7.1.2. Terms used

a) Employee

A person having agreed to work for an employer under a contract concluded between them, and in return for remuneration.

b) Employer

An individual, a public or private entity that employs one or more employees on a permanent or temporary basis.

c) Probation period

The probation period cannot exceed three (3) months.

However, after the written evaluation of the employee's performance has been notified to the employee, the employer can for valid reasons related to the nature of work, employee's performance and conduct, decides that an employee retakes the probation for a period not exceeding three (3) months.

If the probation period comes to an end and proves to be conclusive, the employee is immediately offered employment and notified in writing by the employer.

d) Salary

A fixed regular payment, typically paid on a monthly basis but often expressed as an annual sum, made by an employer to an employee.

e) Wage

A fixed regular payment earned for work or services, typically paid on a daily or weekly basis.

7.1.3. Types of employment contract

a) Permanent employment contact

Permanent employment contracts apply to employees who work regular hours and are paid a salary or hourly rate. The contracts are ongoing until terminated by either the employer or employee and may be for full or part time work.

Employees on these contracts are entitled to the full range of statutory employment rights.

b) Fixed-term contracts

Fixed-term contracts give a set end date, for example six months or one year.

c) Casual employment contracts

The casual employment contract is suitable for scenarios where you want an individual to commit to working for you, but you're not sure how many hours of work you'll be able to offer him/her each week and cannot guarantee a regular working pattern. The contract should specify the minimum number of hours that you expect them to work each week, with the expectation being that the working pattern and hours offered above this minimum, is likely to fluctuate.

7.1.4. The details of employment contract

It must contain the following particulars or details:

- The names of employee and employer;
- The date on which the employment began;
- The date on which the employee's period of continuous employment began, taking into account any previous employment is to count as continuous employment
- The scale or rate of pay and the method of calculation;
- The intervals at which payment is made;
- Any terms and conditions relating to holiday entitlement;

- The end of notice which either party needs to give notice to end an employment;
- The job title of the employee, or a brief description of his duties;
- Where the employment is not intended to be permanent, the period for which it is expected to continue, or if it is a fixed term, the date at which the term is expected to end;
- The place of work;

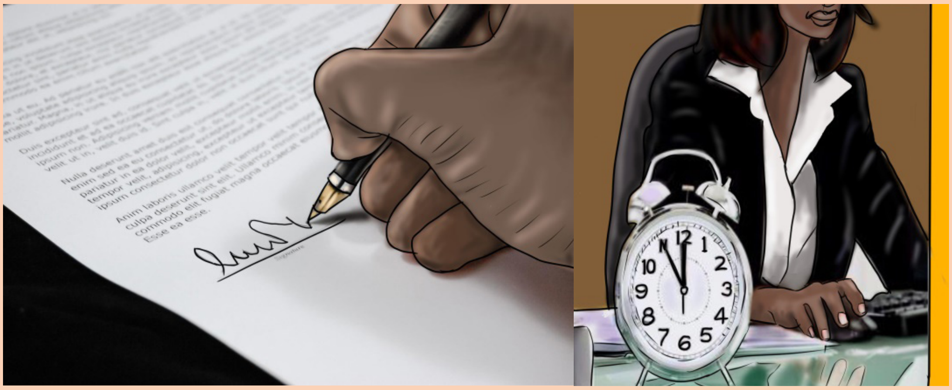
Application activity 7.1

Q1. Explain the different types of an employment contract.

Q.2. Talk about the duration of a probation period

7.2. Valid contract requirements and general working conditions

Activity 7.2



Analyse the Photo above and answer the questions that follow.

Q1. Describe different parties to a valid contract.

Q2. Outline the obligations of employer

7.2.1. Valid contract requirements

a) Parties to a valid contract

Parties of contract are persons who can sign the contract. For a contract to be considered valid, it should include three parties. These are; Offeror who makes an offer, Offeree to whom an offer is made and Witness who sees an event happening.

b) Elements of a valid contract

For a contract to be valid and therefore enforceable by law, it must have the following elements:

- **Intention to be bound by the contract**: the two parties should have intended that their agreement be legal. Domestic agreements between husband and wife are not taken as valid.
- **Offer and acceptance:** there must be an offer and the two parties must lawfully come to acceptance leading to a valid contract. Until an offer is accepted, it's not a valid contract.
- **Consideration/price:** this is the price agreed upon by the parties to the contract and paid by one party for the benefit received or promise of the other parties.
- **Capacity of the parties:** the parties to the contract must have contractual capacity for the contract to be valid, i.e. should be sober, above 18 years, not bankrupt, not insane, and properly registered.
- **Free Consent**: parties to the contract must agree freely without any of the parties being forced to accept or enter the contract.
- **Legality/lawful object:** the object and the consideration of the contract must be legal and not contrary to the law and public policy.
- **Possibility of performance:** if the contract is impossible to be executed in itself either physically or legally, then such contract is not valid and cannot be enforced by law.
- **Certainty:** the terms of the contract must be clear and understandable for a contract to be valid. If the terms are vague or ambiguous, where even the court may not be able to tell what the parties agreed, then it will be declared invalid.

7.2.2. General working conditions

1. Rights and Obligations of employee

a) Rights of an employee

The rights of an employee include the following:

- To work in an environment where health and safety in the workplace are guaranteed;
- To receive equal salary for works of equal value without discrimination of any kind;
- To be provided leave as provided for by Law;
- To join a trade union of his/her choice;
- To be trained by his/her employer;
- To receive information relevant to his/her work.

b) Obligations of an employee

An employee has the following main obligations:

- To personally carry out his/her work or service on time and achieve performance;
- To respect the employer's or his/her representative's instructions;
- To abstain from an act that would threaten his/her security and that of his/her colleagues or that of his/her workplace;
- To keep in good conditions tools given to him/her by the employer;
- To report at work on time;
- To protect the interests of the work.

2. Rights and Obligations of employer

a) Rights of employer

Subject to collective convention, rules of procedure or employment contract, the rights of an employer are the following:

- To recruit an employee;
- To give the employee instructions related to work;
- To evaluate the performance of an employee, promote, transfer, impose disciplinary sanctions and terminate the employment contract of the employee;
- To modify, extend or cease activities.

b) Obligations of an employer

Subject to collective convention, rules of procedure or employment contract, the employer has the following main duties:

- To provide an employee with an employment contract and its copy
- To give the employee the agreed work at the time and place as agreed upon;
- To supervise the employee and ensure that the work is done in suitable working conditions, as far as security and health in the workplace are concerned;
- To pay the employee the agreed salary on time;
- To avoid whatever can hamper the company's life and safety, its employees and the environment
- To affiliate and contribute for an employee to the social security organ in Rwanda;
- To discuss with the employees or their representatives on matters relating to work;
- To provide employees with professional training and continue upgrading their capacity;
- To provide an employee with working equipment;
- To notify the labour inspector work-related accident or death of an employee

3. Disciplinary sanctions

Subject to the favorable provisions of collective conventions, rules of procedure or employment contract and depending on the severity of the misconduct, the disciplinary sanctions that may be imposed on the employee are the following:

- oral warning;
- written reprimand;
- temporary suspension not exceeding eight (8) working days without pay;
- dismissal

4. Working hours

The maximum working hours are forty-five (45) hours a week. However, an employee can work extra hours upon the agreement with his/her employer.

The daily timetable for work hours and break for an employee is determined by the employer. The daily rest granted by the employer to the employee is not counted as work hours.

An Order of the Minister in charge of labour determines modalities for the implementation of working hours a week.

Application activity 7.2

Q1. What are five obligations of each party under employment contract?

Q2. Discuss about Working hours according to the labor law.

7.3. Leaves

Activity 7.3

Analyze the Photos above and answer the following question:talk about types of leave.

7.3.1. Definition of leave

Referring to human resource, leave is simply **taking an off from work day after informing the management formally and sometimes even informally**. Leaves are the days that every working professional is entitled to and paid for, apart from the holidays. Paid leaves are a part of benefits offered by companies apart from medical claim.

What is example of leave?

Leave is defined as permission, or is time off from work. **When you are given permission to attend a party**, this is an example of when you are given leave to attend. When you take two months off work to care for your new baby, this is an example of maternity leave

7.3.2 Types of leaves

a) Annual leave

A public servant is entitled to an annual leave of one month that may be split into three portions maximum. However, a newly recruited public servant is entitled to an annual leave after twelve months including the probationary period.

b) Incidental leave

An immediate supervisor grants incidental leave to a public servant in case of fortunate or unfortunate event that occurs in his/her family as follows:

- Two (2) working days in case of his or her civil marriage;
- Four (4) working days in case of delivery of his wife;
- Seven (7) working days in case of death of his or her spouse;
- Five (5) working days in case of death of his or her child or adoptive child;
- Four (4) working days in case of death of his or her father, mother, father-in law or mother-in-law;
- Four (4) working days in case of death of his or her brother or sister;
- Three (3) working days in case of death of grandfather or grandmother;
- Three (3) working days in case of his or her transfer over a distance of more than thirty (30) kilometers from his or her usual place of work.

A public servant on incidental leave continues to receive his or her salary and fringe benefits.

c) Maternity leave benefits

A female employee who has given birth is entitled to a maternity leave of at least twelve (12) consecutive weeks.

d) Coincidence of leaves

When annual leave coincides with incidental leave or maternity leave, the annual leave is suspended and resumes after the incidental leave or maternity leave.

e) Sick Leave

- Short-term sick leave

An immediate supervisor grants to a public servant a short-term sick leave not exceeding one (1) month for reasons of sickness ascertained by a recognized medical doctor.

- Long-term sick leave

The head of an institution grants to a public servant a long-term sick leave exceeding one 1month but not exceeding six (6) months basing on the decision of a committee of at least three (3) medical doctors, which examines a medical report issued by a medical doctor who treated the public servant, attesting that he or she is unable to work.

f) Authorized absence

For justified reasons, an immediate supervisor may grant to a public servant a written authorized absence from work for one (1) day maximum not deducted from annual leave.

However, the immediate supervisor does not grant an authorized absence for more than ten (10) days per year.

g) Official public holidays

A Presidential Order determines official public holidays.

Examples:

- Jan 01: new year day
- Feb 01: heroes' day
- Apr 07: Genocide against the Tutsi Memorial Day
- May 01: workers day
- Jul 01: Independence Day
- July 04: liberation day
- Dec 25: Christmas day

Application activity 7.3

Q1. State four incidental leaves

Q2. List two official public holidays

7.4. Payroll process

Activity 7.4

Analyze the photos above and answer the following questions:

Q1. What is a payroll?

Q2. State two documents required to produce payroll.

7.4.1. Definition of payroll

Payroll is a list of all employees showing the details of their gross wage, deductions and net wages due to them .it is also known as wage sheet.

In a *company*, payroll is the sum of all *financial* records of *salaries* for an employee, *wages*, bonuses and *deductions*.

In accounting, payroll refers to the amount paid to employees for services they provided during certain period of time. Therefore, for proper accountability, the employer gives the employee an individual monthly pay slip which details the basic salary, other various allowances and bonuses, withholdings and the net salary on employee's request.

7.4.2. Relevant documents required to produce payroll

1. Clock cards: these show the number of hours worked by each employee. One clock card is allocated to each employee for each pay period. IN and OUT times are recorded on clock cards to determine total hours worked including overtime hours so that remuneration payable to each employee can be computed.
2. Piece tickets: these provide information regarding the number of items produced by each worker. They are used for workers who are paid according to the work completed.
3. Employee's personal cards: they provide information regarding wage rates.

7.4.3. Importance of preparing payroll on time

- It helps to pay employees on time
- Reduces conflicts between workers and employers
- It increases employees' motivation

Application activity 7.4

Q1. What are the importance of preparing payroll on time?

7.5. Payroll system and Elements of payroll

Activity 7.5

Case study: In any entity, payroll is very important document for measuring the amount paid to each employee. Besides, it shows the amount to be paid to the different agencies like RSSB, RRA.. Thus, the human resource management unit is supposed to create and control personnel records for the success of organization's operations. The effective management of personnel records enables organizations to manage their employees effectively and efficiently, to initiate informed decision making, to encourage transparency and accountability and to facilitate the monitoring and evaluation of staff performance.

All operations in relation to human resource management, from preparation of pay slips to strategic planning, ultimately depend on reliable and accurate personnel records. The management needs to understand the special characteristics of personnel records, the legal framework for human resource management and the effect of changing technology on the nature and structure of personnel records.

Reference made to the above case study, answer the following questions:

1) Outline any 4 parts included in payroll program
2) State Payroll system

7.5.1. Payroll system

- Manual payroll system means that accounting systems allow you to process all your normal payroll tasks by hand.

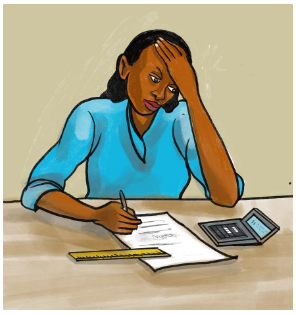


Figure 7.1. Manual Payroll

Advantages of manual payroll system

- Relatively cheaper since you only need to use either the old-fashioned books or use programs like excel.

- Independence from network and electricity
- Doesn't require high knowledge compared to the computerized payroll system

Disadvantages of manual payroll system

- Becomes more difficult as the number of employees grows
- More tedious to prepare
- Does not allow real time reporting and analytics
- Human error can be a major inconvenience since an individual carries out all timesheets, taxes, wages and other processes
- Errors can also be harder to track and might result in various business penalties
- Errors can be also cause employees to be under / over paid

Computerized payroll accounting systems allow you to process all your normal payroll tasks via a computerized system using a software.

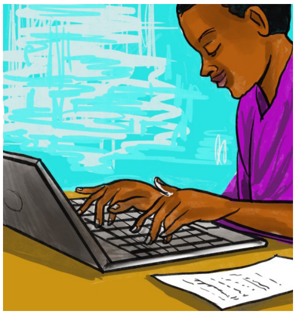


Figure7. 2. Computerized Payroll

Advantages of a computerized payroll system

Avoids most common human errors by implementing a system which requires present data and automatic calculations.

- Payroll computation tends to be more accurate.
- Payroll can be done on a timely basis.
- Number of employees being processed will no longer be a problem.
- It is easier to maintain.
- It is easier to track and correct errors.

Disadvantages of a computerized payroll system

- more expensive compared to manual payroll systems.
- Needs standard computer setup in order to operate it well with certain prerequisites.
- Needs an initial training for those who will maintain the payroll system.

7.5.2. Elements of payroll

a) Serial number

In payroll records there is a serial number which shows the unique number used for identification of employees.

b) Name of employee

In payroll records there are also the names of persons having agreed to work for an employer under a contract concluded between them, and in return for remuneration

c) Account number

An account number is a unique number which show the employee's owner's account.

d) Basic salary

Basic salary is an amount of money paid to an employee for the work performed, which does not include any allowance

e) Allowances

Any monetary benefit offered by the employer to employees so as to facilitate them to perform well. Among allowances we can list for illustration the following examples:

- Transport benefit in Kind: if the employee benefits from use of a motor vehicle provided by the employer during the tax period, add back 10% of the taxable income in FRW, excluding other benefits in kind.
- Housing benefit in Kind: if the employee benefits from accommodation provided by the employer during the tax period, add back 20% of the taxable income in FRW, excluding other benefits in kind.
- Communication allowances. Etc…

f) Gross salary

Gross salary is the amount of money employees receive before any tax deduction or taken out.

g) Deductions

Deductions are money that the employer withholds to contribute to certain agencies like RRA, RSSB, especially from the gross salary. E.g. :

- Pay As You Earn (PAYE)
- RSSB employee contribution

- Contribution to maternity leave
- Etc…

- **Pay As You Earn calculation**

What are the tax rates for 'permanent' employees?

There are different marginal tax rates for permanent employees depending upon their taxable employment income. The groupings of income are called tax brackets. The tax rates for each tax bracket are as follows:

Tax rate

Monthly taxable income in (FRW)		Tax rate
From	To	
0	30 000	0 %
30 001	100, 000	20 %
100,001	And above	30 %

What are the tax rates for 'casual labourers'?

Similarly, there are different marginal tax rates for casual employees depending upon their taxable employment income. The groupings of income are called tax brackets. The tax rates for each tax bracket are as follows:

Tax rate

Monthly taxable income in (FRW)		Tax rate
From	To	
0	30 000	0 %
30 001	And above	15 %

What are the tax rates for 'employees with more than one employer'?

The first employer declares the employee as a 'permanent employee' as normal. Any additional employers must withhold PAYE at the rate of 30% on all taxable income.

Practical example: Dr DUSHIME is a lecturer in University of Rwanda where he is paid a monthly basic salary of FRW600,000, housing allowances of FRW 75,000, transport allowances FRW75,000, responsibility allowances FRW 200,000 as a coordinator of evening program in his faculty.

This one is also a teacher at University of Kigali (UoK) on part time basis and gets the monthly gross salary of FRW 260,000

Required: Calculate the PAYE

Solution: PAYE withheld by UR: Gross salary: FRW 600,000 + FRW 75,000 + FRW 75,000 + FRW 200,000 = FRW 950,000

From FRW 0 to FRW 30,000: 0% = FRW 30,000 x 0% = FRW 0

From FRW30, 001 to FRW 100,000: 20 % = (FRW 100,000 – FRW 30,000) x 20% =FRW14,000

From FRW 100,001 to FRW 950,000: 30 %= (FRW 950,000 –FRW 100,000) x 30% = FRW 255,000

FRW 0 + FRW 14,000 + FRW 255,000 = **FRW 269,000**

PAYE withheld by UoK: FRW 260, 000 x 30% **= FRW 78,000**

- **Rwanda Social Security Board (RSSB) elements**

What are the rates of the pension scheme?

The pension scheme totals a rate of 8%. This is made up of 3% withheld from the employee and 5% paid by the employer including payments to the occupational hazards scheme. This is charged on all employment income except for transport allowances and transport benefits in kind

Therefore, the pension base is equal to:

Pension base = basic salary + benefit in kind house + benefit in kind others + cash allowance house + cash allowance others.

What are the rates of the Maternity leave scheme?

The Maternity Leave scheme totals a rate of 0.6%. This is made up of 0.3% withheld from the employee and 0.3% paid by the employer. This is charged on all employment income except for transport allowances and transport benefits in kind. Therefore, the pension base is equal to:

Pension base = basic salary + benefit in kind house + benefit in kind others + cash allowance house + cash allowance others.

What are the rates of the Medical Scheme?

The Medical Scheme totals a rate of 15%. This is made up of 7.5% withheld from the employee and 7.5% paid by the employer. This is charged on the ‘Basic Salary’.

a) Net salary

The net salary refers to the amount of money employees receive after all deductions?

b) Community-based health insurance (CBHI)

This order has introduced a statutory deduction of 0.5% from every employee's net salary as a contribution to the community-based health insurance scheme. Employers are to remit these contributions to the Rwanda Social Security Board (RSSB) on or before the 15th of the following month.

Application activity 7.5

Q1Amahoro employs Innocent and pays him a basic salary of FRW 57,000 and a cash allowance of FRW 2,000 for transport and FRW 3,000 for airtime related to calls on behalf of the business. Calculate RSSB contributions for pension and maternity leave.

Q2. Discuss about allowances and state 4 examples of allowances?

Q3. Write in full words the following abbreviation used in payroll preparation

a) P.A.Y.E

b) R.S.S.B

7.6. Salary computation and the payment methods of payroll

Activity 7.6

Case study

The major problem is delay of salaries, which is caused by computations that are manually done. These computations are also prone to errors. The whole process is tiresome and takes long. All this can be solved by automating the system. After identifying the problems in the underlying system, an automated computerized system was developed, to curb the loopholes in the manual payroll system. This system is speedy in the calculations of the net salaries and no errors in the salaries. It also stores the payroll information very well. Most computer payroll system keeps track of details like computer payroll numbers, tax identification numbers, district code, department or institution, country, bank code, name of employee, paying code, title of employee, run date, date of payment, gross pay. P.A.Y.E., RSSB contribution, basic pay, salary scale among other things.

After the accounts clerk has deposited the employee's cheques in their banks and given pay slips by the bank, they need to record the payments made in the system for decision making purposes and generation of monthly and annual reports. Analyze the case study above and referring to the last lesson, answer the following questions.

Q1. State RSSB contribution rates you know according to the Rwandan law

Q2. Outline three payment methods

Q3. Explain any five payroll functions.

7.6.1. Salary computation and the payment methods of payroll

1. Salary computation

A. Calculation of gross salary

Gross salary is the amount of money employees receive before any tax deduction.

Gross salary = Basic salary + accommodation allowance + transport allowance + communication allowances+ any other allowance

B. Calculation of deduction

- For PAYE, Rwanda labour law should be enforced by applying Personal Income Tax (PIT) formula with consideration that PAYE is reported on monthly basis while adhering to the three tax bands:

FRW 0-30,000:	0%
FRW 30,001-100,000:	20%
FRW >100,000:	30%

Example: Calculate an annually professional tax of an employee who earns the monthly basic salary of FRW 141,000, housing allowances FRW 19,000, communication allowances of FRW 6,000, transport allowances FRW 12,000

Answer:

Data:

- Monthly income: FRW 141,000
- Housing allowances: FRW 19,000
- Communication allowances: FRW 6,000

- Transport allowance: FRW 12,000
- Gross Salary: 141,000 + 19,000 + 6,000 + 12,000 = FRW178,00
- Annual tax computation:

From	To	Tax rate	
FRW 0	FRW 30,000	0%	FRW 30,000 x 0% = FRW **0**
FRW 30,001	FRW 100,000	20%	(FRW100,000 - FRW 30,000) x 20% = **FRW 14,000**
FRW 100,001	FRW 178,000	30%	(FRW 178,000 - FRW 100,000) x 30% = **FRW 23,400**
PAYE Tax to be pai**d:** FRW **0 +** FRW 14,000 **+** FRW **23,400 = FRW 37,400**			

Annual professional tax: FRW 37,400 x 12 = FRW448,800

- For Rwanda Social Security board (RSSB), the following should be considered:

What are the rates of the Pension Scheme?

The Pension Scheme totals a rate of 8%. This is made up of 3% withheld from the employee and 5% paid by the employer including payments to the occupational hazards scheme. This is charged on all employment income except for transport allowances and transport benefits in kind

Therefore, the Pension Base is equal to:

Pension base = Basic salary + Benefit in kind House + Benefit in kind others + Cash Allowance house + Cash allowance others.

What are the rates of the maternity leave scheme?

The Maternity Leave scheme totals a rate of 0.6%. This is made up of 0.3% withheld from the employee and 0.3% paid by the employer. This is charged on all employment income except for transport allowances and transport benefits in kind. Therefore, the pension base is equal to: Pension base = Basic salary + Benefit in kind House + Benefit in kind others + Cash Allowance house + Cash allowance others

What are the rates of the medical scheme?

The medical scheme totals a rate of 15%. This is made up of 7.5% withheld from the employee and 7.5% paid by the employer. This is charged on the 'Basic salary'.

A. Calculation of net salary

Net salary= Gross salary - Deductions

Format of payroll

Company names:….. Pay period:…………

Company address:…….. Bank names:………

PAYROLL

S/N	Names	Account number	Basic pay	Gross salary	Deductions							Total deductions	Net salary	CBHI	Balance due
					P.A.Y.E	RSSB Pension		RSSB Maternity		RSSB Medical					
						5%	3%	0.3%	0.3%	7.5%	7.5 %			0.5%	

Prepared by:…………….. Verified by:…………..….. Approved by:…………

7.6.2. The payment methods of payroll:

1. Cash payment

Cash payment is a form of liquid funds given by the employer to different institutions entitle to any professional contribution payment like PAYE to RRA and different RSSB contributions through RRA.

2. Mobile money

In this case the employer pays taxes and RSSB contributions using Telephone Mobile Money.

3. Cheque

A cheque is a written order from an account holder (the bank current account holder) addressed to his bank to pay a stated sum of amount to the order of an announced person or its bearer. A cheque is a document of payment in which the holder of an account orders to his bank to pay a certain amount to a payee.

4. Electronic transfer

Include a transfer made between an individual's varies accounts or from one individual account to a corporation account

Application activity 7.6

Q1. Write in full the following abbreviation: a) RSSB

b) PAYE

c) RRA

Q2. Mugisha is entrepreneur. Her small business is located in HUYE District. She employs one employee called Munezero. At the end of every month, she pays him a basic salary of FRW 35,000, a transport allowance of FRW 5,000, and a housing allowance of FRW 8,000. As a student of senior four accounting, calculate:

a) The gross salary paid by Mugisha to Munezero at the end of the month

b) The net salary received by Munezero after paying compulsory deductions (PAYE, Pension, and Maternity leave only).

Q3. Explain a payroll and its details.

Skills Lab 7

After a visit of resource person (accountant of school), students write a note on the following:

- Payroll process
- Preparation of payroll
- Payment methods of payroll prepared

End of unit assessment 7

Q1. Yusufu Kagina is a technician at Fit Metal Industries Limited, receiving a monthly salary of FRW 500,000. He is also allowed a car and an accommodation by the company. How much will be deducted as PAYE from Yusufu's salary?

Q2. MRK ltd company is a small sole trade business of purchasing and selling computers. It is located in Jenda sector, Nyabihu District, Western Province (Tel +250788888888-722222222; P.O Box 1123 Gisenyi).

MRK Ltd company Shop is well known for its services in Society and this attracts clients. Now days MRK Ltd company Shop is facing serious problems related to the use of manual accounting, lack of tool which helps to analyze the challenge of performing an effective payroll system.

Besides all staff being accommodated and transported by the company, the following information has been provide:

S.No	Names	Account Number	Basic salary (FRW)
001	Mahoro	0032	276,000
002	Umuhoza	0123	235,000
003	Kagabo	0309	400,000
004	Karagire	0406	266,000

As a qualified accountant, you are requested to assist the Company to Prepare payroll according to Rwandan law for the month of June 2021. The payment is made through GJ Bank.

UNIT 8 RETIREMENT, OCCUPATION HAZARD BENEFIT AND DISMISSAL COMPENSATION

Key unit competence: Ability to compute retirement, occupation hazard benefits and dismissal compensation

Introductory activity

A Case study

RSSB provides the pension monthly to their retirees, hazard etc. many people around in Rwanda agreed that the Rwanda Social Security Board is operating timely for paying the right amount of pension, proper accountability for the contributions paid by employer for the amount withhold employees. RSSB provides medical insurance to their retirees and family dependency.

There is a high positive and significance relationship between RSSB services and socioeconomic development of retirees in Rwanda

RSSB should implement schemes to rural areas in Rwanda by initiating development projects such as cheaper houses, surveyed plots for sale to the society.

The Government of Rwanda has set objectives of reducing poverty and promoting the welfare of people due to retirement and income decrease as follows: “in line with the vision to make

Rwanda, a country of development and better life for all; considering the importance of protection of social risks as a major component of inclusive social economic development andto improve social protection system and provide adequate protection against the adverse consequences of various life cycle events and risks”.

From the passage above answer the following questions:

Q1. When was the Rwanda Social Security Board (RSSB) established?

Q2. Enumerate the branches currently managed by Rwanda Social Security Board (RSSB).

8.1. Introduction to Rwanda Social Security Board (RSSB)

Activity 8.1

Analyze the photos below and answer the questions that follow.

Question: Observe the picture above then state the main responsibilities of Rwanda Social Security Board (RSSB)

1. Rwanda Social Security Board (RSSB)

Rwanda Social Security Board (RSSB) was established by the law No.45/2010 of 14th/12/2010 that determines its mission, organization and functioning. This institution was established after the merger of Social Security Fund of Rwanda (SSFR) with La Rwandaise d'Assurance Maladies (RAMA). The above Law was modified and completed by the law No 04/2015 of 11th/03/2015 and gave RSSB the responsibility to manage Community Based Health Insurance (CBHI). The mandate of the institution is to administer social security in the country.

The branches currently managed are: pensions, occupational hazard insurance, medical insurance, Community-Based Health Insurance (CBHI) and maternity leave benefits insurance. RSSB as a financial institution is supervised by the National Bank of Rwanda according to the banking law N°55/2007 of 30th/11/2007 whereas its activities are overseen by the Ministry of Finance and Economic Planning.

- Mission of Rwanda Social Security Board (RSSB)

The mission of RSSB is to manage and promote social security in Rwanda

- Vision of Rwanda social security board (RSSB)

RSSB envisions a comprehensive social security system that addresses all social security needs.

2. Rwanda Social Security Board (RSSB) Corporate Values

The Corporate Values of RSSB are:

- Integrity
- Collaboration
- Accountability
- Respect
- Excellent

3. The main responsibilities of RSSB

The main responsibilities of RSSB are:

- To manage and promote pension, medical insurance, occupational hazards insurance; maternity leave insurance, contributions before retirement and other necessary schemes;
- To register employers, employees, beneficiaries and self-insured persons in various schemes managed by RSSB;
- To collect and manage contributions as provided by laws;
- To receive and manage donations;
- To pay benefits for or to beneficiaries;
- To make investments in accordance with laws;
- To contribute to the elaboration of social security policy;
- To advise the Government on matters relating to social security;
- To establish relations and collaborate with other regional or international institutions with similar mission;
- To continue providing medical care for retirees who have monthly pension benefits.

4. The contributions rate of Rwanda Social Security Board (RSSB) branches

The main branches of Rwanda Social Security Board (RSSB) are: pension, occupational hazard, medical insurance and maternity leave.

- The contributions pension and occupational hazards are 8% of the employee's remunerations (employee's gross salary minus transport allowances, retirement benefits and other allowances with refund character),
- Contributions for medical branch are 15% of the employee's basic salary
- Contributions for maternity leave benefits are 0.6% of the employee's remunerations (employee's gross salary minus transport allowances, retirement benefits and other allowances with refund character)

- Contributions for Community-Based Health Insurance in Rwanda are 0.5% of employees net salary.

Except the contributions for occupational hazard and CBHI, all those contributions are paid by both employee and employer as shown in the table below:

	RSSB	Occupational hazard	Contributions
Pension and occupational hazard			
Employee	3%	-	3%
Employer	3%	2%	5%
Total	6%	2%	8%
Medical scheme			
Employee	7.5%	-	7.5%
Employer	7.5%	-	7.5%
Total	15%	-	15%
Maternity leave insurance			
Employee	0.3%	-	0.3%
Employer	0.3%	-	0.3%
Total	0.6%	-	0.6%
Community-Based Health Insurance (CBHI)			
Employee	0.5%	-	0.5%
Employer		-	
Total	0.5%	-	0.5%

Application activity 8.1

Q1. Enumerate Rwanda Social Security Board (RSSB)Corporate Values

Q2. What is the mission of RSSB?

Q3. State the main branches of RSSB

8.2. Pension scheme

Activity 8.2

Case study:

Observe the picture above and answer the following questions.

Q1. Who must register for RSSB Contributions?

Q2. When should people register?

8.2.1. Definition of pension scheme

Pension scheme: pension scheme is a scheme of social security which help workers who become old and incapable of working for a salary or become invalid and incapable of living by working. The scheme helps also the survivors of the deceased worker. The social security benefits offered under pension's scheme are: old age benefits, invalidity benefits, anticipated benefits and survivors' benefits.

8.2.2. Benefits offered in pension scheme

1. **Old age pension- (Eligibility conditions & requirements)**

Eligibility conditions

- To be at least sixty (60) years old or to be of the age provided for by legally recognized specific statutes; example: having attained at least 65 years of age

- To have contributed to the pension scheme for at least fifteen (15) years;
- To have ceased to perform any remuneration activity.

Note:

If the member of the pension scheme reaches the retirement age without having contributed for fifteen (15) years, he/she shall receive a lump-sum retirement allowance.

Requirements for applying for retirement benefits:

- Fill out the application form from RSSB Branch
- Birth certificate issued by the Registry Office
- Life certificate
- Copy of Identification card
- His /Her own Bank account Number opened in Rwanda
- Service testimonial from the last employer for the person who was still in service
- 2 Passport photos

Note:

A person who is outside Rwanda may submit his/her application form duly signed and stamped by Rwandan Embassy or Consulate either electronically or by post. For a person who is unable to go to the office of social security administration due to physical or mental disability; the application form is submitted by his/her representative with a written proxy signed and stamped by the competent authority of his/her residence. For a person who is in a correctional or rehabilitation center, the administration of the center signs and stamp the written proxy of application for pension benefits.

2. **The anticipated/early retirement pension benefits (Eligibility and Requirements)**

Eligibility conditions:

If an insured person becomes prematurely incapable to work and is certified so by a commission composed of recognized medical doctors established by the Minister in charge of health upon request by the employer or employee, he/she is entitled to early retirement.

He/she must also have contributed for at least fifteen (15) years and have ceased to perform any remunerated activity.

Note:

An insured that is eligible for early retirement pension benefits; but who did not contribute 15 years; he/she shall receive a lump-sum pension allowance.

Requirements for applying to early retirement pension benefits (how to apply)

- Fill out the application form at RSSB branch birth certificate issued by the Registry Office
- Life certificate
- Copy of identification card
- Medical certificate of professional inaptitude issued by a legal medical
- Condition certificate of your working capacity issued by the employer
- 2 Passport photos
- His /Her own Bank account number opened in Rwanda

3. Invalidity pension/Non occupational disability benefits (Eligibility & requirements)

Eligibility conditions:

- To have contributed for at least three (3) years;
- To have contributed up to six (6) months within a period of twelve (12) months before the date on which his/her disability is certified by a medical doctor;
- To have ceased to perform any remuneration activity;
- If, upon his/her request or upon the employer's request, the disability is certified by a recognized medical doctor and confirmed by medical officer for the public entity in charge of pension scheme.

Note:

If the disability results from a hazard, the member shall be eligible for disability pension, provided he/she is a member at the time of hazard. Where the insured person is already partially disabled and his/her disability subsequently develops to the point where he/she can no longer perform any remunerated activity, he/she shall be deemed to be disabled.

Requirements

- Fill the application form at RSSB Branch
- Birth certificate issued by the Registry Office
- Life certificate
- Certificate of your working capacity issued by the employer
- Medical certificate of professional inaptitude issued by a doctor approved by the Government
- Bank account number
- 2 passport photos

4. Survivors' pension

Eligibility conditions:

- The surviving spouse who did not divorce the deceased
- The legitimate orphans single, non – employed and under eighteen (18) years of age or twenty-five (25) years of age if still studying. If they suffer from physical or mental disability certified by a recognized medical doctor which renders them unable to perform a remunerated activity shall receive pension benefits until they die
- The deceased's biological or adoptive parent of the deceased.

Requirements

- Fill the application for at RSSB Branch
- Birth certificate of the insured person if the person had not yet received old age pension
- Death certificate issued by an Officer of the Registry Office or by an approved doctor who confirmed the death
- Marriage certificate
- Birth certificates for the deceased's surviving children
- Certificate of guardianship issued by competent tribunal in case of the absence or death of both the parents of the surviving children
- Certificate of legal recognition of natural children
- Certificate of school attendance issued by the Heads of schools for the children who are still at school from age of 18 to 25 years
- Certificate of invalidity issued by medical authority for children who are invalid
- Certificate of bachelorhood or spinsterhood for the insured person who died single
- Life certificates of the beneficiaries and 2 passport photos
- Legal document for adoptive parents
- Copy of identification card of the applicant

Application activity 8.2

Q1. Explain the contributors to RSSB.

Q2. Why does RSSB not provide pension benefits to close relatives (sisters, brothers etc...) in case the contributor dies without leaving any child, spouse or parent

Q3. What are the rates of the pension scheme?

8.3. Retirement benefit calculations

Activity 8.3

Scenario:

In most countries especially in Rwanda, standards of living and healthcare advancements are allowing people to live longer. While this should be celebrated, the implications for the financial systems, designed to meet retirement needs but already in many nations, must be considered. As part of the Rwanda Economic Forum Retirement Investment Systems Reform project of retired person for continuous living without any problem of shortage money for financing their daily expenses with employees who goes the age of retirement.

From the Scenario above answer the following questions:

Q1. Mugisha has just reached age 60, and has contributed for 19 years. His salary has been FRW 100,000 per month for the last 5 years. Find his retirement benefits

8.3.1. Retirement benefit calculations

What are the retirement contributions?

Enrolling for pension benefits is compulsory for the following individuals:

- All employees governed by the Law regulating labour in Rwanda regardless of nationality, type of contract, duration of the contract or the number of wages;
- Employees governed by the General Statutes for public service and civil servants governed by special statutes;

- Political appointees;
- Employees of international organizations, national non-governmental organizations, international non-governmental organizations, faith-based organizations and employees of Embassies accredited to Rwanda.

N.B: Employees working for an enterprise operating in Rwanda but seconded to work for the same enterprise in another country shall remain subjected to pension scheme applicable in Rwanda provided the duration of work does not exceed twelve (12) months.

Employees working for an enterprise operating abroad but seconded to work for the same enterprise in Rwanda remain subject to the pension scheme to which they are affiliated provided the duration of work does not exceed twelve (12) months. And this shall apply subject to international conventions ratified by Rwanda.

The contribution rates are 3% of gross salary of employee minus transport allowances, paid by the employer and 3% by the employee.

Declaration and remittance of contribution to mandatory pension scheme are made on monthly basis; not later than the 15th day of the month following the month to which the contributions relate.

What are the retirement benefits?

Retirement Benefits:

If you have 15 years of service, then your pension will be 30% of your higher average salary in the last 5 years. If you have more than 15 years of service, then you earn an additional 2% for each additional year.

For example:

√ 30% for 15 years

√ 32% for 16 years

√ 34% for 17 years

√ 36% for 18 years, etc.

If you have less than 15 years' service, then you will receive a lump sum settlement.

Pension or lump sum settlement benefits are payable from age 60 (or the pension age fixed by particular statutory arrangements).

Examples:

Retirement Benefits Example (more than 15 years' contributions):

Mugisha has just reached age 60, and has contributed for 19 years. His salary has been FRW 100,000 per month for the last 5 years. His benefits are therefore:

38% x FRW 100,000 = FRW 38, 000 per month pension for the rest of his life

Retirement Benefits Example (less than 15 years' contributions):

Kagabo has just reached age 60, and has contributed towards the pension scheme for a period of 9 years. His monthly salary was FRW 85,000 per month during the last 5 years. His benefits are therefore:

Lump Sum Settlement = FRW 85,000 x 9 = FRW 765,000

There is no pension payable in this case as Kagabo has not contributed for 15 years.

8.3.2. Survivor benefit

What benefits are paid in case of death?

In the event of death, your eligible survivor will be entitled to either a survivor's monthly pension or a survivor's lump sum settlement.

A. Survivor's pension

A survivor's pension is payable when you die in retirement (normal, early or invalidity) and you fulfil the required conditions for receiving a pension.

Who are your eligible survivors?

- The surviving spouse who did not divorce the deceased
- The children who are unmarried, not working for a salary and are either the deceased's legitimate children, legally adopted or those born outside wedlock but recognized as his or hers by law. They must be aged less than 18 years old, or less than 25 years old if still in full time education and without age limit if they are disabled and cannot work for a salary.
- The deceased's own or adopted parents i.e., if he or she left no wife or husband or children.

How is the survivors' pension calculated?

Survivors' pensions are calculated in percentages based on the pension which the deceased was receiving or was eligible to receive at the time of death.

The percentages are:

- 50% of the old age pension for the widow
- 25% for each child (where the other remaining parent is still alive)
- 50% for each child (where both parents are now deceased)
- 25% for each direct or adopted parent when the deceased leaves no wife, husband or children

For example:

If Mugisha had a pension of FRW 38,000 when he died, what will be the survivor's pension be for his wife and son?

- His wife would receive FRW 38,000 x 50% = FRW 19,000 per month
- His son would receive FRW 38,000 x 25% = FRW 9,500 per month
- If Mugisha's wife dies, his son would receive FRW 38,000 x 50% = FRW 19,000 per month
- If Mugisha leaves no wife or children, the direct or adopted parents would receive FRW 38,000 x 25% = FRW 9,500 per month

Please note that the total amount of pension for the survivors cannot exceed 100% of the amount the deceased was entitled to get.

Thus, if Mugisha had a wife and 4 children, the following pension would be payable:

- The wife would have been entitled to 50% pension
- 4 children would have been entitled to 25% x 4 = 100% pension
- Total pension = 50% + 100% = 150% (but this needs to be capped at 100%)
- The revised pension is therefore prorated for the wife, and becomes: FRW 38, 000 x = FRW 12, 666
- The revised pension is therefore prorated for each child, and becomes: 38,000 FRW x = FRW 6, 333

B. Survivor's Lump Sum

This is payable when a pension to the member was not previously payable (as the criteria had not been met – i.e. less than 15 years' service).

How are the survivors' Lump Sum calculated?

The survivor will receive a lump sum equal to the pension to which the beneficiary was entitled if they had completed 15 years of insurance multiplied by the number of 6-month periods they actually completed.

For example:

Rukundo contributed for 4 years (which is 8 complete 6-month periods). If he had contributed for 15 years then he would have received a 30% of salary pension.

Each child will receive half of the widow's lump sum as long as the total for all the children's lump- sum benefits do not exceed the double of the widow's lump-sum.

Lump Sum payment to the wife = 30% x FRW50,000 x 8 (6-month periods) = FRW120,000 Lump sum payment per child = FRW 120,000 x 50% = FRW60,000

Total lump sum payments = FRW 120,000 + (FRW 60,000 x 4) = FRW 360,000

If Rukundo leaves no wife or children, his direct or adopted parent will have a lump sum that is equal to 50% x FRW 120,000 = FRW 60,000 for each parent.

NB: Pension benefit are paid monthly

Application activity 8.3

Q1. Who are eligible for Survivor's pension?

Q2. How is the survivors' pension calculated?

8.4. Occupation hazard computations

Activity 8.4

Case study

In Rwanda, RSSB is facilitates personnel affected by accidents and covers employee health, safety and welfare at the workplaces. Hospitals as the largest group in health care industry in Rwanda, hazards are faced to the employees at the time doing with major hazards categorized as chemical, biological, physical, ergonomic and psychosocial risks. Although Rwanda demonstrates rapid economic growth, amount person saves practically have not been fully enough for financing if an employee is affected by an accident. For this reason, the employer needs to assess risks for health staff, contribute for planning of health services and enhance regulations. Which provides more consistency in decision process and gives an appropriate final rank of hazard types. On conclusion of the hazard control hierarchy, measures are overtaken for the hazards and areas open for improvement are presented so that the employer makes sure that all employees are registered in RSSB in order to fight against the level of inability to meet hospitalization cost.

From the passage above answer the following questions:

Q1. What are occupational hazards?

Q2. What is the contribution of occupational hazards?

Q3. Outline the the benefits for occupational hazards scheme.

8.4.1. Occupational hazards

1. Definition of Occupational hazards

An occupational hazard is a scheme under RSSB which provides assistance to employees and employers in the risk of illnesses or accidents in the workplace. The benefits covered by RSSB under occupational hazard scheme are: medical care, daily sickness allowances, incapacity social security benefits and survivors' benefits.

Meaning that, in case of occupational accident or disease, an employee who has suffered from it while his/her employer has contributed for him/ her in a social security body in Rwanda, he/she is entitled to compensation in accordance with Laws governing social security in Rwanda.

2. What is the contribution of occupational hazards?

A contribution of 2% of salary is paid on behalf of mandatory members by employers. There is no employee contribution towards this benefit.

3. What are the benefits of occupational hazards?

On satisfying the criteria to make a claim, the benefits cover you for:

- Free medical care
- Daily sickness allowances
- Incapacity social security benefits
- Incapacity lump sum benefits
- Survivors' benefits

4. Categories of benefits

- The temporary incapacity benefit is: 75% of average daily earnings in the last 3 months payable until full recovery or certificate of permanent incapacity for a maximum of 180 days.
- The permanent incapacity benefit is: a pension of 85% of average monthly earnings in the last 3 months payable.
- Partial permanent incapacity benefit: is given according to the degree of incapacity in proportion to the pension the beneficiary would get if they had been permanently incapacitated.

– If the degree of the incapacity is at least 15% - the percentage of full pension according to the degree of incapacity.

– If the degree of the incapacity is less than 15% - then a lump sum payment equal to 3 years' pension according to the degree of incapacity is awarded to the beneficiary.

5. How are survivors' allowances calculated?

The survivor's allowances are fixed percentages of salary, as follows:

– 30% for the widow or widower

– 15% for each child of the father or mother (with the other remaining parent surviving)

– 20% for each child of father and mother (with both parents deceased)

– 10% for each direct or adopted parent. An accident befalling a worker at the occasion of a crime or an offence committed by the worker or an intentional fault on his or her part is not covered by RSSB.

6. How do I make a claim?

- Inform your employer and area labour inspector directly, as soon as possible.
- Give precisions relating to circumstances i.e., place of accident, eye witnesses, third party responsible for the accident. As soon as all information is received, the employer will fill the accident declaration (A1) in 6 copies.

- The doctor should fill in the medical certificate of the first-hand state of the injury sustained (A2).
- Ask the doctor to give RSSB a medical certificate of the prolongation of incapacity of injuries every 30 days. This prolongation must not exceed 150 days.
- You must equally inform your employer to give the RSSB a receipt of payment/non-payment.
- At the end of the treatment, ask your doctor to fill the certificate of healing and consolidation of injuries (A5).
- Keep careful the bills for medical treatment or food given by the hospital.

Application activity 8.4

Q1. Discuss about how survivors' allowance for occupation hazard are calculated

Q2. Outline the categories of benefits according to the occupation hazard

8.5. Dismissal compensation (terminal benefits)

Activity 8.5

Scenario

KARERA Company ltd is a company registered with RDB. 10 years ago, it hired employee following employment law. During this week, KARERA Company ltd has gone bankrupted for technical reason.

Employer has decided to cancel all employment contracts.

From the Scenario above answer the following questions:

Q1. What is terminal benefits?

5. Terms used

- Terminal benefits

Terminal benefits can be expressed as benefit given to an employee upon the ending of the employment relationship as a result of economic reasons, technological transfer or sickness

- Definition of dismissal

Dismissal is a process where an employee's employment contract is terminated after an employer expels him from work. In short, the employee's services will no longer be required by the employer. This can be due to a number of reasons such as theft, incompetence, decline in business, incapacitation of the employee due to medical ground, etc.

6. Why dismissed employees should receive their terminal benefits

Under Law n° 66/2018 of 30/08/2018 regulating labour in Rwanda, chapter II: employment contract, apprenticeship and internship contracts, Section 2: Termination of employment contract and dismissal of employee, article 31 it is provided that any employee is entitle of terminal benefits for termination of employment contract as a result of economic reasons, technological transfer or sickness.

Without prejudice to other provisions of this Law, the termination of employment contract due to economic reasons, technological transfer or sickness for an employee having served for at least twelve (12) consecutive months entails the employee's right to terminal benefits.

7. Terminal benefits for termination of employment contract as a result of economic reasons, technological transfer or sickness

Apart from clauses of the collective agreement or individual employment contract more favorable to the employee, terminal benefit can in no way be less than:

- Two (2) times the average monthly salary for the employee having less than five (5) years of service with the same enterprise;
- Three (3) times the average monthly salary for the employee having between five (5) and ten (10) years of service with the same enterprise;
- Four (4) times the average monthly salary for the employee having between ten (10) and fifteen (15) years of service with the same enterprise;
- Five (5) times the average monthly salary for the employee having between fifteen (15) and twenty (20) years of service with the same enterprise;

- Six (6) times the average monthly salary for the employee having between twenty (20) and twenty-five (25) years of service with the same enterprise;
- Seven (7) times the average monthly salary for the employee having over twenty-five (25) years of service with the same enterprise.

The average monthly salary is obtained by dividing by twelve (12) the total salary the employee has received for the last twelve (12) months exclusive of allowances allocated to the employee to enable him/her to perform his/her duties.

The terminal benefits must be paid within seven (7) working days of the dismissal of the employee.

The terminal benefits provided for under this Article are also allocated to an employee whose employment contract is terminated after six (6) months due to sickness in case he/she is unable to resume a work.

Illustration:

Q1. Mahoro is an employee in KEZA Maize Ltd company since year 2000 with an annual average salary of FRW 5,400,000. In 2022, he has received a dismissal notice due to the economic issues of the company.

Required: Calculate Mahoro's dismissal compensation.

Answer

Number of years= (Ending time - Starting Time) + 1

From 2000 to 2022: **23 years**

From 0 to 5: 2 times monthly salary

From 5 to 10: 3 times monthly salary

From 10 to 15: 4 times monthly salary

From 15 to 20: 5 times monthly salary

From 20 to 25: 6 times monthly salary

Monthly average salary: = FRW 450,000

Dismissal compensation: FRW 450,000 x 6 = FRW 2,700,000

Application activity 8.5

Q1. Kagiraneza is an employee in MUSANZE cement LTD company from year 2004 with an annual average salary of FRW 6,600,000. For the year 2022, he has received a dismissal notice due to the economic issues of the company.

Required: Calculate the Kagiraneza's dismissal compensation.

Q2. How do you determine the terminal benefits for termination of employment contract as a result of economic reasons, technological transfer or sickness given the employee office tenure?

Skills Lab 8

Via internet search or visit of resource person from RSSB, students write a note on the following:

- Retirement of employees
- Occupation hazard profits of employees
- Dismissal compensation benefits for employees according to Rwanda Labor Law

End of unit assessment 8

Q1. Fabien Fashaho has been employed by the company for 32 years. He has respectively attained 68 years and wishes to retire ended 2019 from employment.

Five years preceding the admissibility to the pension he received the following salaries:

- 5th year (2015): FRW 480,000
- 4th year (2016): FRW 540,000
- 3th year (2017): FRW 600,000
- 2nd year (2018): FRW 660,000
- 1st year (2019): FRW 720,000

Advise him on the benefits and amounts he is entitled to.

Q2. Amahoro employs Innocent and pays him a basic salary of FRW 57,000 and a cash allowance of FRW 2,000 for transport and FRW 3,000 for airtime related to calls on behalf of the business.

Required: Find the contribution of RSSB Pension for Innocent

Q3. What are RSSB contributions?

Q4. Who collects RSSB contributions?

Q5. After the work accident, AMANI, ALICE, and MUGISHA were seriously hurt. AMANI was hospitalized during 30 days. ALICE's incapacity was total and that of MUGISHA, less than his colleague was evaluated to 20%. Each of them received the following monthly wages during the three (3) months preceding their accident:

July: FRW 340,000; August: FRW 230,000; September: FRW 450,000.

Required: Show the amounts each of them is entitled to.

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