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TO: ALL CABINET SECRETARIES

ALL ACCOUNTING OFFICERS/PRINCIPAL SECRETARIES

ALL COUNTY GOVERNORS

ALL CHIEF EXECUTIVE OFFICERS OF STATE CORPORATIONS

**GUIDELINES FOR PAYMENT OF WITHHOLDING INCOME TAX ON
PAYMENTS MADE TO CONTRACTORS OR OTHER PERSONS ENGAGED IN
THE IMPLEMENTATION OF OFFICIAL AID FUNDED PROJECTS**

I. PURPOSE

1. These Guidelines set out the procedures to be followed by Ministries, Departments and Agencies (MDAs), and County Governments in processing payments and effecting deduction of withholding income tax relating to such payments for work done in respect of the implementation of Official Aid Funded Projects (OAFPs).

II. INTERPRETATION

2. In these Guidelines, unless the context otherwise requires,

“**Concessional loan**” has the same meaning assigned to it under the tax laws.

“**Official aid funded projects**” are projects which are funded through grants and/or concessional loans as specified in financing agreements signed between

Development Partners and the Cabinet Secretary responsible for finance on behalf of the Government of the Republic of Kenya.

“Withholding income tax” is a tax on income deducted at the point of making payment for the services provided or work done.

“Withholding income tax agent” is a resident receiving a service in the implementation of an official aid funded project.

“Resident” has the same meaning assigned to it under the Income Tax Act.

III. BACKGROUND

3. OAFPs are exempt from indirect taxes such as value added tax, import duty, fees and levies imposed by the Government. However, unless exempt under the Income Tax Act and expressly provided for in the financing agreements, income earned by contractors or other persons engaged in the execution of the projects is subject to tax.

4. The Income Tax Act require that withholding income tax be deducted at the appropriate resident or non-resident rate, as the case may be, on any payments made to contractors or other persons engaged in the implementation of OAFPs. In this regard, the implementing MDAs and County Governments are withholding income tax Agents. Development Partners, by virtue of being non-residents, are not withholding income tax Agents under the said Acts.

5. It has been established that MDAs/County Governments, who are the withholding income tax Agents for the Projects, have been facing challenges in withholding income tax on direct payments made by Development Partners to Contractors or other persons engaged in the implementation of the Projects.

6. In order to address these challenges and ensure compliance with the provisions of the Income Tax Act relating to withholding income tax on payments to the contractors or other persons engaged in the implementation of the projects, the following guidelines shall strictly be followed.

IV. THE GUIDELINES

7. Any request for payment by a contractor or other persons involved in the implementation of the Projects shall be submitted to the implementing MDAs/ County Governments, and shall be accompanied by the following documents:

- a) Payment Certificate and Invoice for the work done;
- b) Fee Note and Invoice for consultancy services, if any;
- c) Valid Tax Compliance Certificate;

- d) Proof of payment of withholding income tax on the payment being requested, where applicable;
- e) A letter from the National Treasury and Planning confirming the exemption, if exempt from income tax.

The MDAs/County Governments shall not process any payment request unless the request is accompanied by documents referred to in (a) – ((d) or (e)) above.

8. Upon receipt of the request, under Paragraph 7, the MDAs/County Governments shall verify and confirm that the work has been done. Where the work has been done, the MDAs/County Government shall process the payments to Contractors or other persons engaged in the implementation of the Projects in accordance with the terms and conditions of Contract Agreement and Loan or Grant Agreements.

9. After the processing of the payments, the MDAs/County Governments shall, where:-

- (a) funds are disbursed by Development Partners to the National Government or County Governments for the implementation of the Official Aid Funded Projects, make payments to the Contractor or other persons engaged in the implementation of the Projects. At the point of making such payments, the MDAs/County Governments shall deduct the applicable withholding income tax due from such persons in respect of the payments and remit the same to the Kenya Revenue Authority (KRA).
- (b) Development Partners make payments in respect of the contract sum directly to contractors or other persons involved in the implementation of OAFPs, submit the processed payment request to the National Treasury and Planning for further processing. The request shall be accompanied by proof of exemption or payment of withholding income tax relating to the Payment Certificate/Fee Note for which payment is being requested.

10. Withholding income tax rates shall apply as follows: -

Residents

- (a) Individuals or Companies incorporated in Kenya and Foreign Companies with Branches or Permanent Establishments in Kenya:
 - i) 3% withholding income tax on contractual fees;
 - ii) 5% withholding income tax on management or professional fees other than contractual fees.

Non-Residents

(b) Individuals and Foreign Companies without Branches/Permanent Establishment in Kenya:

- i) 20% withholding income tax on payments made on contractual, professional or management fee, where there is no Double Taxation Agreement (DTA);
- ii) the rate specified in the DTA on payments made for the contractual, management or professional fee, where there is a DTA.

11. Despite the rates specified in paragraph 10, the applicable resident and non-resident withholding income tax rates shall be as provided under the Income Tax Act.

12. In cases where MDAs and County Governments make OAFPs related payments, they shall furnish the contractors or other persons engaged in the implementation of the projects with a certificate of income tax deduction showing the gross amount paid and the total tax deducted, where applicable.

13. The MDAs/County Governments shall remit to the KRA all the amounts of withholding income tax deducted in accordance with the Income Tax Act, the Tax Procedures Act and the Income Tax (Withholding Income Tax) Rules.

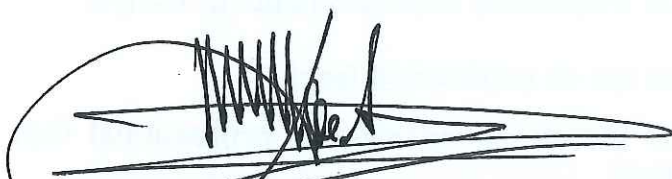
14. These Guidelines shall, where applicable, apply to other projects implemented by the MDAs/County Governments.

V. MAINTENANCE OF RECORDS

15. The Accounting Officer of the respective MDAs/County Governments implementing OAFPs shall maintain records showing payment of withholding income tax in respect of payments made to the contractors or other persons engaged in the implementation of the projects. The records shall be availed to KRA for audit upon request.

VI. CONCLUSION

16. All Cabinet Secretaries, Accounting Officers and County Governors are required to ensure strict adherence to these guidelines and to bring the contents of this Circular to the attention of all officers working under them, including the Heads of Parastatals and Semi-Autonomous Government Agencies (SAGAs).



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AG. CABINET SECRETARY/THE NATIONAL TREASURY AND PLANNING