UNIT 4:

TAXATION OF EMOLUMENTS

4.1 CHARGE OF TAX ON EMOLUMENTS

The provisions of the Income Tax Act under which tax is charged on emoluments are:

- Section 2 - definition of emoluments;
- Section 5 - receipt of income;
- Section 14 - charge of tax; and
- Section 17 - classification of income; and
- Section 71 - collection and payment of tax from emoluments

Section 14 of the Income Tax Act charges tax on income received by a person and income as classified in section 17 includes "emoluments," which are considered further below.

Receipt of income is defined in section 5 of the Income Tax Act. According to section 5, income is received by a person:

> "…when, in money or money's worth, or in the form of any advantage, whether or not that advantage is capable of being turned into money or money's worth, it is paid to him, or it accrues to him or in his favour, or it is in any way due to him or held to his order or on his behalf, or it is in any way disposed of according to his order or in his favour, and the word "recipient" is construed accordingly."

Section 71 of the Income Tax Act provides for a pay as you earn (P.A.Y.E.) mechanism for the collection and payment of taxes from emoluments; which is considered further below.

4.2 MEANING OF EMOLUMENTS

"Emoluments" are defined, in section 2 of the Income Tax Act as meaning-

> "any salary, wage, overtime or leave pay, commission, fee, bonus, gratuity, benefit, advantage (whether or not that advantage is capable of being turned into money or money's worth), allowance, including inducement allowance, pension or annuity, paid, given, or granted <u>in respect of any employment or office</u>, wherever engaged in or held".

By this definition, therefore, tax is charged on "emoluments received in respect of office or employment". Let us first look at the terms 'Office and Employment'. What do they mean? Well as neither of these terms have been defined in the Income Tax Act, we will have to look elsewhere to find out the meaning of these terms.

Meaning of Employment

An employment is regarded as existing where there is a legal relationship of master and servant. An employee will be under a "contract of service" whether written, verbal or implied. It is

important, at the outset to distinguish between an employee and an independent contractor, a contract of service and a contract for service.

An employee would be liable to pay tax under PAYE scheme in respect of his emoluments whereas an independent contractor would be liable to tax on his income in respect of profits arising from the trade or profession he carries on.

Some of the factors considered in distinguishing an employee from an independent contractor include the following:

(a) *Provision of work and skill* – there will be a contract of service where an employer is obliged to provide work and the worker is obliged to perform the work allocate to him.

(b) *Control* - there will be a contract of service where the employer has the right to direct the manner and the method of doing the work. There would be however, a contract for services where one of the parties agrees to have a desired effect produced.

(c) *Substitution* – there will be a contract of service where the worker is required to perform the services themself, without being allowed to provide a substitute. Having a substitution clause in a contract and actually supplying a replacement helps prove that the worker is actually an independent contractor.

(d) *Enterprise test* – this considers whether the worker is in business on their own account (in which case they would be an independent contractor) or if they are part and parcel of the employer's business (in which case they would be an employee). The test was outlined in the case of *Market Investigations Ltd v Minister of Social Security*,[1] where according to Cooke J;

> "The fundamental test to be applied is this: Is the person who has engaged himself to perform these services, performing them as a person in business on his own account? If the answer is yes, then the contract is a contract for service, if the answer is no, then the contract is a contract of service."

In the case of *Davies (Inspector of Taxes) v Braithwaite,*[2] Miss Braithwaite was an actress who was engaged under various separate contracts to perform in stage plays, films and on radio. Miss Braithwaite claimed that the various contracts between her and theatrical producers were contracts of service. The Revenue contended that she was exercising her profession as an actress and was therefore correctly assessed under Case II of Schedule D. It was held that Miss Braithwaite was exercising a profession and the profits were chargeable under Case II of Schedule D. Rowlatt J considered that employments were something like 'offices' and likened them to 'posts'. He states that:

> "Where one finds a method of earning a livelihood which does not contemplate the obtaining of a post and staying in it but essentially contemplates a series of engagements and moving from one to the other that each of those engagements could not be considered an employment but a mere engagement in course of a profession".

[1] 1968 QBD 173
[2] 18 TC 198

(e) *Financial risk*: there will be a contract of service where a worker takes no financial risk relating to the performance of their services. In most cases, employees will not be responsible for any operating costs, and they are not financially liable if they do not fulfil the obligations of their contract. If the worker takes any financial risk this could be an indicator that he is an independent contractor.

In case of *Ready Mixed Concrete (SE) Ltd v Minister of Pensions and National Insurance*[3], RMC Ltd was in the business of making and selling ready mixed concrete. The company decided to introduce a scheme whereby concrete was delivered by owner-drivers working under written contracts. Under this scheme a driver, Mr Latimer, contracted with RMC for the delivery of concrete. The contract declared him an "independent contractor" and set out wages and expenses. The driver was to purchase his own vehicle, yet with a requirement that the vehicle be painted in company colours. He was to drive the vehicle himself but under compliance with certain company's rules including, for example, the manner of vehicle repairs and payments. The question arose as to whether the driver was an "employed person" under a contract of service with RMC for the purposes of the National Insurance Act 1965.

Firstly, the Court held that whether a contract creates a 'master and servant' relationship between an employer and employee is determined on the basis of contractual rights and duties, and that the nomenclature used in the contract is irrelevant. Thus, the fact that the contract termed the driver to be an "independent contractor" is not material. Secondly, the Court held that employment under a contract of service exists when:

(a) a person agrees to a perform a service for a company in exchange for remuneration; and

(b) a person agrees, expressly or impliedly, to subject himself to the control of the company to a sufficient degree to render the company his "master," including control over the task's performance, means, time; and

(c) the contractual provisions are consistent with ordinary contracts of service.

On the facts, the Court held that the driver had sufficient freedom in the performance of his contractual obligations as he was free to decide the vehicle, his own labour, fuel, and other requirements in the performance of the task. In lieu of these freedoms, he was an independent contractor and not an employee of the company.

In the normal way, it is not very difficult to establish whether an individual is (say) an electrician in employment or an electrical contractor on his own account but in the field of professions it is often very difficult to determine whether a person is carrying on a profession or holding an employment. This is because the circumstances, which might determine the point, may be complex and may change frequently. For example, a doctor may have his own private practice and also have a part-time appointment at the University Teaching Hospital as a consultant. Similarly, a musician may have engagement with Zambia National Broadcasting Corporation, be an instrumentalist in a band, give musical instructions to private pupils and teach music at the local school. No hard and fast rule can be laid down in this respect, however, the distinction between a profession or vocation on the one hand and an employment on the other is largely the same as that between a contract for services, which is an incidence in carrying on of a profession or vocation, and a contract of service involving the relationship of master and servant (see Halsbury's Laws 3rd edition, volume 25 pages 447-449).

[3][1968] 2 QB 497

In most cases the distinction does not cause any difficulty, however, one thing is clear, if a person holds an office of an employment, the tax on emoluments from that office, or employment must be collected under PAYE as for example will be the position in respect of a musician's engagement with Zambia National Broadcasting Corporation and the schools where he teaches music as an employee; tax on any income he receives for services rendered otherwise than in the performance of the duties of that office may or may not be collectible under that scheme.

Similarly, an accountant who prepares the accounts of a limited company may be a full-time employee of the company or he may carry on a profession; if the former applies, the tax on his remuneration is collectible under PAYE and, if the latter applies, his remuneration is a receipt of his profession the profits of which are chargeable under section 17(a). If he is also a Director of the company his remuneration in connection with the preparation of accounts is taxed as profits of a profession and any emoluments he receives as a Director, such as Director's fee are chargeable under section 17(b) and the tax collectible under the P.A.Y.E. scheme.

It should be noted further that the terms 'employer' and 'employee' are defined in section 2 as, "an employer in relation of any employee means any person or any partnership which pays, gives or grants any emoluments to the employee" and an employee in relation to any employer as, "an individual who is paid, given or granted an emolument by that employer".

Meaning of Office

The shorter Oxford Dictionary gives the meaning of 'office' as, *"A position to which certain duties are attached, especially a place of trust, authority of service under constituted authority".*

The term has been judicially defined as "a permanent substantive position that exists independent of the person who fills it, and which goes on and on and is filled in succession by successive holders" (Per Rowlatt J in *Great Western Railway Co. v Bater* [1920] 3 KB 266). Examples of office holders are Ministers of the Government of the Republic of Zambia, Town Clerks and similar officers of Local Authorities, most Ministers of Religious denominations and directors of limited companies. It is the judicial definition of office that will be followed in interpreting tax laws.

Does the income arise from the office or employment?

Case reading: *Mr. Justice M.M.S.W. Ngulube v Zambia Revenue Authority* 2003/RAT/29

> This case considered, *inter alia*, whether payments made to a Chief Justice of Zambia in the UK from government funds were payments made in connection with his office as Chief Justice.

In the English case of *Cooper v Blakiston*,[4] the following dictum by the Lord Chancellor was given:

> "where a sum of money is given to an incumbent substantially in respect of his services as incumbent, it accrues to him by reason of his office. Had it been a gift of an exceptional kind such as a testimonial or a contribution for a specific purpose as to provide a holiday or a subscription peculiarly due to the personal qualities of the particular clergyman, it might not have been a voluntary payment for services, but a mere present."

[4] 5 TC 347

The first part of this dictum sets out the rules that where a sum of money is received by a person in respect of services performed by him by virtue of holding an office that sum is liable to tax in his hands. The payment stems from that office.

The second part of the dictum states that if a person received a gift of an exceptional kind in appreciation of his personal qualities then such a gift would be considered as a "present"' and not as a payment even though voluntary, for service performed. It was, therefore, not liable to tax in his hands.

It is very important to understand this distinction at the very outset since it forms the basis of taxability of sums, advantage and benefits etc. – section 17(b).

The above case was concerned with the question "whether voluntary subscriptions made by a congregation to a clergyman were assessable". The Easter offerings were received by a vicar in the normal way collection made at services in the church of England do not go to the vicar who receive his stipend from other sources. In this instance, following long standing practice, the Church wardens gave the collections made on Easter Sunday to the Vicar for his personal use as a free will offering. The question was decided by the House of Lords, and the Easter Offerings were held to be assessable in the hands of the Vicar.

Similarly in the case of *Herbert v McQuade,*[5]a grant made by a Clergy Sustentation Fund to a Clergyman to augment the income of his benefices was held to be assessable because it accrues to him by reason of the office which he holds.

However, in the case of *Turner v Cuxson*,[6] a sum of money received by a curate from a religious society in recognition of his faithful service as a Clergyman was not assessed. It was held that the payment was not in respect of any particular curacy and could not therefore, be an emolument of his office as curate. (Curate - a priest or deacon who assists a Rector or Vicar; curacy – the office of a curate).

To recall, the principles established so far can be summarized as follows:

(a) The fact that there is no local obligation on the payer to pay money is irrelevant in considering whether it is assessable under section 17(b);

(b) "A profit accrues by reason of an office when it comes to the holder of an office as such in that capacity and without the fulfilment of any further or other condition on his part".

(*Herbert v McQuade 4 TC 501*).

Gifts of Exceptional Kind

The dictum of the Lord Chancellor in *Cooper v Blakiston* stated that gifts of exceptional kind cannot be considered as payments made in connection with an office held. It would therefore be necessary to consider what constitutes "gifts of exceptional kind."

[5] 4 TC 489
[6] 2 TC 422

The case of *Cowan v. Seymour*[7] concerned a secretary of a company who received no remuneration for his services. The Company was then wound up and he was appointed as a liquidator. The shareholders, at the final meeting of the company asked him to accept a sum of money which would normally have been distributed to them. This was taxed in his hands and Commissioners agreed that the sum was correctly assessed.

When the case came up before the court, it was admitted that the facts were not conclusive of the point though, the Court placed a great weight on the fact that the office of Secretary had ended sometime before, and that the money was given by the shareholders and not by the natural paymaster – the company. These facts indicated that it was a gift of an exceptional kind such as a testimonial personal in character. *"The personality of the appellant was everything".* The Court, therefore reversed the Commissioner's decision that the sum was assessable.

To some extent, however, the decision turned on the words "accruing by reason of the office" - Young L.J. said that the office may have been a "causa sine qua non" but it was not a "causa causans".

It should be noted that the words "by reason of the office" do not appear in the definition of emoluments in our Income Tax Act, but the distinction expressed by the dictum is very valid and should be examined critically. It must also be remembered that the considerations applicable to "employment", as distinct from an "office", are always not the same.

The case of *Mudd v Collins*[8] on the other hand involved an employee of a company who negotiated the sale of a branch for which he received special payment from his employers. He was assessed on the sum so received, and he unsuccessfully claimed that the sum did not arise by virtue of his office. The court stated that:

> "If an officer is willing to do something outside the duties of his office and his employer gives him something in that respect, that is a profit it becomes a profit of his office which is enlarged a little so as to receive it"

Receipts not assessable - Case I

Reed v. Seymour 11 TC 625

In this case the committee of a Cricket club exercising their absolute discretion, granted a benefit match to a professional cricketer in their service. The proceeds of the match, together with certain public subscription, were invested in the name of the trustees of the Club the income therefrom paid to the beneficiary in accordance with the rules of the Club. Subsequently the investments were realized, and the proceeds were paid over to the beneficiary; who with that sum purchased a farm with the approval of the trustees.

He was assessed on the proceeds of the benefit match (public subscription were excluded), and the assessment was discharged by the General Commissioner. It was held that the award of proceeds of the benefit match to the cricketer was not a profit accruing to him in respect of his office or employment but was the nature of personal gifts and not assessable to Income Tax".

Receipts assessable - Case 2.

[7] 7 TC 372
[8] 9 TC 297.

Davis v Harrison 11 TC 707.

In this case the benefit money paid to a professional footballer by his old club after he had been transferred to another club was held to be assessable remuneration and not as contended compensation for loss of office. The rules of the Football League (in England) allowed a club to agree to pay a player a money-benefit after five or ten years and if he was transferred before the end of the period to pay him a percentage of the promised benefit as a reward for services.

4.3 PAY-AS-YOU-EARN

Under the Income Tax Act, tax in respect of emoluments is collected by means of arrangements generally referred to as the Pay-As-You-Earn (P.A.Y.E.). Under this system, when an employer pays any remuneration he is responsible for deducting tax by reference to tax tables and to a code number supplied to him in respect of each employee by the Commissioner General.

The P.A.Y.E. mechanism is provided for under Part IV of the Income Tax Act and is administered in accordance with the Income Tax (Pay-As-You-Earn) Regulations, 2014 (the "P.A.Y.E. Regulations").

Scope of P.A.Y.E.

The P.A.Y.E. system of deducting tax from salaries and wages applies to all offices and employments. Tax under P.A.Y.E. is to be deducted not only from monthly and weekly payments, but also from daily, annual or other irregular payments – see Reg. 6 and 7 of the P.A.Y.E Regulations. P.A.Y.E. applies to full time employees as well as casual employees (see Reg. 5). Tax is to be deducted from all emoluments paid to an employee (Reg. 4(2)).

Employer's Duty to Deduct Tax

Under section 71 of the Income Tax Act, it is the duty of the employers to deduct tax from payments of emoluments to their employees, whether or not they have been directed to do so by ZRA. All employers are under an obligation to operate P.A.Y.E. Section 71 reads:

> "On the making of any payment of, or on account of, any emolument, tax shall, subject to and in accordance with regulations made by the Minister, be deducted or repaid by the person or partnership making the payment, notwithstanding that when the payment is made no assessment has been made in respect of the emoluments, and notwithstanding that the emoluments are in whole or in part emoluments for some charge year other than the year during which the payment is made, and, for the purposes of this subsection, payment shall be deemed to be made when the emolument is received as provided in section five: or to income, for an individual, on which turnover tax has been assessed in accordance with subsection (2) of section sixty-four A " after the words " non-money fringe benefits,
>
> Provided that with reference to paragraph (1) of section forty-four the requirements of this subsection shall not apply to emoluments provided to employees in the form of non-money fringe benefits."

Under the P.A.Y.E. system therefore, the employer is empowered to:

(a) calculate tax payable by every employee;

(b) deduct tax due from the emoluments, and

(c) remit tax deducted to ZRA.

The employer is wholly liable for the payment of any tax not deducted or under deducted and penalties are chargeable under the Income Tax Act on any employer who fails to comply with the P.A.Y.E. Regulations.

The undoubted importance of P.A.Y.E. in our scheme of taxation must not be allowed to obscure the fact that it is merely a method of collecting tax. Although in most cases the total net tax deducted during the year corresponds closely with the tax chargeable, the amount of an individual's liability depends not on the tax to be deducted under P.A.Y.E. but on the provisions of the Income Tax Act which define the scope and measure of liability from these sources.

4.4 CHARGEABLE EMOLUMENTS

An employer is required to calculate tax deductible from an employee's pay by reference to "chargeable emoluments." It is therefore important to know what the term "chargeable emoluments" means.

Chargeable emoluments for P.A.Y.E. purposes mean "emoluments from an employee's employment that are chargeable to income tax but *does not include any allowable pension contribution or any amount which is exempt from income tax*" (Regulation 2 of the P.A.Y.E. Regulations).

Chargeable emoluments therefore include salaries, wages, overtime or leave pay, commission, fee, bonus, gratuity, any benefit, advantage or allowance (excluding non-money fringe benefits), and payments on taking up or leaving employment. (Section 2, Income Tax Act). In addition, all employee's liabilities borne by the employer and all other payments made by the employer to the employee in respect of that employment form part of his chargeable emoluments.

Benefits

The definition of emoluments under section 2 of the Income Tax Act includes benefits, which may be either in monetary form (cash benefits) or in kind.

Cash benefits

Cash benefits paid in the form of allowances are taxable on the employee under P.A.Y.E. Examples of cash benefits are:

- Education allowance
- Housing allowance
- Transport or fuel allowance
- Domestic utility allowance
- Commuted car allowance
- Settling allowance

Benefits in kind

A benefit in kind generally means a benefit of some sort which is not money. If, for example, an employer gives an employee his salary in the form of saving certificates, he is paying him his salary just as much as if he gives him a cheque for that amount. Both can be cashed; the only difference is that the saving certificates are not negotiable, i.e., they are not money. The difficulty arises however, where the reward is of an intangible nature.

The question whether a benefit in kind is assessable, on the employee was considered in the case of *Tennant v Smith*[9]. In this case, a bank manager, was required as part of his duty to reside in the "bank house adjoining the bank. He lived there rent free; he had no power to sublet and when he retired or moved to another branch of the bank, he would be required to vacate the premises. It was held that the benefit of the house did not constitute an emolument since it was not convertible into money. The House of Lords indicated as a general principle that *"benefits received in kind" was a profit if it represented "money's worth" and where a person receives substantial things of money value capable of being turned into money, they represented money's worth"*. It must be observed in passing that "substantial" in this context does not mean large; the term is used as an antonym to insubstantial. The right to live in a house is not a "substantial thing" *nor in this case was it capable of being converted into money*.

It must be noted that the test applied in *Tennant v Smith* was whether the benefit *could* be lawfully converted into money; it is irrelevant whether the employee actually converts it into money.

The law as decided in *Tennant v Smith* therefore is that *benefits in kind are only taxable if they are of money value capable of being converted into money*.

Value of convertible benefits

If a benefit in kind is convertible into money, tax is levied on the value of the benefit to the employee: this is taken to be the second-hand value. In the case of *Wilkins v Rogerson*,[10] a company arranged with a firm of tailors that each employee would be entitled to obtain clothes of up to £15 in value. Under this arrangement *Rogerson*, an employee of the company, ordered a suit costing £14.5 which his employer paid for directly to the tailors. It was held that Rogerson had received a benefit in kind that was convertible into money because he could sell the suit, but that he could only be taxed on the second-hand value, estimated at £5. As Herman L.J. said at page 353 -

> "The only controversy was whether he was to pay tax on the cost of that perquisite to his employer or on the value of it to him, and it appears to me that this perquisite is a taxable subject matter because it is money's worth. It is money's worth because it can be turned into money and, when turned into money, the taxable subject matter is the value received."

Pecuniary liability of an employee met by the employer

If an employer defrays some expenditure which his employee was under a legal obligation to meet, the employee receives a profit; and if it is a profit from his employment, it is assessable on him. For example, where an employer pays for an employee's bills or expenses such as rent, electricity, telephone bill, water bill, school fees or similar payments, the employer is required to add such payments to the employee's emoluments and deduct tax under P.A.Y.E.

[9] 3 TC 158.
[10] 39 TC 344.

This point was made clear in *Hartland v Diggins*.[11] It was held in this case that the income tax liability of an employee if paid by his employer, the amount assessable on the employee is the remuneration which he actually receives plus the tax liability on the amount assessable. It should also be noted that legal obligation need not be statutory, for it has been held that a premium paid by an employer under an employee's life assurance policy represented money's worth.

In the case of *Nicoll v Austin*,[12]the Managing Director of a company owned and resided in a large and imposing house but found difficulty in meeting the expenses connected therewith. The company agreed in addition to paying a salary, to meet all the outgoings on the house (rates, repairs gardener's wages etc.), on condition that he agreed to continue to reside there. This was rather different from the situation of the bank manager in *Tennant v Smith* because not only was he required to live in the house as manager as a condition of his services, but when his appointment was terminated, or he was moved to another branch he would be required to give up the house. Tennant's occupation of the house was clearly "representative" and all outgoings on such as rates were the legal liabilities of the bank and not of the tenant. In Austin's case the house was his own and liability for rates and repairs was his. The court took the view that the only proper construction to be placed on his agreement with the company was that the terms of his employment provided him with money as his salary, and money's worth as the expenses of the house were defrayed by the company.

Expense Reimbursements

It is a common practice among large companies to make expenses reimbursements to their Directors and higher executives, that is, contribution towards expenses incurred by the employee in connection with his work. In the normal circumstances such payments could not be regarded as emolument since they are not reward for service or anything like it.

On the other hand, an employer cannot relieve an employee of his liability to tax by calling remuneration by some other name. Consider the case of *Dingley v McNulty*.[13] In this case the taxpayer was Vice-President and a Director of a Benevolent Fund incorporated under special Acts of parliament. He attended seventy-four director's meetings and received one guinea in respect of each meeting. On appeal against an assessment of income tax made upon him under schedule E in respect of these sums less allowance of 25% for expenses, he contended that –

(a) his office of Director was not an office of employment of profit assessable under schedule E; and
(b) the whole sum paid was simply an allowance for sums expended wholly exclusively and necessarily in the performance of his duties.

The Special Commissioners decided that the sum paid to the taxpayer constituted remuneration as a Director in respect of which he was assessable under schedule E, and in the absence of detailed evidence, which was not submitted, the allowance made in respect of expenses was adequate. On appeal, the court held that the decision of the Special Commissioners was correct. The principle established by this case was that:

> "Where the employer reimburses a genuine expense incurred on the employer's behalf during the course of his work, the employee will not be taxed on "expenses payment" received if

[11] 10 TC 247.
[12] 19 TC 531.
[13]21 TC 152.

expended fully. But where an employer reimburses an employee for an expense that conferred some benefit on the employee that benefit would be assessable.

4.5 NON-CHARGEABLE EMOLUMENTS

The following emoluments are exempt or otherwise not chargeable to income tax and, consequently need not be included in the chargeable emoluments from which P.A.Y.E. tax is to be deducted: -

- **Ex-gratia Payments –** A voluntary, non–contractual, non–obligatory payment made by an employer to a spouse, child or dependant of a deceased employee is exempt (Para.7(t), Second Schedule of Income Tax Act).

- **Medical Expenses -** Medical expenses paid or incurred by an employer on behalf of an employee or refunds of actual medical expenses incurred by an employee are exempt (The Income Tax (Suspension of Tax) Order, S.I. No. 104 of 1996). *Medical allowances*, however, are taxable and should be included in chargeable emoluments.

- **Benefits not convertible into money or money's worth –** Benefits which cannot be converted into money or money's worth are not taxable to the employee. This includes, for example:

  (a) *Rent free accommodation provided by employer* - Free residential accommodation provided by an employer in a house owned or leased by the employer is not a taxable benefit to the employee.

  See: *Tennant v. Smith, 3 TC 158*
  Gray v. Holmes, 30 TC 467
  Bent v Roberts, 1 TC 199
  Reed v Cattermole, 21 TC 35

  Payments for utilities such as electricity, telephones, water bills, security and similar payments, however, are not included in the meaning of free residential accommodation.

  (b) *Personal to holder vehicles* - The benefit arising out of the provision by an employer of a motor vehicle to an employee on a personal to holder basis is a non–taxable as it is not a convertible benefit. A personal to holder vehicle means a vehicle provided to an employee for both business and personal use and usually involves payment by the employer of all expenses associated with the running and maintenance of the vehicle.

- **Funeral Expenses -** Funeral expenses paid or incurred by an employer on behalf of an employee are exempt from tax (The Income Tax (Suspension of Tax) Order, S.I. No. 104 of 1996).

- **Sitting Allowances for Councillors -** Payments by Local Authorities to councillors as sitting allowance are exempt (paragraph 7(s), Second Schedule of the Income Tax Act).

- **Labour Day Awards** – Labour Day awards paid to employees either in cash or in kind are non-taxable.

4.7 COMPUTATION OF TAX

Tax Tables

Regulation 4(1) of the P.A.Y.E. Regulations requires an employer to deduct tax from emoluments paid to an employee or repay tax to an employee in accordance with appropriate tax tables. Tax tables are provided by ZRA for use by employers to work out how much P.A.Y.E. tax is to be deducted or repaid from chargeable emoluments. There are two sets of tables:

(a) Monthly tables; and

(b) Daily tables

Monthly Tables - These are to be used for all employees who are paid at monthly intervals. The Monthly Tables are divided into two parts. Table A shows the tax rates to be used in arriving at the tax to be deducted or repaid. Table B shows how to calculate tax due before deducting the tax credit by reference to chargeable emoluments paid. Table B assumes that the allowed deductions have been deducted and what is reflected in the table is the chargeable amount.

Daily Tables - These are to be used for casual employees, that is, all employees who are paid at intervals of less than 5 days. Where a worker is paid daily the tax payable is arrived at by simply finding the tax payable for the particular amount paid. Where the payment period is 2, 3 or 4 days, the payment made is divided by 2, 3 or 4 respectively, the tax due calculated by reference to the table and amount then multiplied by 2, 3 or 4, to arrive at the tax to be deducted.

Tax Rates

For the charge year 2022, the tax rates applicable to monthly emoluments are as follows:

First K4,500	@	0%
Next K300	@	25%
Next K2,100	@	30%
Balance	@	37.5%

Calculation of tax

Under the P.A.Y.E. system, the amount of tax which an employer deducts from emoluments depends on:

(a) the employee's total gross pay;

(b) the applicable tax rates; and

(c) statutory deductions (e.g., allowable pension contributions).

Example:

An employee has a gross salary of K14,000 per month in January 2022. The tax liability of this employee will be calculated as follows:

(a) calculation of taxable pay:

Gross Salary:	K 14,000
Less deductions:	K 0
Taxable pay:	K 14,000

(b) Calculation of tax using the tax rates:

	Rate of Tax			Tax Due (K)
Taxable income			K14,000	
	@ 0%	First	4,500	0.00
			9,500	
	@ 25%	Next	300	75.00
			9,200	
	@ 30%	Next	2,100	630.00
	@ 37.5%	Balance	7,100	2,662.50
Tax Due will be				**3,367.50**

Irregular Payments in Addition to Basic Salary

Employers will sometimes make payments in addition to an employee's basic salary or wages on a day that is not the employee's regular pay day, for example, a quarterly bonus paid on a day other than a regular pay day.

The tax to be deducted from such payments is to be calculated by:

- Working out how much tax will be deducted from the employee's next payment of basic salary or wages.
- Working out how much tax would be deducted from the next payment of basic salary or wages if the additional payments were made added to the basic salary or wage.
- The tax deductible is the difference between the two figures.

Example

Suppose an employee is paid a regular salary of K14, 000 per month and a quarterly bonus of K1,000 is paid on 5 March 2022. How much tax should be deducted from the bonus payment?

From the previous example above, we have seen that **K3,367.50** would be payable in taxes from the basic salary of K14,000 at the end of March. If the K 1,000 bonus was also paid at the end of March, the tax to be deducted on the total amount would be:

Gross salary:	K14,000
Plus bonus:	K 1,000
Total taxable pay	K15,000
Less deductions:	K 0
Taxable pay:	K15,000

Using the tax rates:

	Rate of Tax			Tax Due (K)
Taxable income			K15,000	
	@ 0%	First	4,500	0.00
			10,500	
	@ 25%	Next	300	75.00
			10,200	
	@ 30%	Next	2,100	630.00
	@ 37.5%	Balance	8,100	3,037.50
Tax Due will be				**3,742.50**

Therefore, the tax to be deducted on the bonus payment made on 5 March is:

K3,742.50 – K3,367.50 = **K375.00**

4.7 TREATMENT OF NET EMOLUMENTS

Sometimes an employer will enter into an agreement with an employee to pay the employee emoluments that are "free of tax" or "net of tax". This means, in effect, that the employer has agreed to bear on the employee's behalf, any tax chargeable in respect of payments made under the agreement.

Regulation 14 of the P.A.Y.E. Regulations provides that where such an agreement is made between an employer and employee:

(a) The agreement is treated as an agreement by the employer to pay the employee such gross emoluments as will, after deduction of tax will be equal to the net emoluments; and

(b) The employer shall calculate the amount of tax to be deducted from any payment of the employee's emoluments by reference to the gross emoluments of the employee and not by reference to the employee's net emoluments.

In other words, the employer must account for an amount of tax on a gross payment that would, after the deduction of tax in accordance with the Regulations, leave a net amount equal to the amount actually paid/payable to the employee under the agreement.

Any employer entering any such agreement with an employee is obliged to notify the Commissioner General of the details of the agreement within 14 days of the beginning of the charge year or the commencement of the employment in question (Reg. 14(2)).

4.8 MULTIPLE EMPLOYMENTS – PART-TIME EMPLOYEES

The term "part- time" has a special meaning for P.A.Y.E. purposes that is different from the normal meaning of the phrase.

Where an employee has only one employment, that employment is not regarded as part–time, whatever the number of hours of employment. However, where an employee obtains other employment, the second and any subsequent employments are, for P.A.Y.E. purposes, regarded as part–time (Reg. 8(5) and (6) of the PAYE Regulations).

This means, for instance, if an employee is employed as a barman, 5 days a week from 20:00hrs to 24:00hrs, this employment is not regarded as part–time for P.A.Y.E. purposes. If, whilst remaining

employed as a barman in the evening, the employee also starts working as a driver, 6 days a week, from 07:00hrs to 17:00hrs, this second employment is, for P.A.Y.E. purposes, regarded as part – time.

The significance of part – time employment is that tax is to be deducted at the maximum tax rate, that is, the highest marginal rate applicable to individuals for the charge year of payment (37.5% for 2022 tax year). No deduction is to be given for any tax credit to which the employee may be entitled, and no regard is taken of cumulative tax (Reg. 8(1) of the PAYE Regulations.

4.9 PAYMENTS MADE ON CESSATION OF EMPLOYMENT

When an employment terminates through an employee leaving or on death, an employer may make various payments, depending on the circumstances giving rise to the cessation. The employment may cease due to resignation, early or normal retirement, dismissal, redundancy, retirement, or the completion of a fixed – term contract.

Payments on cessation of employment may be of various types and generally fall into the following categories:

(a) payments made on dismissal or resignation;

(b) payments made to an employee at the end of a contract;

(c) payments made to an employee on redundancy;

(d) payments made to an employee on retirement; and

(e) payments made on the termination of employment due to the death of an employee.

When employment is terminated in any of the above circumstances, a number of types of payments can be made to an employee, e.g., unpaid salary, bonuses, commissions, payment in lieu of notice and compensation for loss of office, etc.

The tax treatment of the various payments that may be made to an employee on termination of employment is as follows:

- **Contractual payments** - Contractual payments made to an employee on termination of employment under any circumstances, such as unpaid salary, accrued leave pay, bonuses, commission, overtime pay and other pre-existing contractual payments are fully taxable as emoluments unless otherwise exempt. See *Dale v de Soissons*,[14] where a manager's service contract provided for him to be paid 10,000 pounds if it should be prematurely terminated. The taxpayer argued that this payment was not in return for services. It was held, however, that the payment was one to which he was contractually entitled and therefore taxable.

- **Salary in lieu of notice** - Salary in lieu of notice paid to an employee on termination of employment under any circumstances is also fully taxable as an emolument. In *EMI Group Electronics Ltd v Coldicott*[15] a company had employed individuals on employment contracts,

[14] [1950] 2 All ER 460
[15] 71 TC 455

which provided that the employees may be dismissed with six months' notice. Under the contracts, the company was able to dismiss the employees immediately and pay them the equivalent of salary in lieu of notice. The employees were so dismissed and the paid them six months' salary in lieu of notice. The Inland Revenue contended that the payments were assessable as an emolument from employment; the taxpayer contended that the payments were non-taxable payments in lieu of notice. It was held that the compensation was paid in accordance with provisions in the director's contract and was therefore taxable as emoluments from employment.

- **Severance pay, gratuity, compensation for loss of office and pensions** – The Constitution of Zambia (as amended by Act No. 2 of 2016) exempts from taxation any amount paid to an employee as a "pension benefit." Articles 188 and 189 of the Constitution provide as follows:

  > *188. (1) A pension benefit shall be reviewed periodically to take into account actuarial assessments.*
  >
  > *(2) **A pension benefit shall be exempt from tax**.*
  >
  > *189. (1) A pension benefit shall be paid promptly and regularly.*
  >
  > *(2) Where a pension benefit is not paid on a person's last working day, that person shall stop work but the person's name shall be retained on the payroll, until payment of the pension benefit based on the last salary received by that person while on the payroll.*

  The Constitution defines "pension benefit" under Article 266 as follows:

  > *"Pension Benefit includes a pension, compensation, gratuity or similar allowance in respect of a person's service."*

  The Constitution therefore exempts from taxation any amount of pension, compensation, gratuity, severance pay, repatriation and other similar allowances received in respect of a person's services at termination of employment under any circumstances.

  It must be noted that pensions paid from a pension fund are also exempt from tax under paragraph 7(q) of Second Schedule to the Income Tax Act.

- **Lump sum payments made on discharge medical grounds** - Where an employee is discharged from employment on medical grounds on the advice of a registered medical practitioner or medical institution, any lump sum payment made to the employee on such discharge is exempt from tax under paragraph 7(v) of the Second Schedule of the Income Tax Act.

- **Repatriation allowance paid on redundancy/retrenchment/retirement/death of employee** – where an employee's employment terminates by way of redundancy, retrenchment, retirement or death, and such employee (or the employee's surviving family in the event of death) is paid a repatriation allowance, the repatriation allowance is taxed as follows under section 21(5) as read with paragraph 2(1)(b) of the Charging Schedule of the Income Tax Act:

  (a) the first K35,000 is exempt from tax; and

(b) the balance is taxed at 10%.

- **Ex-gratia payments on death of employee** - Ex-gratia payments made to a spouse, child or dependent of a deceased employee are exempt from tax under paragraph 7(t) of the Second Schedule to the Income Tax Act.

4.10 REMITTANCE OF TAX

P.A.Y.E. tax deducted by an employer, less any refunds, must be remitted to ZRA together within 10 days of the end of the income tax month (Reg. 17 of PAYE Regulations).

Where an employer fails to make a return or to remit tax, ZRA may estimate the tax the employer is required to remit and issue a notice requiring payment of that amount or issue a notice requiring the employer to submit a default return (Reg. 18).

Further, where an employer fails to remit tax deducted to ZRA within the required period, section 71(3) of the Income Tax Act imposes a penalty of 5% of the tax unpaid for each month, or part thereof that tax remains unpaid. In addition, interest under section 78A accrues on the unpaid taxes from the due date to the date of payment at the Bank of Zambia discount rate plus 2% per annum.