



**Revenue
Services**
Lesotho

WITHHOLDING TAX PUBLIC RULING

“Re Tjena Ka Uena”

RSL INCOME TAX PUBLIC RULING ISSUE 1

Subject : WITHHOLDING TAXES

Act : Income Tax Act NO.9 of 1993 as amended

Section : Sections 107,108,157, 158 and 160

Date : April 2010

Background

The Income Tax Act 1993 as amended (the Act) makes provision for the taxation of Lesotho residents on their worldwide income and, for non-residents; tax is levied only on their income that is Lesotho-sourced income. To facilitate taxation of non-resident(s) on the Lesotho-source income, withholding tax system is adopted.

In terms of the withholding tax rules, the payer is required to deduct from the gross amount due to the payee, a percentage prescribed by the law. Thus, the payee receives payment on the invoice amount less the withholding tax deduction. The payer who is referred to as the Withholding Agent is required to pay the amount withheld to the Revenue Services Lesotho (RSL) within a stipulated time period as prescribed by the Act.

Withholding taxes are applicable to the following

- Service fees payable to non-residents for services such as accounting, auditing, economic, financial, legal, management, and consultancy, engineering, architectural and surveying.
- Service fees paid under employment contracts, PAYE.
- Payments to resident contractors. For this purpose, it is important to note that , the Act defines a resident contractor as a person engaged in the business of leasing vehicles, plant, or equipment, or of providing construction, transportation, painting or decorating, plumbing, drainage, or irrigation, roofing or tiling, earthmoving or excavation, landscaping, building demolition, site restoration and installation of services or appliances.
- Passive income. This refers to income which is derived without active involvement in generating it. Examples of passive income are: interest, dividends, royalties, management charge, patent fees, and trade mark fees.
- Amounts paid to artistes, sportspersons and musicians who are entertainers, (including professional clubs but excluding amateur sporting associations).

Notwithstanding the above, where goods are produced or supplied in the process of providing a service then the cost of such goods will be aggregated with the cost of the service and the gross amount (before charging VAT) is subject to withholding tax. Such goods are considered incidental to the provision of the service as they combine to deliver the service.

However, withholding taxes are not payable on utilities. That is, provision of electricity, water and sewage, and telephone. Further, tax is also not withheld on rental for buildings. For instance no withholding tax will be payable on residential accommodation and office space.

This note seeks to provide guidance on the circumstances wherein one is expected to withhold tax. However, special note should be taken as this ruling does not cover the entire spectrum of the withholding tax under the Act, but deals only with the specific areas in respect of the international transactions and construction and related services.

The law and its application

The Act prescribes various circumstances wherein a payer is obligated to withhold tax when making payment. To illustrate the application of the law therein, tables have been drawn which presents the applicable withholding rates as per sections 107, 108, 157, 158 and 160 of the Act. In the column "Filing Requirements", it is shown whether the taxpayer is required to file return(s) after the tax has been withheld or not.

Where no further return is required, the tax received therein is final tax and for the purposes of the illustration hereunder the words "Final tax" are used. Alternatively, the words "Optional" apply where the law allows filing of a return if the Client feels that the income tax paid during the tax year, by way of withholding, is higher than that which is otherwise payable where a return and supporting documents are filed.

Section 107: PASSIVE INCOME

This section applies where payment of Lesotho source income is made to non-residents. Tax is withheld in terms of this section on the gross amount of a Lesotho source dividend, interest, royal, natural resource payment and management fees. However, where dividend is paid out of manufacturing income, no withholding tax is payable. Further where, the royalty is paid for the use of technology that produces manufacturing income subject to tax in Lesotho, the rate of withholding tax is 15%.

| items/Examples | Form used | Withholding Rate | DTA Rate | Filing Requirement |
|--|------------------|-------------------------|-----------------|---------------------------|
| Dividends | WD1(1993) | 25% | 5%/10%/12.5% | Optional |
| Interest | WD1(1993) | 25% | 15% | Optional |
| Natural resources payment/Income from immovable property | WD5(1993) | 25% | - | Optional |
| Management fee | WD4(1993) | 25% | 7.5% 10% | Optional |
| Royalty | WD5(1993) | 25% | 7.5% 10% | Optional |

Section 108: SERVICES

In terms of section 108, tax is withheld where payment is made to a non-resident under a Lesotho source services contract. The contract referred to herein is a contract other than the employment contract of which performance of services therein gives rise to Lesotho source income. The provisions of this section apply to both technical and ordinary services. Management fees are however, not covered under this section, as such are taxed under section 107.

| items/Examples | Form used | Withholding Rate | DTA Rate | Filing Requirement |
|--|-----------|------------------------------------|------------------------------------|---|
| Artistes; Entertainers; Sportspersons; Auditing; Accounting; Economic; Financial; Legal; Engineering; Architectural; etc. | WD3(1993) | 10% For all items in this category | N/A For all items in this category | Optional for all items in this category |

Section 157: RESIDENT CONTRACTORS

This section applies to resident contractors. It does not; apply where the payment relates to construction of an individual's principal residence. However, where the total fee to be paid is less than M3000 no withholding tax is payable.

| items/Examples | Form used | Withholding Rate | DTA Rate | Filing Requirement |
|---|--|--|---|---|
| Leasing vehicles, plant equipment, construction services, painting or decorating, Installation services, plumbing and drainage, water supply, irrigation, roofing, tilling, earthmoving, excavation, landscaping, demolition, restoration works, etc. | WD11(1993) This form is used for all resident contractors | 5% For all items in this category | N/A For all items in this category | Mandatory For all items in this category |

Section 158: INTEREST TO RESIDENTS

Tax is withheld at a source where interest is paid by a Lesotho resident to another. The first M500.00 of interest income is exempt from tax, that is, it should be deducted from the gross amount before applying the 10%. However, special note should be taken that the exemption is only available to resident individuals, that is, it excludes companies and other incorporated bodies.

| items/Examples | Form used | Withholding Rate | DTA Rate | Filing Requirement |
|----------------|-----------|------------------|----------|--------------------|
|----------------|-----------|------------------|----------|--------------------|

| | | | | |
|------------------------------|-----------|-----|-----|-----------|
| Interest paid to individuals | WD1(1993) | 10% | N/A | Final Tax |
| Other resident Clients | WD1(1993) | 10% | N/A | Mandatory |

Section 160: PAYMENTS BY LIQUIDATORS

These are payments made to shareholders in winding up companies and not to ordinary business creditors. Liquidation involves cancellation of shares and therefore, there could be capital gains on the shares. Normal company tax rate of 25% applies on the capital gain.

| items/Examples | Form used | Withholding Rate | DTA Rate | Filing Requirement |
|------------------------|---------------------------------------|-------------------------|-----------------|---------------------------|
| Cancellation of shares | Ordinary notification letter required | 10% | N/A | Filing Mandatory |

Examples

The following examples illustrate the principles and concepts discussed in the forgoing paragraphs in deciding whether or not to withhold.

Example 1

Ladybrand Motors, a South African based company, repaired during the month buses belonging to both Basotho Transport (Pty) Ltd and Kokoptje ea Mara belonging to the Lesotho Defence Force.

Question:

Should tax be withheld by Basotho Transport and the Lesotho Government when making payments to Ladybrand Motors?

Answer:

It is important to note that the service did not take place in Lesotho, and this is the gist of source-based taxation. Both Basotho Transport and Lesotho Government should therefore, not withhold tax. However, had the repairs by the South African based Ladybrand Motors taken place in Lesotho, then both Basotho Transport and the Government would have to withhold. The essence of sub- section 103 (1) (b) is to first and foremost ensure that other taxpayers treat the Government and its ministries as distinct taxpayers for tax purposes.

Example 2

A government ministry earns M1500 interest from its call account with a local bank.

Question:

Is there any withholding tax liability, isn't government exempt from tax?

Answer:

The term "Client" is defined broadly as including government or any subdivision of government. This includes Government ministries, departments, sections and local governments/councils. As such, since property income has been earned, in the form of interest, by the Government Ministry in this case the local bank should withhold the tax at the rate of 10 % (M1500) = M150 and pay this to the RSL.

Example 3

Best Computers (Pty) Ltd sold 500 000 metres wire cable to Lesotho Properties (Pty) Ltd for M1 million. Due to the bulk purchase, Best Computers undertakes the network cabling work free of charge.

Question:

Should there be any withholding tax by Lesotho Property for a free service and if so, how is that quantified?

Answer:

At face value the transaction is purely for the supply of goods and consequently no question of withholding tax arises. However, considering the quantity of the wire cable bought and the fact that it is used ultimately for cabling purposes, a detailed analysis is needed. In principle, it means that by undertaking cabling for the client, Best Computers (Pty) Ltd did not only supply goods but provided a service, the installation service. On the basis of this inference therefore, the supply of the cable wire is thus taken as incidental to the service of installation. So, Best Computers (Pty) Ltd over and above the supply of wire cable has provided the service of installation to Lesotho Properties (Pty) Ltd and because of the latter, Lesotho Properties shall have to withhold tax on the M1 million.

Example 4

New Asia Textiles acquired two buildings, one in Thetsane Industrial Area and the other in Nyenye Industrial Area. The Thetsane building was purchased on an "as is" basis from Development Corporation for M2.5 million. While the Nyenye building which was constructed by Kopanang Construction using the Thetsane plan and specifications also cost M2.5 million.

Question:

How does withholding apply?

Answer:

For the Thetsane building no withholding tax is payable, but the payment to Kopanang Construction should be subject to 5% withholding tax, Kopanang being a resident contractor. In the first case, New Asia Textiles is paying for the purchase of the building and not for a service. In the second case, New Asia is paying for the construction service. The fact that a physical product, a building, was produced in the Nyenye case

does not make the transaction that of a provision of a good/product but a provision of a service, that is, construction service.

Example 5

PHC, a firm of public international accountants wins a tender to undertake a forensic audit at Lesotho University (LU). PHC partners with a local accountancy firm, Y & E Accountants because of logistical and resources requirements. Indeed in the tender document PHC indicated that Y & E will be its main partners. Upon completion of the assignment, the bill/invoice amounting to M2.4 million comes from Y & E and is payable to their account with a local bank.

Question:

Should LU withhold any tax when they pay Y & E, being a local company and not resident contractors under section 157?

What would be the case if the bill was split in portions, say 80% or M1 920 000 coming from PHC and 20% or M480 000 from Y & E?

Answer:

It is important to note that the work has been contracted to PHC and is thus responsible for the delivery or performance, that is, it is PHC who has contractual obligations to deliver. The fact that the whole bill comes from Y & E Accountants is irrelevant in deciding whether to withhold or not. LU must withhold on the whole M2.4 million though the bill comes from Y & E. If the bill is apportioned, it can clearly be seen from the above going paragraph that tax must be withheld on the whole M2.4 million and not on the M1 920 000 claimed by PHC. Taxpayers can enter into agreements in which payments can be made to other persons other than themselves. The guiding principle is to see who ultimately remains liable under the contract and such should accordingly withhold tax.

Example 6:

Amount on which to calculate withholding and VAT

Question

The law states that withholding tax is payable on the “gross amount”. What is this amount?

Answer

The “gross amount” referred to in the law is the amount before inclusion of the VAT. Further note that the VAT is also charged on the same “gross amount” that is, before the deduction of the withholding tax. If a non-resident service provider charges, before VAT, Government of Lesotho M15 000, for services rendered, then both the withholding tax and VAT are calculated on the M15 000 so that the withholding tax is M1 500 and the VAT (14%) M2 100. The service provider will then receive M15 000 – 1 500 + 2 100 = M15 600.

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