



Lesotho Revenue Authority

Interpretation and Application of Section 17 (1) (b) of the VAT Act No.9 of 2001

September 2020

Executive Summary

1.0 Background

The legal opinion on interpretation and application of provisions of section 17 relating to registration attached hereto was birthed by the need to curb improper claim of input credit tax by ‘vendors’ who were not qualified by virtue of not making taxable supplies. Some of these companies did not qualify because they were still in a development stage or otherwise their turnover projections were not accurately assessed. The points highlighted below are key takeaways from the opinion.

2.0 Section 17 (1)(b)

The opinion outlines that most challenges relating to registration are centered around section 17 (1) (b). It is also shown, if properly applied, section 17 as a whole has safeguards against abuses highlighted in the paper.

3.0 Registration

Submission is made that section 17(1) as a whole is a mechanism to ensure that persons who should be in the tax net are registered.

4.0 Taxable Supplies

The qualification for a vendor to validly claim credit for input is premised on the vendor’s ability to make taxable supplies. Vendors who are not yet making taxable supplies should not be able to claim credit for input tax.

5.0 Safeguards Against Loss of Revenue

- Subsection 8 gives the Commissioner powers to consider every application and register only those persons who are eligible for registration. The challenges experienced were caused by the practice of automatically registering most persons who applied for registration without enough scrutiny as to their eligibility.
- Subsection 9 provides that the Commissioner is empowered to prescribe dates of effective registration. This provides the commissioner with control.
- Subsection 11 provides that registration takes effect from the date of registration as specified in the VAT certificate or a later date determined by the Commissioner. Prescribing the date of effective registration prevents vendors who are not qualified from claiming credit for input tax.

6.0 Conclusion and Recommendations

It is recommended that the safeguards found in the law be used to minimize revenue loss through fraudulent claims made by vendors who never intended to make any taxable supplies within the prescribed timelines. Careful assessment of each application for registration needs to be made to ensure that only those who qualify are registered. Secondly, to include appropriate conditions to every registration made to ensure minimal revenue loss and quickly deregister vendors who are not making taxable supplies.

Terms and Definitions

“In this interpretation Note, the following words shall bear the same definitions as they are defined in the VAT Act, unless the context indicates otherwise.”

Authority – means the Lesotho Revenue Authority;

Input tax – means value added tax paid or payable in respect of a taxable supply to, or a taxable import by, any person, but does not include additional tax;

Person – includes a partnership, company, trust, government, political subdivision of a government, or public international organization;

Taxable supply – means a supply of goods or services (other than an exempt supply) made in Lesotho by a vendor for consideration in the course or furtherance of an enterprise carried on by the vendor; and

Vendor – means a person who is, or is treated as, registered under the Act.

Introduction and Background

1. Section 17 of the VAT Act¹ makes provision for registration of taxable persons, commonly known as ‘vendors’ and outlines the different scenarios which qualify and disqualify a person for registration.
2. Upon registration, a person carrying on an enterprise in Lesotho is accountable for Value Added Tax on the taxable supplies of goods and services made by the person. This is normally known as output tax. Effectively the registered vendor becomes the Authority’s agent. The Act outlines the different scenarios which qualify and disqualify a person for registration.
3. Registration of a person as a vendor is key as it has the effect of imposing certain obligations and duties upon the vendor. Amongst the obligations included are collection and remission of the VAT to the Authority.
4. The Act recognises different categories of registration which include compulsory registration and voluntary registration.
5. In addition to this the vendors are then entitled to claim refunds for input tax, that is the VAT they paid in the process of acquiring taxable supplies that are going to be used in their business activities.
6. The aim of this interpretation note is to set out the proper interpretation and application of section 17(1) (b) and demonstrate that the Act itself has inbuilt safeguards against abuses such as those highlighted below. Section 17 (1) (a) and (b) provide that –

“A person who is not already registered is required to apply to be registered as a vendor- (a) within fourteen days of the end of any period of twelve months if during that period the person made taxable supplies the taxable value of which exceeded the registration threshold set out in subsection (2); or

(b) at the beginning of any period of twelve months where there are reasonable grounds to expect that the total taxable value of taxable supplies to be made by the

¹ Act 9 of 2001 as amended.

person during that period will exceed the registration threshold set out in subsection (2).”

7. The provisions discussed below revolve around the concept of ‘taxable supplies’. Section 5 of the Act states that value added tax is imposed on – every taxable supply and every taxable import hence a taxable supply has been explained as a supply or transaction on which VAT is imposed. Two key elements of a taxable supply are that the supply of goods and services must be made as part of the economic activities of the supplier, and against payment (or for consideration) to that person from some other person. Section 12 (1) provides that a taxable supply is a supply of goods or services (other than an exempt supply) made in Lesotho by a vendor for consideration in the course or furtherance of an enterprise carried on by the vendor. Subsection (2) provides that a taxable supply includes a supply by way of an export of goods or services by a vendor for consideration in the course or furtherance of an enterprise carried on by the vendor. VAT is a broad-based indirect tax applicable in respect of a wide range of goods and services supplied by vendors. It is collected at each stage in the production and distribution chain. The liability to charge VAT arises each time a taxable transaction is carried out by a vendor and does not depend on the profitability or outcome of the transaction because VAT is not a tax on business profits or turnover, but on consumption.
8. It has been stated also that the common pattern of an invoice-based VAT is that a charge to VAT is imposed on all transactions within the state and within the scope of the VAT. Each taxable person is allowed a deduction against the total VAT charged by the person to take account of any VAT paid by the person on inputs related to transactions within the scope of the VAT. A transaction within the scope of VAT and on which VAT is imposed is commonly called an output and the VAT collected on it is called output tax. A transaction made to the person making the output is known as an input, and the VAT paid by that person when obtaining the input is an input tax. The internal charge to tax, consistent with the principles noted above, is therefore a charge amounting to the output tax received by a person less the input tax paid by that person. The charge to tax must therefore identify on which outputs, and by which persons, output tax must be collected, and what input tax is available as a deduction against that output tax.

Mandatory Registration

9. Section 17(1)(a), (2) and (6) of the Act compels different categories of persons or entities to

register as VAT vendors regardless whether such persons meet the registration threshold or not
The following are obliged to register:

- a) a person who is an auctioneer ;
- b) a person who carries on an enterprise outside Lesotho but whose goods are consumed in Lesotho;
- c) a local, regional, or local public authority or body that carries on enterprises is required to register at the time it commences the enterprises;
- d) a person who made taxable supplies which exceed registration threshold for a year is expected to register 14 days after the lapse of twelve months period.

Voluntary Registration

10. Section 17(5) permits a person who makes taxable supplies to apply for registration as a vendor even if the person does not meet the registration threshold. On the other hand section 17(1) (b) allows a person or entity to apply for registration at the beginning of twelve months where there are reasonable grounds to expect that the taxable value of taxable supplies made by that person will exceed the registration threshold during that period.

Challenges faced by the Authority following registration of vendors under section 17(1) (b)

11. The Authority has often had to deal with cases where persons registered for VAT claim refunds in circumstances where no taxable supplies were being made and no output VAT was remitted. These persons use section 17 (1) (b) read with other relevant provisions such as section 23 to justify making the claims for refunds. It goes without saying that the claims result in huge revenue losses for the Authority and by extension, the Government of Lesotho. The aim of this interpretation note is to set out the proper interpretation and application of section 17 (1) (b) and demonstrate that the law itself has inbuilt safeguards against abuses such as the one highlighted above.
12. Majority of persons who apply for registration in terms of section 17 (1) (b) often make use of it with a sole intention of enjoying the rights of claiming input tax without any intention of making taxable supplies.
13. In majority of cases the issue has been whether a person who registers for VAT under section

17 (1) (b) is entitled to claim input credit refunds by virtue of being registered but where no taxable supplies were being made. Put in another way, is a vendor entitled to claim input tax credit when they are not making taxable supplies. This will necessarily lead to the correct application of the relevant registration provisions.

14. Section 17 (1) (a) provides that – a person who is not already registered is required to apply to be registered as a vendor within fourteen days of the end of any period of twelve months if during that period the person made taxable supplies, the taxable value of which exceeded the registration threshold set out in subsection (2). This means that a person who is not yet registered, but who is already trading is required to apply for registration within fourteen days of the end of any twelve months period, where taxable supplies exceeding the threshold are made during that period. This is clarified by subsection 4 (a) which explains that the ‘taxable supplies’ referred to here are supplies that would be taxable supplies if the person making the supply were a vendor. A vendor is a person who is, or is treated as registered under the Act.
15. The phrase ‘*end of any period of twelve months*’ means that the twelve months period is used to set the time limit for a person to apply to be registered. It does not preclude a person from applying for registration if the threshold is reached before the period of twelve months elapses. This also applies to people who are just beginning to make taxable supplies. The twelve month period is a management tool which ensures that persons who should register should actually register and those who need not register should not register. It also sets the time period within which persons who have reached the threshold have to register, after reaching the threshold. The twelve month period is not to be taken as applying retrospectively, that is, even before the person starts making taxable supplies.
16. An example is a person who begins trading in the month of May 2016 and reaches threshold at the end of January 2017. If subsection 1 (a) is taken to mean that a person waits for the end of a twelve-month period in order to register, they would have to wait until end of April 2017 to be registered within 14 days in the month of May 2017. It is submitted that this would lead to unintended results because we would have a situation whereby a person who has reached threshold would wait a long time before they can actually register. Therefore a proper interpretation should be that upon reaching the

threshold, a person should register immediately. Therefore sub-section (1) is meant to ensure that persons who should be in the tax net and be registered, are indeed registered.

17. Section 17 (1) (b) provides that a person is required to apply at the beginning of any twelve months where there are reasonable grounds to expect that the total taxable value of taxable supplies to be made by the person during that period will exceed the registration threshold set out in subsection (2). This means that a person not yet registered, who begins trading or has been trading for some time, should register at the beginning of any twelve months period when there are reasonable grounds to expect that the total value of taxable supplies will exceed the applicable threshold.
18. Section 17(1)(b) of the VAT Act, broken down into its essential requirements requires the following:
 - a) An application to be made;
 - b) At the beginning of any period of twelve months;
 - c) Where at the beginning of such period of twelve months, a taxpayer entertained reasonable grounds to expect that it will during the twelve months period make supplies exceeding the registration threshold.
19. Understanding the application of section 17 (1) (b) is key because many of the entities who claim huge refunds but do not make taxable supplies were registered under it. It is important to note that every application still needs to be assessed whether the person qualifies to be registered or not.
20. Section 23 (1) (b) provides that a credit is allowed to a person on becoming registered under section 17 for input tax paid in respect of goods or services on hand at the date of registration held for making taxable supplies, provided the goods or services were acquired by that person not more than two months before the date of registration and an application for the credit is made within two months after the registration date. Section 23 (3) (b) provides that an input tax credit allowed under section 1(b) arises on the date registration takes effect.
21. It is submitted that vendors who are not yet making taxable supplies are not entitled to claim credit for input tax. Credit for input tax is allowable only for input tax paid in respect of taxable supplies. Allowing credit for input tax simply because a person is a

vendor but without making taxable supplies violates the fundamental principles of the VAT system. The importance of making taxable supplies as a vendor is further shown by section 18 (1) which provides that a vendor is required to apply in writing to the Commissioner to have registration cancelled if the vendor has ceased to make taxable supplies. Therefore once a vendor ceases to make taxable supplies they are disqualified from being vendors. This addresses the situation faced by the Authority of 'vendors' who spend years claiming credit for input tax with no corresponding taxable supplies. To further illustrate this, it is well understood that businesses that are not making taxable supplies are not registered even though they are expected to pay VAT when they acquire goods and services which are used to provide non-taxable or exempt supplies. Examples would include commercial banks, which pay VAT on most of the goods and services that are used to supply financial services which are exempt. The input tax paid is never recovered. Furthermore, exempt organizations are not registered for VAT and the input tax paid is recovered using an entirely different process that does not involve registration

22. It is furthermore submitted that an application in terms of section 17(1) (b) of the VAT Act cannot be made by an applicant at the time the applicant is preparing itself to be in a position to start making taxable supplies. Put differently it cannot be made by an applicant who is not yet in a position to carry out its undertaking, or the operations of the business. Applications for registration therefore should be made at the beginning of twelve months period which the business projects to start making taxable supplies. It is clear that a properly functioning VAT system is a coherent interplay of input and output tax at different stages of the value chain ending with a final consumer. Claiming input tax without the corresponding remission of output tax distorts the system and results in businesses funding their operations through VAT.

Safeguards Against Loss of Revenue

23. There are some safeguards that are built into section 17 to protect revenue and guard against abuses such as those highlighted above. Section 17 (8) provides that the Commissioner shall register a person who applies for registration in accordance with subsection (1), (3), or (6) and issue to the person a value added tax registration certificate unless the Commissioner is satisfied that the person is not eligible to apply for registration for the purposes of the Act. This provision allows the Commissioner to

consider the application for registration and register such a person having been satisfied that a person is eligible for registration or refuse to register him if not eligible for registration. It appears that the practice in the past has been to automatically register every client who applied for registration without the necessary scrutiny.

24. Section 17 (9) provides that a value added tax registration certificate issued under this section shall state the name and other relevant details of the vendor, the nature of the vendor's trading activities, *the date on which the registration takes effect*, the taxpayer identification number of the vendor, and any other matters as the Commissioner may prescribe. This provision effectively says that the Commissioner is empowered to prescribe dates of effective registration, which is something that can be determined for every new registrant. Indeed subsection 11 states that registration under section 17 takes effect from the date of registration as specified in the value added tax registration certificate or *such later date as the Commissioner may determine*.

25. Equally, as a means of guarding against revenue loss the Commissioner may set out other terms and conditions in the registration certificate aimed at ensuring final consumers of goods and services do not misuse section 17(1) (b) by applying for registration while there are no reasonable prospects of them reaching registration threshold.

Conclusion and Recommendations

26. It has been established that VAT is meant to work as a system where taxable persons would charge the appropriate rates on the taxable value of goods and services and be entitled to deduct VAT paid in the process of making those taxable supplies. Therefore claiming credits for input without making taxable supplies outside the limits of the law is not allowed.

27. The law, specifically section 17 read holistically, provides safeguards that can be used to minimise revenue loss through fraudulent claims made by vendors who never intended to make any taxable supplies within the prescribed timelines. It is submitted that these safeguards should be used immediately. The safeguards are namely carefully assessing each new application for registration as a vendor to ensure that only those who qualify

are registered, quickly deregistering vendors who were not making taxable supplies and including appropriate conditions to every registration made to ensure minimal revenue loss.