

Responses to questionnaire: Countries experience regarding BEPS issues

1. How does base erosion and profit shifting affect your country?

Answers

BEPS directly affects our tax base. We do not get to collect right amount of tax on some of the transactions by MNEs due to engaging in avoidance schemes. It also undermines our tax system in that it puts burden of tax on the compliant Taxpayers. Lesotho, due to its geographical structure is completely surrounded by South Africa and as such the country imports capital and most companies in the country are foreign owned. It is worth noting that the income tax rates in Lesotho are very high compared to other countries in the region. Consequently, the companies operating in the country engage in serious tax planning to avoid paying the relevant taxes in Lesotho. This has a high negative impact on the domestic revenues of the country.

2. If you are affected by base erosion and profit shifting, what are the most common practices or structures used in your country or region, and the responses to them?

The common factors are practiced around the following areas:

Management fees, inter-company loans, staff/experts secondments, interest and royalties.

The common response is the audit process, though it must be indicated that the skills to audit some of the highly specialized sectors are limited. The aids to the audit process are, domestic tax laws and double taxation agreements wherein in other cases withholding tax will be charged on these transactions, as well as to determine what amount of expenditure will be allowed as a deduction being management fees, interest or royalties.

3. When you consider the MNEs activity in your country, how do you judge whether the MNE has reported an appropriate profit in your jurisdiction?

We do tax audits based on the risks as would be spotted when the MNEs file their tax returns. We would specifically look at the cross border transactions and confirm whether such were declared and recorded correctly for tax purposes. Also during the audit process by comparing profits reported by the similar businesses and this usually give some idea as to whether the respective MNE has

reported appropriate amount of profit. However as indicated, the audit skills herein can do with some improvement.

4. What main obstacles have you encountered in assessing whether the appropriate amount of profit is reported in your jurisdiction and in ensuring that the tax is paid on such profit?

The Subcommittee have identified a number of actions in the Action Plan that impact on taxation in the country where the income is earned (source country), as opposed to taxation in the country in which the MNE is headquartered (the residence country), or seek to improve transparency between MNE's and revenue authorities as being particularly important to many developing countries (while recognising that there will be particular differences between such countries). These are:

- **Action 4 – Limit base erosion via interest deductions and other financial payments:**
- **Action 6 – Prevent Treaty Abuse:**
- **Action 8 – Assure that transfer pricing outcomes are in line with value creation:**
- **Action 9 – Assure that transfer pricing outcomes are in line with value creation: risks and capital**
- **Action 10 - Assure that transfer pricing outcomes are in line with value creation with reference to other high risk transactions(in particular management fees)**
- **Action 11 – Establish methodologies to collect and analyse data on BEPS and the actions to address it**
- **Action 12 – Require taxpayers disclose their aggressive tax planning arrangement**
- **Action 13 – Re-examine transfer pricing documentation**

The main obstacles are always around:

- Lack of voluntary disclosure by MNEs,
- No responsible personnel to discuss the tax issues of the MNE as they are always abroad. There will only be a branch manager at the branch or subsidiary office but who in most cases would not answer any tax related question nor make commits related thereto;

- MNEs doing their reporting on the basis of the tax laws of the Head Office as opposed to the tax laws where the branch/ subsidiary is located (Lesotho).
- In most cases the records of MNE's are kept abroad whereas the law in Lesotho requires that records be kept in Lesotho. This normally creates difficulties wherein the auditors are forced to limited information available or raise estimated assessment ;
- Where MNE's provide information, it is usually not provided on time
- There is lack of exchange of information between Lesotho and countries where MNE's head offices are situated;
- Limited tax audit skills on the part of our Auditors.

5. Do you agree that these are particularly important priorities for developing countries?

Yes. These actions would go a long way in assisting developing countries to deal with BEPS issues.

6. Which of these OECD's Action points do you see as being most important for your country, and do you see that priority changing over time?

Action 4, 10, 12 and 13 would be most important and for a long time these would be priority areas for us if we were seriously to deal with BEPS issues. These priorities will probably change with time as new cases emerge and when the country is in a better position to handle problems related to them.

7. Are there other Action Points currently in the Action Plan but not listed above that you would include as being the most important for developing countries

Action 1 and action 7.

8. Having considered the issues outlined in the Action Plan and the proposed approaches to addressing them (including domestic legislation, bilateral treaties and possible multilateral treaty) do you believe there are other approaches to addressing the practices that might be more effective at the policy or practical levels instead of, or alongside such actions, for your country?

There would be need for technical assistance and capacity building assistance. In particular, it would be very important for Lesotho to get assisted on tax policy matters especially in how to influence a strong tax policy view, i.e. how to get political buy-in when it comes to reducing unnecessary tax incentives.

9. Having considered the issues outlined in the Action Plan, are there other base erosion and profit shifting issues in the broad sense that you consider may deserve consideration by international organizations such as the UN and OECD.

Capital gains taxation generally, the idea being to ensure that there is more source taxation.

10. Do you want to be kept informed on the Subcommittee's work on base erosion and profit shifting issues for developing countries and related work of the UN Committee of Experts on International Cooperation in Tax Matters.

Yes.