

## BOTSWANA INTERNATIONAL FINANCIAL SERVICES CENTRE

### BACKGROUND

Botswana created an International Financial Services Centre (IFSC) with effect from 1 July 1999 by means of various amendments to the Income Tax Act 1995.

It has not been the intention to create a tax haven in Botswana or to be considered as engaging in harmful preferential tax practices. Instead legislation has been introduced to create the fiscal and regulatory environment necessary to make Botswana an attractive location from which a wide range of financial services can be provided to non-residents and in currencies other than the Pula.

### QUALIFICATION AS AN IFSC COMPANY

In order to qualify as an IFSC company the company must:

1. Carry on approved financial operations;
2. With person not resident in Botswana or a resident company under the same management and;
3. Be issued with a tax certificate by the Minister of Finance.

Qualifying companies must only transact business outside of Botswana and in currencies other than the Botswana Pula. This does not preclude an IFSC company from settling its local obligations- e.g. rent, wages, electricity etc. – in Botswana Pula. An IFSC company can, however, hold shares in a subsidiary company incorporated and operating in Botswana.

### APPROVED FINANCIAL OPERATIONS

- Banking and financing operations transacted in foreign currency;
- The broking and trading of securities denominated in foreign currency;
- Investment advice;
- Management and custodial functions in relation to collective investment schemes
- Insurance and related activities;
- Registrars and transfer agency services;
- Exploitation of intellectual property;
- Development and supply of computer software for use in the provision of services described above;
- Accounting and financial administration;
- Other operations that the Minister may declare by order from time to time to be approved financial operations for the purposes of the IFSC legislation.

## TAX CERTIFICATES

Applications for IFSC status are dealt with by a Certification Committee who shall make recommendations to the Minister of Finance for the issue of a tax certificate. A company to whom a tax certificate is issued is an IFSC company as defined and the activities specified in the certificate are approved financial operations as defined. Once a certificate has been issued it is valid until 31 December 2020.

In order to obtain a tax certificate the applicant company must be in possession of a banking licence or a letter of exemption issued under the Bank of Botswana Act or be registered under the Insurance Industry Act. It is anticipated that all companies which are not banks, insurers, insurance brokers or insurance agents will receive a letter of exemption from the Bank of Botswana.

A tax certificate issued to an IFSC company entitles not only that company to carry on the approved financial operations but allows such operations to be carried out through a wholly owned subsidiary.

In considering an application for a tax certificate the certification committee shall have regard to:

- The number of Botswana citizens who will be employed in relation to the approved operation and the capacities in which they will be employed;
- The facilities proposed for the training and imparting of skills to Botswana citizens;
- Provisions made for the eventual replacement of non-citizen employees by Botswana citizens and
- Provisions made for the participation by Botswana citizens in the management of the business.

A tax certificate that has been issued can be revoked by the Minister of Finance if:

1. The company has ceased to carry on business;
2. The company is in breach of any condition laid down by the Minister;
3. The licence granted under the Bank of Botswana Act or the Insurance Industry Act has been cancelled;
4. The company has carried on activities that have had or may have an adverse effect on the IFSC;
5. A change in ownership since the grant of a certificate without prior written approval of the Minister (a change in ownership is defined as 25% or more of the share capital);
6. The company has carried on business with persons who are resident in Botswana and are not IFSC companies.

## TAXATION OF IFSC COMPANIES

### Tax Rates

The tax rate of an IFSC company, which is granted a tax certificate, is 15%. This rate is guaranteed as a maximum rate up to 31 December 2020. A lower rate is, however, not precluded.

A tax rate of 15% puts an IFSC company on the same basis as a manufacturing company in Botswana, which is also taxed at 15%. It is believed that a tax rate of 15% is acceptable to the international community and is not considered to be engaging in harmful preferential tax practices.

### Gross Income of an IFSC

The gross income of an IFSC company shall be the total amount whether in cash or otherwise, accrued or deemed to have been accrued to it in that tax year from all sources both inside and outside Botswana, but shall not include any amount of a capital nature, except the to extent specified in the Income Tax Act.

Accordingly an IFSC company is taxed on a worldwide basis (other than income in a qualifying foreign branch or a foreign participation, which is specifically exempt) but credit is given for any foreign tax suffered

Specified foreign exchange gains shall be included in the gross income of the IFSC company, provided the gain has been credited in the profit and loss account of the company under a commercially recognised system of accounting. A "specified foreign exchange gain" means a gain whether realised or unrealised, that results directly from a change in a rate of exchange and is attributable to a relevant asset, liability or contract.

### Exempt Income of an IFSC

The income of a qualifying branch of an IFSC company is exempt from tax in Botswana. A qualifying branch is one through which the company carries on business outside of Botswana.

Any dividends received by an IFSC company in respect of a qualifying foreign participation are exempt from tax.

A "qualifying foreign participation" means a participation held by an international financial services centre company in a company which is not resident in Botswana, where the IFSC company controls either directly or indirectly, alone or with connected persons, 25% or more of the share capital including 25% or more of the voting rights of the non resident company.

Capital gains arising on the disposal of a qualifying foreign participation are exempt from capital gains tax in Botswana.

#### Allowable Deduction of an IFSC

The normal rules relating to deductions continue to apply except that certain specific deductions only apply to IFSC companies.

A deduction is allowed for the amount of any specified foreign exchange loss, provided the loss has been debited in the profit and loss account of the IFSC company under a commercially recognised system of accounting. A "specified foreign exchange loss" means a loss whether realised or unrealised that results directly from a change in a rate of exchange and is attributable to a relevant asset, liability or a relevant contract.

Foreign debt interest of an IFSC company is an allowable deduction for a particular tax year. However, if at any time during that tax year, the total foreign debt of the taxpayer exceeds the foreign equity product for that year, then the amount of foreign debt interest allowable is ascertained in accordance with the following formula:

$$\text{Non deductible portion of the foreign debt interest} = I \times \frac{A}{B} \times \frac{C}{100}$$

Where:-

- A is the amount of the excess of the total foreign debt over the foreign equity product;
- B is the total foreign debt;
- C is the number of days in that tax year during which the total foreign debt exceeded the foreign equity product by that amount; and
- I is the foreign debt interest,

The foreign equity product is the foreign equity multiplied by the maximum number of times that the foreign debt is divisible by the foreign equity. Application can be made to the Commissioner of Taxes to fix such multiple but in the absence of an application the multiple shall be 12 in the case of banks and 3 in all other cases.

#### Tax credits

Credit can be claimed in respect of foreign taxes suffered arising on gross income accruing to the IFSC company from a source outside Botswana. A credit can be claimed irrespective of whether or not a double taxation agreement exists with that country.

The credit available for foreign tax shall be restricted according to the following formula:

$$\text{Tax payable in Botswana} \times \frac{\text{Gross income from foreign source}}{\text{Gross income}}$$

provided that the credit will be restricted to the tax payable in the foreign country if less than the amount determined by the above formula.

#### Exemption from Withholding Taxes

An IFSC company is exempt from paying withholding tax on any payment of interest, royalty or management fee (whether to a resident or a non-resident). Also an IFSC company is exempt from paying withholding tax on the payment of a dividend to a non-resident, an IFSC company or a collective investment undertaking. However, a payment of a dividend to resident of Botswana is not exempt from withholding tax and any tax withheld is a final charge to tax of the resident shareholder.

Inbound dividends are specifically exempt in the hands of an IFSC company and are accordingly not liable to the normal 15% tax on such dividends. Where a dividend is paid by a wholly owned Botswana subsidiary to its IFSC parent company the IFSC company is treated as a non-resident and withholding tax is payable.

#### Accounts

The accounts of an IFSC company may be prepared in any currency but the return of taxable income must be translated into Botswana Pula at the average foreign exchange rate for the period.

#### Collective Investment Undertakings

A Collective Investment Undertaking (CIU), which includes unit trusts and mutual funds, is defined as a company for tax purposes.

A CIU that is managed by an IFSC company is exempt from tax provided that all the unit holders in the CIU are persons resident outside Botswana. If any of the unit holders are residents of Botswana then the exemption is lost.

## BECOMING AN IFSC COMPANY

### The Application

The Income Tax (Amendment) Act 1999 established the Certification Committee to consider applications and issue approvals to become an IFSC company. Upon the Committee's recommendation the Minister of Financial & Development Planning will issue a tax certificate to the IFSC company certifying that the activities are approved financial operations.

Applications are to include the following details:

- Name of the project
- The principals background information:
  - Business activities
  - Length of time it has been established
  - Financial standing
  - Performance record
  - History and ownership
  - Most recent audited
- The IFSC project
  - Objectives of the project
  - Proposed activities of the project
  - Business plan
- Employment
  - Employment forecast over a three-year period
  - Breakdown of citizens and expatriates, by skill range
- Markets
  - Information on the proposed market
  - Market size estimates
  - Summary of marketing plans
- Financial Projections
  - Projection provided for 3 years
  - To include Balance Sheets, Profit and Loss and Cash Flow Statements
- Benefits to Botswana
  - Indication of how the project will benefit the Botswana IFSC.

## Approval Criteria

To qualify for incentives the following criteria must be met:

- The project is to provide financial services in the form of one of the following:
  - Banking and financing operations transacted in foreign currency;
  - The broking and trading of securities denominated in foreign currency;
  - Investment advice;
  - Management and custodial functions in relation to collective investment schemes
  - Insurance and related activities;
  - Registrars and transfer agency services;
  - Exploitation of intellectual property;
  - Development and supply of computer software for use in the provision of services described above;
  - Accounting and financial administration;
  - Other operations that the Minister may declare by order from time to time to be approved financial operations for the purposes of the IFSC legislation.
  
- The operations must be carried on with persons not resident in Botswana and in currencies other than Pula
- The IFSC company must comply with the reporting requirements in the Bank Of Botswana Act.

In consideration of an application the Committee shall have regard to:

- The number of Botswana citizens who will be employed in relation to the approved operation and the capacities in which they will be employed;
- Facilities proposed for the training and imparting of skills to Botswana citizens;
- Provisions made for the eventual replacement of non resident employees by Botswana citizens; and
- Provision made for the participation by Botswana citizens in the management of the business.

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N.B

This information represents a concise summary of the legislation. Whilst care has been taken to ensure the information is accurate, it should not be used or relied upon as a substitute for detailed advice.

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