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No 50% gratuity tax exemption for some directors in Botswana

Whilst the Income Tax Act (hereinafter referred to as the ITA or Act) exempts 50% of gratuity payments made to employees from tax, some directors do not get to enjoy the said exemption. Gratuity is an amount that an employer pays his employee in return for services offered by him to the business or organisation in recognition of a period of continuous employment. It is common knowledge that some directors are also shareholders of companies they work for, therefore the word employee above also includes a working director.

Just like any ordinary employee, these directors or shareholders are also paid gratuity for the fact that they are employees. Such shareholders/directors are given a special term in the ITA, being 'participator,' which is defined as a person who holds at least 5% of ordinary shares in a private resident company, also termed a close company. It is such working directors who own more than 5% of shares in companies they run that this write up will be focusing on. In this article, words importing the masculine shall be deemed to include the feminine.

More on tax

Going back to the issue at hand, the ITA accords 50% gratuity tax exemption to employees, except for working directors who are participators of the close companies they work for. These shareholders get to suffer tax on the whole amount of gratuity so paid to them. You might be wondering why this is so. We believe that this exclusion was the taxman's way of curbing tax leakages between related parties in order to protect revenue. It doesn't end there! The ITA deems the gratuity amounts paid to such directors as a dividend payment, which triggers withholding tax (WHT) on the hands of the shareholder.

The WHT rate applicable is as provided in the Act, which is now 10% on payments to residents. The close company is also not spared as it has to account for the deemed WHT. Per the Act, failure to deduct WHT from the dividend attracts 200% penalties. The only time this gratuity gets to duck the taxation is when the Commissioner of Taxes is satisfied that the amount so payable is a cost of travel reasonably paid to a participator not more than once in a period of two years.

Tax planning

The planning avenue is for the said directors to be paid severance instead of a gratuity as the Income Tax Act doesn't preclude such payments. The good thing with such severance payments is that they are also subject to the 50% tax exemption just like the gratuity. Therefore, the prohibition brought about by the Income Tax Act may be avoided through the severance pay route.

Conclusion

One can tell from the above that the tax laws generally have special clauses or restrictions for related parties and they try to counter tax losses due to the said relationships. That being the case, if you have related party transactions which are not at arms' length or do not know which transactions are prohibited by the tax laws, you may as well contact us for tax guidance, at a small fee, of course.

Well, folks, we hope that was insightful. As us the two Yours Truly say goodbye, remember to pay Caesar what belongs to him. If you want to consult, join our free Tax WhatsApp group or to know about our 9 Tax e-books, send a text to +267 7181 5836 or email us at jhore@aupracontax.co.bw. You can read more tax articles on our website, www.aupracontax.co.bw under the 'Tax articles' tab.