



Department of Taxes, Government of Botswana

DEPARTMENTAL GUIDANCE NOTE ON TAX DEDUCTIBLE FROM PAYMENTS UNDER CONTRACTS RELATING TO CONSTRUCTION OPERATIONS – (Section 56 and Sixth Schedule to the Income Tax Act, 1995)

1. INTRODUCTION

1.1. Purpose of this DGN:

This Departmental Guidance Note is issued to explain the provisions and procedure relating to deduction of tax from contracts relating to construction operations. The purpose of this Note is to enumerate and explain the respective obligations of the persons entering into a contract relating to construction operation and the procedure to be followed to comply with those obligations under the Income Tax Act 1995.

1.2. Relevant provisions of law:

The law relating to deduction of tax in the case of contracts relating to construction operations is enshrined in Section 56 and the Sixth Schedule of the Income Tax Act 1995. Section 56 which lays down the substantive law in this regard, reads as under:

“(1) Every person who makes any payment to any person under a contract relating to construction operations shall deduct tax from such payment, in accordance with and in the manner specified in the Sixth Schedule and shall carry out such other obligations as are imposed by that Schedule.

Provided that this section shall not apply to contracts with a value less than P2,000,000 being executed by construction companies which fall under categories OC, A and B of the Central Tender Board.¹

The amount of tax to be deducted and the relevant procedure is laid down in the Sixth Schedule as amended by the Income Tax (Amendment) Act 2001.

¹ New sub section 1 inserted by Income Tax Amendment Act 2001

1.3. Registration requirements of persons covered :

The persons covered under the provisions referred to in 1.2 above are

- a. Every person who makes any payment to any person under a contract relating to construction operations; and
- b. Every person who receives any payment under a contract relating to construction operations.

Every person responsible for making payments under contracts relating to construction operations must register with the Commissioner of Taxes for the purposes of withholding tax.

Every person receiving payment under a contract relating to construction operations must register with the Commissioner of Taxes if he or the company is not already registered as a taxpayer.

The relevant form is ITRG 1 which can be obtained from the Central Processing Unit of the Commissioner of Taxes. (Phone: 300723/375988).

2. RELEVANT CONTRACTS

2.1 Contracts covered:

The contracts covered under the provisions of section 56 and the Sixth Schedule of the Income Tax Act are "contracts relating to construction operations".

2.2 Contracts relating to Construction operations:

Though contracts relating to construction operations have not been defined under the Income Tax Act, they include in particular, any contracts or subcontracts where either the entire or part of the work includes activities such as erection, demolition, installation or assembly, site preparation, drilling, road works and any services such as architectural and engineering services related to such activities. A contract where supply of services is incidental to construction operations will be deemed to be a construction contract.

2.3 Exempted contracts:

Provisions of Section 56 and the Sixth Schedule are not applicable in the following situations:

- (i) If the person executing the contract is classified as OC , A or B by the Central Tender Board, **and** the value of such a contract is less than P 2 Million. For exemption, both the conditions must be fulfilled simultaneously.
- (ii) If the person executing the contract is exempt under a Double Taxation Avoidance Agreement with another country (paragraph (xxiv), Part II of Second Schedule).Currently, Botswana has Double Taxation Avoidance Agreements with the UK, South Africa, Sweden, Mauritius and France.
- (iii) If exemption is granted by virtue of an agreement entered into with the Minister and approved by a resolution of the National Assembly(Section 53 and paragraph (xxiv) Part II of Second Schedule).
- (iv) Where business is carried on or services are rendered under an agreement for provision of technical assistance with the Government (Paragraph (xix) Part II of Second Schedule). The exemption must be approved by the Minister under a notice in writing to the Commissioner of Taxes. This exemption will apply only to the contracts between the Government of Botswana and the Government or government agency of another country.
- (v) Where exemption is granted under a tax certificate issued by the Commissioner of Taxes under paragraph 3(3) of the Sixth Schedule of the Income Tax Act.

In cases of claim of exemption under (i) above, the person responsible for payment should ensure that the person executing the contract is actually registered under categories A , B or OC with the Central Tender Board with reference to the certificate issued by the Central Tender Board.

Wherever exemption is claimed by the person executing the contract , the person responsible for payment shall allow exemption only when a ruling to that effect is issued by the Commissioner of Taxes. The payer must verify the claim of exemption with the Commissioner of Taxes if the person executing the contract fails to produce the ruling from the Commissioner of Taxes.

3. NOTIFICATION REQUIREMENTS :

Every person entering into contracts relating to construction operations where the total amount of payments expected to be made under a contract or series of contracts exceeds P5 000.00., shall notify in writing to the Commissioner of Taxes, Private Bag 0013, Gaborone of-

- (a) the nature of the work;
- (b) the likely duration of the contract;
- (c) name and address of the contractor and Taxpayer identification number and
- (d) the total amount payable under the contract.

This notification is to be given in writing within 30 days of the date of entering into the contract and failure to notify is subject to penalty. ***The Commissioner of Taxes has prescribed Form ITW 1A for use by persons entering into relevant contracts.***

4. WITHHOLDING REQUIREMENTS

4.1. Amount to be withheld

From 1 July 2001, any person making any payment under a contract relating to construction operations shall deduct tax @ of 3% from all payments made under such a contract, irrespective of whether the person receiving payment is a resident or a non-resident.

4.2. Payment to the Commissioner

The tax withheld is to be paid over to the Commissioner by the 15th of the month following the month in which the tax was withheld. Delay in paying over the tax creates a liability to charge of interest besides penalty under section 117 (7) and prosecution under section 125 of the Income Tax Act.

4.3. Certificate of Deduction

Every person who deducts any tax @ 3% from payments to be made under contracts relating to construction operations must within 15 days issue a tax deduction certificate to the person whom payment was made , in the prescribed Form ITW 9 after getting it duly approved by the office of the Commissioner of Taxes.

Form ITW 9s are available with the Withholding Taxes Division of the Department (Phone No 3914859), which may be obtained by the payer in advance to facilitate handing over of tax deduction certificates to the payee within the prescribed time of 15 days.

4.4. Credit for the tax withheld

The tax withheld from payments made under a contract relating to construction operations is not a final tax. The amount of tax withheld and paid over to the Commissioner will be available as a credit against the self assessment tax liability in the case of companies. Other taxpayers not covered under the self assessment system can claim the amount of tax withheld as a credit against their tax liability by submitting a tax return for the relevant tax year. Such credit can be claimed by enclosing with the tax return, the tax deduction certificate in duly approved Form ITW9 (i.e. duly stamped by the Commissioner of Taxes).

5. EXCLUSION/EXEMPTION FROM WITHHOLDING IN CERTAIN CASES:

5.1. Exclusion of amounts to be paid to sub-contractors

The Income Tax (Amendment) Act 2001 has amended the provisions of the Sixth Schedule. Under the amended provisions, when a person who is in receipt of payments which are subject to tax deduction at 3% under sixth schedule, engages sub contractors for executing part of the contract work, he may apply (in form ITW 22) to the Commissioner to issue a directive to his principal to exclude that portion of the payments received by him which he has applied or intends to apply for payments to specified sub contractors from deduction of tax at 3%. The Commissioner on being satisfied with his application, may issue the directive to his principal to deduct tax on only so much of the payments under the contract remaining after deduction of payments to subcontractors as given in the application furnished by the contractor.

The following **illustration** will explain this provision contained in sub-paragraph (2) of paragraph 3 of the Sixth Schedule.

Total payments receivable by the Contractor – P10 million

Payments to be made by the contractor to sub contractors as per application furnished by him in Form ITW.22 - P2 million

Commissioner may issue directive that tax be deducted from only P8 million i.e. total payments as reduced by payments to be made to sub contractors (P10 million less P2 million = P8 million) instead of total payment of P10 million. The contractor, in turn will deduct tax at 3% on payments to be made by him to sub-contractors. In a case where the sub-contract is exempt under proviso to section 56 (category OC, A or B contract and the value of contract is less than P 2 Million), no tax will be deducted.

5.2. Variation / Exemption from withholding on the basis of compliance history

Under paragraph 3(3) of the Sixth Schedule, a person due to receive any payment under a contract relating to construction operations may also apply in Form ITW.22 for a tax certificate. This tax certificate is issued only after the Commissioner has scrutinized the tax compliance history of the taxpayer. If the Commissioner is satisfied that the taxpayer is registered with the Commissioner of Taxes and has a very good history of compliance with various tax obligations, including his obligations relating to self-assessment tax and withholding taxes, he may issue a tax certificate. The tax certificate may either exempt the payments made to such contractor from withholding taxes under Sixth schedule or may vary the amount of tax to be withheld from the payments to be made to him.

5.3. Exclusion and Exemption are not mutually exclusive

The provisions discussed at 5.1 and 5.2 above are not mutually exclusive. A person may apply both for exclusion, for the purpose of tax deduction, from payments received

by him of payments in turn made by him to sub contractors and for a tax certificate based on compliance history. However, for the purpose of administrative convenience, the contractor is advised to make a single application in respect of a contract. This application (Form ITW.22) combines the provisions of sub paragraphs (2) and (3) of paragraph 3 of the Sixth Schedule.

5.4. Application for exclusion /exemption is to be made for each tax year

Since the tax withheld under the provision of section 56 is to be set off against the final tax liability of the respective tax year, the application for exclusion or variation is to be made for each tax year separately.

6. LIABILITY IN THE EVENT OF NON-DEDUCTION AND /OR NON-PAYMENT

6.1 Personal liability of the payer:

The person making payments under a contract to which section 56 applies shall be personally liable for the tax to be withheld and in case of his failure to deduct tax, the tax will be recoverable from him.

6.2. Non-deduction and/or non-payment are punishable:

Failure to deduct tax and pay the same and maintain record for inspection by the Commissioner shall, besides inviting interest under Section 100 of the Income Tax Act, also attract penalty under sections 117(6) and 117(7) of the Income Tax Act. Where the failure to deduct is willful with the intent to evade tax, the person responsible for deducting may also be prosecuted under Section 125 and 127 of the Income Tax Act.

7. CONCLUSION

7.1. Payer's Responsibilities

It is the responsibility of the person making the payments under a contract relating to construction operations to deduct tax @ 3% in terms of section 56 and in accordance with the provisions of the Sixth Schedule of the Income Tax Act. The person withholding tax on payment for such a contract relating to construction operations shall do the following:

- (i) Furnish information on such payments in terms of paragraph 1 of the Sixth Schedule.
- (ii) Deduct tax and pay the same within 15 days of such deduction to the Commissioner of Taxes. Taxes withheld and paid by him will be recorded in ITW.7, the statement of monthly tax deduction and payments.

- (iii) Exempt from deduction of tax only if satisfied that the payee falls within categories OC, A and B of the Central Tender Board and the value of contract executed by the payee is less than P2 million.
- (iv) Insist on furnishing a exclusion or exemption certificate from the Commissioner of Taxes, where the payee claims such exclusion or exemption from withholding tax.
- (v) Furnish to the payee certificate of such deduction in ITW.9 with the stamp of the Commissioner of Taxes within 15 days of the deduction. The white copy of ITC9 shall be furnished to the payee, the green copy will be filed with the Commissioner and the pink will be retained by the payer.
- (vi) Furnish annual return of withholding taxes in Form ITW.10 to the Commissioner within 31 days of the end of the relevant tax year.
- (vii) Maintain record of all payments and produce the same for inspection by the Commissioner whenever required by him to do so.

7.2. Payee's responsibilities:

The person receiving payment under a contract relating to construction operation shall do the following:

- (a) Furnish evidence to the payer for supporting the claim that the relevant contract is exempt from withholding due to classification as OC, A or B by the Central Tender Board.
- (b) Apply to the Commissioner of Taxes in Form ITW22 for claiming exclusion or exemption from withholding and once received the ruling / tax certificate , furnish the same to the payer. The exclusion /exemption will be granted tax year wise and therefore application for the same is to be made for each tax year separately.
- (c) Ask the payer to hand over a tax deduction certificate in Form ITW9, duly approved by the Commissioner of Taxes . Do not accept the certificates unless they are approved by the Commissioner of Taxes.
- (d) Enclose the tax deduction certificate in Form ITW 9 with the tax return for the relevant tax year for claiming credit for the tax withheld .

7.3. Assistance available

In need of any clarification, please contact the offices of the Commissioner of Taxes at the addresses and phone numbers given below:

Department of Taxes
Withholding Division
Private Bag 00207
Gaborone

Phone: 3914859
Fax: 581729

Department of Taxes
Collection Division
Private Bag 38
Francistown

Phone: 2412734
Fax: 2414267

Department of Taxes
Collection Division
Private Bag 13
Selebi-Phikwe

Phone: 810795
Fax: 814862

Central Processing Unit
3rd Floor, BSB Building
Opp: BBS Mall
Private Bag 00171
Gaborone.

Phone: 3900723
Fax: 3900778

Commissioner of Taxes
Private Bag 0013
Gaborone

Phone: 3952444
Fax: 3953101

8. **WITHDRAWAL OF EARLIER DGNs**

All earlier Departmental Guidance Notes on the subject covered by this DGN are hereby withdrawn.

12 November 2002



**Commissioner of Taxes
Private Bag 0013, Gaborone**