The Scope of Government Revenue Mobilization in Lesotho

By Selloane Khoabane

Abstract

SACU REVENUE revenue has been the major source of government revenue averaging about 26.0 per cent of GDP between 2000 and 2015. However, it has been characterized by a lot of volatility though tilted more on a downward trajectory. The future trend in SACU revenue is expected to be downwards in line with global trends on customs revenue as a result of trade liberalization. Other sources of revenue, particularly tax revenue have also been sluggish. These have raised the need for alternative sources of revenue for the Government of Lesotho (GoL). Thus this paper identifies possible additional domestic revenue mobilization avenues for Lesotho. This is achieved by comparing Lesotho's tax rates and rates on non-tax revenue sources with those of other SACU member countries and other selected African countries. The areas identified include increasing tax rates on petrol and diesel, mobile telecommunication services. New taxes could also be introduced on alcohol and tobacco, sugar sweetened beverages and plastic bags. Contracts with diamond mining companies could be renegotiated to raise more revenue from the sector. Implementation of revenue raising measures that were proposed to GoL before also needs to be expedited. Other existing taxes such as the gaming levy, which have not been reviewed in a long time, should also be considered. While out of line with the scope of this paper, improvements in government spending efficiency, containing and streamlining public spending and implementation of policies and strategies for enhancing private sector growth could maximize the benefits of the proposed tax revisions.

Keywords: government revenue, customs revenue, taxation, government equity
JEL classification: E62, H20, H27

[1] Selloane Khoabane, Principal Economist – Studies and Analysis Division, Department of Research, Central Bank of Lesotho, email: skhoabane@centralbank.org.ls, Tel: (+266) 2223 2062.

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Selloane Khoabane[1]

1 INTRODUCTION

LESOTHO IS A MEMBER of the Southern African Customs Union (SACU) with Botswana, Namibia, South Africa (SA) and Swaziland. As a customs union, SACU has the following characteristics: first, there is a common external tariff on all goods imported into the union from the rest of the world. Second, the SACU Agreement allows for free movement of SACU manufactured goods within SACU countries under duty and quota free terms. Third is the sharing of revenue collected from the common customs revenue pool through an agreed revenue sharing formula.

The importance of SACU revenue to the Government of Lesotho (GoL) cannot be overemphasized. For a long time, SACU revenue has been the largest source of GOL's revenue accounting for more than half of total revenue and grants. As shown in the Appendix, SACU revenue accounted for 50.9 per cent of total annual revenue, on average from 2005 to 2010. It fell to an annual average of 40.2 per cent as a share of total revenue from 2010 to 2015. As depicted in Figure 1, SACU revenue has been the major source of government revenue averaging about 26.0 per cent of GDP between 2000 and 2015. However, a lot of volatility in SACU revenue was observed during the course of this period. 2000 to 2005 was a period of relative stability with SACU revenue recording an average of 22.2 per cent of GDP with a trough of 19.6 per cent of GDP in 2003 and a peak of 25.3 per cent of GDP in 2005. This was followed by increases up to a peak of 42.3 per cent of GDP in 2007. Thereafter it went on a downward trend to a historical low of 14.0 per cent of GDP in 2011, averaging 23.8 per cent of GDP in 2010 to 2015. In line with global trends on customs revenues, the expected future trajectory of SACU revenue is highly likely downwards as a result of trade liberalization. Over

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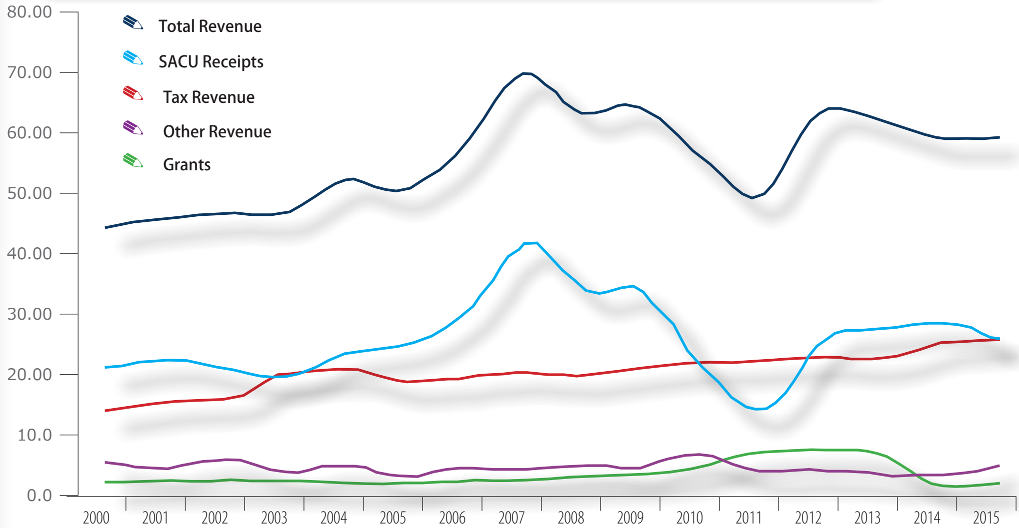
the years, SACU has been engaging in free trade agreements with a number of countries and regions. For instance, the Free Trade Agreement (FTA) with the European Free Trade Association entered into force in 2008 and the Preferential Trade Agreement with the Southern Common Market, *Mercado Comun del Sur* (MERCOSUR) became operational in the first half of 2016, just to mention a few.

Figure 1 Lesotho Government Revenue and its Components (Per cent of GDP)



Source: Ministry of Finance and Central Bank of Lesotho

The second largest component of government revenue, tax revenue, has been stable albeit increasing sluggishly in recent years following the establishment of the Lesotho Revenue Authority (LRA) in 2003. Tax revenue increased from an average of 19.8 per cent of GDP between 2005 and 2009, to an average of 23.4 per cent of GDP between 2010 and 2015. The largest component of tax revenue, taxes on income and taxes on profits and capital gains, accounted for an average of 54.7 per cent of tax revenue between 2000 and 2015. The components of this category, personal income tax, company tax, withholding tax and fringe benefit tax, accounted for 33.2, 13.7, 7.5 and 0.3 per cent of tax revenue, respectively, on average from 2000 to 2015. Revenue from taxes on goods and services accounted for an average of 40.1 per cent of tax revenue from 2000 to 2015. The major component in this category with a contribution of 34.7 per cent of tax revenue was general sales tax (GST) revenue until 2003 and value added tax (VAT) thereafter. This was followed by excise taxes at an average share of 3.8 per cent. Excise taxes included motor vehicle assurance, oil levy, petroleum levy, road maintenance levy, gaming levy, motor vehicle licenses and other licenses. Under taxes on property was Rand compensation that the South African government pays the GoL for loss of seigniorage as a result of free circulation of the SA Rand in Lesotho as provided for under the Common Monetary Area (CMA) Agreement. The revenue accruing from stamp duty payments was negligible. The main contributor to other revenue was water royalties followed by dividends, which accounted for 4.2 per cent and 2.4 per cent of GDP, respectively, on average from 2000 to 2015. The other components of other revenue made individual contributions of less than 1.0 per cent to total revenue, on average, during the same period.

In light of the volatility in SACU revenue while other sources of revenue, particularly tax revenue exhibited sluggishness, the objective of this paper is to identify possible additional domestic revenue mobilization avenues for Lesotho. The potential room for Lesotho to raise more revenue is assessed by comparing Lesotho tax rates and rates on non-tax revenue sources with those of other SACU member countries and other selected African countries. The selection of comparator countries is largely based on data availability though with a preference for SACU member countries as they share similar characteristics with Lesotho.

The rest of the paper is organized as follows: Section 2 covers the literature review on different avenues for public revenue mobilization. Section 3 identifies potential revenue mobilization avenues for Lesotho and estimates the amount of potential revenue gains where data availability allowed and Section 4 concludes the paper and provides recommendations.

2 LITERATURE REVIEW

The importance of public revenue notwithstanding, it falls short of expenditure needs in many countries, especially developing countries. This calls for strategies to increase domestic revenue mobilization in such countries. According to Lagarde (2016) there is a pressing need to generate higher and more reliable revenue in many countries, although not necessarily for the same reason. Many developing countries are facing a dire need to raise more revenue from their own tax bases to, amongst other things, achieve the Millennium Development Goals, meet infrastructure needs and address climate challenges (IMF, 2011). There is evidence that trade taxes have declined in Africa due to trade liberalization, hence a need to replace them (Mubiru, 2010). According to Ebeke and Ehrhart (2010), Sub-Saharan Africa (SSA) is characterized by high tax revenue instability due to higher dependency on trade taxes and lower reliance on domestic indirect taxes. They also found some evidence that high volatility of tax revenue depresses public investment. Even though the evidence is scanty on the effects of trade taxes and tax volatility on growth, the findings of Wacziarg and Welch (2008) that trade liberalization fosters growth imply that lower reliance on trade taxes positively impacts growth. In addition, over reliance on one type of tax exposes a country to shocks to that source of revenue and if it is volatile, revenues are uncertain and volatile, stability of which could be achieved through a balanced mix of taxes (Mubiru, 2010).

A country's economic structure, history and tax structures of its neighboring countries are some of the factors that determine its taxes (Bird and Zolt, 2003). Other factors that are taken into consideration when choosing between different types of taxes are the characteristics of a good tax system such as fairness, the economic effects of different taxes in as far as they discourage economic activity and the administrative costs of tax revenue collection (Bird and Zolt, 2003). Gupta (2007) contends that the sectoral composition of output is an important determinant of revenue performance because some sectors of the economy are easier to tax than others. For example the findings of Tanzi (1981) reveal that mining and non-mineral export share have a positive effect on the tax ratio while Ghura (1998) concludes that tax revenue declines with the share of agriculture in output in SSA. It is on the basis of these that the literature identifies a number of taxation avenues that developing countries could exploit to increase sources of tax revenue and reduce volatility of tax revenue.

2.1 Petroleum Products

In many countries motorists are charged taxes on fuel as a means of generating public revenues and also to reduce the consumption of fossil fuels and greenhouse gas emissions to minimize their contribution to climate change and global warming. Hossain (2003) identifies taxes that can be charged on petroleum products as road user charges to address road damage externality, a tax to address environmental externality, a tax/ subsidy to reduce variability in price, a tax/ subsidy for distributional considerations and a tax for revenue purposes. According to Usui (2011) and UNDP (undated) taxation of gasoline has a number of advantages. First, it is relatively easy to administer with a minimum risk of avoidance or evasion. Second, it is admissible on a large tax base. Third, it is progressive because the richer households spend more on gasoline. Fourth the tax may reduce the negative externalities of gasoline consumption including traffic congestion, accidents and pollution. One of the shortcomings of this type of tax as identified by UNDP (undated) is that the revenues from it may decline as the price elasticity of fuel may increase in the longer term, very high tax rates can reduce consumption.

2.2 The Extractive Sector

The extractive sector in resource rich SSA could provide such countries with the opportunity to raise domestic funds to finance public goods and achieve their development goals (Stürmer and Bochholz, 2009). The resources and minerals rights are owned by governments, on behalf of their nations and they should be compensated for their extraction and the opportunity cost associated with their consumption (Manungo, 2013). Hence the resource rent principle that efficient output from minerals includes a producer surplus that should accrue to the owner of the asset, leaving an adequate rate of return to the producer to encourage investment (Commonwealth Secretariat and International Council on Mining and Metals, 2009).

Governments derive the resource rents through taxation. The revenue accruing to governments from taxing the extractive sector is a key component of its contribution to development (Commonwealth Secretariat and International Council on Mining and Metals, 2009). Furthermore, the design of minerals taxation policy requires trading off government objectives such as attracting investment, maximizing public revenues and enhancing the developmental impact of the mining sector. Stürmer and Bochholz (2009) contend that the minerals taxation system has to be distinct due to the special features of the extractive sector, including the size and timescale of investments and the instability of world market prices. Manungo (2013) is of the view that an effective tax regime for the extractive sector should yield maximum revenue to the state while also balancing the risk to the investor and offering the prospect of stability of contract terms.

Stürmer and Bochholz (2009), and Manungo (2013) identify the features of minerals taxation regimes in most countries. They include royalties, which are calculated on the basis of either the volume or value of production or exports. Their advantages are that they are relatively easy to apply and provide a stable source of revenue to government since production and sales normally vary less than profits. Nonetheless, they may be costly to producers, especially when world prices and profits are low, hence they may deter investments if very high. There is also windfall profit tax that is applied on above normal profits on the basis of a certain threshold such as a specific world market price level. The corporate income tax is payable on profits. It is not an easy tax to impose as profits have to be assessed and it is highly volatile. However, it protects investors from paying even when they are barely making profits or running losses. Sometimes governments hold equity shares in the mining industry with the objective of protecting national interests and maximizing state revenues. Critics of public ownership of equity in mining companies point out that it may expose government to costs relating to reinvestments and expansions of projects and give rise to conflict of interest as government is also expected to regulate the sector on environmental and social impacts. Other resource rents may include surface rent, licensing and registration fees.

2.3 Mobile Telecommunications Sector

The telecommunication sector, particularly the mobile phone sector has grown substantially in many countries and this represents a viable revenue raising mechanism due to the high frequency nature of its transactions (World Health Organization, 2010). For instance, the mobile industry contributed more than US$160.0 million to the budget of the government of the Democratic Republic of the Congo (DRC) and over 37.0 per cent of the revenue collected by the national tax collection agency in 2008 (Deloitte, 2015a).

The World Health Organization (WHO) advocates a consumption tax in the form of a levy on both voice and data use of mobile phones. However, taxing of mobile phone use is criticized on the grounds that it inhibits adoption of mobile technology, hence it is counter-productive. Therefore, an alternative is to tax companies that provide mobile services as in the case of Gabon, which implemented a levy on mobile phone companies. Initially this resulted in an increase in prices as the companies passed the tax to consumers. However, within a short time the companies absorbed the impact on their margins as competition between the major services providers pressured them to lower prices.

As evidenced by Jensen (2007), excise taxes on telecommunications could raise substantial revenues without discouraging use. For instance, according to Deloitte (2015a) the DRC applies a number of taxes on users of mobile phone services. These include VAT at 16.0 per cent on devices and SIM cards as well as VAT at the same rate and excise duty at 10.0 per cent on calls, SMSs and mobile broadband. In Ghana, Deloitte (2015b) identifies a number of taxes that mobile phone users are subject to. These include, VAT at 15.0 per cent, communications service tax at 6.0 per cent and the national insurance levy at 2.5 per cent, all of which are levied on calls, SMSs, data and airtime vouchers. Nonetheless, mobile phone use in both countries is on the rise. According to the International Telecommunications Union (ITU), in the DRC, the number of active mobile phone subscribers rose from 11.82 million in 2010 to 37.1 million in 2014. In Ghana, it rose from 17.4 million in 2010 to 30.4 million in 2014.

2.4 Alcohol and Tobacco

An increase in excise tax on alcohol and tobacco is justifiable on the grounds that it is a partial solution to public financial resources needs as well as health and social ills associated with their consumption (Moshoeshoe, 2012). This is further concurred with by the WHO (2010) in pointing out that there is ample room for increasing the levels of excise taxation on alcohol and tobacco in low income countries because demand for these products is price inelastic. It is estimated that an increase in the excise tax to 40.0 per cent of the retail price would reduce consumption by 18 per cent, which would still result in substantial excise revenues despite the resultant lower consumption. In Lesotho, there is also evidence that the demand for alcohol and tobacco are income inelastic with the income elasticity of alcohol estimated at 0.6553 and of tobacco at 0.3561 (Moshoeshoe, 2012). In the same token, in SA and in many other low income countries, there is also evidence that price elasticity of demand for cigarettes is around 0.6 per cent indicating that people reduce their consumption in response to a price increase despite the addictiveness of tobacco (Van Walbeek, 2012).

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2.5 Small/Informal Businesses

African economies are characterized by large numbers of small and micro businesses. However, according to IMF (2011), despite their high number, these businesses have very limited revenue potential. Efforts towards tax collection from these businesses have proved to be highly financially costly with poor revenue collection results (IMF, 2011). For instance, in Kenya, despite the large informal sector, estimated at 33.7 per cent of GDP, the presumptive tax of 3.0 per cent on gross turnover that targets small businesses has yielded very low revenue at an average of 0.1 per cent of total tax revenue (Maina, 2016). At this level, the yield is found to be far lower than the tax potential of the sector, which is estimated at 4.0 per cent of GDP. In Zimbabwe, it is estimated that informal sector presumptive taxes amounted to 0.45 per cent of total revenue in 2011 (Dube, 2014), which is also very low. The IMF contents that leaving the small businesses out of the tax net could undermine compliance of larger businesses and suggests that the small businesses could be subjected to a simple tax similar to a license fee.

2.6 Sugar Sweetened Beverages

Concerns over obesity and the high rates of chronic and non-communicable diseases including high blood pressure, heart diseases, type 2 diabetes and some forms of cancers have resulted in calls to tax sugar sweetened beverages (SSBs) which are high calorie and low-nutrient (Cawley and Frisvold (2015), Claro et al (2012) and National Treasury Department of South Africa (2016)). Cawley and Frisvold (2015) list the following countries that have recently levied taxes on SSBs (years in brackets); Mexico (2014), France (2012), Finland (2011), Hungary (2011), Nauru (2007), Fiji (2006) and Australia (2000). National Treasury Department of South Africa (2016) adds Denmark, Ireland, Mauritius and Norway to the list and points out that the United Kingdom and Thailand have announced their intention to introduce such taxes soon. In the SACU region, SA has announced in the February 2016 Budget its decision to introduce a tax on SSBs with effect from 1st April 2017. Cawley and Frisvold (2015) indicate that other countries impose taxes on drinks for purposes of revenue generation. For instance, in the United States (US), a number of states have imposed the same tax on both caloric soft drinks and the diet versions.

3 REVENUE MOBILIZATION AVENUES

3.1 Petroleum Products

Governments around the world subject petroleum products to taxation. Lesotho is not an exception; in addition to the VAT and excise taxes[1] other taxes on petrol and diesel include the oil levy, the petroleum fund levy, the motor vehicle assurance levy and the road maintenance levy. However, these taxes make a negligible contribution to public revenue. The combined revenue from these levies accounted for 1.4 and 1.7 per cent of total revenue in 2014 and 2015, respectively.

Table 1 Taxes on Petroleum Products in SACU (in SA cents)

	Botswana+	Lesotho	Namibia	South Africa	Swaziland	SACU Average
Fuel tax, Oil levy, Fuel levy	10.62*	60.00	11.00*	278.00*	220.00	186.00
Petroleum Fund Levy	15.09	11.00	90.00*	0.00	20.00	11.52
Road Accident Fund	5.59	10.00	49.00	154.00	35.00	50.72
Customs and Excise Duty	3.26	4.00	4.00	4.00	4.00	3.85
Road Fund Levy	89.44	30.00	114.00	0.00	0.00	46.69
Total	**124.01**	**115.00**	**268.00**	**436.00**	**279.00**	**244.40**

*Source: Lesotho Petroleum Fund * Average for petrol and diesel where the two were different. Tax rates in Botswana Pula converted to Maloti using the annual average exchange rate for 2016 of R1.30.*

In the SACU region, Lesotho's tax on petroleum products is the lowest and it is below the SACU average. At an aggregate of 115.00 cents per litre of petrol and diesel, Lesotho is followed by Botswana at 124.00 cents, Namibia at 268.00 cents, Swaziland at 279.00 cents and SA is the highest at 436.00 cents.

[1] Excise taxes are the same across all SACU member countries.

Table 2	Tax Level Proposals and Potential Revenue			
	Tax Level (SA Cents)	% Increase in Tax Level	Revenue (Million Maloti)	Revenue Gains from the Higher Tax Level (Million Maloti)
Lesotho's Current Tax Level	115.00	-	313.92*	-
Botswana	124.00	7.83	338.49	24.57
Namibia	268.00	133.04	731.57	417.65
South Africa	436.00	279.13	1190.17	876.25
Swaziland	279.00	142.61	761.60	447.68
SACU Average+	**244.00**	**112.17**	**666.06**	**352.14**

**Preliminary estimate based on three quarters of available data for 2016. + Excluding Lesotho.*

An assessment of the revenue implications of an increase in Lesotho's tax to other SACU countries' tax levels is undertaken and the findings are as follows. The increase to Botswana's tax level of 124.00 cents would result in a negligible increase of M24.57 million in Lesotho's tax revenue from petroleum products. The next higher tax level is the average of all the SACU countries excluding Lesotho at 244.00 cents. Increasing Lesotho's tax to the SACU average is likely to result in a more than double-fold increase in revenue from petroleum products. The increase to Namibia and Swaziland's rates is likely to result in gains in revenue to the tune of M417.65 million and M447.65 million, respectively. SA's tax rate is the highest in the region and raising Lesotho's to it would yield substantial revenue gains. However, the paper recommends a somewhat gradual increase in Lesotho's tax level to minimize the possible distortionary effects of the response by economic agents to a more drastic and abrupt increase. As a first step, the tax level could be raised to the SACU average. It could thereafter be adjusted periodically to protect its value from erosion by inflation.

While empirical evidence on the price elasticity of demand for petrol and diesel in Lesotho could not be found during this research the expectation is that it is inelastic in line with the empirical findings on other African countries, implying that the upward revision of the tax may result in an increase in public revenue. Boshoff (2012) found long-run price elasticities of -0.44 and -0.21 for petrol and diesel, respectively for SA. In the case of Namibia, De Vita *et all* (2005) estimated a long run price elasticity of -0.34 for aggregate energy comprising of petrol, diesel and electricity while Dahl (1994) found price elasticity of demand for energy of -0.94 for Botswana.

3.2 The Diamond Mining Sector

Mineral exploration and mining often fail to make a meaningful economic impact in resource rich economies and in some economies, large discoveries of minerals become a resource curse. For instance, in Ghana, the economic and developmental impact of the sector remains meager despite the massive inflows of foreign direct investment (FDI) into Ghana's mineral mining and the resultant upsurge in exports, (Awudi, 2002). This is attributable to low employment creation capacity of the sector due to its capital intensive nature and export of the minerals in crude form, without any beneficiation or value addition. Nonetheless, there are exceptions such as Botswana which has demonstrated that sustainable resource-led growth is attainable. According to De Beers Group of Companies (undated) the strategy of developing and managing its diamond resources with long term development goals in mind has helped Botswana to avoid the worst effects of the resource curse. Jeffers (2013) explains that Botswana's diamond mining sector is the largest contributor to GDP, exports and government revenues at 25.0 per cent, 86.0 per cent and 41.0 per cent, respectively from 2003 to 2013. As depicted in Table 3, the sources of revenue for the Government of Botswana from the diamond mining sector are Government's equity investments through joint ventures and taxes in the form of royalties, corporate tax and withholding tax on dividends.

Table 3	Diamond Sector Tax and Equity Rates by Country		
	Botswana	Namibia	Lesotho
Royalty Rate	**10% of gross market value**	**10% of Gross Turnover**	**10% of Gross Market Value (6% - 8%)**
Corporate Tax/ Variable Rate Income Tax	22 - 55 %*	55%	25%
Withholding Tax	7.50%	10%	15%
Taxation on Downstream Processing	15%	-	-
Government Equity Interest	- 50% in Debswana -15% in De Beers - 50% Diamond Trading Company Botswana - 80% indirect beneficiary shareholding in Morupule Colliery	- 50% in Namdeb - De Beers Marine Namibia owned 30% by Namdeb and 70% De Beers	-25% Liqhobong Mine - 30% Letšeng Mine - 20% Lemphane Mine - 25% Kao Mine - 20% Kolo Mine - 25% Mothae Mine

Source: Botswana – Mines and Minerals Act 1999, Ministry of Minerals Water and Energy Resources on www.gov.bw/Global/MMWER, MBendi Information Services on www.mbendi.com. Namibia – Minerals (Prospecting and Mining) Act 1992, KPMG (2014), Namibia Country Mining Guide and Ministry of Finance Income Tax Tables. Lesotho – Mines and Minerals Act 2005, Income Tax Act 1993, FIAS, IFC and World Bank (2006), Ministry of Mining and Websites of mining companies or major shareholders.

**Other mining companies except diamonds for which the tax regime is negotiated.*

Regarding Government of Botswana's equity stake in diamond mining, the Botswana Mines and Minerals Act 1999 Section 40 (1) provides for the Government to acquire up to 15.0 per cent working interest participation in the mines. However, being regarded a strategic mineral to the economy of Botswana the diamond sector is treated differently in this regard (MMWER, 2008). The Botswana Mines and Minerals Act 1999 Section 51 (1) stipulates that "the issue, renewal, transfer or amendment of a license to mine diamonds shall initiate a negotiating process, in good faith, between government and the applicant covering all technical, financial and commercial aspects of the proposed project including government participation". This has enabled the Government to acquire a substantial 50.0 per cent stake in the main diamond mining company in Botswana (Debswana) through a joint venture with De Beers and 50.0 per cent or more in other companies. In addition, the Government of Botswana has 15.0 per cent shares in De Beers. According to Jefferis (2013) this was facilitated by engagement of high level technical expertise by the Government to strengthen its negotiating position and using its "leverage points" such as renewal of agreements.

In the case of Namibia, participation of Government in diamond mining is defined by the Minerals (Prospecting and Mining) Act 1992 Section 49. It provides for the Minister of Mines and Energy to enter into an agreement that may include the terms and conditions relating to the participation of Government. This covers the acquisition of equity share capital by the State in production sharing or other joint ventures before a mineral license is issued. According to KPMG (2014) the Government of Namibia has 50 per cent shareholding in Namdeb, which it owns with De Beers. Namdeb is the largest producer of diamonds in Namibia at 95.0 per cent of domestic diamond output and it is the largest tax payer in Namibia (KPMG (2014), FIAS, IFC and World Bank (2006)).

In Lesotho, the Mines and Minerals Act 2005 section 44 (1) provides for the GoL, through the Mining Board, to engage in negotiations with an applicant of the issue, renewal, transfer or amendment of a mineral concession for diamonds. The negotiations cover technical, financial and commercial aspects of the project applied for, including government participation. GoL's shareholding in diamond mining companies ranges from 20.0 per cent to 30.0 per cent.

Regarding the tax regime, the tax on profits differs in the three countries. In Botswana there is a variable rate income tax for mining other than diamond mining. The diamond mining sector is taxed in terms of an agreement with Government. However, the rate cannot be less than 22.0 per cent and increases with profitability of the mine. FIAS, IFC and World Bank (2006) point out that the corporate tax rate for the diamond mines in Botswana ranges from 25.0 per cent to 55.0 per cent. In Namibia, the corporate tax for diamond mining companies is 55.0 per cent and is higher than the standard corporate tax of 33.0 per cent. In Lesotho the standard corporate tax of 25.0 per cent applies to diamond mining companies.

The statutory royalty rate for diamonds is 10.0 per cent in the three countries. The royalty rate for Botswana is stipulated in the Mines and Minerals Act 1999 and Jefferis (2013) confirms that the rate is non-negotiable in Botswana. However, in the case of Lesotho, even though the 10.0 per cent royalty rate is stipulated in the Mines and Minerals Act 2005, the mining companies negotiate lower rates. Consequently, the royalty rates in most of the existing diamond mining contracts in Lesotho range between 7.0 and 8.0 per cent (FIAS, IFC and World Bank, 2006) though the most recent information is that the lowest rate is currently 6.0 per cent. The withholding tax is higher in Lesotho than in comparator countries but does not compensate for the low rates on other taxes, especially because companies do not pay out dividends every year. SA and Swaziland are not included in this analysis because of the following reasons. In SA, the mineral deposits are vast and hence required a lot of huge investments. Consequently, the diamond mining sector tax regime was designed with a bias towards encouraging investments into the mining industry and the mining of marginal ores (Deloitte, undated). As such, the diamond mining industry operates under the general tax system. For instance it is subject to the general income tax rate of 28.0 per cent. In addition, the royalty rate is very low. It is calculated on the basis of profits, with the maximum rates of 5.0 per cent and 7.0 per cent for refined and unrefined mineral resources, respectively and the minimum of 0.5 per cent that applies to both (The Davis Tax Committee, 2014). In the case of Swaziland, the diamond mining industry is barely operational (Mobbs, 2015). As such there is barely anything to learn from it.

Table 4 Revenue from Royalties (Million Maloti)

	Royalties Revenue	Assuming 7.0%	Revenue Gains
2014	11.25	16.07	4.82
2015	121.61	173.73	52.12
2016	203.13	290.19	87.06

***Source**: Ministry of Finance and Author's Calculations*

As discussed earlier, the diamond mining companies in Lesotho are subject to different royalty rates. The royalty rates which apply to existing diamond mining companies range between 6.0 and 8.0 per cent. Attempts to access information on the contractual royalty rates for specific mines proved futile, understandably so because it is confidential contractual information. Consequently, in carrying out an assessment of the potential revenue gains from applying the statutory royalty rate of 10.0 per cent across all diamond mining companies, an average royalty rate of 7.0 per cent, which is the average of 6.0 to 8.0 per cent, was assumed to apply to all diamond mining companies. On the basis of this assumption and the realized royalties revenue, all other factors remaining the same, an increase in the rate to 10.0 per cent would yield a 42.9 per cent increase in revenue from diamond mining royalties.

Table 5	Corporate Income Tax Revenue (Million Maloti)		
	Revenue @ 25.0% Tax Rate	Revenue Gains from 35.0% Tax Rate	Revenue Gains from 50.0% Tax Rate
2014	120.76	169.04	241.52
2015	328.78	459.2	657.56
***Source**: Lesotho Revenue Authority and Author's calculations*			

The corporate income tax revenue from the mining industry amounted to M120.76 million and M328.78 million in 2014 and 2015, respectively. An increase in the income tax rate from the current 25.0 per cent to Botswana and Namibia's levels of 50.0 per cent would result in a doubling of corporate income tax revenue from the diamond mining industry.

Table 6	Dividends Paid to GoL (Million Maloti)	
	Dividends Paid to GoL	Revenue Gains from an Increase in GoL's Equity to 50.0%
2014	1.60	1.07
2015	175.00	291.67
***Source**: Lesotho Revenue Authority and Author's calculations*		

Currently GoL's equity interest in diamond mining companies ranges from 20.0 to 30.0 per cent. Calculations based on withholding tax revenue from the diamond mining sector indicate that government revenue from dividends amounted to M1.6 million and M175.00 million in 2014 and 2015, respectively. On the basis of an assumption that GoL has equity interest of 30.0 per cent in the diamond mining sector , it is estimated that the increase in GoL's equity to 50.0 per cent will result in a 66.7 per cent rise in government revenue from dividends.

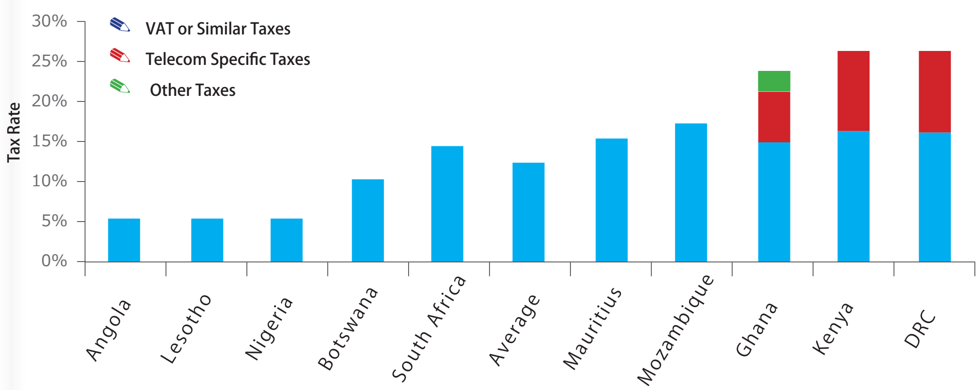
3.3 The Mobile Communications Sector

The key taxes on the mobile communications sector usually comprise of taxes on devices, taxes on services including calls, SMS, and mobile broadband as well as corporate taxes. Mobile services are high frequency transactions and hence represent a viable fiscal resources raising mechanism. VAT is the most common type of tax levied on mobile services. Some countries levy telecom specific taxes on mobile services. For example, the DRC and Kenya charge an excise duty at the rate of 10.0 per cent while in Ghana there is a communications service tax at the rate of 6.0 per cent. Ghana also collects the national health insurance levy from mobile services at the rate of 2.5 per cent.

[2] This is a reasonable assumption because only Letšeng mine paid dividends to GoL in 2015 and 2016.

In Lesotho, VAT is the only tax to which consumers of mobile services are subjected. While the standard VAT rate in Lesotho is 14.0 per cent, the VAT rate on communication services including mobile communications services is 5.0 per cent as stipulated in the Value Added Tax Regulations 2003, Section 6 (b). Consequently, Lesotho's tax rate on mobile phone services is one of the lowest in Africa (Deloitte 2015a) and among selected African countries as demonstrated in Figure 2. At the rate of 5.0 per cent Lesotho's tax is lower than that of its close neighbors, Botswana and SA.

Figure 2 Taxation on Mobile Services by Country

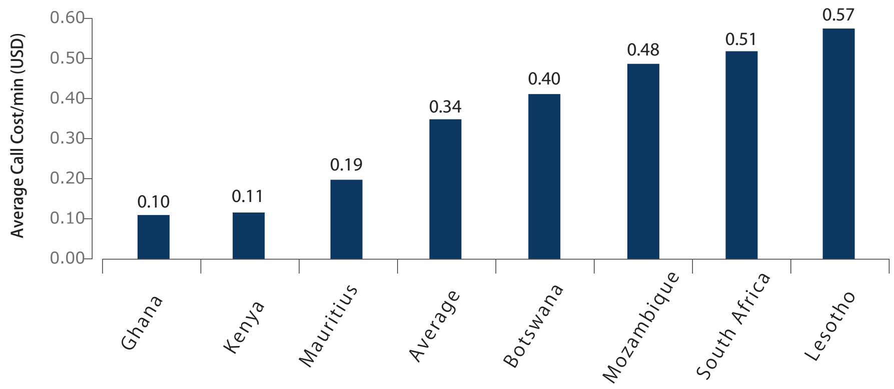


Source: Deloitte (2015b), Digital Inclusion and Mobile Sector Taxation in Ghana.

Lesotho's low tax rate notwithstanding, its tariff rate on mobile services is higher than that of a number of African countries that charge higher taxes than Lesotho. Lesotho's tariff rate is 82.4 and 80.7 per cent higher than Ghana and Kenya's tariff rates, respectively. Mobile tax rates on these two countries are some of the highest in Africa. Lesotho's tariff rate is higher than Botswana and SA's by 29.8 and 10.5 per cent, respectively. This could be an indication that the low tax rate environment has provided room for mobile phone services providers to charge higher tariffs and gain more revenue.

In Lesotho, mobile connections and internet use have grown significantly in recent years. The number of mobile connections in Lesotho grew from 1.75 million in 2013/2014 to 2.29 million in 2014/2015 and the number of internet users on mobile devices rose from 0.55 million to 0.71 million during the same period (Lesotho Communications Authority, 2014/2015). The numbers are growing despite the high tariff rates. Thus Government should consider raising the VAT rate on communications services and mobile services to the standard rate of 14.0 per cent.

Figure 3 Mobile Tariffs by Country



Source: Independent Communications Authority of South Africa (2013), 2014 – 2018 Cost to Communicate Programme, Presentation to Stakeholders.

The GoL's value added tax revenue from the communications sector amounted to M62.35 million and M63.21 million in 2014 and 2015, respectively. Keeping all other factors constant, an increase in the value added tax rate for the communications sector from the current 5.0 per cent to the standard rate of 14.0 per cent could result in revenue gains of more than M110.00 million a year. This is an increase of 180.0 per cent in the VAT revenue from the communications sector.

Table 7	VAT Revenue from the Communications Industry (Million Maloti)		
Period	Revenue @ 5.0% VAT	Estimated Revenue @14.0% VAT	Revenue Gains from the Higher Tax Rate
2014	62.32	174.50	112.18
2015	63.21	176.99	113.78

Source: *Lesotho Revenue Authority and Author's calculations.*

3.4 Alcohol and Tobacco

Within the SACU region, the common taxes on alcohol and tobacco products include VAT and excise taxes. The SACU agreement integrates SA's customs and excise tax rates across all five SACU member states and allows members to levy country-specific levies on goods and services including alcohol and tobacco (Tam and van Walbeek, 2013). Botswana was the first country in the SACU region to subject alcohol and tobacco to a levy. The Government of Botswana introduced the alcohol levy at the rate of 30.0 per cent in 2008 and raised it to 55.0 per cent in 2015 (Sinkamba, 2015). The revenue raised through the alcohol levy amounted to P298.73 million for the 2014/15 fiscal year while the tobacco levy raised P44.67 million during the same period (Botswana Unified Revenue Services, 2015).

Table 8	Alcohol and Tobacco Levy by Country	
	Alcohol	Tobacco
Botswana	55.0	30.0
Lesotho*	4.0	4.0
Swaziland*	10.0 (5.0)+	10.0 (5.0)+

Source: *Botswana – Sinkamba (2015), Alcohol Abuse and Interventions Strategies in Botswana and China: A Preliminary Study, PULA: Botswana Journal of African Studies, Vol. 29, No. 1. Namibia Economist (2014), Botswana: Tobacco Levy Introduced in Botswana Cause for Concern, Windhoek. Lesotho – Budget Speech to Parliament for the 2015/2016 Fiscal Year. Swaziland – The Alcohol and Tobacco Levy Bill, 2016, Bill No.16 of 2016. ()+ for locally manufactured alcohol and tobacco products. *Proposals that are yet to be implemented.*

In Swaziland, the Government has developed the Alcohol and Tobacco Levy Bill, 2016 as part of the legal framework towards introduction of a levy on imports of alcohol and tobacco goods and those manufactured in Swaziland other than for export. The Bill proposes levy rates of 10.0 per cent on imported and 5.0 per cent on locally manufactured alcohol and tobacco products. In Lesotho, the 2014/2015 Budget Speech had proposed a levy of 4.0 per cent on alcohol and tobacco products. The requisite laws for implementation of this proposal including the Alcohol and Tobacco Bill are in the process of being developed. The proposed rate of 4.0 per cent is low compared with Botswana and Swaziland's rates. Introduction of the levy at this rate is neither likely to result in any substantial reduction in the consumption of alcohol and tobacco nor in any meaningful increase in government revenue. WHO (2010) estimated that a 40.0 per cent tax on these products would reduce consumption by 18.0 per cent and result in substantial revenue gains despite the reduction in consumption. As in the case of Botswana, the levy should be introduced at a higher rate of 30.0 per cent for it to have the expected impact. An attempt to estimate the revenue implications of the proposed levy of 30.0 per cent was unsuccessful due to unavailability of data on alcohol and tobacco tax revenue.

3.5 Small Scale / Informal Businesses

There are 88 338 small scale/ informal businesses that are unregistered, privately owned and operated, characterized by a small number of employees (less than 5) in Lesotho (Household Budget Survey, 2010/2011). The majority of these businesses, estimated at 51.4 per cent are in wholesale and retail trade followed by 35.8 per cent in agriculture, hunting and forestry. 3.4 per cent are in manufacturing and 1.7 per cent in construction. However, due to lack of information about the turnover and profitability of these businesses it is challenging to make concrete and meaningful conclusions and recommendations regarding revenue mobilization from this sector. Nonetleless, along the lines of thinking of IMF (2011), small businesses in Lesotho could be subjected to a simple tax, akin to a license fee, of a blanket M100.00 per year to include them in the tax net and also as a way of motivating compliance by larger businesses. This could yield revenue of M8.83 million a year, with the assumption that all the 88 338 businesses remain operational and comply.

As highlighted in the Literature Review, in line with the experiences of other African countries, tax turnover from this sector will be below potential despite the high likelihood that collecting it will result in substantial financial costs. In addition, pursuing this sector might divert attention from more important sectors that have high revenue potential.

3.6 Other Possible Sources of Revenue

A number of revenue mobilization areas have been proposed before but have not yet been implemented. First, in Lesotho, the fees for public services and fines charged to perpetrators of the law have not been reviewed in a long time and hence remain very low. That is why a proposal to revise them was made in the 2015/2016 Government Budget Speech. It is vital that this revision is accelerated. In the years following this revision, the fees and fines should be adjusted for inflation to maintain their value in real terms and avoid another major revision. Second, are some innovative revenue enhancing measures such as the introduction of personalized car registration number plates, which would be offered at higher fees than the normal number plates. Implementation in these regards also needs to be expedited.

There are a number of other options that the GoL could pursue that have the potential to raise revenue while also addressing certain specific externalities. These include, but are not limited to taxation of SSBs and plastic bags. Taxation of SSBs is justifiable on health and revenue raising grounds in the case of Lesotho. Non-Communicable Diseases (NCDs) related deaths are estimated to account for 27.0 per cent of Lesotho's total deaths and in Lesotho, 14.6 per cent of adults are obese (WHO, 2014). In addition, as already indicated the GoL needs to come up with additional sources of revenue to close the gap arising from volatile SACU revenues and the sluggishness observed in the other sources of revenue. Another option is the taxation of plastic bags, which could, in addition to raising revenue, also have a positive externality of promoting environmental cleanliness.

4 CONCLUSIONS AND RECOMMENDATIONS

SACU revenue has been an important source of Lesotho's fiscal revenue. However it has been volatile and more tilted towards a declining trend. This calls for additional avenues for domestic revenue mobilization. Thus this paper has identified a number of areas with the potential of addressing this need and makes the following recommendations:

- Lesotho's tax on petrol and diesel should be raised to the SACU average at which level it will be lower than Namibia, SA and Swaziland's tax levels. This could have raised an additional M352.14 million in revenue in 2016. In the years following the increase, the rate should be adjusted periodically to shield its value from erosion by inflation.

- Contract negotiation capacity needs to be strengthened and contracts with diamond mining companies renegotiated with the objective of implementing the statutory royalty rate as it is and increasing the corporate tax rate and government equity interest in Lesotho's diamond mines along the lines of Botswana and Namibia. This has the potential of increasing royalties revenue by 42.9 per cent, doubling the corporate income tax revenue and raising 66.7 more revenue from dividends.

- Lesotho charges the lowest tax rate on mobile communications services among African peers despite the recent rapid growth of the sector. Mobile Network Operators (MNOs) are taking advantage of this by charging a tariff rate that is higher than the rates of some African countries that charge higher tax rates than Lesotho. The Government should consider raising the VAT on mobile services to the standard rate of 14.0 per cent from the current 5.0 per cent. This could result in GoL's revenue from this source rising by 180.0 per cent.

- Lesotho does not currently levy any tax on alcohol and tobacco other than VAT and excise tax. The recently proposed 4.0 per cent levy on alcohol and tobacco is way lower than Botswana's rates and Swaziland's proposed rates. Lesotho has room to introduce the levy at a higher rate of 10 to 50 per cent to reduce consumption of alcohol and tobacco and the health and social ills related to their consumption while also raising the necessary fiscal revenue.

- An introduction of a tax, similar to a licence fee of M100.00 per year for small/ informal businesses could raise a meagre M8.83 million per year. This is too little for this sector to be pursued, especially because experience of other African countries shows that collections are highly likely to fall below this potential despite the high financial costs that are likely to be incurred in its implementation.

- Implementation of revenue raising measures that have been proposed before, including, amongst others, the revision of stamp duty, fees and fines and introduction of personalised car registration number plates should be expedited. Other existing taxes such as the gaming levy, which have not been reviewed in a long time, should also be considered.

- Taxation of SSBs and plastic bags should also be considered both for raising revenue and addressing negative externalities associated with their use.

Although it is outside the scope of this paper is it worthy to note that improvements in government spending efficiency, for example, by reducing wasteful spending and corruption would make the proposed tax revisions more acceptable and encourage compliance. Containing public recurrent spending, while increasing and streamlining capital spending towards more growth enhancing development projects, would maximize the benefits of higher tax rates. In addition, implementation of policies and strategies for promoting and enhancing private sector growth should be expedited. This is important for reducing the high dependence of Lesotho's economy on Government for employment, hence the burden on the fiscus and for increasing the tax base.

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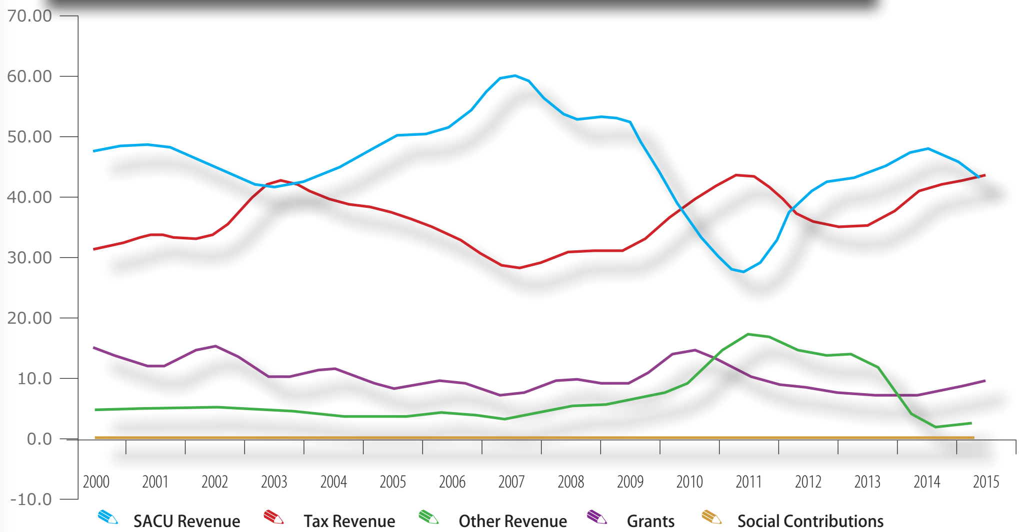
[i] Attempts to obtain data on Namibia and Swaziland were not successful that is why they are not included in the analysis.
[ii] Namibia and SA are not included in the analysis because they do not subject alcohol and tobacco to any levy or additional tax over and above the VAT and excise taxes.

Appendix Components of Lesotho Government Revenue (Per cent of Total Revenue)



Source: Ministry of Finance and Central Bank of Lesotho