

Transfer Pricing applies to local groups with a lowly-taxed resident associate

Transfer pricing (TP) is often associated with multinational groups that have companies operating in different countries. However, this is not always the case. Under Botswana's current TP rules, certain transactions between companies that are both resident in Botswana can also fall within the TP rules where one of the companies is subject to a concessionary tax regime. This means that a local group should not assume that transfer pricing does not apply simply because all the companies involved are based in Botswana. We will analyse this matter in detail below. In this article, words importing the masculine shall be deemed to include the feminine.

Who does this apply to?

The rule is relevant to companies that are associated with each other and enter into transactions between themselves. This could include transactions involving management fees, loans, interest, shared services, the sale of goods or other services. The important point is that the companies do not have to be in different countries for the TP rules to apply. The current Transfer Pricing Regulations generally exclude transactions between two Botswana residents, but this exclusion does not apply where one of the associates is subject to a concessionary tax regime.

For example, assume Company A and Company B are both incorporated and tax resident in Botswana. Company A is taxed under the normal corporate tax rules (24.5%), while Company B enjoys a special concessionary tax rate, say it operates in a SEZA zone where CIT rates are below 24.5%. If Company A charges Company B a management fee, the transaction may fall within the TP rules even though both companies are based in Botswana.

What is the arm's length principle?

The basic rule is that related companies should deal with each other as if they were independent businesses. Section 117 of the Income Tax Act, 2026 (ITA) provides that where a person enters into a transaction with an associate, the taxable income arising from that transaction must be consistent with the arm's length principle. In simple terms, the price and conditions should be similar to what unrelated businesses would have agreed in comparable circumstances.

For example, if Company A provides accounting services to Company B, the group should consider what an independent company would reasonably have charged for the same services. If Company A charges P1 million when an independent provider would have charged P600,000, the difference may require further TP analysis.

Why does the lowly-taxed company matter?

The reason this rule is important is that the price charged between related companies can affect where the group's taxable profit ends up. Imagine a group has two Botswana companies. Company A is taxed at the normal corporate tax rate, while Company B benefits from a lower tax rate. If Company A pays an unusually high fee to Company B, more profit may move to the company enjoying the lower tax rate.

This does not mean that every transaction with a lowly-taxed associate is wrong or that the arrangement is automatically tax avoidance. The issue is whether the transaction has been priced on an arm's length basis.

What should businesses do?

Companies affected by the rule should review transactions with their associated companies, particularly where one company benefits from a concessionary tax regime. They should keep records showing how prices were determined and why the terms are comparable to those that independent parties would have agreed. This could include agreements, invoices, calculations, comparable prices and information showing what services were actually provided.

Tax hint: If you have never had a tax audit/review conducted by a tax consultancy firm to check whether you are tax compliant, or should it be apparent that you are not certain that your tax affairs are good order, then don't wait for the taxman to pounce on you, as that can be very costly. Contact us today so we can help you fix your tax affairs whilst you still have time.

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