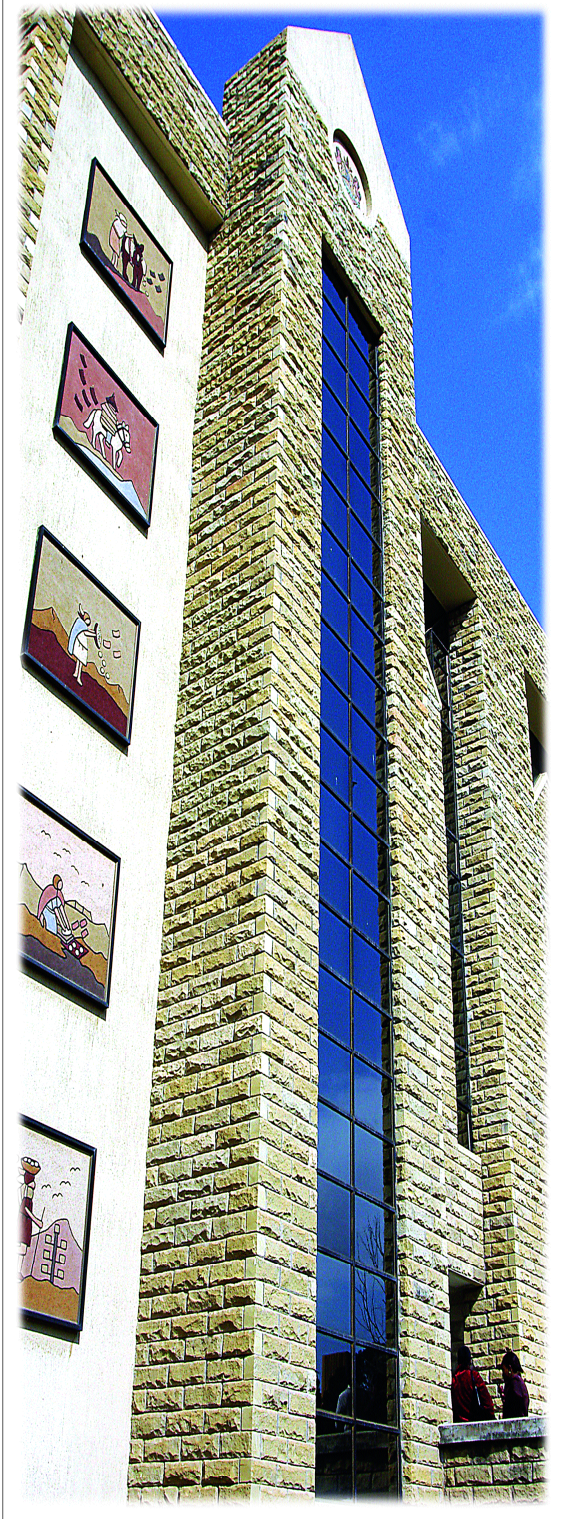




HIGHLIGHTS



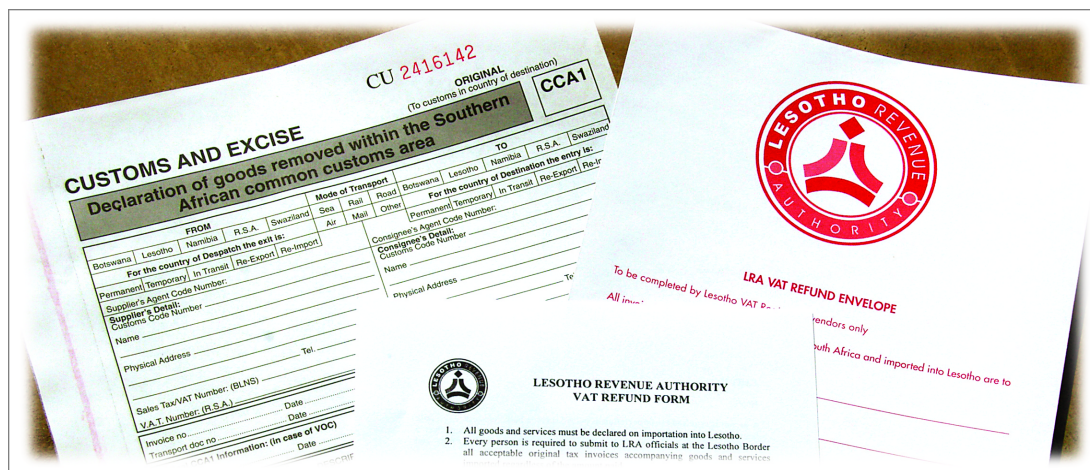
- VAT was introduced successfully at a rate of 14%.
- The waiting time for tax clearance certificates was reduced.
- The Sales Tax Exemption Certificate was eliminated, reducing tax evasion.
- New Import VAT border procedures were introduced.
- We showed increased efficiency at the borders.
- A Hotline was established to combat corruption and fraud.
- PAYE registered more than 400 new employers.
- Fifteen hundred and forty-four (1544) new or previously non-compliant sole traders were registered for Income Tax.
- Three hundred and eighty-seven (387) new or previously non-compliant companies were registered for Company Income Tax.
- The time taken to pay Income Tax Refunds was reduced from 3 months to 21 days.
- We launched the Advice Centre and LRA Website.
- An average of 3,000 individuals per month visited the Advice Centre.
- New Staff were appointed with the highest level of integrity, appropriate qualifications and experience.
- The Corporate Plan was completed.
- Strong cooperative arrangements were established with South African Revenue Service (SARS).
- All HR and Finance policies and manuals were approved and manuals published.





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LIST OF ABBREVIATIONS

LRA – Lesotho Revenue Authority	RSA – Republic of South Africa
SADC – Southern African Development Corporation	IVCF – Import VAT Credit Facility
DFID – Department for International Development	VIPS – VAT Information Processing System
VAT – Value Added Tax	SARS – South African Revenue Service
GoL – Government of Lesotho	GDP – Gross Domestic Product
SACU – Southern African Customs Union	NGO – Non-Governmental Organisations
GST – General Sales Tax	VCT – Voluntary Counselling and Testing



C O R P O R A T E P R O F I L E

The Lesotho Revenue Authority (LRA) is an operationally autonomous body that was established by the Lesotho Revenue Authority Act no. 14 of 2001 to be the:

“Main body responsible for the assessment and collection, on behalf of the Government, of specified revenue; for the administration and enforcement of laws relating to such revenue and for related matters.”

The Authority became operational in January 2003. It incorporates the functions of the old Income Tax, Customs & Excise and Sales Tax Departments of the Ministry of Finance and Development Planning.

The LRA was established to enhance the efficiency and effectiveness of revenue collection and to provide improved service to the public.

Despite operating outside the framework of the Civil Service and having access to appropriate mechanisms to ensure propriety, the Authority is fully accountable to Parliament and is bound by transparent accounting procedures.





VISION, MISSION AND OBJECTIVES

VISION

To become the best Revenue Collection Authority in Africa.

To achieve this vision, the LRA seeks:

To be an incorruptible, professional and efficient Revenue Authority providing excellent services whilst being fair, firm, dedicated and innovative.

MISSION

To maximise revenue collection through efficient, effective, sustainable and transparent systems aimed at developing a culture of voluntary compliance with tax laws, providing quality and responsive services to taxpayers and combating tax fraud and evasion.

CORPORATE OBJECTIVES

The Authority has the following Corporate Objectives:

Revenue Collection

To ensure maximisation of revenue collection for the Government of Lesotho.

Widening of Tax Net

To ensure that all those who have to pay tax do so.

Financial Management

To apply sound and effective financial management that will ensure the optimal utilisation of resources.

Stakeholder/Customer Relations

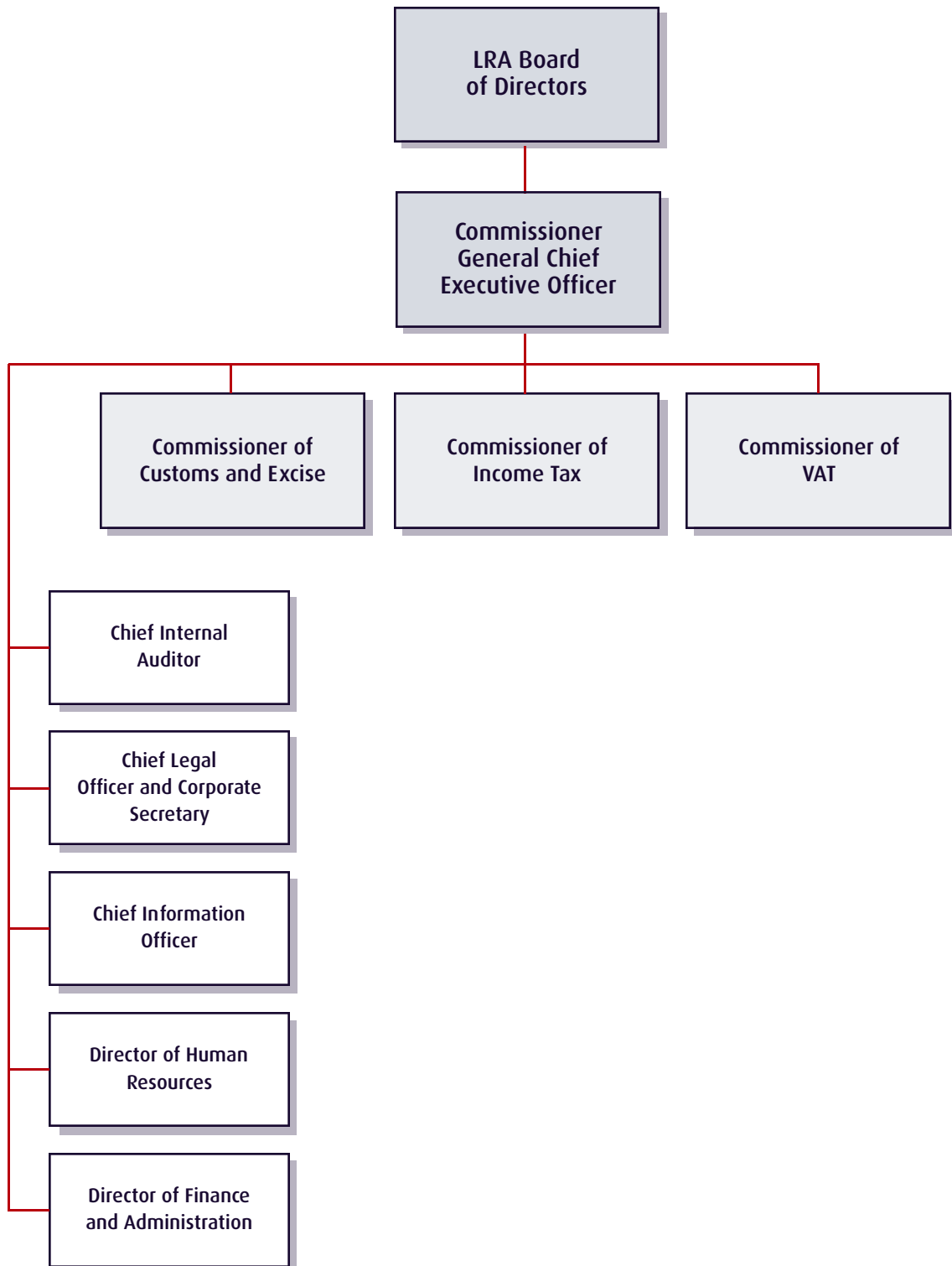
To maintain effective relationships with all stakeholders and customers in order to function optimally.

Organisational Effectiveness

To ensure that the LRA becomes a regional example in its effectiveness in carrying out its mandate.



LRA ORGANISATIONAL STRUCTURE





GOVERNING BOARD



Mrs Lineo Tshabalala
Chairperson

Representing the Ministry of
Finance and Development
Planning



Mr Thuso Thokoa

Representing Lesotho Chamber
of Commerce and Industry



Mr Sam Mphaka

Representing Lesotho Institute
of Accountants



Adv Thabo Makeka

Representing the Association of
Lesotho Employers & Business



Mr Mohlomi Rantekoa

Representing the Ministry of
Trade Industry, Cooperatives
& Marketing



Ms Leonia Lephoto

Representing the Central
Bank of Lesotho



Mr Robert Likhang

Nominated by the Minister
of Finance and Development
Planning



SENIOR MANAGEMENT



Mr Kevin Donovan
Commissioner General



Mr Nthako Sekome
Commissioner Value Added Tax



Mr Thabo Khasipe
Commissioner Customs & Excise



Mrs Maleshoane Morakabi
Commissioner Income Tax



Mr Nelson Monyamane
Director Human Resources



Dr Litlhare Mokitimi
Chief Information Officer



Mr Thabo Letjama
Director Finance & Administration



Dr Seth Macheli
Chief Legal Officer & Corporate
Secretary



Ms Ntefeleng Tsiboho
Chief Internal Auditor

CHAIRPERSON'S STATEMENT



INTRODUCTION

It is a great pleasure to present the first Annual Report of the Lesotho Revenue Authority (LRA) as required by Law and Corporate Governance principles. The report focuses on the background and purpose of the LRA, the operations of the Authority and the Auditors report together with the Audited Financial Statements for 2003/2004 financial year.

In 2001, the Government, as part of tax reform initiatives, abolished the three former tax departments under the Ministry of Finance and Development Planning; namely, Sales Tax, Income Tax, and Customs and Excise. In their place, a semi-autonomous agency, LRA, was established by an Act of Parliament, the Lesotho Revenue Authority Act No 14 of 2001, for the purpose of assessment, collection and receipt of specified revenues.

The Authority was established to maximize revenue collection by employing efficient and effective operational systems, bringing all taxpayers into the tax net, enforcing business principles and practices in the management of the Authority, exercising autonomy in the assessment and collection of tax and attracting and retaining the right calibre of staff.

Currently the revenues being collected are Income Tax, Customs & Excise and Value Added Tax. The Government, through the Ministry of Finance, is responsible for tax policy, while the Authority, under the supervision of the Board of Directors, is responsible for implementation of the policy.

In terms of the Act, the Board membership is diverse, comprising a representative from each of the following agencies:

- The Central Bank of Lesotho;
- Lesotho Chamber of Commerce and Industry;
- Lesotho Association of Employers and Business;

- Lesotho Institute of Accountants;
- Ministry of Finance and Development Planning;
- Ministry of Trade, Industry, Cooperatives and Marketing;
- An Appointee by the Minister of Finance from the private sector, who possesses professional knowledge and experience in finance, commerce, legal or economic affairs; and
- The Commissioner General, who is Secretary to the Board.

The Minister appoints the Chairperson of the Board, and members elect the Vice-Chairperson, who should be from the private sector if the former is from the public sector, and vice-versa.

The members of the LRA's dynamic Board are chosen for their diverse experience, maturity, skill and commitment. The Authority further prides itself on a dedicated team of employees which is under the leadership of a vibrant Management.

WHY DOES LESOTHO NEED A REVENUE AUTHORITY?

Domestic and global imperatives have necessitated radical changes in the administration and management regime of the tax collection function of Government. The former system was fraught with problems such as administrative and operational deficiencies, low taxpayer compliance, corruption by tax officials and taxpayers and low revenue collections.





CHAIRPERSON'S STATEMENT

(continued)



The imminent reduction of customs receipts (which currently constitute over 50% of Government revenue) caused by the renegotiation of the SACU revenue sharing agreement, the introduction of free trade arrangements between SACU and Europe, United States of America, and SADC were also underlying factors in the review of tax administration. The uncertainty surrounding the impact of Lesotho's exports and Lesotho's ceasing to have preferential treatment under the Africa Growth Opportunity Act (AGOA) on the investment climate have also been identified as some of the factors likely to reduce tax revenues.

As the report by the Commissioner General indicates, the review of the tax administration has been successful. This success is illustrated by the fact that tax

collections have increased substantially compared with 2002/03, the year before the LRA was set up. In this first year of the LRA, Income Tax and VAT collections were M846,19 and M498,92 million compared to M669.7 million in Income Tax and M374,8 million in Sales Tax collected in 2002/03, yielding year-on-year growth rates of 26% and 33% respectively.

STRATEGIC OBJECTIVE

In order to comply with the contemporary corporate governance principles, the Board developed a Corporate Governance Code for itself and for the Authority. The Board further approved a Corporate Plan with a vision to ensure that the LRA becomes the best revenue Authority in Africa.

ACHIEVEMENTS OF LRA TO-DATE

Since its inception, the Authority has been striving towards maximisation of revenues through application of fair and equitable policies. Notable achievements have been made and include:

- All administrative and operational systems have been installed;
- The Value Added Tax replaced General Sales Tax and is yielding positive results;
- Customer service is continuously improving;





CHAIRPERSON'S STATEMENT

(continued)



- A Corporate Plan that guides the Authority's performance was completed;
- The Authority is fully operational on commercial principles;
- Governance structures are in place;
- HIV and AIDS Policy exists;
- The revenue targets set by the Ministry of Finance and Development Planning for 2003/2004 have been surpassed.

THE CHALLENGES FACING THE LRA

Funding is the Authority's major challenge. The Authority qualifies for 2% of the estimated revenues in any one financial year. This commission just covers recurrent expenditures and is not adequate for major capital investments. Border refurbishment and computerisation are lagging behind due to the

shortage of funds. The Authority is currently housed at Finance House Government Office Complex Phase III, and thus loses its independent identity; it is unable to afford rented accommodation or a building of its own. Although ready to have district representation, the absence of office and residential accommodation makes it difficult to deploy staff at district level.

STAKEHOLDERS WHO CONTRIBUTED TO THE SUCCESS

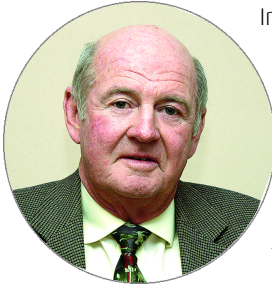
I would like to acknowledge all stakeholders who contributed to the successful first year of the Authority. The Government, through the Ministry of Finance and Development Planning and in particular the Honourable Minister, who provided support at all times; the members of the Board who have steered the Authority in the right direction; the Commissioner General and his management team who implemented the operational mandate of the organization; members of staff who dedicated themselves to the common objective of excellent service delivery. All deserve my deepest gratitude. Also, the support offered by the two Houses of Parliament has been invaluable.

Acknowledgments also go to the individual taxpayers, corporate and professional bodies for their cooperation and print & electronic media that communicated tax messages throughout the country. The British Government's Department for International Development (DFID) has played an important role in funding the capacity building programme of the LRA. The South African Revenue Service and the Zambia Revenue Authority have been active in exchange and training programmes as well as operational support.

Lineo Tshabalala
Board Chairperson



COMMISSIONER GENERAL'S STATEMENT



In order for it to effectively facilitate economic growth, the Government of Lesotho (GoL) identified the importance of increasing and sustaining tax revenues without necessarily increasing the tax burden to the populace. The widening of the tax net, with a view to ensuring that the tax burden is shared by all who are legally bound, was considered the first step towards the achievement of this challenge. To that end, GoL saw the need to restructure its tax revenue administration; and the changes were introduced through the enactment of the Lesotho Revenue Authority (LRA) Act no 14 of 2001. By passing this Act, Parliament abolished the three former revenue departments of Income Tax, Customs & Excise and Sales Tax, and, in their place, established a new and autonomous corporate body, the Lesotho Revenue Authority.

The inherent belief in the effectiveness and efficiency of a corporate approach to what is otherwise a public service provided the impetus for the Government to launch the LRA. It is, therefore, the expectation of the Government, and indeed that of the taxpayers too,

that the Authority will not only raise more revenue than the previous revenue departments but also



improve service delivery. Meeting these expectations was the primary challenge that the Authority dealt with in its first year of operation. Given that the Authority started operations three months prior to the beginning of the financial year, this inaugural Annual Report covers a fifteen month period commencing in January 2003 and ending in March 2004.

The report reflects the main achievements and challenges of the Authority over the last fifteen months. Initially, the main challenges were increasing revenue, improving service delivery, and enhancing





COMMISSIONER GENERAL'S STATEMENT

(continued)

the administrative capability of the Authority. Many aspects of these challenges have gone hand in hand; the improvements in revenue collection have been the result of better procedures and the resulting increase in voluntary compliance. Given the Authority's corporate



objective of maximising revenues, the best way to assess the Authority's performance is by looking at revenue collections and comparing them with the targets for collection set beforehand. I begin by presenting the performance of the revenues collected in the 2003/04 financial year, and then address the ways in which the LRA has responded to more specific challenges. I conclude by taking a look at the challenges the LRA is facing now, and considering the ways in which it hopes to address them.

REVENUE PERFORMANCE

Revenue performance in 2003/04 surpassed all expectations. The LRA remitted M1 371,94 million to Government, exceeding Government fiscal budget targets for the 2003/04 financial year by 19% and the revised targets by 5,5%. It is worth noting that the following presentation excludes revenues derived from Customs and Excise Duties. These revenues are remitted to the SACU revenue pool, which is then shared out according to the SACU formula. Furthermore, the formula works with a two-year lag such that remittances during the reporting period, 2003/04, are reflective of Customs and Excise collections of 2001/02. For the financial year 2003/04, receipts of SACU revenues totalled M1 421,7 million. This indirect remittance of Customs and Excise Duties means that the LRA only remits the revenues from Income Tax and VAT to the Government Consolidated Fund.

In 2003/04, the Authority remitted M852,47 million in Income Tax revenue and M519,47 million in Sales Tax/VAT revenue to the Government. Table 1 shows a quarterly breakdown of the Income Tax components and of Sales Tax/VAT collections for the reporting period.

Table 1: Quarterly Breakdown of Revenue by Tax Type (in millions of Maloti)

	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Total
Personal Income Tax	95.24	146.15	121.27	143.26	505.92
Company Income Tax	21.70	82.79	58.36	75.01	237.86
Other Income Taxes	13.78	31.64	24.53	38.74	108.69
Sales Tax/VAT	75.00	134.95	157.99	151.53	519.47
Total	205.73	395.52	362.16	408.54	1 371.94



COMMISSIONER GENERAL'S STATEMENT

(continued)



Personal Income Tax contributed almost 60% of all Income Tax revenues; the strongest performance occurred in quarters 2 and 4. The relative increases in the tax collections of these quarters were the result of remittances made by sole traders at certain points in the financial year. Company Tax also exhibited this trend. Other Income Tax revenue is derived from Fringe Benefits Tax, Withholding Tax and Gaming Levy. The general trend of these collections, which increase throughout the year, represents increases in efficiency. These efficiency gains resulted from more thorough auditing, a concerted effort to increase the contact of LRA tax collectors with taxpayers and improved cross referencing between the information held on the registers of the different tax types.

To further enhance income tax collections and service delivery, a new Income Tax system referred to as Self Assessment System (SAS) was, by the end of the reporting period, being prepared for a launch on 1 April 2004. This system will only apply to corporate taxpayers, company directors and other self-employed persons as it replaces the current Official Assessment

System (OAS). The virtue of SAS is that it is significantly more taxpayer-friendly and should therefore ensure timely payments are made. With the adoption of SAS, the perennial problem of estimates will, hopefully, be history.

The table further illustrates the success of VAT. To enhance tax revenue, the Government decided to replace Sales Tax with VAT. The LRA, upon becoming operational, was given the challenge of introducing VAT in a short period of six months. Given that the Department of Sales Tax had tried twice before, in October 2001 and in April 2002, to launch VAT, the need for the LRA to succeed became all the more important. To that end, a comprehensive publicity campaign was mounted with a view to educating the public on the new tax system. Furthermore, a series of tax clinics and consultative meetings with various local Business Associations were held, and views expressed in these interactions formed the basis for the amendments that were subsequently made to the VAT Act.



COMMISSIONER GENERAL'S STATEMENT

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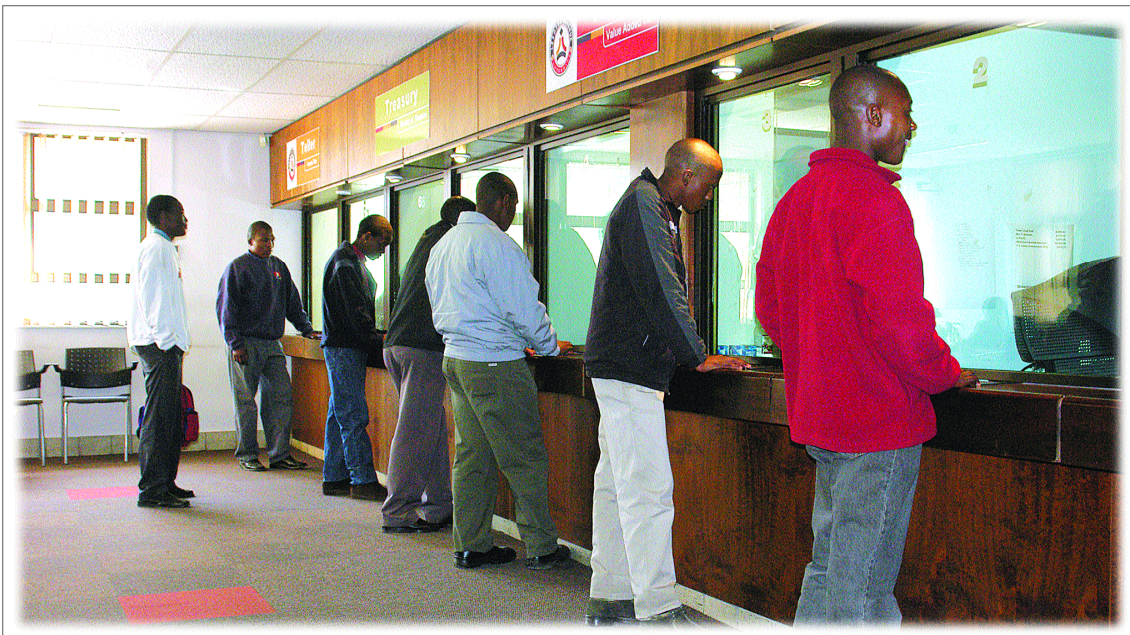


On the 1st of July 2003, the Authority successfully introduced VAT. Apart from the fact that the new tax was introduced at a higher rate of 14%, its most notable feature was that, unlike with GST, a number of goods and services consumed were either exempt or zero-rated from the tax. As such, the Government could use the tax much more effectively as a policy instrument to alleviate poverty. Indeed, basic food stuffs such as maize meal, milk, beans and peas were zero-rated, while crucial services such as educational services, financial services, water and passenger transport were maintained as exempt. The launch of

VAT was preceded by a country-wide publicity campaign mainly comprising VAT clinics held in all ten districts, a series of leaflets, pamphlets, posters, radio and newspaper advertisements and face-to-face sessions with business, diplomatic, NGO and exporter associations.

With respect to collections, the introduction of the new tax, coupled with significant efficiency gains by the Authority, saw VAT collections increase significantly in the second quarter of the year compared with the year before. Apart from the higher rate, the improved VAT revenue collections were due to the major restructuring of administrative procedures that occurred from the 1st of July 2003. The convergence in the standard rates of VAT between RSA and Lesotho enabled the adoption of simpler and yet more revenue-enhancing processes at the border posts.

Most notably, following an agreement between SARS and LRA, the laborious VAT refund processes that previously pertained at border posts were replaced by a system whereby RSA tax invoices are acceptable as payment of Lesotho VAT. The new procedure allows





COMMISSIONER GENERAL'S STATEMENT

(continued)

SARS to refund the LRA, and not the individual importer, all VAT paid on goods purchased in RSA. As a result, the incentive of non-declaration, smuggling and all forms of tax evasion at the border was significantly diminished. For large importers, an Import VAT Credit Facility (IVCF) was devised. The system negates the need for large importers to tie up their cash with LRA as import VAT only to claim it later as input credit. As such, the IVCF is used to defer their payments, smoothing their cash flow.

The VAT Division utilised the VAT computer system (VIPS) to significantly increase compliance levels by vendors. Having benefited from the training offered by

SARS under the bilateral capacity building and cooperation agreement between the two tax Authorities, VAT auditors focussed more of their attention on field audits than was ever the case in the GST era. The increased presence of tax auditors not only compelled vendors to comply but also provided them with increased opportunities to seek guidance and clarity on the new tax system. Consequently, as Table 2 below depicts, remittances of VAT/GST in 2003/04 were 33% more than in 2002/03 whereas those of Income Tax were also impressive at 26%. Total remittances improved by 29% in 2003/04 over that of 2002/03.

Table 2: Remittances in 2002/03 against 2003/04 (in millions of Maloti)

Tax Type	Actual Remittances		Adjusted Remittances		Adjusted Growth Rate
	2002/03	2003/04	2002/03	2003/04	
Income Tax	663.30	852.47	669.70	846.19	26%
Sales/VAT	343.70	519.47	374.80	498.92	33%
Total	1 007.00	1 371.94	1 044.50	1 345.11	29%

Note: Remittances refer to actual cash collections deposited into the Government consolidated fund. The difference between actual and adjusted remittances is due to, inter alia, balances, as at 1 April 2003, in the two tax accounts amounting to M31 million and M6,4 million for VAT and Income Tax respectively. Deducting these and adding district collections that were remitted directly to Government yields adjusted remittances.





COMMISSIONER GENERAL'S STATEMENT

(continued)

As testimony to the resounding success of the border post procedures, Table 3 below presents a comparison of import VAT/GST collections at the five commercial border posts between the pre-LRA year, 2002/03, and the inaugural year of 2003/04. Between the two years, collections at the two biggest border posts Maseru and Maputsoe increased by 167% and 320% respectively adding up to a huge M80 million in additional VAT collections. Combined, all border posts, including the non-commercial ones, collected M102,7 million more import VAT/GST in 2003/04 than the year before, representing a previously unprecedented year-on-year growth of 204%.

However, apart from the evident efficiency brought about by the LRA, the change in tax policy, in the form of introducing VAT at a rate 4% higher than that applying under GST, also contributed to the increased border collections. The introduction of VAT also led to the abolition of the GST exemption certificates which effectively exempted the holder from paying GST at the border. Furthermore, the fact that under the VAT system, all VAT paid on imports by VAT registered vendors will be claimed back as input VAT, implies that a good proportion of the border post collections will be refunded back to the vendors at a later stage.

Table 3: Comparison of Border Collections in 2002/03 with 2003/04¹ (in millions of Maloti)

	2002/2003	2003/04 ²	Increase	% Increase
Caledon Spoort	3.16	12.25	9.09	287%
Maputsoe Bridge	8.77	36.81	28.04	320%
Maseru Bridge	31.24	83.30	52.06	167%
Van Rooyen's Gate	2.89	11.56	8.68	300%
Qacha's Nek Gate	1.16	3.75	2.59	223%
Total	47.22	147.68	100.45	212.7%

¹This table presents figures for the main border posts.

²These totals have been adjusted downward to account for the administration charge levied by the VAT refunds administrator. These totals do not take into account the delay in remittance of funds from SARS.





COMMISSIONER GENERAL'S STATEMENT

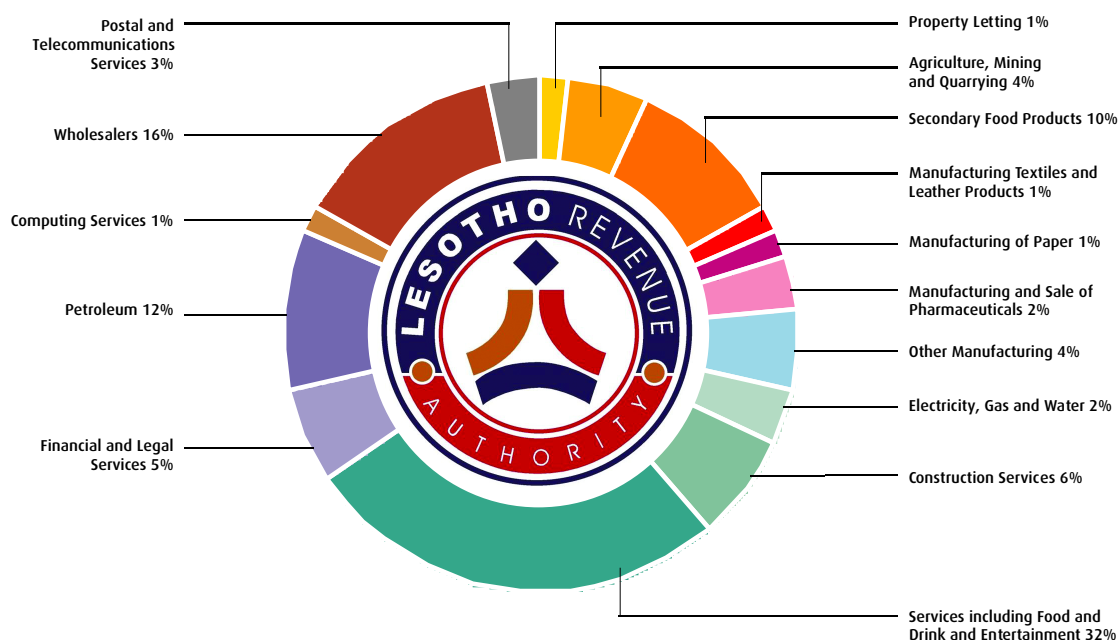
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In view of the evident success of the new border procedures adopted at the five commercial border posts, negotiations with SARS to extend these procedures to all border posts were at their final stages by the end of the financial year. The negotiations included the processing of invoices relating to the purchase of used vehicles, and as a result, we

envisage used cars being treated in the same manner as other goods.

Reflecting the importance of the Services and the Wholesale & Retail sectors in contributing to the Gross Domestic Product (GDP), a break-down of inland VAT into its components is presented in Figure 1 below.

Figure 1: The Sources of Domestic VAT



It is worthwhile noting that despite being the biggest contributor to both GDP and job creation, the manufacturing sector contributes the least to inland VAT. The reason for this incongruity is that almost all vendors within the textile manufacturing sector operate under the Customs rebate conditions whereby they import fabric and all other inputs duty and VAT free. They are then required by law, unless they pay the VAT and Customs duties, to export their produce to outside SACU. Since exports are zero-rated, all VAT paid by exporters on local purchases is then claimed back.

REMITTANCES AGAINST TARGETS

Revisions of annual targets during the course of the year complicate the analysis of revenue performance against targets. A number of developments that occurred during the reporting period led to various adjustments of both VAT and Income Tax targets. With regard to VAT, its introduction at a higher rate of 14% increased the VAT target from M388,88 million to M449,95 million, and the decision that the Government should be liable to for VAT further increased the potential collection to M501,95 million.



COMMISSIONER GENERAL'S STATEMENT

(continued)

The requirement for Government to pay VAT occurred after the fiscal budget was approved by Parliament. As such, the Line Ministries were not adequately funded to comply with their VAT obligations. The question around non-compliance by Government has led to the adoption of M449,85 million as the VAT target. With respect to Income Tax, strong revenue performance in the first half of the year necessitated two revisions of the target; the final revision – made in October – revised the target budget estimate of M760,2 million to M850,47 million. Table 4 shows the annual performance of Income Tax and Sales Tax /VAT remittances against the revised targets.



Table 4: Revenue Performance (in millions of Maloti)

	Remittance	Target	Variance	% Variance
Sales Tax/VAT	519.47	449.95	69.52	15.5%
Income Tax	852.47	850.75	1.72	0.2%
Total	1 371.94	1 300.70	71.24	5.5%

As depicted, VAT collections exceeded the target by M69,5 million, yielding a variance of 15,5%. It is worth noting that even if the VAT revenues were to be assessed against the higher target based on partial Government compliance, the Authority would still have exceeded the VAT target by 3,5%. Income Tax collections, on the other hand, exceeded the target by M1,72 million. Combined, the total LRA remittances to the Government Consolidated Fund for the year 2003/04 add up to M1 371,94 million, which is 5,5% above the challenging target of M1 300,7.

IMPROVING SERVICE DELIVERY AND INCREASING ADMINISTRATIVE CAPACITY

The challenge of improving service delivery can only be achieved with full involvement of the staff, as they are the ones who directly interact with taxpayers. As such, the importance of staff as the most valuable resource of the Authority cannot be overemphasised.

Both Management and the Board are committed to ensuring that the Authority not only recruits the best staff, but also retains them. To that end, an effort towards supporting the welfare of staff was made during the year. An LRA sports day and staff Christmas parties covering all staff including those at border posts are some of the year's notable staff activities.



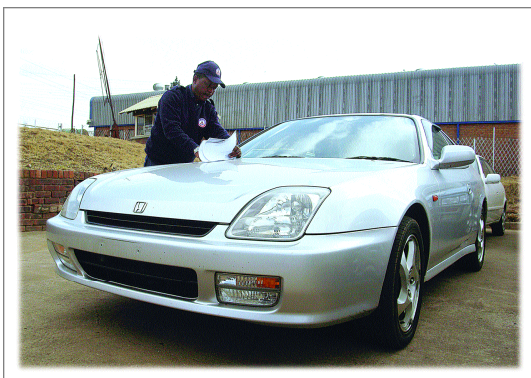


COMMISSIONER GENERAL'S STATEMENT

(continued)



procedure, which was implemented along with the introduction of VAT on the 1st of July, 2003. As earlier described, the new procedure allows the LRA Customs officials to accept tax invoices as a means of payment for import VAT. The LRA uses these invoices to claim back VAT that has been paid in South Africa on goods which are then imported into Lesotho.



The Authority agreed with SARS to extend the refund procedure to include second hand vehicles. The procedures will come into effect at the beginning of the 2004/05 financial year. More generally, the LRA and SARS agreed to share information and knowledge – a cooperation that has improved efforts in combating cross-border tax evasion and also allowed SARS to provide technical support to the LRA. LRA staff members have been attached to SARS, and instructors from SARS have come to Lesotho to train LRA staff.



Another invaluable source of guidance in an attempt to improve service delivery has been the business community, with whom the LRA has been able to communicate through business associations. Several organisations have contributed to the successful implementation of VAT and made general improvements to the administration of the tax system. These interactions have also allowed the LRA to disseminate information, thus increasing tax compliance.

This year's successful revenue performance has been due to the work of LRA staff members, the support of the Board, the support of the Ministry of Finance and Development Planning, especially the Minister, and an improved relationship with the South African Revenue Service (SARS). The most obvious effect of the improved relationship with SARS is the new border

In this first year of operation, the Authority placed a large emphasis on dissemination of information and educating the general public. The creation of an Advice Centre at Finance House in Maseru, in which taxpayers can consult directly with LRA officials, has been very successful – over 3 000 taxpayers have visited the Centre every month since it opened. The opening of the Advice Centre was accompanied by the introduction of the LRA website, which also acts as a conduit for information to taxpayers.



COMMISSIONER GENERAL'S STATEMENT

(continued)



CHALLENGES

In attempting to improve service delivery, a conscious effort was made to enable the public to be tax compliant while also clamping down on corruption, fraud and tax evasion within and outside the Authority. As a starting point, during the recruitment of staff, we ensured that the staff appointed were of the highest integrity and ethical standards. To that end, an independent professional consultancy firm was engaged to manage the whole recruitment process. The use of asset declarations as a pre-requisite for appointment also enhanced recruitment.

To ensure that the fight against corruption and fraud is constant, the Authority has an Internal Affairs Unit, which deals solely with investigations into suspected corruption and fraud within the Authority staff. The LRA aims to lead by example, with all staff being required to live up to the highest standards. In this first year of operation, this policy has helped crack down on potential internal tax fraud, thus saving the country millions of Maloti. The introduction of a toll-free line for

the public to report suspected cases of tax evasion is an effort by the Authority to partner with the public in ensuring tax compliance while also cracking down on smuggling, under-declaration and tax evasion.

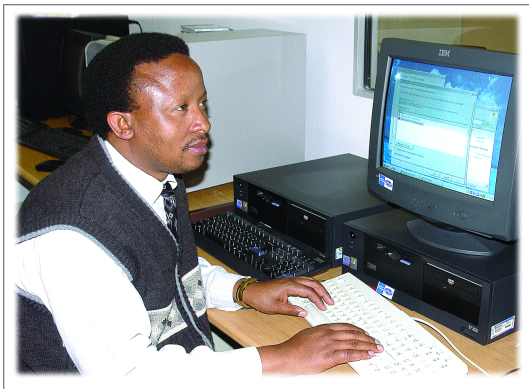
The drive to remove corrupt officials has been one of many ways in which the Authority has tried to foster a united and motivated staff. Other initiatives include the compulsory attendance of workshops, which, in addition to covering the standard staff training, have encouraged a sense of belonging to the LRA rather than one of the pre-existing revenue-raising departments. Most notably, these workshops have a focus on client service. Staff members are also encouraged to attend professional training courses in various tax-related disciplines in addition to the required workshops.

Staff at border posts have seen their conditions improve even though much still remains to be done. LRA resources were used to provide water, sanitation and improved housing for border staff. The neglect of infrastructure over a long period of time means that



COMMISSIONER GENERAL'S STATEMENT

(continued)



the process of improving working conditions will not be completed in one year. In light of this need, donor funds from DFID were secured for a thorough study and costing of the required refurbishments at all border posts. This study, commenced in January 2004, will be concluded in August 2004 with detailed costing and bills of quantities for work that should be undertaken. It is intended that a five-year refurbishment project will be needed to repair the neglected infrastructure.

Another challenge facing the Authority is the retention of quality staff. Keeping employees involves implementation of an integrated and equitable remuneration system, implementation of performance rewards system to motivate staff, and support for their welfare so that they can be healthy and serve the

Authority better and for a longer period. Staff welfare can be supported through a sound policy framework such as the HIV/AIDS policy and introduction of employee assistance programmes that are both cost effective and value-adding to the Authority and staff in general.

In recognition of the threat posed by HIV/AIDS, the Authority has undertaken to provide information and counsellors to its staff. In an attempt to raise awareness, a fun-walk was held on AIDS day. Furthermore, an HIV/AIDS policy was, as at the end of the year, in place. The Policy emphasises the importance of Voluntary Counselling and Testing (VCT) under a guarantee of confidentiality. Discrimination in the workplace is also not to be tolerated. For medical support, the Authority provides staff with medical aid contributions, based on grade, to a Medical Aid programme that provides limited HIV/AIDS support.

The other big challenge faced by the Authority in improving service delivery is to improve and computerise information systems. By the end of the financial year, the only well-functioning data



management system that the Authority had in place was the new VAT Information Processing System (VIPS), which was introduced alongside VAT in July,



COMMISSIONER GENERAL'S STATEMENT

(continued)



2003. The system allows the VAT Division to track vendors and identify non-filers and defaulters more easily than was the case in the Sales Tax era. VIPS also improves service delivery to the clients. For instance, the waiting time for VAT clearance certificates was reduced from five days to twenty-four hours whereas payment of tax refunds is routinely done every month. The success of VIPS stands in contrast to the Income Tax Division's reliance on manual systems. Computerisation of all Income Tax processes is essential for the realisation of the Division's potential.

The new SACU formula makes it even more important that Customs records are kept as accurately and as timely as possible. Without the computerisation of Customs and Excise clearance procedures, such accurate records cannot be achieved. Failure is not an option, given that, under the new SACU revenue sharing formula, each country's share depends on the accuracy of its records on intra-SACU imports. As such, it is one of the priorities of the Authority to computerise all Customs and Excise processes. In order to reap maximum benefits from computerisation, it is our aim to join the separate Operational Divisions' systems into an integrated information system that will allow even more effective service delivery and enforcement by the LRA as a whole.

The last challenge facing the Authority is to undertake a review of the Tax Acts with a view to making them simpler and therefore easier to implement. The review will also be aimed at harmonising the three tax types by eliminating a lot of the procedural duplication that currently exists.





COMMISSIONER GENERAL'S STATEMENT

(continued)



THE FUTURE

The future of the LRA depends on many factors, not least the macroeconomic stability of the country and a growing economy. Two areas of concern are worth pointing out. The first is closely related to the preceding discussion on information systems, where the urgency of computerising both Customs and Excise and Income Tax processes was emphasised. In the coming years, Lesotho's current primary revenue source, SACU revenues, is going to be under extreme pressure. The SACU income, which comprised more than 50% of all tax revenue in 2003/04, is going to decline because of two key developments. The first is the implementation of a new revenue sharing formula, and the other is the imminent free trade agreements that SACU is to sign with some of its major trading partners, most notably the United States of America.

Because the new revenue sharing formula requires better data, improving the Customs information system will help minimise this impending reduction in revenues. In searching for an alternative revenue source, VAT cannot be expected to produce any substantial gains – it is expected to grow only in line with nominal GDP. Therefore the LRA has to computerise Income Tax, which, with a new system that allows proper auditing and inspection techniques, is the tax type with the most potential to increase revenues.

The Authority's funding is the second issue of concern. The monetary allocation for 2003/04 did not cover the expenditures that the LRA incurred throughout the year. This year's shortfall was made up by contributions from the transitional process and interest earned on Customs revenues before they were submitted to the



COMMISSIONER GENERAL'S STATEMENT

(continued)



SACU pool. But a similar insufficiency is forecasted for the next financial year (2004/05). These deficits derive from the funding mechanism outlined in the LRA Act of 2001, which states that 2% of the estimated revenue to be collected shall be used to fund the Authority. There is no credible basis for this figure, and no other similar Authority in Africa, using the same basis for funding, gets less than 3% of the corresponding figure. A different, and more sustainable mechanism will have to be determined during the coming financial year for implementation in 2005/06. The Ministry of Finance and Development Planning has approved the setting up of a technical team to look into the issue. More specific information regarding the LRA's funding mechanisms can be found in the audited financial statements on page 24.

Apart from these concerns, the LRA faces many new challenges, which all stem from the need to maximise revenue collection. Increasing voluntary compliance is going to be the general focus of all initiatives and programmes adopted by the Authority in the coming

year. To that end, the following administrative reforms are worth mentioning: streamlining Tax Clearance and Refund procedures; establishing a Revenue Appeals Tribunal; implementing a short-term Tax Amnesty, introducing the Self Assessment System for Income Tax and decentralising advice centre functions to other regions of the country. The LRA also plans to widen the tax net, refine its financial management, and improve stakeholder and customer relations. It is hoped that with continued support from the Government and a consistently motivated and well-trained staff, the LRA can raise an increasing amount of revenue to build a better society.

Kevin M Donovan

Commissioner General



AUDITED FINANCIAL STATEMENTS

The annual financial statements which are presented here have been audited by PMB Chartered Accountants and approved by the Board of Directors. The Accounts cover a nineteen month period, beginning when the Commissioner General took up his post and finishing at the end of the 2003/04 financial year. This section summarises the annual accounts and their implications for the LRA.

In the period before the LRA became operational, the GoL contributed approximately M32,66 million to cover the transition costs. In the accounts, this contribution is denoted as capital funding; it was used by the Authority to acquire the fixed assets required to supplement the deficit between the normal funding and the running costs that occurred in the 2003/04 financial year.

The Income Statement of the Authority shows that the main source of income in the 2003/04 financial year was the M52,2 million, which was paid by the GoL – this payment represented 2% of the tax collection estimates for the 2003/04 financial year. The total expenditure over the same period is M82,3 million, of which DFID contributed M15,16 million to the strategic infrastructure and operational development costs. The 2% funding from the GoL was lower than the LRA funded expenditure by M14,951 million. This excess of expenditure over income was reduced by interest received from the LRA's own bank accounts of M2,74 million, and storage fees of M1,88 million. This therefore means that the deficit for the year was reduced from M14,951 million to the final deficit of

M10,3 million reported in the income statement. The final deficit was financed from the balance that, after capital expenditure, remained in the capital account. Consequently, there is only M11 430 500 left in capital account, and, because 2% of the financial estimates does not provide a sustainable level of funding, we expect that these funds will have to be used to finance a deficit in the 2004/05 financial year.

The policy of using the transitional savings to fund deficits is only a short term solution, and, looking at the projected deficit for 2004/05, there will be insufficient funds left to pay for the deficit that, on current levels of Government funding, is sure to materialise in 2005/06 when reduced Customs revenues is expected as a result of the new SACU agreement taking effect. If the LRA is unable to cover its expenses it will be technically insolvent.

In order to maintain the revenue gains made in its first year of operation and ensure its future successes, the LRA's funding mechanism must be reassessed. A review has been agreed to by the Ministry of Finance and Development Planning.

Kevin M Donovan

Commissioner General



STATEMENT OF RESPONSIBILITY OF THE GOVERNING BOARD FOR THE FINANCIAL STATEMENTS

The Governing Board is responsible for monitoring the preparation and the integrity of the Financial Statements and the related information included in this report.

In order for the Board to discharge its responsibilities, management has developed, and continues to maintain a system of internal control. The Board has ultimate responsibility for the system of internal control and reviews its operation through close involvement of the Commissioner General.

The internal controls include a risk-based system of internal accounting and administrative controls designed to provide reasonable but not absolute assurance that assets are safeguarded and that transactions are executed and recorded in accordance with generally accepted business practices and the organisation's policies and procedures. These controls are implemented by trained personnel with appropriate segregation of duties, are monitored by management and include a comprehensive budgeting and reporting system operating within strict deadlines and appropriate control framework.

The Financial Statements are prepared in accordance with Statements of Lesotho Generally Accepted Accounting Practice and are based on appropriate accounting policies supported by reasonable and prudent judgment and estimates. There are no events that occurred after the balance sheet date that would have a material impact on these Financial Statements.

In the Financial Statements, reference to Statements of Lesotho Generally Accepted Accounting Practice has been given the same meaning as Statements of International Financial Reporting Standards.

These Financial Statements set out on pages 26 to 35 were approved by the Board, and signed on its behalf by:

A handwritten signature in black ink, appearing to read 'Lineo Tshabalala'.

Lineo Tshabalala

Chairperson

21 June 2004

A handwritten signature in black ink, appearing to read 'Kevin M Donovan'.

Kevin M Donovan

Commissioner General

21 June 2004



REPORT OF THE INDEPENDENT AUDITORS TO THE MEMBERS OF LESOTHO REVENUE AUTHORITY

We have audited the books records and accounts of Lesotho Revenue Authority for the 19-month period ended 31 March 2004, and have obtained information and explanations, which to our knowledge and belief were necessary for the purpose of our audit.

RESPECTIVE RESPONSIBILITIES OF GOVERNING BOARD AND AUDITORS

These financial Statements are the responsibility of the governing Board. Our responsibility is to report on these financial statements.

BASIS OF OPINION

We conducted our audit in accordance with Generally Accepted Auditing Standards. These standards require that we plan and perform the audit to obtain reasonable assurance that, in all material respects, fair presentation is achieved in the financial statements. The audit included an evaluation of the appropriateness of the accounting policies; an audit, on a test basis, of evidence supporting the amounts and disclosure included in the financial statements; an assessment of reasonableness of significant estimates; and a consideration of the appropriateness of the overall financial statement presentation.

OPINION

We considered that our audit procedures were appropriate in the circumstances to express our comments presented below.

The Memorandum of Understanding Government of Lesotho (Ministry of Finance and Development Planning) and the Lesotho Revenue Authority provides for the transference of all assets (non-moveable and moveable) free of charge previously held by the Departments of Customs and Excise, Sales Tax and Income Tax, to the Lesotho Revenue Authority. These assets have not yet been valued and included in these financial statements, since they were never recorded by the Authority's predecessors.

Except for any adjustments which may be required due to the above, to the best of our knowledge and belief and on information supplied to us, the financial statements set out on pages 26 to 35 reflect a true and fair view of the state of the Authority's affairs at 31 March 2004 of its excess expenditure over income and cash flow for the period then ended in accordance with International Financial Reporting Standards.

A handwritten signature in black ink that reads 'Moores Rowland'.

Moores Rowland

Chartered Accounts (L)

Maseru

25 June 2004



INCOME AND EXPENDITURE STATEMENT

for the 19 months ended 31 March 2004

	Notes	2004 M
INCOME		
Government funding		52 200 000
DFID grant received	10	15 158 158
Interest received		2 739 055
Storage income		1 879 213
Commission received		20 200
Total income		71 996 626
EXPENDITURE		
Costs of collection:		
Staff related expenses		38 212 968
Inspection and enforcement expenses		1 503 434
Total costs of collection		39 716 402
Administration expenses:		
Staff related expenses		9 801 145
Administration expenses		16 522 566
Vehicle running expenses		246 111
Computer related expenses		864 353
Total administration expenses		27 434 175
DFID grant expenditure	10	15 158 158
Total expenditure		82 308 735
Excess expenditure over income	3	(10 312 109)



B A L A N C E S H E E T

as at 31 March 2004

	Notes	2004 M
ASSETS		
Non-current assets		
Property, plant and equipment	4	10,920 644
Current assets		
Accounts receivable	5	175 185
Bank and cash	6	23 184 422
Collection Accounts	7	64 176 557
		87 536 164
TOTAL ASSETS		98 456 808
CAPITAL AND LIABILITIES		
Capital and Reserves		
GoL funding		32 663 254
Accumulated excess expenditure over income		(10 312 109)
		22 351 145
Non-current liabilities		
Provisions	8	3 395 883
Current liabilities		
Collection accounts	7	64 176 557
Accounts payable and accruals	9	3 442 559
Interest accrued		5 090 665
		72 709 781
TOTAL CAPITAL AND LIABILITIES		98 456 808



STATEMENT OF CHANGES IN CAPITAL AND RESERVES

for the 19 months ended 31 March 2004

	GOL Funding M	Accumulated excess expenditure over income M	Total M
Balance at date of inception	–	–	–
Excess expenditure over income for the 19 month period ended 31 March 2004	–	(10 312 109)	(10 312 109)
GoL funding	32 663 254	–	32 663 254
Balance at 31 March 2004	32 663 254	(10 312 109)	22 351 145



CASH FLOW STATEMENT

for the 19 months ended 31 March 2004

	2004 M
CASH GENERATED FROM OPERATING ACTIVITIES	
Excess expenditure over income	(10 312 109)
Adjustment for:	
Depreciation	2 911 147
Changes in working capital:	
Increase in accounts receivable	(175 185)
Increase in accounts payables, accruals, collection accounts and interest accrued	72 709 781
	65 133 634
CASH UTILISED IN INVESTING ACTIVITIES	
Purchase of property, plant and equipment	(13 831 792)
Net cash outflow from investing activities	(13 831 792)
CASH FROM FINANCING ACTIVITIES	
GoL funding	32 663 254
Provisions for long term employee benefits	3 395 883
Net cash inflow from financing activities	36 059 137
INCREASE IN CASH AND CASH EQUIVALENTS AT 31 March 2004	87 360 979



NOTES TO THE FINANCIAL STATEMENTS

for the 19 months ended 31 March 2004

1. BACKGROUND

Lesotho Revenue Authority (LRA) was established in 2001 in terms of the Lesotho Revenue Authority Act No. 88 of 2001. LRA started operations on 1 September 2002, but was officially launched on 27 January 2003. As a result thereof, the financial statements are for the 19 month period from the start of operations to 31 March 2004. LRA's objective is the efficient and effective collection of revenue on behalf of the Government of Lesotho. To this end the LRA is required by the Act to:

- Administer and enforce the laws set out in the; Customs and Excise Act 1982, Income Tax Act 1993, Sales Tax Act 1995 and Value Added Tax Act 2001.
- To promote voluntary compliance with tax laws;
- To take such measures as may be required or necessary to counteract tax fraud and other forms of fiscal evasion.
- To advise the Minister on matters of revenue policy and matters relating to the administration and collection of revenue under the laws listed above;
- To keep proper books of account and other records which disclose with reasonable accuracy the financial position of the Authority.

Financial Statements have not been previously prepared. Therefore, there are no comparative figures included in these financial statements.

2. STATEMENT OF ACCOUNTING POLICIES

2.1 Basis of Accounting

The financial statements are prepared on the historical cost basis of accounting, and comply with Statements of Lesotho Generally Accepted Accounting Practice and therefore, International Financial Reporting Standards.

2.2 Income

Income represents funds received from the Government of Lesotho, interest on investments, storage income and grants and commission received during the period. Income is accounted for using the accrual basis of accounting and taking into account the terms of the relevant agreements. DFID grant received is accounted for in accordance with the policy stated in note 12.



NOTES TO THE FINANCIAL STATEMENTS

(continued)

2.3 Property, plant and equipment

All property, plant and equipment are initially recorded at cost. Depreciation is calculated on the straight line method to write off the cost of each asset to their residual values over their estimated useful lives as follows:

Property	10%
Motor vehicles	25%
Furniture and fittings	10%
Office equipment	20%
Computer equipment	33%

2.4 Employee benefits

Short term employee benefits

The costs of all short term employee benefits is recognised during the year in which the employee renders the related service.

The provision for employee entitlements to wages, salaries, and annual sick leave represents the amount which the Authority has a present obligation to pay as a result of employees' services provided to the balance sheet date. The provisions have been calculated at amounts based on wage and salary rates that prevailed over the reporting period.

Long-term employee benefits

The Authority is bound to two long term benefits:

- The severance pay entitlement provided by section 79 of the Labour Code 1992.
- The gratuity granted to contract staff, on completion of their contract of employment.

The respective provision for the above employee entitlements have been accounted for progressively under non-current liabilities.

2.5 Financial assets and liabilities

Financial assets

LRA's principal financial assets are cash and cash equivalents, which comprise collection accounts, bank balances and cash on hand, and deposits and prepayments. These assets are stated at their nominal value and provisions are made against assets where there is a permanent impairment in the expected recoverable amounts from the assets.

Financial liabilities

Financial liabilities are classified according to the substance of the contractual agreement entered into.

Significant financial liabilities include accounts payable and accruals, stated at their nominal value.



NOTES TO THE FINANCIAL STATEMENTS

(continued)

3. EXCESS EXPENDITURE OVER INCOME

M

Excess expenditure over income is stated after charging:

Board fees and expenses	792 344
Provision for Auditor's remuneration	252 621

1 044 965

4. PROPERTY, PLANT AND EQUIPMENT

	Cost	Accumulated depreciation	Carrying amount
	M	M	M
Owned assets			
Land	29 128	–	29 128
Motor vehicles	3 607 461	889 064	2 718 397
Furniture and fittings	1 852 420	267 496	1 584 924
Office equipment	654 766	86 296	568 470
Computer equipment	7 688 016	1 668 291	6 019 725
	13 831 792	2 911 147	10 920 644

The carrying amounts of property, plant and equipment for the 19 months period ended 31 March 2004 can be reconciled as follows:

	Carrying Amount at beginning of period	Additions	Depreciation	Carrying Amount at end of period
	M	M	M	M
Owned assets				
Land	–	29 128	–	29 128
Motor vehicles	–	3 607 461	889 064	2 718 397
Furniture and fittings	–	1 852 420	267 496	1 584 924
Office equipment	–	654 766	86 296	568 470
Computer equipment	–	7 688 016	1 668 291	6 019 725
	–	13 831 792	2 911 147	10 920 644

5. ACCOUNTS RECEIVABLE

M

Deposit	19 598
Prepayments	94 790
Interest receivable	60 797

175 185



NOTES TO THE FINANCIAL STATEMENTS

(continued)

6. BANK AND CASH	M
LRA ordinary call account	10 158 272
LRA current account	263 125
Gratuity account	2 002 577
88 day deposit account	10 737 427
Cash on hand	23 021
	23 184 422
7. COLLECTION ACCOUNTS	
VAT bank accounts	4 565 355
SACU	29 893 937
Customs and Excise bank accounts	28 088 406
Income Tax bank accounts	1 628 859
	64 176 557
The above accounts represent monies collected on behalf of GOL and SACU and held on their behalf pending transfer to the respective institutions.	
8. PROVISIONS	
Gratuity	2 157 393
Severance pay	1 238 489
	3 395 883
9. ACCOUNTS PAYABLE AND ACCRUALS	
Creditors	307 261
Provisional duty	272 635
Other accruals	2 408 705
Employee related accruals	453 959
	3 442 559

10. DFID GRANT RECEIVED AND GRANT EXPENDITURE

A grant for technical assistance was received from DFID (The UK Department for International Development) amounting to GBP 1 185 832. The amount was paid directly to the suppliers for services rendered and no monies were received by LRA. The grant was converted to local currency at the average exchange rate for the period and reflected as income with a corresponding charge against expenditure.



NOTES