sait South African Institute of Tax Professionals

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Dear Ms Nkumanda and Ms Collins

RE: CALL FOR COMMENT: DRAFT TAXATION LAWS AMENDMENT BILL, 2014

Thank you for the opportunity to contribute commentary on the draft Taxation Laws Amendment Bill, 2014.

All commentary is developed from both an internal review of the provisions as well as from consultations with members, stakeholders and industry. The commentary reflects the collective view of members, stakeholders and industry role players consulted.

Please note that all references to 'clause' refer to a clause of the draft Taxation Laws Amendment Bill, 2014, unless indicated otherwise.

PART A: CORPORATE TAX

Set out below, is the consolidated commentary on the **corporate tax issues only.**

1 DIVIDENDS TAX: CONTRIBUTED TAX CAPITAL REFINEMENTS (clause 1/definition of 'contributed tax capital' in s 1 of the Act)

1.1 Order of words in clause 1(d)

Problem statement:

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The wording of clause 1(d) may be reorganised to ensure that the style of the proposed par (b) of the definition of 'contributed tax capital' in section 1 of the Act is consistent with that of the rest of the Act. Clause 1(d) in its current form reads as follow '*in relation to a class of shares issued by a company*, *in the case of any other company, and amount equal to the sum of-*'

Proposed solution / recommendation:

It is proposed that the reference to '*in the case of any other company*' should precede the reference to '*in relation to a class of shares issued by a company*'.

1.2 Possible drafting error in clause 1(f)

Problem statement:

There appears to be a drafting error in clause 1(f) relating to the proposed paragraph (b)(iii) of the definition of 'contributed tax capital' in section 1 of the Act. The reference to 'an amount equal to the sum of' is placed in item (aa) of paragraph (b)(iii).

Proposed solution / recommendation:

It is proposed that the words *'an amount equal to the sum of'* in the proposed par (b)(iii)(aa) be placed immediately after '*occurrence of any specified contingency*' in par (b)(iii) of the definition of 'contributed tax capital' and that it should be deleted in the par (b)(iii)(aa) of the definition.

2 DEFINITION OF 'POST-1990 GOLD MINE' (clause 1(1)(k))

The *draft Explanatory Memorandum on the Taxation Laws Amendment Bill*, 2014 ('EM') at 7(1)(k) notes that the amendment to the 'post-1990 gold mine' definition is merely because a 'mining authority' no longer exists in the Mineral and Petroleum Resources Development Act ('MPRDA') which replaced the Minerals Act in 2004. However, in respect of the definition and the application of such definition in section 36(11), that is not the only problem and it is submitted that the proposed amendment just exacerbates the problems. It is submitted tat various amendments are required to correct the law after the implementation of the MPRDA which substantially changed how the Department of Mineral Resources ('DMR') approves mining operations and how minerals are owned by taxpayers. We set out in detail our various concerns below.

2.1 Definition of post-1990 gold mine – Mining permit

Problem statement:

The proposed definition does not solve the problems created by the MPRDA. Firstly, the proposed addition of only 'mining permit' as per section 27 of the MPRDA results limiting the

definition in post-2004 mines to those who can exploit minerals in less than two years in an area of less than 5 hectares (i.e. small scale mining). The reliance on 'mining permit' as defined in the MPRDA as being an authorization to commence mining in all instances is therefore misplaced.

Proposed solution / recommendation:

At the very least 'mining permit' (i.e. section 27) and 'mining right' (i.e. section 23) should apply as it is actually the latter which would mainly apply to gold mines.

2.2 Definition of post 1990-gold mine – Independent workable proposition

Problem statement:

The proposed definition still contains the requirement of 'independent workable proposition' as determined by DMR as applying to both pre and post-2004 mines. This term also does not exist in the MPRDA anymore due to the change in the manner how minerals are owned and exploited following the MPRDA.

In terms of section 23(1)(a) the Minister must, on deciding to issue the mining right, determine if the mineral can be mined optimally in terms of the submitted mining work program and in section 23(1)(c) that the financing plan is compatible. It is therefore at such stage that a determination is made before the mineral right is even awarded. Historically, persons could own a right to minerals which could be not independently workable and for which they were not compelled to exploit, hence a determination had to be done at the future date once the person decided to exploit the minerals to which the mineral right pertained. It is submitted that following the MPRDA that position does not exist anymore and SARS insistence on DMR continuing to make these determinations that seemingly don't exist is confusing to all concerned.

Furthermore, the conversion of old order common law mining rights to new order mining rights should also be considered, especially as a mining right that is converted is not technically issued for the first time after 1 May 2004 and these rights co-existed with new order rights for 5 years after 1 May 2004 until they lapsed or were converted.

Proposed solution / recommendation:

Only pre-2004 mines should be subject to the DMR issuing a determination that it is satisfied that the mine is an independent workable proposition.

It is proposed that the definition at least state:

"'Post 1990 gold mine' means a gold mine which –

(a) In the opinion of the Director General: Mineral and Energy Affairs or his subsequent equivalent, is an independent workable proposition and in respect of which a mining authorization for gold mining was issued for the first time after 14 March 1990 in terms of the repealed Minerals Act 1990; or
(b) A mining permit or mining right for gold mining, has been issued for the first time or constitutes the conversion of an old order mining right as defined in section 1 of the Mineral and Petroleum Resources Development Act, on or after 1 May 2004 in terms of the Mineral and Petroleum Resources Development Act;".

2.3 Post-1990 gold mine – Scope of section 36(11)

Problem statement:

The capital allowances available to post-1990 gold mines in section 36 per the definition of 'capital expenditure' in section 36(11), do not apply in terms of (aa)(B) for any period that mining operations are not carried on in respect of the terms of the relevant:

- Prospecting right;
- Mining right;
- Exploration right;
- Production right;
- Mining permit; or
- Retention permit

issued in terms of the MPRDA.

If it was therefore the original intention of the legislature to purposefully limit the definition of 'post-1990 gold mine' after the MPRDA to only mining right and mining permit, why did it include all the other rights in the prohibition listed above if the holder of such rights could never qualify as a 'post-1990 gold mine' by definition and therefore never qualify under section 36?

Proposed solution / recommendation:

It is submitted that National Treasury revisit the policy in respect of the scope of the definition of 'post-1990 gold mine'. Should it want to impose a policy that allows the allowances for all the rights listed above, the definition of 'post-1990 gold mine' should be amended. However, if policy is to limit the allowances to the holders of mining rights and permits, then the proviso should be accordingly amended to exclude rights that don't conform to the definition in the first instance.

3 TAX TREATMENT OF ALLOWANCES IRO PUBLIC PRIVATE PARTNERSHIPS (clauses 23 & 13(1)(k)/s12NA, s10(zI)&s12N)

3.1 Effective dates of clause 13(1)(k) and 23(1)

Problem statement:

The effective date of for clause 13(1)(k) and 23(1) as indicated in clause 13(7) and 23(2) is '… *1 January 2015 and applies in respect expenditure incurred to effect improvements during any year of assessment commencing on or after that date*'. However, the EM indicates the effective date as being 1 April 2015.

Proposed solution / recommendation:

It is proposed that the reference to '1 April 2015' in the EM be changed to '1 January 2015'.

3.2 Scope of section 12NA

Problem statement:

The EM at 4.3 indicates that the purpose of 12NA is in essence to extend the relief in section 12N in instances where the right of use or occupation is with government and not with the private party. No indication is given that the scope of the relief should be less than what is currently in section 12N. However, unlike section 12N, the proposed section 12NA only applies to improvements effected in terms of a Public Private Partnership ('PPP') which is limited to national and provincial government. From a public policy perspective, there is seems to be no reason as to why a private party should be excluded from the proposed relief provided by section 12NA of the Act if the other party to the transaction is a municipality or any organ of state or sphere of government as listed in section 12N(1)(b).

Proposed solution / recommendation:

It is proposed that the allowance provided by the proposed section 12NA include the same spheres of government and organs of state as listed in section 12N(1)(b) where such private persons enter into agreements providing service access to those spheres of government and organs of state.

3.2 Scope of section 12N

Problem statement:

The *Explanatory Memorandum on the Taxation Laws Amendment Bill,* 2013 explained at 2.8 why the legislature intended to increase the scope of improvements to include voluntary improvements and not just obligatory improvements. To implement this proposal, section 40(1) of the Taxation Laws Amendment Act 2013 amended section 12N(1)(b) by deleting the words '*incurs and obligation to effect*.

However, it is submitted that the mere deletion of these words do not give the intended result, namely by allowing allowances on voluntary improvements as the wording in section 12N(1)(b) still requires that the improvements must be effected *in terms of* (i) a PPP (which is an agreement) and (ii) and an *agreement* granting the right of use. To include voluntary improvements the said improvements would have to be other than in terms of the PPP agreement and agreement providing the right of use.

Proposed solution / recommendation:

It is proposed that section 12N(1)(b) amended as follows:

'*effects an improvement on the land or building, whether voluntarily or by agreement, in respect of –* '.

4 EXEMPTIONS OF GRATUITIOUS FUNDING IN THE HANDS OF SMME'S (clause 13(1)(l)&36(1))/s10(1)(zK)&23O)

Problem statement:

Although the exemption of funding received is welcome, as noted above it is uncertain as to why small businesses, other than those that qualify as a 'Small Business Corporation' or 'micro-business' as defined are excluded from receiving this exemption as the limitation of the tax regimes applicable to those specific small business were done for a different reason.

Proposed solution / recommendation:

Similar to the small business funding entity requirements, the exemption should also not be limited to only these tax specific small businesses.

5 REVISION OF R&D INCENTIVE (clause 17 & draft regulations/s11D)

5.1 The effective date of the draft regulations on section 11D(1)(d) and (e) (clause 17(3))

Problem statement:

In terms of clause 17(3), clause 17(1)(c) is deemed to have come into operation on 1 October 2012 and applies in respect of expenditure incurred on research and development on or after that date, but before 1 October 2022. However, the draft Regulations in terms of section 11D(1)(d) of the Income Tax Act, 1962, on the other criteria for multisource pharmaceutical products for the purpose of the deduction for research and development ('section 11D(1)(d) regulations') and the Regulations in terms of section 11D(1)(e) of the Income Tax Act, 1962, on the additional criteria for clinical trials in respect of the deduction for research and development ('section 11D(1)(e) regulations') is deemed to have come into operation on 1 January 2014.

Proposed solution / recommendation:

It is proposed that the effective date of the two draft Regulations be backdated to 1 October 2012 to ensure that it is aligned with the effective date of the insertion effected by clause 17(1)(c) of the TLAB.

5.2 Definition of formulation and reformulation in the section 11D(1)(d) draft Regulations

Problem statement:

The draft regulation does not define the terms 'formulation' and 'reformulation' which may cause difficulties when determining whether an activity might qualify for approval in terms of section 11D(9) of the Act.

Proposed solution / recommendation:

The terms 'formulation' and 'reformulation' should be clarified by inserting a definition of each in the draft Regulations.

5.3 Short title of the section 11D(1)(d) draft Regulations

Problem statement:

It seems as if there is a typing error in the short title of the section 11D(1)(d) regulations as it read as follow in par 4(a) of the said regulation (emphasis ours):

> *'are called the Regulations in terms of section 11D(9)(d) of the Income Tax Act, 1962, on the other criteria for multisource pharmaceutical products for the purpose of the deduction for research and development'.*

Proposed solution / recommendation:

It is proposed that the reference to 'section 11D(9)(d)' in par 4(a) of the regulations be changed to 'section 11D(1)(d)' in order to align the name of the regulations with those issued under section 11D(1)(e).

6 REVISION OF SMALL BUSINESS CORPORATION (SBC) TAX RELIEF (clause 19/s12E(4)(a)(i))

6.1 Replacement of the SBC regime

Problem statement:

The statement that the SBC regime does little to support small business growth appears to be contrary to the findings of a survey done by SAIT amongst its members. The results of the survey indicated that the SBC regime provided a substantial benefit to small businesses in the form of reduced taxes having to be paid as well as an upfront deduction of the cost of manufacturing assets. The cash flow of these entities was thus immediately improved. We refer to our letter sent to National Treasury dated 23 June 2014 for further findings of this research.

It is also evident that many businesses chose to be on the SBC regime rather than the turnover tax regime ('TT regime') despite the fact that their 'turnover' was R1 million or less (indicating that they could potentially also qualify for the TT regime). When asked why this was the case, it was found that the main reason was that they would have paid more tax on the TT regime (this is particularly true for businesses that were in a loss position). The SBC regime clearly did support small businesses, and in some cases, it supported small businesses more than the TT regime did. Reasons for replacing the SBC regime with an annual refundable tax compliance rebate (RCR) are thus not clear as it was clearly benefiting small businesses according to the findings of SAIT's survey.

<u>Proposed solution / recommendation:</u>

Only 7 827 businesses were registered on the TT regime in 2012 according to the Davis Committee report. This report also stated that 34 391 businesses had taxable income of R1 million or less and could potentially have chosen the TT regime over the SBC regime but appeared not to have chosen this option. If just the numbers of businesses are taken into account it seems strange that a system that is more widely used is being replaced by a system that is less widely used by small businesses.

We suggest that more consultations and research be performed to establish exactly why businesses chose the SBC regime over the TT regime before a system that appears to be working is replaced in its entirety. The TT regime should also be simplified in order to have any chance of the RCR regime working.

It is submitted that the RCR proposal should be withdrawn until such time as its replacement of the SBC regime can be justified by the relevant facts.

6.2 Refundable tax compliance rebate (RCR) – to replace SBC regime

<u>Problem statement:</u>

It is proposed that the SBC regime be replaced with a RCR of R15 000. Furthermore, all businesses with a turnover of between R1 million and R20 million will pay tax at a rate of 28% as opposed to the sliding scale previously afforded to SBCs. It is assumed that these entities will not be afforded the accelerated asset write offs anymore either, although the amendments are silent on this matter.

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The introduction of a RCR is welcomed for small businesses with a taxable income of R53 574 or less as they will be in a better position than they were using the SBC regime. However, for businesses with a turnover of more than this amount, they will be in a worse off position than if they were on the SBC regime. A small business with taxable income of more than R550 000 (4 519 businesses per the Davis Committee report) will stand to lose R79 298 each year if the new RCR system is introduced. This is a substantial amount that could be used by a small business to employ an additional staff member or purchase assets or trading stock.

Proposed solution / recommendation:

It should be clarified whether the SBCs will still be entitled to the accelerated asset write off periods or not.

The intention of the NDP is to assist small businesses, however, the proposed RCR appears to do the opposite for small businesses that have a taxable income of more than R53 574. Further research and consideration of the proposed changes is warranted. If the RCR regime is to be implemented, it should rather replace the turnover tax to benefit taxpayers with a taxable income of less than R53 574.

6.3 Refundable tax compliance rebate (RCR) - value

Problem statement:

The purpose of the RCR of R15 000 is to assist small businesses with their tax compliance costs. Research conducted by Prof. Sharon Smulders in 2012 indicated that internal tax compliance costs for small businesses amount to R53 356 per annum (with external costs amounting to just under R10 000 per annum). It is evident that the R15 000 is relatively low compared to the total tax compliance costs actually incurred by small businesses.

Proposed solution / recommendation:

Although it is recognized that the National Treasury cannot fully subsidize the tax compliance costs for small businesses, it is evident that the R15 000 is not sufficient for small businesses taking into account the fact that small businesses with taxable income of more than R53 574 will be worse off than they were under the original SBC regime.

Consideration should be given to varying the RCR according to the taxable income band as such a fixed incentive would have the unintended effect of encouraging small businesses to remain small. This is because the fixed amount of R15 000 is a constant and would amount to a much higher relative percentage of tax payable for a smaller business then for a larger one. In our view, the current graduated rate system should be retained or, alternatively, a graduated compliance rebate system which increases to say R100 000 at the highest levels of taxable income (incorporating measures to prevent abuse) should be implemented.

6.4 Refundable tax compliance rebate (RCR) – eligibility

Problem statement:

The RCR of R15 000 will be available to small businesses only if they are compliant in terms of their tax returns and liabilities. It is unclear whether all taxes (that is income tax, VAT, PAYE etc.) and its returns are referred to in the proposals. It is also uncertain when this rebate will be available to the small business on assessment only. Furthermore, the postponement of this RCR will also negatively impact a small business' cash flow.

Proposed solution / recommendation:

It should be made clear when this refund can be taken into account in order to reduce the tax liability of a small business. Furthermore, clarity should be provided in the legislation as to exactly what tax return and liabilities a small business should be compliant with in order to receive this RCR and at what point in time this determination is made. In an ideal world taxpayers would be continuously 100% compliant yet in reality this is seldom if ever the case. Taxpayers should have some time period to work to, for example as on date of submission of the return the taxpayer is fully compliant.

7 BROADENING THE SCOPE OF THE VENTURE CAPITAL COMPANY REGIME (clause 22(1)/s12J)

Problem statement:

The amendments to section 12J are welcomed, however, it will need to be seen if these changes are sufficient to increase the uptake of this regime.

Proposed solution / recommendation:

Further consultations on these proposals should be performed to establish if these changes are sufficient and actually address the reasons for the low uptake of the regime. Further amendments should be made if necessary.

8 DEDUCTIBLE INTEREST LIMITATION IRO DEBTS OWED TO PERSONS NOT SUBJECT TO TAX (clause 24/s23M)

Problem statement:

SAIT wishes the National Treasury to again consider SAIT's submission made on 19 June 2014 to the National Treasury (hereto attached as **Annexure A**) setting out various additional concerns regarding section 23M.

Overall, concerns were raised that capping the debtor's interest deduction at 60 per cent of its 'adjusted taxable income' to combat base erosion has no conceptual basis. No measures to protect the *fiscus* currently apply to businesses not subject to section 23M that are entitled to a full deduction of their interest incurred, irrespective of the level of the interest rate. Debtors suffer economically during times of high interest rates and it is believed that section 23M would cause such debtors to suffer further by limiting their interest deduction.

We would also like to point out that the definition of 'adjusted taxable income' in section 23M(1) does not contain an adjustment for special allowances such as the research and development allowance contained section 11D of the Act, which may cause the adjusted taxable income to be extremely low.

Proposed solution / recommendation:

Please refer to the SAIT submission for specific recommendations. We also refer you to the SAIT submission on international matters that deal with the policy concerns regarding the treatment of interest in the various sections in the Income Tax Act, which include section 23M.

We suggest that the implementation of section 23M be delayed beyond 1 January 2015 in order to ensure that legitimate commercial transactions are not undermined.

We further propose that a par (b)(iv) be added to the definition of 'adjusted taxable income' in section 23M(1) allowing the section 11D allowance to be added back in calculating the adjusted taxable income.

9 PBO: LOWERING THE DISTRIBUTION REQUIREMENT (clause 27/s18A(2D)(b)(i)&(ii))

9.1 Timing of the distribution requirement

Problem statement:

The proposed section 18A(2D)(b)(i), introduced by clause 27(1)(b) would have the effect that section 18A(1)(b) PBOs incorporated after 1 January 2015, would have to distribute all amounts received or accrued in respect of financial instruments held by it to section 18A(1)(a) PBOs by no later than every five years from the date that the section 18A(1)(b) PBO received its reference number from the Commissioner. The proposed section 18A(2D)(b)(ii) would place the above distribution obligation on section 18A(1)(b) PBOs incorporated before 1 March 2015 for '*… every five years from the date of the coming into operation of the Taxation Laws Amendment Act, 2014 …*'

This provision may be cumbersome to administer for section 18A(1)(b) PBO's as they would have to keep track of their distributions on a date other than the end of their years of assessment. In practice, distributions are normally only determined at the end of the year.

Proposed solution / recommendation:

It is suggested that all section 18A(1)(b) PBOs should monitor their distributions from the end of the year of assessment rather than the date they received their reference numbers or the date the Taxation Laws Amendment Act, 2014 becomes effective. It is therefore proposed that the deadline for distribution be 'by the end of the year of assessment ending immediately after the fifth anniversary' of the date on which the PBO received its reference number (in the case of section 18A(2D)(b)(i) PBO's) or the date of coming into operation of the Taxation Laws Amendment Act, 2014 (in the case of section 18A(2D)(b)(i) PBO's).

9.2 Scope of the distribution requirement

Problem statement:

The wording of the proposed section 18A(2D), preceding paragraph (a) of the said section, does not clearly refer to which amounts must be held in the form of financial instruments issued by the institutions listed in subparagraph (i). Although cross reference is made to sec 18A(2A)(b)(i), which deals with the distribution obligation of donations received in respect of which section 18A receipts were issued, there may still be room for doubt whether all other income (i.e. income derived from trading activities or from donations received for which no section 18A receipts were issued) may fall within the scope of the proposed section 18A(2D). This is as a result of the reference to (emphasis ours) '... *in respect of any amount that is not distributed as contemplated in subsection (2A)(b)(i)*...' in the proposed section 18A(2D).

The above ambigiuty then filters through to the proposed section 18A(2D)(b) which imposes the 5 year distribution obligation on the section 18(1)(b) PBO's in respect of (emphasis ours) '... all amounts received or accrued in respect of financial instruments held by it ...'

It is therefore unclear whether the holding of financial instruments requirement and the five yearly distribution requirement would only apply to the donations refered to in section 18A(2A)(b)(i) which were not distributed as stated therein or whether it would apply to all other receipts and accruals *albeit* donations for which no section 18A certificates had been issued or trading income which were not exempt in terms of section 10(1)(cN)(ii) and the financial intruments pruchased with such funds.

This wider interpretation would have the effect that the section 18A(1)(b) PBO would have to distribute '... *all amounts received or accrued in respect of financial instruments held by it* ...' which may include amounts on which the PBOs may have been taxed and for which no section 18A certificates may have been issued.

Proposed solution / recommendation:

It is recommended that the proposed section 18A(2D) must be amended as follow in the words preceding paragraph (a):

'*Any public benefit organisation contemplated in subsection (1)(b), in respect of* *an* ***[any]*** *amount* *contemplated in subsection (2A)(b)(i)* *that is not distributed as contemplated in subsection (2A)(b)(i)...*'

It is further recommended that the proposed section 18A(2D)(b) be amended as follows in the words preceding subparagraph (i) (if it is practically possible for the taxpayers to seperate their protfolios into s18A investments and non-sec18A investments):

'must distribute or incur the obligation to distribute all amounts received or accrued in respect of financial instruments held by it as acquired from the funds envisaged *in subsection (2D)*, *other than amounts received…'*

10 DEDUCTIBLE INTEREST LIMITATION IRO REORGANISATION AND ACQUISITION TRANSACTIONS (clause 35(1)/s23N)

The proposed change to allow the previous year's assessed losses to be excluded from the current year's adjustable taxable income is most welcome.

10.1 Amount of adjusted taxable income (clause 35(1)(b))

Problem statement:

Clause 35(1)(b) does not specify which amount to use in the proposed section 23N(3)(b) of the Act as it requires use of a percentage of the adjusted taxable income for what we assume is one of the three years of assessment listed in the proposed 23N(3)(b)(i)-(iii)

Proposed solution / recommendation:

It is proposed that clause 35(1)(b) specifically states which amount must be used in the proposed section 23N(3)(b) of the Act. It is assumed that the intention is for the debtor to elect the highest 'adjusted taxable income' from the three years of assessment.

10.2 Prior to the year of assessment (clause 35(1)(b))

Problem statement:

It is not clear whether the reference to '*prior to the year of assessment …*' in the proposed section 23N(3)(b)(iii) refers to the year of assessment immediately preceding the year of assessment in which the acquisition transaction or reorganisation transaction was entered into or whether it refers to any year of assessment prior to the year of assessment in which the acquisition transaction or reorganization transaction was entered into, though we assume it refers to the former.

<u>Proposed solution / recommendation:</u>

It is further proposed that the reference to *'prior to the year of assessment contemplated in subparagraph (i)'* in the proposed section 23(3)(b)(iii) should be '*immediately preceding the year of assessment contemplated in subparagraph (i)*'.

11 TAX INCENTIVES FOR PROVISION OF FUNDING TO SMME'S (clause 13, 46 & 65/ s10, 30C & 64F)

11.1 Scope of tax incentive

<u>Problem statement:</u>

The changes to these sections are most welcome, however, the proposed section 30C(1)(b)(i) requires that the sole objective of the small business funding entity is the provision of funding to small, medium and micro-sized enterprises. 'Small, medium or micro-sized enterprise' is inserted into section 1 of the Income Tax Act and is defined as a person that qualifies as a micro business as defined in paragraph 1 of the Sixth Schedule or a small business corporation as defined in section 12E(4). The proposed amendment to section 12E(4) would lead to a 'small business corporation' being defined as (<u>emphasis ours</u>)'*… any close corporation or co-operative or any private company <u>as defined in section 1 of the Companies Act</u> if at all times during the year of assessment <u>all the holders of shares</u> in that company, co-operative or close corporation <u>are natural persons</u>, where the gross income for the year of assessment is not less than an amount of R1 million but does not exceed an amount of R20 million …*'. It is thus clear that not all small, medium or micro-enterprises would fall within this definition and thus the application of section 30C(1)(b)(i) is also limited. The concerns regarding SBC as to splitting of income etc. is also not applicable here as the incentive is for the investor not the investee.

<u>Proposed solution / recommendation:</u>

Section 30C should be expanded to include funding provided by small business funding entities to include all SMMEs and not only those that qualify as SBC's in section 12E(4) or microbusinesses as defined in par 1 of the Sixth Schedule.

11.2 Scope of funding of a 'small business funding entity'

<u>Problem statement:</u>

The proposed section 30C(1)(b)(ii)(aa) requires that the small business funding entity's funding must be provided (emphasis ours) '…*for the benefit of, or is widely accessible to all small, medium and micro-sized enterprises*'. It is submitted that the wording of section 30C(1)(b)(ii)(aa) is too restrictive as it would prevent an entity from obtaining approval as a 'small business funding entity' in terms of section 30C if the entity only wishes to fund a specific industry.

Proposed solution / recommendation:

It is proposed that section 30C(1)(b)(ii)(aa) allow the entity to fund a specific industry and not to discriminate further as to whom will receive funding within a specific industry. It is, however, acknowledged that it would be difficult to determine exactly how to achieve this outcome in section 30C(1)(b)(ii)(aa).

11.3 Limitation on the distribution of funds

Problem statement:

Section 30C(1)(d)(iv) currently states that a 'small business funding entity' may not distribute any of its funds or assets to, *inter alia*, any employee, founder or donor in relation to that entity. This prohibition does not cater for the payment of a *bona fide* salary to an employee of such funding entity.

Proposed solution / recommendation:

It is proposed that section 30C(1)(d)(iv) state that a small business funding entity may not distribute any of its funds or assets to, *inter alia*, any employee… 'other than as set out in subsection (1)(b)(ii)(cc)'.

11.4 Ownership in business of connected person

Problem statement:

The requirement in subsection 30C(1)(d)(ix) that the small business funding entity not have a share or other interest in any business, profession or occupation which is carried on by the persons contemplated in subparagraph (i), does not extend to connected persons in relation to such committee, board or management.

Proposed solution / recommendation:

Should it be the intention to prevent all connected party management relationships, the exclusion should be extended to '*any person contemplated in subparagraph (i) or any person who is a connected person in relation to such person*'. The requirement can currently be

circumvented by, for example, having the spouse of such a person hold the share or other interest as it currently only requires the management to not be connected to each other.

11.5 Effective dates of proposed sections 10(1)(cQ), 10(1)(zK), 30C, 23O & 64F

Problem statement:

There seems to be a problem with the effective dates of the various provisions pertaining to the 'small business funding entities' and the relief provided to the 'small, medium or micro-sized enterprises'. The effective dates of the proposed sections 30C and 64F is 1 April 2015, whilst the exemption to be provided through the proposed section 10(1)(cQ) would become effective on 1 March 2015. Furthermore, the proposed sections 10(1)(zK) and 23O have an effective date of 1 March 2015.

Proposed solution / recommendation:

In order to align the effective dates applicable the concessions made to 'small business funding entities' and 'small, medium or micro-sized enterprises', it is proposed that the effective dates of the proposed section 30C and 64F be made 1 March 2015.

11.6 Reapplication

Problem statement:

Section 30C contains no equivalent to section 30(8), whereby a small business funding entity may reapply for approval.

Proposed solution / recommendation:

Such equivalent should be inserted.

11.7 Insertion of section 64F(1)(i)

Problem statement:

Clause 65(1)(b) determines that the amendment must replace a provision (section 64F(1)(i)) that was deleted by section 78(1)(c) of the *Taxation Laws Amendment Act* (No. 24 of 2011). It is, however, submitted that it is incorrect to insert a new paragraph into the place of a paragraph that was previously deleted.

Proposed solution / recommendation:

It is proposed that the proposed amendment be inserted as section 64F(1)(o) to ensure that the insertion is consistent with the general rules associated with drafting legislation.

12 ALLOWANCE IN RESPECT OF ENVIROMENTAL CONSERVATION (clause 49(1)/s37C)

12.1 Rate of deduction

Problem statement:

It is accepted that a straight line write-off of market value as proposed in the new section 37D is from a higher base for many taxpayers as opposed to 10% of taxable income as was the case for section 37C read with section 18A. However it is unclear why the capital allowance rate is 4% and not at least aligned with section 13*quin* at 5%.

Proposed solution / recommendation:

The rate should be aligned with section 13quin at 5% (i.e. write off period of 20 years).

12.2 Timing of value determination

Problem statement:

For purposes of subsection 3(b) it is not clear on which date the relative market values should be determined. In our view the determination of market value of the declared land and the market value of the declared land had the land not been subject to the right of use, should be made in the year in which the land becomes 'declared land'.

Proposed solution / recommendation:

The timing of the value determination should be linked to the year of assessment in which the land became 'declared land'.

13 RETENTION OF ASSETS BY AMALGAMATED COMPANY – EXTENSION OF ASSETS RETAINED (clause 53/s44)

Problem statement:

The requirement inserted into section 44(1) by the proposed subparagraph 53(a) into the definition of 'amalgamation transaction', seeks according to the EM, to provide relief by expanding on the exclusion as to the purpose for which assets may be retained. However the wording of the proposals results in a compulsion on the amalgamated company to settle all of its debts, other than 'taxes' and liquidation debts. This proposal results in nullifying section 44(4)(b) regarding the assumption of debt.

Proposed solution / recommendation:

It is submitted that the proposed insertion of paragraph (a)(iii) to te definition of amalgamated transaction be deleted. It is proposed that paragraph (a)(i) of the definition of 'amalgamation transaction' be amended as follows:

'(a)(i) in terms of which any company (hereafter referred to as the 'amalgamated company') which is a resident disposes of all its assets (other than assets it elects to use to settle any debts incurred in the ordinary course of its trade, the reasonably anticipated liabilities to any sphere of any government of any country or any costs of administration relating to the liquidation or winding up) to another company...'.

14 RETENTION OF ASSETS BY LIQUIDATED COMPANY (clause 55/s47(1))

Problem statement:

The requirement inserted into section 47(1) by the proposed subparagraph 55(a)(ii) into the definition of 'liquidation transaction', seeks according to the EM, to provide relief by expanding on the exclusion as to the purpose for which assets may be retained. However the wording of the proposals results in a compulsion on the liquidated company to settle all of its debts, other than 'taxes' and liquidation debts if this option is used. This proposal results in nullifying section 47(3A)(b) regarding the assumption of debt which does not seem to be the intention.

Proposed solution / recommendation:

It is submitted that the proposed insertion of paragraph (a)(ii) to the definition of 'liquidation transaction' be deleted. It is proposed that paragraph (a) of the definition of 'liquidation transaction' be amended as follows:

'(a)(i) in terms of which any company (hereafter referred to as the 'liquidating company') which is a resident disposes of all its assets (other than assets it elects to use to settle any debts incurred in the ordinary course of its trade, the reasonably anticipated liabilities to any sphere of any government of any country or any costs of administration relating to the liquidation or winding up) to its shareholders…'.

15 EMPLOYMENT TAX INCENTIVE – TIMING OF REMUNERATION THRESHOLD (clause 106, 107 & 109)

Problem statement:

As presently worded in the insertion of subsection 6(f) of the Employment Tax Incentive Act, it is unclear for which period the remuneration of R6 000 or less should be received as no timing rule applies as is applicable in section 4.

Proposed solution / recommendation:

It should be clarified that the R6 000 limit applies for the month in respect of which the Employment Tax Incentive is claimed.

PART B: INTERNATIONAL TAX

Set out below, is the consolidated commentary on the **international tax issues only.**

This submission is divided into two parts. Part 1 deals with policy matters and Part 2 deals with the Institute's technical submissions on the TLAB.

PART 1 - POLICY MATTERS

1 INTEREST

Problem statement:

Currently there is a three-pronged anti-avoidance approach with regard to interest:

1) Section 23M: Excessive debt;
2) Section 31: Thin capitalization; and
3) Section 50A-H: Withholding tax on interest.

The interaction between these provisions is confusing and it is submitted that all these provisions are unnecessary; increase the compliance burden of taxpayers and are definitely not investor friendly. For instance, where taxpayers have proved that they are not thinly capitalized then the question should be asked as to why the withholding tax on interest is actually necessary.

Furthermore, the treatment of inbound financial investment from a tax perspective is still unclear as the Interpretation Note is still in draft format.

Proposed solution / recommendation:

The treatment of excessive interest should be consolidated in the Income Tax Act. Clarity on the treatment of inbound financial investments is urgently required to bring certainty to taxpayers with regard to their tax liabilities and responsibilities.

2 WITHHOLDING TAX ON SERVICE FEES (WTSF)

Problem statement:

It is unclear what exactly is meant by 'service fees received by or accrued to from a source within South Africa'. It is our understanding that the source of services is where the services are rendered and thus the need for this WTSF is questioned as there are other provisions in the Act

that deal with this. With the introduction of the WTSF in 18 months' time, clarity on these issues would be greatly appreciated.

Proposed solution / recommendation:

The rationale for this tax should be reconsidered and clearly documented.

3 SOURCE

Problem statement:

From an international tax environment the biggest changes that are coming about are due to the supply of electronic goods and services. Our source rules thus need to be clear enough to ensure that South Africa collects its fair share of the tax on these supplies. The concept of a 'resident' is clearly defined in our legislation. Currently under our law, a non-resident with South African sourced income is taxed in South Africa on that income. Although our Act mentions source and 'deemed source' such as in section 9, South Africa does not have clear source rules, especially in respect of electronic transactions.

Currently, we rely on common law to provide this information, but this has not taken into account the change in the way business is today due to the introduction of the internet and electronic services etc. The concerns about base erosion and profit shifting and the changes to the VAT legislation have, to a certain extent, tried to address this problem, but from an income tax perspective, it still needs to be clarified when a service rendered will be regarded as being from a South African source.

Proposed solution / recommendation:

Clear source rules need to be incorporated into the Income Tax Act that specifically deal with the electronic economy.

PART 2 – TECHNICAL SUBMISSIONS ON THE TLAB

1 DELETION OF PARAGRAPH (f) TO SECTION 9D(2A) (clause 11(1)(b)/par (f) to s9D(2A))

Problem statement:

Clause 11(1)(b) in its current form would have the effect that a natural person, special trust or insurer in respect of its individual policyholder fund ('IPF') would be subject to the same inclusion rate in terms of paragraph 10 of the Eighth Schedule to the Act than companies. Therefore, when calculating the net income of the controlled foreign company ('CFC') in terms of section 9D(2A), the capital gains realized by the CFC would be subject to a 66.66 per cent inclusion rate in the hands of the natural person, special trust or insurer in respect of its IPF.

If one takes the example of an individual paying tax at the maximum marginal rate, then this amendment would increase the maximum effective tax rate for the section 9D(2) imputed net income resulting from a disposal by the CFC from 13.33 per cent to 26.66 per cent. When this potential maximum effective tax rate of 26.66 per cent is compared to that of companies (18.66 per cent), then the amendment seems to be detrimental to the taxpayers listed in paragraph (f) to section 9D(2A).

Proposed solution / recommendation:

Based on the above, it is advised that clause 11(1)(b) be deleted or that some concession be made to prevent the maximum effective tax rate for these taxpayers from doubling where a CFC disposes of an asset.

2 SIMPLIFIED FOREIGN BUSINESS ESTABLISHMENT EXEMPTION FOR CONTROLLED FOREIGN COMPANIES (clause 11(1)(c)/s9D(2A))

The proposal that the net income of a controlled foreign company be deemed to be nil if either the high-tax exemption or the foreign business establishment exclusion is met will remove the compliance burden for many taxpayers. The proposed amendment is therefore welcomed.

3 CURRENCY OF REACQUISITION OF ASSETS OF PERSONS CEASING TO BE RESIDENT (clause 12(1)/s9H)

Problem statement:

The amendment in section 9H deeming a person who ceases to be a resident to have disposed of and reacquired shares in property owning companies in South Africa at the currency that the asset was actually acquired in, comes into operation on 12 December 2013. However, the bill first needs to be promulgated before this becomes law and certain taxpayers may have used the incorrect rates when calculating the taxpayer’s second provisional tax payment in respect of the 2014 year of assessment.

Proposed solution / recommendation:

Relief from underestimation penalties should be provided should the taxpayer have underestimated his/her taxable income because of the use of a rate other than the rate used to acquire the asset.

4 TRANSFER PRICING: SECONDARY ADJUSTMENT (clause 47(1)/s31)

4.1 Applicability of section 64FA and DTA relief to the section 31 deemed dividend *in specie*

Problem statement:

Section 64FA provides for an exemption or reduced rate of the dividends tax payable by a (resident) company on the deemed dividend *in specie* (section 64EA) paid to a (foreign) company if that foreign company submitted a declaration or a written undertaking as required in that section. It is uncertain if this section applies to this form of deemed dividend *in specie*.

There is also uncertainty as to whether this provision as well as the DTA relief would apply to this deemed dividend *in specie* if the counter party to the transaction is a shareholder or a fellow group member company.

Proposed solution / recommendation:

If it is the intention that DTA relief is not applicable to the deemed dividends *in specie*, the legislation would need to be amended to cater for this and the draft *Explanatory Memorandum on the Taxation Laws Amendment Bill*, 2014 ('EM') should include reference to this.

As multiple sections in the Income Tax Act are being used to interpret this situation (s64EA, S64FA, s31(2)), a simple solution would be to introduce a separate form of tax being a 15 per cent tax equivalent to the value imposed on the South African company. It is submitted that the use of the deemed dividends *in specie* regime complicates matters.

4.2 Dividend *in specie* declared by resident

Problem statement:

The treatment of the amount as a dividend *in specie* declared by the resident does not seem to consider that the resident may be a natural person or trust.

Proposed solution / recommendation:

The proposal should be considered in light of the nature of the resident person and whether it is appropriate in all instances.

4.3 Timing of dividend *in specie*

Problem statement:

It is not clear when the dividend *in specie* is regarded as having been paid. In our view it is appropriate that such dividend be deemed to be paid on the last day of the year of assessment of the company deemed to be declaring the dividend *in specie* as this is the date on which the affected transaction difference in taxable income of such company can be determined.

Proposed solution / recommendation:

The dividend must be deemed to be paid or declared on the last day of the relevant year of assessment.

4.4 Withholding tax on interest

Problem statement:

The dividend *in specie* treatment also leads to a double taxation problem in that the withholding tax on interest may also apply in cases where excessive interest is charged by a non-resident to a resident connected person. The excessive interest may therefore have been subject to the withholding tax on interest and will additionally be deemed to be a dividend *in specie*.

Proposed solution / recommendation:

A credit against the dividends tax should be given for any withholding tax on interest that is suffered.

4.5 Effective date

Problem statement:

The effective date of the amendments should be determined with reference to a year of assessment rather than 1 January 2015, as taxable income, on which the adjustment is based, is determined in relation to a year of assessment.

Proposed solution / recommendation:

The effective date should be for 'years of assessment commencing on or after 1 January 2015'.

5 EXEMPTION FROM WITHHOLDING TAX ON ROYALTIES (clause 56(2)/s49D)

Problem statement:

It would seem that the wording of clause 56(2) would lead to a circular reference once the Taxation Laws Amendment Act, 2014 has been promulgated.

Proposed solution / recommendation:

It is proposed that clause 56(2) reads as follow:

'*Subsection (1) is deemed to have come into operation on 1 July 2013 and applies in respect of royalties that are paid or that become due and payable on or after that date and in respect of which an exemption under section 49D has not been granted* *up to the date of promulgation of*

the Taxation Laws Amendment Act of 2014'.

6 WITHHOLDING OF WITHHOLDING TAX ON ROYALTIES (clause 57(2)/s49E)

Problem statement:

It appears that clause 57(2) would also lead to a circular reference once the Taxation Laws Amendment Act, 2014 has been promulgated.

Proposed solution / recommendation:

It is proposed that clause 57(2) reads as follow:

'*Subsection (1) is deemed to have come into operation on 1 July 2013 and applies in respect of royalties that are paid or that become due and payable on or after that date and in respect of which withholding tax on royalties has not been withheld under section 49E up to the date of promulgation of the Taxation Laws Amendment Act of 2014*'.

PART C: INDIVIDUALS TAX

Set out below, is the consolidated commentary on the **individuals tax issues only.**

1 RESTRAINT OF TRADE RECEIPTS (clause 1(1)(j)/par (cA) of 'gross income' definition in s1 of the Act)

Problem statement:

The proposed change to the legislation (alignment of the tax treatment of restraint of trade receipts between natural persons, trusts and companies) gives effect to the original intention of the legislator – that is, that the restraint must be linked to an employment relationship before it will be considered to be gross income. The amendment has, however, only been made effective from 1 March 2015 in terms of the *draft Explanatory Memorandum on the Taxation Laws Amendment Bill*, 2014 ('EM') (but in terms of the TLAB, it will become effective on the date of promulgation of the Act for years of assessment ending on/after that date). This has the result that natural persons in previous years have paid tax that was never intended by the legislator to be payable.

As the EM confirms that not all restraints but only those that are in respect of or causally linked to services rendered or an office held, it is unclear why this same principle does not apply equally to personal service providers and labour brokers. For example, if a personal service provider agrees to restrain himself against another personal service provider in respect of the clients in an industry that they will accept or clients in a specific geographical area, why is this any different from the relief to be provided to natural persons?

Proposed solution / recommendation:

As this was a legislative oversight, we submit that relief should be made retrospective to at least 1 March 2014 though technically, it should actually be made retrospective from the date that the section was introduced.

Furthermore, there seems to be no reason why a blanket inclusion should remain for personal service providers and labour brokers if the intention has always been to only include restraints that was casually linked to the services rendered or 'deemed employment' arrangements.

2 LUMP SUM BENEFIT FOR PAST EMPLOYMENT OUTSIDE SOUTH AFRICA (clause 13(1)(c) & 9(1)/s10(1)(gC) & s9(2)(i))

Problem statement:

The proposed amendment to these sections aligns the treatment of lump sum payments to the treatment of pension and annuity payments. Furthermore, it is our understanding that the intention behind section 10(1)(gC) is to provide an exemption for lump sums received from foreign funds. However, the use of the word 'lump sum benefit' instead of just 'lump sum' results in the section 1 definition applying which ostensibly refers back to the Second Schedule, namely a pension, provident or retirement annuity fund that has been approved by the Commissioner. Foreign pension funds are thus not included in this definition and thus the exemption would not apply. These concerns is thus also applicable to section 9(2)(i) of the Act.

Furthermore, it is unclear why the amendments will only come into operation on 1 March 2015 and apply in respect of years of assessment commencing on or after that date and not already from 1 March 2014?

On this note, SAIT and SAICA are busy with a combined submission that sets out further concerns that we have on the recent interpretation of these sections by SARS.

Proposed solution / recommendation:

It is proposed that the word 'retirement lump sum' and not 'lump sum benefit' or 'retirement lump sum benefit' be used, resulting in the normal grammatical meaning of the former applying and not the defined meaning of the latter two clauses.

We also suggest that the amendments be made effective from 1 March 2014 and apply in respect of years of assessment commencing on or after that date.

3 KEY PERSON INSURANCE POLICIES (clause 16(1)(a)/s11(w)(ii)(c))

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Problem statement:

The effective date in the EM is stated as 1 March 2014 whereas the effective date of clause 16(2) in the TLAB is shown as 1 March 2015.

Proposed solution / recommendation:

We propose that the effective date in the EM should be corrected.

4 EXEMPT AMOUNTS RECEIVED OR ACCRUED IRO TAX FREE INVESTMENTS (clause 26(1)/s12T)

4.1 Contribution limits (proposed s 12T(4))

Problem statement:

It is unclear whether the annual limits will be increased on a regular basis to take into account the impact of inflation.

Proposed solution / recommendation:

We suggest that section 12T should incorporate a provision whereby the Minister can adjust the limits annually to account for inflation, especially when the interest exemption in section 10(i) is eroded away. It is proposed that the initial R30 000 and R500 000 threshold be contained in public notice and not the body of the legislation to enable such an annual change.

4.2 Penalty (proposed s12T(7))

Problem statement:

The proposed section 12T(7) deems 40 per cent of the excess contributions to constitute normal tax payable. Clarity is sought whether this 'penalty' would qualify a non-resident for a tax credit as it is a tax on 'income'. It is submitted that no inequity results from this as the tax has been charged and effectively the cost of the investment has been increased and has not been funded by the *fiscus*.

Proposed solution / recommendation:

To ensure continued foreign investment in South Africa, the changes to the legislation should ensure that non-residents having to pay this penalty are not worse off than residents and that double taxation does not occur.

4.3 Treatment of withdrawals that are reinvested

Problem statement:

The EM at 1.2 III makes it clear that the intention is to treat reinvestment of withdrawals as falling within the contribution threshold. However, the exclusion in the proposed section 12T(5) states that '*any amount contemplated in subsection (2) that is reinvested must not be taken into account*...'. Subsection 12T(2) refers to '...*any amount received by or accrued to a person in respect of a tax free investment*'. Ostensibly this includes capital amounts withdrawn from the tax free investment.

Proposed solution:

It is proposed that section 12T(5) be amended as follows:

'Any amount, other than amounts withdrawn from the tax free investment, contemplated in subsection (2) that is reinvested must not be taken into account in determining whether a person contributed in excess in respect of the amounts contemplated in subsections 4(a) and (c)'.

4.4 Treatment of tax free investments on death

Problem statement:

Section 12T(1)(b) allows an estate to hold the tax free investment but inevitably on transfer the amount will be part of the estate. As the target group for this incentive would probably not have an estate exceeding the dutiable amount exemption, the exclusion from the estate would have a negligible effect. However no provision is made in section 12T for the holding of the second tax free investment by the heir who could be a spouse or child. It is therefore unclear how transfers of such investments would be treated going forward for the heir and whether it remains a tax free investment on transfer to the heir.

It is submitted that being able to transfer and keep alive such savings with the corresponding tax benefits would further encourage the target group to invest in such target savings instruments and encourage the recipients to retain the investment even after the original contributor is deceased.

Proposed solution / recommendation:

It is submitted that the proposals in section 12T should include provisions regulating the transfer or part transfer of a tax free investment from a deceased estate to a single heir or multiple heirs. As the contributions limits in subsection 4 apply to the individual taxpayer, the taxpayers receiving the investment would be able to add the investment received to their current tax free investment and continue to contribute to it, subject to the annual and lifetime threshold still applying to such taxpayer.

4.5 Treatment of tax free investments on death

Problem statement:

Section 12T(3) determines that any capital gain or capital loss in respect of the disposal of a tax free investment must be disregarded when determining the aggregate capital gain or loss. No provision for this exclusion has, however, been provided in the Eighth Schedule to the Act.

Proposed solution / recommendation:

It is proposed that provision be made for this exclusion by inserting a paragraph to this effect in PART VIII of the Eighth Schedule to the Act.

5 ACQUISITION OF ASSET AT LESS THAN ACTUAL VALUE (clause 69(2)/par 5(3A) of the Seventh Schedule to the Act)

Problem statement:

Although it is acknowledged that the reference to 'and' at the end of item (b) was a legislative oversight, the retrospective implementation of clause 69(1) would definitely take place to the detriment of many taxpayers who followed the law pre-1 March 2014 to the word.

Proposed solution / recommendation:

It is proposed that clause 69(2) be amended to refer to '1 March 2015' to ensure that taxpayers who were fully compliant with the provisions of par 5(3A) in its current form are not penalized.

6 RIGHT OF USE OF MOTOR VEHICHLE (clause 70/par 7 of the Seventh Schedule to the Act)

6.1 Valuation of company car fringe benefits (clause 70(1)(a)/par 7(1)(a) of the Seventh Schedule to the Act)

Problem statement:

We fully agree with the rationale behind this clause and would recommend that the words 'at the time the employer acquired the vehicle' be inserted immediately after the last bracket in the proposed paragraph 7(1)(a) to prevent uncertainty as to when the retail market value must be determined.

Proposed solution / recommendation:

It is proposed that the words 'at the time the employer acquired the vehicle' be inserted immediately after the last bracket in the proposed paragraph 7(1)(a) to prevent any uncertainty as to when the retail market value must be determined.

6.2 Private use of motor vehicle (clause 70(1)(c)/par 7(4) of the Seventh Schedule to the Act)

Problem statement:

The proposed amendment would substantially increase the scope of travelling that is considered to be for private purposes as a result of the reference to '*or business*' in clause 70(1)(c). This would have the effect that travelling done by an employee having to visit various sites as part of his/her daily duties, undertaken from his place of residence, who does not first stop at his place of employment before enduring the said travel, would be regarded as travel for private purposes. This would have the effect that the employee would not be entitled to claim that the said travelling was done for business purposes even though it was legitimately done for business purposes and not to travel to and from the employee's place of residence and place of employment. It is submitted that this amendment would also severely affect individuals working from a home office who have to visit clients on a daily basis.

Under the current paragraph 7(4), the above travelling would not be considered to be 'travel for private purposes' as the employee's place of employment would be considered to be the office where the employee's duties are mainly performed.

Proposed solution / recommendation:

It is proposed that clause 70(1)(c) reads as follow:

*'Subject to subparagraph (10), the value to be placed on the private use of such vehicle shall be determined for each month or part of a month during which the employee was entitled to use the vehicle for private purposes (including travelling between the employee's place of residence and his or her place of employment **[or business]** or any other travelling done for his or her private or domestic purposes) and the said value shall—'*

7 VALUATION OF FRINGE BENEFITS FOR EMPLOYER PROVIDED RENTAL ACCOMMODATION (clause 71(1)/par 9 of the Seventh Schedule to the Act)

Problem statement:

The amendment to the fringe benefit value in paragraph 9 of the Seventh Schedule is welcomed as it will go a long way in assisting low income earners, especially those in mining towns, where the prices have recently been artificially inflated. This amendment furthermore reduces the compliance burden of taxpayers by not having to apply for directives when the transaction was an arm's length transaction from the start.

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However, no proposals have been made in respect of shared accommodation as announcement in the 2014 Budget Speech that consideration would be given to the value of the fringe benefit arising from shared accommodation. This remains a pressing matter where multiple persons share employer-provided accommodation as a value needs to be placed on the use of the accommodation for every individual based on the space occupied. The employer then needs to apply for a directive in order to apportion the taxable benefit, due to paragraph 9 of the Seventh Schedule not specifically catering for the situation where residential accommodation is shared.

Although paragraph 3(3) of the Seventh Schedule can be used in order to obtain a directive for both instances above, and paragraph 9(5) can be used to place a lower value on the benefit arising from the accommodation, it results in an administrative burden and increased compliance costs for the employer, diluting the relief provided in the proposed amendment.

Proposed solution / recommendation:

It is recommended that paragraph 9 of the Seventh Schedule to the Income Tax Act be amended in order to allow for the apportionment where a single residential unit is shared by two or more employees on a *pro rata* basis based on the number of employees sharing the accommodation and the total value or cost of the accommodation so shared.

8 VALUATION OF COMPANY CAR FRINGE BENEFITS ACCOMMODATION (par 7 of Seventh Schedule to the Act)

Problem statement:

Paragraph 7 of the Seventh Schedule does not address the situation where a single motor vehicle is shared by more than one employee and the current legislation does not seem to provide SARS with any discretion to provide relief in the form of a directive to the employer. Though we acknowledge that National Treasury have undertaken to review this ongoing problem for accommodation and travelling, it is submitted that some form of relief be provided in the interim such as providing SARS the right to issue directives on application.

Proposed solution / recommendation:

We recommend that paragraph 7 of the Seventh Schedule to the Income Tax Act be amended in order to allow for the apportionment where a single motor vehicle is shared by two or more employees by application to SARS for a directive until such time as the legislator has been able to consider the position and provide relevant relief in the legislation.

9 DEEMED EMPLOYEE CONTRIBUTION TO RETIREMENT FUND

Problem statement:

As from 1 March 2015, the Taxation Laws Amendment Act (No. 31 of 2013) ('TLAA 2013') amendments in respect of retirement fund contributions will apply. In essence, the contributions from employers will be deemed a taxable benefit as per paragraph 2(l) of the Seventh Schedule to the Act and a limited deduction will be allowed in terms of the replaced section 11(k) for the employee contribution. To include a deduction for the taxable benefit amount on the employer contribution, the new section 11(k)(iii) will deem the employer contribution, for the 'purposes of this paragraph', to be an employee contribution.

Therefore, when the employees tax liability is determined in the new paragraph 2(4)(a) of the Fourth Schedule, it allows '*any contribution by the employee concerned to any pension fund or provident fund* *which the employer is entitled or required to deduct from that remuneration*...'. It would therefore seem that firstly, this provision does not provide for the deemed contribution per section 11(k)(iii) and merely refers to that section as a threshold. Secondly, employer contributions are not deducted or withheld from remuneration as it is the employers liability to the fund and never forms part of remuneration prior to being a deemed benefit.

Proposal / Recommendation:

Section 11(k) as inserted by section 27(1)(k) of the TLAA 2013 should be amended in (i) - (iv) to refer to '*for the purposes of this subsection (k)*' and not to '*for the purposes of this* ***paragraph***'.

Furthermore, section 11(k)(iii) as inserted by section 27(1)(k) of the TLAA 13 should be amended as follows:

'for the purposes of this section and paragraph 4(a) of the Fourth Schedule, any amount contributed by an employer of the person for the benefit of the person as a taxable benefit in terms of the Seventh Schedule, be deemed to have been contributed by the person and deemed to have been deducted by the employer from such person's remuneration which the employer was entitled to make;'.

PART D: VALUE-ADDED TAX

Set out below, is the consolidated commentary on the **Value-Added Tax issues only.**

1 DEFINITION OF ENTERPRISE - SUPPLY OF ELECTRONIC SERVICES (clause 87(1)(a)/par (b)(vi)(bb) of 'enterprise' definition in s1 of the VAT Act)

Problem statement:

It is unclear what is meant by 'originates' in the proposed amendment to paragraph (b)(vi)(bb) of the definition of 'enterprise; in section 1 of the VAT Act, in respect of the payment made. It is unclear if this refers to both directly and indirectly and if indirectly, only amounts specifically paid indirectly for such supply or also where mixing of funds for different purposes in time occurred or used generally for other purposes is included as well. For example, foreign issued vouchers purchased in South Africa (SA) but utilized for electronic services supplied by a person in an export country or funds transferred generally to PayPal or similar accounts which are not SA banks and partly utilized for such supply. It should be noted that from the foreign supplier's side, it makes it nearly impossible to trace funds that were not directly received from a SA bank.

Proposed solution / recommendation:

It is submitted that 'originates' should be limited to 'directly originates' until such time as National Treasury have had time to consider the ambit of 'indirect payments', that can be practically applied by foreign suppliers. Furthermore, clear guidelines with examples should be issued to provide certainty for taxpayers to ensure they are compliant.

2 DEFINITION OF ENTERPRISE - SUPPLY OF ELECTRONIC SERVICES (clause 87(1)(a)/par (b)(vi)(bb) of 'enterprise' definition in s1 of the VAT Act)

Problem statement:

It is uncertain whether the term 'address in the Republic' in the proposed paragraph (b)(vi)(cc) of the definition of 'enterprise' in section 1 of the VAT Act, includes email addresses or if it is limited to postal and physical addresses as per the normal dictionary meaning. Should it include email addresses, then what is regarded as an 'email address in the Republic'? Although section 23(c) of the Electronic Communications and Transactions Act (No. 25 of 2002) deems receipt to be at the addressees' usual place of residence which may be in SA, it is unclear how the foreign supplier would know that the email address pertains to a recipient addressee with a usual physical address in SA?

Proposed solution / recommendation:

It is submitted that the proposed provision be amended to limit itself to deliveries of tax invoices to physical and postal addresses in SA, and where an electronic invoice is issued and delivered by email, that it only applies where the stated physical or postal address in the tax invoice is an address in SA. Furthermore clear guidelines with examples should be issued to provide certainty for taxpayers to ensure they are compliant.

3 DEFINITION OF SECOND HAND GOODS – PRECIOUS METALS (clause 87(1)(b)/par (ii) of 'second-hand goods' definition in s1 of the VAT Act)

Problem statement:

It would seem that the *Draft Explanatory Memorandum on the Taxation Laws Amendment Bill*, 2014 ('EM') states that the reason for the proposed exclusion of precious metals from the definition of 'second-hand goods' in section 1 of the VAT Act is that vendors are fraudulently claiming the deemed input tax on second hand jewelry by melting such jewelry into gold supplied at a zero rate as per section 11(1)(f) of the VAT Act.

Ostensibly this provision only penalizes vendors who comply with the legal obligations to sell the jewelry at the standard rate with vendors who illegally mix the gold just prevented from getting the additional benefit of the deemed input.

It is submitted that perhaps more could be done to combat this fraud if the amendment is not promulgated, as a VAT 264 form would have to be completed should a vendor wish to claim a notional input tax deduction. This form, however, contains the details of the person from whom the second-hand goods were bought. If this information is handed over to the police, perhaps the persons that are allegedly selling these goods fraudulently could be tracked and prosecuted. If the proposed amendment is promulgated, then SARS will no longer have this information available to them.

Proposed solution / recommendation:

Consideration should be given to retaining the current law rather than accepting this proposed amendment taking into account that information is available to track the sellers of these precious metals.

Furthermore, the vendor claiming the deemed input could still be required to account to SARS in respect of the sale of goods. In this respect it may be more efficient to rather just defer the notional input tax deduction to the period in which the sale of the gold occurs at the standard rate.

4 EXCLUSION OF ELECTRONIC SERVICES IN SECTION 11(2)(l) (clause 88(1)(b)/s11(2) of the VAT Act))

Problem statement:

The implementation of clause 88(1)(b) would have the effect that no vendor would be able to supply electronic services to non-residents at the zero-rate. Should a vendor supply electronic services to a non-resident, who is not registered or required to be registered, the non-resident may effectively pay VAT twice (i.e. the VAT charged by the vendor and the reverse charge by the foreign country). This double taxation effect may therefore make the electronic services supplied by SA's vendors more expensive than those of their international counterparts.

Proposed solution / recommendation:

It is recommended that clause 88(1)(b) reads as follow:

'*Where, but for this section, a supply of services, other than electronic services <u>supplied in terms of section 11(2)(k)</u>, would be charged with tax at the rate referred to in section 7(1)…*'

5 BARGAINING COUNCILS (clause 89(1)(a)/s 12(l) of the VAT Act)

<u>Problem statement:</u>

Section 12(l) of the VAT Act exempts the supply of any goods or services by a bargaining council that is established in terms of section 27 of the Labour Relations Act, 1995 (No. 66 of 1995), to any of its members to the extent that the consideration for such supply consists of membership contributions. The amendment broadens the exemption above to include the supply of administration services for which the bargaining council receives a separate fee and this proposal is welcomed as the essence of the transaction is that it is merely a pass-on of an exempt supply (i.e. interest on money held). However, if the intention behind the amendment was to take the bargaining council off the VAT register, this amendment alone will not achieve this as bargaining councils may for example also receive income from corporates for services rendered.

<u>Proposed solution / recommendation:</u>

It is recommended that it be clarified in the EM that Bargaining Councils should still remain on the register for VAT purposes in respect of all their activities that they render to persons other than their members.

6 DOCUMENTATION (clause 90(1)/s16(2) of the VAT Act))

<u>Problem statement:</u>

The proposed alignment of the documentary requirements contained in this section with the modernized Customs processes and procedures is welcomed. However, this amendment builds on from the previous amendment (effective 1 April 2014) of section 16(3)(a)(iii) of the VAT Act. Our concern with the previous amendment relates to the fact that with the requirement to defer the claim to the tax period in which payment was made to SARS Customs, the input tax claim is now delayed by a further one (1) to two (2) months causing negative cash flow implications for the importer. The accounting treatment of these payments also creates a problem as generally when the clearing agent's invoice is received it is processed in that particular month, however, the VAT can now at the earliest only be claimed in the following month. This also has implications when trying to complete the IT14SD income tax declaration. The administrative burden of all of these requirements has definitely increased.

<u>Proposed solution / recommendation:</u>

We understand that the intention is that no input claim should be allowed until the amount of VAT has been paid by the clearing agent to SARS. However, with deferred payment schemes, SARS has taken a security/guarantee from the clearing agent should the vendor claim an input tax deduction but the clearing agent does not pay the amount over to SARS. Thus, consideration should be given to revert back to the position prior to the April 2014 amendment by allowing an input tax deduction

- In the tax period in which the goods are imported; and
- Provided the VAT return is submitted after the Customs VAT was paid to SARS.

7 CONTRACT PRICES (clause 96(1)/s 67 of the VAT Act)

Problem statement:

Although not stated in the EM, it is assumed the case law referred to is *Die Trustees van die Santinia Trust v Beukes en 'n Ander* (65 SATC 177) (2003). It is our understanding that this amendment seeks to clarify that a person entering into a contract (that will require this person to become registered for VAT), but then fails to actually register for VAT as required, cannot then rely on section 67 to provide relief for the VAT due by it from the recipient of the contract. Section 64(1) will then deem the amount stipulated in the contract to be inclusive of VAT.

Our concern, however, is that at the stage that a contract is signed, and this contract results in a person being required to be registered for VAT, no VAT was allowed to be added to the contract price as the person could only apply for registration after the contract had been signed. Practically it is therefore difficult to comply with this section.

It is also not clear who this amendment is trying to protect as section 67(1) already includes a statement that the right of recovery of the VAT is not available if it is agreed to the contrary by both parties in any agreement in writing. The proposed prohibition therefore seems to merely constitute an additional penalty measure for non-compliance by a vendor.

Proposed solution / recommendation:

Practically, the requirement to add VAT to the contract price and the ability to register and accordingly charge VAT is problematic. An interpretation note on how VAT should be treated when there is a liability to register and charge VAT but SARS does not allow a VAT registration before a legal contract has been concluded is required. Clear examples with solutions of what to do in such cases would be appreciated.

Furthermore, where penalties for non-compliance and protection for the recipient already exists, the relief mechanism should not be amended to further penalize vendors who failed to register and levy VAT.

8 ZERO RATING OF GOODS FOR AGRICULTURAL, PASTORAL OR OTHER FARMING PURPOSES (clause 88(1)(a)/ s 11(1)(g) of the VAT Act & Schedule 2 Part A)

Problem statement:

Due to the abuse of the provision allowing the zero rating of the supply of goods used or consumed for agricultural, pastoral and other farming purposes, the amendment proposes to repeal the zero rating of these supplies in section 11(1)(g) and Schedule 2, Part A. Although we acknowledge that the reason for this amendment is justified in view of the abuse, it does seem to be to the detriment of qualifying transactions as the change will cause negative cash flow implications for those farmers.

Proposed solution / recommendation:

As a primary proposal, it is recommended that paragraph (a) of clause 88(1) be deleted. It is proposed that stronger enforcement against farmers abusing the concession should be implemented to fight non-compliance.

As a secondary proposal, it is recommended that supplies to famers with a turnover of less than R1,5 million may still be zero-rated on the basis that these farmers be required to provide all their suppliers with a declaration stating that they are registered as a farmer and that farming is their main activity and their taxable supplies are less than R1,5 million.

For the larger scale farmers (turnover greater than R1,5 million), they should be required to reduce their tax periods to a one month tax period (despite the probable increase in compliance costs). This would assist these businesses to get their refunds soon after they have paid the VAT.

9 OTHER ISSUES FOR CONSIDERATION

9.1 Branches of foreign entities in South Africa

Problem statement:

Where a branch or office of a foreign company conducts activities (e.g. marketing and support) for its main business outside SA then proviso (ii) of the definition of 'enterprise' in section 1 of the VAT Act deems the main business and its SA operation to be separate persons provided-

- The SA operation is separately identifiable from its main business, and
- The SA operation maintains a separate system of accounting.

Furthermore, section 8(9) of the VAT Act has the effect that the activity of supplying goods or services to the main business by the branch would be deemed to be a supply of such goods and services in the course or furtherance of the branch's enterprise.

We have noted that SARS have begun to refuse registration or to deregister vendors who are branches and merely supply goods or services to the head office on the basis that such activities do not constitute an 'enterprise'. The only reason we can deduce as to why SARS is approaching the matter in this manner, is by applying proviso (ii) to the definition of 'enterprise' in such manner that the word 'enterprise' as used in that proviso is referring to paragraph (a) of the definition of 'enterprise' (i.e. self-referencing) and therefore applying to vendors and not the normal grammatical meaning namely any activity by any person.

Proposed solution:

It is requested that paragraph (a) of the definition of 'enterprise' be amended to specifically include separately identified branches or main businesses as per proviso (ii) and specifically referencing section 8(9) to clarify the legal position. In principle there should be no distinction for VAT purposes whether a branch or subsidiary is used to supply goods or services to its main business outside SA. This is further supported by the fact that the zero rating provisions for both the branch and subsidiary (i.e. section 11(2)(o) and (l), respectively) contain the same requirements.

Please do not hesitate to contact us if you have any queries in this regard.

Yours sincerely,

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