

24 November 2016

The National Treasury
240 Vermeulen Street
PRETORIA
0001

The South African Revenue Service
Lehae La SARS, 299 Bronkhorst Street
PRETORIA
0181

BY EMAIL: Mmule Majola (mmule.majola@treasury.gov.za)
Adele Collins (acollins@sars.gov.za)

RE: ANNEXURE C FOR 2017 BUDGET: COMMENTS PERTAINING TO MINING TAX ISSUES

We have attached the comments from the SAIT Mining Tax Work Group on the Annexure C tax proposals for the 2017 Budget pertaining to key mining tax issues. We appreciate the opportunity to participate in the process and would welcome further dialogue.

Please do not hesitate to contact us should you need further information.

Yours sincerely

Henry Nysschens

Chair of the Mining Tax Work Group

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BUSINESS (MINING)

1. DIESEL REFUND – ONEROUS REQUIREMENTS TO MEASURE USE AND KEEP DETAILED LOGBOOKS

Certain taxpayers who use diesel for primary production (e.g. in farming, fishing and mining) are entitled to diesel refunds. Effectively the diesel refund is a refund of fuel levies and Road Accident Fund levies given that the diesel is not used on public roads. We are in a process of engagement with SARS Customs & Excise regarding the onerous requirements to measure the use of diesel and to keep detailed logbooks in order to qualify for diesel refunds. We attach our letter dated 6 July 2016 (Annexure A) by way of background.

The purpose of this submission is to propose legislative amendments to facilitate a workable solution to the practical problems being experienced, which are preventing many taxpayers from receiving the diesel refunds which they should be entitled to from a policy perspective. This is a major problem concern for taxpayers in the vulnerable farming, fishing and mining industries.

In terms of part 3 of schedule 6 to the Customs & Excise Act, a diesel refund is claimable on “eligible purchases”. These purchases are defined to mean “purchases of distillate fuel by a user for use and used as fuel as contemplated in paragraph (b)...” (our emphasis added)

Part 3 also defines “logbooks” and sets out the logbook requirements. SARS has additionally published draft logbooks for comment and conducted workshops for discussion. Taxpayers must keep two logbooks, namely:

- A **Dispensing and storage logbook** for the purchase of diesel, its storage and the dispensing of the diesel from a storage facility (unit/bowser); and
- A **Usage logbook** for the receiving of diesel from a storage facility into vehicles/equipment and use per activity.

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Maintaining the “usage logbook” (in its proposed format) is proving administratively burdensome and impractical for most taxpayers. The most significant practical difficulty experienced in terms of compliance is the requirement to measure the diesel remaining in vehicles/equipment at the beginning and end of each month. Conformance with this requirement is often impossible as set out in the letter. Non-conformance results in the disallowance of the diesel refund, even if the taxpayer has strict alternative controls over the use of the diesel to prevent misappropriation.

We recommend that, from a practical perspective, the diesel refund compliance should as far as possible be focused on financial data as opposed to physical measurement of diesel used. Ideally, the diesel refund should become claimable as soon as the diesel has been purchased (with the purpose) to be used for qualifying activities. Given that farming, forestry and mining on land are only entitled to a diesel refund based on 80% of eligible purchases and that, generally, a very small percentage of diesel used in these industries is for non-qualifying activities, a *de minimus* exclusion should apply. This should do away with the need to keep detailed logbooks.

We propose that part 3 of schedule 6 to the Customs & Excise Act should be amended to facilitate this recommendation. The definition of “eligible purchases” should be amended to mean “purchases of distillate fuel by a user for use as fuel as contemplated in paragraph (b)...” (our emphasis added). The logbook requirements should also be reconsidered.

2. MINING CAPEX (SECTION 36) – ONGOING ENVIRONMENTAL REHABILITATION

Relief for environmental expenditure is an area of concern. A specific regime exists for deductible payments to a closure rehabilitation trust / company with the regime effectively acting as a semi-government controlled deductible reserve. Environmental rehabilitation that occurs during the life of a mine may also be deductible under section 11(a) as long as the costs are not of capital in nature. However, mining environmental tax relief does not apply to environment treatment, recycling and waste disposal assets (see paragraph (e) of the section 36(11) “capital expenditure” definition) utilised during the existence of mining operations (life of mine). Ongoing environmental expenditure should be encouraged as opposed to delayed reclamation and should include capital/infrastructural rehabilitation expenses.

We submit that the current exclusion of mining rehabilitation within section 36(11)(e) is far too broad. While the explanatory memorandum suggests the exclusion is only for those rehabilitation expenses covered in section 37A (trust contributions), the impact of section 36(11)(e) results in all mining rehabilitation expenses effectively being excluded. The exclusion should be limited solely to mining rehabilitation contemplated in section 37A, namely cash contributions to a rehabilitation trust or company. All other expenses attendant upon the mining rehabilitation that mining companies are required to perform in terms of the Mineral and Petroleum Resources Development Act and the National Environmental Management Act should be allowed under either under section 36(11) or section 11(a), especially mining rehabilitation that occurs during the life of mine (which is preferred from an environmental policy perspective) which includes capital expenditure relating to mining rehabilitation.

We would suggest that these capital expenditures be allowed at 100 per cent subject to ring-fencing under section 36 at least on par with CAPEX environmental expenditure for manufacturing (see section 37B) or an amendment to section 36(11)(e) be affected to remove the reference to “environmental rehabilitation”.

3. MINING CAPEX (SECTION 36(11)(EA)) - SOCIAL AND LABOUR PLAN INFRASTRUCTURE

3.1 Spreading of expenditure may mean loss of deduction

The proposed section 36(11)(eA) recognises the difficulties experienced in differentiating between whether employees or members of the wider community are using developmental infrastructure. However, spreading the expenditure incurred in a particular year over ten years (or the life of the mine if it will be shorter) effectively means that most of the tax relief will be deferred and could even mean that the mining company will never be able to benefit from the tax relief if the expenditure incurred happens during the last years of the life of the mine.

We recommend that the proposal be amended to remove the spreading over the shorter of ten years and the life of mine.

3.2 Holder requirement

The proposal refers to expenditure incurred in respect of a Social and Labour Plan for the purposes of the contributions by holders of mining rights towards the socio-economic development of the areas in which those holders are operating.

A number of mining companies that have to comply with these requirements are not the holders of the mining rights even though these companies are performing the mining operations. For example, there are a number of unincorporated joint ventures between mining companies where the unincorporated joint ventures are the holders of the mining rights and not the underlying joint venture parties i.e. the mining companies. We recommend that these references to the holders of the mining rights be removed so that mining companies obligated to perform under a Social and Labour plan receive the full benefit of the relief. The holding of rights and the obligations under the Social and Labour Plan do not neatly correspond.

3.3 Restriction against houses intended for sale

Both section 36(11)(d)(i) (employee related infrastructure) and the proposed section 36(11)(eA)(i) exclude housing for residential occupation intended for sale. Unfortunately, the nature of what is suitable accommodation in mining communities is evolving. There is a need for ultimate home ownership by employees and mining companies are trying to find ways of meeting this need. Moreover, it is often not possible to know upfront which houses erected in mining towns are eventually going to be sold to employees or other community members. It could be that an entire development could be built with one ambition but to find that subsequent events dictate a different result. Mining companies have little control over this outcome. We recommend that the exclusion be removed and that the tax relief claimed be recouped should the sale tax place.

The proposal does not contain a similar proviso to proviso (dd) to section 36(11)(d) which makes reference to section 12N (deductions in respect of improvements not owned by taxpayers). Given the variety of ways in which mining companies could potentially meet their Social and Labour Plan obligations, we would recommend that provision should be made for the possibility that section 12N may be relevant. For example, a mining company may agree to build and manage a school on government owned land for a management fee. This circumstance often occurs in terms of local municipal land.

Annexure A

6 July 2016

The South African Revenue Service
Lehae La SARS, 299 Bronkorst Street
PRETORIA
0181

BY EMAIL: J Michaletos (JMichaletos@sars.gov.za)

Dear Jed Michaletos

RE: DIESEL REFUND LOGBOOK REQUIREMENTS

1. Introduction

We refer to our comments regarding logbooks under point 4 of the attached submission dated 23 February 2016. The purpose of this submission is to provide SARS with further information regarding the practical difficulties caused by certain logbook requirements. Mainly at issue are the requirements arising from the fact that diesel refunds can only be claimed once diesel is used. In preparing this submission, we obtained inputs from various stakeholders in the farming, fishing, and mining (including quarrying) sectors.

2. Logbook requirements

In terms of part 3 of schedule 6 to the Customs & Excise Act, a diesel refund is claimable on “eligible purchases”. These purchases are defined to mean “purchases of distillate fuel by a user for use and used as fuel as contemplated in paragraph (b)...” (our emphasis added).

Part 3 also defines “logbooks” and sets out the logbook requirements. SARS has additionally published draft logbooks for comment and conducted workshops for discussion. Taxpayers must keep two logbooks, namely:

- A **Dispensing and storage logbook** for the purchase of diesel, its storage and the dispensing of the diesel from a storage facility (unit/bowser); and
- A **Usage logbook** for the receiving of diesel from a storage facility into vehicles/equipment and use per activity.

3. Practical difficulties

Maintaining the “usage logbook” (in its proposed format) is proving administratively burdensome and impractical for most taxpayers. The most significant practical difficulty experienced in terms of compliance is the requirement to measure the diesel remaining in vehicles/equipment at the beginning and end of each month. Conformance with this requirement is often impossible, as set out below.

Farming:

- It is impractical to stop activities that take place on a day-and-night basis during the planting and harvesting season in order to measure the diesel remaining in the tanks of vehicles/equipment used exclusively for qualifying farming activities, such as tractors and combine harvesters. To stop for measurement is simply to halt production.

Fishing:

- Every vessel’s fuel tank is different in construction, material, size and location. Some vessels have multiple tanks with diesel pumped from tank-to-tank during the voyage in order to balance the vessel. Vessels often have multiple pieces of machinery on-board that run on diesel (for example, one or two main engines, two or more compressors and one or more generators). These items draw diesel from the same source and all tanks are interconnected.

- It is often impossible to reliably determine how much diesel is left in one or more tanks and the capacity of the tanks are often unknown. For most tanks, the taking of dip readings is not possible because: (i) tanks are often in obscure positions, (ii) the fillers are curved or have bends or are split to multiple tanks, or (iii) the tanks have split-level floors.
- In addition, vessels often go to sea for extended periods of time and are not necessarily in the harbour at or around month-beginning or month-end. It is impossible to accurately measure diesel on board a vessel in harbour under unfavourable weather conditions or while at sea, especially if the vessel is rocking and moving.

Mining (including Quarrying):

- It is wholly impractical for most mines operating on a 24-hour a day basis to stop operations in order to measure the diesel left in the equipment/vehicles at the beginning or end of the month. Again, to stop for compliance is to halt production.
- The location of mining activities, either in underground or opencast mining areas, makes it impractical to measure the diesel left in the equipment/vehicles. These remote locations also mean that the risk of the diesel being used for purposes other than intended activities once dispensed into the mining equipment/vehicles is low (thereby rendering excessive measuring unnecessary).
- Also of note is the fact that most of the equipment/vehicles do not have accurate gauges to measure the diesel remaining in their tanks.

Other:

Some of the other comments received in relation to practical difficulties arising from the usage logbooks requirements are:

- The usage logbook requirements give rise to a significant administrative burden. While companies have financial personnel dedicated to financial books, companies do not use this personnel to perform physical measurements.
- Diesel is a significant cost to taxpayers. Companies accordingly have internal controls in place to mitigate their risks which SARS should be able to rely upon in terms of misused diesel. Some taxpayers use sophisticated fleet management systems, and SARS could rely on controls and the information provided by these systems without requiring monthly physical measurements.
- Equipment/vehicles are often operated by unskilled labour.
- There is a vast volume of logbooks required. Logbooks can be lost in the remote areas of operation or due to different shifts of workers.
- The tracking of hours and kilometres causes difficulty in certain circumstances. In many instances, equipment/vehicles do not have odometers. For example, in underground mining, some vehicles are disassembled into parts and taken down into shafts, only to be reassembled, modified and maintained underground.
- Some taxpayers have stopped claiming diesel refunds to which they are entitled because these taxpayers are unable to meet the requirements of the usage logbook and would rather not run the risk of SARS penalties. Similarly, some taxpayers find the administrative burden prohibitive.
- Often the nature of the equipment/vehicles, such as vessels, dump trucks and drill rigs mean that they can only be used in qualifying activities given their special purpose nature. This fact should be simple to verify.

- Generally, a very small percentage of diesel used in farming, fishing and mining has been used for non-qualifying activities and ideally a *de minimus* exclusion should apply.

4. Recommendations

In the industries where users qualify for the diesel refund, certain vehicles/equipment are only used for qualifying activities (as set out in part 3 of schedule 6) and certain multi-purpose vehicles/equipment are used for qualifying and non-qualifying activities.

The diesel refund legislation makes provision that in certain industries, such as offshore vessels and harbour vessels, the diesel refund is based on 100% of eligible purchases. On the other hand, in certain other industries namely farming, forestry and mining on land the diesel refund is based on 80% of eligible purchases.

We recommend that, from a practical perspective, the diesel refund compliance should as far as possible be focused on financial data as opposed to physical measurement of diesel used. Although some taxpayers have systems in place to determine the amount of diesel used each month, the compliance burden is onerous and sometimes even prohibitive.

Ideally, the diesel refund should become claimable as soon as the diesel has been purchased (with the purpose) to be used for qualifying activities. Given that farming, forestry and mining on land are only entitled to a diesel refund based on 80% of eligible purchases and that, generally, a very small percentage of diesel used in these industries is for non-qualifying activities, a *de minimus* exclusion should apply. This should do away with the need to keep detailed logbooks.

An alternative approach to overcome these difficulties in keeping the prescribed logbooks, would be that a distinction be made between the logbook requirements for vehicles/equipment that are only used for qualifying activities and for multi-purpose vehicles/equipment that are used for qualifying and non-qualifying activities.

We recommend that once diesel has been dispensed into a vessel, vehicle, equipment or underground bowser that is used in a qualifying activity only, the associated diesel should be treated as having been properly “used” as required by the definition of “eligible purchases”. This approach would be in line with the approach followed by most diesel refund claimants to date, namely to claim the diesel refund based on dispensing records as proof of use. The logbooks can then be simplified to retain information, such as vessel, vehicle, equipment, and underground bowser description and identification, purpose (activity performed) and litres dispensed into the vessel, vehicle, equipment and underground bowser (while excluding opening and closing diesel balances and kilometres/hours used).

It is acknowledged that claiming diesel refunds as soon the diesel has been dispensed into a vessel, vehicle, equipment or underground bowser used in a qualifying activity may result in a timing benefit to the taxpayer to the extent that the diesel is still in the tank at month end. Nonetheless, the diesel in tanks is often only a small percentage of total diesel consumed in a month. More importantly, taxpayers typically paid for diesel (including the fuel levy and Road Accident Fund levy) before receiving the diesel refund, meaning that the timing benefit would not be unfair (with sums paid for the diesel before any refund can come due).

In the case of taxpayers who are entitled to claim diesel refunds on multi-purpose vehicles (such as bakkies, trucks and SUV’s), a different system may be required, unless a *de minimus* exclusion is applied. For this group, logbooks similar to the usage logbook proposed by SARS would be required to prove the split between eligible and ineligible purchases of diesel. In cases where these taxpayers are not able to measure the diesel in the tank at month-end, the diesel refund claim would have to be deferred until the next month.

We thank you for the opportunity to voice our concerns in relation to this critical compliance matter and trust that we can engage at the earliest possible time of convenience.

Sincerely

Keith E Engel

Chief Executive Officer