SOUTH AFRICAN REVENUE SERVICE

INTERPRETATION NOTE: NO. 39

DATE: : 4 December 2007

ACT : VALUE-ADDED TAX ACT, No. 89 of 1991 ("the Act")

SECTIONS : 1, 8, 11, 16, 18, 23 and 40A (set out below)

SUBJECT : SUBJECT: VAT TREATMENT OF PUBLIC AUTHORITIES, GRANTS AND TRANSFER PAYMENTS

Section 1 - Definitions

- "Transfer Payment", "Grant", "Designated Entity", "Public Authority", "Enterprise" (Paragraphs (b)(i), (c) and proviso (viii))

Section 8 – Deemed supplies

- 8(2) - deemed supply of assets on deregistration
- 8(5) - deemed supply of services by designated entities in respect of certain payments from public or local authorities
- 8(5A) - deemed supply of services by a vendor (not being a "designated entity") in respect of certain payments from public or local authorities
- 8(23) – deemed supply of services by vendors in respect of certain housing subsidy payments received from public or local authorities

Section 11 – Zero-rated supplies

- 11(2)(p) – transfer payments
- 11(2)(n) – welfare organisations
- 11(2)(s) – housing subsidies
- 11(2)(t) – grants from public and local authorities
- 11(2)(u) – SETA training grants paid to designated entities

Section 16 – Calculation of VAT

- 16(3)(h) proviso – denial of "claw-back" input tax on the supply of goods or services used partially for taxable purposes before 1 April 2005

Section 18 – Adjustments

- 18(2) and (5) – change in use adjustments
- 18(4) proviso – adjustments for goods and services applied for enterprise purposes

Archived

Section 23 – Registration

- 23(4) proviso – non-registration of certain public entities not already registered on or before 31 March 2005

Section 40A – Liability of public authorities and certain public entities for tax and limitation of refunds

- Relief for past incorrect treatment of certain payments from Government

Important Notes:

1. Due to the length of this note, the volume of supporting information in the Annexures, and the complexity of the issues discussed, an exposition of the contents is provided overleaf for easy reference.

2. This note is primarily about the VAT treatment of public authorities and public entities on the application of the law before and after 1 April 2005. However, since the original draft of this note there have been extensive amendments to the Act in respect of the VAT treatment of municipalities. The most important of these amendments which came into effect on 1 July 2006 are discussed in notes 3 to 5 below. (For more information on amendments to the VAT Act which affect municipalities, refer to the draft interpretation note on the VAT treatment of supplies made by municipalities, which is available on the SARS website).

3. Paragraph (c) of the definition of "enterprise" and the definition of "local authority" were deleted. The effect being that most of the supplies by a municipality (formerly known as a local authority) became taxable at the standard rate under paragraph (a) of the definition of "enterprise". The categories of business activities in Government Notice No. 2570 dated 21 October 1991 also fell away.

4. The definition of "municipality" refers to the definition as contained in section 1 of the Income Tax Act, no. 58 of 1962, which in turn, makes reference to section 12(1) of the Local Government: Municipal Structures Act, 1998, (Act No. 117 of 1998). In effect, the term "municipality" means Category A, B and C municipalities as contemplated in section 155 of The Constitution of the Republic of South Africa, which deals with the establishment of municipalities. As this note is intended to provide an explanation of the law as it applied before and after 1 April 2005, the term "local authority" (and not "municipality") continues to be used in this note in the context of the period prior to 1 July 2006.

5. If an entity previously qualified as a "local authority", that entity would not necessarily qualify as a municipality with effect from 1 July 2006. It follows that the explanations provided in this document in respect of the period on or after 1 July 2006, will only apply to those entities which fall within the definition of "municipality" on or after that date.

Archived

TABLE OF CONTENTS

Paragraph	Topic	Page
1	**PURPOSE**	5
2	**INTRODUCTION** The background and underlying principles upon which the amendments are based are set out in this paragraph.	5
3	**THE LAW BEFORE 1 APRIL 2005** This paragraph contains an extract of the relevant provisions of the Act which are applicable before 1 April 2005.	13
4	**APPLICATION OF THE LAW BEFORE 1 APRIL 2005** The correct application of the law prior to the amendments, as quoted in paragraph 3, is explained in detail. It also sets out the underlying legal principles and interpretation of the law which serves as a foundation for the application of the law after 1 April 2005.	16
5	**THE LAW ON OR AFTER 1 APRIL 2005** This paragraph contains an extract of the relevant provisions of the Act and the amended law which applies after 1 April 2005.	31
6	**APPLICATION OF THE LAW ON OR AFTER 1 APRIL 2005** The law as quoted in paragraph 5 is explained in detail. The reader may be referred to the explanations provided in paragraph 4 where it concerns principles which have already been discussed, and where those principles apply before and after 1 April 2005.	36
7	**PRACTICAL IMPLICATIONS** This paragraph highlights some of the practical issues arising in respect of the deregistration of certain public authorities, public entities and constitutional institutions as a result of the amended law.	57
8	**SUMMARY** The main points on the application of the law prior to, and after 1 April 2005 are summarised.	64

Archived

TABLE OF CONTENTS (CONTINUED)

Paragraph	Topic	Page
9	**EFFECTIVE DATE** This paragraph provides details of the applicable Presidential Proclamation and the Government Gazettes pertaining to the effective date.	66
10	**FURTHER AMENDMENTS** This paragraph highlights some of the latest amendments affecting the VAT treatment of public entities, which at the time of drafting this note were only proposed amendments.	67
Annexures		
A	**DEFINITION OF “TRANSFER PAYMENT”** Various extracts from Government Gazettes concerning the treasury regulations for departments, constitutional institutions and trading entities, as well as section 38(1)(j) of the Public Finance Management Act, 1999.	69
B	**SCHEDULES 1, 2 & 3 OF THE PUBLIC SERVICE ACT, 1994 (PSA)** A list of all the National and Provincial Government Departments in terms of the PSA.	71
C	**SCHEDULES 1, 2 & 3 OF THE PUBLIC FINANCE MANAGEMENT ACT, 1999 (PFMA)** A list of all the public entities in terms of the PFMA as at 6 March 2006.	72
D	**EXAMPLES** Various examples are provided to illustrate the application of the law before and after 1 April 2005.	80

Archived

1. PURPOSE

The general purpose of this note is to set out the VAT treatment of public authorities, grants and transfer payments and to deal with the impact of the amendments in this regard which **came into effect on 1 April 2005.**

This note intends to provide a clear framework for the application of the law, so that vendors who transact with Government departments, public entities and local authorities will have clarity on the application of the Act **before and after 1 April 2005** in respect of the following:

(a) the application of the zero rate in terms of sections 11(2)(p), 11(2)(t), 11(2)(s), 11(2)(n) and 11(2)(u) of the Act in respect of certain payments made by / to public authorities and municipalities (previously known as local authorities);

(b) the application of the deeming provisions in terms of sections 8(5), 8(5A) and 8(23) in respect of certain supplies and payments made by / to public authorities, designated entities and municipalities.

(c) the meaning of the terms “transfer payment”, “grant” and “public authority”;

(d) determining whether or not an entity is a “public authority”, and consequently, whether that entity must register for VAT or not; and

(e) whether certain input tax and output tax adjustments are allowed to, or required by, public authorities.

Archived

2. INTRODUCTION

2.1 Background

The zero-rating of transfer payments in terms of section 11(2)(p) of the Act was introduced as a temporary measure in 1991 when VAT was introduced to allow government departments sufficient time to effect the necessary adjustments to their budgets to take VAT into account. The zero-rating was therefore never intended to be a permanent feature of the Act.

Since 1994 a number of the functions previously performed by the national and provincial departments were delegated to entities outside of the national and provincial departments. The transfer of funds between national and provincial departments, local authorities and public entities has created many interpretation problems because of the different meanings attached to the defined term “transfer payment”. The definition of “transfer payment” was amended three times since the inception of VAT, but there are still differences of opinion amongst role-players on the correct classification of payments such as appropriations, grants-in-aid and subsidies.

Where a public authority or local authority (municipality) acquires “goods” from a vendor, it is normally quite clear that an actual taxable supply is made in terms of section 7(1)(a) of the Act and there is no need to apply any deeming provision. However, with the intangible nature of “services” it is often more difficult to establish whether, in fact, an actual supply of services has occurred or not. It follows that in such cases, it will not be clear whether any payment by the entity concerned qualifies as a “transfer payment”, or if it is in respect of the actual supply of services.

This uncertainty resulted in an inconsistent application of the law in respect of certain payments made by public authorities. An investigation was therefore undertaken by National Treasury (“NT”) and the South African Revenue Service (“SARS”) to determine what the best practices are in regard to the VAT treatment of public bodies and the grants, subsidies or transfers of funds which they make to other vendors. A summary of VAT treatment of various entities impacted by the amendments and the general underlying VAT principles are set out in paragraphs 2.2 to 2.10 below.

The bulk of the amendments on this topic are contained in the Revenue Laws Amendment Act, 2003 (Act No. 45 of 2003) and the Revenue Laws Amendment Act, 2004 (Act No. 32 of 2004). However, amendments on some of the aspects relating to the topics dealt with in this note are included in the following amendment acts:

(i). the Taxation Laws Amendment Act, 2005 (Act No. 9 of 2005);
(ii). the Taxation Laws Second Amendment Act, 2005 (Act No. 10 of 2005);
(iii). the Revenue Laws Amendment Act, 2005 (Act No. 31 of 2005); and
(iv). the Second Small Business Tax Amnesty and Amendment of Taxations Laws Act (Act No. 10 of 2006).

Archived

2.2 General Principles

The South African VAT system is based on the premise that Government is the final consumer of goods and services if it uses those inputs to provide goods and services on a non-commercial basis. In addition, the classification of public entities under the Schedules to the PFMA is now used as a basis for determining whether the entity concerned should be regarded as an enterprise or not. Since most of the supplies made by departments and certain government agencies are generally outside the scope of VAT, it follows that those departments and government agencies will generally not be entitled to register for VAT or to claim input tax in

respect of the VAT incurred on the acquisition of goods and services. Accordingly, VAT is generally not charged by Government on the goods and services it supplies to the public.

Certain public entities which conduct enterprises, as well as welfare organisations and public private partnerships ("PPP's") which make taxable supplies, fall within the definition of "designated entity". If a designated entity receives any payment from a public authority, municipality or constitutional institution, it is deemed to supply a taxable service in terms of section 8(5) of the Act to that entity (provided that there is no actual supply in terms of section 7(1)(a) of the Act to which that payment relates).

The deemed supply is generally taxable at the standard rate, unless the payment is in respect of exempt supplies (e.g. financial services). This is to ensure that entities in which Government has an interest do not have an unfair competitive advantage over other vendors participating in the market for the goods or services concerned. However, where a designated entity receives a training grant from a Sectoral Education Training Authority (SETA), or where the grant recipient is a "welfare organisation", the deemed supply to which that payment relates is taxed at the zero rate.

As discussed later in this note, a "grant" means any appropriation, grant in aid, subsidy or contribution transferred, granted or paid to a vendor by a public authority, municipality or constitutional institution. A grant is zero-rated in the hands of the recipient (not being a "designated entity"), unless the payment concerned is in respect of an actual supply of goods or services procured by that public authority, municipality or constitutional institution.

The amendments result in many of the supplies made by Government bodies and public entities no longer being subject to VAT, and the entity concerned will be required to deregister for VAT. However, these entities are not required to pay output tax on the value of their assets on the date of deregistration in terms of section 8(2), as this will merely result in a circular flow of funds within Government.

It may appear that the changes will have a significant effect on the financial position of the different entities involved and on the total tax collections of the Government. However, the purpose of the investigation was to ensure the most efficient and consistent financing of the activities of the different government bodies. The amendments impact on Government's revenue side and corresponding changes had to be made on the expenditure side to adjust the amount of the grants or transfer payments to ensure that there is little, if any, change to the net position of the different government bodies and the total tax collections of Government.

Archived

2.3 Exempt National and Provincial Departments and Public Entities (Schedules 1, 2 and 3 of the PSA and Schedules 3A and 3C of the PFMA)

The VAT treatment of appropriations to national and provincial departments continues to be treated as outside the scope of VAT where the entity concerned does not make supplies which are in competition with other vendors in the private sector of the economy as described in paragraph 2.4 below. Similarly, national and provincial public entities listed in Parts A and C of Schedule 3 to the PFMA, are now treated on the same basis as national and provincial departments, as the supplies by these entities are generally of a regulatory, administrative or social nature and are not the same or similar to taxable supplies made by other vendors. *(See section 1 - definition of "public authority" and paragraph (b)(i) of "enterprise", paragraphs 3.1.1, 3.1.3, 5.1.1, 5.1.5, 5.2.1, 5.5 and 5.6 of this note, as well as the explanation of those items under paragraphs 4 and 6).*

2.4 Taxable/Partially Taxable National and Provincial Departments and Public Entities (Schedules 1, 2 and 3 of the PSA and Schedules 3A and 3C of the PFMA)

If the Minister of Finance ("the Minister") is satisfied that a department or public entity in paragraph 2.3 above (i.e. a "public authority") makes supplies which are of the same kind or similar to taxable supplies made in competition with other vendors, that specific activity may be regarded as an "enterprise" activity. In such cases, the department or public entity must be notified to register for VAT in respect of those taxable supplies, and to that extent, the entity will be a "designated entity". The VAT registration may apply to all the activities conducted by that entity, or only for specific activities (as the case may be). *(See section 1 - definitions of "public authority", paragraph (b)(i) of "enterprise" and "designated entity", section 8(5), section 18(4) proviso (iv), paragraphs 3.1.1, 3.1.3, 3.2 and 5.1.1, 5.1.3, 5.1.5, 5.2.2, 5.3.5, 5.4, 5.5 and 5.6 of this note, as well as the explanation of those items under paragraphs 4 and 6).*

2.5 Constitutional Institutions (Schedule 1 to the PFMA)

The activities carried on by Constitutional Institutions are not of a commercial nature, nor is it envisaged that these entities will ever carry on activities in competition with any other vendor in the private sector, or become liable to register for VAT in that regard. The activities of constitutional institutions are therefore excluded entirely from the definition of "enterprise".

Archived

Constitutional Institutions are therefore also required to deregister as a result of the amendments to the Act. *(See section 1 – proviso (viii) to the definition of "enterprise" and paragraphs 3.1.3, 5.1.1, 5.1.2, 5.5 and 5.6 of this note, as well as the explanation of those items under paragraphs 4 and 6).*

2.6 Major Public Entities (Schedule 2 to the PFMA)

These entities fall within the definition of "designated entity". Payments to major public entities such as ESKOM, Transnet Ltd and Telkom SA Ltd, fall within paragraph (a) of the definition of "enterprise", and are generally subject to VAT at the standard rate. As these are entities in which Government has a commercial interest, they are treated for VAT in such a way that any subsidy from the Government is regarded as consideration for a taxable supply. This is to ensure that those payments do not give rise to an unfair advantage over their commercial competitors as a result of the VAT treatment of those payments. *(See section 1 – definition of "designated entity", section 8(5), paragraphs 3.1.3, 3.2, 5.1.3 - 5.1.5, 5.2.2 and 5.3.5 of this note, as well as the explanation of those items under paragraphs 4 and 6).*

Archived

2.7 National and Provincial Government Business Enterprises (Schedules 3B and 3D of the PFMA)

These entities fall within the definition of "designated entity", and are treated for VAT purposes in much the same way as the major public entities in paragraph 2.6 above, as their activities fall within paragraph (a) of the definition of "enterprise". Payments to national and provincial government business enterprises are therefore generally subject to VAT at the standard rate.
(See section 1 – definition of "designated entity", section 8(5), paragraphs 3.1.3, 3.2, 5.1.3 - 5.1.5, 5.2.2 and 5.3.5 of this note, as well as the explanation of those items under paragraphs 4 and 6).

2.8 Public Private Partnerships (PPP's) (Regulation 16 of the Treasury Regulations - section 76 of the PFMA)

A PPP (as defined in the Treasury Regulations) is essentially a partnership between Government and the private sector. As such, their activities fall within paragraph (a) of the definition of "enterprise". A PPP also falls within the definition of "designated entity", and is treated for VAT purposes in much the same way as a major public entity in paragraph 2.6 above. Payments to PPP's are generally subject to VAT at the standard rate, unless the PPP

makes exempt supplies as contemplated in section 12 of the Act. *(See section 1 – definition of "designated entity", section 8(5), paragraphs 3.1.3, 3.2, 5.1.3 - 5.1.5, 5.2.2 and 5.3.5 of this note, as well as the explanation of those items under paragraphs 4 and 6).*

2.9 Welfare Organisations (Section 1 of the VAT Act)

The amendments to the Act only affect welfare organisations to the extent that they receive and make grants. Textual amendments have been made to the Act so that a "grant" to a "welfare organisation" continues to be zero-rated, as was the case under the old wording of the Act. A welfare organisation is also a "designated entity", but the zero rate applies in this case to unrequited payments which it receives from any public authority, constitutional institution or municipality, if it does not constitute consideration for a taxable supply in terms of section 7(1)(a) of the Act. *(See section 1 – definitions of "grant", "designated entity", "services", sections 8(5), 11(2)(n), and paragraphs 3.1.4, 3.1.5, 3.2, 3.3.1, 3.3.2, 5.1.3, 5.1.4, 5.2.2, 5.3.1 and 5.3.4 of this note, as well as the explanation of those items under paragraphs 4 and 6).*

Archived

2.10 Local Authorities (Municipalities) (Section 1 of the VAT Act)

Supplies by local authorities (municipalities) of goods and services listed in paragraph (c) of the definition of "enterprise" such as electricity, water, gas and removal of sewage, are subject to VAT at the standard rate, and therefore input tax may be claimed in this regard. However, any VAT incurred which is directly attributable to its non-enterprise activities may not be claimed. As a "local authority" is not a "public authority" as defined in section 1 of the Act, the amendments to the Act only affect local authorities to the extent that they receive and make grants.

Where a local authority receives a "grant" from a public authority, constitutional institution or other local authority, that receipt qualifies for the application of the zero rate of VAT. Similarly, where a local authority makes a "grant" to another vendor which is in respect of taxable supplies made by that vendor to other persons, the payment will also be zero-rated in the hands of the vendor receiving that grant. This would not have been the case prior to the amendments, as only a "public authority" could make a zero-rated "transfer payment". *(See section 1 - definitions of "local authority", "grant", "services", "enterprise" (paragraph (c)), "transfer payment", sections 8(5), 8(5A), 8(23), 11(2)(s), 11(2)(t), paragraphs 3.1.1, 3.1.2, 3.1.4, 3.1.5, 3.2, 3.3.1, 3.3.2, 5.1.4, 5.2.3, 5.2.4, 5.3.2, and 5.3.3 of this note, as well as the explanation of those items under paragraphs 4 and 6).*

Example

If a department ("public authority") pays a municipality ("local authority") for the supply of electricity and water used in the course of conducting that department's operations, the amount paid is not a grant, as it is in respect of an actual supply of goods or services by the municipality to that department.

However, if that same municipality receives an "equitable share" payment in terms of the annual Division of Revenue Act*****, to partly cover the cost of providing free water and electricity to certain domestic consumers, that part of the payment will constitute a "grant" in the hands of the municipality. This is because the department receives no goods or services in return for the payment which it makes to the municipality. The effect is that the supply of water by the municipality to domestic consumers (which is a taxable supply), is partly subsidised by the "equitable share" paid by the Government. Therefore, to the extent that the "equitable share" is paid to the municipality to enable or assist it to make taxable supplies, the payment will constitute a "grant" and will be subject to VAT at the zero rate.

[**Note**: This example applies on or after 1 April 2005. Prior to 1 April 2005, payments in terms of the Division of Revenue Act were not specifically dealt with in the Value-Added Tax Act, 1991, and, as such a payment would not have been a "transfer payment" as defined, it would not have qualified for the zero rate in terms of section 11(2)(p)].*

Important Note:

Refer to the important notes on page 2 with regard to the application of the law with effect from 1 July 2006, as a result of various amendments to the Act in connection with the VAT treatment of supplies made by municipalities.

Archived

2.11 Other Private Sector Vendors (not being designated entities)

The amendments to the Act only affect private sector vendors to the extent that they receive a grant from a public authority, constitutional institution or local authority/municipality. The grant payment is zero-rated in the hands of the recipient vendor, but this does not apply where the payment constitutes "consideration" for an actual supply of goods or services in terms of section 7(1)(a) of the Act made by that vendor in return for the payment. *(See section 1 – definitions of "grant", "services", "enterprise" (paragraph (c)), "transfer payment", sections 8(5), 8(5A), 8(23), 11(2)(s), 11(2)(t), paragraphs 3.1.4, 3.1.5, 3.2, 3.3.1, 3.3.2, 5.1.4, 5.2.3, 5.2.4, 5.3.2, and 5.3.3 of this note, as well as the explanation of those items under paragraphs 4 and 6).*

Example

The Department of Trade and Industry (DTI) allocates a certain amount of public funds each year to the National Research Foundation (NRF), for the funding of innovation and other initiatives. The NRF is listed in Schedule 3A of the PFMA, and therefore it is a "public authority" as defined. If a vendor (not being a "designated entity") receives a payment from the NRF, that payment will qualify as a zero-rated "grant", provided that the NRF or the DTI does not acquire the ownership of any assets, or is supplied with any other goods or services (including intellectual property rights) in return for the payment to that vendor.

2.12 Special Cases (Unlisted entities)

Section 47 of the PFMA reads as follows regarding unlisted public entities:

(1) The Minister, by notice in the national Government Gazette--
- *(a) must amend Schedule 3 to include in the list all public entities that are not listed; and*
- *(b) may make technical changes to the list.*

(2) The accounting authority for a public entity that is not listed in either Schedule 2 or 3 must, without delay, notify the National Treasury, in writing, that the public entity is not listed.

(3) Subsection (2) does not apply to an unlisted public entity that is a subsidiary of a public entity, whether the latter entity is listed or not.

(4) The Minister may not list the following institutions in Schedule 3:
- *(a) A constitutional institution, the South African Reserve Bank and the Auditor-General;*
- *(b) any public institution which functions outside the sphere of national or provincial government; and*
- *(c) any institution of higher education.*

This means that the following are special cases which do not fall naturally into any of the categories dealt with in paragraphs 2.3 to 2.9 above –

(i). the South African Reserve Bank ("SARB") and the Auditor-General ("AG");
(ii). entities in the process of being created and listed (see paragraph 7.7 for more details);
(iii). any public institution which functions outside the sphere of national or provincial government; and
(iv). any institution of higher education.

It follows that the SARB and the AG will be regarded as normal enterprises under paragraph (a) of the definition of "enterprise". The same principle will apply to the entities in (ii), (iii) and (iv) above, to the extent that they may be regarded as making taxable supplies (unless the Minister decides otherwise). However, it should be noted that the supply of education by the entities in (iv) above are exempt, and they will generally not be liable to register for VAT in any event.

Archived

3. THE LAW BEFORE 1 APRIL 2005

The wording of the relevant provisions which need to be considered in regard to the zero-rating of transfer payments made by public authorities is quoted below.

3.1 Definitions – Section 1

3.1.1 "Enterprise" (Paragraphs (b)(i) and (c))

> ***"Enterprise"*** *means*
> *(a) in the case of any vendor other than a local authority, …*
> *(b) without limiting the applicability of paragraph (a) in respect of any activity carried on in the form of a commercial, financial, industrial, mining, farming, fishing or professional concern—*
> *(i) the making of supplies by any public authority of goods or services which the Minister, having regard to the circumstances of the case, is satisfied are of the same kind or are similar to taxable supplies of goods or services which are or might be made by any person other than such public authority in the course or furtherance of any enterprise, if the Commissioner, in pursuance of a decision of the Minister under this subparagraph, has notified such public authority that its supplies of such goods or services are to be treated as supplies made in the course or furtherance of an enterprise;*
> *(ii) …*
> *(iii) …*
> *(c) in the case of a vendor which is a local authority, any activity in the course or furtherance of which any of the following supplies of goods or services are made:*
> *(i) The supply of electricity, gas or water;*
> *(ii) the supply of services consisting of the drainage, removal or disposal of sewage or garbage;*
> *(iii) the supply of goods or services incidental to or necessary for … subparagraph (i) or (ii) apply;*
> *(iv) the making of supplies of goods or services in the course of any business carried on by such local authority, if—*
> *(aa) such supplies are of the same kind or are similar … made by any person other than such local authority …; and*
> *(bb) the revenue normally derived …, together with any grant or subsidy …, sufficient to fund the expenditure … incurred by that local authority in the production of such revenue; and*
> *(cc) (A) such business falls within a category of businesses which the Minister, having regard to the provisions of items (aa) and (bb) as generally applicable, has by notice in the Gazette determined to be a category of businesses in respect of which the provisions of this subparagraph shall be deemed to apply; or*
> *(B) such business (not being a business falling within a category referred to in subitem (A)) is determined by the Minister, having regard to the provisions of items (aa) and (bb) as applicable in the case of such business, to be a business in respect of which the provisions of this subparagraph shall be deemed to apply and the Commissioner, in pursuance of the Minister's determination under this subitem, has notified such local authority accordingly,*
>
> *and, in the case of a regional services council, a joint services board or a transitional metropolitan council, any other activities of that council or board to the extent that they are financed by levies referred to in section 8(6)(b).*

Archived

3.1.2 "Local authority"

"Local authority" *means—*

i) any divisional council, rural council, municipal council, regional services council, town board, local board, village management board or health committee or any joint services board established under the KwaZulu and Natal Joint Services Act, 1990 (Act No. 84 of 1990);

ii) any other body, council, board, committee or institution established or deemed to be established by or under any law which has functions similar to those of the councils, boards and committees enumerated in paragraph (a) and which may levy rates on the value of immovable property within its area of jurisdiction or receive payments for services rendered or to be rendered; and

iii) any water board or regional water services corporation or any other institution which has powers similar to those of any such boards or corporations:

Provided that where any local authority has been disestablished and superseded by a new local authority in terms of the Local Government: Municipal Structures Act,1998 (Act No. 117 of 1998), such disestablished local authority and such new local authority shall for the purposes of this Act be deemed to be and to have been one and the same local authority.

Note: The definition was subsequently deleted and replaced with the definition of "municipality" with effect from 1 July 2006.

3.1.3 "Public authority"

"Public authority" *means any department or division of the public service (including a provincial administration, the South African National Defence Force, the South African Police Service and Correctional Services).*

3.1.4 "Services"

"Services" *means anything done or to be done, including the granting, assignment, cession or surrender of any right or the making available of any facility or advantage, but excluding a supply of goods, money or any stamp, form or card contemplated in paragraph (c) of the definition of "goods".*

3.1.5 Transfer payment

"Transfer payment" *means a transfer payment as contemplated in regulation 8.4 of the Treasury Regulations published in terms of the Public Finance Management Act, 1999 (Act No. 1 of 1999).*

Archived

3.2 Certain supplies of goods or services deemed to be made or not made — Section 8(5)

(5) For the purposes of this Act a vendor shall be deemed to supply services to any public authority or local authority to the extent of any payment made by the authority concerned to or on behalf of the vendor in respect of the taxable supply of goods or services by the vendor to any person.

3.3 Zero-rating — Services ("Transfer payment") — Section 11(2)(p)

(2) Where, but for this section, a supply of services would be charged with tax at the rate referred to in section 7 (1), such supply of services shall, subject to compliance with subsection (3) of this section, be charged with tax at the rate of zero per cent where—

…

(p) the services are in terms of section 8(5) deemed to be supplied to a public authority to the extent that the payment contemplated in that section consists of a transfer payment; or

…

Archived

4. APPLICATION OF THE LAW BEFORE 1 APRIL 2005

The wording of the provisions quoted in paragraph 3 above are analysed and interpreted below:

4.1 Definition of "Enterprise" (Para (b)(i) & (c)) *[Refer to paragraph 3.1.1].*

Paragraphs (b)(i) and (c) of "enterprise" refer to the supplies made by public authorities and local authorities respectively. These paragraphs identify the types of supplies made by these entities which are similar to, or which compete equally with, supplies which would be made by any other vendor in terms of paragraph (a) of the definition.

4.1.1 Paragraph (b)(i) - public authorities

These entities exist to carry out the work of National and Provincial Government. The supplies made are therefore not normally of the same type or nature found in the private sector, nor are they in competition with vendors in that sector. In order for the supplies under this sub-paragraph to be treated as "enterprise" activities, the public authority concerned must be notified to register for VAT in that regard by the Commissioner, acting on instruction from the Minister. The Minister, in turn, must be satisfied that the supplies (or certain of them) are of the same kind or similar to taxable supplies already being made, or which might be made by vendors in the private sector. Certain public authorities and supplies made by them were identified and published in a Media Statement dated 27 September 1991 as follows:

"1. Vaccine production – Administration: House of Assembly.
2. Printing – Government Printer: Department of Internal Affairs.
3. Computer services – Commission for Administration.
4. Timber production and processing – Department of Forestry.
5. State water schemes – Department of Water Affairs.
6. State auditing – Auditor-General."

It is therefore only the above supplies which are regarded as taxable if made by the public authorities concerned. However, as mentioned in the introduction in paragraph 2, since 1994 the responsibility for performing certain functions of Government has been taken over by other government agencies or public entities, some of which were created by an Act of Parliament and others had their own enabling legislation. In some instances the work has been wholly or partially outsourced to private organisations.

Archived

This created some uncertainty as to whether public entities which performed functions on behalf of, or instead of a department would be liable to be registered in terms of the normal rules in terms of paragraph (a) of the definition of "enterprise", or if they were to be regarded as public authorities for VAT purposes, and therefore not be liable to register for VAT unless notified to that effect in terms of paragraph (b)(i) of the definition of "enterprise". It follows that some public entities registered for VAT without being notified, whilst others did not register. One of the objectives of this note is to provide some certainty in respect of the liability of those entities, and to deal with the consequences of their registration or non-registration for VAT purposes. *(See explanation in paragraph 6.5 on the application of the amended definition of "public authority" as quoted in paragraph 5.1.5).*

4.1.2 Paragraph (c) - local authorities

Local authorities exist to bring the resolution of governance issues as close as possible to the people of a particular community and to ensure the provision of certain basic services and facilities. A local authority must strive, within its financial and administrative capacity, to achieve it's objectives in terms of section 152(1) of the Constitution of the Republic of South Africa, Act No. 108 of 1996 ("the Constitution") which states that :

"…the objects of local government are—

- *(a) to provide democratic and accountable government for local communities;*
- *(b) to ensure the provision of services to communities in a sustainable manner;*
- *(c) to promote social and economic development;*
- *(d) to promote a safe and healthy environment; and*
- *(e) to encourage the involvement of communities and community organisations in the matters of local government."*

Archived

At this third tier level of Government, some of the goods and services provided are similar to goods and services which may be provided by other vendors. Local authorities are therefore sometimes in competition with the private sector in respect of specific types of supplies. The following supplies by local authorities have always been treated as taxable, regardless of whether there is competition from the private sector, or whether the activity is profitable or not:

- (i) Electricity, gas or water;
- (ii) Drainage, removal or disposal of sewage or garbage; and
- (iii) Goods or services which are considered incidental to or necessary for making the supplies in paragraphs (i) and (ii) above.

However, when it comes to any other types of supplies mentioned in paragraph (c)(iv) of the definition of "enterprise", **all** of the following requirements must be met before the supplies can be regarded as taxable, namely:

- the supplies must be of the same kind or similar to taxable supplies made by any other vendor; and
- the income derived from the activity (including any grant or subsidy for conducting the business activity) should be sufficient to cover all the costs of conducting that activity (including a reasonable provision for depreciation, but excluding capital expenditure) ; and
- the business activity must fall within the category of businesses determined by the Minister published in Government Notice No. 2570 – 21 October 1991; or, if the activity is not on that list, the Minister must advise the specific local authority that it shall treat the business activity concerned as an enterprise activity.

Government Notice No. 2570 – 21 October 1991 lists the following categories of businesses for the purposes of item (cc)(A) of paragraph (c)(iv) of the definition of "enterprise" as follows:

- Abattoirs.
- Airports.
- Brickyards.
- Farming.
- Cattle pens and auction facilities.
- Caravan parks, pleasure and holiday resorts.
- Cement-making.
- Game farms.
- Hiking trails.
- Letting of commercial and industrial buildings.
- Liquor sales.
- Nurseries.
- Provision of computer services.
- Parking grounds and garages.
- Produce markets.
- Quarries and sale of sand.
- Township development.

Important Note:

Refer to the important notes on page 2 with regard to the application of the law with effect from 1 July 2006, as a result of various amendments to the Act in connection with the VAT treatment of supplies made by municipalities.

Archived

4.2 Definition of "local authority" *[Refer to paragraph 3.1.2].*

A local authority (also known as a "municipality" or "local government") forms part of the third tier of Government which essentially decentralises certain functions of Government so that the local community can have more control over the governance issues which impact them in the region in which they live. The term includes:

- various councils and boards which have authority or jurisdiction over the administration of the affairs of a particular town, city, village, municipality or other area where people live;
- other bodies, committees and institutions which are similar to the above entities which under any law carry out similar functions and which may levy rates on certain immovable property within its area or receive payments for services rendered or to be rendered;
- any water board or regional water services corporation or any other institution which has powers similar to those of any such boards or corporations;
- Joint Services Boards (JSB's) and Regional Services Councils (RSC's) which may be entitled to levies payable by certain persons (normally businesses) in the area; and
- Transitional Metropolitan Councils (TMC's) where several local authorities have either merged with, or been taken over by another local authority (the disestablished local authority and the new local authority being treated as one and the same for VAT purposes).

Important Note:

Refer to the important notes on page 2 with regard to the application of the law with effect from 1 July 2006, as a result of various amendments to the Act in connection with the VAT treatment of supplies made by municipalities.

4.3 Definition of "public authority" *[Refer to paragraph 3.1.3]*

This term is defined as *"any department or division of the public service (including a provincial administration, the South African National Defence Force, the South African Police Service and Correctional Services)."* As the defining line between public authorities and public entities has become somewhat blurred over the years, uncertainty was created as to the VAT status of certain public entities (i.e. the distinction between government "departments" and other government "agencies" was unclear).

Archived

Since the terms, “department”, “division of the public service”, and “provincial administration” are not defined for VAT purposes, it is important to explore other legislation to determine the intended meaning. Whether a particular entity is regarded as a public authority for VAT purposes is essential in that:

- a “public authority” must be **notified to register** for VAT in terms of paragraph (b)(i) of the definition of “enterprise”. If the entity is not a “public authority” as defined, either paragraph (a) or (c) of the definition of “enterprise” could apply (i.e. no notification is required); and
- only a **“public authority”** may make a **“transfer payment”**. It follows that the zero rate in terms of section 11(2)(p) may only apply where the **deemed supply** in section 8(5) arises as a result of a payment being received from a public authority.

To determine if an entity is a “public authority”, one has to examine the aims of the Act in terms of which the entity is established (if any), the nature, functions, powers and funding of operations, the reporting structures and responsibilities of the organisation, and so on. However, even after conducting this exercise, there may still be uncertainty, and in some cases, it becomes necessary to consult other legislative sources for guidance in this regard.

In terms of section 40(1) of the Constitution, “Government” is described as being *“constituted as national, provincial and local spheres of government which are distinctive, interdependent and interrelated”.* It can therefore be concluded that the term **“public authority” refers to the first two tiers of government (i.e. national and provincial spheres), whereas a local authority refers to the third tier of government.** (The terms “local authority” and “public authority” are therefore mutually exclusive).

The public service established by section 197(1) of the Constitution is structured and organised as provided for in section 7 of the Public Service Act, 1994 (Proclamation No. 103 of 1994) (“the PSA”). This legislation will therefore be referred to for guidance, as well as the Public Finance Management Act, 1999 (“the PFMA”) - the provisions of which already have an impact on VAT legislation, and play an even greater role after 1 April 2005.

In terms of section 1 of the PFMA a **"department"** means a “national or provincial department” and makes reference to Schedules 1 and 2 of the PSA. The term “public service” is not defined in the PFMA. The term **“department”** as defined in section 1 of the PSA means a “**national department”,** a **“provincial administration”** or a **“provincial department”**. The meaning of these terms is derived from **section 7(2) of the PSA;** which states as follows:

Archived

"For the purposes of the administration of the public service there shall be national departments and provincial administrations mentioned in the first column of Schedule 1, provincial departments mentioned in the first column of Schedule 2 and the organisational components mentioned in the first column of Schedule 3."

The PSA indicates that the meaning of the term **"public service"** is as contemplated in **section 8 of the PSA -** ***"Composition of public service"***. This provision indicates essentially that the public service consists of persons who hold posts on the "fixed establishment" (i.e. posts created for the normal requirements of a "department"), including temporary and contract employees in addition to the fixed establishment, as follows:

- classified in the A division and the B division;
- in the services (i.e. the Permanent Force of the National Defence Force; the South African Police Service; and the Department of Correctional Services);
- in the Academy or the Agency or the service (i.e. the South African National Academy of Intelligence and South African Secret Service); and
- in state educational institutions where the remuneration and service conditions of educators are determined by law (i.e. institutions wholly or partially funded by the State, including an office controlling such institution, but excluding a university or technikon).

Archived

From both the PSA and PFMA, it can be concluded that a "**department" means any entity listed in Schedules 1, 2 or 3 of the PSA. (See Annexure B for a list of national departments and provincial departments in terms of the PSA).** It is also submitted that the interpretation principles *noscitur a sociis* and *ejusdem generis* apply in respect of the terms "division of the public service" and "department" as discussed above. (i.e. they are very closely associated, and each "takes their colour" from the meaning of the other).

Generally VAT legislation treats divisions, separate enterprises or branches in a very similar manner, which implies that these terms have very similar meanings. The term "division" is defined in the Collins English Dictionary as:

"4. one of the parts, groups, etc., into which something is divided

5. a part of a government, business, country, etc, that has been made into a unit for administrative, political or other reasons".

"Branch" is defined in The Shorter Oxford English Dictionary as:

"5. [a] division; a subdivision; a department

6. A component portion of an organization or system

7. A local and subordinate office of business."

In the case *S v Coetzee 1927 3 SA 526 (O) 529*, it was held that, to be a branch, two requirements must be satisfied, namely:

- o the entity must purport to be a branch or "section" of the main body; and
- o its objects and activities must substantially conform to those of the main body.

An entity will therefore only be a "public authority" for VAT purposes before 1 April 2005 if it is listed in Schedules 1, 2 or 3 of the PSA (including any organisational component of that entity such as an office, division, subsidiary, separate trading account, or branch whose objects and activities substantially conform to those of the main body which it purports to represent). **Therefore, as the scope of the term "public authority" before 1 April 2005 <u>does not include</u> any of the entities listed in the PFMA, those entities would have been liable to register for VAT as an "enterprise" under paragraph (a) of the definition of that term if they made taxable supplies in excess of the registration threshold in section 23(1) (i.e. R150 000 prior to 24 November 1999 and R300 000 thereafter).**

This means that for the period prior to 1 April 2005, there is a potential VAT consequence for those public entities which were liable to register, but did not do so as a result of the uncertainty. (See proviso to section 23(4) – paragraph 5.5 and the explanation to the application of that provision under paragraph 6.13).

The "outsourcing" of activities normally performed by a public authority to private independent businesses does not mean that the entity performing those activities will fall within the ambit of the definition of "public authority". Similarly a partnership/joint venture between a government department or division thereof and a private independent contractor will also fall outside the scope of the definition of "public authority". (For example, a "public-private partnership" as contemplated in the Regulations to the PFMA – often referred to as a PPP).

4.4 Definition of "services" *[Refer to paragraph 3.1.4]*

The term "services" means anything done or to be done, including the granting, assignment, cession or surrender of any right or the making available of any facility or advantage. The definition is meant to be as broad and all-inclusive as possible, but it excludes a supply of goods, and a supply of money. Therefore, if a particular transaction does not constitute a supply of "goods" or "money", it should generally fall within the definition of "services". To fall within the scope of the Act, a payment (consideration) must be in respect of a "supply".

Archived

This can be an actual supply, or a supply which the Act deems the person to make in the circumstances. It follows that a donation will not be subject to VAT as such a payment is given unconditionally and does not constitute payment for a supply of goods or services to the donor.

Although it is normally presumed that a person does not merely part with money or goods, or make available facilities or advantages to another person without some form of *quid pro quo* (mutual consideration, equal exchange, or something given in return for that which is received), the situation may be somewhat different for a public or local authority. This is because many of these entities are used to channel the delivery of government services and assistance programmes to the public at large.

However, in the absence of a written contract, it may be unclear if the vendor has actually rendered a service to the public authority making the payment. In other words, it is sometimes difficult to establish if there is a sufficiently strong link between a particular payment and the specific performance of any identifiable services in return for that payment. (See paragraph 4.5 on the meaning of the term "transfer payment" for more details and the example below which illustrates the point).

Archived

Example

Consider a payment made by a government department to a vendor as an incentive for innovation in developing South African produced goods. The possible perceptions of the parties to the transaction could be any of the following:

- the department may perceive that the vendor is supplying a valuable service, in that it assists that department to fulfil its mandate in meeting the country's export objectives. However, the vendor's view might be that there is no link between the payment and any specific identifiable service supplied in return to that department; or
- the vendor might view the payment as consideration for conducting the enterprise in a particular manner which is intended to compensate for the possible sacrifice of other business opportunities. On the other hand, the department's view may be that it is distributing the funds to that vendor as well as many others as part of its (benevolent) mandate, and therefore, the vendor does not really supply any specific or valuable service to the department in return; or
- neither party perceives that there is a service supplied in return for the payment; or
- both parties regard the payment as being consideration in respect of a specific service supplied by the vendor to the public authority.

This matter was dealt with in VAT NEWS 17 (August 2001 issue) to clarify that **where there is an <u>actual</u> supply of goods or services in terms of section 7(1)(a) of the Act to a government department, section 8(5) does not apply, and hence the zero rate in terms of section 11(2)(p) of the Act does not apply.** In a letter from SARS Head Office to all SARS offices dated 31 March 2003, the official interpretation on this point was set out as follows:

"This office's interpretation of the current legislation is that in the circumstances where a Government Department, Provincial or National Government makes available transfer payments, grants, subsidies or any payment to a vendor and such government department receives a benefit of either goods or services in return for making such payment, then the services supplied by that vendor will no longer fall within the ambit of sections 8(5) and 11(2)(p) of the Value-Added Tax Act, 1991. An actual supply of a service takes place which will be taxable at the standard rate in terms of the provisions of sections 7(1)(a) of the Act."

4.5 Definition of "Transfer payment" *[Refer to paragraph 3.1.5].*

Archived

As previously mentioned, various attempts have been made over the years to clarify the meaning of the term "transfer payment". From Government's perspective, if transfer payments are taxable at the standard rate, state expenditure increases, but more VAT (government income) is collected. If transfer payments are zero-rated, state expenditure does not increase, but VAT collections are less - the net effect on the state being the same.

Initially, this term was defined *"as contemplated in para 1.2.9.3 of the Manual on the Financial Planning and Budgeting System of the State published in terms of s39 of the Exchequer Act 66 of 1975".* In a media statement dated 28 September 1991, examples of transfer payments were given as being payments by a government body to or in respect of the CSIR, the SABS, the Urban Foundation, decentralisation assistance payments, and subsidies under the General Export Incentive Scheme (GEIS). As a result of continued uncertainty, a further media statement dated 18 October 1993 was issued.

The definition as set out in the Manual on Financial Planning and Budgeting of the State was quoted as follows:

"Transfer payments refer to amounts which will not be disbursed on goods or services by the department/administration on whose vote they appear, but will be paid over to other bodies. Included herein … divided in two categories, viz:

Current transfers which include grants in-aid, subsidies, contributions, financial assistance and aid in natura to foreign countries as well as pensions and social benefits,

Capital transfers consisting of ordinary capital transfers, acquisition of shares and loans granted."

The definition was amended when the Exchequer Act was repealed and replaced by the PFMA and the publishing of Treasury Regulations for departments, constitutional institutions and trading entities published in Government Gazette No. 21249 dated 31 May 2000 as follows:

"…all transfers excluding–
(a) all division of revenue grants from the national government; and
(b) any transfers to constitutional institutions and individuals."

The definition subsequently referred to a "transfer payment" as contemplated in regulation 8.4 of the Treasury Regulations published in terms of the PFMA.

In terms of section 214(1) of the Constitution, an annual Act of Parliament (the Division of Revenue Act ("DOR Act")) is required to provide for—

"(a) the equitable division of revenue raised nationally among the national, provincial and local spheres of government;
(b) the determination of each province's equitable share of the provincial share of that revenue; and
(c) any other allocations to provinces, local government or municipalities from the national government's share of that revenue, and any conditions on which those allocations may be made;"

According to GG No. 21249 dated 31 May 2000, "division of revenue grants" refers to allocations from the national government to other spheres of government as listed in Schedules 3A, (Grants to provinces) 3B (Grants for Local Government functions) and 3C (Grants still to be divided between spheres) of the DOR Act, 2000 including transfers in terms of section 16 (transfers not listed in the schedules to the DOR Act).

GG. No. 22219 dated 9 April 2001 and GG 23463 which came into effect on 27 May 2002 defines "division of revenue grants" as:

"allocations from the national government to provinces and local government as listed in the schedules to the annual Division of Revenue Act, including transfers in terms of that Act."

It follows from these provisions, that a "transfer payment" (as defined), does not include a grant, "equitable share" distribution, "Municipal Infrastructure Grant" or any other appropriation paid in terms of the DOR Act before 1 April 2005. Note that section 40B was later introduced to deal with assessments in respect of such payments received prior to 1 April 2005.

[For more information on section 40B, refer to the draft interpretation note on the VAT treatment of supplies made by municipalities, which is available on the SARS website].

Archived

In summary, a transfer payment which may be zero-rated in terms of section 11(2)(p) of the Act can be described as follows:-

- **It is an amount which has been budgeted for, and paid over to other institutions or persons by a public authority (i.e. a payment is made by an entity in National or Provincial Government to a vendor); <u>and</u>**
- **The vendor receiving the payment does not provide any goods or services in return to the public authority itself, but instead makes taxable supplies to a third person (or persons).**

The term "transfer payment" *<u>excludes</u>* :-

- **transfers to constitutional entities and individuals (non-trading entities);**
- **transfers in terms the DOR Act such as "equitable share" distributions to provinces and local government as listed in the schedules to the annual DOR Act, including transfers in terms of that Act; and**
- **a transfer by a local authority or a public entity listed in the PFMA to a vendor (unless the local authority or public entity is, in terms of an agreement, merely acting as the legal agent of the public authority concerned in disbursing that payment).**

Where a payment is made to a vendor by a public entity listed in Parts A & C of Schedule 3 to the PFMA in its capacity as the principal grant provider, that payment does not qualify as a "transfer payment", and may therefore not be zero-rated in terms of section 11(2)(p) of the Act in the hands of the recipient (unless it is clear that the PFMA entity is merely acting as the agent of the relevant public authority (as contemplated in section 54 of the Act)).

Otherwise, if the public entity is not acting on behalf of the public authority, it must be established if the payment is in respect of an actual supply of goods or services in terms of section 7(1)(a) of the Act, or if the payment is unrequited.
[See Annexure A for further details regarding the definition of "transfer payment" in terms of section 38(1)(j) of the PFMA and the Treasury Regulations].

Refer to Annexure D for examples of transfer payments.

Archived

4.6 Section 8(5) - Certain supplies of goods or services deemed to be made or not made (payments received from public and local authorities) *[Refer to paragraph 3.2]*.

☛ *"For the purposes of this Act …"*

The deeming provision contained in section 8(5) of the Act is applicable only for the purposes of the Value-Added Tax Act, 1991.

☛ *"…a vendor shall be deemed to supply services to any public authority or local authority…"*

A vendor may under certain circumstances be **deemed** to supply a service to a public or local authority (i.e. if any payment is received from the authority) where there is **no actual supply** of goods or services made by that vendor to the public or local authority itself **in terms of section 7(1)(a) of the Act**. Since "services" means *"anything done or to be done…",* the payment can relate to a taxable supply that has already taken place, or to a supply that will take place in the future.

☛ *"…to the extent of any payment made by the authority concerned…"*

The services are deemed to be supplied when and to the extent that any payment is made by a public or local authority in respect of the taxable supply of goods or services by the vendor.

☛ *"… to or on behalf of the vendor…"*

The payment does not necessarily have to be received by the vendor personally. The payment could also be made on that vendor's behalf to the vendor's agent, or other person who may apply the payment for that vendor's benefit. E.g. payment could be made to another person to whom the vendor owes money, thus reducing or extinguishing that debt.

☛ *"… in respect of the taxable supply of goods or services by the vendor…"*

There can only be a **deemed supply** by a vendor to the public or local authority if there are 2 elements present, namely:

- there must be a **payment** made by the public or local authority ;and
- there must be a **direct link between the payment and a taxable supply of goods or services <u>by that vendor</u> to another (third) person or persons**.

In various income tax cases with regard to services rendered, the words "in respect of" have been held to mean *"…stands in a direct causal relationship to the services rendered by him".*

Archived

In the present context, there must be a direct causal relationship between the payment made by the public or local authority, and the taxable supply of "goods" or "services" made by the vendor concerned to another (third) person. The payment can therefore not give rise to a deemed supply by the vendor in terms of section 8(5) if the payment is in respect of an exempt supply, or a supply which is otherwise than in the course or furtherance of an "enterprise" as defined in section 1 of the Act.

- *"… to any person"*

The term "any person" in this context means any person other than the public or local authority making the payment. In terms of section 6 of the Interpretation Act, 1957 (Act No. 33 of 1957), the term "any person" (singular) can also mean "any persons" (plural).

Example

If a payment of R10 000 is made by the Department of Housing (public authority) on 1 July 2003 to a vendor to supply building materials (taxable supplies) to low cost housing developers as follows:

- Bricks for R6 000 to be supplied on 15 August 2003 ; and
- Cement for R4 000 to be supplied on 15 October 2003,

the vendor must declare output tax on the full R10 000 (at the zero rate in this case) in the tax period covering 1 July 2003, since the "extent of any payment" at that date was the full amount of R 10 000.

However, if the vendor received payment of R3 000 on 15 August 2003, R3 000 on 20 October 2003 and R4 000 on 20 November 2003, (i.e. payment is received at the time of, or after the supply is made), the vendor would only have to declare VAT on the amounts as and when they were paid (irrespective of the accounting basis), since the vendor is only deemed to make a supply *"to the extent of any payment made by the authority."*

Archived

4.7 Section 11(2) - Zero-rating - Services *[Refer to paragraph 3.3]*.

- *"Where, but for this section, a supply of services would be charged with tax at the rate referred to in section 7(1)…"*

Section 11(2) of the Act contains a list of services and the circumstances under which 0% VAT is applicable. The supply being considered in this section must be of the type that **would otherwise have been subject to the standard rate,** had this provision not been in the Act.

The supply of any exempt services listed in section 12 of the Act or services otherwise than in the course or furtherance of an "enterprise" are therefore excluded. However section 11(2) overrides sections 12(a) (international financial services) and 12(g) (international transportation services), so that these specific supplies are also included in the scope of application of this provision (i.e. they are not precluded from being zero-rated instead of exempt in certain cases).

- *"…such supply of services shall, subject to compliance with subsection (3) of this section,…"*

As with all supplies mentioned in section 11, there is a condition that the vendor must obtain and retain documentary proof acceptable to the Commissioner which substantiates the application of the zero rate. (Refer to Interpretation Note No. 31 dated 31 March 2005 for the prescribed documents).

- *"…be charged with tax at the rate of zero per cent where —…"*

The zero rate applies only where the specific circumstances mentioned in the various sub-paragraphs to section 11(2) are evident. For example, for a payment to be zero-rated in terms of section 11(2)(p), the various conditions set out in sub-paragraph (p) have to be met. E.g. there must be a "transfer payment" (as defined) made by a "public authority" (as defined), there must be a deemed supply in terms of section 8(5) relating to that payment (i.e. no actual supply), etc.

4.8 Section 11(2)(p) - Zero-rated "transfer payment" *[Refer to paragraph 3.3]*.

- *"the services are in terms of section 8(5) deemed to be supplied to a public authority…"*

Section 11(2)(p) of the Act can only be applied where there is a **deemed supply** in terms of section 8(5) of the Act, as discussed in paragraph 4.7 above. Furthermore the deemed supply must be **<u>to a public authority</u>**. **The zero-rating can therefore not apply where there is an actual supply of goods or services to the public authority in terms of section 7(1)(a), or if the payment does not qualify as a "transfer payment", or if the supply contemplated in section 8(5) is deemed to be made to a local authority.**

- *"… to the extent that the payment contemplated in that section consists of a transfer payment; …"*

"..[T]he payment contemplated in that section…" means the payment made by the public or local authority, which in turn, gives rise to the deemed supply in terms of section 8(5) of the Act. If any part of that payment is made by a public authority, it must be determined if that part constitutes a "transfer payment" as discussed in paragraph 4.5 above. Only that part of the payment which falls within the definition of "transfer payment" may be zero-rated.

Archived

An appropriation in terms of the annual DOR Act, is not a zero-rated “transfer payment”.

Therefore:

- if a payment is wholly for the purposes of exempt supplies made, or to be made by a vendor, the entire amount is treated as consideration *“in respect of”* making exempt supplies. Although the payment may be a “transfer payment” as defined, it is not in respect of the making of any taxable supplies by the vendor to whom the payment is made. Sections 8(5) and 11(2)(p) of the Act can therefore not apply, and the receipt is not taxable for VAT purposes (i.e. it is not subject to the zero rate); and
- if a payment is for the purpose of both exempt and taxable supplies made, or to be made by the vendor, then only the part that is properly attributable to taxable supplies qualifies as a zero-rated “transfer payment”.

Any payment from a public or local authority which is not a “transfer payment” must also be taken into account for the purposes of calculating the apportionment percentage in terms of section 17(1) of the Act. For example, when using the turnover based method of apportionment, payments received in terms of the DOR Act will be added to the numerator of the formula to the extent that they are received for the intended purpose of making taxable supplies, and the full amount must be included in the denominator of the formula.

Note that section 40B was later introduced to deal with assessments in respect of payments in terms of the DOR Act which were received prior to 1 April 2005.
[For more information on section 40B, refer to the draft interpretation note on the VAT treatment of supplies made by municipalities, which is available on the SARS website].

Archived

5. THE LAW <u>ON OR AFTER</u> 1 APRIL 2005

The amendments in the RLA Act, 2003 were originally drafted on the basis that grant payments to entities which are not “designated entities” would be regarded as “out of scope” (not taxable), and not zero-rated for VAT purposes. As a result, certain amendments were either deleted or further amended. Those specific amendments have therefore been ignored in this note as they have no effect on the final version of the law. New wording inserted into the law is shown by *<u>underlined text</u>*, and words which have been deleted are shown in square brackets and bold font. i.e. ***[deleted text].***

5.1 Definitions – Section 1

5.1.1 “Enterprise” (paragraph (b)(i))

“Enterprise” *means—*
(a)…
(b) without limiting the applicability of paragraph (a) in respect of any activity carried on in the form of a commercial, financial, industrial, mining, farming, fishing or professional concern—
(i) the making of supplies by any public authority of goods or services which the Minister, having regard to the circumstances of the case, is satisfied are of the same kind or are similar to taxable supplies of goods or services which are or might be made by any person other than such public authority in the course or furtherance of any enterprise, if the Commissioner, in pursuance of a decision of the Minister under this subparagraph, has notified such public authority that its supplies of such goods or services are to be treated as supplies made in the course or furtherance of an enterprise.

5.1.2 “Enterprise” - insertion of a new proviso (viii) to the definition

…
Provided that—
…
<u>(vii) the making of supplies by a constitutional institution listed in Schedule 1 of the Public Finance Management Act, 1999 (Act No. 1 of 1999), shall be deemed not to be the carrying on of an enterprise.</u>

Archived

5.1.3 Designated entity - new definition inserted

"Designated entity" *means a vendor—*
- (i) *to the extent that its supplies of goods and services of an activity carried on by that vendor are in terms of (b)(i) of the definition of 'enterprise' treated as supplies made in the course or furtherance of an enterprise;*
- (ii) *which is a major public entity, national government business enterprise or provincial government business enterprise listed in Schedule 2 or Part B or D of Schedule 3 of the Public Finance Management Act, 1999 (Act No.1 of 1999), respectively; or*
- (iii) *which is a 'Public Private Partnership' as defined in Regulation 16 of the Treasury Regulations issued in terms of section 76 of the Public Finance Management Act, 1999 (Act No. 1 of 1999): or;*
- (iv) *which is a welfare organisation; or*
- (v) *which is a municipal entity as defined in section 1 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000);or*
- (vi) *which has powers similar to those of any water board listed in Part B of Schedule 3 of the Public Finance Management Act, 1999 (Act No. 1 of 1999), which would have complied with the definition of 'local authority' in section 1 prior to the deletion of that definition on 1 July 2006;*

5.1.4 Grant - new definition inserted

"grant" *means any appropriation, grant in aid, subsidy or contribution transferred, granted or paid to a vendor by a public authority,* ***[local authority]*** *municipality or constitutional institution listed in Schedule 1 to the Public Finance Management Act, 1999 (Act No. 1 of 1999), but does not include—*
- (a) *a payment made for the supply of any goods or services to that public authority, or* ***[local authority]*** *municipality, including all goods or services supplied to a public authority,* ***[local authority]*** *municipality or constitutional institution listed in Schedule 1 to the Public Finance Management Act, 1999 (Act No. 1 of 1999) in accordance with a procurement process prescribed—*
  - (i) *in terms of the Regulations issued under section 76(4)(c) of the Public Finance Management Act, 1999 (Act No. 1 of 1999); or*
  - (ii) *in terms of Chapter 11 of the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003), or any other similar process; or*
- (b) *a payment contemplated in section 8(23).*

5.1.5 "Public authority"

"public authority" *means—*
- (i) *any department or division of the public service* ***[(including a provincial administration, the South African National Defence Force, the South African Police Service and Correctional Services)]*** *as listed in Schedules 1, 2 or 3 of the Public Service Act, 1994 (Act No. 103 of 1994); or*
- (ii) *any public entity listed in Part A or C of Schedule 3 to the Public Finance Management Act, 1999 (Act No. 1 of 1999); or*
- (iii) *any other public entity designated by the Minister for the purposes of this Act to be a public authority.*

5.1.6 Transfer payment – definition deleted

Archived

5.1.7 Other definitions - The definition of "services" remained unchanged, as did "local authority", until it was deleted and replaced with the term "municipality" on 1 July 2006. A textual amendment in the definition of "consideration" replaced the term "unconditional gift" with the term "donation". In addition, a proposed change to the definition of "consideration" to exclude a "grant" was deleted so that for all intents and purposes it reverted to the original wording.

5.2 Certain supplies of goods or services deemed to be made or not made – Section 8

5.2.1 Section 8(2) – a new proviso (iv) was inserted

(iv) *this subsection shall not apply to a vendor that is a constitutional institution listed in Schedule 1 to the Public Finance Management Act, 1999 (Act No. 1 of 1999) or a public authority, respectively, where that vendor (other than a vendor who applied and was registered as a vendor during the period 22 December 2003 to 31 March 2005) ceases to be a vendor as a result of—*

(aa) *the substitution of the definition of 'public authority' in the Revenue Laws Amendment Act, 2004 or the insertion of paragraph (viii) to the proviso to the definition of 'enterprise' in the Revenue Laws Amendment Act, (Act No. 45 of 2003); or*

(bb) *the re-classification of that vendor or part of that vendor's activities within the Schedules to the Public Finance Management Act, 1999 (Act No. 1 of 1999) subsequent to the introduction of the Revenue Laws Amendment Act, 2004.*

Archived

5.2.2 Section 8(5)

(5) For the purposes of this Act a ***[vendor]*** *designated entity shall be deemed to supply services to any public authority or* ***[local authority]*** *municipality to the extent of any payment made by the public authority or municipality concerned to or on behalf of* ***[the vendor]*** *that designated entity in respect of the taxable supply of goods or services by* ***[the vendor to any person.]*** *that designated entity.'*

5.2.3 Section 8(5A) – new section inserted

(5A) *For the purposes of section 11(2)(t), a vendor (excluding a designated entity) shall be deemed to supply services to any public authority,* ***[local authority]*** *municipality or constitutional institution listed in Schedule 1 to the Public Finance Management Act, 1999 (Act No. 1 of 1999) to the extent of any grant paid to or on behalf of that vendor in respect of the taxable supply of goods or services by that vendor.'*

5.2.4 Section 8(23) – new section inserted

> (23) For the purposes of this Act a vendor shall be deemed to supply services to any public authority or **[local authority]** municipality to the extent of any payment in terms of the Housing Subsidy Scheme referred to in section 3(5)(a) of the Housing Act, 1997 (Act No. 107 of 1997), made to or on behalf of that vendor in respect of the taxable supply of goods and services by that vendor.'

5.3 Zero-rating - Services – Section 11

5.3.1 Section 11(2)(p) – the provision relating to transfer payments was deleted.

5.3.2 Section 11(2)(t) – new section inserted.

> *(t) the services are deemed to be supplied in terms of section 8(5A).*

5.3.3 Section 11(2)(s) – new section inserted.

> *(s) the services are deemed to be supplied to a public authority or **[local authority]** municipality in terms of section 8(23).'*

5.3.4 Section 11(2)(n) – textual amendment.

> *(n) the services comprise the carrying on by a welfare organization of the activities referred to in the definition of 'welfare organization' in section 1 and to the extent that any payment in respect of those services is made in terms of section 8(5) those services shall be deemed to be supplied by that organisation to a public authority or **[local authority]** municipality.*

5.3.5 Section 11(2)(u) – new section inserted

> *(u) the services are deemed to be supplied in terms of section 8(5) by a designated entity in respect of any payment made in terms of section 10(1)(f) of the Skills Development Act, 1998 (Act No. 97 of 1998), to that designated entity.*

Archived

5.4 Change in use adjustments – denial of input tax – Section 18(4) – new proviso inserted

...
(iv) *this subsection shall not apply where a constitutional institution listed in Schedule 1 or a public entity listed in Part A or C of Schedule 3 to the Public Finance Management Act, 1999 (Act No. 1 of 1999), is re-classified within the Schedules to the Public Finance Management Act, 1999 (Act No. 1 of 1999) and applies those goods or services for the purposes of consumption, use or supply in the course of making taxable supplies.*

5.5 Registration of persons making supplies in the course of enterprises – certain public entities not liable on or before 31 March 2005 – section 23(4) – new proviso inserted

(4) Where any person has-

a) applied for registration … subsection (2) or (3) …, that person shall be a vendor …with effect from such date as the Commissioner may determine;

b) not applied for registration in terms of subsection (2) and the Commissioner is satisfied that that person is liable to be registered …, that person shall be a vendor … with effect from the date on which that person first became liable to be registered in terms of this Act: Provided that the Commissioner may, having regard to the circumstances of the case, determine that person to be a vendor from such later date as the Commissioner may consider equitable.

Provided that where that person is a public entity listed in Schedule 1 or Part A or C of Schedule 3 to the Public Finance Management Act, 1999 (Act No. 1 of 1999), which was liable to be registered as a vendor for any supplies made on or before 31 March 2005, but did not register before 1 April 2005, the Commissioner must not register that person in respect of those supplies.

Archived

5.6 Liability of public authorities and certain public entities for tax and limitation of refunds – Section 40A – new section inserted

(1) This section applies in respect of the supply of goods or services on or before 31 March 2005 by any public authority or public entity listed in Schedule 1 or Part A or C of Schedule 3 to the Public Finance Management Act, 1999 (Act No. 1 of 1999).

(2) Where the Commissioner on or before 31 March 2005 issued an assessment for an amount of tax or additional tax in respect of any supply of goods or services contemplated in subsection (1), to correct a previous incorrect application of the zero per cent rate of tax in terms of section 11(2)(p) in respect of that supply, the Commissioner must, on written application, reduce that assessment to the extent that the amount of tax, additional tax penalty or interest arose as a result of that correction and was not yet paid on that date: Provided that the reduced assessment will not result in a refund to that public authority or public entity.

(3) The Commissioner may not after 31 March 2005 make any assessment to correct a previous incorrect application of the zero per cent rate of tax in terms of section 11(2)(p) in respect of any supply of goods or services contemplated in subsection (1).

(4) If a public authority or public entity incorrectly charged tax at the rate referred to in section 7(1)(a) instead of the zero per cent rate of tax in terms of section 11(2)(p) in respect of any supply contemplated in subsection (1), the Commissioner may not refund any such tax or any penalty or interest that arose as a result of the late payment of such tax, paid by that public authority or public entity to the Commissioner.".

6. APPLICATION OF THE LAW ON OR AFTER 1 APRIL 2005

Note that the general principles and meaning of certain terms which were explained in the application of the law in paragraph 4 are not repeated here, but rather referred to as a cross-reference where necessary. Where those principles and concepts still apply on or after 1 April 2005, they are used as a foundation to augment the analysis and interpretation of the amendments to the law, so that the position after 1 April 2005 may be clearly distinguished from the position prior to that date.

6.1 Definition of "Enterprise" (Para (b)(i). *[Refer to paragraph 5.1.1]*

Prior to the amendment, it was not clear whether certain public entities would be liable to register under paragraph (a) of the definition of "enterprise", or if paragraph (b)(i) of the definition applied. The amendment therefore clarifies that the activities of national and provincial public entities listed in Parts A or C of Schedule 3 to the PFMA (non-business type classification) fall within paragraph (b)(i) of the definition of "enterprise" as these entities are regarded as public authorities with effect from 1 April 2005. (See explanation on the definition of "public authority" in paragraph 6.5 below). Unless the said entities make taxable supplies which are similar to those in the private sector and have been notified by the Commissioner to register (pursuant to the Minister's decision), their activities are generally out of scope for VAT purposes and they will not register for VAT. Public authorities and public entities listed in Parts A or C of Schedule 3 to the PFMA which were registered prior to 1 April 2005 were therefore required to deregister with effect from that date. Relief from the output tax normally due on this taxable event is provided to these entities in terms of proviso (iv) to section 8(2) of the Act. (See paragraph 6.7 below regarding the application of this provision).

The activities of public private partnerships, (or PPP's as they are known), or other joint business ventures between Government and private entities fall within paragraph (a) of the definition of "enterprise" and not paragraph (b)(i).

Where an entity has not yet been classified, or has been re-classified in terms of the PFMA so that the VAT status of the entity is affected, the effective date of the change for VAT purposes will be determined jointly by NT and SARS, taking into account the date of the change as published in the Government Gazette, as well as any other relevant circumstances and conditions prevailing for that entity (or other entities in a similar position).

Archived

One implication of this amendment is that the National Skills Fund (NSF) (Department of Labour) and the Sectoral Education Training Authorities (SETA's) (both Schedule 3A PFMA entities), may no longer be registered for VAT. Consequently, vendors who are employers and liable for the Skills Development Levy (SDL) in terms of the Skills Development Levies Act, 1999, will no longer be allowed to claim input tax on those payments.

The same will apply to any other PFMA entity which now falls within the amended definition of "public authority" which was registered for VAT prior to 1 April 2005, where the entity is funded by means of any levy, duty or similar amount charged or levied by that entity (whether levied in terms of enabling legislation or not). Examples include levies payable to the Financial Services Board (FSB), National or Provincial gambling authorities, the Water Research Council (WRC), the Civil Aviation Authority (CAA), etc. As public authorities were required to deregister for VAT with effect from 1 April 2005, it follows that the amount previously charged or levied will no longer include VAT at the standard rate (unless that levy, duty or similar amount is set by any other Act, Regulation or measure having the force of law as a VAT inclusive amount, and where that legislation has not been amended with effect from 1 April 2005 to exclude the VAT). Consequently, vendors who make payment of the levy, duty or similar amount to such entities will no longer be entitled to claim input tax thereon.

Note that this does not apply to Regional Service Council (RSC) and Joint Services Board (JSB) levies, as these charges were previously levied by **local authorities (municipalities)**.

6.2 Definition of "Enterprise" Proviso (viii) *[Refer to paragraph 5.1.2]*

Constitutional institutions listed in Schedule 1 to the PFMA are treated similar to public authorities in that their activities are not taxable. However, the difference in VAT treatment lies in the following:

- a constitutional institution is not included in the definition of "public authority" in section 1 of the Act; and
- the activities of constitutional institutions are now excluded entirely from the definition of "enterprise" in terms of proviso (viii) to the definition of "enterprise". Accordingly, their activities can never fall within the ambit of the Act, and they may not register for VAT.

Constitutional institutions which were registered prior to 1 April 2005 must therefore deregister. Relief from the output tax normally due on this taxable event has been provided to these entities in terms of proviso (iv) to section 8(2) of the Act. (See paragraph 6.7 below).

Archived

6.3 Definition of "designated entity" *[Refer to paragraph 5.1.3]*

A designated entity is a specific kind of vendor, namely:

- a **"public authority"** which is registered for VAT in terms of **paragraph (b)(i) of "enterprise"** (only to that extent); or
- a **major public entity** listed in **Schedule 2 to the PFMA**; or
- a **National Government Business Enterprise or Provincial Government Business Enterprise** listed in either **Part B or D of Schedule 3 to the PFMA**; or
- a **"Public Private Partnership"** (or PPP as it is known) as defined in the PFMA and the Treasury Regulations; or
- a **"welfare organisation"**; or
- a **"municipal entity"** (as defined in section 1 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000)); or
- an **entity which has powers similar to those of any water board** listed in Part B of Schedule 3 of the PFMA, where that entity would have also complied with the definition of 'local authority' prior to the deletion of that definition on 1 July 2006.

These are entities in which Government has an interest and may therefore assist them by funding their activities. For example, Government may be the majority or sole shareholder, or the entity might be involved in delivering public goods and services. Designated entities are identified as service providers to Government to the extent that the payment is in respect of taxable supplies made by them. (See application of section 8(5) in paragraph 6.8 below).

As the deeming provision in section 8(5) was amended so that it only applies to designated entities, with effect from 1 April 2005, any payment to a designated entity by a public authority in respect of taxable activities will be subject to VAT at the standard rate of 14%. This is because the zero-rating under section 11(2)(p) was deleted. There are two exceptions in this regard, namely:

- where the designated entity is a welfare organisation – in which case the zero rate in terms of section 11(2)(n) will continue to apply; and
- where the designated entity receives a grant in terms of section 10(1)(f) of the Skills Development Act, 1998 (Act No. 97 of 1998) for training its employees, that payment is zero-rated. (Section 11(2)(u)).

Archived

6.4 Definition of "grant" *[Refer to paragraph 5.1.4]*

A grant which is paid by a public authority to a private vendor (i.e. not a "designated entity") will be zero-rated in the hands of the recipient in terms of sections 8(5A) and 11(2)(t) of the Act. Note that subsidies/grants to vendors may also be distributed via local authorities/municipalities and constitutional institutions.

The amended law also allows such payments to qualify for zero-rated VAT treatment, as well as payments made under the DOR Act (mainly to local authorities/municipalities). Prior to 1 April 2005 the receipt of such payments would not have qualified for the zero rate, since they would have been excluded from the definition of "transfer payment".

The term "grant" which replaces the term "transfer payment" in the Act is split into two main parts as described below.

- *"means any appropriation, grant in aid, subsidy or contribution transferred, granted or paid to a vendor by a public authority, municipality or constitutional institution…"*

The first part of the definition describes in general terms which type of payments will qualify as a "grant". The use of the words "appropriation", "grant in aid" and "subsidy", indicate that the receipt constitutes assistance from the state (usually in the form of money). In other words, it is a gratuitous or "unrequited" payment by the grantor, where little or no reciprocity is expected from the recipient in the form of a supply of goods or services of corresponding value.

Where the recipient is required to perform minor actions in regard to the grant, such as providing the grantor with information on how the funds were spent, or reporting on how goods or services granted were applied, these actions are not regarded as constituting a taxable supply of "services" by the grantee to the grantor in terms of section 7(1)(a). However, if a public authority engages a service provider to supply a specific service in return for the payment, that payment is not a "grant" as defined.

A "grant" also excludes financial assistance in the form of a loan where, and to the extent, that the amount must be repaid to the lender ("grantor") either in the form of money, or in the form of a supply of goods or services.

Archived

Example

A department engages a private research consultant to conduct a market survey on the public perceptions of the introduction of new legislation pertaining to the taxi industry. As the department has directly procured the services of the vendor, the activities involved in conducting the research and presenting the research findings to the department do not constitute a statement of how grant funds were spent. The payment in this regard is therefore consideration for the actual supply of goods or services which is subject to VAT at the standard rate and it is not a zero-rated "grant".

- *"…but does not include—*
  - *(a) a payment made for the supply of any goods or services to that public authority or municipality, including … in accordance with a procurement process prescribed—*
  - *(b) …"*

The second part of the definition is essentially a "procurement" test which specifically excludes payment for the actual supply of goods or services by a public authority, local authority/municipality or constitutional institution to the extent that those goods or services are acquired in terms of their respective prescribed procurement procedures. This refers to capital or operating expenditure incurred by a public authority or local authority/municipality, or constitutional institution for its own consumption in conducting the activities of that entity. These expense items should fall under the budget headings *"Current payments"* or *"Payments for capital assets"* of that entity.

The use of the word "including" in the statement *"…**including** …in accordance with a procurement procedure…"* recognises the possibility that goods or services may be acquired by the constitutional institution, public authority or local authority/municipality where the prescribed procurement procedure may not apply. To the extent that there is a reciprocal supply of goods or services in return for the payment, it will not qualify as a "grant".

It should also be noted that where the grantor pays a supplier of goods or services directly on behalf of the grantee, this does not mean that the supplier may charge the zero rate on the supply made to the grantee. In such cases, the grantee is still deemed to make a zero-rated **deemed supply** to the grantor in respect of the payment, but the supplier must charge VAT on the **actual supply** at the standard rate (if it is a taxable supply), and issue a tax invoice to the grantee for purposes of claiming input tax thereon according to the normal VAT rules.

Archived

Examples

- Office supplies paid for out of petty cash where the formal procurement procedure does not apply;
- Funds paid to a vendor in terms of a "grant contract" under the budget item headed *"Transfers and subsidies to:"*, but where part of the funds must be used to purchase fixed assets and create intellectual property which becomes the property of the grantor;
- Any other payment which is incorrectly classified by a public authority as a "grant", where, in substance, the amount represents payment for the actual supply of goods or services which are to be consumed by the public authority making that payment.

- *"."...but does not include—*

  (a) …

  (i) in terms of the Regulations issued under section 76(4)(c) of the Public Finance…; or

  (ii) in terms of Chapter 11 of the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003), or any other similar process; or…"

In the past, Regulations required that the procurement of goods and services by departments should be done through the State Tender Board only. National and Provincial Departments now procure goods or services either through the State/Provincial Tender Boards, or in terms of the PFMA. This dual system applies until the State/Provincial Tender Boards are dismantled, after which, public authorities must procure goods and services in accordance with the PFMA Regulations.

Archived

The Municipal Finance Management Act ("the MFMA") applies to local authorities in the same way that the PFMA applies to public authorities. However, the procurement procedure as set out in Chapter 11 of the MFMA only applies to certain local authorities, because the application of these provisions is being phased in. Until all local authorities/municipalities have been fully phased in, it will be found they will apply either the procedures contained in Chapter 11 of the MFMA, or their existing or transitional procurement methods.

- *"...but does not include—*

  (a) …

  (b) a payment contemplated in section 8(23);"

Housing subsidy payments are also excluded from the definition of "grant". However, these payments qualify for zero-rated VAT treatment under sections 8(23) and 11(2)(s) of the Act. (See the application of these provisions in paragraphs 6.10 and 6.11.3 below).

6.5 Definition of "public authority" *[Refer to paragraph 5.1.5].*

As explained in paragraph 4.3, the terms "department", "division of the public service" and "provincial administration" are not defined for VAT purposes, and this introduced some doubt as to the VAT status of other government agencies. As a result of this uncertainty, some constitutional institutions and regulatory, administrative or statutory bodies registered for VAT in terms of paragraph (a) of the definition of "enterprise" as they did not regard themselves as public authorities. On the other hand, some of these entities regarded themselves as public authorities, and as they had not been notified to register as required in terms of paragraph (b)(i) of the definition of "enterprise", they did not register.

To clarify the situation, the definition of "public authority" was amended to **<u>include</u>**:

- the **entities listed in Parts A & C of Schedule 3 to the PFMA** (including any subsidiary or entity under the ownership control of that entity); and
- all the **national and provincial government departments listed in Schedules 1, 2 or 3 of the PSA** (including any branches, divisions, trading accounts, local offices and other components of that department); and
- **certain other entities** which should be regarded as public authorities. This was introduced primarily to address the following situations:
  - where newly created public entities are in the process of being classified;
  - where entities are re-classified in terms of the PFMA as a result of changes to their functions and mandate from Government; and
  - where entities disagree with their classification in terms of the PFMA and intend to apply for re-classification (or entities which have already applied to be re-classified).

Archived

Note that the definition <u>does not include</u>:

- **constitutional institutions listed in Schedule 1 to the PFMA;**
- **national or provincial government business entities listed in Parts B & D of Schedule 3 to the PFMA;**
- **major public entities listed in Schedule 2 to the PFMA;**
- **public private partnerships (PPP's);**
- **local authorities/municipalities (town councils, TLC's, RSC's, JSB's, etc); or**
- **educational institutions (schools, universities, etc.).**

6.6 Definition of "transfer payment"

The definition was replaced with the definition "grant" (see paragraph 6.4 above). Although the term "grant" includes a wider number of payments than the term "transfer payment", it is more specific so that it provides a greater degree of certainty in identifying the type of payments which are intended to qualify for zero-rated tax treatment.

6.7 Section 8(2) proviso (iv) - Certain supplies of goods or services deemed to be made or not made (deemed supply of assets on ceasing to carry on an enterprise - output tax relief for certain public entities) *[Refer to paragraph 5.2.1].*

Section 8(2) deems a vendor to supply the assets used for enterprise purposes when ceasing the enterprise. It requires that output tax be declared on the lesser of cost or open market value of those assets at the standard rate. However, proviso (iv) was inserted under section 8(2) to provide relief from the output tax which would otherwise have been payable by constitutional institutions and public authorities upon deregistration. The provision is analysed in detail as set out below:

- *"(iv) this subsection shall not apply to a vendor that is a constitutional institution … or a public authority, respectively… where that vendor… ceases to be a vendor"*

No output tax is payable in terms of section 8(2) of the Act upon deregistration where:

- The entity was not a "public authority" prior to 1 April 2005, but falls within the amended definition after that date (e.g. Schedule 3A and 3C PFMA entities); or
- The entity is a constitutional institution listed in Schedule 1 to the PFMA, and from 1 April 2005 may no longer be regarded as an "enterprise" for VAT purposes because of the insertion of proviso (viii) to the definition of "enterprise".

This means that where a public authority or constitutional institution was registered for VAT prior to 1 April 2005, it will not be required to declare output tax on the value of assets deemed to be supplied upon deregistration despite the fact that they may have been allowed to claim input tax on certain assets acquired during the time that it was registered. The provision is primarily to avoid the circular flow of funds within the Government budgeting cycle.

Archived

Similarly, the proviso to section 23(4) was also inserted to deal with the liability of those entities which did not register because of the uncertainty regarding the meaning of the term "public authority", and hence, the application of paragraph (b)(i) of the definition of "enterprise". (See discussion under paragraphs 4.1.1, 4.3, 6.1 and 6.5).

- *"(iv) where that vendor…(other than a vendor who applied and was registered as a vendor during the period 22 December 2003 to 31 March 2005) …"*

However, the relief does not apply where the public authority or constitutional institution applied to register for VAT and was registered during the period 22 December 2003 to 31 March 2005.

This exclusion is intended to prevent abuse whereby entities which were registered for VAT during the aforementioned period and claimed input tax on their assets whilst being aware that no output tax would be required upon deregistration. Alternatively, if the person representing that entity was not aware of the new laws, to prevent the entity from inadvertently acquiring a tax benefit or advantage as a result of the application of the amended law.

- *"(iv) where that vendor… ceases to be a vendor…as a result of –*
  - *(aa) the substitution of the definition of 'public authority' … or the insertion of paragraph (viii) to the proviso to the definition of 'enterprise' …; or*
  - *(bb) the re-classification of that vendor or part of that vendor's activities within the Schedules to the Public Finance Management Act, …subsequent to the introduction of the Revenue Laws Amendment Act, 2004.";*

The relief applies only in the following instances:

1. Where the vendor falls within the amended definition of "public authority", and has not been notified to register in accordance with paragraph (b)(i) of the definition of "enterprise" with effect from 1 April 2005; or
2. Where the vendor is a constitutional institution and as a result of the insertion of proviso (viii) to the definition of "enterprise" with effect from 1 April 2005, its activities are excluded from the definition of "enterprise"; or
3. Where the vendor is a public entity listed in the Schedules to the PFMA, and, as a result of a re-classification under those Schedules on or after 22 December 2003, the entity is classified as a "public authority" or constitutional institution with effect from 1 April 2005 (the implications of which are set out in points 1 and 2 above). Where the re-classification relates to only a part of the public authority's activities, the relief applies only to that extent.

Archived

6.8 Section 8(5) - Certain supplies of goods or services deemed to be made or not made (payment received from public and local authorities – deemed supply by a "designated entity") *[Refer to paragraph 5.2.2].*

- *"For the purposes of this Act a **[vendor]** designated entity shall be deemed to supply services to any public authority or municipality …"*

Refer to paragraph 4.6 on the application of the law as it read prior to 1 April 2005 (as those principles are still relevant after 1 April 2005). The effect of replacing the word "vendor" with the term "designated entity", is that section 8(5) now only applies to designated entities.

As discussed previously, the deemed supply will arise whether the payment is received from a public authority or a local authority/municipality. Since the definition of "public authority" has been expanded to include public entities listed in Parts A & C of Schedule 3 to the PFMA, payments by these entities to a "designated entity" will also give rise to a deemed supply. (Refer also to paragraphs 5.1.3 and 6.3 above for more details about designated entities).

- *"…to the extent of any payment made by the authority concerned…"*

See paragraph 4.6 on the application of the law as it read prior to 1 April 2005.

- *"…to or on behalf of **[the vendor]** that designated entity in respect of the taxable supply of goods or services by **[the vendor to any person.]** that designated entity;"*

See paragraph 4.6 on the application of the law as it read prior to 1 April 2005. The amendment is textual, following on from the fact that this provision now applies only to designated entities. The reference to "any person" has been deleted as it was deemed superfluous to refer to the recipient of the designated entity's taxable supplies within the context of the amended wording.

6.9 Section 8(5A) - Certain supplies of goods or services deemed to be made or not made (payment received from public and local authorities by a vendor (not being a "designated entity")) *[Refer to paragraph 5.2.3]*

- *"For the purposes of section 11(2)(t)…"*

Unlike section 8(5), which applies for the purposes of the Act as a whole, this provision applies specifically for the purposes of the zero-rating provided for grant payments in terms of section 11(2)(t) of the Act.

Archived

- *"…a vendor (excluding a designated entity) shall be deemed to supply services to any public authority, municipality or constitutional institution listed…"*

Since the amendment to section 8(5) makes that provision applicable exclusively to designated entities, a similar provision was introduced to create a deemed supply where a vendor, (not being a designated entity), receives a grant. (See also paragraph 4.6 on the application of section 8(5) for the relevant interpretation principles).

The problem was that under the prior wording of the Act, a "transfer payment" as defined would only qualify for the zero-rate in terms of section 11(2)(p) of the Act, where the grantor was a "public authority". However, a similar subsidy or grant payment by a local authority/ municipality or certain PFMA entities did not qualify for the zero-rating.

Section 8(5A) (through the amended definition of "public authority"), now extends the deeming provision relating to grants (and hence the zero-rating provisions under section 11(2)(t) of the Act) to apply in respect of certain payments made by constitutional institutions, local authorities/municipalities, and public entities listed in Parts A & C of Schedule 3 to the PFMA. The purpose of this deeming provision is to bring a grant payment within the scope of the Act so that the zero-rating in terms of section 11(2)(t) can apply. However, the provision does not apply to a "designated entity", as section 8(5) will apply in that case (and generally be subject to the standard rate).

Section 8(5A) also includes grant payments made between any of the entities mentioned, for example, a grant from one local authority/municipality to another, or from a Schedule 3A PFMA entity to a Schedule 3C PFMA entity. This is to cover the situation where the responsibility to approve and make grants available to the identified beneficiaries is devolved or assigned to another entity.

- *"…to the extent of any grant paid to or on behalf of that vendor in respect of the taxable supply of goods or services by that vendor."*

The deeming provision only applies where the amount paid to the vendor by the public authority, local authority/municipality or constitutional institution is a "grant" as defined. (See also paragraph 4.6 on the application of section 8(5) for the relevant interpretation principles, as well as the explanation on the definition of "grant" in paragraph 6.4 above).

Archived

6.10 Section 8(23) - Certain supplies of goods or services deemed to be made or not made (housing subsidy payments received by a vendor from public or local authorities) *[Refer to paragraph 5.2.4]*

- *"For the purposes of this Act …"*

This provision applies for the purposes of the Act as a whole.

- *"…a vendor shall be deemed to supply services to any public authority or municipality…"*

Previously, housing subsidy payments were treated as zero-rated transfer payments in terms of section 8(5) and 11(2)(p) of the Act. As section 8(5) of the Act was amended so that it now applies exclusively to designated entities, a similar provision was introduced to create a deemed supply where a vendor (e.g. a property developer or builder), is involved in delivering low cost housing projects and that person receives an amount on behalf of the housing subsidy beneficiary. The purpose of this deeming provision is to bring the housing subsidy payment within the scope of the Act so that the zero-rating in terms of section 11(2)(s) of the Act can apply. (See paragraph 4.6 on the application of section 8(5) as it read prior to 1 April 2005 for the interpretation principles).

- *"… to the extent of any payment in terms of the Housing Subsidy Scheme referred to in section 3(5)(a) of the Housing Act, 1997 (Act No. 107 of 1997)…"*

The deemed supply only applies in respect of, and to the extent that, the vendor receives payment of the low cost housing subsidy amount to which certain beneficiaries are entitled in terms of section 3(5)(a) of the Housing Act. If the housing subsidy is insufficient to cover the price of the house, the additional consideration payable by the beneficiary to the vendor is subject to tax at the standard rate .

- *"…made to or on behalf of that vendor in respect of the taxable supply of goods and services by that vendor."*

See paragraph 4.6 above for the relevant interpretation principles.

6.11 Section 11(2) - Zero-rating – Services *[Refer to paragraph 5.3]*

See paragraph 4.7 for an explanation on the application of section 11(2).

Archived

6.11.1 Section 11(2)(p) - Zero-rated "transfer payment" *[Refer to paragraph 5.3.1]*

The provision was deleted. (See also paragraphs 6.4 and 6.6 above).

6.11.2 Section 11(2)(t) - Zero-rated "grant" *[Refer to paragraph 5.3.2].*

☛ *"the services are deemed to be supplied in terms of section 8(5A)."*

Essentially, this provision will apply where a private vendor (not being a "designated entity"), receives some form of financial assistance from the State or a local authority/municipality to enable that person to make taxable supplies. The zero-rating only applies where the amount is a "grant" as defined in section 1, and where the deeming provisions of section 8(5A) of the Act apply. (See also paragraphs 6.4 and 6.9 above, particularly where the grantor makes payment on behalf of the grantee directly to a third person who makes a supply to the grantee). The payment must not constitute the procurement of goods or services in terms of section 7(1)(a) of the Act by a public authority, constitutional institution or local authority/municipality, or be a housing subsidy payment. (The latter payments being specifically dealt with under sections 8(23) and 11(2)(s)).

6.11.3 Section 11(2)(s) - Zero-rated housing subsidy payment. *[Refer to paragraph 5.3.3]*

☛ *"the services are deemed to be supplied to a public authority or municipality in terms of section 8(23)."*

The situation here is slightly different from the explanation on the application of section 11(2)(t) in paragraph 6.11.2 above, as the subsidy beneficiary is generally a private individual (not registered for VAT). Secondly, the amount is normally paid directly to an intermediary (probably a vendor), who will supply the requisite goods and services, and not to the beneficiary.

As mentioned in paragraph 6.10 above, this provision is underpinned by the government policy that housing subsidies should not bear VAT at the standard rate. The zero-rating only applies to the extent that the subsidy amount is used to pay for goods and services which relate to the acquisition of the low cost house itself, or essential services which pertain directly to the ownership and registration of the property in the beneficiary's name. For example, the payment may be made directly to a builder, property developer, building materials supplier, or conveyancer. Where additional consideration is paid to the service provider which is not covered by the housing subsidy amount, VAT at the standard rate of 14% must be charged on that amount. *[See Example 1 in Annexure D].*

Archived

6.11.4 Section 11(2)(n) - Zero-rated payments to welfare organisations *[Refer to paragraph 5.3.4].*

The amendment to section 11(2)(n) of the Act is purely textual in nature. It was necessary due to the amendment to section 8(5) and the inclusion of a welfare organisation in the definition of "designated entity". The effect is that although a welfare organisation is a "designated entity", the zero-rating has been retained for the deemed supply which arises in respect of certain payments received for carrying on welfare activities.

However, it should be noted that where the constitutional institution, public authority or local authority/municipality procures goods or services through that welfare organisation, there may be an actual (standard-rated) taxable supply in terms of section 7(1)(a) of the Act. Payments made to welfare organisations in this regard are therefore not zero-rated in terms of this provision. (See also paragraphs 6.4 and 6.9 above, particularly where the grantor makes payment on behalf of the grantee directly to a third person who makes a supply to the grantee).

6.11.5 Section 11(2)(u) - Zero-rated SETA training grants paid to designated entities *[Refer to paragraph 5.3.5]*

- *"the services are deemed to be supplied in terms of section 8(5) by a designated entity in respect of any payment made in terms of section 10(1)(f) of the Skills Development Act, 1998 (Act No. 97 of 1998), to that designated entity."*

The amendments had the unintended effect that SETA grants payable to designated entities did not qualify for the application of the zero rate of VAT, as is the case for other vendors. Designated entities are also liable for SDL payments and are also entitled to receive training grants in terms of section 10(1)(f) of the Skills Development Act, 1998, once they have submitted their workplace training plans to the Department of Labour. The Act was therefore amended further to ensure that SETA training grants paid to designated entities are zero-rated, otherwise it would have created an iniquitous situation.

6.12 Section 18(4) - Change in use adjustments (Denial of input tax). *[Refer to paragraph 5.4].*

- *"(iv) this subsection shall not apply where a constitutional institution listed in Schedule 1 or a public entity listed in Part A or C of Schedule 3 … is re-classified within the Schedules to the Public Finance Management Act, 1999…"*

Archived

Section 18(4) provides that an input tax credit to be claimed in certain instances where there has been a change in the use or application of goods or services which were originally acquired for exempt, private, or other non-taxable purposes and subsequently applied wholly or partially for taxable use or application. This will apply, for example, where VAT was paid on the acquisition of dwellings used to generate exempt rental income, and subsequently those dwellings are converted into offices or commercial accommodation and rented out as such.

Since the classification of public entities in terms of the PFMA is used as a basis for determining how an entity is treated for VAT purposes, any re-classification of that entity within those Schedules may have a VAT implication. Where an entity is not registered for VAT, as it is classified as a "public authority" or a "constitutional institution", the re-classification of that entity (or a part of its activities) may result in that entity becoming liable to register. If this occurs, proviso (iv) to section 18(4) will prevent that entity from claiming any input tax on the adjustment which would otherwise have been allowed, for any assets brought into the "enterprise" in respect of which it is now required to register.

Example

If an entity in Schedule 3C of the PFMA (Provincial Public Entity) is re-classified under Schedule 3D of the PFMA (Provincial Government Business Enterprise), it will not be able to claim an input tax adjustment on their existing assets which are now applied for taxable purposes as a result of the re-classification.

Archived

- *"… and applies those goods or services for the purposes of consumption, use or supply in the course of making taxable supplies."*

The terms "re-classified" and "applies" in this context, refer to the extent of the change in the taxable status of the entity's activities as a result of the re-classification in terms of the PFMA (and hence the change in application of certain assets for that purpose). This re-classification may require the entity to be notified to register to the extent that the supplies are regarded as taxable in terms of paragraph (b)(i) of the definition of "enterprise". Whether wholly or partially taxable, an input tax adjustment is denied to the extent that the assets are subsequently applied for enterprise purposes as a result of the re-classification.

Examples

- Where a Schedule 3A PFMA entity ("public authority") transfers assets used for exempt "public authority" activities into a separate "ring-fenced" trading account in order to carry on a taxable business activity in respect of which it has been (or will be) notified to register for VAT in terms of paragraph (b)(i) of the definition of "enterprise".
- Where a Schedule 3C PFMA entity ("public authority") provides funds and/or assets for the purposes of conducting a business activity under a separate legal entity formed (or to be formed) for that purpose. E.g. where the entity transfers existing funds or assets originally for exempt/out of scope "public authority" activities to a Schedule 3D PFMA entity (vendor), which it controls, for the purposes of making taxable supplies.

6.13 Section 23(4) proviso - Registration of persons making supplies in the course of enterprises (non-registration of certain public entities not already registered on or before 31 March 2005) *[Refer to paragraph 5.5].*

"(4) Where any person has -

a) applied for registration in accordance with subsection (2) or (3) …; or

b) not applied for registration in terms of subsection (2)…: Provided that .. may consider equitable."

Provided that …where that person is a public entity listed in Schedule 1 or Part A or C of Schedule 3 … (Act No. 1 of 1999), which was liable to be registered …, but did not register before 1 April 2005, the Commissioner must not register that person in respect of those supplies."

Section 23(4) provides that where any person has **applied for registration** within the required 21 day period after becoming liable, or otherwise **qualifies for voluntary registration**, the Commissioner may determine the date that the person shall be a vendor for VAT purposes. Where the person is **required to register** for VAT, and did not apply within the 21 day period allowed, that person is **regarded as a vendor from the date they were first liable to register**. However, having regard to what is considered equitable in the circumstances of the case, the Commissioner may determine a later liability date for that person.

As from 1 April 2005 all public entities listed in Schedule 1 and most of the entities listed in Part A or C of Schedule 3 to the PFMA, which were registered as vendors were required to deregister. Only in very limited circumstances are these entities required to register as vendors or remain on the VAT register (if already registered).

Archived

The proviso to section 23(4) provides that with effect from 1 April 2005, the Commissioner may not register such public entity in respect of any enterprise activities carried on prior to 1 April 2005. By preventing the Commissioner from registering the public entities concerned, those entities will, in effect, not be held liable for the output tax which would otherwise have been payable, nor will they be entitled to claim a refund of any input tax incurred (or interest thereon) in respect of any period prior to 1 April 2005.

The intended effect of this amendment is that public entities who have not registering in the past will not be required to register, account for the input tax and output tax on their transactions, and then deregister with effect from 1 April 2005. This applies whether the public entity concerned was liable to register, or if it could have registered voluntarily. The reason for this is that these entities are largely funded by Government and if there were unbudgeted flows of funds to these entities, their allocations of funds would have to be adjusted.

6.14 Section 40A - Liability of public authorities and certain public entities for tax and limitation of refunds *[Refer to paragraph 5.6]*.

Section 40A deals with the issues pertaining to the recovery of tax from any public entity listed in Schedules 1, 3A or 3C of the PFMA where that entity has been registered for VAT by the Commissioner in respect of any period prior to 1 April 2005. The section basically provides that where certain payments from Government were treated incorrectly for VAT purposes prior to 1 April 2005, the tax will not be recoverable or refundable (as the case may be), and where an assessment has been raised and not yet paid in respect of such amounts, application may be made to reduce the assessment. The provision is analysed and discussed in detail below.

- *"(1) This section applies in respect of the supply of goods or services on or before 31 March 2005 by any public authority or public entity listed in Schedule 1 or Part A or C of Schedule 3 to the Public Finance Management Act, 1999 (Act No. 1 of 1999).*

Sub-section (1) sets the framework for the scope of application of sub-sections (2) to (4). The provision was necessary so that the VAT consequences of the incorrect treatment of certain payments for supplies made by public authorities and certain public entities before 1 April 2005 could be dealt with. As with some of the other amendments, the underlying reason for the provision is to reduce the circular flow of funds within government departments and various government agencies.

Archived

To qualify for the relief provided in this section, the supplier must be a "public authority" or a constitutional institution listed in Schedule 1 to the PFMA, or a national or provincial public entity listed in Part A or C of Schedule 3 to the PFMA (before 1 April 2005). The entity must have an existing or potential liability for VAT in accordance with the specific conditions contained in sub-paragraphs (2) to (4), which are discussed below.

- *"(2) Where the Commissioner on or before 31 March 2005 issued an assessment … contemplated in subsection (1), to correct a prior incorrect application of the zero per cent rate of tax in terms of section 11(2)(p) in respect of that supply,…"*

The first part of sub-section (2) deals with the situation where on or before 31 March 2005 the Commissioner has raised an assessment for the VAT which should have been charged by the vendor at the standard rate in terms of section 7(1)(a) on a payment for a taxable supply, but instead, the vendor incorrectly applied the zero rate in terms of section 8(5) and 11(2)(p), on the assumption that the payment was a "transfer payment" as defined in section 1.

- *"(2) ... the Commissioner must, on written application, reduce that assessment…"*

Any public entity or public authority which has had an assessment raised against them as contemplated in sub-section (1), may apply in writing to the Commissioner to reduce the assessment for the tax period concerned. If all the conditions in the section are met, the Commissioner **must** reduce the assessment accordingly.

- *"(2) … to the extent that the amount of tax, additional tax or penalty arose as a result of that correction and was not yet paid on that date."*

The specific liability which may be reduced, is the total amount of tax, additional tax, penalty or interest **which has arisen directly as a result of any assessment which was issued in respect of the supplies referred to in sections 40A(1) and (2), which were incorrectly regarded as being in respect of a zero-rated "transfer payment".** For example, the reduced assessment will not apply in any of the following circumstances:

- where the VAT declared on the VAT 201 was merely not paid, or was paid late; or
- where there was a failure to submit a return and as a result, an estimated assessment was issued in respect of that tax period; or
- where an assessment was issued because output tax was under-declared for any reason other than the one mentioned in section 40A(2), or if the input tax was overstated in respect of any tax period.

Archived

The relief applies only to the **net balance** of any tax, additional tax, penalty or interest as at 31 March 2005 which remains payable in respect of the incorrectly treated payments referred to in sections 40A(1) and 40A(2). It does not apply to any amount assessed in this regard which has already been paid or otherwise recovered by SARS. This includes debt which was set off (or which could have been set off) against refund credits, arising in another tax period.

- *"(2) … Provided that the reduced assessment will not result in a refund to that public authority or public entity".*

The application of the reduced assessment may not have the effect that the public authority or public entity obtains a refund of any tax (including additional tax, or any amount allocated to penalty or interest) for any period prior to 1 April 2005 to which the assessment relates.

Where a part of, or the entire debt, has been paid or otherwise recovered by SARS, that amount will not be added back before calculating the amount of the reduced assessment. This is because the proviso to this section clearly states that the application of this provision **may not result in a refund** to that public authority or public entity. This means that the balance of existing credits in any other tax periods must first be transferred to the tax period in which the debt exists so that it reduces the outstanding debt, before applying the provisions of section 40A(2).

Archived

This will apply as follows:

- Vendors registered on Category A or C tax period - existing credits, and credits arising in any tax period ending on or before 31 March 2005; and
- Vendors registered on Category B, D or E tax period - existing credits, and credits arising in any tax period ending on or before 28 February 2005, plus any credits arising between the end of that tax period and 31 March 2005. (For example, the last tax period for a vendor on Category B will be from the beginning of March 2005 to the end of April 2005. Credits arising from transactions with a time of supply between 1 March 2005 and 31 March 2005 in the last tax period must be offset against the debt in this case before calculating the amount by which the assessment must be reduced in terms of section 40A(2)). *[See Example 13 in Annexure D which illustrates how this provision works].*

- *"(3) The Commissioner may not after 31 March 2005 make any assessment to correct a previous incorrect application of the zero per cent rate of tax in terms of section 11(2)(p) in respect of any supply of goods or services contemplated in subsection (1)."*

This provision applies to the same incorrectly treated payments as contemplated in sub-section (2). However, under this sub-section, SARS has not issued an assessment for the tax liability concerned, which would otherwise be recoverable from the public authority or public entity (whether registered as a vendor or not). Under subsection (3), SARS may no longer raise an assessment in respect of the tax liability pertaining to those incorrectly treated payments with effect from 1 April 2005.

This means that an assessment may only be raised by SARS on or after 1 April 2005 to recover the VAT payable on taxable supplies prior to 1 April 2005 in circumstances **other than** those covered by this provision. For example, an assessment may still be raised by SARS where:

- there was a failure to submit a return and as a result, an estimated assessment was issued in respect of that tax period;
- the amount due is not connected to any dispute regarding a transfer payment; or
- an assessment was issued in respect of any tax period where the output tax was under-declared (other than in the specific circumstances provided for in section 40A(1)), or the input tax was overstated.

Archived

- *"(4) If a public authority or public entity incorrectly charged tax at the rate referred to in section 7(1)(a) instead of the zero per cent rate of tax in terms of section 11(2)(p) in respect of any supply contemplated in subsection (1), the Commissioner may not refund any such tax or any penalty or interest that arose as a result of the late payment of such tax, paid by that public authority or public entity to the Commissioner."*

This provision deals with the situation where the public authority or public entity has incorrectly treated a "transfer payment" as consideration for a taxable supply and has paid output tax to SARS at the standard rate in terms of section 7(1)(a) instead of at the zero rate in terms of sections 8(5) and 11(2)(p). In such cases, section 40A(4) will override sections 44(2) and (3) (which deal with refunds), so that the public authority or public entity may not claim a refund of the output tax which it may consider as having been overpaid.

Example

A Schedule 3A public entity (vendor) submitted a refund return for R50 000 for the October 2004 tax period. In the meantime, the SARS auditors raised an assessment for R60 000 in respect of a payment for services in the tax period ending December 2003 which the vendor had treated (incorrectly) as a zero-rated "transfer payment". Assuming that the amount of R40 000 was the correct refund amount for the October 2004 period, that amount must first be transferred so that it can reduce the tax, penalty and interest incurred in the December 2003 tax period. The vendor can then apply for the assessment for the December 2003 tax period to be reduced by the amount of the unpaid tax, penalty and interest which remains after having set off the R40 000 credit (Section 40A(2)). SARS may not reduce the December 2003 tax period assessment to nil, plus refund the R40 000 for the October 2004, since this will result in an incorrect application of the law and an incorrect refund to the vendor. (Section 40A(4)).

[For further examples of the application of the provisions contained in this note, refer to Annexure D].

Note that Section 40B was later introduced to deal with payments received in respect of the DOR Act, the wording of which is similar to section 40A, and is mostly applicable in the case of local authorities (municipalities). For more information on section 40B, refer to the draft interpretation note on the VAT treatment of supplies made by municipalities, which is available on the SARS website.

Archived

7. PRACTICAL IMPLICATIONS

The implementation of the changes to the law dealt with in this note will give rise to the following practical issues:

7.1 New registrations

Certain public authorities may be notified by SARS that they should be registered for all or some of their activities in terms of paragraph (b)(i) of the definition of "enterprise", after receiving the decision of the Minister in this regard. This will happen if the supplies made are regarded by the Minister as being in competition with other taxable supplies made in the private sector.

In addition, if a public authority is not notified as stated above, it may nevertheless make an application to register. The details of the case and the public authority's reasons for wanting to register must be clearly motivated in a written application to SARS Head Office, Legal and Policy Division: Indirect Taxes, Private Bag X923, Pretoria, 0001 (facsimile number (012) 422 5043). After considering the merits of the case in consultation with NT, and with reference to the requirements of the PFMA, that entity will be notified whether or not it may register for VAT after a decision to that effect has been made by the Minister.

Note that where a public entity did not register in respect of supplies made during any period prior to 1 April 2005, the Commissioner may not register that entity retrospectively in respect of that period. (Proviso to section 23(4)) (See also paragraph 7.6 below)

7.2 Budgeting

On the expenditure side of the budget, public authorities which are required to deregister for VAT with effect from 1 April 2005 will have to ensure that when they prepare their budgets, they should be calculated on the basis that the VAT incurred on capital and operational expenditure is a cost which cannot be claimed as input tax. When the budgeted amount is paid to that entity, it will not include any output tax to be declared to SARS, unless that public authority is a "designated entity" which is liable to register for VAT (in which case it will pay output tax only to that extent). On the income side, the setting of prices, levies, etc. may need to be revised to take account of the fact that any amounts charged or levied may no longer include VAT at the standard rate with effect from 1 April 2005.

Archived

7.3 Procurement of goods and services versus "unrequited" grant payments

Public and local authorities, constitutional institutions and SARS officials must ensure that they understand the difference in tax treatment between the payment of a grant (0% VAT in the hands of the recipient), and the payment of consideration for a taxable supply (14% VAT payable by the supplier). Also, vendors who receive payments from departments, public entities or local authorities/municipalities should ensure that they are informed quite clearly in terms of their contract or other payment advice, whether the amount constitutes a "grant" (gratuitous or "unrequited" payment), or if it is consideration for a taxable supply of goods or services procured, or otherwise acquired by that entity for their own consumption.

7.4 Procurement and accounting accruals

Inherent administration and accounting delays in the procurement and payment process (e.g. delays in receiving and capturing billing information and/or following up on tax invoices not yet received, etc) may lead to a position where many of the public authorities which are required to deregister cannot immediately and accurately determine their final position for VAT purposes as at 31 March 2005. To overcome this problem, a period of 6 months was allowed (up to 30 September 2005) for those entities to conduct the necessary internal audit procedures, make the final adjustments, and to submit this information to SARS. Refer to VAT News No. 25 and 26 for more details in this regard.

This was purely an administrative arrangement to ensure that the public entities concerned are provided with sufficient time to clear their accounting and administrative systems, and to report on any transactions where the tax point (time of supply in terms of section 9 of the VAT Act) is prior to 1 April 2005, and where the VAT on those transactions has not yet been included on a VAT 201 return, because of accounting/administration system "lag factors".

The following should also be noted in this regard:

a) Public authorities were not required to apply for this dispensation. It was automatically applied to all the public entities affected by the changes in the law.
b) The final VAT return still had to be submitted by the due date, based on the information available at the end of the relevant tax period.
c) The final adjustments are processed separately by SARS once they have been submitted as required, after the 6 months transition period.

Archived

This administrative arrangement **does not mean** that the entities concerned will continue to be VAT vendors and account for the VAT on supplies occurring on or after 1 April 2005. However, there are two cases which require special attention, namely:

- **SDL and other duties, levies, or similar charges by statutory, regulatory or administrative public authorities** – (See paragraphs 7.8 and 7.9 for details).
- **Payments basis of accounting** – where entities are registered on the payments basis of accounting and they pay certain expenses on or after 1 April 2005 (for which tax invoices are held) for supplies which have a time of supply prior to 1 April 2005, no input tax may be claimed in that regard. Similarly, where a debtor pays an amount to the public authority (vendor) on or after 1 April 2005, in respect of taxable supplies which it made prior to 1 April 2005, that public authority will not be required to declare output tax thereon. This is because for the purposes of applying the output tax relief in terms of proviso (iv) to section 8(2) of the Act, the vendor will first be converted to the invoice basis and the balance of debtors and creditors as at 31 March 2005 will be set off against each other. Hence, any debtors or creditors payments made to or by that public authority on or after 1 April 2005 in respect of supplies before that date, would have already been taken into account.

7.5 Outstanding VAT returns, payments, assessments and queries

The VAT files of the vendors affected by the amendments will be placed into suspense mode until all outstanding VAT 201 returns and payments have been submitted, final adjustments have been submitted, and all other queries regarding assessments and other administrative matters have been resolved. Whilst in suspense mode, no further VAT 201 returns will be issued.

On page 31 of the 2005/6 Budget Tax Proposals booklet issued by SARS, the following is stated in this regard:

*"**Public authorities/entities**: SARS raised assessments against many public authorities and entities due to ongoing confusion about the VAT implications of transfer payments. In 2003 and 2004, Government introduced a whole new set of VAT legislation to eliminate this confusion. In order to bring full finality to this matter, Government will write off outstanding assessments raised against public authorities and entities to the extent these assessments stem from this longstanding confusion."*

Any dispute regarding an assessment in respect of payments which have apparently been treated as zero-rated transfer payments in terms of sections 8(5) and 11(2)(p) of the Act, should therefore be resolved in the light of the explanations and interpretations put forward in this note.

Archived

Where it is established that the amount owing is in fact properly payable because the payment was incorrectly treated as a zero-rated "transfer payment" instead of a standard-rated payment in terms of section 7(1)(a), then the vendor may apply in writing to the SARS branch office where they are registered for the assessment to be reduced to the extent that the conditions in terms of section 40A are applicable. (See paragraph 6.14 for details).

7.6 "Ring-fencing" of trading activities

Public authorities, as a general rule, will not be required to register unless they are notified as required in paragraph (b)(i) of the definition of "enterprise". However, in paragraph 7.1 above, the issue of public authorities coming forward to request that their trading activities remain registered (or be considered for a first time VAT registration) was dealt with. Any decision to register a public authority in such cases will be determined as set out in that paragraph.

In order for a public authority to qualify as an "enterprise", the activity which is sought to be treated as taxable must be "ring-fenced" and should be moved out of mainstream non-enterprise activities of that Department or Schedule 3A or 3C PFMA entity, and conducted under a separate legal entity (unless all of the activities conducted by that public authority are regarded as taxable). This separate entity must have a separate accounting system and will be deemed to be a Schedule 3B or 3D "designated entity", if it conducts those taxable activities before it can be officially and properly classified in terms of the PFMA.

Archived

Where it is not possible to conduct the activity under a separate legal entity due to other rules and regulations with which that public authority must comply, the taxable activity must be "ring-fenced" under a separate trading account, branch or division. In such cases, the public authority concerned may be notified to register for the supplies made under that trading account, branch or division. Any transfer of funds or assets from the main public authority (non-vendor) to its taxable trading account or deemed Schedule 3B or 3D "designated entity" (vendor) will have the following VAT implications:

i) *Transfer of funds* – Output tax must be declared by the recipient as the amount constitutes consideration for a taxable supply (section 8(5)). When the taxable trading account/deemed Schedule 3B or 3D incurs VAT inclusive expenses, it is allowed to claim input tax thereon to the extent that it makes taxable supplies, if it meets all the other requirements for claiming input tax (e.g. sections 16(2), 16(3), 17(1), 20, etc).

ii) *Transfer of existing assets and other goods and services held before 1 April 2005* – No input tax adjustment is allowed to the separate taxable trading account/deemed Schedule 3B or 3D entity when it receives those goods or services for taxable application in the enterprise. (Section 18(4) proviso (iv).) If the transaction occurs on or after 1 April 2005, the main public authority must not declare output tax thereon, as it will no longer be a vendor. Where the transfer occurred prior to 1 April 2005, the transfer of the asset constitutes consideration for a taxable supply of services by the recipient (barter transaction), and input tax and output tax on that transaction must be accounted for by the parties respectively.

iii) *Purchase and transfer of goods or services acquired on or after 1 April 2005* – If the main public authority acquires goods or services on or after 1 April 2005 on its budget (as principal) and these are subsequently transferred to its separate taxable trading account/deemed Schedule 3B or 3D entity, neither the main public authority (non-vendor), nor the recipient is able to claim input tax thereon (Section 18(4) proviso (iv)).

iv) *Subsequent sale of goods or services where input tax was denied in terms of Section 18(4) proviso (iv)* – Where goods or services were acquired as discussed in (ii) and (iii) above, and those things are subsequently supplied in the course of an enterprise by that separate taxable trading account/deemed Schedule 3B or 3D entity, output tax must be charged at the standard rate. No input tax is allowed in terms of section 16(3)(h) in respect of that subsequent supply.

Archived

7.7 Classification of new entities and re-classification of existing entities in terms of the PFMA

The VAT treatment of new public entities which are in the process of being classified and existing public entities which are re-classified in terms of the PFMA as at 1 April 2005 will be decided upon by NT in consultation with SARS, based upon the policy principles discussed in this document as well as the circumstances of the particular case and/or similar cases encountered.

The possible VAT consequences of the transfer of funds or assets from public authorities to newly created entities and/or to separate trading accounts, as set out in paragraph 7.6 above should be noted in this regard.

7.8 SETA grants & SDL payments

The amendments ensure that SETA grants received and SDL payments made by vendors on or after 1 April 2005 are treated on a tax neutral basis. The effect is that input tax on current SDL payments made by vendors may no longer be claimed. The last SDL payment upon which a claim for input tax was allowed, is for the period ending March 2005, which was due for payment on 7 April 2005. Vendors were allowed to claim input tax in respect of any arrear SDL payments for SDL tax periods ending no later than 31 March 2005, if that arrear amount is paid on or before 7 April 2005. Where any payments are made after 7 April 2005, no input tax may be claimed thereon, as no output tax will be declared by the public authorities (NSF and SETA's) which will ultimately receive those payments.

The NSF and SETA's cannot claim input tax on training grants paid to vendors on or after 1 April 2005, since they are no longer vendors and do not account for supplies which occur on or after 1 April 2005.

No output tax must be declared by a vendor (including a "designated entity") on any SETA training grants received on or after 1 April 2005, as the zero rate in terms of sections 11(2)(t) or 11(2)(u) will apply (as the case may be).

Archived

7.9 Duties, levies and similar charges by regulatory, statutory or administrative authorities

Where any levy, duty or similar charge is paid to any statutory, regulatory, administrative, or other authority (being a "public authority" on or after 1 April 2005), which was registered for VAT prior to 1 April 2005, that payment no longer attracts VAT. This is because the public authority concerned was required to deregister for VAT in terms of the amended law, as explained in paragraph 7.8 above, and will therefore not account for the VAT on any supplies which occur on or after 1 April 2005. Consequently, vendors are not able to claim input tax on those payments if they are in respect of any period ending after March 2005.

Vendors are allowed to claim input tax in respect of any arrear payments for periods ending no later than 31 March 2005, if that arrear amount includes VAT at the standard rate, and it was paid on or before the due date for the last payment of any such levy, duty or similar charge.

7.10 International donor fund agreements

As a general rule, a “public authority” is not liable or entitled to register for VAT unless it is notified to that effect as contemplated in paragraphs 7.1, 7.6 or 7.7 above. However, some public authorities are involved in implementing certain projects for the general upliftment of South Africa and its citizens. These projects are funded in terms of international agreements between the South African government and foreign governments, or other International Development Agencies (“IDA’s”) such as the European Union, the United Nations, the World Bank, DFID, etc. Foreign governments and IDA’s normally provide that the funds donated should only be used for specific and mutually agreed upon programmes and activities and cannot be utilised for any taxes imposed under South African Law (for example, VAT).

Previously, sections 11(1)(o) and 11(2)(q) of the Act provided that the supply of goods or services may be zero-rated to the extent that the consideration for the goods or services supplied is paid from donor funds granted under any international agreement to which the Government of the Republic is a party. These provisions recognise that such an international agreement overrides South African domestic laws (including the VAT law).

However, the proof that a vendor must keep to substantiate the application of the zero rate in such cases has always been problematic. The difficulty was that under a VAT system, a final consumer should generally not be in a position to acquire goods or services from vendors by producing a certificate to the supplier. This was precisely the problem under the General Sales Tax system (GST), which resulted in extensive abuse of the certificates to obtain goods and services without the payment of tax, and was one of the main reasons why that tax was discontinued in favour of VAT.

The question which arises in this regard is whether a public authority may register as a VAT vendor in order to reclaim the VAT charged on goods or services acquired in terms of the requirements of the contract concerned. Such an arrangement will allow the public authority concerned to claim input tax on goods or services acquired at the standard rate for the project, where payment has been made out of the donor funds allocated for the project concerned, thus achieving the tax neutrality required in terms of the aid agreement.

Archived

In the past, as a result of the difficulty in applying sections 11(1)(o) and 11(2)(q) of the Act, upon written application, special arrangements made to allow a public authority to register for VAT in this regard. The Act was subsequently amended by introducing a deeming provision (section 8(5B)) as well as a zero-rating (amendment to section 11(2)(q)) so that this dispensation for approved projects could formally be integrated into the law. It should be noted that the purpose of any such registration in respect of international donor funded projects is entirely different (tax neutrality reasons), and should not be confused with a liability to register for taxable supplies as contemplated in paragraphs 7.1, 7.6 or 7.7.

Where public authorities have been permitted to register for VAT in respect of approved foreign donor projects, the input tax claims are limited to the VAT incurred on goods or services acquired which are directly in connection with the implementation of the internationally funded project. It does not entitle the public authority concerned to claim input tax on its normal VAT inclusive capital and operating costs (unless that entity has also been notified to register for taxable supplies as set out in paragraphs 7.1, 7.6 and 7.7 above – and then, only to that extent).

Where a public authority is allowed to register in this regard, the words "(international donor funded project)" must follow the trading name on the application form so that the VAT file and registration particulars on the system can be noted accordingly.

8. SUMMARY

8.1 Before 1 April 2005

- The definition of "public authority" was not clear. It included only the national and provincial government departments, and branches and components thereof, but not the public entities (government agencies) as listed in any of the Schedules to the PFMA.
- Public entities (including the non-business orientated entities listed in Schedules 1, 3A and 3C to the PFMA), fell within paragraph (a) of the definition of "enterprise" before 1 April 2005 and were liable to register if their taxable supplies exceeded the threshold of R 300 000 in section 23(1).
- Government departments which registered separate trading accounts for VAT without being notified as required in terms of paragraph (b)(i) of "enterprise", will be treated as normal enterprises in terms of paragraph (a) of "enterprise" until 1 April 2005.

Archived

- The definition of "transfer payment" was unclear. This lead to inconsistent application of the law. To qualify for the zero-rating in terms of section 11(2)(p), there must be a deemed supply in terms of section 8(5) where the payment is "unrequited". The payment must not be in respect of an actual supply of goods or services to the public authority in terms of section 7(1)(a).
- A deemed supply arises in terms of section 8(5) where an "unrequited" payment originates from a local authority but, as the amount paid is not a "transfer payment" (as defined), the zero-rating in terms of section 11(2)(p) does not apply.
- Appropriations in terms of the DOR Act do not comply with the definition of "transfer payment" and are not zero-rated.

8.2 On or after 1 April 2005

- The definition of "public authority" was amended to include all the government departments listed in Schedules 1, 2 and 3 of the PSA, as well as the public entities listed in Schedules 3A and 3C of the PFMA. The term excludes constitutional institutions and business orientated public entities (listed in Schedules 1, 2, 3B and 3D of the PFMA).
- PFMA public entities listed in Schedules 1, 3A and 3C which registered for VAT prior to 1 April 2005, were required to deregister for VAT (unless they were notified as required in terms of paragraph (b)(i) of the definition of "enterprise"). Relief from the output tax which would otherwise have been payable upon deregistration in terms of section 8(2) has been provided to these entities. (Proviso (iv) to section 8(2)).
- SARS may not retrospectively register any public entity listed in Schedules 1, 3A and 3C of the PFMA which failed to register prior to 1 April 2005. Therefore, those entities are not liable for the VAT which would otherwise have been payable, nor can they claim any refund in respect of any period prior to 1 April 2005. (Proviso to section 23(4)).
- If a public authority or any public entity listed in Schedules 1, 3A and 3C of the PFMA has incorrectly treated a payment as a zero-rated "transfer payment" prior to 1 April 2005 and has been assessed for that liability, that entity may apply for the assessment to be reduced accordingly. Where no assessment has been raised in this regard, SARS will not raise an assessment in respect of those incorrectly treated payments. (Sections 40A(2) and (3)).
- The definition of "transfer payment" as well section 11(2)(p) that zero-rated the receipt of those payments were both deleted. The definition of "transfer payment" was replaced with the definition of "grant" to provide more certainty as to which payments (appropriations/subsidies) from government qualify for zero-rated tax treatment.

Archived

- Grants to vendors (other than designated entities) are zero-rated in terms of sections 8(5A) and 11(2)(t). Low cost housing subsidy payments are now zero-rated in terms of section 8(23) and 11(2)(s).
- An appropriation in terms of the DOR Act such as a "Municipal Infrastructure Grant" or "equitable share" also qualifies as a zero-rated "grant", unless the recipient is a "designated entity".
- A "grant" includes subsidy payments by local authorities to private vendors (other than designated entities), as well as subsidies/transfers of funds between public and local authorities.
- A "grant" excludes procurement and other methods of acquiring goods and services by constitutional institutions, public and local authorities (i.e. the payment must not constitute consideration paid in respect of the actual supply of goods or services in terms of section 7(1)(a) to the person making the payment).
- Section 8(5) was amended so that it now only applies to a "designated entity". Payments made to designated entities, which are in respect of taxable supplies made by such entities, generally attract VAT at the standard rate.
- The only instances where designated entities may zero rate payments from constitutional institutions or public or local authorities are where:
  - the amount is a grant for training employees (SETA grants received), or
  - the recipient is a "welfare organisation" and the funds are for the purposes of carrying out "welfare activities".

Archived

9. EFFECTIVE DATE

The amendments dealt with in this note are contained mainly in the Revenue Laws Amendment Act, 2003 (Act No. 45 of 2003) and the Revenue Laws Amendment Act, 2004 (Act No. 32 of 2004) which were promulgated on 22 December 2003 and 24 January 2005 respectively. The effective date is 1 April 2005 in terms of Presidential Proclamation No. R.14, 2005 (Government Gazette No. 27427 dated 1 April 2005).

The reason for not bringing the amendments into operation earlier is that the introduction of the amendments had to be co-ordinated with the government budget cycle so that the necessary adjustments could be made on the expenditure side of the budget.

Further amendments can also be found in the following Acts:

- the Taxation Laws Amendment Act, 2005 (Act No.9 of 2005);
- the Taxation Laws Second Amendment Act, 2005 (Act No.10 of 2005);
- the Revenue Laws Amendment Act (Act No 31 of 2005)

which came into effect on 19 July 2005, 13 July 2005 and 1 February 2006 respectively (unless otherwise indicated in the Act concerned).

The Second Small Business Tax Amnesty and Amendment of Taxation Laws Act (Act No 10 of 2006) which came into effect 25 July 2006 also contains certain amendments in respect of the secrecy provisions relating to certain public entities and municipalities. (All the relevant changes with regard to municipalities came into effect on 1 July 2006 unless otherwise indicated in that Act).

10. FURTHER AMENDMENTS

At the time of drafting this document, proposed changes to the law were included in Revenue Laws Amendment Bill (No. 33 of 2006) and the Revenue Laws Second Amendment Bill (No. 34 of 2006). The Amendment Acts which contained those proposals were promulgated on 7 February 2007 and are discussed briefly in paragraphs 10.1 and 10.2 below.

10.1 Revenue Laws Amendment Act (No. 20 of 2006)

- *Compensation for diseased animals* - compensation paid by a public authority in terms of section 19 of the Animal Diseases Act, 1984 (Act No. 35 of 1984) for the supply of a ‘controlled animal or thing’ as defined in that Act to that public authority is subject to the zero rate.

- *Foreign donor funded projects* – the services which are deemed to be supplied in terms of section 8(5B) are zero-rated in terms of section 11(2)(q), but limited to the extent that the zero-rating has been approved by the Minister after consultation with the Minister of Foreign Affairs.

Archived

10.2 Revenue Laws Second Amendment Act (No. 21 of 2006)

- *Payments basis of accounting* –section 15 of the Act was amended to allow the following entities to use the payments basis of accounting:
  - any water board or regional water services listed in Schedule 3B of the Public Finance Management Act, 1999 (Act No. 1 of 1999);
  - a regional electricity distributor (RED) as defined in section 1 of the Income Tax Act; and
  - a 'municipal entity' as defined in section 1 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000), where that municipal entity supplies electricity, gas, water or drainage, removal or disposal of sewage or garbage.

Legal and Policy Division
SOUTH AFRICAN REVENUE SERVICE

Archived

TREASURY REGULATIONS FOR DEPARTMENTS, CONSTITUTIONAL INSTITUTIONS AND TRADING ENTITIES

[CHAPTER 8 (EXPENDITURE MANAGEMENT)]

A. Per Government Gazette no. 22219 dated 9 April 2001.

"8.4 Transfer payments (excluding Division of Revenue grants and other allocations to municipalities) *[Section 38 (1) (j) of the PFMA]*
8.4.1 An accounting officer must maintain appropriate measures to ensure that transfer payments to entities are applied for their intended purposes. Such measures may include—
- *(a) regular reporting procedures;*
- *(b) internal and external audit requirements and, where appropriate, submission of audited statements;*
- *(c) regular monitoring procedures;*
- *(d) scheduled or unscheduled inspection visits or reviews of performance; and*
- *(e) any other control measures deemed necessary.*

8.4.2 An accounting officer may withhold a transfer payment to an entity if he or she is satisfied that—
- *(a) conditions attached to the transfer payment have not been complied with;*
- *(b) financial assistance is no longer required;*
- *(c) the agreed objectives have not been attained; and*
- *(d) the transfer payment does not provide value for money in relation to its purpose or objectives.*

8.4.3 Treasury Regulations 8.4.1 and 8.4.2 do not apply to transfers to other countries, international bodies and other bodies in terms of economic and financial agreements.
8.4.4 Transfers to other countries, international bodies and other bodies in terms of economic and financial agreements are exempt from the written assurance, as required by section 38 (1) (j) of the Act."

B. Per Government Gazette no 23463 dated 25 May 2002

"8.4 Transfer payments (excluding Division of Revenue grants and other allocations to municipalities) *[Section 38(1)(j) of the PFMA]*
8.4.1 An accounting officer must maintain appropriate measures to ensure that transfer payments to entities are applied for their intended purposes. Such measures may include-
- *(a) regular reporting procedures;*
- *(b) internal and external audit requirements and, where appropriate, submission of audited statements;*
- *(c) regular monitoring procedures;*
- *(d) scheduled or unscheduled inspection visits or reviews of performance; and*
- *(e) any other control measures deemed necessary.*

8.4.2 An accounting officer may withhold a transfer payment to an entity if he or she is satisfied that-
- *(a) conditions attached to the transfer payment have not been complied with;*
- *(b) financial assistance is no longer required;*
- *(c) the agreed objectives have not been attained; and*
- *(d) the transfer payment does not provide value for money in relation to its purpose or objectives.*

8.4.3 Treasury Regulations 8.4.1 and 8.4.2 do not apply to transfers to other countries, international bodies and other bodies in terms of economic and financial agreements.
8.4.4 Transfers to other countries, international bodies and other bodies in terms of economic and financial agreements are exempt from the written assurance, as required by section 38(1)(j) of the Act".

Archived

C. Per Government Gazette No. 27388 dated 15 March 2005.

"8.4 Transfers and subsidies (excluding Division of Revenue grants and other allocations to municipalities) *[Section 38(1)(j) of the PFMA]*

8.4.1 An accounting officer must maintain appropriate measures to ensure that transfers and subsidies to entities are applied for their intended purposes. Such measures may include-

(a) regular reporting procedures;
(b) internal and external audit requirements and, where appropriate, submission of audited statements;
(c) regular monitoring procedures;
(d) scheduled or unscheduled inspection visits or reviews of performance; and
(e) any other control measures deemed necessary.

8.4.2 An accounting officer may withhold transfers and subsidies to an entity if he or she is satisfied that-

(a) conditions attached to the transfer and subsidy have not been complied with;
(b) financial assistance is no longer required;
(c) the agreed objectives have not been attained; and
(d) the transfer and subsidy does not provide value for money in relation to its purpose or objectives.

8.4.3 Treasury Regulations 8.4.1 and 8.4.2 do not apply to transfers and subsidies to other countries, international bodies, to other bodies in terms of economic and financial agreements and to levies and taxes imposed by other levels of government and which are classified as transfers and subsidies in the budgets of departments. Transfers and subsidies in respect of levies and taxes imposed by other levels and entities of government are governed by section 38(1)(e) of the Act.

8.4.4 Transfers and subsidies to other countries, international bodies, other bodies in terms of economic and financial agreements and transfers and subsidies to other levels and entities of government for purposes of paying levies and taxes imposed by legislation are exempt from the written assurance, as required by section 38(1)(j) of the Act."

Archived

SECTION 38(1)(j) OF THE PFMA

"38. General responsibilities of accounting officers.—(1) The accounting officer for a department, trading entity or constitutional institution—

…

(j) before transferring any funds (other than grants in terms of the annual Division of Revenue Act or to a constitutional institution) to an entity within or outside government, must obtain a written assurance from the entity that that entity implements effective, efficient and transparent financial management and internal control systems, or, if such written assurance is not or cannot be given, render the transfer of the funds subject to conditions and remedial measures requiring the entity to establish and implement effective, efficient and transparent financial management and internal control systems;"

SCHEDULE 1

DEPARTMENTS AND HEADS OF DEPARTMENT

Column 1	Column 2
Department of Agriculture	Director-General: Agriculture
Department of Arts and Culture	Director-General: Arts and Culture
Department of Communications	Director-General: Communications
Department of Correctional Services	Commissioner: Correctional Services
Department of Defence	Secretary for Defence
Department of Education	Director-General: Education
Department of Environmental Affairs and Tourism	Director-General: Environmental Affairs and Tourism
Department of Foreign Affairs	Director-General: Foreign Affairs
Department of Government Communications and Information System	Director-General: Government Communications and Information System
Department of Health	Director-General: Health
Department of Home Affairs	Director-General: Home Affairs
Department of Housing	Director-General: Housing
Department of Justice	Director-General: Justice
Department of Labour	Director-General: Labour
Department of Land Affairs	Director-General: Land Affairs
Department of Minerals and Energy	Director-General: Minerals and Energy
Department of Provincial and Local Government	Director-General: Provincial and Local Government
Department of Public Enterprises	Director-General: Public Enterprises
Department of Public Service and Administration	Director-General: Public Service and Administration
Department of Public Works	Director-General: Public Works
Department of Safety and Security	National Commissioner: South African Police Service
Department of Safety and Security	National Commissioner: South African Police Service
Department of Science and Technology	Director-General: Science and Technology
Department of Social Development	Director-General: Social Development
Department of Trade and Industry	Director-General: Trade and Industry
Department of Transport	Director-General: Transport
Department of Water Affairs and Forestry	Director-General: Water Affairs and Forestry
National Intelligence Agency	Director-General: National Intelligence Agency
National Treasury	Director-General: National Treasury
Office of the Public Service Commission	Director-General: Office of the Public Service Commission
The Presidency	Director-General: The Presidency
Provincial Administration: Eastern Cape	Director-General: Office of the Premier of Eastern Cape
Provincial Administration: Free State	Director-General: Office of the Premier of Free State
Provincial Administration: Gauteng	Director-General: Office of the Premier of Gauteng
Provincial Administration: KwaZulu-Natal	Director-General: Office of the Premier of KwaZulu-Natal
Provincial Administration: Mpumalanga	Director-General: Office of the Premier of Mpumalanga
Provincial Administration: Northern Cape	Director-General: Office of the Premier of Northern Cape
Provincial Administration: Northern Province	Director-General: Office of the Premier of Northern Province
Provincial Administration: North West	Director-General: Office of the Premier of North West
Provincial Administration: Western Cape	Director-General: Office of the Premier of Western Cape
South African Management and Development Institute	Director-General: South African Management and Development Institute
South African Secret Service	Director-General: South African Secret Service
Sport and Recreation South Africa	Director-General: Sport and Recreation South Africa
Statistics South Africa	Statistician-General: Statistics South Africa

Archived

SCHEDULE 2

PROVINCIAL DEPARTMENTS AND HEADS OF PROVINCIAL DEPARTMENTS

Column 1	***Column 2***
Eastern Cape	
Department of Agriculture	Head: Agriculture
Department of Economic Affairs, Environment and Tourism	Head: Economic Affairs, Environment and Tourism
Department of Education	Head: Education
Department of Health	Head: Health
Department of Housing [Previously Department of Housing, Local Government and Traditional Affairs" substituted by Proclamation No. R. 11, 2007 dated 18 May 2007]	Head: Housing [Previously Head: Housing, Local Government and Traditional Affairs, substituted by Proclamation No. R. 11, 2007 dated 18 May 2007]
Department of Public Works	Head: Public Works
Department of Roads and Transport	Head: Roads and Transport
Department of Safety and Liaison	Head: Safety and Liaison
Department of Social Development	Head: Social Development
Department of Sport, Recreation, Arts, and Culture	Head: Sport, Recreation, Arts, and Culture
Provincial Treasury	Head: Provincial Treasury
Free State	
Department of Agriculture	Head: Agriculture
Department of Education	Head: Education
Department of Health	Head: Health
Department of Local Government and Housing	Head: Local Government and Housing
Department of Public Works, Roads and Transport	Head: Public Works, Roads and Transport
Department of Public Safety, Security and Liaison	Head: Public Safety, Security and Liaison
Department of Social Development	Head: Social Development
Department of Sport, Arts and Culture [previously "Department of Sport, Arts, Culture, Science and Technology", substituted by R.18(P) of 2006.]	Head: Sport, Arts and Culture [previously "Head: Sport, Arts, Culture, Science and Technology", substituted by R.18(P) of 2006.]
Department of Tourism, Environmental and Economic Affairs	Head: Tourism, Environmental and Economic Affairs
Free State Provincial Treasury	Head: Free State Provincial Treasury
Gauteng	
Department of Agriculture, Conservation and Environment	Head: Agriculture, Conservation and Environment
Department of Community Safety	Head: Community Safety
Department of Economic Development ["Department of Economic Development" inserted by R.18(P) of 2006.]	Head: Economic Development ["Department of Economic Development" inserted by R.18(P) of 2006.]
Department of Education	Head: Education
. . . . . . ["Department of Finance and Economic Affairs" deleted by R.18(P) of 2006.]	. . . . . . ["Head: Finance and Economic Affairs" deleted by R.18(P) of 2006.]
Department of Health	Head: Health
Department of Housing	Head: Housing
Department of Local Government	Head: Local Government
Department of Public Transport, Roads and Works	Head: Public Transport, Roads and Works
Department of Social Development	Head: Social Development
Department of Sports, Arts, Culture and Recreation	Head: Sports, Arts, Culture and Recreation
Gauteng Shared Services	Head: Gauteng Shared Services
Gauteng Treasury ["Gauteng Treasury" inserted by R.18(P) of 2006.]	Head: Gauteng Treasury ["Head: Gauteng Treasury" inserted by R.18(P) of 2006.]

Archived

SCHEDULE 2 (continued)

Column 1	Column 2
KwaZulu-Natal	
Department of Agriculture	Head: Agriculture
Department of Arts, Culture and Tourism	Head: Arts, Culture and Tourism
Department of Community Safety and Liaison	Head: Community Safety and Liaison
Department of Economic Development	Head: Economic Development
Department of Education	Head: Education
Department of Health	Head: Health
Department of Housing	Head: Housing
Department of Local Government and Traditional Affairs [inserted by R.33(P) of 2005.]	Head: Local Government and Traditional Affairs [inserted by R.33(P) of 2005.]
Department of the Royal Household	Head: Royal Household
Department of Sports and Recreation	Head: Sports and Recreation
. . . . . . [“Department of Traditional and Local Government Affairs” deleted by R.33(P) of 2005.]	. . . . . . [“Head: Traditional and Local Government Affairs” deleted by R.33(P) of 2005.]
Department of Transport	Head: Transport
Department of Welfare and Population Development	Head: Welfare and Population Development
Department of Works	Head: Works
Provincial Treasury	Head: Provincial Treasury
Mpumalanga	
Department of Agriculture and Land Administration	Head: Agriculture and Land Administration
Department of Culture, Sport and Recreation	Head: Culture, Sport and Recreation
Department of Economic Development and Planning	Head: Economic Development and Planning
Department of Education	Head: Education
Department of Finance	Head: Finance
Department of Health and Social Services	Head: Health and Social Services
Department of Local Government and Housing	Head: Local Government and Housing
Department of Public Works	Head: Public Works
Department of Roads and Transport	Head: Roads and Transport
Department of Safety and Security	Head: Safety and Security
Northern Cape	
Department of Agriculture and Land Reform	Head: Agriculture and Land Reform
Department of Economic Affairs	Head: Economic Affairs
Department of Education	Head: Education
Department of Health	Head: Health
Department of Housing and Local Government	Head: Housing and Local Government
Department of Safety and Liaison	Head: Safety and Liaison
Department of Social Services and Population Development	Head: Social Services and Population Development
Department of Sport, Arts and Culture	Head: Sport, Arts and Culture
Department of Tourism, Environment and Conservation	Head: Tourism, Environment and Conservation
Department of Transport, Roads and Public Works	Head: Transport, Roads and Public Works
Provincial Treasury	Head: Provincial Treasury
Northern Province	
Department of Agriculture	Head: Agriculture
Department of Education	Head: Education
Department of Finance and Economic Development	Head: Finance and Economic Development
Department of Health and Welfare	Head: Health and Welfare
Department of Local Government and Housing	Head: Local Government and Housing
Department of Public Works	Head: Public Works
Department of Safety, Security and Liaison	Head: Safety, Security and Liaison
Department of Sport, Arts and Culture	Head: Sport, Arts and Culture
Department of Transport	Head: Transport

Archived

SCHEDULE 2 (continued)

Column 1	***Column 2***
North West	
Department of Agriculture, Conservation and Environment [previously "Department of Agriculture, Conservation, Environment and Tourism", substituted by R.64(P) of 2005.]	Head: Agriculture, Conservation and Environment [previously "Head: Agriculture, Conservation and Environment and Tourism" substituted by R.64(P) of 2005.]
Department of Developmental Local Government and Housing	Head: Developmental Local Government and Housing
Department of Economic Development and Tourism [inserted by R.64(P) of 2005.]	Head: Economic Development and Tourism [inserted by R.64(P) of 2005.]
Department of Education	Head: Education
Department of Finance [previously "Department of Finance and Economic Development" substituted by R.64(P) of 2005.]	Head: Finance [previously "Head: Finance and Economic Development" substituted by R.64(P) of 2005.]
Department of Health	Head: Health
Department of Public Works	Head: Public Works
. . . . . . ["Department of Safety and Liaison" deleted by R.64(P) of 2005.]	. . . . . . ["Head: Safety and Liaison" deleted by R.64(P) of 2005.]
Department of Social Development	Head: Social Development
Department of Sports, Arts and Culture	Head: Sports, Arts and Culture
Department of Transport, Roads and Community Safety [previously "Department of Transport and Roads" substituted by R.64(P) of 2005.]	Head: Transport, Roads and Community Safety [previously "Head: Transport and Roads" substituted by R.64(P) of 2005.]
Western Cape	
Department of Agriculture	Head: Agriculture
Department of Community Safety	Head: Community Safety
Department of Cultural Affairs and Sport	Head: Cultural Affairs and Sport
Department of Economic Development and Tourism	Head: Economic Development and Tourism
Department of Education	Head: Education
Department of Environmental Affairs and Development Planning	Head: Environmental Affairs and Development Planning
Department of Finance	Head: Finance
Department of Health	Head: Health
Department of Housing	Head: Housing
Department of Local Government	Head: Local Government
Department of Social Development [previously "Department of Social Services and Poverty Alleviation, substituted by R.26(P) of 2006.]	Head: Social Development [previously "Head: Social Services and Poverty Alleviation, substituted by R.26(P) of 2006.]
Department Transport and Public Works	Head: Transport and Public Works

Archived

SCHEDULE 3

ORGANISATIONAL COMPONENTS AND HEADS THEREOF

Column 1	**Column 2**
Independent Complaints Directorate	Executive Director: Independent Complaints Directorate
Inspectorate for Social Assistance [inserted by R.39(P) of 2006.]	Executive Director: Inspectorate for Social Assistance [inserted by R.39(P) of 2006.]
South African National Academy of Intelligence	Chief Executive Officer: South African National Academy of Intelligence

PUBLIC ENTITIES IN TERMS OF SCHEDULES 1, 2 & 3 OF THE PFMA

NOTE:
This is the PFMA list as at **20 July 2007**. The list changes from time to time as new public entities are listed, classified, re-classified, amalgamated or delisted.

Schedule 1 Constitutional Institutions	Schedule 2 Major Public Entities
1) The Commission on Gender Equality 2) The Commission for the Promotion and Protection of the Rights of Cultural, Religious and Linguistic Communities 3) The Financial and Fiscal Commission 4) The Human Rights Commission 5) The Independent Communications Authority of South Africa 6) The Independent Electoral Commission 7) The Municipal Demarcation Board 8) The Pan South African Language Board 9) The Public Protector	1) Air Traffic and Navigation Services Company 2) Airports Company (ACSA) 3) Alexkor Limited 4) Armaments Corporation of South Africa 5) CEF (Pty) Ltd (formerly Central Energy Fund) 6) DENEL 7) Development Bank of Southern Africa 8) ESKOM 9) Independent Development Trust 10) Industrial Development Corporation of South Africa Limited 11) Land and Agricultural Bank of South Africa 12) SA Broadcasting Corporation Limited 13) SA Forestry Company Limited 14) SA Nuclear Energy Corporation 15) SA Post Office Limited 16) Telkom SA Limited 17) Trans-Caledon Tunnel Authority 18) Transnet Limited 19) Any subsidiary or entity under the ownership control of the above public entities.

Archived

Schedule 3
Other Public Entities
Part A: National Public Entities

1) Accounting Standards Board
2) Africa Institute of South Africa, Pretoria
3) African Renaissance and International Cooperation Fund
4) Afrikaanse Taalmuseum, Paarl
5) Agricultural Research Council
6) AGRISETA
7) Artscape
8) Banking Sector Education and Training Authority
9) Boxing South Africa
10) Business Arts of South Africa, Johannesburg
11) Castle Control Board
12) Chemical Industries Education and Training Authority
13) Clothing, Textiles, Footwear and Leather Sector Education and Training Authority
14) Commission for Conciliation, Mediation & Arbitration
15) Compensation Fund, including Reserve Fund
16) Competition Commission
17) Competition Tribunal
18) Construction Education and Training Authority
19) Construction Industry Development Board
20) Council for the Built Environment (CBE)
21) Council for Geoscience
22) Council for Medical Schemes
23) Council on Higher Education
24) Cross-Border Road Transport Agency
25) Diplomacy, Intelligence, Defence and Trade and Industry Sector Education and Training Authority
26) Education and Labour Relations Council
27) Education, Training and Development Practices Sector Education and Training Authority
28) Electricity Distribution Industry Holdings (Pty) Ltd
29) Energy Sector Education and Training Authority
30) Estate Agency Affairs Board
31) Film and Publication Board
32) Financial and Accounting Services Training Authority
33) Financial Intelligence Centre
34) Financial Services Board
35) Food and Beverages Manufacturing Industry Sector Education and Training Authority
36) Forest Industries Sector Education and Training Authority
37) Freedom Park Trust
38) Godisa Trust
39) Greater St. Lucia Wetland Park Authority
40) Health and Welfare Sector Education and Training Authority
41) Human Sciences Research Council (HSRC)
42) Independent Regulatory Board for Auditors
43) Information Systems, Electronics and Telecommunications Technologies Training Authority
44) Ingonyama Trust Board
45) Insurance Sector Education and Training Authority
46) International Marketing Council (IMC)
47) International Trade Administration Commission (ITAC)
48) Iziko Museums of Cape Town
49) Legal Aid Board
50) Local Government, Water and Related Services Sector Education and Training Authority
51) Luthuli Museum
52) Manufacturing Advisory Council
53) Manufacturing, Engineering and Related Services Education and Training Authority
54) Marine Living Resources Fund
55) Market Theatre Foundation
56) Media, Advertising, Publishing, Printing and Packaging Training Authority
57) Media Development and Diversity Agency
58) Mine Health and Safety Council
59) Mining Qualifications Authority
60) Municipal Infrastructure Investment Unit
61) Natal Museum, Pietermaritzburg
62) National Agricultural Marketing Council
63) National Arts Council
64) National Credit Regulator: Schedule 3A national public entity-
65) National Consumer Tribunal: Schedule 3A national public entity.
66) National Development Agency
67) National Economic, Development and Labour Council
68) National Electronic Media Institute of SA
69) National Empowerment Fund
70) National Energy Regulator
71) National Film and Video Foundation
72) National Gambling Board of South Africa
73) National Health Laboratory Service
74) National Heritage Council (NHC)
75) National Home Builders Registration Council – NHBRC

Archived

Schedule 3
Other Public Entities
Part A: National Public Entities (continued)

76) National Housing Finance Corporation
77) National Library, Pretoria/Cape Town
78) National Lotteries Board
79) National Museum, Bloemfontein
80) National Nuclear Regulator
81) National Productivity Institute
82) National Research Foundation
83) National Student Financial Aid Scheme
84) National Urban Reconstruction and Housing Agency – NURCHA
85) National Youth Commission
86) Nelson Mandela Museum, Umtata
87) Northern Flagship Institution, Pretoria
88) Performing Arts Council of the Free State
89) Perishable Products Export Control Board
90) Police, Private Security, Legal and Correctional Services Training Authority
91) Public Sector Education and Training Authority
92) Railway Safety Regulator
93) Road Accident Fund
94) Road Traffic Management Corporation
95) Robben Island Museum, Cape Town
96) Rural Housing Loan Fund
97) SA Blind Workers Organisation, Johannesburg
98) SA Civil Aviation Authority
99) SA Council for Educators
100)SA Diamond and Precious Metals Regulator
101)SA Heritage Resources Agency
102) SA Institute for Drug-free Sport
103) SA Library for the Blind, Grahamstown
104) SA Local Government Association (SALGA)
105). SA Maritime Safety Authority
106) SA Medical Research Council
107) SA National Accreditation System
108)South African National Biodiversity Institute (SANBI) (formerly National Botanical Institute (NBI)
109) SA National Parks
110) SA National Roads Agency
111)SA Qualifications Authority
112)SA Quality Institute
113)SA Revenue Service
114)SA Social Assistance Agency
115) SA Sport Commission
116) SA Tourism Board
117) SA Weather Service
118) Servcon
119) Services Sector Education and Training Authority
120) Small Enterprise Development Agency
121)Social Housing Foundation
122) Special Investigation Unit
123) State Information Technology Agency
124) State Theatre, Pretoria
125) The National English Literary Museum, Grahamstown
126) The Playhouse Company, Durban
127) Thubelisha Homes
128) Tourism and Hospitality Education and Training Authority
129) Trade and Investment South Africa
130) Transport Education and Training Authority
131) uMalusi Council for Quality Assurance in General and Further Education and Training
132) Unemployment Insurance Fund
133) Universal Service Agency
134) Universal Service Fund
135) Urban Transport Fund
136)Voortrekker Museum, Pietermaritzburg
137)War Museum of the Boer Republics, Bloemfontein
138) Water Research Commission
139)Wholesale and Retail Sector Education and Training Authority
140) William Humphreys Art Gallery
141) Windybrow Centre
142)Any subsidiary or entity under the ownership control of the above public entities

Archived

Schedule 3
Other Public Entities

Part B: National Government Business Enterprises

1) Albany Coast Water Board
2) Amatola Water Board
3) Aventura
4) Bala Farms (Pty) Ltd
5) Bloem Water
6) Botshelo Water
7) Bushbuckridge Water Board
8) Council for Mineral Technology (Mintek)
9) Council for Scientific and Industrial Research (CSIR)
10) Export Credit Insurance Corporation of South Africa Limited
11) Ikangala Water
12) Inala Farms (Pty) Ltd
13) Khula Enterprises
14) Lepelle Northern Water
15) Magalies Water
16) Mhlathuze Water
17) Namakwa Water
18) Ncera Farms (Pty) Ltd
19) Onderstepoort Biological Products
20) Overberg Water
21) Pelladrift Water Board
22) Public Investment Corporation Limited (formerly the Public Investment Commissioners –Sch. 3A)
23) Rand Water
24) SA Bureau of Standards (SABS)
25) SA Rail Commuter Corporation Limited
26) Sasria
27) Sedibeng Water
28) Sentech
29) State Diamond Trader
30) Umgeni Water
31) Umsobomvu Youth Fund
32) Any subsidiary or entity under the ownership control of the above public entities

Part C: Provincial Public Entities

Eastern Cape:

1) Centre for Investment and Marketing in the Eastern Cape
2) Eastern Cape Appropriate Technology Unit
3) Eastern Cape Arts Council
4) Eastern Cape Consumer Affairs Court
5) Eastern Cape Gambling and Betting Board
6) Eastern Cape Liquor Board
7) Eastern Cape Local Road Transport Board
8) Eastern Cape Museums
9) Eastern Cape Parks Board
10) Eastern Cape Provincial Housing Board
11) Eastern Cape Provincially Aided Libraries
12) Eastern Cape Regional Authorities
13) Eastern Cape Rural Finance Corporation Limited
14) Eastern Cape Socio-Economic Consultative Council
15) Eastern Cape Tourism Board
16) Eastern Cape Youth Commission
17) Eastern Region Entrepreneurial Support Centre

Northern Cape:

1) Northern Cape Tourism Authority

KwaZulu-Natal:

1) Amafa Akwazulu Natali
2) Ezemvelo Kwazulu-Natal Wildlife
3) Kwa Zulu-Natal Agricultural Development trust
4) Kwa Zulu-Natal Gambling Board
5) Kwa Zulu-Natal House of Traditional Leaders
6) Kwa Zulu-Natal Taxi Council
7) Kwa Zulu-Natal Tourism Authority
8) Kwa Zulu-Natal Povincial Planning and Development Commission
9) Natal Sharks Board
10) UMsekeli Municipal Support Services

Mpumalanga:

1) Mpumalanga Gambling Board
2) Mpumalanga Gaming Board
3) Mpumalanga Housing Board
4) Mpumalanga Investment Initiative
5) Mpumalanga Parks Board
6) Mpumalanga Regional Training Trust
7) Mpumalanga Tourism Authority

Archived

Schedule 3
Other Public Entities

Part C: Provincial Public Entities (continued)

Free State:

1) Free State Council for Citizenship, Education and Conflict Resolution
2) Free State Gambling and Racing Board (formerly Free State Gambling and Gaming Board)
3) Free State Youth Commission
4) Phakisa Major Sport and Development Corporation

Gauteng:

1) Blue IQ Investment Holdings (Pty) Ltd
2) Gauteng Economic Development Agency
3) Gauteng Gambling Board
4) Gauteng Partnership Fund (GPF)
5) Gauteng Tourism Authority

Western Cape:

1) Commissioner for the Environment
2) WC Cultural Commission
3) WC Gambling and Racing Board
4) WC Investment and Trade Promotion Agency
5) WC Language Committee
6) WC Liquor Board
7) WC Nature Conservation Board
8) WC Provincial Development Council
9) Western Cape Provincial Youth Commission
10) WC Tourism Board

Limpopo (Northern Province):

1) Limpopo Development Enterprise
2) Limpopo Gambling Board
3) Limpopo Tourism and Parks Board
4) Northern Province Appeal Tribunals
5) Northern Province Development Tribunals
6) Northern Province Housing Board
7) Northern Province Liquor Board
8) Northern Province Local Business Centres
9) Northern Province Panel of Mediators
10) Northern Province Planning Commission
11) Northern Province Roads Agency
12) Trade and Investment Limpopo

North West:

1) Invest North West
2) Mmabana Arts, Culture and Sport Foundation
3) NW Agricultural Services Corporation
4) NW Communication Service
5) NW Eastern Region Entrepreneurial Support Centre
6) NW Gambling Board
7) NW Housing Corporation
8) NW Parks and Tourism Board
9) NW Provincial Aids Council
10) NW Provincial Arts and Culture Council
11) NW Youth Development Trust

Any subsidiary or entity under the ownership control of the above public entities.

Part D: Provincial Government Business Enterprises

1) Casidra (Pty) Ltd
2) Cowslip Investments (Pty) Ltd
3) East London Industrial Development Zone Corporation (re-classified 20/09/2005 from Sch. 3C)
4) Eastern Cape Development Corporation
5) Free State Development Corporation
6) Gateway Airport Authority Limited
7) Ithala Development Finance Corporation
8) Mayibuye Transport Corporation
9) Mjindi Farming (Pty) Ltd
10) Mpendle-Ntambanana Agricultural Company (Pty) Ltd
11) Mpumalanga Agricultural Development Corporation
12) Mpumalanga Economic Empowerment Corporation
13) Mpumalanga Housing Finance Company
14) Northern Province Development Corporation
15) NW Development Corporation
16) Any subsidiary or entity under the ownership control of the above public entities

Archived

EXAMPLE 1 : The Dept. of Housing (DOH) pays a low cost housing developer for developing houses for the poor. The applicant also has to pay an additional amount for extra work performed.

Before 1 April 2005

DOH enters into a contract with and pays a property developer R 1 700 000 which constitutes the housing subsidy of R 17 000 each for 100 indigent persons in order to develop low cost housing units. The payment will constitute a transfer payment which will be zero-rated in terms of section 8(5) and 11(2)(p) of the Act. If the completed units are supplied by the developer to the recipients for R 25 000 each, the balance of the consideration attracts VAT at the standard rate. i.e. Only R 1 700 000 of the R 2 500 000 (R 25 000 x 100) received for the houses supplied to the applicants may be zero-rated.

The output tax to be declared by the developer in this example would therefore be calculated as follows:-

	Consideration	**VAT**
Transfer payment	R 1 700 000 at 0%	R nil
Payment by recipients (R 2 500 000 – R 1 700 000)	R 800 000 x 14/114	R 98 245.61

The builder's VAT 201 return (Part A – output tax) for the period would be completed like this:-

A. CALCULATION OF OUTPUT TAX		RANDS ONLY				**R**	**c**
Supply of goods and/or services by you		CONSIDERATION (INCLUDING VAT)				VAT	
Standard rate (excluding capital goods and/or services and accommodation)	1	800 000	•	X r/100+r	4	98 245	61
Standard rate (only capital goods and/or services)	1A	nil	•	X r/100+r	4A	nil	
Zero rate	2	1 700 000	•				
Exempt and non-supplies	3	nil	•				
TAXABLE AMOUNT (EXCL VAT)		TAXABLE VALUE (EXCL VAT)					
Exceeding 28 days — 5: nil • X 60%	6	nil	•				
Not exceeding 28 days	7	nil	•			VAT	
TOTAL	8	nil	•	X r/100	9	nil	
Adjustments		CONSIDERATION (INCLUDING VAT)				VAT	
Change in use and export of second-hand goods	10	nil	•	X r/100+r	11	nil	
Other					12	nil	
TOTAL A: TOTAL OUTPUT TAX (4 + 4A + 9 + 11 + 12)					13	98 245	61

After 1 April 2005

There is essentially no difference in the VAT treatment of the supplies concerned, except that the payments will now be zero-rated in terms of sections 8(23) and 11(2)(s) of the Act which cater specifically for housing subsidy payments.

Archived

EXAMPLE 2 : Dept. of Land Affairs (DLA) pays a local authority/municipality an amount of money to transfer a piece of vacant municipal land to a tribe in the area. DLA also makes funds available to the tribe to build a community hall on the land.

Before 1 April 2005

Since the supply of the vacant land will not constitute a taxable supply by the local authority (as the land is not used for "enterprise" purposes), there is no deemed supply by the local authority to DLA. The payment for the land is reflected as exempt income in Block 3 of the local authority's VAT 201 return and not in Block 2. Since the tribe is not a vendor and is not making any taxable supplies, there is also no deemed supply to the DLA on receipt of the funds to build the community hall.

On or after 1 April 2005

The VAT position remains the same as that described above.

EXAMPLE 3 : The Dept. of Housing (DOH) pays a local authority/municipality an amount to develop land for a township and to provide houses for the poor on the township land.

Before 1 April 2005

Since township development is one of the taxable categories of businesses listed in Government Notice No. 2570 – 21 October 1991, the acquisition and supply of the land and the houses would be in the course or furtherance of the local authority's "enterprise". This is provided that the income (including the transfer payment/grant and a reasonable provision for depreciation) would be sufficient to cover the costs of the development. Therefore, in terms of section 8(5), the local authority is deemed to have supplied a taxable service to DOH (public authority). The payment concerned qualifies as a "transfer payment" and will be zero-rated in the hands of the local authority since DOH (public authority) does not actually receive any goods or services in return for the payment. The taxable supply of land and houses is instead made to the successful housing subsidy applicants. Should the local authority be required to report to DOH from time to time on the progress made in respect of the development, this will be regarded as incidental, and will not be regarded as an actual supply of services to DOH as contemplated in section 7(1)(a) of the Act in return for the payment.

If the local authority appoints a contractor to build the houses, the payment by the local authority to the contractor is subject to VAT at the standard rate since it is in respect of an actual supply of goods and/or services to the local authority. The local authority would claim input tax on VAT expenses incurred in supplying the land and houses, as the township development is a taxable activity conducted by that local authority.

It should however be noted that if the local authority is merely receiving and disbursing the payment to the building contractor on behalf of the public authority (i.e. as an agent of the public authority), the payment is zero-rated in the hands of the building contractor and not the local authority. In such a case, the local authority will not reflect the payment at all on their VAT 201 return since it is not in respect of any supplies made by them.

Archived

On or after 1 April 2005
The same as above, except that the payment to the local authority/municipality would constitute a “grant”, and since it is in respect of that local authority/municipality’s taxable supplies, a deemed supply in terms of section 8(5A) arises which qualifies for the zero rate in terms of section 11(2)(t).

It is also possible that section 8(23) and 11(2)(s) may apply in this case if the payments concerned are made in terms of the Housing Subsidy Scheme referred to in section 3(5)(a) of the Housing Act, 1997 (Act No. 107 of 1997).

EXAMPLE 4 : The Dept. of Trade and Industry (DTI) pays an amount of money in terms of the General Export Incentive Scheme (GEIS) to persons who export goods in excess of a certain value per annum from South Africa.

Before 1 April 2005
Since the export of goods is a taxable supply and the goods exported are supplied to persons other than the DTI (i.e. DTI does not receive any goods or services in return for the GEIS payment), the person receiving the payment is deemed to supply a service in terms of section 8(5) to DTI if registered for VAT. As this is a transfer payment, the GEIS payment will be zero-rated in the hands of the recipient (vendor) in terms of section 11(2)(p). There is no VAT implication for recipients who are not vendors.

On or after 1 April 2005
The same as above would apply, except that the payment would constitute a “grant” (and provided that GEIS payments are still made by DTI). Since it is in respect of that vendor’s taxable supplies, a deemed supply in terms of section 8(5A) arises, which qualifies for the zero rate in terms of section 11(2)(t). However, this will not be the case if the recipient is a “designated entity” (in which case it will be taxed at14% in terms of the deemed supply which arises in terms of section 8(5)).

Archived

EXAMPLE 5 : The Dept. of Home Affairs (DHA) pays an amount to the Government Printing Works (GPW) for the printing of I.D. books and passports.

Before 1 April 2005
GPW was notified to register for VAT with effect from the inception of VAT in South Africa. Since DHA is receiving and paying for an actual service from a registered vendor in terms of section 7(1)(a) of the Act, it does not qualify as a transfer payment, nor is there any deemed supply in terms of section 8(5) of the Act.

On or after 1 April 2005
Same as above.

EXAMPLE 6 : The Dept. of Public Works (DPW) pays a building contractor an amount to paint their office premises and to install an air-conditioning system.

Before 1 April 2005

Since DPW is actually receiving goods and services in return for the payment made, the payment does not qualify as a transfer payment. Section 8(5) of the Act does not apply.

On or after 1 April 2005

Same as above.

EXAMPLE 7 : Dept. of Water Affairs and Forestry (DWAF) pays an amount to a local authority/municipality to sink boreholes and provide necessities such as taps, piping and water storage facilities to enable the poor to get access to free water.

Before 1 April 2005

Since DWAF is a public authority and the payment is in respect of the taxable supply of water in terms of para (c)(i) and (iii) of the definition of enterprise by the local authority to certain members of the community, the local authority is deemed to make a supply to DWAF in terms of section 8(5) of the Act. The payment will be a zero-rated transfer payment if it is not appropriated in terms of the DOR Act.

The fact that this service is provided for free to a specific sector of the community does not alter the fact that the supply of water by the local authority is a taxable supply for nil consideration in terms of section 10(23). Furthermore, it does not matter that the funds are expended on capital infrastructure rather than operational costs. As long as (and to the extent that) the capital infrastructure is for taxable supplies, that receipt will be a zero-rated "transfer payment".

Should the local authority commission a contractor to sink the boreholes and erect the water piping infra-structure, it will be entitled to claim input tax in this regard. The contractor will be required to charge VAT at the standard rate (if registered as a vendor).

On or after 1 April 2005

Same as the above, except that the payment constitutes a "grant" and is zero-rated in terms of section 8(5A) read together with section 11(2)(t). A payment of the "equitable share" in terms of the DOR Act will also qualify for the zero rate in terms of these provisions.

Archived

EXAMPLE 8 : A local authority/municipality pays an amount of money to a welfare organisation (vendor) to assist members of the local rural community to acquire land and teach them about sustainable development / growing of crops.

Before 1 April 2005

The welfare organisation will be making taxable supplies to persons other than the local authority, and it will be deemed to make a supply of services to that local authority in terms of section 8(5) of the Act in respect of the payment made. However, as the payment is not made by a public authority, it cannot be a "transfer payment", and hence it cannot be zero-rated in terms of section 11(2)(p) of the Act. The amount received does not constitute an "unconditional gift" since the funds are directly linked to the condition that they perform certain (taxable) services. The payment does however qualify to be zero-rated in terms of section 11(2)(n) of the Act as the recipient is a "welfare organisation" and the payment is for the carrying on of a welfare activity.

On or after 1 April 2005

Same as the above, except that a welfare organisation is regarded as a "designated entity". The payment also constitutes a "grant" and is zero-rated in terms of section 8(5) read together with section 11(2)(n) (as amended).

EXAMPLE 9 : National Treasury is instructed by Parliament to make available emergency funds to be paid to certain farmers in the Free State and Northern Cape regions as drought subsidies to replace damaged / lost standing crops and livestock. Payments are made available via the Dept. of Land Affairs (DLA) on application.

Before 1 April 2005

Any farmer (vendor) who applies for and receives the subsidy (grant-in-aid) will be deemed in terms of section 8(5) to make a supply to DLA, since the goods lost/damaged were used for taxable supplies made by the farmers and the DLA does not receive any goods or services in return for the subsidy payment. As the subsidy is a "transfer payment", it will qualify for zero-rating in the hands of the farmer (vendor). There is no VAT implication for recipients who are not vendors.

On or after 1 April 2005

Same as the above, except that the payment constitutes a "grant" and is zero-rated in terms of section 8(5A) read together with section 11(2)(t) (provided that the farming enterprise is not a "designated entity").

On or after 7 February2007

Refer to paragraph 10.1 on this note regarding the amendment contained in the Revenue Laws Amendment Act (No. 20 of 2006) which allows the compensation paid by a public authority in terms of section 19 of the Animal Diseases Act, 1984 (Act No. 35 of 1984) for the supply of a 'controlled animal or thing' as defined in that Act to that public authority, to be subject to the zero rate.

Archived

EXAMPLE 10 : Dept. of Transport (DOT) makes a payment to a local authority/municipality to provide public roads and street lighting for the general public in the local authority/municipality's jurisdiction.

Before 1 April 2005

DOT is a public authority, but the supply of public roads and street lighting is usually funded out of the local authority's rates account. Such supplies are therefore not normally considered to be taxable as contemplated in para. (c)(iv) of the definition of "enterprise" and no deemed supply arises between the local authority and DOT in terms of section 8(5) of the Act.

Although the payment is a "transfer payment", it can not be zero-rated in terms of section 11(2)(p) - since this section can only apply if there is a deemed supply in terms of section 8(5) of the Act, being in respect of taxable supplies made by the local authority to "any person".

It follows that the local authority cannot claim any input tax on any goods or services acquired in order to provide the public roads and street lighting to the general public which are acquired with the funds made available for that purpose.

Should the particular local authority concerned charge a flat rate for its services as contemplated in terms of section 8(6)(a) of the Act, all the goods and services provided by that local authority are deemed to be taxable. In such a case, there will be a deemed supply to DOT in terms of section 8(5) of the Act and the payment will be zero-rated in terms of section 11(2)(p) of the Act. The local authority in this instance will be allowed to claim the input tax incurred in providing public roads and street lighting.

On or after 1 April 2005

Same as above, except that a local authority is not a "designated entity". Consequently, with the amendments to section 8(5), this section no longer applies to the local authority. If the grant payment is in respect of the local authority's taxable supplies (e.g. a local authority that charges the "flat rate"), the payment will be zero-rated in terms of section 8(5A) and 11(2)(t). Alternatively, if the payment is in respect of the exempt supplies of the local authority, the payment will be out of scope for VAT purposes.

On or after 1 July 2006

With effect from 1 July 2006, paragraph (c) of the definition of "enterprise" and the definition of "local authority" was deleted. The effect of this is that from 1 July 2006, most of the supplies by a municipality (formerly known as a local authority) became taxable at the standard rate under paragraph (a) of the definition of "enterprise". Therefore, the payment will be regarded as a zero-rated grant in terms of sections 8(5A) and 11(2)(t) as it is received in respect of taxable supplies made by the municipality. It follows that the VAT incurred in providing those facilities may be claimed as input tax.

In addition, it should be noted that if an entity previously qualified as a local authority, that entity would not necessarily qualify as a municipality with effect from 1 July 2006. It follows that from 1 July 2006, the explanations provided in respect of local authorities will apply only to municipalities.

Archived

EXAMPLE 11 : Dept. of Transport (DOT) , as part of its recapitalisation programme to scrap 10 000 old taxis makes a payment (scrapping allowance) of R50 000 to taxi owners for each legally registered old minibus that was scrapped.

Before 1 April 2005

No such payments were made before 1 April 2005

On or after 1 April 2005

DOT is a public authority, but some of the recipients concerned may make both taxable supplies (zero-rated international transport) and exempt supplies (local fare-paying passenger transport) in terms of sections 11(2)(a) and 12(g) of the Act respectively. Each vendor is therefore deemed to make a supply to DOT in terms of section 8(5A) of the Act only to the extent that it is "in respect of" making taxable supplies of transportation to "any person" by that enterprise.

For instance, assume the following facts regarding one of the recipients (vendor):

- Payment of R 50 000 received to buy a new taxi;
- The new taxi costs R 228 000 (inc. VAT) ;
- The vendor makes 70% taxable supplies (international bus transport) and 30% exempt supplies (local taxi transport).

In this example, the vendor will zero rate 70% of the payment (R 35 000) in terms of section 11(2)(t) of the Act as it will constitute a "grant" (declared in block 2 on the VAT 201 return). The balance (R 15 000) is declared in block 3 of the VAT 201 return as non-taxable (out of scope) income. The vendor will be allowed to claim input tax on the expense relating to the new taxi as follows:
R 228 000 x 14/114 x 70% = R 19 600.

However, it should be noted that the most common situation will be that there will be no deemed supply at all, as the payment will in most cases relate exclusively to exempt activities (local passenger transport by road). The payment in most cases will therefore be out of scope for VAT purposes as the recipients will not be vendors.

Where the taxi owner does not make taxable supplies with the taxi, but is registered for VAT in respect of other taxable supplies, e.g. if the taxi owner has a taxi business as well as a building supplies business, the entire receipt (R 50 000) must be declared in block 3 of the VAT 201 return as non-taxable (out of scope) income. The vendor will not be allowed to claim input tax on the expenses incurred in buying the new taxi as the expense is not in the course or furtherance of the building supplies business to which the VAT registration applies.

Archived

EXAMPLE 12 : Calculation of the amount of a reduced assessment contemplated in section 40A(2)

Consider a Schedule 3A public entity which was registered for VAT prior to 1 April 2005 and had the following tax period balances as at 31 March 2005.

Tax period	Balance	Comments/Details
11/04	(R20 000)	Refund per VAT 201 return not yet verified
01/05	R100 000	R50 000 of the amount was in respect of an assessment where a payment for services was treated as a "transfer payment" at 0%. The balance relates to an assessment for the overstatement of input tax for the period.
03/05	R 40 000	Balance of tax, penalty and interest payable as a result of underpayment for the period.
	R120 000	Total liability (payable)

In this example, the vendor may apply for the assessment raised in period 01/05 (January 2005) to be reduced. The provision does not apply to the other tax periods as these balances have arisen as a result of circumstances other those provided for in section 40A(2).

Although the Commissioner **<u>must</u>** reduce the assessment if the conditions in section 40A(2) are met, **<u>this does not mean</u>** that:

- the whole of the original assessment amount of R 50 000 in tax period 01/05 will be reduced to nil; or
- any balance in tax period 01/05 relating to the assessment in respect of the overstatement of input tax for the period will be reduced; or
- that the balance of tax, penalty and interest payable as a result of underpayment for the period 03/05 will be reduced; or
- the refund for the 11/04 tax period will be dealt with separately and refunded before calculating the amount of the reduced assessment.

In the case at hand, once the refund in tax period 11/04 has been verified and released for payment, the credit of R20 000 will be applied to tax period 01/05, leaving a balance of R30 000. Therefore after applying section 40A(2), the balances on the vendor's account will look like this:

Tax period	Balance	Comments
11/04	Nil	R20 000 refund credit transferred to 01/05 tax period
01/05	R50 000	R100 000 less R20 000 credit from 11/04, less R30 000 reduced assessment in terms of s40A(2)
03/05	R40 000	Balance of tax, penalty and interest payable as a result of underpayment for the period
	R90 000	Total liability (payable)

The net result is that the total liability is reduced to R90 000 from R120 000, which is equivalent of the amount of the reduced assessment which the vendor qualifies in terms of section 40A(2) (i.e. R30 000).

Archived

Example 13 : General application of section 40A : Management services supplied by a Schedule 3C PFMA public entity to a Schedule 3A PFMA public entity. Payment for services was incorrectly treated as a zero-rated "transfer payment".

A Schedule 3C PFMA public entity supplies management services to a Schedule 3A PFMA public entity. VAT should have been charged at 14% on the services in terms of section 7(1)(a), but both parties were under the mistaken impression that the payment was a zero-rated "transfer payment."

SARS raised an assessment against the Schedule 3C PFMA entity for an amount of R50 000 in the tax period ending March 2003. Since that date, SARS has recovered R35 000 of that amount by offsetting refunds which were due to that entity. As at 31 March 2005, the Schedule 3C PFMA public entity is required to deregister, but it still has a VAT liability of R15 000 plus penalty and interest thereon.

If the conditions in section 40A(1) and (2) are met, the Commissioner **must** reduce the assessment for the tax period ending March 2003 by R15 000, plus the penalty and interest thereon, if written application is made by the vendor in this regard. The Commissioner may not reduce the assessment for that tax period by reversing the original assessment of R35 000, or any part of the tax, additional tax, penalty or interest which was already recovered, as this will result in the vendor obtaining a refund (which would be in contravention of the proviso to section 40A(2)).

In terms section 40A(3), where an assessment has not been issued in regard to those supplies by 31 March 2005, SARS will not raise an assessment to recover those amounts on or after 1 April 2005. In addition, if the vendor had incorrectly declared output tax at 14% on a "transfer payment", the Commissioner may not refund the output tax, or any amount paid which has been applied to penalty or interest in respect of that outstanding tax. (Section 40A(4)).

Archived

Example 14 : General application of the proviso to section 23(4)

Assume that the Schedule 3C PFMA entity in example 13 above did not register for VAT in respect of the management services which it supplied. In such a case, with effect from 1 April 2005, the Commissioner will not be allowed to retrospectively register the Schedule 3C PFMA entity and make it account for the input tax and output tax for any period prior to 1 April 2005.

With effect from 1 April 2005, the Schedule 3C public entity is regarded as a "public authority" and will therefore not be liable (or allowed) to register for VAT in respect of those management services, unless it is notified to register in terms of paragraph (b)(i) of the definition of "enterprise".