

BINDING CLASS RULING: BCR 053

DATE: 9 June 2016

The guidance contained in this ruling is affected by new legislation. Refer to the repeal of section 12K effective 1 June 2019 and the enactment of the Carbon Tax Act No 15 of 2019.

ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)
: VALUE-ADDED TAX ACT NO. 89 OF 1991 (VAT Act)
SECTION : SECTIONS 12K AND 22 OF THE ACT
: SECTION 11(2)(f) OF THE VAT ACT
SUBJECT : PROGRAMME OF ACTIVITIES OF A CLEAN DEVELOPMENT MECHANISM PROJECT

1. Summary

This ruling determines the tax consequences for the participants in a “Clean Development Mechanism project”, as defined in section 12K of the Act, carried on under a programme of activities modality.

2. Relevant tax laws

This is a binding class ruling issued in accordance with section 78(2) and published in accordance with section 87(2) of the Tax Administration Act No. 28 of 2011.

In this ruling references to sections are to sections of the relevant Act applicable as at 10 February 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of the provisions of –

- the Act –
 - section 12K; and
 - section 22.
- the VAT Act –
 - section 11(2)(f).

3. Class

The class members to whom this ruling will apply will be the participants referred to as CPA owners in 4, registered under a programme of activities.

4. Parties to the proposed transaction

The Applicant: A non-profit association of green energy producers

Project developer: Project developer and sponsor of the registration of the Clean Development Mechanism project (CDM project) with the Executive Board of the United Nations Framework Convention on Climate Change (UNFCCC)

CPA owners: Owners of the CDM projects registered under the programme of activities

5. Description of the proposed transaction

The Applicant is a non-profit organisation established as a collaborative entity of concerned parties interested in raising awareness and facilitating the transition to a climate resilient society within South Africa. The Applicant achieves its objectives by –

- a) creating a platform for voluntary and mandatory carbon disclosure through the Kyoto Protocol Registry; and
- b) providing an independent platform for the hosting of programmes of activities for CDM projects registered under the Kyoto Protocol.

The Applicant acts as the coordinating and management entity for these programmes of activities.

The Applicant and the Project developer who is also a CPA owner have established a CDM project in a programmatic form, contemplated in Article 12 of the Kyoto Protocol.

The Kyoto Protocol is an international agreement under the UNFCCC. Its main feature is that it sets binding targets for 37 industrialised countries for reducing greenhouse gas emissions. In order to reach these targets the UNFCCC allows industrialised countries with emission-reduction commitments to meet part of their commitments by investing in projects in developing countries that reduce greenhouse gas emissions while contributing to the local sustainable development needs of the host country.

The CDM project is registered with the CDM executive board.

The CPA owners intend to produce carbon emission reduction credits under the programme of activities which will be sold to industrialised countries. The sale of carbon emission reduction credits is to be undertaken in terms of emission reduction purchase agreements.

The relationship between the parties will be governed by a programme of activities agreement with the following salient terms:

- a) The programme of activities is to be registered with the CDM executive board together with the first CDM project undertaken by the Project developer. Other potential CPA owners who wish to participate in the programme of activities will be invited to do so upon payment of an inclusion fee and will be added by way of supplemental deeds of inclusion to the programme of activities in the manner provided for by the CDM rules.
- b) The Applicant will –
 - i) act as the coordinating and management entity for the programme of activities;
 - ii) provide the framework and incentives for the CDM project activities to achieve greenhouse gas emission reductions;

- iii) enter into a programme of activities agreement with the CPA owners in order to regulate the rights, duties and obligations of the parties in relation to the development and operation of the programme of activities;
 - iv) act as the point of contact with the CDM executive board on all matters pertaining to the programme of activities; and
 - v) develop a programme of activities design document setting out, amongst others, the eligibility criteria, concept, methodology and management aspects of the programme of activities.
- c) The object of the programme of activities will be to coordinate and implement several voluntary CDM project activities carried on by the CPA owners to generate carbon emission reduction credits for their individual benefit.
- d) The carbon emission reduction credits sales process will be managed by the Applicant and the revenue (carbon revenue) will be collected by it in its capacity as manager of the programme of activities on behalf of the CPA owners .
- e) The Project developer will fund the development phase budget to establish the programme of activities. All CPA owners will pay an annual fee to cover expenses of the programme of activities.
- f) The carbon emission reduction credits generated by the programme of activities will be jointly owned by the Project developer and the other CPA owners on the following basis:
- i) The carbon emission reduction credits of the programme of activities are generated by the carrying on and operation of the programme of activities by the CPA owners in collaboration with one another.
 - ii) Ownership of a certain specified percentage of the gross carbon emission reduction credits will accrue to the Project developer as the project sponsor (project sponsor carbon emission reduction credit accrual) and the balance will be jointly owned by all CPA owners and will accrue individually to each CDM program of activities proportionally according to each ones contribution of carbon emission reduction credits in the relevant period.
- g) The Applicant will pay all the expenses related to the running of the programme of activities from the inclusion fees, annual fees and carbon revenue if required. The surplus will be distributed to the CPA owners according to their proportional share of revenue calculated based on the carbon emission reduction credits contributed in the relevant period.
- h) The Applicant will receive a fee for services rendered as manager of the programme of activities.

6. Conditions and assumptions

This binding class ruling is not subject to any additional conditions and assumptions.

7. Ruling

The ruling made in connection with the proposed transaction is as follows:

- a) The programme of activities will be a qualifying “Clean Development Mechanism project” as defined in section 12K(1) of the Act.
- b) The CPA owners and the first CDM project owner will be the persons carrying on the “qualifying CDM project” as defined in section 12K(1).
- c) The proceeds from the disposal of the carbon emission reduction credits (carbon revenue) generated by the programme of activities will be exempt from income tax under section 12K(2) of the Act in the hands of the CPA owners. The exemption is not affected by virtue of the fact that the carbon revenue will be received by the Applicant acting in its capacity as manager of the programme of activities.
- d) Only carbon revenue from the carbon emission reduction credits that the first CDM project owner derives from conducting its own CDM project of activities will qualify for exemption under section 12K(2) of the Act. Consequently, the carbon revenue from the disposal of the extra carbon emission reduction credits accrued in terms of the programme of activities agreement will not be exempt from normal tax under section 12K(2) of the Act.
- e) The carbon emission reduction credits need not be accounted for as “trading stock” as defined in section 1(1) of the Act.
- f) The sale of carbon emission reduction credits to non-resident purchasers will be subject to VAT at a zero rate under section 11(2)(l) of the VAT Act, provided all the requirements of that section are complied with.

8. Period for which this ruling is valid

This binding class ruling is valid for a period of 5 years from 10 February 2016.

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