

2 February 2024

**Final Response Document on the 2023 Draft Rates and Monetary  
Amounts and Amendment of Revenue Laws Bill, 2023 Draft Taxation  
Laws Amendment Bill and 2023 Draft Tax Administration Laws  
Amendment Bill.**

**(Based on hearings by the Standing Committee on Finance in Parliament)**



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## **1. BACKGROUND**

### **1.1. PROCESS AND PUBLIC COMMENTS**

The 2023 Draft Taxation Laws amendment Bill (TLAB) and 2023 Draft Tax Administration Laws Amendment Bill (TALAB) contain the remainder of the tax announcements made in Chapter 4 and Annexure C of the 2023 Budget Review, which are more complex, technical and administrative in nature. Due to the complex nature of these draft bills, greater consultation with the public is required on their content. The 2023 Draft TLAB and TALAB were published for public comments on 30 July 2023. While the 2023 Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill (Rates Bill) was first published on Budget Day (22 February 2023) and published again on 30 July 2023. The closing date for all public comments on the 2023 Draft TLAB, 2023 Draft Rates Bill and 2023 Draft TALAB was 31 August 2023.

For legal reasons, the draft tax amendments continue to be split into two separate bills, namely, a money bill in terms of section 77 of the Constitution, dealing with money bill issues, for example, 2023 Draft TLAB and an ordinary bill in terms of section 75 of the Constitution, dealing with tax administration issues, for example 2023 Draft TALAB.

National Treasury and SARS received in total written comments from 83 organisations and 258 individuals (list of commentators attached as Annexure A).

The National Treasury and SARS briefed the Standing Committee on Finance (SCoF) on the 2023 Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill (Rates Bill), 2023 Draft TLAB and 2023 TALAB on 29 August 2023. Workshops with stakeholders to discuss their written comments on the 2023 Draft TLAB and 2023 Draft TALAB were held on 6 and 8 September 2023 respectively. Subsequently, oral presentations by taxpayers and tax advisors on the 2023 Draft TLAB and 2023 Draft TALAB were made at hearings held by the SCoF on 20 September 2023.

On 25 October 2023, National Treasury and SARS presented to the SCoF the Draft Response Document on the 2023 Draft Rates Bill, 2023 Draft TLAB and 2023 Draft TALAB (2023 Draft Tax Bills). The 2023 Draft Response Document contained a summary of draft responses from National Treasury and SARS officials to the public comments received and proposed steps to be taken in addressing the key issues raised during the consultation process.

Once the responses are considered by SCoF, they will be presented to the Minister for approval, including to approve consequential amendments to the 2023 Draft Tax Bills prior to the formal introduction/tabling by the Minister in Parliament.

## **1.2. POLICY ISSUES AND RESPONSES**

Provided below are the responses to the key issues raised by the public in respect of the 2023 Draft Tax Bills in the form of written submissions as well as during the public hearings. These comments will be considered in finalising the 2023 Draft Tax Bills to be tabled by the Minister of Finance on 1 November 2023. Comments that are outside the scope of the 2023 Draft TLAB and 2023 Draft TALAB are not considered for purposes of this response document.

## **1.3. SUMMARY**

This response document includes a summary of the written comments received on the 2023 Draft Rates Bill, 2023 Draft TLAB and 2023 Draft TALAB that were published for public comment on 30 July 2023, as well as a summary of all the written and oral presentations made during public hearings on the 2023 Draft TLAB and 2023 Draft TALAB held by the SCoF on 20 September 2023.

## 2023 Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill

### 2. CUSTOMS AND EXCISE: INCREASE IN THE EXCISE DUTY ON ALCOHOL AND TOBACCO

(Main reference: Schedule No. 1 to Customs and Excise Act, 1964: Clause 7 of the DraftRates Bill)

Government has a guideline to direct excise duty policy where duty should be 11, 23 and 36 per cent of weighted average retail price for wine, beer and spirits and 40 per cent of price of most popular brand for cigarettes. In 2023, Government proposes to increase excise duties on alcohol and tobacco in line with expected inflation of 4.9 per cent.

#### 2.1. General inflationary increase in the excise duty on alcohol

*Comment:* Excise duties for categories 104.01.10 (i.e. Traditional African beer powder) and 104.10.10 (i.e. Traditional African beer) have not been increased with inflation. Further, the CPI changes between July 2022 and July 2023 for alcoholic drinks were 6.1% for Spirits, 9.8% for Wine and 7.4% for Beer, Therefore, the excise tax on alcoholic beverages should be those products CPIs or at least the average of 7.8%.

*Response:* Noted. Annual excise adjustments on alcoholic beverages (with the exception of traditional African beer and similar products) are calculated based on either tax incidence derived from projected prices for the next fiscal year or the expected inflation rate, whichever is higher. Traditional African beer has often been taxed lower to account for the negative distributional effect of alcohol taxation on the poor as this market is very informal and very small in South Africa. However, with the excise policy review currently underway all such inputs from stakeholders will be considered.

*Comment:* Welcomes the in line with projected inflation excise adjustment for beer of 4.9% across the alcohol category. In particular, welcome two consecutive excise adjustments that have fallen relatively within the guidelines set out in the Excise Policy. Recommend to SCOF that there be a long-term and sustainable application of the excise adjustment, by providing the same certainty afforded to industries that must prescribe to the payment of an environment levy. This would fundamentally include ensuring that the excise adjustment in the Rates Bill is in line with projected inflation, not merely as an exception, as we have seen over the last couple of years, but that it becomes the rule where there is a long, sustainable trend in which the excise adjustment is applied in accordance with the Excise Policy governing it.

*Response:* Noted. However, adjustments in excise duties refer to current policy guidelines where the annual adjustments are calculated based on either tax burdens derived from projected prices for the next fiscal year or the expected inflation rate, whichever is higher. Any changes in the guidelines will be considered in the excise policy framework review process, which will consider all stakeholder inputs.

*Comment:* Introduce a multi-year taxation approach, where taxes on tobacco products, e-cigarettes and alcohol increase annually by a pre-announced amount (or percentage) above the inflation rate.

*Response:* Noted. However, adjustments in excise duties refer to current policy guidelines where the annual adjustments are calculated based on either excise tax incidence derived from projected prices for the next fiscal year or the expected inflation rate, whichever is higher. Any changes in the guidelines will be considered in the current excise policy framework review process, which will consider all stakeholder inputs.

*Comment:* The current low-growth environment, where price stability remains a concern, has affected the economic performance of the beer industry and therefore suggest only increasing the 2024/25 excise adjustment below or in line with the projected inflation rate. Have noted that the latest revision in the Reserve Bank's forecast for inflation for 2024, have put this at 4.9%.

*Response:* Noted. However, the adjustments in excise duties prioritise the main policy objectives communicated to all stakeholders – discouraging harmful consumption and revenue generation. National Treasury cannot give a commitment to not increase the rate by more than inflation. It is the Minister of Finance that is empowered to make the decisions about the annual excise duty rates adjustments.

*Comment:* Systemically, the application of an Alcohol-By-Volume (ABV) or an alcohol content-based system be applied to the full alcohol category, similar to -that which currently applies to beer and spirits. In particular that there be a removal of the market distortionary effect due to the preferential treatment afforded to the wine industry in the excise system.

*Response:* Noted. In theory, the taxation of alcoholic beverages based on alcohol content would be ideal for public health purposes. However, in reality the excise policy structures implemented globally are such that the other factors are considered. The alcohol content for wines varies quite substantially (i.e. between 4.5 & 16.5% vol for natural wine, and 15 & 22% vol for fortified wine) and changing the base to ABV will complicate the administration of the system. Therefore, application of low excise duties and on a per litre basis on wine is not unique to South Africa. This is prevalent mostly in wine producing countries such as Australia, France, Italy, USA because of strong economic backward linkages,

employment contribution, export and tourism potential. Also, as an example, the European Union Directive 92/84/EEC provides for different treatment of categories of alcoholic products (i.e. wine taxed per product volume, whereas beer and spirit based on alcohol content) and special rates for small producers. However, the excise policy framework for alcoholic products is currently under review, and inputs from all stakeholders will be considered as part of the review process.

## **2.2. General inflationary increase in the excise duty on tobacco**

*Comment:* As with the 2022/23 cigarette excise increase, we would like to commend National Treasury for continuing with a balanced approach on cigarette excise increases in the 2023/24 fiscal year. The Draft Rates Bill proposes to increase the excise rate on cigarettes by 4.9% in the context of the 2022 inflation rate of 6.9%. This excise hike has placed the excise incidence on cigarette's Most Popular Price Category ("MPPC") at 45.2% compared to a targeted incidence of 40% as per the National Treasury's excise policy. The total tax incidence on the MPPC currently sits at 58.3% against the background of falling consumer affordability and unprecedented levels of illicit trade.

*Response:* Noted. Although the proposed increases keep the tax incidence above the 40 per cent policy guideline, the industry has continued to absorb a portion of the excise increases as opposed to passing them through to consumers, which leads to an overestimated tax incidence. The adjustments correct for any price movements that tend to undermine government's policy intention to reduce consumption and improve public health. The excise increases also seek to ensure that tobacco products do not become more affordable over time as this will increase consumption of tobacco products, which goes against public health policy objectives. The excise policy framework for tobacco products is currently under review and once completed, all the stakeholders will be informed, and a consultative process initiated.

*Comment:* Request National Treasury to continue to increase cigarette excise in a balanced manner which fully appreciates the extent of the illicit trade problem in South Africa, the effect that this has had on the MPPC concept, and the affordability issues currently being faced by the majority of South Africans.

*Response:* Noted. However, the adjustments in excise duties prioritise the main policy objectives communicated to all stakeholders, which is discouraging consumption of tobacco (and similar products), reducing affordability of these products over time and revenue generation.

*Comment:* Request National Treasury to revise the base on which the current cigarette excise increases/levels are determined as the MPPC concept with Peter Stuyvesant as an anchor brand is no longer relevant in the current market. In line with global best practice, South African fiscal policy in respect of cigarettes should be determined on Weighted Average Price ("WAP") in the market.

*Response:* Noted. However, a revision of the Most Popular Price Category (“MPPC”) to the Weighted Average Price (“WAP”) will be a fundamental or substantive policy change with significant ramifications for tobacco control policy in South Africa. The current benchmarking using MPPC already has differential impacts on cigarette products in terms of excise burdens, so National Treasury does not envisage a situation where there is a reversal on the current levels of excise duty rates. However, the excise policy framework for tobacco products is currently under review and some of these issues will be considered and inputs from all stakeholders are welcome.

*Comment:* It is well-documented that tobacco use imposes a significant health and economic burden on countries, and that consistent, year-on-year increases in tobacco excise taxes reduce tobacco use. The cost of smoking in South Africa amounted to nearly 1% of the South African GDP in 2016. These costs are likely to have increased as a result of the observed rise in smoking prevalence over the past five years. Within this context, we urge National Treasury to substantially increase the excise tax on tobacco products in the 2024/2025 budget cycle. We suggest a 10% increase in the excise tax above the inflation rate.

*Response:* Noted. However, adjustments in excise duties refer to current policy guidelines where the annual adjustments are calculated based on either excise tax incidence derived from projected prices for the next fiscal year or the expected inflation rate, whichever is higher. Any changes in the guidelines will be considered in the current excise policy framework review process, which will consider all stakeholder inputs.

### **2.3. Illicit Trade issues**

*Comment:* South Africa has a large and growing illicit alcohol market which offers consumers access to more affordable alternatives, potentially with more associated harm. Pricing policies, such as excise and Minimum Unit Pricing (MUP) that effectively widen the price gap between the licit and illicit markets, need to take cognizance of this. A recent exercise by the industry working closely with SARS has shown that sugar fermented beverages (Ales) do not attract the correct excise tariff.

*Response:* Noted. SARS as the implementing agency of excise policy is committed to ensuring that all the necessary measures for effective enforcement of the legislation are implemented. SARS has committed itself to detect taxpayers and traders who do not comply with their tax obligations and make non-compliance hard and costly for them. Issues of MUP will be considered in the context of the current review process.

*Comment:* The lack of law enforcement in South Africa is a significant hinderance, and therefore consideration, to any policy implementation. Policy changes, in the absence of improved enforcement, are unlikely to make an impact. The cost of enforcement is a key variable to assess ahead of policy implementation, as part of a

full cost-benefit analysis.

*Response: Noted.* It is possible for Government to concurrently oversee the implementation of an effective customs and excise administration system while reviewing the existing excise policy framework, subsequently, implement the necessary changes. The two processes are not mutually exclusive. SARS is implementing a number of compliance measures, including collaborating with other law enforcement agencies to address issues in the tobacco supply chain.

*Comment:* Real excise tax revenue from alcohol has been increasing consistently over the past two decades, other than a substantial dip in 2020 for beer and wine, which can be attributed to the numerous alcohol sales bans in that year. The increase in alcohol revenue (and therefore sales) is not due to rapid increases in household income because macro-economic performance during this period has been weak. Any arguments about the increase in alcohol illicit trade should be questioned. Whereas the increase in the illicit trade in tobacco products is reflected in the tax revenue numbers, there is nothing in the alcohol revenue numbers to suggest that this is a problem.

*Response: Noted.* The illicit trade in alcoholic products is not as pronounced as is the case with tobacco products, and also not as was the case during COVID19 sales bans. However, they are both receiving attention as they undermine government public health policy objectives. Indeed, the observed revenues from alcoholic products over the years has increased and will be subject of the current review process.

*Comment:* The current cigarette excise increase (which took effect in February 2023) has curtailed the widening of the gap between the lowest priced products at the bottom of the legal market and illicit products. This has in turn slowed down the rate of migration of legal cigarette volume into illicit cigarette volume.

*Response: Noted.* However, the problem of illicit trade is an act of criminality and cannot be attributed or dealt with through excise policy but needs to be effectively addressed through robust compliance and law enforcement mechanisms.

*Comment:* South Africa now has one of the highest illicit cigarette trade levels in the world at up to 70% of annual consumption. Unfortunately, illicit products continue to sell on a mass scale for as little as R10 for a pack of 20 cigarettes and, with a Minimum Collectable Tax (MCT) alone of R23.92 on a pack of 20 cigarettes, it is not possible for the legal industry to “win back” any volume from this illegal market segment. The vast majority of all consumption (illicit and licit), approximately 80%, takes place in the informal trade. The informal trade is dominated by single stick sales, and given the DNP price points, the legal market can simply not compete.

*Response: Noted.* National Treasury acknowledges the problem of illicit trade and that it undermines the health and excise policy objectives. However, the problem of illicit trade is also an act of criminality and cannot be dealt with through excise

rate adjustments but needs to be effectively addressed through robust compliance and law enforcement mechanisms. SARS is harnessing its capabilities to make non-compliance with legal tax obligations hard and costly to those who are engaged in these criminal pursuits.

*Comment:* The illicit market accounted for 58% of total cigarette sales in 2022. Factors that facilitate illicit trade are insufficient enforcement, organised crime syndicates, high levels of corruption, inadequate sanctions for offenders, porous borders. In some contexts, there is a link between excise taxes and illicit trade, but not in South Africa. Illicit trade should be addressed through effective enforcement mechanisms which include, amongst other things, measures to secure the tobacco supply chain, not by lowering the excise tax. We recommend that South African government should ratify the Protocol to Eliminate Illicit Trade in Tobacco Products and implement its provisions

*Response:* Noted. The National Department of Health is leading Government on the matter of ratifying the World Health Organisation's Protocol to Eliminate Illicit Trade in Tobacco Products.

*Comment:* A track-and-trace system should be implemented in South Africa for cigarettes and vaping products. This system should be fully digital and allow for interoperability with the different Southern African Customs Union ("SACU") markets and trade blocs such as the European Union, strengthening the ability of the Authorities to enforce and ultimately clamp down on illicit trade. The process towards the implementation of a track-and-trace system should be expedited.

*Response:* Noted. In the meantime, SARS is implementing a number of compliance measures including collaborating with other law enforcement agencies such as the South African National Defence Force (SANDF), the South African Police Service (SAPS) and its Hawks unit, as well as the Immigration division of the Department of Home Affairs to address issues in the tobacco supply chain.

*Comment:* Request National Treasury to introduce into the Act, through a primary legislation change, a Minimum Retail Price ("MRP") point of R34 per pack of 20 cigarettes to achieve effective enforcement and to address retail tax compliance. This change should not take place as part of the excise policy framework review (as previously noted by National Treasury in a response to our proposals) but rather through an amendment to the Customs and Excise Act 91 of 1964 ("the Act"). A primary legislation change will allow all manufacturers to provide support (through detailed public consultation) to National Treasury as to why the R34 is too high or too low. In addition, it will allow the MRP to be adjusted annually through secondary legislation and will allow for the MRP to be "turned off" once illicit trade has been brought under control.

*Response:* Noted. The excise policy framework for tobacco products is currently under review. Inputs from all stakeholders such as this will be considered.

## 2.4. Administration and technical issues

*Comment:* There is an overlap between unfortified wine (from 4.5 to 16.5%) and fortified wine (from 15% to 22%). Is there a risk that some wine can fall within both categories?

*Response:* Noted. There is no risk of wine falling in both categories. Wine is either fortified by means of adding distilled grape spirits to the final product of fermenting grapes or not. The alcohol range for fortified wine is between 15% and 22% in terms of the Regulations to the Liquor Products Act. The alcohol range for unfortified “natural” wine according to the Regulations to the Liquor Products Act, is 4.5% to 15%. These percentages also appear on the labelling of wine.

*Comment:* There is a distinction between wine in containers holding 2li or less, wine in containers above 2li and below 10li, and other wine. However, the excise duties are the same for each of those categories. What is the purpose of making this distinction?

*Response:* Noted. The distinction is on an international 6-digit level. As a signatory to the Harmonised System Convention, RSA is obligated to incorporate this structure in its national tariff structure. The purpose of the distinction is therefore not related to the excise duty structure but rather the trade of the goods in the international arena.

*Comment:* A distinction is also made here for Vermouth and other wine of fresh grapes flavoured with plants or aromatic substances but, again, the excise duty rates are exactly the same as the ones for the former category of wine. What is the purpose of making this distinction?

*Response:* Noted. In this instance the distinction is on the Harmonised System (HS) 4-digit level. The excise categories are harmonised with the structure applicable to imported goods, which assists with identifying all the taxes applicable to specific goods classified under a specific category number (tariff code).

*Comment:* For spirits and liquors, there is again a distinction between containers (less than 2 li and other) but no difference in the excise duty rate associated to each of them. Shouldn't this distinction be met with different rates?

*Response:* Not accepted. No, as correctly stated, the excise applies uniformly to spirits on the absolute alcohol content. The category structure for excise is aligned with the HS tariff structure for imported goods. This structure is also aligned with the latest HS 2022 up to a 6-digit level that is used internationally. The container size is on the binding 6-digit level.

*Comment:* All spirits are subject to an excise duty of R257.23/li aa except for brandy, which is subject to a lower excise duty rate. This may be considered discriminatory.

Is there a justification for the lower duty on brandy?

*Response: Noted.* In Budget 2015 the Minister of Finance announced a proposal for specific provision for excise duty on pot stillled and vintage brandy as defined in the Liquor Products Act, being a 10% lower excise duty, based on litres of absolute alcohol content. The rationale is that brandy is at a cost disadvantage compared with other forms of alcoholic spirits because it takes 4-5 litres of wine to produce a litre of brandy. Further, pot stillled brandy and vintage brandy have an extended maturation period.

Pot stillled brandy must be matured by storage for a period of at least three years, and up to eight years, in oak casks with a capacity of not more than 340 litres.

### **3. CUSTOMS AND EXCISE: HEALTH PROMOTION LEVY**

#### **3.1. Delaying the increase to the health promotion levy for two years**

(Main reference: Section 58 of Customs and Excise Act, 1964: Clause 7 of the Draft Rates Bill)

The 2022 Budget stated that the HPL would be increased by inflation at 4.5 per cent to 2.31 cents per gram from 1 April 2022. On 1 April 2022, the Minister of Finance released a media statement to delay the implementation of the increase on the HPL to 1 April 2023. However, in the February 2023, the Minister further announced that there will be no increase in the HPL in 2023/24 and 2024/25. A discussion paper on the HPL Review will still be published for consultation on proposals to extend the levy to pure fruit juices and lower the 4-gram threshold.

*Comment:* Notes with disappointment that the Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill as published on 31 July 2023, yet again, fails to bring the South African Health Promotion Levy (HPL) in line with the international best practice of a 20% sugar-sweetened beverage tax. This failure occurs in the context of Treasury's express acknowledgment that an annual adjustment for inflation is necessary to support the purpose of the tax to promote health. In fact, the continued failure of government to adjust the HPL to account for inflation has led to worrying erosion of the tax.

*Response: Noted.* The delays in the inflationary adjustment to the HPL is to enable stakeholders in the sugar industry to restructure, given the challenges from greater regional competitive pressures and the effect of recent floods.

*Comment:* The rate of the Health Promotion Levy has not been increased compared to the 2022 rates with inflation at around 5%. This may contribute to beverages that are high in sugar being relatively affordable. The increase in prices between July 2022 and July 2023 for non-alcoholic beverages has been much higher than the average increase in overall prices of goods (8.8% vs 4.7%). It is therefore suggested

to increase the levy by 8.8% to avoid erosion of the levy. If aiming to lower affordability of SSBs, the tax should be increased more than inflation plus GDP growth.

*Response: Noted.* The Minister announced in 2023 Budget that there will be no increase in the health promotion levy in 2023/24 and 2024/25 to enable stakeholders in the sugar industry to restructure, given the challenges from greater regional competitive pressures and the effect of recent floods.

*Comment:* The proposed increase of HPL from 2.21 cents/g to 2.31 cents/g, in nominal terms represents an increase of 4.5%, but one needs to question whether this amounts to a real increase. In fact, inflation eroded the value of the HPL between 2018 and 2022. In real terms, the HPL declined by 11% from ZAR0.026/g in 2018 to ZAR0.023/g in 2022 because of inflation. Given the cost-effective nature of fiscal policies in controlling unhealthy consumption, SA's HPL on sugary drinks must be increased regularly and should take account of inflation in view of the specific tax structure being used. For 2023, an inflation adjusted HPL would be 2.32 cents/g (=1.05 x 0.221 cents). Thus, the HPL should be increased by more than 5% for the levy to be effective. In order to ensure that the HPL is effective, we propose a 10% increase, which brings the HPL to 2.43 cents/g.

*Response: Noted.* The Minister announced in 2023 Budget that there will be no increase in the health promotion levy in 2023/24 and 2024/25 to enable stakeholders in the sugar industry to restructure, given the challenges from greater regional competitive pressures and the effect of recent floods.

*Comment:* We further commend the Treasury for the efforts to extend the levy to fruit juice, as announced in the 2023–2024 budget speech. We recommend that this policy initiative be implemented as soon as possible. In this time of government financial constraints, doing this would not only improve the health of South Africans but also help boost the fiscus. Like the tobacco and alcohol industries, the sugar industry will always lobby against health taxes without any consideration of the health impact of sugary drink consumption and its true costs to society. Industry players have no place in policies that affect population health given that they will always prioritise profits over public and planetary health.

*Response: Noted.* The Minister announced in 2023 Budget that there will be consultation on proposals to extend the levy to pure fruit juices and lower the 4-gram threshold.

*Comment:* We have previously denounced the decision by National Treasury to postpone the 2022 inflationary increase to April 2023. This increase – an already below inflation increase from 2.21 cents to 2.31 cents per gram of sugar for sugar-sweetened beverages (SSBs) above the threshold of 4 grams of sugar per 100 ml – is now delayed until 2025 in the proposed draft. This delay is an unacceptable and unjustifiable failure to protect the rights of South Africans to health, access to nutritious food, life and dignity.

*Response:* Noted. However, the HPL is not the only intervention being implemented but rather complements other interventions such as promoting overall healthy eating in various settings and consumer education. Hence, we fully support continued efforts by the National Department of Health through the Strategy for the Prevention and Management of Obesity 2023 – 2028, National Strategic Plan for the Prevention and Control of Non-Communicable Diseases 2022 –2027 and related regulations / plans, to promote the well-being of South Africans. We will publish a discussion paper on the HPL for consultation on proposals to extend the levy to pure fruit juices and lower the 4-gram threshold.

*Comment:* The 4g threshold before taxation should also be reduced, as it was based on unsubstantiated claims by industry.

*Response:* Noted. National Treasury determined the 4 grams threshold, and it is based on the fact that a teaspoon of sugar is equivalent to 4 grams<sup>1,2,3</sup>.

*Comment:* Earmark the HPL revenue to social and economic projects that benefit South Africans in need.

*Response:* Noted. All tax revenues accrue to the National Revenue Fund for general government expenditure, as per determined priorities, however there is a commitment for budgetary support for health promotion programmes identified by the NDoH. The legislative earmarking of revenue is not supported as it will introduce rigidities in the budgeting process. The government has committed to increasing investments in health promotion targeting NCDs and has published this commitment in National Treasury documents and international WHO publications.

*Comment:* The tariff categories (i.e. 191.07.15 and 191.07.25) exclude items 'with a basis of milk'. It is recommended that consideration be given to revising the exclusion of milk-based items from the category of products to which the health promotion levy applies.

*Response:* Not accepted. The health promotion levy applies to all preparations and beverages containing sugar. These preparations and beverages fall to be classified in headings 18.06, 19.01, 21.06 and 22.02 as listed in Part 7A. Although milk is not included, beverages with a basis of milk, but containing ingredients not allowed for milk, are included in the tax net for sugary beverages under 7A. The exclusion referred to are just because those milk-based beverages should be classified in the residual category listed in the structure of Part 7A (191.07.20 and 191.07.90)

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<sup>1</sup> <http://www.newhealthguide.org/How-Many-Grams-Of-Sugar-In-A-Teaspoon.html>

<sup>2</sup> [https://www.canr.msu.edu/news/how\\_to\\_convert\\_grams\\_of\\_sugars\\_into\\_teaspoons](https://www.canr.msu.edu/news/how_to_convert_grams_of_sugars_into_teaspoons)

<sup>3</sup> [https://www.who.int/news-room/fact-sheets/detail/healthy-diet#:~:text=Less%20than%2010%25%20of%20total%20energy%20intake%20from%20free%20sugars,additonal%20health%20benefits%20\(7\).](https://www.who.int/news-room/fact-sheets/detail/healthy-diet#:~:text=Less%20than%2010%25%20of%20total%20energy%20intake%20from%20free%20sugars,additonal%20health%20benefits%20(7).)

*Comment:* The Sugar Master Plan (SMP) under the auspices of the Ministry of Trade, Industry and Competition is currently seized with the process of developing a detailed restructuring diversification plan, as well as industry proposals for a long-term policy framework, with the view of engaging government on strategies relating to the remodelling of the HPL. We firmly believe that the potential of our industry's diversification should be fully harnessed prior to any rates adjustments on the HPL.

*Response:* Noted. The Minister announced in 2023 Budget that there will be no increase in the health promotion levy in 2023/24 and 2024/25 to enable stakeholders in the sugar industry to restructure, given the challenges from greater regional competitive pressures and the effect of recent floods and public violence.

*Comment:* The completion of the Socio-Economic Impact Assessment (SEIAS) process by the Office of the Presidency is currently underway and is also integral to comprehending the broader socioeconomic effects of any potential policy changes on the HPL. Further, any shift in the reformulation of public health policy and/or interventions in relation to the HPL must be preceded by a National Dietary Intake Survey (NDIS), which is also in the process of being finalised by the relevant policy department and these should be preceded by a meaningful engagement with all stakeholders as promised.

*Response:* Noted. An inflation-linked adjustment to the HPL is to preserve the value of the rate (like any other excise duties) and represent a policy change. It merely seeks to preserve the real value of the levy rate like it is done with other excise duty rates. Any fundamental change to the policy such as was announced by the Minister will be followed an engagement with all relevant stakeholders.

*Comment:* The industry has repeatedly requested two core issues to be further interrogated: first, consideration of the effectiveness of the HPL in achieving the alleged public health benefits as a critical precursor to its increase and, secondly, transparency around the decision-making on this issue. To date, industry stakeholders have had no opportunity to enquire into the reasoning or the justification for the increase. This is especially important since government has provided no data demonstrating the effectiveness of the levy in achieving its stated objective of reducing obesity and the prevalence of obesity-related diseases in South Africa. National Treasury has failed to respond to a request submitted in December 2022 under the Promotion of Access to Information Act to disclose the information considered in decision-making around the HPL, including any reports or studies on the effectiveness of the intervention in reducing obesity. In the absence of any substantive evidence that the levy has been effective, and considering the demonstrated economic destruction of the levy, consultation is needed to determine whether the HPL should in fact be eliminated altogether. Consideration should also be given to a more holistic approach to health that takes into account all of the factors that contribute to obesity in South Africa

*Response:* Not accepted. The proposed increase is just an inflation-linked adjustment to the HPL tax rate to preserve the value. The introduction of the HPL followed the normal policy and legislative process where a discussion document<sup>4</sup> which details the policy rationale for the HPL was published and consultations with all interested parties were conducted. The policy rationale for the HPL remains unchanged, so is the evidence that informed the recommendation to introduce the tax. Notable early successes that followed the introduction of the HPL, include manufacturers:

- reformulating products by reducing the sugar content;
- increase their product portfolio with less or no sugar products;
- reduced the package sizes of normal products together with increased pricing;
- increased the package sizes of new low or no sugar products, together with reduced pricing of these products, to encourage consumers to switch to lower sugar alternatives.

See also<sup>5,6,7,8</sup> for empirical evidence that signals reduced availability / intake of SSBs following the introduction of the HPL.

*Comment:* Given that we do not believe that there is rationale for the HPL's scope to be extended, it is our assertion that only products with added sugar should be levied and products with intrinsic sugar only, should be exempted. The HPL should exclude all dairy products (unless sugar is added), as well as exclude pure and 100% fruit juices where fructose is intrinsic (unless sugar in any form is added). In cases where sugar is added to a product with intrinsic sugars, higher thresholds are required to accommodate the intrinsic sugar. Further, the HPL should incentivize industry to reformulate. Targets and timelines should be established through negotiations between public health authorities and food industry with assistance from independent food technology experts and in some cases inputs of consumers.

*Response:* Noted. The current HPL excludes 100% fruit juice and milk and milk products without added sugar. Any fundamental change to the policy such as was announced by the Minister in the 2023 Budget will be followed by an engagement with all relevant stakeholders.

*Comment:* The main issue is still around ring-fencing the HPL. HPL is being paid, but without any impact whatsoever of the health outcomes of South Africans, as was confirmed in the latest WHO/UNICEF report. We propose that the increase and extension of the HPL is further deferred until such time the full obesity strategy is agreed and approved, and we can see the health impact on South Africans.

<sup>4</sup><https://www.treasury.gov.za/public%20comments/sugar%20sweetened%20beverages/policy%20paper%20and%20proposals%20on%20the%20taxation%20of%20sugar%20sweetened%20beverages-8%20july%202016.pdf>

<sup>5</sup> Hofman, K.J., Stacey, N., Swart, E.C., Popkin, B.M., Ng, S.W. (2021). 'South Africa's Health Promotion Levy: Excise tax findings and equity potential'. *Obes. Rev. Off. J. Int. Assoc. Study Obes.* <https://doi.org/10.1111/obr.13301>

<sup>6</sup> Stacey, N., Edoka, I., Hofman, K., Swart, E.C., Popkin, B., Ng, S.W. (2021). 'Changes in beverage purchases following the announcement and implementation of South Africa's Health Promotion Levy: an observational study'. *Lancet Planet. Health* 5, e200–e208. [https://doi.org/10.1016/S2542-5196\(20\)30304-1](https://doi.org/10.1016/S2542-5196(20)30304-1).

<sup>7</sup> Ross A, Swart EC, Frank T, Lowery CM, Ng SW. South Africa's Health Promotion Levy on Pricing and Acquisition of Beverages in Local Spazas and Supermarkets. *Public Health Nutr.* 2022 Mar 7;25(5):1-26. doi: 10.1017/S1368980022000507. Epub ahead of print. PMID: 35249582; PMCID: PMC9991735.

<sup>8</sup> Essman M, Taillie LS, Frank T et al. (2021) Taxed and untaxed beverage intake by South African young adults after a national sugar-sweetened beverage tax: a before-and-after study. *PLoS Med* 18, e1003574.

*Response:* Not accepted. The HPL is not the only intervention being implemented but rather complements other interventions such as promoting overall healthy eating in various settings and consumer education. Hence, we fully support continued efforts by the National Department of Health through the Strategy for the Prevention and Management of Obesity 2023 – 2028, National Strategic Plan for the Prevention and Control of Non-Communicable Diseases 2022 –2027 and related regulations / plans, to promote the well-being of South Africans.

#### **4. CUSTOMS AND EXCISE: ELECTRONIC CIGARETTE TAXATION**

Government implemented a tax on electronic nicotine and non-nicotine delivery systems (ENDS / ENNDS) with effect from 01 June 2023. This was a culmination of a process that started with an announcement made in budget 2019 and subsequently in budget 2020 due the growing evidence that these products are not harmless. The initial proposal as announced in the 2022 Budget was to implement the excise duty from 1 January 2023. However, in the 2022 draft TLAB a decision was made to have a later implementation date of 01 June 2023 to provide SARS and taxpayers sufficient time for the administration of the system. Section 25 of the Taxation Laws Amendment Act, 2022, gave effect to the implementation as of 1 June 2023.

*Comment:* From 1 June 2023, e-liquid is taxed at a flat excise duty rate of R2.90/ml. In 2022, 9 schools in 3 provinces were surveyed, 27% of grade 12 learners vaped. E-cig tax is not well-targeted at reducing consumption of vaping products among youth. Disposable vaping devices typically have less than 6ml of e-liquid. Seasoned vapers use open systems where e-liquid is sold in containers ranging from 20ml to 100ml. For the tax to better target youth vapers, government should introduce a minimum excise tax amount on e-liquid. A minimum tax amount of R50 per unit/container would have no additional tax impact for e-liquid containers with more than 17.5 ml but would have a sizable impact on the price of disposables.

*Response:* Noted. The current proposed rate is an introductory rate that may be adjusted in the short to medium term during the budget process. The Minister of Finance is empowered to make proposals about the annual excise rates and adjustments.

*Comment:* In respect of the new Vaping Excise which was introduced via the Taxation Laws Amendment Act, 2022, and discussed in the Budget Statements, as previously noted to National Treasury, based on detailed analysis performed by ourselves and also separately by Oxford Economics, we remain of the view that the rate of R2.90 per ml is far too high in the South African context and may have unintended consequences in the medium to long term.

*Response:* Noted. The proposed excise rate is comparable to other rates applied in other jurisdictions that have implemented excise duties on ENDS/ENNDS. The Minister of Finance is empowered to make proposals about the annual excise rates and adjustments.

*Comment:* We appreciate that National Treasury, the Select Committee on Finance and the Standing Committee on Finance consulted extensively with all affected stakeholders for approximately one year to determine the introductory rate. Therefore, it would be too soon at this juncture (i.e. 3 months after the vaping excise has been introduced) to call for a marked change in the excise rate as the impact of the excise needs to be fully observed over the medium to long term. We therefore recommend that for the 2024/2025 Budget Year, National Treasury hold the vaping excise rate at R2.90 per/ml.

*Response:* Noted. The implemented rate was an introductory rate, as previously indicated, that may be adjusted in the short to medium term during the budget process. It is the Minister of Finance that is empowered to make proposals about the annual excise duty rates adjustments.

## 2023 Draft Taxation Laws Amendment Bill

### 5. CUSTOMS AND EXCISE: PROVIDING FOR A PARTIAL REFUND OF THE ROAD ACCIDENT FUND LEVY

#### 5.1. Providing for a partial refund of the Road Accident Fund Levy applicable to the purchase and use of fuel for the manufacture of foodstuffs, in Schedule No. 6 to the Customs and Excise Act

(Main reference: Schedule No.6 to the Customs and Excise Act, 1964: Clause 45 of the Draft TLAB)

In light of the current electricity crisis, a refund similar to the diesel refund for farming, forestry, fishing and mining sectors will be extended to the manufacturers of foodstuffs on the RAF levy for diesel used in the manufacturing process. The new RAF levy refund for foodstuffs manufacture will be in respect of the new refund item 670.05 subject to the new Note 14. The refund will apply to the purchase and use of distillate fuel for the manufacture of foodstuffs during the period 1 April 2023 to 31 March 2025.

Persons that may apply for the new refund are those persons that both purchase and use distillate fuel for the manufacture of foodstuffs, that have successfully applied for refund user and manufacturing premises registration for purposes of refund item 670.05 and that are also registered for value-added tax purposes. The listed manufacturing activities must be performed by the registered refund user at the registered manufacturing premises in the realisation of foodstuffs for commercial gain.

*Comment:* Stakeholders broadly welcomed and accepted the relief and extension of the diesel refund to the manufacturers of foodstuffs. The rationale for the relief to limit the impact of power cuts on food prices was noted. There was a view that the manufacturing process is just one element of the food supply chain and if the objective is to limit the impact of power cuts on food prices then the relief should apply to the entire food supply chain and not just manufacturing of foodstuffs. The rebate should be extended to all businesses and not just manufacturers of foodstuffs.

*Response:* Not accepted. The limitation of the diesel refund is due to the fiscal constraints and administrative complexities. This is also in line with the policy objectives of introducing the refund, to cushion primary sectors from potential adverse impacts of high fuel prices and maintain their international competitiveness. There are high risks of abuse and enforcement complexities of including the entire food supply chain and other sectors.

*Comment:* Stakeholders noted that only the RAF levy qualifies for the refund and not the general fuel levy. There was a request for the policy rationale for the RAF levy

relief noting that for mining, fishing, agriculture and forestry and the generation of electricity by Eskom, at least a portion of the general fuel levy qualifies for the refund.

*Response:* Noted. The limitation of the rebate is due to the fiscal constraints and administrative complexities. There is limited scope within the fiscal framework to extend the relief beyond the RAF levy.

*Comment:* Stakeholders noted that 80 per cent of the RAF levy is subject to the refund and the refund should apply to the entire RAF levy and not only 80 per cent. While the budget did not explicitly state that the full amount of the RAF levy would be refunded, there was a view that “a similar refund on the RAF levy for diesel used in the manufacturing process (such as for generators) will be extended to the manufacturers of foodstuffs.”

*Response:* Not accepted. The Budget 2023 policy announcement was for a RAF levy refund similar to the current diesel refund for primary producers, which is at 80 per cent of the RAF levy. A higher rate would be inequitable and lead to abuse by current diesel refund item 670.04 users who could instead fraudulently claim their diesel under the new RAF levy refund item 670.05 to illegally benefit from the disproportionately higher rate. For example, farmers under the current diesel refund scheme who will also access the new refund as manufacturers of foodstuffs pose this risk.

## **6. CARBON TAX**

### **6.1. Clarifying the carbon budget allowance**

(Main reference: Section 12 of the Carbon Tax Act: Clause 66 of the Draft TLAB)

In October 2020, the DFFE gazetted an extension of the voluntary carbon budget system and the piloting of new methodologies for determining company-level carbon budgets. Changes were subsequently made to Section 12(1) of the Carbon Tax Act to align with the dates of the voluntary carbon budget system. The mandatory carbon budget system was planned to be implemented on 1 January 2023, once the Climate Change Bill would have been enacted.

In Budget 2022, it was announced that a higher carbon tax rate would apply to greenhouse gas emissions exceeding the carbon budget once the mandatory carbon budgets are implemented by the DFFE. These amendments to the Carbon Tax Act will be legislated once the Climate Change Bill is enacted, at which time the carbon budget allowance of five per cent will fall away.

The DFFE has not yet enacted the Climate Change Bill, therefore mandatory carbon budgets are not in place. An amendment to the Carbon Tax Act is required to provide clarity to taxpayers that a carbon budget allowance may be claimed until the

mandatory carbon budgets are implemented.

It is proposed that the period specified for carbon budget allowance in section 12 of the Carbon Tax Act is extended to 31 December 2024 to provide taxpayers clarity to continue claiming the carbon budget allowance.

*Comment:* The extension of the carbon budget allowance is welcomed and provides clarity to taxpayers. The proposed amendment is necessary in the absence of the mandatory carbon budgets pending the enactment of the Climate Change Bill.

*Response:* Noted. The extension of the carbon budget allowance until 31 December 2024 is broadly supported by stakeholders. The proposed extension of the allowance is to address ambiguity since the Climate Change Bill is not yet enacted and provide policy certainty to taxpayers. The extension of the allowance is in place until the mandatory carbon budgets are implemented.

## **6.2. Adjusting the formula for fugitive emission factors**

(Main reference: Schedule 1 of the Carbon Tax Act: Clause 67 of the Draft TLAB)

Section 4(2) of the Carbon Tax Act provides for the formulae to be used to calculate the greenhouse gas emissions for fuel combustion, fugitive and industrial process emissions, using emission factors in Schedule 1 to the Carbon Tax Act. In 2019, changes were made to the formula for fugitive emissions to provide for converting the unit of the emission factors for the different greenhouse gases from volume to mass through multiplying by a density factor, followed by multiplying by 1 000 to convert to tonnes. The changes that were made to the formula for fugitive emissions in 2019 were accurate for some Intergovernmental Panel on Climate Change code activities but not all, depending on the units of measurement in which the emission factors are expressed. Where the multiplication of the emission factors is inaccurate, it results in overestimated liability for the carbon tax. Changes are proposed to amend Table 2 of Schedule 1 to the Carbon Tax Act because amending the formulae would result in administrative challenges for SARS as the tax filing systems would have to be amended.

In order to correct for the overestimation of the tax liability for certain activities, it is proposed that the decimal places for the affected activities be removed by three places in order to align with the current tax filing system. The emission factors for activities with the following units of measurement are to move the decimal places by three:

- M3/Tonne
- Gg-CO<sub>2</sub> / year / km
- Gg-CO<sub>2</sub> / year / M3
- Gg / 103M3

*Comment:* The purpose of this proposed amendment to correct errors in the factors that erroneously multiplied by 1000 on e-filing for certain activities and to align Table 2 of Schedule 1 to the Carbon Tax Act with the current SARS tax filing system was

noted. Although there is agreement that the error should be fixed, there is concern that the proposed amendment fixes a system error rather than aligning Table 2 of Schedule 1 of the Carbon Tax Act with the Methodological Guidelines. The effect of the proposed amendment is to create a misalignment between the Carbon tax Act and the Methodological Guidelines.

*Response:* Not accepted. The proposed amendment seeks to correct the emission factors in Table 2 for which the multiplication by 1000 would result in an overestimation of the carbon tax liability for some activities. The changes are not due to SARS systems error as clarified in the TLAB Stakeholder consultation workshop held in September 2023. This approach was taken as it was the least disruptive from an administrative and legal perspective.

### **6.3. Aligning the fuel emissions factors with methodological guidelines and regulations**

(Main reference: Schedule 1 of the Carbon Tax Act: Clause 70 of the Draft TLAB)

The tax base of the Carbon Tax Act is greenhouse gas emissions reported to the Department of Forestry, Fisheries and the Environment (DFFE). The emissions are reported according to the 2016 National Greenhouse Gas Emission Reporting Regulations, which were gazetted in terms of the National Environmental Management: Air Quality Act, No.39 of 2004. The DFFE published the methodological guidelines for quantifying greenhouse gas emissions to provide the approach for companies to report greenhouse gas emissions. Section 4 of the of the Carbon Tax Act defines the tax base according to activities with emissions factors in Schedule 1 of the Carbon Tax Act.

In October 2022, the DFFE gazetted amended methodological guidelines for quantifying greenhouse gas emissions. The amendments include updated carbon dioxide emission factors for domestic (tier 2) emissions reporting for existing fuel types and also added fuel types. The guidelines further include default emission factors for fugitive emissions based on the 2019 Intergovernmental Panel on Climate Change (IPCC) refinements study on emission factors. To align the Carbon Tax Act with these guidelines, it is proposed that tables are added to Table 1 and Table 2 of Schedule 1 of the Carbon Tax Act to provide the tier 2 emission factors and default emission factors for fugitive emissions.

*Comment:* The Draft TLAB published, the Net Calorific Values (NCVs) in Schedule 1, Table 1 which are reflected in TJ/tonne. The TJ/tonne for petrol, diesel and jet kerosene have been incorrectly calculated. The litres have not been converted into kilograms using the densities. This must be done to ensure the NCVs in Schedule 1, Table 1 are correctly reflected. It is recommended that each country-specific NCV in Table of Schedule 1 of the Carbon Tax Act should have its own units specified next to it in order to align with Table D.1. in the Methodological Guidelines.

*Comment:* There was a suggestion for improved collaboration between the South

African Revenue Service, Department of Forestry, Fisheries and the Environment and the National Treasury to ensure that the GHG emissions methodological frameworks align with the prescribed carbon mitigation system, thereby establishing a clear basis for the prescribed methods.

*Response: Accepted.* Considering the comments by stakeholders and to ensure the appropriate alignment of the Carbon Tax Act Schedules and the DFFE technical guidelines, it is proposed that the table on country specific carbon dioxide emission factors is withdrawn from the TLAB. Further consultations will be held with DFFE and SARS on the application of the tier 2 emission factors and determination of the appropriate net calorific values to be used for the different fuel types and for calculation of greenhouse gas emissions under the Carbon Tax Act. It is also proposed that the table on the default emission factors for fugitive emissions from coal mining, oil and gas operations is withdrawn. Further announcements will be made in Budget 2024. For purposes of the Act, taxpayers can use the default factors in Schedule 1 to calculate their greenhouse gas emission where appropriate, and in terms of section 4(1) emissions can be determined using the emissions determination methodology as approved by the DFFE.

## **7. INCOME TAX: INDIVIDUALS, SAVINGS AND EMPLOYMENT**

### **7.1. Apportioning the tax-free investment contribution & retirement contribution**

(Main reference: Sections 11F and 12T of the Income Tax Act: Clauses 13 and 20 of the Draft TLAB)

In 2022 changes were made in the Act to provide that when an individual ceases to be a South African tax resident, the annual interest exemption available to individuals in terms of section 10(1)(i) is apportioned; and the capital gains tax annual exclusion available to individuals in terms of paragraph 5(1) of the Eighth Schedule to the Act is limited. The main aim of the above-mentioned changes was to address an anomaly that arises because of the two years of assessment which are created during a single 12-month tax period when an individual ceases to be a South African tax resident.

It has come to Government's attention that there are other provisions in the Act that contain inconsistencies as a result of the two years of assessment created during a single 12-month period when an individual ceases to be a South African tax resident. These provisions include section 12T(4)(a) of the Act which limits the annual contributions that can be made to a Tax Free Savings Account (TFSA) should an individual wish to have returns from such investment fully exempt, and section 11F(2) of the Act which makes provision for the deduction of aggregate amounts contributed to a retirement fund.

As a result of an individual having two years of assessment in a single 12-month tax period when he or she ceases to be a South African tax resident, the individual may double-up on the TFSA annual contribution limitation as well as the amount utilised to calculate the allowable section 11F deduction. To address this anomaly and ensure alignment with other provisions of the Act, it is proposed that changes be made to section 12T(4)(a) and section 11F(2) of the Act to apportion the TFSA contribution limitation and limit the amount utilised to calculate the allowable retirement contribution deduction in the above instances.

*Comment:* Apportioning on a days basis is not appropriate, consideration should be given to rather drafting the legislation in such a manner that the R350 000 is capped in any 12-month period.

*Response:* Accepted. Amendments will be made to the draft legislation to ensure that the apportionment is calculated based on the principle of capping the available amount in any 12-month period.

*Comment:* Apportioning on a days basis is not appropriate, consideration should be given to rather drafting the legislation in such a manner that the R36 000 is capped in any 12-month period. Further to the above, the apportionment should not apply to the lifetime contribution limit.

*Response:* Accepted. Amendments will be made to the draft legislation to ensure that the apportionment is calculated based on the principle of capping the available amount in any 12-month period.

*Comment:* Consequential amendments are required to section 12T(7) of the Act to ensure that the penalty is correctly calculated in instances where an individual contributes in excess of the annual contribution limit.

*Response:* Accepted. Amendments will be made to the draft legislation to ensure that the relevant penalty is correctly calculated.

## **7.2. Clarifying anti-avoidance rules for low-interest or interest free-loans to trusts**

(Main reference: Section 7C of the Income Tax Act: Clause 3 of the Draft TLAB)

The Act contains anti-avoidance rules aimed at curbing the tax-free transfer of wealth to trusts using low-interest or interest-free loans, advances or credit. These rules deem any interest foregone in respect of a transfer for low-interest or interest-free loans, advances or credit to a trust to be a donation subject to a donations tax where the deemed donation is calculated as the amount by which the official rate of interest exceeds any amount of interest incurred in this regard.

These anti-avoidance rules have certain exclusions. For example, the rules do not apply if the low-interest or interest-free loan, advance or credit is used to purchase a

primary residence for the person advancing that low-interest or interest-free loan, advance or credit to the trust, company or spouse of such person.

It has also come to government's attention that:

- The above-mentioned exclusion does not fully encompass what constitutes a primary residence in terms of the Eighth Schedule to the Act; and
- In instances where the low-interest or interest-free loan, advance or credit is denominated in foreign currency, the rules do not provide clarity on how and when this amount should be translated to South African rands.

Proposed amendments to the legislation were included in the Draft TLAB to provide clarity in this regard.

*Comment:* Given possible monthly payments of interest of funding advanced under the arrangements that are subject to section 7C of the Act as well as possible periodic repayments of capital amounts during the year, translation of the deemed donation at the average rate is more appropriate. Furthermore, it should be the lender doing the translation and not the borrower.

*Response: Accepted.* Changes will be made to the Draft TLAB to firstly, focus on the person contemplated in subsection (1), (1A) and (1B) as the party responsible for the translation of amounts that are to be treated as donations which denominated in a currency other than that of the Republic and secondly, provide for such translation to be effected by applying the average exchange rate for the relevant year of assessment.

*Comment:* The proposal to fully encompass the intended scope of a primary residence is not achieved under the proposed provision as it does not consider improvements made of the acquired property.

*Response: Accepted.* Changes will be made to include funding advanced to effect improvements undertaken on a primary residence.

*Comment:* The proposed amendment to expand the exclusion for debt used to fund primary residences is welcomed. However, the practicality for linking this to paragraph 46 of the Eighth Schedule to the Act is questionable and may lead to uncertainties. Paragraph 46 of the Eighth Schedule to the Act seeks to limit the primary residence exclusion for CGT purposes where the size of the property exceeds 2 hectares and/or where a portion of the land disposed of is not used mainly for domestic or private purposes. On the other hand, the provisions of section 7C of the Act in question relates to the funding of the acquisition or improvement of a primary residence where the debt funding remains outstanding while the asset is still held. The intension to expand the exclusion to include land used for domestic or personal purposes should be clearly set out in the provisions of section 7C of the Act.

*Response: Accepted.* Changes will be made to clarify that a loan, advance or

credit used to acquire or to fund an improvement of a primary residence or land on which it is situated is excluded from the application of the anti-avoidance measure, where, that primary residence and the land on which it is situated (including unconsolidated adjacent land) as does not exceed two hectares are used together mainly for domestic or private purposes.

### **7.3. Solar energy tax credit**

(Main reference: New section 6C and section 25 of the Income Tax Act: Clauses 2 and 28 of the Draft TLAB)

The tax system does not generally allow for deductions in respect of personal consumption, for example, expenses incurred in respect of a motor vehicle used for private purposes or expenses incurred in respect of a salary paid to a domestic worker.

However, in certain circumstances, either for purposes of encouraging individuals to save for retirement or for philanthropic purposes, or in instances where the expenditure is directly linked to employment income, the Act allows individuals who derive employment income, and or passive income, a credit or deduction in respect of a limited number of expenses.

In response to the severe energy crisis currently being experienced by the country, Government is proposing various policy measures to the renewable energy mix to improve energy efficiency and reduce pressure on the electricity grid. To encourage households to invest in clean electricity generation capacity, which can supplement electricity supply, Government proposed a rooftop solar tax incentive for individuals who invest in solar photovoltaic (PV) panels.

It is proposed that individuals who are liable for personal income tax be granted a solar energy tax credit, which will apply as follows:

- To new and unused solar PV panels brought into use for the first time on or after 1 March 2023 and before 1 March 2024, with a generation capacity of not less than 275W each. The solar PV panels should form part of a system that is connected to the distribution board of a residence that is mainly used for domestic purposes and in respect of which an electrical certificate of compliance is issued.
- The credit will only be available for a 1 year period.
- The allowable credit is calculated as 25 per cent of the cost of the solar PV panels, up to a maximum of R15 000.
- The credit is available to any individual who owns, rents or occupies a residence to which the panels are affixed, and has also incurred the costs of the panels.
- To ensure that there is no duplication of tax incentives in respect of a solar PV panel, the energy tax credit shall not be allowed for a solar PV panel in

respect of which an allowance is granted in terms of sections 12B or 12BA of the Act.

- Where an individual sells a solar PV panel on or before 1 March 2025 that qualified for a solar energy tax credit, the amount of the solar energy tax credit that was allowed as a deduction in respect of the solar PV panel will be regarded as an additional amount of normal tax payable by that individual in the year of assessment in which he or she sold the solar PV panel.
- However, there will be no recoupment of the amount of the solar energy tax credit that was allowed as a deduction if the individual disposes of or vacates the residence to which the solar PV panel is affixed.

*Comment:* High level of general support for the rebate and the objective to increase residential solar power generation. There was also specific support for the inclusion of expansion of existing systems.

*Response:* Noted. The comment is noted.

*Comment:* A tax incentive through the PIT system will only benefit the upper income groups.

*Response:* Noted. The personal income tax system is indeed highly progressive, including a relatively high tax threshold. This measure takes the form of a rebate to ensure that the benefit is equalised for all taxpayers who can claim the incentive. This measure is part of a policy package from Government, which also includes support for other affordable options (like the Energy Bounce Back loan guarantee scheme and on-budget support for specific projects.)

*Comment:* The objective would be better met through a VAT zero-rating of solar panels.

*Response:* Not accepted. Beyond the fact that VAT zero-rating have impact far beyond residential use, there is no evidence that the benefits of previous zero-rating were passed on to consumers.

*Comment:* A duration of 1 year is insufficient time for the incentive to be effective. Reasons included the time required for households to plan, save and acquire expensive components and engage contractors; the legislative process itself takes almost a year; and the scope of the electricity problem.

*Response:* Not accepted. The rebate will only be available for 1 year to incentivise the fastest possible mobilisation of additional generation at residences with urgency. An extension would add to a pressurised fiscal position. Moreover, the large increase in solar panel imports in the first 2 quarters of 2023 suggests that behaviour has been very responsive. Tax incentives tend to work best when they are targeted and temporary.

*Comment:* Clarify claims under diplomatic privileges and immunities.

*Response:* Comment misplaced. The taxpayer must have a tax liability to offset the rebate against.

*Comment:* In order for the incentive to be more effective, the cap should be removed (or increased).

*Response:* Not accepted. The cap represents a value that is fiscally responsible while still significant to taxpayers. There were also some commentators that supported the cap on equity grounds.

*Comment:* Increase the percentage of the cost of solar PV panels that determines the value of the credit.

*Response:* Not accepted. This impedes fiscal affordability. The percentage implies that Government subsidises 1 in 4 panels bought and installed (up to a value of R60 000).

*Comment:* Limiting the incentive to only solar panels is too restrictive. Suggestions for additions included: batteries, inverters, installation costs and solar geysers. The main contention was that these components work as a system. Another strain of comments to the same effect suggested aligning the eligible components to that of the energy generation incentives available to businesses. An alternative suggestion was to make batteries a prerequisite to claim the incentive (for panels and batteries).

*Response:* Not accepted. The rebate is aimed at expanding generation capacity – and the component in solar PV systems that is most closely related to that objective is the panels. Indeed, batteries and inverters do not require the installation with panels – in which case it increases demand from the electrical grid (with no additional supply). The batteries, inverters and installation costs are certainly required for panels to be effective, but they are also the components with the highest private benefit (to avoid the impacts of loadshedding) and lowest public benefit (as it does not benefit anyone else beyond the residents of the dwelling). This is also the main difference between residential use and the energy use of a business: customers and employees are reliant on a business' ability to remain operational during load shedding. A system of prerequisites would impose a very high administrative burden – while the current design is simple to administer and understand.

*Comment:* Remove requirement to obtaining a Certificate of Compliance, as it is costly and takes long.

*Response:* Not accepted. It is an existing regulatory requirement, Government cannot incentivise unsafe installations. Government notes the potential delays, which should not pose any difficulties if the certificate is still issued during the same year of assessment. Government will monitor developments and any potential administrative remedies.

*Comment:* In the case of home rental, the Certificate of Compliance may not be issued in the name of the renter who may want to claim the rebate (but in the name of the owner).

*Response:* Accepted. In such cases, the supporting documentation to claim the incentive should include a rental agreement to indicate the names of the renter and the owner.

*Comment:* Extend to “rent-to-buy” and asset leasing arrangements.

*Response:* Not accepted. The personal income tax system is ill-equipped for a rebate in those circumstances. To keep the incentive as simple as possible to understand and administer, it pertains to assets that are acquired (in full) and brought into use. Alternative mechanisms – like the Energy Bounce Back guarantee scheme – are better placed to support such arrangements.

*Comment:* The recoupment and apportionment provisions – while well-intentioned – introduce a lot of unintended complexity to the extent that the additional administrative burden outweighs gains in compliance.

*Response:* Accepted. The draft legislation will be amended to effect the deletion of the relevant provisions.

#### **7.4. Clarifying the amount of employer contribution to a retirement fund to be deductible**

(Main reference: Section 11F of the Income Tax Act: Clause 13 of the Draft TLAB)

Section 11F(4) of the Act, read together with paragraphs 2(h), 2(l), 12D and 13 of the Seventh Schedule to the Act makes provision for contributions made by the employer to a retirement fund, made on behalf of an employee, to be regarded as an amount equal to the cash equivalent of the value of the taxable fringe benefit and also to be taxable in the employee’s hands. In accordance with section 11F(4) of the Act, amounts paid or contributed by an employer to a retirement fund on behalf of an employee are deemed to have been contributed by the employee and are therefore taken into consideration when determining the employee’s allowable deduction in terms of section 11F of the Act. Currently, section 11F(4) of the Act does not have a requirement that the cash equivalent (so calculated as employer contributions to a retirement fund on behalf of an employee) be included in the employee’s income when determining the allowable deduction in terms of section 11F of the Act. As a result, even if an employer’s contribution to the retirement fund is not subject to fringe benefit tax because the employee’s remuneration qualifies for income tax exemption in terms of section 10(1)(o)(ii) of the Act, the employee may still be entitled to a deduction in terms of section 11F of the Act. This anomaly therefore creates a scenario where an employee may be entitled to a deduction of the employer contribution in terms of section 11F of the Act, even though the employee was not

subject to fringe benefit tax on that contribution. Further to the above, if all their income is tax exempt, the employer contribution may be carried forward to withdrawal or retirement from their respective retirement fund and be allowed as a deduction against the employee's lump sum or annuity, this again, without the employee having been taxed on such employer contribution. The above anomaly goes against the policy intent. As is evident in sections 6A and 6B of the Act (which deal with the allowable medical tax credits), the policy intent is for a deduction or tax credit to only be afforded to amounts included in the taxpayer's income (i.e., a deduction or tax credit should not be available for tax exempt amounts).

To address this anomaly and ensure parity with other provisions of the Act, it is proposed that changes be made in section 11F(4) of the Act so that the deduction in terms of this section only apply to the extent that the cash equivalent (so calculated as employer contributions to a retirement fund on behalf of an employee) is included in the employee's income as a taxable benefit.

*Comment:* The effective date as relates to the requirement that the deduction is only allowed for taxable contributions seems overly generous. The effective date should rather be retrospective from 1 March 2023.

*Response:* Noted. However, the prospective effective date is to afford affected parties the ability to effect the necessary system changes by the implementation date.

## **7.5. Transfers between retirement funds by members who are 55 years or older**

(Main reference: Section 1, definition "pension fund" and "provident fund" and paragraph 6A of the Second Schedule to the Income Tax Act: Clause 1 of the Draft TLAB)

Paragraph 2(1)(c) of the Second Schedule to the Act regulates the amount to be included in gross income for any year of assessment, namely, any amount transferred for the benefit of a member of a retirement fund on or after normal retirement age (as defined in the rules of the fund), but before retirement date (as defined in section 1(1) of the Act), less any deductions allowed under paragraph 6A of the Second Schedule to the Act. With effect from 1 March 2022 transfers into a similar fund by a member of a pension preservation or provident preservation fund (who has reached normal retirement age in terms of the fund rules but has not yet opted to retire from the respective fund) were also included in the ambit of Paragraph 6A of the Second Schedule to the Act. As a result, any individual transfers between preservation funds where the transfer is between similar funds and the member involved has reached normal retirement age in terms of the fund rules but has not yet opted to retire from the relevant fund, are tax-free.

It has come to Government's attention that there are some instances where active contributing pension and provident fund members (who have reached normal retirement age in terms of the fund rules but have not yet opted to retire from the

respective fund) are being subjected to involuntary transfers to another pension or provident fund, and such transfers are being subjected to tax. To address this issue and ensure parity amongst members of retirement funds who have reached normal retirement age in terms of the fund rules but have not yet opted to retire from their respective fund, and are subject to an involuntary transfer, it is proposed that the following changes be made in the Act: (i) members of pension or provident funds who have reached normal retirement age as stipulated in the fund rules, but have not yet opted to retire from said fund, and are subject to an involuntary transfer, are able to have their retirement interest transferred from a less restrictive fund to an equally or more restrictive retirement fund without incurring a tax liability; and (ii) the value of the retirement interest, including any growth thereon, will remain ring-fenced and preserved in the receiving pension or provident fund until the member elects to retire from that fund. This means that these members will not be entitled to the payment of a withdrawal benefit in respect of the amount transferred.

*Comment:* The interaction between the proposed amendment (more specifically the ring-fencing requirement in the transferee fund) and the two-pots regime is unclear, clarity in this regard is sought.

*Response:* Noted. The draft legislation in the draft TLAB is based on the current status quo, the interaction between this proposal and the two-pots regime will be clarified in the subsequent version of the RLAB.

*Comment:* The rationale for preventing withdrawals from the transferee fund is unclear, clarity in this regard is sought as we are of the view that members should be allowed to withdraw from the transferee fund irrespective of whether or not they have reached normal retirement age.

*Response:* Noted. In the event that the amount had been transferred to a preservation fund or retirement annuity fund, a once-off withdrawal would not be possible. As such and based on the desire to ensure parity between various fund types, transfers to occupational funds are therefore subject to the withdrawal limitation.

*Comment:* Reference to members over the age of 55 in the Explanatory Memorandum should be removed as occupational funds have a higher normal retirement age. Further to the above, legislative drafting in paragraph 6A of the Second Schedule to the Act should specifically refer to a pension fund.

*Response:* Accepted. The Explanatory Memorandum heading will be amended accordingly. Further to the above, the draft legislation as relates to the proposed amendment to paragraph 6A of the Second Schedule to the Act shall be amended to refer to a pension fund as opposed to the current wording which reads “.....pension or preservation fund”.

*Comment:* The current retirement interest definition does not cater for transfers between occupational funds, this is required to give proper effect to the proposed

amendment. Further to the above, additional amendments are also required to paragraph (ii)(dd) of the provisos to the pension and provident fund definitions.

*Response:* Accepted. Amendments will be made to the draft legislation to incorporate the necessary changes to the retirement interest, pension fund, and provident fund definitions.

*Comment:* Paragraph 2(1)(c) of the Second Schedule to the Act currently references the transfer of an amount (which is currently not a defined term) and not that of a retirement interest. An amendment is required to ensure reference to a retirement interest.

*Response:* Not accepted. Reference to an amount fully caters for the transfer of a retirement interest as a retirement interest is in and of itself an amount. Further to the above, it is common cause that any terminology that is not defined in the Act bears its ordinary meaning.

*Comment:* The Explanatory Memorandum only makes reference to active members being affected by this scenario, this is however not the case as other members may also be impacted.

*Response:* Accepted. Given the understanding that inactive members may also be affected, the Explanatory Memorandum shall be amended to indicate as such.

*Comment:* The proposed amendment does not cater for transfers between retirement annuity funds, these should also be catered for.

*Response:* Noted. The argument that there should be parity between the treatment on various funds is noted. Given the fact that the announcement made in the 2023 Budget Review only catered for occupational funds, retirement annuity funds have not been included in this legislative cycle. Commentators are welcome to include submissions for the inclusion of retirement annuity funds as part of future legislative cycles.

*Comment:* There is uncertainty with regard to whether the proposed amendment is intended to only apply to involuntary transfers as the Explanatory Memorandum references involuntary transfers while the draft legislations does not.

*Response:* Noted. The intention is for the amendment to only apply to involuntary transfers, the draft legislation shall be amended to reflect this. This amendment does not preclude members of retirement funds from making voluntary transfers to a preservation fund or a retirement annuity fund.

## 8. INCOME TAX: GENERAL BUSINESS TAX

### 8.1. Reviewing the principles of practice note 31 of 1994

(Main reference: New section 11G of the Income Tax Act: Clause 14 of the Draft TLAB)

In 1994, Practice Note 31 of 1994, titled “Interest paid on moneys borrowed” was issued. On 16 November 2022, the South African Revenue Service (SARS) issued a notice informing the public of the intention to withdraw this practice note, with effect from years of assessment starting on or after 1 March 2023 due to the increasing abuse of the tax deduction concession provided for in Practice Note 31.

After reviewing the public comments received on the withdrawal of the practice notes, government considered the impact of the proposed withdrawal and is proposing changes to tax legislation to accommodate legitimate transactions affected by such withdrawal. As a general principle, deductions are allowed where the requirements of the general deduction formula is met (i.e. trade requirement, income production requirement and revenue nature requirement). Where one of these is not satisfied and a deduction is justified and intended, specific rules are introduced (for example section 24O of the Act that allows for the deduction of interest in respect of share acquisitions in qualifying operating companies).

As such, the practice under Practice Note 31 was limited to minimise the adverse effect of withdrawal on companies and proposed legislation was included in the Draft TLAB that was published for public comment to allow for a deduction of interest where one company within a group of companies raises debt that it on-lends to a fellow group company that uses the debt for income producing purposes within its trade. Any deduction in this regard is limited to the interest income accruing directly or indirectly from that other company during that year of assessment.

#### **Comments raised in written submissions**

*Comment:* The proposed concession under section 11G provides that for an amount to be deductible against interest income, such amount should not be of a capital nature. In addition, the Income Tax Act already contains rules in section 24J for the deduction of borrowing costs. The scope of the interest that is eligible for deduction under section 11G should be comparable to that which is eligible for deduction under section 24J of the Act. As such, it is proposed that reference be made to the definition of interest as set out under section 24J of the Act and that no regard should be given to whether the amount to be deducted is of a capital nature or not.

*Response:* Accepted. Changes will be made to the Draft TLAB to ensure that the borrowing costs eligible under section 11G are comparable to those eligible for deduction under section 24J by referring to the definition of “interest” in section 24J of the Act. The requirement that the interest should not be of a capital nature will be withdrawn.

*Comment:* The proposal under section 11G is extremely limited in that it caters for back-to-back lending arrangements within a group of companies. This proposal results in back-to-back lending arrangements that involve trusts and natural persons that are partners in professional firms and shareholders not being able to raise debt funding necessary for their businesses or firms without the unjustified tax leakage that would arise in the absence of a concession similar to that granted by Practice Note 31. In addition, by limiting the relief to lending arrangements between groups of companies, many arrangements between parties where the lender holds less than 70 per cent of the equity shares in the borrower are excluded. Amongst these are funding arrangements involving BEE partners and limited partners of private equity funds where the shareholdings are considerably lower.

*Response:* Noted. It is Government's intention that access to business funding should not be adversely affected by the proposed withdrawal of practice note 31. As a result, the concession contained in section 11G will be expanded to apply to any person that incurs interest expenditure in the production of interest income (limited to said interest income) without regard to any shareholding threshold of any back-to-back lending arrangement.

**Comments raised during public workshops hosted by National Treasury and the public hearing of the Standing Committee on Finance**

*Comment:* It is welcomed and noted that Government intends to ensure that access to funding for business purposes (whether raised by corporates, natural persons or trusts) should not be negatively impacted. However, it is equally concerning that the same concession is not being extended to back-to-back lending arrangements entered into to raise funding to cover personal expenses or the acquisition of personal use assets. These arrangements do not result in any tax avoidance but rather ensure that the natural person that is able to raise debt with a lending institution to on-lend to another (typically a child or relative that would otherwise not be able to access such debt) is not unfairly taxed on interest income that is merely passed on to the lending institution (and will consequently be subject to tax in its hands) while the ultimate user of the debt funding to fund expenditure of a personal nature will also not eligible to deduct the interest expense he or she incurs.

*Response:* Noted. The introduction and continued existence of the interest exemption the was intended, despite the absence of business activities, also to limit any tax liability that may arise in the hands of a natural person that earns interest income outside of a trade. It is noted that the interest exemption may be at a level much lower than the interest income that may arise under some of the lending arrangements of concern. As such, there will be no exclusion in respect of natural persons entering into back-to-back arrangements to fund personal expenditure. It is noted, that further consultation on the proposed section 11G may be desired by taxpayers on the amended provisions of section 11G. It is therefore proposed that section 11G should only come into effect on 1 January 2025 in respect of years of assessments commencing on or after that date. In the

interim, Practice Note 31 will remain in effect until this newly proposed effective date.

## **8.2. Clarifying anti-avoidance rules dealing with third-party backed shares**

(Main reference: Section 8EA of the Income Tax Act: Clause 5 of the Draft TLAB)

The Act contains anti-avoidance rules targeting debt-like equity instruments – for example, third-party backed shares – and deems any dividend or foreign dividend received by or accrued to any person in respect of a third-party backed share as income. The anti-avoidance rules do not apply if the funds derived from the issue of the shares in question are used for a qualifying purpose. The qualifying purpose test, generally, is when there is a direct or indirect acquisition of an equity instrument in a company that is an operating company at the time of the receipt or accrual of any dividend or foreign dividend in respect of that equity instrument.

The current wording of the Act could result in certain dividends or foreign dividends received by or accrued in respect of a third-party backed share not being deemed as income when the shares in that operating company are no longer held by the person who initially acquired them, at the time of the receipt or accrual of any dividend or foreign dividend. It is proposed that the legislation be amended to:

- specifically introduce an ownership requirement, of the equity shares in the targeted operational company by the person that acquired those equity shares, at the time of the receipt or accrual of any dividend or foreign dividend; and
- limit the structuring around these anti-avoidance rules through the retrospective effective date of these amendments.

*Comment:* The proposed ownership requirement intends that the original equity shares held in the targeted operating company that were acquired using the proceeds from the preference shares subscription must be held at the time of receipt or accrual of any dividend. The new ownership requirement will affect many commercially driven transactions which is not intended to undermine the fiscus. There are various legitimate commercial reasons why a disposal or substitution of the equity shares held in an operating company should be allowed, including:

- Disposal of operating company equity shares for the full or partial redemption of over-arching preference shares;
- Part disposal of operating company equity shares to meet scheduled dividend payments of the over-arching preference shares;
- Disposal of operating company equity shares to acquire equity shares in a different more profitable operating company;
- Corporate actions (e.g. share-for-share transaction) on the operating company equity shares outside the control of any of the parties involved; or
- Intra-group restructures.

*Response:* Partially accepted. Section 8EA of the Act is an anti-avoidance measure with intentional structured exceptions to cater for the limited application

of a qualifying purpose of the funds derived from the issue of preference shares. To balance the integrity of the anti-avoidance measure but to also acknowledge the commercial reality of preference shares changes will be made in the 2023 draft TLAB to cater for certain corporate actions and identified commercial transactions when applying the new ownership requirements.

*Comment:* The proposed amendment is retrospective and is deemed to have come into operation on 31 July 2023. The impact of the proposed effective date is that it applies in respect of dividends and foreign dividends received or accrued during years of assessment ending on or after that date, which means that the amendment will apply to existing structures (i.e. it will apply to existing structures where the equity shares in the "operating company" may no longer be held by the preference share issuer, and will taint any dividends declared in respect of such preference shares going forward). As such, it may not be possible for affected preference shares issuers to arrange their affairs to comply with the amended provisions.

*Response:* Noted. Given the required amendments around identified and accepted public submissions pertaining to the draft 2023 TLAB, changes will be made in the 2023 Draft TLAB to postpone the effective date from 30 July 2023 to 1 January 2024 where it will apply in respect of any dividend or foreign dividend received or accrued during years of assessment commencing on or after that date.

### **8.3. Addressing the abuse of the definition of contributed tax capital**

(Main reference: Section 1, definition of contributed tax capital of the Income Tax Act: Clause 1 of the Draft TLAB)

The contributed tax capital (CTC) of any company is a notional and ring-fenced tax amount derived from either contributions made to a resident company by shareholders for the issue of a class of shares or as an deemed market value amount when a foreign company becomes a South African resident for tax purposes. It is reduced by any amounts referred to as capital distributions, transferred by the company to the shareholders.

Government has identified a structure where a foreign holding company (FH Co) that holds shares in a valuable South African operating company (SA Co) through a foreign intermediary company (FI Co) could avoid dividends tax by changing the tax residency of FI Co to South Africa.

When this takes place, the CTC in the hands of FI Co is recognised as an amount equal to the market value of its shares in SA Co. The SA Co then distributes dividends to the new South African tax resident intermediate company (FI Co), and those dividends are exempt from tax because dividends between South African companies are not subject to tax. When FI Co makes distributions to FH Co, the distributions are shielded by CTC and regarded as capital distributions, and are then not subject to dividends tax for the FH Co.

The offending structure does not create any additional investment or benefit into the South Africa economy but merely changes the tax status of the foreign intermediary to that of a South African tax resident by replacing its foreign directors with SA directors which effectively changes its place of effective management to South Africa. This leads to a permanent erosion of the South African tax base as these capital distributions are now not subject to tax. To address this abuse, it is proposed that amendments be made to the tax legislation.

*Comment:* There is a perceived lack of clarity on the effective date of the proposed provision which as a result could be interpreted to mean that the provision is also applicable to any change of tax residence prior to the effective date of 1 January 2024.

*Response:* Accepted. Effective date will be amended so that the amendment will apply to any company becoming a resident on or after 1 January 2024.

*Comment:* If the migration of the tax residence to SA is done solely or mainly for purposes of obtaining a tax benefit then available tools like GAAR should be used instead of additional targeted rules that inevitably could have unintended consequences.

*Response:* Not accepted. Addressing tax avoidance structures by the fiscus requires a multi-faceted approach including dedicated and identified anti-avoidance measures, GAAR and enforcement.

*Comment:* There are possible instances where a company migrating to South Africa could be worse off than is the case prior to the migration due to the proposed amendment. As such, the CTC of the migrating company should not be less than that of its SA resident subsidiary companies, similar to the provisions of section 8G of the Act.

*Response:* Accepted. Changes will be made to the 2023 Draft TLAB to ensure that the proposed provisions would still limit the potential for mischief yet acknowledge the value of available CTC of resident companies in scenarios where the foreign company directly holds at least 50% of the equity shares or voting rights in each of those resident companies immediately before the date on which that foreign company becomes a tax resident in South Africa.

#### **8.4. Translating contributed tax capital from foreign currency to rands**

(Main reference: New section 25E of the Income Tax Act: Clause 30 of the Draft TLAB)

CTC, in the case of a foreign company, is an amount equal to the market value of all the shares in that company of that class immediately before the date on which that company becomes a resident and the consideration received by or accrued to that company in exchange for the issue of shares of a particular class, on or after the date

on which that company became a resident of South Africa. It is reduced by any amounts referred to as capital distributions, transferred by the company to the shareholders. When a company changes its tax residence to South Africa, it is possible for that company's functional currency and share capital to be denominated in a currency other than the Rand.

The Act contains specific rules dealing with the translation of amounts received by or accrued to, or expenditure or loss incurred by a person, denominated in foreign currency to Rand. However, these rules do not specifically cater for the translation of contributed tax capital to Rand.

It is proposed that rules be introduced for the translation of the elements of CTC from a foreign currency to the currency of the Republic. More specifically, the proposed amendments will require that companies to apply the applicable spot rate on the date that the relevant amount is recognised for income tax purposes.

*Comment:* Whilst there is no objection to the proposed insertion of section 25E in the Act for the translation of CTC denominated in foreign currency to Rands, the proposed legislation seems to unintentionally only cover scenarios where there is a change in tax residency to South Africa with an accompanying change in the functional currency to Rand at that point. As such, it is unclear from the wording of the proposed provision whether the amount of CTC returned to a shareholder, when the taxpayer is a tax resident in South Africa with a functional currency other than Rand, should be translated into Rand at the spot rate at the date of transfer or whether the spot rate on the date when the CTC was created should be used, so as to determine a rand amount of CTC available for distribution that would not be affected by subsequent currency fluctuations.

*Response:* Accepted. It is proposed that the effective date be postponed to 1 January 2025 in an effort to facilitate the extension of the proposed provisions to various possible different scenarios.

*Comment:* Why a proposed stand-alone section 25E within the Act? The proposed translation rule should be included in the definition of CTC or alternatively in the existing ambit of section 25D of the Act that currently deals with the translation of certain amounts.

*Response:* Not accepted. The current drafting style, structure and placement best facilitates an ease of distinction and understanding within the Act. However, it is proposed that the effective date be postponed to 1 January 2025.

*Comment:* The translation methodology should apply to both paragraphs (a) and (b) of the definition of CTC. A company that is incorporated in a foreign jurisdiction (i.e. shares issued in a foreign currency) but that has been a tax resident in South Africa since its inception should be allowed to maintain its CTC in that foreign currency.

*Response:* Accepted. The proposed provisions of section 25E of the Act will be extended to also cover paragraph (b) of the CTC definition. However, it is

proposed that the effective date be postponed to 1 January 2025.

*Comment:* It should be considered to rather provide taxpayers with the option to choose the translation methodology by allowing taxpayers (companies) to elect between the spot rate or an average yearly rate when determining CTC for income tax purposes.

*Response:* Not accepted. Although a separate new section is proposed, the provisions in question follow the accepted tax principles and rationale already contained section 25D of the Act that generally limits taxpayers (and more specifically companies – as only they have the ability to issue CTC) to the application of spot rate when translating from a functional currency other than the Rand. However, it is proposed that the effective date be postponed to 1 January 2025.

## **8.5. Clarification of the interest limitation rules**

(Main reference: Section 23M of the Income Tax Act: Clause 26 of the Draft TLAB)

In 2021, changes were made to the Act as part of the corporate income tax package to broaden the tax base and reduce the headline corporate income tax rate in a revenue neutral manner. One of these measures included strengthening the rules dealing with the limitation of interest deductions for debts owed to certain persons not subject to tax in section 23M of the Act.

Government received requests for further clarity on these rules and the 2023 Budget outlined several issues that would be considered. These include, for example, how assessed losses are considered in the definition of “adjusted taxable income”, whether a definition for “creditor” is required, and if the definition of “controlling relationship” is appropriate.

It is proposed that legislation be amended to align with the policy intent of adding only the balance of assessed losses from prior years to taxable income. The starting point for adjusted taxable income should be taxable income calculated before applying section 23M of the Act and setting off any assessed loss.

It is proposed that the definition of the term "creditor" be included in section 23M to clarify that any person to whom interest is payable is considered a creditor for the purpose of the section.

To address the uncertainty arising from the treatment of exchange gains and losses, it is proposed that exchange gains be classified as interest received or accrued for the purposes of section 23M of the Act.

Government has considered how the definition of “controlling relationship” in section 23M(1) of the Act and the provisions of 23M(2) of the Act interact in light of the

intended policy outcome, and proposes to retain the current stance.

Government proposes that the legislation be clarified to make it clear that the proviso to section 23M(2) is only applicable to interest when the recipient is a non-resident.

Government proposes that section 23M(6) of the Act be amended to extend the exclusion for lending institutions to apply to South African banks.

*Comment:* The proposed changes to adjusted taxable income with respect to how assessed losses are incorporated are ambiguous and require further clarity. For example, there appears to be a potential circular reference between section 23M and section 20 of the Act. In addition, it is not clear whether it is the balance of assessed loss struck at the end of the current year or carried forward from the preceding year that should be added back; and whether “taxable income” and “adjusted taxable income” can be a negative amount.

*Response:* Accepted. The policy objective is to start the “adjusted taxable income” calculation with taxable income for the current year of assessment. Accordingly, the definition of adjusted taxable income will clarify that it is the balance of assessed loss that has been carried forward from the preceding year of assessment that is to be added back. Consequently, the need to add back the amounts contemplated in paragraph (b)(iii) of this definition will no longer be necessary and the paragraph will be deleted. It is recognised that applying the interest limitation rule is problematic if “adjusted taxable income” is a negative number. For this reason, changes will be made to clarify that “adjusted taxable income” may not be less than zero. However, government sees it appropriate for taxable income (before setting of any balance of assessed loss that has been carried forward from the preceding year of assessment) to be less than zero. Deeming taxable income to be zero would create inequity between a taxpayer that has a taxable profit and a taxpayer that has a taxable loss. If, for example, a taxpayer’s taxable loss for the current year of assessment is R100 – deeming that to be zero may result in “adjusted taxable income” being R100 more. This contrasts with the taxpayer with a positive taxable income that has no means of increasing “adjusted taxable income”. This is in line with the policy intent of 23M, which is to consider the company’s ability to cover their interest payments relative to their earnings.

*Comment:* While not included in the draft 2023 TLAB, there were requests for clarity on the ordering of section 23M with respect to other provisions that deal with a percentage or portion of taxable income, such as section 18A and section 23A of the Act.

*Response:* Noted. Section 23M should be applied last – after all other provisions of the Act that base certain deductions or other amounts on a specified amount of taxable income.

*Comment:* The proposed substitution of paragraph (b) of the definition of controlling

relationship is not aligned between the EM and draft 2023 TLAB. furthermore, paragraph (b) both in its current form and revised form appears to be redundant.

*Response: Accepted.* The proposed substitution may not make any difference to the interpretation of the definition of “controlling relationship” and paragraph (b) will rather be deleted.

*Comment:* The proposed definition of a creditor needs to be revisited. Given the broad definition of interest for the purposes of section 23M, not all interest is ‘payable’, e.g. interest constituting an exchange difference. Nor does an exchange loss incurred by a debtor necessarily translate to a corresponding accrual for the counterparty.

*Response: Accepted.* The definition of creditor will be amended to mean a person to whom a debtor owes a debt. It is noteworthy to highlight to taxpayers that for purposes of this amended definition, the defined terms of debtor and debt contained in section 23M are relied upon to include amounts that would not be covered by the ordinary meaning of debt that is owed such as exchange differences that are included within the ambit of section 23M.

*Comment:* The objective in respect of the proposed changes to the proviso to section 23M(2) of the Act is not clear. If it is implemented, there will be arbitrage between taxpayers that obtain funding directly from the creditor and interest withholding tax is payable, and companies that procure funding on a back-to-back basis.

*Response: Not accepted.* Firstly, it necessary to retain the proposed amendment to clarify that interest in respect of domestic loans are not subject to the proviso. When it comes to the outcome for back-to-back loans versus direct loans, there is no policy intention to create a different outcome for these two scenarios. In the proviso to subsection 2, the first test is whether interest is not taxed (in South Africa) for any of the creditors in subsection (2)(a), (b), (c) or (d). If exempt, the second test is whether withholding tax was or will be levied when that interest is paid. That interest is the same interest that is exempt. Therefore, the focus is on the non-resident creditor and withholding tax on interest at that level – not the intermediary persons for back-to-back loans. It does not matter who pays the withholding tax – the test is payment of withholding tax on that interest. Secondly, while the South Africa person paying the interest to the non-resident withholds the tax and pays it to SARS, it is borne by the non-resident.

*Comment:* The proposed wording in the proviso to section 23M(2) of the Act creates the impression that in order to be included in the formula, the interest must have suffered interest withholding tax in terms of the provisions of section 50B of the Act as the word ‘payable’ is used. It is clear that this is not the intention of the proposed amendment as items ‘B’ and ‘C’ of the formula are not proposed to be amended and still refer to ‘amounts of interest incurred or paid’ in respect to which the provisions of Part IVB of this Chapter are or will be applicable.

*Response: Accepted.* The proposed wording in the proviso to section 23M(2) will be amended to be aligned with items 'B' and 'D' of the formula.

*Comment: It was questioned whether 30 per cent of adjusted taxable income is a reasonable level considering interest rate increases.*

*Response: Noted.* The interest limitation in section 23M used to fluctuate with changes to the repo rate. However, when a review was conducted following the OECD best practice recommendations in respect of this policy area, it was determined that no other country's rules had such flexibility. The proposal was for net interest expense to be limited to 10 to 30 per cent of earnings ("tax EBITDA"). Government proposed 30 per cent given that South Africa's interest rate environment is higher relative to advanced economies. During the time the analysis was conducted for the review, which was published with the February 2020 Budget, interest rates were only 1 to 2 percent lower than they are currently. There was a significant decrease in interest rates during 2020 and 2021 (following the proposal), which was followed by the recent increases. The analysis showed that most companies would have been able to deduct all their interest expense. For those that exceed the limit, the interest expense can be carried forward. It is also important to recognise that a decrease in interest rates is possible in future. The policy position for now is to keep the 30 per cent limit as is.

*Comment: The unlisted property industry relies on debt funding to grow and create asset pools that can be utilised by other industries (listed REITs). This industry is funded by regulated institutions like pension funds, retirement funds and insurers and plays a crucial role in the South African economy – particularly in undertaking new developments, resulting in it being a major employer. To limit the impact of the current interest limitation rules and create a more even playing field with the listed REIT sector, the industry proposes extending the exclusion in section 23M(6), section 8F(3)(d) and section 8FA(3)(d) of the Act to debt funding where these vehicles are owned and funded by regulated institutions such as pension funds, long-term insurers and short-term insurers.*

*Response: Noted.* Government notes that it is not a proposed amendment contained in the draft 2023 TLAB that the unlisted property industry is seeking to remedy by this comment. Rather, it is an interrelated set of issues which ranges from the fact that: (i) the 30 per cent limitation in section 23M of the Act may not be commercially viable in terms of funding real estate; (ii) removing the current reference to 'linked units' issued prior to 1 January 2013 to rather refer to 'funding by creditors who are long-term insurers, pension funds and provident funds'; and (iii) finalisation of the Conduct of Financial Institution Bill (CoFI). It is Government's intention to allow the Financial Sector Conduct Authority to regulate the unlisted property industry via the CoFI Bill because the current listed REIT framework that requires a regulatory function (to assess conformance with leverage limits, use of funds etc), which is currently being performed by the Exchanges in a quasi-regulatory function in the case of listed REITs, is not sustainable given that this industry is not listed. In government's view, this

function needs to be performed by the regulator first before any tax concessions are considered.

## **8.6. Refining the provisions applicable to unbundling transactions**

(Main reference: Section 46 of the Income Tax Act: Clause 37 of the Draft TLAB)

In 2020, changes were made to unbundling transaction rules to curb tax avoidance aimed at using unbundling transaction tax deferral rules to distribute shares in an unbundled company tax free to tax exempt persons and non-resident investors. Consequently, there is no tax deferral in terms of an unbundling transaction in respect of any equity share that is distributed by an unbundling company to any shareholder that is a disqualified person and holds at least 5 per cent of the equity shares in the unbundling company immediately before that unbundling transaction.

These changes resulted in the “pro-rata” operation of the anti-avoidance rule and gives effect to a more equitable outcome in respect of unbundling transactions as only shares distributed to persons that are not disqualified persons will benefit from roll-over relief. In 2021, further changes were made in the unbundling transaction rules to allow shareholders in an unbundling company that only partially qualifies for tax deferral to benefit from an uplift in the base cost of the shares in the unbundled company to the extent that the unbundling company did not qualify for tax deferral in accordance with their respective shareholding. It was proposed in the Draft TLAB that the amount by which the base cost should be increased should still be limited to tax payable by the unbundling company and there be no effect where the unbundling company is not in a taxable position as it is the tax payable that results in the most adverse result for shareholders who qualify for tax deferral.

*Comment:* We recommend that the proposed amendment comes into operation on 1 January 2024 and that it applies in respect of the allocation of expenditure to unbundled shares acquired on or after that date.

*Response:* Not accepted. It is noted that as the previous mechanism to reduce the negative impact of tax paid on the distribution of unbundled shares to disqualified persons, on qualifying shareholders included a split of such tax expense between the unbundling share and the unbundled shares whilst the proposed mechanism simplifies the allocation by only increasing the base cost of the unbundled shares, taxpayers may be disadvantaged depending on which shares they subsequently disposed of. To back date the effective date based on the adverse effect of one group of taxpayers affected is not justifiable and as such, the prospective effective date will remain.

*Comment:* The proposed proviso is added to section 46(3)(b) in the draft bill whereas it should be added to section 46(3)(a).

*Response:* Accepted. This will be rectified in the Draft TLAB.

## 9. INCOME TAX: TAXATION OF FINANCIAL INSTITUTIONS AND PRODUCTS

### 9.1. Impact of IFRS17 insurance contracts on the taxation of short term and long- term insurers

(Main reference: Section 28 and 29A of the Income Tax Act: Clause 31 and 32 of the Draft TLAB)

In 2022 changes were made in the tax treatment of short-term and long-term insurers in sections 28 and 29A of the Act. The aim of those changes were to accommodate the new accounting standard for insurers, International Financial Reporting Standard 17 Insurance Contracts (IFRS 17), update the terminology of the sections so they are in line with IFRS 17 and to mitigate the tax impact as a result of the difference between the methodologies applied in IFRS 4, which is the old accounting standard for insurers, and IFRS 17.

It has come to Government's attention that there may be uncertainty regarding certain third-party cell captive arrangements that are treated as reinsurance arrangements for IFRS purposes. As a result, there are reinsurance assets and liabilities recognised for IFRS purposes in relation to a portion of cell profits due to or from the cell owner. On the other hand, for tax purposes, these third-party cell captive arrangements are not true commercial reinsurance arrangements these balances should be disregarded in determining a cell captive insurer's taxable income.

Also, where a separate liability is recognised in respect of profits due to the cell owner, it may be possible that such a liability may also be included in the "value of liabilities" definition in section 29A of the Act, resulting in the double-counting.

To address the issues mentioned above, Government proposes that reinsurance contract assets and liabilities relating to a cell owner as contemplated in the definition of "cell structure" in section 1(1) of the Insurance Act, No.18 of 2017 be disregarded in symbol "L" of the "adjusted IFRS value" definition in section 29A of the Act. In addition, it is proposed that a change be made to the definition of "value of liabilities" in section 29A of the Act to exclude all other liabilities relating to a cell owner.

It is further proposed that this change be mirrored in section 28(3A) of the Act to cater for foreign long-term insurers that conduct insurance business through a branch in South Africa and fall under the ambit of section 28 of the Act.

#### Comments on short term insurance

*Comment:* The proposed amendment is not adequate because, as far as short-term insurers are concerned, it only deals with the value of liabilities as set out in section 28(3A) of the Act for foreign reinsurers who conduct insurance business in South Africa through a branch. The proposed amendment therefore does not cater for reinsurance assets and liabilities that are recognised for IFRS purposes in relation to cell profits due to or due from the cell owner in the context of an ordinary short-term insurer.

*Response:* Noted. National Treasury and SARS will as a first step engage the industry to ascertain if any further amendments are required to section 29A of the Act in respect of first party cell arrangements. Thereafter, those long-term insurance companies that also conduct short-term insurance can then review whether an amendment is required to section 28 of the Act in respect of first party cell arrangements.

*Comment:* The newly inserted section 28(3C)(b) of the Act in the 2022 provides for a deduction of the liabilities for remaining coverage calculated for the last year of assessment commencing on or after 1 January 2022 but before 1 January 2023, had IFRS 17 been applied at the end of that year of assessment. Since the adjustments for insurance liabilities under IFRS 4 were made net of reinsurance, it follows that the deduction for the LRC should also be net of reinsurance to avoid an over-deduction of the LRC in the year of implementation.

*Response:* Accepted. The draft legislation will be changed to take into account reinsurance in the determination of the deduction for LRC.

*Comment:* The implementation of IFRS 17 has been a complex process and is ongoing with the first of the short-term insurers starting to report on the new IFRS 17 basis during the 2023 financial year. In applying the amended tax legislation, a number of anomalies and unintended consequences have come to the fore. The current wording of the legislation may be interpreted to mean that the 'phasing-in amount' would be the difference between the deduction allowed under section 28(3) prior to amendment (i.e. LRC plus LIC net of reinsurance which represents the total insurance liabilities) and the deduction under the amended section 28(3) (i.e. LIC net of reinsurance which represents only a portion of the total insurance liabilities). Simplistically, one would be comparing total insurance liabilities determined under IFRS 4 to only a portion of the liabilities determined under IFRS 17, resulting in an overstatement of the 'phasing-in amount'.

*Response:* Noted. The simplistic view is not accurate as the treatment of premiums under the new system and the disclosure of liabilities for incurred claims under IFRS 17 on which the deduction for tax purposes is based are different from the tax treatment under the previous system. Government is not proposing any further changes to the tax treatment of short-term insurers until the full implementation of IFRS 17 by the industry is done.

#### Comments on long term insurance

*Comment:* The proposed changes currently only adjust third-party cells captive arrangements, and first-party cell captive arrangements were inadvertently omitted from the proposed legislative amendments.

*Response:* Noted. Awaiting an example to see if this request will be accepted or not. The National Treasury and SARS will further engage the industry during the 2024 legislative cycle to ascertain if any further amendments are required to section 29A in respect of first party cell arrangements.

*Comment:* With respect to the 2022 changes that were made in 29A of the Act to accommodate IFRS 17, the current 'phasing-in' amount wording needs some clarification to ensure that insurers only adjust for the premium debtors and policy loans reclassified under IFRS 17 and that they should exclude IFRS 9 premium debtors and policy loans.

*Response:* Accepted. An amendment will be made to ensure that the phasing-in amount only takes into account premium debtors and policy loans determined in accordance with IFRS, had IFRS 17 been applied during the year of assessment commencing on or after 1 January 2022, but before 1 January 2023.

## **10. INCOME TAX: BUSINESS INCENTIVES**

### **10.1. Extension of the UDZ tax incentive sunset date**

(Main reference: Section 13quat of the Income Tax Act: Clause 21 of the Draft TLAB)

The Act contains the Urban Development Zone (UDZ) tax incentive in section 13quat of the Act, which came into effect in 2003. This incentive was introduced to increase investment in 16 designated inner cities thereby encouraging property investment in central business districts and to address the problem of urban decay in these central business districts through the promotion of investment in urban renewal. The UDZ tax incentive currently has a sunset date of 31 March 2023.

It has come to Government's attention that the public consultation as part of the policy review process of the UDZ tax incentive will not be concluded before the incentive's sunset date. Further engagement with key stakeholders, especially sourcing and evaluating important data from municipalities on the incentive's uptake, is necessary to assess the contribution of the incentive to achieving its intended objectives.

Based on the above, it is proposed that the UDZ tax incentive be extended by another period of two years from 31 March 2023 to 31 March 2025 to allow additional time for the review to be completed.

*Comment:* The proposed amendment is welcomed. However, there are other tax incentives with nearing sunset dates, more specifically, the section 12H Learnership incentive which essentially has a sunset date of 1 April 2024. As such, it is requested that government indicates whether the Learnership incentive will be extended beyond 2024?

*Response:* Noted. Comment is outside of scope of the proposed change in legislation contained in the draft TLAB 2023. However, given the earnest interest in the section 12H Learnership incentive, government will indicate the policy direction on the Learnership incentive in the 2024 Budget Review.

## 10.2. Refinements to the research and development tax incentive

(Main reference: Section 11D of the Income Tax Act: Clause 12 of the Draft TLAB)

On 15 December 2021, Government published a discussion document titled *Reviewing the Design, Implementation and Impact of South Africa's Research and Development Tax Incentive*. This review sought to determine whether to extend the R&D tax incentive beyond its sunset date and, if so, in what form.

Following the review, government proposes to extend a revised R&D tax incentive to 31 December 2033. It is also proposed that changes be made to the definition of R&D to clarify that the incentive should only apply to activities with an aim of solving scientific or technological uncertainty – in line with the original policy intent. It is further proposed that the intellectual property purpose tests in the first part of the definition be deleted, so that the test for R&D is aligned to the principles outlined in the Guidelines for Collecting and Reporting Data on Research and Experimental Development published by the Organisation for Economic Co-operation and Development, 2015 (OECD Frascati Manual). In addition, it is proposed that activities be measured against the requirements set out in the definition of R&D, rather than the nature of the activities and whether they are intended for sale / licensing or not (exclusion for internal business processes be deleted).

To address additional administrative issues, it is proposed that applicants be allowed a six-month grace period to submit pre-approval applications; extend circumstances under which the SARS Commissioner discloses information to the Minister of Higher Education, Science and Innovation for the purposes of monitoring R&D; and include sanctions for any person who contravenes the secrecy provisions.

*Comment:* The words such as “novel” and “inventive” from the Patents Act; and/or “new” and “original” from the Designs Act have very specific meanings, and well-defined definitions in those contexts. It would be inappropriate to adopt those words (with their defined terms) into Section 11D of the Act.

*Response:* Noted. The proposed revised definition of R&D shifts away from the intellectual property purpose tests. R&D eligibility will be determined by considering some of the principles in the OECD Frascati Manual. In line with this, the proposed amendments are intended to replace the intellectual property purpose test with the OECD Frascati principles that an R&D activity must be carried on for the purpose of creating or developing new knowledge, or new or significantly improved products, processes or services.

*Comment:* Consider including a definition of ‘new’.

*Response:* Not accepted. This is not deemed to be necessary and Government is not aware of any other countries that have such a definition.

*Comment:* The proposal that the exclusion for internal business process be deleted on the basis that the internal business process exclusion has now become, in our

view, superfluous and request that the final legislation avoid reference to the wording “software and computer programmes”. This potentially implies that software and computer programmes are two different things.

*Response:* Noted. The proposed revised definition of R&D refers to new knowledge or new or significantly improved products, processes or services.

*Comment:* Guidelines on clinical trials have been updated and the legislation should now reference “Department of Health, 2020. South African Good Clinical Practice: Good Clinical Trials”.

*Response:* Not accepted. Although the Guidelines for South African Good Clinical Practice: Good Clinical Trials issued by the Department of Health in 2020 provide for a definition of a clinical trial, these Guidelines do not include a definition for the four phases of clinical trials. Government has decided to retain the reference to Guidelines for good practice in the conduct of clinical trials with human participants in South Africa issued by the Department of Health in 2006 as these provide a definition of a clinical trial, as well as the four phases of clinical trials.

*Comment:* The current proposed wording relating to the new sunset date does not explicitly state that no deduction shall be allowed in respect of qualifying expenditure incurred after 31 December 2033. To make Government’s intention clear that the research and development tax incentive will cease on 31 December 2033, it should be stated that no deduction shall be allowed in respect of applications received and expenditure incurred after 31 December 2033.

*Response:* Not accepted. The sunset date is linked to when applications are received. Under the pre-approval system, a taxpayer can claim eligible expenditure only after the Minister of Higher Education, Science and Innovation has granted approval of the project. It is government’s intention to allow taxpayers that submit applications up to and including 31 December 2033 to deduct eligible expenditure on the approved project up until the end of the approved project, which will be after the proposed sunset date of 31 December 2033.

*Comment:* Draft legislation states that no deduction shall be allowed in respect of applications received after 31 December 2033. A concern was raised as to whether Government will have the capacity and ability to adjudicate such submissions (in 2034).

*Response:* Comment misplaced. The pre-approval process is administered by the Department of Science and Innovation (DSI), supported by an adjudication committee comprising of three officials from the DSI, three officials from the South African Revenue Service and one official from the National Treasury. In addition, alternates have been appointed to ensure continuity of the process if any of the appointed officials are unable to fulfil their duties.

*Comment:* The requirements of section 11D(9)(d) and section 11D(22) appear to be

a duplication in that they both provide that applications must be made by 31 December 2033 to qualify for the deduction. This is a prerequisite for the approval to be granted.

*Response: Accepted.* Amendments will be made to draft legislation to remove the duplication.

*Comment:* The proposed wording that amends subsection 2(a)(iv) does not make it clear that the 6-month grace period only applies to qualifying expenditure incurred on/after 1 January 2024. Further, it is unclear why all applicants should not be treated equally, being that all expenditure incurred 6 months prior to an application submitted on or after 1 January 2024 should be included.

*Response: Partially accepted.* The proposed amendment is intended to apply only to qualifying expenditure incurred on/after 1 January 2024. Government does not intend to apply the revised R&D tax incentive retrospectively, so the transition (including expenditure in respect of approved projects from 1 January 2024 onwards) to the 6-month grace period will be fully effective from 1 July 2024. Applicants will not be treated unequally as two companies applying in April 2024, for example, will both be able to claim for expenditure incurred from 1 January 2024 onwards. The table below seeks to clarify how the regime will work – depending on when an application is submitted.

<b>Apply</b>	<b>Approval</b>	<b>Qualifying spending</b>	<b>Applicable regime</b>
1 Nov 2023	5 Dec 2023	All expenditure from 1 Nov 2023	Existing regime
1 Nov 2023	22 Jan 2024	All expenditure from 1 Nov 2023	Existing regime
15 Jan 2024	2 Mar 2024	All expenditure from 1 Jan 2024	New regime (2023 Tax Laws Amendment Act (TLAA))
15 Mar 2024	1 Jul 2024	All expenditure from 1 Jan 2024	New regime (2023 TLAA)
15 Aug 2024	1 Nov 2024	All expenditure from 15 Feb 2024	New regime (2023 TLAA)

*Comment:* Section 11D(20)(a)(i) is not aligned with the proposed 6-month grace period as it only allows for expenditure from the date of application.

*Response: Accepted.* Amendments will be made to draft legislation to include the proposed 6-month grace period.

*Comment:* The substitution of section 11D(20) omits the word “if” at the end of paragraph (a).

*Response:* Accepted. Amendments will be made to draft legislation to include the omitted word.

*Comment:* The legislation does not allow for a deduction under the general deduction formula (section 11(a)) if that deduction may be allowed under any other provision. It appears that unless approval is obtained for the deduction of R&D expenditure as contemplated in section 11D(2) within the grace period allowed, no deduction would be allowed for such expenditure under section 11(a) where it meets the requirements of that section. The result of this is that, in effect, a taxpayer would either be entitled to the 150 per cent deduction for R&D expenditure or no deduction at all.

*Response:* Not accepted. It should be noted that this provision was not part of the 2023 draft TLAB proposals on the R&D tax incentive. Government notes the uncertainty that exists and will investigate the matter to ensure consistency and certainty regarding the interpretation and application of the provision. However, the intent is that if a taxpayer may not claim under section 11D, they are entitled to claim under section 11(a).

*Comment:* The requirement that the R&D must be carried on by that taxpayer in instances where the taxpayer funds another person that conducts R&D on behalf of the taxpayer appears to be either internally contradictory (if another person conducts R&D on behalf of the taxpayer then the taxpayer can't itself be carrying on the R&D) or superfluous since the provision already requires the R&D to be carried on behalf of the taxpayer.

*Response:* Not accepted. It should be noted that this provision was not part of the 2023 draft TLAB proposals on the R&D tax incentive. Parties undertaking R&D activities often do so on behalf of others (those funding the activities). To the extent these circumstances exist, the parties funding the R&D obtain the 150 per cent deduction as opposed to the parties undertaking the R&D activities. Even though another person conducts R&D on behalf of the taxpayer, the taxpayer will be considered as carrying on the R&D if they determine or can alter the methodology of the research. In addition, this provision was intended to shift the 150 per cent deduction to the party undertaking the R&D activity if the funder cannot deduct the amount funded (e.g. because the funder is tax-exempt or outside the tax system or a company forming part of the same group of companies).

*Comment:* Government to consider an increase of the current tax incentive rate to 200 per cent from the current 150 per cent, to compensate for the reduced net tax benefit with effect of reduced corporate tax rate of 27 per cent for years of assessment after 1 April 2022.

*Response:* Not accepted. Government still considers the current R&D tax incentive rate of 150 per cent to be sufficient after the corporate tax rate reduction to 27 per cent. In addition, an increase in the current allowance is not considered

feasible due to fiscal affordability – many basic service and infrastructure budgets have recently been cut considering fiscal constraints. It would be difficult to find a compelling argument to extend the fiscal envelope for this type of incentive under the current circumstances.

*Comment:* The draft EM and proposed amendments are not clear on whether the incentive is available, in principle, for both operating expenditure as well as capital expenditure and if the rate at which the capital expenditure is to be claimed is 150 per cent.

*Response:* Not accepted. It should be noted that this provision was not part of the 2023 draft TLAB proposals on the R&D tax incentive. It is government's intention to retain the current rules, which allows for only expenditure incurred in respect of a prototype or pilot plant created solely for purpose of the process of R&D (and not intended for use or used in the production process after the R&D is completed) to be deducted at the incentive rate of 150 per cent. All other eligible assets used for R&D activity qualify for the accelerated depreciation allowance under section 12C and section 13 of the Act.

### **10.3. Enhanced deduction in respect of certain machinery, plant, implements, utensils and articles used in the production of renewable energy**

(Main reference: Sections 8,11, new section 12BA,12E,12N,12P,15,23A,23G and paragraph 66 of the Eighth Schedule to the Income Tax Act : Clauses 4,11,16,17,18, 19,22,24,25 and 43 of the Draft TLAB)

Given the country's continued struggle to produce reliable electricity through the national grid, government is proposing to enhance the attractiveness of the existing tax incentive that seeks to encourage greater private investment in renewable energy. To stimulate rapid private investment to alleviate this energy crisis – in the 2023 Budget Review, Government proposed to temporarily enhance the current renewable energy tax incentive available in section 12B of the Act. The enhanced renewable energy tax incentive will be available for qualifying assets brought into use from 1 March 2023 until and including 28 February 2025. It will apply in respect of the currently eligible renewable energy sources under section 12B of the Act listed below, but there will be no electricity generation limits for the duration of this temporary incentive. Assets will qualify if they are used together in the generation of electricity. While eligibility will be based on facts and circumstances, it is the policy intention that assets will qualify if used to generate electricity from:

- Wind power
- PV solar energy
- Concentrated solar energy
- Hydropower
- Biomass comprising organic wastes, landfill gas or plant material

The enhanced renewable energy tax incentive will also apply to supporting structures as per section 12B of the Act in which the above-mentioned assets are

mounted on or are affixed to, provided that:

- the foundation or supporting structure is designed for the above-mentioned asset and constructed in such a manner that it is or should be regarded as being integrated with that asset; and
- the useful life of the foundation or supporting structure is or will be limited to the useful of the asset mounted thereon or affixed thereto.

Taxpayers should please note that the content of this document is supplemented by an [FAQ Document](#) published on the National Treasury website on 20 November 2023.

*Comment:* The two-year period is insufficient and will exclude several large projects that are in the pipeline – causing a further delay in the alleviation of the current pressure. Many of the projects are delayed by regulatory approvals.

*Response:* Not accepted. The purpose of the incentive is to change behaviour and encourage as many businesses as possible to invest in renewable energy generation capacity as soon as possible – i.e. accelerate investment within a constrained fiscal envelope. The intention is not to assist with projects that were already planned, and which would have proceeded without government assistance. As an example, the independent power producer projects will happen regardless as it is their business model to generate electricity. Government does not need to subsidise these efforts. It is recognised that larger companies investing in large-scale embedded electricity generation require regulatory approval for offsite grid connections, which has been taking longer than is ideal. However, a one-stop shop has been set up by the Department of Trade Industry and Competition, and the time taken for approvals is being reduced. Government wants to assist those businesses that do not have the means to invest in electricity generation as they contribute to our economy and employ people. Many such businesses do not meet the generation threshold required to apply for regulatory approval or perform environmental impact assessments as they will be able to produce electricity on-site, so approvals are not a stumbling block for them. Our sense is that small and medium firms requiring systems of less than 1MW (less than 2000 solar panels and falling into the small-scale embedded generation category) would be able to make use of the incentive within the two-year timeframe. This should be the case even if Nersa registration and municipal/Eskom approval is required. Many businesses may not have sufficient cash to take advantage of the incentive. For this reason, the tax incentive is complemented by the recently announced Energy Bounce Back Scheme which provides loan funding to enable qualifying investment. There is also a blended finance option for agri-businesses, which it is part grant and part loan funding.

*Comment:* There is no definition for eligible assets, which is creating confusion. This is particularly because the solar rebate incentive for individuals has explicitly excluded storage and conversion assets, and there is no clarity whether such assets are eligible for the business incentive.

*Response: Noted.* Government recognises the source of confusion. However, it would be difficult to create a definition that includes a list of assets as some cases may be viewed differently depending on which assets are being claimed for. In the public workshop, it was stated that the policy intent would be explained in this document. The bold and underlined word “*in*” in the following words of the draft section 12BA “... assets used ***in*** the production of renewable energy” is intended to imply that the incentive is not solely for assets that produce electricity. If storage and conversion assets form part of a system of assets that together produce electricity, it is likely that they will qualify for this incentive. If there is a scenario where a taxpayer is simply drawing power from the grid and storing it, these assets will likely not qualify. The latter example is not aligned to the policy objective of encouraging more generation capacity and should not be claimable under proposed section 12BA. This is why it is important that SARS retains the ability to apply a facts and circumstances approach to each case.

With respect to eligibility for the solar rebate available to individuals, it is important to highlight that the personal income tax and corporate income tax systems operate differently. It is not common for an individual to deduct the cost of an expense or investment from their taxable income. The solar rebate is an exception to this rule and targets solar panels exclusively given that they are directly linked to additional generation capacity. While batteries and inverters can be used on their own to provide a private benefit to a particular household, the addition of solar panels enhances generation supply, which provides a public benefit. In contrast, it is common for a business to deduct costs in relation to assets used in the production of income and there is no reason to specifically exclude assets such as batteries and inverters, unless they are being used in isolation to draw and store power from the grid (as this detracts from the primary objective of the temporarily enhanced renewable energy incentive – to encourage investment in additional generation capacity).

To further enhance clarity, Government will publish an FAQ document along with this Response Document so that investors can have all the information in one document and gain a better understanding of how this incentive works.

*Comment:* There is a concern that limiting the section 12BA allowance to rental income detracts from the purpose of the incentive and forces taxpayers to rather enter into power purchase agreements.

*Response: Not accepted.* This matter was discussed in the public workshops on 7 September 2023. From government’s perspective, it is not desirable to move away from the principle underlying section 23A that restricts the setting off of such deductions against rental income. The lessor will not lose out on the allowance as it can be carried forward to the following year of assessment.

*Comment:* Limiting the section 12BA allowance in respect of limited partnerships does not make sense given the incentive to accelerate investments.

*Response:* Not accepted. The objective is to accelerate investments in this space, but not at the cost of established principles. The 25 per cent additional allowance is not denied – it is carried forward to the next year. There is no good policy rationale in government’s view to allow the additional 25 per cent uplift to be set off against partners’ passive / other income.

*Comment:* There appears to be confusion and different interpretations for how the recoupment provision should be implemented.

*Response:* Noted. If the qualifying assets are sold prior to 1 March 2026, the intention is to recoup 25 per cent of the cost of the asset(s) that has/have been recouped. The total recoupment in respect of section 8(4)(a) and 8(4)(nA) should not exceed the total section 12BA allowance in respect of that/those asset(s). The example below sets out how recoupments should be applied depending on whether the asset(s) is/are sold before or on/after 1 March 2026.

	Cost	Allowance				
Section 12BA	100	125				
<i>Sale before 1 March 2026 for</i>			80	100	120	150
Section 8(4)(a) recoupment			80	100	120	125
Section 8(4)(nA) recoupment			20	25	5	0
<b>Total recoupment</b>			<b>100</b>	<b>125</b>	<b>125</b>	<b>125</b>
<i>Sale on/after 1 March 2026 for</i>			80	100	120	150
Section 8(4)(a) recoupment			80	100	120	125
Section 8(4)(nA) recoupment			0	0	0	0
<b>Total recoupment</b>			<b>80</b>	<b>100</b>	<b>120</b>	<b>125</b>

*Comment:* The draft legislation is not clear on whether taxpayers have a choice between claiming section 12B and section 12BA. It is important that there is certainty on whether taxpayers can rely on section 12B of the Act.

*Response:* Accepted. Changes will be made to section 12B of the Act to stipulate that no deduction is allowed for any asset granted such under section 12BA.

*Comment:* The proposed amendment to section 12E of the Act to deny a deduction in terms of that section where an allowance has been granted under s12BA is unnecessary, because section 23B(1) of the Act provides for a general rule to prevent amounts being deducted more than once.

*Response:* Not accepted. There was only one comment in this regard and, in line with the issue raised in respect of the choice between section 12BA and section 12B above, government prefers that taxpayers have certainty that only one allowance can be claimed.

*Comment:* Mining companies should be able to claim the renewable energy tax incentive as normal capital expenditure. Deductible capital expenditure utilised for mining purposes in terms of section 36(11) of the Act does not consider the additional 25 per cent available under section 12BA. Remedying this will facilitate more clarity in the application of section 37 of the Act, when applicable, and simplify the application of the renewable energy tax incentive in mining companies.

*Response:* Accepted. Changes will be made to include qualifying section 12BA assets within mining capital expenditure. While mining companies were not specifically excluded from this incentive, it is recognised that changes are required to simplify application and avoid unintended consequences in the mineral royalty calculation, for example.

*Comment:* Commentators have questioned some of the constraints in the leasing space, e.g. why operating leases are eligible whereas finance leases are subject to stricter requirements. Some hold the view that finance leases should qualify rather than operating leases. The draft legislation currently requires that the lessee in a finance lease arrangement be conducting a trade for eligibility. There are also requests for clarity in respect of ownership between the lessee and lessor.

*Response:* Accepted. Government recognises the source of confusion and wishes to instil certainty. From a strict policy eligibility perspective, those businesses who lease out qualifying assets under operating lease arrangements do not require a subsidy as the demand for their investment is driven by those businesses and individuals who are leasing the assets. This type of business model does not require government assistance in the current environment where demand is high due to the need for generating electricity. It is also impossible for government to require that lessors pass the benefit on to lessees. However, because section 12BA's design was based on section 12B, lessors in an operating lease context were included from the outset because they own the assets. Ownership is an important criterion that runs through the Income Tax Act as it is a prerequisite for capital allowances.

It would be unfair to remove eligibility at this stage (given that the incentive has commenced, and investor certainty is key). For this reason, government is proposing to apply the same treatment to finance lease arrangements. The trade requirement for lessees will be removed so that there are no hurdles for claiming this incentive. Because the ownership of assets only transfers at the end of a finance lease arrangement and the incentive is only available for two years, the lessors of these types of arrangements will be eligible to claim section 12BA. To achieve the desired outcome, government proposes to delete section 12BA(4)(a).

## 11. INTERNATIONAL TAX

### 11.1. Extending the anti-avoidance provision to cover foreign dividends from shares listed in SA

(Main reference: Section 10B of the Income Tax Act: Clause 10 of the Draft TLAB)

Currently, section 10B of the Act exempts foreign dividends received or accrued from shares listed on a South African stock exchange from normal tax. The rationale for this exemption is that these foreign dividends are subject to dividends tax and the collection of dividends tax on the basis of withholding taxes is more effective than taxing shareholders receiving those foreign dividends under the income tax system.

It has come to Government's attention that schemes have been devised to exploit the exemption of foreign dividends received or accrued from shares listed on a South African stock exchange from normal tax. These schemes involve South Africans investing in the shares of a non-resident company listed on a South African stock exchange and the non-resident company directly or indirectly investing in interest-bearing financial instruments in South Africa. The result is that a deduction for an interest expense is not matched with a taxable foreign dividend.

It is proposed that the exemption mentioned above be denied for foreign dividends received or accrued from shares listed on a South African stock exchange if the foreign dividends are directly or indirectly funded by amounts that were deductible in South Africa. In order to limit the impact on legitimate transactions, it is proposed that these rules only apply in respect of foreign dividends that are declared from profits provided that at least 20 per cent of the profits were generated from transactions with persons that deducted the amounts paid or payable from income.

*Comment:* There is no objection to this proposed amendment and the reference to the 20 per cent rule is welcomed. However, there is a drafting error as the proposed amendment is different from the current wording of the proviso with respect to the words paid or payable. In addition, the text "any amount paid or payable by any person to any other person;" applies to both items (aa) and (bb).

*Response:* Accepted. The proposed amendment will be reworded to cater for the drafting errors pointed out.

*Comment:* The proposed amendment creates uncertainty as the recipient of the foreign dividend would need to know whether 20 per cent or more of the profits were generated from amounts received from persons who deducted the payment. The proposed amendment is unlikely to be effective in addressing the schemes mentioned in the Draft Explanatory Memorandum.

*Response:* Noted. The 20 per cent rule is aimed at addressing some valid concern that may arise with respect to tracing when a non-resident companies listed on the South African Exchange indirectly fund foreign dividends from amounts that

are deductible in RSA.

*Comment:* An investor would not have knowledge in respect of where the profits from which the dividend are declared, are sourced, unless the investor who holds greater than 50 per cent holding in the declaring company or the listed company supplies the appropriate information to its shareholders. In addition, this proposal will require system changes for tax reporting of foreign dividends which will be costly to unit trust managers and create a compliance burden for investors.

*Response:* Partially accepted. Foreign dividends from portfolios of foreign collective investment schemes will be excluded from the application of this extension to the anti-avoidance provisions.

## **11.2. Clarifying the foreign business establishment exemption for controlled foreign companies**

(Main reference: Section 9D of the Income Tax Act: Clause 8 of the Draft TLAB)

The Act contains anti-avoidance rules in section 9D aimed at taxing South Africa residents on an amount equal to the net income of a controlled foreign company (CFC). In order to strike a balance between protecting the South African tax base and the need for South African multinationals to be competitive offshore, the South African CFC rules contains various exemptions of certain types of income.

For example, certain amounts that are attributable to a foreign business establishment (FBE) of a CFC, as defined in section 9D, are excluded from the net income of the CFC. A foreign business establishment must consist of a fixed place of business located outside South Africa that is used or will continue to be for the carrying on of business of the CFC for a period of at least 1 year.

In addition, a FBE must satisfy additional requirements relating to the nature of the business, for example, the business must have a minimum specified structure (e.g. an office), the fixed place of business should be suitably staffed with on-site managerial and operational employees of that CFC, the fixed place of business should be suitably equipped and have suitable facilities for conducting the primary operations of the business.

Furthermore, the definition of a foreign business establishment allows for structures the utilisation of, employees, equipment and facilities of the another company to be taken into account if the structures, employees, equipment and facilities are located in the same country as the fixed place of business of the CFC, the other company is subject to tax in the country in which the CFC place of business is located and the other company forms part of the same group of companies as the CFC. It has come to Government's attention that some taxpayers are retaining certain management functions but outsourcing other important functions for which the CFC is also being compensated by its clients. The location of the 'primary operations', is vital in determining whether a company meets the definition of an FBE as defined in the Act.

It is proposed that all important functions for which a CFC is compensated should be performed either by the CFC or by another CFC in the same group of companies that is located and subject to tax in the same country as the CFC's fixed place of business, to qualify for the foreign business establishment exclusion.

*Comment:* The proposed amendment should be withdrawn and the existing concept of “primary operations” be retained in the FBE definition because this proposed amendment is following on from the court decision in the CSARS v Coronation Investment Management SA (Pty) Ltd. Currently, the judgement that was delivered by the Supreme Court of Appeal upholds that which National Treasury and SARS have placed in the legislation.

*Response:* Accepted. The proposed amendment will be withdrawn pending a Constitutional court judgment on this matter.

*Comment:* If the proposed amendment is to be enacted in its current form, the effective date of the amendment should be postponed enabling companies with CFCs to align their business models.

*Response:* Accepted. The proposed amendment will be withdrawn pending the Constitutional court judgement.

*Comment:* The proposed amendment should be delayed in order to consider the broader policy issues on a granular level.

*Response:* Accepted. The proposed amendment will be withdrawn pending a Constitutional court judgment on this matter.

### **11.3. Taxation of non-resident beneficiaries of trusts**

(Main reference: Section 25B of the Income Tax Act: Clause 29 of the Draft TLAB)

The gradual relaxation of exchange control regulations has led to an increase in applications for confirmations of tax compliance status of persons by SARS for purposes of transferring funds offshore via authorised dealers.

Government is concerned about the difference between the rules covering the normal tax treatment of income attributed to beneficiaries of trusts in section 25B of the Act and the rules covering the tax treatment of capital gains in relation to beneficiaries in paragraph 80 of the Eighth Schedule to the Act.

Section 25B of the Act does not have a limitation on who the beneficiaries of a South African trust may be; they could be residents or non-residents. The flow through of amounts by South African trusts to non-residents places SARS in a difficult position to collect income tax from those beneficiaries as they may not be taxed on foreign sourced amounts, tax recovery actions may be difficult and in the case of non-resident trusts that are beneficiaries, SARS may not have information on the persons in whom the foreign trusts vest the income.

It is accordingly proposed that changes be made to section 25B of the Act to align it with the provisions of paragraph 80 of the Eighth Schedule to the Act by limiting the flow through principle only to resident beneficiaries.

*Comment:* This proposed amendment could result in economic double taxation for

foreign beneficiaries of South African trusts because when the South African trust distributes a taxable amount to a non-resident beneficiary, the trust will be subjected to tax on the amount distributed in South Africa and the non-resident beneficiary may also be subject to tax on the amount received in another country.

*Response:* Noted. Article 1(2) of the OECD Model Tax Convention would address this situation for entities or arrangements that one or both States treat as wholly/partly fiscally transparent. On 30 September 2022 South Africa deposited its instrument of ratification for the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI). The MLI entered into force in South Africa on 1 January 2023. Article 3(1) of the MLI applies to transparent entities and state that the income derived by or through an entity or arrangement that is treated as wholly or partly fiscally transparent under the tax law of either Contracting State shall be considered to be income of a resident of a Contracting State but only to the extent that the income is treated, for purposes of taxation by that Contracting State, as the income of a resident of that Contracting State. The effect thereof, would be that the resident is allowed relief from economic double taxation with reference to the South African tax paid by the South African trust. It should also be noted that the OECD commentary in relation to Article 1(2), at paragraph 5, confirms the principle that States should not be expected to grant the benefits of a bilateral tax convention in cases where they cannot verify whether a person is truly entitled to these benefits.

*Comment:* The proposed amendment to section 25B of the Act of disallowing the flow-through principle based solely on the residency status of a beneficiary is in direct conflict with the majority of South African DTAs which contain non-discrimination clauses based on article 24(1) of the 2017 OECD Model Tax Convention.

*Response:* Not accepted. Article 24 of the OECD Model Tax Convention and UN Model Tax Convention takes into account that all tax systems incorporate legitimate distinctions based, for example, on differences in liability to tax or ability to pay. The non-discrimination provisions of the Article seek to balance the need to prevent unjustified discrimination with the need to take account of these legitimate distinctions.

The OECD Commentary clarifies that the expression “in particular with respect to residence” under Article 24(1), that the residence of the taxpayer is one of the factors that are relevant in determining whether taxpayers are placed in similar circumstances. It continues clarifying that the expression “in the same circumstances” would be sufficient by itself to establish that a taxpayer who is a resident and one who is not a resident are not in the same circumstances.

In applying Article 24 (1) of the OECD Model Tax Convention and UN Model Tax Convention, the underlying question is whether two persons who residents of the same State are are being treated differently solely by reason of having a different nationality. The proposed amendment to section 25B of the Act does not provide different treatment based on nationality and therefore there is no discrimination

in terms of Article 24(1).

*Comment:* The trust could be taxed on interest income in terms of the proposed amendment but so could the non-resident beneficiary in terms of the interest withholding tax provisions. A similar issue can arise with respect to dividends from a REIT that are subject to income tax in the trust but also subject to dividends tax for a non-resident beneficiary. Therefore, trusts should be treated as regulated intermediaries for amounts payable to foreign beneficiaries.

*Response:* Partially accepted. Exemptions will be provided for withholding tax on interest and withholding tax on royalties for amounts paid by South African trusts.

*Comment:* The tax years for resident trusts end on the last day of February and therefore the proposed amendment's effective date of 31 July 2023 is already effective for trustees that have made a distribution to beneficiaries during the period of 1 March 2023 to 31 July 2023.

*Response:* Accepted. The effective date will be deferred until 1 March 2024 and the amendment will apply in respect of any year of assessment commencing on or after that date.

*Comment:* The proposed amendment will impact the issuance of sukuk bonds because the foreign investors will be taxed indirectly.

*Response:* Noted. South Africa's tax treaties that incorporate the principles of Article 1(2) of the OECD Model Tax Convention would address this situation by providing relief from economic double taxation for foreign investors.

#### **11.4. Refining the participation exemption for the sale of shares in foreign companies**

(Main reference: Paragraph 64B of the Eighth Schedule to the Income Tax Act: Clause 42 of the Draft TLAB)

In 2003, changes were made to the tax legislation to introduce a participation exemption relating to foreign dividends from foreign companies (currently in section 10B) of the Act as well as a participation exemption relating to the sale of shares in foreign companies in paragraph 64B of the Eighth Schedule to the Act. The main aim of these exemptions is to encourage the repatriation to South Africa of foreign dividends and the proceeds on the sale of shares in foreign companies to non-connected non-residents.

Government has identified that the participation exemption is being used in ways that was never intended. These transactions include for example, instances where restructuring of a group of companies entails the sale of shares to recently formed non-resident companies although there is no change in the ultimate shareholders.

It is proposed that changes be made in the tax legislation by not granting the participation exemption if the sale of shares is either to a non-resident company that formed part of the same group of companies as the company disposing of the shares, or the shareholders are substantially the same as the shareholders of any company in the group of companies of the companies disposing of the shares.

*Comment:* The proposed exclusion of a non-resident that formed part of the same group of companies as the seller is overly broad in that it will apply regardless of the amount of time that the purchaser and seller were no longer part of the same group of companies. The current provisions of paragraph 64B of the Eighth Schedule to the Act applies an eighteen-month holding period before a relief can be applied.

*Response:* Accepted. An 18-month rule will apply to this proposed exclusion similar to the current provisions of paragraph 64B of the Eighth Schedule to the Act.

*Comment:* In the proposed amendment, the expression “substantially the same as the shareholders of any company in the group of companies” is open to interpretation and needs to be clarified as it provides no rule as to at which point the shareholding should be tested.

*Response:* Accepted. The test for shareholding will be applied immediately after the disposal.

## 12. VALUE-ADDED TAX

### 12.1. Reviewing the VAT treatment of specific supplies in the short-term insurance industry

(Main reference: Section 8 of the VAT Act: Clause 48 of the TLAB)

Section 72 of the VAT Act provides for the discretionary powers of the Commissioner to make arrangements or decisions relating to difficulties, anomalies or incongruities in applying the provisions of the VAT Act. In 2019, changes were made to section 72, which impacted on arrangements or decisions that were already in existence that were made under the previous rules. One such decision relates to the excess payments made in terms of non-life or short-term insurance contracts.

In terms of SARS Binding General Ruling 14 (BGR 14), where an insured pays an excess amount directly to a third-party supplier, the supplier must issue two tax invoices, that is, one to the insured to the extent of the excess payment and one to the insurer to the extent of the trade payment. Where the insurer pays the full amount, including the excess payment, to the third-party supplier and then recovers only the excess amount from the insured, the receipt of such excess payment from the insured does not constitute “consideration” as defined in section 1(1) of the VAT Act, since the payment received is not in respect of any taxable supply made by the insurer to the insured. As such, the insurer would have been denied an input tax claim on the amount of the excess payment, but for the arrangement provided for in BGR 14.

The 2019 amendments to section 72 imply that the decision under section 72 contained in BGR 14 is no longer applicable. As a result, such decision was withdrawn with effect from 1 January 2022. Hence, it is proposed that the VAT Act be amended to cater for these situations and to formalise the decisions contained in BGR 14 into the VAT Act.

*Comment:* The deletion of the current further proviso to section 8(8) results in an additional cost of the claim to the insurer in respect of indemnity payments made for goods stolen or damaged beyond economic repairs for which an input tax deduction was denied in terms of section 17(2). Consider re-instating the proviso to prevent these additional costs.

*Response:* Accepted. The further proviso will be re-instated.

*Comment:* The wording in the proposed section 8(8A)(b) does not seem to address the scenario where the insurer pays the full amount for the reinstatement to the supplier, and recovers the excess due from the insured.

*Response:* Accepted. Further amendments will be made to cater for these scenarios.

## **12.2. Clarifying the VAT treatment of prepaid vouchers in the telecommunications industry**

(Main reference: Section 21 of the VAT Act: Clause 51 of the TLAB)

In the early years of the mobile telecommunications industry in South Africa, prepaid subscribers to mobile telecommunication services could use prepaid vouchers only to purchase the services offered by that mobile telecommunications company such as calls and short message services (“SMS”). The evolution and technological advances in the telecommunications industry have made it possible for subscribers to utilise the prescribed services purchased from the telecommunications company to acquire other services from third-party service providers. Examples include, the supply of financial services (life and non-life insurance), downloads of music or movies, and mobile money services.

In terms of the provisions of section 10(19), the telecommunications company would declare output tax in the tax period when the vouchers are sold to retailers or agents who then on-sell these vouchers to consumers. Since the time of supply is triggered when the telecommunications supplier supplies the vouchers, the redemption of the vouchers does not trigger any further VAT for the telecommunications company.

However, in the event that the subscriber does not wish to utilise the services from the telecommunications company but acquires further taxable supplies from third parties, there would be a further output tax liability on the part of the third-party

supplier with no corresponding VAT adjustment for the telecommunications company.

The fiscus would thus be receiving output tax from the telecommunications company at the point that the prepaid voucher is sold, and from the third-party to the extent that services are supplied by the third-party.

The proposed amendment seeks to introduce a provision in the VAT Act to permit the telecommunications companies to deduct input tax to the extent that a subscriber acquires services from a third-party supplier, whether taxable or exempt, in instances where the telecommunications company acts as an agent for such supplies.

*Comment:* It is not clear based on the current proposed amendments how telecommunication companies and other suppliers in the supply chain (if applicable) would practically be in possession of the information required to issue a valid credit note containing the details required by section 21(3).

*Response:* Noted. SARS and National Treasury will engage further with industry in this regard to determine how this can practically be resolved in a manner that works for the industry.

### **12.3. Clarifying VAT rules dealing with documentary requirements for gold exports**

(Main reference: New section 54(2C) of the VAT Act: Clause 52 of the TLAB)

The main purpose of gold refineries is to refine and smelt gold or ore received from various customers, namely depositors. In most instances, the refineries also act as agents and sell or export gold on behalf of these depositors. Gold from more than one depositor is typically required to make up the volume ordered for sale or export. The refinery and smelter require large quantities of gold or ore to operate effectively and efficiently, and no single depositor provides sufficient quantities of gold or ore. It is accordingly not possible for each depositor to have its gold or ore treated separately from the gold or ore of other depositors. It follows that once a specific depositor's gold or ore enters the refining or smelting process, it is co-mingled with the gold or ore of other depositors and effectively loses its identity as belonging to a specific depositor.

Hence, it is difficult to determine which depositor's gold is sold or exported. As a result, depositors find it difficult to obtain the documentary evidence to support the application of the zero rate on a transaction-by-transaction basis in relation to their gold as contemplated in the regulations issued in terms of section 74(1) of the VAT Act read with paragraphs (a) and (d) of the definition of "exported" in section 1(1) of the VAT Act.

In order to address these challenges, it is proposed that changes be made in section 54 of the VAT Act, dealing with agents and auctioneers by introducing a provision

allowing an agent under the above-mentioned circumstances to retain the necessary documentation and to assume the liability relating to the zero-rating of the export in the event of non-compliance.

*Comment:* The amendment is welcomed as it incorporates the previous section 72 ruling, however, our understanding is that section 72 ruling also covered the export of silver which is subject to the same refining process as gold.

*Response:* Not accepted. The checks and balances present with the refinery of gold and the export thereof are not the same as those relating to silver and other metals.

*Comment:* Consider including sections 11(1)(f) and 11(1)(k) in the proposed amendment.

*Response:* Partially accepted. Section 11(1)(f) will be included, but not section 11(1)(k) since the intention of the proposed amendment is to cover situations where gold is refined by refineries before being exported or sold to the entities envisaged in section 11(1)(f). Section 11(1)(k) deals with the zero-rating of gold coins that are legal tender. As such, these will not be refined further by gold refineries.

*Comment:* The reference to “depositor” must be removed and be replaced with “principal” because registered banks are permitted to trade in gold.

*Response:* Accepted. The word “depositor” will be replaced with “principal”.

## 2022 Draft Tax Administration Laws Amendment Bill

### 13. CUSTOMS AND EXCISE ACT: ADMINISTRATION

#### 13.1. Providing for a single window concept in relation to the collection of advance passenger and passenger name record information

(Main reference: Section 7A Customs and Excise Act, 1964; clause 17 of the Draft TALAB)

*Comment:* The amendments to section 7A of the Customs and Excise Act relate to enabling and enhancing information sharing between the Department of Home Affairs and SARS. The amendment in our view enhances the current practice from purely an airport environment perspective and will now include all ports of entry. It is unclear how, for example, a bus operator will need to convey the information to the Department of Home Affairs and SARS - but it is presumed that this will form part of the Rules that the Commissioner is empowered to make as suggested by the provisions of section 120 of the Customs and Excise Act. We note that the exemptions will also apply in cases where another government authority has already provided the necessary information.

*Response:* Noted. Currently the receipt of passenger data from airline operators is at an advanced stage. In line with the objectives of a single window, provision is now made for also obtaining passenger data from operators of other conveyances arriving in or departing from the Republic.

Rules dealing with the type of conveyances in respect of which transmission of passenger data will be required, as well as any particular requirements as may be necessary for different conveyances will be prescribed. The rules will be published for public comment in due course. The publication of the rules depends on the effective date of this amendment which must be co-ordinated with the Department of Home Affairs.

*Comment:* The proposed changes accord with the undertakings indicated in the Budget Review which would eliminate the administrative burden of submitting the required information separately to two organs of state (i.e. SARS and the Department of Home Affairs) which in practice already have systems in place for certain data collection and sharing. An extension of innovative processing systems to the air travel industry is welcomed as it would also assist the South African government in monitoring the cross-border movement of individuals and ensuring compliance with the requirements of the Customs and Excise Act.

*Response:* Noted.

### **13.2. Providing for a single window concept in relation to the collection of advance passenger and passenger name record information**

(Main reference: Sections 15 and 120 Customs and Excise Act, 1964; clauses 18 and 22 of the Draft TALAB)

*Comment:* The proposed amendments relating to the traveller declaration requirement are welcomed as they accord with the undertakings in the Budget Review documentation and will strengthen SARS' ability to enforce legislative compliance and detect non-compliance by travellers.

As it is proposed that section 120 of the Customs and Excise Act is amended to enable the Commissioner for SARS to prescribe rules for various matters proposed under the draft TALAB, it will be interesting to see the rules to be prescribed in relation to these proposals for further regulation.

*Response:* Noted. The rules under section 120 dealing with the traveller management system will be published for public comment in due course.

*Comment:* This clause in our view aims to empower the electronic declaration system for travellers, which will effectively allow a traveller to declare any currency prior to arrival.

We have no commentary on this amendment as it seems like a consequential amendment to the Section 7A of the Customs and Excise Act requirement. This amendment is welcomed.

*Response:* Noted. Although not consequential to the amendment of section 7A, the amendments are related in that section 15 is also aimed at better monitoring and control of cross-border movements of persons, their goods and currency. The distinction between the two sections is that section 7A deals with the submission of advance passenger information by the operator of the conveyance for purposes of risk assessment, while section 15 deals with the submission of traveller declarations by travellers, mainly for purposes of tax collection and enforcement of requirements relating to prohibited and restricted goods.

### **13.3. Providing for conditions for deferment of duties by rule**

(Main reference: Sections 39 and 120 Customs and Excise Act, 1964; clauses 19 and 22 of the Draft TALAB)

*Comment:* This proposed amendment appears to be an enabling provision that will introduce rules and controls for deferments.

It is recommended that SARS clarify how these proposed rules for conditions under which deferment of duties will be allowed, will impact on traders and Customs brokers who are currently using deferment accounts and whether there are also any special deferment concessions/benefits for authorised economic operator accredited clients. Overall, the legislated rules that will provide for the governance of deferments would

be welcomed.

*Response: Noted.* Currently the conditions relating to deferment are provided for in policy. For legal certainty and clarity and to comply with international obligations that require conditions for deferment to be included in legislation, the amendment provides for conditions for deferment to be prescribed by rule. Draft rules will be published for public comment in due course.

The intention is not to revise the substance of the current deferment scheme as contained in policy, but rather to include the current scheme in the rules. Provision will be made in the rules for transitional arrangements as may be necessary.

*Comment:* As South Africa is a contracting party to the Revised Kyoto Convention, the proposal that the Commissioner for SARS be enabled to prescribe conditions under which the deferment of duties would be allowed, is welcomed. This will provide certainty and hopefully narrow the scope of the circumstances or conditions under which a deferral can be requested. This would hopefully promote consistency and accountability on the part of SARS, as the Commissioner would be bound by the prescribed conditions, rather than permitting deferments on an ad hoc basis, which could prove difficult in practice and potentially lead to disputes where taxpayers are aggrieved by SARS' decision not to allow the deferment of the payment of duties.

*Response: Noted.* As stated, it is not foreseen that the substance of the current deferment scheme will be revised when transposed into rules.

#### **13.4. Providing for the liquidation of provisional payments that serve as security**

(Main reference: Sections 76 and 120 of the Customs and Excise Act, 1964; clauses 20 and 22 of the Draft TALAB)

*Comment:* The proposed amendments are welcomed as they present an opportunity to close the administrative gap and provide procedural certainty and solutions for taxpayers who wish to claim a refund.

As the above amendments tie in with the proposed amendment to section 120 of the Customs and Excise Act that provides for the Commissioner to make rules to further enhance the processes relating to the refund of provisional payments, it will be interesting to see what the rules will stipulate in relation to unclaimed amounts falling outside the prescription period.

*Response: Noted.* Draft rules will be published for public comment in due course.

*Comment:* In our view, this proposed amendment aligns with the proposed amendment to section 120 of the Customs and Excise Act that provides for the Commissioner of SARS to make rules to further enhance the current processes and

procedures relating to liquidation of provisional payments.

It is proposed that SARS provide guidelines regarding the refund process, that is, will it be a manual and/or electronic application, the time expiry of these refund applications bearing in mind that many provisional payments may be older than two years, etc. Given this situation, will SARS allow for a transition period to allow traders and Customs brokers to apply for refunds that are older than two years?

*Response: Noted.* The amendment provides that refunds of provisional payments (PPs) used as security will be included in the refund process provided for in section 76, in other words it will be refunded via the voucher of correction (VOC) process by removing the PP payment amount by way of an amendment of the original or previous bill of entry. To save traders the cost of a VOC in the case of small amount PPs, rules will prescribe the circumstances in which the liquidation process may be initiated by the Commissioner and the requirements for such initiation.

The rules will also deal with equitable procedures to be followed in respect of unliquidated PPs that are older than two years at the effective date. Draft rules will be published for public comment in due course.

## **14. TAX ADMINISTRATION ACT**

### **14.1. Alignment with anti-money laundering and combatting terrorism developments**

(Main reference: Section 30, 30A, 30B and 30C of the Income Tax Act, 1962: Clauses 6, 7, 8 and 9 of the Draft TALAB)

*Comment:* It is proposed that legislation be amended to clarify that only natural persons can accept fiduciary responsibility for public benefit organisations, recreational clubs, and certain dedicated associations. In order to get consistency between the various sections the definition of a “person” for purposes of sections 30, 30A and 30B must be aligned with the definition of “person” as contained in section 30C.

*Response: Noted.* The draft Taxation Laws Amendment Bill contains amendments aimed to clarify that only natural persons can accept fiduciary responsibility for public benefit organisations, recreational clubs and certain dedicated associations. The proposed amendments will be moved to the draft TALAB, as they are of an administrative nature.

*Comment:* The proposal references a “similar” (but not same) clause in the various sections to impose the disqualification. However, the scope of the sections referenced differ.

Sections 30(3)(i) and 30A(2)(a)(i) refer to at least three people that will take fiduciary responsibility and in practice they sign an affidavit to this effect on registration with SARS. Arguably, a fiduciary responsibility towards SARS is therefore only created in respect of these persons and in practice, that is how it is tabled for adoption of such decisions to nominate such persons. Sections 30B(2)(b)(i) and 30C(1)(d)(i) however require the entity to have a committee or board of management or similar governing body, who are at least three people, to take the fiduciary responsibility, i.e. the whole board or committee has to take responsibility.

The scope of exclusion also seems unclear when sections 30(11), 30A(9), 30B(10) and 30C(7) are concerned. These sections extend fiduciary responsibility to persons “responsible for the management and control of the income and assets”, i.e. they extend to the Executive/Top management as well. Therefore, for sections 30 and 30A, only three people with the fiduciary responsibility will be possibly subject to disqualification, whereas for sections 30B and 30C, the whole committee, board or governing body can be subject to disqualification. It seems that the intent was to disqualify all persons with a fiduciary responsibility that hold certain “office” at the exempt entity. In light of the above discussion, it is submitted that the scope of the disqualified persons be clarified and that sections 30 and 30A be aligned to sections 30B and 30C to cover the whole Board or Committee.

It should also be clarified whether the intention is to apply the disqualification to Executive/Top management as well who are usually responsible for the management and control of the income and assets.

*Response: Accepted.* The intention is that all persons who accepted fiduciary responsibility in respect of the relevant organisation or entity will be subject to the disqualification. Changes will be effected to the proposed amendment to clarify the intention.

As far as other employees or agents representing the organisation are concerned, the proposed amendment aims to align with other pieces of legislation relevant to this issue in an effort to achieve the same outcome. These pieces of legislation are individually quoted in the proposed amendments and focus on persons who accept fiduciary responsibility for the affairs of the organisation. They are not aiming to regulate the conduct of employees working for the organisation or agents representing the organisation. It is submitted that the persons who have accepted this fiduciary responsibility should take the responsibility to manage the employees or agents acting on behalf of the organisation who are not regulated in terms of the proposed amendment. Some employees, for example an accountant, may also be regulated by other governing bodies in terms of other legislative frameworks.

*Comment:* The Trust Property Control Act and the Companies Act, which have been incorporated by reference, both disqualify a person that “has been removed from an office of trust, on the grounds of misconduct involving dishonesty”.

The scope of this provision seems unclear and needs to be clarified as well as to the forum and sanctions that are in scope as to “what is an office of trust?” and “what forum should have removed the person?”. An example of this is an employee removed as social fund treasurer for lying about being on sick leave. In particular, would “office” only be a formal office held, for example a trustee or director or does it include any form of “leadership role” such as at a voluntary body that does not have a formal “office to be held”? Would “removed” include a settlement agreement or just disciplinary hearing in the context of a voluntary association or other unincorporated entity?

*Response:* Noted. These concepts form part of the amendments made by the General Laws (Anti-money Laundering and Combatting Terrorism Financing) Amendment Act, 2022, which implemented amendments to various pieces of legislation. These include, inter alia, the Trust Property Control Act, 1988, the Nonprofit Organisation Act, 1997, and the Companies Act, 2008. It is submitted that the concept of “has been removed from an office of trust, on the grounds of misconduct involving dishonesty”, was fully debated at the time. The concept is also recognised in South African law and applies widely through a variety of different statutes. Interpretative assistance can be obtained by looking at case law developed in this regard.

*Comment:* The proposed amendment makes the holding of an office while being disqualified an offence. Invariably SARS will be requiring these entities to annually monitor and report on the status of such individuals.

However, given the seriousness of such a bar, it would be legally prudent that the disqualified person has an obligation to report their disqualification to the relevant entity as well so that the entities’ tax exemption is not placed at risk due to the individual’s conduct. It is submitted that a person who holds such a fiduciary position must within seven days of becoming disqualified, notify the entity where such position is held, of such disqualification.

*Response:* Comment misplaced. A fiduciary office holder who is disqualified must resign immediately to comply with the law, hence any additional legislative duty on the office holder to notify the entity would be superfluous.

## **14.2. Insertion of an Advance Pricing Agreement Programme**

(Main reference: Chapter III of the Income Tax Act, 1962: Clause 10 of the Draft TALAB)

### **14.2.1 General Comments**

*Comment:* The confidentiality of agreed Advance Pricing Agreements (APAs) has not been discussed in the supporting guidance document. SARS should include guidance as to how it will ensure that agreed APAs will be kept confidential and it

should also clarify in what instances the tax authorities can obtain external industry experts to assist with the APA process.

*Response:* Noted. The APA information will constitute taxpayer information, which is protected by the secrecy provisions of the Tax Administration Act, 2011. SARS will be bound by these secrecy provisions, as well as double taxation agreement confidentiality in the case of bilateral and multilateral APAs.

Regarding engaging or contracting external industry experts to assist SARS with the APA process, it needs to be noted that the transfer pricing community in South Africa is small. Although SARS could engage or contract members of this community for expert assistance, including industry experts, this will only be to the extent permitted by the secrecy provisions that prohibit the on-disclosure of taxpayer information. It is, however, intended that SARS builds its own internal capacity to implement the APA programme to ensure continuity.

*Comment:* The proposed implementation outline also does not address instances where an APA between the tax authorities is not reached. The lack of some level of certainty that an APA will be reached results in taxpayers deciding against pursuing an APA application, and it is recommended that a suitable mechanism to ensure that an APA can be reached is developed. This aspect should also be addressed in the guidance.

*Response:* Noted. Although the intention of the APA programme is to provide certainty, the fact that multiple role players are involved including the competent authorities of other countries, means that it will not always be possible to reach consensus. Should consensus on an APA not be reached, taxpayers are free to continue on the basis that they initially proposed or another basis, informed by the feedback they have received in the APA process.

*Comment:* It is understood that the APA unit will require independence from the transfer pricing audit unit as the two have different purposes. We understand SARS is building capacity in its Competent Authority for transfer pricing matters who are currently handling a number of MAPs, this is welcomed. However, SARS should confirm in its guidance that APAs will be handled by the Competent Authority currently tasked with MAP application and not referred to the transfer pricing audit team, i.e. there must exist a “Chinese Wall” between SARS audit teams and the APA team to the extent that the subject of an audit is also the basis for the APA.

*Response:* Noted. SARS will draw on its experience from its advanced tax ruling system and voluntary disclosure programme to address this concern. It is also important to note that transfer pricing skills are in short supply and SARS may need to draw on these skills from across the organisation, particularly in the pilot phase of the APA programme. In this regard, it is important to note that APAs are primarily forward looking, while audits are generally historical, so the overlap should be limited.

*Comment:* A pilot project for APA implementation is planned as soon as possible after the draft legislation is promulgated. It is stated that the APA pilot will be limited to bilateral APA applications. We appreciate that the initial applications will be limited to bilateral APAs only in order to ensure SARS gains the valuable training through the process. We also acknowledge the draft legislation remains flexible to allow incorporation of unilateral and bilateral APAs in the future. We recommend that the program be extended as soon as possible and that the guidance in support of the legislation also be flexible to allow the implementation of unilateral and multilateral APAs.

*Response:* Partially accepted. The draft TALAB caters for bilateral and multilateral APAs but not unilateral APAs. As with most other countries around the world, SARS relies on the OECD transfer pricing principles and guidelines extensively. These are widely publicised as a reference for all parties. The OECD (2022), *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*, advocate the use of bilateral and multilateral APAs as far as possible. This is further underscored by the OECD/G20 Base Erosion and Profit Shifting (BEPS) final reports. The OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14 - 2015 Final Report* Best Practice 4 is that countries should implement bilateral APA programmes. The OECD (2015), *Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5 - 2015 Final Report* provides for compulsory exchange of unilateral APAs with other affected countries. In addition to this, SARS has capacity constraints that do not allow for the inclusion of unilateral APAs in the APA programme at this time.

However, unilateral APAs may be considered at a later stage, and changes will be effected to enable this. The criteria for acceptance of applications for unilateral APAs, as well as the effective date will be determined by the Commissioner by public notice.

*Comment:* The application of the APA program is too narrow. Simple transactions should not be excluded. It may be easier to start with simple transactions to set the standard. The bilateral limit is enough, otherwise SARS should have full discretion on the choice.

*Response:* Partially Accepted. The proposed section 76J(1) provides that the Commissioner will reject an advance pricing agreement application if inter alia an affected transaction is not complex enough. It is proposed that the criteria for an APA application (proposed section 76G) as well as the criteria for the rejection of an APA application (proposed section 76J) be changed to provide that the criteria will be determined by the Commissioner by public notice, to permit the widening of the ambit of the programme over time.

*Comment:* The supporting guidance document stipulates a specified number of days

for specific steps by SARS and/or the applicant, but it is not clear whether this reference is to business or calendar days. The applicable sections referred to are sections 76F(2) and (4), 76G(1), 76H(1), 76K(5), 76N(1) and 76O(3) and (4). It is recommended that these sections refer to 'business days' as already defined in the TAA.

*Response:* Not accepted. It was not the intention to use "business days" as defined in the Tax Administration Act, 2011. In the context of that Act, a "day" means a calendar day unless a business day is specified. The same scheme applies in the Income Tax Act.

### **14.2.2 Time periods in general**

*Comment:* Various commentators raised concerns with regards to the time periods contained in the draft APA legislation. Contradicting views were expressed, where some commentators called for the shortening of time periods and others called for the extension of time periods in certain instances.

For example, it was requested that time periods that form part of the pre-application process (section 76F) should be shortened to 30 and 60 business days respectively in due course as SARS builds capability, and that the 90 day period for making an application after a successful pre-application consultation (section 76G) is too short given the information and analysis required to prepare the application.

*Response:* Partially Accepted. Given the divergent views and need for flexibility with regards to the time periods contained in the draft TALAB, it is proposed that a similar approach to that adopted as part of the advance tax ruling (ATR) system, where SARS publishes service standards containing turnaround times, also be adopted for purposes of the APA programme. Changes will be effected to remove time periods as far as possible. SARS will endeavour to comply with Best Practice 5 of the OECD (2022), *Bilateral Advance Pricing Arrangement Manual*, in so far as the completion of a bilateral APA application is concerned.

### **14.2.3 Section 76A – Definitions**

*Comment:* The definition of 'affected transaction' in section 76A is an "affected transaction" as defined in section 31 of the Income Tax Act, excluding paragraph (b) of the definition.

This definition is confusing in that the term "affected transaction" as defined in section 31 of the Income Tax Act and the definition in the proposed section 76A of the Income Tax Act are different. It may provide more certainty to refer, in the proposed new Chapter IV to part (a) of the 'affected transaction' definition only, as contained in section 31 of the Income Tax Act.

*Response: Not accepted.* The distinction as it now stands in the draft TALAB is intentional. The inclusion of paragraph (b) of the definition of section 31 of the Income Tax Act would imply that the affected transaction considered for an APA is non-arm's length from the outset, as “*any term and condition of that transaction, operation, scheme, agreement or understanding is different from any term or condition that would have existed had those persons been independent persons dealing at arm's length;*”.

*Comment:* The definition in the Public Notice 1117, which refers to potentially affected transactions excludes subsection (5), (6) and (7) of section 31 of the Income Tax Act and would therefore not be suitable.

*Response: Noted.* As the transactions, operations, schemes, agreements or understandings provided for in subsections (5), (6) and (7) of section 31 are not subject to the provisions of subsections (2) and (3) of section 31, there would be no need to apply for an APA to cover them.

*Comment:* ‘Critical assumptions’ are defined in section 76A as meaning the fundamental factors that are necessary for each party to an APA to remain bound by the APA. SARS should provide guidance on what factors will be included in these critical assumptions.

*Response: Noted.* This will be taken into consideration in the drafting of the relevant public notice and guidance.

#### **14.2.4 Section 76E – Fees for APAs**

*Comment:* The Commissioner may, by public notice, prescribe fees payable for an APA by an applicant. Included in these fees is a cost recovery fee for processing an application. SARS should give some indication of the proposed fee structure. The fact that there are fee levels could create some concern without knowing the proposed amounts.

*Response: Noted.* The associated fees with each relevant stage will be dealt with in a public notice that will be released for public comment before implementation. As noted in the draft TALAB and by the commentator, the fees are intended to defray the costs of administering the APA programme and the processing fee is on a cost recovery basis.

*Comment:* Propose that SARS considers international best practice on fees. Our understanding is that pre-filing fees are uncommon, and a once-off fee at the time of formal application seems to be the norm.

*Response: Not accepted.* Transfer pricing skills are scarce and come at a premium. Fees will be important for SARS to try and recoup its expenditure in this regard. The pre-filing fees will also help ensure that an applicant is serious when

engaging SARS for purposes of an APA application.

*Comment:* SARS should also clarify whether the cost recovery fees will include international travel of SARS officials and/or other indirect costs and if the taxpayer will be consulted on this.

*Response:* Noted. Costing aspects are still to be finalised, with the principal of cost recovery being foundational in the successful implementation of an APA project. The details of cost recovery fees will be dealt with in the public notice and guidance to be issued.

#### **14.2.5 Section 76J – Rejection of an application**

*Comment:* This section provides that SARS may reject an application if the application does not meet the requirements in the legislation including, inter alia, if the value of the affected transaction is less than an amount prescribed by the Commissioner by public notice or if the application is in respect of a frivolous or vexatious issue.

SARS should give some indication of the "minimal value of affected transactions" it proposes introducing. It is proposed that this aligns to the Master File/Local File thresholds.

SARS should also provide clarity on how it will determine if an application is in respect of a "frivolous or vexatious issue".

*Response:* Noted. It will not be practical to legislate for every eventuality. However, SARS will endeavour to provide as much clarity as it can by way of subordinate legislation or guidelines and procedures with regards to "minimum value of affected transactions" or "frivolous or vexatious issue" as being some of the factors that will be taken into account. It needs to be noted that the term "frivolous or vexatious" is a well understood litigation term and that the common law meaning will apply. This concept has also been used in legislation SARS administers before, for example in the ATR system.

It is proposed that the criteria for an application for an APA (proposed section 76G) as well as the criteria for the rejection of an APA (proposed section 76J) be changed to provide that the criteria will be determined by the Commissioner by public notice, to provide for the necessary flexibility in implementing the APA programme.

*Comment:* SARS should provide guidance on its interpretation of the level of complexity it requires for subsection (a) to be met.

*Response:* Noted. SARS will endeavour to provide as much clarity as it can by way of public notice and guidance.

*Comment:* Section 76J does not explain what the process is if an applicant disagrees with SARS' rejection of its APA application. We suggest that before issuing a formal rejection notice, an opportunity is provided to the taxpayer to explain/present its case of why an APA should be allowed.

*Response:* Partially accepted. In the ATR system, SARS engages with a taxpayer before rejecting the advance tax ruling application. A similar system will be considered for purposes of the APA programme.

*Comment:* Clarity should be provided on what the process is if an application is rejected by SARS and the applicant disagrees with this, for instance, who can this be escalated to and would the disagreement be covered by a review process under section 9 of the Tax Administration Act.

*Response:* Noted. The internal review remedy contained in section 9 of the Tax Administration Act, 2011, would be available to the taxpayer. However, if SARS, the other competent authority and the taxpayer cannot come to consensus, the taxpayer may submit its return on the basis as proposed in the APA. Should SARS dispute the correctness of the return and issue a contrary assessment, the taxpayer may dispute the assessment, which dispute will be dealt with in the normal course of the dispute resolution process.

*Comment:* Clarity on whether SARS can still use the factual information that was disclosed as part of the APA application process should also be provided.

*Response:* Noted. SARS will draw on its experience from the ATR system and voluntary disclosure programme to address this concern.

#### **14.2.6 Section 76L – Finalisation of an APA**

*Comment:* Section 76L(4) provides that an APA will not come into effect until subsections (1), (2) and (3) of the section are met. These subsections deal with signing of an APA by the applicant, SARS officials and the competent authority. Time limits should be inserted in respect of these processes.

*Response:* Noted. Given the divergent views and need for flexibility with regards to the time periods contained in the draft TALAB, it is proposed that a similar approach to that adopted as part of the ATR system, where SARS publishes service standards containing turnaround times, also be adopted for purposes of the APA programme.

SARS will also endeavour to comply with Best Practice 5 of the OECD (2022), *Bilateral Advance Pricing Arrangement Manual* which states the following:

“Jurisdictions and taxpayers should aim for a BAPA agreement to be signed within

30 months from the receipt of a complete BAPA application (containing sufficient information) by both competent authorities. Once jurisdictions have taken sufficient efforts to streamline and optimise their BAPA processes and resources in line with this Manual, this aim should be reduced to 24 months.

In some instances, competent authorities may not be able to meet these timeframes. In such situations, competent authorities may simply continue their discussions or may find it useful to agree to a reasonable timeframe with the taxpayer within which they expect to be able to resolve the case.

For cases that have exceeded, or are likely to exceed the suggested period, discussions should still continue and it is advisable for senior officials in the competent authority functions for both jurisdictions to review the case to determine the reasons for the delay and for both competent authorities to then agree upon an approach to ensure the efficient completion of the case.”.

#### **14.2.7 Section 76M – Compliance report**

*Comment:* It not clear if or how the proposed compliance reports will be shared with the other tax jurisdiction(s). The guidance should clarify whether SARS will share the compliance reports with the other jurisdictions or whether the taxpayer must submit it separately.

*Response:* Noted. This will be considered when guidance is drafted.

#### **14.2.8 Section 76O – Termination of an APA**

*Comment:* Section 76O which seemingly seeks alignment with section 85 of the Tax Administration Act, 2011, which applies to ATRs, should be deleted. Section 85 would make sense in the context of an ATR as the ATR relates to an interpretation of law that is sought by the taxpayer. However, in the case of an APA the taxpayer is not seeking an interpretation of law but rather an agreement on the price of an affected transaction, which does not heavily rely on the interpretation of the legislation but rather the application of the OECD transfer pricing methodology.

*Response:* Not accepted. In the interests of administrative transparency, section 76O provides certain criteria with respect to the circumstances that will contribute to the Commissioner terminating an APA. It permits the prospective termination of the APA under circumstances where there is an amendment to the underlying legislation on which the APA is based, there is a change to the double taxation agreement on which the APA is based, a court overturns or modifies an interpretation of the legislation on which the APA is based, or the applicant fails to comply with the terms of the APA. It is also important to note that due to international concerns about base erosion and profit shifting, which is also

prevalent in developing countries such as South Africa, it is important for SARS to reserve the right to terminate an APA.

Given international concerns about base erosion and profit shifting, which is also prevalent in developing countries such as South Africa, it is important for SARS to reserve the right to terminate an APA under specified circumstances, subject to the checks and balances in the draft TALAB. For example, section 76O(5) provides that the party that chooses to terminate an APA must first provide the other parties to the agreement with a notice of the proposed termination, the grounds for termination and an opportunity to make representations prior to the decision to terminate.

#### **14.2.9 Section 76P – Record retention**

*Comment:* This section only affords the applicant 30 days from receipt of a written request from SARS to submit information to confirm compliance with the APA. This information can be extensive and may result in additional time being required by a taxpayer. Only one extension is available to the taxpayer which may be problematic where for example the initial request is sent to an incorrect address or is misplaced and does not reach the relevant person timeously. The final demand may then not be sufficient time for the applicant to collate and submit all information required.

The time period to submit additional information to SARS should be extended from 30 days to 60 days and there should be at least two extensions granted to taxpayers considering the current practical challenges with the delivery of SARS' communication to taxpayers.

*Response:* Comment misplaced. The comment appears to be based on a previous version of the draft legislation. The proposed section 76P(2) had already been amended to provide for more flexibility in this regard, as is done in section 46 of the Tax Administration Act, 2011.

#### **14.3. Non-resident employers' obligation to deduct employees' tax**

(Main reference: Paragraph 2 of Fourth Schedule to Income Tax Act, 1962: Clause 13 of the Draft TALAB)

*Comment:* The current structure of the employees' tax system in South Africa is that where there is no representative employer in South Africa, the employee is responsible to pay their taxes by way of the provisional tax system. Why try and introduce a law that will attempt to enforce a foreign employer to both register, deduct and pay employees tax, SDL and unemployment insurance fund contributions in respect of a South African-based employee that is going to cause significant administrative costs for that foreign company where we already have a provisional tax system that addresses this.

*Response:* Partially accepted. Changes will be effected to only require non-resident employers conducting business through a permanent establishment in South Africa to withhold employees' tax. This will alleviate the administrative burden on non-resident employers in general and limit the obligation to non-resident employers that have business activities in South Africa.

*Comment:* The new 'remote/hybrid' working arrangement, has become the norm across the globe and creates employment opportunities for South African youth who are seen as reasonably cheaper and skilled compared to their foreign counterparts. The global talent pool is sought by many global employers who may never have a business activity in South Africa. The proposed legislation will add an administration burden on these employers, making South African labour resources less attractive. These include the employer's registration with the Companies and Intellectual Property Commission (CIPC), as well as the opening of a local bank account, both of which may not be feasible or possible for a non-resident employer. This will come at an additional cost to the employer as they would have to engage a third-party service provider/employer of record or employ additional staff to assist with the monthly employees' tax obligations.

With unemployment in South Africa at record highs, this amendment may affect the ability of South African residents to participate in the global labour market.

*Response:* Partially accepted. Changes will be effected to only require non-resident employers conducting business through a permanent establishment in South Africa to withhold employees' tax. This will alleviate the administrative burden on non-resident employers in general and limit the obligation to non-resident employers that have business activities in South Africa.

*Comment:* It may be difficult to implement the proposed amendment as SARS has no authority over offshore employers who may very well have no business activity/presence in South Africa. Non-resident employers will now be required to register as an employer with SARS and account for payroll taxes on remuneration paid to "employees" who live and work in South Africa, as well as those who remain SA tax residents but are "employees" who live and work outside South Africa.

*Response:* Accepted. The changes to be effected will relieve non-resident employers with no business activity/presence in South Africa from withholding employees' tax.

*Comment:* "Representative employers", i.e. any agent with the authority to pay remuneration on behalf of a non-resident employer, are also required to register as an "employer" with SARS. In addition to the non-resident principal employer's registration with SARS, it is therefore unclear whether foreign banks and payroll companies located in other countries, which often act as agents of the non-resident employers (with authority to pay remuneration), will also be required to register as an employer with SARS.

*Response:* Noted. Changes will be effected to only require non-resident employers conducting business through a permanent establishment in South Africa to withhold employees' tax. A resident representative taxpayer would be likely in these circumstances.

*Comment:* The proposed amendment lacks a 'trigger clause' that would activate the PAYE withholding requirement, and further does not indicate what the link to South Africa needs to be for a non-resident employer to be subject to the registration and withholding requirement in South Africa.

*Response:* Accepted. Changes will be effected to only require non-resident employers conducting business through a permanent establishment in South Africa to withhold employees' tax.

*Comment:* It is proposed that a further amendment be effected via a change to the definition of 'employer' as contained in the Fourth Schedule, in addition to the proposed amendment to paragraph 2 of the Fourth Schedule.

A 'carve-out' for foreign employers of South African tax resident employees living and working outside South Africa on a full-time basis should be inserted in the definition of "employer".

*Response:* Not accepted. The commentator's proposal has been overtaken by the changes to be effected that will relieve non-resident employers with no permanent establishment in South Africa from withholding employees' tax.

*Comment:* There may be instances where a South African tax-resident employee is physically based abroad, where he works for a foreign employer. Where such a South African tax-resident employee is physically in South Africa (working remotely for such employer) for a certain number of days, we recommend a *de minimis* 'carve-out' rule (we suggest thirty days in aggregate).

Further, where a foreign employer, whose non-resident employee is physically present in the Republic for less than 183 days in a year of assessment, a further *de minimis* should apply so that the foreign employer will not be considered an 'employer', and consequently, not be required to withhold PAYE in respect of remuneration paid to that foreign employee temporarily in SA. This will align the non-resident employees' tax status with the taxing rights under a double taxation agreement.

*Response:* Not accepted. The commentator's first proposal has been overtaken by the changes to be effected that will relieve non-resident employers with no permanent establishment in South Africa from withholding employees' tax. In as far as the second proposal is concerned, double taxation agreements already provide relief in these cases.

*Comment:* It is recommended that the amendment be postponed for a year, i.e., 1 March 2025. Given the far-reaching implications and foreseeable, practical challenges for non-resident employers, we further propose extensive consultation with stakeholders (in the interim), after which the proposed amendment may then be updated.

In addition, practical employer registration requirements for foreign employers will also need to be created that are more efficient and less onerous than the current registration and deregistration requirements (for example opening a SA Bank account and appointing a SA resident public officer), noting that some of the existing registration requirements may be challenging to obtain by virtue of the employer being non-resident.

*Response:* Not accepted. The commentator's proposal has been overtaken by the changes to be effected that will relieve non-resident employers with no permanent establishment in South Africa from withholding employees' tax.

*Comment:* The proposed amendment potentially undermines any progress made with digital nomad visas.

*Response:* Not accepted. The changes to be effected will relieve non-resident employers with no permanent establishment in South Africa from withholding employees' tax. More importantly, double taxation agreements are available to relieve non-residents from taxation in South Africa in respect of short stays. As an example, if a double taxation agreement follows the current OECD or UN models for the taxation of employees, non-resident employees of a non-resident employer are not subject to personal income tax on their remuneration if they remain in South Africa no more than 183 days in a twelve month period and their remuneration is not borne by a permanent establishment of their employer in South Africa.

#### **14.4. Insertion of definition of beneficial ownership**

(Main reference: Section 1 of the Tax Administration Act, 2011: Clause 24 of the Draft TALAB)

*Comment:* The insertion of a beneficial ownership definition in the Tax Administration Act, which appears to align with the Trust Property Control Act, 1988, is welcomed. However, the definition appears to be a standalone definition that is not applied in the Tax Administration Act. Also, uniformity is required in respect of beneficial ownership information of trusts requested by the Master of the High Courts' Office, SARS and the Financial Intelligence Centre (FIC).

*Response:* Noted. Beneficial ownership (BO) information is a type of information that may be prescribed in a return in terms of section 25(2) or 26(2) of the Tax Administration Act, which provide that a return must contain the information prescribed and be a full and true return. The proposed amendments make it clear

that BO is to be interpreted consistently with the foundational legislation in this area and corresponds to the term “beneficial owner” as described in the Financial Action Task Force (FATF) Recommendation 10 and the Interpretative Note on Recommendation 10 of the 2012 FATF Recommendations.

As set out in the Memorandum of Objects, the purpose of obtaining BO information by SARS is primarily for tax administration purposes as referred to in section 3(2) of the Tax Administration Act, for example to establish the identity of a beneficial owner for purposes of determining liability for tax or to investigate if a tax offence, such as tax evasion, has been committed. BO information will help SARS to identify the actual owners of assets, income, companies, trusts and partnerships. This transparency is essential for ensuring that individuals and entities pay the correct amount of tax. Without this information, people can hide their assets or income behind complex legal structures, making it difficult for SARS to assess and collect tax accurately.

Secondly, the purpose is to align with South Africa’s National Strategy on Anti-Money Laundering, Counter Terrorism Financing and Counter Financing Proliferation (AML/CTF/CFP) in developing a national integrated, interoperable and harmonised BO framework, comprising of BO registries and other sources to provide timely access to law enforcement and other competent authorities to adequate and accurate information on beneficial ownership and control in line with the FATF Recommendations.

*Comment:* With respect to the proposed definition of “beneficial owner” for partnerships, potential interpretation challenges are foreseen given that the Financial Intelligence Centre Act, 2001, definition of beneficial owner includes other terms defined for purposes of the Act only, such as “client” and “accountable institution”.

*Response:* Accepted. Changes to the proposed definition will be effected to address these concerns.

*Comment:* At present there are different channels to lodge information relating to beneficial ownership. There is an urgent need to centralise this reporting function because this is time consuming.

*Response:* Not accepted. In line with the National Strategy on AML/CTF/CPF, given effect to in General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Act, 2022 (GLA Act), and related statutory law, SARS is committed to the implementation of new beneficial owner transparency requirements for companies and legal arrangements (such as trusts and partnerships), which will be kept in a repository. This repository will function as a Tier 2 replicator BO registry within the envisaged National BO registry framework, the Tier 1 repositories being Companies and Intellectual Property Commission (CIPC) and the Master of the High Court. Although BO information will primarily be used in the execution of SARS’ mandate and the administration of tax, the

information will ultimately be checked against other BO information held by the CIPC and the Master of the High Court, thus serving as a second layer of BO information to ensure the information is accurate and up-to-date as required under the FATF Recommendations (in particular Recommendations 24 and 25).

This approach under the National Strategy is supported by the revised FATF Interpretation Note to Recommendation 24, i.e. that countries should follow a multi-pronged approach and decide on the basis of risk, context and materiality, what forms of registry or alternative mechanisms they will use to enable efficient access to information by all competent authorities. Companies should also be required to obtain and hold information on their own BO. Competent authorities or entities such as tax authorities, financial intelligence units, companies' registries or BO registries should also be required to hold BO information.

*Comment:* This imposes a large administrative burden because the trust tax return data regarding the same beneficial owner has to be captured per role, such as the founder, trustee and beneficiary. How often must this be done – for every change?

*Response:* Noted. For trusts, there is general consensus in international policy spheres (for example in the FATF Recommendations, European Union Directives and OECD tax standards) that the settlor(s), trustee(s), protector(s), beneficiaries, and any other person exercising ultimate control through direct or indirect ownership or any other means over a trust or the trust assets, would be deemed beneficial owners of a trust. Accordingly, the prescribed basic information in respect of all these persons is required in all jurisdictions with AML/CTF/CFP policies, laws and procedures.

Under the Trust Property Control Act, 1988, as amended by the GLA Act, the duty to obtain and maintain records of the beneficial owners of a trust is on the trustee. Thus, if a trustee obtains and maintains BO information, providing it to more than one competent authority, each with its own mandate and purpose for requiring it, is not unduly burdensome or inconsistent with international law.

As for updating BO information, the objectives of the Trust Property Control Act, 1988, which imposes the obligation on trustees to register the trust and to obtain and provide BO information, differ from the objectives of tax administration. For purposes of tax administration, up to date BO information must be provided when requested, for example in a return or when requested during a verification, audit or criminal investigation.

#### **14.5. Extension of period to request an additional or reduced assessment following an assessment based on an estimate**

(Main reference: Section 95(6) of the Tax Administration Act, 2011: Clause 28 of the Draft TALAB)

*Comment:* The amendment seeks to remedy part of the unlawful application of section 95 as the enabling legislation for auto assessments, and therefore does not achieve the desired retroactive result.

Auto assessments legally do not fall within section 95 as it is a punitive provision applied to non-compliant taxpayers. For this reason, it deviates from the normal compliance obligations of the law and imposes a harsher process on the taxpayer.

It is proposed that the amendment be withdrawn and SARS refrains from its unlawful practice of issuing “auto assessments” under section 95. A new section should be drafted in Chapter 8 of the Tax Administration Act that legally regulates the issuance of “auto assessments” under a fair and efficient law that aligns to the objects of the Act and enhances voluntary compliance and public trust, rather than undermine it.

*Response:* Not accepted. In 2020, SARS launched the auto assessment initiative on a wide scale. SARS issued simplified prepopulated returns to taxpayers based on third-party data sufficient for this purpose, available to SARS. These taxpayers were afforded the option to either accept or reject the prepopulated return to facilitate ease of compliance.

Acceptance of the prepopulated return would lead to an original assessment being issued by SARS, whereas the rejection of the prepopulated return would require the taxpayer to submit a full return containing the correct information as determined by the taxpayer, with an original assessment subsequently being issued by SARS based on the return submitted by the taxpayer.

As explained in the Memorandum of Objects of the Tax Administration Laws Amendment Act, 2020, the set of amendments introduced at the time created a framework for SARS to make assessments based on estimations where no return is required or there is no failure to pay tax, to support and further enhance the auto assessment initiative. It is clear that these amendments enable SARS to also make assessments based on estimations where no tax is due or a refund is due to the taxpayer.

This in essence changed the nature of section 95, from a provision where SARS could only issue estimated assessments if a taxpayer failed to submit a return or relevant material as required or owed SARS money, to a more balanced provision where the ability of SARS to issue assessments based on estimations is housed together, easing the compliance burden on taxpayers of having to submit a return.

In 2021 SARS implemented a pure auto assessment model instead of the hybrid model of accepting or rejecting a simplified pre-populated return. Under the auto assessment model, SARS issues an assessment based on an estimation that is informed by the third party data sufficient for this purpose available to SARS. Should a taxpayer disagree with the assessment, the taxpayer has the opportunity to submit a return reflecting the correct information. SARS may then issue a reduced or additional assessment, as the case may be, based on the return submitted by the taxpayer. Should SARS decide not to issue a reduced assessment or additional assessment, the taxpayer has the option to object to and, if necessary, appeal the original auto assessment issued by SARS.

The application of section 95 for the purposes of auto assessment is neither punitive nor unlawful but a service orientated policy decision that relieves the administrative burden of taxpayers who previously had to file returns. The taxpayer still has the option to file a return where the taxpayer disagrees with the auto assessment issued by SARS. Hence the auto assessment process in no way denies the taxpayer the usual rights and remedies available to the taxpayer.

*Comment:* Due to being a punitive provision, section 95(6) requires the taxpayer to request SARS for extension, and even with the proposed amendment, does not empower the Commissioner for SARS to issue a “notice to submit a return” similar to section 25. The proposal will merely allow the Commissioner to extend the period for the taxpayer to request to submit a return, it does not actually achieve extension of the submission date for the return based on a public notice.

*Response:* Comment misplaced. The proposed amendment does not empower the Commissioner to issue a notice to submit a return additional to the existing powers that the Commissioner has to do so. It is intended to ensure that the date by which taxpayers may submit their requests for reduced or additional assessments does not fall before the date prescribed by public notice for the filing of non-provisional normal returns under section 25 of the Tax Administration Act. Sections 25 and 95(6) are two separate provisions that should not be conflated.

*Comment:* The use of section 95 for auto assessments also means SARS is required to comply with section 96, including that the statement of the grounds of assessment must accompany the estimate assessment. Not a single auto assessment to our knowledge has complied with this requirement.

*Response:* Comment misplaced. As is demonstrated by Annexure B, the grounds for the assessment are clearly stated in the assessment, along with the information upon which the assessment is based. More detailed information is available on eFiling should a taxpayer wish to access it, for example third party tax certificates. It is not clear what additional grounds or information for the assessment would be required in addition to that already provided. The commentator is invited to make suggestions in this regard through the channels that are available to recognised controlling bodies.

*Comment:* Another anomaly is the interaction of section 95(6) with section 95(8). Where SARS have issued an incorrect auto assessment, the process to correct this is that the taxpayer must submit the return within 40 business days from that date of the auto assessment. This “submission of return” is then used by SARS as the request for a reduced or additional assessment by the taxpayer in terms of section 95(6). Where SARS requests verification information, the legal status of that request as relates the process of requesting a reduced or additional assessment remains unclear.

*Response:* Comment misplaced. In terms of section 40 of the Tax Administration Act, SARS may select a taxpayer for verification or audit based on any consideration relevant for the proper administration of a tax Act. In terms of section 3(2)(a) of the Act, the administration of a tax Act would include obtaining full information in relation to anything that may affect the liability of the taxpayer for tax in respect of a previous, current or future tax period. In terms of section 3(2)(b) of the Act, the administration of a tax Act would include ascertaining whether a person has filed correct returns, information or documents in compliance with the provisions of a tax Act, such as section 95 of the Act. SARS may then use its information gathering powers under Chapter 5 of the Act to request or obtain additional information relevant for purposes of the administration of a tax Act.

*Comment:* Section 95 blocks a taxpayer from objecting to the incorrect assessment until SARS has made a decision to either reject the “return” or make a reduced or additional assessment. There is, however, no time period prescribed within which SARS must make this decision.

*Response:* Noted. SARS is required to respond within a reasonable period in terms of the general principles of administrative justice. What a reasonable period would be is dependent on the facts and complexity of a particular case. If the taxpayer believes there has been undue delay, this may be escalated within SARS and, if necessary, to the Tax Ombud.

As will be seen from Annexure B, the interest free grace period for an auto assessment issued at the beginning of the 2023 filing season is synchronised with the date that would apply if the taxpayer submitted a request for a reduced or additional assessment at the end of filing season. Taxpayers, who disagree with their auto assessments and file their requests shortly after receiving the auto assessment, thus have a longer period before payment needs to be made.

If SARS’ review of the requests submitted is not finalised by the end of the period, whether due to complexity or the requests being submitted close to or at the end of filing season, SARS accepts that the filing of the requests indicate an intention to dispute the auto assessments. The taxpayers may thus make application for suspension of payment in terms of the existing provisions for doing so.

*Comment:* Section 95(8) deems the date of assessment for the purposes of any objection, not to be the date that SARS actually informs the taxpayer of the outcome of its “request to amend”, but actually the date of the auto assessment.

Should SARS therefore make this decision after 80 days, the taxpayer would lose its rights to automatically object as the objection would be late in terms of section 104 of the Tax Administration Act.

It is proposed that section 95(8), should be amended to deem the date of the decision taken in section 95(6) as the date that the decision was actually taken in terms of section 95(6) and not the date of the estimate assessment originally issued.

*Response:* Partially accepted. As noted in the Memorandum of Objects for the Tax Administration Laws Amendment Act, 2021, this provision changes the date of assessment to be the date of the decision not to make a reduced or additional assessment under section 95(6). The result is that the time-period within which the taxpayer may object against the assessment is calculated from this extended date. Nevertheless, amendments will be proposed to section 95(8) to ensure the necessary clarity in this regard.

*Comment:* It should be noted that errors on auto assessments for 2023 and prior years ranged from incomplete information populated to third parties submitting incorrect/incomplete information (for example, like the SA Post Office) to SARS’ system, thereby populating incorrect information (in 2022 it was interest and 2023 it was rental “doubling”). The current SARS practice penalises taxpayers for others mistakes and prevents them from submitting the correct information whilst facing punitive consequences for these mistakes.

*Response:* Noted. At the outset it should be noted that the vast majority of auto assessments are accepted by taxpayers. For the 2022 filing season, 94.7% of the 2.9 million auto assessments issued were accepted by taxpayers. Although the high acceptance rate demonstrates the overall quality of the data used, SARS acknowledges that the data supplied by third parties is not always accurate and continues to engage with third party data providers to improve the quality of their data. It may, however, become necessary to penalise third party data providers for inaccurate data in the light of the knock-on effect on personal income taxpayers.

It should further be noted that if taxpayers provide SARS with information that is contrary to the third party data that SARS received, the taxpayer would likely be subject to a verification or audit to determine the cause of the inconsistency and verify the correctness of the return information submitted by the taxpayer. It is thus in taxpayers’ own interests to also engage with providers of inaccurate third party data to address the situation.

## **ANNEXURE A: LIST OF COMMENTATORS**

1. Actuarial Society of South Africa
2. Association for Monitoring and Advocacy of Government Employees' Pensions (AMAGP)
3. Autonomi Capital
4. Baker & McKenzie
5. Banks Development Agency
6. BDO
7. BEVSA
8. BOWMANS
9. British American Tobacco South Africa (BATSA)
10. Business Leadership South Africa
11. Charteredeb
12. Chemprotech
13. Cliffe Dekker Hofmeyr (CDH)
14. Consumer Goods Council of South Africa (CGCSA)
15. Coronation Fund Managers
16. Culminit
17. Dear SA
18. Deloitte
19. Department of Health
20. Department of Water and Sanitations
21. ENSafrica
22. EY
23. Fiduciary Institute of Southern Africa (FISA)
24. Futuregrowth
25. Government Employees Pension Fund (GEPF)
26. Government Pensions Administration Agency (GPAA)
27. Harmony
28. Imperial Logistics Group
29. Institute of Retirement Funds Africa (IRFA)
30. Keystone Actuarial Solutions
31. KPMG
32. Law Society of South Africa
33. Limpopo Tobacco Processors
34. Mazars
35. Meadow Cape
36. Metal Concentrators SA
37. Minerals Council
38. Momentum Metropolitan
39. MTN
40. NOVARE Holdings
41. Old Mutual
42. Payroll Authors Group of South Africa (PAGSA)
43. PKF

44. Premier FMCG
45. Public Health and Social Development Sectoral Bargaining Council (PHSDSBC)
46. Purple Group
47. PwC
48. Reunert Limited
49. Richards Bay Industrial Development Zone
50. South African Breweries(SAB)
  
51. Seshego Benefit Consulting,
52. Simeka Consult
53. Sizakala Customer Service Unit
54. South Africa Wine
55. South African Cane Growers' Association
56. South African Institute of Tax Practitioners (SAIT)
57. South African Maritime Safety Authority (SAMSA)
58. South African Policing Union (SAPU)
59. South African Sugar Association
60. South African Tobacco Transformation Alliance (SATTA)
61. Stonehage Fleming Financial Services
62. Telkom
63. The African Association of Accountants-General (AAAG)
64. The Association for Savings and Investment South Africa (ASISA)
65. The Banking Association South Africa
66. The Banking Association South Africa (BASA)
67. The Cement & Concrete SA (CCSA)
68. The Financial Intermediaries Association (FIA)
69. The Office of the Pension Funds Adjudicator (OPFA)
70. The South African Democratic Teachers Union (SADTU)
71. The South African Institute of Chartered Accountants (SAICA)
72. The South African Institute of Professional Accountants (SAIPA)
73. The South African Institute of Stockbrokers (SAIS)
74. The South African Insurance Association (SAIA)
75. The South African Insurance Association (SAIA)
76. The South African Liquor Brandowners' Association (SALBA)
77. The South African Property Owners Association (SAPOA)
78. UGU District Municipality
79. UX Refinery
80. Vodacom
81. Webber Wentzel
82. Werksmans Attorneys
83. Willis Towers Watson